II. ANALYSIS

A. *Standard of Review*

In considering a motion to dismiss under Court of Chancery Rule 12(b)(6), the Court must assume the truthfulness of all well-pleaded facts contained in the complaint and view those facts and all reasonable inferences drawn from them in the light most favorable to the plaintiff.[2] Conclusory allegations unsupported by facts contained in the complaint, however, will not be accepted as true.[3] Dismissal is appropriate under Rule 12(b)(6) only where it appears with a reasonable certainty that the plaintiff would not be entitled to the relief sought under any reasonable set of facts properly supported by the complaint.[4]

B. *Common Law and Equitable Fraud Claims Against All Defendants*

Plaintiffs fraud claims on behalf of the proposed class are dismissed with prejudice because individual issues of justifiable reliance predominate over issues common to the members of the class. Plaintiffs fraud claims on behalf of herself as an individual are dismissed without prejudice because the amended complaint fails to adequately allege justifiable reliance and cognizable damages.

Plaintiff alleges that the various misrepresentations made by Rite Aid over the course of the three years in question constitute both common law and equitable fraud. The elements of common law fraud are: (1) a false representation of fact by the defendant; (2) the defendant knows or believes the representation to be false or acts with reckless indifference to its truth or falsity; (3) the defendant intends to induce the plaintiff to rely on the representation; (4) the plaintiff actually and justifiably relies on the false representation; and (5) the plaintiff incurs damages as a result of such reliance.[5] For the purposes of ruling on this motion to dismiss, the only difference between common law and equitable fraud is that the second element, scienter, need not be proven to make out a claim of equitable fraud because "equity provides a remedy for negligent or innocent

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[2]*See Grobow v. Perot*, 539 A.2d 180, 187 (Del. 1988) (stating that "upon a motion to dismiss, only well-pleaded allegations of fact must be accepted as true" and that the Court "need not blindly accept as true all allegations, nor must it draw all inferences from them in plaintiffs' favor unless they are reasonable inferences").

[3]*Id.* (stating that "conclusionary allegations of fact or law not supported by allegations of specific fact may not be taken as true").

[4]*Rabkin v. Philip A. Hunt Chem. Corp.*, 498 A.2d 1099, 1104 (Del. 1985).

[5]*Gafin v. Teledyne, Inc.*, 611 A.2d 467, 472 (Del. 1992).

misrepresentations."[6] Because I find the pleadings are sufficient to constitute a well-pleaded allegation of scienter as to all defendants, the analyses of the common law fraud and equitable fraud claims are identical for the purposes of this ruling.

1. Making False Representations

As to the first element, plaintiff more than adequately alleges that false representations were made by the company, through the director defendants[7], and with the assistance of KPMG.

2. Knowledge, Belief, or Reckless Disregard As to the Truth or Falsity

Plaintiffs amended complaint also adequately alleges scienter in that the magnitude and scope of the misrepresentations alleged support a reasonable inference that each and all of the defendants acted with at least reckless disregard for the truth or falsity of at least some of the various financial statements, press releases, and other public disclosures alleged to be materially false and misleading.

3. Intent That Plaintiff Rely

Plaintiff alleges that false and misleading disclosures were made in financial statements, annual reports, various SEC filings, public statements to analysts, to major shareholders, and to the press regarding the financial performance of the company and regarding the company's explanations for variations from anticipated financial performance. Due to the nature of these disclosures, the Court can draw the reasonable inference

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[6]*Zirn v. VLI Corp.*, 681 A.2d 1050, 1061 (Del. 1996).

[7]The audit committee directors assert that plaintiff failed sufficiently to allege that they "made" any of the misleading statements. The allegations are adequate to support an inference that the audit committee members' participation in the review and approval of the financial statements in question could constitute "making" such statements for the purposes of plaintiffs prima facie claim of fraud.

The audit committee directors also assert a defense of good faith reliance on the reports of corporate advisors and officers as permitted under 8 *Del. C.* § 141(e). As the complaint does not include allegations regarding the reports of experts (other than co-defendant KPMG—allegedly an aider and abettor in the directors breaches of fiduciary duties), the protections of § 141(e) would constitute an affirmative defense for which evidence may be brought at trial. It cannot affect the ruling on a motion to dismiss because at this stage, the plaintiffs allegations must be taken as true, notwithstanding any defenses that may be raised in a trial on the merits.

that plaintiff would be able to prove that Rite Aid, the director defendants, and KPMG intended that shareholders rely on their truth.

4. Actual and Reasonable Reliance

The requirement that plaintiff plead and prove actual and reasonable reliance on the false representations made by the defendants is fatal to a class action claim of either common law or equitable fraud. Delaware law is clear that neither equitable nor common law fraud claims may be maintained as class actions because (1) certification of a class requires that "questions of law or fact common to the members of the class predominate over any questions affecting only individual members"[8] and (2) in a common law or equitable fraud case the individual question of "justifiable reliance[] will inevitably predominate over common questions."[9] Plaintiff cannot rely on a presumption of reliance based on a type of "fraud on the market" theory because the Supreme Court has determined that Delaware does not recognize such a claim.[10]

Plaintiff points out that *Gaffin* proscribes class certification only "in a *purely* common law or equitable fraud case."[11] Plaintiff asserts that the class may be certified in this case because they have also stated a claim for breach of fiduciary duty. This argument is unavailing because, as discussed below, the breach of fiduciary duty claim is dismissed on other grounds.

Finally, plaintiff contends that class certification issues need not be decided at this stage in the proceedings. It is true that the Court need not reach all the issues relevant to class certification on this motion to dismiss. Nonetheless, where the claim stated cannot *by its nature* form the basis of a class action, no class could be entitled to relief under any set of facts and it is appropriate to dismiss the claim as to the purported class under Rule 12(b)(6).

The inability to certify a class for a fraud claim, however, is not dispositive of defendants' liability to plaintiff as an individual for frauds alleged. Thus it is necessary to examine whether plaintiff adequately pleads that *she* actually and justifiably relied on misrepresentations by defendants. The amended complaint fails to allege reliance except in the most conclusory fashion.[12] Only one factual statement from the amended

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[8]Court of Chancery Rule 23(b)(3).

[9]*Gaffin*, 611 A.2d at 474.

[10]*See Malone v. Brincat*, 722 A.2d 5, 12-13 (Del. 1998).

[11]Pl.' s Answering Br. at 50 (emphasis in original) (quoting *Gaffin*, 611 A.2d at 474).

[12]Pl.'s Am. Compl. ¶ 2 (stating that plaintiffs injuries resulted from the "defendants' wrongful conduct (and, to the extent required, plaintiffs and class members' reliance on that

complaint is relevant to an evaluation of whether plaintiff did in fact rely on defendants' misrepresentations when deciding to hold her stock in Rite Aid. The amended complaint states, "Plaintiff Stacey Feinglass Manzo has owned Rite Aid stock since the early 1970's and continues to own it today."[13] This assertion is made in the context of establishing standing to bring this claim. Nonetheless, the fact that plaintiff has decided to hold her Rite Aid stock continuously over some thirty years undercuts, to some extent, any later assertions that between March 1, 1997, and October 18, 1999, that decision was based on the inaccurately positive picture presented in the company's financial disclosures. Perhaps plaintiff did rely on defendants' misrepresentations, but so far she has failed to allege any facts to support such an inference.

5. Damages

Similarly, plaintiffs fraud claims are dismissed without prejudice because she has failed to allege legally cognizable damages suffered as a result of reliance on any false representations. In order to survive a motion to dismiss a fraud claim, plaintiff must allege damages.[14] Plaintiff makes two attempts to articulate a damages theory; neither is successful.

Plaintiff alleges "investment opportunity losses," yet fails to cite a single case to support such a theory of damages. Under this theory, the Court is asked to presume that plaintiffs investment in Rite Aid stock would have been deployed in other more successful investments had plaintiff been privy to accurate information concerning Rite Aid's financial performance. First, this presupposes reliance by plaintiff upon false representations about Rite Aid's financial condition, which, as discussed above, is unsupported in the amended complaint. Second, awarding money damages to compensate plaintiff for the return she *could* have earned had she invested elsewhere—as she was free to do, but didn't do—amounts to speculation founded upon uncertainty. As plaintiff has failed to direct this Court to any precedent or policy to support such an award, plaintiffs assertion of "investment opportunity losses" does not, in my opinion, state a cognizable injury.

In addition, plaintiff asserts that she is entitled to "benefit of the bargain damages." The amended complaint fails to articulate any specific

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conduct)"), *id.* ¶ 274 (stating that plaintiff and class members "received and relied" on various communications of the company), *id.* ¶ 279 (same).

[13]Pl.' s Am. Compl. ¶ 6.

[14]*See Gaffin*, 611 A.2d at 472.

bargain from which these benefits purportedly flow and, therefore, does not state a cognizable injury. [15]

C. Breach of Loyalty Claim Against Director Defendants

Plaintiffs breach of fiduciary duty claims are dismissed with prejudice because they are derivative in nature, and plaintiff has (1) failed to make demand on the board of directors, (2) failed to allege facts to support excusing demand under Court of Chancery Rule 23.1, and (3) disavowed in the amended complaint any intention to bring a derivative action. *Malone* contemplates that intentional misrepresentations to "holders" of stock when, as alleged in this case, the board is not seeking shareholder action could give rise to *either* a direct or a derivative claim.[16] It leaves unchanged, however, the method of distinguishing a direct claim from a derivative one.[17]

In order to determine whether a claim is direct or derivative, the Court looks to the nature of the harm and the relief available upon success of the suit.[18] To state a direct claim, the shareholder must allege either an injury that is different from what is suffered by other shareholders or one that involves a contractual right of shareholders that is independent of the corporation's rights.[19] As discussed above, the specific injury asserted by plaintiff is unclear. To the extent that plaintiff was deprived of accurate information upon which to base investment decisions and, as a result, received a poor rate of return on her Rite Aid shares, she experienced an injury suffered by all Rite Aid shareholders in proportion to their pro rata share ownership. This would state a derivative claim. Although plaintiff seeks to remedy the injury on behalf of only "holders" of Rite Aid, who neither bought nor sold their stock between March 1, 1997, and October 18, 1999, this does not indicate that "holders" suffered an injury that is distinct from that suffered by buyers or sellers. Rather, holders who neither bought nor sold would have suffered any injury for the entire period during which misrepresentations are alleged to have occurred. Injury to purchasers would have begun later (at the time of purchase) and injury to sellers would

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[15]The Plaintiffs Answering Brief in Opposition to Defendants' Motion to Dismiss similarly neglects to identify a bargain under which plaintiff could claim "benefit" and, even if the brief were to specify the particulars of any bargain, this Court would be bound to rely solely upon the allegations contained in the amended complaint. *See Orman v. Cullman*, 794 A.2d 5, 28 n.59 (Del. Ch. 2002).

[16]*Malone*, 722 A.2d at 16-17.

[17]*Id.* at 17 n.45.

[18]*Kramer v. W. Pac. Indus., Inc.*, 546 A.2d 348, 352 (Del. 1988).

[19]*Moran v. Household Int'l, Inc.*, 490 A.2d 1059,1070 (Del. Ch. 1985).

have terminated earlier (at the time of sale). The temporal duration is different, but the substance of the injury is the same.

Plaintiffs amended complaint and brief obliquely assert some sort of contractual right of shareholders to accurate information from the company and from its officers, directors, and advisors. Indeed it is true, as recognized in *Malone*, that directors are obligated to be truthful in all communications with shareholders.[20] This obligation exists even, as in this case, with regard to statements that do not seek shareholder action and those that are general public statements.[21] This obligation arises from the fiduciary duties that directors of Delaware corporations owe *both* to the shareholders and to the corporation itself.[22] Even if such a legal duty may in some context be properly characterized as a contractual right,[23] such a right cannot be characterized as belonging *solely* to the shareholders because it is also a right of the corporation. Therefore, any breach of fiduciary duty claim based upon the *mere* fact of knowing misrepresentation is necessarily derivative. To state a *direct* claim on that basis, plaintiff must identify some resultant injury that either affects some shareholders disproportionately to their pro rata stock ownership, or affects those rights of shareholders that are traditionally regarded as "incidents" of stock ownership.[24] Plaintiff has failed to state such an injury.

D. Aiding and Abetting Breach of Fiduciary Duty Claim Against KPMG

Because the breach of fiduciary claims are dismissed with prejudice, the claim against KPMG for aiding and abetting breach of fiduciary duty is similarly dismissed with prejudice.

III. CONCLUSION

The class action claims for both common law and equitable fraud are dismissed with prejudice because the individual question of justifiable reliance will inevitably predominate over questions common to the class. Plaintiffs individual common law and equitable fraud claims are dismissed without prejudice because the amended complaint fails to adequately allege

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[20] *Malone*, 722 A.2d at 10-11.

[21] *Id.*

[22] *Id.*

[23] I question whether in any context such a characterization would be appropriate.

[24] *See In re Digex, Inc. S'holder Litig.*, 789 A.2d 1176, 1189-90 (Del. Ch. 2000) (quoting DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 9-2(a), at § 17-18 (1998)).

reliance and damages. The breach of fiduciary duty claim against the director defendants is dismissed with prejudice because the amended complaint does not state a direct claim and disavows any derivative claim. Furthermore, even were a derivative claim intended, plaintiff has not made demand on the board of directors and has not plead facts sufficient to show why demand should be excused. Finally, for the same reasons that require dismissal of the underlying breach of fiduciary duty claim, the claim against KPMG for aiding and abetting a breach of fiduciary duty is similarly dismissed with prejudice.

IT IS SO ORDERED.

TOOLEY v. DONALDSON, LUFKIN & JENRETTE, INC.

No. 18,414-NC (Consolidated)

Court of Chancery of the State of Delaware, New Castle

January 21, 2003

Joseph A. Rosenthal, Esquire, and Herbert W. Mondros, Esquire, of Rosenthal, Monhait, Gross & Goddess, P.A., Wilmington, Delaware; and Abbey Gardy, LLP, New York, New York, of counsel, and Schiffrin & Barroway, LLP, Bala Cynwyd, Pennsylvania, of counsel, for plaintiffs.

David C. McBride, Esquire, and John J. Paschetto, Esquire, of Young Conaway Stargatt & Taylor, LLP, Wilmington, Delaware; and Alan S. Goudiss, Esquire, of Shearman & Sterling, New York, New York, of counsel, for defendant Donaldson, Lufkin & Jenrette, Inc.

Robert K. Payson, Esquire, and Donald J. Wolfe, Jr., Esquire, of Potter Anderson & Corroon, Wilmington, Delaware; Paul K. Rowe, Esquire, of Wachtell, Lipton, Rosen & Katz, New York, New York, of counsel, for individual defendants.

CHANDLER, *Chancellor*

Plaintiff stockholders originally brought this class action suit to enjoin a delay in the closing of a tender offer in the proposed merger between Donaldson, Lufkin & Jenrette, Inc. ("DLJ") and Credit Suisse Group. They planned to tender their shares and alleged that the DLJ board members breached their fiduciary duties by wrongfully agreeing to a 22-day delay in the closing. Plaintiffs further alleged that they were harmed by this delay because of the lost time value of the consideration paid for their shares at the close of the tender offer.

The tender offer closed and plaintiffs' shares were cashed out on November 2, 2000. The merger has been consummated and plaintiffs continue to seek damages for the lost time value of their $90 per share that was occasioned by the postponed closing. Defendants have now moved to dismiss the complaint for lack of standing.

I. STATEMENT OF FACTS[1]

Plaintiffs are former stockholders of DLJ, a Delaware corporation that provides various investment and banking services to institutional, governmental and individual clients. Before its acquisition by Credit Suisse Group, DLJ's largest stockholder was AXA Financial, Inc., owning approximately 71% of DLJ. AXA Financial, in turn, is majority-owned (approximately 60%) by its parent, AXA. All the individual defendants are former directors of DLJ.

On August 30, 2000, AXA Financial announced that Credit Suisse Group and DLJ had entered into a $13.4 billion merger agreement. The merger agreement was between Credit Suisse Group, Diamond Acquisition Corporation,[2] and DLJ, and expressly disavowed any third-party beneficiaries to the contract. According to this agreement, DLJ's public minority would receive $90 cash per DLJ share in a first-step tender offer to the DLJ public stockholders, and AXA Financial would subsequently receive the cash and stock combination equivalent of $90 per share. The first-step tender offer was intended to expire 20 days after its commencement, unless the offer was extended.

The merger agreement provided for two main types of extensions for the tender offer period. The first, a five-day extension, could be invoked without DLJ's consent if payment obligations were not satisfied,

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[1]All facts are taken as alleged in the Class Action Complaint and the documents upon which the Complaint relies.

[2]Diamond Acquisition Corporation was a wholly owned subsidiary of Credit Suisse Group, formed to effect the merger. For purposes of this opinion, I treat Diamond Acquisition the same as Credit Suisse Group.

or as required by the SEC, or if more than 10% but less than 20% of all outstanding DLJ shares were tendered. The second type of extension allowed Credit Suisse Group to extend the offer under various enumerated conditions, one of which included an agreement between DLJ and Credit Suisse Group to postpone acceptance of DLJ stock for payment. Credit Suisse Group used both of these options to extend its tender offer.

Credit Suisse Group began its Tender Offer on September 8, 2000. This offer was set to expire on October 5, 2000. Credit Suisse then invoked a five-day extension of the offer, announced on October 6, 2000. At the end of this first extension, the parties agreed upon a second extension of the offer in a letter agreement. This letter agreement amended various terms of the merger agreement and extended the tender offer until November 2, 2000, a date 22 days later than the first extension date. In the letter agreement, Credit Suisse Group also removed several contingencies set forth in the merger agreement, such as material adverse changes and representations and warranties, by deeming them satisfied by DLJ. The tender offer closed on November 2, 2002, and the public minority shareholders were cashed out for $90 per share.

Plaintiffs filed this class action complaint, alleging that the second extension was not authorized by the merger agreement, lacked consideration, and was wrongfully approved "solely to accommodate the administrative needs of AXA Financial." Plaintiffs contend this was a breach of the DLJ board members' fiduciary duties, namely a breach of their duty of loyalty, because the board had a duty to proceed with the tender offer so that the DLJ shareholders would receive cash for their shares as soon as possible. Instead, the closing of the tender offer was delayed by 22 days. Plaintiffs contend they were injured because they lost the time value of the cash paid for their shares. In essence, plaintiffs' entire complaint[3] rests upon the assertion not that the merger consideration was unfair, but that it was received 22 days later than initially agreed because of a wrongfully granted extension.

II. DIRECT OR DERIVATIVE NATURE OF THE CLAIM

Defendants move to dismiss the complaint for lack of standing. They argue that, even if there was a breach of fiduciary duty by the board members, the complaint alleges, at most, a derivative claim. Therefore, plaintiffs lost standing to pursue the claim, pursuant to Chancery Court

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[3]Plaintiffs additionally alleged harm based upon the failure of the board to declare a quarterly dividend and for corporate waste, but both these claims were abandoned in plaintiffs' Opposition Brief.

Rule 23.1, when their shares were cashed out.[4] Once DLJ shareholders were cashed out, they would lose standing to sue on behalf of the corporation. Additionally, defendants assert that plaintiffs suffered no special injury resulting from the 22-day delay because this delay fell equally upon all shareholders and did not injure any contractual right of the shareholder separate from the corporation. Thus, because defendants contend that the complaint fails to allege a direct claim, they assert that plaintiffs' standing to bring this suit was extinguished when plaintiffs were cashed out. Thus, the complaint (they argue) should be dismissed.

Plaintiffs disagree and assert that the complaint alleges special injury, because only the tendered minority shares were subject to the 22-day delay in the closing of the tender offer. Plaintiffs reason that although the extension had a direct adverse economic impact on the class, the extension of the tender offer actually benefited AXA Financial, the majority shareholder, by accommodating its administrative needs. Thus, plaintiffs conclude, they have alleged the requisite special injury required to bring a direct suit, and the complaint cannot be dismissed for lack of standing.

Because plaintiffs are no longer DLJ stockholders, their standing to bring this suit depends upon whether it is direct or derivative in nature. A direct action seeks compensation for a special injury different from injury to the corporation or other shareholders. A derivative action seeks compensation for injury to the corporation.

According to Rule 23.1, derivative actions may only be maintained by shareholders of a corporation. Thus, standing to bring a derivative action is extinguished when a shareholder sells its shares in the corporation, even if the shareholder initially had standing to bring the suit. In such situations, the derivative suit can no longer be maintained by the shareholder, and the suit is traditionally dismissed.

In order to bring a *direct* claim, a plaintiff must have experienced some "special injury."[5] A special injury is a wrong that "is separate and distinct from that suffered by other shareholders, . . . or a wrong involving a contractual right of a shareholder, such as the right to vote, or to assert majority control, which exists independently of any right of the corporation."[6] Suits alleging special injuries may be maintained as a direct action, even though the same wrong injures the corporation as well.[7]

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[4]Rule 23.1 governs derivative actions and generally requires a plaintiff to be a shareholder of a corporation in order to bring suit on behalf of the corporation.

[5]*Lipton v. News Int'l.*, 514 A.2d 1075, 1079 (Del. 1986).

[6]*Moran v. Household Int'l, Inc.*, 490 A.2d 1059, 1070 (Del. Ch. 1985), *aff'd*, 500 A.2d 1346 (Del. 1986).

[7]*Id.* at 1079.

Additionally, shareholders do not lose standing to bring suit to recover for special injuries when their shares in the corporation are sold.

The Court will independently examine the nature of the wrong alleged and any potential relief to make its own determination of the suit's classification.[8] This determination is for the Court to make based upon the body of the complaint; plaintiffs' designation of the suit is not binding.[9]

Here, it is clear that plaintiffs have no separate contractual right to bring a direct claim, and they do not assert contractual rights under the merger agreement. First, the merger agreement specifically disclaims any persons as being third party beneficiaries to the contract. Second, any contractual shareholder right to payment of the merger consideration did not ripen until the conditions of the agreement were met. The agreement stated that Credit Suisse Group was not required to accept any shares for tender, or could extend the offer, under certain conditions—one condition of which included an extension or termination by agreement between Credit Suisse Group and DLJ. Because Credit Suisse Group and DLJ *did* in fact agree to extend the tender offer period, any right to payment plaintiffs could have did not ripen until this newly negotiated period was over. The merger agreement only became binding and mutually enforceable at the time the tendered shares ultimately were accepted for payment by Credit Suisse Group.[10] It is at that moment in time, November 3, 2000, that the company became bound to purchase the tendered shares, making the contract mutually enforceable. DLJ stockholders had no individual contractual right to payment until November 3, 2000, when their tendered shares were accepted for payment. Thus, they have no contractual basis to challenge a delay in the closing of the tender offer up until November 3.[11] Because this is the date the tendered shares were accepted for payment, the contract was not breached and plaintiffs do not have a contractual basis to bring a direct suit.

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[8]*Kramer v. Western Pacific Indus., Inc.*, 546 A.2d 348, 352 (Del. 1988).

[9]*Id.*

[10]*Johnson v. Shapiro*, 2002 WL 31438477 at *5 (Del. Ch.) (finding that tender offer was mutually binding when the tendered shares were *accepted* while the fiduciary relationship extended until the time the payment was actually made for those shares).

[11]Aside from this, it is notable that the merger agreement contained a much later termination date of March 31, 2001. This is the date on which the merger agreement would expire by its own terms, if the merger had not yet been consummated. The agreement anticipated various contingencies that could lead to delays in the consummation of the merger. Thus, it should not have surprised plaintiffs that a delay could have occurred, as it did here. Further, as compared to the final March 31, 2001, termination date contained in the merger agreement—a date over four months after the tender offer period actually closed—a delay of only 22 days hardly seems unexpected or unreasonable.

The only other type of special injury that would provide the stockholder plaintiffs with a basis to bring a direct claim is one that is separate and distinct from the injury suffered by the other shareholders or the corporation. Here, plaintiffs, as a class, allege that their injury is the lost time value of their $90 per share caused by the 22-day extension. They allege that this injury is different from both the non-tendering shareholders and the majority DLJ shareholder (*i.e.*, AXA Financial). As the argument goes, the injury is different from the non-tendering shareholders for the simple reason that the non-tendering shareholders did not tender their shares in the offer, so any delay in its closing was irrelevant to them. Similarly, the majority stockowner, AXA Financial, allegedly did not lose the time value of its money when the tender offer was extended because it was not subject to the tender offer either. Further, they allege, AXA Financial actually benefited from this extension because it was agreed upon solely to accommodate its administrative needs.

This argument is logically flawed, however. A delay in one step of the merger must logically lead to a delay in the subsequent steps of the staged merger because of the domino effect of the steps leading up to its closing. Although neither the non-tendering stockholders nor AXA Financial tendered their shares in the tender offer, it is not plausible that they did not suffer a similar delay in receiving the consideration paid for their shares. Neither the non-tendering stockholders nor AXA Financial could be cashed out until the tendering shareholders were cashed out. Thus, any 22-day delay occasioned by an extension of the tender offer would also result in a similar delay for the second step of the merger—the step that included both the minority stockholders and AXA Financial. Because this delay affected all DLJ shareholders equally, plaintiffs' injury was not a special injury, and this action is, thus, a derivative action at most. Accordingly, plaintiffs no longer have standing to bring this suit and it must be dismissed.

III. CONCLUSION

For the foregoing reasons, defendants' motion to dismiss the complaint for lack of standing is GRANTED. An Order has been entered in accordance with this Memorandum Opinion.

ORDER

For the reasons assigned in this Court's Memorandum Opinion entered in this case on this date, it is

ORDERED that the complaint in these consolidated proceedings is dismissed because the plaintiffs lack standing to bring the claims asserted therein.

WEST CENTER CITY NEIGHBORHOOD ASSOCIATION, INC. v. WEST CENTER CITY NEIGHBORHOOD PLANNING ADVISORY COMMITTEE, INC.

No. 19,557-NC

Court of Chancery of the State of Delaware, New Castle

January 24, 2003

Samuel L. Guy, Esquire of The Law Office of Samuel L. Guy, Wilmington, Delaware, for plaintiffs.

David J. Ferry, Jr., Esquire and Rick S. Miller, Esquire of Ferry, Joseph & Pearce, P.A., Wilmington, Delaware, for defendant.

NOBLE, *Vice Chancellor*

This unusual case involves membership on the board of directors of Defendant West Center City Neighborhood Planning Advisory Committee, Inc. ("WCCNPAC"), a not-for-profit Delaware corporation, established, *inter alia*, as a conduit for the allocation and distribution of grant funds for several neighborhoods in the city of Wilmington (the "City"). The Plaintiffs in this action, brought under 8 *Del. C.* § 225, are Bessie C. Ashe ("Ashe"), Dwight L. Davis ("Davis"), Harold Chambers, Jr. ("Chambers"), Rhonda M. Davis, Frauline Trotter ("Trotter"), Mercedes Fields ("Fields"), John McNeil ("McNeil"), and Caren Turner ("Turner") (collectively, the "Individual Plaintiffs"), who, along with Plaintiff West Center City Neighborhood Association, Inc. ("WCCNA"), a not-for-profit Delaware corporation (collectively with the Individual Plaintiffs, the "Plaintiffs"), assert the rights of the Individual Plaintiffs to hold office as directors on the WCCNPAC board of directors (the "Board"). This post-

trial memorandum opinion sets forth my findings of fact and conclusions of law.[1]

I. BACKGROUND[2]

A. *The Public Character of WCCNPAC*

The overriding aspect of this controversy, and thus the logical starting point for any discussion of it, is WCCNPAC's mission of public service. WCCNPAC, which serves the West Center City Analysis Area (the "WCCAA "),[3] represents a link in the chain of entities designed to deliver government funding aimed at urban development. WCCNPAC consists primarily of three geographic constituencies: Quaker Hill, Trinity Vicinity, and West Center City. Each of these neighborhoods is served by its own neighborhood association: Quaker Hill Neighborhood Association, Trinity Vicinity Neighborhood Association, and WCCNA, respectively (collectively, the "Neighborhood Associations").[4]

Title I of the Housing and Community Development Act of 1974 was amended in 1977 to add the Urban Development Action Grant ("UDAG") Program.[5] Under the UDAG Program, "urban development action grants [are made] to cities and urban counties which are experiencing severe economic distress to help stimulate economic development activity needed to aid in economic recovery."[6] To administer the UDAG funds granted to City, a chain of entities was created. The city established the Wilmington UDAG Corporation ("WUC"), a not-for-profit

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[1]Because Rhonda M. Davis failed to pursue her claim, it was dismissed at trial.

[2]The facts set forth in this memorandum opinion are the product of my best attempt to overcome a poor evidentiary record. I note two serious obstacles: first, the testimony of witnesses often not only conflicted with other witnesses' testimony on the most basic of facts, but also was internally inconsistent; second, the parties were unable to produce many of the material records and documents.

[3]The WCCAA embraces that area of the City "as bounded by Tatnall Street on the east to Seventh Street, west on Seventh Street to West Street, north on West Street to Ninth Street, west on Ninth Street to Jefferson Street, north on Jefferson Street to Delaware Avenue, along Delaware Avenue to Adams Street, south on Adams Street to Front Street, east on Front Street to Washington Street, north on Washington Street to Second Street and east on Second Street to Tatnall Street." Bylaws of West Center City Neighborhood Planning Advisory Committee, Inc., Def.'s Ex. ("DX") 1 (hereinafter the "Bylaws"), Art. II.

[4]WCCNA serves the WCCAA except for the Quaker Hill and Trinity Vicinity neighborhoods. I note that there is evidence that would support the inference that WCCNA's mission involves all of the WCCAA.

[5]*Society Hill Towers Owners' Ass'n v. Rendell*, 20 F. Supp. 2d 855, 863 (E.D.Pa. 1998) (citing 42 U.S.C. §5301 *et seq.*; HCDA, Pub. L. No. 95-128, § 110(b); 91 Stat. 1125, codified as amended at 42 U.S.C. § 5318).

[6]42 U.S.C. §5318(a).

Delaware corporation; UDAG grants, which flow through WUC, provide most of the funding for WCCNPAC. This relationship was formally established when, in 1984, WCCNPAC and WUC entered into the UDAG Agreement.[7] Therefore, for the residents of the WCCAA, WCCNPAC is a critical and proximate link in the chain to distribute UDAG funds to enhance their community's economic and social well-being.

A motivational force behind the creation of WCCNPAC, with its more focused geographical scope, was the expectation that a more responsive and efficient program would evolve. In order to fulfill its role of fairly and efficiently distributing UDAG funds to its WCCAA constituency and representing the residents' interests, WCCNPAC needed to acquire and convey information accurately to WUC and other City and State bodies.[8] Both the information and decision-making functions required a process that accounted for the interests of the community. That could best be achieved if the governing body of WCCNPAC, at least in a general sense, was representative of the community. Accordingly, such democratic ideals were expressly set forth in the Bylaws, Article III of which provided:

> The objectives of WCCNPAC shall be:
>
> Section 1. To promote, in any way consistent with applicable Federal, State, and Local standards, the common good and general welfare of the residents of the WCCAA.
> Section 2. To serve as liaison between the several departments of the City of Wilmington or the State of Delaware and residents of WCCAA.

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[7]The funds granted pursuant to the UDAG Agreement have not been insubstantial. WCCNPAC has received funding of approximately $300,000 annually in UDAG grants. Thus, by early 1997, "over $2 million [had] been spent by WCCNPAC." Letter from The Hon. James Baker to Ms. Brenda Phillips, received Feb. 20, 1997 (hereinafter "Letter from The Hon. James Baker"), at 1. As a consequence of the UDAG Agreement, WCCNPAC is subject to numerous conditions and reporting requirements.

[8]The 1982 City Council resolution creating WCCNPAC (the "City Council Resolution") expressly noted the information-gathering function that WCCNPAC was to serve in the WCCAA: "WHEREAS, it is anticipated that this coalition of civic organizations will provide first-hand advisory information to the City regarding . . . matters regarding the future growth and direction of the West Center City neighborhood." City Council Resolution (June 10, 1982), Def.'s Answering Post-Trial Mem. Ex. A at 1. In a sense, one of WCCNPAC's primary purposes was to serve as an "umbrella" organization to coordinate and reconcile the interests of the various civic groups within the WCCAA. *See id.* Although not presented as an exhibit at trial, I take judicial notice of the City Council Resolution. *See* D.R.E. 201.

> Section 3. To represent residents of the WCCAA in appropriate matters which arise requiring discussion or negotiation between the City of Wilmington or the State of Delaware and any interests within the WCCAA.
> Section 4. To establish and maintain the means for collecting any funds flowing from the City of Wilmington to WCCNPAC or otherwise granted to WCCNPAC from any other source.

Thus, the concept of democratic representation goes to the very essence of WCCNPAC. If "form ever follows function,"[9] one would anticipate that the structure of WCCNPAC, through its certificate of incorporation and the Bylaws, would seek to guarantee that its directors are representative of the constituencies that they are selected to serve.

B. *The Structure of WCCNPAC*

The internal structure of WCCNPAC was designed to achieve these lofty goals of representation and public service. The Fourth Article of the WCCNPAC certificate of incorporation provides:

> FOURTH: The corporation shall not have any capital stock, and the conditions of membership shall be stated in the By-Laws of the Corporation.[10]

The Bylaws establish the right of various WCCAA civic organizations, including WCCNA, to participate in the governance of WCCNPAC. As "[c]omplete control of WCCNPAC" is "vested in the Board,"[11] the proper designation of those WCCNPAC directors is of paramount importance in assuring that the purposes of WCCNPAC are met.

Article IV of the Bylaws, which establishes the manner in which the directors are to be designated, provides in part:

> Article IV - Board of Directors
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> * * *

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[9]Louis Henri Sullivan, *quoted in* JOHN BARLETT, BARTLETT'S FAMILIAR QUOTATIONS 681 (15th ed. 1980).

[10]DX 10 at 2.

[11]Bylaws, Art. IV, § 1.

Section 2. Board of Directors. The Board of Directors shall include not less than six (6) and not more than nineteen (19) voting directors appointed from categories 1, 2, 3, 4 and 5 below. The Board of Directors may also include up to three (3) non-voting directors from category 6 below. Beginning in 1986, the non-profit agency in this category shall be recognized by the Board of Directors biannually to serve for a term of two (2) years.

1. First Category. Four (4) residents from [WCCNA]; these residents may not hold or be registered as a candidate for election to any elective public office or hold any paid appointive City office.

2. Second Category. Four (4) residents from the Trinity Vicinity Neighborhood Association; these residents may not hold or be registered as a candidate for election to any elective public office or hold any paid appointive City office.

3. Third Category. Four (4) residents from the Quaker Hill Neighborhood Association; these residents may not hold or be registered as a candidate for election to any elective public office or hold any paid appointive City office.

4. Fourth Category. One (1) resident from each of five (5) recognized block clubs within the WCCAA; these residents may not hold or be registered as a candidate for election to any elective public office or hold any paid appointive City office. The recognized block clubs are identified in Appendix A attached hereto and made a part hereof.

5. Fifth Category. One (1) representative from one (1) recognized non-profit agency resident in the WCCAA. The non-profit agency of this category shall be recognized by [the] Board of Directors annually to serve for a term of one year. The recognized non-profit

> agency is identified in Appendix A attached hereto and made a part hereof.
>
> 6. Sixth Category. Any member of City Council representing any portion of the affected neighborhoods may, upon written request and with the approval of the voting members of the Board, serve as an Ex-Officio Director, but Ex-Officio Directors shall have no voting right.

Appendix A to the Bylaws lists the "recognized block clubs" as: i) Penn Square Association, ii) Madison Lane Block Club, iii) Ninth Street Block Club, iv) 800 Block W. 5th Street Block Club, and v) 200 Block Club (collectively, the "Block Clubs").[12]

The operative power to designate WCCNPAC directors is found in Article IV, Section 3 of the Bylaws, which provides in pertinent part:

> Section 3. Appointment and Term of Office. Residents in the first, second, third and fourth categories shall be selected by their respective neighborhood organizations and shall serve for a term of two (2) years, unless removed pursuant to Section 8 of Article IV or until residence in the neighborhood has ceased.

A director may be removed by a greater than two-thirds vote of the Board "whenever, in [the Board's] judgment, the best interests of . . . WCCNPAC would be served thereby, but removal shall be without prejudice to the rights of the neighborhood association, block club, or agency experiencing the removal."[13] Additionally, "any Director not attending three (3) consecutive meetings may be considered to have abandoned his membership on the Board of Directors and may be removed by a two-thirds (2/3) plus one (1) vote of the Board."[14]

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[12]An amendment, dated November 25, 1996, added a sixth block club, West Village Neighborhood Association. Thus, a total of 19 voting director slots are to be filled. It is not clear from the record why these six Block Clubs were those granted the authority to designate members of the Board.

In addition to the designation process, the Bylaws, in Article V (Membership), set forth other qualifications to serve as a director by implicitly imposing on directors the requirements of WCCNPAC membership. Article V directs one to Appendix B; Appendix B requires voting members, *inter alia*, to "have their primary residence within the WCCAA" and to "submit [a] written application for membership."

[13]Bylaws, Art. IV § 8.

[14]*Id.*

C. *Problems Develop*

By the mid-1990s, however, WCCNPAC was beset by problems, problems so severe that the City and WUC threatened to halt funding of WCCNPAC. In February 1997, the then-City Council President wrote a letter in which he complained that "the members of WCCNPAC [have] had a great deal of difficulty organizing themselves into a well functioning administrative operation."[15] After severely criticizing WCCNPAC, the City Council President turned to WCCNA:

> West Center City Neighborhood Association is dead, with hardly anyone being involved. I have met with the board, committees, single board members, groups of board members but to no avail. They listen, nod their heads and go back to business as usual. I want to make it clear, the board members intend to do well and want to make their community better, but are confused as to how to do it."[16]

He concluded: "New leadership, new direction is absolutely necessary for a better future of a once great community."[17] The WUC board of directors also sent a letter to the Board, dated October 22, 1998, noting "growing concerns regarding [WCCNPAC]" which caused WUC to be "suspect of WCCNPAC's ability to carry out its commitment and fiduciary responsibilities to the residents of the [WCCAA] and the City."[18]

In response to these criticisms, WCCNPAC and WUC hired a consulting firm to recommend changes in order to increase efficiency. Among the improvements suggested were strict enforcement of the attendance policy for directors and elimination of the Block Clubs because the presence of the Block Clubs resulted in a disproportional representation of WCCNA.[19] Furthermore, the consultant characterized the Block Clubs as unrepresentative of the constituencies they were supposed to serve, as many of the Block Club designees were selected in an undemocratic

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[15]Letter from The Hon. James Baker at 1.

[16]*Id.*

[17]*Id.*

[18]DX 13 at 1. This letter informed the Board that the WUC board of directors was "prepared to take action . . . to suspend UDAG repayment funds until certain conditions have been met." *Id.* WUC further recommended that, *inter alia*, "WCCNPAC undertake . . . (a) a third party evaluation of the organization's programs. . .; [and] (b) evolve a newly formed (or reconfirmed) Board." *Id.* at 2.

[19]Most of the Block Clubs, including those represented in this proceeding, are within the area served by WCCNA.

fashion. Finally, the consultant recommended rotating directorships to combat a perceived entrenchment problem.

WCCNPAC then sought to implement the recommended changes. It began to enforce the attendance policy against its absent directors, and a unanimous decision[20] was made to remove non-attending directors.[21] WCCNPAC then sought from the Neighborhood Associations and the Block Clubs information about their selection processes and meetings, an effort that was largely unproductive. The Board also attempted to improve WCCNPAC's effectiveness through several amendments to the Bylaws, including a reduction in the number of directors. However, the procedures employed for achieving these changes in the Bylaws were deficient, and this Court declared those amendments invalid.[22]

Other problems also arose. For example, in July 2000, Davis was suspended after the Board received a letter from an attorney representing a clerical employee of WCCNPAC who set forth a complaint of sexual harassment against Davis. Davis was suspended by a unanimous vote at a special meeting; although Davis was notified of the special meeting and afforded the opportunity to state his position on the matter, he did not attend.[23] Since the suspension, no formal process for resolving Davis' status has been implemented.

D. *The February Appointments*

On February 6, 2002, a portion of the WCCNA board of directors (the "WCCNA board") met (the "February Meeting") and selected Ashe, Davis, Rhonda M. Davis and Chambers to be the WCCNA designees to the Board.[24] Before the February Meeting, the WCCNA designees to the Board

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[20]Thus, voting for the removal of the non-attending directors was Davis.

[21]The three Individual Plaintiffs removed for this reason on November 5, 1999, Trotter, Fields, and Turner, subsequently sought re-appointment to the Board. Their attempts were rebuffed by letters dated February 22, 2000, and the Board directed their respective Block Clubs to appoint different candidates. No new candidates emerged. No challenge is presented here to the validity of their removal in November 1999.

Not all directors appointed by the Block Clubs were removed for poor attendance. For example, the designee of the 800 Block West 5th Street Block Club remained on the Board since her record of attendance was not deficient.

[22]*See West Center City Neighborhood Ass'n, Inc. v. West Center City Neighborhood Planning Advisory Comm.*, 2002 WL 1403322 (Del. Ch. June 20, 2002).

[23]Davis had been previously removed from the Board for seeking his political party's nomination to run for New Castle County Council. He was reinstated after he lost.

[24]*See* Pls.' Ex. ("PX") 3 (hereinafter the "February 6th Minutes") at 2. Ashe, Davis and Chambers assert that they are directors of WCCNPAC by virtue of their selection as WCCNA designees.

had been Jacqueline B. Watson ("Watson"),[25] Zachariah Lingham ("Lingham"), Davis and Ashe.[26] The details of the February Meeting have been disputed by the parties. They debate whether the February Meeting was properly convened and conducted according to WCCNA' s bylaws. However, what is certain is that the only notice of the meeting was provided by Davis to eight people (Ashe, Trotter, Fields, McNeil, Turner, Bertha Lingham, Derrick El, and Marla Garris). Thus, Watson and Lingham, who were serving as directors of WCCNA and as representatives of WCCNA on the Board before the February Meeting, did not receive notice of the February Meeting.[27]

Thereafter, WCCNA forwarded to WCCNPAC a copy of a resolution, dated February 25, 2002,[28] endorsing the designees chosen at the February Meeting to serve as WCCNA representatives on the Board.[29] In a letter, dated April 15, 2002, WCCNPAC informed WCCNA and its designees that WCCNPAC "does not recognize those individuals listed on the February 25th Resolution [as the representatives of WCCNA] as members of the Board . . . and will not seat them."[30] The Individual Plaintiffs then met in order to consider what further steps should be taken, ultimately agreeing upon initiating litigation.[31] As a result, the Plaintiffs

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[25]Watson, who is the President of WCCNPAC, also claims to be President of WCCNA as the successor to Umar Khalif Hassan-El.

[26]There remains a question whether Ashe is an alternate member of the Board or is now a current Board member, after having succeeded her husband who was a WCCNA representative on the Board.

[27]In addition, at the February Meeting, a motion was made to revive the WCCNA corporate charter, which had lapsed for nonpayment of franchise taxes. February 6th Minutes at 2. A motion also passed to reestablish monthly meetings of WCCNA, "recognizing that there had not been a meeting called in quite some time." *Id.* at 1.

[28]PX 4 (hereinafter the "February 25th Resolution"). The February 25th Resolution purports merely to reiterate any resolution adopted earlier at the February Meeting. However, discrepancies exist between the two documents. *See infra* notes 29 and 31.

[29]It should be noted that while the February 25th Resolution lists only those designees properly selected by WCCNA, the February 6th Minutes also purport to designate, in the "[r]esolution to appoint," Trotter, Fields, Turner and McNeil. *Compare* February 25th Resolution at 1 *with* February 6th Minutes at 2. Even more puzzling is that the designation of these representatives, who should properly be appointed by their respective Block Clubs, seemingly asserts that these nominees are also from WCCNA. In the February 6th Minutes, the names of Board designees are followed by the name of the civic organization which purportedly nominated them. However, the names of Trotter, Fields, Turner, and McNeil are followed by, in addition to their respective Block Club, "WCCNA" in parentheses. *See* February 6th Minutes at 2. I note that WCCNA has no authority to appoint the Board representatives from the Block Clubs.

[30]PX 2 at 2.

[31]By this time, the Penn Square Association, the 200 Block Club, the Ninth Street Block Club, and the Madison Lane Block Club were operating under the umbrella of WCCNA. *See* February 25th Resolution at 1 (WCCNA "welcomes [these four] organizations in West Center under the structure of the WCCNA"). However, no such welcoming of these Block Clubs appears

have brought this suit seeking a declaration that the Individual Plaintiffs are entitled to be seated on the Board as representatives of WCCNA and the Block Clubs.

II. CONTENTIONS

The Plaintiffs commenced this action under 8 *Del. C.* §225, seeking a declaration that the Individual Plaintiffs are entitled to serve on the Board. The Plaintiffs claim that "[o]ver the years [WCCNPAC] has engaged in a pattern and practice of usurpation and failure to honor the selection of members to the Board by neighborhood organizations."[32] Furthermore, the Plaintiffs argue that "[t]he method of selection is a matter of the internal affairs of the selecting organization. WCCNPAC . . . has no authority or standing to interfere or officiously intermeddle into selection matters."[33] Therefore, according to the Plaintiffs, because the Individual Plaintiffs were selected in a manner consistent with the claimed practices of their respective neighborhood organizations, WCCNPAC should respect their appointments and recognize them accordingly.

WCCNPAC argues that the Individual Plaintiffs are not qualified under the Bylaws to serve as directors on the Board. WCCNPAC contends that the Individual Plaintiffs were not duly selected by WCCNA or their respective Block Clubs. It specifically asserts that the February Meeting "was not validly conducted and therefore all actions taken at such meeting are null and void."[34] Ultimately, WCCNPAC claims that, although "there is a paucity of case law" to guide the Court, "[l]ogic and common sense dictate that a community organization with the significant responsibilities of WCCNPAC must be permitted to demand of its constituent organizations that which is demanded of itself: that they be representative of the community."[35] WCCNPAC also interposes the equitable defense that the Plaintiffs are guilty of unclean hands.

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in the February 6th Minutes. *Compare* February 25th Resolution at 1 *with* February 6th Minutes.

[32]Pls.' Opening Br. at 2.

[33]Pls.' Bylaws Resp. at 2.

[34]Answer to Verified Compl. ¶ 21.

[35]Def.'s Answering Post-Trial Mem. at 4.

III. ANALYSIS

A. *The Right of WCCNPAC to Question the Selection Processes of the Neighborhood Organizations*

The Plaintiffs initially challenge the right of WCCNPAC to dispute the selection processes employed by the neighborhood organizations or to contest the designations of the Individual Plaintiffs by their respective nominating entities to serve on the Board. In substance, the Plaintiffs argue that the various organizations are given the right and the power to designate Board members and that the processes which each employs is of no concern to WCCNPAC.

The simple answer to the Plaintiffs' argument is that it is their burden in this action to demonstrate that the Individual Plaintiffs are entitled to serve on the Board.[36] In this instance, the Plaintiffs must demonstrate that the Individual Plaintiffs were duly selected by their respective neighborhood organizations. As an adverse party, WCCNPAC is free to question and to challenge whether the Plaintiffs can meet their burden.[37]

Moreover, at the core of WCCNPAC's existence is the need for the Board to be fairly representative, in a general sense, of the WCCAA community. If the processes used by the constituent organizations are so closed to their respective constituencies as to preclude any semblance of community involvement, WCCNPAC cannot credibly carry out its important public service functions. Thus, because the selection processes employed by the various nominating entities implicate important interests of WCCNPAC, it has the right to challenge whether its directors have been designated through a process that is inconsistent with the purposes for which it was formed as manifested in its corporate governance documents.

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[36]*Rohe v. Reliance Training Network, Inc.*, 2000 WL 1038190, at *16 (Del. Ch. July 21, 2000).

[37]I reject the Plaintiffs' arguments to the extent they implicate the concept properly called "standing." "The concept of "standing," in its procedural sense, refers to the right of a party to invoke the jurisdiction of a court to enforce a claim or redress a grievance. It is concerned only with the question of who is entitled to mount a legal challenge and not with the merits of the subject matter of the controversy.'" *Committee of Merchants and Citizens Against the Proposed Annexation, Inc. v. Longo*, 669 A.2d 41, 44 (Del. 1995) (quoting *Stuart Kingston, Inc. v. Robinson*, 596 A.2d 1378, 1382 (Del. 1991)). WCCNPAC is neither asserting a claim nor asking the Court to redress any grievance.

B. *The Selection Process*

The Plaintiffs seek a declaration that the Individual Plaintiffs are entitled to serve on the Board. This Court may determine the right of each of the Individual Plaintiffs to hold the office of director of WCCNPAC, a corporation without capital stock.[38] However, "although [plaintiffs] may obtain a personal benefit if their claims to office are sustained, a § 225 proceeding has long been recognized as serving the interests of the corporation as a whole."[39] The purpose of §225 "is to right wrongs done to a corporation, not to its individual stockholders, through the unlawful usurpation of its management and offices by persons not entitled thereto."[40] Thus, this litigation not only can be viewed as vindicating the rights of the Individual Plaintiffs to hold office, but also may be more broadly perceived as protecting against possible wrongs to WCCNPAC and its mission.

Because the structure of WCCNPAC is established by WCCNPAC's certificate of incorporation and the Bylaws, any determination of whether the Individual Plaintiffs are entitled to seats on the Board necessitates an analysis of those documents. "It is a fundamental principle that the rules used to interpret statutes, contracts, and other written instruments are applicable when construing corporate charters and bylaws."[41] Therefore, in construing the Bylaws, "[f]irst I look to the four corners of the [Bylaws] and, applying a common sense analysis, determine whether the [Bylaws are] reasonably subject to more than one interpretation."[42] "When the contract language, read in the context of the entire contract, is not reasonably susceptible to more than one meaning, this 'objective' meaning will govern."[43] If the language of the Bylaws is susceptible to only one meaning, I must confme my review to the face of the document.[44] In addition, the Bylaws "should be read as a whole and, if

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[38]8 *Del. C.* §225.

[39]*Kirby v. Kirby*, 1987 WL 14862, at *7 (Del. Ch. July 29, 1987).

[40]*Fleer v. Frank H. Fleer Corp.*, 125 A. 411, 416 (Del. Ch. 1924), *quoted in Kirby*, 1987 WL 14862, at *7.

[41]*Gentile v. SinglePoint Fin., Inc.*, 788 A.2d 111, 113 (Del. 2001); *see also Harrah's Entertainment, Inc. v. JCC Holding Co.*, 802 A.2d 294,309 (Del. Ch. 2002).

[42]*Supermex Trading Co. v. Strategic Solutions Group, Inc.*, 1998 WL 229530, at *2 (Del. Ch. May 1, 1998).

[43]*Bell Atl. Meridian Systems v. Octel Communications Corp.*, 1995 WL 707916, at *6 (Del. Ch. Nov. 28, 1995) (citations omitted).

[44]*Eagle Indus., Inc. v. DeVilbiss Health Care, Inc.*, 702 A.2d 1228, 1232 (Del. 1997); *McIlquham v. Feste*, 2002 WL 244859, at *5 (Del. Ch. Feb. 13, 2002).

possible, interpreted to reconcile all of the provisions of the document."[45] With this in mind, I turn to the specific text of the Bylaws.[46]

Article IV, Sections 2 and 3 of the Bylaws entitles WCCNA and the Block Clubs to designate a certain number of directors to serve on the Board. Article IV, Section 2 provides that the Board shall be comprised of "voting directors *appointed* from categories 1, 2, 3, 4, and 5."[47] Article IV, Section 3 directs that residents III the WCCNA, Trinity Vicinity Neighborhood Association, Quaker Hill Neighborhood Association, and the Block Clubs "shall be *selected* by their respective neighborhood organizations."[48] The Bylaws provide no express guidance or restrictions upon how the neighborhood organizations are to fulfill their role to "select" those representatives to serve on the Board. However, this seemingly unfettered grant of authority must not be interpreted in isolation, because the Bylaws are to be read as a whole. Therefore, Article IV, Section 3 must be interpreted in harmony with the other provisions of the Bylaws. The public character of WCCNPAC, as proclaimed in Article III, must not be forgotten amidst efforts to interpret the provisions of Article IV. To achieve its goals, WCCNPAC must fulfill one of its expressly stated purposes, that is, "[*t*]*o represent residents of the WCCAA* in appropriate matters which arise requiring discussion or negotiation between the City of Wilmington or the State of Delaware and any interests within the WCCAA."[49] Thus, the entitlement bestowed upon the neighborhood organizations by Article IV, Section 3 cannot be read so broadly as to permit actions by those neighborhood organizations in abrogation of the stated goal of representing the residents of the WCCAA. In sum, I conclude the unambiguous language conferring a right upon the neighborhood organizations to "select" directors to serve on the Board carries with it, by force of the Bylaws when read as a whole, the duty to

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[45]*Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 395 (Del. 1996).

[46]I acknowledge that applying the principles and spirit of the Delaware General Corporation Law to resolve a dispute concerning the non-profit entity before me creates some tension. Typically, corporate directors are selected by shareholders who base their decisions, in large part, upon their own economic self-interest. Here, the neighborhood organizations have no direct economic interest in WCCNPAC; they have been assigned the task of designating directors who can represent the interests of the neighborhood organizations and the residents of the neighborhoods in making decisions critical to the community. Thus, the interests which they may claim in the selection of WCCNPAC directors are different from those of shareholders who have invested in what they hope will be "for profit" corporations.

[47]Emphasis added.

[48]Emphasis added.

[49]Bylaws, Art. III, § 3 (emphasis added).

employ democratic processes in exercising that power to "select" directors.[50]

1. *Block Club Designees*

As provided by Article IV, Section 2, Sub-Section 4 the Block Clubs are each entitled to one representative on the Board. Purportedly, the Ninth Street Block Club selected Trotter, the 200 Block Club selected Fields, the Madison Lane Block Club selected McNeil, and the Penn Square Association selected Turner. The Block Clubs are rather informal organizations established to address the needs of a small community of neighbors, perhaps those living in an area of no more than a block in size. Membership is a function of where one resides. The purposes and activities of the Block Clubs may range from the practical – community beautification efforts – to the political – assuring adequate governmental services. Because they are informal organizations, it is not reasonable to expect strict compliance with any formal set of rules for their governance. However, I find from the evidence presented at trial, that, with the exception of Trotter, the processes used in selecting the Block Club designees were so deficient that they fail to provide any reasonable assurance as to the representative nature of the director's selection, thereby violating the Bylaws.

a. Trotter

Trotter was removed from the Board on November 5, 1999, for missing three consecutive meetings. After informal attempts at reconciliation with the Board, she returned and met with the Ninth Street Block Club. The Ninth Street Block Club includes the residents of the sixth block of West Ninth Street and consists, according to the unchallenged estimates of Trotter, of only seven or eight members.[51] Any

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[50]This is not to say that the selection process must comport with the fullest procedural strictures of, say, an election for state-wide office. I recognize that the size and character of the Block Clubs do not allow for such a requirement. Clearly, a variety of processes are scattered across the spectrum of possible methodologies that would lead to a representative selection. I venture no judgment as to the specific processes that must be followed by any particular neighborhood organization.

[51]Trotter initially testified that the Ninth Street Block Club also indirectly included the 500 block of West Ninth Street. However, because she stated under cross-examination that the Ninth Street Block Club was limited to the sixth block, I shall consider the Ninth Street Block Club to encompass only the sixth block of West Ninth Street. Trotter's testimony identifies two recurring problems with the Block Clubs: what territory do they serve and who are their members?

meetings have been informal, occurring at Trotter's residence or the local community center; records are sporadically kept and could not be produced at trial.[52] According to the uncontradicted testimony of Trotter, after she had been removed, a meeting at which she was reselected to represent the Ninth Street Block Club occurred in front of her house and was attended by five other constituents.[53] Trotter claims she volunteered to represent the Ninth Street Block Club, and those present accepted her offer. Thus, I find that, while not adhering to the strictest of procedures, such actions were adequate to assure the representation of the constituency of the Ninth Street Block Club, particularly in light of the relatively high percentage of members who attended the meeting. As such, the selection of Trotter to be the Ninth Street Block Club representative did not violate the Bylaws, and Trotter is entitled to recognition as a member of the Board.

WCCNPAC argues that, even if Trotter was validly elected by her respective Block Club, since she has been previously removed from the Board, she is precluded from being renominated. I reject WCCNPAC's argument. Nothing in the WCCNPAC certificate of incorporation or Bylaws prevents the renomination of a once removed director. While one would question the collective logic of a community group that continually re-designates a representative who does not attend meetings of the governing body, that is not the question before me. Thus, Trotter is entitled to serve on the Board.[54]

b. Fields

Fields is the purported President of the 200 Block Club, and has served on the Board for at least 10 years. She too was removed in

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[52]Nor could Trotter produce the document from the Ninth Street Block Club she claimed to have presented to the Board to demonstrate that she was the proper representative. She claimed that the records, to the best of her knowledge, were destroyed in a flood which inundated the basement where they were stored.

[53]Trotter could not remember its exact date. As no minutes or records were kept of this meeting, the date of this meeting and any details, other than the attendance and outcome of the vote as recalled by Trotter, are lost.

[54]I also reject WCCNPAC's equitable defense of unclean hands. The doctrine of unclean hands applies "when a party who seeks relief in this Court 'has violated conscience or good faith or other equitable principles in his conduct, then the doors of the Court of Equity should be shut against him.'" *E. J. Stephen, Inc. v. Ceccola*, 1984 WL 8238, at *2 (Del. Ch. July 9, 1984) (quoting *Bodley v. Jones*, 59 A.2d 463,469 (Del. 1947)), *quoted in SmithKline Beecham Pharms. Co. v. Merck & Co.*, 766 A.2d 442, 449 (Del. 2000). Here, WCCNPAC has not produced any evidence that Trotter has not acted in good faith. Thus, pursuant to my broad discretion in applying the doctrine of unclean hands, I reject WCCNPAC's argument. *See SmithKline Beecham Pharms. Co.*, 766 A.2d at 448 ("The Court of Chancery has broad discretion in determining whether to apply the doctrine of unclean hands.").

November 1999 for missing three consecutive meetings.[55] The 200 Block Club includes over 25 residents from the 200 block of Madison Street. While records were kept by its Secretary, Eva Carter, or by Fields, these too were destroyed in a deluge. Also destroyed in the deluge was the letter submitted to the Board by Fields, purportedly from the 200 Block Club, attesting that Fields was the 200 Block Club's chosen representative. Though Fields claimed that she was selected to be the Board representative for the 200 Block Club in 1982, and that she was reselected in subsequent annual meetings, she could not recall with any precision the year that she was last reselected to serve as the board representative of the 200 Block Club (or even any other details regarding her appointment).

Based upon the record before me, I am unable to find that Fields has satisfied her burden. The record, or lack thereof, surrounding her appointment falls well short of that required to sustain her burden. No description of any meeting was presented. No records were produced; not one document regarding the workings of the 200 Block Club was put forward. Fields could not recall with precision the year of her latest reappointment, and she did not testify about any procedures followed at any point in time that would remotely resemble democratic processes. As such, I find that Fields is not entitled to recognition as a member of the Board.

c. McNeil

McNeil is the purported President of the Madison Lane Block Club and claims to have represented the Madison Lane Block Club on the Board for approximately two to three years.[56] Prior to this, McNeil served as Vice-President of the Madison Lane Block Club and as an alternate to then-President and Board representative Derrick El.[57] McNeil assumed the presidency, with no election, of the Madison Lane Block Club when his brother moved outside of the Madison Lane Block Club's boundaries. Currently, McNeil is the only officer of the Madison Lane Block Club. Except for a miscellaneous letter irrelevant to issues at hand,[58] no records have ever been produced.[59]

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[55]Fields denies ever having received a letter from WCCNPAC notifying her of any action taken in response to her attendance problems.

[56]The frequency of McNeil's participation on the Board during this period is uncertain, although McNeil claims to have voted on several matters.

[57]McNeil is the brother of Derrick El.

[58]The letter informed Madison Lane Block Club constituents of WCCNPAC's proposal to increase the number of rental units, and the possible negative impact this would have upon property values.

[59]It is unclear whether McNeil was ever recognized by WCCNPAC as the proper

McNeil apparently seeks to justify through general theories of political succession his ascendance to the position of Board representative for the Madison Lane Block Club. Analogizing himself and his brother to Vice President Cheney and President Bush, respectively, McNeil testified that he was elected to serve as Vice-President and, therefore, is the successor to Derrick El.[60] No election was or has since been held. Although McNeil recalls being elected to the vice-presidency of the Madison Lane Block Club at one point, he claims that it was so long ago that he does not remember any of the details regarding the election. McNeil claims that he had at one point given WCCNPAC a letter declaring him to be the alternate for the Madison Lane Block Club; however, no such letter has been produced. Thus, no evidence has been produced explaining how McNeil became the Vice-President or the alternate Board representative. As such, I cannot find with any confidence that the processes by which McNeil claims his office at any point involved anything resembling a democratic process. Therefore, McNeil has not met his burden.

Essentially, any entitlement McNeil enjoys to serve on the Board stems from having been acknowledged for some period of time by the Board as representing the Madison Lane Block Club in some capacity.[61] However, this history does not negate the underlying, and more important, defect in McNeil's claim: McNeil has not demonstrated that he is the properly selected representative of the Madison Lane Block Club. One cannot circumvent the basic requirements of the Bylaws on the mere assertion that at some point one was acknowledged in an uncertain capacity and permitted to participate in the meetings. As such, McNeil is not entitled to recognition as a member of the Board.

d. Turner

Turner has been the President of the Penn Square Association since 1993. The Penn Square Association encompasses the 500 block and the 600 Block of West 3rd Street, and the 500 Block and 600 Block of Lafayette Boulevard, an area that includes approximately 120 people.[62]

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representative of the Madison Lane Block Club. What is more puzzling, and never fully explained by any party, is how and whether McNeil, whose votes as a Board member may have been counted, was ever removed from the Board.

[60]This logic also explains how McNeil now claims to be the current Board representative for the Madison Lane Block Club.

[61]Once again, testimony on this state of affairs has been inconsistent and conflicting.

[62]I acknowledge that the number of members of the various Block Clubs seems to vary widely.

Turner was removed from the Board in November 1999 for failure to attend three consecutive meetings.[63] By her admission under cross-examination, Turner stepped in and became President after the former President departed in 1993. Turner also admitted that the Penn Square Association has not had any meetings since 1994, although communications with the general membership have occurred by means of flyers placed on doors.[64] There are no officers of the Penn Square Association other than Turner. Turner believes that no notice need be provided to residents of any meeting of the Penn Square Association, or that she must request of her constituents that they select her to represent the Penn Square Association on the Board. Indeed, she herself typed the letter which was submitted to WCCNPAC claiming that she was the proper representative of the Penn Square Association. Apparently, she concluded that anytime she was removed by WCCNPAC, she could simply reselect herself.

I find that the processes, if any, used in selecting Turner as the representative of the Penn Square Association were so deficient as to violate any basic assurance of representative selection demanded by the Bylaws. Essentially, the reign of Turner has only been approved by Turner. Clearly, such practices are inconsistent with any notion of a democratic process producing a result representative of the community. Thus, Turner is not entitled to recognition as a member of the Board.

2. *The WCCNA Designees*

WCCNPAC also refused to acknowledge the validity of the representatives designated by WCCNA at the February Meeting. I find that only Ashe and Davis, who is subject to suspension, are entitled to recognition as members of the Board.

a. Ashe

"WCCNPAC considers Ms. Ashe to be an alternate [B]oard member from WCCNA."[65] As WCCNPAC concedes that there are two vacancies[66] among the director slots allocated WCCNA, "Ashe may attend

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[63]Turner also claims to have never received a letter from WCCNPAC notifying her of any attendance problems or action taken in response.

[64]These flyers apparently provided notice of Block Club activities and answered practical questions, such as trash collection on holidays.

[65]Def.'s Answering Post-Trial Mem. at 10.

[66]This treats Davis' suspension as having created a vacancy.

WCCNPAC and vote if she so chooses."[67] Therefore, I find that Ashe is entitled to recognition as a member of the Board.[68]

b. Davis

WCCNPAC conceded that "Davis is, and at all times relevant to this case, has been, a member of the [Board]."[69] Thus, "[a]side from his suspension, there is no dispute that . . . Davis represents WCCNA on the [Board]."[70] Because the issue of whether the suspension was validly imposed upon Davis was not raised in the complaint or the pre-trial stipulation, I refrain from deciding the merits of that issue.[71]

c. Chambers

Chambers, prior to the February Meeting, did not serve as a representative of WCCNA on the Board. Thus, his only claim to status as a director of WCCNPAC rests upon the validity of the February Meeting. Because I find that the February Meeting was improperly convened, Chambers is not entitled to recognition as a member of the Board.

While conflicting testimony was provided about the practices of WCCNA[72] in selecting its representatives to WCCNPAC, specifically,

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[67]Def.'s Answering Post-Trial Mem. at 10.

[68]While WCCNPAC contends that "Ashe is not entitled to a seat as a regular member from WCCNA for the reason that the alleged February [Meeting] appointing her as such was invalid," it does not argue that the processes that first installed Ashe as President of WCCNA and its representative to WCCNPAC somehow preclude her recognition even as an alternate. *Id.*

[69]*Id.* at 8.

[70]*Id.* at 9.

[71]I pause to note the obvious. Assuming that the suspension was a valid exercise of the Board's powers, the suspension should not serve as a permanent or even long-term solution to issues concerning Davis. A final resolution should be reached promptly in order to determine the extent of Davis' right to serve on the Board as the selected representative of WCCNA.

[72]WCCNA was unable to produce a copy of its bylaws despite WCCNPAC's diligent use of this Court's discovery rules. The record, following trial, was left open for submission of the WCCNA bylaws if they were discovered. Shortly after the period specified for submission of the WCCNA bylaws expired, WCCNPAC, through its efforts, was able to obtain a copy of the WCCNA bylaws. WCCNA nevertheless opposes the admission of its own bylaws because of the delay and because of unspecified questions about authenticity. I now admit the WCCNA bylaws as transmitted by the Defendant's Answering Post-Trial Memorandum into evidence. I do so because there is no prejudice to WCCNA; because I find unpersuasive WCCNA's unspecified argument with respect to authenticity; and because WCCNA had its chance to produce its own copy and failed to do so. WCCNA speculates that its bylaws may have been amended. I simply note that no one should be in a better position than WCCNA to produce any amendments, if, indeed, there ever were any. I do not, however, rely upon the WCCNA bylaws for any decision that I make.

whether historically the WCCNA President (Ashe)[73] or the WCCNA board made the selection, I find that the practice was that the WCCNA board selected the representatives to serve on the Board. The Plaintiffs have pointed to no provision in the WCCNA bylaws that grants the President such power.[74] Davis testified that the historical practice had arisen that the WCCNA President would appoint the directors to serve on the Board.[75] Yet, documentary evidence, in the form of the February 6th Minutes, evidences that a "[m]otion was made and seconded to appoint" the Individual Plaintiffs to serve on the Board.[76] Such a practice is inconsistent with the claimed custom of the selection power exclusively residing in the WCCNA President.[77] If anything, custom supports the testimony of Watson that the practice had been that the WCCNA board appointed the representatives to the Board. Thus, I find by a preponderance of the evidence that it is the practice for the WCCNA board, and not the WCCNA President, to select the directors to serve on the Board. Therefore, the issue becomes whether, given this past practice, the February Meeting can be considered properly convened.

Even if the issue of compliance with the WCCNA bylaws is ignored,[78] I, nevertheless, find that the February Meeting was not appropriately noticed. The Plaintiffs admit that notice, in the form of a telephone call from David, was only given to Ashe, Trotter, Fields, McNeil, Derrick El, Turner, Bertha Lingham, and Marla Garris.[79] Ashe admitted

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[73]Like many other facts in this case, even Ashe's Presidency of WCCNA is disputed and shrouded in mystery. Ashe claims to have been appointed President for life in 1984. However, conflicting evidence, in the form of a letter, dated August 6, 1998, with WCCNA letterhead, was produced evidencing that Umar Khalif Hassan El had been President for some period of time. No records exist as to Ashe's rise to power. Yet, I will assume for purposes of this discussion that Ashe is the current President of WCCNA. For a cryptic review of Watson's claim that she is WCCNA's President, *see supra* note 25.

[74]Though not dispositive, it is interesting to note that appointing WCCNA representatives to the Board is not among the WCCNA President's enumerated powers. *See* West Center City Neighborhood Association, Inc., Bylaws, Art. VIII, § 1.

[75]Davis claims that the authority for such a practice is derived from Bylaws, Article 9, Section 3, which states that "[o]ne member of each committee shall be appointed by the President to be chairman of that committee." I merely note that this section provides no authority for the practice of the alleged WCCNA President Ashe selecting the delegates herself.

[76]February 6th Minutes at 2.

[77]Davis claims that the appointments were made before the February Meeting. However, no documentation was produced corroborating this statement. Furthermore, Davis failed to satisfactorily explain what the purpose of the motion, and the seconding of that motion, then served.

[78]As noted above, however, WCCNA was not able to produce its ow bylaws. Furthermore, serious questions have been raised, and serious defects have been admitted, with respect to compliance with the quorum requirements and the requirement of holding regular meetings of both the WCCNA board and WCCNA's general membership.

[79]Davis also gave personal notice to the same individuals.

that notice should have been given to Watson and Lingham, who were being replaced as WCCNPAC directors and, thus, had an obvious interest in the outcome of any such proceeding.[80] Providing notice of the February Meeting solely to a limited group that did not even include all of WCCNA's directors silences the properly heard voices of the WCCNA constituency and provides no assurance that the will of the people is heeded.[81] Given this lack of notice, I cannot find that the appointment of Chambers was a proper exercise of the WCCNA board's historic or intrinsic powers. Therefore, Chambers is not entitled to recognition as a member of the Board.

CONCLUSION

For the foregoing reasons, Trotter, Ashe and Davis are entitled to entry of judgment confirming their status as members of the Board. WCCNPAC is entitled to entry of judgment in its favor as to the claims asserted by the other Individual Plaintiffs of a right to serve on the Board.[82]

An order will be entered in accordance with this memorandum opinion.[83]

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[80]Notice is all the more important if one believes Watson was then President of WCCNA.

[81]"[T]he rationale of the requirement for notice . . . is not only to convenience directors, but also to assure that the corporate body, including its stockholders, is given the 'benefit of the judgment, counsel and influence of all' of its directors." *Schroder v. Scotten, Dillon Co.*, 299 A.2d 431, 435 (Del. Ch. 1972) (quoting 2 FLETCHER, CYCLOPEDIA CORPORATIONS § 406).

[82]Nothing in this memorandum opinion prevents these Individual Plaintiffs from being re-designated by their respective Neighborhood Associations or Block Clubs to serve on the Board, as long as an appropriate selection process is employed.

[83]These conclusions resolve the dispute presented for decision. They do not, however, address the larger questions of how WCCNPAC should be structured to carry out its significant functions or whether, given its existing structural limitations, it can reasonably be expected to meet its objectives. These questions are beyond the scope of this memorandum opinion; indeed, they are questions which should be answered in the appropriate political forum.

ZIMMERMAN v. BRADDOCK

No. 18,473-NC

Court of Chancery of the State of Delaware, New Castle

December 20, 2002
Revised December 31, 2002

R. Bruce McNew, Esquire, of Taylor & McNew, Greenville, Delaware; and Robert B. Weiser, Esquire, and Eric L. Zager, Esquire, of Schiffrin & Barroway, LLP, Bala Cynwyd, Pennsylvania, of counsel, for plaintiff.

Bruce L. Silverstein, Esquire, Christian Douglas Wright, Esquire, and Danielle Gibbs, Esquire, of Young Conaway Stargatt & Taylor, LLP, Wilmington, Delaware; and Evan R. Chesler, Esquire, and Daniel Slifkin, Esquire, of Cravath, Swaine & Moore, New York, New York, of counsel, for defendants priceline.com incorporated, Richard S. Braddock, and Daniel H. Schulman.

Anne C. Foster, Esquire, and Catherine G. Dearlove, Esquire, of Richards, Layton & Finger, Wilmington, Delaware, for defendants Jay S. Walker, Paul A. Allaire, Ralph M. Bahna, Paul J. Blackney, William E. Ford, Marshall Loeb, N.J. Nicholas, Jr., and Nancy B. Peretsman; Martin Glenn, Esquire, of O'Melveny & Myers LLP, New York, New York, of counsel, for defendant Jay S. Walker; Steven B. Rosenfeld, Esquire, of Paul, Weiss, Rifkind, Wharton & Garrison, New York, New York, of counsel, for defendant William E. Ford; and Sheldon H. Elsen, Esquire, of Orans, Elsen & Lupert LLP, New York, New York, of counsel, for defendant Marshall Loeb.

NOBLE, *Vice Chancellor*

Plaintiff Mark Zimmerman (the "Plaintiff") initiated this shareholder derivative action on behalf of the Nominal Defendant priceline.com Incorporated ("priceline" or the "Company") against Defendants Richard S. Braddock ("Braddock"), Jay S. Walker ("Walker"), Daniel H. Schulman ("Schulman"), Paul A. Allaire ("Allaire"), Ralph M. Bahna ("Bahna"), Paul J. Blackney ("Blackney"), William E. Ford ("Ford"), Marshall Loeb ("Loeb"), N. J. Nicholas, Jr. ("Nicholas"), and Nancy B. Peretsman ("Peretsman") (collectively, the "Individual Defendants"), who

along with Heidi G. Miller ("Miller"), constituted priceline's board of directors (the "Board') at the time of the original complaint.[1]

Plaintiff alleges in his June 21, 2001, Amended Derivative Complaint (the "Complaint") that Braddock, Walker, and Nicholas (collectively, the "Selling Defendants") breached their fiduciary duties by engaging in insider trading and misappropriating confidential corporate information. Furthermore, the Complaint asserts that the Individual Defendants, in their failure to exercise good faith and loyalty in the performance of their duties, including the dissemination of misleading information regarding the Company, have proximately caused significant harm to the Company in litigation claims, the repricing of certain warrants, and the loss of goodwill in the marketplace. Finally, the Plaintiff claims that, as no consideration was received, the Selling Defendants' use of priceline's confidential information during the course of their alleged insider trading, and the Individual Defendants' failure to act, constituted corporate waste. Because of the damages sustained by the Company, Plaintiff seeks the imposition of a constructive trust over the profits reaped by the Selling Defendants and damages from the Individual Defendants for the alleged breaches of fiduciary duties and acts of corporate waste.

The Individual Defendants have moved to dismiss this action pursuant to Court of Chancery Rules 23.1 ("Rule 23.1) and 12(b)(6) ("Rule 12(b)(6)"). They contend that the Plaintiff has failed to plead particularized facts excusing his failure to make a demand upon the Board. Furthermore, even if demand is excused, the Individual Defendants argue that the allegations of the Complaint fail to state a claim upon which relief can be granted.

As set forth in this memorandum opinion, I conclude that the Plaintiff has not alleged sufficient facts with particularity to excuse demand and, therefore, this action must be dismissed under Rule 23.1.

I. BACKGROUND

A. The Company

Priceline, a Delaware corporation with executive offices in Connecticut, was founded by Walker in July 1997 and began operations in April 1998. The Company principally provides a self-described "Name Your Own Price" Internet pricing system. Using this system, customers can establish the price of travel, automotive, home finance, and

[1]Plaintiff is, and has been at all relevant times, a shareholder of priceline.

telecommunications products they seek to purchase. The Company's stock, since a successful March 1999 initial public offering, has been traded on the NASDAQ.

The origins of the "Name Your Own Price" technology lie in another Walker-founded venture. In 1998, Walker Digital Corporation ("Walker Digital"), a privately-held "think tank" founded by Walker, developed and patented the "demand collection system," an e-commerce pricing system that is the basis of the "Name Your Own Price" technology.[2] After being licensed to priceline by Walker Digital, the technology was first harnessed to sell airline tickets, a product which by May 2001 still generated 98% of priceline's revenues. The demand pricing system purportedly creates value by "enabl[ing] consumers to use the Internet to save money on products and services while at the same time enabling sellers to generate increased incremental revenue."[3]

B. Individual Defendants and Interconnected Companies

The licensing of the demand collection system by Walker Digital to priceline is not the only instance of a connection between priceline and a business entity of one of the Individual Defendants. In fact, a review of the myriad linkages alleged among priceline, the Individual Defendants, and companies affiliated with the Individual Defendants, is necessary to understand the basis for the Plaintiffs claims and my decision regarding whether demand is excused.

1. Walker

Walker was the driving force in the evolution of priceline. In addition to founding priceline, Walker served as the Company's Chief Executive Officer (until August 1998) and Vice Chairman of the Board (from August 1998 until January 2001). Walker, also, was the founder of and "is the largest equity owner and the Chairman of the Board [of Directors] of Walker Digital."[4] In turn, Walker Digital owned

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[2]Through the demand collection system, as implemented with the "Name Your Own Price" technology, priceline satisfies consumer demand collected over the Internet. Customers convey offers, guaranteed by a credit card and held open for a specified period of time, for a particular product or service. Priceline then communicates such offers directly to participating sellers or determines, from accessing participating sellers' private databases, whether the offer can be met.

[3]Pl.'s Compl. ¶ 27.

[4]*Id.* ¶ 7. Significantly, the Plaintiff never states what percentage of Walker Digital equity is controlled by Walker.

approximately 35% of priceline at the time (November 1, 2000) the initial complaint was filed in this action.[5] In addition to his ongoing involvement with Walker Digital, Walker serves as the non-executive Chairman of the Board of Directors of the Synapse Group, Inc. ("Synapse"). Synapse, co-founded as NewSub Services, Inc. ("NewSub") in 1992 by Walker and Michael Loeb,[6] is a privately-held direct marketing firm through which priceline offers magazine subscription services. Walker owns approximately 11.5% of Synapse.[7]

2. Braddock

Braddock, one of priceline's original investors, has served as Chairman of the Board (since August 1998) and as Chief Executive Officer (resuming his duties after the termination of Schulman in May 2001). Braddock had previously served as Chief Executive Officer from August 1998 through May 2000, when he resigned as Chief Executive Officer to spend more time with Walker Digital. "Braddock is a director and one of the largest equity owners of Walker Digital, having personally invested at least $20 million in Walker Digital."[8] Like Walker, in addition to his involvement with Walker Digital, "Braddock is also a substantial equity owner and director of [Synapse]."[9] In 1999, Braddock received options to purchase an underlying 35,000 shares of Synapse common stock, at a strike price of $8.00 per share (the "Synapse Options").

Braddock's involvement with the connected business entities does not end with Walker Digital and Synapse. Braddock also serves as a director of WebHouse Club, Inc. ("WebHouse"), a privately-held, "Name Your Own Price" website for groceries and other retail items which figured significantly in priceline's attempt to diversify the products it offered. WebHouse was an independent licensee of priceline; in consideration for the Company's licensing its name and business model, WebHouse agreed to a royalty arrangement and granted a fully-vested, non-forfeitable warrant to the Company to acquire a majority stake of WebHouse, exercisable under certain conditions (the "WebHouse Warrant"). Walker Digital owned a 34% stake in WebHouse.[10] Braddock also served as a special

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[5] *Id.* ¶ 6.

[6] *Id.* ¶ 13. Michael Loeb is the son of Defendant Loeb.

[7] *Id.* ¶ 8.

[8] *Id.* ¶ 6. Again, significantly, the Plaintiff fails to note the percentage of Walker Digital equity controlled by Braddock.

[9] *Id.*

[10] *Id.*

advisor to General Atlantic Partners, LLC ("General Atlantic"), and invested (as a limited partner) in several General Atlantic partnerships.[11]

3. Nicholas

Nicholas, the third of the Selling Defendants, is connected to both the Company and Synapse. He has been a director of priceline since July 1998. Additionally, he serves a director of Synapse and, either personally or through affiliated entities, "is also a substantial equity owner of Synapse."[12] Like Braddock, Nicholas was granted the Synapse Options.[13]

4. Blackney

Blackney has been a director of priceline since July 1998. Furthermore, Blackney serves as President and Chief Executive Officer of Worldspan LP ("Worldspan"), a position he has held since October 1999. Worldspan is a privately-held, global travel distribution system ("GDS") and was the exclusive GDS booking agent for customers of priceline.[14] "Priceline entered into an amendment to its subscriber agreement with Worldspan pursuant to which Worldspan paid [p]riceline three million dollars . . . in exchange for [p]riceline's committing to a certain minimum volume of bookings for the five year term of the agreement."[15] As such, priceline remains one of Worldspan's "biggest clients."[16]

5. Ford

Ford has been a director of priceline since July 1998, and also serves on the boards of both Walker Digital and Synapse.[17] Additionally, he is Managing Member of General Atlantic. General Atlantic has actively invested in priceline and entities connected to various Individual

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[11]Braddock's relationship with General Atlantic is significant because Ford, another priceline director, is Managing Member of General Atlantic. In addition, Braddock and Ford serve together as directors of E* Trade Group, Inc., a company that has a marketing agreement with priceline.

[12]Pl.'s Compl. ¶ 8.

[13]Nicholas also serves on the board of directors of Xerox Corporation ("Xerox"). Allaire, another priceline director, is the Chairman of Xerox's board of directors and its Chief Executive Officer.

[14]During the period 1998-2000, priceline sold in excess of 6,000,000 airline tickets through Worldspan. In 1998, Worldspan's revenues equaled $637.3 million.

[15]Pl.'s Compl. ¶ 11.

[16]*Id.*

[17]Like Braddock and Nicholas, Ford received the Synapse Options.

Defendants. During the course of 1998, General Atlantic purchased 21,581,059 shares of priceline stock.[18] It then sold 6,567,130 shares of priceline common stock, for $356,555,000, during January and February of 2000.[19] General Atlantic also owns 17.5% of privately-held Synapse.[20] Finally, General Atlantic also has invested in privately-held priceline.com Europe.

6. Peretsman

While Peretsman has served as a director of the Company since February 1999, the Plaintiff alleges that her principal professional occupation is that of Managing Director and Executive Vice-President of Allen & Company, Inc. ("Allen & Co."), an investment banking firm. Peretsman had previously served as a director of NewSub and currently serves as a director of Synapse.[21]

Allen & Co. has had significant financial dealings with priceline and companies connected to the Individual Defendants. It purchased 275,000 shares of priceline stock, at $4.00 per share, in priceline's third round of private financing (completed on December 8, 1998), and received $850,000 in consulting fees from the Company in 1999. Allen & Co. has also provided services to Synapse. It was scheduled to be one of the lead underwriters in the initial public offering planned for Synapse, an offering eventually canceled in December 2000. Synapse also generated for Allen & Co. $750,000 in consulting fees. Finally, "Allen & Co[.] was an investor in NewSub and, along with Peretsman, is one of the largest equity owners of Synapse."[22]

Peretsman, and the entities with which she is affiliated, sold 204,641 shares of priceline common stock, for proceeds of $15,225,807 in March and April of 2000.

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[18]This investment occurred in three separate transactions. In February 1998, an affiliate of General Atlantic purchased from priceline 2,854,875 shares of priceline common stock at $.70 per share. Next, in August 1998, "two partnerships affiliated with General Atlantic purchased 17,288,684 of [p]riceline stock" during the Company's second round of private financing at a price per share of $1.16. Lastly, in December 1998, "two partnerships affiliated with General Atlantic purchased 1,437,500 shares of [p]riceline stock"in the Company's third round of private financing at a per share price of $4.00. Pl.'s Compl. ¶ 12.

[19]*Id.*

[20]*Id.* General Atlantic affiliates had invested in excess of $59 million in NewSub. *Id.*

[21]Peretsman, along with Braddock, Wallace, Nicholas and Ford, collectively constitute a majority of the Synapse board of directors. Peretsman, as did Braddock, Nicholas, and Ford, received the Synapse Options.

[22]Pl.'s Compl. ¶ 14.

7. Loeb

Loeb has been a director of the Company since July 1998. Additionally, Loeb was an equity investor in NewSub, a company that his son, Michael Loeb, co-founded with Walker, who is now its chairman, Michael Loeb is now an employee of Synapse. Loeb has also invested in excess of $3 million in Synapse. Both Loeb and his son are affiliated with the Loeb Family Limited Partnership, an entity that owns approximately 8.23% of Synapse.[23]

8. Schulman

Schulman served as President, CEO and director of priceline until his termination in May 2001.[24] Upon starting work at the Company, on June 14, 1999, Schulman and priceline entered into an employment agreement (the "Schulman Agreement"). The terms of the Schulman Agreement established that Schulman reported directly to Braddock, was to receive a minimum base salary of $300,000 annually, was granted 3,000,000 options to purchase priceline common stock, and was loaned $6,000,000 by priceline.[25]

9. Miller

Miller, who is not a defendant in this action, served as the Chief Financial Officer and as a director of priceline for the period of February through November 2000, when she resigned. Plaintiff alleges that at the time of the filing of the original complaint, this employment at priceline was Miller's principal profession. Miller entered into an employment agreement with the Company on February 18, 2000 (the "Miller Agreement"). The Miller Agreement provided that Miller would report directly to Braddock, would receive a minimum base salary of $300,000 annually, would receive 2,500,000 options to purchase priceline common stock, and would be loaned $3,000,000 by priceline.[26]

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[23] *Id.* ¶ 13.

[24] Schulman, who was appointed Chief Executive Officer in June 2000, had served as a director of priceline starting in July 1999.

[25] Priceline subsequently (during the fourth quarter of 2000) forgave the loan in its entirety.

[26] This loan, like that to Schulman, was forgiven in its entirety in November 2000.

10. Allaire

Allaire has served as a director of priceline since February 1999. He also is the Chairman of the Board and Chief Executive Officer of Xerox.

11. Bahna

Bahna has served as a director of the Company since July 1999.

* * *

Thus, many of the Individual Defendants can be connected to one another through various entities outside of priceline. These entities, in turn, often have significant business dealings with, or own a percentage interest in, priceline.

C. Problems Emerge

Although priceline enjoyed initial success, at least as measured by the market's reception of its initial public offering and subsequent trading activity, the Company soon recognized that it would need to diversify the product base embraced by its "Name Your Own Price" system to encompass more than airline tickets.[27] Therefore, during September 1999, it was announced that groceries would be available for "Name Your Own Price" purchasing at WebHouse, starting November 1, 1999, in New York City. Walker publicly commented on the future growth prospects of priceline and WebHouse, noting that priceline "will continue its rapid growth in the travel, financial services and automotive sectors while the WebHouse Club focuses its resources entirely to the retail-store segment of buyer-driven commerce."[28] WebHouse's strategic role went beyond that of diversifying
the product base; Wall Street analysts and Company executives viewed WebHouse as a test for the scalability of the priceline business model. Positive remarks flowed from priceline management.[29]

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[27]In September 1999, airline tickets accounted for 92% of priceline's revenue.

[28]Pl.'s Compl. ¶ 34 (quoting Sept. 21, 1999, Company press release).

[29]Walker publicly stated that "'[t]he rapid expansion of [WebHouse] 's grocery service . . . demonstrates the scalability of [WebHouse].'" *Id.* ¶ 37 (quoting a June 8, 2000, Company press release). A July 25, 2000, priceline press release claimed that WebHouse was "'America's leading Internet service for groceries.'" *Id.* ¶ 44. Walker also noted during an August 1, 2000, conference call that "WebHouse would achieve positive gross margins in both groceries and

While self-congratulatory praise abounded, what investors could not gather were hard facts regarding the financial condition of WebHouse. Despite only realizing $33,777 in revenues from royalties pursuant to the WebHouse licensing structure, priceline recognized $188.8 million in income (the WebHouse Warrant's estimated fair value) upon the receipt of the WebHouse Warrant in the fourth quarter of 1999. Because WebHouse was privately-held, investors (and those interested in priceline's convertible interest in WebHouse) needed to rely solely upon information provided by priceline. And what that information allegedly masked was the failure of WebHouse. Around January 2000, senior management at WebHouse and Braddock voiced concerns regarding technological, financial, and conceptual problems with WebHouse.[30] Yet, WebHouse's launch continued at its scheduled pace. The Plaintiff alleges that the reason why WebHouse was launched, and the reason why the Synapse-WebHouse Agreement was entered into, was that, "despite the serious concerns raised by both senior WebHouse management and Braddock . . . due to the power that Walker exercised over both [p]riceline and WebHouse, his vote was the only vote that counted."[31]

Adding to priceline's woes was increased competition from the airlines themselves. On June 29, 2000, six major carriers announced the creation of a new online ticket service at Hotwire.com ("Hotwire"). While essentially offering surplus airline seats at cheap prices, much like priceline, Hotwire allowed greater consumer choice as now customers could designate the specifics of their flight and dictate a set price.[32] Other travel websites that did not use the "Name Your Own Price" bidding concept also arose.[33]

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gasoline by the end of the year," and that he believed that "'[WebHouse] demonstrates yet again just how scalable the [priceline] business model really is.'" *Id.* ¶ 45.

[30]An example of the troubles plaguing WebHouse cited by the Plaintiff was the "partnership agreement" entered into between WebHouse and Synapse (the "Synapse-WebHouse Agreement"). Synapse was to solicit consumers into trial magazine subscriptions in exchange for tokens redeemable for savings at WebHouse. Yet while customers signed up, and thus received the tokens for WebHouse, they did not renew their subscriptions. Furthermore, these "token users" were not returning to WebHouse once the "token savings" were expended. This deal was struck at Walker's insistence and despite the objections of WebHouse managers. *Id.* ¶¶ 48-50.

[31]*Id.* ¶ 47.

[32]Priceline "require[d] customers to commit to purchasing tickets before knowing the exact scheduled time of departure, scheduled time of arrival, and other material details." *Id.* ¶ 52.

[33]Examples include Expedia.com and Travelocity.com.

D. The Alleged Wrongful Conduct

The Plaintiff contends that from March 1999 through September 2000, "the Individual Defendants made a series of inaccurate and misleading public statements regarding [p]riceline's financial condition, business, and future growth prospects,"[34] allegedly in the face of the known reality that the Company "could not match the hyper-aggressive public guidance . . . provided to Wall Street."[35] Walker is alleged to have minimized the threat of the increased competition from Hotwire and other travel websites.[36] Plaintiff contends that, while stating publicly that priceline would achieve profitability imminently or in the near future,[37] the Individual Defendants "knew that [p]riceline's revenues and earnings were under tremendous pressure due to, *inter alia*, increased competition and loss of customers."[38] Also regarding priceline's business condition, the Plaintiff alleges that the Individual Defendants portrayed the Company's customer base as satisfied and growing,[39] when in fact the Individual Defendants knew of increasing customer dissatisfaction and a shrinking customer base. Moreover, the Individual Defendants allegedly made misleading public misstatements regarding the prospects of the critical WebHouse venture; the Individual Defendants publicly stated that WebHouse had been successful, thereby demonstrating the scalability of the priceline business model.[40] In fact, the Individual Defendants were aware of technological, financial and conceptual problems experienced by WebHouse. Thus, the Plaintiff complains that numerous misleading statements were made to the public regarding the business condition and prospects of priceline.[41]

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[34]Pl.'s Ans. Br. in Opp'n to Defs.' Joint Mot. to Dismiss at 3.

[35]*Id.* at 4.

[36]For example, Walker predicted that "Hotwire would 'not really' compete with [p]riceline because Hotwire 'is not a name your own price website.'" Pl.'s Compl.¶ 54 (quoting a June 29, 2000, interview on the Fox News Network).

[37]For example, Schulman claimed that priceline was "'rounding the final turn and on the home stretch towards profitability.'" *Id.* ¶ 58. Miller told *Bloomberg News* that "'[p]riceline could be profitable now, but we are investing in our growth.'" *Id.* ¶ 59.

[38]Pl.'s Ans. Br. in Opp'n to Defs.' Joint Mot. to Dismiss at 3.

[39]For example, Schulman noted that priceline "'continue[d] to attract record new customers, but even more importantly, our loyalty among existing customers is accelerating.'" Pl.'s Compl. ¶ 58. He later noted in a July 24, 2000, interview with Fox News, that priceline is "'really focused on assuring that we have the best value proposition—a unique one that generates great satisfaction for customers.'" *Id.* ¶ 60.

[40]*See supra* note 29. Additionally, Schulman claimed "'[p]riceline has a wonderful model . . . . That type of model would play exceptionally well in a downturned economy.'" Pl.'s Compl. ¶ 59 (quoting a July 24, 2000, appearance on CNBC financial news network).

[41]Plaintiff also complains that the Individual Defendants made misleading public

This series of misleading statements ultimately afforded the Selling Defendants the opportunity about which Plaintiff now principally complains. In August and September of 2000, the Selling Defendants collectively sold in excess of 10 million shares of the Company's stock, reaping collective proceeds of more than $247 million.[42] These sales were executed based on material, non-public information concerning the truth about the Company's profitability and customer base, the increased competition facing the Company, and the troubles besetting WebHouse. In particular, it is alleged that Walker needed to inflate the market value of his priceline holdings in order to use the proceeds from the sales executed at artificially high levels to support WebHouse.[43]

Soon after the completion of the alleged insider trading by the Selling Defendants, the market learned the truth regarding the Company's condition. On September 27, 2000, the Company warned that its revenues and earnings would fall short of Wall Street's projections.[44] On October 5, 2000, priceline announced that WebHouse would be suspending operations for 90 days.[45] Therefore, the Plaintiff concludes that because of the materially inaccurate and misleading statements made by the Individual Defendants, priceline has suffered damages in the form of the profits reaped by the Selling Defendants who allegedly engaged in insider trading, liability and costs incurred in connection with defending securities suits, and a deterioration of the Company's goodwill.[46]

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statements that they were "'very comfortable'" with priceline's condition and future. *Id.* ¶ 71(f).

[42]The Plaintiff alleges that on August 1, 2000, Walker sold 8 million shares of priceline's common stock, netting $190 million. That same day, Nicholas exercised 200,000 priceline options (at $0.80 per share), and then sold 100,000 shares of priceline's common stock for $2,519,000. The following day, acting as trustee of a family trust, Nicholas sold another 100,000 shares of priceline's common stock, earning $2,532,000. On August 15, 2000, Braddock exercised his priceline options (at $0.80 per share) and then sold 72,000 shares of priceline's common stock, for proceeds of $1,764,720. The next day, Braddock again exercised priceline options (at $0.80 per share) and sold 28,000 shares of priceline's common stock for proceeds of $692,160. Walker sold another 2 million shares of priceline's common stock, this time for a total of $50 million, on September 11, 2000. *Id.* ¶¶ 61, 62, 69, 70.

[43]*Id.* ¶ 55.

[44]Upon this release, priceline's stock plummeted 42% to establish a 52-week low of $10.75 per share.

[45]The day of this release, priceline's stock plunged another 38% to close at 5 13/16.

[46]Plaintiff contends that another consequence of the misleading stockholders was a $9 million charge absorbed by priceline for re-pricing warrants held by Delta Airlines. Pl.'s Compl. ¶ 92.

2. ANALYSIS

Plaintiffs failure to make a demand upon the Board prior to initiating this action necessitates a threshold inquiry into whether the particularized facts alleged in the Complaint demonstrate that demand would have been futile. A fundamental precept of Delaware corporate law is that the board of directors, not the shareholders, manages the corporation;[47] this managerial autonomy for decision-making extends to the determination to initiate litigation to vindicate the rights of the corporation.[48] Rule 23.1, regulating the encroachment on management's sphere of decision-making presented by shareholder derivative suits, has been characterized as the "procedural embodiment of this substantive principal."[49]

Rule 23.1, in pertinent part, provides:

> In a derivative action brought by 1 or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, the complaint shall . . . *allege with particularity* the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and the reasons for the plaintiffs failure to obtain the action or for not making the effort."[50]

However, a complaining shareholder need not always make a demand upon a corporation's board of directors. In this case, because the Complaint alleges that the Company's directors breached their fiduciary duties by failing to act, as opposed to a conscious decision to act or abstain from acting, the proper test for determining demand futility is "whether or not the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint is

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[47]8 *Del. C.* § 141(a).

[48]*White v. Panic*, 783 A.2d 543, 546-47 (Del. 2001).

[49]*Rales v. Blasband*, 634 A.2d 927, 932 (Del. 1993). Rule 23.1 is designed, among other things, to provide the corporation with the opportunity to address the alleged wrong without litigation and to bestow control over the litigation if such litigation is indeed brought for the corporation's benefit. *In re Delta & Pine Land Co. S'holders Litig.*, 2000 WL 875421, at *5 (Del. Ch. June 21, 2000).

[50]Emphasis added.

filed, the board of directors could have properly exercised its independent and disinterested business judgment in responding to a demand."[51]

Critical to my resolution of this case is the particularity requirement of Rule 23.1. "Pleadings in derivative suits . . . must comply with stringent requirements of factual particularity that differ substantially from the permissive notice pleadings governed solely by Chancery Rule 8(a)."[52] In deciding whether demand is excused, I am limited to those particularized facts alleged in the Complaint, not those set forth only in the briefs.[53] Furthermore, at this stage in the proceedings, I accept as true the particularized facts of the Complaint, and the Plaintiff is entitled to all reasonable logical inferences drawn from those particularized facts.[54] However, "conclusory allegations are not considered as expressly pleaded facts or factual inferences."[55] With these standards in mind, I turn to deciding whether the Complaint has set forth such particularized facts so as to excuse the demand requirement of Rule 23.1.

At the time of the filing of the original complaint, the Company's board consisted of eleven directors.[56] Thus, in order to excuse demand as futile, Plaintiff must allege particularized facts raising a reasonable doubt as to the independence or disinterestedness of at least six of the Company's directors. Because I find that the allegations set forth in the Complaint have not done so, Defendants' motion to dismiss under Rule 23.1 is granted.[57] "Directorial interest exists whenever divided loyalties are present, or a director either has received, or is entitled to receive, a personal financial benefit from the challenged transaction which is not equally shared by the stockholders."[58] Defendants do not dispute for the purposes of this motion that the three Selling Defendants are interested in light of the Complaint's allegations that they wrongfully profited by trading on inside information. Because Plaintiff does not argue that any of the eight remaining directors are interested for purposes of demand excusal

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[51] *Rales*, 634 A.2d at 934.

[52] *Brehm v. Eisner*, 746 A.2d 244, 254 (Del. 2000) (citations omitted).

[53] *Orman v. Cullman*, 794 A.2d 5, 28 n.59 (Del. Ch. 2002). For example, Plaintiff asserts in his brief that he "has alleged that Walker is the . . . *majority* equity owner of Walker Digital." Pl.'s Ans. Br. in Opp'n to Defs.' Mot. to Dismiss at 13 (citing Pl.'s Compl. ¶¶ 6-7) (emphasis added). The paragraphs of the Complaint referenced by Plaintiff allege, instead, only that Walker is the "largest equity owner" of Walker Digital.

[54] *Pogostin v. Rice*, 480 A.2d 619, 622 (Del. 1984), *overruled on other grounds*, *Brehm*, 746 A.2d. 244.

[55] *Brehm*, 746 A.2d at 255.

[56] In addition to the ten directors named as defendants in this case, the eleventh director of priceline at the time this action was initiated was Miller.

[57] Thus, I need not address Defendants' motion to dismiss under Rule 12(b)(6).

[58] *Pogostin*, 480 A.2d at 624 (citing *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984)).

analysis,[59] I turn to an assessment of the particularized facts in the Complaint to determine if they raise a reasonable doubt as to the independence of those directors from the interested Selling Defendants.[60]

"Independence means that a director's decision is based on the corporate merits of the subject before the board rather than extraneous considerations or influences."[61] In arguing that at least six of the remaining eight directors are not dependent for the purposes of this inquiry, Defendants assert that Plaintiff has failed to demonstrate that the interested directors held the power to control "unilaterally" the positions, dealings, and holdings of many of the remaining directors. In support of this argument, Defendants point to *Orman v. Cullman* for the proposition that:

> A director may be considered beholden to (and thus controlled by) another when the allegedly controlling entity has the *unilateral* power (whether direct or indirect through control over other decision makers), to decide whether the challenged director continues to receive a benefit, financial or otherwise, upon which the challenged director is so dependent or is of such subjective material importance to him that the threatened loss of that benefit might create a reason to question whether the controlled director is able to consider the corporate merits of the challenged transaction objectively.[62]

Contrary to Defendants' unduly restrictive reading of the above quoted passage, *Orman* is clear in providing that a director's independence may be called into question when the allegedly controlling director 'has the power, whether solely in his own capacity or in conjunction with others who share his purpose, to exert pressure on the challenged director of such a nature as to compromise that challenged director's ability to consider the merits of a demand for suit objectively.[63]

The Plaintiffs arguments can be generally characterized as asserting that the Selling Defendants exerted control over a majority of the Board through various interconnected entities controlled or dominated by the Selling Defendants. Of course, this line of argument presumes that the *particularized facts* of the Complaint establish that such entities were, in

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[59]*See* Pl.'s Ans. Br. in Opp'n to Defs.' Joint Mot. to Dismiss at 11-28.

[60]Plaintiff does not offer any argument that the alleged misstatements of the Individual Defendants affect the determination of whether demand was necessary. *See id.*

[61]*Aronson*, 473 A.2d at 816.

[62]*Orman*, 794 A.2d at 25 n.50 (emphasis added).

[63]*Id.*; *see also Telxon Corp. v. Meyerson*, 802 A.2d 257, 264 (Del. 2002).

fact, controlled or dominated by the Selling Defendants, individually or collectively. Thus, my resolution of demand futility begins with a determination of which, if any, entities have been shown by the Plaintiffs particularized facts to be controlled or dominated by the interested Selling Defendants.[64]

A. Entities Controlled by the Selling Defendants

The particularized facts of the Complaint, and the reasonable inferences drawn therefrom, fail to establish that the Selling Defendants directly or indirectly controlled priceline. The Plaintiff alleges in the Complaint that Walker was the Company's founder and that he served first, as the Company's Chief Executive Officer until August 1998, and, second, as the Vice-Chairman of the Board from August 1998 until January 2001. The Complaint, however, is silent as to Walker's personal equity interest in priceline. The Complaint also sets forth that Braddock, a long-serving director of priceline who has served as the Company's Chairman of the Board since 1998, is the Company's Chief Executive Officer, having resigned in May 2000, and having been subsequently reinstated approximately six months before the initiation of this action. Additionally, he is also alleged to have been one of the Company's "original investors." However, the Complaint, as with its treatment of Walker, contains no allegations as to Braddock's specific personal equity interest in priceline. Finally, Nicholas is merely alleged to serve as a director of the Company. As such, the Complaint fails to state any particularized facts from which I can draw the inference that the Selling Defendants directly controlled priceline. I am unable even to fathom a guess as to what percentage of priceline is owned by the three interested directors. Furthermore, their positions alone are not sufficient to exert control over the Company.[65]

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[64]As stated previously, the Defendants do not contest that Walker and Braddock, along with Nicholas, are interested for the purposes of this motion. The discussion that follows focuses on the allegations in the Complaint as to Walker and Braddock's investments, positions, relationships, and dealings in order to lay the necessary foundation for my analysis of the independence of the remaining directors vis-à-vis Walker and Braddock. Because Plaintiff does not seriously argue that Nicholas controlled or dominated the business affairs of priceline or the members of the Company's board, the specific allegations as to Nicholas' dealings are not discussed separately in this section. Instead, any relevant allegations about Nicholas are explored in my analysis of the director defendants who are alleged to have been under the control of the Selling Defendants, including Nicholas.

[65]I note that this determination is in light of the fact that Walker's tenure as priceline's CEO ended in August 1998, more than two years before Plaintiff initiated this action.

Therefore, it must be determined whether the Selling Defendants controlled priceline through their control of other, connected entities, namely Walker Digital and Synapse.

Were the Selling Defendants sufficiently alleged to control Walker Digital, an entity that owns 35% of priceline, it could be argued that they indirectly control priceline.[66] While the Complaint does allege that Walker "is the largest equity owner" of Walker Digital, and sets forth that Walker Digital owns approximately 35% of priceline, the Complaint is devoid of any allegation as to Walker's specific personal interest in Walker Digital. The bald allegation that Walker "is the largest equity owner" of Walker Digital does not provide the factual predicate necessary for an inference that he was the controlling equity holder of that company.[67] In an even weaker fashion, the Complaint also alleges Braddock to have been "one of the largest equity owners of Walker Digital." Thus while Braddock is detailed to have "personally invested at least $20 million in Walker Digital," no facts are plead that could establish his percentage ownership in that entity. Therefore, given the positions of Walker and Braddock, and the absence of any particularized facts as to their holdings in Walker Digital as pleaded in the Complaint, I am unable to conclude that the Selling Defendants controlled Walker Digital, an entity that arguably could be said to exert material influence over priceline.

Shortcomings of the Complaint also prevent me from ascertaining that the Selling Defendants, through their involvement with Synapse, control priceline. The Complaint sets forth that Walker is the non-executive Chairman of Synapse's board of directors and the owner of 11.5% of Synapse. Additionally, the Plaintiff alleges that Braddock is "a substantial equity owner" as well as a director of Synapse. Finally, like Braddock, Nicholas is alleged to be a director and "a substantial equity owner of Synapse."[68] However, the particularized facts of the Complaint fail, on two levels, to demonstrate that the Selling Defendants could exert control over priceline. Even assuming that the Selling Defendants were able to control Synapse, an assumption that is not supported by the allegations of the Complaint, I cannot conclude that control of Synapse would have enabled the Selling Defendants to exert material influence over

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[66]As the Plaintiff has alleged no relationship between Nicholas and Walker Digital, I will only address the possible control exerted by Walker and Braddock over Walker Digital.

[67]He could, for example, be a 5% owner in Walker Digital, and the other investors in that entity be owners of yet smaller stakes. *See, e.g., Moran v. Household Int'l, Inc.*, 490 A.2d 1059, 1070 (Del. Ch. 1985) (noting that the defendant corporation's largest shareholder held "approximately 5% of its stock").

[68]The Complaint also specifies the Braddock and Nicholas were each granted the Synapse Options.

priceline and its directors.[69] More specifically, there simply are no allegations as to Synapse's equity interest in priceline from which one can conclude that the individuals in control of that company could influence the affairs or directors of priceline.

Accordingly, I am of the opinion that the Complaint alleges insufficient particularized facts from which a reasonable inference may be drawn that the interests and positions of the interested directors, whether individually or collectively, empowered them with the means to dominate and control the Board and affairs of priceline, Walker Digital or Synapse.[70]

B. The Independence of Individual Defendants

1. Peretsman

Plaintiff argues that the independence of Peretsman, a director of the Company since 1999, is called into question on account of (1) her substantial and material investments in and directorial positions with entities controlled by Walker and Braddock and (2) her principal employment as a managing director and executive vice-president of Allen & Co., an investment banking firm that purchased and sold shares of the Company's stock, received consulting fees from the Company averaging $800,000 in 1999 and 2000, and was scheduled to be one of the lead underwriters for Synapse's since cancelled initial public offering.

The Complaint alleges that Peretsman previously served as a director of NewSub and now serves as a director of Synapse. Peretsman is further alleged to have been granted the Synapse Options in connection with her board position with that company. Having previously concluded that the Complaint's allegations as to Walker and Braddock's relationships with Synapse were insufficient to conclude that either could, or collectively could, unilaterally influence that company's affairs, I fail to see how the Complaint's allegations regarding Peretsman's options in Synapse and dealings with that company call into question her ability to act

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[69]I note, by way of example, the absence of any particularized allegations addressing Synapse's equity interest in, or business dealings with, the Company (i.e., that Synapse's marketing services were material to the affairs, success, or viability of priceline).

[70]Having concluded that the record before me precludes a finding for this motion's purposes that Walker and Braddock in their individual capacities could control priceline and its board, I acknowledge the possibility that the two individuals (along with Nicholas for that matter) could collectively dominate the affairs of the Company. Based on the allegations of the Complaint, however, Plaintiff has failed to plead particularized facts calling into question the interested directors' collective abilities to do so for most, if not all, of the same reasons set forth in the above analysis of those directors in their separate capacities.

independently of Walker and Braddock. Moreover, a director's holdings in a given company do not *ipso facto* cast into doubt that director's ability to act independently of an allegedly dominating director and/or shareholder of that company. If anything, "[tlhe only reasonable inference that . . . can [be] draw[n] . . . is that [t]he shareholder-director in question] is an economically rational individual whose priority is to protect the value of his . . . shares."[71] Of course, this discussion presupposes that Walker, Braddock, or Nicholas controlled the companies that Peretsman is alleged to have substantially invested in.

If one concludes for the purposes of this motion, as I have, that the Complaint contains insufficient particularized facts from which an inference may be drawn that Walker and Braddock controlled priceline, the allegations as to Peretsman's principal employment with Allen & Co. and the consulting fees that Allen & Co. received from priceline fail to rebut the presumption that Peretsman would have acted independently as well. Even assuming that the fees were material to Allen & Co. or that Peretsman derived a material personal benefit from them, however, the Plaintiff must demonstrate that Peretsman was beholden to Walker or Braddock on account of their supposed ability to affect the continued services generating those fees. Because of my finding that Plaintiff has failed to set forth particularized facts establishing Walker and Braddock's control over the affairs of priceline, I find that the Complaint's allegations fail to raise a reasonable doubt as to Peretsman's ability to act independently and impartially in her capacity as a director of priceline.

2. Ford

Plaintiff argues that Ford, who serves as Managing Member of General Atlantic, lacks independence for the purposes of this motion on account of the Synapse Options granted to him in connection with his directorship with that company and the fact that General Atlantic and its affiliates have invested heavily in priceline, Synapse and Walker Digital. Specifically, the Complaint alleges that General Atlantic invested over $59 million in NewSub, owns approximately 17.5% of Synapse, and is "one of the largest equity owners of Walker Digital." Ford also serves as a director of Walker Digital and Synapse.

Having found the absence of particularized facts from which one may reasonably conclude that Walker or Braddock controlled Synapse, there is no factual predicate from which one may infer that the options

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[71] *In re the Walt Disney Co. Deriv. Litig.*, 731 A.2d 342, 356-57 (Del. Ch. 1998), *rev'd on other grounds sub nom. Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

granted to Ford are attributable to the control of either of those individuals. As such, Ford's receipt of the Synapse Options fails to establish that either Braddock or Walker had the power to assert control or domination over him as a director of priceline. Moreover, the allegation that General Atlantic and its affiliates invested heavily in priceline (or entities with interests in priceline) does not militate in favor of Plaintiffs requisite showing because the mere investment in those companies does not suggest that the Walker or Braddock had dominion over Ford. With respect to Ford's directorships with Walker Digital and Synapse, allegations as to one's position on multiple boards does not in and of itself call into question one's independence from an interested director sitting with him on such boards. Accordingly, Plaintiff has failed to set forth particularized facts raising a reasonable doubt as to Ford's ability to act objectively as a director of priceline.

3. Loeb

The Complaint alleges that Loeb was an equity investor in Synapse and that company's predecessor (NewSub). The Complaint further alleges that Michael Loeb, Loeb's son, co-founded NewSub in 1992 with Walker and that his position with Synapse serves as his principal employment.

As stated previously, the Complaint's allegations as to Walker's position as the non-executive Chairman of Synapse with an interest of less than 12% in that company, without more, fails to create a record from which one may conclude that he dominates the business affairs of Synapse or the employment of that company's employees. The same holds true of Braddock who, like Walker, is alleged to be a substantial equity owner of Synapse.[72] Having already found that Peretsman and Ford are not beholden to the Selling Defendants, Plaintiff's argument that Loeb's son is "beholden to defendants Walker, Braddock, Nicholas, Ford and Peretsman, who collectively make up a majority of the Synapse Board,"[73] is unpersuasive. Even if Loeb's son were somehow "beholden" to all five individuals collectively, the Plaintiff has not alleged any basis for the Court to conclude that Ford and Peretsman, who are not under the control of the Selling Defendants, based on the allegations of the Complaint, would join with the Selling Defendants in any effort within Synapse that would somehow adversely affect Loeb's son and, thus, affect Loeb's independence

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[72]The Complaint alleges that "Walker, Braddock, Ford (through General Atlantic), . . . Nicholas (and/or entities with whom he is affiliated), and Peretsman are all substantial equity owners of Synapse, each having invested millions of dollars in Synapse." Pl.'s Compl. ¶ 100(e).

[73]*Id.*

as a priceline director. Consequently, Loeb's son's position with Synapse does not call into question Loeb's ability to act independently of Walker, Braddock or Nicholas for the purposes of this motion. Regarding Loeb's investments in Synapse, as stated in my analysis of Peretsman and Ford, a director's investment in another company allegedly controlled by the same individual who is said to be a dominating force in the company under analysis does not suggest, without more, that the investing director lacks independence. As such, I conclude that Plaintiff has alleged insufficient particularized facts to raise a reasonable doubt as to Loeb's independence.

4. Miller

The Complaint alleges that priceline served as Miller's principal employment and that "at the time this action [was] initiated, . . . [she] was preparing to leave her employment with [p]riceline and was beholden to defendants Braddock and Walker to approve the terms of her departure."[74] Having previously found that Plaintiff has alleged insufficient particularized facts from which a reasonable inference can be drawn that Braddock or Walker exerted control over the Company, I fail to see how Miller could be beholden to them, especially considering that Miller was leaving her position with the Company. While Plaintiff argues that Miller was beholden to Walker and Braddock on account of their influence over her departing compensation package, again, Plaintiff has alleged insufficient particularized facts calling into question their ability to dominate or control the terms of her departure. For this reason, the Complaint's allegations as to priceline's forgiveness of $3 million of Miller's personal debt (and the options granted to her by the Company to purchase priceline stock) also fail because there are insufficient allegations from which one can conclude that Walker or Braddock had the power to compromise the presumptive independence of Miller.

5. Bahna

The Complaint merely alleges that Defendant Bahna has served as a director or the Company since July 1999. With nothing more, this fact fails to impugn the independence of Bahna with respect to evaluating any demand to vindicate the Company's rights. Plaintiff does not contend that Bahna is not independent.

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[74] *Id.* ¶ 100(d).

6. Allaire

While the Complaint notes that Defendant Allaire is a director of the Company and also serves as Chairman of the Board of Directors and CEO of Xerox Corporation, an entity for which Nicholas serves as a director, nothing in the Complaint or the Plaintiffs arguments can be viewed as seriously contending that the Selling Defendants exerted material influence over Allaire. Thus, on these limited allegations, I consider Allaire to be independent for purposes of determining whether demand is excused. As with Bahna, the Plaintiff does not challenge Allaire's independence.

* * *

Because the Plaintiff has failed to allege particularized facts raising a reasonable doubt as to the independence or disinterestedness of at least six of priceline's eleven directors, the Plaintiff has not met his burden under Rule 23.1 to justify excusing his failure to make a demand on the Board.[75]

3. CONCLUSION

For the foregoing reasons, Defendants' motion to dismiss under Rule 23.1 for the Plaintiffs failure to make pre-suit demand on the Board is granted. Dismissal is without prejudice.[76] An order will be entered in accordance with this memorandum opinion.

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[75]My finding that the Plaintiff has not met his burden with respect to the independence or disinterestedness of six of priceline's eleven directors obviates the need to consider the status of Schulman and Blackney.

[76]I conclude that dismissal with prejudice would not "be just under the circumstances" because of the complex and intertwined relationships among priceline, the Individual Defendants, and the various entities with which they are associated and because of the apparently non-public status of certain facts, the absence of which may have materially affected the outcome. Court of Chancery Rule 15(aaa). It is appropriate to remember the admonition of Justice Hartnett in his concurring opinion in *Brehm v. Eisner*: "Plaintiffs must not be held to a too-high standard of pleading because they face an almost impossible burden when they must plead facts with particularity and the facts are not public knowledge." 746 A.2d at 268 (Hartnett, J., concurring).