

2011-194626

STATE OF SOUTH CAROLINA
IN THE
SUPREME COURT

RECEIVED

JUL 07 2011

S.C. SUPREME COURT

Appeal From The Court Of Common Pleas
For Greenville County
The Honorable Edward W. Miller, Circuit Court Judge
C.A. No. 2008-CP-23-2701

South Carolina Court of Appeals
Opinion No. 4810, filed March 23, 2011

Brian P. Menezes,

Petitioner,

v.

WL Ross & Co. LLC, Wilbur, L. Ross, Jr., Michael J. Gibbons,
David H. Storper, David L. Wax, Joseph L. Gorga, Stephen B.
Duerk, WLR Recovery Fund II, L.P., WLR Recovery Fund III, L.P.,
WLR Recovery Associates II LLC, and WLR Recovery
Associates III LLC,

Respondents.

APPENDX TO
PETITION FOR WRIT OF CERTIORARI

William D. Herlong, Esquire
THE HERLONG LAW FIRM, LLC
Post Office Box 2003
Greenville, South Carolina 29602
Telephone: 864.382.3801
Telecopier: 864.752.0820
E-Mail: william@herlonglaw.com

Thomas L. Stephenson, Esquire
NEXSEN PRUET, LLC
Post Office Drawer 10648
Greenville, South Carolina 29603
Telephone: 864.370.2211
Telecopier: 864.477.2620
E-Mail: tstephenson@nexsenpruet.com

Attorneys for the Petitioner
(see over)

Russell T. Burke, Esquire
NEXSEN PRUET, LLC
1230 Main Street, Suite 700
Columbia, South Carolina 29201
Telephone: 803.771.8900
Telecopier: 803.253.8277
E-Mail: rburke@nexsenpruet.com

Stephen P. Groves, Sr., Esquire
NEXSEN PRUET, LLC
205 King Street, Suite 400
Charleston, South Carolina 29401
Telephone: 843.720.1725
Telecopier: 843.414.8206
E-Mail: sgroves@nexsenpruet.com

Attorneys for the Petitioner

TABLE OF CONTENTS

	<u>Page</u>
Table of Contents	ii
<u>Menezes v. WL Ross & Co., LLC, ___ S.C. ___,</u> 709 S.E.2d 114 (Ct.App. 2011) (Westlaw version)	1
<u>Menezes v. WL Ross & Co., LLC, ___ S.C. ___,</u> 709 S.E.2d 114 (Ct.App. 2011) (South Carolina Judicial Dept. version).....	10
Petition for Rehearing with Petition for Rehearing <u>En Banc</u> dated and filed 7 April 2011	20
Memorandum in Support of Petition for Rehearing with Petition for Rehearing <u>En Banc</u> dated and filed 7 April 2011	34
Motion to Supplement Record on Appeal dated and filed 7 April 2011	73
South Carolina Court of Appeals Order Denying Motion to Supplement the Record on Appeal dated and filed 12 April 2011	92
Appellants' Return to Respondent's Petition for Rehearing dated 21 April 2011	94
South Carolina Court of Appeals Order Denying Petition for Rehearing (<i>per curiam</i>) dated and filed 1 June 2011	108
Letter from Renee S. Johnson to Russell Thomas Burke, Esquire dated 1 June 2011 (indicating the Court of Appeals had denied the Petition for Rehearing <u>En Banc</u>)	110

709 S.E.2d 114
(Cite as: 709 S.E.2d 114)

▷

Court of Appeals of South Carolina.
Brian P. MENEZES, Respondent,

v.

WL ROSS & CO. LLC, Wilbur L. Ross, Jr., Michael J. Gibbons, David H. Storper, David L. Wax, Joseph L. Gorga, Stephen B. Duerk, WLR Recovery Fund II, L.P., WLR Recovery Fund III, L.P., WLR Recovery Associates II LLC, and WLR Recovery Associates III LLC, Appellants.

No. 4810.

Heard Oct. 6, 2010.

Decided March 23, 2011.

Rehearing Denied June 1, 2011.

Background: Shareholder and former chief financial officer (CFO) of surviving corporation brought breach of fiduciary duty action against investment firm which owned shares in both the acquired corporation and the surviving corporation. Investment firm counterclaimed for breach of release that shareholder signed when settling employment action against surviving corporation. The Circuit Court, Greenville County, Edward W. Miller, J., dismissed investment firm's counterclaim and struck its affirmative defense of release. Investment firm appealed.

Holding: The Court of Appeals, Konduros, J., held that issue of whether shareholder's breach of fiduciary duty claim accrued before he signed release in employment action could not be resolved on motion to dismiss.

Reversed and remanded.

Pieper, J., concurred and filed an opinion.

West Headnotes

[1] Pretrial Procedure 307A ⚡624

307A Pretrial Procedure

307AIII Dismissal

307AIII(B) Involuntary Dismissal

307AIII(B)4 Pleading, Defects In, in General

307Ak623 Clear and Certain Nature of Insufficiency

307Ak624 k. Availability of relief under any state of facts provable. Most Cited Cases

The question on a motion to dismiss a counterclaim is whether in the light most favorable to the complainant, and with every doubt resolved on his behalf, the counterclaim states any valid claim for relief. Rules Civ.Proc., Rule 12(f).

[2] Corporations and Business Organizations 101 ⚡3187

101 Corporations and Business Organizations

101XIII Foreign Corporations

101XIII(A) In General

101k3186 Subjection to Requirements as Imposed by State of Incorporation; What Law Governs

101k3187 k. In general. Most Cited Cases

Generally, the rights and obligations of stockholders, including the relative rights of stockholders as respects the corporation itself, are determined and controlled by the law of the state of incorporation.

[3] Pretrial Procedure 307A ⚡644

307A Pretrial Procedure

307AIII Dismissal

307AIII(B) Involuntary Dismissal

307AIII(B)5 Particular Actions or Subject Matter, Defects in Pleading

307Ak644 k. Corporations and associations; bank and trust companies; securities. Most Cited Cases

Issue of whether breach of fiduciary duty claim, asserted by shareholder and former chief financial officer (CFO) of surviving corporation against investment firm that owned shares in both the surviving corporation and the acquired corporation, accrued before or after shareholder signed release in his em-

709 S.E.2d 114
(Cite as: 709 S.E.2d 114)

ployment action against surviving corporation, which release barred shareholder from bringing any claim based upon ownership of a stock interest arising prior to execution of release, could not be resolved on motion to dismiss investment firm's affirmative defense of release and firm's counterclaim for breach of release; merger agreement was executed before shareholder signed release in employment action, a majority of surviving corporation's shareholders had indicated they would approve merger agreement, and once merger agreement was signed shareholder had a legally enforceable right to enjoin merger.

*115 H. Sam Mabry, III, Charles M. Sprinkle, III, and James Derrick Quattlebaum, all of Greenville; Michael J. McConnell and Joseph E. Finley, of Atlanta, Georgia and N. Scott Fletcher, of Houston, TX, for Appellants.

William D. Herlong, of Greenville, for Respondent.

KONDUROS, J.

W.L. Ross & Co., LLC (WLR) and several of its board members (Appellants) ^{FN1} appeal the circuit court's striking of two of their defenses and dismissal of their counterclaim in the direct shareholder lawsuit filed by Brian **Menezes**. We reverse and remand.

^{FN1} Stephen B. Duerk was not a member of the board but was president of SCI and executed the merger agreement on its behalf.

FACTS/PROCEDURAL BACKGROUND

Safety Components International, Inc. (SCI) was a publicly traded Delaware corporation with its headquarters in South Carolina. SCI was in the business of designing and manufacturing airbag fabric and airbag cushions. From 1999 to 2006, **Menezes** was employed by SCI as Chief Financial Officer, and for a time, interim Chief Executive Officer. He was terminated from his employment with SCI in June of 2006 but remained a shareholder. **Menezes** sued SCI to recover additional severance pay he alleged he was due and a "change of control" bonus included in his employment contract.

While **Menezes's** employment lawsuit was proceeding, SCI entered into discussions with the former International Textile Group, Inc. (FITG), a privately held Delaware corporation headquartered in North Carolina, about a possible merger. ^{FN2} WLR, an in-

vestment firm, owned shares in both SCI and FITG, either directly or indirectly through affiliate entities.

^{FN2} FITG refers to International Textile Group prior to the merger with SCI. After the merger, the newly formed entity took the name International Textile Group.

On August 29, 2006, the SCI board of directors approved the merger agreement between SCI and FITG. The merger agreement provided that FITG would merge into SCI and that SCI's certificate of incorporation would be amended to reflect the new combined entity. FITG shareholders would receive one share of SCI stock for every 1.4379 shares of FITG stock surrendered. ^{FN3} The terms of the merger were made public via a press release and the filing of a Form 8-K with the Securities and Exchange Commission (SEC) on August 30 and again on September 1, when a preliminary Joint Proxy Statement/Prospectus was filed with the SEC. A final Proxy Statement was mailed to stockholders on September 25, 2006. According to the Proxy Statement, FITG stockholders needed to take no action to effect the merger as a majority of stockholders had approved it in writing contemporaneous with the signing of the merger agreement. The Proxy Statement also indicated "no action by the stockholders of SCI is required to approve the merger agreement or to consummate the merger." SCI stockholders did need to satisfy a condition precedent by agreeing to amend the certificate of incorporation to reflect the existence of the newly formed entity and by re-electing five of the current board members. However, according to the Proxy Statement, "stockholders of SCI holding approximately 75.6% of SCI's outstanding common stock have indicated that they intend to vote to adopt the amended and re-instated certificate of incorporation--and--to--elect--the--directors--nominated--for--re-election. Approval of the matters to be voted on at the 2006 Annual Meeting is therefore assured."

^{FN3} According to **Menezes's** complaint, this exchange ratio had the effect of significantly diluting SCI stockholders' ownership in the newly formed entity.

On September 28, 2006, in exchange for payments totaling approximately \$575,000, **Menezes** signed a Settlement Agreement and Release of All Claims (the Release) to settle the employment law-

709 S.E.2d 114
(Cite as: 709 S.E.2d 114)

suit. The Release stated *116 **Menezes** agreed to “re-release, acquit and forever discharge” defendants of:

Any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which plaintiff either has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is [p]laintiff's intention to release all rights and claims that he may lawfully release.

The Release specifically barred **Menezes** from bringing “any claim based upon or as an owner of any stock or interest ... arising prior to the execution” of the Release and from pursuing any claims “made or which may have been made” in the employment lawsuit.^{FN4} On October 20, 2006, the merger between SCI and FITG was completed in that all pre-conditions were either satisfied or waived.

^{FN4} Appellants argued to the circuit court that **Menezes** could have brought his shareholder claim in the employment lawsuit. **Menezes** provided opposing counsel with a draft amended complaint in the employment lawsuit. That amended complaint contains an allegation, although stricken through, that the proposed merger agreement was made on unfair terms.

Menezes brought this lawsuit in 2008 alleging breaches of fiduciary duties on the part of the Appellants in the following particulars:

- (a) by proposing the [m]erger and then allowing it to close notwithstanding the financial condition of FITG;
- (b) by approving the [m]erger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders to 35%, or at all [sic];
- (c) by not providing accurate and complete information regarding FITG ... or ensuring that such in-

formation was provided to them;

(d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account or see that it was taken into account with regard to the [m]erger;

(e) by failing to ensure that proper due diligence was conducted on behalf of SCI or FITG;

(f) by allowing the representation at the [m]erger closing that MAC ^{FN5} Clause condition was satisfied;

^{FN5} MAC stands for materially adverse changes.

(g) by failing to call off or renegotiate the [m]erger (or cause it to be called off or renegotiated) because of the financial condition of FITG;

(i)[sic] by allowing the debt previously held by FITG to be transferred to Combined Company and/or by allowing that debt to be converted into preferred stock;

(j)[sic] by allowing or causing the renegotiation [of] the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith; and/or

(k)[sic] by otherwise failing to protect the interests of the minority stockholders of SCI.

Appellants answered, relying on the Release as an affirmative defense to **Menezes's** claims and counterclaiming for breach of the Release.^{FN6} Appellants also moved to dismiss **Menezes's** complaint or in the alternative for summary judgment arguing the Release barred the claims as a matter of law. **Menezes** filed a motion to dismiss Appellants' counterclaims. The circuit court concluded **Menezes's** breach of fiduciary duty claim accrued at the time the merger was completed in October 2006, meaning the claims in this lawsuit were not barred by the Release. The circuit court therefore denied Appellants' motion to dismiss or for summary judgment, dismissed Appellants' counterclaim, and struck Appellants' defenses related to the Release. Appellants filed a mo-

709 S.E.2d 114
(Cite as: 709 S.E.2d 114)

tion to reconsider*117 with the circuit court and that motion was denied. This appeal followed.^{FN7}

FN6. Stephen Duerk filed an individual answer but asserts the same positions as all Appellants.

FN7. Appellants then filed an appeal with this court requesting review of the entire circuit court's order. **Menezes** filed a motion to dismiss the appeal arguing the order was interlocutory. A single judge denied the motion but limited appellate review to the dismissal of Appellants' counterclaims and the striking of their affirmative defenses citing section 14-3-330(2)(c) of the South Carolina Code (1977). Appellants filed a petition for rehearing of this ruling, arguing the single issue on appeal (accrual of the breach of fiduciary duty claim) would determine all the points addressed in the circuit court's order. Ultimately a three-judge panel of this court affirmed the single judge's ruling limiting appellate review to the circuit court's dismissal of Appellants' counterclaims and the striking of Appellants' defenses. Therefore, we limit our discussion to those issues.

LAW/ANALYSIS

Appellants contend the circuit court erred in dismissing their counterclaim and striking their affirmative defenses relating to the Release because **Menezes's** claim could not have accrued prior to the closing of the merger. They argue the circuit court's reliance on certain Delaware cases is misplaced in light of more recent case law and the facts of this case. We agree.

before us narrowly: Could **Menezes's** claim have only accrued after completion of the merger? Neither party has disputed that Delaware law controls the question of the accrual date as claims concerning the fiduciary duties of corporate officers is governed by the state of incorporation. See Restatement (First) of Conflicts of Laws § 187 (1934) ("[T]he existence and extent of the liability of shareholders, officers, or directors of a corporation ... is determined by the law of the state of incorporation."). "Generally, the rights and obligations of stockholders, including the relative rights of stockholders as respects the corporation itself, are determined and controlled by the law of the state of incorporation." 18 Am.Jur.2d Corporations § 21. South Carolina courts generally follow the traditional choice of law rules as stated in the Restatement of Conflicts of Laws. See McDaniel v. McDaniel, 243 S.C. 286, 292, 133 S.E.2d 809, 813 (1963).

The circuit court cites four Delaware cases in its order for the proposition that the claim accrued no earlier than the closing of the merger.^{FN8} The first case cited is Kaufman v. Albin, 447 A.2d 761 (Del.Ch.1982). In Kaufman, a shareholder filed a derivative suit alleging waste of corporate assets by the corporation's board of directors. Id. at 761-62. On August 22, 1977, the board voted to accept and recommend a tender offer by another business to purchase a majority of the corporation's stock. Id. at 762. The defendants argued their alleged misdeeds relating to the transaction all occurred prior to September 1, 1977, when a statute affecting service of corporate officers took effect. Id. at 763. If the claim accrued before September 1, the complaint would be dismissed for ineffective service; if afterwards, the claims would go forward. In determining the plaintiff's claims accrued after September 1, the court noted:

[1] "[U]pon the court's own initiative, at any time the court may order stricken from any pleading any insufficient defense or any redundant, immaterial, impertinent or scandalous matter." Rule 12(f), SCRCP. "The question [on a motion to dismiss a counterclaim] is whether in the light most favorable to the complainant, and with every doubt resolved on his behalf, the counterclaim states any valid claim for relief." Charleston Cnty. Sch. Dist. v. Laidlaw Transp. Inc., 348 S.C. 420, 424, 559 S.E.2d 362, 364 (Ct.App.2001).

[2] The circuit court's order frames the question

FN8. Appellants raised to the circuit court at the hearing and in their motion for reconsideration whether **Menezes's** claim "may have been made" (under subparagraph 8 of the Release) in the employment lawsuit. The circuit court does not specifically address this point in its order. However, whether or not the claim may have been brought would seem to turn on whether or not the claim had accrued. Therefore, we believe that argument is subsumed in the accrual analysis.

709 S.E.2d 114

(Cite as: 709 S.E.2d 114)

After August 22, the tender offer still had to be commenced and [the corporation's] stockholders had to be advised that the directors ... recommended that the tender offer be accepted. This was done on *118 September 12, 1977. [The purchasing company] also had available many options which would have enabled it to terminate the tender offer if certain events took place before October 3, 1977. Even more importantly, the tender offer was contingent upon it being accepted by the tendering of at least 52% of the outstanding shares of stock.

Id. at 763-64.

The court then quoted from the preeminent treatise in Delaware corporate law. "In *Folk*, *The Delaware General Corporation Law*, 487 (1967) it is stated: 'Accordingly, the circumstances of the case will determine whether the transaction is executed or continuing. If the action complained of requires stockholder approval, the transaction is not considered complete until the stockholders have approved it.' " *Kaufman*, 447 A.2d at 764.

The *Kaufman* court further relied on the case of *Lavine v. Gulf Coast Leaseholds, Inc.*, 122 A.2d 550 (Del.Ch.1956), for the proposition that when "exchanges of stock are contingent upon shareholder approval, the transaction is not completed until the shareholder vote takes place." ^{FN9} *Kaufman*, 447 A.2d at 764. The court concluded the transaction in *Kaufman* commenced on August 22, but was not consummated until the close of the tender offer on October 3. *Id.* "The alleged wrong was therefore a continuing wrong and any cause of action attacking it arose or accrued" after September 1, 1977. *Id.*

FN9. *Lavine* was a shareholder standing case as are many of the cases discussed herein. In *Lavine*, the issue was whether the plaintiff had standing to sue for breach of fiduciary duty relating to a merger when plaintiff purchased shares after the board's approval of the merger and the announcement of its terms but before the final shareholder vote. *Id.* at 550-51.

However, more recent case law suggests in a standing to sue case, the courts are looking to the date of the wrong for purposes of determining accrual as opposed to the date of shareholder approval. See

Dieter v. Prime Computer, Inc., 681 A.2d 1068, 1072 (Del.Ch.1996) (finding plaintiff lacked standing to be class representative because "[t]he challenged transaction is [the Board's] approval of the Merger. The alleged breach of fiduciary duty occurred at the time the Board approved the Merger Agreement.... It is not the Merger that constitutes the wrongful act of which Plaintiffs complain; it is the 'fixing of the terms of the transaction.' ") (quoting *Brown v. Automated Mktg. Sys., Inc.*, No. 6715, 1982 WL 8782 at *2 (Del.Ch.1982)); see also *In re Beatrice Co.*, Nos. 155 and 156, 1987 WL 36708 at *3 (Del.1987) ("In the case of a proposed merger, the plaintiff must have been a stockholder at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged."); *FMC Corp. v. R.P. Scherer Corp.*, No. 6889, 1982 WL 17888 at *2 (Del.Ch.1982) (relying on *Brown* to find plaintiff lacked standing to sue when she purchased stock after board's approval of supermajority anti-takeover provisions and announcement of merger terms but before shareholder approval of those provisions).

Additionally, *Kaufman* relies on *Folk* as it read in 1967. As Appellants point out, *Folk* has been amended, and the relevant section now states:

Generally, the determinative issue is when the specific acts of alleged wrong doing occurred, and not when their effect is felt. Therefore, the circumstances of the case will determine whether the transaction is executed or continuing. For instance, an offer made by the corporation to certain of its stockholders to exchange one class of stock for another, which was specifically conditioned on approval by the corporation's other stockholders, was held not be completed until stockholder approval was obtained. On the other hand, both a proposed merger and a proposed supermajority voting provision have been held to be consummated when their terms were fixed and announced by the board of directors, and not to be continuing transaction up to the time of stockholder approval.

2 Edward P. Welch et al., *Folk on the Delaware General Corporation Law: Fundamentals* § 327.3.2 (2010) (footnotes omitted).

The next case relied upon by the circuit court is *119 *Dofflemeyer v. W.F. Hall Printing Co.*, 558

709 S.E.2d 114
(Cite as: 709 S.E.2d 114)

F.Supp. 372 (D.Del.1983). In *Dofflemeyer*, the plaintiffs, former shareholders, filed a derivative action alleging various directors breached their fiduciary duties in relation to orchestrating a merger. *Id.* at 375. The plaintiffs alleged the directors procured a faulty investment opinion, maneuvered to avoid a supermajority provision in the by-laws, and issued a false and misleading proxy statement. *Id.* at 379. The court, in determining when the statute of limitations began to run on these claims stated: “The plaintiffs could not have sued for damages until the merger was actually accomplished—until that time, they had suffered no injury by the defendants’ acts.” *Id.* The court relied primarily on *Kaufman* in its analysis, but nowhere in *Kaufman* is the issue of money damages discussed.

More recent cases that address the requirement of damages prior to bringing suit seem out of step with *Dofflemeyer*. In *Albert v. Alex Brown Management Services, Inc.*, No. 762–N, 2005 WL 1594085, *18 (Del.Ch.2005),^{FN10} plaintiffs, limited partners in an investment fund, sued managers for various breaches of fiduciary duties including “unhedging” their funds and exposing them to more financial risk. The plaintiffs waited to sue while the stocks were rising and then sued for damages upon their fall. In finding plaintiffs’ complaints were untimely, the court stated:

FN10. *Albert* is a statute of limitations case.

The law in Delaware is crystal clear that a claim accrues as soon as the wrongful act occurs. This is so because the plaintiffs were harmed as soon as the alleged wrongful acts occurred. Whether or not the plaintiffs could have sued for damages is not dispositive as to whether the claim accrued, since, as soon as the alleged wrongful act occurred, the plaintiffs could have sought injunctive relief.

Id.

This reasoning is evident in other cases as well. See *In re SunGard Data Sys., Inc.*, No. 1221–N, 2005 WL 1653975 at *2 (Del.Ch.2005) (“[T]he optimal time to bring a disclosure claim in connection with a proposed merger, or in a like context where the company requests shareholder action or approval is before the stockholder vote is taken and the deal closes.”); *Kahn v. Seaboard Corp.*, 625 A.2d 269, 271 (Del.Ch.1993) (“Any such wrong occurred at the time that enforceable legal rights against Seaboard

were created. Suit could have been brought immediately thereafter to rescind the contract and for nominal damages which are traditionally available in contract actions. Complete and adequate relief, if justified, could be shaped immediately or at any point thereafter.”); see also *Seidel v. Lee*, 954 F.Supp. 810, 816 (D.Del.1996) (citing *Dofflemeyer* parenthetically for the proposition “fiduciary duty claim accrues when [the] breach is accomplished”).

We next turn our attention to *Baron v. Allied Artists Pictures Corp.*, 717 F.2d 105 (3rd Cir.1983), also cited by the circuit court. *Baron* involved the statute of limitations relating to a violation of SEC regulations for issuing a misleading proxy statement. *Id.* at 106. There, the court concluded the plaintiff’s cause of action for damages resulting from a breach of fiduciary duty/misleading proxy statement did not accrue until the merger was accomplished and a suit for damages could be successfully maintained. *Id.* at 108–09. However, the reasoning in that case has been superseded by statute and now is arguably in favor of finding a cause of action accrues at the time of the wrongdoing, not at the time the merger closes. See *In re Exxon Mobil Corp.*, 387 F.Supp.2d 407, 421 (D.N.J.2005) (“*Baron* pre-dates [the] Sarbanes–Oxley [Act of 2002] and the decisions of the courts in this Circuit which have held that actions under Sections 10(b) and 14(a) arise on the date that the allegedly false or misleading statement underlying the claims was made.”).

Finally, we examine *In re Coca-Cola Enterprises, Inc.*, No.1927–CC, 2007 WL 3122370 (Del.Ch.2007), *aff’d*, *International Brotherhood Teamsters v. Coca-Cola*, No. 601.2007, 2008 WL 2484587 (Del.2008). In that case, disgruntled shareholders of Coca-Cola’s biggest bottler claimed breach-of-fiduciary-duty-by-its-board-members. *Id.* at *1. The plaintiffs claimed Coca-Cola was essentially controlling plaintiffs’ business, for *120 Coca-Cola’s profit and to plaintiffs’ detriment, and plaintiffs’ board was allowing this to happen. *Id.* The parties had entered into a contract in 1986 that gave Coca-Cola the authority to do the offensive acts. *Id.* Plaintiffs brought suit in 2006, alleging damages from specific acts that occurred under the contract in 2002 and 2004. *Id.* at *5. The court, in determining whether plaintiffs’ claims were barred by the statute of limitations or laches concluded: “Under Delaware law, a plaintiff’s cause of action accrues at the moment of

709 S.E.2d 114
(Cite as: 709 S.E.2d 114)

the wrongful act—not when the harmful effects of the act are felt—even if the plaintiff is unaware of the wrong.” *Id.* Plaintiffs’ claims were dismissed as time-barred because “[t]he actions challenged in the amended complaint represent the manifestation of the bargain struck in 1986....” *Id.* at *6.

In reaching this conclusion, the *Coca-Cola* court relied on *Kahn* wherein the plaintiff filed a derivative action against directors and the corporation relating to transactions carried out under the terms of a time charter agreement. The court stated: “[T]he ‘continuing wrong’ is performance of a contract.... So long as the time charter is not rescinded, the payments it calls for are legal obligations, not wrongs.” *Kahn*, 625 A.2d at 272. Any wrong occurred at the time “enforceable legal rights against Seaboard were created.” *Id.* at 271.

Another oft-cited case is *Elster v. American Airlines*, 100 A.2d 219 (Del.Ch.1953). Presented with a similar situation, the court explained:

Assuming that the individual defendants did wrong to the Corporation by entering into the contract, it does not follow that they committed any wrong in carrying out the contract once it had been made. Indeed, had they not done so, the corporation would presumably have been subject to liability for breach of contract.

Id. at 224 (quoting *Leviton v. Stout*, 97 F.Supp. 105, 119 (W.D.Ky.1951)).

[3] After reviewing the facts of the case *sub judice* and all the relevant case law, we conclude the circuit court’s reliance on the four cases cited above was misplaced.

Kaufman relies heavily on *Lavine*, which was a case involving the plaintiff’s standing to bring suit. As discussed, more recent standing cases indicate a claim accrues at the time of the wrongdoing by the fiduciary, not necessarily at the time a merger closes. Furthermore, *Kaufman* did not involve a merger but a tender offer and the court indicated a claim does not accrue until shareholders approve the action if shareholder approval is required. In *Menezes*’s case, according to the Proxy Statement, FITG stockholders needed to take no action to effect the merger as a majority of stockholders had approved it in writing

contemporaneous with the signing of the merger agreement. Notably, the Proxy Statement also said “no action by the stockholders of SCI is required to approve the merger agreement or to consummate the merger.” (emphasis added). SCI stockholders did need to satisfy a condition precedent by agreeing to amend the certificate of incorporation to reflect the existence of the newly formed entity and by reelecting five of the current board members. However, according to the Proxy Statement, “stockholders of SCI holding approximately 75.6% of SCI’s outstanding common stock have indicated that they intend to vote to adopt the amended and re-instated certificate of incorporation and to elect the directors nominated for re-election. Approval of the matters to be voted on at the 2006 Annual Meeting is therefore assured.” *Menezes* acknowledged in his complaint that the closing of the merger was “merely a formality.” In light of recent case law indicating the date of the wrong is the relevant time and because *Kaufman* is not factually on all fours with this case, *Kaufman* does not dictate a finding *Menezes*’s claim could have accrued only at the time of the merger’s consummation.

Dofflemeyer seems out of step with more recent case law on fiduciary duty claims because those cases indicate a claim may be brought prior to the incurring of money damages in the form of a request for injunctive relief. *Menezes* could have brought a claim for injunctive relief prior to the signing of the Release, and this thought was at least contemplated as evidenced by the inclusion of such an allegation in his draft amended complaint*121 given to opposing counsel in the employment litigation. *Menezes*’s remedy, money damages, may have been different, but the claim, breach of fiduciary duty, would be the same.

Finally, we do not believe the “legally enforceable rights” language in *Kahn* and *Coca-Cola* necessitate a finding that *Menezes*’s claim accrued after the merger. Once the merger agreement was signed, SCI and FITG had legally enforceable rights against each other to proceed with all aspects of the merger agreement in good faith. If they did not, they would be in breach of the agreement and subject to suit. More importantly, once the merger agreement was signed, *Menezes*, as a shareholder, had a legally enforceable right to enjoin the merger from being consummated.

709 S.E.2d 114
(Cite as: 709 S.E.2d 114)

For all of the foregoing reasons, the circuit court's reliance on the cited cases was erroneous. Because **Menezes's** claim could have arisen prior to the closing of the merger, the Appellants' defenses relating to the Release were not insufficient. Additionally, their counterclaim arising out of the Release does not, resolving all doubts in their favor, fail to state a valid claim for relief. Consequently, it was error for the circuit court to dismiss Appellants' defenses and counterclaim relating to the Release. The decision of the circuit court is therefore

REVERSED AND REMANDED.

WILLIAMS, J., concurs.

PIEPER, J., concurs in a separate opinion.

I concur in the decision to reverse and remand. However, I write separately because I would like to address the combination of **Menezes's** ten claims for breach of fiduciary duty into one claim by the circuit court.

Menezes brought this lawsuit in 2008 alleging breach of fiduciary duty on the part of the Appellants in all of the following particulars:

- (a) by proposing the [m]erger and then allowing it to close notwithstanding the financial condition of FITG;
- (b) by approving the [m]erger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders to 35%, or at all [sic];
- (c) by not providing accurate and complete information regarding FITG or ensuring that such information was provided to them;
- (d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account or see that it was taken into account with regard to the [m]erger;
- (e) by failing to ensure that proper due diligence was conducted on behalf of SCI or FITG;
- (f) by allowing the representation at the [m]erger

closing that MAC Clause condition was satisfied;

(g) by failing to call off or renegotiate the [m]erger (or cause it to be called off or renegotiated) because of the financial condition of FITG;

(i) [sic] by allowing the debt previously held by FITG to be transferred to Combined Company and/or by allowing that debt to be converted into preferred stock;

(j) [sic] by allowing or causing the renegotiation [of] the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith; and/or

(k) [sic] by otherwise failing to protect the interests of the minority stockholders of SCI.

The circuit court ruled that the breach of fiduciary duty claims could not have arisen prior to the closing of the merger. Appellants neither argued that the claims should be considered separately, nor asked the court to alter or amend its ruling on the issue. Thus, I would find the question of whether or not the court erred in considering **Menezes's** claims in combination is not preserved for appellate review. See *Wilder Corp. v. Wilke*, 330 S.C. 71, 76-77, 497 S.E.2d 731, 733-34 (1998) (finding an issue must have been raised to the trial court in order to be preserved for appellate review and holding post trial motions are necessary to preserve issues that were raised to the trial court but not ruled upon).

Despite this preservation concern, and in light of the reversal and remand of the case by the majority opinion, I note some of the *122 claims could have arisen prior to the closing of the merger and others could have arisen after the closing of the merger. On August 29, 2006, the SCI board of directors approved the merger agreement between SCI and FITG. On September 28, 2006, in exchange for payments totaling approximately \$575,000, **Menezes** signed a Settlement Agreement and Release of All Claims to settle the claims involved in the employment lawsuit. Finally, on October 20, 2006, the merger between SCI and FITG was completed and all preconditions were either satisfied or waived. Importantly, we should recognize the fact that any claims arising between the signing of the release on September 28, 2006, and the finalizing of the merger on October 20,

709 S.E.2d 114

(Cite as: 709 S.E.2d 114)

2006, were valid claims. Furthermore, by analyzing each of **Menezes's** claims independently of one another, as opposed to combining them, some of the claims may be barred by **Menezes's** release whereas others may not be barred. Although I agree with the majority in distinguishing the cases relied upon by the circuit court, I would find the cases nonetheless shed some light on the limiting nature of combining **Menezes's** ten claims for breach of fiduciary duty into one claim. Therefore, on remand, even though the court did not do so initially, I would urge the court to break down the acts alleged by **Menezes** separately, as one or more acts could be deemed a separate breach of fiduciary duty based on when each act occurred.

S.C.App.,2011.

Menezes v. WL Ross & Co. LLC

709 S.E.2d 114

END OF DOCUMENT

**THE STATE OF SOUTH CAROLINA
In The Court of Appeals**

Brian P. Menezes, Respondent,

v.

WL Ross & Co. LLC, Wilbur L. Ross, Jr.,
Michael J. Gibbons, David H. Storper, David L.
Wax, Joseph L. Gorga, Stephen B. Duerk,
WLR Recovery Fund II, L.P., WLR Recovery
Fund III, L.P., WLR Recovery Associates II
LLC, and WLR Recovery Associates III LLC,
Appellants.

Appeal From Greenville County
Edward W. Miller, Circuit Court Judge

Opinion No. 4810
Heard October 6, 2010 – Filed March 23, 2011

REVERSED AND REMANDED

H. Sam Mabry, III, Charles M. Sprinkle, III, and
James Derrick Quattlebaum, all of Greenville;
Michael J. McConnell and Joseph E. Finley, of
Atlanta, Georgia and N. Scott Fletcher, of
Houston, Texas, for Appellants.

William D. Herlong, of Greenville, for
Respondent.

KONDUROS, J: W.L. Ross & Co., LLC (WLR) and several of its board members (Appellants)[1] appeal the circuit court's striking of two of their defenses and dismissal of their counterclaim in the direct shareholder lawsuit filed by Brian Menezes. We reverse and remand.

FACTS/PROCEDURAL BACKGROUND

Safety Components International, Inc. (SCI) was a publicly traded Delaware corporation with its headquarters in South Carolina. SCI was in the business of designing and manufacturing airbag fabric and airbag cushions. From 1999 to 2006, Menezes was employed by SCI as Chief Financial Officer, and for a time, interim Chief Executive Officer. He was terminated from his employment with SCI in June of 2006 but remained a shareholder. Menezes sued SCI to recover additional severance pay he alleged he was due and a "change of control" bonus included in his employment contract.

10

While Menezes's employment lawsuit was proceeding, SCI entered into discussions with the former International Textile Group, Inc. (FITG), a privately held Delaware corporation headquartered in North Carolina, about a possible merger.^[2] WLR, an investment firm, owned shares in both SCI and FITG, either directly or indirectly through affiliate entities.

On August 29, 2006, the SCI board of directors approved the merger agreement between SCI and FITG. The merger agreement provided that FITG would merge into SCI and that SCI's certificate of incorporation would be amended to reflect the new combined entity. FITG shareholders would receive one share of SCI stock for every 1.4379 shares of FITG stock surrendered.^[3] The terms of the merger were made public via a press release and the filing of a Form 8-K with the Securities and Exchange Commission (SEC) on August 30 and again on September 1, when a preliminary Joint Proxy Statement/Prospectus was filed with the SEC. A final Proxy Statement was mailed to stockholders on September 25, 2006. According to the Proxy Statement, FITG stockholders needed to take no action to effect the merger as a majority of stockholders had approved it in writing contemporaneous with the signing of the merger agreement. The Proxy Statement also indicated "no action by the stockholders of SCI is required to approve the merger agreement or to consummate the merger." SCI stockholders did need to satisfy a condition precedent by agreeing to amend the certificate of incorporation to reflect the existence of the newly formed entity and by re-electing five of the current board members. However, according to the Proxy Statement, "stockholders of SCI holding approximately 75.6% of SCI's outstanding common stock have indicated that they intend to vote to adopt the amended and re-instated certificate of incorporation and to elect the directors nominated for re-election. Approval of the matters to be voted on at the 2006 Annual Meeting is therefore assured."

On September 28, 2006, in exchange for payments totaling approximately \$575,000, Menezes signed a Settlement Agreement and Release of All Claims (the Release) to settle the employment lawsuit. The Release stated Menezes agreed to "release, acquit and forever discharge" defendants of:

Any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which plaintiff either has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is [p]laintiff's intention to release all rights and claims that he may lawfully release.

The Release specifically barred Menezes from bringing "any claim based upon or as an owner of any stock or interest . . . arising prior to the execution" of the Release and from pursuing any claims "made or which may have been made" in the employment lawsuit.^[4] On October 20, 2006, the merger between SCI and FITG was completed in that all pre-conditions were either satisfied or waived.

Menezes brought this lawsuit in 2008 alleging breaches of fiduciary duties on the part of the Appellants in the following particulars:

(a) by proposing the [m]erger and then allowing it to close notwithstanding the financial condition of FITG;

11

- (b) by approving the [m]erger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders to 35%, or at all [sic];
- (c) by not providing accurate and complete information regarding FITG . . . or ensuring that such information was provided to them;
- (d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account or see that it was taken into account with regard to the [m]erger;
- (e) by failing to ensure that proper due diligence was conducted on behalf of SCI or FITG;
- (f) by allowing the representation at the [m]erger closing that MAC[5] Clause condition was satisfied;
- (g) by failing to call off or renegotiate the [m]erger (or cause it to be called off or renegotiated) because of the financial condition of FITG;
- (i) [sic] by allowing the debt previously held by FITG to be transferred to Combined Company and/or by allowing that debt to be converted into preferred stock;
- (j) [sic] by allowing or causing the renegotiation [of] the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith; and/or
- (k) [sic] by otherwise failing to protect the interests of the minority stockholders of SCI.

Appellants answered, relying on the Release as an affirmative defense to Menezes's claims and counterclaiming for breach of the Release.[6] Appellants also moved to dismiss Menezes's complaint or in the alternative for summary judgment arguing the Release barred the claims as a matter of law. Menezes filed a motion to dismiss Appellants' counterclaims. The circuit court concluded Menezes's breach of fiduciary duty claim accrued at the time the merger was completed in October 2006, meaning the claims in this lawsuit were not barred by the Release. The circuit court therefore denied Appellants' motion to dismiss or for summary judgment, dismissed Appellants' counterclaim, and struck Appellants' defenses related to the Release. Appellants filed a motion to reconsider with the circuit court and that motion was denied. This appeal followed.[7]

LAW/ANALYSIS

Appellants contend the circuit court erred in dismissing their counterclaim and striking their affirmative defenses relating to the Release because Menezes's claim could not have accrued prior to the closing of the merger. They argue the circuit court's reliance on certain Delaware cases is misplaced in light of more recent case law and the facts of this case. We agree.

"[U]pon the court's own initiative, at any time the court may order stricken from any pleading any insufficient defense or any redundant, immaterial, impertinent or scandalous matter." Rule 12(f), SCRCP. "The question [on a motion to dismiss a counterclaim] is whether in the

light most favorable to the complainant, and with every doubt resolved on his behalf, the counterclaim states any valid claim for relief." Charleston Cnty. Sch. Dist. v. Laidlaw Transit, Inc., 348 S.C. 420, 424, 559 S.E.2d 362, 364 (Ct. App. 2001).

The circuit court's order frames the question before us narrowly: Could Menezes's claim have only accrued after completion of the merger? Neither party has disputed that Delaware law controls the question of the accrual date as claims concerning the fiduciary duties of corporate officers is governed by the state of incorporation. See Restatement (First) of Conflicts of Laws § 187 (1934) ("[T]he existence and extent of the liability of shareholders, officers, or directors of a corporation . . . is determined by the law of the state of incorporation."). "Generally, the rights and obligations of stockholders, including the relative rights of stockholders as respects the corporation itself, are determined and controlled by the law of the state of incorporation." 18 Am. Jur. 2d Corporations § 21. South Carolina courts generally follow the traditional choice of law rules as stated in the Restatement of Conflicts of Laws. See McDaniel v. McDaniel, 243 S.C. 286, 292, 133 S.E.2d 809, 813 (1963).

The circuit court cites four Delaware cases in its order for the proposition that the claim accrued no earlier than the closing of the merger.^[8] The first case cited is Kaufman v. Albin, 447 A.2d 761 (Del. Ch. 1982). In Kaufman, a shareholder filed a derivative suit alleging waste of corporate assets by the corporation's board of directors. Id. at 761-62. On August 22, 1977, the board voted to accept and recommend a tender offer by another business to purchase a majority of the corporation's stock. Id. at 762. The defendants argued their alleged misdeeds relating to the transaction all occurred prior to September 1, 1977, when a statute affecting service of corporate officers took effect. Id. at 763. If the claim accrued before September 1, the complaint would be dismissed for ineffective service; if afterwards, the claims would go forward. In determining the plaintiff's claims accrued after September 1, the court noted:

After August 22, the tender offer still had to be commenced and [the corporation's] stockholders had to be advised that the directors . . . recommended that the tender offer be accepted. This was done on September 12, 1977. [The purchasing company] also had available many options which would have enabled it to terminate the tender offer if certain events took place before October 3, 1977. Even more importantly, the tender offer was contingent upon it being accepted by the tendering of at least 52% of the outstanding shares of stock.

Id. at 763-64.

The court then quoted from the preeminent treatise in Delaware corporate law. "In Folk, The Delaware General Corporation Law, 487 (1967) it is stated: 'Accordingly, the circumstances of the case will determine whether the transaction is executed or continuing. If the action complained of requires stockholder approval, the transaction is not considered complete until the stockholders have approved it.'" Kaufman, 447 A.2d at 764.

The Kaufman court further relied on the case of Lavine v. Gulf Coast Leaseholds, Inc., 122 A.2d 550 (Del. 1956), for the proposition that when "exchanges of stock are contingent upon shareholder approval, the transaction is not completed until the shareholder vote takes place."^[9] Kaufman, 447 A.2d at 764. The court concluded the transaction in Kaufman commenced on August 22, but was not consummated until the close of the tender offer on

October 3. Id. "The alleged wrong was therefore a continuing wrong and any cause of action attacking it arose or accrued" after September 1, 1977. Id.

However, more recent case law suggests in a standing to sue case, the courts are looking to the date of the wrong for purposes of determining accrual as opposed to the date of shareholder approval. See Dieter v. Prime Computer, Inc., 681 A.2d 1068, 1072 (Del. Ch. 1996) (finding plaintiff lacked standing to be class representative because "[t]he challenged transaction is [the Board's] approval of the Merger. The alleged breach of fiduciary duty occurred at the time the Board approved the Merger Agreement It is not the Merger that constitutes the wrongful act of which Plaintiffs complain; it is the 'fixing of the terms of the transaction.'" (quoting Brown v. Automated Mktg. Sys., Inc., No. 6715, 1982 WL 8782 at *2 (Del. Ch. 1982)); see also In re Beatrice Co., Nos. 155 and 156, 1987 WL 36708 at *3 (Del. 1987) ("In the case of a proposed merger, the plaintiff must have been a stockholder at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged."); FMC Corp. v. R.P. Scherer Corp., No. 6889, 1982 WL 17888 at *2 (Del. Ch. 1982) (relying on Brown to find plaintiff lacked standing to sue when she purchased stock after board's approval of supermajority anti-takeover provisions and announcement of merger terms but before shareholder approval of those provisions).

Additionally, Kaufman relies on Folk as it read in 1967. As Appellants point out, Folk has been amended, and the relevant section now states:

Generally, the determinative issue is when the specific acts of alleged wrong doing occurred, and not when their effect is felt. Therefore, the circumstances of the case will determine whether the transaction is executed or continuing. For instance, an offer made by the corporation to certain of its stockholders to exchange one class of stock for another, which was specifically conditioned on approval by the corporation's other stockholders, was held not be completed until stockholder approval was obtained. On the other hand, both a proposed merger and a proposed supermajority voting provision have been held to be consummated when their terms were fixed and announced by the board of directors, and not to be continuing transaction up to the time of stockholder approval.

2 Edward P. Welch et al., Folk on the Delaware General Corporation Law: Fundamentals § 327.3.2 (2010) (footnotes omitted).

The next case relied upon by the circuit court is Dofflemyer v. W.F. Hall Printing Co., 558 F.Supp. 372 (D. Del. 1983). In Dofflemyer, the plaintiffs, former shareholders, filed a derivative action alleging various directors breached their fiduciary duties in relation to orchestrating a merger. Id. at 375. The plaintiffs alleged the directors procured a faulty investment opinion, maneuvered to avoid a supermajority provision in the by-laws, and issued a false and misleading proxy statement. Id. at 379. The court, in determining when the statute of limitations began to run on these claims stated: "The plaintiffs could not have sued for damages until the merger was actually accomplished – until that time, they had suffered no injury by the defendants' acts." Id. The court relied primarily on Kaufman in its analysis, but nowhere in Kaufman is the issue of money damages discussed.

More recent cases that address the requirement of damages prior to bringing suit seem out of step with Dofflemyer. In Albert v. Alex Brown Management Services, Inc., No. 672-N,

14

2005 WL 1594085, *18 (Del. Ch. 2005),^[10] plaintiffs, limited partners in an investment fund, sued managers for various breaches of fiduciary duties including "unhedging" their funds and exposing them to more financial risk. The plaintiffs waited to sue while the stocks were rising and then sued for damages upon their fall. In finding plaintiffs' complaints were untimely, the court stated:

The law in Delaware is crystal clear that a claim accrues as soon as the wrongful act occurs. This is so because the plaintiffs were harmed as soon as the alleged wrongful acts occurred. Whether or not the plaintiffs could have sued for damages is not dispositive as to whether the claim accrued, since, as soon as the alleged wrongful act occurred, the plaintiffs could have sought injunctive relief.

Id.

This reasoning is evident in other cases as well. See In re SunGard Data Sys., Inc., No. 1221-N, 2005 WL 1653975 at *2 (Del. Ch. 2005) ("[T]he optimal time to bring a disclosure claim in connection with a proposed merger, or in a like context where the company requests shareholder action or approval is before the stockholder vote is taken and the deal closes."); Kahn v. Seaboard Corp., 625 A.2d 269, 271 (Del. Ch. 1993) ("Any such wrong occurred at the time that enforceable legal rights against Seaboard were created. Suit could have been brought immediately thereafter to rescind the contract and for nominal damages which are traditionally available in contract actions. Complete and adequate relief, if justified, could be shaped immediately or at any point thereafter."); see also Seidel v. Lee, 954 F. Supp. 810, 816 (D. Del. 1996) (citing Dofflemeyer parenthetically for the proposition "fiduciary duty claim accrues when [the] breach is accomplished").

We next turn our attention to Baron v. Allied Artists Pictures Corp., 717 F.2d 105 (3rd Cir. 1983), also cited by the circuit court. Baron involved the statute of limitations relating to a violation of SEC regulations for issuing a misleading proxy statement. Id. at 106. There, the court concluded the plaintiff's cause of action for damages resulting from a breach of fiduciary duty/misleading proxy statement did not accrue until the merger was accomplished and a suit for damages could be successfully maintained. Id. at 108-09. However, the reasoning in that case has been superseded by statute and now is arguably in favor of finding a cause of action accrues at the time of the wrongdoing, not at the time the merger closes. See In re Exxon Mobil Corp., 387 F. Supp.2d 407, 421 (D.N.J. 2005) ("Baron pre-dates [the] Sarbanes-Oxley [Act of 2002] and the decisions of the courts in this Circuit which have held that actions under Sections 10(b) and 14(a) arise on the date that the allegedly false or misleading statement underlying the claims was made.").

Finally, we examine In re Coca-Cola Enterprises, Inc., No. 1927-CC, 2007 WL 3122370 (Del. Ch. 2007), aff'd, International Brotherhood Teamsters v. Coca-Cola, No. 1927-cc, 2008 WL 2484587 (Del. 2008). In that case, disgruntled shareholders of Coca-Cola's biggest bottler claimed breach of fiduciary duty by its board members. Id. at *1. The plaintiffs claimed Coca-Cola was essentially controlling plaintiffs' business, for Coca-Cola's profit and to plaintiffs' detriment, and plaintiffs' board was allowing this to happen. Id. The parties had entered into a contract in 1986 that gave Coca-Cola the authority to do the offensive acts. Id. Plaintiffs brought suit in 2006, alleging damages from specific acts that occurred under the contract in 2002 and 2004. Id. at *5. The court, in determining whether plaintiffs' claims were barred by the statute of limitations or laches concluded: "Under Delaware law, a plaintiff's cause of action accrues at the moment of the wrongful act – not when the harmful

15

effects of the act are felt – even if the plaintiff is unaware of the wrong." Id. Plaintiffs' claims were dismissed as time-barred because "[t]he actions challenged in the amended complaint represent the manifestation of the bargain struck in 1986" Id. at *6.

In reaching this conclusion, the Coca-Cola court relied on Kahn wherein the plaintiff filed a derivative action against directors and the corporation relating to transactions carried out under the terms of a time charter agreement. The court stated: "[T]he 'continuing wrong' is performance of a contract. . . . So long as the time charter is not rescinded, the payments it calls for are legal obligations, not wrongs." Kahn, 625 A.2d at 272. Any wrong occurred at the time "enforceable legal rights against Seaboard were created." Id. at 271.

Another oft-cited case is Elster v. American Airlines, 100 A.2d 219 (Del. Ch. 1953). Presented with a similar situation, the court explained:

Assuming that the individual defendants did wrong to the Corporation by entering into the contract, it does not follow that they committed any wrong in carrying out the contract once it had been made. Indeed, had they not done so, the corporation would presumably have been subject to liability for breach of contract.

Id. at 224 (quoting Levitan v. Stout, 97 F. Supp. 105, 119 (W.D. Ky. 1951)).

After reviewing the facts of the case sub judice and all the relevant case law, we conclude the circuit court's reliance on the four cases cited above was misplaced.

Kaufman relies heavily on Lavine, which was a case involving the plaintiff's standing to bring suit. As discussed, more recent standing cases indicate a claim accrues at the time of the wrongdoing by the fiduciary, not necessarily at the time a merger closes. Furthermore, Kaufman did not involve a merger but a tender offer and the court indicated a claim does not accrue until shareholders approve the action if shareholder approval is required. In Menezes's case, according to the Proxy Statement, FITG stockholders needed to take no action to effect the merger as a majority of stockholders had approved it in writing contemporaneous with the signing of the merger agreement. Notably, the Proxy Statement also said "no action by the stockholders of SCI is required to approve the merger agreement or to consummate the merger." (emphasis added). SCI stockholders did need to satisfy a condition precedent by agreeing to amend the certificate of incorporation to reflect the existence of the newly formed entity and by re-electing five of the current board members. However, according to the Proxy Statement, "stockholders of SCI holding approximately 75.6% of SCI's outstanding common stock have indicated that they intend to vote to adopt the amended and re-instated certificate of incorporation and to elect the directors nominated for re-election. Approval of the matters to be voted on at the 2006 Annual Meeting is therefore assured." Menezes acknowledged in his complaint that the closing of the merger was "merely a formality." In light of recent case law indicating the date of the wrong is the relevant time and because Kaufman is not factually on all fours with this case, Kaufman does not dictate a finding Menezes's claim could have accrued only at the time of the merger's consummation.

Dofflemeyer seems out of step with more recent case law on fiduciary duty claims because those cases indicate a claim may be brought prior to the incurring of money damages in the form of a request for injunctive relief. Menezes could have brought a claim for injunctive relief prior to the signing of the Release, and this thought was at least contemplated as

16

evidenced by the inclusion of such an allegation in his draft amended complaint given to opposing counsel in the employment litigation. Menezes's remedy, money damages, may have been different, but the claim, breach of fiduciary duty, would be the same.

Finally, we do not believe the "legally enforceable rights" language in Kahn and Coca-Cola necessitate a finding that Menezes's claim accrued after the merger. Once the merger agreement was signed, SCI and FITG had legally enforceable rights against each other to proceed with all aspects of the merger agreement in good faith. If they did not, they would be in breach of the agreement and subject to suit. More importantly, once the merger agreement was signed, Menezes, as a shareholder, had a legally enforceable right to enjoin the merger from being consummated.

For all of the foregoing reasons, the circuit court's reliance on the cited cases was erroneous. Because Menezes's claim could have arisen prior to the closing of the merger, the Appellants' defenses relating to the Release were not insufficient. Additionally, their counterclaim arising out of the Release does not, resolving all doubts in their favor, fail to state a valid claim for relief. Consequently, it was error for the circuit court to dismiss Appellants' defenses and counterclaim relating to the Release. The decision of the circuit court is therefore

REVERSED AND REMANDED.

WILLIAMS, J., concurs.

PIEPER, J., concurs in a separate opinion.

I concur in the decision to reverse and remand. However, I write separately because I would like to address the combination of Menezes's ten claims for breach of fiduciary duty into one claim by the circuit court.

Menezes brought this lawsuit in 2008 alleging breach of fiduciary duty on the part of the Appellants in all of the following particulars:

- (a) by proposing the [m]erger and then allowing it to close notwithstanding the financial condition of FITG;
- (b) by approving the [m]erger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders to 35%, or at all [sic];
- (c) by not providing accurate and complete information regarding FITG . . . or ensuring that such information was provided to them;
- (d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account or see that it was taken into account with regard to the [m]erger;
- (e) by failing to ensure that proper due diligence was conducted on behalf of SCI or FITG;
- (f) by allowing the representation at the [m]erger closing that MAC Clause condition was satisfied;

(g) by failing to call off or renegotiate the [m]erger (or cause it to be called off or renegotiated) because of the financial condition of FITG;

(i) [sic] by allowing the debt previously held by FITG to be transferred to Combined Company and/or by allowing that debt to be converted into preferred stock;

(j) [sic] by allowing or causing the renegotiation [of] the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith; and/or

(k) [sic] by otherwise failing to protect the interests of the minority stockholders of SCI.

The circuit court ruled that the breach of fiduciary duty claims could not have arisen prior to the closing of the merger. Appellants neither argued that the claims should be considered separately, nor asked the court to alter or amend its ruling on the issue. Thus, I would find the question of whether or not the court erred in considering Menezes's claims in combination is not preserved for appellate review. See Wilder Corp. v. Wilke, 330 S.C. 71, 76-77, 497 S.E.2d 731, 733-34 (1998) (finding an issue must have been raised to the trial court in order to be preserved for appellate review and holding post trial motions are necessary to preserve issues that were raised to the trial court but not ruled upon).

Despite this preservation concern, and in light of the reversal and remand of the case by the majority opinion, I note some of the claims could have arisen prior to the closing of the merger and others could have arisen after the closing of the merger. On August 29, 2006, the SCI board of directors approved the merger agreement between SCI and FITG. On September 28, 2006, in exchange for payments totaling approximately \$575,000, Menezes signed a Settlement Agreement and Release of All Claims to settle the claims involved in the employment lawsuit. Finally, on October 20, 2006, the merger between SCI and FITG was completed and all preconditions were either satisfied or waived. Importantly, we should recognize the fact that any claims arising between the signing of the release on September 28, 2006, and the finalizing of the merger on October 20, 2006, were valid claims. Furthermore, by analyzing each of Menezes's claims independently of one another, as opposed to combining them, some of the claims may be barred by Menezes's release whereas others may not be barred. Although I agree with the majority in distinguishing the cases relied upon by the circuit court, I would find the cases nonetheless shed some light on the limiting nature of combining Menezes's ten claims for breach of fiduciary duty into one claim. Therefore, on remand, even though the court did not do so initially, I would urge the court to break down the acts alleged by Menezes separately, as one or more acts could be deemed a separate breach of fiduciary duty based on when each act occurred.

[1] Stephen B. Duerk was not a member of the board but was president of SCI and executed the merger agreement on its behalf.

[2] FITG refers to International Textile Group prior to the merger with SCI. After the merger, the newly formed entity took the name International Textile Group.

[3] According to Menezes's complaint, this exchange ratio had the effect of significantly diluting SCI stockholders' ownership in the newly formed entity.

18

[4] Appellants argued to the circuit court that Menezes could have brought his shareholder claim in the employment lawsuit. Menezes provided opposing counsel with a draft amended complaint in the employment lawsuit. That amended complaint contains an allegation, although stricken through, that the proposed merger agreement was made on unfair terms.

[5] MAC stands for materially adverse changes.

[6] Stephen Duerk filed an individual answer but asserts the same positions as all Appellants.

[7] Appellants then filed an appeal with this court requesting review of the entire circuit court's order. Menezes filed a motion to dismiss the appeal arguing the order was interlocutory. A single judge denied the motion but limited appellate review to the dismissal of Appellants' counterclaims and the striking of their affirmative defenses citing section 14-3-330(2)(c) of the South Carolina Code (1977). Appellants filed a petition for rehearing of this ruling, arguing the single issue on appeal (accrual of the breach of fiduciary duty claim) would determine all the points addressed in the circuit court's order. Ultimately a three-judge panel of this court affirmed the single judge's ruling limiting appellate review to the circuit court's dismissal of Appellants' counterclaims and the striking of Appellants' defenses. Therefore, we limit our discussion to those issues.

[8] Appellants raised to the circuit court at the hearing and in their motion for reconsideration whether Menezes's claim "may have been made" (under sub-paragraph 8 of the Release) in the employment lawsuit. The circuit court does not specifically address this point in its order. However, whether or not the claim may have been brought would seem to turn on whether or not the claim had accrued. Therefore, we believe that argument is subsumed in the accrual analysis.

[9] Lavine was a shareholder standing case as are many of the cases discussed herein. In Lavine, the issue was whether the plaintiff had standing to sue for breach of fiduciary duty relating to a merger when plaintiff purchased shares after the board's approval of the merger and the announcement of its terms but before the final shareholder vote. Id. at 550-51.

[10] Albert is a statute of limitations case.

STATE OF SOUTH CAROLINA
In the
Court of Appeals

APPEAL FROM COURT OF COMMON PLEAS
FOR GREENVILLE COUNTY
The Honorable Edward W. Miller, Circuit Court Judge
C.A. No. 2008-CP-23-2701
South Carolina Court of Appeals
Opinion No. 4810, filed March 23, 2011

RECEIVED
APR 07 2011
SC Court of Appeals

Brian P. Menezes, ...Respondent,

v.

WL Ross & Co. LLC, Wilbur, L. Ross, Jr.,
Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC, ...Appellants.

PETITION FOR REHEARING
With
PETITION FOR REHEARING *EN BANC*
(Opinion No. 4810, filed March 23, 2011)

Respondent petitions this Court for a rehearing and a rehearing *en banc* based on the grounds that the Court 1) did not recognize that the Merger agreement was conditional on third party approval which was not obtained until October 20, 2006, well after the release was executed; (2) did not consider the holding of *Teachers' Retirement System of Louisiana v. Aidinoff*, 900 A.2d 654 (Del. Ch. 2006), that a breach of fiduciary duty claim on an underlying contract that is subject to termination accrues at each point it is not terminated, and (3) did not correctly apply the holdings of *Int'l Bhd. Teamsters v. Coca-Cola Co.*, 954 A.2d 910 (Sup. 2008),

aff'g In re Coca-Cola Enterprises, Inc., 2007 WL 3122370 (Del. Ch. Oct. 17, 2007), and the cases which address claim accrual in the specific context of mergers. In short, while this Court's Opinion turns on whether Respondent could have filed suit to enjoin the merger after the announcement of the merger on August 30, 2006, the Opinion does not recognize that such a claim would have been entirely different than a claim alleging that the closing, or the failure to terminate the process, was a breach of fiduciary duty. As the *Teacher's* case instructs, where the underlying contract can be terminated, a new claim arises at each point when the contract can be terminated. Here the merger could have been terminated at any point prior to closing. Likewise, under *Coca-Cola*, because the conditions to closing had not been satisfied (e.g., the Wachovia consent had not been obtained), an actual breach of fiduciary duty claim based on the merger agreement could not have been brought prior to Closing. A prior claim would have had to have been based on some other theory.

A Memorandum in Support of Petition for Rehearing and Rehearing *En Banc* is being filed contemporaneously in support of this Petition.

William D. Herlong (S.C. Bar #14283)
The Herlong Law Firm, LLC
531 S. Main St., Ste. 201
P.O. Box 2003
Greenville, SC 29602-2003
Tel. (864) 382-3801
Fax (864) 752-0820


Thomas L. Stephenson (SC Bar #5332)
Russell T. Burke (SC Bar #1024)
Nexsen Pruet, LLC
PO Drawer 10648
Greenville, SC 29603
Tel (864) 370-2211

April 7, 2011

Attorneys for Respondent

[Execution]

AMENDMENT NO. 7 AND CONSENT
TO
LOAN AND SECURITY AGREEMENT

As of October 20, 2006

Wachovia Bank, National Association
110 East Broward Boulevard
Suite 2050
Fort Lauderdale, Florida 33301
Attention: Portfolio Manager

Re: Loan and Security Agreement, dated October 11, 2000, as Amended

Ladies and Gentlemen:

Wachovia Bank, National Association, successor by merger to Congress Financial Corporation (Southern) ("Lender"), Valentec Wells, LLC, formerly known as Valentec International Corporation, LLC ("Valentec"), Safety Components Fabric Technologies, Inc. ("SCFT"), Automotive Safety Components International, Inc. ("Automotive International"), Automotive Safety Components International GmbH & Co. KG ("German Borrower"), Automotive Safety Components International Limited ("UK Borrower" and together with Valentec, SCFT, Automotive International and German Borrower, individually each a "Borrower" and collectively, "Borrowers"), Safety Components International, Inc. ("Safety"), ASCI Holdings Germany (DE), Inc. ("ASCI Germany"), ASCI Holdings U.K. (DE), Inc. ("ASCI UK"), ASCI Holdings Mexico (DE), Inc. ("ASCI Mexico"), ASCI Holdings Czech (DE), Inc. ("ASCI Czech"), Automotive Safety Components International, S.A. de C.V. ("Automotive Safety Mexico") and Automotive Safety Components International s.r.o. ("Automotive Safety Czech" and together with Safety, ASCI Germany, ASCI UK, ASCI Mexico, ASCI Czech and Automotive Safety Mexico, each individually a "Guarantor" and collectively, "Guarantors") have entered into financing arrangements pursuant to which Lender has made and may, subject to certain terms and conditions, hereafter make loans and advances to Borrowers as set forth in the Loan and Security Agreement, dated October 11, 2000, by and among Lender, Borrowers and Guarantors, as amended by Amendment No. 1 and Consent to Loan and Security Agreement, dated as of November 2, 2001, Amendment No. 2 to Loan and Security Agreement, dated as of October 11, 2002, Amendment No. 3 and Consent to Loan and Security Agreement, dated as of October 8, 2003, Amendment No. 4 to Loan and Security Agreement, dated as of July 20, 2004, Amendment No. 5 and Consent to Loan and Security Agreement, dated as of October 1, 2004 and Amendment No. 6 and Consent to Loan and Security Agreement, dated as of October 6, 2006 (as the same now exists or may hereafter be amended, modified, supple-

738770.4

FURSA-0034963

mented, extended, renewed, restated or replaced, the "Loan Agreement") and other agreements, documents and instruments referred to therein or at any time executed and/or delivered in connection therewith or related thereto, together with this Amendment (all of the foregoing, including the Loan Agreement, as the same now exist or may hereafter be amended, modified, supplemented, extended, renewed, restated or replaced, being collectively referred to herein as the "Financing Agreements"). All capitalized terms used herein shall have the meaning assigned thereto in the Loan Agreement, unless otherwise defined herein.

WHEREAS, Safety, SCI Merger Sub, Inc., a Delaware corporation which is a wholly-owned Subsidiary of Safety ("Merger Sub") and International Textile Group, Inc., a Delaware corporation ("ITG"), have entered into the Agreement and Plan of Merger, dated as of August 29, 2006 (the "ITG Merger Agreement" as hereinafter further defined), pursuant to which Merger Sub will merge with and into ITG with ITG being the surviving corporation (the "ITG Merger"), all in accordance with the terms of the ITG Merger Agreement (as in effect on the date hereof);

WHEREAS, Borrowers and Guarantors have requested that Lender agree to, among other things, consent to the consummation of the ITG Merger; and

WHEREAS, Lender is willing to consent to such requests subject to the terms and conditions contained herein.

NOW THEREFORE, in consideration of the foregoing and the agreements and covenants contained herein, and for other good and valuable consideration, the adequacy and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

1. Amendments

(a) Definitions

Amendment to Definitions. The definition of "Subsidiary" in Section 1.09 of the Loan Agreement is hereby amended by adding the following at the end of such definition: "Notwithstanding anything to the contrary contained herein, and solely for purposes of the Loan Agreement and the other Financing Agreements, in no event shall any of the ITG Companies be deemed to be Subsidiaries of any Borrower or Guarantor."

(i) Additional Definitions. The following terms shall have the meanings given to them below and the Loan Agreement shall be deemed and is hereby amended to include, in addition and not in limitation, the following definitions:

(A) "Amendment No. 7" shall mean Amendment No. 7 and Consent to Loan and Security Agreement, dated as of October 20, 2006, by and among Lender, Borrowers and Guarantors.

(B) "ITG Companies" shall mean, collectively, ITG and its direct and indirect Subsidiaries; provided, that, in no event shall the ITG Companies include any Borrower or Guarantor.

(C) "ITG Merger Agreement" shall mean the Agreement and Plan of Merger, dated as of August 29, 2006, by and among ITG, Safety and Merger Sub.

2. Consent to ITG Merger. Subject to the terms and conditions contained herein and notwithstanding anything to the contrary contained in Section 9.7(a) of the Loan Agreement, Lender hereby consents to the consummation of the ITG Merger in accordance with the terms of the ITG Merger Agreement (as in effect on the date hereof); provided, that, each of the following conditions shall have been satisfied: (a) as of the effective date of the ITG Merger and after giving effect thereto, no Event of Default or act, condition or event which with notice or passage of time would constitute an Event of Default shall exist or have occurred and be continuing, (b) Lender shall have received true, complete and correct executed copies of the ITG Merger Agreement and all other material documents, agreements or instruments relating thereto to which any Borrower or Guarantor is a party or by which any Borrower or Guarantor (or its assets) is bound (together with the ITG Merger Agreement, the "ITG Merger Documents"), (c) no Borrower or Guarantor shall, directly or indirectly, pay or be liable for any merger consideration or any other amounts payable in connection with the ITG Merger, except that: (i) Safety may use shares of its common stock as merger consideration, and (ii) Safety may make cash payments for fractional shares and transaction expenses in connection with the ITG Merger up to the aggregate amount of \$3,000,000, so long as, both before and after giving effect to any such cash payment, the aggregate Excess Availability of Borrowers shall not be less than the US Dollar Equivalent of US\$15,000,000, (d) notwithstanding anything to the contrary in the Loan Agreement, in no event shall any Borrower or Guarantor: (i) become liable for any Indebtedness or other obligations (contingent or otherwise) of any of the ITG Companies or (ii) become liable for any Indebtedness or other obligations (contingent or otherwise) as a result of the ITG Merger except (as to this clause (ii) only) as otherwise permitted under the Loan Agreement, (e) notwithstanding anything to the contrary contained in the Loan Agreement, Borrowers and Guarantors shall not, and shall not permit any of their respective Subsidiaries (other than the ITG Companies) to, directly or indirectly, make loans or advances to, make any investments in, or pay any dividends to, any of the ITG Companies, (f) all actions and proceedings required by the ITG Merger Agreement, applicable law or regulation and the transactions contemplated thereby shall have been duly and validly taken in accordance with the terms thereof, and all required consents thereto shall have been obtained and be in full force and effect, and no court of competent jurisdiction shall have issued any injunction, restraining order or other order which prohibits the consummation of the transactions described in the ITG Merger Agreement or modifies such transactions, and no governmental or other action or proceeding shall have been commenced, seeking any injunction, restraining order or other order which seeks to void or otherwise modify the transactions described in the ITG Merger Agreement;

3. Representations, Warranties and Covenants. Each Borrower and Guarantor, jointly and severally, represents, warrants and covenants with and to Lender as follows, which representations, warranties and covenants are continuing and shall survive the execution and delivery hereof, the truth and accuracy of, or compliance with each, together with the

representations, warranties and covenants in the other Financing Agreements, being a continuing condition of the making or providing of any Loans or Letter of Credit Accommodations by Lender to Borrowers:

(a) neither the execution and delivery of this Amendment, or the documents, agreements or instruments executed or delivered in connection therewith or related thereto including, without limitation the ITG Merger Agreement (collectively, together with this Amendment, the "Amendment Documents") nor the consummation of the transactions herein or therein contemplated, nor compliance with the provisions hereof or thereof are in contravention of any law or regulation or any order or decree of any court or Governmental Authority applicable to Borrowers or Guarantors or any of their respective Subsidiaries, or conflict with or result in the breach of, or constitutes a default under any mortgage, deed of trust, security agreement, agreement or instrument to which any Borrower or Guarantor is a party or may be bound, or violates any provision of the Certificate of Incorporation, Certificate of Formation, Operating Agreement or By-Laws (or similar organizational documents) of any Borrower or Guarantor;

(b) the Amendment Documents have been duly authorized, executed and delivered by all necessary action on the part of each Borrower and Guarantor which is a party hereto and thereto and, if necessary, their respective equity holders, and the agreements and obligations of each Borrower and Guarantor contained herein and therein constitute legal, valid and binding obligations of each Borrower and Guarantor enforceable against such entities in accordance with their respective terms, except as such enforceability may be limited by bankruptcy, insolvency, moratorium or similar laws limiting creditors' rights generally and by general equitable principles;

(c) no consent, approval or other action of, or filing with or notice to any Governmental Authority is required in connection with the execution, delivery and performance of any of the Amendment Documents by any Borrower or Guarantor, except for those which have been made or obtained and are in full force and effect;

(d) all of the representations and warranties set forth in the Loan Agreement and the other Financing Agreements, each as amended hereby, are true and correct in all respects on and as of the date hereof as if made on the date hereof, except to the extent any such representation or warranty is made as of a specified date, in which case such representation or warranty shall have been true and correct as of such date;

(e) Borrowers and Guarantors have delivered to Lender true, complete and correct copies of all ITG Merger Documents;

(f) after giving effect to the consummation of the ITG Merger, Safety is Solvent; and

(g) no Event of Default or act, condition or event which with notice or passage of time or both would constitute an Event of Default, exists or has occurred and is continuing.

4. Conditions Precedent. The amendments and consents set forth herein shall be effective upon the satisfaction of each of the following conditions precedent in a manner satisfactory to Lender:

(a) Lender shall have received an original of this Amendment, duly authorized, executed and delivered by each of the parties hereto;

(b) all requisite corporate action and proceedings in connection with this Amendment and the other Amendment Documents shall be in form and substance satisfactory to Lender, and Lender shall have received all information and copies of all documents, including records of requisite corporate action and proceedings which Lender may have requested in connection therewith, such documents where requested by Lender or its counsel to be certified by appropriate corporate officers or governmental authorities;

(c) no Event of Default or act, condition or event which with notice or passage of time or both would constitute an Event of Default shall exist or have occurred and be continuing; and

(d) Lender shall have received a true and correct copy of any consent, waiver or approval to or of this Amendment or any of the other Amendment Documents, which any Borrower or Guarantor is required to obtain from any other Person, and such consent, approval or waiver shall be in form and substance satisfactory to Lender.

5. General.

(a) Effect of this Amendment. Except as expressly provided herein, no other changes or modifications to the Financing Agreements are intended or implied, and in all other respects the Financing Agreements are hereby specifically ratified, restated and confirmed by all parties hereto as of the date hereof. To the extent any conflict exists between the terms of this Amendment and the Financing Agreements, the terms of this Amendment shall control.

(b) Further Assurances. The parties hereto shall execute and deliver such additional documents and take such additional actions as may be necessary to effectuate the provisions and purposes of this Amendment.

(c) Governing Law. The rights and obligations hereunder of each of the parties hereto shall be governed by and interpreted and determined in accordance with the internal laws of the State of New York (without giving effect to principles of conflicts of laws or other rules of law that would result in the application of the law of any jurisdiction other than the State of New York).

(d) Binding Effect. This Amendment is binding upon and shall inure to the benefit of Lender, Borrowers, Guarantors and their respective successors and assigns. Any amendment or consent contained herein shall not be construed to constitute an amendment or consent to any other or further action by Borrowers or Guarantors or to entitle Borrowers or Guarantors to any other amendment or consent. The Loan Agreement and this Amendment shall be read and construed as one agreement.

(e) Counterparts, etc. This Amendment may be executed in one or more counterparts, each of which when so executed shall be deemed to be an original but all of which when taken together shall constitute one and the same instrument. In making proof of this Amendment, it shall not be necessary to produce or account for more than one counterpart hereof signed by each of the parties hereto. This Amendment may be executed and delivered by telecopier or other method of electronic transmission with the same force and effect as if it were a manually executed and delivered counterpart.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed and delivered by their respective duly authorized officers as of the date first written above.

SAFETY COMPONENTS FABRIC
TECHNOLOGIES, INC.

By: Vicki Coyle

Title: Treasurer

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL, INC.

By: Vicki Coyle

Title: Treasurer

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG

By: _____

Title: _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL LIMITED

By: Stephen B. Daniel

Title: President

VALENTEC WELLS, LLC (formerly known
as Valentec International Corporation, LLC)

By: Vicki Coyle

Title: Treasurer

[SIGNATURES CONTINUED ON NEXT PAGE]

[SIGNATURES CONTINUED FROM PREVIOUS PAGE]

738720.4

B-1

28

FURSA-0034969

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed and delivered by their respective duly authorized officers as of the date first written above.

SAFETY COMPONENTS FABRIC
TECHNOLOGIES, INC.

By: _____

Title: _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL, INC.

By: _____

Title: _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG

By:  *HD*

Title: HD

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL LIMITED

By: _____

Title: _____

VALENTEC WELLS, LLC (formerly known
as Valencor International Corporation, LLC)

By: _____

Title: _____

[SIGNATURES CONTINUED ON NEXT PAGE]

[SIGNATURES CONTINUED FROM PREVIOUS PAGE]

73K2704

B-1

29

FURSA-0034970

SAFETY COMPONENTS INTERNATIONAL, INC.

By: V. L. C. Co. Inc.

Title: Treasurer

ASCI HOLDINGS GERMANY (DE), INC.

By: V. L. C. Co. Inc.

Title: Treasurer

ASCI HOLDINGS U.K. (DE), INC.

By: V. L. C. Co. Inc.

Title: Treasurer

ASCI HOLDINGS MEXICO (DE), INC.

By: V. L. C. Co. Inc.

Title: Treasurer

ASCI HOLDINGS CZECH (DE), INC.

By: V. L. C. Co. Inc.

Title: Treasurer

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL, S.A. de C.V.

By: V. L. C. Co. Inc.

Title: Treasurer

[SIGNATURES CONTINUED ON NEXT PAGE]

[SIGNATURES CONTINUED FROM PREVIOUS PAGE]

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL S.R.O.

By: PAVEL MOOT

Title: DIRECTOR

AGREED:

WACHOVIA BANK, NATIONAL ASSOCIATION,
successor by merger to Congress Financial Corporation
(Southern)

By: _____

Title: _____

[Execution]

AFFIDAVIT OF EXECUTION AND DELIVERY

The undersigned _____ (the "Affiant") hereby deposes and says:

1. That Affiant is a duly authorized officer of Automotive Safety Components International GmbH & Co. KG ("German Borrower" and, together with certain other entities, individually each a "Borrower" and collectively, "Borrowers") or Automotive Safety Components International s.r.o. ("Automotive Safety Czech" and together with certain other entities, each individually a "Guarantor" and collectively, "Guarantors") for the purposes of executing and delivering, on behalf of each Borrower and Guarantor, certain loan documents executed outside of the State of Florida by borrowing customers of Wachovia Bank, National Association ("Wachovia").

2. On October 20, 2006, Affiant, acting as a duly authorized officer of German Borrower or Automotive Safety Czech, as applicable, executed Amendment No. 7 to Loan and Security Agreement, dated as of October 20, 2006, by and among Borrowers, Guarantors and Wachovia in the country of _____ and delivered it to Steven Cole of Wachovia in the State of North Carolina.

FURTHER AFFIANT SAYETH NOT.

Dated: October 20, 2006

**AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG**

By: _____

Title: _____

**AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL S.R.O.**

By: _____

Title: _____

[Execution]

AFFIDAVIT OF EXECUTION AND DELIVERY

The undersigned _____ (the "Affiant") hereby deposes and says:

1. That Affiant is a duly authorized officer of Automotive Safety Components International GmbH & Co. KG ("German Borrower" and, together with certain other entities, individually each a "Borrower" and collectively, "Borrowers") or Automotive Safety Components International s.r.o. ("Automotive Safety Czech" and together with certain other entities, each individually a "Guarantor" and collectively, "Guarantors") for the purposes of executing and delivering, on behalf of each Borrower and Guarantor, certain loan documents executed outside of the State of Florida by borrowing customers of Wachovia Bank, National Association ("Wachovia").

2. On October 20, 2006, Affiant, acting as a duly authorized officer of German Borrower or Automotive Safety Czech, as applicable, executed Amendment No. 7 to Loan and Security Agreement, dated as of October 20, 2006, by and among Borrowers, Guarantors and Wachovia in the country of _____ and delivered it to Steven Cole of Wachovia in the State of North Carolina.

FURTHER AFFIANT SAYETH NOT.

Dated: October 20, 2006

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG

By: _____

Title: _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL S.R.O.

By: PAVEL MODZ 

Title: DIRECTOR

STATE OF SOUTH CAROLINA

In the
Court of Appeals

APPEAL FROM COURT OF COMMON PLEAS
FOR GREENVILLE COUNTY
The Honorable Edward W. Miller, Circuit Court Judge
C.A. No. 2008-CP-23-2701
South Carolina Court of Appeals
Opinion No. 4810, filed March 23, 2011

RECEIVED
APR 07 2011
SC Court of Appeals

Brian P. Menezes, ...Respondent,

v.

WL Ross & Co. LLC; Wilbur, L. Ross, Jr.,
Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC, ...Appellants.

MEMORANDUM IN SUPPORT OF PETITION FOR REHEARING
With
PETITION FOR REHEARING *EN BANC*
(Opinion No. 4810, filed March 23, 2011)

William D. Herlong (S.C. Bar #14283)
The Herlong Law Firm, LLC
531 S. Main St., Ste. 201
P.O. Box 2003
Greenville, SC 29602-2003
Tel. (864) 382-3801
Fax (864) 752-0820

Thomas L. Stephenson (SC Bar #5332)
Russell T. Burke (SC Bar #1024)
Nexsen Pruet, LLC
PO-Drawer-10648
Greenville, SC 29603
Tel (864) 370-2211

April 7, 2011

Attorneys for Respondent

TABLE OF CONTENTS

TABLE OF AUTHORITIES	4
STATEMENT OF THE CASE.....	7
SUMMARY OF ARGUMENT	11
ARGUMENT.....	13
I. The Trial Court Correctly Held That Respondent's Breach Of Fiduciary Duty Claims Did Not Accrue Before The Closing Of The Merger On October 20, 2006, Well After The Release Was Executed On September 28, 2006.....	13
A. The General Principles Of Claim "Accrual" Under Delaware Law.....	13
B. Under These Principles of Delaware Law, As Shown By The <i>Coca-Cola</i> Case From The Delaware Supreme Court, A Fiduciary Duty Claim That Relates To An Underlying Contract Accrues When The Contract Becomes <i>Legally</i> <i>Enforceable</i>	14
C. Under <i>Coca-Cola</i> , Respondent's Claims Could Not Have Accrued Prior To The Closing Since the Merger Agreement Was Not Legally <i>Enforceable</i> Until That Time.....	17
D. The <i>Teachers</i> Case Confirms That Respondent's Claims Could Not Have Accrued Since The Merger Was Subject To Cancellation on Short Notice, Just Like the Contract in <i>Teachers</i>	21
E. Every Case To Address The Issue of Claim Accrual In The Context Of A Merger Has Held That Such Claims Accrue Upon The Closing Of The Merger, Just As <i>Coca-Cola</i> and <i>Teachers</i> Dictate.	22
E. The Shareholder "Standing" Cases Appellants Rely Upon Do Not Support Their Argument.....	28
1. Those Cases Deal With "Standing" And Not Claim "Accrual" And Thus Are Not Applicable.....	28

2.	The "Standing" Cases Do Not Apply If The Closing Of A Merger Is Not A Mere "Technicality."	30
3.	The "Standing" Cases Support Respondent's Position Because He Is Challenging The <i>Fact</i> Of The Merger, Not Merely Its <i>Terms</i>	32
CONCLUSION.....		36

TABLE OF AUTHORITIES

Cases

<i>7547 Partners v. Beck</i> , 682 A.2d 160 (Del. 1996)	35, 36
<i>Albert v. Alex. Brown Mgmt. Servs., Inc.</i> , 2005 Del. Ch. LEXIS 100, 2005 WL 1594085 (June 29, 2005)	passim
<i>Baron v. Allied Artists Pictures Corporation</i> , 717 F.2d 105 (3d Cir. 1983)	passim
<i>Bilinski v. Farmers Bank of State</i> , 1982 WL 172848 (Del. Super. Nov. 9, 1982)	11
<i>Bren v. Capital Realty Group Senior Housing, Inc.</i> , 2004 WL 370214 (Del. Ch. Feb. 27, 2004)	23, 24
<i>Brown v. Automated Mktg. Sys., Inc.</i> , 1982 WL 8782 (Del. Ch. Mar. 22, 1982)	passim
<i>Cannon & Son, Inc. v. Fidelity & Casualty Co.</i> , 484 F. Supp. 1375 (D. Del. 1980)	22
<i>City of Newark v. Edward H. Richardson Associates, Inc.</i> , 375 A.2d 475 (Del. Super. 1977)	10
<i>City of Philadelphia v. Lieberman</i> , 112 F.2d 424 (3d Cir. 1940)	22
<i>Dofflemyer v. W.F. Hall Printing Company</i> , 558 F. Supp. 372 (D. Del. 1983)	passim
<i>Freedman v. Beneficial Corporation</i> , 406 F. Supp. 917 (D. Del. 1975)	10, 22
<i>Grayson v. Harris</i> , 279 U.S. 300 (1929)	22
<i>Howmet Corp. v. City of Wilmington</i> , 285 A.2d 423 (Del. Super. 1971)	10
<i>In re Beatrice Cos., Inc. Litig.</i> , 522 A.2d 865 (Del. 1987)	passim
<i>Int'l Bhd. Teamsters v. Coca-Cola Co.</i> , 954 A.2d 910 (Sup. 2008), <i>aff'g</i>	

<i>In re Coca-Cola Enterprises, Inc.</i> , 2007 WL 3122370 (Del. Ch. Oct. 17, 2007)	passim
<i>Kahn v. Seaboard Corporation</i> , 625 A.2d 269 (Del. Ch. 1993).....	12, 13, 14, 19
<i>Kaufman v. Albin</i> , 447 A.2d 761 (Del. Ch. 1982).....	passim
<i>Kaufman v. C.L. McCabe & Sons, Inc.</i> , 603 A.2d 831 (Del. 1992)	9
<i>Krahmer v. Christie's Inc.</i> , 903 A.2d 773 (Del. Ch. 2006).....	9
<i>Lembert v. Gilmore</i> , 312 A.2d 335 (Del. Super. Ct. 1973).....	22
<i>Marvel Enter. Group, Inc. v. Mafco Holdings, Inc.</i> (<i>In re Marvel Enter. Group, Inc.</i>), 273 B.R. 58 (D. Del. 2002).....	14
<i>Montgomery v. Aetna Plywood Inc.</i> , 231 F.3d 399 (7 th Cir. 2000)	36, 38
<i>Montgomery v. Aetna Plywood, Inc.</i> , 956 F. Supp. 781 (N.D. Il. 1997)	24
<i>Nardo v. Guido DeAscanis & Sons, Inc.</i> , 254 A.2d 254 (Del. Super. Ct. 1969)	9, 10, 22, 26
<i>Newkirk v. W.J. Rainey, Inc.</i> , 76 A.2d 121 (Del. Ch. 1950).....	36
<i>Rose Hall, Ltd. v. Chase Manhattan Overseas Bank</i> , 494 F. Supp. 1139 (D. Del.1980).....	22
<i>State ex rel. Secretary of Dept. of Transp. v. Regency Group, Inc.</i> , 598 A.2d 1123 (Del. Super. 1991).....	9
<i>Teachers' Retirement System of Louisiana v. Aidinoff</i> , 900 A.2d 654 (Del. Ch. 2006) ..	19, 20, 32, 39
<i>Tooley v. Donaldson, Lufkin & Jenrette, Inc.</i> , 2003 WL 203060 (Del. Ch. Jan. 21, 2003).....	18
<i>Tooley v. Donaldson, Lufkin & Jenrette, Inc.</i> , 845 A.2d 1031 (Del. 2004)	18

United States v. Wurts,
303 U.S. 414 (1938)..... 22

Wal-Mart Stores, Inc. v. AIG Life Ins. Co.,
860 A.2d 312 (Del. 2004) 13, 14

Weiss v. Northwest Broadcasting Inc.,
140 F. Supp. 2d 336 (D. Del. 2001)..... 19

Other Authorities

C.J.S., *Limitations of Actions*, §109..... 26

Treatises

Edward P. Welch, et al., *Folk on Delaware General
Corporation Law*, Sec. 327.3.2 (5th Ed. 2006 & Supp. 2007) 33, 34

Folk, *The Delaware General Corporation Law* (1967)..... 34

Rubenstein, Conte and Newberg,
7 Newberg on Class Actions, §22:95 (4th ed. 2009)..... 32

STATEMENT OF THE CASE

The Complaint in this action was filed on April 9, 2008. It concerns a Merger that occurred on October 20, 2006, in which a North Carolina private company known as International Textile Group, Inc. (hereinafter "former ITG" or "FITG"), merged into a public company then based in Greenville and known as Safety Components International, Inc. ("SCI"). After the merger, the combined company was renamed "International Textile Group, Inc." (hereinafter "new ITG" or "NITG"). (Compl. ¶¶20, 1 & 10 [R. pp. 11, 6, & 8].) SCI provided consideration worth \$167 million in connection with the Merger. (*Id.* ¶29 [R. p. 13].)

Appellants controlled SCI, owning a 75.6% interest in the company and having four of the five directors on the Board. They also controlled FITG, owning a 85.4% interest in that company and having five of the six directors on the Board. (*Id.* ¶¶7, 9 & 12 [R. pp. 8-9].) Consistent with their ownership of FITG, they received more than \$130 million of the consideration for the Merger they engineered. (*Id.* ¶¶30-31 [R. pp. 13-14].) It was, therefore, a self-dealing transaction and subject to the "entire fairness" standard of review. (*Id.* ¶¶ 97-98 & 103 [R. pp. 28-29].)

Respondent was a minority shareholder in SCI before the announcement of the Merger and has continued to be a minority shareholder in the company (now NITG) since the Merger. (*Id.* ¶4 [R. p. 7].) He alleges that FITG's business was collapsing financially at the time of the Merger, a fact which was revealed in the NITG 10-K six months after the Merger. (*Id.* ¶50 [R. p. 17].) In the weeks prior to the Merger, FITG is alleged to have been losing more than eight million dollars each month. (*Id.* ¶52, [R. p. 17].) It appeared

to have borrowed \$31 million between September 22, 2006, when the Proxy¹ was issued, and October 20, 2006, when the Merger closed (the “Closing”). (*Id.* ¶65 [R. p. 20].) The equity associated with its business declined from \$123 million at the end of the first half of 2006 to approximately \$80 million at the end of that year. (*Id.* ¶58 [R. p. 19].)

Respondent alleges that Appellants violated their fiduciary duties as the controlling shareholder and officers and directors of SCI by, among other things, “proposing the Merger and then *allowing it to close notwithstanding the financial condition of FITG*” and “*by failing to call off or renegotiating the Merger (or cause it to be called off or renegotiated) because of the financial condition of FITG.*” (*Id.* ¶¶99(a) & (g) & 104(a) & (g), emphasis added [R. pp. 28-30].) He seeks to represent a class composed of the minority shareholders of SCI. (*Id.* ¶89 [R. p. 26].)

In response, Appellants asserted affirmative defenses and a counterclaim and moved for judgment on the pleadings or in the alternative for summary judgment based on a release (the “Release”) that Respondent had executed on September 28, 2006, to resolve a separate lawsuit. That lawsuit was an employment action by Respondent against SCI and its CEO, Appellant Gorga, relating to Respondent’s dismissal without cause from SCI and seeking payment of wages and a declaratory judgment regarding his entitlement to a future bonus. (*See Complaint, Menezes v. Safety Components International, Inc., and Gorga, C.A. 2006-CP-23-4326* [R. pp. 517-551].) It was resolved by a settlement in which Respondent released all claims he “has had or now has” against

¹ The complete Proxy, dated September 22, 2006, can be found online at: <http://www.sec.gov/Archives/edgar/data/918964/000119312506195834/d424b3.htm> (R. pp. 756-1110).

the "Released Parties"² "up to and including the date of execution hereof [September 28, 2006]." (Release, ¶7 [R. p. 610].) With regard to shareholder claims specifically, the Release stated that it applied to "any claim based upon or as an owner of any stock or interest in any of the Released Parties *arising prior to the execution of this Confidential Settlement Agreement* [September 28, 2006]." (*Id.*, emphasis added.)

Oral argument on the motion took place before Judge Edward W. Miller on July 31, 2008. Multiple supplemental briefs were filed as issues were further fleshed out. On February 17, 2009, the trial court issued an order denying Appellants' motion. The court wrote:

Plaintiff alleges that the defendants breached their fiduciary duties to the minority shareholders of SCI (including the plaintiff) by allowing the merger to go forward or close. . . .

The pertinent question is whether Plaintiff's claims regarding the merger accrued when the merger closed on October 20, 2006, as Plaintiff contends, or sometime prior to September 28, 2006, as Defendants argue.

(Order of Feb. 17, 2009, at 1-2 [R. pp. 1-2].)

The court found that there were "extensive conditions precedent to the merger that were not satisfied before the closing date." Accordingly, Respondent's claims "accrue[d] no earlier than the closing of the Merger":

Under controlling Delaware law, these claims accrue no earlier than the closing of the merger. *Kaufman v. Albin*, 447 A.2d 761 (Del. Ch. 1982) (claim accrues on closing of merger); *see also Dofflemyer v. W.F. Hall Printing Company*, 558 F. Supp. 372 (D. Del. 1983) (same); *cf. Baron v. Allied Artists Pictures Corporation*, 717 F.2d 105 (3d Cir. 1983) (claim

² "Released Parties" were defined as Gorga and SCI, and "any parent, subsidiary and affiliated person, company, business, entity or enterprise of Gorga and [SCI], along with all current and former officers, directors, agents, employees, insurers, representatives, attorneys, successors, and assigns of the same, which shall also include by way of enumeration but not limitation, [FITG], W.L. Ross & Co. L.L.C., and David L. Wax." (Release ¶7 [R. p. 610].)

accrues when merger consummated). This is especially true here since there were extensive conditions precedent to the merger that were not satisfied before the closing date. The merger could not have been enforced by FITG against SCI prior to the closing date. As recently re-affirmed by the Delaware Supreme Court, there can be no breach of fiduciary duty claim regarding an underlying contract until the contract is legally enforceable. See *Int'l Bhd. Teamsters v. Coca-Cola Co.*, [954 A.2d 910] (Del. Sup. 2008), *aff'g In re Coca-Cola Enterprises, Inc.*, 2007 WL 3122370 (Del. Ch. [Oct. 17,] 2007) (no claim regarding underlying contract until "enforceable legal rights . . . were created.") Accordingly, since FITG had no right to enforce the merger until the closing date, plaintiff's claims for breach of fiduciary duty did not accrue until that date.

(*Id.* at 2 [R. p. 2].)

In addition to denying Appellants' motion, the court, at Appellants' request (Letter, Mabry to Court, Feb. 10, 2006 [R. pp. 750-752]), also struck their affirmative defenses based on the Release and granted Respondent's motion to dismiss their counterclaim based on the Release. (Order at 2 [R. p. 2].)

Appellants' motion for reconsideration was denied on March 4, 2009. (R. p. 3.) The Notice of Appeal was filed on March 5, 2009. (R. pp. 389-392.)

The Court of Appeals filed its decision on March 23, 2011. It held that it was error for the circuit court to dismiss Appellants' defenses and counterclaim relating to the Release. Accordingly, the Court reversed and remanded to circuit court.

Appellant now files this Petition for Rehearing and Rehearing *En Banc*.

SUMMARY OF ARGUMENT

The essence of Respondent's claims against Appellants, the officers, directors, and controlling shareholders of SCI, is that they breached their fiduciary duties to him as a minority shareholder by allowing the merger between SCI and FITG to close on October 20, 2006, even though FITG was in disastrous financial condition. As revealed in the 10-K filed six months later, in the period before the merger, FITG was losing millions of dollars each week. It appeared to have borrowed \$31 million in the month before the merger. Its equity value dropped by more than a third from the end of the first half of 2006 to the end of the second half.

The trial court held that the Release Respondent executed on September 28, 2006, to resolve his employment dispute with SCI had no application to the claims in this action. It applied only to claims that accrued prior to its execution, while the Merger closed more than three weeks after the Release was executed.

Delaware law is clear that a breach of fiduciary duty claim regarding an underlying contract does not accrue until the underlying contract is legally "enforceable." The Merger agreement was not legally "enforceable," as the trial court held, until October 20, 2006, at the earliest because of the conditions precedent which could not and have been and were not satisfied before that time. Accordingly, Respondent's claims could not have accrued prior to then. Further, as to the financial conditions in the agreement, they could not have been satisfied at all in light of how FITG was hemorrhaging money. They had to have been waived at the Closing. It is the waiver of those conditions, effectively, that Respondent alleges was a breach of fiduciary duty. That claim, obviously, accrued at the Closing when the conditions were waived.

All three cases addressing the issue of when a breach of fiduciary duty claim regarding a merger accrues hold that the claim accrues at the closing of the merger, as one would expect. The cases cited by Appellants and reviewed by this Court do not address that question but go to the issue of whether a shareholder has "standing." The sensible rule in Delaware and many other states is that a shareholder who wishes to challenge the terms of a merger cannot purchase his stock after those terms are publicly announced.

Appellants' "standing" cases (assuming they are relevant here) cannot be interpreted to hold that claims such as Respondent's accrue before the underlying agreement is "enforceable," as Appellants argue. To do so (aside from taking them beyond their holdings) would specifically violate long-standing Delaware law. Accordingly, even under those cases, Respondent's claims could not accrue until the closing of the Merger.

Accordingly, the decision of the trial court was exactly correct. It should be affirmed.

ARGUMENT

I. The Trial Court Correctly Held That Respondent's Breach Of Fiduciary Duty Claims Did Not Accrue Before The Closing Of The Merger On October 20, 2006, Well After The Release Was Executed On September 28, 2006.

A. The General Principles Of Claim "Accrual" Under Delaware Law.

There is nothing particularly unusual about Delaware's law on the accrual of tort claims. The long-standing principle is that such claims "accrue at the time of *the injury*." *Nardo v. Guido DeAscanis & Sons, Inc.*, 254 A.2d 254, 256 (Del. Super. Ct. 1969) (emphasis added) ("A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of the injury."); *see also, e.g., Kaufman v. C.L. McCabe & Sons, Inc.*, 603 A.2d 831 (Del. 1992) ("A cause of action in tort accrues at the moment when "an injury, although slight, is sustained in consequence of the wrongful act of another...."); *Krahmer v. Christie's Inc.*, 903 A.2d 773 (Del. Ch. 2006) ("For tort claims, a cause of action accrues at the time of the injury."); *State ex rel. Secretary of Dept. of Transp. v. Regency Group, Inc.*, 598 A.2d 1123, 1128 (Del. Super. 1991) ("Tort actions accrue at the time of injury."); *City of Newark v. Edward H. Richardson Associates, Inc.*, 375 A.2d 475, 476 (Del. Super. 1977) ("It has been held repeatedly that tort actions accrue at the time of the injury and that the statute of limitations begins to run at that time."); *Freedman v. Beneficial Corporation*, 406 F. Supp. 917 (D. Del. 1975) ("Causes of action sounding in tort, such as this one, accrue at the time of injury."); *Howmet Corp. v. City of Wilmington*, 285 A.2d 423, 425 (Del. Super. 1971) (citing *Nardo*).

Indeed, while in a contract case it is the “breach” which is the wrongful act, in a tort case it is the “injury” that is the “wrongful act.” *Bilinski v. Farmers Bank of State*, 1982 WL 172848, *2 (Del. Super. Nov. 9, 1982) (“In Delaware it is well settled that the limitations period begins to run at the time of the wrongful act. . . . A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of injury.”)

B. Under These Principles of Delaware Law, As Shown By The Coca-Cola Case From The Delaware Supreme Court, A Fiduciary Duty Claim That Relates To An Underlying Contract Accrues When The Contract Becomes *Legally Enforceable*.

It would seem plain from these principles of Delaware (and general) law that a breach of fiduciary duty claim relating to an underlying contract would not accrue until the underlying contract becomes legally enforceable. It would be an enormous waste of judicial resources to allow litigation of “hypothetical” matters, matters that may or may not occur. *See Baron v. Allied Artists Pictures Corporation*, 717 F.2d 105, 109 (3d Cir. 1983) (“the necessary effect of the trial court’s confusion of the separate issues of accrual and tolling would be to encourage lawsuits which in many instances would be premature”).

This principle is confirmed in the recent Delaware Supreme Court decision in *Int’l Bhd. Teamsters v. Coca-Cola Co.*, 954 A.2d 910 (Del. 2008), affirming *In re Coca-Cola Enterprises, Inc.*, 2007 WL 3122370 (Del. Ch. Oct. 17, 2007). That case involved a “Master Bottle Contract” between the Coca-Cola Company and one of its distributors that had been entered into in 1986. The plaintiffs were complaining “about the painful effects of the terms of the 1986 MBC” 2007 WL 3122370 at *4. There were apparently no conditions precedent to performance of the contract and thus no “closing” after it was

signed. "Execution" and "closing" were one and the same. The court, relying on *Kahn v. Seaboard Corporation*, 625 A.2d 269 (Del. Ch. 1993), held that the wrong "occurred at the time that enforceable legal rights [in the 1986 MBC] . . . were created." 2007 WL 3122370 at *5 (quoting *Kahn*, 625 A.2d at 271). Accordingly, the plaintiff's claims accrued in 1986 when the MBC contract had been entered into since that was when "enforceable legal rights . . . were created." This Court's Opinion cited this language from *Coca-Cola*, and the underlying *Kahn* decision, but, respectfully, did not properly apply those decisions to the facts of this case.

Kahn was a derivative action against the controlling stockholder and three members of the board of Seaboard Corporation. The alleged wrong was the defendants' use of their control over Seaboard to cause it to enter into a ten-year lease contract that was detrimental to it and beneficial to them. As in *Coca-Cola*, there were apparently no conditions precedent to performance of the contract, no "closing" after it was signed, and "execution" and "closing" were one and the same. The defendants argued that the claims were barred by the statute of limitations. The court held that the wrong "occurred at the time that enforceable legal rights against Seaboard [under the lease contract] were created." 625 A.2d at 271. Accordingly, since the lease contract had been immediately enforceable, the claims had accrued when it was entered into in 1986 and were time-barred.

This Court's discussion of *Coca-Cola* and *Kahn* does not address the distinction that neither of those cases involved conditions precedent to enforcement of the underlying contract. That is not the case here. Further, under those cases, as the trial court held, there can be no claim that it was a breach of fiduciary duty for a board to

authorize entry into a contract before that contract became legally “enforceable.” Indeed, if Appellants’ theory were correct, the breach of fiduciary duty claims in *Coca-Cola* and *Kahn* would have accrued even earlier, when the defendants in each case *authorized* entry into the contracts at issue. In fact, this is exactly how Appellants presented the holding to the trial court below. At the hearing on the motion, Appellants’ counsel represented that *Coca-Cola* had held that that claim accrued from the “*approving* [of] the terms of the agreement.” (Hearing Tr. 15:16-19 [R. p. 566].) That representation to the court was flatly wrong. *Coca-Cola* held that the claim accrued when “enforceable legal rights” were created in the underlying contract, not when the contract was “approved.”

The same is true for *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 860 A.2d 312 (Del. 2004). That case involved Wal-Mart’s purchase of various life insurance (“COLI”) policies between 1993 and 1995. The company alleged that the defendants failed to disclose material facts and risks of the plan to purchase the COLI policies. *Id.* at 317. As in *Coca-Cola* and *Kahn*, there were apparently no conditions precedent and no “gap” between the “execution” of the contracts and the “closing.” The court held that Wal-Mart’s claim had accrued when it purchased the COLI policies, which would have been the point at which those contracts were enforceable against it. Again, as in *Coca-Cola*, it is noteworthy that the court did not hold, as would be expected if Appellants’ theory were valid, that the claim accrued even earlier when the defendants had received proposals from various insurance companies and recommended that Wal-Mart purchase the COLI policies of AIG and Hartford. 860 A2d. at 315.³

³ Appellants also cite *Marvel Enter. Group, Inc. v. Mafco Holdings, Inc. (In re Marvel Enter. Group, Inc.)*, 273 B.R. 58 (D. Del. 2002), as supporting their theory. Again, as with *Coca-Cola*, *Kahn*, and *Wal-Mart*, Appellants have the import of the case

Since, as shown in the next section, the Merger Agreement did not become “enforceable” until the Closing date, as the trial court found, Respondent’s claims could not have accrued until that time.

C. Under *Coca-Cola*, Respondent’s Claims Could Not Have Accrued Prior To The Closing Since the Merger Agreement Was Not Legally Enforceable Until That Time.

The Merger Agreement, as one might expect for a \$167 million deal, was long and detailed, over fifty single-spaced pages. (Proxy, Annex A [R. pp. 1035-1090].) The “conditions precedent” section alone was several single-spaced pages long. (*Id.*, Annex A at A34-A36 [R. pp. 1072-1074].) The conditions were so important that they were separately summarized in the main body of the Proxy. The summary itself was more than two single-spaced pages long. (Proxy at 82-83, emphasis added [R. pp. 850-851]; see also Merger Agreement, Proxy at A34-A36 [R. pp. 1072-1074].)

Further, apart from the explicit conditions precedent, the transaction was subject to multiple termination events, any one of which could have killed it. For example, it could be terminated by “mutual agreement” of SCI and ITG, which meant that it could be terminated by Appellants at any time since they controlled SCI and ITG. It could be terminated by either party “if the merger shall not have been consummated by March 31, 2007.” It could be terminated by either party if SCI had not amended its certificate of

backwards. The relevant claim there was based on the terms and conditions of a tax sharing agreement. It was alleged that the defendant parent company and directors breached their fiduciary duty by causing the defendant’s subsidiary to enter into that agreement with the parent company. The court held that the claim accrued when the contract was adopted. *Id.* at 73. This is consistent with *Coca-Cola* since that was the point in time when it became enforceable. If Appellants’ theory were correct, as with *Coca-Cola*, *Kahn*, and *Wal-Mart*, the claim would have accrued even earlier, when the defendant-directors voted to *authorize* the company to enter into the tax sharing agreement.

incorporation or ITG stockholders had not approved the merger agreement by March 31, 2007. And it could be terminated by either party if the other “breached or failed to perform” in any “material respect” any of the representations or warranties and the failure had not been cured in thirty days of written notice. (Proxy at 83-84 [R. pp. 851-852].)

Accordingly, it cannot be seriously disputed, as held by the trial court, that the Merger was subject to “extensive conditions precedent.” (Order at 2 [R. p. 2].) For example, approval had to be obtained from FITG shareholders. SCI shareholders had to approve the amendment to its certificate of incorporation.⁴ The representations and warranties as to the businesses had to be true as of the Closing date. There had to be no material adverse changes as of the Closing date in either company and the fairness opinions could not have been withdrawn (both key provisions in light of how FITG was hemorrhaging money at the time of the merger⁵). Further, the Escrow Agreement through which the Merger would be accomplished had to have been duly executed.

These were fundamental conditions to the merger and not mere “technicalities.” Indeed, the whole point, for example, of the representations and warranties and the “no material adverse effect”⁶ clauses in mergers is to ensure that a merger partner’s business

⁴ The SCI annual shareholder meeting to adopt the required amendments to its certificate of incorporation was not even scheduled to occur until October 20, 2006. (See Proxy at viii [R. p. 763].)

⁵ The Complaint alleges that FITG was in disastrous financial condition at the time of the Merger, as revealed in the NITG 10-K six months after the Merger. At the time of the Merger, it was losing nearly \$2 million a week and \$8 million a month; it appeared to have borrowed \$31 million in the *four weeks* between the issuance of the Proxy on September 22, 2006 and the Merger on October 20, 2006; and the equity associated with its business declined from \$123 million at the end of the first half of 2006 to approximately \$80 million at the end of that year. (Complaint ¶¶50, 52, 65, & 58 [R. pp. 17 & 19-20].)

⁶ The Merger agreement (Proxy, A-46 [R. p. 1084]) defines this term as follows:

remains essentially the same when the merger takes place as when it was agreed to. And proposed mergers are cancelled or go "bust" all the time when that does not happen. Indeed, the financial press make something of a "sport" of tracking this. (See, e.g., "Buyouts Gone Bust," Ex. A to Pltf's 2nd Mem. In. Opp. To Defs' Mot. To Dismiss [R. pp. 363-366].) It is highly likely that a sophisticated New York LBO firm such as Appellant W.L. Ross & Co. has cancelled many deals for these reasons.

In any event, it is now completely clear that the Merger was subject to conditions outside the control of any party to the agreement. The lender, Wachovia Bank, had to approve of the merger and a modification of its lending agreement with SCI. That consent was not obtained until October 20, 2006, the date the Merger closed and weeks after the Release was filed. The consent executed by Wachovia reads, in pertinent part:

2. Consent to ITG Merger. Subject to the terms and conditions contained herein and notwithstanding anything to the contrary contained in Section 9.7(a) of the Loan Agreement, Lender hereby consents to the consummation of the ITG Merger in accordance with the terms of the ITG Merger Agreement (as in effect on the date hereof); provided, that, each of the following conditions shall have been satisfied: (a) as of the effective date of the ITG Merger and after giving effect thereto, no Event of Default or act, condition or event which with notice or passage of time would constitute an Event of Default shall exist or have occurred and be continuing, (b) Lender shall have received true, complete and correct executed copies of the ITG Merger Agreement and all other material

"Material Adverse Effect" means, when used in connection with ITG or SCI, any change, effect, event, occurrence or state of facts (i) that is materially adverse to the business, operations, conditions (financial or otherwise), assets or liabilities of such party (or the Surviving Corporation when used with respect to ITG) and its Subsidiaries, taken as a whole, or (ii) preventing or materially delaying the consummation of the Merger, other than any change, effect, event, occurrence or state of facts (x) relating to the economy in general which does not have a disproportionate impact on such party or (y) relating to the industries in which such party operates in general and not specifically relating to such party".

documents, agreements or instruments relating thereto to which any Borrower or Guarantor is a party or by which any Borrower or Guarantor (or its assets) is bound (together with the ITG Merger Agreement, the "ITG Merger Documents"), (c) no Borrower or Guarantor shall, directly or indirectly, pay or be liable for any merger consideration or any other amounts payable in connection with the ITG Merger, except that: (i) Safety may use shares of its common stock as merger consideration, and (ii) Safety may make cash payments for fractional shares and transaction expenses in connection with the ITG Merger up to the aggregate amount of \$3,000,000, so long as, both before and after giving effect to any such cash payment, the aggregate Excess Availability of Borrowers shall not be less than the US Dollar Equivalent of US\$15,000,000, (d) notwithstanding anything to the contrary in the Loan Agreement, in no event shall any Borrower or Guarantor: (i) become liable for any Indebtedness or other obligations (contingent or otherwise) of any of the ITG Companies or (ii) become liable for any Indebtedness or other obligations (contingent or otherwise) as a result of the ITG Merger except (as to this clause (ii) only) as otherwise permitted under the Loan Agreement, (e) notwithstanding anything to the contrary contained in the Loan Agreement, Borrowers and Guarantors shall not, and shall not permit any of their respective Subsidiaries (other than the ITG Companies) to, directly or indirectly, make loans or advances to, make any investments in, or pay any dividends to, any of the ITG Companies, (f) all actions and proceedings required by the ITG Merger Agreement, applicable law or regulation and the transactions contemplated thereby shall have been duly and validly taken in accordance with the terms thereof, and all required consents thereto shall have been obtained and be in full force and effect, and no court of competent jurisdiction shall have issued any injunction, restraining order or other order which prohibits the consummation of the transactions described in the ITG Merger Agreement or modifies such transactions, and no governmental or other action or proceeding shall have been commenced, seeking any injunction, restraining order or other order which seeks to void or otherwise modify the transactions described in the ITG Merger Agreement; . . . [7]

It cannot be disputed that, under Delaware law, until all of the conditions precedent in the Merger agreement were satisfied, the Merger was not legally

⁷ A copy of the consent is not in the record as it had not been discovered at that time. It is, however, a public document filed with the SEC (at <http://www.sec.gov/Archives/edgar/data/918964/000119312506216011/dex101.htm>) of which the Court may take judicial notice. A complete copy of the letter as filed with the SEC is attached to this Motion. In accordance with the Appellate Rules, Respondent is also filing a Motion to Supplement the Record on Appeal.

“enforceable.” The Delaware Supreme Court has recently made this point very plainly: a “merger agreement” only becomes “binding and mutually enforceable” when “the conditions of the agreement [are] met.” *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1034-35 (Del. 2004), quoting *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 2003 WL 203060 (Del. Ch. Jan. 21, 2003) (“Second, any contractual shareholder right to payment of the merger consideration did not ripen until the conditions of the agreement were met. . . . The merger agreement only became binding and mutually enforceable at the time the tendered shares ultimately were accepted for payment by Credit Suisse Group. 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.”); *see also Weiss v. Northwest Broadcasting Inc.*, 140 F. Supp. 2d 336 (D. Del. 2001) (“As a general matter, a condition precedent is an act or event, other than a lapse of time, which, unless the condition is excused, must occur before a duty to perform a promise in the agreement arises.”), *citing Gilbert v. El Paso Co.*, 575 A.2d 1131, 1142 (Del. 1990).

Hence, as *Coca-Cola* and *Kahn* instruct and as the trial court held, Respondent’s breach of fiduciary duty claims concerning the Merger did not accrue prior to the Closing and, therefore, the Release was irrelevant.

D. The Teachers Case Confirms That Respondent’s Claims Could Not Have Accrued Since The Merger Was Subject To Cancellation on Short Notice, Just Like the Contract in Teachers.

This Court did not address *Teachers’ Retirement System of Louisiana v. Aidinoff*, 900 A.2d 654 (Del. Ch. 2006), which supports Respondent’s reading of *Coca-Cola*. In *Teachers’*, the plaintiff Teachers’ brought a derivative action alleging a breach of fiduciary duty based on the fact that various officers of AIG were receiving additional

compensation pursuant to a contract between AIG and another company, Starr, for doing what they should have been doing as employees of AIG. The defendants moved to dismiss based on the same arguments as the Appellants have made here, asserting that "when a contract is contended to have resulted from fiduciary misconduct, the statute of limitations begins running at the time of the decision to contract, as the date of the key wrong. Performance under the contract, then, is generally considered as a natural consequence flowing from the original decision by the defendant-fiduciaries to obligate the corporation to the contract." *Id.* at 665-66.

The court rejected the argument because the contract was subject to termination each year on short notice:

Each of those contracts contains a provision granting AIG an annual right to terminate without penalty upon certain notice. As Teachers argues, what the complaint challenges is the discretionary decision of the AIG director-defendants to continue doing business with Starr on terms that Teachers alleges were grossly unfair. Therefore, the complaint is not challenging the original decision of AIG to sign the MGA Agreements in the 1970s. It is attacking the allegedly disloyal and self-enriching decision of Greenberg, Matthews, and Smith to perpetuate an unfair relationship with Starr, with the supine complicity of the outside directors of AIG, who breached their duty of care by failing to understand, much less knowingly approve, the Starr-AIG relationship.

Id. at 666-67 (emphasis added).

Here, the Appellants had multiple opportunities to cancel, or simply not proceed with, the Merger. Under the clear teaching of *Teachers*, Respondent's breach of fiduciary duty claims could not, then, have accrued prior to the expiration of those opportunities – that is, prior to the Closing of the Merger.

E. Every Case To Address The Issue of Claim Accrual In The Context Of A Merger Has Held That Such Claims Accrue Upon The Closing Of The Merger, Just As *Coca-Cola* and *Teachers* Dictate.

As the discussion of *Coca-Cola* and *Teachers* ' above shows, under Delaware law Respondent's claims could not have accrued prior to the Closing date because the underlying Merger Agreement was not "enforceable" before that time. Contrary to this Court's reading of the Delaware caselaw, all three cases to address this specific issue have reached this conclusion. See *Kaufman v. Albin*, 447 A.2d 761 (Del. Ch. 1982); *Baron v. Allied Artists Pictures Corporation*, 717 F.2d 105 (3d Cir. 1983); and *Dofflemyer v. W.F. Hall Printing Company*, 558 F. Supp. 372 (D. Del. 1983).

The first case, *Kaufman v. Albin*, 447 A.2d 761 (Del. Ch. 1982), like this case, involved the question of whether a claim of breach of fiduciary duty ("corporate waste" in that context) accrued when the merger was approved by the board or when it was consummated. The point was important because of the effective date of a statute by which plaintiff had accomplished service. If the claim arose when the merger had been approved, it predated that statute and service was ineffective (and impossible). If it arose after the effective date of the statute, service was effective.

The Delaware Chancery Court held that the claim accrued when the transaction closed. It had "commenced with the adoption of the two resolutions on August 22, 1977 [by the board authorizing the merger], but was not consummated until October 2, 1977 [when sufficient shares were tendered and the merger was successfully concluded]." 447 A.2d at 764. Accordingly, it had accrued after the effective date of the statute regarding service of process, and service was therefore effective.

The United States Court of Appeals for the Third Circuit (which covers Delaware) addressed the same question in *Baron v. Allied Artists Pictures Corporation*, 717 F.2d 105 (3d Cir. 1983). The court of appeals held that a shareholder action based on false and

misleading materials effecting a merger accrued when the merger was consummated and not earlier when the shareholder had knowledge of the falsity. While plaintiff's claim was based on federal law, the court noted that it was "in the nature of" an action for "damages for breach of fiduciary duty" under Delaware law and analyzed it as such. *Id.* at 108. Moreover, the court's opinion as to when the claim accrued was premised on a "rule of general application" which, it held, Delaware "*adheres to.*" *Id.* at 108. The court wrote:

It is a rule of general application that a cause of action for the recovery of damages accrues only when it could be prosecuted to a successful conclusion. *E.g., United States v. Wurts*, 303 U.S. 414, 418, 58 S. Ct. 637, 82 L. Ed. 932 (1938)[]; *Grayson v. Harris*, 279 U.S. 300, 304-05, 49 S. Ct. 306, 73 L. Ed. 700 (1929); *City of Philadelphia v. Lieberman*, 112 F.2d 424, 428 (3d Cir.1940). Delaware, whose statute of limitations governs, adheres to that rule. "A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of the injury." *Nardo v. Guido DeAscanis & Sons, Inc.*, 254 A.2d 254, 256 (Del. Super. Ct.1969). The state recognizes "the basic rule that, in general, the statute of limitations begins to run from the date of the injury caused by the defendant" *Lembert v. Gilmore*, 312 A.2d 335, 337 (Del. Super. Ct. 1973). The United States District Court in Delaware has consistently recognized as much. *Rose Hall, Ltd. v. Chase Manhattan Overseas Bank*, 494 F. Supp. 1139, 1157 (D. Del.1980); *Oliver B. Cannon & Son, Inc. v. Fidelity & Casualty Co.*, 484 F. Supp. 1375, 1388 (D. Del. 1980); *Freedman v. Beneficial Corp.*, 406 F. Supp. 917, 922 (D. Del.1975).

Id.

In the third case precisely on point, *Dofflemyer v. W.F. Hall Printing Company*, 558 F. Supp. 372 (D. Del. 1983), the merger had been approved by the defendant directors on November 27, 1978. The approval was followed on January 29, 1979, by the distribution of a proxy statement to the shareholders. The merger was approved by shareholder vote and became effective on February 21, 1979. *Id.* at 375. Like Appellants here, the defendants argued that the breach of fiduciary duty claims accrued when the board approved the merger agreement and not when the merger was consummated.

The Delaware district court disagreed. It held that the claim accrued when the merger closed since “the merger transaction which is the subject of this suit was not accomplished and *no injury occurred* until the merger was effected.” *Id.* at 379 (emphasis added). As the court noted, “[i]t is a basic principle of limitations law that a cause of action does not accrue before the right to institute suit arises.” *Id.* (citing C.J.S., *Limitations of Actions*, §109.) The court then observed that “[t]he plaintiffs could not have sued for damages until the merger was actually accomplished – until that time, they had *suffered no injury by the defendants’ acts.*” *Id.* (emphasis added). Since they had not suffered any *injury* until the merger was consummated, their claim did not accrue until then.

Dofflemyer is not “out of step” with more recent Delaware law on breach of fiduciary duty, as this Court suggests, but in fact is persuasive since as recently as 2004 it was cited approvingly by the Delaware Court of Chancery for this exact point. *Bren v. Capital Realty Group Senior Housing, Inc.*, 2004 WL 370214, *4 (Del. Ch. Feb. 27, 2004).⁸ Further, *Dofflemyer* was followed in 1997 in yet another case involving Delaware

⁸ The *Bren* decision is not otherwise similar to our case. As described above, the plaintiff there was a noteholder who was suing the general partner of a partnership for failing to prosecute a claim regarding a contract that had been breached long before. The noteholder alleged that the general partner had committed a breach of fiduciary duty by failing to prosecute the claim. He alleged that his claim did not accrue until the expiration of the statute of limitations on the underlying breach of contract claim. His theory was that the claim did not “accrue” as to him until he specifically (not the company) was owed a fiduciary duty. In a creative bit of argument, he cited *Dofflemyer* as supporting this “novel” theory. 2004 WL 370214 at *4. The court said that he “read[] too much” into *Dofflemyer*. The *Dofflemyer* decision, it said, held that “plaintiffs could not sue for damages until the merger was consummated. Prior to that time, plaintiffs had suffered no injury from the defendants’ acts.” The *Bren* court found *Dofflemyer* irrelevant to the issue before it because *Dofflemyer* “focused on when the injury occurred, not when a fiduciary duty arose, for purposes of determining the limitations period.” The *Bren* court held that the claim there accrued when the underlying contract had been breached. *Id.*

law. *Montgomery v. Aetna Plywood, Inc.*, 956 F. Supp. 781 (N.D. Ill. 1997). The question there was whether, under Delaware law, a breach of fiduciary duty claim against a company's directors regarding a stock repurchase accrued at the time of the repurchase or earlier when the board authorized the repurchase. The court, relying on *Dofflemyer* and *Kaufman*, held that the claim "accrued" upon the "consummation of the sale," not at the time of the resolution authorizing it. *Id.* at 787.⁹

The case that this Court cites for the proposition that *Dofflemyer* is not consistent with current Delaware law, and that "injury" is not necessary for a claim to accrue, *Albert v. Alex. Brown Mgmt. Servs., Inc.*, 2005 Del. Ch. LEXIS 100, 2005 WL 1594085 (June 29, 2005), is actually to the contrary. That case involved two investment funds that the plaintiffs had invested in. The plaintiff alleged, among other things, that the defendants violated their fiduciary duty by "unhedging" the investment funds. 2005 Del. Ch. LEXIS 100, *44-45. There was obviously a gap between when the defendants decided to stop "hedging" the funds and when they actually did stop. Under this Court's reading of *Albert*, the claim would have accrued when the defendants made the decision to stop hedging. The court, however, held that it accrued "at the time the Funds became unhedged." 2005 Del. Ch. LEXIS 100, *45, 2005 WL 1594085, *14. That was when there was "harm" or "injury." As such, it is precisely consistent with *Baron* and

Dofflemyer (and *Coca-Cola*).

⁹ It should also be noted that this Court's Opinion did not address *Brambles USA, Inc. v. Blocker*, 731 F. Supp. 643 (D. Del. 1990). *Brambles* also involved a different twist on a breach of fiduciary duty claim relating to a merger. The merger agreement there had been approved by the company's board on March 3, 1988, and became effective on May 1, 1988. The plaintiff argued that its claim accrued much later when the effects of the merger were felt. The court held that the wrong occurred when the merger "became effective in May, 1988, thereby finalizing the conditional aspects of the agreement." *Id.* at 652 (emphasis added).

Indeed, *Albert* is even more clearly consistent with *Baron* and *Dofflemyer* in how it treated the first claim in the case, which this Court did not discuss. The first claim was that “the Managers breached their fiduciary duties in initially screening the stocks allowed into the Funds, failing to properly diversify the Funds, and that, generally, the entire structure of the Fund[s] was *fatally flawed* from the outset.” 2005 Del. Ch. LEXIS 100 at *43 (emphasis added). The court held that plaintiffs’ injuries on this first claim occurred when the “Funds closed,” and that was when the claim “accrued”:

Accepting these allegations as true, the plaintiffs’ *injuries occurred when the Funds closed*, at which time the Funds were not (allegedly) properly diversified nor properly screened. *This was the time of the wrongful act.* Fund I *closed* on May 5, 1997, and Fund II *closed* on April 17, 1998. Likewise, *claims that the Funds were improperly structured accrued at the time the Funds closed.*

Id. (emphasis added, footnotes omitted). Again, as with the unhedging claim, if this Court’s reading of new Delaware cases was accurate, the first claim would have accrued much earlier. It would have accrued well before the closing of the funds, when the plaintiff received the private placement memorandum disclosing how the funds were to be operated (April 14, 1997, for fund I and October 3, 1997, for fund II – *id.* at *11), or perhaps when the plaintiff sent in his investment and subscription agreement. That it did not accrue until the funds “closed” is, again, precisely consistent with *Baron* and *Dofflemyer* (and *Kaufman* and *Coca-Cola*).

The portion of *Albert* that this Court relies upon simply relates to the argument of the plaintiffs there that their claims had not accrued until their investment collapsed because until then they suffered no “harm.” The court did not hold that “harm” was unnecessary for claim “accrual.” Indeed, such a holding would be inconsistent with Delaware law. Instead, the court (using the language of the plaintiffs there) held that

60

plaintiffs had in fact been "harmed" and the harm had occurred as soon as the "unhedging" occurred and, because of that "harm," could have brought their claim at that time. *Id.* at *58-60. This is not inconsistent with *Dofflemyer* since *Dofflemyer* held that the plaintiff suffered no "injury" "until the merger was accomplished" and that was why his claim "accrued" at that point. 558 F. Supp. at 379. *Baron* is to the same effect. Basically, *Dofflemyer* and *Baron* speak in terms of "injury," while *Albert* speaks both in terms of "injuries" and "harm." There is no difference.

Moreover, if *Albert* actually supported accrual of Respondent's claims prior to the Closing of the Merger, it would be contrary to the Delaware Supreme Court's decision in *Coca-Cola*, which it obviously cannot be. This reading puts *Albert* in context. Under *Coca-Cola*, there is no claim until the underlying contract is "enforceable." Under *Albert*, there must be a "harm" but there need not be a "loss" or "damages." In context, it is clear that *Albert* is referring to quantifiable financial "losses" or financial "damages" and not to "harm" or "injury" (or non-financial damages). In light of *Coca-Cola*, Respondent was not "harmed" or "injured" (or "damaged" in any sense) until the Merger agreement became enforceable, as also held by *Kaufman*, *Baron*, and *Dofflemyer*.

F. The Shareholder "Standing" Cases Appellants Rely On Do Not Support Their Argument.

1. Those Cases Deal With "Standing" And Not Claim "Accrual" And Thus Are Not Applicable.

This Court also discusses standing cases to support reversal of the lower court's decision, and notes that the more recent Delaware cases look to the date of the wrong for purposes of determining accrual, as opposed to the date of shareholder approval. See *Brown v. Automated Mktg. Sys., Inc.*, 1982 WL 8782, *2 (Del. Ch. Mar. 22, 1982) and *In*

re Beatrice Cos., Inc. Litig., 522 A.2d 865 (Del. 1987). The standing cases, however, do not involve the issue of claim “accrual.” Rather, they involve the issue of “standing,” *i.e.*, whether a plaintiff has “standing” to bring derivative claims for injunctive relief. The import of these cases is that to have “standing” in a derivative action challenging a merger, a plaintiff must own his stock at the time the merger is announced.

This is not a controversial or new rule and is almost universal. *See Rubenstein, Conte and Newberg, 7 Newberg on Class Actions*, §22:95 (4th ed. 2009). The reason behind the rule is very simple. It prevents persons (particularly, competitors) from learning of a merger and then purchasing stock in the company and seeking to prevent the transaction from closing, attempting to get a better deal, or attempting to buy the company themselves. In *Brown* and *Beatrice* the plaintiffs did not own stock when the mergers were announced, and thus the cases were dismissed.

This Court ignores that *Dofflemyer* had rightly distinguishes the standing cases:

Brown is also inapplicable. In that case, the Court of Chancery held that a plaintiff who purchased shares after reading a press release indicating that the board of directors had approved a plan of merger did not have standing to challenge the merger when it was carried out according to the plan. *The holding of that case involved a determination of the times when a plaintiff must own stock in a corporation in order to have standing to challenge a merger and is not pertinent to when, if standing had existed, the plaintiff could have sued for damages.*

558 F. Supp. at 379 n.5 (emphasis added). That another standing case (*Dieter v. Prime Computer, Inc.*, 681 A.2d 1068, 1072 (Del.Ch. 1996)) was decided after *Dofflemyer* does not make *Dofflemyer's* explanation of why the standing cases are distinguishable “old law.”

Likewise, this Court’s discussion of the change in the *Folk* treatise has not been accepted by any scholar or treatise. The Court notes the change in the *Folk* treatise from

1967 to 2006, and accepts Appellants' argument that the change indicates endorsement of *Brown*. The section of *Folk* where the change occurs, however, relates to "standing" and not claim "accrual." This is obviously why *Kaufman*, *Baron*, and *Dofflemyer* are not noted there.

This Court's Opinion does discuss the *Folk* treatise's reference to *Lavine v. Gulf Coast Leaseholds*, 122 A.2d 550 (Del. Ch. 1956), which held that "where exchanges of stock are contingent upon shareholder approval, the transaction is not completed until the shareholder vote takes place." *Folk, supra*. The holding of *Lavine* was the basis for the statement in the 1967 edition of *Folk* that "the circumstances of the case will determine whether the transaction is executed or continuing. If the action complained of requires stockholder approval, the transaction is not considered complete until the stockholders have approved it." See *Kaufman*, 447 A.2d 761, 764 (Del. Ch. 1982), quoting *Folk, The Delaware General Corporation Law*, 487 (1967). Under the teaching of *Lavine* (to the extent a "standing" case is relevant), the claims of Respondent would not have been "completed" until the Closing of the Merger on October 20, 2006, well after the date of the Release simply because shareholder votes were required.

Folk, however, can not be seen as either endorsing or criticizing *Brown* or *Lavine* or any other case. The treatise is merely reporting cases that have dealt with the "standing" issue.

2. The "Standing" Cases Do Not Apply If The Closing Of A Merger Is Not A Mere "Technicality."

The "standing" cases must also be read in light of the Delaware Supreme Court's long-standing principle, as stated in *Coca-Cola* and *Teachers'* and discussed at length above, that a fiduciary duty claim regarding an underlying contract accrues when the

underlying contract becomes "enforceable." To the extent *Brown* and *Beatrice* could be read to support Appellants' theory, they would directly contradict *Coca-Cola* and the cases cited in Part II.A above. In other words, as demonstrated above, there can be no claim such as Respondent's until all the conditions precedent to a merger are completed.

It is not difficult to reconcile the "standing" cases with this principle. The *Beatrice* case, for example, states that "[i]n the case of a proposed merger, the plaintiff must have been a stockholder at the time the *terms* of the merger were agreed upon because it is the terms of the merger, rather than the *technicality* of its *consummation*, which are challenged." 522 A.2d 865, *3 (Del. 1987) (emphasis added). On its face, it is clear that the "consummation" of the merger at issue there was a mere "technicality." As such, the merger agreement would have already been "enforceable," thus meeting the requirement of *Coca-Cola*.

There is, in fact, an example of that kind of "technicality" in this case. The Merger agreement here provided that the Merger "shall become effective at such time as the Certificate of Merger is duly filed with the Delaware Secretary of State." (Proxy, A1-A2 §1.3 [R. pp. 1039-1040].) That is a "ministerial" act, a simple "technicality." If everything about the Merger had been done except for the filing of the certificate of merger but SCI or FITG refused to go through with the Merger, the other party would certainly have had legal rights regarding the Merger. In other words, the Merger agreement would have been "enforceable."

The conditions precedent that are at issue here, however, are not mere "technicalit[ies]." As already discussed, there were fundamental conditions that had to be met. Aside from approval of FITG and SCI shareholders, the representations and

64

warranties as to the businesses had to be true as of the Closing date, and there had to be no material adverse changes as of the Closing date in either company.

If FITG had sued SCI prior to the Merger to compel it to go forward or for damages for refusing to do so, the lawsuit would have turned on whether the conditions to the merger had been satisfied. Given that FITG was losing nearly \$2 million a week and \$8 million a month and appears to have borrowed \$31 million in the *four weeks* between the issuance of the Proxy on September 22, 2006 and the Merger on October 20, 2006 (Compl. ¶¶50, 52, 65, & 58 [R. pp. 17-20]), FITG would have had a very difficult case. In any event, the satisfaction of the financial conditions would have been the critical issue. Obviously, therefore, satisfaction of those conditions was no mere “technicality.”

Accordingly, under *Beatrice* and *Coca-Cola*, since the Merger agreement was not “enforceable” by the date of the Release and the “consummation” of the Merger was not a mere “technicality,” Respondent’s claims could not have accrued prior to the Closing (or prior to when all the conditions precedent were met). Since that happened well after the date of the Release, the Release is irrelevant.

3. The “Standing” Cases Support Respondent’s Position Because He Is Challenging The *Fact Of The Merger*, Not Merely Its *Terms*.

In the “standing” cases, the plaintiffs were all merely challenging the “terms” of proposed mergers. In *Brown*, the plaintiff felt the \$10 per share she would receive was “inadequate.” 1982 WL 8782, at *467. In *Beatrice*, the plaintiff objected to settlement that would have paid him \$50 for his shares. 522 A.2d 865 at *2. In both cases, the challenger knew the amount it would receive when it bought its shares.

Here, by contrast, Respondent was not “receiving” a price that might have been too high or too low, a situation that could have been corrected simply by adjusting the price. Rather, the company in which Respondent owns shares (SCI) was absorbing another company which Appellants also controlled. Respondent was “receiving” nothing. He did not even “receive” appraisal rights (only FITG shareholders had “appraisal” rights – Proxy at 3 [R. p. 768]). Further, Respondent already owned his stock. He had not bought in with any expectation of selling in a merger. His only expectation was that Appellants would act in accordance with their fiduciary duties.

The question then is what do the “standing” cases actually mean (assuming they are relevant at all here). The case of *7547 Partners v. Beck*, 682 A.2d 160 (Del. 1996), not mentioned in this Court’s Opinion, is helpful on this point. The plaintiffs there alleged that the defendant officers and directors, in order to enrich themselves, had set an “absurdly low” price of \$20 per share for a private placement of stock that immediately preceded an IPO. The defendants were able to purchase stock at \$18.60 a share (\$20 less the underwriter’s discount). When the IPO opened, the price went to \$45 a share. Plaintiffs purchased 100 shares at that price. *Id.* at 161. The question was whether the plaintiffs had standing to bring the action. The court noted that the plaintiffs were not challenging the overall transaction or attempting to set it aside (“not seeking cancellation of any . . . stock” – 682 A.2d at 162). They were merely challenging the “terms.” Still, they argued that the wrongful transaction occurred at the time of the IPO. The defendants argued that it occurred earlier when the price was set.

The Delaware Supreme Court held that the “timing of the allegedly wrongful transaction must be determined by identifying the ‘wrongful acts which [Partners]

want[s] remedied and which are susceptible of being remedied in a legal tribunal.” *Id.*, quoting *Newkirk v. W.J. Rainey, Inc.*, 76 A.2d 121, 123 (Del. Ch. 1950). Since the plaintiff there was challenging the “terms” of the private placement, “rather than the technicality of its consummation,” the relevant time was when those terms were set. *Id.*, quoting *Beatrice, supra*.

Following *7547 Partners*, it is necessary here to identify “the wrongful act” here that Respondent seeks to have remedied. In the words of the United States Court of Appeals for the Seventh Circuit in a case applying Delaware law and interpreting these principles, it is necessary to identify “what about the transaction is being challenged.” *Montgomery v. Aetna Plywood Inc.*, 231 F.3d 399, 406 (7th Cir. 2000).

Here, Respondent’s objection, his fundamental issue, is that the Merger was allowed to close *at all* in light of FITG’s deteriorating financial condition. The specific financial terms are relevant mainly as background, showing how the value of the merged company’s stock collapsed (showing what the market thought of the Merger) and how extremely self-interested the Appellants were in the transaction.¹⁰ The fundamental claim is that Appellants’ violated their fiduciary duty by allowing this Merger to consummate.

This was how the trial court construed Respondent’s allegations: “Plaintiff alleges that the defendants breached their fiduciary duties to the minority shareholders of SCI (including the plaintiff) by allowing the merger to go forward or close.” (Order at 1 [R. p. 1].) And it follows directly from the Complaint. The very *first* “specification” in the very *first* cause of action is that the Appellant controlling shareholders breached their fiduciary

¹⁰ By the time the Complaint here was filed (well before the current economic downturn), the value had declined by nearly 90%. (Compl. 84 [R. p. 24].) Appellants received over \$130 million of the Merger consideration. (*Id.* ¶¶30-31 [R. pp. 13-14].)

duty by “allowing [the Merger] to close notwithstanding the financial condition of FITG.” (Compl. ¶99(a) [R. p. 28].) The *first* “specification” in the second cause of action makes the same allegation as to the Appellant directors and officers of SCI. (*Id.* ¶104(a) [R. pp. 29-30].) And the *first* “common question” in the Class Allegations is whether Appellants breached their fiduciary duty by “allowing [the Merger] to close notwithstanding the financial condition of FITG.” (*Id.* ¶91(a) [R. p. 26].).

This question permeates the main body of the Complaint. In Paragraph 66, for example, it is alleged that, given FITG’s losses, the Merger was “indefensible on the terms agreed to on August 29, 2006, and *probably indefensible generally. It should have been cancelled or dramatically re-negotiated.*” (R. p. 20, ¶66, emphasis added.) Paragraph 67 alleges that Defendants “*could easily have cancelled the Merger . . . based on the ‘MAC clause’ in the Merger agreement.*” (R. p. 20, ¶67, emphasis added.) And Paragraph 68 alleges that “[n]otwithstanding the information they knew or should have known regarding the deterioration of FITG’s business, and *notwithstanding that non-deterioration was a condition precedent to the Merger, Defendants allowed the Merger (which benefited them enormously) to proceed and be consummated*, thereby violating their fiduciary duties to the minority shareholders including Plaintiff[].” (R. p. 21, ¶68, emphasis added.)

In light of the specific allegations of the Complaint, it is clear that the principal item “about the transaction” that is “being challenged” here (to use the language of *Montgomery v. Aetna Plywood Inc.*, above) is that it was allowed “to close notwithstanding the financial condition of FITG.” (*Id.* ¶¶99(a) & 104(a) [R. pp. 28-30].) In other words, Respondent’s fundamental claim is that the Merger was “fatally flawed” (to use

the language of *Albert v. Alex. Brown Mgmt. Servs., Inc.*). The Merger simply should not have been allowed to close in light of the collapse of FITG's business.

SCI and Appellants did not have to proceed with the Merger. They had every right not to close since FITG could not meet the conditions precedent. But they closed anyway. They waived the conditions precedent and closed the merger. That is, fundamentally, what Respondent is challenging. (*See* Compl. ¶¶67-68 [R. p. 20-21].)

That waiver took place when the Merger was allowed to close on October 20, 2006. That is when Respondent's claims accrued. Since the Release was executed on September 28, 2006, Respondent's claims unquestionably post-date it. And the Release is irrelevant. Respectfully, the trial court's reading of the Delaware cases under the facts of this case was correct.

CONCLUSION

Under long-standing Delaware law and the Delaware Supreme Court's decision in *Coca-Cola*, Respondent had no claim until the underlying merger agreement was "enforceable."

Since the Merger could not have been "enforceable" before the Closing date because of the extensive conditions precedent, as held by the trial court, and since it was subject to cancellation at any time (a la *Teachers'*), Respondent's claims, as common sense would dictate, could **not** have accrued prior to that date.



Since the Release was executed well before the Closing date, it had no application to Respondent's claims here.

Accordingly, the trial court's ruling was correct. It should be affirmed.

Respectfully submitted,



William D. Herlong (S.C. Bar #14283)
The Herlong Law Firm, LLC
531 S. Main St., Ste. 201
P.O. Box 2003
Greenville, SC 29602-2003
Tel. (864) 382-3801
Fax (864) 752-0820

Thomas L. Stephenson (SC Bar#5332)
Russell T. Burke (SC Bar #1024)
Nexsen Pruet, LLC
PO Drawer 10648
Greenville, SC 29603
Tel (864) 370-2211

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

Brian P. Menezes, Respondent,

v.

WL Ross & Co. LLC, Wilbur L. Ross, Jr.,
Michael J. Gibbons, David H. Storper, David L. Wax,
Joseph L. Gorga, Stephen B. Duerk,
WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P., WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC, Appellants.

Appeal From Greenville County
Edward W. Miller, Circuit Court Judge

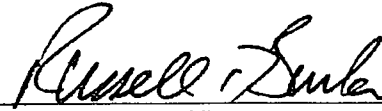
Opinion No. 4810
Filed March 23, 2011

PROOF OF SERVICE

The undersigned certifies that a copy of **Respondent's Petition for Rehearing on Enbanc**, has been served upon all parties via Electronic Mail and United States Mail, first-class postage prepaid, to the addresses shown below on the 7th day of April, 2011.

H. Sam Mabry, III
J.D. Quattlebaum
Haynsworth Sinkler Boyd, P.A.
Two Liberty Square – 11th Floor
75 Beattie Place
Greenville, SC 29601
smabry@hsblawfirm.com
dquattlebaum@hsblawfirm.com

Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Atlanta, GA 30309-3053
mmcconnell@jonesday.com
jfinley@jonesday.com



NEXSEN PRUETT, LLC
1230 Main Street, Suite 700 (29201)
Post Office Drawer 2426
Columbia, South Carolina 29202
Tel: 803.771.8900
Fax: 803.253.8277

Attorneys for Plaintiffs

April 7, 2011

STATE OF SOUTH CAROLINA
In the
Court of Appeals

APPEAL FROM COURT OF COMMON PLEAS
FOR GREENVILLE COUNTY
The Honorable Edward W. Miller, Circuit Court Judge
C.A. No. 2008-CP-23-2701
South Carolina Court of Appeals

RECEIVED
APR 07 2011
SC Court of Appeals

Brian P. Menezes, ...Respondent,

v.

WL Ross & Co. LLC, Wilbur, L. Ross, Jr.,
Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC, ...Appellants.

MOTION TO SUPPLEMENT THE RECORD ON APPEAL

Pursuant to SCACR, Rule 212(b), Respondent hereby moves the Court to supplement the Record on Appeal. This Court recently filed Opinion No. 4810, dated March 23, 2010, which reversed and remanded the case to the Circuit Court. Respondent contends that one additional document, Wachovia's consent to the merger that is contested in this case, should be considered in light of whether there were significant conditions precedent to the close of the merger such that the Respondent's claims concerning the merger had *not* accrued at the time he signed a release of his employment claims. As set forth in an accompanying memorandum, the Wachovia consent to the merger should be considered as part of the Record on Appeal, in conjunction with

Respondent's Petition for Rehearing and Rehearing En Banc, filed contemporaneously with this Motion.

William D. Herlong (S.C. Bar #14283)
The Herlong Law Firm, LLC
531 S. Main St., Ste. 201
P.O. Box 2003
Greenville, SC 29602-2003
Tel. (864) 382-3801
Fax (864) 752-0820


Thomas L. Stephenson (SC Bar #5332)
Russell T. Burke (SC Bar #1024)
Nexsen Pruet, LLC
PO Drawer 10648
Greenville, SC 29603
Tel (864) 370-2211

April 7, 2011

Attorneys for Respondent

STATE OF SOUTH CAROLINA
In the
Court of Appeals

APPEAL FROM COURT OF COMMON PLEAS
FOR GREENVILLE COUNTY
The Honorable Edward W. Miller, Circuit Court Judge
C.A. No. 2008-CP-23-2701
South Carolina Court of Appeals

Brian P. Menezes, ...Respondent,

v.

WL Ross & Co. LLC, Wilbur, L. Ross, Jr.,
Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC, ...Appellants.

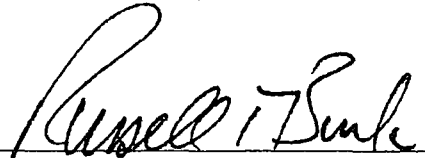
MEMORANDUM IN SUPPORT OF MOTION
TO SUPPLEMENT THE RECORD ON APPEAL

This Court's Opinion has remanded the case to the Circuit Court on the grounds that the Respondent's claims contesting the merger "could have arisen prior to the closing of the merger," and therefore Appellants' defenses related to the Release were not insufficient. The Circuit Court, which had found that Respondent's claims were not released because they had not accrued until the close of the merger, did *not* rely on a condition precedent to the merger, the consent to the merger by Wachovia, the financing company for SCI. In fact, Wachovia's consent had not been produced by the Appellants until well after the hearing at the Circuit Court concerning the Release, and therefore was not a part of the Record on Appeal.

Wachovia's consent to the merger was given on October 20, 2006, the date of the merger, and was given well after the Release in question. Wachovia's consent was necessary before the merger could close, and was therefore a significant condition precedent to the merger. In other words, without Wachovia's consent, the merger could not have happened, and Respondent's claims could not have accrued prior to Wachovia's consent.

Given this Court's reversal and remand, and the reasoning in this Court's Opinion, Wachovia's consent represents a significant condition precedent to the merger. Therefore, Respondent requests leave to supplement the Record on Appeal to add the Wachovia consent form (attached hereto), so that this Court can properly consider Respondent's Petition for Rehearing and Rehearing *En Banc*. Pursuant to SCACR, Rule 212(b), since this Motion is made after argument in this case, Respondent must move this Court for leave to supplement the Record.

William D. Herlong (S.C. Bar #14283)
The Herlong Law Firm, LLC
531 S. Main St., Ste. 201
P.O. Box 2003
Greenville, SC 29602-2003
Tel. (864) 382-3801
Fax (864) 752-0820


Thomas L. Stephenson (SC Bar #5332)
Russell T. Burke (SC Bar #1024)
Nexsen Pruet, LLC
PO Drawer 10648
Greenville, SC 29603
Tel (864) 370-2211

April 7, 2011

Attorneys for Respondent

[Execution]

AMENDMENT NO. 7 AND CONSENT
TO
LOAN AND SECURITY AGREEMENT

As of October 20, 2006

Wachovia Bank, National Association
110 East Broward Boulevard
Suite 2050
Fort Lauderdale, Florida 33301
Attention: Portfolio Manager

Re: Loan and Security Agreement, dated October 11, 2000, as Amended

Ladies and Gentlemen:

Wachovia Bank, National Association, successor by merger to Congress Financial Corporation (Southern) ("Lender"), Valentec Wells, LLC, formerly known as Valentec International Corporation, LLC ("Valentec"), Safety Components Fabric Technologies, Inc. ("SCFT"), Automotive Safety Components International, Inc. ("Automotive International"), Automotive Safety Components International GmbH & Co. KG ("German Borrower"), Automotive Safety Components International Limited ("UK Borrower" and together with Valentec, SCFT, Automotive International and German Borrower, individually each a "Borrower" and collectively, "Borrowers"), Safety Components International, Inc. ("Safety"), ASCI Holdings Germany (DE), Inc. ("ASCI Germany"), ASCI Holdings U.K. (DE), Inc. ("ASCI UK"), ASCI Holdings Mexico (DE), Inc. ("ASCI Mexico"), ASCI Holdings Czech (DE), Inc. ("ASCI Czech"), Automotive Safety Components International S.A. de C.V. ("Automotive Safety Mexico") and Automotive Safety Components International s.r.o. ("Automotive Safety Czech" and together with Safety, ASCI Germany, ASCI UK, ASCI Mexico, ASCI Czech and Automotive Safety Mexico, each individually a "Guarantor" and collectively, "Guarantors") have entered into financing arrangements pursuant to which Lender has made and may, subject to certain terms and conditions, hereafter make loans and advances to Borrowers as set forth in the Loan and Security Agreement, dated October 11, 2000; by and among Lender, Borrowers and Guarantors, as amended by Amendment No. 1 and Consent to Loan and Security Agreement, dated as of November 2, 2001, Amendment No. 2 to Loan and Security Agreement, dated as of October 11, 2002, Amendment No. 3 and Consent to Loan and Security Agreement, dated as of October 8, 2003, Amendment No. 4 to Loan and Security Agreement, dated as of July 20, 2004, Amendment No. 5 and Consent to Loan and Security Agreement, dated as of October 1, 2004 and Amendment No. 6 and Consent to Loan and Security Agreement, dated as of October 6, 2006 (as the same now exists or may hereafter be amended, modified, supple-

738270.4

77

FURSA-0034963

mented, extended, renewed, restated or replaced, the "Loan Agreement") and other agreements, documents and instruments referred to therein or at any time executed and/or delivered in connection therewith or related thereto, together with this Amendment (all of the foregoing, including the Loan Agreement, as the same now exist or may hereafter be amended, modified, supplemented, extended, renewed, restated or replaced, being collectively referred to herein as the "Financing Agreements"). All capitalized terms used herein shall have the meaning assigned thereto in the Loan Agreement, unless otherwise defined herein.

WHEREAS, Safety, SCI Merger Sub, Inc., a Delaware corporation which is a wholly-owned Subsidiary of Safety ("Merger Sub") and International Textile Group, Inc., a Delaware corporation ("ITG"), have entered into the Agreement and Plan of Merger, dated as of August 29, 2006 (the "ITG Merger Agreement" as hereinafter further defined), pursuant to which Merger Sub will merge with and into ITG with ITG being the surviving corporation (the "ITG Merger"), all in accordance with the terms of the ITG Merger Agreement (as in effect on the date hereof);

WHEREAS, Borrowers and Guarantors have requested that Lender agree to, among other things, consent to the consummation of the ITG Merger; and

WHEREAS, Lender is willing to consent to such requests subject to the terms and conditions contained herein.

NOW THEREFORE, in consideration of the forgoing and the agreements and covenants contained herein, and for other good and valuable consideration, the adequacy and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

1. Amendments.

(a) Definitions.

Amendment to Definitions. The definition of "Subsidiary" in Section 1.09 of the Loan Agreement is hereby amended by adding the following at the end of such definition: "Notwithstanding anything to the contrary contained herein, and solely for purposes of the Loan Agreement and the other Financing Agreements, in no event shall any of the ITG Companies be deemed to be Subsidiaries of any Borrower or Guarantor."

(i) Additional Definitions. The following terms shall have the meanings given to them below and the Loan Agreement shall be deemed and is hereby amended to include, in addition and not in limitation, the following definitions:

(A) "Amendment No. 7" shall mean Amendment No. 7 and Consent to Loan and Security Agreement, dated as of October 20, 2006, by and among Lender, Borrowers and Guarantors.

(B) "ITG Companies" shall mean, collectively, ITG and its direct and indirect Subsidiaries; provided, that, in no event shall the ITG Companies include any Borrower or Guarantor.

(C) "ITG Merger Agreement" shall mean the Agreement and Plan of Merger, dated as of August 29, 2006, by and among ITG, Safety and Merger Sub.

2. Consent to ITG Merger. Subject to the terms and conditions contained herein and notwithstanding anything to the contrary contained in Section 9.7(a) of the Loan Agreement, Lender hereby consents to the consummation of the ITG Merger in accordance with the terms of the ITG Merger Agreement (as in effect on the date hereof); provided, that, each of the following conditions shall have been satisfied: (a) as of the effective date of the ITG Merger and after giving effect thereto, no Event of Default or act, condition or event which with notice or passage of time would constitute an Event of Default shall exist or have occurred and be continuing, (b) Lender shall have received true, complete and correct executed copies of the ITG Merger Agreement and all other material documents, agreements or instruments relating thereto to which any Borrower or Guarantor is a party or by which any Borrower or Guarantor (or its assets) is bound (together with the ITG Merger Agreement, the "ITG Merger Documents"), (c) no Borrower or Guarantor shall, directly or indirectly, pay or be liable for any merger consideration or any other amounts payable in connection with the ITG Merger, except that: (i) Safety may use shares of its common stock as merger consideration, and (ii) Safety may make cash payments for fractional shares and transaction expenses in connection with the ITG Merger up to the aggregate amount of \$3,000,000, so long as, both before and after giving effect to any such cash payment, the aggregate Excess Availability of Borrowers shall not be less than the US Dollar Equivalent of US\$15,000,000, (d) notwithstanding anything to the contrary in the Loan Agreement, in no event shall any Borrower or Guarantor: (i) become liable for any Indebtedness or other obligations (contingent or otherwise) of any of the ITG Companies or (ii) become liable for any Indebtedness or other obligations (contingent or otherwise) as a result of the ITG Merger except (as to this clause (ii) only) as otherwise permitted under the Loan Agreement, (e) notwithstanding anything to the contrary contained in the Loan Agreement, Borrowers and Guarantors shall not, and shall not permit any of their respective Subsidiaries (other than the ITG Companies) to, directly or indirectly, make loans or advances to, make any investments in, or pay any dividends to, any of the ITG Companies, (f) all actions and proceedings required by the ITG Merger Agreement, applicable law or regulation and the transactions contemplated thereby shall have been duly and validly taken in accordance with the terms thereof, and all required consents thereto shall have been obtained and be in full force and effect, and no court of competent jurisdiction shall have issued any injunction, restraining order or other order which prohibits the consummation of the transactions described in the ITG Merger Agreement or modifies such transactions; and no governmental or other action or proceeding shall have been commenced, seeking any injunction, restraining order or other order which seeks to void or otherwise modify the transactions described in the ITG Merger Agreement;

3. Representations, Warranties and Covenants. Each Borrower and Guarantor, jointly and severally, represents, warrants and covenants with and to Lender as follows, which representations, warranties and covenants are continuing and shall survive the execution and delivery hereof, the truth and accuracy of, or compliance with each, together with the

representations, warranties and covenants in the other Financing Agreements, being a continuing condition of the making or providing of any Loans or Letter of Credit Accommodations by Lender to Borrowers:

(a) neither the execution and delivery of this Amendment, or the documents, agreements or instruments executed or delivered in connection therewith or related thereto including, without limitation the ITG Merger Agreement (collectively, together with this Amendment, the "Amendment Documents") nor the consummation of the transactions herein or therein contemplated, nor compliance with the provisions hereof or thereof are in contravention of any law or regulation or any order or decree of any court or Governmental Authority applicable to Borrowers or Guarantors or any of their respective Subsidiaries, or conflict with or result in the breach of, or constitutes a default under any mortgage, deed of trust, security agreement, agreement or instrument to which any Borrower or Guarantor is a party or may be bound, or violates any provision of the Certificate of Incorporation, Certificate of Formation, Operating Agreement or By-Laws (or similar organizational documents) of any Borrower or Guarantor;

(b) the Amendment Documents have been duly authorized, executed and delivered by all necessary action on the part of each Borrower and Guarantor which is a party hereto and thereto and, if necessary, their respective equity holders, and the agreements and obligations of each Borrower and Guarantor contained herein and therein constitute legal, valid and binding obligations of each Borrower and Guarantor enforceable against such entities in accordance with their respective terms, except as such enforceability may be limited by bankruptcy, insolvency, moratorium or similar laws limiting creditors' rights generally and by general equitable principles;

(c) no consent, approval or other action of, or filing with or notice to any Governmental Authority is required in connection with the execution, delivery and performance of any of the Amendment Documents by any Borrower or Guarantor, except for those which have been made or obtained and are in full force and effect;

(d) all of the representations and warranties set forth in the Loan Agreement and the other Financing Agreements, each as amended hereby, are true and correct in all respects on and as of the date hereof as if made on the date hereof, except to the extent any such representation or warranty is made as of a specified date, in which case such representation or warranty shall have been true and correct as of such date;

(e) Borrowers and Guarantors have delivered to Lender true, complete and correct copies of all ITG Merger Documents;

(f) after giving effect to the consummation of the ITG Merger, Safety is Solvent; and

(g) no Event of Default or act, condition or event which with notice or passage of time or both would constitute an Event of Default, exists or has occurred and is continuing.

4. Conditions Precedent. The amendments and consents set forth herein shall be effective upon the satisfaction of each of the following conditions precedent in a manner satisfactory to Lender:

- (a) Lender shall have received an original of this Amendment, duly authorized, executed and delivered by each of the parties hereto;
- (b) all requisite corporate action and proceedings in connection with this Amendment and the other Amendment Documents shall be in form and substance satisfactory to Lender, and Lender shall have received all information and copies of all documents, including records of requisite corporate action and proceedings which Lender may have requested in connection therewith, such documents where requested by Lender or its counsel to be certified by appropriate corporate officers or governmental authorities;
- (c) no Event of Default or act, condition or event which with notice or passage of time or both would constitute an Event of Default shall exist or have occurred and be continuing; and
- (d) Lender shall have received a true and correct copy of any consent, waiver or approval to or of this Amendment or any of the other Amendment Documents, which any Borrower or Guarantor is required to obtain from any other Person, and such consent, approval or waiver shall be in form and substance satisfactory to Lender.

5. General.

(a) Effect of this Amendment. Except as expressly provided herein, no other changes or modifications to the Financing Agreements are intended or implied, and in all other respects the Financing Agreements are hereby specifically ratified, restated and confirmed by all parties hereto as of the date hereof. To the extent any conflict exists between the terms of this Amendment and the Financing Agreements, the terms of this Amendment shall control.

(b) Further Assurances. The parties hereto shall execute and deliver such additional documents and take such additional actions as may be necessary to effectuate the provisions and purposes of this Amendment.

(c) Governing Law. The rights and obligations hereunder of each of the parties hereto shall be governed by and interpreted and determined in accordance with the internal laws of the State of New York (without giving effect to principles of conflicts of laws or other rules of law that would result in the application of the law of any jurisdiction other than the State of New York).

(d) Binding Effect. This Amendment is binding upon and shall inure to the benefit of Lender, Borrowers, Guarantors and their respective successors and assigns. Any amendment or consent contained herein shall not be construed to constitute an amendment or consent to any other or further action by Borrowers or Guarantors or to entitle Borrowers or Guarantors to any other amendment or consent. The Loan Agreement and this Amendment shall be read and construed as one agreement.

(e) Counterparts, etc. This Amendment may be executed in one or more counterparts, each of which when so executed shall be deemed to be an original but all of which when taken together shall constitute one and the same instrument. In making proof of this Amendment, it shall not be necessary to produce or account for more than one counterpart hereof signed by each of the parties hereto. This Amendment may be executed and delivered by telecopier or other method of electronic transmission with the same force and effect as if it were a manually executed and delivered counterpart.

[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed and delivered by their respective duly authorized officers as of the date first written above.

**SAFETY COMPONENTS FABRIC
TECHNOLOGIES, INC**

By: Vick Coug
Title: Treasurer

**AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL, INC.**

By: Vick Coug
Title: Treasurer

**AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG**

By: _____
Title: _____

**AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL LIMITED**

By: Shy B. Duml
Title: President

**VALENTEC WELLS, LLC (formerly known
as Valentec International Corporation, LLC)**

By: Vick Coug
Title: Treasurer

[SIGNATURES CONTINUED ON NEXT PAGE]

[SIGNATURES CONTINUED FROM PREVIOUS PAGE]

738270.4

B-1

83

FURSA-0034969

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be duly executed and delivered by their respective duly authorized officers as of the date first written above.

SAFETY COMPONENTS FABRIC
TECHNOLOGIES, INC.

By: _____

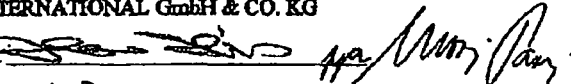
Title: _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL, INC.

By: _____

Title: _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG

By:  _____

Title: HD _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL LIMITED

By: _____

Title: _____

VALENTEC WELLS, LLC (formerly known
as ValenTec International Corporation, LLC)

By: _____

Title: _____

[SIGNATURES CONTINUED ON NEXT PAGE]

[SIGNATURES CONTINUED FROM PREVIOUS PAGE]

7382704

B-1

84

FURSA-0034970

SAFETY COMPONENTS INTERNATIONAL, INC.

By: Vicki Carly

Title: Treasurer

ASCI HOLDINGS GERMANY (DE), INC.

By: Vicki Carly

Title: Treasurer

ASCI HOLDINGS U.K. (DE), INC.

By: Vicki Carly

Title: Treasurer

ASCI HOLDINGS MEXICO (DE), INC.

By: Vicki Carly

Title: Treasurer

ASCI HOLDINGS CZECH (DE), INC.

By: Vicki Carly

Title: Treasurer

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL, S.A. de C.V.

By: Vicki Carly

Title: Treasurer

[SIGNATURES CONTINUED ON NEXT PAGE]

[SIGNATURES CONTINUED FROM PREVIOUS PAGE]

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL S.R.O.

By: PAVEL MOOZ

Title: DIRECTOR

AGREED:

WACHOVIA BANK, NATIONAL ASSOCIATION,
successor by merger to Congress Financial Corporation
(Southern)

By: _____

Title: _____

734270.4

B-3

86

FURSA-0034972

[Execution]

AFFIDAVIT OF EXECUTION AND DELIVERY

The undersigned _____ (the "Affiant") hereby deposes and says:

1. That Affiant is a duly authorized officer of Automotive Safety Components International GmbH & Co. KG ("German Borrower" and, together with certain other entities, individually each a "Borrower" and collectively, "Borrowers") or Automotive Safety Components International s.r.o. ("Automotive Safety Czech" and together with certain other entities, each individually a "Guarantor" and collectively, "Guarantors") for the purposes of executing and delivering, on behalf of each Borrower and Guarantor, certain loan documents executed outside of the State of Florida by borrowing customers of Wachovia Bank, National Association ("Wachovia").

2. On October 20, 2006, Affiant, acting as a duly authorized officer of German Borrower or Automotive Safety Czech, as applicable, executed Amendment No. 7 to Loan and Security Agreement, dated as of October 20, 2006, by and among Borrowers, Guarantors and Wachovia in the country of _____ and delivered it to Steven Cole of Wachovia in the State of North Carolina.

FURTHER AFFIANT SAYETH NOT.

Dated: October 20, 2006

**AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG**

By: _____

Title: _____

**AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL S.R.O.**

By: _____

Title: _____

739037.1

87

FURSA-0034973

[Execution]

AFFIDAVIT OF EXECUTION AND DELIVERY

The undersigned _____ (the "Affiant") hereby deposes and says:

1. That Affiant is a duly authorized officer of Automotive Safety Components International GmbH & Co. KG ("German Borrower" and, together with certain other entities, individually each a "Borrower" and collectively, "Borrowers") or Automotive Safety Components International s.r.o. ("Automotive Safety Czech" and together with certain other entities, each individually a "Guarantor" and collectively, "Guarantors") for the purposes of executing and delivering, on behalf of each Borrower and Guarantor, certain loan documents executed outside of the State of Florida by borrowing customers of Wachovia Bank, National Association ("Wachovia").

2. On October 20, 2006, Affiant, acting as a duly authorized officer of German Borrower or Automotive Safety Czech, as applicable, executed Amendment No. 7 to Loan and Security Agreement, dated as of October 20, 2006, by and among Borrowers, Guarantors and Wachovia in the country of _____ and delivered it to Steven Cole of Wachovia in the State of North Carolina.

FURTHER AFFIANT SAYETH NOT.

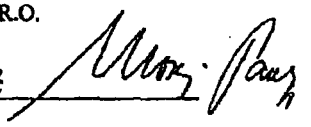
Dated: October 20, 2006

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL GmbH & CO. KG

By: _____

Title: _____

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL S.R.O.

By: PAVEL MODZ 

Title: DIRECTOR

739037.1

88

FURSA-0034974

[SIGNATURES CONTINUED FROM PREVIOUS PAGE]

AUTOMOTIVE SAFETY COMPONENTS
INTERNATIONAL S.R.O.

By: _____

Title: _____

AGREED:

WACHOVIA BANK, NATIONAL ASSOCIATION,
successor by merger to Congress Financial Corporation
(Southern)

By:  _____

Title: Managing Director

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

Brian P. Menezes, Respondent,

v.

WL Ross & Co. LLC, Wilbur L. Ross, Jr.,
Michael J. Gibbons, David H. Storper, David L. Wax,
Joseph L. Gorga, Stephen B. Duerk,
WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P., WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC, Appellants.

RECEIVED
APR 07 2011
SC Court of Appeals

Appeal From Greenville County
Edward W. Miller, Circuit Court Judge

Opinion No. 4810
Filed March 23, 2011

PROOF OF SERVICE

The undersigned certifies that a copy of **Respondent's Motion to Supplement the Record on Appeal (S.C. Rule 212(b))**, has been served upon all parties via Electronic Mail and United States Mail, first-class postage prepaid, to the addresses shown below on the 7th day of April, 2011.

H. Sam Mabry, III
J.D. Quattlebaum
Haynsworth Sinkler Boyd, P.A.
Two Liberty Square – 11th Floor
75 Beattie Place
Greenville, SC 29601
smabry@hsblawfirm.com
dquattlebaum@hsblawfirm.com

Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Atlanta, GA 30309-3053
mmcconnell@jonesday.com
jfinley@jonesday.com



NEXSEN PRUET, LLC
1230 Main Street, Suite 700 (29201)
Post Office Drawer 2426
Columbia, South Carolina 29202
Tel: 803.771.8900
Fax: 803.253.8277

Attorneys for Plaintiffs

April 7, 2011

The South Carolina Court of Appeals

Brian P. Menezes,

Respondent,

v.

WL Ross & Co. LLC, Wilbur L. Ross,
Jr., Michael J. Gibbons, David H.
Storper, David L. Wax, Joseph L.
Gorga, Stephen B. Duerk, WLR
Recovery Fund II, L.P., WLR Recovery
Fund III, L.P., WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC,

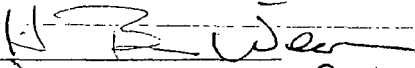
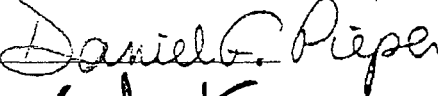
Appellants.

The Honorable Edward W. Miller
Greenville County
Trial Court Case No. 2008-CP-23-2701

ORDER

The Motion to Supplement the Record on Appeal was not filed in a timely fashion and is therefore denied.

"Motion Denied."

s/ 
s/ 
s/ 

IT IS SO ORDERED.

92

Columbia, South Carolina
4/12/2011

cc: H. Sam Mabry, III, Esquire
Charles M. Sprinkle, III, Esq.
James Derrick Quattlebaum, Esquire
Joseph N. Finley
Michael J. McConnell
N. Scott Fletcher
Russell Thomas Burke, Esquire
William D. Herlong, Esquire

**THE STATE OF SOUTH CAROLINA
In The Court Of Appeals**

**APPEAL FROM GREENVILLE COUNTY
Court of Common Pleas**

Edward W. Miller, Circuit Court Judge

Case No. 2008-CP-23-2701
**South Carolina Court of Appeals
Opinion No. 4810, filed March 23, 2011**

Brian P. Menezes,

Respondent,

v.

WL Ross & Co. LLC, Wilbur
L. Ross, Jr., Michael J.
Gibbons, David H. Storper,
David L. Wax, Joseph L.
Gorga, Stephen B. Duerk,
WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P.,
WLR Recovery Associates II,
LLC, and WLR Recovery
Associates III, LLC,

Appellants.

APPELLANTS' RETURN TO RESPONDENT'S PETITION FOR REHEARING

Michael J. McConnell
N. Scott Fletcher
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Suite 800
Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

H. Sam Mabry, III
James Derrick Quattlebaum
Charles M. Sprinkle III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square, 11th Floor
75 Beattie Place
Greenville, South Carolina 29601
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

Attorneys for Appellants

94

INTRODUCTION

Respondent's Petition for Rehearing with Petition for Rehearing en Banc ("Pet.") marks a classic misuse of the rehearing procedure merely to re-hash arguments the Court already considered. *See Checker Yellow Cab Co. v. Checker Cab and Parcel Svc., Inc.*, 287 S.C. 608, 612, 340 S.E.2d 549, 552 (Ct. App. 1986) (The "purpose [of a motion for rehearing] is not to present points the lawyers of losing parties overlooked themselves or to have the case tried in the Court of Appeals a second time."). Respondent premises his request on (i) a publicly available document he failed to even try to include in the Record on Appeal until after this appeal was decided, which this Court has already declined to add to the appellate record, and which, in any event, is redundant of Respondent's previous arguments; (ii) a 2006 case, which Respondent failed to include in his briefs to the circuit court or this Court or to raise by a Notice of Supplemental Citation, but nevertheless discussed at oral argument, and which, in any event, does not alter the result; and (iii) a rehash of the same arguments that Respondent already made in Respondent's Brief. None of these is grounds for rehearing.

For similar reasons, nothing in Respondent's Petition warrants re-hearing *en banc*. The Court's decision fully addresses and resolves, without dissent, the controlling issue of Delaware law; it is not inconsistent with any prior or subsequent opinion of this Court; and it involves no South Carolina rule or principle of law but only the narrow question of when Respondent's alleged claims accrued under the law of Delaware. Accordingly, Respondent's Petition should be denied.

95

ARGUMENT

This case concerns the merger of Safety Components International, Inc. (“SCI”) with the former International Textile Group, Inc. (“FITG”). (*See* *Menezes v. WL Ross & Co., L.L.C.*, Op. No. 4810 (S.C. Ct. App. filed March 23, 2011) (Shearouse Adv. Sh. No. 11 at 40), 2011 WL 1118841 (“Op.”) *1.) The merger agreement was approved by SCI’s board on August 29, 2006. After that, Respondent’s Complaint alleges, the closing of the merger was “merely a formality.” (*Id.* *7.)

Respondent had previously served as SCI’s Chief Financial Officer and, for a time, Chief Executive Officer. (*Id.* *1.) After his employment was terminated in June 2006, he filed an employment lawsuit against SCI, which was pending as the merger was being negotiated and completed. (*Id.*) During his negotiations to settle Respondent’s employment litigation, his attorney presented to SCI’s counsel a draft amended complaint, which included an allegation (albeit stricken through) challenging the merger terms as unfair. (*Id.* n. 4.) Ultimately Respondent settled the employment case and, in exchange for substantial consideration, entered a broad release of claims against the Appellants. (*Id.* *1-2.) He signed the release on September 28, 2006—after the merger agreement had been signed but before the merger’s closing, which occurred on October 20, 2006. (*Id.*)

In 2008, Respondent filed this action challenging the merger. (*Id.* *2.) The Appellants asserted affirmative defenses based on the release as well as a counterclaim for breach of the release. The trial court dismissed the counterclaim and struck the affirmative defenses, ruling that the release did not apply because Respondent’s claims against the merger did not accrue until the merger closed—*i.e.*, after Respondent signed

the release—as opposed to accruing when the merger agreement was signed. (*Id.*) This Court reversed by its Opinion issued March 23, 2011.

Respondent has now petitioned for rehearing and rehearing *en banc*. His alleged grounds, however, are not meritorious.

I. Respondent's Petition Is Not Well Founded Because It Relies On Redundant Material That Is Not Part Of The Record And, In Any Event, Does Not Alter This Court's Well-Reasoned Analysis.

The Petition relies, first of all, on evidence that Respondent never attempted to place in the record before now—a certain third-party statement approving the merger. (Pet. 1 (asserting, “the Court [] did not recognize that the [m]erger agreement was conditional on third party approval”).) This reliance is misplaced, not only because this Court has already denied Respondent's untimely request to add the document to the record but also because the document makes no difference.

The new document in question is a Consent issued by Wachovia Bank, N.A. to the Merger. The Consent is dated October 20, 2006, more than four-and-a-half years ago, and Respondent concedes the Consent has been publicly available. (Mem. in Supp. of Pet. for Reh'g (“Pet. Mem.”) 20, n. 7.) Respondent, however, failed to cite this document in the circuit court or anywhere in Respondent's Brief. Although he discussed it during his oral argument in this Court,¹ he never, before now, moved to add it to the appellate record. Only now, after losing the appeal, has Respondent asked to supplement the record with this document. This Court has rejected that request as untimely, and it

¹ The reference can be heard at the audio recording of oral argument, beginning at minute 11:40 and ending at 12:15.

follows that neither the document nor any argument based on it can be grounds for rehearing.

Moreover, the Consent adds nothing to the arguments Respondent previously submitted in Respondent's Brief and oral argument. Respondent uses it to reiterate his position that the Merger's closing was conditional, but this is hardly a new position. Respondent's Brief to this Court was replete with assertions and argument regarding conditions to closing the merger (Respondent's Br. ("Resp. Br.") 6, 17-24), and this Court's Opinion acknowledges and addresses Respondent's arguments. (See Op. *2.) Indeed, Respondent discussed the Consent at oral argument, leaving no doubt that the Court was apprised of its existence and Respondent's position as to its supposed significance. Thus, even if Respondent's untimely request to supplement the record had been granted, Appellants respectfully submit the document does not change the outcome or the rationale of this Court's opinion.

II. Respondent's Petition Is Not Well Founded Because It Relies On A Redundant Case Citation That Was Discussed At Oral Argument And That Does Not Alter This Court's Well Reasoned Analysis.

As his second alleged ground for rehearing, Respondent asserts that this Court "did not consider the holding of *Teachers' Retirement System of Louisiana v. Aidinoff*["] (Pet. 1.) But the facts are (i) Respondent discussed this case in detail at oral argument, even though he never properly served a Notice of Supplemental Citations under Rule 208(b)(7) SCACR, and (ii) the case does not change the outcome.

Although the *Teachers' Retirement System* case was decided in 2006, Respondent never mentioned it in any of his briefs to the circuit court nor in his Brief to this Court. He also never submitted any Notice of Supplemental Citations under Rule 208(b)(7),

SCACR.² What Respondent did do, however, was devote substantial time to the case during his oral argument in this Court,³ such that the Court was unquestionably informed of the case and Respondent's interpretation of it. *See Hicks v. Hicklin*, 187 S.C. 355, 364, 197 S.E. 390, 393 (1938) (rejecting argument in petition for rehearing that points had been overlooked where the "propositions have already been presented to this Court in the printed briefs and in the oral argument").

Having heard this argument, the Court reversed the circuit court anyway, and the Court was correct. Far from contradicting this Court's ruling, the *Teachers' Retirement System* opinion notes the general rule that "when a contract is contended to have resulted from fiduciary misconduct, the statute of limitations begins running at the time of the decision to contract, as the date of the key wrong." *Teachers' Retirement System of Louisiana v. Aidinoff*, 900 A.2d 654, 666 (Del. Ch. 2006). The opinion thus neatly accords with this Court's ruling that "once the merger agreement was signed, [Respondent] as a shareholder, had a legally enforceable right to enjoin the merger from being consummated." (Op. *8.)

² Rule 208(b)(7) provides the mechanism for submitting new or overlooked authority to the Court. It requires that "[w]hen pertinent and significant authorities come to the attention of a party after his initial brief(s) has been served and filed, the party shall promptly advise the clerk of the appellate court, by letter, with a copy to all counsel, setting forth the citations." Respondent never sent such a letter.

³ The discussion can be heard at the audio recording of oral argument, beginning at minute 12:17 and ending at 13:32.

III. Respondent's Petition Is Not Well Founded Because It Merely Rehashes Arguments From His Earlier Brief, Which This Court Properly Considered And Rejected.

As the third supposed basis for rehearing, Respondent merely reiterates the same argument he made before—that “an actual breach of fiduciary duty claim based on the merger agreement could not have been brought prior to Closing.” (Pet. 2.) The argument is incorrect; it has been ruled on; and repeating it yet again is not a valid ground for rehearing.

“The purpose of a petition for rehearing is not to present points which lawyers for losing parties have overlooked or misapprehended, nor is it the purpose of the petition for rehearing to have the case tried in the appellate court a second time.” Jean Hoefer Toal *et al.*, *Appellate Practice in South Carolina* 293 (2d ed. 2002). Thus, as this Court has held, “there is no basis for granting a rehearing” where “the Court is unable to discover that any material fact or principle of law has either been overlooked or disregarded.” *Wellman, Inc. v. Square D Co.*, 366 S.C. 61, 64, 620 S.E.2d 86, 87 (Ct. App. 2005). “It is not intended that [a petition for rehearing] shall be taken advantage of to reargue questions which were fully argued at the hearing, and were considered and decided by the Court.” *Huggins v. Atlantic C.L.R. Co.*, 96 S.C. 267, 283, 79 S.E. 406, 412 (1913).

Ignoring this rule, Respondent's Petition just rehashes arguments he already made. *See Arnold v. Carolina Power & Light Co.*, 168 S.C. 163, 173, 167 S.E. 234, 238 (1933) (“Usually [petitions for rehearing] are dismissed with a simple order to that effect, for the reason that they contain nothing but a ‘rehash’ of what the losing party has said before.”). Respondent's 37-page Memorandum in support of his Petition largely just repeats, *verbatim*, his earlier Brief to this Court. The only “new” material is his

discussion of the Wachovia Consent document and the *Teachers' Retirement System* case—both discussed above—and some attempted rejoinders to this Court's analysis of the pertinent Delaware law. (*Compare, e.g.,* Pet. Mem. 14-21 with Resp. Br. 12-17.)

The redundancy of this Petition is clear from the opening sections of Respondent's supporting Memorandum. The Memorandum's Table of Contents shows that its argument headings are virtually identical to those in Respondent's Brief, except that Respondent has deleted one argument and also added a section devoted to the *Teachers' Retirement System* case. (*Compare* Resp. Br. ii-iii, with Mem. 2-3.) The Memorandum's Summary of Argument is likewise substantially identical to that in Respondent's Brief—the only difference being that the Memorandum omits two paragraphs that appeared in the Brief.⁴ (*Compare* Resp. Br. 6-7, with Pet. Mem. 11-12.) The Summary of Argument in the current Memorandum contains not a single new word that Respondent did not already argue to this Court.

This Court has already addressed all of Respondent's points. First, Respondent devotes many pages to reiterating his "legally enforceable rights" argument, based on the *Teachers Retirement System* case and *In re Coca-Cola Enters.*, No. 1927-CC, 2007 WL 3122370 (Del. Ch. 2007), *aff'd*, *Int'l Brotherhood Teamsters v. Coca-Cola*, No. 1927-cc, 2008 WL 2484587 (Del. 2008). (*See* Pet. Mem. 14-21.) But this Court considered and rejected the argument, including a detailed examination of the *Coca-Cola* precedent. (*See* Op. *8.) Ultimately, this Court determined,

⁴ In addition, Respondent changes an assertion concerning the pace of losses being incurred by FITG from "\$1.9 million each week" to "millions of dollars each week."

[W]e do not believe the “legally enforceable rights” language in *Kahn* and *Coca-Cola* necessitate a finding that [Respondent’s] claim accrued after the merger. Once the merger agreement was signed, [the merging entities] had legally enforceable rights against each other to proceed with all aspects of the merger agreement in good faith. If they did not, they would be in breach of the agreement and subject to suit. More importantly, once the merger agreement was signed, [Respondent] as a shareholder, had a legally enforceable right to enjoin the merger from being consummated.

(*Id.*)⁵

Respondent also revisits his argument that three other cases, upon which the circuit court relied, compel a result in Respondent’s favor (*see* Pet. Mem. 22-28)—another argument that this Court fully addressed and refuted. Indeed, most of this Court’s opinion is comprised of a careful analysis of these cases, including their antecedents and their subsequent interpretation and treatment by Delaware courts. (*See* Op. *3-8.) And, after this multi-page discussion, the Court observed, “[a]fter reviewing the facts of the case *sub judice* and all the relevant case law, we conclude the circuit court’s reliance on the four cases cited above was misplaced.” (*Id.* *7.) This Court did not overlook or in any way fail to address Respondent’s contentions.⁶

Next, Respondent repeats his argument that certain “standing” cases relied upon by Appellants and cited by this Court are inapposite—even though they show beyond question that shareholders, including Respondent, could have brought a claim to enjoin the merger as soon as the merger agreement was signed. Here again, this Court has

⁵ Although the Appellants will not burden the Court with a detailed restatement of their response to this argument, their response appears at Appellants’ Reply Br., pp. 10-14.

⁶ Appellants’ response to this argument appears at Appellants’ Reply Br., pp. 15-17.

already considered Respondent's positions. The Court's opinion devotes several paragraphs to discussing some of these cases and the pertinence of their holdings. (*Id.* *2, n. 9 & *3.) The Opinion notes that even Respondent's cited authorities look to standing cases as precedent, thus establishing the relevance of those cases to the issues here. (*Id.* *7 ("Kaufman relies heavily on *Lavine*, which was a case involving the plaintiff's standing to bring suit."). Moreover, the Court specifically addressed Respondent's argument that cases concerning standing could only apply where the closing of a merger was a "mere technicality" (*see* Pet. Mem. 30)—by noting undisputed facts showing that the shareholder approvals required for the merger to close were "assured," as well as Respondent's own allegation that the closing in this case was "merely a formality." (*Id.*)⁷

The Court's citations to the law and the record, including Respondent's own Complaint, also dispensed with the final argument that Respondent made in his Respondent's Brief and now repeats in his Petition—namely, his attempt to frame this case as concerning only the "fact" of the merger, and not its terms.⁸ The Court specifically noted Respondent's allegation in the Complaint that the defendants breached their fiduciary duty "*by approving the merger on terms* which gave 65% ownership to the FITG shareholders and diluted the minority shareholders to 35%, or at all." (*Id.* *2 (emphasis added).)⁹ Furthermore, countering Respondent's assertion that no claim for

⁷ Appellants' response to this argument appears at Appellants' Reply Br., pp. 8-9.

⁸ Appellants' response to this argument appears at Appellants' Reply Br., pp. 17-20.

⁹ Indeed, Respondent's Complaint specifically alleges that the Appellants knew or should have known the supposed facts about FITG's declining business before Respondent signed his broad release. (*See* R p.19.)

breach of fiduciary duty could have arisen prior to closing, the Court noted that Respondent himself contemplated a claim for injunctive relief before the merger closed, going so far as to include such a claim in a draft pleading given to opposing counsel in the employment litigation:

Dofflemeyer [one of Respondent's cited cases] seems out of step with more recent case law on fiduciary duty claims because those cases indicate a claim may be brought prior to the incurring of money damages in the form of a request for injunctive relief. [Respondent] could have brought a claim for injunctive relief prior to the signing of the Release, and this thought was at least contemplated as evidenced by the inclusion of such an allegation in his draft amended complaint given to opposing counsel in the employment litigation. [Respondent's] remedy, money damages, may have been different, but the claim, breach of fiduciary duty, would be the same.

(*Id.* *7.)

In sum, this Court's detailed opinion has addressed Respondent's contentions. Respondent has failed to identify any point that was overlooked or misapprehended. His mere rehashing of previously asserted arguments, already made in Respondent's Brief and during oral argument, is not grounds for rehearing.

IV. Respondent's Petition For *En Banc* Review Is Not Well Founded For All The Foregoing Reasons And Because The Court's Opinion Is Not Inconsistent With Any Prior or Subsequent Decision Of This Court And Raises No Issue Of South Carolina Law.

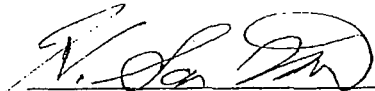
Additionally, there is no reason or basis to support Respondent's request that this Court rehear this appeal *en banc* pursuant to Rule 219, SCACR. The opinion issued by the Court in this matter was fully resolved without dissent, and the opinion is not inconsistent with any prior or subsequent decision of the South Carolina Court of Appeals or South Carolina Supreme Court. Indeed, it is undisputed that the issue on appeal is purely a question of controlling Delaware law (*see* Op. *3), and does not raise or implicate any issue of South Carolina law. As the parties conceded and this Court has

held, this case involved the narrow question of when Respondent's alleged claims accrued under Delaware law. This is not an issue as to which future guidance is needed by the trial courts of South Carolina. Rehearing *en banc* is not warranted.

CONCLUSION

For the reasons stated herein, Appellants respectfully request that Respondent's Petition for Rehearing with Petition for Rehearing *En Banc* be denied.

Respectfully submitted,



H. Sam Mabry, III
James Derrick Quattlebaum
Charles M. Sprinkle III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square, 11th Floor
75 Beattie Place
Greenville, South Carolina 29601
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

Michael J. McConnell
N. Scott Fletcher
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Suite 800

Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

Attorneys for Appellants WL Ross & Co. LLC,
Wilbur L. Ross, Jr., Michael J. Gibbons, David H.
Storper, David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund III, L.P., WLR
Recovery Associates II LLC, and WLR Recovery
Associates III LLC.

April 21, 2011
Greenville, South Carolina

105

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM GREENVILLE COUNTY
Court of Common Pleas

Honorable Edward W. Miller, Circuit Court Judge

C.A. No. 2008-CP-23-2701

Brian P. Menezes Plaintiff/Respondent,

v.

WL Ross & Co., LLC, Wilbur L. Ross, Jr., Michael J.
Gibbons, David H. Storper, David L. Wax, Joseph L.
Gorga, Stephen B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P., WLR Recovery Associates
II, LLC and WLR Recovery Associates III, LLC, ... Defendants/Appellants.

PROOF OF SERVICE

The undersigned employee of the law offices of Haynsworth Sinkler Boyd, P.A.,
attorneys for Defendants/Appellants do hereby certify that I have served counsel
specified below in this action with one (1) copy of the documents below by serving
copies of the same, via electronic and United States Mail, first-class postage prepaid, to
the addresses shown below on this the 21st day of April, 2011:

DOCUMENTS SERVED:

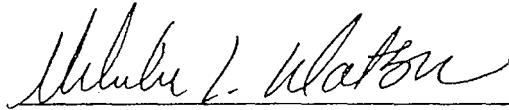
APPELLANTS' RETURN TO RESPONDENT'S PETITION FOR REHEARING

106

COUNSEL SERVED:

William D. Herlong, Esquire
Herlong Law Firm, LLC
P.O. Box 2003
Greenville, SC 29602-2003
william@herlonglaw.com

Thomas L. Stephenson, Esquire
Russell T. Burke, Esquire
Nexsen Pruet, LLC
Post Office Drawer 10648
Greenville, SC 29603-0648
tstephenson@nexsenpruet.com
rburke@nexsenpruet.com



Melodie L. Watson, CP
Paralegal
Haynsworth Sinkler Boyd, P.A.
75 Beattie Place, 11th Floor
Post Office Box 2048 (29602)
Greenville, South Carolina 29601
(864) 240-3200 Tel
(864) 240-3300 Fax

The South Carolina Court of Appeals

Brian P. Menezes,

Respondent,

v.

WL Ross & Co. LLC. Wilbur L. Ross,
Jr., Michael J. Gibbons, David H.
Storper, David L. Wax, Joseph L.
Gorga, Stephen B. Duerk, WLR
Recovery Fund II, L.P., WLR Recovery
Fund III, L.P., WLR Recovery
Associates II LLC, and WLR Recovery
Associates III LLC,

Appellants.

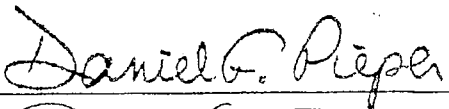
The Honorable Edward W. Miller
Greenville County
Trial Court Case No. 2008-CP-23-2701

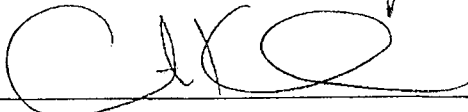
ORDER DENYING PETITION FOR REHEARING

PER CURIAM: After a careful consideration of the Petition for Rehearing, the Court is
unable to discover that any material fact or principle of law has been either overlooked or
disregarded and hence, there is no basis for granting a rehearing.

It is, therefore, ordered that the Petition for Rehearing be denied.

 J.

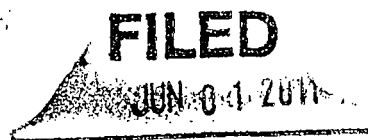
 J.

 J.

109

Columbia, South Carolina

cc: H. Sam Mabry, III, Esquire
Charles M. Sprinkle, III, Esq.
James Derrick Quattlebaum, Esquire
Joseph N. Finley
Michael J. McConnell
N. Scott Fletcher
Russell Thomas Burke, Esquire
William D. Herlong, Esquire





RECEIVED
JUN 02 2011
NEXSEN PRUET, LLC

The South Carolina Court of Appeals

TANYA A. GEE
CLERK

V. CLAIRE ALLEN
DEPUTY CLERK

POST OFFICE BOX 11629
COLUMBIA, SOUTH CAROLINA 29211
1015 SUMTER STREET
COLUMBIA, SOUTH CAROLINA 29201
TELEPHONE: (803) 734-1890
FAX: (803) 734-1839
www.sccourts.org

June 1, 2011

Russell Thomas Burke, Esquire
Nexsen Pruet, LLC
P.O. Drawer 2426
Columbia, SC 29202-2426

Re: Menezes, Brian P. v. WL Ross & Co.

Dear Mr. Burke:

Enclosed is a copy of an Order of the Court denying your Petition for Rehearing in the above case.

Your Petition for Rehearing En Banc was distributed to the judges, but it has been rejected. See Rule 219, SCACR (amended April 28, 2011).

The Remittitur in this case will be held in this Court only so long as required by Appellate Court Rule 221 (b).

Please notify this office, in writing, within ten (10) days from the date of this letter, whether or not you want any of the remaining Records on Appeal and briefs we may have in this case. Also enclose a check payable to the S. C. Court of Appeals, in the amount of \$7.50, to cover mailing costs. If we have not heard from you within ten (10) days, the Record on Appeal and briefs will be disposed of.

Sincerely,

A handwritten signature in black ink, appearing to read "Renee S. Johnson".

Renee S. Johnson
Administrative Specialist

110


TAG/rj

cc: H. Sam Mabry, III, Esquire
Charles M. Sprinkle, III, Esq.
James Derrick Quattlebaum, Esquire
Joseph N. Finley
Michael J. McConnell
N. Scott Fletcher
William D. Herlong, Esquire

///

17906

THE STATE OF SOUTH CAROLINA
In the Court of Appeals

APPEAL FROM GREENVILLE COUNTY
Court of Common Pleas

Honorable Edward W. Miller, Circuit Court Judge

C.A. No. 2008-CP-23-2701

Brian P. Menezes..... Respondent,

v.

WL Ross & Co., LLC, Wilbur L. Ross, Jr., Michael J.
Gibbons, David H. Storper, David L. Wax, Joseph L.
Gorga, Stephen B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P., WLR Recovery Associates
II, LLC and WLR Recovery Associates III, LLC, ...I Appellants.

RECORD ON APPEAL
VOL. I

William D. Herlong, SC Bar No. 14283
Anderson & Herlong, LLC
111 E. North Street (29601)
P.O. Box 2105
Greenville, SC 29602-2105
Telephone: (864) 752-0011
Facsimile: (864) 752-0820

ATTORNEY FOR RESPONDENT

H. Sam Mabry, III, SC Bar No. 3490
Charles M. Sprinkle III, SC Bar No. 70630
HAYNSWORTH SINKLER BOYD, P.A.
75 Beattie Place, 11th Floor (29601)
P.O. Box 2048
Greenville, SC 29602
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E., Suite 800
Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

ATTORNEYS FOR APPELLANTS

INDEX

Order of Judge Edward W. Miller dated February 17, 2009 denying Defendants' Motion for Judgment on the Pleadings or Summary Judgment, granting Plaintiff's Motion to Dismiss Defendants' counterclaim and striking Defendants' affirmative Defenses	1
Order of Judge Edward W. Miller dated March 4, 2009 denying Defendants' Motion for Reconsideration	3
Order of Court of Appeals dated April 21, 2009 denying Plaintiff's Motion to Dismiss.....	4
Plaintiff's Complaint dated April 9, 2008.....	6
Answer and Defenses of Stephen B. Duerk dated June 6, 2008	33
Answer, Defenses and Counterclaim of WL Ross & Co. LLC; Wilbur L. Ross, Jr.; Michael J. Gibbons; David H. Storper; David L. Wax; Joseph L. Gorga; WLR Recovery Fund II, L.P.; WLR Recovery Fund III, L.P.; WLR Recovery Associates II LLC; and WLR Recovery Associates III LLC dated June 6, 2008.....	53
Defendants' Motion for Judgment on the Pleadings Or, Alternatively, Motion for Summary Judgment dated June 6, 2008	94
Plaintiff's Motion to Dismiss Counterclaim dated July 2, 2008.....	113
Memorandum in Support of Motion for Judgment on the Pleadings or, Alternatively, Motion for Summary Judgment dated July 28, 2008.....	116
Plaintiff's Memorandum in Opposition to Defendants' Motion to Dismiss dated July 31, 2008	250
Reply Memorandum in Support of Motion of Judgment on the Pleadings or, Alternatively, Motion for Summary Judgment dated August 8, 2008.....	291
Plaintiff's Second Memorandum in Opposition to Defendants' Motion to Dismiss dated August 20, 2009	343
Defendants' Sur-Reply Memorandum in Support of Defendants' Motion for Judgment on the Pleadings or, Alternatively, Motion for Summary Judgment dated August 21, 2008.....	367
Defendants' February 25, 2009 Motion for Reconsideration of Court's Order	

dated February 17, 2009 and filed February 18, 2009.....	379
Defendants' Notice of Appeal dated March 5, 2009	389
Motion to Dismiss Interlocutory Appeal and Memorandum in Support dated March 6, 2009	396
Petition for Rehearing to Clarify Order on Plaintiff/Respondent's Motion to Dismiss the Appeal dated May 14, 2009	408
Complaint in <i>Menezes v. Safety Components International, Inc. and Gorga</i> , C.A. 2006-CP-23-4326	517
Transcript of Record for July 31, 2008 Hearing	552
Affidavit of Stephen B. Duerk dated June 5, 2008	604
Affidavit of Matthew K. Johnson dated June dated July 30, 2008	619
Letter dated February 10, 2009 from H. Sam Mabry, III to Judge Edward W. Miller	750
Letter dated June 16, 2009 from Clerk of Court of Appeals to H. Sam Mabry, III returning original Motion for Rehearing to Clarify Order.....	753
Letter dated June 23, 2009 from H. Sam Mabry, III to Clerk of Court of Appeals refiling Petition for Rehearing	754
Proxy Statement from SCI-FITG Merger (including Merger Agreement between SCI and FITG, attached as Annex A) filed with the Securities and Exchange Commission September 22, 2006.....	756
Certificate of Counsel.....	1111

STATE OF SOUTH CAROLINA)

) IN THE COURT OF COMMON PLEAS

COUNTY OF GREENVILLE)

Brian P. Menezes,

2009 FEB 18 CA No 2008-CP-23-2701

Plaintiff,

v.

FILED IN THE COURT
OF COMMON PLEAS
GREENVILLE, S.C.
2009 FEB 18

WL Ross & Co. LLC, Wilbur L. Ross,
Jr., Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR
Recovery Associates II LLC, and WLR
Recovery Associates III LLC,

Defendants.

ORDER

ENTERED COMPUTER

This action relates to a merger between Safety Components International, Inc. ("SCI"), and the former International Textile Group, Inc. ("FITG"), that closed on October 20, 2006.

Plaintiff alleges that the defendants breached their fiduciary duties to the minority shareholders of SCI (including the plaintiff) by allowing the merger to go forward or close. Defendants moved for judgment on the pleadings or in the alternative for summary judgment based on a release Plaintiff signed to settle an employment lawsuit on September 28, 2006, which released claims up through that date. In their Answer, Defendants have asserted Third and Fourth affirmative defenses related to the release, and filed a counterclaim based on the release. The Plaintiff filed a motion to dismiss Defendants' counterclaim.

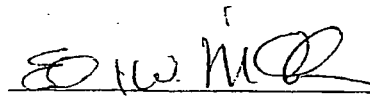
The Court heard lengthy oral argument on this issue and has carefully reviewed the multiple, extensive filings by the parties on this issue. The pertinent question is whether

Plaintiff's claims regarding the merger accrued when the merger closed on October 20, 2006, as Plaintiff contends, or sometime before September 28, 2006, as Defendants argue.

Under controlling Delaware law, these claims accrue no earlier than the closing of the merger. Kaufman v. Albin, 447 A.2d 761 (Del. Chan. May 11, 1982) (claim accrues on closing of merger); see also Dofflemyer v. W.F. Hall Printing Company, 558 F. Supp. 372 (D. Del. 1983) (same); cf. Baron v. Allied Artists Pictures Corporation, 717 F.2d 105 (3d Cir. 1983) (claim accrues when merger consummated). This is especially true here since there were extensive conditions precedent to the merger that were not satisfied before the closing date. The merger could not have been enforced by FITG against SCI prior to the closing date. As recently re-affirmed by the Delaware Supreme Court, there can be no breach of fiduciary duty claim regarding an underlying contract until the contract is legally enforceable. See Int'l Bhd. Teamsters v. Coca-Cola Co., 2008 WL 2484587 (Del. Sup. 2008), *aff'g* In re Coca-Cola Enterprises, Inc., 2007 WL 3122370 (Del. Ch. 2007) (no claim regarding underlying contract until "enforceable legal rights . . . were created.") Accordingly, since FITG had no right to enforce the merger until the closing date, plaintiff's claims for breach of fiduciary duty did not accrue until that date.

Defendants' Motion for Judgment on the Pleadings or, Alternatively, Motion for Summary Judgment is therefore DENIED; Plaintiffs' Motion to Dismiss Defendants' Counterclaim is GRANTED; and Defendants' Third and Fourth affirmative defenses based on the release are hereby STRICKEN.

IT IS SO ORDERED.


Edward W. Miller, Circuit Court Judge

Date: 2/17/08

214109

STATE OF SOUTH CAROLINA

COUNTY OF GREENVILLE

Brian P. Menezes,

Plaintiff,

v.

WL Ross & Co. LLC, Wilbur L. Ross,
Jr., Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR
Recovery Associates II LLC, and WLR
Recovery Associates III LLC,

Defendants.

)
) IN THE COURT OF COMMON PLEAS
)
) 2009 MAR -4 P 1:56
) C.A. No. 2008-CP-23-2701
)
)

) FILED-CLERK OF COURT
) GREENVILLE CO. S.C.
) PAUL B. WICKENSIMER
)
)
)

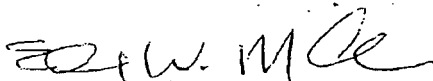
ORDER

On February 25, 2009, the Court received "Defendants' Motion for Reconsideration of Court's Order Dated February 17, 2009, and Filed February 18, 2009," along with "Defendants' Motion for Protective Order Staying Discovery" which asked for discovery to be stayed pending the Court's decision on the Motion for Reconsideration. Defendants did not ask for a hearing.

The order that Defendants sought to have reconsidered had denied "Defendants' Motion for Judgment on the Pleadings or, Alternatively, Motion for Summary Judgment," granted Plaintiff's "Motion to Dismiss Defendants' Counterclaim," and struck Defendants' Third and Fourth affirmative defenses.

The Court has carefully reviewed the Motion for Reconsideration and the arguments made therein. The Court finds no basis to change its prior ruling. Accordingly, the Motion for Reconsideration is DENIED. The Motion for Protective Order Staying Discovery is moot.

IT IS SO ORDERED.


Edward W. Miller, Circuit Court Judge

Date: 3/4/09

A Certified Copy
Paul B. Wickensimer
Clerk of Court C.P. & G.S.
Greenville County, SC
Dated 3-4-09

The South Carolina Court of Appeals

Brian P. Menezes.

Respondent.

v.

WL Ross & Co. LLC, Wilbur L. Ross,
Jr., Michael J. Gibbons, David H.
Storper, David L. Wax, Joseph L.
Gorga, Stephen B. Duerk, WLR
Recovery Fund III, L.P., WLR
Recovery Associates II LLC, and WLR
Recovery Associates III LLC,

Appellants.

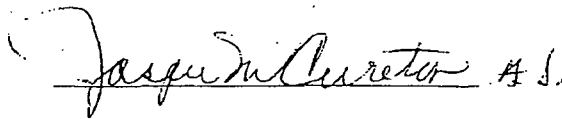
The Honorable Edward W. Miller
Greenville County
Trial Court Case No. 2008-CP-23-2701

ORDER

Appellants filed notice of appeal from the February 17, 2009 order of the circuit court denying their motion for judgment on the pleadings (Rule 12(c), SCRCP); denying their motion for summary judgment (Rule 56, SCRCP); granting Respondent's motion to dismiss their counterclaim; and striking Appellants' third and fourth affirmative defenses. Thereafter, Respondent submitted a motion asking this court to dismiss the appeal on the ground that Appellants were appealing from an interlocutory order and the issues raised were not immediately appealable. After careful review of Respondent's memorandum in support of the motion and Appellants' return, we hereby deny Respondent's motion to dismiss the appeal. Further, on appeal, this court's review of the circuit court's February 17, 2009 order will be confined to the rulings dismissing Appellants' counterclaim and striking Appellants' third and

fourth affirmative defenses. See S.C. Code Ann. § 14-3-330(2)(c) (1976) (stating an order affecting a substantial right that strikes an answer or any part of a pleading is appealable). This court will not review the circuit court's denial of Appellants' motion for judgment on the pleadings or denial of summary judgment. See Rose v. Thrash, 291 S.C. 459, 354 S.E.2d 378 (1987) (holding denial of a motion for judgment on the pleadings is not directly appealable, even if it raises only a question of law); Olson v. Faculty House of Carolina, Inc., 354 S.C. 161, 580 S.E.2d 440 (2003) (holding the denial of summary judgment is not appealable).

IT IS SO ORDERED.

 Jasper M. Clureton #1.

Columbia, South Carolina

April 21, 2009

cc: H. Sam Mabry, III, Esquire
William D Herlong, Esquire

FILED
4/29/09 

STATE OF SOUTH CAROLINA

COUNTY OF GREENVILLE

Brian P. Menezes,

Plaintiff,

v.

WL Ross & Co. LLC, Wilbur L. Ross.
Jr., Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR
Recovery Associates II LLC, and WLR
Recovery Associates III LLC,

Defendants.

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23- 2701

COMPLAINT - Proposed Class Action
Jury Trial Demanded

Plaintiff alleges:

Introduction

1. In this case, the owners and managers of a Wall Street leveraged buyout firm with a major investment in a failing private company in North Carolina, engineered the merger of that company into a small public company in Greenville that the LBO firm came to control also. The terms of the merger were inconsistent with the true values of the two companies and to the GREAT disadvantage of the minority stockholders of the public company.

2. By this process, the LBO firm and its managers enhanced their own economic interests dramatically while undermining the economic interests of the minority stockholders of the Greenville company by more than 90%, from approximately \$20 million before the merger was announced to just over \$2 million today.

3. Plaintiff was one of those minority stockholders. The value of his interest was undermined from approximately \$1.5 million before the merger was announced to less than \$170,000 today.

THE PARTIES AND REFERENCED ENTITIES

4. Plaintiff Brian P. Menezes is an adult individual resident of South Carolina residing at 307 Block House Road, Greenville, Greenville County, South Carolina 29615. He was employed by Safety Components International, Inc. ("SCI") as CFO and then Interim CEO from 1999 through June 2006. Since prior to the events at issue here, he has owned 102,000 shares of SCI stock. On August 29, 2006, the day before the announcement of the merger at issue here (the "Merger"), SCI shares traded at \$14.65 a share. On April 2, 2008, the most recent trade, the stock traded for \$1.65 a share.

5. Defendant WL Ross & Co. LLC ("WLR"), is an investment firm based in New York City that specializes in leveraged restructurings, buyouts, and industry consolidations ("LBOs") of financially distressed companies. Individual Defendants Ross, Gibbons, Storper, Wax and Gorga were and are employees, agents, and/or affiliates of WLR, and it is responsible for their actions under the principal of respondeat superior.

6. The former International Textile Group, Inc. ("FITG"), was a privately held Delaware corporation with its headquarters in Greensboro, NC. It was formed by WLR in 2004 to consolidate the assets of Burlington Industries, Inc., and Cone Mills Corporation which WLR had purchased out of bankruptcy. FITG had four principle lines of business: bottom-weight woven apparel fabrics (including denim, synthetic and worsted fabrics), interior furnishings (including mattress fabrics and upholstery fabrics), government uniform fabrics (including fabrics for military dress and battle uniforms), and specialty fabrics and services (including

commission printing and finishing). FITG was merged into and took over Safety Components International, Inc., in 2006 in the transaction at issue in this matter (the "Merger").

7. WLR was at the time of the Merger the controlling shareholder of FITG, owning directly or beneficially 14,310,497 shares of FITG, constituting 85.4% ownership, and holding through affiliates five of the six seats on the FITG Board.

8. Safety Components International, Inc., was a publicly traded Delaware company with its headquarters in Greenville, SC, in the business of designing and developing airbag fabric and airbag cushions. As of 2005, SCI had a 66% share of the North American outsourced airbag cushion market, and an 11% share of the total North American air-bag cushion market, along with a 38% share of the European outsourced airbag cushion market, and a 16% share of the total European airbag cushion market, according to CSM Worldwide.

9. WLR was at the time of the Merger the controlling shareholder of SCI, owning directly or beneficially 4,162,394 shares of SCI stock, constituting 75.6% ownership of the company, and holding through affiliates four of the five seats on the SCI Board. WLR purchased its stock in SCI and became the controlling shareholder in December 2005.

10. After the merger of SCI and FITG (the "Merger"), the name of the combined company was changed to International Textile Group, Inc. To avoid confusion, the new company will be referred to hereinafter as the "Combined Company" or "NITG."

11. Nomenclature:

- (1) SCI, as used herein, refers to Safety Components International, Inc., prior to the merger of FITG into it.
- (2) FITG, as used herein, refers to the former International Textile Group, Inc., prior to its merger into SCI. And

- (3) The "Combined Company," or "NITG," refers to SCI after the merger of FITG into it and the name change to International Textile Group, Inc.

12. Defendant Wilbur L. Ross, Jr. ("Ross"), is an individual resident of New York. Ross created WLR in 2000. He is Chairman and CEO of WLR and has been at all relevant times, directly or indirectly or through affiliated persons or entities, its principal and/or controlling owner and has held, directly or indirectly, a major financial stake in WLR and/or its affiliated companies. Further, he was Chairman of the Boards of SCI and FITG prior to the Merger. Since the Merger, he has been Chairman of the Board of the Combined Company.

13. Each of Defendants Michael J. Gibbons ("Gibbons"), David H. Storper ("Storper"), and David L. Wax ("Wax") is an individual resident of New York or Connecticut. At all relevant times, each has been an employee, agent and/or affiliate of WLR and has had, directly or indirectly, a major financial stake in WLR and/or its affiliated companies. Gibbons and Storper were members of the Board of SCI and since the Merger have been members of the Board of the Combined Company. Wax was a member of the Board of FITG and since the Merger has been a member of the Board of the Combined Company.

14. Defendant Joseph L. Gorga ("Gorga") is an individual resident of North Carolina. Prior to the Merger, he was President and CEO of FITG. Since the Merger, he has been President and CEO of the Combined Company. Further, like Ross, he was a member of both the Boards of FITG and SCI prior to the Merger and has been a member of the Board of the Combined Company since. Prior to the merger, Gorga beneficially owned 213,750 shares of FITG stock, or 1.3% of the company. Upon information and belief, he did not own any stock of SCI prior to the Merger.

15. Gorga's compensation from FITG in 2005 included \$600,000 in base salary, \$297,301 in bonus, and \$511,559 for taxes incurred upon the vesting of restricted stock in 2005. In 2005, he was issued restricted stock valued at \$1,423,800 and options valued at \$1,017,000. Upon information and belief, he was granted additional restricted stock and/or options in 2006. Upon information and belief, all or a substantial portion of the restricted stock and stock options issued to Gorga vested upon consummation of the Merger.

16. Defendant Stephen B. Duerk is an individual resident of Greenville County, South Carolina. He was President of SCI prior to the Merger and after it was President of the Automotive Safety Group (what had been SCI) of the Combined Company. He was involved in the events at issue in this action and, in fact, executed the Merger agreement and closing documents on behalf of SCI. He retired on December 31, 2007.

17. Defendant WLR Recovery Fund II, L.P. ("WLR-Fund-II"), was the actual owner of 241,419 of the shares of SCI that WLR controlled prior to the Merger. Its general partner is Defendant WLR Recovery Associates II LLC ("WLR-Associates-II"), and its investment manager is WLR. Ross was/is the general manager of WLR-Associates-II. Ross and WLR-Associates-II had and have share voting and dispositive power over the shares owned by WLR-Fund-II. WLR and Ross are the beneficial owners of the shares held by WLR-Fund-II.

18. Defendant WLR Recovery Fund III, L.P. ("WLR-Fund-III"), was the actual owner of the 3,920,975 of the shares of SCI that WLR controlled prior to the Merger. Its general partner is WLR Recovery Associates III LLC ("WLR-Associates-III"), and its investment manager is WLR. Ross was/is the general manager of WLR-Associates-III. Ross and WLR-Associates-III had and have share voting and dispositive power over the shares owned by WLR-Fund-III. WLR and Ross are the beneficial owners of the shares held by WLR-Fund-III.

19. References to WLR, as used above and below herein, include WLR-Fund-II, WLR-Associates-II, WLR-Fund-III, and WLR-Associates-III.

THE MERGER

20. At some time during 2006, Defendants decided to combine FITG and SCI. The Merger took place on October 20, 2006.

21. The publicly stated reason for the Merger was that it would "allow the Combined Company to better serve its markets and customer base, more efficiently execute its business strategies, and result in greater long-term growth opportunities than either pre-merger company could achieve operating alone." It was said that the Merger would enable the Combined Company to "benefit from cost and operational synergies," "leverage scale and management expertise in international sales and operations," "improve its access to capital," "better leverage research and new product development capabilities," and "diversify financial and economic risks." (Prospectus, p.6.)

22. Since, as noted, WRL and Ross owned directly or indirectly 75.6% of the stock of SCI and 85.4% of the stock of FITG and controlled four of five directors on the SCI Board and five of six directors on the FITG Board, WLR and Ross were in a position cause the Merger to occur regardless of the interests of the minority stockholders, and no action was required of them. The approval process was a formality.

23. The Prospectus for the Merger (the "Prospectus") was straightforward about the fact that approval was a formality. As to SCI, it stated:

"No action by the stockholders of SCI is required to approve the merger agreement or to consummate the merger. However, it is a pre-condition to the merger that the stockholders of SCI adopt an amended and restated certificate of incorporation. Therefore, at SCI's 2006 Annual Meeting of Stockholders, holders of SCI common stock are being asked to adopt the amended and restated

certificate of incorporation and also to re-elect the five current members of the board of directors of SCI, all as described more fully in the accompanying joint proxy statement/prospectus. Stockholders of SCI holding approximately 75.6% of SCI's outstanding common stock have indicated that they intend to vote to adopt the amended and restated certificate of incorporation and to elect the directors nominated for re-election. Approval of the matters to be voted on at the 2006 Annual Meeting is therefore assured.

(Prospectus, first page, emphasis added.) As to FITG, it stated:

Approval of the merger agreement by the stockholders of ITG is required to consummate the merger. International Textile Holdings, Inc. [an affiliate of WLR], the owner of approximately 85.4% of ITG's common stock, has consented in writing to the approval of the merger agreement and the merger. As a result, no additional ITG stockholder approval is required, and ITG stockholders need not do anything further at this time.

(*Id.*, emphasis added.)

24. The minority stockholders of SCI had no ability to stop the Merger had they wanted to. In fact, unlike the minority stockholders of FITG, the minority stockholders of SCI did not even have appraisal rights. This was because of the structure of the Merger and the fact that FITG was technically being merged into SCI (even though, in truth, FITG acted as the dominant party acquiring SCI).

25. When the Merger took place on October 20, 2006, each shareholder of FITG surrendered his FITG stock and received shares of SCI on the ratio of 1.4739 to 1 (the "Exchange Ratio"). In other words, for each 1.4739 shares of FITG stock surrendered, the FITG shareholder received 1 share of SCI stock. (In addition, each restrictive share and option to purchase shares of FITG stock was converted into the same for shares of SCI on the same ratio.)

26. After the Merger, the stock issued to the former FITG stockholders amounted to 65% of the stock of the Combined Company, which equated to 65% ownership of the Combined Company. The stock that pre-merger SCI stockholders held amounted to 35% of the stock of the Combined Company, which equated to 35% ownership of the Combined Company. In other

words, FITG stockholders owned 65% of the value of the Combined Company and pre-merger SCI stockholders owned 35% of the value.

27. As this shows, the SCI stockholders went from owning 100% of pre-merger SCI to owning just 35% of the Combined Company. More importantly, the minority stockholders of SCI (those other than WLR and its affiliates) went from owning 24.4% of pre-merger SCI to owning a little more than seven percent of the Combined Company. Plaintiff went from owning 1.85% of pre-merger SCI to owning only slightly more than one-half of one percent of the Combined Company.

28. The consideration to FITG stockholders for the Merger can also be looked at in dollar amounts. Pursuant to the Exchange Ratio, SCI issued a total of 11,975,943 additional shares of SCI stock and options for the purchase of 641,495 more shares. The total number SCI shares issued (or to-be-issued) to FITG stockholders and optionholders pursuant to the merger was 12,617,438. (Prospectus, p.9.)

29. The price of SCI stock was \$14.65 per share on August 29, 2006, the day the Merger terms were agreed to. Effectively, the SCI Board had agreed to pay approximately \$185 million for FITG (or 12,617,438 shares times \$14.65/share). After the Merger was announced on September 22, 2006, the price of SCI stock dropped until on October 20, 2006 (the day of the Merger), it was \$13.25 per share. This meant that SCI in effect gave consideration in the Merger worth at \$167 million as of that date.

30. WLR, as already noted, owned 85.4% of FITG which amounted to 14,310,497 shares of FITG. Based on the Exchange Ratio, WLR received 9,709,273 shares of SCI stock in return for its FITG stock. Using the SCI share price as of the Merger date, WLR received consideration valued at \$129 million in the Merger.

31. Gorga owned 213,750 shares of FITG stock. Based on the Exchange Ratio, he received 145,023 shares of SCI stock for the FITG stock that he owned (including beneficial stock on both side). Using the SCI share price as of the Merger date, Gorga received consideration valued at \$1.92 million in the Merger.

32. The dilution of Plaintiff and other minority SCI stockholders' ownership interest in SCI and the consideration that SCI paid for FITG might have been appropriate if FITG had been worth the \$167 million in consideration that SCI gave.

33. FITG was not, however, worth even close to that amount.

The Background for The Exchange Ratio
And the Consideration Given By SCI for FITG

34. The Exchange Ratio effectively set the price that SCI paid for FITG in the Merger.

35. The Exchange Ratio was agreed to on August 23, 2006, by Dr. Daniel Tessori in his capacity as the SCI Special Committee appointed by the SCI Board with "exclusive authority on behalf of SCI to review, evaluate, investigate, negotiate and, if appropriate, approve the terms of any potential transaction between SCI and WLR, or any of its affiliates." (Prospectus, p. 46.)

36. Dr. Tessori, the sole independent director of SCI, was the sole member of the SCI Special Committee.

37. The Exchange Ratio, as its name implies, was agreed to based on the relative values of SCI to FITG.

38. As to the business and value of SCI, Dr. Tessori, from his position as a member of the Board of SCI, had extensive information and, upon information and belief, received

additional information from Ross, Storper and Duerk and also from Wax who was involved in the "due diligence" that FITG had conducted on SCI.

39. As to the business and value of FITG, Dr. Tessori, upon information and belief, received information directly or indirectly from Gorga, as well as others including Storper, Ross and Wax.

40. Dr. Tessori did not make any independent verification of the information provided regarding FITG.

41. Dr. Tessori, on behalf of SCI, agreed to the Exchange Ratio on August 23, 2006, in reliance on the accuracy of the information he had been given, as referenced above.

42. Regarding the fairness of the Exchange Ratio, Dr. Tessori also received the opinion of RSM EquiCO Capital Markets, LLC ("RSM"). RSM had been retained by the SCI Special Committee (Dr. Tessori) solely for that specific task.

43. On August 28, 2006, RSM advised Dr. Tessori that the Exchange Ratio was fair to SCI. The following day it submitted a written "Fairness Opinion" to that effect.

44. In arriving at its opinion, RSM considered financial information on SCI and FITG that was publicly available or provided by them, including financial forecasts. It had met with SCI and FITG management "to discuss the business, operations, historical financial results and future prospects" of SCI and FITG. It had compared certain financial and securities data of SCI and FITG and "compared that data with similar data for other publicly-held companies in businesses similar to those of" SCI and FITG. It had "considered the financial terms of certain recent acquisitions of companies in businesses similar to those" of SCI and FITG. It had "performed a discounted cash flow analysis" of SCI and FITG. And it had considered various

other information such as “financial studies, analyses and investigations and financial, economic and market criteria.” (Prospectus, C-1.)

45. However, RSM, like Dr. Tessoni himself, did not perform actual due diligence and thus did not independently verify the information it was provided. The Fairness Opinion made this clear. It stated that “[i]n arriving at our opinion, we have relied upon and assumed, without independent verification, the accuracy and completeness of all financial and other information that was publicly available or furnished to us by” SCI or FITG. Further, it stated that “[w]ith respect to the financial forecasts examined by us, we have assumed that they have been reasonably prepared on bases reflecting the best currently available estimates and judgments of [SCI and FITG’s] management as to the future financial performance of” SCI and FITG. (Prospectus, C-2, emphasis added.)

46. Based on RSM’s Fairness Opinion and Dr. Tessoni’s approval, the SCI Board approved the Merger on August 29, 2006, voting that FITG was worth approximately \$185 million. Defendants Ross, Gorga and Storper voted this way even though they knew, or should have known, that FITG was not worth even close to the consideration being paid.

47. Ironically, while the SCI Board had voted to authorize FITG to conduct due diligence on SCI and FITG had done so for two months (see Prospectus, p.46 – “Throughout April and May 2006. [F]ITG conducted a due diligence review of SCI, and, along with WLR, considered various approaches to a possible combination of SCI and [F]ITG”), SCI did not conduct due diligence on FITG.

48. SCI did not conduct due diligence on FITG (at least not like FITG did on SCI) because WLR and all members of the SCI board other than Tessoni were intimately familiar with the business of FITG and because in reality FITG was acquiring and taking over SCI.

49. In any event, the information supplied by or for FITG and relied upon by Dr. Tessonni and by RSM regarding FITG and the value of FITG's business was inaccurate and deeply flawed. This rendered the Special Committee and RSM's Fairness Opinion essentially a sham.

The Disastrous Financial Condition of FITG

50. The disastrous financial condition of FITG in the second half 2006 did not become known until the Combined Company issued its 10-K on April 24, 2007. That document provided financial information for the first half of 2006 and, separately, for the second half of 2006. In addition, the document included "segment" information on the businesses that had been SCI and FITG as if they were still separate companies.

51. The 10-K segment information showed that FITG had a net income of negative \$3.4 million in the first half of 2006, which amounted to a loss of approximately \$130,000 per week. While not good, that was not news. It had been disclosed publicly in the Prospectus in September 2006.

52. What was new and shocking was the disclosure regarding FITG's losses in the second half of 2006. In that period, FITG's net income was negative \$49 million! That amounted to a loss in the second half of 2006 of \$1.9 million each week, and more than \$8 million each month!

53. This meant that, by the time the Prospectus was issued on September 22, 2006, FITG would already have had losses of \$20 million or more, based on its weekly rate of losses. By the time of the Merger on October 20, the losses would have been in the range of at least \$30 million.

54. Further, the 10-K revealed that FITG's almost \$54 million loss for 2006 (\$4.9 million in the first half of the year, \$49 million in the second half) included a write-down of approximately \$11 million arising from a December 13, 2006, decision by the Board of the Combined Company to discontinue FITG's mattress business. This business had been responsible for approximately 15% of FITG's pre-Merger revenues according to the segment information in the 10-K. Accordingly, \$25 million of the Merger consideration from SCI was attributable to it.

55. Nothing in the 10-K, however, revealed any post-Merger market-changing event that justified a sudden closure of the mattress business. Likewise, nothing had been revealed before the Merger that closure of the mattress business was even under consideration (had it been, Dr. Tessoni and RSM should obviously have taken it into account and set the acceptable consideration from SCI at least \$25 million lower for that reason alone). Indeed, to the contrary, the revenues from that business had, as noted above, been part of the analysis in which FITG's value was determined. Basically, a major line of the FITG business, one for which SCI paid \$25 million, was simply discontinued.

56. Further, a comparison of SCI versus FITG based on the numbers in the 10-K showed that SCI's net income had increased by 11% in the second half of 2006 over what would have been expected based on the first half results (from positive \$1.72 million to positive \$2.1 million). At the same time, FITG's negative results had increased by 900% in the second half of 2006 over what would have been expected from the first half results (from negative \$4.9 million to negative \$49 million).

57. Likewise, the 10-K segment disclosures implied that SCI's shareholder equity or book value rose from the end of the first half of 2006 to the end of the second half of 2006 from \$84.7 million to over \$88 million (an increase of four percent).

58. During the same period, the 10-K segment disclosures implied that the equity associated with FITG's business had dropped from \$123 million at the end of the first half of 2006 to approximately \$80 million at the end of the second half of 2006 (a decrease of almost forty percent).

59. Upon information and belief, the Defendants, particularly Ross, Wax, and Gorga by virtue of their positions at FITG and on its Board, knew or should have known prior to the Merger on October 20, 2006, of the losses and reduction of shareholder equity that FITG was experiencing.

60. Upon information and belief, the Defendants, particularly Ross, Wax, and Gorga by virtue of their positions at FITG and on its Board, knew or should have known prior to the issuance of the Prospectus on September 22, 2006, of the losses and reduction of shareholder equity that FITG was experiencing.

61. Indeed, upon information and belief, the Defendants, particularly Ross, Wax, and Gorga by virtue of their positions at FITG and on its Board, knew or should have known prior to SCI's Board vote in favor of the Merger on August 29, 2006, of the losses and reduction of shareholder equity that FITG was experiencing.

62. In fact, it is simply inconceivable that Defendants, particularly Ross, Wax, and Gorga by virtue of their positions at FITG and on its Board, if they were doing their jobs, were unaware prior to the Merger in October 2006 of the extraordinary losses and reduction of shareholder equity that FITG was experiencing, of the near collapse of FITG's business.

63. It is equally inconceivable that Defendants, particularly Ross, Wax, and Gorga by virtue of their positions at FITG and on its Board, if they were doing their jobs, were unaware prior to the issuance of the Prospectus on September 22, 2006, or prior to the SCI Board vote on August 29, 2006, of the extraordinary losses and reduction of shareholder equity that FITG was experiencing, of the near collapse of FITG's business.

64. In fact, it is hardly necessary to infer knowledge by the Defendants' of FITG's deteriorating situation since the 10-K also revealed that WLR had injected nearly \$31 million in cash into FITG between July 2 and October 20, 2006. This injected cash took the form of unsecured subordinated notes drawing interest from FITG at 4.78%. Basically, this was a loan from WLR to FITG.

65. As of October 2, 2005, there had been no loan. Over the next nine months FITG borrowed \$36.3 million in the form of the unsecured subordinated notes. In the next three and one-half months, FITG borrowed the additional \$31 million. Indeed, since the additional borrowings were not mentioned in the Prospectus dated September 22, 2006, it would appear that FITG borrowed the additional \$31 million in the four weeks between the Prospectus and the Merger.

66. Given this information, the Merger was indefensible on the terms agreed to in August 29, 2006, and probably indefensible generally. It should have been cancelled or dramatically re-negotiated.

67. Defendants could easily have cancelled the Merger (even if they had control of both sides of the deal – control of both SCI and FITG) based on the "MAC Clause" in the Merger agreement. Pursuant to that clause, it was a condition to closing the Merger that

... there shall have been no changes, other than changes contemplated by the merger agreement, in the business, operations, condition (financial or otherwise),

assets or liabilities of [F]ITG and its subsidiaries (regardless of whether such events or changes are inconsistent with the representations and warranties of [F]ITG set forth in the merger agreement) that, individually or in the aggregate, has had or would reasonably be expected to have a material adverse effect with respect to [F]ITG

(Prospectus, p.83. emphasis added.)

68. Notwithstanding the information that they knew or should have known regarding the deterioration of FITG's business, and notwithstanding that non-deterioration was a condition precedent to the Merger, Defendants allowed the Merger (which benefited them enormously) to proceed and be consummated, thereby violating their fiduciary duties to the minority shareholders including Plaintiffs.

69. Indeed, on information and belief, Defendants even allowed an affirmation representation to be made as part of the closing of the Merger on October 20, 2006, to the effect that the condition in the MAC Clause was satisfied. Upon information and belief, Gorga, as CEO of FITG, made that representation.

70. With these losses in income and decrease in shareholder equity, FITG was not worth the \$167 million in consideration that SCI gave for it. Indeed, FITG was probably worth even substantially less than the \$80 million book value implied in the 10-K as of December 31, 2006.

71. Further, in terms of share dilution, the value of FITG did not justify FITG stockholders receiving 65% of the Combined Company, with the existing SCI stockholders being diluted from 100% down to 35% (with a corresponding reduction in voting power). Indeed, the ratio should probably have been at least reversed, with existing SCI stockholders ending up with more than 65% of the Combined Company and FITG stockholders ending up with less than 35% of the Combined Company.

72. In terms of share dilution of the minority stockholders, if the ownership ratio had been reversed, they would have gone from owning 24.4% of SCI to owning close to 16% of the Combined Company instead of owning slightly more than seven percent of the Combined Company. Plaintiff would have gone from owning 1.85% of SCI to owning roughly 1.3% of the Combined Company instead of owning less than one-half of one percent of the Combined Company.

73. As to the Defendants, WLR and Ross, instead of receiving consideration of \$129 million in the Merger, would have received less than half that amount. Gorga, instead of receiving consideration valued at \$1.92 million in the Merger, would have received less than half that amount.

74. Failing to take into account the losses of FITG prior to the Merger on October 20, 2006, resulted in the stockholders of FITG including the Defendants receiving far more than fair value for assets they controlled at the direct expense of the minority stockholders of SCI including Plaintiff who received far less than fair value in return and had their voting rights substantially further diluted.

Further Negative Consequences Of The Merger

75. New Credit Facility. As a result of the Merger and/or the decline FITG during the period surrounding the Merger, the Combined Company was forced to negotiate a new credit facility to replace the former credit facilities of SCI and FITG. The negotiations were consummated on December 29, 2006. The new facility was announced on January 11, 2007.

76. The terms, conditions and credit availability of the new facility were less favorable than the credit arrangements it replaced. Further, the lender required a minimum of \$100 million in commitments of new equity capital from the majority shareholder WLR.

77. On March 2, 2007, WLR and Ross and the Combined Company entered into an agreement that WLR's new capital contribution would be in the form of the purchase of preferred stock. This preferred stock included a cumulative dividend (effectively an interest rate) of 7.5% per year and was convertible into common stock of the Combined Company. The conversion price was set at the book value as of December 31, 2006. WLR also receives an automatic premium of 33% in additional common stock if the conversion takes place in connection with a future Public Offering of company stock, as it logically would (in order for WLR to take advantage of the premium).

78. Aside from having terms that were inappropriate and unfair to SCI's minority stockholders, this additional preferred stock further diluted the SCI minority stockholders including Plaintiff and damaged their economic interests and voting rights.

79. Debt for Equity Swap. As shown in the 10-K, by the time of the Merger WLR had injected a cash of \$68 million into FITG, with \$31 million being injected between July 2 and October 20, 2006, and probably in fact between September 22 and October 20, 2006. (See Paragraphs 64-65 above.) As noted above, the loan from WLR to FITG took the form of unsecured subordinated notes drawing interest at the low rate of 4.78% per year. Considering FITG's actual financial condition, this unsecured, subordinated debt was basically worthless. With the Merger, however, WLR caused the debt to be transferred to the Combined Company and thereby caused it to have value at the expense of the SCI minority shareholders.

80. In any event, on March 8, 2007, WLR and Ross and the Combined Company entered into an agreement that WLR could exchange the \$68 million in unsecured subordinated notes (this enormous debt owed to it by FITG) for preferred stock in the Combined Company. This preferred stock had the same terms as that received by WLR in connection with the new

credit facility: a cumulative dividend of 7.5% per year, convertible into common stock based on book value as of December 31, 2006, and an automatic 33% premium in additional common stock if the conversion takes place in connection with a Public Offering which it logically would.

81. And like the preferred stock issued in connection with the new credit facility, aside from having terms that were inappropriate and unfair to SCI's minority stockholders, this additional preferred stock diluted even further the SCI minority stockholders including Plaintiff and damaged their economic interests and voting rights.

82. Upon information and belief, but for the Merger, this new credit facility and the debt for equity swap, and the enormous additional dilution of the minority stockholders they entailed, would not have taken place.

83. By these and other actions (e.g., purchase of BST from WLR affiliates and the issuance of preferred stock to WLR in connection with that purchase and in connection with \$50 million in working capital provided by WLR to the Combined Company, capital which would not have been needed but for the Merger), Defendants have dramatically and wrongfully diluted the interests of SCI's minority stockholders including Plaintiff and greatly undermined the value of those interests and their voting rights.

84. This reduction in value is reflected in the stock price. On the day the Merger was publicly announced, August 30, 2006, SCI stock was trading at \$14.65 a share. The most recent trade, on April 2, 2008, for the stock of the Combined Company (SCI's name since the Merger) was at \$1.65. This is a reduction in value of nearly 90%. In terms of dollars, the value of the minority shareholder's interest has dropped from nearly \$20 million before the Merger was announced to just over \$2 million now. The value of Plaintiff's interest has dropped from approximately \$1.5 million before the Merger was announced to roughly \$168,000 now.

85. Based on the true condition of FITG and the knowledge of it that Ross, Gorga, Storper and Wax had or should have had, WLR and they should not have proposed the Merger on the terms initially proposed (or allowed it to be proposed on those terms), should not have allowed Dr. Tessoni and RSM to proceed without knowledge of the true condition of FITG, should not have approved the Merger (or allowed it to be approved) on the final terms (even more favorable to WLR and less favorable to the minority stockholders of SCI), and should not have allowed the Merger to close, all of which were clear breaches of their fiduciary duties to the minority stockholders of SCI including Plaintiff.

86. Likewise, Duerk, as President of SCI and the person who agreed to the Merger on behalf of SCI and executed the Merger documents, should not have allowed the Merger to go forward or close without assuring the fairness to the minority stockholders.

87. Upon information and belief, if the true condition of FITG prior to the Merger had been made known to Dr. Tessoni and RSM, they could not and would not, consistent with their duties, have approved of SCI providing consideration then worth \$185 million for FITG or even consideration worth \$167 million, the value as of the date the Merger closed, and would not have recommended that to the SCI Board. (The failure of the Special Committee to have that information rendered it a sham.)

88. In that case, upon information and belief, the Merger would not have occurred. Similarly, neither the New Credit Facility, the Debt for Equity Swap nor the other dilutive actions that have taken place since the Merger would have occurred. If any did occur, it would have had to be on terms substantially more favorable to the minority stockholders including Plaintiff.

CLASS ALLEGATIONS

89. Plaintiff brings this action on his own behalf and seeks to bring it also as a class action. The proposed class ("Class") would be defined as the stockholders of SCI as of the Merger excluding Defendants and persons or entities affiliated with Defendants, and excluding all persons who would otherwise be members but whose damages do not exceed one hundred dollars - i.e., the Class would be defined as all minority stockholders of SCI (non-WLR affiliated stockholders) with damages in excess of \$100.

90. The proposed Class is so numerous that joinder of all members is impracticable. Upon information and belief, there are more than two hundred members of the Class.

91. There are questions of law or fact common to the Class. The common questions include, but are not limited to:

(a) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by proposing the Merger and then allowing it to close notwithstanding the financial condition of FITG;

(b) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by approving the Merger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders down to 35%, or at all;

(c) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by not providing accurate and complete information regarding FITG to Dr. Tesson and RSM or ensuring that such information was provided to them;

(d) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class, to the extent any one of Defendants was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account, or see that it was taken into account, with regard to the Merger;

(e) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by failing to ensure that proper due diligence was conducted on behalf of SCI on FITG;

(f) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by allowing the representation at the Merger closing that MAC Clause condition was satisfied;

(g) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by failing to call off or renegotiate the Merger (or cause it to be called off or renegotiated) because of the financial condition of FITG;

(h) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by allowing the debt previously held by FITG to be transferred to the Combined Company and/or by allowing that debt to be converted into preferred stock;

(i) whether Defendants breached their fiduciary duties (including loyalty and due care) to the minority stockholders who would constitute the Class by allowing or causing the renegotiation the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith;

(j) whether Defendants were self-interested in the transactions at issue (they were) and therefore whether the "entire fairness" standard under Delaware law applies (it does);

(k) whether the Merger and the other actions at issue here satisfied the applicable standard of review ("entire fairness");

(l) whether Defendants aided and abetted others in breaching any of the others' fiduciary duties to the minority stockholders who would constitute the Class;

(m) the amount to which Defendants were unjustly enriched by their actions; and

(n) the amount which to the minority stockholders who would constitute the Class was damaged (on a per share basis).

92. The claims of Plaintiff are typical of the claims of the minority stockholders who would constitute the Class, and Plaintiff does not have any interests adverse to them.

93. Plaintiff is an adequate representative of the minority stockholders who would constitute the Class and has retained competent counsel experienced in litigation of this nature and will fairly and adequately protect the interests of the minority stockholders.

94. The amount in controversy for each minority stockholder who would be part of the Class exceeds one hundred dollars.

FIRST CAUSE OF ACTION
BREACH OF FIDUCIARY DUTY
CONTROLLING SHAREHOLDER

Against WLR and Ross

(Including WLR Recovery Fund II, L.P., WLR Recovery Fund III, L.P., WLR Recovery Associates II, LLC, and WLR Recovery Associates III, LLC)

95. The foregoing allegations are incorporated here by reference.

96. SCI was a Delaware corporation and, accordingly, governed by the Delaware law regarding fiduciary duty.

97. WLR and Ross were the controlling shareholder of SCI and, under Delaware law, had fiduciary duties (including loyalty and due care) to the minority stockholders of SCI including Plaintiff. See Gentile v. Rossette, 906 A.2d 91 (Del. Supr. 2006).

98. Further, WLR and Ross were self-interested in the transactions and acts at issue. Accordingly, the "entire fairness" standard is applicable under Delaware law. Id.

99. WLR and Ross breached their fiduciary duties to the minority stockholders of SCI including Plaintiff in the respects alleged above, and also more specifically as follows:

(a) by proposing the Merger and then allowing it to close notwithstanding the financial condition of FITG;

(b) by approving the Merger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders down to 35%, or at all;

(c) by not providing accurate and complete information regarding FITG to Dr. Tessonni and RSM or ensuring that such information was provided to them;

(d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account, or see that it was taken into account, with regard to the Merger;

(e) by failing to ensure that proper due diligence was conducted on behalf of SCI on FITG;

(f) by allowing the representation at the Merger closing that MAC Clause condition was satisfied;

(g) by failing to call off or renegotiating the Merger (or cause it to be called off or renegotiated) because of the financial condition of FITG;

(i) by allowing the debt previously held by FITG to be transferred to the Combined Company and/or by allowing that debt to be converted into preferred stock;

(j) by allowing or causing the renegotiation the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith; and/or

(k) by otherwise failing to protect the interests of the minority stockholders of SCI.

100. The minority stockholders including Plaintiff were damaged as a proximate result of these breaches of fiduciary duty and are entitled to actual and punitive damages in amounts to be determined by a jury.

SECOND CAUSE OF ACTION
BREACH OF FIDUCIARY DUTY
Directors & Officers
Ross, Gorga, Storper & Duerk

101. The foregoing allegations are incorporated here by reference.

102. Ross, Gorga, Storper and Duerk owed fiduciary duties (including loyalty and due care) to the minority stockholders of SCI including Plaintiff as Directors and Officers of SCI.

103. Ross, Gorga, Storper and Duerk were self-interested in the transactions and acts at issue. Accordingly, the "entire fairness" standard is applicable under Delaware law. Id.

104. Each of these defendants breached their fiduciary duties to the minority stockholders of SCI including Plaintiff in one or more of the respects alleged above and also more specifically as follows:

(a) by proposing the Merger and then allowing it to close notwithstanding the financial condition of FITG;

(b) by approving the Merger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders down to 35%, or at all;

(c) by not providing accurate and complete information regarding FITG to Dr. Tessonì and RSM or ensuring that such information was provided to them;

(d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account, or see that it was taken into account, with regard to the Merger;

(e) by failing to ensure that proper due diligence was conducted on behalf of SCI on FITG;

(f) by making or allowing to be made the representation at the Merger closing that MAC Clause condition was satisfied;

(g) by failing to call off the Merger (or cause it to be called off) because of the financial condition of FITG;

(h) by allowing the debt previously held by FITG to be transferred to the Combined Company and/or by allowing that debt to be converted into preferred stock;

(i) by allowing or causing the renegotiation the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith; and/or

(j) by otherwise failing to protect the interests of the minority stockholders of SCI.

105. The minority stockholders including Plaintiff were damaged as a proximate result of these breaches of fiduciary duty and are entitled to actual and punitive damages in amounts to be determined by a jury.

THIRD CAUSE OF ACTION
AIDING AND ABETTING
BREACH OF FIDUCIARY DUTY
All Defendants

106. The foregoing allegations are incorporated here by reference.

107. The elements under Delaware law for a claim of aiding and abetting a breach of fiduciary duty are: 1) the existence of a fiduciary relationship; 2) a breach of an associated fiduciary duty; 3) knowingly participating in the breach by a Defendant who is not a fiduciary; and 4) damages proximately caused by the breach. Carlson v. Hallinan, 925 A.2d 506 (Del. Ch. 2006); Malpiede v. Townson, 780 A.2d 1075, 1096 (Del. 2001).

108. Defendants each owed fiduciary duties (including loyalty and due care) to the minority stockholders of SCI and Plaintiff as alleged above.

109. Defendants breached those duties as alleged above.

110. Each Defendant, to the extent not found to be a fiduciary itself or himself, knowingly participated in those breaches of fiduciary duties by others persons or entities who were fiduciaries.

111. The minority stockholders including Plaintiff were damaged as a proximate result of these breaches of fiduciary duty and are entitled to actual and punitive damages in amounts to be determined by a jury.

112. WHEREFORE, Plaintiff prays for judgment as follows:

(A) On Count I – Against WLR (including WLR Recovery Fund II, L.P., WLR Recovery Fund III, L.P., WLR Recovery Associates II, LLC, and WLR Recovery Associates III, LLC) for actual and punitive damages;

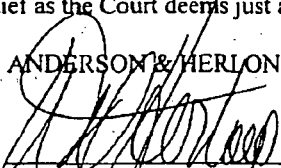
(B) On Count II – Against Ross, Gorga, Storper, and Duerk jointly and severally for actual and punitive damages;

(C) On Count III – Against all Defendants jointly and severally for actual and punitive damages;

(D) For recovery of all costs, attorneys' fees and expenses reasonably incurred in the prosecution of the instant action to the extent permitted by law;

(E) For such other and further relief as the Court deems just and proper.

ANDERSON & HERLONG, LLC


William D. Herlong
SC Bar No. 14283
111 E. North Street [Zip 29601]
P.O. Box 2105
Greenville, SC 29602-2105
(864) 255-9255
william@ahlf.us

Attorneys for Brian Menezes

April 9, 2008

PLAINTIFF HEREBY DEMANDS TRIAL BY JURY

STATE OF SOUTH CAROLINA)

COUNTY OF GREENVILLE)

Brian P. Menezes,)

Plaintiff,)

v.)

WL Ross & Co. LLC, Wilbur L. Ross,)

Jr., Michael J. Gibbons, David H. Storper,)

David L. Wax, Joseph L. Gorga, Stephen)

B. Duerk, WLR Recovery Fund II, L.P.,)

WLR Recovery Fund III, L.P, WLR)

Recovery Associates II LLC, and WLR)

Recovery Associates III LLC,)

Defendants.)

WL Ross & Co. LLC, Wilbur L. Ross,)

Jr., Michael J. Gibbons, David H. Storper,)

David L. Wax, Joseph L. Gorga, WLR)

Recovery Fund II, L.P., WLR Recovery)

Fund III, L.P, WLR Recovery Associates II)

LLC, and WLR Recovery Associates III)

LLC;)

Counterclaimants,)

v.)

Brian P. Menezes,)

Counterclaim Defendant.)

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

FILED-CLERK OF COURT
GREENVILLE CO. S.C.
JUN 6 2008

2008 JUN -6 P 2:24

ANSWER AND DEFENSES OF DEFENDANT STEPHEN B. DUERK

ANSWER AND DEFENSES

Defendant Stephen B. Duerk, by and through his undersigned counsel, answers the Complaint of Brian P. Menezes as follows:

AFFIRMATIVE DEFENSES

FIRST DEFENSE

Defendant answers the Complaint upon his knowledge and otherwise upon information and belief, and responds to the individually numbered paragraphs as follows.

1. Defendant admits that Plaintiff was a minority stockholder in Safety Components International, Inc. ("SCI"). Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 1.

2. Defendant admits that Plaintiff was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 2.

3. Defendant admits that Plaintiff was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 3.

4. Defendant admits that Plaintiff was an officer of SCI from September 1999 through June 2006. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 4.

5. Defendant admits that WL Ross & Co., LLC ("WLR") is an investment firm based in New York City that invests in financially distressed companies in various ways, including leveraged buyouts and restructurings. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 5.

6. Defendant admits that International Textile Group, Inc. ("ITG") merged into SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 6.

7. On information and belief, Defendant admits that, at the time of the merger, affiliates of WLR were the majority stockholders of ITG and held five of the six seats on ITG's Board of Directors. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 7.

8. Defendant admits the allegations in Paragraph 8.

9. Defendant admits that, at the time of the merger, affiliates of WLR were the majority stockholders of SCI and held four of the five seats on SCI's Board of Directors. Defendant further admits that affiliates of WLR purchased their interests in SCI in December 2005. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 9.

10. Defendant admits the allegations in Paragraph 10.

11. The allegations in Paragraph 11 and its subparts are not subject to admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 11.

12. Defendant admits that Wilbur L. Ross was Chairman of the Boards of SCI and ITG before the merger, and is now Chairman of the Board of the merged ITG and SCI ("combined company"). Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 12.

13. Defendant admits that Messrs. Gibbons and Storper were members of SCI's Board of Directors and have remained as members of the Board of Directors of the combined company. Defendant further admits that Mr. Wax is a member of the Board of Directors of the combined company. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 13.

14. Defendant admits that Mr. Gorga is the President and CEO of the combined company and was a member of the Board of SCI before the merger. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 14.

15. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 15.

16. Defendant admits that he is a resident of Greenville County, South Carolina, was President of SCI before the Merger, and was President of the Automotive Safety Group of the combined company. Defendant further admits that he executed the merger agreement at the direction of SCI's Board. Except as expressly admitted, Defendant denies any remaining allegations in Paragraph 16.

17. Defendant admits that WLR Recovery Fund II, L.P. owned shares of SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 17.

18. Defendant admits that WLR Recovery Fund III, L.P. owned shares of SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 18.

19. The allegations in Paragraph 19 and its subparts are not subject to admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 19.

20. Defendant admits that ITG and SCI merged on October 20, 2006. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 20.

21. Defendant admits that Plaintiff purports to paraphrase and quote from the Prospectus and further states that the Prospectus speaks for itself. Except as expressly admitted, Defendant denies any remaining allegations in Paragraph 21.

22. Defendant admits that, at the time of the merger, affiliates of WLR were the majority stockholders of ITG and SCI. Defendant further admits that WLR, via affiliates, held five of the six seats on ITG's Board of Directors, and four of the five seats on SCI's Board of Directors. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 22.

23. Defendant admits that Plaintiff purports to paraphrase and quote from the Prospectus and further states that the Prospectus speaks for itself. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 23.

24. Defendant admits that ITG was merged into SCI and that SCI stockholders did not have appraisal rights. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 24.

25. Defendant admits the allegations in Paragraph 25.

26. Defendant admits the allegations in Paragraph 26.

27. Defendant admits that, after the merger, SCI stockholders owned 35% of the combined company. Defendant further admits that 35% of 24.4% equals 8.54%. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 27.

28. Defendant admits that Plaintiff purports to paraphrase the Prospectus and further states that the Prospectus speaks for itself. Except as expressly admitted, Defendant is without

knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 28.

29. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 29.

30. Defendant admits that affiliates of WLR owned a majority of shares of ITG and received a majority of shares of SCI stock pursuant to the Exchange Ratio. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 30.

31. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 31.

32. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 32.

33. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 33.

34. Defendant admits that the Exchange Ratio set the conversion ratio for ITG stock into SCI stock. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 34.

35. Defendant admits that Plaintiff purports to paraphrase and quote from the Prospectus, and further states that the Prospectus speaks for itself. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 35.

36. Defendant admits the allegations in Paragraph 36.

37. Defendant admits the allegations in Paragraph 37.

38. On information and belief, Defendant admits that, as a Board member of SCI, Dr. Tessonni likely had access to information concerning the business and value of SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 38.

39. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 39.

40. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 40.

41. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 41.

42. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 42.

43. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 43.

44. Defendant admits that Plaintiff purports to paraphrase and quote from RSM EquiCo Capital Markets, LLC's written opinion ("Fairness Opinion") to Dr. Tessonni, and further states that the Fairness Opinion speaks for itself. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 44.

45. Defendant admits that Plaintiff purports to paraphrase and quote from the Fairness Opinion, and further states that the Fairness Opinion speaks for itself. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 45.

46. Defendant admits that SCI's Board of Directors approved the merger on August 29, 2006. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 46.

47. Defendant admits that Plaintiff purports to paraphrase and quote from the Prospectus, and further states that the Prospectus speaks for itself. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 47.

48. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 48.

49. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 49.

50. Defendant admits that the combined company's 10-K provided financial information for the combined company for 2006, and included segment information for the combined company. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 50.

51. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 51.

52. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 52.

53. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 53.

54. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 54.

55. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 55.

56. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 56.

57. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 57.

58. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 58.

59. Defendant denies he was a Board member of ITG, SCI or the combined company, and further denies that he had knowledge regarding the alleged financial condition of ITG. Except as expressly denied, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 59.

60. Defendant denies he was a Board member of ITG, SCI or the combined company, and further denies that he had knowledge regarding the alleged financial condition of ITG. Except as expressly denied, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 60.

61. Defendant denies he was a Board member of ITG, SCI or the combined company, and further denies that he had knowledge regarding the alleged financial condition of ITG. Except as expressly denied, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 61.

62. Defendant denies he was a Board member of ITG, SCI or the combined company, and further denies that he had knowledge regarding the alleged financial condition of ITG.

Except as expressly denied, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 62.

63. Defendant denies he was a Board member of ITG, SCI or the combined company, and further denies that he had knowledge regarding the alleged financial condition of ITG. Except as expressly denied, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 63.

64. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 64.

65. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 65.

66. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 66.

67. Defendant admits that Plaintiff purports to paraphrase and quote from the Prospectus, and further states that the Prospectus speaks for itself. Defendant denies that he was able to cancel the merger. Except as expressly admitted and denied, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 67.

68. Defendant admits that he was a minority stockholder in SCI. Defendant denies that he was able to cancel the merger or that he had the alleged information about ITG's business. Except as expressly admitted and denied, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 68.

69. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 69.

70. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 70.

71. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 71.

72. Defendant admits that 65% of 24.4% equals 15.86%. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 72.

73. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 73.

74. Defendant admits that he was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 74.

75. Defendant admits that the combined company negotiated a new credit facility. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 75.

76. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 76.

77. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 77.

78. Defendant admits that he was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 78.

79. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 79.

80. Defendant admits that WLR was issued preferred stock in the combined company. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 80.

81. Defendant admits that he was a minority stockholder in SCI and that the issuance of preferred stock in the combined company, like any additional equity, can have a dilutive effect. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 81.

82. Defendant admits that he was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 82.

83. Defendant admits that he was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 83.

84. Defendant admits that he was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 84.

85. Defendant admits that he was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 85.

86. Defendant admits that he is a minority stockholder and executed certain merger documents at the direction of SCI's Board. Except as expressly admitted, Defendant denies any remaining allegations in Paragraph 86.

87. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 87.

88. Defendant admits that he was a minority stockholder in SCI. Except as expressly admitted, Defendant is without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 88.

89. Defendant states that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 89.

90. Defendant denies the allegations in Paragraph 90.

91. Defendant states that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 91 and all of its subparts.

92. Defendant denies the allegations in Paragraph 92.

93. Defendant denies the allegations in Paragraph 93.

94. Defendant denies the allegations in Paragraph 94.

95. Defendant incorporates herein by reference his responses to paragraphs 1 through 94 of the Complaint as if fully set forth herein.

96. Defendant admits that SCI was a Delaware corporation. Except as expressly admitted, any remaining allegations in Paragraph 96 state a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 96.

97. Defendant admits that affiliates of WLR were majority stockholders of SCI and that Delaware law applies to this lawsuit. Except as expressly admitted, any remaining allegations in Paragraph 97 state a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 97.

98. Defendant is without knowledge or information to form a belief as to the truth of the allegations in Paragraph 98.

99. Defendant denies the allegations in Paragraph 99 and all of its subparts.

100. Defendant denies the allegations in Paragraph 100.

101. Defendant incorporates herein by reference his responses to paragraphs 1 through 100 of the Complaint as if fully set forth herein.

102. Defendant states that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 102.

103. Defendant states that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 103.

104. Defendant denies the allegations in Paragraph 104 and all of its subparts.

105. Defendant denies the allegations in Paragraph 105.

106. Defendant incorporates herein by reference his responses to paragraphs 1 through 105 of the Complaint as if fully set forth herein.

107. Defendant states that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 107.

108. Defendant states that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendant denies the allegations in Paragraph 108.

109. Defendant denies the allegations in Paragraph 109.

110. Defendant denies the allegations in Paragraph 110.

111. Defendant denies the allegations in Paragraph 111.

112. Defendant denies the allegations in Paragraph 112.

113. Defendant denies any and all allegations of the Complaint not expressly admitted herein and denies that Plaintiff is entitled to any form of relief and that he take nothing by way of this lawsuit.

SECOND DEFENSE

114. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

115. The Complaint fails to state sufficient facts to constitute a claim or cause of action.

THIRD DEFENSE

116. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

117. Plaintiff's claims are barred in whole or in part because they were released by Plaintiff on September 28, 2006. All of the claims Plaintiff asserts in this lawsuit arose or accrued before Plaintiff signed the release. Attached hereto as Exhibit A is a true and correct copy of the Confidential Settlement Agreement and Release ("Settlement Agreement") wherein Plaintiff released all asserted claims against the named Defendants.

FOURTH DEFENSE

118. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

119. Plaintiff's claims are barred in whole or in part because there has been an accord and satisfaction. As set forth in the Settlement Agreement, Plaintiff disputed, among other things, the amount owed to him under his employment agreement. In satisfaction of that dispute, including any of Plaintiff's disputes that were based upon or as an owner of any stock or interest, Plaintiff accepted and cashed several payments made in January, March and August 2007.

FIFTH DEFENSE

120. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

121. Plaintiff's claims are barred in whole or in part by the doctrines of estoppel, waiver, acquiescence, and/or ratification. Plaintiff was aware of the claims that he asserts in his lawsuit and, on information and belief, either voted for or acquiesced to the merger at issue in his lawsuit.

SIXTH DEFENSE

122. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

123. Plaintiff's claims are barred in whole or in part by the business judgment rule. Disinterested and independent special committees of SCI and ITG, acting in good faith and using due care and relying on independent advisors and fairness opinions, approved the merger as a valid business decision. The Boards of the merging companies relied on the special committees' recommendation.

SEVENTH DEFENSE

124. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

125. To the extent that Plaintiff's claims are derivative in nature, they are barred because Plaintiff failed to make a demand on the Board of Directors of the combined company and failed to meet the other procedural and substantive requirements for a derivative action as specified in Rule 23(b)(1) of the South Carolina Rules of Civil Procedure..

EIGHTH DEFENSE

126. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

127. Plaintiff's claims are barred in whole or in part because he lacks standing and is an inadequate representative for the purported class because, among other reasons, he released his claims against the Defendants.

NINTH DEFENSE

128. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

129. Plaintiff's claims are barred in whole or in part because the Defendants acted in good faith, relied in good faith on the recommendation of the special committees approving the merger, and did no unlawful act or thing directly or indirectly: The disinterested and independent special committees of SCI and ITG each relied in good faith on independent advisors and fairness opinions when recommending and approving the merger and related transactions.

TENTH DEFENSE

130. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

131. Plaintiff's claims are barred in whole or in part because Plaintiff cannot show causation between the conduct of Defendant and the damages alleged. Any alleged reduction in stock price was due to events and circumstances unrelated to the allegations sets forth in the Complaint.

ELEVENTH DEFENSE

132. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

133. Plaintiff's claims are barred in whole or in part under the doctrine of laches. Plaintiff's claims arose and accrued no later than when the merger was agreed upon, and Plaintiff should have brought his lawsuit at that time.

TWELFTH DEFENSE

134. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

135. Plaintiff's aiding and abetting claims are barred in whole or in part to the extent that Defendant is a fiduciary or did not knowingly participate in any alleged breach.

THIRTEENTH DEFENSE

136. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

137. Plaintiff's claims are barred in whole or in part because involvement with the merger agreement was limited to a ministerial act pursuant to the requirements of 8 Del. C. §

251(b) and § 103. Pursuant to these code sections, Defendant was directed by SCI's Board to execute certain merger documents because he was an officer of a merging company.

FOURTEENTH DEFENSE

138. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

139. Plaintiff's claims are barred in whole or in part because they were claims related to those asserted by Plaintiff in his earlier lawsuit captioned *Menezes v. SCI, et. al.* (C.A. No.: 2006-CP-23-4236), that were expressly dismissed on September 29, 2006, "with prejudice and are hereby res judicata."

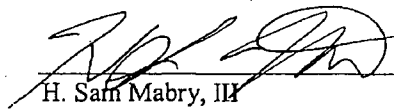
FIFTEENTH DEFENSE

140. Defendant repeats the relevant and consistent allegations of his previous Defenses as if fully set forth herein.

141. Defendant hereby gives notice that he intends to rely upon such other and further defenses as may become available or apparent during pretrial proceedings in this action and hereby reserves all rights to amend this Answer and to assert all such defenses.

Dated: June 6, 2008

Respectfully submitted,



H. Sam Mabry, III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square - 11th Floor
75 Beattie Place
Greenville, South Carolina 29601
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

OF COUNSEL:

George T. Manning
JONES DAY
2727 N. Harwood Street
Dallas, Texas 75201-1515
Telephone: (214) 220-3939
Facsimile: (214) 969-5100

Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Suite 800
Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

Counsel for Defendant Stephen B. Duerk

STATE OF SOUTH CAROLINA)

COUNTY OF GREENVILLE)

Brian P. Menezes,)

Plaintiff,)

v.)

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, Stephen)
B. Duerk, WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P, WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC,)

Defendants.)

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

FILED CLERK OF COURT
GREENVILLE CO. S.C.
BY: JAMES V. WARD

2008 JUN -6 P 2:24

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, WLR)
Recovery Fund II, L.P., WLR Recovery)
Fund III, L.P, WLR Recovery Associates II)
LLC, and WLR Recovery Associates III)
LLC;)

Counterclaimants,)

v.)

Brian P. Menezes,)

Counterclaim Defendant.)

**ANSWER, DEFENSES AND COUNTERCLAIM OF WL ROSS & CO. LLC;
WILBUR L. ROSS, JR.; MICHAEL J. GIBBONS; DAVID H. STORPER; DAVID L.
WAX; JOSEPH L. GORGA; WLR RECOVERY FUND II, L.P.; WLR RECOVERY
FUND III, L.P.; WLR RECOVERY ASSOCIATES II LLC; AND WLR RECOVERY
ASSOCIATES III LLC.**

ANSWER AND DEFENSES

Defendants WL Ross & Co. LLC; Wilbur L. Ross, Jr.; Michael J. Gibbons; David H.
Storper; David L. Wax; Joseph L. Gorga; WLR Recovery Fund II, L.P.; WLR Recovery Fund

III, L.P.; WLR Recovery Associates II LLC; and WLR Recovery Associates III LLC, by and through their undersigned counsel, answer the Complaint of Brian P. Menezes as follows.

AFFIRMATIVE DEFENSES

FIRST DEFENSE

Defendants answer the Complaint upon their knowledge and otherwise upon information and belief, and respond to the individually numbered paragraphs as follows.

1. Defendants deny the allegations in Paragraph 1.
2. Defendants deny the allegations in Paragraph 2.
3. Defendants deny the allegations in Paragraph 3.
4. Defendants admit that Plaintiff was an officer of Safety Components International, Inc. ("SCI") from September 1999 through June 2006. Defendants further admit that on August 29, 2006, the day before the merger between SCI and International Textile Group, Inc. ("ITG") was announced, the asked for price for SCI's stock was \$14.65 a share on the Over The Counter Bulletin Board ("OTCBB") and on that day trading volume was minimal. Defendants further admit that on April 2, 2008, the asked for price for SCI's stock was \$1.65 a share on the OTCBB and on that day trading volume was minimal. Except as expressly admitted, Defendants are without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 4.

5. Defendants admit that WL Ross & Co., LLC ("WLR") is an investment firm based in New York City that invests in financially distressed companies in various ways, including leveraged buyouts and restructurings. Defendants further admit that Messrs. Ross, Storper, Gibbons and Wax are employees or officers of WLR. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 5.

6. Defendants deny that ITG “took over” SCI, whatever Plaintiff means by that phrase. Except as expressly denied, Defendants admit the remaining allegations in Paragraph 6.

7. Defendants admit that, at the time of the merger, affiliates of WLR were the majority stockholders of ITG and owned 14,310,497 shares of ITG constituting approximately 85.4% ownership and held five of the six seats on ITG’s Board of Directors. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 7.

8. Defendants admit the allegations in Paragraph 8.

9. Defendants admit that, at the time of the merger, affiliates of WLR were the majority stockholders of SCI and owned 4,162,394 shares of SCI constituting approximately 75.6% ownership and held four of the five seats on SCI’s Board of Directors. Defendants further admit that affiliates of WLR purchased their interests in SCI in December 2005. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 9.

10. Defendants admit the allegations in Paragraph 10.

11. The allegations in Paragraph 11 and its subparts are not subject to admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 11.

12. Defendants deny that Mr. Ross is a resident of New York. Except as expressly denied, Defendants admit any remaining allegations in Paragraph 12.

13. Defendants admit that Messrs. Gibbons and Storper are residents of New York, Mr. Wax is a resident of Connecticut, and all are employees or officers of WLR. Defendants further admit that Messrs. Gibbons and Storper were members of SCI’s Board of Directors and have remained as members of the Board of Directors since SCI and ITG merged (the “combined company” or “NITG”). Defendants further admit that Mr. Wax was a member of the Board of

Directors of ITG and is now a member of the Board of Directors for the combined company.

Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 13.

14. Defendants admit the allegations in Paragraph 14.

15. Defendants admit that Mr. Gorga's compensation from ITG in 2005 included \$600,000 in base salary, \$297,301 in bonus, and \$511,559 for taxes incurred upon the vesting of restricted stock in 2005. Defendants further admit that, in 2005, he was issued restricted stock valued at \$1,423,800 and options valued at \$1,017,000. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 15.

16. Defendants admit that Mr. Duerk is a resident of Greenville County, South Carolina, was President of SCI before the Merger, and was President of the Automotive Safety Group of the combined company. Defendants further admit that Mr. Duerk executed the Merger agreement at the direction of SCI's Board of Directors. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 16.

17. Defendants admit that WLR Recovery Fund II, L.P. owned 241,419 shares of SCI and that its general partner is WLR Recovery Associates II LLC and its investment advisor is WLR. Defendants further admit that Mr. Ross was and is general manager of WLR Recovery Associates II LLC, which had voting power over the shares owned by WLR Recovery Fund II, L.P. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 17.

18. Defendants admit that WLR Recovery Fund III, L.P. owned 3,920,975 shares of SCI and that its general partner is WLR Recovery Associates III LLC and its investment advisor is WLR. Defendants further admit that Mr. Ross was and is general manager of WLR Recovery Associates III LLC, which had voting power over the shares owned by WLR Recovery Fund III, L.P. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 18.

19. The allegations in Paragraph 19 and its subparts are not subject to admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 19.

20. Defendants admit that WLR, ITG, and SCI explored the combination of ITG and SCI in early 2006, and that ITG and SCI were ultimately combined on October 20, 2006. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 20.

21. Defendants admit that Plaintiff purports to paraphrase and quote from the Joint Proxy Statement/Prospectus of SCI and ITG, dated September 22, 2006 ("Prospectus") and further state that the Prospectus speaks for itself. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 21.

22. Defendants admit that, at the time of the merger, affiliates of WLR were the majority stockholders of ITG and SCI, owning 85.4% and 75.6% of each company's respective stock. Defendants further admit that WLR, via affiliates, held five of the six seats on ITG's Board of Directors, and four of the five seats on SCI's Board of Directors. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 22.

23. Defendants admit that Plaintiff purports to paraphrase and quote from the Prospectus and further state that the Prospectus speaks for itself. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 23.

24. Defendants admit that ITG was combined with SCI, that ITG became a wholly-owned subsidiary of SCI, and that SCI stockholders did not have appraisal rights. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 24.

25. Defendants admit the allegations in Paragraph 25.

26. Defendants admit the allegations in Paragraph 26.

27. Defendants admit that, after the merger, SCI stockholders owned 35% of the combined company. Defendants further admit that 35% of 24.4% equals 8.54% and that 34% of 1.85% equals 0.6475%. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 27.

28. Defendants admit that Plaintiff purports to paraphrase the Prospectus and further state that the Prospectus speaks for itself. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 28.

29. Defendants admit that the asked for price of SCI's stock was \$14.65 a share on the OTCBB on August 29, 2006, and on that day trading volume was minimal. Defendants further admit that the merger was announced on August 30, 2006. Defendants further admit that, on September 22, 2006, the asked for price of SCI's stock was \$14.30 a share on the OTCBB, and that, on October 20, 2006, the asked for price of SCI's stock was \$13.25 a share on the OTCBB, and that on those days trading volume was minimal. Defendants further admit that 12,617,438 times 14.65 equals 184,845,466.70. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 29.

30. Defendants admit that affiliates of WLR owned 14,310,497 shares of ITG (85.4%) and received 9,709,273 shares of SCI stock pursuant to the Exchange Ratio. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 30.

31. Defendants admit that Mr. Gorga owned 213,750 shares of ITG and received 145,023 shares of SCI stock pursuant to the Exchange Ratio. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 31.

32. Defendants deny the allegations in Paragraph 32.

33. Defendants deny the allegations in Paragraph 33.

34. Defendants admit that the Exchange Ratio set the conversion ratio for ITG stock into SCI stock. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 34.

35. Defendants admit that Plaintiff purports to paraphrase and quote from the Prospectus, and further state that the Prospectus speaks for itself. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 35.

36. Defendants admit the allegations in Paragraph 36.

37. Defendants admit the allegations in Paragraph 37.

38. Defendants admit that Dr. Tessori, in his role as a member of the special committee, had access to information concerning the business and value of SCI, and that advisors to Dr. Tessori conducted legal and financial due diligence. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 38.

39. Defendants admit that Dr. Tessori, in his role as member of the independent SCI Special Committee, had access to information concerning the business and value of ITG as part of the legal and financial due diligence process. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 39.

40. Defendants are without knowledge or information to form a belief as to the truth of the allegations in Paragraph 40.

41. Defendants admit that, after consulting with his legal and financial advisors and receiving RSM EquiCo Capital Markets, LLC's ("RSM") verbal opinion, Dr. Tessori, in his role as member of the independent SCI Special Committee, agreed to the Exchange Ratio. Except as expressly admitted, Defendants are without knowledge or information to form a belief as to the truth of any remaining allegations in Paragraph 41.

42. Defendants admit the allegations in Paragraph 42.
43. Defendants admit the allegations in Paragraph 43.
44. Defendants admit that Plaintiff purports to paraphrase and quote from the RSM Fairness Opinion to Dr. Tessori, and further state that the Fairness Opinion speaks for itself. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 44.
45. Defendants admit that Plaintiff purports to paraphrase and quote from the RSM Fairness Opinion, and further state that the Fairness Opinion speaks for itself. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 45.
46. Defendants admit that SCI's Board of Directors approved the merger on August 29, 2006 in reliance on the recommendation of its special committee. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 46.
47. Defendants admit that Plaintiff purports to paraphrase and quote from the Prospectus, and further state that the Prospectus speaks for itself. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 47.
48. Defendants deny the allegations in Paragraph 48.
49. Defendants deny the allegations in Paragraph 49.
50. Defendants admit that the combined company's 10-K provided financial information for the combined company for 2006, and included segment information for the combined company. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 50.
51. Defendants admit that ITG had a net income of negative \$3.4 million in the first half of 2006, which was disclosed in the Prospectus. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 51.

52. Defendants deny the allegations in Paragraph 52.

53. Defendants deny the allegations in Paragraph 53.

54. Defendants admit that the combined company recognized approximately \$11 million in restructuring and impairment charges in 2006. Defendants further admit that the combined company sold certain assets that were part of its discontinued mattress product line, and that sale was authorized by the combined company's Board of Directors. Defendants further admit that the interior furnishings segment had approximately \$4 million in losses from October 4, 2004 to January 1, 2006. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 54.

55. Defendants admit that, in 2006, the combined company entered into an agreement that, among other things, transitioned all future production of U.S. produced mattress fabrics to a leased facility, and that the combined company received proceeds from the related sale of plant assets of \$3.9 million. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 55.

56. Defendants deny the allegations in Paragraph 56.

57. Defendants deny the allegations in Paragraph 57.

58. Defendants deny the allegations in Paragraph 58.

59. Defendants deny the allegations in Paragraph 59.

60. Defendants deny the allegations in Paragraph 60.

61. Defendants deny the allegations in Paragraph 61.

62. Defendants deny the allegations in Paragraph 62.

63. Defendants deny the allegations in Paragraph 63.

64. Defendants admit that the combined company had borrowings of approximately \$66 million from WLR Recovery Fund II, L.P. pursuant to five unsecured subordinated demand notes bearing interest at 4.78%. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 64.

65. Defendants admit that ITG had borrowings of approximately \$36 million from WLR Recovery Fund II, L.P. in May and June 2006. Defendants further admit that ITG borrowed \$20 million from WLR Recovery Fund II, L.P. in September 2006. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 65.

66. Defendants deny the allegations in Paragraph 66.

67. Defendants admit that Plaintiff purports to paraphrase and quote from the Prospectus, and further state that the Prospectus speaks for itself. Defendants further admit that the Merger Agreement contained representations from ITG and SCI that there was an absence of certain changes or events. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 67.

68. Defendants deny the allegations in Paragraph 68.

69. Defendants admit that, at the time of closing, Gary Smith executed a "bring down" certificate on behalf of ITG. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 69.

70. Defendants deny the allegations in Paragraph 70.

71. Defendants deny the allegations in Paragraph 71.

72. Defendants admit that 65% of 24.4% equals 15.86% and that 65% of 1.85% equals 1.2025%. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 72.

73. Defendants deny the allegations in Paragraph 73.

74. Defendants deny the allegations in Paragraph 74.

75. Defendants admit that the combined company negotiated a new credit facility that was completed on December 29, 2006. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 75.

76. Defendants deny the allegations in Paragraph 76.

77. Defendants admit that, on March 2, 2007, the combined company and WLR agreed that a capital contribution would be in the form of preferred stock. Defendants further admit that the preferred stock in the combined company allowed for a cumulative dividend of 7.5% per year, was convertible into common stock of the combined company based on book value as of December 31, 2006, and established a premium of additional common stock if the conversion took place in connection with a future public offering. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 77.

78. Defendants deny the allegations in Paragraph 78.

79. Defendants admit that the combined company had borrowed approximately \$66 million from WLR Recovery Fund II, L.P. pursuant to five unsecured subordinated demand notes bearing interest at 4.78%. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 79.

80. Defendants admit that the combined company and affiliates of WLR agreed to exchange the \$68 million in debt for preferred stock in the combined company. Defendants further admit that the preferred stock in the combined company allowed for a cumulative dividend of 7.5% per year, was convertible into common stock of the combined company based on book value as of December 31, 2006, and established a premium of additional common stock

if the conversion took place in connection with a future public offering. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 80.

81. Defendants admit that the issuing of preferred stock in the combined company, like any additional equity, can have a dilutive effect. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 81.

82. Defendants admit that the combined company, but for the merger, would not have entered into the new credit facility or engaged in the debt for equity swap. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 82.

83. Defendants admit that the combined company purchased BST US Holdings, Inc. in April 2007, issued preferred stock to affiliates of WLR in connection therewith, and engaged in various financial arrangements. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 83.

84. Defendants admit that on August 30, 2006, the merger was announced and the asked for price of SCI's stock was \$14.65 a share on the OTCBB, and on that day trading volume was minimal. Defendants further admit that on April 2, 2008, the asked for price of SCI's stock was \$1.65 a share on the OTCBB and on that day trading volume was minimal. Except as expressly admitted and stated, Defendants deny any remaining allegations in Paragraph 84.

85. Defendants deny the allegations in Paragraph 85.

86. Defendants admit that Mr. Duerk executed certain merger documents at the direction of SCI's Board of Directors. Except as expressly admitted, Defendants deny any remaining allegations in Paragraph 86.

87. Defendants deny the allegations in Paragraph 87.

88. Defendants deny the allegations in Paragraph 88.

89. Defendants state that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 89.

90. Defendants deny the allegations in Paragraph 90.

91. Defendants state that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 91 and all of its subparts.

92. Defendants deny the allegations in Paragraph 92.

93. Defendants deny the allegations in Paragraph 93.

94. Defendants deny the allegations in Paragraph 94.

95. Defendants incorporate herein by reference their responses to paragraphs 1 through 94 of the Complaint as if fully set forth herein.

96. Defendants admit that SCI was a Delaware corporation. Except as expressly admitted, any remaining allegations in Paragraph 96 state a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 96.

97. Defendants admit that affiliates of WLR were majority stockholders of SCI and that Delaware law applies to this lawsuit. Except as expressly admitted, any remaining allegations in Paragraph 97 state a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 97.

98. Defendants deny the allegations in Paragraph 98.

99. Defendants deny the allegations in Paragraph 99 and all of its subparts.

100. Defendants deny the allegations in Paragraph 100.

101. Defendants incorporate herein by reference their responses to paragraphs 1 through 100 of the Complaint as if fully set forth herein.

102. Defendants state that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 102.

103. Defendants state that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 103.

104. Defendants deny the allegations in Paragraph 104 and all of its subparts.

105. Defendants deny the allegations in Paragraph 105.

106. Defendants incorporate herein by reference their responses to paragraphs 1 through 105 of the Complaint as if fully set forth herein.

107. Defendants state that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 107.

108. Defendants state that this is a legal conclusion that is not subject to an admission or denial. To the extent a response is possible, Defendants deny the allegations in Paragraph 108.

109. Defendants deny the allegations in Paragraph 109.

110. Defendants deny the allegations in Paragraph 110.

111. Defendants deny the allegations in Paragraph 111.

112. Defendants deny the allegations in Paragraph 112.

113. Defendants deny any and all allegations of the Complaint not expressly admitted herein and deny that Plaintiff is entitled to any form of relief and that he take nothing by way of this lawsuit.

SECOND DEFENSE

114. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

115. The Complaint fails to state sufficient facts to constitute a claim or cause of action.

THIRD DEFENSE

116. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

117. Plaintiff's claims are barred in whole or in part because they were released by Plaintiff on September 28, 2006. All of the claims Plaintiff asserts in this lawsuit arose or accrued before Plaintiff signed the release. Attached hereto as Exhibit A is a true and correct copy of the Confidential Settlement Agreement and Release ("Settlement Agreement") wherein Plaintiff released all asserted claims against the named Defendants.

FOURTH DEFENSE

118. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

119. Plaintiff's claims are barred in whole or in part because there has been an accord and satisfaction. As set forth in the Settlement Agreement, Plaintiff disputed, among other things, the amount owed to him under his employment agreement. In satisfaction of that dispute,

including any of Plaintiff's disputes that were based upon or as an owner of any stock or interest, Plaintiff accepted and cashed several payments made in January, March and August 2007.

FIFTH DEFENSE

120. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

121. Plaintiff's claims are barred in whole or in part by the doctrines of estoppel, waiver, acquiescence, and/or ratification. Plaintiff was aware of the claims that he asserts in his lawsuit and, on information and belief, either voted for or acquiesced to the merger at issue in his lawsuit.

SIXTH DEFENSE

122. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

123. Plaintiff's claims are barred in whole or in part by the business judgment rule. Disinterested and independent special committees of SCI and ITG, acting in good faith and using due care and relying on independent advisors and fairness opinions, approved the merger as a valid business decision. The Boards of Directors of the merging companies relied in good faith on the special committees' recommendation.

SEVENTH DEFENSE

124. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

125. To the extent that Plaintiff's claims are derivative in nature, they are barred because Plaintiff failed to make a demand on the Board of Directors of the combined company

and failed to meet the other procedural and substantive requirements for a derivative action as specified in Rule 23(b)(1) of the South Carolina Rules of Civil Procedure.

EIGHTH DEFENSE

126. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

127. Plaintiff's claims are barred in whole or in part by Article VII of the Amended and Restated Certificate of Incorporation of International Textile Group, Inc. (f/k/a Safety Components International, Inc.) and by principles of exculpation under Delaware law. More specifically, Article VII provides that "no Director of the Corporation will be personally liable to the Corporation or its stockholders for or with respect to any acts or omissions in the performance of his or her duties as a Director of the Corporation."

NINTH DEFENSE

128. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

129. Plaintiff's claims are barred in whole or in part because he lacks standing and is an inadequate representative for the purported class because, among other reasons, he released his claims against the Defendants.

TENTH DEFENSE

130. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

131. Plaintiff's claims are barred in whole or in part because the Defendants acted in good faith, relied in good faith on the recommendation of the special committees approving the merger, and did no unlawful act or thing directly or indirectly. The disinterested and

independent special committees of SCI and ITG relied in good faith on independent advisors and fairness opinions when recommending and approving the merger and related transactions.

ELEVENTH DEFENSE

132. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

133. Plaintiff's claims are barred in whole or in part because Plaintiff cannot show causation between the conduct of any of the Defendants and the damages alleged. Any alleged reduction in stock price was due to events and circumstances unrelated to the allegations set forth in the Complaint.

TWELFTH DEFENSE

134. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

135. Plaintiff's claims are barred in whole or in part under the doctrine of laches. Plaintiff's claims arose and accrued no later than when the merger was agreed upon, and Plaintiff should have brought his lawsuit at that time.

THIRTEENTH DEFENSE

136. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

137. Plaintiff's aiding and abetting claims are barred in whole or in part to the extent that Defendants are fiduciaries or did not knowingly participate in any alleged breach.

FOURTEENTH DEFENSE

138. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

139. Plaintiff's claims are barred in whole or in part because they were claims related to those asserted by Plaintiff in his earlier lawsuit captioned *Menezes v. SCI, et. al.* (C.A. No.: 2006-CP-23-4236), that were expressly dismissed on September 29, 2006, "with prejudice and are hereby res judicata."

FIFTEENTH DEFENSE

140. Defendants repeat the relevant and consistent allegations of their previous Defenses and their Counterclaim as if fully set forth herein.

141. Defendants hereby give notice that they intend to rely upon such other and further defenses as may become available or apparent during pretrial proceedings in this action and hereby reserve all rights to amend this Answer and to assert all such defenses.

COUNTERCLAIMS AGAINST PLAINTIFF

142. Brian Menezes is a disgruntled former employee who is suing released parties on released claims in breach of his agreement with Counterclaimants.

143. In mid-2006, Menezes was removed as interim Chief Executive Officer ("CEO") of Safety Components International, Inc. ("SCI"). At that time, Menezes, knowing that a merger of SCI and International Textile Group, Inc. ("ITG") was in advanced stages, demanded to be paid a change of control bonus based on the contemplated merger. SCI refused to pay this bonus in reliance on the terms of Menezes' employment agreement, and Menezes sued SCI in July 2006.

144. From July to mid-September 2006, while Menezes' employment lawsuit was pending, SCI and ITG negotiated and agreed to the merger, publicly disclosed its terms, and filed the merger prospectus with the SEC. On September 28, 2006, Menezes signed a settlement agreement where he broadly released all known and unknown claims against SCI and related parties, including the ones asserted in his Complaint.

145. Menezes' lawsuit against the Counterclaimants is based on claims that arose or accrued before September 28, 2006 and were expressly released in the settlement agreement. Menezes is in breach of that agreement and that breach has harmed and continues to harm Counterclaimants.

PARTIES

146. On information and belief, Plaintiff and Counterclaim Defendant Brian P. Menezes is an individual domiciled in the State of South Carolina.

147. Counterclaimants WL Ross & Co. LLC ("WLR"), Wilbur L. Ross, Michael J. Gibbons, David H. Storper, David L. Wax, Joseph L. Gorga, WLR Recovery Fund II, L.P. ("Fund II"), WLR Recovery Fund III, L.P. ("Fund III"), WLR Recovery Associates II LLC ("Associates II"), and WLR Recovery Associates III LLC ("Associates III") are residents of states other than the State of South Carolina.

FACTS

148. Historically, SCI's principal business was supplying automotive airbag fabric and cushions for automotive airbag modules.

149. In September 1999, Menezes was promoted to Chief Financial Officer ("CFO") of SCI after working in senior management with the company. In May 2001, he signed an employment agreement with SCI that contained a "change of control" provision that provided for a one-time only payment that was more than double his six figure salary upon the occurrence of certain events, including when stockholders approved a business combination or where certain Board of Directors members failed to maintain majority control.

150. Menezes' change of control provision was intended to correct the pricing difference of certain stock options given to him by SCI. More particularly, in the event of a

change of control, other SCI employees' strike price for stock options was reduced to one cent, whereas Menezes' stock option price remained at \$8.75.

151. As such, if Menezes had exercised these options and sold his SCI stock after a change in control, he would have been paid \$8.74 less per share than other SCI employees whose strike price reduced to \$0.01 after a change in control.

152. To offset this different treatment upon a change in control, SCI agreed to pay Menezes a \$393,300 upon the occurrence of a change of control event. The amount of this change of control "bonus" was calculated by taking the difference between Menezes' strike price and other employees' strike prices (\$8.75 – \$0.01) and multiplying it by the number of shares at issue (45,000). Unlike the other SCI employees, who had to sell shares to be paid, Menezes received this bonus without having to sell any shares in SCI.

153. In September 2003, Zapata Corporation acquired 53.7% of SCI, which triggered Menezes' change of control bonus provision.

154. Shortly thereafter, SCI paid Menezes a \$393,300 change of control bonus. Because this bonus was based on the disparity in share prices, Menezes' employment agreement limited it to "a one-time bonus [to be paid] . . . at the time the change of control [was] consummated." (2001 Menezes Employment Agreement; emphasis added.)

155. Although the employment agreement plainly confirms the change of control provision provided for a one-time bonus, Menezes sought to use it again. In connection with the December 2005 purchase by affiliates of WLR of approximately 75% of SCI from Zapata Corporation, Menezes demanded a *second* bonus. SCI refused to pay based on the express language and intent of the employment agreement. After all, Menezes had already been

compensated for his higher strike price. But Menezes escalated the dispute to such a degree that SCI paid Menezes \$406,000 bonus to avoid a lawsuit and minimize business disruption.

156. Menezes was interim CEO for approximately five months before the termination of his employment. Menezes, as CFO and interim CEO, took part in discussions concerning the merger of SCI and ITG, and had access to information about future transactions for SCI.

157. In April and May 2006, SCI and ITG respectively appointed special committees to explore a possible combination of the companies. In May 2006, WLR proposed preliminary merger terms to ITG's and SCI's special committees.

158. In response to the proposed merger, Menezes made a *third* demand for a change of control bonus from SCI. SCI refused his demand.

159. On July 6, 2006, Menezes sued SCI and Mr. Gorga for various claims, including SCI's refusal to pay the change of control bonus for the proposed merger of ITG and SCI. When he filed his lawsuit, Menezes knew that ITG and SCI were in advanced merger discussions and negotiations.

160. For example, even before Menezes had left SCI, due diligence was under way and special committees at SCI and ITG had been established to assess the merger. By June 2006, ITG's and SCI's special committees had separate legal and financial advisors conducting due diligence and interviewing management of both entities.

161. Between August 22 and 23, 2006, ITG's and SCI's special committees and their advisors negotiated each company's respective value and contribution to the merger. Finally, on August 23, 2006, ITG's and SCI's special committees agreed on an exchange ratio, subject to negotiation of the more definite terms of the merger agreement and receipt of respective fairness

opinions, where ITG stockholders would receive 65% of the combined company, and SCI stockholders would receive 35% of the combined company.

162. Between August 24 and 28, 2006, the legal advisors for the special committees finalized the terms and conditions of the merger, and on August 28, 2006, the financial advisor to SCI's special committee opined that the exchange ratio was fair from a financial point of view to SCI's stockholders other than those affiliated with WLR.

163. On August 29, 2006, after the special committees reviewed the terms of the merger with their respective Boards of Directors, ITG and SCI signed the merger agreement.

164. On August 30, 2006, while Menezes' employment lawsuit was still in its early stages, SCI and ITG publicly announced the merger and disclosed its material terms, including the exchange ratio to be used to convert the ITG stock into SCI stock, and that affiliates of WLR would own approximately 82% of the combined company.

165. On September 1, 2006, ITG and SCI publicly filed a preliminary Joint Proxy Statement/Prospectus ("Prospectus") with the SEC for the SEC's review and comment. The Prospectus included a detailed description of the background and reasons for the proposed merger, the terms and conditions of the merger agreement and the transactions related thereto, the financial analyses performed by RSM EquiCo Capital Markets, LLC's ("RSM") to the SCI Special Committee, and the fairness opinion delivered by RSM.

166. On September 22, 2006, ITG and SCI publicly filed the definitive Prospectus for the combined company with the SEC and mailed it to stockholders shortly thereafter. Pursuant to that Prospectus, SCI's record stockholders as of September 19, 2006 were entitled to vote on the Amended and Restated Certificate of Incorporation and to re-elect five director-nominees to SCI's Board of Directors.

167. Upon information and belief, Menezes knew that the upcoming merger would provide him increased settlement leverage in his employment lawsuit against SCI and Gorga. In an effort to capitalize upon the upcoming merger, Menezes prepared an amended complaint asserting additional allegations and related claims against ITG, WLR, and David Wax. Menezes never filed his amended complaint, but provided it to opposing counsel.

168. Paragraph 36 of the copy of the amended complaint stated that "[u]pon information and belief, the terms of the proposed merger are unfair to SCI and effectively transfer value from the shareholders of SCI, including Plaintiff, to the shareholders of ITG."

169. In an effort to bring a quick end to Menezes' lawsuit and preclude him from further interfering with the merger and the combined company's future business, SCI and Gorga agreed to settle the matter with Menezes without admitting any liability. Among other consideration, Menezes received a \$197,500 payment in lieu of a change of control bonus.

170. In sum, what should have been a one-time change of control payment to put Menezes on equal footing with other SCI employees, became a windfall of nearly \$1 million without Menezes selling a single share of SCI stock.

171. After ITG's and SCI's merger was announced and the prospectus was mailed to stockholders, on September 28, 2006, Menezes executed the Confidential Settlement Agreement and Release of All Claims ("Settlement Agreement") concerning his employment lawsuit. Notably, the attorney representing Menezes in his current lawsuit was the same one who negotiated and drafted the Settlement Agreement. The Settlement Agreement included the following provision:

Releases by Plaintiff. As a material inducement to Employer to enter into this Confidential Settlement Agreement, Plaintiff does hereby release, acquit and forever discharge Gorga and Safety Components, and any parent, subsidiary and affiliated person,

company, business, entity or enterprise of Gorga and Safety Components, along with all current and former officers, directors, agents, employees, insurers, representatives, attorneys, successors, and assigns of same, which shall also include by way of enumeration but not a limitation, the International Textile Group, Inc., W.L. Ross & Co. L.L.C., and David Wax, a resident of the State of Connecticut (collectively, the "Release Parties"), from any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments, and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute or otherwise, which Plaintiff either has had or now has against Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is Plaintiff's intention to release all rights and claims that he may lawfully release.

(Settlement Agreement at ¶ 7; attached hereto as Exhibit A.) While Menezes executed this release "[w]ithout in any way limiting the generality of the foregoing" provision, he specifically released "any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement." (*Id.*)

172. Indeed, Menezes expressly released all possible claims, recognizing that certain facts and consequences may have been unknown to him: "Plaintiff understands, acknowledges, and voluntarily agrees that this Confidential Settlement Agreement, except as otherwise explicitly stated, is a total and complete release by him of any and all claims which he has against Employer as of the effective date of this Confidential Settlement Agreement, both known or unknown, even though there may be facts or consequences which are unknown to Plaintiff." (*Id.* at ¶ 8.)

173. Plaintiff also agreed that he would not disparage the parties, promising that he would not publicly or privately criticize or disparage "in a manner intended or reasonably calculated to result in public embarrassment to, or injury to the business reputation of the Parties."

174. Plaintiff did not live up to his promises. On information and belief, Menezes falsely agreed to release his claims and not disparage Counterclaimants in order to maximize his settlement payment while secretly planning a lawsuit based on released claims.

175. On September 29, 2006, the parties agreed to dismiss Menezes' lawsuit with prejudice, and on October 9, 2006, the Court closed the matter.

176. On October 20, 2006, ITG was combined with SCI. On or about that time, ITG became a wholly-owned subsidiary of SCI, and SCI changed its name to International Textile Group, Inc. (the "Combined Company")

177. On April 9, 2008, Menezes filed this lawsuit asserting claims that arose or accrued before September 28, 2006 against parties that were expressly within the scope of the release in the Settlement Agreement. Menezes' lawsuit is based on released claims and is in breach of the Settlement Agreement.

CAUSE OF ACTION

Breach of Contract Against Menezes

178. The foregoing allegations are incorporated herein by this reference.

179. Menezes, SCI (now the Combined Company), and Gorga competently entered into a binding contract – the Settlement Agreement – wherein there was a clear offer, mutual acceptance, and valuable consideration exchanged among the parties, as set forth above and agreed to in the Settlement Agreement.

180. In the Settlement Agreement, Menezes agreed to release all claims against SCI, Gorga, and the Counterclaimants to this action. Counterclaimants were contemplated by the Settlement Agreement, were intended to be direct third party beneficiaries to the Settlement Agreement, and were intended to be included in the release provisions. The release of these

direct third party beneficiaries was part of the consideration exchanged for the Settlement Agreement.

181. In the Settlement Agreement, Menezes further agreed not to disparage SCI, Gorga, and the Counterclaimants to this action. Counterclaimants were contemplated by the Settlement Agreement, were intended to be direct third party beneficiaries to the Settlement Agreement, and were intended to be included in the non-disparagement provision. The non-disparagement of these direct third party beneficiaries was part of the consideration exchanged for the Settlement Agreement.

182. SCI, Gorga, and the Counterclaimants to this action performed all or substantially all of the material things that the Settlement Agreement required, and all conditions required for Menezes' performance have occurred.

183. Alternatively, performance by SCI, Gorga, and the Counterclaimants to this action has been excused, forgiven or rendered impossible by Menezes' prior material breach of the Settlement Agreement.

184. Menezes breached the Settlement Agreement and has acted in bad faith by, among other things, bringing this lawsuit on claims that have been expressly released in the Settlement Agreement.

185. Counterclaimants have been directly and proximately damaged by Menezes' foregoing breaches, and are entitled to actual and consequential damages in an amount to be proven at trial.

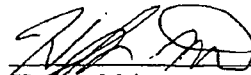
186. WHEREFORE, Counterclaimants pray for judgment as follows:

A) For actual and consequential damages against Menezes;

- B) For recovery of all costs, attorneys fees and expenses reasonably incurred in the defense and prosecution of this action to the extent permitted by law; and
- C) For such other and further relief as the Court deems just and proper.

Dated: June 6, 2008

Respectfully submitted,



H. Sam Mabry, III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square – 11th Floor
75 Beattie Place
Greenville, South Carolina 29601
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

OF COUNSEL:

George T. Manning
JONES DAY
2727 N. Harwood Street
Dallas, Texas 75201-1515
Telephone: (214) 220-3939
Facsimile: (214) 969-5100

Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Suite 800
Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

Counsel for Defendants and Counterclaimants
WL Ross & Co. LLC; Wilbur L. Ross, Jr.;
Michael J. Gibbons; David H. Storper; David
L. Wax; Joseph L. Gorga; WLR Recovery
Fund III, L.P.; WLR Recovery Fund III, L.P.;
WLR Recovery Associates II LLC; And
WLR Recovery Associates III LLC

**CONFIDENTIAL SETTLEMENT AGREEMENT
AND RELEASE OF ALL CLAIMS**

This CONFIDENTIAL SETTLEMENT AGREEMENT AND RELEASE OF ALL CLAIMS (hereinafter "Confidential Settlement Agreement") by and between **Brian P. Menezes**, a resident of Greenville, South Carolina (hereinafter "Plaintiff"), and his heirs, executors, administrators, successors and assigns, and **Safety Components International, Inc.**, a company with an office and place of doing business in Greenville, South Carolina (hereinafter "Safety Components" or "Employer"), its officers, directors, board members, shareholders, its affiliates and controlling persons (if any), employees, attorneys, insurers, representatives, bailees, agents, servants, heirs, executors, administrators, personal representatives, predecessors, successors, assigns, parent companies, subsidiaries, related companies, divisions, and the officers, directors, board members, shareholders, employees, bailees, agents and servants of their parent companies, subsidiaries, related companies, divisions, and affiliates, and all persons acting by, through, under, or in concert with any of them, and **Joseph L. Gorga**, a resident of Greensboro, North Carolina (hereinafter "Gorga"). Safety Components and Gorga may be identified collectively hereinafter as "Employer" solely for the purpose of identification in this document. Plaintiff, Safety Components, and Gorga may also be identified collectively hereinafter as the "Parties."

WITNESSETH:

WHEREAS, on or about July 6, 2006, Plaintiff filed a complaint entitled "*Brian P. Menezes, Plaintiff, vs. Safety Components International, Inc., and Joseph L. Gorga, Defendants*," bearing civil action no. 2006-CP-23-4236, in the South Carolina Court of Common Pleas for the Thirteenth Judicial Circuit, County of Greenville (hereinafter "the Underlying Lawsuit"), in which Plaintiff alleged, among other things, that the Defendants were liable for violation of the South Carolina Payment of Wages Act (S.C. Code Ann. § 41-10-10 et seq.) and breach of contract arising out of Plaintiff's employment with Safety Components and an "Employment Agreement" between Menezes and Safety Components, entered into on May 18, 2001, as subsequently amended (hereinafter "Employment Agreement"), and wrongful termination of Menezes' employment from Safety Components (hereinafter collectively "Plaintiff's Claims"), and seeking damages and a declaratory judgment on Plaintiff's Claims;

WHEREAS, Plaintiff also prepared an Amended Complaint incorporating Plaintiff's Claims against Employer, but which also contained additional allegations against International Textile Group, Inc., W.L. Ross & Co., LLC, and David Wax, a resident of the State of Connecticut, for, among others, tortious interference with contract and civil conspiracy (hereinafter collectively "Plaintiff's Amended Claims"), which Amended Complaint was not filed with any court or served upon Employer, International Textile Group, Inc., W.L. Ross & Co., LLC, or David Wax;

WHEREAS, the Parties have engaged in sufficient investigation upon which to evaluate the claims and potential defenses in the Underlying Lawsuit;

WHEREAS, Defendants deny and dispute Plaintiff's Claims and Plaintiff's Amended Claims, in whole or in part, and any liability therefore;

EXHIBIT

A

WHEREAS, the Parties have reached an agreement to resolve any and all claims arising out of Plaintiff's Claims and Plaintiff's Amended Claims, or any right to damages or a declaratory judgment, prior to Employer filing an Answer responding to Plaintiff's Claims or Plaintiff's Amended Claims;

WHEREAS, the Parties have agreed upon a compromise settlement and now wish to forever resolve, settle, compromise, and end any and all claims either or both may have against the another arising from Plaintiff's employment, and the termination thereof, and in the Underlying Lawsuit and as expressed in Plaintiff's Amended Claims;

WHEREAS, Plaintiff acknowledges that Employer has paid to him all wages earned, all unused vacation benefits accrued (if any), and all other amounts which may have been owed to him by Employer pursuant to the Employment Agreement or otherwise by Employer's policy, contract, or applicable law through the date of Plaintiff's termination, June 9, 2006 (hereinafter the "Termination Date"), less standard payroll withholding and any authorized deductions.

NOW, THEREFORE, in consideration of the mutual covenants contained herein and the exchange of other good and valuable consideration, the receipt and sufficiency of which are hereby expressly acknowledged, the Parties hereto agree to the following terms of settlement in full satisfaction, accord and settlement of all claims against one another:

1. **Payment by Employer to Plaintiff in Lieu of Severance Pay.** The Parties agree that subject to the expiration of the seven-day (7-day) revocation period (as described in Section 18 below) and receipt by Employer of an executed Stipulation of Dismissal with Prejudice of the Underlying Lawsuit, the Employer will pay to Plaintiff, in full satisfaction, accord, and settlement for any and all claims, and specifically for any claim for severance payments as contemplated pursuant to §7.4(b)(1) of the Employment Agreement, the amounts set forth below on the dates indicated:

- (a) A first payment on January 9, 2007, in the amount of Ninety Thousand Two Hundred Ten and no/100ths (\$90,210.00) Dollars (which takes into consideration the payments previously made by the Employer of Fifty Four Thousand Two Hundred Ten and no/100ths (\$54,210.00) Dollars).
- (b) A second payment on March 2, 2007 in the amount of One Hundred Forty-Four Thousand Four Hundred Twenty and no/100ths (\$144,420.00) Dollars.
- (c) A third and final payment on August 7, 2007 in the amount of One Hundred Forty-Four Thousand Four Hundred Twenty and no/100ths (\$144,420.00) Dollars.

Each of the aforementioned payments is to be paid minus all applicable withholdings as required by law.

2. **Payment by Employer to Plaintiff in Lieu of Change in Control Bonus.** The Parties dispute the right to any change in control bonus payment under the Employment Agreement, but agree that in full satisfaction, accord, and settlement for any claim, right or entitlement to any payment for a change in control bonus payments, whether pursuant to §7.4(b)(4) of the Employment Agreement, or from any other part of the Employment Agreement, or otherwise from any Released Party, Safety Components will pay to the Plaintiff the total sum of One Hundred Ninety Seven

Thousand Five Hundred and no/100ths (\$197,500.00) Dollars, again subject to the expiration of the seven-day (7-day) revocation period (as described in Section 18 below) and receipt by Employer of an executed Stipulation of Dismissal with Prejudice of the Underlying Lawsuit.

This sum shall be paid in three (3) separate payments of Sixty Five Thousand Eight Hundred Thirty Three and 33/100ths (\$65,833.33) Dollars, each of which is to be paid on or before January 9, 2007, March 2, 2007, and August 7, 2007, respectively, and from which shall be deducted all applicable withholdings as required by law. If applicable, the aforesaid payment, in compromise and settlement of any and all rights to any change in control bonus, shall be "grossed up" as provided in the Employment Agreement at Paragraph 10. Compliance with Internal Revenue Code §280G.

3. **Benefits.** All of Plaintiff's benefits, and any right thereto, shall be deemed terminated as of the Termination Date (other than, where applicable, health, dental, and vision insurance, which shall terminate effective as of the last day of the month in which Plaintiff was terminated) unless the terms of the benefit plans provide otherwise, or except to the extent inconsistent with the remainder of this paragraph. Employer shall provide at no expense to Plaintiff for a period of eighteen (18) months following the Termination Date continued health insurance coverage as in effect from time to time (but which shall include coverage under Execucare or a plan or program providing coverage substantially equivalent to that Plaintiff had immediately prior to the Termination Date) and, to the extent they continue to be eligible for such coverage under COBRA, his dependents who were covered by Employer's health insurance plan immediately prior to the Termination Date. Otherwise, Plaintiff acknowledges that Plaintiff shall not be entitled to any other or additional benefits, sums or amounts, including without limitation, any right to any bonus, vacation pay, sick pay, life insurance, disability income policies, car allowance, contributions for 401(k) or similar plans nor any other benefits, except for the payments of premiums for medical insurance set forth above, and except as otherwise provided in the benefit plans, or specifically identified in this Confidential Settlement Agreement. Plaintiff shall be entitled, at Plaintiff's sole expense to any COBRA benefits to which he may be entitled by law.

4. **Payment by Employer to Counsel for Plaintiff.** On Plaintiff's behalf, and at his request, the Parties agree that Employer will pay Plaintiff's attorney, William D. Herlong, Esq., of Anderson & Herlong, L.L.C., the sum of Seven Thousand Five Hundred and no/100ths (\$7,500.00) Dollars, payable pursuant to a Form 1099. Plaintiff's attorneys agree to hold harmless and indemnify Employer for any liability for tax payments and filings for which Plaintiff's attorneys are responsible, if any.

5. **Nature of Consideration.** The mutual promises and sums described herein are acknowledged to be good and valuable consideration in full and final payment and accord and satisfaction of all claims by Plaintiff against Employer by virtue of his employment, the Employment Agreement, or otherwise.

6. **Dismissal of the Underlying Lawsuit.** The Parties hereby agree to direct their respective counsel to dismiss the Underlying Lawsuit, and any and all claims, counterclaims, cross-claims, or related claims that have been or could have been asserted in the Underlying Lawsuit, with prejudice. The Underlying Lawsuit and any and all related claims, counterclaims, cross-claims, or related claims shall henceforth be res judicata.

7. **Releases by Plaintiff.** As a material inducement to Employer to enter into this Confidential Settlement Agreement, Plaintiff does hereby release, acquit and forever discharge Gorga and Safety Components, and any parent, subsidiary and affiliated person, company, business, entity or enterprise of Gorga and Safety Components, along with all current and former officers, directors, agents, employees, insurers, representatives, attorneys, successors, and assigns of the same, which shall also include by way of enumeration but not limitation, the International Textile Group, Inc., W. L. Ross & Co. L.L.C., and David L. Wax, a resident of the State of Connecticut (collectively, the "Released Parties"), from any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which Plaintiff either has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is Plaintiff's intention to release all rights and claims that he may lawfully release.

Without in any way limiting the generality of the foregoing, this Release applies to and waives: (1) any and all claims, causes of action, or rights, which Plaintiff has had or may now have under or pursuant to Title VII of the Civil Rights Act of 1964, as amended; Civil Rights Act of 1991; Title 42, United States Code, Section 1981; the Americans with Disabilities Act; the Age Discrimination In Employment Act, as amended, the Older Workers Benefit and Protection Act; and any other statute, rule, or executive order prohibiting discrimination in employment on the basis of age, disability, religion, national origin, sex, race, color, or veteran's status; (2) any and all claims, causes of action, or rights, which Plaintiff has had or may now have under or pursuant to the Employment Retirement Income Security Act; (3) any claims, causes of action, or rights which Plaintiff might have or has had for employment discrimination, unlawful employment practices, or relating in any way to his employment or termination thereof, and arising under local, state, or federal law; (4) any claims or causes of action which Plaintiff might have or have had for personal injuries; and (5) any claims or causes of action which Plaintiff might have or have had for breach of contract or based upon any agreement with the Released Parties, specifically including but not limited to the Employment Agreement; (6) any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement; (7) any claims or causes of action which Plaintiff might have or have had for defamation, tortious conduct and wrongful discharge and (8) all of Plaintiff's Claims, Plaintiff's Amended Claims and all claims made or which may have been made in the Underlying Lawsuit or Amended Complaint.

Additionally, without waiving any prospective or retrospective rights under the Family and Medical Leave Act ("FMLA"), Plaintiff admits that he has received from Employer all rights and benefits, if any, potentially due to him pursuant to the FMLA. Similarly, without waiving any prospective or retrospective rights under the Fair Labor Standards Act ("FLSA"), Plaintiff admits that he has received from Employer all salary, wages, or other compensation, if any, potentially due to him pursuant to the FLSA.

8. **Releases by Plaintiff— Additional Information.** Plaintiff specifically agrees that his release of claims identified in Section 7, above, is knowing and voluntary and that he has had sufficient opportunity to consult with his attorney to ensure that he understands the language used in this Confidential Settlement Agreement and the rights and obligations created herein and he had in fact consulted with his attorney regarding the same. Plaintiff understands, acknowledges, and voluntarily agrees that this Confidential Settlement Agreement, except as otherwise explicitly stated, is a total and

complete release by him of any and all claims which he has against Employer as of the effective date of this Confidential Settlement Agreement, both known or unknown, even though there may be facts or consequences of facts which are unknown to Plaintiff.

9. **Other Claims.** Plaintiff represents that besides the Underlying Lawsuit, he has not filed any other complaints, claims, or actions against the Released Parties with any state, federal, or local agency or court, or that if Plaintiff has, Plaintiff agrees to withdraw and dismiss with prejudice (or cause to be withdrawn and dismissed with prejudice) any such complaint, claim, action, or charge. Plaintiff acknowledges that he knows of no facts which may lead to or support any complaints, claims, actions, or charges against Employer in or through any state, federal, or local agency or court other than Plaintiff's Claims and/or Plaintiff Amended Claims as described hereinabove and asserted in the Underlying Lawsuit and/or described in the Amended Complaint, which are hereby released and forever settled.

10. **Status of "Employment Agreement."** Plaintiff further agrees that he and Safety Components entered into the Employment Agreement on May 18, 2001, which agreement was subsequently amended by the Parties on September 22, 2003. The Parties hereby agree that the prior Employment Agreement, including all amendments thereto, is hereby rescinded, terminated, cancelled, or otherwise null and void as of June 9, 2006, and the Parties shall be relieved of any obligations or liability thereunder, except with the sole exceptions addressed herein. While it is the Parties' intent to otherwise rescind the Employment Agreement, the following provisions contained in the Employment Agreement shall remain in full force and effect and are incorporated herein by reference:

- Sec. 8. Confidential Information, Inventions (including §§ 8.1 - 8.5); and
- Sec. 9. Non-Competition, Non-Solicitation (including §§ 9.1 - 9.5).

Plaintiff agrees and understands that, notwithstanding the provisions contained in Paragraph 24 herein, the foregoing provisions contained in the Employment Agreement, and amendments thereto, shall remain in full force and effect despite the execution and terms of this Confidential Settlement Agreement, are subject to separate valid consideration previously paid by Employer to Plaintiff, and are subject to enforcement pursuant to the original terms of the Employment Agreement.

11. **Releases by Employer.** As a material inducement to Plaintiff to enter into this Confidential Settlement Agreement, Employer hereby releases, acquits, and forever discharges Plaintiff from any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which the Employer either has had or now has against Plaintiff for or related to any matter or thing, whatsoever, from the beginning of time up to and including the date of execution hereof, except for the provisions in the Employment Agreement enumerated and described above in Section 10 entitled "Status of Employment Agreement", and with regard to that provision, only any existing claims predating the execution of this agreement are released. Other than the provisions set forth in Section 10, above, it is the Employer's intention to release all rights and claims that the Employer may lawfully release.

12. **Non-Disparagement.** The Parties agree that they will not publicly criticize or disparage the each other, or privately criticize or disparage each other in a manner intended or reasonably calculated to result in public embarrassment to, or injury to the business or reputation of the Parties. Employer shall take reasonable efforts to ensure that David Wax and the executive officers of International Textile Group, Inc., and W.L. Ross & Co., LLC, comply with this provision as if each was Employer.

13. **Cooperation.** Plaintiff agrees that for a period of one year he will provide such cooperation, information or reasonable assistance that the Released Parties (as defined above) may reasonably request of him upon reasonable prior notice, including making himself available to be a witness in judicial or other legal proceedings, with respect to any matters that he may have been familiar with or responsible for during his tenure with the Employer. The Employer will reimburse all related and reasonable expenses and shall compensate Plaintiff at the rate of Two Hundred and No/100ths (\$200.00) Dollars per hour, with a minimum of four (4) hours, per request for such future services.

14. **Resignation From Offices.** Plaintiff confirms that effective June 9, 2006, he ceased to be employed with Safety Components and that he does resign from all offices and positions with Safety Components, including (a) from all offices of Safety Components to which he has been elected by the Board of Directors of Safety Components or any Released Party (or to which he has otherwise been appointed), (b) from all directorships or offices of any entity that is a subsidiary of, or is otherwise related to or affiliated with, Safety Components or any Released Party, (c) from all administrative, fiduciary or other positions he may hold with respect to arrangements or plans for, of or relating to Safety Components or any Released Party, and (d) from any other directorship, office, or position of or with any corporation, partnership, joint venture, trusts of any other enterprise (each, an "Other Entity") insofar as Plaintiff is serving in the directorship, office or position of the Other Entity at the request of Safety Components or any Released Party.

15. **Future Employment.** Plaintiff agrees that Employer is not obligated to offer employment to Plaintiff (or to accept services or the performance of work from Plaintiff directly or indirectly) now or in the future. Plaintiff agrees not to seek or accept employment or any direct independent contractor relationship with the Released Parties, as defined herein, now or at any time in the future. Plaintiff agrees that in the event such employment or other relationship occurs in the future, this provision shall serve as good and just cause for termination of same. Plaintiff knowingly and voluntarily waives all rights, if any, he may have under federal and/or state law to re-hire by, or reinstatement of employment with, Employer. This provision does not apply to the extent Plaintiff is an employee or independent contractor with a company that is acquired by a Released Party. Further, this provision is void after five (5) years.

16. **Non-Admission.** The Parties agree and understand that this Confidential Settlement Agreement is a compromise of disputed claims and shall not in any way be construed as an admission by any of the Parties or Released Parties that it has acted wrongfully with respect to any other Party or Released Party or any other person, which is expressly denied, or that they have any rights whatsoever against each other. The Parties further agree that Employer and the Released Parties specifically disclaim any liability to or alleged wrongful acts against Plaintiff or any other person, on the part of itself, its affiliates, and their respective representatives, officers, employees, attorneys, and agents.

17. **Confidentiality and Breaches.** Except as required to comply with legal disclosure

requirements (e.g., subpoenas) or as otherwise required or protected by law or otherwise allowed in this paragraph, the Plaintiff represents and agrees that he will keep the terms, and amount of this Confidential Settlement Agreement completely confidential and he has not disclosed and will not disclose any information regarding this Confidential Settlement Agreement (or discussions preceding this Confidential Settlement Agreement) to anyone other than his attorneys, tax advisors, financial advisors, his spouses and/or other individuals who have a reasonable need to know and who have been approved in writing to receive such information by Employer. The Plaintiff agrees that he will not describe this Confidential Settlement Agreement or the settlement of his Claims in any way (e.g., substantial/insubstantial, generous/parsimonious, large/small, fair/unfair, etc.). The Plaintiff may discuss this Confidential Settlement Agreement with his attorneys, tax advisors, financial advisors, his spouses and/or other individuals who have a reasonable need to know and have been approved to receive such information by Employer, but Plaintiff will inform them of these confidentiality provisions, and will remain responsible for any further disclosures that may result. The Plaintiff agrees that the unauthorized disclosure of the terms or amount of this Confidential Settlement Agreement is a material breach of this Confidential Settlement Agreement. In the event there is a breach of this Confidential Settlement Agreement, the remaining provisions of this Settlement Agreement shall remain in full force and effect for the benefit of the Employer. The Parties and the Released Parties will limit their public disclosure of this settlement to a simple statement that the matter has been resolved on confidential terms.

18. Acknowledgment.

(a) The release set forth herein includes a waiver of rights and claims which Plaintiff may have arising under the Age Discrimination in Employment Act of 1967 (Title 29, United States Code, Sections 621, *et seq.*) ("ADEA"). Plaintiff is advised to consult with his attorney regarding his waiver of rights and claims under the ADEA. Plaintiff understands that by signing this release, he waives his rights or claims under the ADEA. Plaintiff further understands that he is not waiving rights or claims under that ADEA that may arise after the effective date of this fully executed Confidential Settlement Agreement.

(b) Plaintiff agrees that he has been advised to consult with an attorney prior to executing this Confidential Settlement Agreement. Plaintiff acknowledges that he has had the opportunity to consult with an attorney to review this agreement, prior to signing, and that he has in fact done so. Plaintiff acknowledges that his attorney has fully explained in a manner understood by him the waiver of any rights or claims contained in this Confidential Settlement Agreement.

(c) Plaintiff certifies that he has been given a period of up to twenty-one (21) days to study this Confidential Settlement Agreement, and to consult with an attorney, accountant, or other advisor before signing the Confidential Settlement Agreement, and that the actual time he has taken for such purposes was adequate for all appropriate consultations.

(d) Plaintiff represents that he has read and thoroughly discussed all aspects of this Confidential Settlement Agreement with his attorney, understands its provisions, and understands that this Confidential Settlement Agreement establishes binding contractual rights. Plaintiff acknowledges that this Confidential Settlement Agreement and the release and waiver of claims contained herein are given knowingly and voluntarily.

(e) Plaintiff understands that this Confidential Settlement Agreement shall not be effective and enforceable until seven (7) days from the date he executes this Confidential Settlement Agreement. During this seven-day period, Plaintiff may change his mind and revoke this Confidential Settlement Agreement by notifying Employer, in writing, of his wish to revoke this Confidential Settlement Agreement. Any such revocation must be in the form of a signed, written statement delivered to Employer's counsel, *M. Baker Wyche, III, at Ogletree, Deakins, Nash, Smoak & Stewart, P.C., 300 N. Main Street, PO Box 2757, Greenville, SC 29602.*

19. **Waiver of Breach.** Either Party may waive or excuse the other's failure to perform any provision of this Confidential Settlement Agreement; provided, however, that any such waiver shall be in writing and shall not preclude the enforcement of this Confidential Settlement Agreement upon any subsequent breach, whether or not similar in character.

20. **Assignment.** This Confidential Settlement Agreement and the rights and obligations of Employer hereunder may be assigned by Employer and shall inure to the benefit of, shall be binding upon and shall be enforceable by any such assignee. This Confidential Settlement Agreement and the rights and obligations of Plaintiff hereunder may not be assigned by Plaintiff and, further, Plaintiff expressly states that he has not assigned any rights or obligations arising out of his employment with Employer, his separation therefrom, or pursuant to this Confidential Settlement Agreement.

21. **Successorship.** This Confidential Settlement Agreement shall be binding upon and inure to the benefit of Gorga and Safety Components and its affiliates, successors, and assigns, and, subject to Section 21 above, Plaintiff, his heirs, personal representatives, administrators, beneficiaries, and assigns. If Plaintiff should die while any amount would still be payable to him under this Confidential Settlement Agreement had Plaintiff continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Confidential Settlement Agreement to his devisee, legatee, or other designee or, if there is no such designee, to his estate.

22. **Non-Reliance.** Plaintiff represents and acknowledges that in executing this Confidential Settlement Agreement he does not rely, and has not relied, upon any representation or statement not set forth herein by Employer or any of Employer's agents, representatives, or attorneys.

23. **Entire Agreement.** Plaintiff further represents and acknowledges that this Confidential Settlement Agreement constitutes the entire agreement between the Parties. Except as stated otherwise herein, any oral or written representations, prior agreements, or understandings not reflected in this Confidential Settlement Agreement shall have no force or effect, and are superseded by this Confidential Settlement Agreement.

24. **Severability.** The terms of this Confidential Settlement Agreement, including paragraph subparts, are severable, and if any part or subpart is found to be unenforceable, the other terms shall remain in full force and effect and are valid and enforceable.

Likewise, the Parties expressly recognize that the obligations set forth in this Confidential Settlement Agreement are independent of one another, in that a breach of one provision does not extinguish any duties or rights set forth in other provisions of this Confidential Settlement Agreement.

25. **Interpretation.** The Parties agree that this Confidential Settlement Agreement shall be interpreted according to South Carolina law and shall not be construed against the drafters. In the event for any reason that any provision or portion of this Confidential Settlement Agreement shall be found to be void or invalid, then such provision or portion shall be deemed to be severable from the remaining provisions or portions of this Confidential Settlement Agreement, and it shall not affect the validity of the remaining provisions or portions, which provisions or portions shall be given full effect as if the void or invalid provision or portion had not been included herein.

26. **Modification.** This Confidential Settlement Agreement shall not be modified or amended except by an instrument in writing signed by Plaintiff and Employer.

27. **Cooperation in Drafting.** The Parties agree that they have cooperated in the drafting and preparation of this Confidential Settlement Agreement with the assistance of counsel. In any construction to be made of this Confidential Settlement Agreement, the same shall not be construed against either party but shall be viewed as each sharing an equal role in the negotiation and drafting of its terms.

28. **Legal Counsel.** Plaintiff agrees that he has been advised to seek the advice of legal counsel, and that he has had the opportunity to have legal counsel review this agreement, prior to signing.

29. **Governing Law, Jurisdiction, and Venue.** This Confidential Settlement Agreement has been entered into under and shall be governed by and construed in accordance with the laws of the State of South Carolina, without regard to its conflicts of laws provision. The parties agree that the Greenville County Court of Common Pleas or the Federal District Court for the District of South Carolina, Greenville Division, shall be the sole and exclusive jurisdiction and venue for all disputes between the Parties under this Confidential Settlement Agreement. Plaintiff hereby irrevocably consents to the jurisdiction and venue of these courts for adjudication of all disputes between the Parties under this Confidential Settlement Agreement. Plaintiff hereby waives any objections or defenses to jurisdiction or venue in any such proceeding before such court(s).

30. **Effective Date.** The terms of this Confidential Settlement Agreement shall become final and binding only upon the execution of this Confidential Settlement Agreement by both parties and upon the expiration of the seven (7) day revocation period discussed above.

* * * * *

IN WITNESS WHEREOF the Parties have caused this Confidential Settlement Agreement to be signed. By signing this agreement, the Parties warrant that they have read and understand each provision of this Confidential Settlement Agreement, that they voluntarily agree to and have signed the Confidential Settlement Agreement, that in so doing they are not relying upon any inducements, representations, agreements, or understandings other than as are set forth herein, and that they are acting with full advice of and explanation by their respective legal counsel.

* * * * *

The Parties recognize and agree that this Confidential Settlement Agreement and Release may be signed and executed in one or more parts or counterparts and/or by facsimile signature. Each counterpart, including a signature page executed by each party, shall be an original counterpart of this Confidential Settlement Agreement and Release, but all such counterparts shall constitute one instrument.

WITNESSES:

Brian P. Menezes

Janice Varat

[Signature]

Brian P. Menezes

Date: Sept 28th, 2006

Reviewed and Approved:

Janice Varat

[Signature]

William D. Herlong,
Attorney for Plaintiff, Brian P. Menezes

Date: 9/28/2006

Safety Components International, Inc.

By: _____

Its: _____

Date: _____

* * * * *

The Parties recognize and agree that this Confidential Settlement Agreement and Release may be signed and executed in one or more parts or counterparts and/or by facsimile signature. Each counterpart, including a signature page executed by each party, shall be an original counterpart of this Confidential Settlement Agreement and Release, but all such counterparts shall constitute one instrument.

WITNESSES:

Brian P. Menezes

Janice Varat

Brian P. Menezes

Brian P. Menezes

Date: Sept 28th, 2006

Reviewed and Approved:

Janice Varat

William D. Herlong

William D. Herlong,

Attorney for Plaintiff Brian P. Menezes

Date: 9/28/2006

Safety Components International, Inc.

Brenda S. Swofford

By: Steph B. Dunk

Its: President

Date: Sept. 29, 2006

Joseph L. Gorga

Cheryl A. Hollis

Joseph L. Gorga
Joseph L. Gorga

Date: Sept. 29, 2006

4386701.1

STATE OF SOUTH CAROLINA)

COUNTY OF GREENVILLE)

Brian P. Menezes,)

Plaintiff,)

v.)

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, Stephen)
B. Duerk, WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P, WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC,)

Defendants.)

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, WLR)
Recovery Fund II, L.P., WLR Recovery)
Fund III, L.P, WLR Recovery Associates II)
LLC, and WLR Recovery Associates III)
LLC;)

Counterclaimants,)

v.)

Brian P. Menezes,)

Counterclaim Defendant.)

FILED
CLERK OF COURT
GREENVILLE CO. S.C.
JUN 6 2008

2008 JUN - 6 P 2:24

DEFENDANTS' MOTION FOR JUDGMENT ON THE PLEADINGS OR,
ALTERNATIVELY, MOTION FOR SUMMARY JUDGMENT

To: William D. Herlong
ANDERSON & HERLONG, LLC
P.O. Box 2105
Greenville, SC 29602-2105

Pursuant to South Carolina Rule of Civil Procedure 12(c), Defendants WL Ross & Co. LLC; Wilbur L. Ross, Jr.; Michael J. Gibbons; David H. Storper; David L. Wax; Joseph L. Gorga; Stephen B. Duerk; WLR Recovery Fund II, L.P.; WLR Recovery Fund III, L.P.; WLR Recovery Associates II LLC; and WLR Recovery Associates III LLC (collectively, "Defendants") hereby move the above-captioned Court for an Order granting Defendants judgment on the pleadings or, alternatively, summary judgment on Plaintiff's Complaint.

Taking the allegations in the Plaintiff's Complaint and Defendants' Answers and Third Affirmative Defenses as true, Defendants are entitled to judgment as a matter of law because before the filing of this lawsuit, Plaintiff released all of the claims asserted in his Complaint. Alternatively, given Plaintiff's admissions *in judicio* in his Complaint and the Release that he executed on September 28, 2006 – in exchange for substantial consideration – there are no genuine issues of material fact, and the undisputed facts establish the complete and total release of the claims asserted against the Defendants.

The specific grounds for this Motion are:

1. On September 28, 2006, Plaintiff, a former officer of Safety Components International, Inc. ("SCI") (now known as International Textile Group, Inc. ("ITG")), executed a Confidential Settlement Agreement and Release of All Claims (the "Release"), which resolved a prior lawsuit he brought over his compensation. The scope of the Release is extensive:

[A]ny and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which Plaintiff either has now or has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is Plaintiff's intention to release all rights and claims that he may lawfully release.

Release, executed September 29, 2006, ¶ 7 (attached to the Affidavit of Stephen B. Duerk as Exhibit A, filed contemporaneously herewith) (emphasis added).

2. Notably, Plaintiff, “[w]ithout in any way limiting the generality of the foregoing” Release, also surrendered “*any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement.*” *Id.* (emphasis added). The Defendants are “Released Parties” under the terms of the Release. (*Id.* ¶ 7.)

3. All of Plaintiff’s claims in this action, which he asserts as a shareholder of SCI, arise from a merger agreement approved by the SCI Board of Directors at the recommendation of an independent Special Committee of the SCI Board of Directors on August 29, 2006 (*id.* ¶ 46) – well before Plaintiff executed the Release.

4. Under controlling law, all of Plaintiff’s claims accrued and arose on or before August 29, 2006. As a result, they have been released and are legally barred.

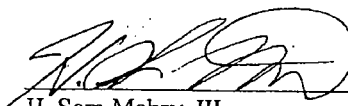
5. Furthermore, because Plaintiff has released his claims against the Defendants, he lacks standing to bring the class claims he purports to assert because he is an inadequate representative of the purported class.

6. As a result, Defendants are entitled to judgment on the pleadings, or alternatively, summary judgment. This Motion is dispositive as to all Causes of Action in Plaintiff’s Complaint.

This Motion is further based on the applicable statutory and common law, the Affidavit of Stephen B. Duerk, the Release attached to that Affidavit, the Memorandum that Defendants will file in support of this Motion, the papers and pleadings on file with the Court, and any argument at the hearing on this Motion.

Dated: June 6, 2008

Respectfully submitted,



H. Sam Mabry, III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square – 11th Floor
75 Beattie Place
Greenville, South Carolina 29601
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

OF COUNSEL:

George T. Manning
JONES DAY
2727 N. Harwood Street
Dallas, Texas 75201-1515
Telephone: (214) 220-3939
Facsimile: (214) 969-5100

Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Suite 800
Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

Counsel for Defendants WL Ross & Co.
LLC; Wilbur L. Ross, Jr.; Michael J.
Gibbons; David H. Storper; David L. Wax;
Joseph L. Gorga; Stephen B. Duerk; WLR
Recovery Fund III, L.P.; WLR Recovery
Fund III, L.P.; WLR Recovery Associates II
LLC; And WLR Recovery Associates III
LLC

STATE OF SOUTH CAROLINA)

COUNTY OF GREENVILLE)

Brian P. Menezes,)

Plaintiff,)

v.)

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, Stephen)
B. Duerk, WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P, WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC,)

Defendants.)

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, WLR)
Recovery Fund II, L.P., WLR Recovery)
Fund III, L.P, WLR Recovery Associates II)
LLC, and WLR Recovery Associates III)
LLC;)

Counterclaimants,)

v.)

Brian P. Menezes,)

Counterclaim Defendant.)

FILED
CLERK OF COURT
GREENVILLE CO. S.C.
JUN 6 2008

2008 JUN -6 P 2:24

AFFIDAVIT OF STEPHEN B. DUERK

I, Stephen B. Duerk, hereby state as follows:

1. I am over the age of 18 and reside in Greenville, South Carolina. I make this affidavit in support of Defendants' Motion for Judgment on the Pleadings or, Alternatively, Motion for Summary Judgment, and for all other purposes permitted by law. The facts contained in this affidavit are based upon my personal knowledge and my review of corporate records as

described herein. I suffer from no disability which would preclude me from giving the testimony herein and, if I were called upon to testify, I could and would competently do so.

2. I have worked for Safety Components International, Inc. ("SCI") or its predecessors since June 21, 1965 until my retirement at the end of last year (December 31, 2007). I served as SCI's President from June 9, 2006 to approximately October 20, 2006 when SCI merged with International Textile Group, Inc. Thereafter, I became President of the Automotive Safety Group of the combined company.

3. During my tenure at SCI, I worked with Brian P. Menezes and, over the years, grew familiar with his signature after seeing it regularly on correspondence and other corporate documents.

4. In July 2006, Mr. Menezes sued SCI and Joseph Gorga for employment related grievances arising from his separation from SCI. That lawsuit was resolved when the parties agreed to a settlement. Specifically, Mr. Menezes agreed to enter into a settlement and release in exchange for certain payments as part of that settlement.

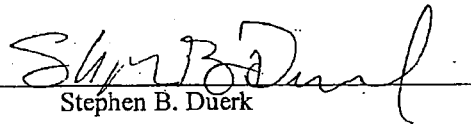
5. On or about September 29, 2006, I received the final version of the Confidential Settlement Agreement and Release of All Claims ("Settlement Agreement"), and signed it on behalf of SCI. Attached hereto as Exhibit A is a true and correct copy of the Settlement Agreement, which is signed by Mr. Menezes and dated September 28, 2006. I am familiar with Mr. Menezes' signature, and I swear and confirm that the first signature on Page 10 of the Settlement Agreement (Exhibit A to this Affidavit), which purports to be the signature of Mr. Menezes, is in fact the signature of Mr. Menezes. I also swear and confirm that the third signature on Page 10 of the Settlement Agreement (Exhibit A to this Affidavit) is my signature. After executing this Settlement Agreement, Mr. Menezes, by way of his attorney, dismissed his

lawsuit against SCI and Mr. Gorga pursuant to the terms of the Settlement Agreement. It is my understanding that SCI fully performed all of its obligations under the Settlement Agreement and made all of the monetary payments to Mr. Menezes and his lawyer required by the Settlement Agreement.

I declare under penalty of perjury under the laws of the State of South Carolina that the foregoing is true and correct.

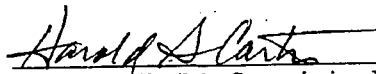
FURTHER AFFIANT SAYETH NOT.

June 5, 2008


Stephen B. Duerk

Subscribed and sworn to before me

this 5 day of June, 2008.


Notary Public (My Commission Expires 9-4-17)

**CONFIDENTIAL SETTLEMENT AGREEMENT
AND RELEASE OF ALL CLAIMS**

This CONFIDENTIAL SETTLEMENT AGREEMENT AND RELEASE OF ALL CLAIMS (hereinafter "Confidential Settlement Agreement") by and between **Brian P. Menezes**, a resident of Greenville, South Carolina (hereinafter "Plaintiff"), and his heirs, executors, administrators, successors and assigns, and **Safety Components International, Inc.**, a company with an office and place of doing business in Greenville, South Carolina (hereinafter "Safety Components" or "Employer"), its officers, directors, board members, shareholders, its affiliates and controlling persons (if any), employees, attorneys, insurers, representatives, bailees, agents, servants, heirs, executors, administrators, personal representatives, predecessors, successors, assigns, parent companies, subsidiaries, related companies, divisions, and the officers, directors, board members, shareholders, employees, bailees, agents and servants of their parent companies, subsidiaries, related companies, divisions, and affiliates, and all persons acting by, through, under, or in concert with any of them, and **Joseph L. Gorga**, a resident of Greensboro, North Carolina (hereinafter "Gorga"). Safety Components and Gorga may be identified collectively hereinafter as "Employer" solely for the purpose of identification in this document. Plaintiff, Safety Components, and Gorga may also be identified collectively hereinafter as the "Parties."

WITNESSETH:

WHEREAS, on or about July 6, 2006, Plaintiff filed a complaint entitled "*Brian P. Menezes, Plaintiff, vs. Safety Components International, Inc., and Joseph L. Gorga, Defendants*," bearing civil action no. 2006-CP-23-4236, in the South Carolina Court of Common Pleas for the Thirteenth Judicial Circuit, County of Greenville (hereinafter "the Underlying Lawsuit"), in which Plaintiff alleged, among other things, that the Defendants were liable for violation of the South Carolina Payment of Wages Act (S.C. Code Ann. § 41-10-10 et seq.) and breach of contract arising out of Plaintiff's employment with Safety Components and an "Employment Agreement" between Menezes and Safety Components, entered into on May 18, 2001, as subsequently amended (hereinafter "Employment Agreement"), and wrongful termination of Menezes' employment from Safety Components (hereinafter collectively "Plaintiff's Claims"), and seeking damages and a declaratory judgment on Plaintiff's Claims;

WHEREAS, Plaintiff also prepared an Amended Complaint incorporating Plaintiff's Claims against Employer, but which also contained additional allegations against International Textile Group, Inc., W.L. Ross & Co., LLC, and David Wax, a resident of the State of Connecticut, for, among others, tortious interference with contract and civil conspiracy (hereinafter collectively "Plaintiff's Amended Claims"), which Amended Complaint was not filed with any court or served upon Employer, International Textile Group, Inc., W.L. Ross & Co., LLC, or David Wax;

WHEREAS, the Parties have engaged in sufficient investigation upon which to evaluate the claims and potential defenses in the Underlying Lawsuit;

WHEREAS, Defendants deny and dispute Plaintiff's Claims and Plaintiff's Amended Claims, in whole or in part, and any liability therefore;



Exhibit A
Stephen R. Duerk
St. R. Duerk

Harold A. Carter

WHEREAS, the Parties have reached an agreement to resolve any and all claims arising out of Plaintiff's Claims and Plaintiff's Amended Claims, or any right to damages or a declaratory judgment, prior to Employer filing an Answer responding to Plaintiff's Claims or Plaintiff's Amended Claims;

WHEREAS, the Parties have agreed upon a compromise settlement and now wish to forever resolve, settle, compromise, and end any and all claims either or both may have against the another arising from Plaintiff's employment, and the termination thereof, and in the Underlying Lawsuit and as expressed in Plaintiff's Amended Claims;

WHEREAS, Plaintiff acknowledges that Employer has paid to him all wages earned, all unused vacation benefits accrued (if any), and all other amounts which may have been owed to him by Employer pursuant to the Employment Agreement or otherwise by Employer's policy, contract, or applicable law through the date of Plaintiff's termination, June 9, 2006 (hereinafter the "Termination Date"), less standard payroll withholding and any authorized deductions.

NOW, THEREFORE, in consideration of the mutual covenants contained herein and the exchange of other good and valuable consideration, the receipt and sufficiency of which are hereby expressly acknowledged, the Parties hereto agree to the following terms of settlement in full satisfaction, accord and settlement of all claims against one another:

1. **Payment by Employer to Plaintiff in Lieu of Severance Pay.** The Parties agree that subject to the expiration of the seven-day (7-day) revocation period (as described in Section 18 below) and receipt by Employer of an executed Stipulation of Dismissal with Prejudice of the Underlying Lawsuit, the Employer will pay to Plaintiff, in full satisfaction, accord, and settlement for any and all claims, and specifically for any claim for severance payments as contemplated pursuant to §7.4(b)(1) of the Employment Agreement, the amounts set forth below on the dates indicated:

- (a) A first payment on January 9, 2007, in the amount of Ninety Thousand Two Hundred Ten and no/100ths (\$90,210.00) Dollars (which takes into consideration the payments previously made by the Employer of Fifty Four Thousand Two Hundred Ten and no/100ths (\$54,210.00) Dollars).
- (b) A second payment on March 2, 2007 in the amount of One Hundred Forty-Four Thousand Four Hundred Twenty and no/100ths (\$144,420.00) Dollars.
- (c) A third and final payment on August 7, 2007 in the amount of One Hundred Forty-Four Thousand Four Hundred Twenty and no/100ths (\$144,420.00) Dollars.

Each of the aforementioned payments is to be paid minus all applicable withholdings as required by law.

2. **Payment by Employer to Plaintiff in Lieu of Change in Control Bonus.** The Parties dispute the right to any change in control bonus payment under the Employment Agreement, but agree that in full satisfaction, accord, and settlement for any claim, right or entitlement to any payment for a change in control bonus payments, whether pursuant to §7.4(b)(4) of the Employment Agreement, or from any other part of the Employment Agreement, or otherwise from any Released Party, Safety Components will pay to the Plaintiff the total sum of One Hundred Ninety Seven

Thousand Five Hundred and no/100ths (\$197,500.00) Dollars, again subject to the expiration of the seven-day (7-day) revocation period (as described in Section 18 below) and receipt by Employer of an executed Stipulation of Dismissal with Prejudice of the Underlying Lawsuit.

This sum shall be paid in three (3) separate payments of Sixty Five Thousand Eight Hundred Thirty Three and 33/100ths (\$65,833.33) Dollars, each of which is to be paid on or before January 9, 2007, March 2, 2007, and August 7, 2007, respectively, and from which shall be deducted all applicable withholdings as required by law. If applicable, the aforesaid payment, in compromise and settlement of any and all rights to any change in control bonus, shall be "grossed up" as provided in the Employment Agreement at Paragraph 10. Compliance with Internal Revenue Code §280G.

3. **Benefits.** All of Plaintiff's benefits, and any right thereto, shall be deemed terminated as of the Termination Date (other than, where applicable, health, dental, and vision insurance, which shall terminate effective as of the last day of the month in which Plaintiff was terminated) unless the terms of the benefit plans provide otherwise, or except to the extent inconsistent with the remainder of this paragraph. Employer shall provide at no expense to Plaintiff for a period of eighteen (18) months following the Termination Date continued health insurance coverage as in effect from time to time (but which shall include coverage under Execucare or a plan or program providing coverage substantially equivalent to that Plaintiff had immediately prior to the Termination Date) and, to the extent they continue to be eligible for such coverage under COBRA, his dependents who were covered by Employer's health insurance plan immediately prior to the Termination Date. Otherwise, Plaintiff acknowledges that Plaintiff shall not be entitled to any other or additional benefits, sums or amounts, including without limitation, any right to any bonus, vacation pay, sick pay, life insurance, disability income policies, car allowance, contributions for 401(k) or similar plans nor any other benefits, except for the payments of premiums for medical insurance set forth above, and except as otherwise provided in the benefit plans, or specifically identified in this Confidential Settlement Agreement. Plaintiff shall be entitled, at Plaintiff's sole expense to any COBRA benefits to which he may be entitled by law.

4. **Payment by Employer to Counsel for Plaintiff.** On Plaintiff's behalf, and at his request, the Parties agree that Employer will pay Plaintiff's attorney, William D. Herlong, Esq., of Anderson & Herlong, L.L.C., the sum of Seven Thousand Five Hundred and no/100ths (\$7,500.00) Dollars, payable pursuant to a Form 1099. Plaintiff's attorneys agree to hold harmless and indemnify Employer for any liability for tax payments and filings for which Plaintiff's attorneys are responsible, if any.

5. **Nature of Consideration.** The mutual promises and sums described herein are acknowledged to be good and valuable consideration in full and final payment and accord and satisfaction of all claims by Plaintiff against Employer by virtue of his employment, the Employment Agreement, or otherwise.

6. **Dismissal of the Underlying Lawsuit.** The Parties hereby agree to direct their respective counsel to dismiss the Underlying Lawsuit, and any and all claims, counterclaims, cross-claims, or related claims that have been or could have been asserted in the Underlying Lawsuit, with prejudice. The Underlying Lawsuit and any and all related claims, counterclaims, cross-claims, or related claims shall henceforth be res judicata.

7. **Releases by Plaintiff.** As a material inducement to Employer to enter into this Confidential Settlement Agreement, Plaintiff does hereby release, acquit and forever discharge Gorga and Safety Components, and any parent, subsidiary and affiliated person, company, business, entity or enterprise of Gorga and Safety Components, along with all current and former officers, directors, agents, employees, insurers, representatives, attorneys, successors, and assigns of the same, which shall also include by way of enumeration but not limitation, the International Textile Group, Inc., W. L. Ross & Co. L.L.C., and David L. Wax, a resident of the State of Connecticut (collectively, the "Released Parties"), from any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which Plaintiff either has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is Plaintiff's intention to release all rights and claims that he may lawfully release.

Without in any way limiting the generality of the foregoing, this Release applies to and waives: (1) any and all claims, causes of action, or rights, which Plaintiff has had or may now have under or pursuant to Title VII of the Civil Rights Act of 1964, as amended; Civil Rights Act of 1991; Title 42, United States Code, Section 1981; the Americans with Disabilities Act; the Age Discrimination In Employment Act, as amended, the Older Workers Benefit and Protection Act; and any other statute, rule, or executive order prohibiting discrimination in employment on the basis of age, disability, religion, national origin, sex, race, color, or veteran's status; (2) any and all claims, causes of action, or rights, which Plaintiff has had or may now have under or pursuant to the Employment Retirement Income Security Act; (3) any claims, causes of action, or rights which Plaintiff might have or has had for employment discrimination, unlawful employment practices, or relating in any way to his employment or termination thereof, and arising under local, state, or federal law; (4) any claims or causes of action which Plaintiff might have or have had for personal injuries; and (5) any claims or causes of action which Plaintiff might have or have had for breach of contract or based upon any agreement with the Released Parties, specifically including but not limited to the Employment Agreement; (6) any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement; (7) any claims or causes of action which Plaintiff might have or have had for defamation, tortious conduct and wrongful discharge and (8) all of Plaintiff's Claims, Plaintiff's Amended Claims and all claims made or which may have been made in the Underlying Lawsuit or Amended Complaint.

Additionally, without waiving any prospective or retrospective rights under the Family and Medical Leave Act ("FMLA"), Plaintiff admits that he has received from Employer all rights and benefits, if any, potentially due to him pursuant to the FMLA. Similarly, without waiving any prospective or retrospective rights under the Fair Labor Standards Act ("FLSA"), Plaintiff admits that he has received from Employer all salary, wages, or other compensation, if any, potentially due to him pursuant to the FLSA.

8. **Releases by Plaintiff - Additional Information.** Plaintiff specifically agrees that his release of claims identified in Section 7, above, is knowing and voluntary and that he has had sufficient opportunity to consult with his attorney to ensure that he understands the language used in this Confidential Settlement Agreement and the rights and obligations created herein and he had in fact consulted with his attorney regarding the same. Plaintiff understands, acknowledges, and voluntarily agrees that this Confidential Settlement Agreement, except as otherwise explicitly stated, is a total and

complete release by him of any and all claims which he has against Employer as of the effective date of this Confidential Settlement Agreement, both known or unknown, even though there may be facts or consequences of facts which are unknown to Plaintiff.

9. **Other Claims.** Plaintiff represents that besides the Underlying Lawsuit, he has not filed any other complaints, claims, or actions against the Released Parties with any state, federal, or local agency or court, or that if Plaintiff has, Plaintiff agrees to withdraw and dismiss with prejudice (or cause to be withdrawn and dismissed with prejudice) any such complaint, claim, action, or charge. Plaintiff acknowledges that he knows of no facts which may lead to or support any complaints, claims, actions, or charges against Employer in or through any state, federal, or local agency or court other than Plaintiff's Claims and/or Plaintiff Amended Claims as described hereinabove and asserted in the Underlying Lawsuit and/or described in the Amended Complaint, which are hereby released and forever settled.

10. **Status of "Employment Agreement."** Plaintiff further agrees that he and Safety Components entered into the Employment Agreement on May 18, 2001, which agreement was subsequently amended by the Parties on September 22, 2003. The Parties hereby agree that the prior Employment Agreement, including all amendments thereto, is hereby rescinded, terminated, cancelled, or otherwise null and void as of June 9, 2006, and the Parties shall be relieved of any obligations or liability thereunder, except with the sole exceptions addressed herein. While it is the Parties' intent to otherwise rescind the Employment Agreement, the following provisions contained in the Employment Agreement shall remain in full force and effect and are incorporated herein by reference:

- Sec. 8. Confidential Information, Inventions (including §§ 8.1 - 8.5); and
- Sec. 9. Non-Competition, Non-Solicitation (including §§ 9.1 - 9.5).

Plaintiff agrees and understands that, notwithstanding the provisions contained in Paragraph 24 herein, the foregoing provisions contained in the Employment Agreement, and amendments thereto, shall remain in full force and effect despite the execution and terms of this Confidential Settlement Agreement, are subject to separate valid consideration previously paid by Employer to Plaintiff, and are subject to enforcement pursuant to the original terms of the Employment Agreement.

11. **Releases by Employer.** As a material inducement to Plaintiff to enter into this Confidential Settlement Agreement, Employer hereby releases, acquits, and forever discharges Plaintiff from any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which the Employer either has had or now has against Plaintiff for or related to any matter or thing, whatsoever, from the beginning of time up to and including the date of execution hereof, except for the provisions in the Employment Agreement enumerated and described above in Section 10 entitled "Status of Employment Agreement", and with regard to that provision, only any existing claims predating the execution of this agreement are released. Other than the provisions set forth in Section 10, above, it is the Employer's intention to release all rights and claims that the Employer may lawfully release.

12. **Non-Disparagement.** The Parties agree that they will not publicly criticize or disparage the each other, or privately criticize or disparage each other in a manner intended or reasonably calculated to result in public embarrassment to, or injury to the business or reputation of the Parties. Employer shall take reasonable efforts to ensure that David Wax and the executive officers of International Textile Group, Inc., and W.L. Ross & Co., LLC, comply with this provision as if each was Employer.

13. **Cooperation.** Plaintiff agrees that for a period of one year he will provide such cooperation, information or reasonable assistance that the Released Parties (as defined above) may reasonably request of him upon reasonable prior notice, including making himself available to be a witness in judicial or other legal proceedings, with respect to any matters that he may have been familiar with or responsible for during his tenure with the Employer. The Employer will reimburse all related and reasonable expenses and shall compensate Plaintiff at the rate of Two Hundred and No/100ths (\$200.00) Dollars per hour, with a minimum of four (4) hours, per request for such future services.

14. **Resignation From Offices.** Plaintiff confirms that effective June 9, 2006, he ceased to be employed with Safety Components and that he does resign from all offices and positions with Safety Components, including (a) from all offices of Safety Components to which he has been elected by the Board of Directors of Safety Components or any Released Party (or to which he has otherwise been appointed), (b) from all directorships or offices of any entity that is a subsidiary of, or is otherwise related to or affiliated with, Safety Components or any Released Party, (c) from all administrative, fiduciary or other positions he may hold with respect to arrangements or plans for, of or relating to Safety Components or any Released Party, and (d) from any other directorship, office, or position of or with any corporation, partnership, joint venture, trusts of any other enterprise (each, an "Other Entity") insofar as Plaintiff is serving in the directorship, office or position of the Other Entity at the request of Safety Components or any Released Party.

15. **Future Employment.** Plaintiff agrees that Employer is not obligated to offer employment to Plaintiff (or to accept services or the performance of work from Plaintiff directly or indirectly) now or in the future. Plaintiff agrees not to seek or accept employment or any direct independent contractor relationship with the Released Parties, as defined herein, now or at any time in the future. Plaintiff agrees that in the event such employment or other relationship occurs in the future, this provision shall serve as good and just cause for termination of same. Plaintiff knowingly and voluntarily waives all rights, if any, he may have under federal and/or state law to re-hire by, or reinstatement of employment with, Employer. This provision does not apply to the extent Plaintiff is an employee or independent contractor with a company that is acquired by a Released Party. Further, this provision is void after five (5) years.

16. **Non-Admission.** The Parties agree and understand that this Confidential Settlement Agreement is a compromise of disputed claims and shall not in any way be construed as an admission by any of the Parties or Released Parties that it has acted wrongfully with respect to any other Party or Released Party or any other person, which is expressly denied, or that they have any rights whatsoever against each other. The Parties further agree that Employer and the Released Parties specifically disclaim any liability to or alleged wrongful acts against Plaintiff or any other person, on the part of itself, its affiliates, and their respective representatives, officers, employees, attorneys, and agents.

17. **Confidentiality and Breaches.** Except as required to comply with legal disclosure

requirements (e.g., subpoenas) or as otherwise required or protected by law or otherwise allowed in this paragraph, the Plaintiff represents and agrees that he will keep the terms, and amount of this Confidential Settlement Agreement completely confidential and he has not disclosed and will not disclose any information regarding this Confidential Settlement Agreement (or discussions preceding this Confidential Settlement Agreement) to anyone other than his attorneys, tax advisors, financial advisors, his spouses and/or other individuals who have a reasonable need to know and who have been approved in writing to receive such information by Employer. The Plaintiff agrees that he will not describe this Confidential Settlement Agreement or the settlement of his Claims in any way (e.g., substantial/insubstantial, generous/parsimonious, large/small, fair/unfair, etc.). The Plaintiff may discuss this Confidential Settlement Agreement with his attorneys, tax advisors, financial advisors, his spouses and/or other individuals who have a reasonable need to know and have been approved to receive such information by Employer, but Plaintiff will inform them of these confidentiality provisions, and will remain responsible for any further disclosures that may result. The Plaintiff agrees that the unauthorized disclosure of the terms or amount of this Confidential Settlement Agreement is a material breach of this Confidential Settlement Agreement. In the event there is a breach of this Confidential Settlement Agreement, the remaining provisions of this Settlement Agreement shall remain in full force and effect for the benefit of the Employer. The Parties and the Released Parties will limit their public disclosure of this settlement to a simple statement that the matter has been resolved on confidential terms.

18. Acknowledgment.

(a) The release set forth herein includes a waiver of rights and claims which Plaintiff may have arising under the Age Discrimination in Employment Act of 1967 (Title 29, United States Code, Sections 621, *et seq.*) ("ADEA"). Plaintiff is advised to consult with his attorney regarding his waiver of rights and claims under the ADEA. Plaintiff understands that by signing this release, he waives his rights or claims under the ADEA. Plaintiff further understands that he is not waiving rights or claims under that ADEA that may arise after the effective date of this fully executed Confidential Settlement Agreement.

(b) Plaintiff agrees that he has been advised to consult with an attorney prior to executing this Confidential Settlement Agreement. Plaintiff acknowledges that he has had the opportunity to consult with an attorney to review this agreement, prior to signing, and that he has in fact done so. Plaintiff acknowledges that his attorney has fully explained in a manner understood by him the waiver of any rights or claims contained in this Confidential Settlement Agreement.

(c) Plaintiff certifies that he has been given a period of up to twenty-one (21) days to study this Confidential Settlement Agreement, and to consult with an attorney, accountant, or other advisor before signing the Confidential Settlement Agreement, and that the actual time he has taken for such purposes was adequate for all appropriate consultations.

(d) Plaintiff represents that he has read and thoroughly discussed all aspects of this Confidential Settlement Agreement with his attorney, understands its provisions, and understands that this Confidential Settlement Agreement establishes binding contractual rights. Plaintiff acknowledges that this Confidential Settlement Agreement and the release and waiver of claims contained herein are given knowingly and voluntarily.

(e) Plaintiff understands that this Confidential Settlement Agreement shall not be effective and enforceable until seven (7) days from the date he executes this Confidential Settlement Agreement. During this seven-day period, Plaintiff may change his mind and revoke this Confidential Settlement Agreement by notifying Employer, in writing, of his wish to revoke this Confidential Settlement Agreement. Any such revocation must be in the form of a signed, written statement delivered to Employer's counsel, *M. Baker Wyche, III, at Ogletree, Deakins, Nash, Smoak & Stewart, P.C., 300 N. Main Street, PO Box 2757, Greenville, SC 29602.*

19. **Waiver of Breach.** Either Party may waive or excuse the other's failure to perform any provision of this Confidential Settlement Agreement; provided, however, that any such waiver shall be in writing and shall not preclude the enforcement of this Confidential Settlement Agreement upon any subsequent breach, whether or not similar in character.

20. **Assignment.** This Confidential Settlement Agreement and the rights and obligations of Employer hereunder may be assigned by Employer and shall inure to the benefit of, shall be binding upon and shall be enforceable by any such assignee. This Confidential Settlement Agreement and the rights and obligations of Plaintiff hereunder may not be assigned by Plaintiff and, further, Plaintiff expressly states that he has not assigned any rights or obligations arising out of his employment with Employer, his separation therefrom, or pursuant to this Confidential Settlement Agreement.

21. **Successorship.** This Confidential Settlement Agreement shall be binding upon and inure to the benefit of Gorga and Safety Components and its affiliates, successors, and assigns, and, subject to Section 21 above, Plaintiff, his heirs, personal representatives, administrators, beneficiaries, and assigns. If Plaintiff should die while any amount would still be payable to him under this Confidential Settlement Agreement had Plaintiff continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Confidential Settlement Agreement to his devisee, legatee, or other designee or, if there is no such designee, to his estate.

22. **Non-Reliance.** Plaintiff represents and acknowledges that in executing this Confidential Settlement Agreement he does not rely, and has not relied, upon any representation or statement not set forth herein by Employer or any of Employer's agents, representatives, or attorneys.

23. **Entire Agreement.** Plaintiff further represents and acknowledges that this Confidential Settlement Agreement constitutes the entire agreement between the Parties. Except as stated otherwise herein, any oral or written representations, prior agreements, or understandings not reflected in this Confidential Settlement Agreement shall have no force or effect, and are superseded by this Confidential Settlement Agreement.

24. **Severability.** The terms of this Confidential Settlement Agreement, including paragraph subparts, are severable, and if any part or subpart is found to be unenforceable, the other terms shall remain in full force and effect and are valid and enforceable.

Likewise, the Parties expressly recognize that the obligations set forth in this Confidential Settlement Agreement are independent of one another, in that a breach of one provision does not extinguish any duties or rights set forth in other provisions of this Confidential Settlement Agreement.

25. **Interpretation.** The Parties agree that this Confidential Settlement Agreement shall be interpreted according to South Carolina law and shall not be construed against the drafters. In the event for any reason that any provision or portion of this Confidential Settlement Agreement shall be found to be void or invalid, then such provision or portion shall be deemed to be severable from the remaining provisions or portions of this Confidential Settlement Agreement, and it shall not affect the validity of the remaining provisions or portions, which provisions or portions shall be given full effect as if the void or invalid provision or portion had not been included herein.

26. **Modification.** This Confidential Settlement Agreement shall not be modified or amended except by an instrument in writing signed by Plaintiff and Employer.

27. **Cooperation in Drafting.** The Parties agree that they have cooperated in the drafting and preparation of this Confidential Settlement Agreement with the assistance of counsel. In any construction to be made of this Confidential Settlement Agreement, the same shall not be construed against either party but shall be viewed as each sharing an equal role in the negotiation and drafting of its terms.

28. **Legal Counsel.** Plaintiff agrees that he has been advised to seek the advice of legal counsel, and that he has had the opportunity to have legal counsel review this agreement, prior to signing.

29. **Governing Law, Jurisdiction, and Venue.** This Confidential Settlement Agreement has been entered into under and shall be governed by and construed in accordance with the laws of the State of South Carolina, without regard to its conflicts of laws provision. The parties agree that the Greenville County Court of Common Pleas or the Federal District Court for the District of South Carolina, Greenville Division, shall be the sole and exclusive jurisdiction and venue for all disputes between the Parties under this Confidential Settlement Agreement. Plaintiff hereby irrevocably consents to the jurisdiction and venue of these courts for adjudication of all disputes between the Parties under this Confidential Settlement Agreement. Plaintiff hereby waives any objections or defenses to jurisdiction or venue in any such proceeding before such court(s).

30. **Effective Date.** The terms of this Confidential Settlement Agreement shall become final and binding only upon the execution of this Confidential Settlement Agreement by both parties and upon the expiration of the seven (7) day revocation period discussed above.

* * * * *

IN WITNESS WHEREOF the Parties have caused this Confidential Settlement Agreement to be signed. By signing this agreement, the Parties warrant that they have read and understand each provision of this Confidential Settlement Agreement, that they voluntarily agree to and have signed the Confidential Settlement Agreement, that in so doing they are not relying upon any inducements, representations, agreements, or understandings other than as are set forth herein, and that they are acting with full advice of and explanation by their respective legal counsel.

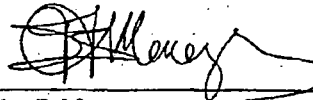
* * * * *

The Parties recognize and agree that this Confidential Settlement Agreement and Release may be signed and executed in one or more parts or counterparts and/or by facsimile signature. Each counterpart, including a signature page executed by each party, shall be an original counterpart of this Confidential Settlement Agreement and Release, but all such counterparts shall constitute one instrument.

WITNESSES:

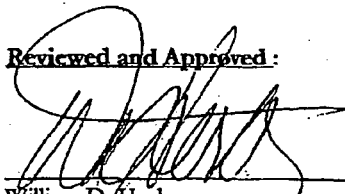
Janice Varat

Brian P. Menezes


Brian P. Menezes
Date: Sept 28th, 2006

Janice Varat

Reviewed and Approved:


William D. Herlong
Attorney for Plaintiff, Brian P. Menezes
Date: 9/28/2006

Safety Components International, Inc.

By: _____

Its: _____
Date: _____

* * * * *

The Parties recognize and agree that this Confidential Settlement Agreement and Release may be signed and executed in one or more parts or counterparts and/or by facsimile signature. Each counterpart, including a signature page executed by each party, shall be an original counterpart of this Confidential Settlement Agreement and Release, but all such counterparts shall constitute one instrument.

WITNESSES:

Brian P. Menezes

Janice Varat

[Signature]

Brian P. Menezes

Date:

Sept 28th, 2006

Reviewed and Approved:

Janice Varat

[Signature]

William D. Herlong,

Attorney for Plaintiff, Brian P. Menezes

Date:

9/28/2006

Safety Components International, Inc.

[Signature]
Brenda S. Suffer

By:

Steph B. Durr

Its:

President

Date:

Sept. 29, 2006

Joseph L. Gorga

Cheryl L. Hollis

Joseph L. Gorga
Joseph L. Gorga

Date: Sept. 29, 2006

4386701.1

STATE OF SOUTH CAROLINA

COUNTY OF GREENVILLE

Brian P. Menezes,

Plaintiff,

v.

WL Ross & Co. LLC, Wilbur L. Ross,
Jr., Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P, WLR
Recovery Associates II LLC, and WLR
Recovery Associates III LLC,

Defendants.

)
) IN THE COURT OF COMMON PLEAS

2008 JUL -2 P 4: 43

) C.A. No. 2008-CP-23-2701

)
) FILED-CLERK OF COURT
) GREENVILLE CO. S.C.
)

) **Plaintiff's Motion to**
) **Dismiss Counterclaim**

Defendants' Counterclaim is based on a mutual non-disparagement provision in a settlement agreement between the parties in a prior, different action. Defendants apparently contend that plaintiff violated that provision (and disparaged defendants) by filing the Complaint in this case. (See Counterclaim, Para. 181-85.)

Even if the allegations of the Counterclaim were taken as true, the Counterclaim fails to state a claim and should be dismissed. Under South Carolina law, pleadings are absolutely privileged. See Pond Place Partners, Inc. v. Poole, 351 S.C. 1, 23, 567 S.E.2d 881, 893 (Ct. App. 2002):

South Carolina has long recognized that relevant pleadings, even if defamatory, are absolutely privileged. McKesson & Robbins v. Newsome, 206 S.C. 269, 33 S.E.2d 585 (1945); Texas Co. v. C.W. Brewer & Co., 180 S.C. 325, 185 S.E. 623 (1936); Rodgers v. Wise, 193 S.C. 5, 7 S.E.2d 517 (1940); Sanders v. Rollinson, 33 S.C. Law (2 Strob.) 447 (1848) (stating an action for slander based on a defamatory affidavit was a non-suit; the proper attack is under malicious prosecution); accord Lone v. Brown, 199 N.J. Super. 420, 489 A.2d 1192, 1195 (App.Div.1985) ("It is well established that statements, written or oral, made by judges, attorneys, witnesses, parties or jurors in the course of judicial

proceedings, which have some relation thereto, are absolutely privileged from slander or defamation actions, even if the statements are made with malice.”); Kropp v. Prather, 526 S.W.2d 283, 286 (Tex.Civ.App.1975) (“Any communication, oral or written, uttered *24 or published in the due course of a judicial proceeding is absolutely privileged and cannot form the basis for a cause of action in libel or slander.”).

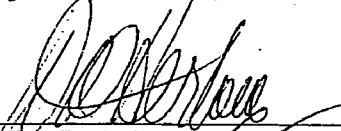
This is true as well of allegations with the body of a complaint itself. See McKesson & Robbins, Inc. v. Newsome, 206 S.C. 269, 33 S.E.2d 585 (S.C. 1945). There, the defendant lodged a counterclaim for defamation that, like the claim of disparagement here, claimed the allegations of the Complaint itself as its basis. The plaintiff moved to dismiss on the grounds that “the alleged acts of the plaintiff therein, even if defamatory as alleged, are absolutely privileged in law and cannot constitute a defense.” The South Carolina Supreme Court affirmed. As the Court wrote:

Liberally interpreted, there are allegations in the complaint which are relevant to [the defendant’s] liability for the alleged indebtedness Therefore, it was correctly held that the statements contained in the complaint were privileged and could not furnish a defense, or the basis for an action in libel.

Id., 206 S.C. at __, 33 S.E.2d at 587.

Because it is impossible to commit disparagement through pleadings and allegations relevant to the points at issue in an action, the Counterclaim is without legal foundation and fails to state a claim.¹ Accordingly, it should be dismissed.

Respectfully submitted,


William D. Herlong
SC Bar No. 14283
ANDERSON & HERLONG, LLC
111 E. North Street [Zip 29601]
P.O. Box 2105
Greenville, SC 29602-2105
Tel. (864) 255-9255
Fax (864) 752-0820
william@ahlf.us

Attorneys for Brian Menezes

July 2, 2008.

¹ South Carolina is not unique in this regard. The South Carolina Court of Appeals includes an extensive discussion of the law in other states in the Pond Place opinion referenced above. See 351 S.C. at 25-31, 567 S.E.2d at 893-97.

7/28/08

STATE OF SOUTH CAROLINA)

COUNTY OF GREENVILLE)

Brian P. Menezes,)

Plaintiff,)

v.)

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, Stephen)
B. Duerk, WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P, WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC,)

Defendants.)

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

FILED-CLERK OF COURT
GREENVILLE CO S.C.
PAUL B. WICKENS-IR

2008 JUL 28 P 1:23

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga,)
WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P, WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC;)

Counterclaimants,)

v.)

Brian P. Menezes,)

Counterclaim Defendant.)

**MEMORANDUM IN SUPPORT OF MOTION FOR JUDGMENT ON THE
PLEADINGS OR, ALTERNATIVELY, MOTION FOR SUMMARY JUDGMENT**

This matter is before the Court on the Motion of Defendants WL Ross & Co. LLC, Wilbur L. Ross, Jr., Michael J. Gibbons, David H. Storper, David L. Wax, Joseph L. Gorga, Stephen B. Duerk, WLR Recovery Fund II, L.P., WLR Recovery Fund III, L.P, WLR Recovery Associates II LLC, and WLR Recovery Associates III LLC (collectively, the "Defendants") for Judgment on the Pleadings Or, Alternatively, for Summary Judgment based on a Settlement

Agreement and Release of All Claims executed by Plaintiff on September 28, 2006.¹ This Motion is scheduled to be argued before the Court at 2:00 PM on Thursday, July 31, 2008. Defendants submit this Memorandum in support of their Motion.

PRELIMINARY STATEMENT

Defendants are entitled to judgment on the pleadings or, alternatively, summary judgment because, in exchange for \$576,550 and other valuable consideration, and with the advice of counsel, Plaintiff executed a Settlement Agreement and Release of All Claims in which he released the Defendants from all of the claims asserted in the present case as a matter of law. Plaintiff is a shareholder and the former Chief Financial Officer ("CFO") and former interim Chief Executive Officer ("CEO") of Safety Components International, Inc. ("SCI"), now known as International Textile Group, Inc. ("ITG"). On July 6, 2006 Plaintiff sued SCI in a lawsuit styled Menezes v. Safety Components International, Inc. and Joseph L. Gorga, Civil Action No. 2006-CP-23-4236, claiming that he was entitled to additional compensation. William Herlong, Plaintiff's counsel here, represented him in that prior action. The parties agreed to resolve that dispute through settlement. The resulting settlement agreement was the product of arms-length negotiations between Mr. Herlong, on behalf of the Plaintiff, and defense counsel on behalf of SCI.

This Motion involves a simple principle of law – a party cannot bring a lawsuit on a claim he has already voluntarily released for valuable consideration. In the Settlement Agreement and Release of All Claims, Plaintiff released Defendants not only from claims for compensation, but from "any and all manner of actions, causes of actions, suits [or]

¹ Consistent with Rule 12(c), SCRCP, and to the extent necessary for the Court to rule on this Motion, Defendants respectfully request the Court to treat this Motion as one for Summary Judgment pursuant to Rule 56 of the South Carolina Rules of Civil Procedure.

claims . . . whether known or unknown, for or related to any matter or thing from the beginning of time up to and including the date of execution" of the Release, including, but not limited to, "any claim based upon or as an owner of any stock or interest in any of the [Defendants] arising prior to the execution of . . ." the Release and "all claims made or which may have been made in" the original lawsuit. (Hereafter, the "Settlement Agreement and Release," at 4, ¶ 7, attached as Exhibit A to the Aff. of Stephen B. Duerk, filed June 6, 2008, attached hereto as Exhibit 1). Under Delaware law, which Plaintiff acknowledges in his Complaint controls in this case, all of the causes of action Plaintiff asserts in this case arose or accrued prior to the date of this Settlement Agreement and Release and are barred under that agreement. There can be no dispute of fact given that Defendants' arguments are based exclusively on the clear and unambiguous terms of the Settlement Agreement and Release, which Plaintiff's counsel negotiated, and facts alleged in Plaintiff's Complaint, which are admissions *in judicio*.

Defendants' Motion should be granted in its entirety and judgment should be entered as to all of Plaintiff's claims in favor of Defendants.

STATEMENT OF FACTS

Plaintiff seeks to recover damages on claims arising from the merger of the former International Textile Group, Inc. ("FITG") with a subsidiary of SCI. (Compl. ¶¶ 1-3.) Both companies were organized under the laws of the State of Delaware. At the time of the merger, Plaintiff was an SCI stockholder; however, he had also served as SCI's CFO from September 1999 to January 15, 2006, and then as interim CEO from January 16, 2006 until June 9, 2006. (*Id.* ¶ 4.) The crux of Plaintiff's claims is that SCI, in effect, paid merger consideration worth \$167 million in exchange for all outstanding stock of FITG, which Plaintiff contends was worth less than \$167 million. (*Id.* ¶¶ 29-33.) Accordingly, Plaintiff contends that the Exchange Ratio

which effectively set the price that SCI paid for FITG under the merger agreement, was inaccurate and unfair, resulting in the overpayment by SCI.² (*Id.* ¶¶ 34-39.)

Plaintiff alleges that the Exchange Ratio, “was agreed to on August 23, 2006, by [SCI Director] Dr. Daniel Tessori in his capacity as the SCI Special Committee appointed by the SCI Board with ‘exclusive authority’ on behalf of SCI to review, evaluate, investigate, negotiate and, if appropriate, approve the terms of any potential transaction between SCI and WLR, or any of its affiliates.’ (Prospectus, p. 46.).” (*Id.* ¶ 35) (emphasis added).³ Even though the SCI Special Committee received a fairness opinion regarding the Exchange Ratio from RSM EquiCo Capital Markets, LLC (“RSM”) (Compl. ¶ 42), Plaintiff claims the information supplied by FITG, on which the Special Committee and RSM relied regarding FITG’s value and business, “was inaccurate and deeply flawed.” (*Id.* ¶ 49.) Plaintiff further claims that WL Ross & Co. LLC (“WLR”), which Plaintiff contends was the controlling shareholder of both FITG and SCI (*id.* ¶¶ 7 & 9), and all the members of the SCI Board other than Tessori, were intimately familiar with the business of FITG (*id.* ¶ 48), and therefore breached their fiduciary duties to the minority shareholders (including Plaintiff) in connection with approving the merger agreement. The merger agreement was approved by the SCI Board at the recommendation of the SCI Special Committee on August 29, 2006. (*Id.* ¶ 46.) A press release announcing the terms of merger was issued on August 30, 2006, and a Form 8-K disclosing the terms of the merger agreement, including the Exchange Ratio, was filed on that same date.⁴ On September 1, 2006, a

² The Exchange Ratio established a conversion rate where for every 1.4739 shares of FITG surrendered, the FITG stockholder would receive 1 share of SCI stock.

³ Plaintiff has not joined Dr. Tessori, a New York resident, SCI Director, and the member of SCI’s Special Committee, or alleged that he breached any of his fiduciary duties.

⁴ While not critical to the resolution to this Motion, this fact demonstrates the extent to which merger-related events were occurring publicly before Plaintiff released his claims against Defendants. The fact that this filing was made with the Securities and Exchange Commission on August 30, 2006 is not subject to reasonable

Preliminary Joint Proxy Statement/Prospectus ("Proxy Statement") was publicly filed with the SEC, which included a detailed description of the background of, and reasons for, the proposed merger, the terms and conditions of the merger agreement and the transactions related thereto, the financial analyses performed by RSM, and the fairness opinion delivered by RSM to the SCI Special Committee.⁵

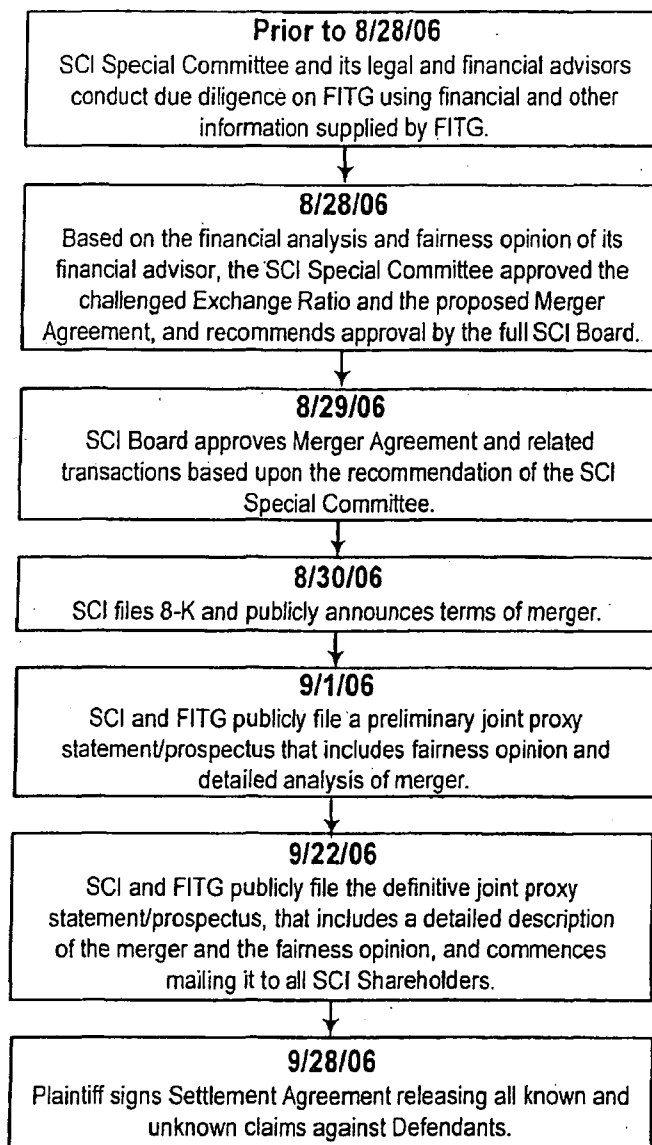
On September 28, 2006—approximately one month after the SCI Special Committee and the SCI Board approved the transaction he challenges here and after detailed public disclosure of the terms, conditions and background of the transaction was made by SCI – Plaintiff signed the Settlement Agreement and Release, which resolved a prior lawsuit between the parties that Plaintiff had filed in July 2006. The merger ultimately closed. (Compl. ¶ 89.)

In summary, the relevant timeline of events is as follows:

(continued...)

dispute and therefore can be judicially noticed pursuant to Rule of Evidence 201(b), SCRE, because it is "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned," such as www.sec.gov. See Richards v. City of Columbia, 227 S.C. 538, 557, 88 S.E.2d 683, 692 (1955) (court may take judicial notice of federal census figures); Massey v. War Emergency Coop. Ass'n, 209 S.C. 292, 304, 39 S.E.2d 907, 913 (1946) (court properly took judicial notice of Interstate Commerce Commission's rules and regulations); Lovelace v. Software Spectrum Inc., 78 F. 3d 1015, 1017-18 (5th Cir. 1996) (In ruling on motion to dismiss, district court may take judicial notice of the contents of documents filed with the Securities and Exchange Commission); Kramer v. Time Warner, Inc., 937 F.2d 767, 774 (2d Cir. 1991) (district court may take judicial notice of documents filed with Securities and Exchange Commission). Additionally, Plaintiff's Complaint concedes the public announcement of the merger occurred on August 30, 2006. Paragraph 4 of the Complaint describes August 29, 2006, as "the day before the announcement of the merger at issue here" and Paragraph 84 states "the day the merger was publicly announced, August 30, 2006...." Nevertheless, as demonstrated *infra*, the only dates critical to the outcome of this Motion are (i) August 29, 2006, the day the SCI board of directors approved the merger agreement and (ii) September 28, 2006, the day Plaintiff released all claims against the Defendants, both known and unknown.

⁵ As above, n.4. This fact also is not subject to reasonable dispute and can be judicially noticed. The Definitive Joint Proxy/Prospectus, filed on September 22, 2006, contained the same basic information and is cited or quoted in Plaintiff's Complaint at paragraphs 23, 28, 35, 45, 46, and 47.



Pursuant to the Settlement Agreement and Release, Plaintiff received payments totaling \$576,550 in exchange for, among other things, a broad release in favor of the Defendants. (Settlement Agreement and Release ¶¶ 1-2 & 7-8.) Nearly one and a half years later, Plaintiff filed this lawsuit alleging claims barred by the Settlement Agreement and Release. Before filing

suit, Plaintiff made no attempt to return the \$576,550 he received under the Settlement Agreement and Release, and therefore cannot void the release or avoid its effects.

ARGUMENT

A motion for judgment on the pleadings should be granted where, after taking the facts alleged in the Complaint as true, a plaintiff would still not be entitled to relief. Hambrick v. GMAC Mortgage Corp., 370 S.C. 118, 122, 634 S.E.2d 5, 7 (Ct. App. 2006); Rule 12(c), SCRCP. A motion for judgment on the pleadings may be treated as a motion for summary judgment if matters outside the pleadings are presented and not excluded by the Court. Rule 12(c), SCRCP. Summary judgment is appropriate where, as here, there is “no genuine issue of any material fact and the moving party is entitled to judgment as a matter of law.” Houck v. State Farm Fire & Cas. Ins. Co., 366 S.C. 7, 11, 620 S.E.2d 326, 329 (2005); see also Rule 56(c), SCRCP. Indeed, “[t]he purpose of summary judgment is to expedite disposition of cases which do not require the services of a fact finder.” George v. Fabri, 345 S.C. 440, 452, 548 S.E.2d 868, 874 (2001). Summary judgment is “completely appropriate when a properly supported motion sets forth facts that remain undisputed or are contested in a deficient manner.” David v. McLeod Reg'l Med. Ctr., 367 S.C. 242, 250, 626 S.E.2d 1, 5 (2006).

Where a plaintiff has released his claims against a defendant, the defendant is entitled to judgment as a matter of law. See, e.g., S. Glass & Plastics, Co. v. Duke, 367 S.C. 421, 427-29, 626 S.E.2d 19, 22-23 (Ct. App. 2005) (reversing summary judgment in favor of Plaintiff and awarding summary judgment to Defendant where claims had been released); Bowers v. S. C. Dep't of Transp., 360 S.C. 149, 153-54, 600 S.E.2d 543, 545-46 (Ct. App. 2004) (affirming summary judgment where nonparty to release was entitled to enforce it because its plain terms

were general and all encompassing in scope and it intended to release all claims that arose against the nonparty).⁶

A release is a specific type of contract governed by the same principles of interpretation as other contracts. Wilson Group, Inc. v. Quorum Health Res., Inc., 880 F. Supp. 416, 425 (D.S.C. 1995); Abu-Shawareb v. S.C. State Univ., 364 S.C. 358, 363, 613 S.E.2d 757, 760 (Ct. App. 2005). In M & M Group, Inc. v. Holmes, Op. No. 4427 (S.C. Ct. App. filed July 15, 2008) (Shearouse Adv. Sh. No. 30 at 29) (attached as Exhibit 3), the South Carolina Court of Appeals recently discussed the principles applicable to contract construction in affirming the grant of summary judgment to a defendant on the meaning of a written contract. The court stated that, “[t]o discover the intention of a contract, the court must first look to its language – if the language is perfectly plain and capable of legal construction, it alone determines the document’s force and effect.” Id. at 35 (citations omitted). The court further stated that the “[p]arties are governed by their outward expressions and the court is not free to consider their secret intentions.” Id. According to the court, “[w]hen a contract is clear and unambiguous, the construction of the contract is a question of law for the court.” Id. (citations omitted). Similarly, the question of whether a release is unambiguous is a matter of law for the court to decide. Wilson Group, Inc., 880 F. Supp. at 425 (citing Campbell v. Bi-Lo, Inc., 301 S.C. 448, 392 S.E.2d 477 (Ct. App. 1990)).

As shown below, Plaintiff has released all of his claims against Defendants brought in this action. Moreover, because Plaintiff did not return the \$576,550 in consideration he received under the Settlement Agreement and Release before filing this action, he cannot attempt to void

⁶ South Carolina courts have a strong policy of enforcing settlement agreements to avoid costly litigation and to fulfill the settling parties’ intentions. Bowers, 360 S.C. at 153-155, 600 S.E.2d at 545-46; Fowler v. Hunter, Op. No. 4422 (S.C. Ct. App. filed July 8, 2008) (Shearouse Adv. Sh. No. 29 at 86-87) (attached as Exhibit 2).

the release or escape its effect. See, e.g., Dunaway v. United Ins. Co. of Am., 239 S.C. 407, 410, 123 S.E.2d 353, 354 (1962) (holding “one who seeks to avoid the effect of a release must first return or tender the consideration paid therefor”); Taylor v. Palmetto State Life Ins., 196 S.C. 195, 200, 12 S.E.2d 708, 710 (1940) (consideration received for release must be returned before action can be instituted); Gray v. Petroseed Co., 985 F. Supp. 625, 629 (D.S.C. 1996) (same).

For these reasons, and those that follow, Defendants’ motion should be granted.

I. Plaintiff’s Merger-Related Claims Fail As A Matter Of Law Because Plaintiff Released Those Claims Against Defendants Prior To Bringing This Action.

On September 28, 2006, Plaintiff executed the Settlement Agreement and Release, which resolved a prior lawsuit he brought. The document itself is titled and captioned on each page “Settlement Agreement and Release of All Claims.” The scope of the release is extensive:

[A]ny and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which Plaintiff either has now or has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is Plaintiff’s intention to release all rights and claims that he may lawfully release.

(Settlement Agreement and Release ¶ 7) (emphasis added). Notably, Plaintiff, “[w]ithout in any way limiting the generality of the foregoing” release, also surrendered “*any claim based upon or as an owner of any stock or interest* in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement.” Id. (emphasis added). Plaintiff had the assistance of legal counsel (id. ¶ 28) when he expressly released all “known and unknown” claims he “has now or has had or now has,” including, but not limited to, “all of Plaintiff’s Claims, Plaintiff’s Amended Claims and all claims made or which may have been made in the Underlying Lawsuit or Amended Complaint.” (Id. ¶ 7.)

Plaintiff also broadly released related third parties. The Settlement Agreement and Release identified the "Released Parties" as:

Gorga and [SCI], and any parent, subsidiary, and affiliated person, company, business, entity or enterprise of Gorga and [SCI], along with all current and former officers, directors, agents, employees, insurers, representatives, attorneys, successors, and assigns of the same, which shall also include by way of enumeration but not limitation, the International Textile Group, Inc., W.L. Ross & Co. L.L.C. and David L. Wax.

(Id. ¶ 7.) Plaintiff's Complaint confirms that all Defendants are "Released Parties" under the Settlement Agreement and Release. More specifically, Plaintiff released Defendants W.L. Ross & Co. L.L.C. ("WLR"), David Wax, and Joseph Gorga by name. Id. Defendants Ross, Gibbons, Storper and Duerk were all current or former officers or directors of SCI. See Compl., ¶¶ 12-13. Defendants WLR Recovery Fund II, L.P., WLR Recovery Fund III, L.P., WLR Recovery Associates II, L.L.C., and WLR Recovery Associates III, L.L.C. (collectively, the "Recovery Entities") were affiliated entities of SCI, all of which shared voting and dispositive power over the shares of SCI, and through which WLR allegedly controlled SCI. (Id. ¶¶ 17-19.) Indeed, Plaintiff's Complaint treats WLR and the Recovery Entities as one in the same, (id.), and all Defendants are within the ambit of the release provision.

On August 29, 2006 – exactly one month before Plaintiff executed the Settlement Agreement and Release – the allegedly unfair merger terms at issue were established. See Compl. ¶ 29. The next day the merger was publicly announced, disclosing the exchange ratio to be used to convert the ITG stock into SCI stock, (id. ¶¶ 4 & 35), and on September 1, 2006, a preliminary Proxy Statement/Prospectus for the Merger was filed with the SEC. As such, and as set forth below, Plaintiff released any and all claims against Defendants related to the merger when he executed the Settlement Agreement and Release.

A. Plaintiff's Claim Against Defendants Arose and Accrued When the SCI Board Approved the Merger Agreement Within the Timeframe Covered by the Settlement Agreement and Release.

The sole issue is whether the claims asserted by Plaintiff in the current Complaint existed at the time the Plaintiff executed the Settlement Agreement and Release on September 28, 2006. The question of when a cause of action arises or accrues is a question of law for the court. See Stephens v. Draffin, 327 S.C. 1, 5, 488 S.E.2d 307, 309 (1997) (Supreme Court determines when cause of action arose as a matter of law); Brown v. Finger, 240 S.C. 102, 111-12, 124 S.E.2d 781, 785, 86 (1962) (court determines when claim for loss consortium accrues as a matter of law). Plaintiff's claims concern the fiduciary duties of officers, directors and controlling shareholders of a Delaware corporation, and thus are claims under Delaware law – a point that Plaintiff concedes in his Complaint and one that is consistent with South Carolina's traditional choice of law rules. See Compl. ¶ 96;⁷ Charleston Cty. Sch. Dist. v. Laidlaw Transit, Inc., 348 S.C. 420, 425, 559 S.E.2d 362 (Ct. App. 2001) (holding "allegations, statements, or admissions contained in a pleading are conclusive against the pleader, and a party cannot subsequently take a contrary or inconsistent position"); Restatement of Conflicts of Laws § 187 (1934) ("the existence and extent of the liability of shareholders, officers, or directors of a corporation ... is determined by the law of the state of incorporation").⁸ As shown below, under Delaware law, all of Plaintiff's claims accrued and arose as a matter of law before September 28, 2006 – the date of the execution of his Settlement Agreement and Release – and thus all of his claims are barred as a matter of law.

⁷ See also Compl. ¶ 97 (Plaintiff alleging that "WLR and Ross were the controlling shareholder of SCI and, under Delaware law, had fiduciary duties . . . to the minority stockholders of SCI including Plaintiff") (emphasis added); Compl. ¶ 98 (Plaintiff alleging that "WLR and Ross were self-interested in the transactions and acts at issue. Accordingly, the 'entire fairness' standard is applicable under Delaware law.").

⁸ The traditional choice of law rules followed in South Carolina are stated in the Restatement of Conflicts of Laws. See McDaniel v. McDaniel, 243 S.C. 286, 292, 133 S.E.2d 809, 813 (1963).

A cause of action for breach of fiduciary duty accrues "at the time of the wrongful act, even if the plaintiff is ignorant of the cause of action." Wal-Mart Stores, Inc. v. AIG Life Ins. Co., 860 A.2d 312, 319 (Del. 2004) (attached as Exhibit 4). This remains true even if the harmful effects of the act are not felt by plaintiff until long after the wrongful act occurred. In re Coca-Cola Enters., Inc. S'holder Litig., C.A. No. 1927-CC, 2007 WL 3122370, at *5 (Del. Ch. Oct. 17, 2007) (attached as Exhibit 5).

Where, as here, a shareholder's lawsuit arises from the terms of a merger agreement, the claim arises or accrues when the board passes the "resolution approving the merger on terms" the plaintiff feels are unfair. Brown v. Automated Mktg. Sys., Inc., No. 6715, 1982 WL 8782, at *2 (Del. Ch. Mar. 22, 1982) (attached as Exhibit 6). The fact that the merger technically closes at a later date is immaterial to when the claim arises or accrues:

[I]t is not the merger itself that constitutes the wrongful act of which plaintiff complains, but rather it is the fixing of the terms of the transaction which will be finalized by the consummation of the merger which provides the foundation for the suit. *So viewed, there is no continuing wrong but only an alleged wrong which occurred [when the board approved the terms of the merger].*

Id. (emphasis added); see also In re Beatrice Cos., Inc. Litig., 522 A.2d 865, 1987 WL 36708, at *3 (Del. Mar. 24, 1987) (holding that when a merger is challenged, the claim arises, and hence the plaintiff has standing to sue, "at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged.") (attached as Exhibit 7). Indeed, as soon as the SCI board approved the merger agreement, Plaintiff had standing to sue to rescind the agreement or enjoin the merger. See Kahn v. Seaboard Corp., 625 A.2d 269, 271 (Del. Ch. 1993) ("Suit could have been brought immediately [after the board approved the challenged contract] to rescind the contract and for nominal damages") (attached as Exhibit 8); In re SunGard Data Sys., Inc. S'holder Litig., C.A. No. 1221-N, 2005 WL 1653975, at *2 (Del. Ch. July 8, 2005) (noting that the "optimal

time" to bring a claim challenging a merger transaction is before the transaction closes) (attached as Exhibit 9).

Moreover, the fact that plaintiff may have been purportedly unaware of the gravity of the alleged wrongdoing until sometime after the terms of the merger were approved by the board is inconsequential to when the claim for breach of fiduciary duty arose and accrued under Delaware law. As the Delaware Chancery Court explained in Brown, where the plaintiff sued for breach of fiduciary duty over a merger whose terms she deemed unfair, just like Plaintiff Menezes does here: "[T]here is no merit in her contention that because she was unaware of the gravity of the alleged wrongdoings until such time as she received the proxy statement, her right to sue should be measured from that point rather than from the time of her purchase. Nor can there be an argument that no wrong occurs until the merger is voted upon and approved." Brown, 1982 WL 8782, at *2; see also Omnicare, Inc. v. NCS Healthcare, Inc., 809 A.2d 1163, 1169 (Del. Ch. 2002) (claim for breach of fiduciary duties arose when the directors decided to approve the merger, not when plaintiff became aware of the merger or the alleged wrongdoing) (attached as Exhibit 10); Stephens, 327 S.C. at 5, 488 S.E.2d at 309 (holding that "cause of action accrues at the moment when the plaintiff has a legal right to sue on it").

Here, all of Plaintiff's claims stem from the terms of the merger agreement, specifically the Exchange Ratio, which Plaintiff argues was unfair. According to Plaintiff's own Complaint, the Exchange Ratio was agreed to by the SCI Special Committee on August 28, 2006 (Compl. ¶ 35; Prospectus). Fisher v. S.C. Dep't of Health & Envtl. Control, 309 S.C. 10, 12, 419 S.E.2d 794, 795 (Ct. App. 1992) (plaintiff "judicially bound" by statements contained in her complaint). The allegedly wrongful acts of providing the SCI Special Committee "inaccurate and deeply flawed" financial information about ITG, which was used to arrive at the Exchange Ratio,

necessarily occurred before then. The approval of the merger agreement by SCI's Board admittedly occurred on August 29, 2006 (Compl. ¶ 46). Under Delaware law, this approval by the Board is the allegedly wrongful act that determined when the Plaintiff's claims arose or accrued. Brown, 1982 WL 8782, at *2. But Plaintiff executed the Settlement Agreement and Release, which released all claims, on September 28, 2006 – well after these claims arose and accrued. Therefore, Plaintiff has released his claims against the Defendants under the unambiguous terms of the Settlement Agreement and Release. In fact, because the claims asserted by Plaintiff in this case arose at least a month before the Settlement Agreement and Release was executed on September 28, Plaintiff's claims are expressly released by subparagraph (6) of the "Releases by Plaintiff" as "any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this confidential Settlement Agreement." Moreover, since Kahn and In re SunGard Data Sys., *supra*, clearly hold that the Plaintiff's right to sue here arose when the merger agreement was approved on August 29, 2006, the claims asserted in the Complaint here are barred by subparagraph (8) because they "may have been made in the Underlying Lawsuit" when the Settlement Agreement and Release was executed on September 28, 2006. See subparagraph (8), Settlement Agreement and Release at 4, ¶ 7.

II. The Alleged Post-Merger Agreement Conduct Does Not Change The Fact That Plaintiff's Claim Arose And Accrued When the Board Approved The Merger Agreement, And Thus Have Been Released.

Plaintiff's Complaint repeatedly attempts to characterize the merger as occurring in October 2006, when the merger was closed. Delaware law, however, is clear that acts in connection with the merger or in performance of the merger agreement occurring after it is approved by the board do not give rise to new causes of action or constitute some kind of "continuing wrong." See Kahn, 625 A.2d at 271 (rejecting that board members' "performance of

a [challenged] contract” constituted a “continuing wrong”; rather the claim accrued, and hence the wrong occurred, when the board approved the contract); In re Coca-Cola Enters., Inc., 2007 WL 3122370, at *5-6. Indeed, in Coca-Cola Enterprises, the Chancery Court held that the plaintiffs’ claims for breach of fiduciary duty against directors over challenged corporate actions taken from 2002 to 2005 under certain licensing agreements accrued at the moment the board approved those agreements in 1986. In reaching its conclusion, the court cited the well-settled rule that “[u]nder Delaware law, a plaintiff’s cause of action accrues at the moment of the wrongful act – not when the harmful effects of the act are felt – even if the plaintiff is unaware of the wrong.” Id. at *5. Furthermore, because the board’s actions in 2002 through 2005 each hinged upon and related to the terms and conditions of the licensing agreements, which were allegedly unfair to plaintiffs, they did not constitute “continuing wrongs,” but rather arose from the allegedly wrongful act of entering into the licensing agreements. Id. at *6. Thus, the allegedly “wrongful act” for accrual purposes was the board’s original approval of the agreements’ terms. Id. Other courts applying Delaware law to breach of fiduciary duty claims have affirmed this principle where the claim arose from the terms of a contract that plaintiff deemed was unfair:

Here, as in *Kahn [v. Seaboard Corp.]*, the plaintiffs’ breach of fiduciary duty claim hinges upon the allegations that the terms and conditions established by a contract are unfair to the plaintiff corporation. Accordingly, the court finds that here, as in *Kahn*, the cause of action accrued when the contract fixed the parties’ rights (in 1993) and not when an allegedly harmful legal obligation arose under the contract (in 1997). This finding is consonant with the principal that in discerning when a cause of action accrues, ‘the determinative issue is when the specific acts of alleged wrongdoing occurred, and not when their effect is felt.’ Ernest L. Folk, III, *et al.*, *Folk on Delaware General Corporation Law* § 327.3 (4th ed.).

In re Marvel Entm’t Group, Inc., 273 B.R. 58, 74 (D. Del. 2002) (attached as Exhibit 11).

Accordingly, the fact that Plaintiff's Complaint identifies alleged acts taken by the Defendants under the Merger Agreement, such as allowing the merger to close (Compl. ¶ 68), do not constitute "continuing wrongs" that take the accrual of Plaintiff's claim outside the time period covered by the Settlement Agreement and Release. Nor do allegations of harm or "negative consequences" occurring as a result of the merger alter the analysis. (See Compl. ¶ 82, under the heading "Further Negative Consequences of the Merger," alleging that "but for the Merger, [the] new credit facility and debt for equity swap," which diluted SCI's minority shareholders, "would not have taken place"); see also Stephens, 327 S.C. at 5, 488 S.E.2d at 309 (holding "fact that substantial damages did not occur until later is immaterial to determining when the action accrued or arose"). The fact remains that the allegedly wrongful act that caused Plaintiff's claims to arise and accrue under Delaware law was the Board's approval of the terms of the merger agreement – an event that Plaintiff's Complaint admits occurred within the scope of Plaintiff's release. It is irrelevant that the Defendants continued to perform under the Merger Agreement or that Plaintiff allegedly suffered harmful effects at some later time. Kahn, 625 A.2d at 271; In re Coca-Cola Enters., Inc., 2007 WL 3122370, at *6; In re Marvel Entm't Group, Inc., 273 B.R. at 74; see also Gecy v. Prudential Ins. Co. of Am., 273 S.C. 437, 440, 441-42, 257 S.E.2d 709, 711-12 (1979) (holding released party entitled to summary judgment in a lawsuit for injuries unknown at the time the release was executed where the express terms of the release was executed with a lawyer involved for the plaintiff).

In sum, because all of Plaintiff's claims arose or accrued within the time frame covered by the Settlement Agreement and Release, Plaintiff has released Defendants from the claims

asserted and is barred from bringing them here.⁹ Accordingly, Plaintiff's Complaint should be dismissed with prejudice.

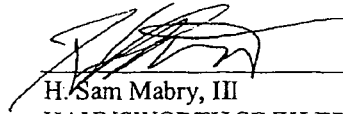
CONCLUSION

For the foregoing reasons, Defendants respectfully request that their motion be granted and that judgment be entered against Plaintiff and in favor of Defendants.

⁹ Moreover, because Plaintiff has released his individual claims he cannot have his putative class action certified or serve as a class representative. In particular, the third and fourth requirements for class certification – that a representative party's claims be typical of the class, and that the representative party fairly and adequately protect the interests of the class – cannot be met here because Plaintiff released his individual claims. Rule 23(a)(3-4), SCRCP. Because Plaintiff's "action does not survive, there is no representative party to satisfy the third and fourth requirements." Gardner v. S.C. Dep't. of Revenue, 353 S.C. 1, 23 n.14, 577 S.E.2d 190, 201 n.14 (2003) (a named plaintiff may not maintain a class action where named plaintiff has no personal standing to assert a claim); Ferguson v. Charleston Lincoln/Mercury, Inc., 344 S.C. 502, 510, 544 S.E.2d 285, 289 (Ct. App. 2001) (where individual action is barred, a representative action becomes impossible and class certification moot); Norberg v. Sec. Storage Co. of Wash., No. 12885, 2000 WL 1375868, at *28 (Del. Ch. Sept. 19, 2000) (plaintiff held to be an inadequate class representative after individual claims were dismissed) (attached as Exhibit 12).

Dated: July 28, 2008

Respectfully submitted,



H. Sam Mabry, III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square – 11th Floor
75 Beattie Place
Greenville, South Carolina 29601
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

OF COUNSEL:

Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Suite 800
Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

Counsel for all Defendants and
Counterclaimants

**Defendants' Motion for Judgment on the Pleadings
or, alternatively, Motion for Summary Judgment**

EXHIBITS

**Exhibits to Defendants' Motion for Judgment on the Pleadings
or, alternatively, Motion for Summary Judgment**

INDEX

<u>Exhibit</u>	<u>Tab</u>
Affidavit of Stephen B. Duerk, filed June 6, 2008	1
<u>Fowler v. Hunter</u> , Op. No. 4422 (S.C. Ct. App. filed July 8, 2008) (Shearouse Adv. Sh. No. 29 at 82).....	2
<u>M & M Group, Inc. v. Holmes</u> , Op. No. 4427 (S.C. Ct. App. filed July 15, 2008) (Shearouse Adv. Sh. No. 30 at 29).....	3
<u>Wal-Mart Stores, Inc. v. AIG Life Ins. Co.</u> , 860 A.2d 312, 319 (Del. 2004)	4
<u>Coca-Cola Enters., Inc. S'holder Litig.</u> , C.A. No. 1927-CC, 2007 WL 3122370 (Del. Ch. Oct. 17, 2007).....	5
<u>Brown v. Automated Mktg. Sys., Inc.</u> , No. 6715, 1982 WL 8782 (Del. Ch. Mar. 22, 1982).....	6
<u>In re Beatrice Cos., Inc. Litig.</u> , 522 A.2d 865, 1987 WL 36708 (Del. Mar. 24, 1987)	7
<u>Kahn v. Seaboard Corp.</u> , 625 A.2d 269 (Del. Ch. 1993).....	8
<u>In re SunGard Data Sys., Inc. S'holder Litig.</u> , C. A. No. 1221-N, 2005 WL 1653975 (Del. Ch. July 8, 2005).....	9
<u>Omnicare, Inc. v. NCS Healthcare, Inc.</u> , 809 A.2d 1163 (Del. Ch. 2002)	10
<u>In re Marvel Entm't Group, Inc.</u> , 273 B.R. 58, 74 (D. Del. 2002)	11
<u>Norberg v. Sec. Storage Co. of Wash.</u> , No. 12885, 2000 WL 1375868 (Del. Ch. Sept. 19, 2000)	12

STATE OF SOUTH CAROLINA)
COUNTY OF GREENVILLE)
Brian P. Menezes,)
Plaintiff,)
v.)
WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, Stephen)
B. Duerk, WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P, WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC,)
Defendants.)

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, WLR)
Recovery Fund II, L.P., WLR Recovery)
Fund III, L.P, WLR Recovery Associates II)
LLC, and WLR Recovery Associates III)
LLC;)
Counterclaimants,)
v.)
Brian P. Menezes,)
Counterclaim Defendant.)

FILED
CLERK OF COURT
GREENVILLE, S.C.
JUN 10 2008

2008 JUN -6 P 2:24

AFFIDAVIT OF STEPHEN B. DUERK

I, Stephen B. Duerk, hereby state as follows:

1. I am over the age of 18 and reside in Greenville, South Carolina. I make this affidavit in support of Defendants' Motion for Judgment on the Pleadings or, Alternatively, Motion for Summary Judgment, and for all other purposes permitted by law. The facts contained in this affidavit are based upon my personal knowledge and my review of corporate records as

described herein. I suffer from no disability which would preclude me from giving the testimony herein and, if I were called upon to testify, I could and would competently do so.

2. I have worked for Safety Components International, Inc. ("SCI") or its predecessors since June 21, 1965 until my retirement at the end of last year (December 31, 2007). I served as SCI's President from June 9, 2006 to approximately October 20, 2006 when SCI merged with International Textile Group, Inc. Thereafter, I became President of the Automotive Safety Group of the combined company.

3. During my tenure at SCI, I worked with Brian P. Menezes and, over the years, grew familiar with his signature after seeing it regularly on correspondence and other corporate documents.

4. In July 2006, Mr. Menezes sued SCI and Joseph Gorga for employment related grievances arising from his separation from SCI. That lawsuit was resolved when the parties agreed to a settlement. Specifically, Mr. Menezes agreed to enter into a settlement and release in exchange for certain payments as part of that settlement.

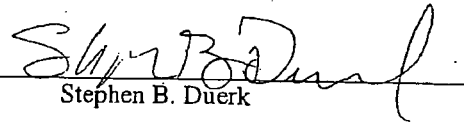
5. On or about September 29, 2006, I received the final version of the Confidential Settlement Agreement and Release of All Claims ("Settlement Agreement"), and signed it on behalf of SCI. Attached hereto as Exhibit A is a true and correct copy of the Settlement Agreement, which is signed by Mr. Menezes and dated September 28, 2006. I am familiar with Mr. Menezes' signature, and I swear and confirm that the first signature on Page 10 of the Settlement Agreement (Exhibit A to this Affidavit), which purports to be the signature of Mr. Menezes, is in fact the signature of Mr. Menezes. I also swear and confirm that the third signature on Page 10 of the Settlement Agreement (Exhibit A to this Affidavit) is my signature. After executing this Settlement Agreement, Mr. Menezes, by way of his attorney, dismissed his

lawsuit against SCI and Mr. Gorga pursuant to the terms of the Settlement Agreement. It is my understanding that SCI fully performed all of its obligations under the Settlement Agreement and made all of the monetary payments to Mr. Menezes and his lawyer required by the Settlement Agreement.

I declare under penalty of perjury under the laws of the State of South Carolina that the foregoing is true and correct.

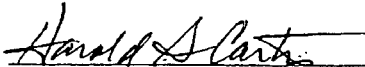
FURTHER AFFIANT SAYETH NOT.

June 5, 2008


Stephen B. Duerk

Subscribed and sworn to before me

this 5 day of June, 2008.


Notary Public (My Commission Expires 9-4-17)

**CONFIDENTIAL SETTLEMENT AGREEMENT
AND RELEASE OF ALL CLAIMS**

This CONFIDENTIAL SETTLEMENT AGREEMENT AND RELEASE OF ALL CLAIMS (hereinafter "Confidential Settlement Agreement") by and between **Brian P. Menezes**, a resident of Greenville, South Carolina (hereinafter "**Plaintiff**"), and his heirs, executors, administrators, successors and assigns, and **Safety Components International, Inc.**, a company with an office and place of doing business in Greenville, South Carolina (hereinafter "**Safety Components**" or "**Employer**"), its officers, directors, board members, shareholders, its affiliates and controlling persons (if any), employees, attorneys, insurers, representatives, bailees, agents, servants, heirs, executors, administrators, personal representatives, predecessors, successors, assigns, parent companies, subsidiaries, related companies, divisions, and the officers, directors, board members, shareholders, employees, bailees, agents and servants of their parent companies, subsidiaries, related companies, divisions, and affiliates, and all persons acting by, through, under, or in concert with any of them, and **Joseph L. Gorga**, a resident of Greensboro, North Carolina (hereinafter "**Gorga**"). Safety Components and Gorga may be identified collectively hereinafter as "**Employer**" solely for the purpose of identification in this document. Plaintiff, Safety Components, and Gorga may also be identified collectively hereinafter as the "**Parties**."

WITNESSETH:

WHEREAS, on or about July 6, 2006, Plaintiff filed a complaint entitled "*Brian P. Menezes, Plaintiff, vs. Safety Components International, Inc., and Joseph L. Gorga, Defendants*," bearing civil action no. 2006-CP-23-4236, in the South Carolina Court of Common Pleas for the Thirteenth Judicial Circuit, County of Greenville (hereinafter "the Underlying Lawsuit"), in which Plaintiff alleged, among other things, that the Defendants were liable for violation of the South Carolina Payment of Wages Act (S.C. Code Ann. § 41-10-10 et seq.) and breach of contract arising out of Plaintiff's employment with Safety Components and an "Employment Agreement" between Menezes and Safety Components, entered into on May 18, 2001, as subsequently amended (hereinafter "**Employment Agreement**"), and wrongful termination of Menezes' employment from Safety Components (hereinafter collectively "**Plaintiff's Claims**"), and seeking damages and a declaratory judgment on Plaintiff's Claims;

WHEREAS, Plaintiff also prepared an Amended Complaint incorporating Plaintiff's Claims against Employer, but which also contained additional allegations against International Textile Group, Inc., W.L. Ross & Co., LLC, and David Wax, a resident of the State of Connecticut, for, among others, tortious interference with contract and civil conspiracy (hereinafter collectively "**Plaintiff's Amended Claims**"), which Amended Complaint was not filed with any court or served upon Employer, International Textile Group, Inc., W.L. Ross & Co., LLC, or David Wax;

WHEREAS, the Parties have engaged in sufficient investigation upon which to evaluate the claims and potential defenses in the Underlying Lawsuit;

WHEREAS, Defendants deny and dispute Plaintiff's Claims and Plaintiff's Amended Claims, in whole or in part, and any liability therefore;

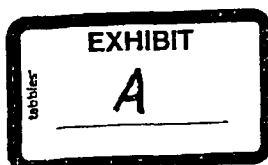


Exhibit A
Stephen B. Duerk
S B Duerk

Harold A. Carter

WHEREAS, the Parties have reached an agreement to resolve any and all claims arising out of Plaintiff's Claims and Plaintiff's Amended Claims, or any right to damages or a declaratory judgment, prior to Employer filing an Answer responding to Plaintiff's Claims or Plaintiff's Amended Claims;

WHEREAS, the Parties have agreed upon a compromise settlement and now wish to forever resolve, settle, compromise, and end any and all claims either or both may have against the another arising from Plaintiff's employment, and the termination thereof, and in the Underlying Lawsuit and as expressed in Plaintiff's Amended Claims;

WHEREAS, Plaintiff acknowledges that Employer has paid to him all wages earned, all unused vacation benefits accrued (if any), and all other amounts which may have been owed to him by Employer pursuant to the Employment Agreement or otherwise by Employer's policy, contract, or applicable law through the date of Plaintiff's termination, June 9, 2006 (hereinafter the "Termination Date"), less standard payroll withholding and any authorized deductions.

NOW, THEREFORE, in consideration of the mutual covenants contained herein and the exchange of other good and valuable consideration, the receipt and sufficiency of which are hereby expressly acknowledged, the Parties hereto agree to the following terms of settlement in full satisfaction, accord and settlement of all claims against one another:

1. **Payment by Employer to Plaintiff in Lieu of Severance Pay.** The Parties agree that subject to the expiration of the seven-day (7-day) revocation period (as described in Section 18 below) and receipt by Employer of an executed Stipulation of Dismissal with Prejudice of the Underlying Lawsuit, the Employer will pay to Plaintiff, in full satisfaction, accord, and settlement for any and all claims, and specifically for any claim for severance payments as contemplated pursuant to §7.4(b)(1) of the Employment Agreement, the amounts set forth below on the dates indicated:

- (a) A first payment on January 9, 2007, in the amount of Ninety Thousand Two Hundred Ten and no/100ths (\$90,210.00) Dollars (which takes into consideration the payments previously made by the Employer of Fifty Four Thousand Two Hundred Ten and no/100ths (\$54,210.00) Dollars).
- (b) A second payment on March 2, 2007 in the amount of One Hundred Forty-Four Thousand Four Hundred Twenty and no/100ths (\$144,420.00) Dollars.
- (c) A third and final payment on August 7, 2007 in the amount of One Hundred Forty-Four Thousand Four Hundred Twenty and no/100ths (\$144,420.00) Dollars.

Each of the aforementioned payments is to be paid minus all applicable withholdings as required by law.

2. **Payment by Employer to Plaintiff in Lieu of Change in Control Bonus.** The Parties dispute the right to any change in control bonus payment under the Employment Agreement, but agree that in full satisfaction, accord, and settlement for any claim, right or entitlement to any payment for a change in control bonus payments, whether pursuant to §7.4(b)(4) of the Employment Agreement, or from any other part of the Employment Agreement, or otherwise from any Released Party, Safety Components will pay to the Plaintiff the total sum of One Hundred Ninety Seven

Thousand Five Hundred and no/100ths (\$197,500.00) Dollars, again subject to the expiration of the seven-day (7-day) revocation period (as described in Section 18 below) and receipt by Employer of an executed Stipulation of Dismissal with Prejudice of the Underlying Lawsuit.

This sum shall be paid in three (3) separate payments of Sixty Five Thousand Eight Hundred Thirty Three and 33/100ths (\$65,833.33) Dollars, each of which is to be paid on or before January 9, 2007, March 2, 2007, and August 7, 2007, respectively, and from which shall be deducted all applicable withholdings as required by law. If applicable, the aforesaid payment, in compromise and settlement of any and all rights to any change in control bonus, shall be "grossed up" as provided in the Employment Agreement at Paragraph 10. Compliance with Internal Revenue Code §280G.

3. **Benefits.** All of Plaintiff's benefits, and any right thereto, shall be deemed terminated as of the Termination Date (other than, where applicable, health, dental, and vision insurance, which shall terminate effective as of the last day of the month in which Plaintiff was terminated) unless the terms of the benefit plans provide otherwise, or except to the extent inconsistent with the remainder of this paragraph. Employer shall provide at no expense to Plaintiff for a period of eighteen (18) months following the Termination Date continued health insurance coverage as in effect from time to time (but which shall include coverage under Execucare or a plan or program providing coverage substantially equivalent to that Plaintiff had immediately prior to the Termination Date) and, to the extent they continue to be eligible for such coverage under COBRA, his dependents who were covered by Employer's health insurance plan immediately prior to the Termination Date. Otherwise, Plaintiff acknowledges that Plaintiff shall not be entitled to any other or additional benefits, sums or amounts, including without limitation, any right to any bonus, vacation pay, sick pay, life insurance, disability income policies, car allowance, contributions for 401(k) or similar plans nor any other benefits, except for the payments of premiums for medical insurance set forth above, and except as otherwise provided in the benefit plans, or specifically identified in this Confidential Settlement Agreement. Plaintiff shall be entitled, at Plaintiff's sole expense to any COBRA benefits to which he may be entitled by law.

4. **Payment by Employer to Counsel for Plaintiff.** On Plaintiff's behalf, and at his request, the Parties agree that Employer will pay Plaintiff's attorney, William D. Herlong, Esq., of Anderson & Herlong, L.L.C., the sum of Seven Thousand Five Hundred and no/100ths (\$7,500.00) Dollars, payable pursuant to a Form 1099. Plaintiff's attorneys agree to hold harmless and indemnify Employer for any liability for tax payments and filings for which Plaintiff's attorneys are responsible, if any.

5. **Nature of Consideration.** The mutual promises and sums described herein are acknowledged to be good and valuable consideration in full and final payment and accord and satisfaction of all claims by Plaintiff against Employer by virtue of his employment, the Employment Agreement, or otherwise.

6. **Dismissal of the Underlying Lawsuit.** The Parties hereby agree to direct their respective counsel to dismiss the Underlying Lawsuit, and any and all claims, counterclaims, cross-claims, or related claims that have been or could have been asserted in the Underlying Lawsuit, with prejudice. The Underlying Lawsuit and any and all related claims, counterclaims, cross-claims, or related claims shall henceforth be res judicata.

7. **Releases by Plaintiff.** As a material inducement to Employer to enter into this Confidential Settlement Agreement, Plaintiff does hereby release, acquit and forever discharge Gorga and Safety Components, and any parent, subsidiary and affiliated person, company, business, entity or enterprise of Gorga and Safety Components, along with all current and former officers, directors, agents, employees, insurers, representatives, attorneys, successors, and assigns of the same, which shall also include by way of enumeration but not limitation, the International Textile Group, Inc., W. L. Ross & Co. L.L.C., and David L. Wax, a resident of the State of Connecticut (collectively, the "Released Parties"), from any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which Plaintiff either has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof. It is Plaintiff's intention to release all rights and claims that he may lawfully release.

Without in any way limiting the generality of the foregoing, this Release applies to and waives: (1) any and all claims, causes of action, or rights, which Plaintiff has had or may now have under or pursuant to Title VII of the Civil Rights Act of 1964, as amended; Civil Rights Act of 1991; Title 42, United States Code, Section 1981; the Americans with Disabilities Act; the Age Discrimination In Employment Act, as amended, the Older Workers Benefit and Protection Act; and any other statute, rule, or executive order prohibiting discrimination in employment on the basis of age, disability, religion, national origin, sex, race, color, or veteran's status; (2) any and all claims, causes of action, or rights, which Plaintiff has had or may now have under or pursuant to the Employment Retirement Income Security Act; (3) any claims, causes of action, or rights which Plaintiff might have or has had for employment discrimination, unlawful employment practices, or relating in any way to his employment or termination thereof, and arising under local, state, or federal law; (4) any claims or causes of action which Plaintiff might have or have had for personal injuries; and (5) any claims or causes of action which Plaintiff might have or have had for breach of contract or based upon any agreement with the Released Parties, specifically including but not limited to the Employment Agreement; (6) any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement; (7) any claims or causes of action which Plaintiff might have or have had for defamation, tortious conduct and wrongful discharge and (8) all of Plaintiff's Claims, Plaintiff's Amended Claims and all claims made or which may have been made in the Underlying Lawsuit or Amended Complaint.

Additionally, without waiving any prospective or retrospective rights under the Family and Medical Leave Act ("FMLA"), Plaintiff admits that he has received from Employer all rights and benefits, if any, potentially due to him pursuant to the FMLA. Similarly, without waiving any prospective or retrospective rights under the Fair Labor Standards Act ("FLSA"), Plaintiff admits that he has received from Employer all salary, wages, or other compensation, if any, potentially due to him pursuant to the FLSA.

8. **Releases by Plaintiff – Additional Information.** Plaintiff specifically agrees that his release of claims identified in Section 7, above, is knowing and voluntary and that he has had sufficient opportunity to consult with his attorney to ensure that he understands the language used in this Confidential Settlement Agreement and the rights and obligations created herein and he had in fact consulted with his attorney regarding the same. Plaintiff understands, acknowledges, and voluntarily agrees that this Confidential Settlement Agreement, except as otherwise explicitly stated, is a total and

complete release by him of any and all claims which he has against Employer as of the effective date of this Confidential Settlement Agreement, both known or unknown, even though there may be facts or consequences of facts which are unknown to Plaintiff.

9. **Other Claims.** Plaintiff represents that besides the Underlying Lawsuit, he has not filed any other complaints, claims, or actions against the Released Parties with any state, federal, or local agency or court, or that if Plaintiff has, Plaintiff agrees to withdraw and dismiss with prejudice (or cause to be withdrawn and dismissed with prejudice) any such complaint, claim, action, or charge. Plaintiff acknowledges that he knows of no facts which may lead to or support any complaints, claims, actions, or charges against Employer in or through any state, federal, or local agency or court other than Plaintiff's Claims and/or Plaintiff Amended Claims as described hereinabove and asserted in the Underlying Lawsuit and/or described in the Amended Complaint, which are hereby released and forever settled.

10. **Status of "Employment Agreement."** Plaintiff further agrees that he and Safety Components entered into the Employment Agreement on May 18, 2001, which agreement was subsequently amended by the Parties on September 22, 2003. The Parties hereby agree that the prior Employment Agreement, including all amendments thereto, is hereby rescinded, terminated, cancelled, or otherwise null and void as of June 9, 2006, and the Parties shall be relieved of any obligations or liability thereunder, except with the sole exceptions addressed herein. While it is the Parties' intent to otherwise rescind the Employment Agreement, the following provisions contained in the Employment Agreement shall remain in full force and effect and are incorporated herein by reference:

- Sec. 8. Confidential Information, Inventions (including §§ 8.1 - 8.5); and
- Sec. 9. Non-Competition, Non-Solicitation (including §§ 9.1 - 9.5).

Plaintiff agrees and understands that, notwithstanding the provisions contained in Paragraph 24 herein, the foregoing provisions contained in the Employment Agreement, and amendments thereto, shall remain in full force and effect despite the execution and terms of this Confidential Settlement Agreement, are subject to separate valid consideration previously paid by Employer to Plaintiff, and are subject to enforcement pursuant to the original terms of the Employment Agreement.

11. **Releases by Employer.** As a material inducement to Plaintiff to enter into this Confidential Settlement Agreement, Employer hereby releases, acquits, and forever discharges Plaintiff from any and all manner of actions, causes of action, suits, claims, setoffs, debts, compensation, salary, benefits, sums of money, accounts, covenants, trespasses, damages, judgments and demands, whatsoever, in law or in equity, whether known or unknown, liquidated, contingent, absolute, or otherwise, which the Employer either has had or now has against Plaintiff for or related to any matter or thing, whatsoever, from the beginning of time up to and including the date of execution hereof, except for the provisions in the Employment Agreement enumerated and described above in Section 10 entitled "Status of Employment Agreement", and with regard to that provision, only any existing claims predating the execution of this agreement are released. Other than the provisions set forth in Section 10, above, it is the Employer's intention to release all rights and claims that the Employer may lawfully release.

12. **Non-Disparagement.** The Parties agree that they will not publicly criticize or disparage the each other, or privately criticize or disparage each other in a manner intended or reasonably calculated to result in public embarrassment to, or injury to the business or reputation of the Parties. Employer shall take reasonable efforts to ensure that David Wax and the executive officers of International Textile Group, Inc., and W.L. Ross & Co., LLC, comply with this provision as if each was Employer.

13. **Cooperation.** Plaintiff agrees that for a period of one year he will provide such cooperation, information or reasonable assistance that the Released Parties (as defined above) may reasonably request of him upon reasonable prior notice, including making himself available to be a witness in judicial or other legal proceedings, with respect to any matters that he may have been familiar with or responsible for during his tenure with the Employer. The Employer will reimburse all related and reasonable expenses and shall compensate Plaintiff at the rate of Two Hundred and No/100ths (\$200.00) Dollars per hour, with a minimum of four (4) hours, per request for such future services.

14. **Resignation From Offices.** Plaintiff confirms that effective June 9, 2006, he ceased to be employed with Safety Components and that he does resign from all offices and positions with Safety Components, including (a) from all offices of Safety Components to which he has been elected by the Board of Directors of Safety Components or any Released Party (or to which he has otherwise been appointed), (b) from all directorships or offices of any entity that is a subsidiary of, or is otherwise related to or affiliated with, Safety Components or any Released Party, (c) from all administrative, fiduciary or other positions he may hold with respect to arrangements or plans for, of or relating to Safety Components or any Released Party, and (d) from any other directorship, office, or position of or with any corporation, partnership, joint venture, trusts of any other enterprise (each, an "Other Entity") insofar as Plaintiff is serving in the directorship, office or position of the Other Entity at the request of Safety Components or any Released Party.

15. **Future Employment.** Plaintiff agrees that Employer is not obligated to offer employment to Plaintiff (or to accept services or the performance of work from Plaintiff directly or indirectly) now or in the future. Plaintiff agrees not to seek or accept employment or any direct independent contractor relationship with the Released Parties, as defined herein, now or at any time in the future. Plaintiff agrees that in the event such employment or other relationship occurs in the future, this provision shall serve as good and just cause for termination of same. Plaintiff knowingly and voluntarily waives all rights, if any, he may have under federal and/or state law to re-hire by, or reinstatement of employment with, Employer. This provision does not apply to the extent Plaintiff is an employee or independent contractor with a company that is acquired by a Released Party. Further, this provision is void after five (5) years.

16. **Non-Admission.** The Parties agree and understand that this Confidential Settlement Agreement is a compromise of disputed claims and shall not in any way be construed as an admission by any of the Parties or Released Parties that it has acted wrongfully with respect to any other Party or Released Party or any other person, which is expressly denied, or that they have any rights whatsoever against each other. The Parties further agree that Employer and the Released Parties specifically disclaim any liability to or alleged wrongful acts against Plaintiff or any other person, on the part of itself, its affiliates, and their respective representatives, officers, employees, attorneys, and agents.

17. **Confidentiality and Breaches.** Except as required to comply with legal disclosure

requirements (e.g., subpoenas) or as otherwise required or protected by law or otherwise allowed in this paragraph, the Plaintiff represents and agrees that he will keep the terms, and amount of this Confidential Settlement Agreement completely confidential and he has not disclosed and will not disclose any information regarding this Confidential Settlement Agreement (or discussions preceding this Confidential Settlement Agreement) to anyone other than his attorneys, tax advisors, financial advisors, his spouses and/or other individuals who have a reasonable need to know and who have been approved in writing to receive such information by Employer. The Plaintiff agrees that he will not describe this Confidential Settlement Agreement or the settlement of his Claims in any way (e.g., substantial/insubstantial, generous/parsimonious, large/small, fair/unfair, etc.). The Plaintiff may discuss this Confidential Settlement Agreement with his attorneys, tax advisors, financial advisors, his spouses and/or other individuals who have a reasonable need to know and have been approved to receive such information by Employer, but Plaintiff will inform them of these confidentiality provisions, and will remain responsible for any further disclosures that may result. The Plaintiff agrees that the unauthorized disclosure of the terms or amount of this Confidential Settlement Agreement is a material breach of this Confidential Settlement Agreement. In the event there is a breach of this Confidential Settlement Agreement, the remaining provisions of this Settlement Agreement shall remain in full force and effect for the benefit of the Employer. The Parties and the Released Parties will limit their public disclosure of this settlement to a simple statement that the matter has been resolved on confidential terms.

18. **Acknowledgment.**

(a) The release set forth herein includes a waiver of rights and claims which Plaintiff may have arising under the Age Discrimination in Employment Act of 1967 (Title 29, United States Code, Sections 621, *et seq.*) ("ADEA"). Plaintiff is advised to consult with his attorney regarding his waiver of rights and claims under the ADEA. Plaintiff understands that by signing this release, he waives his rights or claims under the ADEA. Plaintiff further understands that he is not waiving rights or claims under that ADEA that may arise after the effective date of this fully executed Confidential Settlement Agreement.

(b) Plaintiff agrees that he has been advised to consult with an attorney prior to executing this Confidential Settlement Agreement. Plaintiff acknowledges that he has had the opportunity to consult with an attorney to review this agreement, prior to signing, and that he has in fact done so. Plaintiff acknowledges that his attorney has fully explained in a manner understood by him the waiver of any rights or claims contained in this Confidential Settlement Agreement.

(c) Plaintiff certifies that he has been given a period of up to twenty-one (21) days to study this Confidential Settlement Agreement, and to consult with an attorney, accountant, or other advisor before signing the Confidential Settlement Agreement, and that the actual time he has taken for such purposes was adequate for all appropriate consultations.

(d) Plaintiff represents that he has read and thoroughly discussed all aspects of this Confidential Settlement Agreement with his attorney, understands its provisions, and understands that this Confidential Settlement Agreement establishes binding contractual rights. Plaintiff acknowledges that this Confidential Settlement Agreement and the release and waiver of claims contained herein are given knowingly and voluntarily.

(e) Plaintiff understands that this Confidential Settlement Agreement shall not be effective and enforceable until seven (7) days from the date he executes this Confidential Settlement Agreement. During this seven-day period, Plaintiff may change his mind and revoke this Confidential Settlement Agreement by notifying Employer, in writing, of his wish to revoke this Confidential Settlement Agreement. Any such revocation must be in the form of a signed, written statement delivered to Employer's counsel, *M. Baker Wyche, III, at Ogletree, Deakins, Nash, Smoak & Stewart, P.C., 300 N. Main Street, PO Box 2757, Greenville, SC 29602.*

19. **Waiver of Breach.** Either Party may waive or excuse the other's failure to perform any provision of this Confidential Settlement Agreement; provided, however, that any such waiver shall be in writing and shall not preclude the enforcement of this Confidential Settlement Agreement upon any subsequent breach, whether or not similar in character.

20. **Assignment.** This Confidential Settlement Agreement and the rights and obligations of Employer hereunder may be assigned by Employer and shall inure to the benefit of, shall be binding upon and shall be enforceable by any such assignee. This Confidential Settlement Agreement and the rights and obligations of Plaintiff hereunder may not be assigned by Plaintiff and, further, Plaintiff expressly states that he has not assigned any rights or obligations arising out of his employment with Employer, his separation therefrom, or pursuant to this Confidential Settlement Agreement.

21. **Successorship.** This Confidential Settlement Agreement shall be binding upon and inure to the benefit of Gorga and Safety Components and its affiliates, successors, and assigns, and, subject to Section 21 above, Plaintiff, his heirs, personal representatives, administrators, beneficiaries, and assigns. If Plaintiff should die while any amount would still be payable to him under this Confidential Settlement Agreement had Plaintiff continued to live, all such amounts, unless otherwise provided herein, shall be paid in accordance with the terms of this Confidential Settlement Agreement to his devisee, legatee, or other designee or, if there is no such designee, to his estate.

22. **Non-Reliance.** Plaintiff represents and acknowledges that in executing this Confidential Settlement Agreement he does not rely, and has not relied, upon any representation or statement not set forth herein by Employer or any of Employer's agents, representatives, or attorneys.

23. **Entire Agreement.** Plaintiff further represents and acknowledges that this Confidential Settlement Agreement constitutes the entire agreement between the Parties. Except as stated otherwise herein, any oral or written representations, prior agreements, or understandings not reflected in this Confidential Settlement Agreement shall have no force or effect, and are superseded by this Confidential Settlement Agreement.

24. **Severability.** The terms of this Confidential Settlement Agreement, including paragraph subparts, are severable, and if any part or subpart is found to be unenforceable, the other terms shall remain in full force and effect and are valid and enforceable.

Likewise, the Parties expressly recognize that the obligations set forth in this Confidential Settlement Agreement are independent of one another, in that a breach of one provision does not extinguish any duties or rights set forth in other provisions of this Confidential Settlement Agreement.

25. **Interpretation.** The Parties agree that this Confidential Settlement Agreement shall be interpreted according to South Carolina law and shall not be construed against the drafters. In the event for any reason that any provision or portion of this Confidential Settlement Agreement shall be found to be void or invalid, then such provision or portion shall be deemed to be severable from the remaining provisions or portions of this Confidential Settlement Agreement, and it shall not affect the validity of the remaining provisions or portions, which provisions or portions shall be given full effect as if the void or invalid provision or portion had not been included herein.

26. **Modification.** This Confidential Settlement Agreement shall not be modified or amended except by an instrument in writing signed by Plaintiff and Employer.

27. **Cooperation in Drafting.** The Parties agree that they have cooperated in the drafting and preparation of this Confidential Settlement Agreement with the assistance of counsel. In any construction to be made of this Confidential Settlement Agreement, the same shall not be construed against either party but shall be viewed as each sharing an equal role in the negotiation and drafting of its terms.

28. **Legal Counsel.** Plaintiff agrees that he has been advised to seek the advice of legal counsel, and that he has had the opportunity to have legal counsel review this agreement, prior to signing.

29. **Governing Law, Jurisdiction, and Venue.** This Confidential Settlement Agreement has been entered into under and shall be governed by and construed in accordance with the laws of the State of South Carolina, without regard to its conflicts of laws provision. The parties agree that the Greenville County Court of Common Pleas or the Federal District Court for the District of South Carolina, Greenville Division, shall be the sole and exclusive jurisdiction and venue for all disputes between the Parties under this Confidential Settlement Agreement. Plaintiff hereby irrevocably consents to the jurisdiction and venue of these courts for adjudication of all disputes between the Parties under this Confidential Settlement Agreement. Plaintiff hereby waives any objections or defenses to jurisdiction or venue in any such proceeding before such court(s).

30. **Effective Date.** The terms of this Confidential Settlement Agreement shall become final and binding only upon the execution of this Confidential Settlement Agreement by both parties and upon the expiration of the seven (7) day revocation period discussed above.

* * * * *

IN WITNESS WHEREOF the Parties have caused this Confidential Settlement Agreement to be signed. By signing this agreement, the Parties warrant that they have read and understand each provision of this Confidential Settlement Agreement, that they voluntarily agree to and have signed the Confidential Settlement Agreement, that in so doing they are not relying upon any inducements, representations, agreements, or understandings other than as are set forth herein, and that they are acting with full advice of and explanation by their respective legal counsel.

* * * * *

The Parties recognize and agree that this Confidential Settlement Agreement and Release may be signed and executed in one or more parts or counterparts and/or by facsimile signature. Each counterpart, including a signature page executed by each party, shall be an original counterpart of this Confidential Settlement Agreement and Release, but all such counterparts shall constitute one instrument.

WITNESSES:

Brian P. Menezes

Janice Varot

[Signature]
Brian P. Menezes
Date: Sept 28th, 2006

Reviewed and Approved:

Janice Varot

[Signature]
William D. Herlong,
Attorney for Plaintiff, Brian P. Menezes
Date: 9/28/2006

Safety Components International, Inc.

By: _____

Its: _____
Date: _____

* * * * *

The Parties recognize and agree that this Confidential Settlement Agreement and Release may be signed and executed in one or more parts or counterparts and/or by facsimile signature. Each counterpart, including a signature page executed by each party, shall be an original counterpart of this Confidential Settlement Agreement and Release, but all such counterparts shall constitute one instrument.

WITNESSES:

Brian P. Menezes

Janice Varat

Brian P. Menezes

Brian P. Menezes

Date:

Sept 28th, 2006

Reviewed and Approved:

Janice Varat

William D. Herlong

William D. Herlong,

Attorney for Plaintiff Brian P. Menezes

Date:

9/28/2006

Safety Components International, Inc.

Brenda S. Swafford

By:

Steph B. Dush

Its:

President

Date:

Sept. 29, 2006

Settlement Agreement and Release of All Claims

Joseph L. Gorga

Cheryl L. Hollis

Joseph L. Gorga
Joseph L. Gorga

Date: Sept. 29, 2006

4386701.1

THE STATE OF SOUTH CAROLINA
In The Court of Appeals

Eric U. Fowler and
Melissa W. Dawn Fowler, Appellants/Respondents,

v.

Sallie Hunter, Gynecologic
Oncology Associates,
Selective Insurance Company
of South Carolina, and
Insurance Associates, Inc., Defendants,

Of whom: Selective Insurance
Company of South Carolina, is, Respondent/Appellant,

and

Insurance Associates, Inc. is, Respondent.

Appeal From Greenville County
Larry R. Patterson, Circuit Court Judge

Opinion No. 4422
Heard June 4, 2008 – Filed July 8, 2008

REVERSED

Rodney M. Brown, of Fountain Inn, for Appellants/Respondents.

Andrew F. Lindemann, of Columbia, for Respondent/Appellant.

E. Matlock Elliott and Joshua L. Howard, of Greenville, for Respondent.

KONDUROS, J.: Eric and Melissa Fowler ("the Fowlers") appeal the dismissal of their assigned cause of action for professional negligence against Insurance Associates, Inc. ("Insurance Associates"). Selective Insurance Company of South Carolina, Inc. ("Selective") appeals the dismissal of its cross-claim for equitable indemnification against Insurance Associates. We reverse.

FACTS

The Fowlers were seriously injured when the motorcycle they were riding was struck by a car driven by Sallie Hunter. The car was owned by Gynecologic Oncology Associates ("GOA") for use by Mrs. Hunter's husband, Dr. James Hunter. Auto-Owners Insurance Company insured the car under a business automobile policy with limits of one million dollars. At least two other policies potentially provided coverage. One was a commercial umbrella policy for four million dollars procured by GOA through Insurance Associates and issued by Selective. The other policy at issue was a personal catastrophic liability policy for two million dollars carried by the Hunters and also issued by Selective.

The Fowlers filed suit against Mrs. Hunter, and it was discovered that due to an inadvertent computer error by Insurance Associates, GOA's umbrella policy did not provide automobile liability coverage. The Fowlers then filed a declaratory judgment action to see what coverage was available under the above-referenced policies. The Hunters and GOA answered and filed cross-claims against Selective for reformation and against Insurance

Associates for professional negligence. Additionally, Selective filed a cross-claim against Insurance Associates for indemnity.

Eventually, the parties settled many of the claims in the two lawsuits. The Fowlers received one million dollars from GOA's automobile policy, two million dollars from the Hunter's personal umbrella policy, and an additional one and one-half million dollars from Selective. Additionally, the Hunters and GOA assigned their professional negligence claim against Insurance Associates to the Fowlers, and the Fowlers signed a covenant not to execute against the Hunters and GOA. The Hunters and GOA agreed to cooperate with the Fowlers in the prosecution of the professional negligence claim, and the Fowlers and Selective agreed to split equally any recovery from either the professional negligence or indemnification claim.

Insurance Associates filed a summary judgment motion seeking dismissal of the only remaining claims: the professional negligence claim assigned to the Fowlers and Selective's claim for indemnification. The circuit court granted these motions finding that because neither the Hunters, GOA, nor Selective could prove they were damaged by Insurance Associate's negligence, the claims failed. These appeals followed.

STANDARD OF REVIEW

When reviewing the grant of a summary judgment motion, this court applies the same standard of review as the trial court under Rule 56, SCRCF. Cowburn v. Leventis, 366 S.C. 20, 30, 619 S.E.2d 437, 443 (Ct. App. 2005). Summary judgment is proper when there is no genuine issue as to any material fact and the moving party is entitled to a judgment as a matter of law. Rule 56(c), SCRCF. To determine whether any triable issues of fact exist, the reviewing court must consider the evidence and all reasonable inferences in the light most favorable to the non-moving party. Law v. S.C. Dep't of Corrs., 368 S.C. 424, 434, 629 S.E.2d 642, 648 (2006). However, when a party has moved for summary judgment the opposing party may not rest upon the mere allegations or denials of his pleading to defeat it. Rule 56(e), SCRCF. Rather, the non-moving party must set forth specific facts demonstrating to the court there is a genuine issue for trial. Id.

LAW/ANALYSIS

I. Professional Negligence

The Fowlers argue the circuit court erred in granting summary judgment to Insurance Associates as to their assigned claim for professional negligence. We agree.

The circuit court reasoned because the Hunters and GOA were insulated from execution of any judgment, the Fowlers, standing in the Hunter's shoes, could never prove damages flowing from the negligence of Insurance Associates. While this analysis is technically correct, the majority of courts having addressed this issue have elected to allow such an assigned claim to proceed. We are persuaded by the rationale set forth in those cases.

In Campione v. Wilson, 661 N.E.2d 658, 660-61 (Mass. 1996), an injured party settled with an insurer and insured for a stipulated amount of damages and a release of the insured. The Massachusetts Supreme Court determined that even though the settlement included a release, the injured party could proceed in prosecuting the insured's assigned negligence claim against the insurance brokers. Id. at 663. The court considered the competing policy considerations at play under these circumstances noting there is a risk of collusion between the settling parties even though there is benefit to allowing injured parties and tortfeasors to settle claims. Id. at 662-63. Nevertheless, the court rejected the "somewhat metaphysical contention" that the legal basis for the claim against the insurer [and broker] disappeared when the insured became insulated from liability due to a release or a covenant not to execute." Id. at 662 (quoting Gray v. Grain Dealers Mut. Ins. Co., 871 F.2d 1128, 1132-33 (D.C. Cir. 1989)).

An examination of other jurisdictions reveals most courts are approving of settlement arrangements similar to the one in this case, so long as the risk of collusion is minimized. See Gray, 871 F.2d at 1133 (applying North Carolina law and allowing injured party to pursue assigned bad faith claim against insurer even though insured was insulated from liability by release); Damron v. Sledge, 460 P.2d 997, 999 (Ariz. 1969) (holding an assignment of the insured's bad faith claim plus a covenant not to execute was not ipso

facto collusive); United Servs. Auto. Ass'n v. Morris, 741 P.2d 246, 254 (Ariz. 1987) (holding settlement between insured and claimant in which insurer was to defend under reservation of rights did not violate policy's cooperation clause); Red Giant Oil Co. v. Lawlor, 528 N.W.2d 524, 532-33 (Iowa 1995) (holding insured could still suffer damages from agent's negligence when settlement was coupled with a covenant not to execute that did not extinguish liability as would a release; therefore, assigned claim for agent's negligence would be valid); Glenn v. Fleming, 799 P.2d 79, 92-93 (Kan. 1990) (approving of a settlement between insured and injured party coupled with an assignment of a prejudgment claim and covenant not to execute when the settlement is entered into in good faith and the settlement amount is shown to be reasonable).

South Carolina has shown a willingness to depart from the common law in order to promote reasonable settlements between tortfeasors and injured parties. In Bartholomew v. McCartha, 255 S.C. 489, 179 S.E.2d 912 (1971), our Supreme Court concluded the common-law rule regarding the release of one joint tortfeasor was not in the best interests of justice.

Being untrammelled by the ancient rule which, in our view, tends to stifle settlements, defeat the intention of parties and extol technicality, we adopt the view that the release of one tort-feasor does not release others who wrongfully contributed to plaintiff's injuries unless this was the intention of the parties, or unless plaintiff has, in fact, received full compensation amounting to a satisfaction.

Id. at 492, 179 S.E.3d at 914.

While acknowledging the inherent benefits of settlement, we also note South Carolina promotes the careful examination of settlement agreements to avoid the potential for complicity or wrongdoing.

We are cognizant that litigants are free to devise a settlement agreement in any manner that does not contravene public policy or the law. In fact, this

Court encourages such compromise agreements because they avoid costly litigation and delay to an injured party. However, these settlement agreements must be carefully scrutinized in order to determine their efficiency and impact upon the integrity of the judicial process.

Ecclesiastes Prod. Ministries v. Outparcel Assocs., 374 S.C. 483, 493, 649 S.E.2d 494, 499 (Ct. App. 2007) (quoting Poston by Poston v. Barnes, 294 S.C. 261, 263-64, 363 S.E.2d 888, 889-90 (1987)).

In the instant case, there is little evidence of collusion between the settling parties. The injuries suffered in the case were extremely serious. Furthermore, the parties did not put a stipulated amount of damages in their agreement so as to reduce the appearance of collusion, and because they contemplated that the underlying tort claim would be tried to a conclusion.¹ The result of the settlement was the Fowlers were able to procure a three and one-half million dollar recovery under the other insurance policies in place while litigation against a negligent party, Insurance Associates, is not foreclosed. This was clearly the intent of the parties as shown by the express language of the settlement agreement and covenant not to execute. The catastrophic injuries suffered by the Fowlers begged a resolution that would give them the benefit of the uncontested proceeds promptly. In light of our State's willingness to place the interests of the injured party above such a technical application of the law, we believe it was inappropriate for the claim to be dismissed at the summary judgment stage. We therefore reverse the circuit court's grant of summary judgment in favor of Insurance Associates.

¹ The Fowlers and Selective argued to the circuit court if a judgment in excess of the policy limits was required prior to determining the summary judgment motions, the motion hearing should be stayed and the underlying tort claim tried. However, the circuit court elected to proceed with ruling on summary judgment motions.

II. Equitable Indemnification

Selective contends the circuit court erred in granting summary judgment in favor of Insurance Associates regarding Selective's cross-claim for equitable indemnification. We agree.

Under South Carolina law, a party seeking equitable indemnification must show three things: "(1) the indemnitor was liable for causing the Plaintiff's damages; (2) the indemnitee was exonerated from any liability for those damages; and (3) the indemnitee suffered damages as a result of the Plaintiff's claims against it which were eventually proven to be the fault of the indemnitor." Vermeer Carolina's, Inc. v. Wood/Chuck Chipper Corp., 336 S.C. 53, 63, 518 S.E.2d 301, 307 (Ct. App. 1999).

Under the settlement, the Fowlers received one and one-half million dollars from Selective that was not directly traceable to any policy. The circuit court determined Selective admitted liability under the commercial umbrella policy by making this payment. If so, Selective actually benefitted from the negligence of Insurance Associates. Had the automobile liability not been inadvertently excluded under the policy, the defendants' potential exposure would have been the full amount of the policy limits amounting to four million dollars.

Selective offered an alternative explanation for the one and one-half million dollar payment. Selective contends the payment was made as part of a global settlement to avoid a professional negligence claim asserted by the Hunters and GOA. Insurance Associates admitted its negligence in failing to request automobile coverage on the umbrella policy. If Insurance Associates was acting as an agent for Selective, Selective could be vicariously liable for that negligence. Consequently, Selective argues it settled that claim for one and one-half million dollars, paid to the Fowlers, and decided to pursue indemnification from Insurance Associates. We find Selective's position raises a question regarding the indemnification claim, but only if we can conclude Selective would not have issued the policy had the application been correctly submitted. In other words, if Selective would have issued the policy anyway, it was not damaged by Insurance Associates' negligence as it would have been exposed for the full four million dollars.

As the moving party, Insurance Associates relied upon the deposition testimony of Roy Phillips indicating that Selective would have definitely issued the policy had it been submitted correctly to include automobile coverage. Insurance Associates also submitted a set of guidelines related to the "one and done" computer software program that allowed "agents" to automatically secure policies if certain criteria are met. In response, Selective submitted guidelines produced by Insurance Associates during discovery showing that a policy would not automatically be secured unless the underlying policy was also issued by Selective. In this case, the underlying policy was not issued by Selective, but by Auto-Owners.

We conclude the competing sets of guidelines raise a genuine issue of material fact precluding summary judgment. Further inquiry into the facts may show Selective would not have issued the policy without the automobile exclusion. If so, Selective's claim for indemnification as to the one and one-half million dollar settlement may prove viable. If Selective cannot produce such evidence, the claim will likely fail. However, we find the issue presented was too uncertain at this stage for the grant of summary judgment to be appropriate.

Finally, Insurance Associates contends Selective failed to mitigate its damages, barring its indemnification claim, by entering into the global settlement and not litigating coverage under the commercial umbrella policy. We disagree.

While Selective may have a viable coverage defense as to the Hunter's professional negligence claim, that defense was not a certainty. Had they not settled, Selective could have been found responsible for the full four million dollars contemplated under the policy. By settling, Selective made a calculated decision to minimize its own risk. Furthermore, this mitigated the potential damages Selective can seek via indemnification from Insurance Associates.

CONCLUSION

We are persuaded settlements like the one in this case are favorable, so long as the risk of collusion is minimized. Therefore, we conclude the grant of summary judgment in favor of Insurance Associates should be reversed. Furthermore, we believe the existence of the competing guidelines created a genuine issue of fact regarding Selective's claim for indemnification making the grant of summary judgment inappropriate. Consequently, the decision of the circuit court is

REVERSED.

HEARN, C.J., and SHORT, J., concur.

**THE STATE OF SOUTH CAROLINA
In The Court of Appeals**

M&M Group, Inc.,

Appellant,

v.

Suzette A. L. Holmes, Gregory
M. Kopatch d/b/a Empire
Business Brokers, Empire
Business Brokerage, LLC, and
Gregory M. Kopatch
Individually,

Respondents.

Appeal From Charleston County
R. Markley Dennis, Jr., Circuit Court Judge

Opinion No. 4427
Submitted June 2, 2008 - Filed July 15, 2008

AFFIRMED

William J. Cutchin, of Mt. Pleasant, for Appellant.

Brian G. Burke, of Charleston, for Respondents.

THOMAS, J.: In this breach of contract action, M&M Group, Inc. appeals the trial court's grant of summary judgment to Suzette Holmes,

Gregory M. Kopatch¹ d/b/a Empire Business Brokers, Empire Business Brokerage, LLC, and Gregory M. Kopatch. We affirm.²

FACTS

M&M Group, Inc. ("M&M") was the owner of a carwash and lube business located in Mt. Pleasant. Wishing to sell the business and its assets, M&M signed an exclusive Listing Agreement with Gregory Kopatch (Kopatch), a commercial sales broker doing business as Empire Business Brokerage, L.L.C. (Brokerage). Pursuant to the Listing Agreement, the Brokerage would sell the business and M&M would then pay a commission to the Brokerage.

Kopatch identified Suzette Holmes ("Holmes") as a potential buyer, and on April 12, 2005, M&M and Holmes executed a sales contract ("Contract"). Under the terms of the Contract, M&M agreed to transfer its assets to Holmes in exchange for Holmes' payment of \$675,000 to M&M. The first page of the Contract stated, "[w]hereas, the parties agree that Buyer's obligation to purchase the assets of the business and Seller's obligation to sell the assets is contingent upon Buyer's ability to secure commercial financing at prevailing interest rates." The Contract provided that Holmes was to secure \$225,000 of the purchase price through commercial financing and M&M was to finance \$250,000 with a sixty-month promissory note. The seven page Contract also set the closing date as May 22, 2005, and stated that time was of the essence.³

¹ Initially we must note that summary judgment was granted solely to Holmes on M&M's breach of contract action. Although Holmes, Kopatch, and Empire Business Brokerage, L.L.C. are represented by the same attorney, the attorney made clear at the beginning of the hearing that Kopatch and the Brokerage were not parties to the Motion for Summary Judgment. As such, this appeal and opinion pertain only to the action against Holmes.

² We decide this case without oral argument pursuant to Rule 215, SCACR.

³ "19. TIME IS OF THE ESSENCE. It is agreed by both Buyer and Seller that time is of the essence in all regards in connection with this Agreement." (emphasis in original).

On May 9, 2005, Holmes' request for a loan was denied. No closing occurred on May 22, 2005, and the sales transaction was never consummated thereafter. An affidavit by M&M's President, Sean Mummert, states the Brokerage called him on May 22 and told him a proposed lender needed additional information from Holmes before it would approve her financing request. Mummert affirms he told the Brokerage he would grant Holmes an extension in order for her to obtain financing needed to complete the transaction. No further communication occurred until October 12, 2005, when M&M received a letter informing them the proposed transaction was voided when Holmes was unable to obtain financing. A bank turndown letter regarding the May 9th denial of Holmes' loan request was also attached to the October 12th letter.

On November 14, 2005, M&M filed a complaint alleging breach of contract against Holmes as well as breach of fiduciary duty, breach of contract, and breach of contract accompanied by a fraudulent act against Kopatch and the Brokerage. Holmes subsequently filed a Motion for Summary Judgment which was heard by the trial court on March 16, 2007. Ruling from the bench, the trial court granted Holmes' summary judgment motion. M&M now appeals.

STANDARD OF REVIEW

In reviewing an order for summary judgment, the appellate court applies the same standard which governs the trial court under Rule 56 of the South Carolina Rules of Civil Procedure. South Carolina Elec. & Gas Co. v. Town of Awendaw, 359 S.C. 29, 34, 596 S.E.2d 482, 485 (2004). Summary judgment is appropriate when "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Rule 56(c), SCRPC. "On appeal from an order granting summary judgment, the appellate court will review all ambiguities, conclusions, and inferences arising in and from the evidence in a light most favorable to the appellant, the non-moving party below." Willis v. Wu, 362 S.C. 146, 151, 607 S.E.2d 63, 65 (2004).

"The purpose of summary judgment is to expedite disposition of cases which do not require the services of a fact finder." George v. Fabri, 345 S.C. 440, 452, 548 S.E.2d 868, 874 (2001). "A court considering summary judgment neither makes factual determinations nor considers the merits of competing testimony; however, summary judgment is completely appropriate when a properly supported motion sets forth facts that remain undisputed or are contested in a deficient manner." David v. McLeod Reg'l Med. Ctr., 367 S.C. 242, 250, 626 S.E.2d 1, 5 (2006).

LAW/ANALYSIS

I. Motion for Summary Judgment

M&M contends the trial court erred by granting Holmes summary judgment in light of the fact that Holmes' motion failed to state with particularity the grounds for summary judgment. We disagree.

Holmes' motion for summary judgment stated, "[t]he grounds for this motion shall be set forth in a Memorandum of Law to be timely filed with supporting documents and affidavits as required." No such memorandum was filed with the trial court or provided to M&M. At the summary judgment hearing, M&M objected to the hearing itself since Holmes failed to follow Rule 7(b)(1)⁴ of the South Carolina Rules of Civil Procedure. However, M&M did not ask the trial court for any sort of relief or request the motion be dismissed or continued in order to better prepare for the motion. M&M simply objected to the hearing.⁵ The trial court evidently assumed

⁴ Rule 7(b)(1), SCRPC, provides, "[a]n application to the court for an order shall be by motion which, unless made during a hearing or trial in open court with a court reporter present, shall be made in writing, shall state with particularity the grounds therefor, and shall set forth the relief or order sought. The requirement of writing is fulfilled if the motion is stated in a written notice of the hearing of the motion."

⁵ At the hearing M&M's counsel argued, "First I would like to object to this Motion hearing itself in that counsel failed to follow Rule 7(b)(1) of the South Carolina Rules of Civil Procedure... In the Motion itself there are no

M&M was making such a motion for a continuance and denied it. M&M now appeals claiming it was "unable to properly prepare for arguing the Motion for Summary Judgment."

M&M correctly asserts Holmes did not comply with the technical requirements of Rule 7(b)(1), SCRCP. However, M&M did not argue at the trial court that Holmes' failure to follow Rule 7(b)(1), SCRCP, prejudiced it or caused unfair surprise in any way. As such, we find M&M's current argument of prejudice is not preserved for our review. Staubes v. City of Folly Beach, 339 S.C. 406, 412, 529 S.E.2d 543, 546 (2000) ("It is well-settled that an issue cannot be raised for the first time on appeal, but must have been raised to and ruled upon by the trial court to be preserved for appellate review.").

Were we to consider the merits of this argument, this Court would be forced to find M&M cannot make the requisite showing of prejudice necessary to reverse the trial court's denial of a continuance. The grant or denial of a continuance lies with the sound discretion of the trial court and such ruling will not be reversed absent a clear showing of abuse of discretion. State v. Tanner, 299 S.C. 459, 462, 385 S.E.2d 832, 834 (1989). "Moreover, the denial of a motion for a continuance on the ground that counsel has not had time to prepare is rarely disturbed on appeal." Plyler v. Burns, 373 S.C. 637, 650, 647 S.E.2d 188, 195 (2007). M&M has demonstrated no such prejudice at either the trial court or this court.

II. Condition Precedent Located in a Recital

M&M contends the contingency in Paragraph 4 of the Contract is a recital and cannot be construed as a condition precedent. M&M further argues summary judgment was inappropriate because the placement of a

grounds whatsoever given for this Motion. So I would like to object to it on that stance to start with." The trial court stated, "Okay. Well, that Motion is denied." M&M's counsel replied, "Thank you. ...Secondly, your Honor, there are two reasons why counsel should fail on its Motion."

contingency in a recital clause creates a question of fact as to whether a condition precedent existed at all. We disagree.

Paragraph 4 of the Contract states, in full, “[w]hereas, the parties agree that Buyer’s obligation to purchase the assets of the business and Seller’s obligation to sell the assets is contingent upon Buyer’s ability to secure commercial financing at prevailing interest rates.” The Contract also contains a section entitled “Contingencies.” Language similar to Paragraph 4 does not appear in the “Contingencies” section; however, the Contract itself states the headings do not define, limit, or describe the scope or intent of the Contract’s provisions.⁶

Black’s Law Dictionary defines “recital” as “[a]n account or description of some fact or thing; ... [a] preliminary statement in a contract or deed explaining the background of the transaction or showing the existence of particular facts.” (7th ed. 2000). Recitals also traditionally begin with the word “whereas.” Black’s Law Dictionary (8th ed. 2004). Although whereas clauses typically describe the background leading to a contract, the foremost rule of contract interpretation is that courts “must give effect to the intentions of the parties by looking to the language of the contract.” Moser v. Gosnell, 334 S.C. 425, 430, 513 S.E.2d 123, 125 (Ct. App. 1999) (citing Conner v. Alvarez, 285 S.C. 97, 101, 328 S.E.2d 334, 336 (1985)); see Superior Auto. Ins. Co. v. Maners, 261 S.C. 257, 199 S.E.2d 719 (1973) (holding the intention of an instrument is determined by its language, regardless of whether such language is in a whereas clause; language in a recital clearly set forth an agreement’s purpose as a modification); Horry v. Frost, 10 Rich. Eq. 109, 1858 WL 3728 (Ct. App. Eq. 1858) (“A covenant may be as obligatory when expressed by way of recital as if expressed in the formal part of the agreement.”).

⁶ “**HEADINGS AND CONSTRUCTION.** The caption headings are used in this Agreement only as a matter of convenience and for reference and do not define, limit, or describe either the scope of this Agreement or the intent of any provision.” (emphasis in original).

"To discover the intention of a contract, the court must first look to its language – if the language is perfectly plain and capable of legal construction, it alone determines the document's force and effect." Ecclesiastes Production Ministries v. Outparcel Assocs., L.L.C., 374 S.C. 483, 498, 649 S.E.2d 494, 501 (Ct. App. 2007) (citing Superior Auto. Ins., 261 S.C. at 263, 199 S.E.2d at 722); Ellie, Inc. v. Miccichi, 358 S.C. 78, 93, 594 S.E.2d 485, 493 (Ct. App. 2004) ("If its language is plain, unambiguous, and capable of only one reasonable interpretation, no construction is required and the contract's language determines the instrument's force and effect."). If practical, documents will be interpreted to give effect to all of their provisions. Ecclesiastes, 374 S.C. at 498, 649 S.E.2d at 502 (citations omitted); Brady v. Brady, 222 S.C. 242, 246-47, 72 S.E.2d 193, 195 (1952).

The primary test of a contract's character is "the intention of the parties, such intention to be gathered from the whole scope and effect of the language used." Barnacle Broadcasting, Inc. v. Baker Broadcasting, Inc., 343 S.C. 140, 147, 538 S.E.2d 672, 675 (Ct. App. 2000). "The question of whether a provision in a contract constitutes a condition precedent is a question of construction dependent on the intent of the parties to be gathered from the language they employ." Brewer v. Stokes Kia, Isuzu, Subaru, Inc., 364 S.C. 444, 449, 613 S.E.2d 802, 805 (Ct. App. 2005) (citations omitted). "In ascertaining intent, the court will strive to discover the situation of the parties, along with their purposes at the time the contract was entered." Ellie, 358 S.C. at 94, 594 S.E.2d at 493. Parties are governed by their outward expressions and the court is not free to consider their secret intentions. Id. at 94, 594 S.C. at 494.

In the present case, Paragraph 4 clearly states, "the parties agree that Buyer's obligation to purchase the assets of the business and Seller's obligation to sell the assets is contingent upon Buyer's ability to secure commercial financing." (emphasis added). The use of the language "is contingent upon" is unequivocal and patently indicates the parties' respective obligations to buy and sell the business are contingent on Holmes' ability to secure financing. No other meaning could be deduced from such clear and commonly used language. "When a contract is clear and unambiguous, the construction of the contract is a question of law for the court." Moser, 334

S.C. at 430, 513 S.E.2d at 125 (citing Conner, 285 S.C. at 101, 328 S.E.2d at 336). Accordingly, we agree with the trial court that Paragraph 4 of the Contract contains a condition precedent. We will now discuss whether such condition was met.

III. Condition Precedent

M&M contends the trial court erred in awarding summary judgment on the basis of Holmes' inability to meet a condition precedent resulting in a void contract. We disagree.

A condition precedent to a contract is "any fact other than the lapse of time, which, unless excused, must exist or occur before a duty of immediate performance arises." Brewer v. Stokes Kia, Isuzu, Subaru, Inc., 364 S.C. 444, 449, 613 S.E.2d 802, 805 (Ct. App. 2005) (citing Worley v. Yarborough Ford, Inc., 317 S.C. 206, 210, 452 S.E.2d 622, 624 (Ct. App. 1994)). Here, the Contract contained a condition precedent⁷ that Holmes' obligation to purchase the business was subject to her ability to secure commercial financing.

On May 9, 2005, Holmes' request for a loan was denied. At the summary judgment hearing, no evidence was presented regarding Holmes' ability to secure commercial financing, and no evidence was presented to show Holmes obtained financing by the Contract's closing date of May 22, 2005. "The failure of one to perform under a contract because of his inability to obtain financing from a third party on whom he relied to furnish the money will not excuse performance, in the absence of a contract provision in that regard." Worley, 317 S.C. at 209, 452 S.E.2d at 624 (citing 17A Am.Jur.2d Contracts § 680 (1991)). This Contract contained just such a provision relating to Holmes' ability to obtain financing.

⁷ Black's Law Dictionary defines "condition precedent" as "[a]n act or event, other than a lapse of time, that must exist or occur before a duty to perform something promised arises. If the condition does not occur and is not excused, the promised performance need not be rendered." (8th ed. 2004).

In light of this Contract's language and the foregoing reasons, the order of the trial court granting summary judgment in favor of Holmes on M&M's causes of action is

AFFIRMED.

WILLIAMS and PIEPER, JJ., concur.



LEXSEE 860 A2D 312

WAL-MART STORES, INC., a Delaware Corporation, and WACHOVIA BANK OF GEORGIA, N.A., in its capacity as Trustee of the WAL-MART STORES, INC. CORPORATION GRANTOR TRUST, Plaintiffs Below, Appellants, vs. AIG LIFE INSURANCE COMPANY, a Delaware Corporation; HARTFORD LIFE INSURANCE COMPANY, a Connecticut Corporation; WESTPORT MANAGEMENT SERVICES, INC., a Delaware Corporation; INTERNATIONAL CORPORATE MARKETING GROUP, LLC, a Delaware limited liability company; NATIONAL BENEFITS GROUP, INC., dba MARSH FINANCIAL SERVICES, a Minnesota Corporation; SEABURY & SMITH, INC., a Delaware Corporation; MARSH & McLENNAN NATIONAL MARKETING CORPORATION, now known as J&H MARSH & McLENNAN PRIVATE CLIENT SERVICES, INC., a Delaware Corporation, Defendants Below, Appellees.

No. 126, 2004

SUPREME COURT OF DELAWARE

860 A.2d 312; 2004 Del. LEXIS 500; 34 Employee Benefits Cas. (BNA) 1587

August 18, 2004, Submitted
November 4, 2004, Decided

SUBSEQUENT HISTORY: On remand at, Complaint dismissed at *Wal-Mart Stores v. AIG Life Ins. Co.*, 872 A.2d 611, 2005 Del. Ch. LEXIS 44 (Del. Ch., 2005)

PRIOR HISTORY: [**1] Court Below: Court of Chancery of the State of Delaware in and for New Castle County. C.A. No. 19875.

Wal-Mart Stores, Inc. v. AIG Life Ins. Co., 2004 Del. Ch. LEXIS 19 (Del. Ch., Mar. 2, 2004)

DISPOSITION: Reversed and remanded.

COUNSEL: Robert K. Payson and Gregory A. Inskip, Esquires, of Potter Anderson & Corroon LLP, Wilmington, Delaware; Of Counsel: Michael Y. Horton (argued) and David S. Cox, Esquires, of Morgan, Lewis & Bockius LLP, Los Angeles, California; Paul A. Zevnik, Esquire, of Morgan, Lewis & Bockius LLP, Washington, DC; for Appellants.

Richard D. Heins and Carolyn S. Hake, Esquires, of Ashby & Geddes, Wilmington, Delaware; Of Counsel: James F. Jorden and Paul A. Fischer, Esquires, of Jorden Burt LLP, Washington, DC; for Appellee AIG Life Insurance Company.

Elizabeth A. Wilburn, Esquire, of Blank Rome LLP, Wilmington, Delaware; Of Counsel: Ian M. Comisky and Roger F. Cox, Esquires, of Blank Rome LLP, Philadelphia, Pennsylvania; for Appellee National Benefits Group, Inc.

Edward P. Welch, Julie T. Saunders and Edward B. Micheletti, Esquires, of Skadden, Arps, Slate, Meagher & Flom LLP, Wilmington, Delaware; Of Counsel: Marco [**2] E. Schnabl and Michael S. Davi, Esquires, of Skadden, Arps, Slate, Meagher & Flom LLP, New York, New York; for Appellees Marsh Financial Services, Seabury & Smith, Inc., Marsh, Inc., and Marsh & McLennan National Marketing Corporation, now known as J&H Marsh & McLennan Private Client Services.

R. Franklin Balotti, Lisa A. Schmidt and Michael R. Robinson, Esquires, of Richards, Layton & Finger, P.A., Wilmington, Delaware; Of Counsel: Barry A. Chasnoff (argued), and David R. Nelson, Esquires, of Akin Gump Strauss Hauer & Feld LLP, San Antonio, Texas; Michael Quigley and Jeffrey P. Kehne, Esquires, of Akin Gump Strauss Hauer & Feld LLP, Washington, D.C.; Michael Small, Esquire, of Akin Gump Strauss Hauer & Feld LLP, Los Angeles, California; for Appellees Hartford Life Insurance Company and International Corporate Marketing Group.

JUDGES: Before HOLLAND, BERGER and JACOBS, Justices.

OPINION

[*314] *Per Curiam*:

On September 3, 2002, the plaintiff below-appellant, Wal-Mart Corporation ("Wal-Mart"), brought an action in the Court of Chancery. In its amended complaint Wal-Mart asserted legal and equitable claims arising out of insurance policies that Wal-Mart had purchased between 1993 and [*3] 1995 from the defendants, who are certain insurance brokers and insurance providers. The Court of Chancery granted the defendants' motion to dismiss the amended complaint, determining as a matter of law that all of Wal-Mart's claims had accrued between 1993 and 1995, the period during which the policies were purchased. The Court further concluded that there was no basis to toll the running of the three-year statute of limitations. Because Wal-Mart's claims were found to be time-barred, the Court of Chancery granted the motion to dismiss.

Wal-Mart appealed to this Court, contending that: (1) none of its claims accrued before October 19, 1999, a date less than three years before this Chancery action was filed; (2) even if Wal-Mart's claims did accrue before October 19, 1999, the statute of limitations was tolled at least until then; and (3) in any event, the motion to dismiss should have been denied because the issues of when the causes of action accrued and whether the statute of limitations was tolled were fact-intensive and could not be decided on the face of the complaint.

We agree that the limitations defense poses issues that require a more developed record, for which reason [*4] this matter was improperly disposed of on a motion to dismiss. Accordingly, we reverse the judgment of the Court of Chancery and remand the case for further proceedings.

FACTS

The Parties

The pertinent facts, which for present purposes are assumed to be true, appear from the well-pleaded allegations of the complaint. ¹ Wal-Mart is a national retailer that is incorporated in Delaware and whose principal place of business is in Bentonville, Arkansas. ² The defendants are insurance providers and insurance brokers from or through whom Wal-Mart purchased policies of insurance between 1993 and 1995. ³

¹ DEL. CH. R. 56; *Grobow v. Perot*, 539 A.2d 180, 187 (Del. 1988). All references in this Opin-

ion to the "complaint" are to the amended complaint.

² The co-plaintiff, Wachovia Bank of Georgia, is the trustee of the Wal-Mart Corporation Grantor Trust, which was established in December 1993 to purchase the insurance policies at issue in this case. In this Opinion, both plaintiffs are referred to collectively as "Wal-Mart." *Wal-Mart v. AIG Ins. Co.*, 2004 Del. Ch. LEXIS 19, C.A. No. 19875, 2004 WL 405913 (Del. Ch. Mar. 8, 2004) (hereinafter "Op.")

[**5]

³ Defendant AIG Life Insurance Company ("AIG") is a Delaware corporation with its principal place of business in Wilmington, Delaware. Defendant Westport Management Services, Inc. ("Westport") is a Delaware corporation with its principal place of business in Trumbull, Connecticut. Westport served as AIG's representative in connection with the policies at issue in this case. Defendant Hartford Life Insurance Company ("Hartford") is a Connecticut corporation with its principal place of business in Hartford, Connecticut. Defendant International Corporate Marketing Group, LLC ("ICMG") is a Delaware limited liability company with its principal place of business in Florham, New Jersey. ICMG served as Hartford's representative in connection with the policies at issue in this case. In this Opinion, AIG, Hartford, and their respective representatives are referred to collectively as "the insurer-defendants." Defendants Seabury & Smith, Inc., Marsh Financial Services, Marsh, Inc. and Marsh & McLennan National Marketing Corporation ("the Marsh entities"), and National Benefits Group, Inc. ("NBG") acted as insurance brokers for Wal-Mart in obtaining the insurance policies at issue in this case. In this Opinion, the Marsh Entities and NBG are referred to collectively as "the broker-defendants."

[**6] [*315] *Facts Relating to the Dismissal Motion*

Wal-Mart's claims arise out of its purchase from the insurer-defendants of some 350,000 corporate-owned life insurance ("COLI") policies, under which Wal-Mart was named as the beneficiary. Those COLI policies, which insured the lives of Wal-Mart's employees, were purchased as part of a plan whereby the insurers granted Wal-Mart loans that were used to pay the premiums on the policies. Wal-Mart would then deduct the interest payments on those loans from its income for purposes of reducing its federal income taxes. ⁴ During the 1980s and early 1990s, many large corporate employers besides

Wal-Mart had purchased COLI policies under similar tax-reducing COLI plans.

4 Another favorable benefit of the COLI plan was that any policy benefits paid out thereunder would be tax exempt.

In August 1993, Wal-Mart retained the broker-defendants to advise it about using COLI policies to obtain tax benefits. After proposals from several insurance companies were received, [**7] the broker-defendants recommended that Wal-Mart purchase COLI policies from AIG and Hartford. The broker-defendants also recommended that Wal-Mart create and use a Georgia "grantor trust" as the vehicle to purchase the policies, so that Georgia law would govern any "insurable interest" issues that might arise after the policies were purchased. The broker-defendants advised Wal-Mart that Georgia law would provide a favorable result if any employee(s) challenged whether Wal-Mart had a legally valid insurable interest in the lives of its workers.

Between 1993 and 1995, Wal-Mart purchased approximately 350,000 COLI policies from the insurer-defendants, and retained Marsh, Inc. to administer and service those policies. Wal-Mart sought—and obtained—assurances from both the insurer defendants and the broker defendants that: (i) the policies complied with the Internal Revenue Code, (ii) future changes to the tax law were unlikely to impact the policies adversely, and (iii) Wal-Mart had a valid insurable interest in the lives of its employees.

Through 1995, Wal-Mart claimed the federal tax deductions as contemplated under the COLI plan. In 1996, however, the legal landscape changed. As [**8] part of the *Health Insurance Portability and Accountability Act* ("HIPAA"), Congress prospectively disallowed interest deductions for loans used to fund COLI plans. HIPAA also provided for "transitional relief" that allowed taxpayer companies to take deductions in 1997 and 1998 for up to a maximum of 20,000 COLI policies. HIPAA did not, however, disallow any deductions that were taken before January 1, 1996. In response to the HIPAA legislation, Wal-Mart [**16] immediately began "unwinding" its COLI policies, although it took whatever deductions for 1997 and 1998 were allowed under HIPAA's transitional relief provision.⁵

5 The unwinding process was completed in January 2000. 6 113 T.C. 254 (1999), *aff'd*, 254 F.3d 1313 (11th Cir. 2001).

Of importance to Wal-Mart's claims is that HIPAA eliminated the deductibility of interest payments for loans funding COLI policies *prospectively*, but did not disallow deductions taken before 1996; *i.e.*, *retrospec-*

tively. In 1997, nonetheless, [**9] the United States Internal Revenue Service ("IRS") brought several lawsuits in which it sought to disallow *retrospectively* COLI-related tax deductions that the defendants in those cases had taken before 1996. In those lawsuits the IRS characterized the COLI programs as "sham transactions." Wal-Mart was not included among the companies that were named as defendants in the IRS lawsuits.

The first of the IRS cases, *Winn-Dixie Stores Inc. v. C.I.R.*,⁶ was decided by the United States Tax Court on October 19, 1999. In that case, the Tax Court disallowed deductions that were taken in 1993 for the interest that had accrued on Winn-Dixie's COLI policies. After the *Winn-Dixie* decision, two other federal courts retrospectively disallowed COLI tax deductions that had been taken before 1996.⁷ After those adverse decisions were handed down, Wal-Mart negotiated a settlement with the IRS. In that settlement, which was concluded in 2002, most of the COLI-related tax deductions that Wal-Mart had claimed before 1996 were retrospectively disallowed.⁸

6 113 T.C. 254 (1999), *aff'd*, 254 F.3d 1313 (11th Cir. 2001).

[**10]

7 *American Elec. Power, Inc. v. U.S.*, 136 F. Supp. 2d 762 (S.D. Ohio 2001), *aff'd*, 326 F.3d 737 (6th Cir. 2003) (upholding IRS disallowance of deductions of interest paid on loans funding COLI plans); *IRS v. CM Holdings, Inc.*, 254 B.R. 578 (Bankr. D. Del. 2000), *aff'd*, 301 F.3d 96 (3d Cir. 2002) (upholding IRS claim for unpaid taxes after deductions taken for COLI policies).

8 In its complaint, Wal-Mart alleges that the IRS was threatening litigation against it, and that in the face of the decisions in *Winn-Dixie*, *In re CM Holding*, and *American Electric Power, Inc.* Wal-Mart had little choice but to settle. In their answering brief the defendants argue that Wal-Mart "voluntarily" settled with the IRS, and point to cases decided after that settlement which found that the deductions were not sham transactions. See, *Dow Chem. Co. and Subsidiaries v. U.S.*, 250 F. Supp. 2d 748 (E.D. Mich. 2003) *appeal pending*, No. 00-10331-BC (6th Cir.) (filed Oct. 10, 2003). For purposes of a motion to dismiss, however, we accept as true all of the plaintiffs' well-pleaded facts. It is for the trial court ultimately to resolve whether Wal-Mart should have settled with the IRS.

[**11] Separate and apart from the tax deductibility issue, beginning in 2001 Wal-Mart found itself confronted with lawsuits brought by the estates of deceased employees, wherein the estates claimed that Wal-Mart

860 A.2d 312, *; 2004 Del. LEXIS 500, **;
34 Employee Benefits Cas. (BNA) 1587

had no legally valid insurable interest in its employees' lives. In August 2002, in one of these lawsuits, *Mayo v. Hartford Life Ins. Co.*, the Court held that Texas law, rather than Georgia law, governed the insurable interest question, and that under Texas law Wal-Mart had no valid insurable interest in the lives of its Texas employees.⁹ Similar lawsuits challenging Wal-Mart's insurable interest in the employees' lives were pending in other jurisdictions at the time Wal-Mart filed its Court of Chancery action on September 3, [*317] 2002.¹⁰

9 220 F. Supp. 2d 714 (S.D.Tex. 2002), *aff'd*, 354 F.3d 400 (5th Cir. 2004). The Mayo Court imposed a constructive trust in favor of the insured employees' estates upon the policy benefits that had been paid to Wal-Mart under the COLI policies.

10 See, *Rice v. Wal-Mart Stores, Inc.*, 2004 DNH 108, 2004 U.S. Dist. LEXIS 14109, C.A. No. 02-390-B (D.N.H., filed July 23, 2002); *Waller v. AIG Life Ins. Co.*, C.A. No. 4:02-CV-120-Y (N.D. Tex., filed July 3, 2001); *Miller v. Wal-Mart Stores, Inc.*, 102 S.W.3d 706, 46 Tex. Sup. Ct. J. 530 (S.D. Tex., filed Oct. 22, 2002); *Lewis v. Wal-Mart Stores, Inc.*, C.A. No. 02-CV-944-EA(M) (N.D. Okla., filed Dec. 18, 2002).

[**12] Procedural History

Wal-Mart's Chancery complaint alleges several claims arising out of both the retrospective disallowance of the COLI-related tax deductions and the adverse "insurable interest" litigation. Specifically, Wal-Mart's complaint asserts claims against all defendants for: (i) unjust enrichment and restitution, (ii) breach of fiduciary duty, (iii) equitable fraud, (iv) breach of contract, (v) violation of the *Delaware Consumer Fraud Act*, and (vi) declaratory relief. Wal-Mart also asserts a separate claim against the broker defendants for negligence.

With one possible exception, the gravamen of those claims is that the defendants failed to disclose material facts and risks of the COLI plan at the time that Wal-Mart, in reliance upon the defendants' advice, purchased the COLI policies. Wal-Mart contends, however, that one of its claims--unjust enrichment--rests upon a different (non-disclosure) basis, *viz.* frustration of commercial purposes, a ground that is not attributable to any wrongful conduct of the defendants.

The relief that Wal-Mart seeks is an award of money damages equal to the "hard dollar losses" that Wal-Mart incurred by reason of the failure [**13] of the contemplated benefits of the COLI policies. Wal-Mart also seeks to recover all profits the defendants made in connection with the COLI transactions. In addition to and apart from damages, Wal-Mart seeks a declaratory

judgment that the defendants are liable for any future losses Wal-Mart may incur that are associated with the failed policies, including the costs of future "insurable interest" litigation to which Wal-Mart may be subjected. Importantly, however, Wal-Mart does not seek to recover any COLI-related deductions that were prospectively disallowed under HIPAA. Rather, Wal-Mart seeks to recover only those tax benefits that were disallowed *retrospectively* as a result of the adverse federal court rulings, plus the costs it incurred as a result of the insurable interest litigation.

In December 2002, the defendants moved to dismiss Wal-Mart's complaint on the ground that all Wal-Mart's claims were time barred and (alternatively) that Wal-Mart's complaint failed to state a claim upon which relief could be granted. The Court of Chancery granted the motion on the first ground, concluding as a matter of law that all of Wal-Mart's claims were barred by 10 Del. C. § 8106 [**14], the applicable statute of limitations.¹¹

11 Op. at 12, 14. Having determined that the claims were time barred, the Court did not reach the defendants' alternative ground for dismissal.

The Decision of the Court of Chancery

In reaching that result, the Court of Chancery determined that Wal-Mart's claims had accrued between 1993 and 1995, and that accordingly, the action was commenced after the three-year limitations period had expired. The Court also concluded that the running of the limitations period was not tolled because Wal-Mart had been on inquiry notice of its claims more than three years before its lawsuit was commenced.

In concluding that all of Wal-Mart's claims had accrued at the time Wal-Mart purchased the COLI policies--between [*318] 1993 and 1995¹²--the Court identified as the common premise of all the claims (including the claim for unjust enrichment) Wal-Mart's contention that the defendants had failed to disclose the risks inherent in the COLI policies at the time those policies [**15] were purchased.¹³ Because the claims had accrued by 1995, the Court held that Wal-Mart's September 3, 2002 lawsuit was barred by the three-year statute of limitations.

12 *Id.* at 13.

13 *Id.* at 13-14. The Court did not expressly determine whether Wal-Mart's unjust enrichment claim was fault-based (in which case it would also be predicated upon the defendant's alleged failure to disclose), or whether it was no-fault based (in which case the claim would be grounded upon Wal-Mart's frustration of commercial purpose). In a footnote, the trial court suggested, without deciding, that even if Wal-

Mart had stated a claim for unjust enrichment predicated upon the doctrine of commercial frustration (in which case the claim would not accrue until Wal-Mart's commercial purposes had been frustrated) it could not recover under that theory because Wal-Mart had notice of the risks at the time of purchase, with the result that all risks had been contractually allocated to Wal-Mart. Op. at 17, n 53.

The Court of [**16] Chancery also determined as a matter of law that the statute of limitations had not been tolled because Wal-Mart's claims were not inherently unknowable.¹⁴ The Court grounded that conclusion upon various news articles, all published between 1992 and 1995, that discussed certain risks related to COLI policies. The Court also considered two technical advisory memoranda ("TAM") that the IRS had issued to companies other than Wal-Mart. Those TAMs expressed the IRS's legal position that COLI interest deductions should be disallowed because they were "sham" transactions.¹⁵ Although these materials were extrinsic to Wal-Mart's complaint, the Court did not treat those articles and TAMs as having converted the Rule 12(b)(6) motion into a motion for summary judgment. Instead, the Court took judicial notice of the articles and the TAMs, and proceeded to decide the motion under Rule 12(b)(6).

14 *Id.* at 18-19.

15 *Id.* at 6-8, 18-19.

Standard of Review

This Court reviews *de novo*, for errors [**17] of law, the dismissal of a complaint under Court of Chancery Rule 12(b)(6).¹⁶ Under Rule 12(b)(6), the facts alleged in the complaint are taken as true and all inferences are viewed in the light most favorable to the non-moving party (here, Wal-Mart).¹⁷ A dismissal of the claims will be upheld only if it appears from the well-pleaded allegations of the complaint that the plaintiffs would not be entitled to relief under any set of facts that could be proven to support the claims asserted.¹⁸ We find, for the reasons discussed below, that the Court of Chancery erroneously dismissed Wal-Mart's complaint.

16 *VLIW Tech., LLC. v. Hewlett-Packard Co.*, 840 A.2d 606, 610 (Del. 2003).

17 See, *Id.* at 611.

18 *Id.* at 610-11.

Accrual of Wal-Mart's Claims

A critical basis for the Court of Chancery's conclusion that Wal-Mart's claims were time-barred was its determination as a matter of law that all of Wal-Mart's claims had accrued at the time the [**18] COLI policies

were purchased, *i.e.*, between 1993 and 1995. The Court found that the gist of Wal-Mart's claims was the defendants' alleged failure to disclose to Wal-Mart, at the time the policies were purchased, the [**19] material risks associated with the COLI policies, including the tax deductibility and the insurable interest risks.

The starting point of the Court of Chancery's analysis (with which all parties agree) is that the applicable statute of limitations is 10 Del. C. § 8106, which imposes a three-year period of limitations on Wal-Mart's tort, contract, and fiduciary duty claims; and that that three-year period applies by analogy to proceedings in equity.¹⁹ The Court further found that Wal-Mart's claim for unjust enrichment was also controlled by the three-year statute of limitations.²⁰ Accordingly, the Court concluded, for Wal-Mart's lawsuit to have been timely filed, the claims must have accrued no earlier than September 3, 1999 (three years before Wal-Mart filed its action), because under Section 8106, the three-year period of limitations begins to run when the cause of action "accrues."²¹

19 Op. at 12 (citing 10 Del. C. § 8106 and *Fike v. Ruger*, 754 A.2d 254, 260 (Del. Ch. 1999), *aff'd* 752 A.2d 112 (Del. 2000)).

[**19]

20 Op. at 12 (citing *Merck v. SmithKline Beecham Pharms. Co.*, 1999 Del. Ch. LEXIS 242, C.A. No. 15443-NC, 1999 WL 669354 at *42 (Del. Ch. Aug. 5, 1999), *aff'd*, 766 A.2d 442 (Del. 2000)).

21 Op. at 13.

This Court has repeatedly held that a cause of action "accrues" under Section 8106 at the time of the wrongful act, even if the plaintiff is ignorant of the cause of action.²² As noted, the Court of Chancery found as a matter of law, that the wrongful acts charged in the complaint occurred at the time Wal-Mart purchased the COLI policies. Although Wal-Mart contends that that conclusion was improperly reached in the context of a Rule 12(b)(6) dismissal motion, we need not decide that question. Even if it is assumed that Wal-Mart's cause of action accrued by 1995 at the latest, the pleaded facts permit a reasonable inference that the statute of limitations was tolled, *i.e.*, did not begin to run, until October 19, 1999—less than three years before this lawsuit was filed.

22 *SmithKline Beecham Pharms. Co. v. Merck & Co.*, 766 A.2d 442, 450 (Del. 2000); *Isaacson, Stolper & Co. v. Artisan's Sav. Bank*, 330 A.2d 130, 132 (Del. 1974).

[**20] *Tolling of the Statute of Limitations*

The trial court held as a matter of law that the statute of limitations period was not tolled as to Wal-Mart's claims. Even after a cause of action accrues, the "running" of the limitations period can be "tolled" in certain limited circumstances.²³ Under the "discovery rule" the statute is tolled where the injury is "inherently unknowable and the claimant is blamelessly ignorant of the wrongful act and the injury complained of."²⁴ In such a case, the statute will begin to run only "upon the discovery of facts 'constituting the basis of the cause of action or the existence of facts sufficient to put a person of ordinary intelligence and prudence on inquiry which, if pursued, would lead to the discovery' of such facts."²⁵

23 *Coleman v. PriceWaterhouseCoopers, LLC*, 854 A.2d 838, 842-43 (Del. 2004) (discovery rule applied to malpractice action against accounting firm, because a layperson is unable to detect negligence in accounting practices); *Layton v. Allen*, 246 A.2d 794 (Del. 1968) (statute of limitations was tolled when both patient and doctor were unaware that a foreign object was left in the patient; the injury was inherently unknowable until the patient first experienced pain as a result of the object).

[**21]

24 *Coleman*, 854 A.2d at 842.

25 *Id.* (quoting *Becker v. Hamada, Inc.*, 455 A.2d 353, 356 (Del. 1982) (emphasis in original)). 26 *In re Santa Fe Pacific Corp. S'holder Litig.*, 669 A.2d 59, 68 (Del. 1995).

The Court of Chancery held as a matter of law that Wal-Mart was on inquiry notice of its claims more than three years [*320] before it filed its Chancery action. Rejecting Wal-Mart's contention that its claims were "inherently unknowable" before September 3, 1999, the Court cited a "barrage of relevant information" that (it held) was available to Wal-Mart and put Wal-Mart on inquiry notice of its claims. The cited information included the TAMs issued by the IRS, as well as several newspaper articles that had been published during the mid 1990s.

That conclusion was erroneous for three separate reasons. First, the trial court was not free to consider the TAMs and newspaper articles on this Rule 12(b)(6) motion, because these materials were neither attached to, nor incorporated by reference into, the complaint. Matters extrinsic to a complaint [**22] generally may not be considered in a ruling on a motion to dismiss.²⁶ Court of Chancery Rule 12(b) provides that if the court considers matters outside the pleadings, the motion shall be "treated as one for summary judgment" and the parties must be given an opportunity to take discovery. On a motion to dismiss, the Court may consider documents

that are "integral" to the complaint, but documents outside the pleadings may be considered only in "particular instances and for carefully limited purposes."²⁷ Here, Wal-Mart's complaint did not refer to any newspaper articles or TAMs, and the record does not otherwise establish that these documents were publicly filed.²⁸ Accordingly, the Court could not properly consider those materials, under judicial notice principles, to resolve conflicting factual inferences on a Rule 12(b)(6) motion to dismiss.

26 *In re Santa Fe Pacific Corp. S'holder Litig.*, 669 A.2d 59, 68 (Del. 1995).

27 *Id.* at 69.

28 See, *DiLorenzo v. Edgar*, 2004 U.S. Dist. LEXIS 4991, C.A. No. 03-841-SLR, 2004 WL 609374 at *2 (D. Del. Mar. 24, 2004) (On a motion to dismiss, the court may take judicial notice of the contents of documents *required by law to be filed, and actually filed, with federal or state officials*) (emphasis added); *Southmark Prime Plus, L.P. v. Falzone*, 776 F. Supp. 888, 891-92 (D. Del. 1991) (court could judicially notice contents of court records from another jurisdiction and SEC filings, but not letters sent by defendants because the letters addressed disputed facts); *Coca-Cola v. Whistle Co. of America*, 20 F.2d 261, 262 (D. Del. 1927) (court may not take judicial notice of the patents of prior art cited in motion to dismiss); *In re Wheelbrator Technologies, Inc. S'holders Litig.*, C.A. No. 11495, 1992 WL 212595 (Del. Ch. Sept. 1, 1992) (publicly filed documents, including certificate of incorporation, are judicially noticeable on a motion to dismiss).

[**23] Second, even if the articles and TAMs were properly before the Court, they do not conclusively demonstrate that Wal-Mart was on inquiry notice of its claims before September 3, 1999. The cited articles, all published between 1992 and 1995, discussed the existence of the COLI tax loophole and their use by many companies. The articles also discussed proposed legislation that could *prospectively* eliminate the loophole. But, the articles did not discuss *retrospective* disallowance of the deductions, which is the gravamen of Wal-Mart's tax-related claims. Moreover, on this record it is far from clear that the TAMs were sufficient to put Wal-Mart on inquiry notice of its tax-related claims against these defendants. TAMs are IRS rulings issued to private companies. As such, those rulings have questionable value either as binding or persuasive authority as to non-parties.²⁹ The record does not [**321] disclose whether these TAMs were publicly available before 1999, an important consideration because under 26 *USCA* § 6110(g)(5), the Secretary of the Treasury is not invariably required to make technical advice memoranda publicly available.

29 See, *Amtel, Inc. v. U.S.*, 31 Fed Cl. 598 (Fed. Cl. 1994), *aff'd* 59 F.3d 181 (Fed. Cir. 1995); *Teichgraeber v. Commissioner*, 64 T.C. 453 (1975) (TAM was not subject to discovery and was exempted from disclosure under 5 *USCA* § 522(b), and private letter rulings that may have been issued by IRS to other taxpayers were not relevant to taxpayers case).

[**24] Third, and finally, neither the newspaper articles nor the TAMs contain any facts that would alert Wal-Mart to its claims relating to the insurable interest question. The newspaper articles and TAMs do not discuss the insurable interest-related issue, nor did the Court of Chancery make any specific determination of how Wal-Mart was placed on inquiry notice of its insurable interest-related claims.

What the complaint does allege is that Wal-Mart did not settle the retrospective tax deduction claims with the IRS until 2002, and that no court had retrospectively disallowed the pre-1996 tax deductions until the Tax Court's *Winn-Dixie* decision was handed down on October 19, 1999. The first case that challenged whether Wal-Mart had a legally valid insurable interest in its employees was not filed until 2001. Wal-Mart alleges that it

relied on the advice of the broker-defendants in establishing the Georgia Grantor Trust, and that its injuries resulting from the insurable interest litigation were inherently unknowable until at least one court had determined that Georgia law did not govern the insurable interest issue. Those pleaded facts create a reasonable inference that Wal-Mart's [**25] tax-related injuries were inherently unknowable before October 1999, and that Wal-Mart's insurable interest-related injuries were inherently unknowable before 2002. Those same pleaded facts also create a reasonable inference that Wal-Mart was blamelessly ignorant of the "wrongful acts." To be sure, the pleaded facts also create reasonable inferences to the contrary. A Rule 12(b)(6) motion, however, is not a proper procedural vehicle to resolve conflicting inferences of fact.

Accordingly, the Court of Chancery legally erred in deciding, as a matter of law, that the statute of limitations was not tolled.

CONCLUSION

For the foregoing reasons, the judgment of the Chancery Court is reversed, and this case is remanded for further proceedings consistent with this Opinion.

C In re Coca-Cola Enterprises, Inc. Shareholders
Litigation
Del.Ch., 2007.

Only the Westlaw citation is currently available.

UNPUBLISHED OPINION. CHECK COURT
RULES BEFORE CITING.

Court of Chancery of Delaware.
In re **COCA-COLA ENTERPRISES, INC.**
SHAREHOLDERS LITIGATION.
C.A. No. 1927-CC.

Submitted: Aug. 6, 2007.

Decided: Oct. 17, 2007.

Norman M. Monhait, of Rosenthal, Monhait & Goddess, P.A., Wilmington, Delaware; of Counsel: James E. Miller, Patrick A. Klingman, and Karen M. Leser, of Shepherd, Finkelman, Miller & Shah, LLC, Chester, Connecticut; Scott R. Shepherd, James C. Shah, and Nathan Zipperian, of Shepherd, Finkelman, Miller & Shah, LLC, Media, Pennsylvania; Mark C. Gardy and James S. Notis, of Gardy & Notis, LLP, Englewood Cliffs, New Jersey; Nadeem Faruqi, of Faruqi & Faruqi, LLP, New York, New York; Craig B. Smith, of Smith, Katzenstein & Furlow, LLP, Wilmington, Delaware, Attorneys for Plaintiffs.
Edward P. Welch and Jennifer C. Voss, of Skadden, Arps, Slate, Meagher & Flom LLP, Wilmington, Delaware; of Counsel: Jay B. Kasner, of Skadden, Arps, Slate, Meagher & Flom LLP, New York, New York, Attorneys for Defendants The Coca-Cola Company, J. Alexander M. Douglas, Gary P. Fayard, Irial Finan, Steven J. Heyer, Robert A. Keller, James E. Chestnut, Joseph R. Gladden, Jr., and Deval L. Patrick.

Samuel A. Nolen, Srinivas M. Raju, and Michael R. Robinson, of Richards, Layton & Finger, P.A., Wilmington, Delaware; of Counsel: Todd R. David, John A. Jordak, Jr., and Ambreen A. Delawalla, of Alston & Bird LLP, Atlanta, Georgia, Attorneys for Nominal Defendant Coca-Cola Enterprises, Inc. and Defendants Fernando Aguirre, John R. Alm, E. Liston Bishop III, Howard G. Buffet, John L. Clendenin, James E. Copeland, Jr., Calvin Darden, Rick L. Engum, J. Trevor Eyton, Marvin J. Herb, L. Phillip Humann, John E. Jacob, Donna A. James,

Summerfield K. Johnston III, Summerfield K. Johnston, Jr., Jean-Claude Killy, Lowry F. Kline, Patrick J. Mannelly, Paula R. Reynolds, and G. David Van Houten.

MEMORANDUM OPINION

CHANDLER, Chancellor.

*1 While there may never be a decisive victory in the Great American Cola Wars,^{FN1} the plaintiffs in this action seem to think they got the wrong stock, baby-uh huh.^{FN2} Plaintiffs, who are shareholders in Coca-Cola Enterprises, Inc. ("CCE"), the primary bottler and distributor of Coca-Cola products, conclude their fifty-page complaint with a lengthy and unfavorable comparison between the stock price performance of their company, CCE, with Pepsi Bottlers Group, its counterpart in the world of Pepsi. Dismayed that the Pepsi Bottlers Group has outperformed CCE despite the fact that the Coca-Cola Company ("Coke") has outperformed PepsiCo, plaintiffs have authored a tale of abuse spanning two decades, in which defendant Coke has, "[s]ince CCE's creation,"^{FN3} somehow high jacked the CCE board and forced its members to operate CCE solely to benefit Coke. Stripped of its histrionics, however, the amended complaint essentially alleges claims that challenge the fundamental nature of the relationship between Coke and CCE—a relationship that plaintiffs acknowledge was established over twenty years ago in a perpetual Master Bottle Contract. Sobered from their rhetorical high by defendants' motions to dismiss, plaintiffs have attempted to save their case by showing equitable tolling, but their attempt has not satisfied their burden. Consequently, for the reasons described later, plaintiffs' amended complaint is dismissed as time-barred.

^{FN1} See *Pepsico, Inc. v. The Coca-Cola Co.*, 114 F.Supp.2d 243, 245 (S.D.N.Y.2000) (noting the fabled marketing battle between Coke and Pepsi).

^{FN2} Cf. The Pepsi Legacy 1990, http://www.pepsi.com/ads_and_history/legacy/1990/1990.php (last visited Oct. 17, 2007) (recalling the Diet Pepsi Commercial featuring Ray Charles and the

"Uh Huh Girls" singing "You've Got the Right One, Baby").

FN3. Am. Compl. ¶ 1.

I. BACKGROUND

A. Procedural History

On February 7, 2006, the International Brotherhood of Teamsters filed a derivative action in this Court on behalf of CCE against Coke and current and former members of the CCE board of directors alleging breaches of fiduciary duty. In March and April of the same year, two substantially similar complaints were filed here by Robert Lang and Natalie Gordon. Lang and Gordon moved to consolidate, and the Teamsters filed a competing consolidation motion. After a brief dispute between the plaintiffs, the three filed an amended, consolidated complaint on September 29, 2006. On October 16, 2006, defendants filed their motions to dismiss. Following briefing and oral argument, this is my decision on the motions.

B. Facts

Nominal defendant CCE is the largest bottler and distributor of Coke beverage products in the world. Initially formed as a wholly owned subsidiary of Coke, CCE was spun off in 1986 as an independent, public company. Its relationship with former parent Coke, of course, continued pursuant to a series of contracts and licensing agreements, the most important of which is the 1986 Master Bottle Contract ("MBC").

The MBC defines the contours of the relationship between CCE and Coke that persists today.^{FN4} In addition to establishing that CCE may buy Coke's syrup and concentrate, bottle, and sell the soda, the MBC grants Coke certain rights and saddles CCE with certain responsibilities. For example, CCE must allow Coke representatives access to CCE facilities to conduct inspections to assure Coke that CCE is "complying with instructions" and other standards.^{FN5} The MBC also provides that: (1) Coke has the right to pull the final product if it is not satisfied and can force CCE to recall the product after shipment;^{FN6} (2) Coke has the right to set and revise prices of its concentrates and syrups;^{FN7} (3) CCE must "develop and stimulate and satisfy fully the demand" for Coke beverages;^{FN8}

(4) CCE must "cooperate in and vigorously promote" all joint marketing programs with Coke;^{FN9} (5) CCE must present for approval to Coke its "plans for the ensuing year" and the plans must be approved by Coke;^{FN10} (6) CCE must report on its progress to Coke at least quarterly if not more frequently;^{FN11} (7) Coke may give to CCE technology it has or develops;^{FN12} and (8) CCE must furnish financial or other records to Coke upon request.^{FN13}

FN4. The Court may properly consider the contract in deciding this motion to dismiss because plaintiffs expressly refer to and rely on the contract in their amended complaint. *In re Dean Witter P'ship Litig.*, C.A. No. 14816, 1998 WL 442456, at *6 n. 46 (Del. Ch. July 17, 1998), *aff'd*, 725 A.2d 441 (Del. 1999); see also *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 860 A.2d 312, 320 (Del. 2004) ("On a motion to dismiss, the Court may consider documents that are 'integral' to the complaint"). The amended complaint references the MBC and its terms repeatedly. See Am. Compl. ¶¶ 6, 46, 55, 56, 66, 94-97.

FN5. MBC art. IV, ¶ 11.

FN6. *Id.* at ¶ 13.

FN7. *Id.* at art. V., ¶ 14.

FN8. *Id.* at art. VI, ¶ 17.

FN9. *Id.* at ¶ 18.

FN10. *Id.* at ¶ 20(a).

FN11. *Id.* at ¶ 20(b).

FN12. *Id.* at art. XII, ¶ 36.

FN13. *Id.* at ¶ 40(c).

*2 Plaintiffs allege that Coke and the directors of CCE have worked together to abuse the relationship between the two companies. At the heart of the amended complaint is the contention that by maximizing sales volume, CCE has maximized Coke's profits at the expense of CCE's. CCE's decisions to

push for increased volume can only be explained, plaintiffs contend, by Coke and the individual defendants' desire to aid Coke's financial future. Connected to this core theme are arterial sections flowing with vitriol about Coke's domination, channel stuffing, and harmful experimentation in various warehouse delivery systems.

1. *Coke's Alleged Domination and Abuse*

Despite conceding that Coke has directly named just three of CCE's thirteen directors and that Coke owns just a thirty-six percent share of CCE, plaintiffs maintain that Coke controls and dominates CCE. Plaintiffs trace the history of this domination to CCE's origins in the mid-1980s.

Plaintiffs stuff much of the amended complaint with conclusory allegations of control and abuse.^{FN14} An allegation is conclusory when it merely states a generalized conclusion with no supporting facts. For example, the bald assertion that "Coke ultimately controls virtually every aspect of CCE's operations and profitability in a manner designed to maximize Coke's own financial condition" is conclusory.^{FN15} That allegation does not explain how Coke controls CCE; it perfunctorily concludes that Coke exerts control without offering any support. Plaintiffs' amended complaint is riddled with similar, conclusory statements.^{FN16}

^{FN14} On a motion to dismiss, this Court assumes that the well-pleaded allegations in a complaint are true, but does not accept the truthfulness of conclusory allegations. *In re Gen. Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 168 (Del.2006).

^{FN15} Am. Compl. ¶ 54.

^{FN16} See, e.g., Am. Compl. ¶ 50 ("For all practical purposes, Coke controls CCE.").

There are, however, several substantive allegations of control and abuse. First, the MBC provides "Coke with the ability to manipulate its own financial condition from sales to CCE through, among other things, price changes, sales volume changes, financing terms, and other terms of payment and conditions."^{FN17} Second, Coke forces "CCE to pay a

higher price for beverage base and concentrate than CCE otherwise would have paid" if the MBC were negotiated at arm's length.^{FN18} Third, a 2002 Sales Growth Initiative Agreement between Coke and CCE incentivized increased sales volume at the expense of profit by providing CCE with payments from Coke if it hit certain sales volume thresholds.^{FN19} Fourth, "Coke is directly involved in CCE's annual business planning process" and can manipulate this process by withholding its approval.^{FN20}

^{FN17} Am. Compl. ¶ 55.

^{FN18} *Id.* at ¶ 56.

^{FN19} *Id.* at ¶¶ 59-64.

^{FN20} *Id.* at ¶¶ 66-67.

2. *Channel Stuffing*

The plaintiffs define "channel stuffing" as "last minute forced sales increases,"^{FN21} and argue that Coke pushed this practice on CCE. Plaintiffs allege that Coke caused CCE to engage in channel stuffing by giving advance warning of future price increases, giving discounts in price for increased orders in volume or other incentives for ordering more, and over-delivery of product. Plaintiffs cite as an example the fact that CCE allegedly parked numerous trailers filled with product in the parking lots of various accounts in the early 1990s. Plaintiffs contend that this practice persisted (albeit to a lesser extent) in 2004 in the Kansas City area and that CCE would count this parked product as having been sold.

^{FN21} *Id.* at ¶ 85.

3. *Wal-Mart Delivery*

*3 Finally, plaintiffs assert that the individual defendants and Coke forced CCE to change the way it delivers products to the Wal-Mart account. Previously, CCE and the other Coke bottlers utilized a direct store delivery distribution method whereby the bottlers could negotiate for the pricing and marketing of the beverages at each individual retail location. For large, national accounts (like Wal-Mart), CCE negotiated on behalf of all Coke's major bottlers. The amended complaint alleges that in 2004 Coke somehow

"forced" CCE to test a new warehouse delivery system for the Wal-Mart account. In 2005, plaintiffs say, "Coke directed that CCE propose [to the other bottlers] the switch to the Warehouse Delivery system"^{FN22} for delivery of the Powerade energy drink for all Wal-Mart stores. Plaintiffs stress that CCE did so without following the proper notice procedures outlined in its agreement with the other bottlers and that this switch is detrimental to "the long-term best interests of CCE."^{FN23}

FN22. Pls.' Answering Br. 9.

FN23. Am. Compl. ¶ 112.

C. Defendants' Motions to Dismiss

Defendants have moved to dismiss the complaint pursuant to Court of Chancery Rule 12(b)(6) for failure to state a claim upon which relief can be granted and Rule 23.1 for failure to adequately plead demand futility. Defendants offer a litany of reasons to dismiss this action. First, defendants argue that the amended complaint is barred by the statute of limitations or the doctrine of laches, because plaintiffs' claims arise out of contractual agreements formed in the mid-1980s. Second, defendants assert that the amended complaint's allegations are factually insufficient to state a claim as a matter of law, because the allegations are conclusory and speculative. Third, defendants say that the CCE board of directors is comprised of a majority of independent directors and that the decisions challenged in the amended complaint were well informed and made in the exercise of sound business judgment.

D. Plaintiffs' Response

Plaintiffs obviously disagree. They challenge whether a statute of limitations / laches defense can appropriately be raised at this stage in the litigation and argue that, even if such a defense is properly presented now, it is inapplicable in this case. Further, plaintiffs stress that their allegations are legally sufficient and that demand would have been futile.

II. ANALYSIS

A. Standard of Review and Pleading Requirements

Court of Chancery Rule 8(a) requires that pleadings give notice of the claim being asserted through a "short and plain statement" that shows "the pleader is entitled to relief."^{FN24} When a complaint fails to do so, it must be dismissed under Rule 12(b)(6). In reviewing a motion to dismiss, this Court must, as noted above, take as true all well-pleaded factual allegations and make every reasonable inference in favor of the plaintiff. The Court will not, however, give any credence to conclusory allegations or wildly speculative and unreasonable conjecture.^{FN25}

FN24. Ct. Ch. R. 8(a).

FN25. See *Malpiede v. Townson*, 780 A.2d 1075, 1083 (Del.2001).

*4. Plaintiffs' amended complaint purports to state a cause of action for breach of the duty of loyalty against Coke ^{FN26} and the individual defendants. To establish a breach of the fiduciary duty of loyalty, plaintiffs must show that the defendants either (1) "stood on both sides of the transaction and dictated its terms in a self-dealing way," or (2) "received in the transaction a personal benefit that was not enjoyed by the shareholders generally."^{FN27}

FN26. Coke strenuously denies that it is a controlling shareholder of CCE and, therefore, denies that it owes any fiduciary duties. Because I have decided to dismiss the complaint on other grounds, I need not address this issue.

FN27. *Chaffin v. GNI Group, Inc.*, C.A. No. 16211-NC, 1999 WL 721569, at *5 (Del. Ch. Sept. 3, 1999); see also *Joyce v. Cuccia*, C.A. No. 14953, 1997 WL 257448, at *5 (Del. Ch. May 14, 1997) ("To state a legally sufficient claim for breach of the duty of loyalty, plaintiffs must allege facts showing that a self-interested transaction occurred, and that the transaction was unfair to the plaintiffs.").

Immediately, the Court may dispose of the claim related to the distribution of beverages to Wal-Mart because the amended complaint manifestly fails to allege facts showing that a breach of the duty of loyalty occurred in connection with that transaction. The switch to a warehouse distribution arrangement with Wal-Mart was effected by an agreement between

CCE (on behalf of the consortium of bottlers) and Wal-Mart. Plaintiffs have not alleged that either Coke or any of the individual defendants are somehow on Wal-Mart's side, nor are there any facts that show any of the defendants will derive a personal benefit from the transaction. Plaintiffs have included a conclusory assertion that this distribution arrangement will harm the long-term interests of CCE and will help Coke, but this amorphous allegation is insufficient.^{FN28} By failing to allege facts showing the elements of a breach of the fiduciary duty of loyalty with respect to the Wal-Mart distribution arrangement, plaintiffs have failed to state a claim upon which relief can be granted.

FN28. If a complaint were held sufficient simply because it restates the legal elements of a particular cause of action, Rule 8(a) would be rendered meaningless. Plaintiffs need not offer prolix tales of abuse belabored by needless details, but plaintiffs must allege facts sufficient to show that the legal elements of a claim have been satisfied.

Plaintiffs' other claims are supported by more robust factual allegations, but they are ultimately no more successful. Because plaintiffs' other claims are really complaints about the painful effects of the terms of the 1986 MBC, the claims accrued in 1986 and are time-barred.

B. Statute of Limitations and Doctrine of Laches

Courts of Equity came into being because universally applicable legal rules are bound to work injustice in certain individual cases.^{FN29} As such, it would be antithetical for a court of equity to blindly apply a statute of limitations to bar equitable claims.^{FN30} Nevertheless, because "equity follows the law,"^{FN31} it is firmly established that this Court can and will apply a statute of limitations by analogy.^{FN32} In fact, the Supreme Court has held that "[a]bsent unusual circumstances, a court of equity will deny a plaintiff relief when suit is brought after the analogous statutory period."^{FN33} Where, as here, a plaintiff seeks money damages for breach of fiduciary duties, the claim will "be subject to the three-year limitations period of 10 Del. C. § 8106" and this Court need not "engage in traditional laches analysis."^{FN34}

FN29. H. Jefferson Powell, "*Cardozo's Foot*": *The Chancellor's Conscience and*

Constructive Trusts, 56 LAW & CONTEMP. PROBS. 7, 7-8 (1993).

FN30. A statute of limitations sets a strict time period after which a claim, if not made, is barred. The doctrine of laches, on the other hand, bars a particular plaintiff from bringing a claim about which he had knowledge where the plaintiff's unreasonable delay prejudiced a defendant. Laches is an intensely factual analysis. See *Fed. United Corp. v. Havender*, 11 A.2d 331, 345-346 (Del.1940) (noting that delays of even as short as two months have been held to constitute laches under Delaware law).

FN31. E.g., *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 584 (Del. Ch.2007).

FN32. *Acerno v. Goldstein*, C.A. No. 20056, 2004 WL 1488673, at *2 (Del. Ch. June 29, 2004) ("The time fixed by the analogous statute of limitations is deemed to create a time period beyond which delay is presumptively unreasonable for purposes of laches."); *Fike v. Ruger*, 754 A.2d 254, 260 (Del. Ch.1999), *aff'd*, 752 A.2d 112 (Del.2000); *In re MAXXAM, Inc.*, 659 A.2d 760, 769 (Del. Ch.1995); *Bovay v. H.M. Bylesby & Co.*, 29 A.2d 801, 803 (1943); see also 27A AM.JUR.2d Equity § 198 (West 2007).

FN33. *U.S. Cellular Inv. Co. of Allentown v. Bell Atl. Mobile Svs., Inc.*, 677 A.2d 497, 502 (Del.1996).

FN34. *Atlantis Plastics Corp. v. Sanunons*, 558 A.2d 1062, 1064 (Del. Ch.1989).

Defendants argue that the claims in the amended complaint all arise from the 1986 MBC. As such, defendants contend, those claims are time-barred under section 8106. Plaintiffs have three responses. First, plaintiffs argue that defendants may not use the statute of limitations or the doctrine of laches as a defense in a motion to dismiss. Second, plaintiffs say their claims are based on discrete actions that occurred within the past three years rather than on the 1986 contract. Third, plaintiffs contend that if the statute of

limitations applies, it has been equitably tolled. For the reasons stated below, none of these responses is persuasive and the claims in the amended complaint are barred under section 8106.

1. *This Court May Properly Consider the Statute of Limitations and the Doctrine of Laches when Reviewing a Motion to Dismiss.*

*5 Plaintiffs devote considerable energy attempting to persuade this Court that a motion to dismiss is an improper mechanism by which one might determine whether claims are time barred. In so doing, plaintiffs (at best) misunderstand or (at worst) disregard well settled Delaware law. As this Court has stated time and time again, when the allegations of a complaint show the action was commenced too late, a defendant may properly seek dismissal under the statute of limitations or the doctrine of laches.^{FN35} Plaintiffs have in fact correctly conceded that the statute of limitations is used as a presumptive guide for this Court,^{FN36} but plaintiffs have failed to overcome that presumption. The allegations of the amended complaint itself affirmatively establish the plaintiffs' claims are based on the 1986 MBC.

FN35. E.g., *Tyson Foods*, 919 A.2d at 585; *Kahn v. Seaboard*, 625 A.2d 269, 277 (Del. Ch.1993); *Boeing Co. v. Shrontz, C.A. No. 11273*, 1992 WL 81228, at *2 (Del. Ch. Apr. 20, 1992); see also 1 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS § 13.8 (3d ed., supp.2006).

FN36. Pls.' Answering Br. at 17.

2. *The Wrath of Kahn: Claims Accrue at the Moment of Initial Wrongdoing-Not when their Effects Are Felt.*

In *Kahn v. Seaboard Corp.*, Chancellor Allen dismissed a complaint that alleged a breach of fiduciary duty claim against directors who "structure[d] the contract] so as to obtain better terms for Flour than would have been the case had the transactions been negotiated on an arm's length basis."^{FN37} Specifically, he found that "[t]he wrong attempted to be alleged is the use of control over Seaboard to require it to enter into a contract that was

detrimental to it and beneficial, indirectly, to the defendants. Any such wrong occurred at the time that enforceable legal rights against Seaboard were created."^{FN38} Ultimately, it is that principle that dooms plaintiffs' amended complaint.

FN37. 625 A.2d 269, 270 (Del. Ch.1993) (quoting complaint).

FN38. *Id.* at 271.

Under Delaware law, a plaintiff's cause of action accrues at the moment of the wrongful act-not when the harmful effects of the act are felt-even if the plaintiff is unaware of the wrong.^{FN39} Defendants contend plaintiffs' claims of abuse by Coke and so-called "channel stuffing" are really challenges to the 1986 MBC. Plaintiffs, of course, resist this characterization. Instead, plaintiffs counter, their complaint challenges certain transactions that occurred within the last three years. Specifically, they challenge: (1) a 2002 Sales Growth Initiative Agreement that incentivized increased volume in sales; (2) the revisions to the 2004 Rocky Mountain Division business plan; (3) the use of databases by Coke to track daily CCE sales; and (4) channel-stuffing practices.

FN39. *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 860 A.2d 312, 319 (Del.2004) ("This Court has repeatedly held that a cause of action 'accrues' under Section 8106 at the time of the wrongful act, even if the plaintiff is ignorant of the cause of action."); *Albert v. Alex Brown Mgmt. Servs., Inc.*, C.A. No. 762-N, 2005 WL 1594085, at * 18 (Del. Ch. June 29, 2005) ("The court reiterates that a claim accrues at the time of the alleged wrongdoing, and not when the plaintiff suffered a loss."); *Fike v. Ruger*, 754 A.2d 254, 260 (Del. Ch.1999) ("A cause of action accrues at the moment of the wrongful act, even if the plaintiff is ignorant of the wrong."); *aff'd*, 752 A.2d 112 (Del.2000); *In re Dean Witter P'ship Litig.*, C.A. No. 14816, 1998 WL 442456, at *4 (Del. Ch. July 17, 1998) ("The general law in Delaware is that the Statute of Limitations begins to run, i.e., the cause of action accrues, at the time of the alleged wrongful act, even if the plaintiff is ignorant of the cause of action."); *aff'd*, 725

A.2d 441 (Del.1999); cf. Schreiber v. R.G. Bryan, 396 A.2d 512, 516 (Del. Ch.1978) (“[W]hat must be decided is when the specific acts of alleged wrongdoing occur, and not when their effect is felt.”); 2 EDWARD P. WELCH, ET AL., FOLK ON THE DELAWARE GENERAL CORPORATION LAW § 327.32 (2007-1 supp.) (“Generally, the determinative issue is when the specific acts of alleged wrongdoing occurred, and not when their effect is felt.”).

The claim challenging the 2002 Sales Growth Initiative is clearly time-barred under the three-year statute of limitations. The amended complaint quotes from the agreement itself and challenges actual provisions and terms of the contract. Plaintiffs appear to have conceded as much by abandoning this argument in their answering brief.

The claim challenging the revisions to the 2004 Rocky Mountain Division Business Plan is also time barred. Plaintiffs argue that in 2004 Coke forced CCE to revise the plan to push for an increase in sales volume at the expense of CCE's profits. Under the 1986 MBC, however, CCE is *obligated* to submit its annual plans to Coke and those plans must be approved by Coke.^{FN40} The revised plan did not call for a waste of CCE's assets or resources; rather, it called for a 5.5% gross profit gain combined with an increase in projected sales volumes instead of the 7.3% gain combined with a decrease in projected sales called for in the original plan. This was clearly permitted and expected under the terms of the 1986 MBC. If plaintiffs have a valid claim on this point, they had it in 1986.

FN40. MBC art. VI, § 20(a).

*6 The claim challenging the use of databases by Coke to track sales of CCE also appears to have been abandoned by plaintiffs. Even if it were not, the use of databases provided by Coke to CCE is clearly permitted by and contemplated in the 1986 MBC.^{FN41} Again, if there is a valid claim, it is a claim that existed in 1986.

FN41. See *id.* at art. XII, § 36.

Finally, the crux of the claim challenging the alleged channel stuffing is that “Coke routinely has forced

CCE to purchase additional beverage base or concentrate beyond CCE's immediate needs, and/or has raised prices on such materials, without adequate notice, all in order to improve Coke's own financial condition and meet Coke's earnings guidance and sales volume projections.”^{FN42} Coke has every right, however, under the 1986 MBC to “revise at any time, in its sole discretion, the price of any of the Concentrates or Syrups, the terms of payment, and other terms and conditions of supply, any such revision to be effective immediately upon notice to the Bottler.”^{FN43} Plaintiffs have alleged only that Coke exercised its rights under the contract.

FN42. Am. Compl. ¶ 85.

FN43. MBC art. V, § 14(a).

Each one of these claims is, therefore, time-barred because each “hinges upon the allegations that the terms and conditions established by a contract are unfair to the plaintiff[s].”^{FN44} Plaintiffs attempt to avoid dismissal by claiming that they are challenging the actions taken in the last three years,^{FN45} but concede that the contract “may have provided the means by which the Defendants effectuated their breaches of fiduciary duty.”^{FN46} Plaintiffs took a similar position (and made a similar concession) at oral argument.^{FN47} This is precisely the argument considered and rejected by Chancellor Allen in *Kahn*^{FN48} and by the Federal District Court in *Marvel*.^{FN49} I likewise reject it. The actions challenged in the amended complaint represent the manifestation of the bargain struck in 1986 between Coke and CCE.^{FN50} Absent tolling, therefore, these claims are barred by section 8106.^{FN51}

FN44. *In re Marvel Entm't Group, Inc.*, 273 B.R. 58, 74 (D.Del.2002) (interpreting Delaware law).

FN45. Plaintiffs' reliance on *Teachers' Ret. Sys. of La. v. Aidinoff* is misplaced. There, the Court found a claim based on actions taken under a contract was not time-barred because the contract had a provision that granted an annual right of termination. 900 A.2d 654, 666 (Del. Ch.2006). The Court found that the complaint was actually challenging the decision of the defendants to continue to honor the harmful contract when they could

have opted out each year. *Id.* Here, the 4 plaintiffs admit that the MBC is perpetual. Am. Compl. ¶ 95; MBC art. VIII, ¶ 24.

FN46. Pls.' Answering Br. at 21.

FN47. Transcript of Oral Argument at 53.

FN48. *Kahn v. Seaboard Corp.*, 625 A.2d 269, 271 (Del. Ch. 1993).

FN49. *Marvel*, 273 B.R. at 74.

FN50. Compare *Kahn*, 625 A.2d at 270 (quoting complaint: "defendants have violated their duty of loyalty by structuring such transaction so as to obtain better terms for Flour than would have been the case had the transaction been negotiated on an arm's-length basis"), with Am. Compl. ¶ 56 ("Coke also requires CCE to pay a higher price for beverage base and concentrate than CCE otherwise would have paid to Coke if CCE's beverage base agreements with Coke had been negotiated at arms' length").

FN51. Plaintiffs' claims may also be barred under 8 Del. C. § 327, which requires ownership of stock contemporaneously with the wrongs challenged in a derivative suit. Plaintiffs have only alleged that they owned CCE stock from October 15, 2003, to the present, but the wrong actually complained of is the 1986 MBC. See 7547 *Partners v. Beck*, 682 A.2d 160 (Del. 1996) (strictly applying section 327 to bar a derivative suit).

3. *Plaintiffs Have Not Met their Burden of Establishing that the Statute has Been Equitably Tolled.*

When a complaint asserts a claim that is, as here, on its face barred by the statute of limitations, plaintiffs bear the burden of pleading specific facts demonstrating that the statute was tolled.^{FN52} Equitable tolling will toll the statute of limitations "for claims of wrongful self-dealing, even in the absence of actual fraudulent concealment, where a plaintiff reasonably relies on the competence and good faith of a fiduciary."^{FN53} Nevertheless, neither equitable tolling

nor any other theory can toll the statute of limitations beyond the point at which the plaintiff had actual knowledge or should have been aware of the facts giving rise to the wrong.^{FN54}

FN52. *In re Dean Witter P'ship Litig.*, C.A. No. 14816, 1998 WL 442456, at *6 (Del. Ch. July 17, 1998), *aff'd*, 725 A.2d 441 (Del. 1999); *Yaw v. Talley*, C.A. No. 12882, at *6 (Del. Ch. Mar. 2, 1994).

FN53. *Dean Witter*, 1998 WL 443456, at *6; see also *Kahn*, 625 A.2d at 275.

FN54. *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 585 (Del. Ch. 2007) ("Even where a defendant uses every fraudulent device at its disposal to mislead a victim or obfuscate the truth, no sanctuary from the statute will be offered to the dilatory plaintiff who was not or should not have been fooled.").

Plaintiffs summarily state that they "did not know or have reason to know of Defendants' self-interested wrongdoing prior to 2004."^{FN55} The amended complaint itself, however, belies that assertion by relying on and quoting from documents publicly filed with the SEC prior to 2004.^{FN56} Moreover, plaintiffs undercut their own argument with the affected rhetoric of the complaint's allegations. In the amended complaint, plaintiffs conjure images of the long-suffering whipping boy CCE, mistreated "[s]ince [its] creation"^{FN57} by Coke, whose abuses are recounted by CCE's former employees with "unanimity."^{FN58} With respect to the channel stuffing allegations, the amended complaint details practices from the "early 1990s,"^{FN59} and it chronicles Coke's alleged domination from the 1980s to the present.^{FN60} Finally, Coke and CCE have publicly disclosed their agreements with one another and their individual finances in filings under the Federal securities laws. The plaintiffs have railed against particular actions that have occurred in the last three years, but those actions were the foreseeable results of a contract formed in 1986. Intermittently, plaintiffs seem to acknowledge as much.^{FN61} As in *Tyson*, "[i]f plaintiffs believed that these contracts were unfair, they could reasonably have been aware of their injuries in [1986]."^{FN62} Consequently, plaintiffs have failed to meet their burden of establishing that the

statute of limitations has been tolled.

In re Coca-Cola Enterprises, Inc.
Not Reported in A.2d, 2007 WL 3122370 (Del.Ch.)

FN55. Pls.' Answering Br. at 20.

END OF DOCUMENT

FN56. See, e.g., Am. Compl. ¶¶ 62-64.

FN57. Id. at ¶ 1.

FN58. Id. at ¶¶ 68-73.

FN59. Id. at ¶ 91.

FN60. Id. at ¶¶ 46-49.

FN61. See Pls.' Answering Br. at 21 (admitting that the MBC "may have provided the means by which the Defendants effectuated their breaches of fiduciary duty"); Transcript of Oral Argument at 53 ("[W]e believe that the control arises as a result of the contractual relationships and the actions taken pursuant to those contractual relations....").

FN62. In re Tyson Foods, Inc. Consol. S'holder Litig., 919 A.2d 563, 586 (Del. Ch.2007).

III. CONCLUSION

*7 CCE's relationship with Coke may not be optimal, but it is guided by a contract formed in 1986. If the plaintiffs in this action or if CCE's shareholders in general believe it is time CCE took a more aggressive, competitive stance vis-à-vis Coke, they ought to put pressure on management; they cannot seek to do so by dressing up their frustration in the guise of fiduciary duty claims. Because the amended complaint objects to so-called wrongs that all rationally flow from Coke and CCE's 1986 agreement, plaintiffs' claims accrued in 1986. Because plaintiffs have alleged facts that show they either were or should have been aware of these claims for far more than three years before filing this action, the amended complaint is dismissed as time-barred.

IT IS SO ORDERED.

Del.Ch.,2007.

**BROWN v. AUTOMATED MARKETING
SYSTEMS, INC.**
Del.Ch. 1982

UNPUBLISHED OPINION. CHECK COURT
RULES BEFORE CITING.

Court of Chancery of Delaware, Sussex County.
BROWN
v.
AUTOMATED MARKETING SYSTEMS, INC.
No. 6715

March 22, 1982

Plaintiff brought a putative class action against Automated Marketing Systems, Inc. to enjoin the consummation of a merger which had been overwhelmingly approved by the shareholders. Plaintiff had not become a shareholder of defendant until after the proposed merger had been publicly announced. Defendants moved for summary judgment. The court of chancery, per Vice-Chancellor Brown, held that summary judgment should be entered in favor of defendants based on the fact that plaintiff was not a stockholder at the time of the transaction complained of (public announcement of a resolution approving a merger plan) and that the plaintiff, being charged with knowledge of the merger plan, has no standing to bring an action based on that plan after purchasing stock in the corporation.

[1] Corporations 101 ↪ 207

101 Corporations

101X Members and Stockholders

101X(C) Suing or Defending on Behalf of Corporation

101k207 k. Persons Entitled to Sue or Defend. Most Cited Cases

Corporations 101 ↪ 211(2)

101 Corporations

101X Members and Stockholders

101X(C) Suing or Defending on Behalf of Corporation

101k211 Pleading

101k211(2) k. Allegations as to Interest of or Injury to Plaintiff or Complainant. Most Cited Cases

Corporations 101 ↪ 320(4)

101 Corporations

101X Officers and Agents

101X(C) Rights, Duties, and Liabilities as to Corporation and Its Members

101k320 Actions Between Shareholders and Officers or Agents

101k320(4) k. Right to Sue, and Parties in General. Most Cited Cases

In order to bring any type of derivative action to correct alleged acts of corporate mismanagement, it is necessary that the plaintiff either be a stockholder at the time of the transaction complained of, or that his stock thereafter devolve upon him by operation of law. DEL. CODE ANN. tit. 8, § 327.

[2] Corporations 101 ↪ 320(4)

101 Corporations

101X Officers and Agents

101X(C) Rights, Duties, and Liabilities as to Corporation and Its Members

101k320 Actions Between Shareholders and Officers or Agents

101k320(4) k. Right to Sue, and Parties in General. Most Cited Cases

The right of a stockholder to sue exists because of special injury to him for which otherwise he is without redress. If his interest is trifling, and the injury therefore of no consequence, he cannot sue to compel righting of wrongs to the corporation.

[3] Corporations 101 ↪ 207

101 Corporations

101X Members and Stockholders

101X(C) Suing or Defending on Behalf of Corporation

101k207 k. Persons Entitled to Sue or Defend. Most Cited Cases

Corporations 101 ↪ 320(4)

101 Corporations

101X Officers and Agents

101X(C) Rights, Duties, and Liabilities as to Corporation and Its Members

101k320 Actions Between Shareholders and Officers or Agents

101k320(4) k. Right to Sue, and Parties in General. Most Cited Cases

One who held no stock at the time of the mismanagement ought not to be allowed to sue, unless the mismanagement or its effects continue and are injurious to him, or it affects him specially and peculiarly in some other manner.

141 Corporations 101 ↪ 207

101 Corporations

101X Members and Stockholders

101X(C) Suing or Defending on Behalf of Corporation

101k207 k. Persons Entitled to Sue or Defend. Most Cited Cases

Corporations 101 ↪ 320(4)

101 Corporations

101X Officers and Agents

101X(C) Rights, Duties, and Liabilities as to Corporation and Its Members

101k320 Actions Between Shareholders and Officers or Agents

101k320(4) k. Right to Sue, and Parties in General. Most Cited Cases

The purchaser of corporate stock ought to take things as he found them when he voluntarily acquired an interest. So long as he is not injured in what he got when he purchased, and holds exactly what he got and in the condition in which he got it, there is no ground for complaint.

151 Equity 150 ↪ 1

150 Equity

150I Jurisdiction, Principles, and Maxims

150I(A) Nature, Grounds, Subjects, and Extent of Jurisdiction in General

150k1 k. Nature and Source of Jurisdiction. Most Cited Cases

Parties 287 ↪ 1

287 Parties

287I Plaintiffs

287I(A) Persons Who May or Must Sue

287k1 k. Capacity and Interest in General.

Most Cited Cases

Where a plaintiff has no standing to bring an action in equity, he may not be availed by the fact that others have been injured by the defendants' wrongdoing.

Where a plaintiff has no standing to bring an action in equity, he may not be availed by the fact that others have been injured by the defendants' wrongdoing.

****467 BROWN, Vice-Chancellor**

***1 Gentlemen:**

Defendants have moved for summary judgment in this purported class action brought on behalf of the public shareholders of Automated Marketing Systems, Inc. ('Automated'). The basis for the motion is that plaintiff purchased her shares in Automated after the public announcement of the merger proposal which she now seeks to attack on behalf of herself and other shareholders of Automated. Because of this factor, which came to light only after discovery and after defendants had agreed voluntarily to defer the consummation of the merger pending the outcome of an expedited trial on the merits, defendants, expressing appropriate outrage, contend that the plaintiff lacks standing and that she is estopped from maintaining a suit to challenge the terms of the merger.

The undisputed facts indicate that on December 16, 1981 a press release was made by Automated indicating that its board of directors had unanimously adopted a resolution approving a plan of merger under the terms of which the public shareholders of Automated would receive \$10.00 per share in return for their elimination from the surviving corporate entity. At the time plaintiff was not a shareholder of Automated.

On December 21, 1981, through a broker, plaintiff purchased 100 shares of Automated. By that time the market price of the shares had risen to 9 1/2. Thus, including brokerage commissions, it cost the plaintiff

\$986 to purchase shares for which, according to the previous public announcement, she stood to receive \$1,000 upon completion**468 of the merger. Thus, at the time, her \$986 purchase carried the potential for a \$14 profit.

On February 16, 1982, Automated sent out its proxy statement concerning the merger, indicating that a shareholders meeting would be held on March 9, 1982 for the purpose of voting on the proposition. Plaintiff thereupon brought this suit to enjoin the merger, alleging an improper purpose and alleging also that an inadequate consideration was being paid for the interests of the public shareholders. Since the filing of defendants' motion for summary judgment, plaintiff has moved to amend her complaint so as to allege deficiencies in the proxy statement.

Defendants charge that plaintiff is attempting to assert a purchased grievance and that as a consequence her suit should be dismissed. While that conclusion is certainly inferable from the foregoing facts, it is not something which is indisputably established on the present record, and consequently I decline to rely on this premise in reaching a decision.

[1] At the same time I do feel that the defendants' motion for summary judgment should be granted. At § Del.C. § 327 it is expressed as the policy of our corporate law that in order to bring any type of derivative action to correct alleged acts of corporate mismanagement it is necessary that the plaintiff either be a stockholder at the time of the transaction complained of, or that his stock thereafter devolve upon him by operation of law. The policy embodied in this section is the prevention of the evil of purchasing stock in order to maintain a derivative action designed to attack a transaction which occurred prior to the purchase of the stock. Maclary v. Pleasant Hills, Inc., Del.Ch., 109 A.2d 830 (1954); Newkirk v. W. J. Rainey, Inc., Del.Ch., 76 A.2d 121 (1950).

*2[2][3][4] This seems no more than an extension of the general equitable principles long ago set forth by Roscoe Pound in Home Fire Ins. Co. v. Barber, Neb. Supr., 93 N.W. 1024 (1903) with regard to the standing of a shareholder to sue for corporate wrongs. As stated at 93 N.W. 1029:

'The right of the stockholder to sue exists because of special injury to him for which otherwise he is without

redress. If his interest is trifling, and the injury therefore of no consequence, he cannot sue to compel righting of wrongs to the corporation. (Citations omitted.) Hence there is obvious reason for holding that one who held no stock at the time of the mismanagement ought not to be allowed to sue, unless the mismanagement or its effects continue and are injurious to **469 him, or it affects him specially and peculiarly in some other manner.

'Except in such cases, the purchaser ought to take things as he found them when he voluntarily acquired an interest. If he was defrauded in the purchase, he should sue the vendor. As to the corporation and its managers, so long as he is not injured in what he got when he purchased, and holds exactly what he got and in the condition in which he got it, there is no ground for complaint.'

So here, and giving plaintiff the benefit of the doubt that her shares were not purchased for the purpose of placing her in a position to institute litigation, plaintiff purchased her 100 shares for \$986 with full knowledge, or at least charged with knowledge, that she would receive \$1,000 for them when and if the merger was approved. The vote taken at the March 9, 1982 shareholders meeting overwhelmingly approved the terms of the merger, even discounting any votes controlled by the individual defendants. Thus, the plaintiff has not been injured in her expectation and she is in a position to receive exactly that which the defendants announced publicly that she would receive prior to the time that she made her purchase. Under Dean Pound's rationale she has no grounds to complain as to the judgment of the defendants in determining the \$10 per share price of as to the purpose which motivated the board of Automated to adopt the merger plan.

Moreover, there is no merit in her contention that because she was unaware of the gravity of the alleged wrongdoings until such time as she received the proxy statement, her right to sue should be measured from that point rather than from the time of her purchase. Nor can there be an argument that no wrong occurs until the merger is voted upon and approved.

The transaction of which she complains is the act of Automated's board in passing a resolution approving the merger on terms which she feels to be unfair to the public shareholders. As in Newkirk v. W. J. Rainey,

Not Reported in A.2d

Page 4

Not Reported in A.2d, 1982 WL 8782 (Del.Ch.), 7 Del. J. Corp. L. 466

(Cite as: Not Reported in A.2d, 1982 WL 8782 (Del.Ch.), 7 Del. J. Corp. L. 466)

Inc., supra, it is not the merger itself that constitutes the wrongful act of which plaintiff complains, but rather it is the fixing of the terms of the transaction which will be finalized by the consummation of the merger which provides the foundation for the suit. So viewed, there is no continuing wrong but only an alleged wrong which occurred prior to the date on which plaintiff purchased her stock.

*3**470 Finally, I take note that in resisting the summary judgment motion plaintiff has argued mightily that the facts so far unearthed by discovery and analysis show, in the opinion of her counsel, an unprecedented breach of fiduciary duty on the part of the individual defendants, thus, presumably, indicating that this action should be maintained as a class action on behalf of all other public shareholders regardless of any personal drawbacks attributable to her position.

[5] However, as stated in *Home Fire Ins. Co. v. Barber* at 93 N.W. 1035, and more recently approved in *Bangor Punta Operations v. Bangor & A. R. Co.*, 417 U.S. 703, 94 S.Ct. 2578, 41 L.Ed.2d 418 (1974):

'If a wrongdoer deserves to be punished, it does not follow that others are to be enriched at his expense by a court of equity. A plaintiff must recover on the strength of his own case, not on the weakness of the defendant's case. It is his right, not the defendant's wrongdoing, that is the basis of recovery. When it is disclosed that he has no standing in equity, the degree of wrongdoing of the defendant will not avail him.'

Compare *Courtland Manor, Inc. v. Leeds*, Del.Ch., 347 A.2d 144 (1975).

Accordingly, I conclude that summary judgment should be entered in favor of the defendants and the complaint of the plaintiff dismissed for lack of standing to maintain the cause of action alleged. The plaintiff's motion to amend the complaint is denied. An appropriate order may be submitted.

Del.Ch. 1982

Brown v. Automated Marketing Systems, Inc

Not Reported in A.2d, 1982 WL 8782 (Del.Ch.), 7 Del.

J. Corp. L. 466

END OF DOCUMENT

In re Beatrice Companies, Inc. Litigation
Del., 1987.

(The decision of the Court is referenced in the Atlantic Reporter in a 'Table of Decisions Without Published Opinions.')

Supreme Court of Delaware.
In re BEATRICE COMPANIES, INC.
LITIGATION.
Nos. 155 and 156, 1986.

Submitted: Nov. 6, 1986.

Decided: Feb. 20, 1987.

Rehearing Denied: March 24, 1987.

Chancery Court, New Castle County

AFFIRMED.

Before CHRISTIE, Chief Justice, and HORSEY, and MOORE, Justices.

ORDER

HORSEY, Justice.

*1 This 20th day of February, 1987, upon consideration of the briefs of the parties, it appears to the Court that:

(1) Appellants, William Leighton ("Leighton") and Joseph A. and Shirley S. Yablonski ("the Yablonskis"), appeal from a decision of the Court of Chancery approving the settlement and dismissal of consolidated stockholders' class and derivative actions against Beatrice Companies, Inc. ("Beatrice"); its Board of Directors; James L. Dutt, a former officer of Beatrice; Kohlberg, Kravis, Roberts & Co. ("KKR"); and Joel E. Smilow, a member of the KKR investment group. The settlement disposed of all claims arising out of the acquisition of Beatrice, through a leveraged buy-out, organized by KKR.

(2) On October 16, 1985, KKR submitted to Beatrice's Board of Directors an offer to acquire the company in a transaction in which Beatrice's stockholders would receive \$40 in cash and preferred stock valued at \$5 per share for each share of Beatrice common stock. The Board, however, after consulting its investment

bankers, unanimously rejected the offer as inadequate.

(3) On October 29, 1985, KKR made a second proposal in which it increased its offer to \$40 in cash and \$7 in market value of preferred stock. The Board authorized management to begin discussions with KKR in respect to its revised offer and to explore alternatives that would maximize the value of Beatrice to its stockholders. Thereafter, Beatrice's investment bankers contacted approximately seventy-five potential buyers to determine whether they were interested in acquiring all or part of Beatrice. In response to these inquiries, Dart Group Corp. expressed an interest in acquiring Beatrice for \$48 per share in cash.

(4) On November 12, 1985, KKR made a revised offer to acquire Beatrice in a transaction consisting of \$43 in cash and preferred stock valued at \$7 per share. This offer, however, contained the following conditions: (a) a provision (the "Termination Payment Provision") that, if the acquisition was not completed and another party acquired thirty percent of Beatrice's common stock or made a firm proposal to acquire Beatrice for more than \$50 per share, KKR would be entitled to a cancellation fee of \$123 million; and (b) a provision (the "Asset Option Provision") granting KKR an option to purchase either Beatrice's grocery food and Tropicana subsidiaries for \$2.391 billion or certain alternative assets, including the Tropicana subsidiary, for a price of \$2.412 billion. The November 12 offer was conditioned upon its acceptance by the Board by no later than November 13, 1985.

(5) On November 13 and 14, 1985, at a special Board meeting, Beatrice's investment bankers indicated that from a financial point of view, KKR's November 12 offer was fair to Beatrice's stockholders. The Board also learned that the Dart Corp. had withdrawn its earlier offer. Additionally, KKR agreed to cause Beatrice, after the proposed merger, to honor amendments to existing executive compensation and severance agreements that the Board had authorized prior to the initial KKR proposal.

*2 (6) On November 14, 1985, the Board accepted KKR's November 12 offer and entered into (a) a merger agreement with BCI, a corporation KKR

formed for the acquisition, which included the Termination Payment Provision; and (b) a separate agreement with BCI adopting the Asset Option Provision. The merger agreement also prohibited the solicitation of alternative proposals or offers for Beatrice or any of its subsidiaries.

(7) Plaintiffs filed nine class and derivative claims in the Court of Chancery and seven related actions were filed in Illinois. These actions were subsequently consolidated in this proceeding. The complaints basically alleged (a) that Beatrice's officers and directors, aided and abetted by KKR, had breached their fiduciary duties to the Beatrice stockholders in entering into the merger agreement and the executive compensation and severance agreements; and (b) that the Termination Payment Provision was excessive and illegal and the Asset Option Provision invalid. Plaintiffs sought damages, an order enjoining the operation of the Termination Payment and Asset Option Provisions; and an order enjoining consummation of the proposed merger.

(8) Following extensive negotiations between Beatrice, KKR, and the plaintiffs, the parties entered into a memorandum of understanding on February 1, 1986. The memorandum: terminated the agreement containing the Asset Option Provision; reduced the \$123 million Termination Payment Provision to approximately \$19 million; revised the merger agreement to delete the no-shopping provision, thus, allowing Beatrice to solicit other offers or proposals; confirmed Beatrice's right to pay a cash dividend of up to \$.45 per share of common stock; and increased the annual interest rate on the BCI preferred stock issue in connection with the merger from 14 percent to 15- 1/4 percent to be paid on a quarterly instead of a semiannual basis. Beatrice and its executives also agreed to reductions of \$23 million in their executive compensation and severance agreements.

(9) On March 11, 1986, the parties entered into a stipulation and agreement of settlement in accordance with the terms of the memorandum. Thereafter, the Court of Chancery certified a class consisting of all Beatrice stockholders at the close of business on February 20, 1986 (the record date for the stockholder vote on the proposed merger) and ordered a hearing to determine if the settlement was fair and adequate. Notice of the hearing was mailed to the February 20 holders of record, advising them of their right to

appear and object.

(10) Although Leighton and the Yablonskis did not appear at the hearing, both parties submitted written statements objecting to the settlement. Leighton objected on the grounds that BCI was in violation of various provisions of the federal securities laws. The Yablonskis challenged the certification of the class, the conduct of the parties' attorneys, the adequacy of the terms of the proposed settlement, and the plaintiffs' attorneys' fee request.

*3 (11) After careful review, the Court of Chancery determined that the benefits provided to Beatrice and the class constituted "fair and reasonable compensation for the claims." The Court also found the application of plaintiffs' counsel for attorneys' fees to be "fair and reasonable in the light of the work involved, the contingent nature of the undertaking and the other appropriate factors." Thereafter, on April 16, 1986, the Court entered an order dismissing the claims with prejudice.

(12) On appeal, Leighton raises numerous arguments, many of which were not raised below, based upon provisions of the federal securities laws. Leighton, however, concedes that he did not purchase his Beatrice stock until sometime after: (a) the time of the Beatrice directors' alleged breach of fiduciary duty; (b) February 20, 1986, the record date for the stockholder vote on the proposed merger; and (c) he reviewed the March 11, 1986 proxy statement and the terms of the merger and settlement.

(13) Under settled Delaware law, an objector who purchases a claim by buying stock after the alleged wrongdoing has occurred lacks standing to challenge the wrongdoing in a derivative capacity. See 8 Del.C. § 327; Newkirk v. W.J. Rainey, Inc., Del.Ch., 76 A.2d 121, 123 (1950). Section 327 provides that a plaintiff cannot maintain a derivative action challenging corporate mismanagement unless he was a stockholder at the time of the transaction complained of or had his stock devolve upon him by operation of law. 8 Del.C. § 327. The purpose of this section is to prevent potential plaintiffs from purchasing stock in order to maintain a derivative action attacking a transaction which occurred prior to the purchase of the stock. Schreiber v. Bryum, Del.Ch., 396 A.2d 512, 516 (1978); Jones v. Taylor, Del.Ch., 348 A.2d 188, 191 (1975); Newkirk, supra.

(14) In the case of a proposed merger, the plaintiff must have been a stockholder at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged. *Newkirk, supra*. Therefore, Leighton clearly lacks standing to challenge derivatively the merger; and he concedes he does not meet class certification. Therefore, his claims must be dismissed.

(15) The Yablonskis assert essentially two arguments: *one*, the settlement was not fair and reasonable to the shareholders because it extinguished valuable claims for inadequate consideration; and that as to absentee shareholders, the settlement procedures lacked due process; and *two*, that the Chancery Court abused its discretion in its award of attorneys fees.

(16) The Yablonskis' due process argument was not raised prior to or at the settlement hearing, which the Yablonskis did not attend. It was included in a post-hearing letter to the Court by the Yablonskis, taking exception to the

proliferating abuse of the class action mechanism to extinguish legitimate damage claims, to insulate corporate wrongdoers from judicial scrutiny and to sanction the payment of grossly excessive, wholly-unwarranted attorneys fees to class counsel by an opposing party. My due process rights and the due process rights of thousands of other Beatrice stockholders require, at a minimum, close scrutiny if not presumptive invalidity of settlements such as the one involved here.

*4 An examination of the record and of the Court of Chancery's careful consideration of the issues that were timely raised require rejection of the asserted due process claim as factually and legally unsubstantiated. Here, there is no assertion that the settlement procedure of the derivative and class suits did not fully comply with the controlling rules of the Court of Chancery, Rules 23 and 23.1. Thus, *Weid v. Valhi, Inc., Del.Supr., 466 A.2d 9 (1983)*, upon which the Yablonskis rely, is clearly inapposite.

(17) The Yablonskis' due process argument is simply an inarticulated use of a code word for their principal assertion that the settlement was "intrinsically unfair" and is, thus, subsumed within their argument *one*,

attacking the fairness of the settlement to the Beatrice shareholders.

(18) Our standard of review of the settlement of a class or derivative action is well established. This Court should "review the record solely for the purpose of determining whether or not, by the exercise of his business judgment, the Chancellor abused his discretion." *Neponsit Inv. Co. v. Abramson, Del.Supr., 405 A.2d 97, 100 (1979)*. It is not our function to determine the intrinsic fairness of the settlement or to exercise our own business judgment respecting its merits. *Polk v. Good, Del.Supr., 507 A.2d 531, 536 (1986)*. Rather, we limit ourselves solely to the question of whether the Court abused its discretion in exercising its business judgment. *Polk, supra*. If its findings are supported by the record and are the product of an orderly and logical deductive process, they will be accepted. *Levitt v. Bouvier, Del.Supr., 287 A.2d 671, 673 (1972)*.

(19) The Court-after considering the benefits conferred on Beatrice's stockholders due to the negotiated changes, the financial improvements that the settlement contemplated, and the arguments of the stockholders who objected to the merger-concluded that the settlement was fair and reasonable. Based upon our review of the record, we find ample evidence to support the Chancellor's conclusion that "both Beatrice and the class ... will receive real and substantial benefits from the settlement." Accordingly, the Court of Chancery did not abuse its discretion in approving the proposed settlement.

(20) Our standard of review of the Yablonskis' second argument, *two*, is whether the Court abused its discretion in its award of attorneys' fees. *Krinsky v. Helfand, Del.Supr., 156 A.2d 90, 95 (1959)*. Here, the Court found "that the amount requested is fair and reasonable in the light of the work involved, the contingent nature of the undertaking and the other appropriate factors." The record discloses that the Court properly considered counsel's time and effort in the lawsuit and the Court's reasoning for its conclusion. It also weighed the amount of the award with the benefits the Beatrice stockholders received. Hence, we find no abuse of discretion and conclude that the Court properly approved the application for attorneys' fees.

*5 NOW, THEREFORE, IT IS ORDERED that the judgment of the Court of Chancery be and the same

522 A.2d 865
522 A.2d 865, 1987 WL 36708 (Del.Supr.)
(Cite as: 522 A.2d 865, 1987 WL 36708 (Del.Supr.))

Page 4

hereby is

AFFIRMED.

Del., 1987.
In re Beatrice Companies, Inc. Litigation
522 A.2d 865, 1987 WL 36708 (Del.Supr.)

END OF DOCUMENT



LEXSEE 625 A2D 269

ALAN R. KAHN, Plaintiff, v. SEABOARD CORPORATION, SEABOARD FLOUR CORPORATION, H. HARRY BRESKY, OTTO BRESKY, JR., and CHARLES M. GOLDMAN, Defendants.

Civil Action No. 11485

COURT OF CHANCERY OF DELAWARE, NEW CASTLE

625 A.2d 269; 1993 Del. Ch. LEXIS 2

July 30, 1992, Submitted
January 14, 1993, Decided

COUNSEL: [**1] Robert D. Goldberg, Esquire, of BIGGS AND BATTAGLIA, Wilmington, Delaware; Attorney for Plaintiff.

Samuel A. Nolen, Esquire and Daniel A. Dreisbach, Esquire, of RICHARDS, LAYTON & FINGER, Wilmington, Delaware; Attorneys for Defendants.

JUDGES: ALLEN

OPINION BY: ALLEN

OPINION

[*270] *OPINION*

ALLEN, Chancellor

The complaint purports to be brought derivatively on behalf of Seaboard Corporation against Seaboard's controlling (75 %) stockholder, Seaboard Flour Corporation ("Flour") and three individuals who comprise the board of directors of Seaboard, two of whom are the controlling (71 %) shareholders of Flour. The charge is that the individual defendants "required the Company to enter into numerous transactions with Flour . . . which benefit Flour at the Company's expense." Cplt. P5. Identified are three transactions, only one of which is relevant to the present motion. It concerns a ten year time charter of seven vessels entered into in 1986 between a wholly owned subsidiary of Seaboard ("Overseas Limited") and subsidiaries of H & O Shipping Ltd., a subsidiary of Flour. It is alleged that:

Pursuant to said agreements, Overseas is required to pay substantial management fees and other sums, pur-

portedly for administration [**2] and insurance (collectively "Fees"), in addition to time charter costs. For the year ended December 31, 1986, Overseas paid \$ 3,347,000 in time charter costs and an additional \$ 4,273,000 in fees. For the year ended December 31, 1987, Overseas paid \$ 3,019,000 in time charter costs and an additional \$ 3,609,000 in fees.

* * *

In the transaction described above, [defendants] have violated [their duty of loyalty] by structuring such transaction so as to obtain better terms for Flour than would have been the case had the transactions been negotiated on an arm's-length basis.

Cplt. PP5A and 6.

This action was commenced in April 1990, more than three years after the creation of the time charter. Delaware Code *Section 8106* of title 10 establishes three years as the governing limitation of actions period for any:

action to recover damages caused by an injury unaccompanied with force or resulting indirectly from the act of the defendant . . .

10 Del. C. § 8106 (1991). Relying upon this statute, defendants have now moved that so much of the complaint as purports to state a claim predicated on the 1986 time charter be dismissed as untimely.

Plaintiff, of course, resists. He contends [**3] that the wrongs allegedly arising from the 1986 time charter are continuing wrongs [*271] that are not barred by applicable limitation provisions in any event. Secondly, he asserts that what is alleged constitutes wrongful self-dealing by a corporate fiduciary and is not subject to the

terms of *Section 8106* but to the more flexible equitable doctrine of laches, which it is implied would not justify dismissal here. Finally, plaintiff argues that the record is not sufficiently developed to permit the court to rule on the timeliness of the institution of the suit at this time.

For the reasons that follow I conclude that defendants' motion must be granted, but that plaintiff shall have sixty days in which he may file an amended complaint that sets forth facts constituting good grounds to toll the running of the statute in this instance.

I.

I turn first to the continuing wrong theory offered by plaintiff. The facts alleged, if they constitute a wrong, do not, in my opinion, constitute a continuing wrong for purposes of analyzing a limitations bar. The wrong attempted to be alleged is the use of control over Seaboard to require it to enter into a contract that was detrimental to it and beneficial, [**4] indirectly, to the defendants. Any such wrong occurred at the time that enforceable legal rights against Seaboard were created. Suit could have been brought immediately thereafter to rescind the contract and for nominal damages which are traditionally available in contract actions. Complete and adequate relief, if justified, could be shaped immediately or at any point thereafter.

This type of case is unlike a continuing tort where the defendant continues, without right, an action injurious to plaintiff. Where a continuing wrong acts as an answer to the defense of limitations it is typically the case that plaintiff can prove her claim by reference only to actions within the limitations period. Thus, for example, if plaintiff is complaining about a nuisance (a noise for example) emitted by a neighboring plant for, say five years, plaintiff can prove her claim by proving the elements of the claim which occur daily or weekly or whenever, within the limitation period. It is irrelevant for limitations purposes that these daily or weekly invasions have been going on for years.¹ Here, however, the "continuing wrong" is performance of a contract. It is implicitly admitted that payments were [**5] made by Seaboard as provided in the contract. There is no claim that payments in excess of those contemplated by the time charter have been made. So long as the time charter is not rescinded, the payments it calls for are legal obligations, not wrongs. Thus, unlike a continuing wrong the only liability matter to be litigated involves defendants' 1986 actions in authorizing the creation of these contract rights and liabilities.

1 Although failure to complain might in some circumstances constitute strong evidence of acquiescence in defendants' conduct. See *Bay New-*

foundland Co. v. Wilson & Co., Inc., Del. Ch., 4 A.2d 668, 671 (1939).

II.

I turn now to the second ground advanced by plaintiff why the motion to dismiss the complaint as time-barred should be denied: that the complaint charges a fiduciary with wrongful self-dealing.

If the claim asserted arose in 1986 it would, absent tolling, fall outside of the period established by *Section 8106*, which is quoted above, for the timely commencement [**6] of actions. It is, however, generally said that such statutes of limitations do not apply directly in equity, but that equity follows the law and therefore such statutes will, in appropriate cases, be applied analogously. E.g., *Adams v. Jankouskas, Del. Supr., 452 A.2d 148, 157 (1982)*; *Atlantis Plastics Corp. v. Sammons, Del. Ch., 558 A.2d 1062, 1064 (1989)*; *Haas v. Sinaloa Exploration & Dev. Co., 17 Del. Ch. 253, 152 A. 216, 217-18 (1930).*

I start then with the obvious counterpoint observation that statutes of limitations could apply directly to causes in Chancery of every sort. It is within the constitutional power of our legislature to do so. Indeed in England, whence our own [**7] law on the subject originates, actions against trustees are now (since at least 1980) subject to a comprehensive statute of limitations.² Since the proposition that equitable claims could be subjected to a statute of limitation appears to be hardly contestable,³ when courts say that statutes of limitations do not directly apply to actions in equity, they are in effect interpreting particular statutory language as not [**7] intending to reach such claims. They do so for good historical reasons.

2 England has departed from the organic law respecting limitation of actions against fiduciaries for breach of trust by enacting a comprehensive six year limitation period for such actions. See Harold G. Hansbury & Ronald H. Maudsley, *Modern Equity* (Martin ed. 1985) at 626. That statute however continues the traditional law with respect to claims of fraud or self-dealing by the trustee of an express trust. See, e.g., *Tito v. Waddell*, 3 All E.R. 129 (1977).

3 2 Pomeroy's *Equity Jurisprudence* § 419b (5th ed. 1941).

But whether the history is good or not, courts have for several centuries drawn a distinction between the operations of the statute of limitations at law and in equity. They have held that such statutes are intended to apply to actions at law, but not to exclusively equitable claims. See, e.g., *Bush v. Hillman Land Co., 22 Del. Ch.*

374, 2 A.2d 133, 134 (1938). Where no [**8] statute of limitations is thus available to test the timeliness of a complaint, the Court of Chancery will approach the problem of timeliness as one of laches. Under this approach, the court will inquire into the particulars of the matter to determine whether there is such unfairness to the defendant occasioned by a delay in asserting the claim as to disable the plaintiff from pressing the claim. *E.g.*, *Gardner v. Panama R.R. Co.*, 342 U.S. 29, 96 L. ed. 31, 72 S. Ct. 12 (1951). When the court applies a statute of limitation by analogy, however, it makes no such specific inquiry; it makes no assessment of fairness or prejudice.

This an important question is which claims will be treated under which doctrine. The answer given by Chancellor Kensey Johns, Jr. in 1845, in an early Delaware case, and well documented before and since, is that laches would not apply to equitable claims (Chancery's exclusive jurisdiction) but that the statute would apply by analogy to legal claims that find their way into Chancery in search of an equitable remedy (*i.e.*, Chancery's concurrent jurisdiction, *e.g.*, specific performance of a contract). The rationale for this metaphysical distinction [**9] was stated by Chancellor Johns, as follows:

The statute operates as a bar to the remedy at law, and is applied by analogy in equity, and *therefore, cannot be applied to those trusts which are the mere creatures of equity, for there is no ground in such cases for comparison; but when the same subject matter . . . can also be made the subject . . . of action at law the rule of analogy applies . . .*

Perkins v. Cartmell's Adm'r. Del. Err. & Apps., 4 Harr. 270, 271 (1845) at note (a). (emphasis added).

As the Court of Errors and Appeals put the same point on review of the Chancellor's decree in *Perkins*:

It is an established rule that where the statute bars the legal remedy, it shall bar the equitable remedy in analogous cases or in reference to the same subject matter and where the legal and the equitable claim so far correspond that the only difference is that one remedy may be enforced in a court of law and the other in a court of equity.

Id. at 274.

Thus, when required to decide whether laches or the statute provided the appropriate analytic structure for the Court of Chancery in deciding an issue of timeliness, [**10] 19th century courts made a conceptual inquiry. In effect they asked, what is the source of the right asserted by the plaintiff; is it a legal right that a court of law would recognize or is it a strictly equitable right (an equitable estate for instance or a "trust [which is] the mere creature of equity"). If it were a right cognizable at

law (*i.e.*, one for which a remedy was available at law), it fell within Chancery's concurrent jurisdiction and the statute of limitation [**273] would apply, albeit analogously. If, however, the claim was not cognizable at law, but was one of equitable origin -- an action by a beneficiary against a trustee for example -- the claim would fall under equity's exclusive jurisdiction, to which the laches analysis would apply. See 2 Pomeroy's Equity Jurisprudence §§ 419a, 419e (5th ed. 1941).

The workability of this doctrinal structure is dependent upon an understanding of the "nature" of various sorts of jurisdiction that the English Court of Chancery and, by adoption, our own court, possesses. As decades passed, however, this knowledge evolved from every day practical knowledge of lawyers to professional exotica. By the mid-twentieth century, judges [**11] were beginning to grow less comfortable with those old concepts of concurrent and exclusive chancery jurisdiction. In 1934 Chancellor Wolcott applied the old learning in an easy case, *Cochran v. F. H. Smith & Co.*, 20 Del. Ch. 159, 174 A. 119 (1934). The case was easy because the right asserted was not of equitable origin (the claim was common law fraud). It could have been brought in the Superior Court. Thus, it plainly was a concurrent jurisdiction case to which the statute should apply by analogy and it was so applied. But in reaching its decision to apply the statute of limitations by analogy to bar the action, the court noticed that "the bill does not seek any remedy peculiar to equity." *Id.* at 121. The comment reflects, I think, a weakening of the old system because the request for an equitable remedy would not in any case have altered the character of the jurisdiction that had been invoked or the correct outcome of the motion.

In 1944 our Supreme Court faced a timeliness question in the context of suit by a trustee in bankruptcy asserting claims of fraud, waste and breach of fiduciary duty against directors of the bankrupt [**12] corporation. See *Bovay v. H. M. Byllesby & Co.*, 27 Del. Ch. 381, 38 A.2d 808 (1944). The action was brought many years after the wrong alleged. The directors asserted that since they were not trustees of an express trust (as to whom equity's jurisdiction was certainly seen as exclusive) the jurisdiction that the Court of Chancery was called upon to exercise was "concurrent" with law. It was argued, therefore, that the statute of limitation should be applied by analogy. The Court accepted that the case was one of concurrent jurisdiction (although arguably it was not *) but nevertheless declined to permit the defendants to invoke the statute:

Sound public policy requires the acts of corporate officers and directors in dealing with the corporation to be viewed with a reasonable strictness. Where suit is brought in equity to compel them to account for loss or damage resulting to the corporation through passive ne-

glect of duty, without more, the argument that they ought not to be deprived of the benefit of the statute of limitations is not without weight; but *where they are required to answer for wrongful acts of commission by which they have enriched themselves* [**13] *to the injury of the corporation, a court of conscience will not regard such acts as mere torts, but as serious breaches of trust, and will point the moral and make clear the principle that corporate officers and directors, while not in strictness trustees, will, in such case, be treated as though they were in fact trustees of an express and subsisting trust, and without the protection of the statute of limitations, especially where insolvency of the corporation is the result of their wrongdoing.*

38 A.2d at 820 (emphasis added).

4 The claims were generally that payments made pursuant to contracts between the corporation and its directors were unfair to the corporation and constituted wrongful self-dealing. Since the payments were called for by apparently valid contracts it is doubtful that these payments did constitute a wrong at law. Unlike law, however, which does not generally weigh the adequacy of consideration, equity does impose an obligation on fiduciaries in their dealing with trust property. In such contracts equity will evaluate the consideration and adjust bargains. Thus, in my opinion, the case arguably was one falling into equity's exclusive jurisdiction to which, under the old doctrine, laches not limitations apply.

[**14] By the middle part of the twentieth century Delaware courts had begun less frequently [*274] to express their conclusions in terms of the lore of exclusive or concurrent jurisdiction. In the derivative suit context this is especially apparent in three cases: *Glassberg v. Boyd*, Del. Ch. 116 A.2d 711 (1955); *Bokat v. Getty Oil Co.*, Del. Supr., 262 A.2d 246 (1970) and *Halpern v. Barran*, Del. Ch., 313 A.2d 139 (1973).

Bokat being an opinion of the Supreme Court is the most significant of these. The complaint sought compensation for alleged self-dealing from the individual defendant who, it was claimed, controlled the beneficiary corporation. The moving defendant had appeared in the action under compulsion of the old sequestration process, in September 1967, more than three years after the date of the wrongs alleged. *Id.* at 248. The Supreme Court dismissed the defendant. Citing *Glassberg v. Boyd*, it stated quite broadly:

the claims sought to be asserted . . . are for the payment of money, essentially damages. Actions seeking such damages must be instituted in three years from the time the [**15] causes of action accrued.

Bokat, 262 A.2d at 250. The primary holding of *Bokat* on this point may be interpreted to mean that any action for damages requires Chancery to apply the statute of limitations:

When the relief sought in Chancery is legal in nature, it is clear that Chancery will apply the statute of limitations rather than the equitable doctrine of laches [citing *Perkins and Cochran*].

Id. (emphasis added). Relief "legal in nature" need not include every claim for which money damages are sought. For example, an action to require a trustee to pay the fair value of trust property he personally consumed or expended would be an action for money but, traditionally, would not be considered an action for "relief legal in nature" since a court of law would not award any remedy. One therefore might best interpret "legal relief" to mean "relief that a court of law will grant" (i.e., relief for a legal claim). But the claim dismissed in *Bokat*, unfair self-dealing, was not a claim "legal in nature," but a claim of equitable origin; technically a court of law would not evaluate whether a contract between a corporation [**16] and its controlling shareholder was on fair terms. Assuming that is the case, the meaning of the quoted language must be that, whether the claim asserted is legal in nature or equitable, whenever plaintiff seeks money in a derivative suit, her claim is subject to the statute of limitations. This is the interpretation that has been accorded to *Bokat*. See, e.g., *Laventhol, Krechstein, Horwath & Horwath v. Tuckman*, Del. Supr., 372 A.2d 168, 169 (1976); *Boeing Co. v. Shrontz*, Del. Ch., No. 11273, Berger, V.C. (Apr. 20, 1992).

For our purposes however, a secondary (albeit implicit) holding of *Bokat*, on this point, is equally important. The *Bokat* court distinguished the 1944 *Bovay* case on the ground that the complaint in *Bokat* made it clear that plaintiffs *had known all of the acts alleged to give rise to liability* for more than three years before they attempted to add the defendant as a party. *Bokat*, 262 A.2d at 251. Thus, the Supreme Court treated *Bovay* as a case in which the running of the statute had been tolled by ignorance of defendants' actionable self-dealing. See p. 15 *infra*.

In 1973 [**17] this Court applied the primary *Bokat* holding, in the case of *Halpern v. Barran*, Del. Ch., 313 A.2d 139 (1973). That was a derivative suit brought on behalf of Shell Oil Co. against its 69% owner, Royal Dutch Shell Petroleum Company. The complaint alleged that Shell Oil had been required to enter into business transactions with affiliates of Royal Dutch Shell that were unfair to Shell. The court held "it is by now firmly established that the three year statute of limitations . . . applies to shareholder derivative actions which seek the

recovery of money or other legal relief." *Halpern*, 313 A.2d at 141. The *Halpern* court refused to apply the *Bovay* approach finding *Bovay* a "particularly egregious" case and noting *Bovay* "has been consistently restricted in later decisions." *Halpern*, 313 A.2d 139.

Thus today it no longer seems apparent to judges as it would have to Chancellor [*275] Johns, or other 18th or 19th century jurists, that just because equity had created the corporate directors' duty to exercise corporate power loyally, (the fiduciary duty of loyalty being an example of [**18] a "trust that is the mere creature of equity" (p. 6 *supra*)) there is, for that reason, "no ground" to compare that duty -- or regard it as analogous -- to duties created at law and governed by the legal statute of limitation.

Modernly in law, as in much else, we tend to think functionally rather than metaphysically. The intricacies of 18th and 19th century equity jurisprudence are of intellectual and historical interest, but our law today must be explained and justified in terms that seem operationally significant to people today, whose interests are to be determined by that law. Thus, in my opinion, when we ask whether the passage of time alone should bar a stockholder from suing corporate directors in the corporation's name, we are asking a very practical question whose answer should make practical sense, while being consistent with our legal traditions.

In functional terms there are good reasons why a corporate stockholder ought to be treated differently than a plaintiff who is a stranger to the defendant from whom he seeks compensation for a tort. That good reason arises out of the assigned roles of stockholder and director in our corporation law. The corporate shareholder [**19] commits capital to the supervision and management of the corporate board. In doing so the stockholder becomes dependent upon the skill and loyalty of those in control of the corporate enterprise. Legally sanctioned relationships of dependence and trust are important for the law to enforce for both instrumental and expressive reasons. Given the fiduciary duties that the law imposes upon the relationship among those serving as corporate directors, stockholders are entitled to rely on the good faith of the directors when they act with respect to the corporation's property or processes. There is, of course, great social utility in the willingness of some to trust others in this way.

Since trust and good faith are the essence of this relationship, it would be corrosive and contradictory for the law to punish reasonable reliance on that good faith by applying the statute of limitations woodenly or automatically to alleged self-interested violations of trust. It does not, in my opinion, do so. Reasonable reliance upon

the competence and good faith of others who have assumed legal responsibilities towards a plaintiff have not infrequently been held sufficient to toll the running of an applicable [**20] statute of limitations.⁵

5 A failure to detect the existence of a claim will not infrequently be held to toll the running of the statute of limitations where plaintiff reasonably relies upon the competence and good faith of one with special skills or knowledge who accepts a legal responsibility towards plaintiff. I refer here especially to professional malpractice claims. See, e.g., *Isaacson, Stolper & Co. v. Artisan's Sav. Bank*, Del. Supr., 330 A.2d 130 (1974); *Child, Inc. v. Rodgers*, Del. Supr., 377 A.2d 374, 376-77 (1977) *aff'd in relevant part, rev'd on other grounds*, Del. Supr., 401 A.2d 68 (1979); see also *Shane v. Shane*, 891 F.2d 976, 985 (1st Cir. 1989) (fiduciary's failure to disclose relevant facts tolls the statute); *Riddell v. Riddell Washington Corp.*, 275 U.S. App. D.C. 362, 866 F.2d 1480, 1496 (D.C. Cir. 1989); *Hobbs v. Bateman*, *Eichler, Hill, Richards, Inc.*, 164 Cal. App. 3d 174, 210 Cal. Rptr. 387 (1983).

[**21] Thus, in my opinion, fraudulent concealment of a wrong is not the only circumstance that may toll the running of the statute. See *Halpern v. Barran*, *supra*. Chancery has long exercised a certain discretion in applying the statute of limitation in cases involving fraud for example, even where affirmative acts of concealment have not been alleged.

The old Chancery case *Sparks v. Farmers' Bank*, Del. Ch., 3 Del. Ch., 274 (1869) reflects equity's long-standing flexibility in tolling limitations with respect to actions involving fraud:

But most especially does equity relieve against any attempt to use the statute as a cover for fraud. In such case this court will even interfere in an action at law to restrain a defendant from pleading the statute; *a fortiori* will it refuse in the furtherance of fraud, to enforce the statute by its own decree in a case [*276] which, like this, is one of equitable jurisdiction. It treats the statute as running from the discovery of the fraud, not before. There has been controversy whether courts of law can afford this relief against the statute, but none whatever as to the power of a court of equity. [**22] 2 *Sto. Eq. Jur.*, 1521, 1521a; *South Sea Co. v. Wymondsell*, 3 *P. Wms.*, 143; [24 Eng. Rep. 1004 (1732)] *Deloraine v. Browne*, 3 *Bro. C.C.*, 363; [29 Eng. Rep. 739 (1792)] *Booth v. Ld. Warrington*, 4 *Bro. P. C.*, 163 [2 Eng. Rep. 111 (1714)].

There is nothing in the present case to except it from the operation of the rule. It is true that equity will not relieve against the bar of the statute in favor of a party

who has been in laches in not using means within his power to discover the fraud.

3 Del. Ch., at 306 (English Reports citations added). The same rule is widely acknowledged today. See *Holmberg v. Armbrrecht*, 327 U.S. 392, 397, 90 L. Ed. 743, 66 S. Ct. 582 (1946); *Lopez v. Swyer*, 62 N.J. 267, 300 A.2d 563, 567 n. 2 (1973); *Merchants Mortgage Co. v. Lubow*, 275 Md. 208, 339 A.2d 664, 669 (1975); *Rothman v. Fillette*, 503 Pa. 259, 469 A.2d 543, 546 n. 3 (1983).⁶

6 On this subject the opinion of Judge Leahy in *Tobacco and Allied Stocks v. Transamerica Corp.*, D. Del. 143 F. Supp. 323 (1956) is instructive:

The strict rule, obtaining in courts of law, recites the cause of action for fraud accrues, and the period begins to run, when the fraud is successfully perpetrated. The equitable rule . . . counts from the time of the discovery of the fraud, as qualified in many decisions confining it substantially to cases of fraudulent concealment. The leading case in the federal courts applying the equitable rule to suits at law is *Bailey v. Glover*, 21 Wall. 342, 88 U.S. 342, 22 L.Ed. 636, decided in 1874.

Restated, the federal doctrine means limitation and laches does not begin to run until evidence of fraud is discovered or could have been discovered had reasonable diligence been exercised; for whatever is notice calling for inquiry is notice of everything to which such inquiry might have led.

143 F. Supp. at 328-29.

[**23] Thus, while in *Mastellone v. Argo Oil Co.*, 46 Del. 102, 82 A.2d 379 (1951), (which was not a fraud case) our Supreme Court held that ignorance of the occurrence of a wrong did not toll the running of the statute, the Court did note that:

There are, of course, certain well defined exceptions such as . . . certain types of fraud or concealment of the facts which would have disclosed the tort.

Id. at 383. I take it that one of the "types of fraud" that falls within the exception of the rule of *Mastellone* is fraud perpetrated by one who, because he has legal power over the property of others, has fiduciary obligations to those others. E.g., *Giehrach v. Rupp*, N.J. Err. & Apps., 64 A. 465 (1933) (running of statute tolled until time of discovery of wrong by self-dealing executor). Therefore, in the context of an existing fiduciary rela-

tionship and a claim of actionable self-dealing, I must express a contrary opinion to that expressed in *Halpern v. Barran*, *supra*, to the effect that without an affirmative act of concealment by defendant, plaintiff's ignorance [**24] of the facts constituting the alleged wrong cannot act to toll the running of the statute of limitations. In my opinion, at least in some circumstances, it can. See *Brown v. Dolese*, 38 Del. Ch. 471, 154 A.2d 233, 239 (1959) (failure to disclose, but no misrepresentation with respect to, the corporation's cash position).

In some circumstances, even an attentive and diligent shareholder relying, in complete propriety, upon the good faith of corporate directors may be completely ignorant of transactions that do constitute self-interested acts injurious to the corporation.

A close reading of *Bokat* demonstrates the soundness of the principle that the statute of limitations applies, but is tolled in derivative actions charging actionable self-dealing, until the shareholders knew or had reason to know of the facts constituting the alleged wrong. In *Bokat*, which did allege unfair self-dealing, the Supreme Court distinguished *Bovay* on the ground that in *Bokat* the limitations period had run out, counting from the time at which plaintiffs had known of the facts alleged. Thus, *Bokat*, in harmonizing *Bovay*, recognized in its implicit secondary holding that [**25] where [**27] wrongful self-dealing is alleged in a derivative action, the statute does not run against the plaintiff until he or she knew or had reason to know the facts alleged to give rise to the wrong.

At all events this is the rule I deduce from the foregoing and the rule I will apply to this aspect of this motion.

III.

Let me now turn to the application of this rule to the complaint here. Generally, of course, the bar of limitations is an affirmative defense. *Brown v. Dolese*, 38 Del. Ch. 471, 154 A.2d 233 (1959) *aff'd Del. Supr.*, 157 A.2d 784 (1960). But it is equally well settled that where the complaint itself alleges facts that show that the complaint is filed too late, the matter may be raised by defendants' motion to dismiss, as here. *Mayer v. Adams*, *supra*; *Boeing Co. v. Shrontz*, Del. Ch., No. 11273, *Berger*, V.C. (Apr. 20, 1992); *Brooks v. Savitch*, Del. Supr., 576 A.2d 1329, 1330 (1989); *Glassberg v. Boyd*, *supra* at 717.

The complaint does allege wrongful self-dealing as to the defendants Seaboard Flour Corporation and Mr. Harry Bresky and Mr. Otto Bresky, Jr. The allegations [**26] are very sparse with respect to the time charter claim. In all material respects they are quoted above. No fact is alleged that supports the critical conclusion of fact that Flour received better than arm's-length terms, but for

present purposes I assume that, under notice pleading rules, this lack of specificity creates no fatal defect in the pleading. Thus, while the facts alleged show that the time contemplated by *Section 8106* would have run if the tolling rule implicitly recognized by *Bokat* has no application, the complaint also pleads facts that, if true, establish at least the predicate (wrongful self-dealing by a fiduciary) for the application of that tolling principle.

But in no event do the pleadings or the record contain sufficient admissions or undisputed facts to permit the court to rule dispositively on the applicability or not of the fiduciary tolling principle at this time.

Since I believe at this stage of the proceeding that plaintiff now has the burden to plead and prove facts that will qualify his case for the tolling principle, I conclude that the better practice would be to dismiss this claim with leave to file an amended complaint within sixty days. See generally [**27] Annot. Limitations - Mode of Raising Defense, 61 A.L.R. 2d 300, 312; 51 Am. Jur. 2d, Limitations § 464 (1970).

7 The annotation states in pertinent part:

Most of the cases noted [above] . . . contemplate that [a] demurrer will be sustained if it appears that the action was commenced after the statutory period had run, and that it is not necessary that it also show, in the first instance, that none of the possible exceptions to the statute are applicable, the burden being on the plaintiff to raise these exceptions if he wishes to rely thereto. *Id.* § 6.

Since matters relating to when plaintiff learned of the existence of the time charter, when he learned or should have learned of the relationship that the parties to it bore to each other; when he had notice of facts concerning possible unfairness of the terms; and the reasonable steps he took to oversee his investment, are matters within plaintiff's knowledge further discovery in aid of drafting an amended complaint is inappropriate. [**28] Thus the request for a commission to take Mr. Rotobin's deposition will be denied at this time.

Defendant shall submit a form of order consistent with the foregoing on notice.

Not Reported in A.2d, 2005 WL 1653975 (Del.Ch.)
(Cite as: 2005 WL 1653975 (Del.Ch.))

Only the Westlaw citation is currently available.

UNPUBLISHED OPINION. CHECK COURT
RULES BEFORE CITING.

Court of Chancery of Delaware.
In re SUNGARD DATA SYSTEMS, INC. SHARE-
HOLDERS LITIGATION
No. Civ.A. 1221-N.

Submitted July 6, 2005.
Decided July 8, 2005.

Dear Counsel:
LAMB, Vice Chancellor.

*1 Certain shareholders of SunGard Data Systems, Inc. ("SunGard" or the "Company"), filed this purported class action suit claiming breach of fiduciary duty in the proposed merger of the Company with Solar Capital Corp. ("Solar"). ^{FN1} Pursuant to the merger agreement, if approved, the Company's shareholders are to receive \$36 per share, representing a 44.4% premium over the prior market price of the shares. The plaintiffs' basic claims are two-fold. First, they claim that the defendants breached their fiduciary duties by agreeing to inadequate consideration, i.e. an unfair price claim. Second, they claim that the defendants breached their fiduciary duties by failing to provide adequate disclosure of the proposed merger.

^{FN1} The named defendants in the suit are SunGard, Solar, and the individual directors of SunGard.

The plaintiffs have moved for an order expediting proceedings for the purpose of presenting a motion for preliminary injunction. I heard that motion by teleconference on July 6, 2005. For the following reasons, the request to expedite proceedings is denied.

A. Factual Allegations

It is unnecessary to the disposition of this motion to describe in detail the complex facts surrounding this

large merger transaction. Indeed, the plaintiffs made it clear during the teleconference that they were not seeking preliminary injunctive relief in their fair price or *Revlon* type claims. Instead, they seek expedited discovery and proceedings only with regard to their disclosure claims. Nevertheless, a few facts are necessary to understand the weakness of these limited disclosure claims.

- In October of 2004, the Company announced that its board of directors had unanimously approved a plan to spin off one of its three business segments to stockholders through a distribution of shares. In adopting the proposal to merge with Solar, the Company abandoned this spin-off plan.
- In connection with the proposed merger, Credit Suisse First Boston ("CSFB") and Lazard Freres & Co. LLC ("Lazard") both provided fairness opinions that the merger price was within the range of fairness.
- On April 12, 2005, the Company filed a Schedule 14A preliminary proxy statement with the SEC disclosing the proposed transaction. That same day, the Company also filed a Schedule 13E-3 Transaction Statement (the "Schedule 13E-3"), attaching as exhibits each of the written presentations made by CSFB to the Company's board of directors, and both the preliminary and final valuation materials prepared by Lazard for the board.
- On June 27, 2005, the Company filed with the SEC and mailed to the Company's shareholders a definitive proxy statement (the "Proxy Statement") soliciting the shareholders' votes on the merger.

B. Standard

"This Court does not set matters for an expedited hearing or permit expedited discovery unless there is a showing of good cause why that is necessary." ^{FN2} To make the necessary showing, a plaintiff must articulate a sufficiently colorable claim and show a sufficient possibility of a threatened irreparable injury to justify imposing on the defendants and the public the extra (and sometimes substantial) costs of

Not Reported in A.2d, 2005 WL 1653975 (Del.Ch.)
(Cite as: 2005 WL 1653975 (Del.Ch.))

an expedited preliminary injunction proceeding.^{FN3}

FN2. *Greenfield v. Caporella*, 1986 Del. Ch. LEXIS 493, at *5, 1986 WL 13977 (Del. Ch. Dec. 3, 1986).

FN3. *Giammargo v. Snapple Beverage Corp.*, 1994 Del. Ch. LEXIS 199 at *6, 1994 WL 672698 (Del. Ch. Nov. 15, 1994).

C. Analysis

*2 The defendants argue that the plaintiffs have failed to make the necessary showing of either a colorable claim or a possibility of irreparable harm. The defendants also contend that the plaintiffs have been dilatory in bringing their motion, waiting a full five business days after the final proxy statement was filed to amend their complaint and move for expedition. Due to that delay, the defendants contend, there is too short a period left in which to fairly present the issues in advance of the stockholder meeting date. The defendants also argue that the plaintiffs have failed to demonstrate any likelihood of a material failure in disclosure.

The record does not support a conclusion that the plaintiffs unduly delayed in making their application. While it is true that they could have filed their motion a few days earlier than they did, that delay is not fatal to their application, which is, in any event rather narrow in scope and easily discovered into. Moreover, the optimal time to bring a disclosure claim in connection with a proposed merger, or in a like context where the company requests shareholder action or approval, is before the stockholder vote is taken and the deal closes.^{FN4} Before a transaction closes, the court is best able to provide a full and adequate remedy to the class of stockholders if the likelihood of a material disclosure violation is shown—namely, requiring the company to correct its false or misleading disclosures. Therefore, the court is generally amenable to motions for expedited proceedings in this context and will not deny expedition on account of the minor delay encountered here.

FN4. See, e.g., *In re MONY Group Inc. S'holder Litig.*, 852 A.2d 9, 32 (Del.Ch.2004) (holding that a misinformed stockholder vote on a merger threatens irreparable harm).

That being said, a plaintiff still needs to raise a colorable claim of a disclosure violation. In this case, the plaintiffs have not done so. The amended complaint lists ten deficiencies in the Proxy Statement, all of which involve alleged failures to disclose information. None allege any active misrepresentation. The plaintiffs urge two of these ten as supporting their application for expedited proceedings.

The plaintiffs complain that the Company failed to adequately disclose the investment bankers' analysis of the merger in the Proxy Statement. Among other things, they claim that Lazard's analysis fails to disclose whether Lazard considered a control premium in its calculations. This claim, and similar ones advanced by the plaintiffs, viewed in the context of this premium transaction, is, at best, of marginal significance and is aptly characterized as merely "quibbl[ing] with the analyses and conclusions reached by Lazard."^{FN5}

FN5. Letter to the court from Gregory P. Williams, Esquire, dated July 6, 2005, at 13.

The Proxy Statement devotes over 15 pages to a description of the investment bankers' analyses.^{FN6} None of these disclosures are alleged to be affirmatively misleading. Moreover, the Company filed the full text of the CSFB written opinion and the Lazard opinions as attachments to its Schedule 13E-3. Thus this information is public and readily available to the shareholders. Viewed in relation to the "total mix" of available disclosure, this claim does not give rise to a colorable claim of breach of the duty of disclosure.

FN6. See Proxy Statement at 28-44.

*3 The plaintiffs also complain that the Company failed to adequately disclose why it chose to abandon its spin-off strategy. This claim is also weak. The Proxy Statement specifically stated that the Company believes that the merger provided greater value for the Company's shareholders than did the spin-off. Specifically, the Proxy Statement stated that the "previously announced spin off of [the Company's] availability services business into a separate publicly traded company would not provide greater value to stockholders...."^{FN7} No more elaborate explanation would seem necessary.

Not Reported in A.2d, 2005 WL 1653975 (Del.Ch.)
(Cite as: 2005 WL 1653975 (Del.Ch.))

FN7. *Id.* at 24.

CONCLUSION

For reasons likely related to their assessment of the weakness of their challenge to the fairness of the terms of the proposed merger, the plaintiffs have chosen to seek expedition only as to their allegations of improper disclosure. Because those claims do not appear to present colorable issues for litigation, the court, in the exercise of its discretion, declines to order expedited proceedings or to schedule a hearing on the plaintiffs' motion for preliminary injunctive relief. Thus, the plaintiffs' motion to expedite is DENIED. IT IS SO ORDERED.

Del.Ch.,2005.
In re SunGard Data Systems, Inc. Shareholders Litigation
Not Reported in A.2d, 2005 WL 1653975 (Del.Ch.)

END OF DOCUMENT



LEXSEE 809 A.2D 1163

OMNICARE, INC., Plaintiff, v. NCS HEALTHCARE, INC., JON H. OUTCALT,
KEVIN B. SHAW, BOAKE A. SELLS, RICHARD L. OSBOURNE, GENESIS
HEALTH VENTURES, INC., and GENEVA SUB, INC., Defendants.

C.A. No. 19800

COURT OF CHANCERY OF DELAWARE, NEW CASTLE

809 A.2d 1163; 2002 Del. Ch. LEXIS 120

October 24, 2002, Submitted

October 25, 2002, Decided

SUBSEQUENT HISTORY: Companion case at *Omnicare, Inc. v. NCS Healthcare, Inc.*, 825 A.2d 264, 2002 Del. Ch. LEXIS 131 (Del. Ch., 2002)

Appeal dismissed by *Omni Care, Inc. v. NCS Healthcare, Inc.*, 2002 Del. LEXIS 723 (Del., Dec. 10, 2002)
Appeal dismissed by *Omnicare, Inc. v. NCS Healthcare, Inc.*, 818 A.2d 914, 2003 Del. LEXIS 195 (Del., 2003)

DISPOSITION: [**1] Motion to dismiss Plaintiffs' claims granted in part and denied in part.

COUNSEL: Donald J. Wolfe, Jr., Esquire, Kevin R. Shannon, Esquire, Michael A. Pittenger, Esquire, John A. Seaman, Esquire, POTTER ANDERSON & CROON LLP, Wilmington, Delaware; Robert C. Myers, Esquire, Seth C. Farber, Esquire, James P. Smith III, Esquire, David F. Owens, Esquire, Melanie R. Moss, Esquire, DEWEY BALLANTINE LLP, New York, New York; Attorneys for Plaintiff, Omnicare, Inc.

Edward P. Welch, Esquire, Edward B. Micheletti, Esquire, Katherine J. Neikirk, Esquire, James A. Whitney, Esquire, SKADDEN ARPS SLATE MEAGHER & FLOM, LLP, Wilmington, Delaware; Mark A. Philips, Esquire, Megan L. Mehalko, Esquire, H. Jeffrey Schwartz, Esquire, BENESCH, FRIEDLANDER, COPLAN & ARONOFF LLP, Cleveland, Ohio; Attorneys for Defendants NCS Healthcare, Inc., Boake A. Sells, and Richard L. Osbourne.

Jon E. Abramczyk, Esquire, MORRIS, NICHOLS, ARSHT & TUNNELL, Wilmington, Delaware; Frances Floriano Goins, Esquire, Thomas G. Kovach, Esquire, SQUIRES, SANDERS & DEMPSEY, LLP, Cleveland, Ohio; Attorneys for Defendant, John H. Outcalt

Edward M. McNally, Esquire, Michael A. Weidinger, Esquire, [**2] Elizabeth A. Brown, Esquire, MORRIS, JAMES, HITCHENS & WILLIAMS, LLP, Wilmington, Delaware; James R. Bright, Esquire, Timothy G. Warner, Esquire, SPIETH, BELL, McCURDY & NEWELL CO., L.P.A., Cleveland, Ohio; Attorneys for Defendant, Kevin B. Shaw

David C. McBride, Esquire, Bruce L. Silverstein, Esquire, Christian Douglas Wright, Esquire, Adam W. Poff, Esquire, YOUNG CONAWAY STARGATT & TAYLOR, LLP, Wilmington, Delaware; Paul Vizcarondo, Jr., Esquire, Theodore N. Mirvis, Esquire, Mark Gordon, Esquire, John F. Lynch, Esquire, Lauryn P. Gouldin, Esquire, WACHTELL, LIPTON, ROSEN & KATZ, New York, New York; Attorneys for Defendants, Genesis Health Ventures, Inc. and Geneva Sub, Inc.

JUDGES: LAMB, Vice Chancellor.

OPINION BY: LAMB

OPINION

[*1165] LAMB, Vice Chancellor

I.

This action arises out of a proposed merger between a Delaware corporation and a Delaware subsidiary of a Pennsylvania corporation. The plaintiff is a rival Delaware corporation that also has made a bid for the target corporation. The complaint alleges that the target corporation's directors breached their fiduciary duties to the target corporation's stockholders. The complaint also seeks a declaratory judgment that, in accordance [**3]

with charter provisions restricting the transfer of the target's high-voting common stock, certain voting agreements entered into in connection with the merger by holders of such high-vote shares caused an automatic conversion of those shareholdings into single-vote common stock. If this is so, it will greatly diminish the chances that the merger will be consummated.

The defendants have moved to dismiss, arguing that the plaintiff lacks standing to sue because it did not own stock in the target corporation until after the public disclosure of the merger agreement and associated voting agreements. The plaintiff argues that it has standing because it is now a stockholder and is making a bona fide bid for control of the target corporation. Plaintiff also argues it has standing [*1166] to bring the claim for a declaratory judgment because that judgment may affect the outcome of the vote on the merger, due to occur in the near future, and affects plaintiff's own voting power and that of all other owners of the low-vote stock.

The motion to dismiss must be granted with respect to plaintiff's claims for breach of fiduciary duties. The definitive terms of the merger were agreed to, and publicly [**4] disclosed, before plaintiff acquired shares in the target corporation. Therefore, if any breach of fiduciary duty occurred, it occurred before plaintiff was ever owed a fiduciary duty by the target corporation's directors. Further, the court is unwilling to extend the current state of fiduciary duty standing rules to allow bidders who were not stockholders at the relevant time to assert claims on behalf of others who were.

The motion to dismiss will not be granted as to the declaratory judgment sought by plaintiff. Plaintiff, by virtue of its current shareholding, has a right to obtain that relief and, given its status as a bona fide bidder for control, will not be prevented from suing at this time to enforce what it believes is the proper operation of the corporation's charter simply because it purchased its shares after notice of the facts giving rise to this contract based claim.

II.

A. The Parties

1. The Plaintiff

The plaintiff in this action is Omnicare, Inc. ("Omnicare"), a Delaware corporation with its principal place of business in Covington, Kentucky. Omnicare provides pharmacy services to long-term care institutions such as skilled nursing facilities, [**5] assisted living facilities, and other institutional health care facilities. It also provides clinical research for pharmaceutical and biotechnology industries.

2. The Defendants

NCS Healthcare, Inc. ("NCS") is a Delaware corporation with its principal place of business in Beachwood, Ohio. NCS is an independent provider of pharmacy and related services to long-term care and acute care facilities, including skilled nursing centers, assisted living facilities, and hospitals.

Genesis Health Ventures, Inc. ("Genesis") is a Pennsylvania corporation with its principal place of business in Kennett Square, Pennsylvania. Geneva Sub, Inc. ("Geneva Sub"), a wholly owned subsidiary of Genesis, is a Delaware corporation formed by Genesis for the purpose of acquiring NCS.

Defendant Jon H. Outcalt is chairman of NCS's board of directors ("Board"). He is a founding principal of NCS and has been a member of the Board since 1986. Defendant Kevin B. Shaw is a founding principal and has been the president and a director of NCS since 1986. Defendant Boake A. Sells has been a member of the NCS Board since 1993. Defendant Richard L. Osborne has been a Board member since 1986.

B. The Merger

[**6] On Sunday, July 28, 2002, the Board authorized a merger with Genesis whereby Genesis would acquire the entire equity interest in NCS ("Merger").¹ According to the agreement and plan of merger ("Merger Agreement"), each share of NCS common stock would be converted into a [*1167] fraction of a share of Genesis common stock valued at approximately \$ 1.60 per share of NCS common stock. On the preceding Friday, July 26, 2002, Omnicare had sent a letter to Chairman Outcalt proposing negotiations related to the acquisition of NCS by Omnicare at a price of \$ 3 per share in cash.²

1 For purposes of this motion only, the following facts are taken from Omnicare's well-pleaded allegations in its Second Amended Complaint.

2 The letter stated in part:

In the context of a negotiated transaction, we are prepared to discuss all aspects of our proposal with you, including structure, economics and your views as to the proper roles for our respective management and employees in the combined company.

We would also consider a stock transaction in order to allow NCS stockholders to share in the upside of the combined companies. With respect to structure, we

would be willing to discuss acquiring the securities of NCS in a tender offer. We wish, and are prepared, to meet immediately with you and your directors, management and advisors to answer any questions about our proposal and to proceed with negotiations leading to the execution of a definitive merger agreement.

Second Am. Compl., at 11.

[**7] The Merger Agreement provides that the Board may not terminate the Merger before the NCS stockholders have an opportunity to vote on it. Relatedly, in connection with and shortly after the NCS directors voted to approve the Merger Agreement, Genesis and NCS entered into voting agreements with Outcalt and Shaw whereby those individuals (1) granted Genesis an irrevocable proxy to vote all of their shares of NCS common stock in favor of the Merger Agreement and against any other proposal, (2) agreed to vote all such shares in a like manner, and (3) agreed to avoid disposing of or otherwise encumbering their shares of NCS common stock before consummation of the merger with Genesis ("Voting Agreements").

NCS has a dual class voting structure consisting of Class A Common Stock, which entitles the holder to one (1) vote per share, and Class B Common Stock, which entitles the holder to ten (10) votes per share. The Voting Agreements were required by Genesis because Outcalt and Shaw, through their extensive holdings of Class B shares, collectively own more than 65% of the total voting power of all NCS stockholders. Aside from the voting rights associated with Class A and Class B shares, the [**8] shares are identical in every other respect, except as described below.

The NCS certificate of incorporation strictly limits the class of persons to whom shares of Class B common stock can be transferred. This includes a narrow category of "Permitted Transferees." If a transfer is made to anyone other than a Permitted Transferee, the Class B shares automatically convert into Class A shares, thus eliminating the benefit of the additional voting rights. The NCS charter also provides that no transfer is deemed to have occurred when a proxy has been given in connection with a solicitation of proxies subject to the provisions of Section 14 of the Securities Exchange Act of 1934.

On the morning of Monday, July 29, 2002, before the market opened, Genesis and NCS issued a joint press release announcing the Merger and outlining in detail the specific terms of the Merger Agreement and the Voting

Agreements. Later in the same day, after learning of the terms of the Merger, Omnicare purchased 1,000 shares of NCS Class A Common Stock.³ Omnicare did not hold any stock in NCS before this purchase. Omnicare [**1168] has since commenced a tender offer for NCS shares at \$ 3.50 per share.

3 This fact is evidenced in Omnicare's Schedule TO filed with the Securities and Exchange Commission on August 8, 2002. The court may take judicial notice of facts publicly available in filings with the SEC. See, e.g., *In re Santa Fe Pacific S'holder Litig.*, 669 A.2d 59, 69-70 (Del. 1995).

[**9] III.

On August 1, 2002, Omnicare initiated this lawsuit. On September 23, 2002, Omnicare filed a Second Amended Complaint. In its Second Amended Complaint, Omnicare alleges that: (1) the voting agreements between Genesis, Outcalt, and Shaw violated NCS's charter and thus automatically converted Outcalt's and Shaw's Class B shares into Class A shares (Count I); (2) the Board violated 8 Del. C. § 141(a) by entering into an exclusivity agreement with Genesis on July 3, 2002, and approving the Voting Agreements and the Merger Agreement on July 28, 2002 in violation of their fiduciary duties (Count II); (3) the Board breached their fiduciary duties by approving the Genesis merger and by refusing to consider Omnicare's July 26, 2002 indication of interest (Count III); (4) Genesis aided and abetted these alleged breaches of fiduciary duties (Count IV); and (5) the termination fee provided for in the Merger Agreement is the result of a fiduciary breach and, thus, is invalid and unenforceable (Count V).

On October 3, 2002, NCS and other defendants filed a motion to dismiss Omnicare's Second Amended Complaint due to an alleged lack of standing by Omnicare. [**10] Genesis and Geneva Sub have joined NCS's motion to dismiss.

IV.

When deciding a motion to dismiss a complaint under Court of Chancery Rule 12(b)(6) for failure to state a claim upon which relief can be granted, the court is to assume the truthfulness of all well-pleaded allegations of fact in the complaint.⁴ A complaint must be dismissed for failure to state a claim unless it alleges facts that "establish each and every element of a claim upon which relief could be granted."⁵ Furthermore, Delaware courts have held that questions of standing can properly be considered on a motion to dismiss.⁶

4 See *Grobow v. Perot*, 539 A.2d 180, 187 & n.6 (Del. 1988).

5 *Lewis v. Austen*, 1999 Del. Ch. LEXIS 125, 1999 WL 378125 at *4 (Del. Ch. June 2, 1999) (citing *Santa Fe*, 669 A.2d at 65-66; *In re Tri-Star Pictures, Inc. Litig.*, 634 A.2d 319, 326 (Del. 1993)).

6 See, e.g., *Andra v. Blount*, 772 A.2d 183, 188 (Del. Ch. 2000) (granting motion to dismiss for lack of standing); *Guy v. Sills*, 1998 Del. Ch. LEXIS 119, 1998 WL 409346 at *1 (Del. Ch. July 10, 1998) (same).

[**11] Standing to maintain a lawsuit "refers to the 'right of a party to invoke the jurisdiction of a court to enforce a claim or redress a grievance.'" 7 In deciding whether a party has standing to bring a claim, the court shall "consider[] who is entitled to bring a lawsuit rather than the merits of the particular controversy." 8 To successfully achieve standing, "the plaintiff's interest in the controversy must be distinguishable from the interest shared by ... the public in general." 9 Courts have applied the concept of standing "as a matter of self-restraint to avoid the rendering of advisory opinions at the behest of parties who are 'mere intermeddlers'." 10

7 *U-H Acquisition Co. v. Barbo*, 1994 Del. Ch. LEXIS 9, 1994 WL 34688 at *3 (Del. Ch. Jan. 31, 1994) (quoting *Stuart Kingston, Inc. v. Robinson*, 596 A.2d 1378, 1382 (Del. 1991)).

8 *Id.* (citing *Stuart Kingston*, 596 A.2d at 1382).

9 *Stuart Kingston*, 596 A.2d at 1382 (citing *Sprague v. Casey*, 520 Pa. 38, 550 A.2d 184 (Pa. 1988)).

10 *Id.* (quoting *Crescent Park Tenants Ass'n v. Realty Equities Corp. of New York*, 58 N.J. 98, 275 A.2d 433 (N.J. 1971)).

[*1169]

[**12] V.

A. Omnicare's "Bidder Standing" Argument

Omnicare recognizes that, as a general rule, only persons who were stockholders at the time of an alleged wrongdoing have standing to sue corporate directors for breach of fiduciary duty. Indeed, under established Delaware law, a breach of fiduciary duty claim must be based on an actual, existing fiduciary relationship between the plaintiff and the defendants at the time of the alleged breach. Nevertheless, Omnicare invites the court to recognize an exception to this rule to allow it standing on the basis of its current status as a competing bidder for control of NCS. It argues, with some force, that a realistic assessment of its position reveals both that the alleged fiduciary misconduct adversely affects its

chances of succeeding in its takeover bid and that its interest in obtaining injunctive relief to remedy that alleged misconduct is largely congruent with the interests of NCS stockholders in receiving a better offer for their shares. For the reasons discussed below, the court declines to permit an entity that could not sue in its own right to sue directors for breach of a fiduciary duty owed to others.

1. Public [**13] Policy Detests The "Purchase" Of A Lawsuit

It is undisputed that Omnicare was not a stockholder at the time of the alleged misconduct stated in its complaint. 11 Omnicare purchased NCS stock only after becoming aware of the Merger and the associated Voting Agreements from a press release issued earlier in the day on July 29, 2002. It would seem elementary that ownership of those shares does not afford Omnicare standing to pursue a lawsuit alleging breaches of fiduciary duties arising out of the directors' decision to approve the Merger because to do so would violate a longstanding Delaware public policy against the "evil" of purchasing stock in order "to attack a transaction which occurred prior to the purchase of the stock." 12 This policy has been vigorously enforced through recent times. 13

11 A stockholder-plaintiff is barred from bringing claims when she purchases stock after the board of directors has approved a transaction and the transaction has been publicly disclosed. See *In re Beatrice Cos., Inc. Litig.*, 522 A.2d 865, 1987 WL 36708 at *3 (1987) ("In the case of a proposed merger, the plaintiff must have been a stockholder at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged.") (citing *Newkirk v. W.J. Rainey, Inc.*, 31 Del. Ch. 433, 76 A.2d 121, 123 (Del. Ch. 1950); *Brown v. Automated Mktg. Sys., Inc.*, 1982 Del. Ch. LEXIS 571, 1982 WL 8782 at *2 (Mar. 22, 1982) ("It is not the merger itself that constitutes the wrongful act of which plaintiff complains, but rather it is the fixing of the terms of the transaction") (citation omitted).

[**14]

12 *Rosenthal v. Burry Biscuit Corp.*, 30 Del. Ch. 299, 60 A.2d 106, 111 (Del. Ch. 1948).

13 See, e.g., *IM2 Merchandising & Mfg., Inc. v. Tirex Corp.*, 2000 Del. Ch. LEXIS 156, 2000 WL 1664168 at *6 (Nov. 2, 2000) (dismissing a breach of fiduciary duty claim where the alleged breach occurred before plaintiffs' acquisition of shares).

The policy against purchasing lawsuits involving the internal relations of Delaware corporations was codified in the derivative suit context by 8 Del. C. § 327.¹⁴ [*1170] The policy animating 8 Del. C. § 327 is not, however, limited to derivative claims alone. Rather, that policy is derived from "general equitable principles"¹⁵ and has been applied to preclude stockholders who later acquire their shares from prosecuting direct claims as well.¹⁶ Similarly, our courts have held that plaintiffs who purchase stock after disclosures have been made cannot pursue claims for breaches of the duty of disclosure.¹⁷

14 This section requires that the complaint allege "that the plaintiff was a stockholder of the corporation at the time of the transaction of which such stockholder complains or that such stockholder's stock thereafter devolved upon such stockholder by operation of law." See also *Alabama By-Products Corp. v. Cede & Co.*, 657 A.2d 254, 264 n.12 (1995); *Schreiber v. Bryan*, 396 A.2d 512, 516 (Del. Ch. 1978); *Harff v. Kerkorian*, 324 A.2d 215, 218 (Del. Ch. 1974); *aff'd in part, rev'd in part*, 347 A.2d 133 (Del. 1975); *Maclary v. Pleasant Hills, Inc.*, 35 Del. Ch. 39, 109 A.2d 830, 833 (Del. Ch. 1954).

[**15]

15 See *Brown*, 1982 Del. Ch. LEXIS 571, 1982 WL 8782 at *2 (citing *Home Fire Ins. Co. v. Barber*, 67 Neb. 644, 93 N.W. 1024, 1029 (Neb. 1903)); see also *Bangor Punta Operations, Inc. v. Bangor & A.R. Co.*, 417 U.S. 703, 711, 41 L. Ed. 2d 418, 94 S. Ct. 2578 (1974) (noting the basic equitable principle that plaintiffs who acquire shares after disputed transactions occur are barred from recovery).

16 See *In re Gaylord Container Corp. S'holders Litig.*, 747 A.2d 71, 82 & n.15 (Del. Ch. 1999) (noting that plaintiffs "who buy stock and challenge the earlier adoption of properly disclosed defensive measure" should be "barred from recovery").

17 See *Thorpe v. CERBCO, Inc.*, 1993 Del. Ch. LEXIS 16, 1993 WL 35967 at *3 (Del. Ch. Jan. 26, 1993) ("While plaintiffs may have standing to complain about breach of duty that occurs while they are shareholders. They have no direct right to be awarded judicial relief for [acts that occurred before they purchased stock]."); *Sanders v. Devine*, 1997 Del. Ch. LEXIS 131, 1997 WL 599539 at *5 (Del. Ch. Sept. 24, 1997) ("In the present case, plaintiff was not a stockholder at the time the prospectus was issued, therefore, as a matter of law, there can be no liability under any fiduciary duty theories for the disclosures made in connection with the offering.").

[**16] Delaware's policy against allowing plaintiffs to purchase stock and then challenge transactions agreed upon before the purchase "might easily be frustrated if individuals could place orders to purchase stock on the same day the challenged transaction occurred."¹⁸ Delaware courts enforce this policy by denying standing to after-the-fact purchasers and dismissing their complaints.¹⁹ Thus, it would appear that because there is such a strong policy against the purchase of a lawsuit, and because there is no doubt that Omnicare purchased stock in NCS after the relevant information came to light, Omnicare is precluded from asserting any fiduciary duty claims arising out of actions taken by the NCS Board before Omnicare's purchase of shares on July 29, 2002.

18 *Avacus Partners, L.P. v. Brian*, 1990 Del. Ch. LEXIS 178, 1990 WL 161909 at *6 (Del. Ch. Oct. 24, 1990).

19 See, e.g., *IM2 Merchandising*, 2000 Del. Ch. LEXIS 156, 2000 WL 1664168 at *6.

2. "Bidder Standing"

Acknowledging the foregoing authority, Omnicare suggests [**17] that it nonetheless should be accorded standing to pursue these claims because it is making a bona fide bid for control of NCS. Omnicare argues that the policy limiting the right to initiate litigation relating to the internal affairs of a Delaware corporation to those who were participants in the corporate enterprise at the time of the alleged misconduct is designed to prevent "strike suits" and should not prevent a person such as Omnicare, which has a substantial and legitimate interest in the outcome of the litigation, from filing or prosecuting its suit. Instead, Omnicare urges the court to adopt a policy-based approach and allow standing for bidders without regard to their stock ownership in breach of fiduciary duty cases if failure to do so would disserve the interests of the parties, the stockholders, and the public.²⁰ For the [**171] reasons that are briefly discussed hereinafter, the court is unwilling to extend the law in this fashion.

20 See *Emerson Radio Corp. v. International Jensen, Inc.*, 1996 Del. Ch. LEXIS 100, 1996 WL 483086 at *14 (Del. Ch. Aug. 20, 1996); see also J. Travis Laster, *The Line Item Veto and Unocal: Can a Bidder qua Bidder Pursue Unocal Claims Against a Target Corporation's Board of Directors?*, 53 Bus. Law. 767 (1998).

[**18] Initially, it must be observed that Omnicare's argument finds little or no support in our law and is inconsistent with established principles that limit standing in fiduciary duty based cases to those to whom a duty was owed at the time of the breach.²¹ Moreover,

Omnicare is unable to cite any case holding that a bidder that did not own shares at the time of the alleged breach of fiduciary duty by the target board nonetheless had standing to sue. In the two principal cases that Omnicare cites to support its position, the bidders whose standing was at issue (and for whom standing was ultimately held to exist) were stockholders at the time of the alleged fiduciary duty breaches.²¹ The question in each of those cases was whether the plaintiff's bidder status deprived it of its ability to sue as a stockholder, not whether that status sufficed to create standing where there was none before. Finally, it must be observed that, in every case that found standing to sue cited by Omnicare, the plaintiffs owned stock at the time of the alleged fiduciary breach.²²

21 See *Sanders v. Devine*, 1997 Del. Ch. LEXIS 131, 1997 WL 599539 at *5 ("In order to prevail on a breach of fiduciary duty claim, plaintiff ... must first establish that at the time [of the wrong] he was a person to whom a fiduciary duty was owed."); *Thorpe v. CERBCO, Inc.*, 1993 Del. Ch. LEXIS 16, 1993 WL 35967 at *3; see also *Leung v. Schuler*, 2000 Del. Ch. LEXIS 41, 2000 WL 264328 at *6 (Del. Ch. Feb. 29, 2000) (to prevail on breach of fiduciary duty claim, one must be owed such a duty); *Arnold v. Society for Savs. Bancorp, Inc.*, 1995 Del. Ch. LEXIS 86, 1995 WL 376919 at *6-7 (Del. Ch. June 15, 1995) (same); *Weiss v. Leewards Creative Crafts, Inc.*, 1993 Del. Ch. LEXIS 73, 1993 WL 155493 at *3 (Del. Ch. Apr. 29, 1993) (same).

[**19]

22 See *Tate & Lyle PLC v. Staley Continental, Inc.*, 1988 Del. Ch. LEXIS 61, 1988 WL 46064 at *4 (Del. Ch. May 9, 1988); *MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc.*, 1985 Del. Ch. LEXIS 545, 1985 WL 21129 at *1 (Del. Ch. Oct. 9, 1985).

23 See *Lipton v. News Int'l*, 514 A.2d 1075, 1076 (Del. 1986); *Williams v. Geier*, 1987 Del. Ch. LEXIS 436, 1987 WL 11285 at *3 (Del. Ch. May 20, 1987); *Moran v. Household Int'l, Inc.*, 490 A.2d 1059, 1064 (Del. Ch. 1985), *aff'd*, 500 A.2d 1346 (Del. 1985); *Condec Corp. v. Lunkenheimer Co.*, 43 Del. Ch. 353, 230 A.2d 769, 772 (Del. Ch. 1967); *GM Sub Corp. v. Liggett Group, Inc.*, 1980 Del. Ch. LEXIS 581, 1980 WL 6430 at *1 (Del. Ch. Apr. 25, 1980); *Packer v. Yampol*, 1986 Del. Ch. LEXIS 413, 1986 WL 4748 at *5 (Del. Ch. Apr. 18, 1986); *In re Tri-Star Pictures, Inc., Litig.*, 634 A.2d at 321.

Omnicare cites only one case, *Emerson Radio Corp. v. International Jensen, Inc.*,²⁴ to support its argument that a bidder-plaintiff can bring a breach of fiduciary

duty claim without regard to the bidder's ownership of shares. [**20]²⁵ A careful reading of *Emerson*, however, shows that it does not support Omnicare's argument. The court in *Emerson* clearly held that the plaintiff bidder had no standing:

In its capacity as a bidder, Emerson has no claims to raise, because neither Jensen nor its Board owes a duty to an interested potential acquirer to deal with that acquirer. As the Chancellor has aptly put it:

It is a simple and I would have thought well understood fact that one [in the position of a tender offeror] possesses no legal right to have an owner of an asset supply him with information or negotiate with him. Thus, it simply is not a legal wrong to a would-be buyer for an owner to ignore or reject an offer of sale.

Gagliardi v. Trifoods Int'l Inc., Del. Ch., 683 A.2d 1049 (1996). Rather, any duty Jensen's board may have to deal with Emerson as a potential buyer was [*1172] owed solely to Jensen's stockholders, as a corollary of the Board's fiduciary duty to achieve the highest available value for shareholders. That is why plaintiffs who seek to assert breach of fiduciary duty claims of this kind have been persons to whom such fiduciary duties [**21] were owed, i.e., stockholders of the target corporation.²⁶

The court in *Emerson* specifically noted, "no Delaware court has recognized the standing of a non-stockholder bidder for a target company."²⁷ Although the court acknowledged the argument that the bidder-plaintiff should be denied standing, the court found it was not necessary to decide the point, which was raised only at the preliminary injunction hearing itself:

This question need not be decided to resolve Emerson's motion. That motion can be determined on other grounds with no different result. Moreover, a refusal by this Court to entertain the fiduciary duty claims on this threshold ground would

disserve the interests of the parties and the public. Although the Shareholder Plaintiffs do not advance the same claims as Emerson, they do own Jensen stock and have joined in Emerson's position. And, importantly, the merits of the defendants' conduct have now been the subject of discovery, briefing and argument (albeit expedited). For this Court now to refuse to review that conduct would be wasteful of the parties' considerable investment of effort and resources, and deprive Jensen's shareholders and the public [**22] of such benefit that this Court's (and any reviewing Court's) determinations might have.

Accordingly, the Court will proceed on the assumption, *but without deciding*, that Emerson has standing to assert its claims.²⁴

24 1996 Del. Ch. LEXIS 100, 1996 WL 483086.

25 1996 Del. Ch. LEXIS 100, 1996 WL 483086 at *16.

26 1996 Del. Ch. LEXIS 100, 1996 WL 483086 at *13.

27 *Id.*

28 1996 Del. Ch. LEXIS 100, 1996 WL 483086 at *14 (emphasis added).

The court then went on to deny the preliminary injunction sought by the plaintiff-bidders. Therefore, *Emerson* does not provide support for Omnicare's "bidder standing" argument. Moreover, even if the court were to consider the other factors enumerated in *Emerson*, there would be no compelling reason to allow Omnicare to proceed on its fiduciary duty claims. The time, effort, and resources expended in *Emerson* have not been similarly spent in this controversy. The standing issue was raised well before any deposition discovery was taken and also before the preliminary injunction hearing now scheduled to be heard in three weeks' time.

[**23] Finally, addressing Omnicare's policy arguments, the court concludes that they are not sufficiently compelling to permit a person who is not in any respect a participant in the corporation to sue on claims relating to the internal affairs of that enterprise. Delaware courts have shown considerable latitude in entertaining fiduciary duty litigation brought by stockholders who are also themselves bidders for control. The only consistent limitation placed on those persons is that they also be stockholders at all relevant times and, thus, among those

to whom a duty was owed, even if they only own one share. Of course, this rule is not based on the economic significance of such a bidder's investment, which often is immaterial. Instead, it is based on a purely legal or equitable notion that limits to those having a relationship with the corporation the right to sue over its internal affairs.²⁹

29 If, as Omnicare suggests, persons external to those relationships are acknowledged to have standing to sue to enforce them, it is not immediately apparent why competing bidders are the only ones to whom such standing might be accorded. See *Laster, supra*, 53 *Bus. Law.* 767, note 20.

[*1173] [**24] Therefore, the court will dismiss Counts II through V of Omnicare's complaint for lack of standing.

B. Omnicare's Count I "Voting Rights" Argument

Omnicare's claim relating to the effect of the Voting Agreements on the Class B shares held by Outcalt and Shaw stands on a different footing. Count I is not a fiduciary duty based claim and does not seek any coercive remedy against either the corporation or its directors. Instead, in Count I, Omnicare seeks a declaration that the Voting Agreements resulted in the automatic conversion of those Class B shares into Class A shares, pursuant to the terms of the NCS certificate of incorporation. If Omnicare prevails on this claim, the voting power of the shares of common stock that are subject to the Voting Agreements will be diminished from more than 65% to approximately 20% of the total voting power of NCS.

As distinguished from the balance of Omnicare's complaint, the relief sought in Count I does not relate to or seek to remediate any alleged fiduciary misconduct that preceded Omnicare's ownership of NCS stock. Rather than seek to undo anything or remedy any wrong committed in the past, Count I of the complaint merely demands [**25] to know whether Outcalt and Shaw continue to own high-voting Class B shares or, instead, whether those shares have been converted into Class A shares.

This is a question of immediate and continuing interest to all stockholders of NCS. It is also a question to which Omnicare, as the owner of 1,000 Class A shares will eventually be entitled to an answer. If Omnicare were to wait until after the vote to approve the Merger takes place, there is no dispute that it would have standing to challenge the result of that vote by bringing a claim under 8 *Del. C.* § 225(b).³⁰ And, in that proceeding, the court would have the power and, assuming an appropriate set of facts, the duty to resolve the issue. The question is whether Omnicare currently has standing to

challenge what it no doubt would have standing to challenge at some future date. The court finds that it does.

30 8 Del. C. § 225(b) provides:

Upon application of any stockholder or any member of a corporation without capital stock, the Court of Chancery may hear and determine the result of any vote of stockholders or members, as the case may be, upon matters other than the election of directors, officers or members of the governing body.

[**26] There is, as already discussed, a strong public policy against the purchase of a lawsuit involving the internal relations of a Delaware corporation.³¹ If Omnicare brought this claim for declaratory relief solely as a holder of a small number of shares purchased with knowledge of the Voting Agreements, this public policy would doubtless present an overwhelming obstacle to the maintenance of that suit.³² Nevertheless, Omnicare is also a bidder, with an existing cash tender offer priced much higher than the Merger, factors that merit special consideration.³³ Omnicare has powerful resources, is highly motivated, [*1174] and fully prepared to litigate

this issue. If it is successful, there is a substantial likelihood that the NCS stockholders will be able to achieve a superior transaction in the sale of their corporation.³⁴ Considering all of these circumstances, the policy against purchasing a claim should give way to permit the prompt, efficient and effective litigation of the issues asserted in Count I. Therefore, the court finds that Omnicare has standing to pursue Count I of its complaint.

31 See Section V(A)(1), *supra*.

[**27]

32 In addition to the considerations already discussed, that conduct would raise substantial issues about the motivation of both Omnicare and its attorneys.

33 See *MacAndrews & Forbes*, 1985 Del. Ch. LEXIS 545, 1985 WL 21129 at *4-5; *Tate & Lyle PLC*, 1988 Del. Ch. LEXIS 61, 1988 WL 46064 at *8.

34 The merger consideration is currently valued at approximately \$ 1.30 per share in NCS stock. Omnicare's tender offer is priced at \$ 3.50 per share in cash.

VI.

For the foregoing reasons the motion to dismiss Omnicare's claims is granted as to Counts II through V. The motion to dismiss Count I is denied. **IT IS SO ORDERED.**



LEXSEE 273 BR 58

IN RE: MARVEL ENTERTAINMENT GROUP, INC.; THE ASHER CANDY COMPANY; FLEER CORP.; FRANK H. FLEER CORP.; HEROES WORLD DISTRIBUTION, INC.; MALIBU COMICS ENTERTAINMENT, INC.; MARVEL CHARACTERS, INC.; MARVEL DIRECT MARKETING INC.; and SKYBOX INTERNATIONAL, INC., and MARVEL ENTERPRISES, INC., Debtors. MARVEL ENTERTAINMENT GROUP, INC.; MEI HOLDING CO. F; MEI HOLDING CO. FHF MEI HOLDING CO. S; MALIBU COMICS ENTERTAINMENT INC; MARVEL CHARACTERS, INC.; and MARVEL ENTERPRISES, INC., Plaintiffs, v. MAFCO HOLDINGS, INC.; MARVEL III HOLDINGS INC.; MARVEL (PARENT) HOLDINGS, INC.; MARVEL HOLDINGS INC.; RONALD O. PERELMAN; WILLIAM C. BEVINS; and DONALD G. DRAPKIN, Defendants.

Civil Action No. 97-638-RRM, Civil Action No. 98-756-RRM

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF DELAWARE

273 B.R. 58; 2002 U.S. Dist. LEXIS 2033; 2002-1 U.S. Tax Cas. (CCH) P50,302

February 6, 2002, Decided

SUBSEQUENT HISTORY: Partial summary judgment granted by *In re Marvel Entm't Group, Inc.*, 274 B.R. 99, 2002 U.S. Dist. LEXIS 3114 (D. Del., 2002)

DISPOSITION: [**1] Court held that Defendant and Director defendants not liable to Plaintiff. Plaintiff's breach of contract claim held moot.

COUNSEL: David B. Stratton, Esquire, M. Duncan Grant, Esquire, Andrea B. Unterberger, Esquire, and Joseph S. Naylor, Esquire, Pepper Hamilton LLP, Wilmington, Delaware, for plaintiffs.

Anthony W. Clark, Esquire, Eric M. Davis, Esquire, and Paul J. Lockwood, Esquire, Skadden, Arps, Slate, Meagher & Flom LLP, Wilmington, Delaware, for defendants.

Robert E. Zimet, Esquire, Susan L. Saltzstein, Esquire, and W.H. Ramsay Lewis, Esquire, Skadden, Arps, Slate, Meagher & Flom LLP, New York, New York, for defendants.

JUDGES: MCKELVIE, District Judge.

OPINION BY: MCKELVIE

OPINION

[*61] MEMORANDUM OPINION

Wilmington, Delaware

February 6, 2002

MCKELVIE, District Judge

This is a dispute between a parent and subsidiary over a tax-sharing agreement involving claims for breach of fiduciary duty, breach of contract, fraudulent conveyance, and avoidable transfer under the Bankruptcy Code. Plaintiff Marvel Entertainment Group, Inc. is a Delaware corporation and is the reorganized debtor in case number 97-638-RRM, pending in this court ("the Marvel bankruptcy case"). [**2] Plaintiffs MEI Holding Company F. Corp. (formerly known as Fleer Corp.), MEI Holding Co. FHF (formerly known as Frank H. Fleer Corp.), MEI Holding Company S Corp. (formerly known as Skybox International Inc.), Marvel Characters, Inc., and Malibu Comics Entertainment Inc. are each Delaware corporations, reorganized debtors in the Marvel bankruptcy case, and direct or indirect subsidiaries of Marvel Entertainment. In 1998, Marvel Entertainment was merged into a holding company controlled by Toy Biz, Inc. Subsequently, Toy Biz changed its name to Marvel Enterprises. Plaintiff Marvel Enterprises, [*62] Inc. is a

Delaware corporation. In this opinion, the court will refer to the plaintiffs collectively as the Marvel Group.

Defendant Mafco Holdings, Inc. is a Delaware corporation. During the time period relevant to this dispute, May 19, 1993 through April 24, 1997, Mafco's indirect ownership of Marvel Entertainment exceeded 80%. By virtue of its direct and indirect ownership of a majority of Marvel Entertainment's issued and outstanding stock, Mafco had the ability to participate in the determination of the size and elect all members of Marvel Entertainment's board of directors. Defendants Marvel [**3] III Holdings, Inc., Marvel Holdings Inc., and Marvel (Parent) Holdings Inc. (collectively, "the Marvel Holdings Companies") are direct or indirect subsidiaries of Mafco.¹ The Marvel Holdings Companies also are all former direct or indirect parent companies of Marvel Entertainment and its direct and indirect 80%-owned domestic subsidiaries. The defendant corporations (Mafco and the Marvel Holdings Companies) will be collectively referred to as the corporate defendants.

1 The Marvel Holdings Companies are debtors in proceedings under Chapter 7 of the Bankruptcy Code and are controlled by trustees appointed thereunder. Because the Marvel Holdings Companies are in Chapter 7 proceedings and the automatic stay provision of *section 362 of the Bankruptcy Code*, 11 U.S.C. § 362 they have not been named as defendants to the breach of fiduciary duty claim or the breach of contract claim. They have only been named defendants to Count IV of the amended complaint, the claim for avoidable transfer under 11 U.S.C. § 549.

[**4] Defendants Ronald O. Perelman, William C. Bevins, and Donald O. Drapkin (collectively, "the director defendants") are former members of the board of directors of Marvel Entertainment and served on its board during the period from May 13, 1997 through April 24, 1997. During the period relevant to this dispute, Perelman held a beneficial interest in 100% of the outstanding common stock Mafco. Due to his ownership interest in Mafco, Perelman had the capability to direct Mafco with respect to its ability to determine the size and elect all members of Marvel Entertainment's board of directors. During the period from May 13, 1997 through April 24, 1997, Perelman, Bevins, and Drapkin were members of the executive committee of the Marvel Entertainment Board of Directors.

This case is an adversary proceeding of the Marvel bankruptcy case that has been filed in the district court. After filing their initial complaint on December 23, 1998, and later amending their complaint on April 22, 1999 to add claims against the director defendants, plaintiffs filed their second amended complaint on February

20, 2001. The second amended complaint alleges: (i) a state law claim against the director defendants [**5], for breach of fiduciary duties; (ii) a state law breach of contract claim against Mafco for breach of two provisions of a tax sharing agreement; (iii) a fraudulent conveyance claim against Mafco under 11 U.S.C. § 548; and (iv) an avoidable transfer claim against the corporate defendants under 11 U.S.C. § 549. All of the claims relate to a tax sharing agreement that was entered into between Mafco and Marvel Entertainment, under which Mafco used the operating losses of Marvel Entertainment in its federal income tax returns for periods when both were members of the same consolidated tax group. It is alleged that when the parties entered into the tax sharing agreement during the period of May 19, 1993 through April 24, 1997 the corporate defendants and the director defendants were in a position of conflict.

On March 2, 2001, Mafco and the director defendants moved for summary judgment [**63] on all the claims, arguing, among other things: (i) that plaintiffs' claims against Mafco and the director defendants fail because they are "claims related to or arising out of the Tax Sharing Agreement" which have been expressly released by Marvel Entertainment [**6] under a release agreement that was entered into between the parties; (ii) that the breach of fiduciary duty claim is barred by the statute of limitations and also fails because the plaintiffs cannot show that the Tax Sharing Agreement was unfair; (iii) that the breach of contract claim is barred by the statute of limitations and also fails because the provision at issue does not apply during taxable periods when Marvel Entertainment is no longer part of the Mafco consolidated tax group; (iv) that the avoidable transfer claims under 11 U.S.C. §§ 548, 549, and 550 fail because no "transfers" occurred during the relevant periods within the meaning of the Code; (v) that the avoidable transfer claims also fail because the post-petition actions under the tax sharing agreement were authorized by the bankruptcy court and undertaken in the ordinary course of Marvel Entertainment's business; and (vi) that all of plaintiffs' claims should fail because they have suffered no damages. Also on March 2, 2001, the defendants answered the plaintiffs' second amended complaint and filed amended counterclaims. Defendants' counterclaims allege that plaintiffs breached a stipulation [**7] and order, the release agreement, and the tax sharing agreement. Defendants' counterclaims also allege that Marvel Enterprises tortiously interfered with Mafco's contractual rights.

On March 20, 2001, the Marvel Group moved to dismiss the defendants' amended counterclaims, answered Mafco's motion for summary judgment, and filed a Rule 56(f) motion to obtain a continuance for discovery. Mafco's motion for summary judgment, Marvel

Group's motion to dismiss the defendants' counterclaims, and Marvel's Rule 56(f) motion are currently pending before the court. On October 3, 2001, the court held a pre-trial conference. At the pre-trial conference the parties informed the court that, because the trial was to be a bench trial, the issues were fully briefed, and a large number of facts, especially those relating to liability, are undisputed, they would be amenable to postponing the trial, bifurcating the liability and damages issues, and having the court, with the aid of any supplemental briefing that the parties deem necessary, resolve the liability issues on the briefing. See Oct. 3, 2001 Pre-Trial Conf. Tr. at 6-9. Accordingly, the parties filed supplemental briefing and on October 31, 2001, the [*8] court heard oral argument on the liability issues.

This is the court's decision on Mafco's motion for summary judgment and Marvel Group's motion to dismiss the defendants' counterclaims. Because the parties agree as to the underlying facts, the court need only resolve the questions of law raised by the parties motion in order to resolve the liability issues in the case.

I. STATEMENT OF FACTS AND BACKGROUND

The essential facts are undisputed. The court draws the following facts from the undisputed facts section of the pre-trial order and from documents submitted in support of the parties' briefs.

A. Net Operating Losses and Consolidated Federal Income Tax Groups

Because the claims asserted in this case concern Mafco's use of net operating losses (NOLs) generated by Marvel Entertainment in federal income tax returns filed by Mafco for periods during which both were members of the same consolidated tax group, it will be instructive to briefly review [*64] the Internal Revenue Code rules governing the use of NOLs, consolidated tax groups, and the use of NOLs by consolidated tax groups.

1. Net Operating Losses

NOLs occur when a corporation's operating losses exceed income. [*9] In such instances, corporate taxpayers are entitled to deduct NOL carryovers and NOL carrybacks in determining their taxable income in each taxable year. Carrying back NOLs for that purpose entitles the taxpayer to a refund of taxes attributable to the prior year's income offset by the carryback. See *Internal Revenue Code*, § 172. When carrying back NOLs, the taxpayer must first apply the NOLs to the oldest tax year to which it is permitted to carry back NOLs and in which it had reported income. See *id.* The taxpayer's income for a given tax return year could be reduced to zero if the NOLs carried back are large enough to cancel out in-

come entirely for that year. Under IRS regulations during the period relevant to this dispute, NOLs incurred by a corporation could be carried back three years and could also be carried forward for fifteen taxable years.

2. Consolidated Tax Groups

A consolidated group of corporations consists of one parent corporation that owns, directly or indirectly, 80% or more, by vote and value, of the other corporations in the group. 26 U.S.C. § 1504(a). The Internal Revenue Code of 1986, as amended ("the [*10] IRC"), and the Treasury Regulations promulgated thereunder, permit, but do not require, a parent corporation to file one consolidated federal income tax return on behalf of all members of the consolidated group that includes the parent's own income and the income of each of its domestic subsidiaries of which the parent corporation owns 80% or more of the stock by vote and value.

If a parent corporation elects to file a consolidated federal income tax return, it must, with certain exceptions not relevant here, include in all such tax periods the gains and losses of all of its domestic subsidiaries in which it owns at least 80% by vote and value. When a parent corporation and its subsidiaries file a consolidated federal income tax return, each corporate entity in the consolidated group first calculates its taxes as if it were a stand-alone taxpayer (with certain consolidating adjustments), and the gains and losses are then combined to determine the consolidated group's federal income tax liability. Thus, under the IRC and Treasury Regulations, a consolidated group is permitted to file one federal income tax return on behalf of all members of the consolidated group that reflects the [*11] income, losses, gains, deductions, and credits of all the members as if they were a single business enterprise conducted by one corporation. See Crestol, Hennessey & Yates, *The Consolidated Tax Return* at 1-2 (Warren, Gorham & Lamont 5th ed. 1998).

3. The Use of Member NOLs by Consolidated Tax Groups

As described above, consolidated tax returns allow the corporate taxpayer to offset the taxable gains of one member corporation against the operating losses of another member corporation in determining the tax liability of the group. However, when a NOL generated by a member of a consolidated tax group is absorbed by the group, a member of the group owning stock in the subsidiary that generated the NOL must reduce its basis in the stock of that subsidiary by the amount of the NOL absorbed. See *Treasury Regulations*, § 1.1502-19. If the subsidiary continues to generate NOLs that are absorbed by the [*65] group, the subsidiary's losses can continue to be deducted against the other member's taxable in-

come even after the stock basis in the subsidiary is reduced to zero. If the amount of the NOL generated by a subsidiary that is absorbed exceeds the group [**12] member's basis in the stock of the subsidiary, the group member's basis in the stock is reduced below zero, creating a "negative basis." Id. This negative basis is called an "excess loss account" ("ELA"). The ELA provisions require that a parent's negative basis with respect to subsidiary stock be "recaptured" as taxable income when a triggering event, generally the parent disposing of stock in the subsidiary, occurs. ELA recapture is triggered, for example, when a parent ceases to own 80% of the shares of the subsidiary.

In sum, the ELA Treasury Regulations require that, if the stock of the subsidiary is sold to a non group member, any balance in the excess loss account is recognized as capital gain income. When the subsidiary ceases to be a member of the consolidated group, the amount of the ELA must be "recaptured" as income to the consolidated group.

If one of the members of a consolidated group has generated a NOL for the taxable year, that loss must be used in the group's federal income tax return to reduce the group's total taxable income and may not be used again. See *Treasury Regulations* §§ 1.1502-2; 1.1502-11; 1.1502-12; 1.1502-21A. Nothing [**13] in the IRC or the Treasury Regulations requires members of a consolidated group to compensate the group, the parent, or any other member for the incurrence of income or loss that may generate either tax liability or benefit for the group. Although neither the IRC or the Treasury Regulations mandate, mention, or refer to the use of tax sharing agreements, it is not uncommon for the members of a consolidated group to provide for the allocation of the economic impact of these liabilities and benefits among themselves by entering into private agreements that prescribe whether and how payments shall be made within the consolidated group to take account of the income and losses of the members. See Bitker & Eustice, *Federal Income Taxation of Corporations and Shareholders*, at P13.41[4][b] (Warren, Gorham & Lamont 7th ed. 2000). In this case, Marvel Entertainment and Mafco entered into such an agreement; that agreement forms the basis for all of the claims asserted by Marvel in this action.

B. The Tax Sharing Agreement

On or about May 19, 1993, when Mafco increased its direct and indirect ownership of Marvel Entertainment to a level in excess of 80%, the Marvel Group became [**14] part of Mafco's consolidated tax filing group. Marvel and Mafco remained members of the same consolidated group until April 24, 1997, when Marvel Entertainment was "deconsolidated" from the Mafco consolidated group after a change in control of Marvel Enter-

tainment's immediate parent company, Marvel Holdings, Inc.

While the parties were members of the same consolidated tax group, Marvel Entertainment and Mafco's responsibilities and obligations with regard to the consolidated group's federal income tax liability were governed solely by the IRC. Under the IRC, Mafco was primarily responsible to pay the consolidated tax liability of the entire consolidated tax group, including the Marvel Group's portion. Following the consolidation, in order to allocate the financial consequences of the federal income tax laws among the members of the consolidated group, Marvel Entertainment and Mafco entered into the Tax Sharing Agreement.

[*66] Under the Tax Sharing Agreement, the Marvel Group was to calculate its federal income tax liability each year while it was a member of Mafco Group as if it were a hypothetical stand-alone taxpayer rather than part of the Mafco consolidated group. If the Marvel Group [**15] stand-alone entity had positive taxable income in a given tax year, Marvel Entertainment would pay to one or more of the corporate defendants an amount equal to the tax that would be due on such income, whether or not the Mafco group actually had taxable income. Conversely, if Marvel Entertainment generated NOLs (again computed on the assumption that it was a stand-alone entity) that it could have carried back to offset its previously earned taxable income had it been filing its own income tax return, Mafco would pay to Marvel Entertainment an amount equal to the tax benefit that would have inured to Marvel Entertainment had it not been part of the Mafco consolidated tax group. Mafco was required to make such payments whether or not the Mafco consolidated tax group was otherwise liable for federal income tax, due to the fact that other members of the Mafco consolidated tax group had no taxable income or were generating NOLs. Thus, pursuant to the Tax Sharing Agreement, Marvel Entertainment was paid for the hypothetical tax benefit that arose from its stand-alone NOLs even when the other parties to the Tax Sharing Agreement would derive no benefit from them. Any portions of NOLs that [**16] remained after they were carried back against the Marvel Group's separate income in prior years on a stand-alone basis, could be carried forward for tax-sharing purposes and used to reduce the Marvel Group's future years' taxable income, and thus reduce or eliminate the Marvel Group's tax payment obligation to the defendants.

In effect, under the Tax Sharing Agreement, Mafco acted as a proxy for the IRS. If Marvel Group as a stand-alone taxpayer would have owed taxes to the IRS, it made a tax-sharing payment to Mafco, but if Marvel Group as a stand-alone taxpayer would have received a

refund from the IRS, Mafco made a tax-sharing payment to Marvel Group.

The Agreement did not have any provisions directly addressing the effects of deconsolidation of the Marvel Group from the Mafco consolidated tax group. It did, however, have a provision that addressed "any situation or circumstance concerning such calculation and allocation that is not specifically contemplated" by the Agreement. That provision, section 12, provided that such calculations and allocations should be "dealt with in a manner consistent with the underlying principles of calculation and allocation in the Agreement." The [**17] parties to the Agreement also provided that they would cooperate to provide each other with any necessary information, stating in paragraph 8(b) that:

Parent, Marvel and Marvel III shall provide one another with such information concerning such returns and the application of payments made under this Agreement as Parent, Marvel or Marvel III may reasonably request of one another.

The Tax Sharing Agreement was publicly disclosed no later than March 31, 1994, when it was filed with the Securities and Exchange Commission as an exhibit to Marvel Entertainment's 1993 Form 10-K.

C. The Marvel Group's 1995 and 1996 NOLs

As a result of Marvel Entertainment's addition to the Mafco group as of May 19, 1993, Marvel Entertainment's three tax years preceding 1995 were (i) the January 1 to May 18, 1993 short tax year, when the Marvel was not a part of the Mafco group; [**67] (ii) the May 19 to December 31, 1993 tax year, and (iii) the January 1 to December 1994 tax year. In 1993 and 1994, Marvel generated taxable income and, under the terms of the Tax Sharing Agreement, made payments to Mafco in the amounts of approximately \$ 12.7 million in 1993 and \$ 13.7 million in 1994.

In 1995, while [**18] Marvel Entertainment was still a member of the Mafco consolidated tax group, the Marvel Group generated an NOL for the first time in several years. Computed on a stand-alone basis, the amount of the Marvel Group's NOL in 1995 was \$ 61.8 million. Pursuant to the IRC and Regulations, Marvel Entertainment carried a portion of its 1995 NOL back to its May 18, 1993 short tax year, to offset approximately \$ 23 million in income that it had reported for that short tax year, and received the appropriate refund from the IRS. Under the Agreement, the remainder of the 1995 NOL was applied to offset Marvel Entertainment's in-

come (computed on a stand-alone basis) for its short tax year ending December 31, 1993 and for its 1994 tax year. The Mafco group reimbursed the Marvel Group in the amount of approximately \$ 15.1 million, in accordance with the Agreement, for such application of the Marvel Group's 1995 NOL.

Marvel Entertainment has not been profitable since before 1995. Thus, in 1996 and in the portion of 1997 during which it was part of Mafco's consolidated tax group, Marvel again generated stand-alone NOLs. Computed on a stand-alone basis, the amount of Marvel's 1996 NOL was \$ 139.9 million. [**19] As required by the federal income tax laws governing consolidated tax groups, Marvel's 1996 NOL was, like its 1995 NOL, consolidated with income and losses generated by other members of the Mafco consolidated tax group in the consolidated tax returns for the group for those years.

Unlike its 1995 NOL, whose entire value could have been used to offset income earned by Marvel in prior tax years had it been filing as a stand-alone entity, only a portion of Marvel's 1996 stand-alone NOL, approximately \$ 40.5 million, could have been used to offset income in this manner. Therefore, under the Agreement, in consideration of Marvel's hypothetical 1995 \$ 61.8 million stand-alone NOL and the \$ 40.5 million portion of its hypothetical 1996 stand-alone NOL, Marvel Entertainment was ultimately paid in full by Mafco under the Tax Sharing Agreement for its hypothetical tax refund, approximately \$ 25 million -- \$ 15.1 million for the 1995 NOL and \$ 10.4 million for the 1996 NOL -- by virtue of carrying back those NOLs on a stand-alone basis. Approximately \$ 100 million of Marvel Entertainment's 1996 NOL, however, could not be carried back to any prior Marvel Group tax year. Accordingly, under the [**20] terms of the Agreement, Mafco did not reimburse Marvel for this portion of the 1996 NOL that could not be applied to offset Marvel's stand-alone income for prior tax years. Because the Mafco consolidated tax group used the 1996 Marvel NOL in its consolidated federal income return, as it was required to by the tax code, Marvel is prohibited by the IRC and Regulations from using that NOL in its own tax returns in the future.

D. Marvel Entertainment's Deconsolidation from the Mafco Group

On December 27, 1996, Marvel Entertainment and certain of its subsidiaries filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code. During 1997, both Marvel Entertainment and Chase Manhattan Bank, as agent for the debtor-in-possession (the "DIP Agent") lenders, made demands on Mafco for payment [**68] of \$ 10.4 million then owned to Marvel Entertainment under the Tax Sharing Agreement for the por-

tion of Marvel's 1996 NOL that could have been used to offset income earned by it in prior years.

Thereafter, as part of a settlement concerning the use of the lenders' cash collateral, Marvel Entertainment agreed that Mafco would make the post-petition payment due under the Agreement directly [**21] to the DIP Agent, which would release \$ 4.2 million of the funds to Marvel Entertainment for working capital, credit another \$ 2.5 million to interest owed by Marvel Entertainment under its DIP financing agreement, and hold the balance as cash collateral for Marvel Entertainment's obligations under the DIP financing agreement. The Bankruptcy Court approved and memorialized this agreement in a Stipulation and Order With Respect to the Limited Use of Cash Collateral dated October 21, 1997.

In connection with obtaining court approval of the Stipulation and Order, Marvel Entertainment also gave a release and indemnity to Mafco and the director defendants in a Release Agreement dated October 27, 1997. In the Release Agreement, Marvel Entertainment "acknowledges that the payment to Chase Manhattan Bank" pursuant to the Stipulation and Order "satisfies all remaining obligations of Mafco to make refunds to Marvel or to the Marvel Group under Section 5(b) of the Tax Sharing Agreement" and thus releases Mafco and its officers, directors, and employees from "claims related to or arising out of the Tax Sharing Agreement for payment due to [Marvel] under Section 5(b) of the Tax Sharing Agreement. [**22] " Section 5(b) of the Tax Sharing Agreement provides:

Refund of Tax Sharing Payment: In the event that the calculation of the Marvel Group's Federal Taxable Income . . . for any Taxable Period results in a loss, such loss may be carried back and deducted in calculating the Marvel Group's Federal Tax . . . for prior Taxable Periods in the same manner as it would have been carried back and deducted had it constituted a net operating loss deduction under [certain sections of the IRC]

The scope and effect of this release is disputed by the parties.

E. Marvel Entertainment's April 24, 1997 NOL

On or about April 24, 1997, Marvel Entertainment was deconsolidated from the Mafco tax sharing group when a third party obtained voting control of Marvel Entertainment. As a result, Marvel had a short tax year from January 1 to April 24, 1997 and another short tax

year from April 25 to December 31, 1997. Because Marvel was again not profitable during the portion of 1997 for which it was part of Mafco's consolidated tax group, Marvel again generated a stand-alone NOL. Computed on a stand-alone basis, the Marvel Group had a NOL of approximately \$ 66 million for its short tax year [**23] ending April 24, 1997.

Upon deconsolidation, the Marvel Group was allocated \$ 18.8 million of NOLs generated by it during the period in which the Marvel Group was consolidated with the Mafco Group, in accordance the IRC and applicable regulations. This left the Mafco group a \$ 47.2 million stand-alone NOL that had been generated by Marvel during the short-year 1997 tax year. As required by the federal income tax laws, as with Marvel's stand-alone 1995 and 1996 NOLs, Marvel's short-year 1997 stand-alone NOL was consolidated with income and losses generated by other members of the Mafco consolidated tax group in the consolidated tax returns for the group. Marvel Entertainment's 1997 NOL, however, could not [**69] be carried back to any prior Marvel Group tax year. Accordingly, under the Tax Sharing Agreement, Mafco did not reimburse Marvel for its 1997 NOL. Because the Mafco consolidated tax group used the 1997 Marvel NOL in its consolidated federal income return, as it was required to do so, Marvel is prohibited by the IRC and Regulations from using that NOL in its own tax returns in the future.

Due to the deconsolidation of the Marvel Group from the Mafco group, the ELAs of the Mafco group [**24] relating to the Marvel Group were triggered and, as a result, the Mafco group had to recognize \$ 150.6 million in taxable income. Thus, in accordance with IRS regulations, upon the deconsolidation of Marvel from the Mafco consolidated tax group, Mafco was required to give up any tax benefit that it may have gained from the Marvel's NOLs through the income tax adjustments that arose from the triggering of the ELAs. Because the Mafco group had an inventory of several billion dollars of consolidated NOLs from its other members, the recognition of such income did not result in any actual tax liability for the Mafco group, but it did result in \$ 150.6 million of NOLs being used to offset such income.

F. The Continuing Losses of Marvel Entertainment

On July 31, 1998, this court entered a consent order confirming the Fourth Amended Joint Plan of Reorganization Proposed By the Secured Lenders and Toy Biz, Inc. Under the Joint Plan, Marvel Entertainment was to be merged into a holding company controlled by Toy Biz. On October 1, 1998, Toy Biz and the secured lenders consummated the plan, and Toy Biz changed its name to Marvel Enterprises, Inc.

Since leaving the Mafco consolidated tax group in April 1, 1997, Marvel Entertainment has not had any operating profits, nor has the Marvel Enterprises consolidated tax group of which Marvel Entertainment became a member in October 1998. For the tax period from April 25 to December 31, 1997, the Marvel Group generated NOLs in the amount of \$ 87.4 million. For the tax period from January 1 to October 1, 1998, the Marvel Group generated NOLs in the amount of \$ 80.9 million. For the tax period from January 1, 1998 to December 31, 1998, the Marvel Enterprises consolidated tax group generated NOLs in the amount of \$ 43.1 million. For the tax period from January 1, 1999 to December 31, 1999, the Marvel Enterprises consolidated tax group generated taxable income in the amount of \$ 797,679.²

2 Despite this factual recitation in the pre-trial order, the parties appear to dispute whether the overall Marvel Enterprises family of corporations (including foreign subsidiaries, whose results may not be included in a U.S. consolidated federal income tax return) had positive operating results in 1999 and in the first quarter of 2001. Mafco contends in its briefing that since leaving the Mafco consolidated group in April 1997, Marvel Entertainment has not had any operating profits, nor has the Marvel Enterprises consolidated tax group of which Marvel Entertainment became a member in October 1998. Mafco notes that Marvel Enterprises generated \$ 17 million of NOLs in 1999 and, in a February 27, 2001 press release, reported a net loss of \$ 89.9 million for the year ended December 31, 2000.

[**26] Each of Marvel Enterprises' 1999 and 2000 Form 10-K filed with the Securities and Exchange Commission states that "no benefit was provided for . . . the Federal . . . net operating loss carryforwards" at the end of that year. This statement means that the independent auditors of Marvel Enterprises believed that for the purposes of GAAP, it was more likely than not that the current NOLs of the [*70] Marvel Enterprises' group, including the Marvel Group, would not be realized because the group will not have any taxable income to offset with those NOLs before they expire.

G. Marvel's Lawsuit Against Mafco

The Marvel Group, in this lawsuit, alleges that while it was part of the Mafco consolidated tax group from May 19, 1993 through April 24, 1997, it generated approximately \$ 147 million in NOLs, which were used on Mafco's 1996 and 1997 federal tax returns, for which it was not fairly compensated. The \$ 147 million in NOLs for which Marvel asserts it was not fairly compensated is comprised of a \$ 100 million portion of its 1996 NOL

and its entire \$ 47 million short tax year 1997 NOL. Marvel asserts that it should be compensated for Mafco's use of these NOLs, because once they were used [*27] by Mafco in its federal tax returns, they can no longer be used by Marvel Entertainment or its successor, Marvel Enterprises.

Marvel raises three legal theories that it believes entitles them to the relief they seek. First, the Marvel Group raises a breach of fiduciary duty claim contending that Mafco's failure to compensate Marvel for the use of its NOLs in 1996 and 1997 under the Tax Sharing Agreement constitutes an act of "gross and palpable overreaching" in a parent-subsidiary relationship. Marvel also asserts a claim for breach of contract under paragraphs 12 and 8(b) of the Tax Sharing Agreement. Last, Marvel contends that Mafco's use of Marvel's NOLs constitutes a non-ordinary course transfer of Marvel's property that is avoidable under the Bankruptcy Code.

ii. DISCUSSION

The parties have stipulated to the facts as set forth by the court above. To resolve the disputed liability issues, the court has considered the arguments made both at oral argument and in parties' briefing accompanying Mafco's summary judgment motion and Marvel's motion to dismiss Mafco's counterclaims, as well as the supplemental briefing that has been submitted by the parties.

A. Are Marvel's [*28] Claims Barred by the Release Agreement?

Before reaching at the merits of the parties dispute, the court must first consider Mafco's contention that Marvel Entertainment released Mafco from all of the claims it now brings in this action in its October 1997 Release Agreement. According to Mafco, the terms of the release indicate that as quid pro quo for obtaining the benefit of the \$ 10.4 million payment, Marvel Entertainment agreed to "release, acquit, and forever discharge" Mafco from any and all claims "related to or arising out of the Tax Sharing Agreement for payment due to [Marvel] under Section 5(b) of the Tax Sharing Agreement," and that this release shall be "a complete defense and bar to any action, claim, or demand" brought on such claims for payment. Mafco asserts that since section 5(b) is the only section of the Tax Sharing Agreement that addresses NOLs generated by Marvel Entertainment and its right to be compensated on account of them, the release acts to bar the claims raised in Marvel's complaint. Thus, Mafco concludes, because the Marvel's breach of contract claims "directly arise out of the Tax Sharing Agreement" and the other claims -- including those for breach [*29] of fiduciary duty for causing Marvel Entertainment to enter into the contract and to avoid alleged transfers of NOLs pursuant to the contract -- are "related

to" the Tax Sharing Agreement, these claims have been released and should be dismissed.

[*71] According to Marvel, it never released Mafco from the claims brought in this litigation. Marvel contends that because the release is limited to claims arising out of section 5(b), it does not act to bar its claims, which are based on other sections of the Tax Sharing Agreement or on fiduciary duties, which Marvel argues the director defendants breached by causing Marvel to enter the Agreement.

Section 5(b) of the Agreement deals specifically with reimbursement to the Marvel Group of past tax sharing payments as a result of the Marvel Group's ability to carry back, on a hypothetical stand-alone basis, losses to years in which it made such payments. This release accompanied the settlement of the dispute between the DIP Agent and Marvel Entertainment as to which of them was entitled to receive the \$ 10.4 million owed by Mafco to Marvel pursuant to section 5(b) of the Tax Sharing Agreement in consideration for Marvel's 1996 NOL.

The release [*30] was not, as Mafco asserts, the quid pro quo for getting the \$ 10.4 million payment; the parties did not dispute the fact that the money \$ 10.4 million payment for its 1996 NOL was owed by Mafco under the Tax Sharing Agreement. The only dispute was as to which party -- the DIP Agent or Marvel -- should receive the payment. "In construing a release, the intent of the parties as to its scope and effect are controlling, and the court will attempt to ascertain their intent from the overall language of the document." *Adams v. Jankouskas*, 452 A.2d 148, 155 (Del. 1982). In view of the circumstances surrounding the release and the language in the release stating that it released claims relating to or arising from section 5(b) of the Tax Sharing Agreement, the intent of the release was to prevent Marvel from asserting that it was owed more than what it got for past payments under the terms of the agreement and to prevent Mafco from being liable to Marvel for such past payments once it had satisfied its obligation by paying the money to the DIP Agent. Had Marvel asserted a claim against Mafco in this lawsuit that Mafco still owed it money under the Agreement in consideration [*31] of its use of the one of the past year's NOLs, the release would bar Marvel's claim because that claim would necessarily arise out of section 5(b) of the Tax Sharing Agreement.

In this litigation, however, Marvel does not dispute the correctness of Mafco's past payments for NOLs under the Agreement. Rather, Marvel claims that Mafco's refusal to compensate the Marvel Group for the lost future benefit of its NOLs after deconsolidation is either a breach of section 12 of the Tax Sharing Agreement, that

causing Marvel to enter into the Tax Sharing Agreement itself was a breach of fiduciary duty, or that Mafco's use of Marvel's NOLs without fair compensation constitutes an avoidable transfer under the Bankruptcy Code. These claims do not arise out of or relate to section 5(b) of the Agreement, as required by the language of the release. While these claims are surely related to the Tax Sharing Agreement, the scope of the release does not cover all claims arising out of or relating to the Tax Sharing Agreement. Instead the release only covers those claims arising out of or relating to section 5(b) of the Agreement. Accordingly, because the court finds that Marvel is proceeding under legal [*32] theories that are not grounded in section 5(b) of the Tax Sharing Agreement, Marvel's claims are not barred by the release.³

3 Mafco argues, in part, that at least Marvel's section 12 breach of contract claim should be barred because section 5 is the only section in the Agreement that addresses compensation for NOLs. Mafco claims that while Marvel is facially proceeding under the section 12 "catch-all" provision, the breach of contract claim is in truth a disguised claim under section 5 because section 12 states only that all allocations must be "dealt with in a manner consistent with underlying principles of calculation and allocation in the Agreement." While the court acknowledges that this argument carries some force, the court is hesitant to collapse Marvel's section 12 breach claim into a section 5 breach claim based on Marvel's contention that section 12 set forth additional rights exclusive of section 5. Therefore, the court will evaluate the breach of contract claim on the merits.

[*72] B. Are the Director [*33] Defendants Liable for Breach of Fiduciary Duty?

1. Is the Breach of Fiduciary Duty Claim Time-Barred?

Before turning to the merits of the Marvel Group's breach of fiduciary duty claim, the court must first address Mafco's defense that the claim is barred by the applicable statute of limitation. Mafco claims that the Marvel Group's breach of fiduciary duty claim is time-barred because the applicable three year statute of limitations, see 10 Del. C. § 8106, which it asserts began to run when the Tax Sharing Agreement was executed on May 19, 1993, expired before this action was commenced on December 28, 1998. See *Kahn v. Seaboard Corp.*, 625 A.2d 269, 274 (Del. Ch. 1993) (applying three year limitations period to breach of fiduciary duty claim premised on unfair contract between parties); *Dofflemyer v. W.F. Hall Printing Co.*, 558 F. Supp. 372, 379 (D. Del. 1983) (applying 10 Del. C. § 8106 to fiduciary duty claim). Mafco asserts that where, as here, the claimed breach is prem-

ised on an allegedly unfair contract, the limitations period begins to run when the contract is formed. See *Kahn*, 625 A.2d at 270-71. Mafco also contends [**34] that the limitations period should not be tolled until April 24, 1997, when Mafco lost "control" of Marvel, because although Marvel itself was powerless to bring a lawsuit against Mafco by virtue of the director defendants' domination of its board, Marvel's stockholders had the power to challenge the Tax Sharing Agreement at any time through a derivative suit on the corporation's behalf. See *Levine v. Smith*, 591 A.2d 194, 200 (Del. 1991), overruled in part on other grounds by, *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

Marvel, in response, acknowledges that the breach of fiduciary duty claim is subject to the three year limitations period set forth in 10 Del. C. § 8106, but argues that the limitations period did not begin to run until September 15, 1997, the extended due date for corporations to file their 1996 tax returns. Marvel argues that this was when Mafco first engaged in the alleged wrongful conduct that caused injury to the plaintiff by using the Marvel NOLs in its consolidated tax return for the 1996 tax year without compensating Marvel for such use. Alternatively, Marvel contends that even if the wrongful conduct were deemed to have occurred [**35] before September 15, 1997, the statute of limitations was tolled until April 24, 1997, because until that date, the plaintiffs were dominated and controlled by the defendants and were thus unable to file an action against them. See 3A James Solheim & Kenneth Elkins, *Fletcher Encyclopedia of the Law of Private Corporations* § 1306.20 (1994 & Supp. 1998) (under the theory of "adverse domination," the statute of limitations is tolled for as long as a corporate plaintiff continues under the domination of the alleged wrongdoers).

This action was commenced on December 28, 1998. There is no disagreement between the parties that Delaware's three year statute of limitations, 10 Del. C. § 8106, applies to the fiduciary duty claim. See *Fike v. Ruger*, 754 A.2d 254, 260 (Del. [**73] Ch. 1999). The disputed issues with respect to whether the action was timely filed are (i) when the statute of limitations period began to run, and (ii) whether the limitations period should be tolled due to the defendants' adverse domination of the plaintiffs' board of directors.

a. When did limitations period begin to run?

In addressing whether an action is time-barred, the court must first determine [**36] the time when the cause of action accrued. The court agrees with Mafco that because the fiduciary duty claim is based on the adoption of the terms and conditions set forth in the Tax Sharing Agreement dated May 19, 1993, that, under Delaware case law, Marvel's fiduciary duty claim ac-

crued on the date of the adoption of that contract. More specifically, because this claim is premised on Mafco and the director defendants having caused Marvel Entertainment to enter into the Tax Sharing Agreement, the elements of this claim -- a duty, and an alleged breach -- were established no later than May 19, 1993, when Marvel Entertainment entered into the Tax Sharing Agreement.

Delaware law supports finding that where the claimed breach of fiduciary duty is an allegedly unfair contract, the limitations period begins to run when the contract is formed. For example in *Kahn v. Seaboard Corp.*, 625 A.2d at 274, on a similar set of allegations that a majority shareholder forced the corporation they controlled into a detrimental long-term contract in breach of fiduciary duties, the Delaware Court of Chancery held that the three year limitations period barred the claim, noting that: [**37]

the wrong attempted to be alleged is the use of control over Seaboard to require it to enter into a contract that was detrimental to it and beneficial, indirectly, to defendants. Any such wrong occurred at the time that enforceable legal rights against Seaboard were created. Suit could have been brought immediately thereafter to rescind the contract . . . Complete and adequate relief, if justified, could be shaped immediately or at any point thereafter.

Kahn, 625 A.2d at 271. Similarly, in *Schreiber v. Bryan*, 396 A.2d 512, 516 (Del. Ch. 1978), a case involving a derivative claim of waste based on a tax sharing agreement, the Chancery Court, in concluding that the shareholder plaintiff who had purchased stock after the transaction had occurred did not have standing, stated that "what must be decided is when the specific acts of alleged wrongdoing occur, and not when their effect is felt." *Id.* Here, as in those cases, the alleged wrongful acts were consummated at the time the tax sharing agreement at issue was entered into.

Marvel seeks to distinguish the present case from *Kahn*, arguing that here the wrongful conduct was not [**38] the execution of the Agreement, but rather Mafco's performance under the Agreement. Marvel submits that because Marvel generated no hypothetical stand-alone NOLs in 1993 and 1994 and was reimbursed in full by Mafco for its 1995 hypothetical stand-alone

NOL, Mafco did not treat Marvel unfairly by using its NOLs without fair compensation until Mafco filed its 1996 tax return. Thus, Marvel argues that its fiduciary duty claim first accrued on September 15, 1997 (the date on which Mafco filed its 1996 tax return), even though the alleged injury to Marvel is based on the terms and conditions previously established by the Agreement entered into by the parties in 1993. This same argument was considered and rejected by the Chancery Court in Kahn, when Chancellor Allen stated:

[*74]

It is implicitly admitted that payments were made by Seaboard as provided in the contract . . . the payments it calls for are legal obligations, not wrongs. Thus, unlike a continuing wrong, the only liability matter to be litigated involves defendants' 1986 actions in authorizing the creation of these contract rights and liabilities.

Kahn, 625 A.2d at 271.

Here, as in Kahn, the [**39] plaintiffs' breach of fiduciary duty claim hinges upon the allegations that the terms and conditions established by a contract are unfair to the plaintiff corporation. Accordingly, the court finds that here, as in Kahn, the cause of action accrued when the contract fixed the parties' rights (in 1993) and not when an allegedly harmful legal obligation arose under the contract (in 1997). This finding is consonant with the principle that in discerning when a cause of action accrues, "the determinative issue is when the specific acts of alleged wrongdoing occurred, and not when their effect is felt." Ernest L. Folk, III, et al., *Folk on Delaware General Corporation Law* § 327.3 (4th ed.).⁴

4 Moreover, Mafco correctly points out that if the court agreed with Marvel that the fiduciary duty claim accrued, not in May 1993, but in September 1997, that would lead to the absurdity of allowing a fiduciary duty claim to proceed against persons who were not fiduciaries when the claim accrued. This is so because according to the complaint, the time period during which the defendants allegedly owed fiduciary duties ended on April 24, 1997, five months prior to the date that Marvel asserts should be the accrual date of the fiduciary duty claim. See Sec. Am. Compl. P 106.

[**40] b. Is there a basis to equitably toll the limitations period?

Having found that the plaintiffs' fiduciary duty claim accrued on May 19, 1993, when the director defendants caused Marvel to enter into the Tax Sharing Agreement, the court must next determine whether the statute of limitations should nonetheless be tolled until April 24, 1997 under the doctrine of "adverse domination," because until that date the plaintiffs were dominated and controlled by the defendants and were unable to file an action against them. If the court were to find such tolling appropriate, because this action was initiated within three years of the date when the defendant directors ceased to control Marvel's board, it would not be time-barred. Absent tolling, however, the action would be time-barred because the suit was filed well after the three year limitations period ended on May 19, 1996.

Under the adverse domination doctrine, the statute of limitations on a corporation's claim against its officers and/or directors is equitably tolled while the corporation's board of directors is controlled by culpable directors. The premise underlying the adverse domination doctrine is that a corporation acts through [**41] its board of directors, and when that board of directors is controlled by culpable directors it will not cause the corporation to bring a lawsuit against themselves. See *Federal Deposit Ins. Corp. v. Bird*, 516 F. Supp. 647, 652 (D.P.R. 1981); *Hecht v. Resolution Trust Corp.*, 333 Md. 324, 635 A.2d 394, 402 (Md. 1994). Since the advent of this doctrine in the Bird case, there have been a multitude of cases in many jurisdictions accepting various versions of the adverse domination tolling doctrine. See *Hecht*, 635 A.2d at 401-02 (collecting cases). Delaware courts, however, have neither accepted nor rejected the use of the adverse domination doctrine, and, as far as the court can discern, the issue has not been addressed by a Delaware court.

In those jurisdictions where the doctrine has been accepted, the adverse domination [**75] doctrine has generally been applied to a specific type of case. As the Supreme Court of Kansas noted, in reviewing the history of the doctrine:

most reported cases referring to the doctrine were decided in the 1980's or 1990's and involve failed banks or savings and loans. Plaintiffs in the action wherein [**42] the doctrine is referred to are most likely to be the FDIC, FDSLIC, or RTC [because] given the customarily short statute of limitations . . . the statute would run before the action could be brought by the federal agency unless some special doctrine or exception exists which tolls

the statute Adverse domination has been recognized in many jurisdictions as the vehicle to overcome a statute of limitations defense in such situations.

Resolution Trust Corp. v. Scaletty, 257 Kan. 348, 891 P.2d 1110, 1114 (Kan. 1995).

While the doctrine has not been expressly limited to application in receivership cases, its use in those types of cases is relevant because it illuminates the rationale behind the theory. The District of Puerto Rico in *Bird* recognized that the touchstone of the adverse domination theory lies in ensuring that claims are not barred before the underlying wrongs are disclosed to those who can represent the corporation in a suit against the directors, when it stated that its holding was based on "the realities of the shareholders' position, that, without knowledge of wrongful activities committed by directors, shareholders have no meaningful [**43] opportunity to bring suit." 516 F. Supp. at 651. Subsequent cases addressing the doctrine have similarly recognized that the statute of limitations is allowed to run once someone has sufficient knowledge and ability to seek redress on the corporation's behalf. See *Federal Deposit Ins. Co. v. Hudson*, 673 F. Supp. 1039, 1042 (D. Kan. 1987) (stating that "other federal district courts have followed the lead of . . . *Bird* . . . , recognizing" that "the emphasis has shifted from a right of shareholders to inspect corporate records and affairs to a duty of corporate managers to disclose"); *Scaletty*, 891 P.2d at 1116 (adverse domination will be determined by when injurious facts are readily ascertainable by corporation); *Hecht*, 635 A.2d at 406 (presumption of tolling "can be rebutted . . . by evidence that someone other than the wrongdoing directors had knowledge of the cause of action, and both the ability and the motivation to bring suit")⁵. Moreover, some courts have adopted a version of the doctrine under which "the plaintiff has the burden of showing 'full, complete, and exclusive control' by culpable directors charged [**44] with wrongdoing and must negate the possibility that an informed director or shareholder could have induced the corporation to institute suit." *Hecht*, 635 A.2d at 403 (citing *Farmers & Merchants Nat. Bank v. Bryan*, 902 F.2d 1520 (10th Cir. 1990) and *Resolution Trust Corp. v. Fleischer*, 826 F. Supp. 1273, 1278 (D. Kan. 1993)); cf. *Clark v. Milam*, 192 W. Va. 398, 452 S.E.2d 714 (W. Va. 1994) (holding that doctrine of adverse domination tolls statutes of limitation notwithstanding that claims similar to plaintiff's claims could have been raised by shareholders of company, where shareholders of the parent company had little interest in redressing the wrongs to the subsidiary insurance company).

5 Significantly, before adopting the adverse domination doctrine and allowing the corporation to proceed with its suit, the *Hecht* court noted that (unlike Delaware) as a general rule in Maryland, shareholders are barred from bringing actions on behalf of the corporation. *Hecht*, 635 A.2d at 398 (citing *Davis v. Gemmell*, 70 Md. 356, 376, 17 A. 259 (1889)).

[**45] Marvel cites no Delaware authority on point in support of its request to toll the [**76] statute of limitations based on the defendants "adverse domination" of the plaintiff's board. Nor can the court find any Delaware case that recognizes the adverse domination doctrine as a tolling mechanism. Moreover, the cited cases from foreign jurisdictions are unhelpful in resolving whether the adverse domination theory should be available to toll the statute of limitations in cases such as this one, where, although the director defendants dominated the plaintiff's board, the alleged harmful act (i.e. the entering of the Tax Sharing Agreement) was disclosed to plaintiff's shareholders who could have instituted derivative actions on behalf of the corporation. See, e.g., *In re Mi-Lor Corp. v. Gottsegen, et al.*, 233 B.R. 608, 1999 Bankr. LEXIS 519, 1999 WL 301205 (Bankr. D. Mass. 1999) (basing decision that tolling is appropriate partially on the fact that the plaintiffs' did not and could not have reasonably learned of the misdeeds until after the defendants ceased to be a board majority).

However, certain courts that recognize the adverse domination theory of tolling have stated that "if . . . shareholders [**46] learn of the misconduct that harms their corporation, the [adverse domination] rule may no longer toll the limitations period." *Clark*, 452 S.E.2d at 720. In the absence of authority in Delaware to the contrary, the court finds that when disclosures of the alleged harmful acts are made to shareholders, the corporate entity is no longer without redress against those who control it because the shareholders have both the knowledge and authority to protect the corporation's rights, and that therefore, there is no reason to toll the statute of limitations. See *Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984) ("The derivative action developed in equity to enable shareholders to sue in the corporation's name where those in control of the company refused to assert a claim belonging to it."); see also *Meyerson v. El Paso Natural Gas Co.*, 246 A.2d 789 (Del. Ch. 1967) (derivative action challenging tax sharing agreement).

The tolling doctrines that have been recognized in Delaware provide support for the above stated proposition that, where representatives of the corporation have both notice and opportunity to redress the alleged wrongs against [**47] the corporate entity, tolling is inappropriate. For example, courts have consistently rejected "equitable tolling" of limitations periods where the facts un-

273 B.R. 58, *; 2002 U.S. Dist. LEXIS 2033, **;
2002-1 U.S. Tax Cas. (CCH) P50,302

derlying the claims were disclosed in publicly filed documents. See, e.g., *In re Dean Witter P'ship Litig.*, 725 A.2d 441, 1999 Del. LEXIS 3, 1998 WL 442456, at *8 (Del. Ch. 1998) (refusing to toll limitations period because information in defendants' annual reports should have provided the plaintiffs with adequate notice of their claims), *aff'd mem.*, 725 A.2d 441 (Del. 1999); *Seidel v. Lee*, 954 F. Supp. 810, 817 (D. Del. 1996); *United States Cellular Inv. Co. v. Bell Atlantic Mobile Sys. Inc.*, 677 A.2d 497, 503-04 (Del. 1996) (refusing to toll statute of limitations because public documents could have put plaintiff on notice of any alleged misconduct by defendants); *In re USACafes, L.P. Litig.*, C.A. No. 11146, 1993 Del. Ch. LEXIS 12, 1993 WL 18769, at *5 (Del. Ch. Jan. 21, 1993) (refusing to toll statute of limitations to allow plaintiff to amend by adding time-barred claims, because public filings had put plaintiffs on notice that their rights had been infringed.).

Marvel contends [**48] that these cases are inapposite because they address whether the plaintiffs were on notice that their rights were violated and do not address what would happen if those claims belonged to corporations that were adversely dominated. The court disagrees. While Delaware courts that have addressed tolling have not directly focused on adverse [**77] domination, *per se*, they have instead focused on the assumption that underlies the adverse domination doctrine-- that "with control comes non-disclosure and without knowledge of directors' wrongful activities plaintiffs have no meaningful opportunity to bring suit." *Hecht*, 635 A.2d at 401. Therefore, in determining whether to toll a statute of limitations, Delaware courts inquire as to whether the facts underlying the plaintiffs' allegations were publicly disclosed such that derivative suits could have been filed. As the *Dean Witter* court stated in describing equitable tolling as it exists in Delaware:

underlying the doctrine is the idea that 'even an attentive and diligent [investor] relying . . . upon the good faith of [fiduciaries] may be completely ignorant of transactions that constitute self-interested acts injurious [**49] to the [Partnership]. This doctrine tolls the limitations period until an investor knew or had reason to know of facts constituting the wrong.

Significantly, if the limitations period is tolled under any of these theories [inherently unknowable injuries, equitable tolling, or fraudulent concealment], it is tolled only until the plaintiff discovers (or exercising reasonable diligence should have discovered) his injury. Thus, the limitations begins to run when the plain-

tiff is objectively aware of the facts giving rise to the wrong, i.e., on inquiry notice.

Dean Witter, 725 A.2d 441, 1999 Del. LEXIS 3, 1998 WL 442456, at *6 (emphasis added); see also *Kahn*, 625 A.2d at 276-77 (where wrongful self-dealing is alleged in a derivative action, the statute does not run against the plaintiff until he or she knew or had reason to know the facts alleged to give rise to the wrong).

Because the court believes that Delaware's tolling mechanisms, in combination with the availability of shareholder derivative actions, already address the concerns that underlie the adverse domination doctrine, the court declines to recognize adverse domination as a viable tolling mechanism in Delaware. [**50] Moreover, even if the court were to accept that the adverse domination doctrine could be applied in Delaware, the court would decline to do so upon these facts, because the fiduciaries disclosed the tax sharing agreement at issue here in its 1993 Form 10-K.

c. Would Marvel's breach of fiduciary duty claim have been successful on the merits

To Marvel, it might seem eminently unsatisfactory for the court to find that its claim was barred by the statute of limitations due to the failure of its minority shareholders to institute a derivative suit in a timely manner, especially in consideration of equitable estoppel principles that have, in certain cases, been applied to prevent a fiduciary from using the statute of limitations to prevent claims of misconduct raised against it. See, e.g., *Banco De Desarrollo Agropecuario, S.A. v. Gibbs*, 709 F. Supp. 1302, 1310 (S.D.N.Y. 1989); cf. *Adams*, 452 A.2d at 157 (stating that "while the limitations of actions applicable in a court of law are not controlling in equity, absent unusual circumstances, the analogous statute of limitations will be given great weight in deciding whether the plaintiff's claim is [**51] barred by laches."); but see *United States Cellular*, 677 A.2d at 502 ("Absent some unusual circumstances, a court of equity will deny a plaintiff relief when suit is brought after the analogous statutory period."). However, based upon the court's consideration of the parties' briefs on the merits of the fiduciary duty claim, the court notes here that even if it were to conclude, based on some equitable consideration, see *Kahn*, 625 A.2d at 272-76 (recounting equitable considerations relied on by the Chancery Court in the past to prevent statutes of limitation from barring [**78] fiduciary claims), that Marvel's claims were timely brought, the court would nonetheless agree with Mafco and find that the Tax Sharing Agreement is not unfair as a matter of law. Thus, while the court need not reach the merits of the fiduciary duty claim, in order to demonstrate that there are also substantive grounds for ruling in favor of

273 B.R. 58, *; 2002 U.S. Dist. LEXIS 2033, **;
2002-1 U.S. Tax Cas. (CCH) P50,302

Mafco on this claim, the court will briefly set forth its reasons in the following paragraphs.

On the merits, the parties dispute whether the decision to allocate tax liabilities according to the terms of the Tax Sharing Agreement constituted [**52] "gross and palpable overreaching," such that Mafco and the director defendants breached a fiduciary duty that was owed to Mafco's subsidiary, Marvel. Marvel claims that it is entitled to compensation for the value of the NOLs that were available to Mafco as a result of Marvel's membership in Mafco's consolidated tax group. Underlying the parties' dispute is a disagreement about the proper standard to be applied to directors in a parent-subsidary tax sharing arrangement. While the Chancery court has stated that the standard to be applied to such agreements is "one of business judgment with which the court should not interfere absent a showing of 'gross and palpable overreaching,'" *Meyerson v. El Paso Natural Gas Co.*, 246 A.2d 789, 794 (Del. Ch. 1967), the parties dispute whether this standard is one of business judgment or whether a more exacting 'entire fairness' inquiry is called for.

In cases like this, the standard to be applied is often outcome determinative. See *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361, 1371 (Del. 1995) (stating that "because the effect of a proper invocation of the business judgment rule is so powerful and the standard [**53] of entire fairness so exacting, the determination of the appropriate standard of review frequently is determinative of the outcome of litigation."). Under the standard of entire fairness, the burden is on the parent corporation to prove, subject to exacting scrutiny, that its transactions with the subsidiary were objectively fair. See *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 719-20 (Del. Ch. 1971). Conversely, "under the business judgment rule . . . a court will not interfere with the judgment of a board of directors unless there is a showing of gross and palpable overreaching." *Id.* Thus, under the business judgment rule, a board's "decisions will not be disturbed if they can be attributed to any rational purpose" and a court "will not substitute its own notions of what is or is not sound business judgment." *Id.*

The question of which standard to apply in parent/subsidiary tax sharing situations was settled in *Meyerson* and confirmed again in *Wolfensohn v. Madison Fund, Inc.*, 253 A.2d 72 (Del. 1969). In *Meyerson*, the plaintiff, a minority stockholder of an 80% owned subsidiary, asserted that the parent corporation, which controlled [**54] the subsidiary through ownership, had breached its fiduciary duties by including the subsidiary in its consolidated tax group without implementing a "fair" tax sharing agreement. 246 A.2d at 790. There the plaintiff alleged that the inclusion of the NOLs generated by the subsidiary in calculating the tax liability of the

consolidated group was unfair because the parent received tax benefits and did not share any of those benefits with the subsidiary. The relief sought by the plaintiff included payment for the NOLs generated by the subsidiary and a "fair allocation" of future benefits. The court granted summary judgment to the parent corporation, holding that the question of how much tax benefit is to be allocated between the parent and subsidiary in a tax sharing agreement is "one of business judgment. . . ." [**79] *Id.* at 794. This holding was later expressly approved of by the Delaware Supreme Court in *Wolfensohn*, 253 A.2d at 76. See also *Getty Oil Co. v. Skelly Oil Co.*, 267 A.2d 883, 888 (Del. 1970) (applying business judgment rule to parent-subsidiary allocation agreement and finding that subsidiary failed to demonstrate [**55] "gross and palpable overreaching.").

Marvel seeks to conflate the 'gross and palpable overreaching' standard with that of entire fairness, arguing that this standard is not identical with the unexacting business judgment rule. In light of *Meyerson* and *Wolfensohn*, the court disagrees, and finds that the business judgment rule is the correct standard to be applied. Marvel's efforts to distinguish those cases are unpersuasive. The application of an entire fairness test that requires tax sharing agreements to be dollar-for-dollar fair to the parent and subsidiary would both be undesirable and unworkable. First it is better to leave such issues to the discretion of directors under the business judgment rule because "it is impossible, as between parent and subsidiary, to set fair standards for allocation agreements." *Meyerson*, 246 A.2d at 794; see also Mary Siegel, *The Erosion of the Law of Controlling Shareholders*, 24 Del. J. Corp. L. 27, 37 n.39 (1999) (internal citations omitted) ("Courts treat decisions to file a consolidated tax return, which is available to a parent owning at least 80% of the shares of its subsidiary, under the deferential [**56] business judgment rule . . . primarily due to the fact that there is no marketplace counterpart by which to measure the fairness of these transactions."). Second, an entire fairness inquiry would make little sense because the consequences of tax consolidation are not dictated by the parent corporation, but by the IRS. Here, Marvel's hypothetical stand-alone NOLs were required to be included in the determination of the taxable income of the Mafco consolidated tax group.

Applying the business judgment rule to the transaction at issue, the court would thus find that causing Marvel to enter the Tax Sharing Agreement was not a breach of fiduciary duty. Absent the tax sharing agreement, Mafco would have had to pay Marvel's portion of the Mafco consolidated group's federal income tax liability if, in the same year, the other members of the Mafco group had also generated income. The court agrees with Mafco that the Agreement served the rational purpose of

273 B.R. 58, *; 2002 U.S. Dist. LEXIS 2033, **;
2002-1 U.S. Tax Cas. (CCH) P50,302

raising funds for the payment of the Mafco group's consolidated tax liabilities from those members of the group, including Marvel, which generated the income that gave rise to those liabilities. See *Brehm v. Eisner*, 746 A.2d 244, 264 (Del. 2000) [**57] (in applying the business judgment rule, the court will not measure, weigh, or quantify directors' judgments unless they are found to be wholly irrational).

Moreover, even if the court were to apply the "gross and palpable overreaching" standard in a manner that is more exacting than the standard of "waste" or the "business judgment rule," and were to analyze this transaction from the perspective that "self-dealing occurs when the parent, by virtue of its domination of the subsidiary, causes the subsidiary to act in such a way that the parent receives something from the subsidiary to the exclusion of, and detriment to, the minority shareholders of the subsidiary," *Sinclair Oil*, 280 A.2d at 720, the court would nonetheless come to the same conclusion. It is undisputed that Mafco enjoyed no unfair tax benefits from the Tax Sharing Agreement as a result of Marvel's deconsolidation because the tax laws, which Mafco complied with, require the adjustment of any Marvel NOLs that were used. [**80]

Any alleged incidental non-tax benefits⁶ that accrued to Mafco as a result of the agreement are not egregious enough to merit a finding that this transaction constituted "gross and [**58] palpable overreaching." The two non-tax benefits cited by Marvel pertain to benefits to Mafco arising merely from the use of money that Marvel paid to it under the Agreement. Such benefits are not unfair because in other years, under the terms of the Agreement, Mafco paid out substantial monies to Marvel. From Marvel's perspective, therefore, the Tax Sharing Agreement eased the impact of the tax laws on Marvel, because absent such an agreement, under the tax laws it could not receive any refunds with respect to taxes paid during the period it was a member of the Mafco consolidated group, even had it been entitled to such refunds as a stand-alone taxpayer. Under the Agreement, however, Marvel received millions of dollars from Mafco on account of the NOLs it generated. Had Marvel been a stand-alone taxpayer, it would have had to pay the same amount that it paid to Mafco to the IRS and would have received the same refunds that Mafco paid to it from the IRS.

6 In its supplemental briefing, Marvel concedes that Mafco gained no tax benefits from its use of Marvel's NOLs. However, Marvel contends that Mafco unfairly enjoyed the following non-tax benefits: (i) cash flow benefits from monies paid to Mafco by Marvel under the terms of the Agreement in 1993 and 1994; (ii) interest rate

differential benefits based on Mafco's ability to negotiate a lower interest rate on bonds that it issued, due to monies it received from Marvel under the Agreement.

[**59] Because under the terms of the Tax Sharing Agreement, Mafco essentially acted as a proxy for the IRS, Marvel cannot be said to be harmed by paying to Mafco monies that it would have had to pay to the IRS had it not been a member of the Mafco consolidated group. The injury that Marvel complains of, however, -- its loss of the use of its future NOLs -- resulted from the operation of the IRC and applicable Treasury Regulations and not from any wrong committed by the defendants. Accordingly, the court would not substitute its judgment for the judgment of the director defendants regarding the proper allocation of taxes in a consolidated tax group.

C. Is Mafco Liable for Breach of Paragraph 12 of the Tax Sharing Agreement?

Marvel's next claim is that Mafco breached the Tax Sharing Agreement by failing to compensate Marvel for the use of approximately \$ 147 million in NOLs pursuant to paragraph 12 of the Tax Sharing Agreement. This claim was first raised by Marvel when it amended its complaint in February 2001.

1. Is Marvel's Paragraph 12 Breach of Contract Claim Time-Barred?

Mafco first argues that Marvel's claim for breach of paragraph 12 of the Tax Sharing Agreement is time-barred [**60] because it was raised more than three years after the applicable three year limitations period. See Del C. § 8106; see also *Aronow Roofing Co. v. Gilbane Bldg. Co.*, 902 F.2d 1127, 1128 (3d Cir. 1990). Under Delaware law, the statute of limitations for breach of contract claims begins to run when the contract is breached. *Freedman v. Beneficial Corp.*, 406 F. Supp. 917, 923 (D. Del. 1975). Mafco asserts that because the contract was allegedly breached on April 24, 1997, the date on which the Marvel Group was deconsolidated from the Mafco Group, Marvel's breach of contract claim is untimely.

Marvel contends that its claim is not untimely because it relates back to [**81] December 23, 1998, the date on which Marvel filed its initial complaint. See *Fed. R. Civ. P. 15(c)*. Rule 15 of the Federal Rules of Civil Procedure allows a party to amend its complaint to assert a new claim, even if the statute of limitations has run on the new claim, if that claim "arose out of the conduct, transaction, or occurrence set forth or attempted to be set forth in the original pleading. . . ." *Id.* "The purpose of Rule 15 is to provide maximum opportunity for each

claim [**61] to be decided on the merits rather than on procedural technicalities." *United States v. Thomas*, 221 F.3d 430, 435 (3d Cir. 2000) (internal quotes omitted).

The court disagrees with Mafco's argument that this breach of contract claim is "completely different" from its original claims. It is simply another legal theory grounded in the same set of facts. Marvel's paragraph 12 breach of contract theory for relief arises out of the same conduct, transaction, and facts that were set forth in its initial complaint, because it relates to the Tax Sharing Agreement. Therefore, the initial complaint sufficiently put Mafco "on notice of the facts and claims that gave rise to" this later added claim. 3 James W. Moore et. al, *Moore's Federal Practice*, § 15.19 (Matthew Bender 3d ed.). Accordingly, the court finds that under *Rule 15* this claim relates back to December 23, 2001, the date on which the plaintiffs filed their initial complaint. Because December 23, 1998 is within three years of April 24, 1997, plaintiffs' paragraph 12 breach of contract claim will be considered timely filed. The court will therefore turn to the merits of the claim.

2. Is Mafco liable for Breaching [**62] Paragraph 12 of the Tax Sharing Agreement?

Paragraph 12 of the Tax Sharing Agreement, entitled "Interpretation," states:

This Agreement is intended to calculate and allocate certain Federal and state and local income tax liabilities of the members of the [Mafco] Group and the Marvel Group, and any situation or circumstance concerning such calculation and allocation that is not specifically contemplated hereby or provided for herein shall be dealt with in a manner consistent with the underlying principles of calculation and allocation in this Agreement.

Marvel contends that because the Tax Sharing Agreement does not specifically address deconsolidation, the catch-all provision, paragraph 12, requires Mafco to pay Marvel Entertainment for its lost future use of NOLs generated while it was in the Mafco consolidated group. According to Marvel, compliance with paragraph 12 requires Mafco to compensate Marvel Entertainment for Mafco's use of its NOLs, because such compensation would be consistent with the underlying principles of the Agreement, which are to put the Marvel Group in the tax and economic position that it would have been in had it been a stand-alone [**63] consolidated tax-filing group. Thus, Marvel contends it is entitled to payments for NOLs that allegedly "would have provided future benefit to Marvel had the Marvel Group either: (1) remained part

of the Mafco Group; or (2) always been a stand alone group."

Mafco argues in response that the language of the Agreement does not provide Marvel with any such post-deconsolidation entitlement and that paragraph 12 of the Agreement does not obligate Mafco to make any payments to Marvel after deconsolidation. Mafco's only obligations were to pay Marvel in accordance with paragraph 5, which it did. Mafco concludes, therefore, that Marvel's claim for [**82] breach of paragraph 12 of the Agreement is not cognizable as a matter of law. To support its argument, Mafco focuses on paragraph 23 of the Agreement, which provides that "none of the parties hereto shall have any obligations or liabilities under this Agreement with respect to any Taxable Period during which Marvel is not a member of the [Mafco] Group . . ." Thus, the defendants reason that because Marvel has not been a member of the Mafco Group since April 1997, Marvel cannot invoke the "obligations and liabilities" of paragraph 12 to obtain [**64] any future benefits. In addition, Mafco argues that even if paragraph 23 does not expressly bar Marvel's breach of contract claim, the claim should nonetheless fail because in seeking a lump sum payment for the future use of its NOLs, it is not "consistent with the underlying principles of calculation and allocation in this Agreement," as paragraph 12 requires. Rather, Mafco asserts, Marvel's demands for payment to offset its potential tax liabilities in future years violates a fundamental principle of calculation and allocation in the Agreement. All such calculations and allocations apply only to a "Taxable Period," which is defined as "any taxable year or portion thereof . . . with respect to which a consolidated Federal income tax return is properly filed on behalf of the Group which includes Marvel . . ."

As a threshold matter, the court does not agree with Mafco that paragraph 23 or the definition of "Taxable Period," necessarily bars Marvel's claim. Marvel's claim is related to the disposition of stand-alone NOLs that were generated during "Taxable Periods" when it was a member of the Mafco consolidated tax group and a party to the Tax Sharing Agreement.

However, turning [**65] to the merits of Marvel's claim, the court concludes that Mafco did not breach paragraph 12 of the Agreement. To find that Mafco breached paragraph 12 of the Tax Sharing Agreement, the court would have to interpret paragraph 12 in such a manner that would create the affirmative obligation in Mafco to pay Marvel for the future use of its NOLs, once it has already compensated Marvel in the manner set forth in section 5(b) of the Agreement. The court declines to do so.

Under the Agreement, if Marvel had taxable income, calculated as a stand-alone entity, Marvel would pay to Mafco the amount of its tax liability that it would have had to pay to the IRS. By contrast, if Marvel had a stand-alone NOL and it could have carried that NOL back to offset its taxable income in a prior tax year, Mafco would pay to Marvel the amount of the tax refund that it would have received from the IRS. The agreement does not state that Mafco had to compensate Marvel for the use of its NOL if Marvel could not carry that NOL back to any prior taxable year. Such a reading would be inconsistent with the principles of calculation and allocation as set forth in the Agreement.

A review of the parties' performance [**66] under the Agreement demonstrates that Mafco and Marvel did act under the agreement, "in a manner consistent with the underlying principles of calculation and allocation in [paragraph 5 of] this Agreement." In 1993, in consideration of its taxable income, Marvel paid to Mafco \$ 12.7 million. In 1994, in consideration of its taxable income, Marvel paid to Mafco \$ 13.7 million. In 1995, because Marvel generated a \$ 61.8 million NOL that was could be fully offset by prior years income, Mafco paid to Marvel \$ 15.2 million. In 1996, however, only \$ 40 million of the \$ 140 million NOL generated by Marvel could have been applied to offset Marvel's prior year's income. In accordance with the terms of [**83] the agreement, Mafco compensated Marvel \$ 10.4 million for that portion of the NOL that could be carried back. In 1997, none of Marvel's adjusted \$ 47 million NOL could be carried back by Marvel. In accordance with the terms of the agreement, Mafco did not pay Marvel because no portion of the NOL could be carried back. This summary demonstrates that during each year that the Agreement was in effect, the parties complied with its terms. Accordingly, paragraph 12 should not be read to impose any [**67] additional obligation on Mafco to compensate Marvel for its loss of the future use of its NOLs.

During 1995, 1996, and 1997, as required by the IRC, Mafco applied Marvel's entire NOLs to its consolidated tax returns. While it is true that this action had the legal effect of preventing Marvel from ever using those NOLs in the future once it was deconsolidated from the Mafco tax group, nothing in the Agreement or the IRC mandates that Marvel must be compensated for NOLs generated while a member of a consolidated tax group. Moreover, in consideration of the ELA's that are triggered under the IRC upon deconsolidation, whose purpose is to adjust for any tax benefits that Mafco may have enjoyed from using Marvel NOLs during the period when Marvel was a member of its consolidated tax group, imposing an obligation upon Mafco to further compensate Marvel would make little sense.

D. Can Marvel Avoid the Transfer of Its NOLs Under the Bankruptcy Code?

In Count III and IV of its Second Amended Complaint, Marvel raises claims under *Bankruptcy Code* sections 548 and 549 contending that the defendants' use of \$ 147 million of Marvel Group's 1996 and April 24, 1997 NOLs constitutes both (i) [**68] a transfer of Marvel Group's interest in property in the year prior to the bankruptcy filing without the debtors "receiving reasonably equivalent value in exchange for such transfer" that is therefore avoidable under section 548; and (ii) a post-petition transfer of Marvel Group's interest in property that was not authorized by the Bankruptcy Code or any order of the court that is avoidable under section 549. See 11 U.S.C. §§ 548(a)(1), 549, and 363; *In re Roth American*, 975 F.2d 949, 952 n.3 (3d Cir. 1992) (stating transfers taken outside the ordinary course for which court approval has not been obtained are avoidable). *Bankruptcy Code* section 548 provides that a debtor may "avoid any transfer of an interest of the debtor in property . . . that was made . . . within one year before the date of the filing of the petition" where the debtor "received less than a reasonably equivalent value." 11 U.S.C. § 548(a)(1). *Bankruptcy Code* section 549, provides that a debtor "may avoid a transfer of property of the estate . . . that occurs after the commencement of the case; and . . . that is not authorized under the [Bankruptcy [**69] Code] or by the court." 11 U.S.C. § 549(a).

Mafco, in opposition, asserts (i) that the consolidation of financial results for a tax calculation does not amount to a "transfer" of NOLs between members of a consolidated tax group, within the meaning of section 548 or 549; (ii) that as a member of the Mafco consolidated group, Marvel did not hold an ownership interest in its NOLs because the existence of its own stand-alone NOLs while a member of the consolidated group was merely hypothetical, see *United Dominion Indus. v. United States*, 532 U.S. 822, 150 L. Ed. 2d 45, 121 S. Ct. 1934 (2001), and thus could not transfer them within the meaning of sections 548 and 549, and (iii) that even if the court were to consider the transactions "transfers" or property "owned" by Marvel, Marvel's post-petition section 549 claim must fail [**84] both because the post-petition transfer was authorized by an order of the bankruptcy court and was otherwise authorized by the Bankruptcy Code because they were effected in the ordinary course of Marvel's business. Moreover, Mafco contends that, as a matter of policy, the alleged transfers of NOLs should not implicate the avoidance power [**70] because the NOLs have no value to Marvel. See *Begier v. IRS*, 496 U.S. 53, 58, 110 L. Ed. 2d 46, 110 S. Ct. 2258 (1990) ("If the debtor transfers property that would not have been available for distribution to his creditors in a

273 B.R. 58, *; 2002 U.S. Dist. LEXIS 2033, **;
2002-1 U.S. Tax Cas. (CCH) P50,302

bankruptcy proceeding, the policy behind the avoidance power is not implicated.").

To resolve this dispute, the court must first determine whether there was a transfer of property in which Marvel had an ownership interest that would implicate the avoidable transfer sections of the Bankruptcy Code. See 11 U.S.C. §§ 548(a)(1) and 549(a); see also *Musso v. Brooklyn Navy Yard Dev. Corp. (In re Westchester Tank Fabricators, Ltd.)*, 207 B.R. 391, 397 (Bankr. E.D.N.Y. 1997) (threshold question under section 549 is whether transfer of estate property occurred); *Brandt v. Hicks, Muse & Co. (In re Healthco Int'l, Inc.)*, 201 B.R. 19, 22 (Bankr. D. Mass. 1996) ("for a transfer to be avoided as fraudulent it is necessary that the debtor make an actual transfer"). Bankruptcy Code section 101(54) defines a "transfer" as "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, [**71] of disposing of or parting with property or with an interest in property . . ." 11 U.S.C. § 101(54).

It is undisputed that Mafco, in accordance with the IRC, filed consolidated federal income tax returns for its consolidated group and in doing so was required to apply the group's consolidated NOLs -- including income and losses generated by all members of the group. Mafco, as the group's parent corporation, was responsible for filing the consolidated federal income tax return and for paying any federal income tax due on behalf of all group members. See 26 C.F.R. §§ 1.1502-6. In order to calculate the federal taxable income of the Mafco consolidated group, each member had to first calculate its taxable income in approximately the same manner as if it were filing its own federal income tax return; the items that would have appeared on the individual members' returns were then aggregated, with certain adjustments to account for consolidation. See 26 C.F.R. §§ 1.1502-11, 1.1502-12; see also Federal Income Taxation of Corporations and Shareholders P 13.43 (Warren, Gorham & Lamont, 6th ed. 1998) [**72] (explaining that a consolidated federal income tax return reflects the income and losses of a consolidated tax group as a single entity). The NOLs were computed and applied to the group entity on a consolidated basis in accordance with IRC section 172. Mafco did not have discretion as to whether to "take" NOLs from its group members; rather, the manner in which NOLs were consolidated and applied was statutorily mandated. See *Nisselson v. Drew Indus. (In re White Metal Rolling & Stamping Corp.)*, 222 B.R. 417, 424 (Bankr. S.D.N.Y. 1998) ("the parent has no discretion; the consolidated NOL is applied to prior years in the statutorily mandated order, and then carried forward only if the prior years' consolidated income does not fully absorb it.").

Thus, during the period that Mafco was required to file returns on behalf of the entire consolidated group, it

was the application of tax consolidation principles and the IRC that resulted in certain tax attributes of the group being diminished or eliminated. Moreover, as a result of this regulatory scheme provided for in the federal income tax laws for consolidated tax groups, the individual members of [**73] the [**85] Mafco consolidated group did not possess separate tax attributes such as NOLs. See *United Dominion Indus.*, 532 U.S. 822, 150 L. Ed. 2d 45, 121 S. Ct. 1934 (concept of separate NOLs for individual members of a consolidated tax group does not exist). In the context of the consolidated tax filing group, the hypothetical stand-alone NOLs that were calculated for the purposes of the Tax Sharing Agreement were not property of the debtor because they were a legal fiction. Thus, no actual transfer occurred when those NOLs were applied to the calculation of income tax due. Accordingly, the court finds that Mafco's application of NOLs attributable to Marvel in the federal income tax filings of the Mafco consolidated group does not constitute a transfer from Marvel to Mafco that is cognizable under the Bankruptcy Code.

The deconsolidation of Marvel from the Mafco Group, which was caused by a change in control of Marvel's majority ownership, also did not cause a transfer for the purposes of the Bankruptcy Code. Marvel and the other members of the Mafco Group did not make an election in 1997 to consolidate their tax attributes as part of a consolidated group. As a result of the deconsolidation, [**74] Marvel had two tax years in 1997, one as a member of the Mafco Group and one when it was filing independently. While the method of calculating Marvel's taxes changed as a result of the deconsolidation, there was no transfer of property between Marvel and Mafco. Rather, Marvel's NOLs were attributed to the entire consolidated tax group pursuant to the tax laws.⁷ While courts have avoided or stayed conduct that could have affected the existence or usefulness of NOLs to a debtor, see, e.g. *Gibson v. United States (In re Russell)*, 927 F.2d 413 (8th Cir. 1991) (debtor's election to carry forward an NOL avoided), in this case the plaintiffs do not challenge any conduct that would have affected the viability or existence of the NOLs; they merely complain that the Mafco Group computed its tax liabilities and filed its tax return as required by the IRC. Such a transaction cannot constitute an avoidable transfer.

⁷ Mafco correctly notes that the only allegedly offensive "act" or "transfer" occurred, if at all, when Marvel became a member of the consolidated tax group on May 19, 1993, thereby causing its tax liabilities to be calculated as a single entity with the other members of the Mafco consolidated tax group. This purported transfer, however, occurred more than three and a half years before the bankruptcy petitions were filed

and therefore falls outside of the reach of *Section 548* and *549*. See *11 U.S.C. § 549(a)(1)* (granting trustee the ability to avoid a transfer that occurs after the commencement of the case); *11 U.S.C. § 548(a)(1)* (trustee may avoid transfer that was made within one year before the date of the filing of the petition).

[**75] E. Is Mafco Liable for Breaching Paragraph 8(b) of the Tax Sharing Agreement?

Marvel also asserts that Mafco is liable for breaching paragraph 8(b) of the Tax Sharing Agreement. Paragraph 8(b) creates a mutual duty of cooperation among the parties to the Agreement, stating that each "shall provide one another with such information concerning such returns and the application of payments made under this Agreement as [each party] may reasonably request of one another." Marvel asserts that Mafco breached this provision of the Agreement by failing to provide to Marvel Entertainment tax returns and work papers from Mafco and its advisors. Mafco, in response, asserts that this claim is moot because "Mafco provided Plaintiffs with copies of these returns and work papers, and Plaintiffs received thousands more documents related to the tax returns and work papers from Mafco's advisors."

While conceding that it has received a multitude of documents, Marvel disagrees [**86] that its claim is moot because, it claims, "certain key work papers and analyses still have not been produced that simply must exist." According to the second amended complaint, one of the reasons that Marvel requested these [**76] work papers was to investigate whether the \$ 18 million of NOLs that was apportioned to the Marvel Group by Mafco upon deconsolidation in 1997 was the proper allocation amount. Marvel asserts that "Mafco has failed to produce work papers or related analyses that show why the amount of NOLs apportioned to Marvel upon deconsolidation in 1997 was approximately one-half of what Mafco originally projected" and contends that certain documents that have been produced, such as a 1997 Ernst & Young Memorandum, suggest that Mafco's tax accountants were urged to find ways to reduce the amount of NOLs apportioned to Marvel.

This issue was briefed as part of Mafco's motion for summary judgment. In this opinion the court has, at the urging of the parties, elected to consider that motion as the basis for resolving the liability issues in the case. However, as opposed to the other three claims that the

court has addressed in this opinion, in which only legal issues remained in dispute, there are factual issues that remain in dispute with respect to this claim. Put simply, Marvel contends that Mafco's disclosures were not complete, while Mafco asserts that they were.

In its second amended complaint, [**77] the relief that Marvel requests on this breach of contract claim is "that the Court enter an order requiring Mafco Holdings to provide Marvel Entertainment with copies of the Mafco Group's tax returns and related work papers for the years 1993 through 1997." Based on the lack of factual record concerning this issue, the court is not in a position to rule on whether Mafco has already complied with its obligation to cooperate in the production of documents that Marvel would reasonably request. In essence, at this point in the case, the paragraph 8(b) breach of contract claim appears to be a discovery dispute relating to the apportionment of NOLs upon consolidation. Based on its above findings that Mafco has no liability to Marvel under Marvel's theories of breach of fiduciary duty, breach of contract, or avoidable transfer, this claim appears to be moot. To the extent Marvel desires to pursue its paragraph 8(b) claim as an independent claim against Mafco, despite the court's findings with respect to its other claims, Marvel may petition the court to do so.

iii. CONCLUSION

For the reasons stated above the court finds that Mafco and the director defendants are not liable to Marvel [**78] under either of the three theories set forth in Marvel's complaint. The breach of fiduciary duty claim is time-barred, and even if the court were to substantively entertain the claim, the court would find no breach of fiduciary duty on the merits. Next, based on the language of the Tax Sharing Agreement, the court finds that Mafco did not breach paragraph 12 breach of that Agreement. Finally, Marvel's avoidable transfer claims cannot succeed as a matter of law because the consolidation of Marvel's NOLs onto Mafco's consolidated tax form, while Marvel was a member of Mafco's consolidated tax group, is not a "transfer" that is cognizable under the Bankruptcy Code. Given that these findings will resolve the case in favor of Mafco, the court finds Marvel's paragraph 8(b) breach of contract claim, pursuant to which it seeks further discovery, to be moot.

The court will issue an order consistent with this opinion.

▶ *Norberg v. Security Storage Co. of Washington*
Del.Ch., 2000.

UNPUBLISHED OPINION. CHECK COURT
RULES BEFORE CITING.

Court of Chancery of Delaware.

John NORBERG on behalf of himself and all others
similarly situated, Plaintiff,

v.

SECURITY STORAGE COMPANY OF
WASHINGTON, Childs F. Burden, I. Townsend
Burden III, John D. Firestone, Peter P. van Roijen,
Robert D. van Roijan, Jr., Robert L. Tull, Conrad S.
Posey, Conrad S. Reid, George M. Elsey, Philip L.
Gore, Robert E. Windham and Security Acquisition
Corporation, Defendants.
No. 12885.

Submitted May 31, 2000.

Decided Sept. 19, 2000.

R. Bruce McNew of Taylor & McNew, LLP,
Greenville, Delaware; Robert J. Kriner, Jr. of
Chimicles & Tikellis LLP, Wilmington, Delaware,
for Plaintiff.

Thomas A. Beck of Richards, Layton & Finger,
Wilmington, Delaware, Alfred W. Putnam, Jr. and
Mary Catherine Roper of Drinker Biddle & Reath
LLP, Philadelphia, Pennsylvania, for Defendants, of
counsel.

MEMORANDUM OPINION

STEELE, J.

I. INTRODUCTION

*1 This is the Court's response to the parties' cross motions for summary judgment arising out of a cash-out merger in which the defendant majority shareholder allegedly squeezed-out the minority. One of the minority shareholders, plaintiff John Norberg, challenged the merger individually and on behalf of a purportedly similarly injured class of minority shareholders. Specifically, he alleges that the defendants, in breach of their fiduciary duties,

squeezed-out the minority at a grossly inadequate price, in an unfairly timed transaction using an unfair process and without providing them information material to a decision to tender their shares or seek appraisal.

The defendants seek summary judgment arguing that Norberg acquiesced in the merger transaction when he tendered his shares of common stock for the merger consideration. Norberg moves for summary judgment arguing that there can be no factual dispute that the majority acted to freeze out the minority at an unfair price and with an unfair process. Norberg also seeks class certification under Court of Chancery Rules 23(a), 23(b)(1) and 23(b)(3).

The issues presented on these cross motions are narrowly drawn.

First, are Norberg's claims barred by acquiescence as a result of accepting the merger consideration 17 months after filing suit detailing a laundry list of reasons why the majority breached their fiduciary duties of disclosure and loyalty to the minority?

Second, should Norberg's acquiescence bar his individual claims, can he serve as an adequate class representative under Court of Chancery Rule 23?

Third, are there genuine issues of material fact in dispute about the merger process and the fairness of the merger consideration?

After reviewing the parties' briefs and hearing oral argument, I conclude defendants' motion for summary judgment should be granted and Norberg's cross motion should be denied because, as a matter of law, Norberg acquiesced in the merger transaction by accepting the \$120 cash-out consideration. Although not argued by the parties in their briefs or at oral argument, I note that Norberg's conduct also fits squarely within the doctrinal parameters of waiver. Therefore, he is precluded from pursuing any litigation individually and can not adequately represent the interests of the purported class of minority shareholders which he now seeks to represent. In light of the above conclusions,

consideration of the fairness of the merger process and price, the adequacy of the disclosures and class certification would be premature.

II. BACKGROUND

A. The Parties

Norberg is a minority shareholder who holds 43 shares of common stock of defendant Security Storage Co. of Washington in an Individual Retirement Account ("IRA"). Security Storage, a Delaware corporation with its principal place of business in Washington, D.C., is principally engaged in the shipping and storage industry. Security Storage has acquired significant real estate holdings and investment properties in Washington D.C. and surrounding areas. In addition, the company operates a United Van Lines franchise.

*2 Defendants Childs F. Burden, I. Townsend Burden, III, John D. Firestone, Peter P. van Roijen and Robert D. van Roijen (collectively the "Acquiring Directors") are members of Security Storage's board of directors and majority shareholders who collectively hold 82 percent of Security Storage's outstanding stock.^{FN1} The remaining members of the Security Storage board of directors are defendants Robert E. Windham, Philip L. Gore, Robert L. Tull, George M. Elsey, Conrad S. Posey and Conrad S. Reid (collectively the "Independent Directors").^{FN2}

^{FN1} Childs F. Burden is also the owner of Security Acquisition, director of Control Laser and partner of the Secor Group. I. Townsend Burden, III is also Director of Control Laser and partner of Secor. John D. Firestone and Peter P. van Roijen are also partners of Secor; and, Robert D. van Roijen, R., is also Chairman of Control Laser and a partner of Secor.

^{FN2} Defendants Gore, Tull, Elsey, Posey, Reid, and Windham, while purportedly not owners of Security Acquisition, are alleged to be interested in the transaction and/or dominated by the Acquiring Directors.

Defendant Security Acquisition Corporation is a

corporate entity formed by the majority shareholders as a vehicle to acquire the remaining shares of Security Storage.

B. Nature of the Proceedings

On March 4, 1993, Norberg filed a purported class action challenging a cash-out merger transaction in which the 82 percent majority shareholder, Security Acquisition, allegedly squeezed-out the remaining 18 percent minority shareholders. On June 24, 1998, Norberg filed a motion for class certification under Court of Chancery Rules 23(a), 23(b)(1) and (3). On February 2, 1999, the defendants filed a motion for summary judgment contemporaneously with a brief in opposition to the class certification. On September 8, 1999, Norberg filed briefs in support of class certification and a cross motion for summary judgment. This is the Court's response to (1) the defendants' motion for summary judgment; (2) Norberg's cross motion for summary judgment; and (3) Norberg's request for class certification.

C. Relevant Facts

While the parties dispute several of the underlying facts, I need only address those facts that are undisputed in order to resolve the issues immediately pertinent.

In the early part of December 1992, the board of directors met to discuss the current financial condition and the future economic potential of Security Storage as an operating enterprise. At that meeting, the directors considered the possibility of a cash-out merger which the Acquiring Directors would orchestrate. In order to determine the viability of this transaction, the directors retained the Berwind Financial Group, Inc., a private investment banking and merchant banking firm, to prepare an appraisal of the company as a going concern. After evaluating and reviewing the appraisal, the Acquiring Directors proposed a cash-out merger in which they, as 82 percent majority shareholders, would form Security Acquisition as an acquisition vehicle to buy out the remaining minority interests and acquire all of Security Storage's outstanding common stock.

On December 21, 1992, the board of directors voted unanimously to approve an Agreement and Plan of Merger through which Security Acquisition would

buy the remaining 18 percent of Security Storage shares at \$120.00 per share without interest. They unanimously agreed that the \$120 cash-out price was fair to Security Storage's shareholders. In reaching their decision, the directors examined a variety of factors including the Berwind appraisal,^{FN3} the financial condition of the company, the historical and projected operating results, the absence of a trading market for the shares, and the results of a "Dutch Auction" ^{FN4} which Security Storage completed in 1991. The auction resulted in the repurchase of 1,600 shares at \$120 per share.

FN3. There is an irrelevant dispute over whether the Acquiring Directors or the board of directors retained Berwind.

FN4. A self-tender offer at \$120 per share that enabled certain shareholders to sell their shares of the company's stock and to simplify the administration of the company by reducing the number of shareholders. Because the "Dutch Auction" did not result in the purchase of a substantial amount of the minority shareholders shares, the board of directors initiated the freeze-out merger described in the February 3, 1993 Notice of Merger sent to shareholders.

*3 Using a discounted cash flow analysis, the Berwind appraisal valued Security Storage as a going concern at \$7,800,000 and concluded that \$120 merger per share constituted (1) a 25 percent premium over the appraised per share value of \$95.89 as of November 1, 1992 and (2) a 45 percent premium over the net book value of \$82.76 per share as of December 31, 1991. On this basis, Berwind concluded that the \$120 would be fair to the minority shareholders.

On January 28, 1993, Security Acquisition, now the majority shareholder, unanimously agreed to approve the merger transaction. The Independent Directors, who were not financially interested in the transaction, and the Acquiring Directors approved the merger transaction. On February 3, 1993, notice of the merger was sent to the minority shareholders informing them that the merger was to become effective February 4, 1993, one day after the notice was mailed, and that each minority share would be converted into \$120, the cash-out price. Along with

the Notice of Merger, minority shareholders received a Letter of Transmittal, a copy of the Agreement and Plan of Merger and the Berwind appraisal. The directors also informed the shareholders of their appraisal rights under 8 Del.C. Section 262 in the event they sought to challenge the fairness of the consideration.

While many of the minority shareholders tendered their shares of stock for the merger consideration, some dissented from the merger and filed an appraisal action in the early part of 1993.^{FN5} One of the dissenting shareholders later agreed to settle his appraisal claim for \$120 per share. This Court approved the settlement and the parties mailed a notice of the settlement to the remaining dissenters on August 24, 1993, giving them 20 days to join in the settlement. Neither Norberg, nor any of the remaining dissenters took any further steps to join the settlement during the 20-day window. In light of this, Security Storage agreed to leave the \$120 settlement offer open beyond the 20-day deadline.

FN5. Affidavit of Raymond E. O'Meara at ¶ 6. O'Meara is the Secretary of Security Storage. The appraisal action was dismissed for lack of prosecution on March 16, 1996.

On March 4, 1993, Norberg filed his Complaint, styled as a class action, challenging the fairness of the transaction and seeking rescission of the merger or in the alternative, rescissory damages resulting from the merger's consummation. Norberg alleges that the defendants squeezed-out the purported class members at an unfair price, in an unfairly timed transaction using an unfair process and without providing the purported class with material information in breach of the defendants' fiduciary duties. Specifically, he alleges the \$120 consideration to be unfair because it fails to account for Security Storage's real estate holdings and the United Van Lines franchise. Norberg also alleges that the merger was unfairly timed to deprive minority shareholders of the benefits from the development of the "Braddock Road" property. This investment property sits on two acres zoned industrial within the Braddock Road Metro Station in Alexandria, Virginia. Although the Braddock Road property is currently leased to the federal government, Norberg alleges that it is "underutilized" and "ripe for redevelopment." Norberg argues that the Berwind

fairness opinion can not be relied upon because Berwind failed to consider the development potential of Security Storage's real estate, failed to account for any residual value and employed a flawed methodology in assessing the fairness of the consideration. Finally, Norberg alleges that the Notice of Merger contained misdisclosures in breach of the defendants' fiduciary duty of disclosure.

*4 On August 24, 1994, approximately 17 months after filing his Complaint alleging unfairness of process and price and the defendants' failure to comply with their duty of disclosure in numerous ways designed to frustrate a rational determination of the value of his shares, Norberg voluntarily instructed his IRA custodian to tender his shares for the \$120 merger price. Norberg now seeks rescission of the merger, rescissory damages and an opportunity to serve as lead plaintiff for a class of minority shareholders who did not tender their shares.

IV. ANALYSIS

A. Summary Judgment

Under Court of Chancery Rule 56, summary judgment will be granted when no genuine issue as to any material fact exists and the moving party is entitled to judgment as a matter of law.^{FN6} The moving party must demonstrate clearly the absence of any genuine issue of material fact and any doubt concerning the existence of such an issue will be resolved against the moving party.^{FN7} The function of the trial judge is to determine whether or not there is any evidence supporting a favorable conclusion to the nonmoving party.^{FN8} The fact that the parties have filed cross-motions for summary judgment does not alter this standard.^{FN9}

FN6. Ch. Ct. R. 56.

FN7. Scureman v. Judge, Del. Ch., 626 A.2d 5 (1992).

FN8. Continental Oil Co. v. Pauley Petro., Inc., Del. Supr., 251 A.2d 824 (1969).

FN9. United Vanguard Fund, Inc. v. TakeCare, Inc., Del. Supr., 693 A.2d 1076, 1079 (1997).

B. Acquiescence

The availability of acquiescence as a defense is as narrowly drawn at this stage of the litigation as it would be at a trial on the merits. Therefore, this issue is appropriate for disposition on summary judgment without additional testimony or discovery.

The availability of this defense is pivotal. If available, as a matter of law, Norberg may be estopped from seeking a *Weinberger*^{FN10} claim and therefore, can not adequately represent the interests of the purported class. If the defense is not available, Norberg may continue to pursue the litigation individually and on behalf of the class of minority shareholders he now seeks to represent. I conclude that Norberg's acceptance of the merger consideration 17 months after filing his Complaint detailing the defendants' alleged inequitable conduct constitutes acquiescence.

FN10. Weinberger v. UOP, Inc., Del. Supr., 457 A.2d 701 (1983).

Defendants allege that Norberg acquiesced in the merger by tendering his shares after the merger had been consummated. They argue that because Norberg dissented from the cash-out merger, filed suit claiming unfairness in the transaction but later tendered his shares and accepted the benefits of the transaction, he can no longer maintain his unfairness claim. Defendants argue that Norberg's only remedy is an appraisal action under 8 Del.C. Section 262, a claim that he has, however, abandoned.

At oral argument, Norberg argued that the defense of acquiescence is unavailable under Court of Chancery Rule 8(c) and the defendants' failure to plead it as a defense in their Answer operates as a waiver. Norberg's tender and acceptance of the \$120 per share merger consideration occurred on August 24, 1994, approximately 17 months after the Complaint challenging the fairness of the consideration paid in the merger. It could hardly have been raised in the original answer, although no request to amend that answer has ever been filed. It is only now, in the briefs and at oral argument, that the defendants assert acquiescence as a defense.

*5 Generally, a party arguing acquiescence as an affirmative defense must state their claim in their answer.^{FN11} However, if evidence were offered at trial to support the defense and objected to on the ground that it was not within the issues asserted in the pleadings, Court of Chancery Rule 15(b) would nevertheless permit me to allow the pleadings to be amended when the "presentation of the merits of the action" will be facilitated.^{FN12} It is within my discretion to allow the pleadings to be amended to reflect any new issues not asserted in the pleadings so long as the responding party is not prejudiced by its admission.^{FN13}

FN11. Ch. Ct. R. 8(c).

FN12. Ch. Ct. R. 15(b) provides in relevant part:

If evidence is objected to at the trial on the ground that it is not within the issues made by the pleadings, the Court may allow the pleadings to be amended and shall do so freely when the presentation of the merits of the action will be subserved thereby and the objecting party fails to satisfy the Court that the admission of such evidence would prejudice the party in maintaining an action or defense upon the merits. The Court may grant a continuance to enable the objecting party to meet such evidence.

FN13. *Id.*

Here, the defendants' conceded at oral argument that they did not plead acquiescence in their Answer because the plaintiff had not yet tendered his shares and made the defense available. I note that the defendants did not amend their answer to include acquiescence as a defense soon after they learned of Norberg's share tender. Nonetheless, Norberg's own actions 17 months after filing the action triggered the applicability of the defense and he can hardly claim prejudice from simply being held accountable for his own actions. Generally, Rule 15(b) permits me discretion to grant a continuance to the objecting party to respond to the newly admitted evidence.^{FN14} But, in the absence of a genuine issue of disputed fact regarding Norberg's acceptance of the merger consideration I do not need to exercise even

this discretion. I consider the pleadings amended to conform to the undisputed evidence.

FN14. See *supra* note 12.

Generally under the doctrine of acquiescence, a shareholder who tenders his shares and accepts the benefits of a transaction may be barred from seeking equitable relief.^{FN15} In order for the defense to operate as a bar, the shareholder must have been adequately informed of all material facts relevant to the transaction.^{FN16} In other words, acquiescence may result in an estoppel precluding the acquiescing shareholder, who accepted the pecuniary benefits of a transaction with knowledge of the alleged inequitable conduct, from challenging the transaction's validity.^{FN17}

FN15. *Bershad v. Curtiss-Wright Corp.*, Del.Supr., 535 A.2d 840, 848 (1987).

FN16. *Id.* at 842; *Papaionanu v. Commissioners of Rehoboth, Del. Ch.*, 186 A.2d 745, 749-50 (1962) (quoting Herman, Commentaries on the Law of Estoppel, at 1194).

FN17. DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 11-3 (1998 & Supp.2000).

For Norberg, the decisive issue becomes whether he was fully informed of the merger process and price defects when he accepted the benefits of the merger transaction.^{FN18} Norberg argues that the Notice failed to inform any of the minority shareholders that acceptance of the merger consideration constituted a waiver of any right other than appraisal.^{FN19} He also argues that he was not fully informed of all material facts because of the alleged "misdisclosures" contained in the Notice. Thus, Norberg contends that the acquiescence defense, even if timely raised, can not bar his action attacking the fairness of the transaction.^{FN20}

FN18. *Bershad*, at 842, 846-847; *Siegman v. Columbia Pictures Entertainment, Inc.*, Del. Ch., C.A. No. 11152, mem. op. at 19,

Hartnett, V.C. (Jan. 12, 1993).

FN19. Norberg relies in part on *Turner v. Bernstein*, Del. Ch., C. A. No. 16190, mem. op. at 21-24 (Feb. 9, 1999) in an attempt to draw a factual analogy. In that case, Vice Chancellor Jacobs held that granting summary judgment in favor of the plaintiff shareholders, who argued that they were not fully informed, would be imprudent given the fact that the Letter of Transmittal and Notice of Merger pointedly told the shareholders that acceptance of the merger consideration would operate as a waiver of their appraisal rights. I find this argument admittedly compelling when there is clear and explicit notice to shareholders advising that acceptance of the merger consideration bars a demand for appraisal. In this case, neither the Letter of Transmittal nor the Notice gave any notice of waiver that Norberg claims should have been given. It did inform shareholders of their appraisal rights. However, *Turner* offers Norberg little help. He suggests that the Letter of Transmittal and Notices should have informed him that acceptance of the merger consideration operates as a waiver of *all rights* in order to operate as a bar to his claims, not merely appraisal rights as discussed in *Turner*. He ignores the fact that he had an action pending for months which asserted *all his rights* and argues that the very consideration he accepted 17 months later was unfair and the product of an unfair process.

FN20. I note that on September 14, 2000, plaintiff's counsel provided the Court a copy of *INCE & Co. v. Silgan Corp.*, Del. Ch., C.A. No. 10941, 1991 WL 17171, Chandler, V.C. (Feb. 7, 1991). In an attached letter, plaintiff's counsel indicated that *INCE & Co.* was submitted for the proposition that a disclosure violation claim should not be dismissed where shareholders are not advised that the defense of acquiescence would be asserted against them in the event they tendered their shares for the merger consideration. Generally, a party can not submit case law decided after the briefing

has been closed as support for its claims, particularly where the case law submitted by plaintiff's counsel predates the events that led to this litigation. After reviewing *INCE & Co.*, I do not agree with plaintiff's counsel's interpretation. In that case, Chancellor Chandler merely refused to dismiss a disclosure claim that the disclosure documents were misleading because they failed to disclose that shareholders who tendered their shares would be barred from pursuing an unfairness claim. Chancellor Chandler's opinion fails to address, as plaintiff's counsel suggests it does, the doctrine of acquiescence as it is applied to a shareholder who tenders his shares for merger consideration after filing a lawsuit detailing with specificity all the reasons why he could not fairly conclude that he had been offered a fair price for his shares.

The record is clear from Norberg's Complaint that he knew all of the arguments suggesting that he had been misled about the value of his shares at the time that he tendered them. It is an undisputed fact that Norberg accepted the benefits of the transaction after declaring in a court pleading that the defendants orchestrated an unfair price through an inequitable process. First, he abandoned his appraisal claim by failing to tender his shares during the extended 20-day window offered by Security Storage. Next, he filed his Complaint, styled as a class action, detailing the nature of the alleged inequitable conduct of the defendants which made it impossible for him to value his shares, more than 17 months before voluntarily instructing his IRA custodian to tender his shares for the \$120 actually offered.

*6 Norberg's Complaint is replete with allegations of false and misleading disclosures concerning the value of Security Storage and the fairness of the consideration. For instance, Norberg alleges that the board of directors failed to disclose to the minority shareholders the most recent values in the real estate appraisals. He alleges that these values were disclosed to Berwind, yet not related to the shareholders. In addition, Norberg alleges that the Notice improperly describes Berwind's conclusions concerning the merger transaction. For example, the Notice fails to note that Berwind did not perform a fair value analysis of Security Storage or that the

appraisal makes no assessment of the value of the company other than on a discounted cash flow basis. The Notice also stated that Berwind considered the "replacement value of fixed assets" when, in fact, the appraisal ignored this value. It also implied that Berwind relied on the most recent appraisals when, as Norberg alleges, Berwind and the board of directors ignored those values as well. Norberg's tender, in the face of his declared knowledge of the inadequacy of the price constitutes acquiescence.

I agree with the defendants' assertion that our Supreme Court's ruling in *Bershad*^{FN21} is controlling with regard to shareholder acquiescence on its own and similar facts.^{FN22} *Bershad*, like this case, involved a minority shareholder challenging a cash-out merger in a pleading styled as a class action.^{FN23} *Bershad* alleged, *inter alia*, that the shareholder vote approving the merger was invalid since the proxy statement omitted material facts.^{FN24} On summary judgment, the Court of Chancery dismissed the claims of *Bershad* and "all stockholders who either voted in favor of the merger or accepted its benefits by tendering their shares for payment under the merger agreement."^{FN25} In other words, *Bershad* forfeited any rights he had to seek rescission of the merger by accepting the merger consideration. This Court found that the proxy statement fully informed the minority shareholders of all material facts regarding the merger.^{FN26} On appeal, the Supreme Court affirmed the Court of Chancery's finding that the minority shareholders were adequately informed of all material information.^{FN27} After determining the shareholder vote was an informed one, the Supreme Court held that when informed shareholder's either vote in favor of the merger or accept the benefits thereof, they are precluded from attacking the fairness of the transaction.^{FN28} Thus, *Bershad* logically could not challenge the fairness of the transaction because after being made aware of all facts material to the merger he tendered his shares and accepted the merger consideration.

^{FN21}*Bershad*, at 840. Defendants also cite *Trounstone v. Remington Rand, Inc.*, Del. Ch., 194 A. 95, 99 (1937); *Frank v. Wilson & Co., Inc.*, Del.Supr., 32 A.2d 277 (1943) for the proposition that when an informed minority shareholder either votes in favor of a merger or accepts the benefits of the transaction, he cannot thereafter attack the

fairness of the transaction. In other words, acquiescence operates as a bar to any later action.

^{FN22} I invite the reader to review Vice Chancellor Hartnett's opinion in *Siegman v. Columbia Pictures Entertainment, Inc.*, Del. Ch., C.A. No. 11152, Hartnett, V.C. (Jan. 15, 1993) to understand the development of the defense of acquiescence under Delaware law. His opinion demonstrates the progression of the defense from *Trounstone* through *Bershad* and succinctly exposes the progressive nature of the defense and the nuances that trigger its use.

^{FN23}*Bershad*, at 841.

^{FN24}*Id.*

^{FN25}*Id.*

^{FN26}*Id.*

^{FN27}*Id.* at 842, 847.

^{FN28}*Id.* at 842, 848. See also *Trounstone* at 99 (stockholder claims barred by acquiescence when shared in the benefits which he later challenged as wrongful).

Norberg was fully informed of all material facts or had, at least according to his Complaint, recognized all of the deficiencies in the information he had been given when he voluntarily instructed his IRA custodian to tender his shares for \$120. Having accepted the amount of consideration offered, he can not challenge the fairness of the transaction by continuing to assert that the very consideration he has accepted does not reflect the shares' real value because of defects in the process that led to the offer he accepted. I recognize that the *Bershad* courts made or affirmed actual findings that no breach of the duty of disclosure occurred and that the shareholders were informed of all facts material to their decision to tender. No such conclusion need be reached here because Norberg tendered after admitting in his Complaint 17 months earlier that he knew the deficiencies in the disclosures, process and price but chose to tender nonetheless.

*7 In the alternative, Norberg argues that the doctrine of acquiescence can not be applicable to an involuntary cash-out merger transaction where the minority interests are squeezed out by the majority shareholder. In this circumstance, Norberg contends, even an informed shareholder surrendering his shares has no other alternative but to accept the merger consideration. However, even if he could not vote against the merger, rather than tendering his shares and accepting the consideration, he could have maintained his appraisal action and/or continued to litigate his fairness claim. Instead, he abandoned his appraisal claim, challenged the fairness of the price and the process and later, despite his declared assessment of the unfairness of the transaction, freely and voluntarily accepted the merger consideration. I conclude that under these circumstances, Norberg's tender constitutes acquiescence.

C. Waiver

The parties chose to focus their contentions on the equitable defense of acquiescence. For those preoccupied with doctrinal pigeonholes, I am persuaded that some discussion of waiver is helpful.

For the doctrine of waiver to apply, the Court must be persuaded that the party intended to voluntarily relinquish a known right.^{FN29} The intent to relinquish is a prerequisite to applying waiver as an equitable defense.^{FN30} Thus, the issue becomes whether the facts unequivocally establish Norberg's intention to relinquish his right to challenge the fairness of the merger.^{FN31} I conclude that they do and so hold for the following reasons.

FN29. *Realty Growth Inv. v. Council of Unit Owners*, Del.Supr., 453 A.2d 450, 456 (1982); *Pepsi-Cola Bottling Co. of Asbury Park v. PepsiCo, Inc.*, Del.Supr., 297 A.2d 28, 32-33 (1972); 28 Am.Jur.2d, Estoppel and Waiver, § 158 (1966).

FN30. 28 Am.Jur.2d, Estoppel and Waiver, § 158 (1966); see also *Realty Growth Inv.*, 453 A.2d at 456 (waiver implies knowledge of all material facts, and intent to waive).

FN31. 28 Am.Jur.2d, Estoppel and Waiver, §

206 (1966); see also *Realty Growth Inv.*, 453 A.2d at 456 (in the context of waiver "[t]he facts relied upon for proof must be unequivocal in character").

The record is clear that Norberg relinquished his right to challenge the fairness of the merger transaction when he voluntarily instructed his IRA custodian to tender his shares for the \$120 cash-out value. It is an undisputed fact that Norberg accepted the benefits of the transaction after declaring in a court pleading that the defendants orchestrated an unfair price through an inequitable process. First, he abandoned his appraisal claim by failing to tender his shares during the extended 20-day window offered by Security Storage. Next, he filed his Complaint, styled as a class action, detailing the nature of the alleged inequitable conduct of the defendants more than 17 months before voluntarily instructing his IRA custodian to tender his shares for the \$120 consideration. Rather than offering some caveat to his tender that he intended to pursue his litigation further, Norberg freely and voluntarily accepted the merger consideration he so fiercely attacked in his Complaint.

It is difficult to see how Norberg's conduct under these circumstances does not imply an intent to relinquish his right to challenge the fairness of the merger transaction. Generally, "an implied waiver can be established by acts and conduct from which an intention to waive may reasonably be inferred."^{FN32} In other words, conduct that impliedly expresses an intent to relinquish a known right can be designated as waiver. In my view, Norberg, by his conduct, intended to relinquish any rights he had as a minority shareholder when he voluntarily instructed his IRA custodian to tender his shares. Norberg's act fits squarely within the parameters of the equitable defense of waiver and establishes his intent to relinquish any right he had to continue to challenge the litigation he started nearly 17 months earlier.

FN32. 28 Am.Jur.2d, Estoppel and Waiver, § 209 (1966)

D. The Remaining Claims

*8 While Norberg's Complaint is replete with allegations of false and misleading disclosures concerning the value of Security Storage and the

fairness of the consideration, this opinion need not address nor rule on the adequacy of these disclosures in light of the fact that both waiver and acquiescence bar Norberg's individual claim and make him an inadequate class representative.

For the reasons articulated above, defendants' motion for summary judgment is granted.

Having decided that defendants are entitled to summary judgment because Norberg's claims are barred by his acquiescence and/or waiver there, is no need to address Norberg's cross motion for summary judgment asking me to assess the defendants' conduct in the merger transaction under the entire fairness standard articulated in *Weinberger*. Since Norberg's acceptance of the merger consideration bars his claims, and that, in turn makes him atypical of the class he seeks to certify and represent, there is no need to determine class certification in the absence of an adequate class representative. An appropriate Order is attached.

ORDER

For the reasons set forth in this Court's opinion entered in this case on September 19, 2000, it is ORDERED that:

1. Defendants' motion for summary judgment is *granted*;
2. Norberg's cross motion for summary judgment is *denied*; and,
3. A decision on class certification is reserved pending an application by an adequate class representative.
4. The action will remain active for thirty days in order to allow substitution of a suitable plaintiff for the remaining claims.

Del.Ch.,2000.
Norberg v. Security Storage Co. of Washington
Not Reported in A.2d, 2000 WL 1375868 (Del.Ch.),
27 Del. J. Corp. L. 378

END OF DOCUMENT

STATE OF SOUTH CAROLINA	)	
	)	IN THE COURT OF COMMON PLEAS
COUNTY OF GREENVILLE	)	
Brian P. Menezes,	)	C.A. No. 2008-CP-23-2701
	)	
Plaintiff,	)	
	)	
v.	)	
	)	
WL Ross & Co. LLC, Wilbur L. Ross,	)	<u>Plaintiff's Memorandum</u>
Jr., Michael J. Gibbons, David H. Storper,	)	<u>In Opposition to Defendants'</u>
David L. Wax, Joseph L. Gorga, Stephen	)	<u>Motion To Dismiss</u>
B. Duerk, WLR Recovery Fund II, L.P.,	)	
WLR Recovery Fund III, L.P, WLR	)	
Recovery Associates II LLC, and WLR	)	
Recovery Associates III LLC,	)	
	)	
Defendants.	)	

The issue here is when a claim for damages for breach of fiduciary duty in connection with a merger of two corporations "accrues."

Does it accrue when the decision to merge is made and announced?

Or does it accrue when the merger actually takes place?

This is pertinent because the Release at issue falls between those dates.

Delaware law is very clear that the claim does not accrue until the merger takes place.

Indeed, how could it since there are no damages until the merger takes place?

Accordingly, the Release is not relevant, and Defendants' Motion to Dismiss should be denied.

I. Factual Background

A. The Release

The circumstances behind the Release are not really relevant given its plain language. Plaintiff feels compelled, however, to address the implication in defendants' Memorandum that the Release had anything to do with the Merger. It did not.

The Release relates solely to litigation that plaintiff commenced in 2006 (the "Employment Lawsuit"). As stated in the complaint in that action (C.A. No. 2006-CP-23-4236), plaintiff was employed by Safety Components International, Inc. ("SCI") as CFO and then Interim CEO from 1999 through June 2006 when he was terminated without cause. At the time of his termination, he had general knowledge that defendants intended to merge SCI and FITG (former International Textile Group, Inc.) together.

Under his employment contract, he was entitled to a "change of control" bonus for any merger that occurred within ten years after his termination without cause. He believed, therefore, that he was entitled to the bonus in connection with the contemplated merger.

SCI disputed his right to the change of control bonus and refused even to pay severance that it did not dispute unless and until he waived his right to the change of control bonus. Accordingly, plaintiff brought suit for breach of contract and failure to pay wages. The suit also included a claim for declaratory judgment since the proposed merger had not then occurred and the "change of control" bonus was not then due.

The Employment Lawsuit was resolved by compromise (obviously). The original release proposed by SCI provided that plaintiff was releasing "any claims based upon or as an owner of any stock or interest in any of the Released Parties." At plaintiff's request, SCI agreed to add the language underlined below to clarify that plaintiff was only releasing shareholder claims that had arisen prior to the execution of the settlement agreement:

Released Parties, specifically including but not limited to the Employment Agreement; (6) any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement; (7) any claims or causes of action which Plaintiff

(Release, Sec. 7(6), emphasis added -- a copy of the Release is attached to the Duerk affidavit which is Exhibit 1 to Defendant's Memorandum.)

The obvious point on plaintiff's part was to preserve shareholder claims regarding the upcoming Merger in the event it was unfair.

The Release with this clarifying language was executed by plaintiff on September 28, 2006.

B. The Merger

The SCI Board approved the Merger of SCI into FITG on August 29, 2006. On August 30, 2006, the Merger was announced. On September 1, 2006, SCI and FITG filed a preliminary joint proxy statement with details of the Merger. On September 22, 2006, SCI and FITG filed a joint definitive joint proxy statement regarding the merger and began mailing it to all SCI shareholders and FITG shareholders.

The September 22 Proxy Statement was hundreds of pages long.¹ The Merger Agreement was included and it alone was 51 single-spaced pages long. (Proxy, Annex A.) As would be expected in a transaction of this magnitude, there were many many contingencies – the “conditions precedent” section alone was several single-spaced pages long. (Proxy, Annex A, at A34-A36.) The “summary” of the conditions precedent in the main body of the Proxy took more than two pages:

Conditions Precedent

Conditions to Each Party's Obligation To Effect the Merger

The respective obligation of each party to effect the merger is subject to the satisfaction or waiver on or prior to the Closing Date of the following conditions:

- *ITG stockholder approval of the merger agreement and the merger shall have been obtained;*
- *SCI stockholder approval to adoption of the Amended and Restated Certificate of Incorporation of SCI shall have been obtained;*
- *any waiting period (and any extension thereof) applicable to the merger under the HSR Act shall have been terminated or shall have expired;*
- *no Restraints (as defined in the merger agreement) shall be in effect, and there shall not be pending any suit, action, proceeding or investigation by any governmental entity (i) seeking to prevent or delay consummation of the merger or any material part of the transactions, or that is reasonably likely to require any material divestiture of the business of ITG or SCI or (ii) which otherwise is reasonably likely to have a material adverse effect on ITG or SCI, as applicable; provided, however, that each of the parties shall have used its reasonable efforts to prevent the entry of any such Restraints and to appeal as promptly as possible any such Restraints that may be entered;*
- *the registration statement on Form S-4 shall have become effective under the Securities Act and shall not be the subject of any stop order or proceedings seeking a stop order and, if the issuance of SCI common stock in connection with the merger is subject to the state securities or “blue sky” laws of any state, shall not be subject to a stop order of any state securities commissioner;*
- *the parties shall have obtained any and all permits, authorizations, consents, waivers, clearances or approvals required under contracts or agreements or otherwise required for the lawful consummation of the merger and the consummation of the transactions contemplated by the merger agreement, and all such permits, authorizations, consents, waivers, clearances or approvals shall be in full force and effect, in each case, with such exceptions as would not,*

¹ The Court can obviously take judicial notice of documents filed with the Securities and Exchange Commission (*Lovelace v. Software Spectrum, Inc.*, 78 F.3d 1015, 1017-18 (5th Cir. 1996); *Kramer v. Time Warner, Inc.*, 937 F.2d 767, 774 (2nd Cir. 1991)), as defendants have asserted. (Def. Mem. n.4.)

individually or in the aggregate, be reasonably likely to have a material adverse effect on ITG or SCI, as applicable; and

- appraisal rights pursuant to Section 262 of the DGCL shall have not have been exercised in connection with the merger in respect of more than 365,850 shares of ITG common stock.

Conditions to Obligations of SCI and SCI Merger Sub

The obligations of SCI and SCI Merger Sub to effect the merger are further subject to satisfaction or waiver of the following conditions:

- the representations and warranties of ITG set forth in the merger agreement (without giving effect to any qualifications contained therein as to materiality or material adverse effect) shall be true and correct as of the Closing Date as if made at and as of such time, with only such exceptions to be true and correct as would not, individually or in the aggregate, reasonably be expected to result in a material adverse effect with respect to ITG, and ITG shall have delivered to SCI a certificate to such effect signed on behalf of ITG by an executive officer of ITG and dated as of the Closing Date;
- ITG shall have performed in all material respects all obligations required to be performed by it under the merger agreement at or prior to the Closing Date, and ITG shall have delivered to SCI a certificate to such effect signed on behalf of ITG by an executive officer of ITG and dated as of the Closing Date;
- the opinion of RSM EquiCo Capital Markets LLC, financial advisor to the SCI Special Committee, shall not have been withdrawn or changed in a manner adverse to SCI;
- SCI shall have received an affidavit of ITG certifying that it is not a United States real property holding corporation under Section 897 of the Code;
- there shall have been no changes, other than changes contemplated by the merger agreement, in the business, operations, condition (financial or otherwise), assets or liabilities of ITG and its subsidiaries (regardless of whether such events or changes are inconsistent with the representations and warranties of ITG set forth in the merger agreement) that, individually or in the aggregate, has had or would reasonably be expected to have a material adverse effect with respect to ITG; and
- the Escrow Agreement shall have been duly executed by the parties thereto.

Conditions to Obligations of ITG

The obligation of ITG to effect the merger is further subject to satisfaction or waiver of the following conditions:

- the representations and warranties of SCI and SCI Merger Sub set forth in the merger agreement (without giving effect to any qualifications contained therein as to materiality or material adverse effect) shall be true and correct as of the Closing Date as if made at and as of such date, with only such exceptions to be true and correct as would not, individually or in the aggregate, reasonably be expected to result in a material adverse effect with respect to SCI, and SCI shall have delivered to ITG a certificate to such effect signed on behalf of SCI by an executive officer of SCI and dated as of the Closing Date;
- SCI and SCI Merger Sub shall have performed in all material respects all obligations required to be performed by them under the merger agreement at or

prior to the Closing Date, and SCI shall have delivered to ITG a certificate to such effect signed on behalf of SCI by an executive officer of SCI and dated as of the Closing Date;

- *the opinion of SunTrust Robinson Humphrey to the ITG Special Committee shall not have been withdrawn or changed in a manner adverse to ITG;*
- *the SCI Charter Amendment shall have been duly filed with the Delaware Secretary of State and shall be in full force and effect;*
- *there shall have been no changes, other than changes contemplated by the merger agreement, in the business, operations, condition (financial or otherwise), assets or liabilities of SCI and its Subsidiaries (regardless of whether such events or changes are inconsistent with the representations and warranties of SCI set forth in the merger agreement) that, individually or in the aggregate, has had or would reasonably be expected to have a Material Adverse Effect with respect to SCI; and*
- *the Escrow Agreement shall have been duly executed by the parties thereto.*

(Proxy, at 83-84,² emphasis added.)

Apart from the conditions precedent, the transaction was also subject to multiple explicit termination events, any one of which could have killed it. Again, quoting the summary in the Proxy:

Termination

The merger agreement may be terminated at any time prior to the Effective Time, whether before or after ITG Stockholder Approval or SCI Stockholder Approval:

- *by mutual written consent of SCI and ITG;*
- *by either SCI or ITG;*
- *if the merger shall not have been consummated by March 31, 2007;*
- *if SCI stockholder approval of the adoption of the Amended and Restated Certificate of Incorporation of SCI or ITG stockholder approval of the merger agreement and the merger, has not been obtained by March 31, 2007; or*
- *if any Restraint shall be in effect and shall have become final and nonappealable; provided that the party seeking to terminate the merger agreement shall have used reasonable best efforts to prevent the entry of and to remove such Restraint;*
- *by SCI, if ITG shall have breached or failed to perform in any material respect any of its representations, warranties, covenants or other agreements contained in the merger agreement, which breach or failure to perform (A) would give rise to the failure of a condition precedent relating to the accuracy of ITG's representations and warranties or performance of covenants described under "Conditions to Obligations of SCI and SCI Merger Sub" above, and (B) has not been or is incapable of being cured by ITG within 30 calendar days after receipt of written notice from SCI; or*

² The reference is to the page numbers embedded in the Proxy and not to the numbers at the bottom of each page which may be different.

- *by ITG, if SCI shall have breached or failed to perform in any material respect any of its representations, warranties, covenants or other agreements contained in the merger agreement, which breach or failure to perform (A) would give rise to the failure of a condition precedent relating to the accuracy of SCI's representations and warranties or performance of covenants described under "Conditions to Obligations of ITG" above, and (B) has not been or is incapable of being cured by SCI within 30 calendar days after receipt of written notice from ITG.*

(Id.)

As shown above, the Merger was subject to numerous conditions. For example, approval had to be obtained from FITG shareholders. There had to be no material adverse changes in either company. The Fairness Opinions regarding the merger consideration had to remain in place and not be withdrawn. The Escrow Agreement through which the Merger would be accomplished had to have been duly executed. SCI shareholders had to approve at their annual meeting certain amendments to its certificate of incorporation.

The Merger closed on October 20, 2006.

The conditions precedent to the Merger were obviously not satisfied until the closing which was well after plaintiff signed the Release on September 28, 2006. Indeed, the SCI annual shareholder meeting when the required amendments to its certificate of incorporation were adopted did not even occur until October 20, 2006. (Proxy at 5.) That was also the first day upon which the escrow agents were authorized to execute the Escrow Agreement. (Proxy, A-38 & A-41.) And until those conditions were satisfied, the Merger could not go forward. In other words, there was no Merger until the "closing" on October 20, 2006. Indeed, that is the point of a "closing" – it is when a transaction "closes."

II. Discussion

A. The Release Is Irrelevant Since It Pre-Dates The Accrual of Plaintiff's Claim for Damages for Breach of Fiduciary Duty.

As noted above, the relevant question here is when a claim for damages for breach of fiduciary duty in connection with a merger of two corporations "accrues." This follows directly from the statute of limitations at issue, 10 Delaware Code § 8106, which reads:

§ 8106. Actions subject to 3-year limitation

No action to recover damages for trespass, no action to regain possession of personal chattels, no action to recover damages for the detention of personal chattels, no action to recover a debt not evidenced by a record or by an instrument under seal, no action based on a detailed statement of the mutual demands in the nature of debit and credit between parties arising out of contractual or fiduciary relations, no action based on a promise, no action based on a statute, and no action to recover damages caused by an injury unaccompanied with force or resulting indirectly from the act of the defendant shall be brought after the expiration of 3 years from the accruing of the cause of such action; subject, however, to the provisions of §§ 8108-8110, 8119 and 8127 of this title.

(Emphasis added.)

It would seem patently obvious that a claim for "damages" cannot "accrue" until there are in fact "damages." And it would seem further patently obvious that there can be no damages regarding a merger between two corporations until the merger actually takes place.

This is indeed the law of Delaware (and the rest of the United States) as shown by every case to address the issue (none of which were addressed or even mentioned in defendants' Memorandum).

The only appellate case on point is Baron v. Allied Artists Pictures Corporation, 717 F.2d 105 (3d Cir. 1983) [COPY ATTACHED]. The issue there was whether under Delaware law a shareholder's action for damages based on false and misleading materials effecting a merger accrued when the shareholder had knowledge of the falsity or when the merger was

consummated. The trial court had held that the cause of action accrued when the shareholder had knowledge of the falsity (which was prior to consummation of the merger) and that, since this was more than three years before he had brought the lawsuit, the lawsuit was time-barred.

The Third Circuit reversed. The court of appeals noted that the action was in the nature of a claim for breach of fiduciary duty. Id. at 108. The court then quoted the general rule that "a cause of action for the recovery of damages accrues only when it could be prosecuted to a successful conclusion." Id. (citing United States v. Wurtz, 303 U.S. 414, 418 (1938)). The court observed that Delaware follows this same rule: "'A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of the injury.'" Id. (quoting Nardo v. Guido DeAscanis & Sons, Inc., 254 A.2d 254, 256 (Del. Super. Ct. 1969); citing numerous other cases).

The Third Circuit pointed out that if the plaintiff had filed his complaint seeking monetary damages prior to the merger it "would have been properly dismissed under Fed. R. Civ. Pro. 12(b)(6) for failure to state a claim upon which money damages could be awarded." Id. 109. Finally, the court held that: "Until the plaintiff can allege facts which would survive such a motion, his cause of action for damages, personal or derivative, has not accrued. Until it has accrued the statute of limitations does not come into operation." Id. Accordingly, the claim did not accrue until consummation of the merger and, therefore, was not time-barred.

Also directly on point is Dofflemeyer v. W.F. Hall Printing Company, 558 F. Supp. 372 (D.Del. 1983) [COPY ATTACHED], which defendants' Memorandum also failed to address. The plaintiffs there, like plaintiff here, sought damages for violations of fiduciary duty in connection with a merger. The defendants moved to dismiss on the basis on the three year

statute of limitations. Like the defendants here, they argued that the claims accrued when the board approved the merger agreement and not when the merger was consummated.

The court held that the claim for damages for breach of fiduciary duty under Delaware law did not accrue until the consummation of the merger. As the court noted, "It is a basic principle of limitations law that a cause of action does not accrue before the right to institute suit arises." *Id.* at 379 (citing C.J.S., Limitations of Actions, sec. 109.) The court then observed that "[t]he plaintiffs could not have sued for damages until the merger was actually accomplished -- until that time, they had suffered no injury by the defendants' acts." *Id.* Since they had not suffered any injury until the merger was consummated, their claim for damages for breach of fiduciary duty did not accrue until then.

The third case directly on point (also ignored by defendants' Memorandum) is Kaufman v. Albin, 447 A.2d 761 (Del.Ch. 1982) [COPY ATTACHED]. Kaufman also involved whether a claim breach of fiduciary duty ("corporate waste" in that context) had accrued when the merger there was approved by the board or when the merger was consummated. The point was important because of the effective date of a statute by which plaintiff had accomplished service. If the claim arose when the merger had been approved, it predated that statute and service was ineffective (and impossible). If it arose after the effective date of the statute, service was effective.

The court began its analysis with a look at general principles as outlined in C.J.S. and Am.Jur. According to C.J.S., "Where a party's right depends on the happening of an event in the future, the cause of action accrues, and the statute of limitations begins to run, only at the time when the event happens." *Id.* 763 (quoting C.J.S., Limitation of Actions, sec. 110 (p.15) (1948)). According to Am.Jur., "If a right of action depends upon some contingency or a condition

precedent, the cause of action does not accrue and the statute of limitations does not begin to run until that contingency occurs or the conditions precedent is complied with.” Id. (quoting Am. Jur., Limitations of Actions, sec. 127 (pp.3 & 6) (1979)).

Kaufman then looked at the leading treatise on Delaware corporate law, Folk’s The Delaware General Corporation Law (1967, page 487), which states: “the circumstances of the case will determine whether the transaction is executed or continuing. If the action complained of requires shareholder approval, the transaction is not complete until the shareholders have approved of it.” 447 A.2d at 764. Finally, it referred to Lavine v. Gulf Coast Leaseholds, 122 A.2d 550 (Del.Ch. 1956), which held that “where exchanges of stock are contingent upon shareholder approval, the transaction is not completed until the shareholder vote takes place.”

Based on these principles, the court in Kaufman held that the transaction there had “commenced with the adoption of the two resolutions on August 22, 1977 [by the board authorizing the merger], but was not consummated until October 2, 1977 [when sufficient shares were tendered and the merger was successfully concluded].” 447 A.2d at 764 (emphasis added). Accordingly, it had accrued after the effective date of the statute regarding service of process, and service was therefore effective.

Here, as in Kaufman, the merger was subject to numerous conditions precedent (see pages 4-6 above). For example, as already noted, approval had to be obtained from FITG shareholders. There had to be no material adverse changes in either company. The Fairness Opinions regarding the merger consideration had to remain in place and not be withdrawn. The Escrow Agreement through which the Merger would be accomplished had to have been duly executed. And SCI shareholders had to approve at their annual meeting certain amendments to its certificate of incorporation.

These conditions were not satisfied until the closing on October 20, 2006, several weeks after plaintiff signed the Release. For two quick and clear examples, that was the date of the SCI annual shareholder meeting when the required amendments to its certificate of incorporation were adopted. (Proxy at 5.) That was also the first day upon which the escrow agents were authorized to execute the Escrow Agreement. (See Proxy, A-38 & A-41.) And until those conditions were satisfied and the Merger closed, the Merger was subject to cancellation or termination.

Since the conditions precedent were not satisfied until the closing of the Merger, under Kaufman, plaintiff's claim for damages for breach of fiduciary duty regarding the merger did not accrue until that point in time.

Further, since plaintiff had no damages until the consummation of the merger on October 20, 2006, under Baron and Dofflemeyer, his claim for damages for breach of fiduciary duty did not accrue until that day. Indeed, it is, frankly, nonsensical for defendants to suggest that the claim accrued before then since any claim for damages he might have brought prior to the merger would have been subject to dismissal for failure to state a claim. (See Baron, *supra*, 717 F.2d at 109.)

B. Defendants' Memorandum Mis-States Delaware Law.

Defendants Memorandum states that "[w]here, as here, a shareholder's lawsuit arises from the terms of a merger agreement, the claim arises or accrues when the board passes the 'resolution approving the merger terms' the plaintiff feels are unfair." (Def. Mem. At 12). As support for this proposition, defendants cite Brown v. Automated Marketing Systems, Inc., 1982 WL 8782 (Del.Ch. 1982), and In re Beatrice Companies, Inc. Litigation, 522 A.2d 865 (Del. Ch. 1987).

Neither of these cases deals with the issue presented here. As the court in Dofflemeyer explained in response to a similar argument from the defendant there:

Brown is . . . inapplicable. In that case, the Court of Chancery held that a plaintiff who purchased shares after reading a press release indicating that the board of directors had approved a plan of merger did not have standing to challenge the merger when it was carried out according to the plan. The holding of that case involved a determination of the times when a plaintiff must own stock in a corporation in order to have standing to challenge a merger and is not pertinent to when, if standing had existed, the plaintiff could have sued for damages.

538 F. Supp. at 379 (emphasis added).

In other words, the issue in Brown and in Beatrice was whether the plaintiffs had "standing" to attempt to block mergers when they had not purchased their stock until after those mergers had been announced. The courts found that they did not have standing based on the policy of preventing the "evil of purchasing stock in order to maintain a derivative action designed to attack a transaction which occurred prior to the purchase of the stock." Brown, 1982 WL 8782 at *2. Those cases had nothing to do with the question at issue here, namely, as Dofflemeyer put it, "when, if standing had existed, the plaintiff could have sued for damages." 538 F. Supp. at 379.

Brown and Beatrice are also irrelevant because they involved requests for injunctive relief regarding proposed mergers. Since the mergers had not taken place, there were no damages. As explained by the Third Circuit in Baron (discussed above), the point of such litigation is to prevent damages.³ Since there were no damages, there could not possibly have

³ The court in Baron discussed at some length the United States Supreme Court opinion in J.I. Case Co. v. Borak, 377 U.S. 426 (1964), where the Court recognized a derivative cause of action for damages which accrued as a result of a merger. As the court in Baron noted, had the plaintiff in Borak or the plaintiff in Baron succeeded in obtaining injunctions to prevent the mergers, there would have been no damages. See 717 F.2d 105, 107.

been a claim for damages for breach of fiduciary duty, and the issue of when such a claim accrues was not presented.⁴

Omnicare, Inc. v. NCS Healthcare, Inc., 809 A.2d 1163 (Del.Ch. 2002), is irrelevant for the same reasons as Brown and Beatrice. It involved a proposed merger and the issue presented was whether the plaintiff had standing since it had purchased its stock after the announcement of the merger at issue. Id. at 1169. Contrary to the implication of defendants' Memorandum (at 13), the case in no way involved the issue of when a claim for damages for breach of fiduciary duty accrues.

In re SunGard Data Sys., Inc. S'Holder Litig., 2005 WL 1653975 (Del.Ch. 2005), merely involved the question of whether the court would allow expedited discovery and an early hearing regarding the fairness of a proposed merger. The court was prepared to do so because the "optimal time" to bring the claim was before the deal closed. Id. at *2. The court said nothing about when a claim for damages would accrue, or, for that matter, when any claim would accrue.

Kahn v. Seaboard Corp., 625 A.2d 269 (Del.Ch. 1993), In re Coca-Cola Enters., Inc., 2007 WL 3122370 (Del.Ch. 2007), and In re Marvel Entm't Group, Inc., 273 B.R. 58 (D.Del. 2002), are even less relevant since they did not involve mergers. They merely involved contracts that had no conditions precedent.

Accordingly, none of the cases cited by defendants even goes to the issue of when a claim for damages for breach of fiduciary duty regarding a merger accrues. As noted above, the

⁴ To the extent the Court may find it pertinent, it should be pointed out that the Brown decision was an unpublished decision and subject to citation warnings. Further, it preceded the decision of the Delaware Court of Chancery in Kaufman (discussed above) which was published and explicitly held that a claim for damages for breach of fiduciary duty regarding a merger between two corporations did not accrue until the consummation of the merger. The unpublished decision in Brown was dated March 22, 1982; the published decision in Kaufman was dated May 11, 1982.

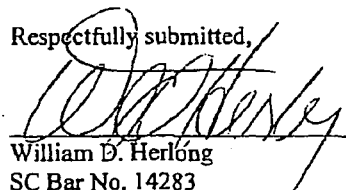
only cases to address that point hold that under Delaware law such a claim accrues when the merger is consummated.

CONCLUSION

Delaware law is clear. An action for damages for breach of fiduciary duty regarding a merger between two corporations accrues when the merger is consummated. This is the only common sense and logical result. And it is the holding of every case to address the issue: Baron v. Allied Artists Pictures Corporation, 717 F.2d 105 (3d Cir. 1983); Dofflemyer v. W.F. Hall Printing Company, 558 F. Supp. 372 (D. Del. 1983); and Kaufman v. Albin, 447 A.2d 761 (Del.Ch. 1982). Defendants have produced no authority to the contrary; the cases they have cited are inapposite.

Accordingly, since under Delaware law plaintiff's claim did not accrue until after the execution of the Release, and since it was therefore expressly excluded from the scope of the Release, defendants' Motion to Dismiss should be denied.

Respectfully submitted,



William D. Herlong
SC Bar No. 14283
ANDERSON & HERLONG, LLC
111 E. North Street [Zip 29601]
P.O. Box 2105
Greenville, SC 29602-2105
Tel. (864) 255-9255
Fax (864) 752-0820
william@ahlf.us

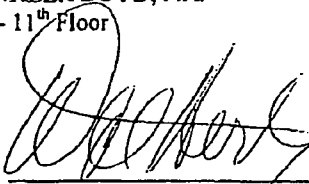
Attorneys for Brian Menezes

July 31, 2008.

CERTIFICATE OF SERVICE

I hereby certify that I have this 31st day of July 2008 served a copy of the foregoing memorandum upon counsel for defendants by hand at the following address:

II. Sam Mabry, III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square – 11th Floor
75 Beattie Place
Greenville, SC 29601



William D. Herlong

fact in the Middle District of Pennsylvania between December 25, 1982, the effective date of the model rule, and August 1, 1983, the effective date of the new bankruptcy rules, see *White Motor Corp. v. Citibank, N.A.*, 704 F.2d 254 (6th Cir.1983), we hold today that subsequent to August 1, 1983, any local rule governing procedure, as distinguished from jurisdiction, in bankruptcy cases must yield to the bankruptcy rules duly promulgated under the Supreme Court's statutory authority. 28 U.S.C. § 2075. Therefore, to the extent that the model rule and the new bankruptcy rules provide for differing standards of appellate review, the latter must prevail.

IV.

The judgment of the district court will be vacated and the cause remanded for proceedings consistent with the foregoing.



John G. BARON, on behalf of himself and derivatively on behalf of Allied Artists Pictures Corporation, Appellant,

v.

ALLIED ARTISTS PICTURES CORPORATION, Kalvex, Inc., PSP, Inc., Allied Artists Industries, Inc., Price Waterhouse & Co., Emanuel Wolf, Robert Sisk, Jack Sattinger, Peter Strauss, Carl Prager, Herbert Blumenthal, Robert Sabel, William Lurie, Jay Feldman, Joseph Gruenberg, Andrew Jaeger, Stuart Marks, Robert Ingis, and Abraham Reback.

No. 82-1720.

United States Court of Appeals,
Third Circuit.

Argued June 1, 1983.

Decided Sept. 19, 1983.

Shareholder appealed from an order of the United States District Court for the

District of Delaware, James L. Latchum, Chief Judge, which granted summary judgment dismissing his complaint for damages based on use of alleged false and misleading proxy solicitation materials in effecting a merger. The Court of Appeals, Gibbons, Circuit Judge, held that under Delaware law, a shareholder's action for damages based on use of alleged false and misleading proxy solicitation materials in effecting a merger accrued not when shareholder had knowledge of the alleged deficiencies in the materials but when the damages occurred by the consummation of the merger; while shareholder's knowledge of the deficiencies in the materials might have entitled him to injunctive relief, a complaint seeking money damages would have been premature at that time.

Reversed and remanded.

1. Limitation of Actions ⇐43

Generally, a cause of action for recovery of damages accrues only when it could be prosecuted to a successful conclusion.

2. Federal Courts ⇐424

With respect to federal law causes of action, question of which state statute of limitations is applicable is a question of federal law; furthermore, federal standards determine when concealment tolls running of state statute of limitations otherwise applicable; moreover, question of when a cause of action is so complete that it may be enforced by suit and thus has accrued is a federal question.

3. Limitation of Actions ⇐100(6)

Under Delaware law, a shareholder's action for damages based on use of alleged false and misleading proxy solicitation materials in effecting a merger accrued not when shareholder had knowledge of the alleged deficiencies in the materials but when the damages occurred by the consummation of the merger; while shareholder's knowledge of the deficiencies in the materials might have entitled him to injunctive relief, a

complaint seeking money damages would have been premature at that time. 10 Del.C. § 8106; Securities Exchange Act of 1934, § 14, 15 U.S.C.A. § 78n.

John C. Phillips, Jr., Wilmington, Del., David M. Olasov (argued), Edward & Angell, New York City, for appellant; Michael R. Newman of Miller & Daar, Beverly Hills, Cal., of counsel.

Edmund N. Carpenter, II, William J. Wade, Richards, Layton & Finger, Wilmington, Del., for Price Waterhouse; Bartlett H. McGuire (argued), Paul W. Bartel, II, Davis, Polk & Wardwell, New York City, of counsel.

Stephen P. Lamb (argued), Skadden, Arps, Slate, Meagher & Flom, Wilmington, Del., for Robert J. Sisk; Jeffrey Glekel, Dana H. Freyer, Skadden, Arps, Slate, Meagher & Flom, New York City, of counsel.

Dannenberg, Hazen & Lake, New York City, for William Lurie; Lee Hazen, New York City, of counsel.

Before GIBBONS and BECKER, Circuit Judges, and WEBER, District Judge.*

OPINION OF THE COURT

GIBBONS, Circuit Judge.

John G. Baron, a stockholder in Allied Artists Pictures Corporation (Allied Pictures) appeals from a summary judgment dismissing his complaint as time barred.¹ The complaint is brought on his own behalf and derivatively on behalf of Allied Pictures against Allied Artists Industries (Allied Industries), Price Waterhouse & Co.,

* Hon. Gerald J. Weber, United States District Judge for the Western District of Pennsylvania, sitting by designation.

1. The order granting summary judgment was entered in favor of Price Waterhouse & Co. Later a stipulation was filed making it applicable to each of the defendants who were served. A stipulation of dismissal was filed as to one defendant who was not served. Thus we have appellate jurisdiction under 28 U.S.C. § 1291 (1976).

2. Although the complaint was filed on January 19, 1979 it was not served until almost a year

and a number of individual defendants. It seeks money damages and declaratory relief with respect to a merger between Allied Pictures and Allied Industries which consummated on January 20, 1976. Proxy solicitations were made for the merger pursuant to a Proxy Statement and Prospectus dated November 24, 1975, and the complaint alleges that this document was false and misleading. Baron's complaint was filed in the district court on January 19, 1979.² That court held that it is time barred by virtue of Del.Code Ann. Tit. 10, § 8106 (1974). We reverse.

I.

The proxy solicitation materials on which Baron relies as false and misleading were, as noted above, issued on November 24, 1975. It is undisputed that at least by December 17, 1975 Baron was aware of the deficiencies in those statements upon which he relies, for on that date he filed in the Delaware Chancery Court an action seeking to enjoin the merger.³ The parties agree that no federal statute of limitations applies, and that the appropriate state statute to borrow is Del.Code Ann. Tit. 10, § 8106, which provides:

No action to recover damages for trespass, no action to regain possession of personal chattels, no action to recover damages for the detention of personal chattels, no action to recover a debt not evidenced by a record or by an instrument under seal, no action based on a detailed statement of the mutual demands in the nature of debit and credit between parties arising out of contractual or fiduciary relations, no action based on

later. A motion to dismiss for failure to prosecute with due diligence was made by Price Waterhouse & Co. but was not passed upon by the district court.

3. That court lacked jurisdiction to grant relief for a violation of section 14(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78n(a) (1976), because section 27 of that Act vests exclusive jurisdiction in the United States District Courts. 15 U.S.C. § 78aa (1976).

a promise, no action based on a statute, and no action to recover damages caused by an injury unaccompanied with force or resulting indirectly from the act of the defendant shall be brought after the expiration of 3 years from the accruing of the cause of such action;

We are called upon in this appeal to determine when the cause of action alleged in Baron's complaint accrued. If, as the defendants contend, it accrued no later than December 17, 1975, when Baron had knowledge of the alleged deficiencies in the proxy solicitation materials, the three-year limitations period expired on December 17, 1978. The district court so held, reasoning that the statute of limitations on Baron's federal law cause of action commenced running as soon as he had knowledge of the defendants' conduct, violative of section 14(a), of which he complains. Baron urges, however, that the cause of action for damages which he pursues both on his own behalf and derivatively did not accrue until such time as he could first have maintained a damage action to a successful conclusion. That, he urges, was when the damages occurred by the consummation of the merger on January 20, 1976. Since the complaint was filed within three years of that date, under Baron's theory it was timely.

To put the respective positions of Baron and the defendants in context, it is necessary to review briefly the seminal case of *J.I. Case Co. v. Borak*, 377 U.S. 425, 84 S.Ct. 1555, 12 L.Ed.2d 423 (1964). That case started with the filing of a two-count complaint. One count alleged diversity jurisdiction. The second relied for jurisdiction on section 27 of the Securities Exchange Act of 1934, 15 U.S.C. § 78aa (1976). Both sought injunctive relief against a merger for which allegedly misleading proxy statements had been solicited. No preliminary injunctive relief was granted and, as here, the merger was consummated. Thereafter Borak filed an amended complaint charging that the use of the proxy materials, obtained in violation of section 14(a) of the Act and rule 14a-9 of the Securities and Exchange Commission, caused damage to the corporation and its shareholders. The Supreme Court

held that the derivative complaint seeking damages resulting from the consummation of the merger stated a cause of action which could be entertained by virtue of the jurisdiction conferred in section 27 over "suits in equity and actions at law brought to enforce any liability or duty created by this title." 377 U.S. at 433. It expressly rejected the contention that remedies for violation of section 14 are limited to prospective relief. *Id.* at 434, 84 S.Ct. at 1560.

The situation in *Borak* and in this case are analytically similar. In *Borak* the diversity plaintiff was unsuccessful in preventing a merger. Here Baron's state court efforts to prevent the merger proved to be equally unavailing. In *Borak* the Court recognized a derivative cause of action for the damages which accrued as a consequence of the merger. Baron seeks such damages. Further, common to both cases is the plain and indisputable fact that had either succeeded in obtaining an injunction no damages would have been inflicted. *Borak* did not involve a statute of limitations issue. It did, however, recognize that there is a separate cause of action for damages resulting from the unjustifiable use of proxies obtained in violation of section 14. The Court reasoned that recognition of such a separate cause of action was necessary for "if the law of the State happened to attach no responsibility to the use of misleading proxy statements, the whole purpose of the section might be frustrated." 377 U.S. at 434-35, 84 S.Ct. at 1561. The holding in *Borak* that use of a misleading proxy statement is separately actionable was reiterated unequivocally in *Mills v. Electric Auto-Lite*, 396 U.S. 375, 383, 90 S.Ct. 616, 621, 24 L.Ed.2d 593 (1970).

When, then, does a cause of action for damages flowing from the unjustifiable use of proxies obtained in violation of section 14 accrue? The district court held that it accrues when the plaintiff has sufficient knowledge of the misleading nature of the proxies that he could bring an action under section 27 for injunctive relief. That analysis is in our view inconsistent with the court's recognition in *Borak* of a separate

cause of action for damages. The cause of action for damages is in the nature of an action in tort for breach of the fiduciary duty to refrain from making use of illegal proxies to the detriment of the corporation and its stockholders. If Borak had succeeded in enjoining the use of the proxies, such a cause of action would never have accrued. The cause of action recognized by the Supreme Court could never have been prosecuted to a successful conclusion because a necessary element of an action for damages is actual injury.

[1] It is a rule of general application that a cause of action for the recovery of damages accrues only when it could be prosecuted to a successful conclusion. *E.g., United States v. Wurts*, 303 U.S. 414, 418, 58 S.Ct. 637, 82 L.Ed. 932 (1938); *Grayson v. Harris*, 279 U.S. 300, 304-05, 49 S.Ct. 306, 73 L.Ed. 700 (1929); *City of Philadelphia v. Lieberman*, 112 F.2d 424, 428 (3d Cir.1940). Delaware, whose statute of limitations governs, adheres to that rule. "A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of the injury." *Nardo v. Guido DeAscanis & Sons, Inc.*, 254 A.2d 254, 256 (Del.Super.Ct.1969). The state recognizes "the basic rule that, in general, the statute of limitations begins to run from the date of the injury caused by the defendant...." *Lembert v. Gilmore*, 312 A.2d 335, 337 (Del.Super.Ct.1973). The United States District Court in Delaware has consistently recognized as much. *Rose Hall, Ltd. v. Chase Manhattan Overseas Bank*, 494 F.Supp. 1139, 1157 (D.Del.1980); *Oliver B. Cannon & Son, Inc. v. Fidelity & Casualty Co.*, 484 F.Supp. 1375, 1388 (D.Del. 1980); *Freedman v. Beneficial Corp.*, 406 F.Supp. 917, 922 (D.Del.1975).

[2] The district court held, however, that when state statutes of limitations are borrowed, federal standards determine the question of accrual. Certainly which state statute of limitations should be borrowed is a question of federal law. *E.g., Knoll v. Springfield Township School District*, 699 F.2d 137, 141 (3d Cir.1983); *Biggans v. Bache*

Halsey Stuart Shields, 638 F.2d 605, 607 & n. 3 (3d Cir.1980); *Roberts v. Magnetic Metals Co.*, 611 F.2d 450, 452 (3d Cir.1979). In addition, with respect to federal law causes of action, it is well settled that federal standards determine when concealment tolls the running of a state statute of limitations otherwise applicable. *Holmberg v. Armbrrecht*, 327 U.S. 392, 395-97, 66 S.Ct. 582, 90 L.Ed. 743 (1946). Moreover the question of when a cause of action is so complete that it may be enforced by suit, and thus has accrued, is a federal question. *Cope v. Anderson*, 331 U.S. 461, 464, 67 S.Ct. 1340, 1341, 91 L.Ed. 1602 (1947); *Rawlings v. Ray*, 312 U.S. 96, 98, 61 S.Ct. 473, 474, 85 L.Ed. 605 (1941). Thus we agree with the district court that when the cause of action alleged in the complaint accrued for purposes of the application of Del.Code Ann. Tit. 10, § 8106 (1974) is in this case a federal law question.

[3] Where we part company with the district court, however, is in the identification of the question. In deciding the question of when the cause of action was so complete that it could be successfully prosecuted to completion, a determination such as that in *Cope v. Anderson* and *Rawlings v. Ray*, the court applied the knowledge test which determines the quite different question of when concealment permits tolling. See *Holmberg v. Armbrrecht*, 327 U.S. 392, 66 S.Ct. 582, 90 L.Ed. 743 (1946). The policy issues involved in these separate questions are not identical. For purposes of tolling we look to reasons why, in equity, a cause of action which could have been prosecuted to completion within the period of the statute of limitations had the plaintiff known about it, may still be brought during some longer period. When, as here, knowledge is not disputed, there is no federal policy suggesting that the generally accepted test for the accrual of a cause of action—whether the action could be prosecuted to a successful completion—should not govern.

Indeed the rule announced by the district court, that knowledge of the violation of a substantive federal standard, rather than fact of injury, determines the accrual of a

direct or derivative action for money damages, would be likely to have unfortunate ramifications. There are federal statutes with respect to which plaintiff standing to seek money damages and to seek injunctive relief is not identical. See, e.g., *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 491, 97 S.Ct. 690, 698, 50 L.Ed.2d 701 (1977) (no standing to sue for treble damages under section 4, Clayton Act; remand for consideration of injunctive relief under section 16, Clayton Act). The necessary effect of the trial court's confusion of the separate issues of accrual and tolling would be to encourage lawsuits which in many instances would be premature. It is often the case that litigation seeking injunctive relief with respect to conduct allegedly violating some regulatory scheme lasts longer than the period specified in a statute of limitations. If preliminary injunctive relief has been granted, on behalf of the United States or a third party, thereby insulating a potential plaintiff from actual injury, no reason suggests itself that should require the filing of a lawsuit in anticipation of injury merely because the potential plaintiff knows of the violation.

Had Baron filed his complaint seeking money damages caused by anticipated use of the proxies in consummation of the merger, that complaint would properly have been dismissed under Fed.R.Civ.P. 12(b)(6) for failure to state a claim upon which money damages could be awarded. Until the plaintiff can allege facts which would survive such a motion, his cause of action for damages, personal or derivative, has not accrued. Until it has accrued the statute of limitations does not come into operation. Thus the court erred in dismissing the complaint on the authority of Del.Code Ann. Tit. 10, § 8106 (1974).

II.

Perhaps recognizing that the cause of action pleaded in the complaint did not accrue until January 20, 1976, the defendants urge as a separate ground for affirmance the fact that the complaint was not served for over a year after it was filed. The United States Magistrate to whom the

Price Waterhouse motion to dismiss was referred recommended to the district court that this ground for dismissal should be rejected. In making that recommendation the magistrate relied on the approving citation in *Walker v. Armco Steel Corp.*, 446 U.S. 740, 751 n. 11, 100 S.Ct. 1978, 1985 n. 11, 64 L.Ed.2d 659 (1980), and in *Ragan v. Merchants Transfer Co.*, 337 U.S. 530, 533, 69 S.Ct. 1233, 1234, 93 L.Ed. 1520 (1949) of Judge Learned Hand's decision in *Bomar v. Keyes*, 162 F.2d 136, 141 (2d Cir.), cert. denied, 332 U.S. 825, 68 S.Ct. 166, 92 L.Ed. 400 (1947). The district court did not consider the possible effect of delay in issuance and service of the summons. Baron here takes issue with the defendants' version of the reason for the delay in service. In these circumstances we deem it inappropriate to consider the delay in issuance and service of the summons as an alternative ground for affirmance. The present record is not adequate for the resolution of that question.

III.

The summary judgment in favor of the defendants will be reversed and the case remanded for further proceedings.



Daniel J. MILLER, Jr., Petitioner,

v.

UNITED STATES of America and Department of the Army, Respondents.

No. 82-3404.

United States Court of Appeals,
Third Circuit.

Argued May 31, 1983.

Decided Sept. 21, 1983.

Petition was filed for review of final order of the Merit Systems Protection

In the case at bar, plaintiffs' claim arose in November, 1979; they instituted suit approximately sixteen months later. Since their § 1983 claim is most closely akin to the state law tort of false arrest and imprisonment and assault and battery, the motion to dismiss will be denied as suit was commenced within the prescribed two-year time limit. 42 Pa.C.S.A. § 5524(1).



Robert T. DOFFLEMYER and Josephine C. Dofflemyer, Plaintiffs,

v.

W.F. HALL PRINTING COMPANY, a corporation of the State of Delaware, Mobil-Hall Corporation, a corporation of the State of Delaware, Mobil Holdings Corporation, a corporation of the State of Delaware, Mobil Corporation, a corporation of the State of Delaware, Canadian Imperial Bank of Commerce Trust (Bahamas) Limited, Canadian Imperial Bank of Commerce, Anthony J. Allegretti, Robert L. Epstein, Robert S. Knox, Morris L. Leibman, William G. Maloney, Herbert F. Moeller, Patrick L. O'Malley, Jay A. Pritzker, Robert A. Pritzker, Directors of Mobil-Hall Corporation, Directors of Mobil Holdings Corporation, Directors of Mobil Corporation, Beneficiaries of Various Trusts for the Benefit of Certain Descendants of Nicholas J. Pritzker, Deceased, and their Spouses as their Interest may Appear in Trusts Administered by Canadian Imperial Bank of Commerce Trust (Bahamas) Limited as Trustee, Salomon Brothers, a corporation of the State of New York and J. Ira Harria, Defendants.

Civ. A. No. 82-77.

United States District Court,
D. Delaware.

Jan. 28, 1983.

Former shareholders brought class and derivative action arising out of actions by

defendants in connection with merger of corporation, alleging violations of federal securities law and breach of fiduciary duty under state law. The District Court, Stapleton, J., held that: (1) three-year limitations period normally applicable to actions for common-law fraud and breach of fiduciary duty applied to suit; (2) chancellor's prior finding of appraised value of plaintiffs' stock did not preclude an award of damages in present action; (3) derivative claims asserted by former shareholders on behalf of corporation against corporation which arose out of merger were moot; and (4) categories of allegedly omitted or misleading information from proxy statements were sufficiently material to state cause of action under sections 10(b) and 14(a) of the Securities Exchange Act.

Ordered accordingly.

1. Federal Courts ⇐ 426

Because there is no federal statute imposing an express limitation on private actions brought under sections 10(b) and 14(a) of Securities Exchange Act, federal court must apply limitations law of forum state. Securities Exchange Act of 1934, §§ 10(b), 14(a), 15 U.S.C.A. §§ 78j(b), 78n(a).

2. Securities Regulation ⇐ 134

Where a plaintiff has no remedy under state's blue-sky law, but operative facts alleged in complaint give rise to claim under state's common law, it is limitations period applicable to common-law claim rather than blue-sky period which governs federal claims under Rule 10b-5. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b).

3. Securities Regulation ⇐ 134

Delaware's two-year limitations period applicable to actions under its blue-sky law was not applicable to action by former shareholders under sections 10(b) and 14(a) of Securities Exchange Act arising out of merger of corporations, where parties did

not suggest any connection between events challenged in action and state of Delaware other than fact that defendant corporations were incorporated there, and where plaintiffs, former shareholders, resided in California and received their proxy solicitation there while merger vote apparently took place in Illinois. Securities Exchange Act of 1934, §§ 10(b), 14(a), 15 U.S.C.A. §§ 78j(b), 78n(a); 6 Del.C. § 7323(e, h).

4. Securities Regulation ⇐134

Even if cause of action by Delaware corporation's former shareholders residing in California, in alleging violations of sections 10(b) and 14(a) of the Securities Exchange Act arising out of merger, arose in California, Delaware court would not apply California's one-year blue-sky limitations period under "borrowing statute," because California law does not limit any liability existing under common law, so that California court would apply three-year period applicable to common-law fraud actions to claim of common-law fraud based on misrepresentation in proxy statement; therefore, three-year limitations period normally applicable to action for common-law fraud and breach of fiduciary duty applied to suit. Securities Exchange Act of 1934, §§ 10(b), 14(a), 15 U.S.C.A. §§ 78j(b), 78n(a); 10 Del.C. § 8121; West's Ann.Cal.Corp.Code § 25506; West's Ann.C.C.P. § 338.

5. Fraud ⇐38

Delaware three-year statute of limitations applicable to claims for common-law fraud and breach of fiduciary duty applies to common-law claims of mismanagement and breach of fiduciary duty. 10 Del.C. § 8106.

6. Limitation of Actions ⇐43

Cause of action does not accrue before right to institute suit arises.

7. Securities Regulation ⇐134

Where former shareholders alleged that defendants, in breach of their fiduciary duty, engineered merger which fraudulently benefited majority shareholders' interests and which served no valid business purpose, they could not have sued for damages until merger was actually accomplished, because

until that time they had suffered no injury by defendants' acts; therefore, applicable Delaware three-year statute of limitations began to run at time of accomplishment of merger. 10 Del.C. § 8106.

8. Judgment ⇐720

In order to claim benefit of issue preclusion, party asserting it must show that same issue of fact to be determined was, in former action, litigated by parties, determined by court and necessarily so determined.

9. Securities Regulation ⇐155

Section of Securities Exchange Act providing that no person permitted to maintain suit for damages under Act shall recover total in excess of his actual damages on account of conduct complained of prohibits recovery of punitive damages, but does not limit plaintiff's recovery of actual damages to out-of-pocket loss. Securities Exchange Act of 1934, § 28(a), 15 U.S.C.A. § 78bb(a).

10. Securities Regulation ⇐155

In context of merger carried out by means of misleading solicitation of proxies for shareholder approval of merger, "actual damages," within meaning of section of Securities Exchange Act providing that no person permitted to maintain suit for damages under Act shall recover total in excess of his actual damages on account of conduct complained of, may include loss of possible profit, unless wholly speculative, from securing merger agreement more favorable to plaintiff. Securities Exchange Act of 1934, § 28(a), 15 U.S.C.A. § 78bb(a).

See publication Words and Phrases for other judicial constructions and definitions.

11. Securities Regulation ⇐154

Where former shareholders' theory in securities case was that, but for misleading proxy statement and breach of fiduciary duty with regard to merger, they would have either been able to stop merger or obtain agreement more favorable to them, damages to which former shareholders would be entitled under sections 10(b) and 14(a) of the Securities Exchange Act would

presumably be difference between what shareholders received in appraisal action and what they would have received if there had been no wrongdoing; therefore, chancellor's prior finding of appraised value of their stock did not preclude former shareholders from receiving an award of damages in present action. Securities Exchange Act of 1934, §§ 10(b), 14(a), 15 U.S.C.A. §§ 78j(b), 78n(a); 8 Del.C. § 262.

12. Corporations ⇐584

Stockholder of Delaware corporation who elects to pursue his appraisal remedy under Delaware General Corporation Law cannot thereafter sue derivatively on behalf of corporation. 8 Del.C. § 101 et seq.

13. Corporations ⇐584

Under Delaware law, stockholder electing appraisal is foreclosed from attacking merger through fraud claim asserted on his own behalf.

14. Corporations ⇐584

Under Delaware law, stockholder who elects appraisal in ignorance of fraud in merger will be entitled to rescind that election upon discovery of fraud even though his election would otherwise be irrevocable under appraisal statute; therefore, former shareholders, claiming that they were ignorant of fraud they subsequently asserted at time they elected their appraisal remedy, stated cause of action under Delaware law.

15. Corporations ⇐584

Since a corporation cannot sue itself for its own benefit, derivative claims asserted by former shareholders on behalf of corporation against corporation which arose out of merger with former shareholders' corporation were moot.

16. Securities Regulation ⇐52, 63

One requirement for cause of action under Rule 10b-5 and section 14(a) of the Securities Exchange Act alleging that a proxy statement was misleading because of an omission or misrepresentation of fact is that the fact must be material; standard for materiality is that there is a substantial likelihood that reasonable shareholder would consider it important in deciding how

to vote; this does not require proof that disclosure would have caused a reasonable shareholder to change his or her vote, it is only necessary that omitted facts would have assumed actual significance in deliberations of reasonable shareholder. Securities Exchange Act of 1934, § 14(a), 15 U.S.C.A. § 78n(a).

17. Securities Regulation ⇐51, 63

Categories of allegedly omitted or misleading information from proxy statements were sufficiently material to state cause of action under sections 10(b) and 14(a) of Securities Exchange Act on part of former shareholders alleging that such omissions and misrepresentations in proxy statement led to approval of merger of corporation. Securities Exchange Act of 1934, §§ 10(b), 14(a), 15 U.S.C.A. §§ 78j(b), 78n(a).

18. Securities Regulation ⇐136

Complaint by former shareholders alleging violations of federal securities laws in corporation's merger failed to state cause of action against New York corporation and one of its partners as defendants. Securities Exchange Act of 1934, §§ 10(b), 14(a), 15 U.S.C.A. §§ 78j(b), 78n(a).

19. Securities Regulation ⇐136

Former shareholders alleging violations of federal securities law with respect to corporation's merger stated cause of action against owner of 45.2% of corporation's stock as trustee under various trusts, and bank exercising control over actions of that owner; allegations of control alone were sufficient to state claim under section 20(a) of Securities Exchange Act, which renders controlling parties liable for violations of controlled party. Securities Exchange Act of 1934, §§ 10(b), 14(a), 20(a), 15 U.S.C.A. §§ 78j(b), 78n(a), 78u(a).

20. Federal Courts ⇐261

District court has personal jurisdiction over foreigners not present in United States in actions arising under Securities Exchange Act to extent permitted by due process clause of Fifth Amendment. U.S. C.A. Const. Amend. 5; Securities Exchange Act of 1934, § 1 et seq., 15 U.S.C.A. § 78a et seq.

21. Constitutional Law — 305(5)

Under due process clause, if defendant's contacts with forum are so numerous that they reach "minimum contacts" required by *International Shoe*, such that maintenance of suit does not offend traditional notions of fair play and substantial justice, then personal jurisdiction over defendant may be asserted consistent with due process clause. U.S.C.A. Const.Amend. 5.

22. Federal Courts — 261

Exercise of control, on part of banks, owner of corporation's stock as trustee under various trusts, and bank exercising control over actions of that owner, respectively, was sufficient contact with corporation upon which to predicate jurisdiction over banks as defendants in federal securities law fraud action, even though banks were foreign entities. Securities Exchange Act of 1934, §§ 10(b), 14(a), 15 U.S.C.A. §§ 78j(b), 78n(a); U.S.C.A. Const.Amend. 5.

Lester J. Taufen, Connolly, Bove & Lodge, Philip D. Saxon, Wilmington, Del., for plaintiffs.

Lewis S. Black, Jr., Donald E. Reid, Morris, Nichols, Arant & Tunnell, Wilmington, Del., Alan R. Sloate, New York City, for defendants W.F. Hall Printing Co., Mobil Holdings Corp. and Mobil Corp.

Louis J. Finger, Helen L. Winslow, Richards, Layton & Finger, Wilmington, Del., for defendants Jay A. Pritzker, Canadian Imperial Bank of Commerce, and Canadian Imperial Bank of Commerce Trust Co. (Bahamas) Ltd.

Michael D. Goldman, Gregory A. Inskip, Potter, Anderson & Corroon, Wilmington, Del., Theodore Gewertz, Wachtell, Lipton, Rosen & Katz, New York City, for defendants Salomon Brothers, Inc. and J. Ira Harris.

OPINION

STAPLETON, District Judge:

Robert Dofflemyer and Josephine Dofflemyer, former shareholders of W.F. Hall

Printing Company, a Delaware corporation ("Hall"), have brought this class and derivative action on behalf of themselves and other Hall shareholders owning Hall stock at the time of the acts complained of in the complaint. The litigation arises out of actions by defendants in connection with a merger of Hall and a second-tier subsidiary of Mobil Corporation, Mobil-Hall Corporation ("Mobil-Hall"). The complaint alleges violations of Sections 10(b) and 14(a) of the Securities Exchange Act of 1934, as well as claims of breach of fiduciary duty under state law. The case is currently before me on defendants' motion to dismiss.

The agreement effecting the merger of Mobil-Hall into Hall provided that all shares of Hall would be converted into the right to receive \$27.50 in cash and all shares of Mobil-Hall would be converted into shares of Hall. As a result of the merger, Hall became the wholly-owned subsidiary of Mobil Holdings Corporation ("Mobil Holdings"), which in turn is the wholly-owned subsidiary of Mobil Corporation ("Mobil").

The merger agreement was approved by the respective boards of directors of Mobil Holdings, Hall, and Mobil-Hall on or about November 27, 1978. A proxy statement detailing the proposed merger was thereafter distributed to Hall shareholders on January 29, 1979 and the proposed merger was submitted to the shareholders of Hall for their approval on February 20, 1979. The merger was approved by an affirmative vote of 83.6% of the shares of Hall and became effective on February 21, 1979.

Plaintiffs are two former shareholders of Hall. Approximately two weeks before the Hall shareholders voted to approve the merger, plaintiffs objected to the merger and demanded an appraisal of the value of their shares. By letter dated February 23, 1979, Hall advised plaintiffs of the effectiveness of the merger and of their right to withdraw their demand for appraisal if they so requested prior to April 23, 1979. Plaintiffs elected not to withdraw their demand and instead filed an action for an appraisal in the Delaware Chancery Court on June 14, 1979.

On July 20, 1979, plaintiffs brought a second action in the Delaware Chancery Court which sought to rescind the merger on the grounds, among others, that the \$27.50 per share price paid to the shareholders under the terms of the merger was unfair, that the Proxy Statement contained material omissions, and that the directors of Hall breached their fiduciary duties to the shareholders of Hall. Over the course of the next six months, plaintiffs filed three separate motions seeking to stay the appraisal action pending resolution of their action challenging the merger. Those motions were all denied by the Chancery Court. Finally, six days before the date set for the appraisal hearing, plaintiffs filed a motion to dismiss the appraisal action. That motion was likewise denied by the Court.

A hearing was held on plaintiffs' appraisal petition on January 30, 1980 and the Chancery Court found that the appraisal value of plaintiffs' shares of Hall stock at the time of the merger was \$22.22 per share. *Dofflemyer v. W.F. Hall Printing Company*, C.A. No. 5906 (Del.Ch. September 17, 1980). Pursuant to an Order and Judgment entered by the Chancery Court subsequent to the hearing, plaintiffs surrendered their Hall stock and were paid \$22.22 per share plus 11.8% interest from the date of the merger to the date of payment.

Plaintiffs did not appeal from the Chancery Court determination of the appraisal value of the Hall stock, but on December 17, 1980, they did appeal from the Chancellor's denial of their motion to dismiss the appraisal action. The Delaware Supreme Court affirmed the Chancellor's denial of the plaintiff's motion to dismiss and held that plaintiffs' exercise of their appraisal rights was irrevocable. *Dofflemyer v. W.F. Hall Printing Co.*, 432 A.2d 1198 (Del.1981).

In the merger action, plaintiffs filed a motion for class certification on November 27, 1979. Plaintiffs have not filed a brief in support of this motion, and have taken no other action in their second Chancery Court action since April 14, 1981.

On February 19, 1982, the plaintiffs filed this third action relating to the Hall merger. This latest action by the plaintiffs seeks to challenge the merger on the same grounds asserted in the second Chancery action. The complaint also asserts, however, that the defendants violated the federal securities laws in connection with the merger. Defendants have moved the Court to dismiss this action on a number of grounds.

I. LIMITATIONS AND THE SECTIONS 10(b) AND 14(a) CLAIMS

[1] Because there is no federal statute imposing an express limitation upon private actions brought under Section 10(b) and 14(a) of the Securities Exchange Act, a federal court must apply the limitations law of the forum state. *Roberts v. Magnetic Metals Co.*, 611 F.2d 450, 452 (3d Cir.1979). Typically, the selection of the appropriate limitations period involves a choice between the limitations period of the state's Blue Sky Law and the period for common law fraud. Delaware has a two-year period applicable to actions under its Blue Sky Laws, 6 Del.C. § 7323(e), but a three-year period for common law fraud, 10 Del.C. § 8106. The Third Circuit, in two recent cases, has delineated the path to be followed in making this choice.

In the first case, *Roberts v. Magnetic Metals Co.*, 611 F.2d 450 (3d Cir.1979), a selling shareholder brought suit in New Jersey against the corporation, its merger partner, and their broker agent. The complaint alleged that defendants had made misrepresentations and omissions in connection with the solicitation of shareholder approval of the merger of the corporation and its partner in violation of Sections 10(b) and 14(a). The majority held that the suit was governed by the New Jersey six-year statute of limitations for common law fraud, and not by the New Jersey two-year Blue Sky limitations period. Although Judge Gibbons and Judge Sloviter, comprising the majority, wrote separately, they both agreed that since the operative facts did not give rise to a cause of action under New Jersey's Uniform Securities Act but did give rise to one

under its common law of fraud, the six-year limitation period for fraud applied.

In the second case, *Biggans v. Bache Halsey Stuart Shields*, 638 F.2d 605 (3d Cir. 1980), an investor who was the client of a brokerage house sued the brokerage house in Pennsylvania for "churning" his account in violation of Section 10(b). The court, again, held that the common law limitations period rather than the Blue Sky limitations period applied. The court noted that although the Pennsylvania Blue Sky law arguably prohibits "churning," no damage relief is available in an action brought under that statute. Further, the Pennsylvania Blue Sky law expressly stated that its remedies were not intended to limit any liability existing under common law. The court concluded that the lack of a Blue Sky remedy and the fact that the Blue Sky law was a supplement to the common law compelled the application of the common law limitations period.

[2] It is clear from these two cases that where a plaintiff has no remedy under the state's Blue Sky law, but the operative facts alleged in the complaint give rise to a claim under the state's common law, it is the limitations period applicable to a common law claim rather than the Blue Sky period which governs federal claims under Rule 10b-5. Thus, the first step in deciding which Delaware's limitations period applies to the current action is to examine whether the facts alleged state a cause of action under the Delaware Blue Sky law.

The Delaware Supreme Court has addressed the question of the applicability of the Delaware Blue Sky law, enacted in 1973, only once. In *Singer v. Magnavox*, 380 A.2d 969 (Del.Super.1977), plaintiff claimed that defendants had violated 6 Del.C. § 7303 of the Act by issuing false and misleading statements of material fact relating to a merger. The court held that the Delaware Blue Sky Law did not apply:

[W]e read the Securities Act as a Blue Sky Law governing transactions which are subject to Delaware jurisdiction under traditional tests. To state it another way, we do not read the Act as an at-

tempt to introduce Delaware commercial law into the internal affairs of corporations merely because they are chartered here. Of course, a Delaware corporation is bound by the Act, if it is otherwise applicable. But it is not bound simply because the company is incorporated here.

There is, of course, a presumption that a law is not intended to apply outside the territorial jurisdiction of the State in which it is enacted. [cites omitted]

Plaintiffs are residents of Pennsylvania and were not solicited here. Nor does it appear that the contract was made in Delaware nor that any part of the "sale" occurred here. It follows that the Delaware Securities Act does not apply and that the judgment of the Court of Chancery was correct in so ruling.

We are not persuaded that because the corporate merger vote was held in Delaware this is a sufficient connection with the alleged fraud to permit plaintiffs to invoke the Act. That is simply too fragile a basis on which to establish subject matter jurisdiction over an alleged fraud in Pennsylvania or over a contract made in New York. And plaintiffs' arguments based on registration of the merger documents in Delaware, see 8 Del.C. § 103, and the statutory situs of the Magnavox stock in this State, 8 Del.C. § 169, are equally tenuous and we reject them for the same reason.

[3] The parties have not suggested that there is any connection between the events challenged in the present action and the State of Delaware, other than the fact that the defendant corporations are incorporated here. Plaintiffs reside in California and received their proxy solicitation there, while the merger vote apparently took place in Illinois. These facts provide an even more tenuous connection with Delaware than existed in *Singer*, where, even though the plaintiff resided outside the state as here, the merger vote took place within the state. Thus, on the basis of these facts, it is clear from *Singer* that a Delaware court would not entertain an action under the Delaware

Blue Sky law. Moreover, it is clear from the text of the statute itself that Delaware's Blue Sky law is not intended to supplant existing common law remedies. 6 Del.C. § 7323(h). Accordingly, I conclude that the two-year limitations period is not applicable to this action. *Roberts, Biggans, supra*.

[4] A Delaware state court would, however, entertain an action for common law fraud and breach of fiduciary duty based on the operative facts alleged in the complaint. The limitations period normally applicable to such claims is three years. 10 Del.C. § 8106. Defendants suggest, however, that this Court must further look to Delaware's "borrowing statute," 10 Del.C. § 8121, and apply the shorter of the three-year period or the period provided for by the law of the state "where the cause of action arose."¹ Defendants have suggested only one candidate, namely, California, the state of plaintiffs' residence, as the place "where the cause of action arose." The limitations period applicable to claims of misrepresenta-

tion under California's Blue Sky law, is the shorter of one-year from the date of discovery of the facts, or four years from the violation itself. Cal.Corps.Code § 25506.² California has a three-year limitations period, however, which is applicable to common law fraud actions. Cal.Civil Proc. § 338.³ Defendants argue that if the cause of action in this case arose in California, it is the one-year Blue Sky period which applies and not the three-year period for common law fraud.

Defendants' argument misconstrues the nature of the required inquiry into state law. The inquiry is what limitations period a Delaware court would apply to a claim of common law fraud in a hypothetical state action based on the facts in the federal action. If because of the particular facts here, a Delaware court would look to California limitations law pursuant to Delaware's "borrowing statute", the inquiry it would make would be whether the claim is time-barred in the California courts.⁴ The

1. 10 Del.C. § 8121 provides in part:

Where a cause of action arises outside of this State, an action cannot be brought in a court of this State to enforce such cause of action after the expiration of whichever is shorter, the time limited by the law of this State, or the time limited by the law of the state or country where the cause of action arose, for bringing an action upon such cause of action....

2. California Corporations Code, Section 25401, makes it unlawful to engage in certain securities transactions:

It is unlawful for any person to offer or sell a security in this state or offer to buy a security in this state by means of any written or oral communication which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.

Section 25501 establishes a civil action for violations of Section 25401:

Any person who violates Section 25401 shall be liable to the person who purchases a security from him or sells a security to him, who may sue either for rescission or for damages (if the plaintiff or the defendants, as the case may be, no longer owns the security), unless the defendant proves that the plaintiff knew the facts concerning the untruth or omission or that the defendant exercised rea-

sonable care and did not know (or if he had exercised reasonable care would not have known) of the untruth or omission....

Section 25506 provides the applicable statute of limitations:

No action shall be maintained to enforce any liability created under Section 25500, 25501, or 25502 (or Section 25504 or Section 25504.1 insofar as they related to those sections) unless brought before the expiration of four years after the discovery by the plaintiff of the facts constituting the violation, which ever shall first expire.

3. Cal.Civil Proc. § 312, provides:

Civil actions, without exception, can only be commenced within the periods prescribed in this title, after the cause of action shall have accrued, unless where, in special cases, a different limitation is prescribed by statute.

Section 338 then provides in part:

Within three years:

4. An action for relief on the ground of fraud or mistake.

4. I assume, without deciding, that the forum state's "borrowing statute" is properly applied to a federal action based on federal securities laws claims where the cause of action arose outside the forum state. For decisions in the Second Circuit applying a "borrowing statute," see *Robertson v. Seidman & Seidman*, 609 F.2d

policy behind the Delaware statute is to provide repose in situations where the defendant would have repose in the state where the claim arose and the question thus would be whether a California court would entertain an action based on the operative facts alleged in this complaint. Because the California Blue Sky law does not limit any liability existing under common law, a California court would apply the three-year period of Section 338 to a claim of common law fraud based on misrepresentation in a proxy statement and would entertain this suit. *Bowden v. Robinson*, 67 Cal.App.3d 705, 136 Cal.Rptr. 871 (Cal.App.1977). Thus, a Delaware court would not apply California's one-year Blue Sky period under the "borrowing statute." Accordingly, under the authority of *Roberts and Biggans*, this Court must likewise apply a three-year period. Defendants do not contend that the federal claims are barred by a three-year limitations period.

II. LIMITATIONS AND THE STATE COMMON LAW CLAIMS

[5, 6] There is no disagreement among the parties that the Delaware three-year statute of limitations, 10 Del.C. § 8106, applies to the common law claims of mismanagement and breach of fiduciary duty. *Halpern v. Barran*, 313 A.2d 139 (Del.Ch. 1973). The disputed issue is when the three-year period began to run. Under Section 8106, the three-year period does not begin to run until the cause of action has accrued. It is a basic principle of limitations law that a cause of action does not accrue before the right to institute a suit arises. See e.g., 54 C.J.S. *Limitations of Actions* § 109.

583 (2d Cir.1979); *Gluck v. Amicor, Inc.*, 487 F.Supp. 608 (S.D.N.Y.1980).

5. The cases relied upon by defendants, *Delaware State College v. Ricks*, 449 U.S. 250, 101 S.Ct. 498, 66 L.Ed.2d 431 (1980) and *Brown v. Automated Marketing Systems, Inc.*, C.A. No. 6715 (Del.Ch. March 22, 1982), are inapposite.

In *Ricks*, the Supreme Court held that a claim under the civil rights laws charging discriminatory denial of academic tenure accrued at the time that tenure was denied, not at the

[7] The plaintiffs' state law claims are that the defendants, in breach of their fiduciary duty, engineered a merger which fraudulently benefited the majority shareholders' interests and which served no valid business purpose. In order to consummate this merger, the majority shareholders and the board of directors are alleged to have (1) obtained an investment opinion of a banking firm they knew was not independent; (2) maneuvered to avoid an 80 percent "supermajority" provision in the by-laws; and (3) issued a proxy statement which was false and misleading.

The plaintiffs could not have sued for damages until the merger was actually accomplished—until that time, they had suffered no injury by the defendants' acts. This case is analogous to *Kaufman v. Albin*, 447 A.2d 761 (Del.Ch.1982), where the Chancery Court denied defendants' motion to dismiss on the ground that the claim was time-barred. Plaintiffs' allegations were that the directors had wasted corporate assets by improperly permitting the officer-optionees of the corporation to surrender their stock options in connection with a tender offer for the corporation's stock. The Court of Chancery held that the limitations period began to run at the time the tender offer was accepted by the tendering of 52% of the outstanding shares and not at the time of the directors' resolution accelerating the exercise date of unexercised options. Until that time, the transaction which was the subject of the suit was not accomplished and there had been no injury. Similarly in the present case, the merger transaction which is the subject of this suit was not accomplished and no injury occurred until the merger was effected.⁵

time plaintiff's employment actually ended. It was the habitual practice of the defendant college to give a one year terminal contract to those professors, including Ricks, denied tenure. Ricks did not complain that he was discriminated against with respect to his termination at the end of the one year contract, rather he complained only with respect to the denial of tenure. Thus, the injury was the denial of tenure and not the loss of employment.

Brown is also inapplicable. In that case, the Court of Chancery held that a plaintiff who

III. ISSUE PRECLUSION

[8] Under certain circumstances, an issue of fact or law determined in one action between two parties is binding upon the parties in a later action. Defendants contend that the valuation of Hall stock made in the appraisal proceeding in the Court of Chancery is binding upon this court and precludes the award of any damage relief because the stock was appraised at \$22.22 per share, as of the time of the merger, an amount \$5.28 less than the \$27.50 per share offered in the merger agreement. In order to claim the benefit of this "issue preclusion," defendants must show that the same issue of fact to be determined here was, in the former action, (1) litigated by the parties, (2) determined by the court, and (3) necessarily so determined. Restatement of Judgments, Second § 27. *Haize v. Hanover Ins. Co.*, 536 F.2d 576, 579 (3d Cir.1976).

The Court of Chancery determined that the value of Hall stock at the time of the merger was \$22.22. In reaching this conclusion the court accepted the testimony of defendants' experts that the earnings value at the time of the merger was \$21.20 per share, the asset value was \$22.47 per share, and the market value was \$23.00 per share. The estimate of the market value of Hall stock at the time of the merger in February, 1979, was based on the stock's price of \$23.00 per share on the New York Stock Exchange in mid-September of 1978. The expert chose this value because the price of Hall stock rose during the period after mid-September apparently due, at least in part, to a leak of information about the proposed merger. Because the price of two other major printing firms declined during the same period, the expert attributed the en-

tire amount of the rise to the market's expectation of a merger and pursuant to the express command of 8 Del.C. § 262(f) disregarded that amount in determining market value.

The Court also accepted the experts' testimony that there were no factors peculiar to Hall and its operation which would warrant giving a greater weight to one valuation approach over the other. Accordingly, equal weight was given to each of the three factors in arriving at the final figure of \$22.22 per share.

[9, 10] If the valuation by the Court of Chancery is to have the preclusive effect on the issue of damages that defendants say it does, the Court of Chancery must actually have determined the same "value" that this Court would determine for the purposes of computing damages under the federal securities laws. Section 28(a) of the Act, 15 U.S.C.A. § 78bb, which is applicable to actions under Section 10(b), as well as Section 14(a), provides that "no person permitted to maintain a suit for damages under the provisions of this chapter shall recover . . . a total amount in excess of his actual damages on account of the act complained of." This section prohibits the recovery of punitive damages but does not limit a plaintiff's recovery of actual damages to out-of-pocket loss. *Gould v. American Hawaiian SS. Co.*, 535 F.2d 761 (3d Cir.1970). In the context of a merger carried out by means of misleading solicitation of proxies for shareholder approval of a merger, "actual damages" may include the loss of possible profit, unless wholly speculative, from securing a merger agreement more favorable to plaintiff. *Gould* at 782.⁶

purchased shares after reading a press release indicating that the board of directors had approved a plan of merger did not have standing to challenge the merger when it was carried out according to the plan. The holding of that case involved a determination of the times when a plaintiff must own stock in a corporation in order to have standing to challenge a merger and is not pertinent to when, if standing had existed, the plaintiff could have sued for damages.

6. The holding of *Gould* came in the context of a claim under 14(a). Likewise, for a 10b-5 claim, the Third Circuit has held that "the measure of damages is the difference between what the buyer paid for his stock and what he would have paid had there been no fraudulent conduct." *Sharp v. Coopers & Lybrand*, 649 F.2d 175 (3d Cir.1981), cert. denied, 455 U.S. 938, 102 S.Ct. 1427, 71 L.Ed.2d 648 (1982). In the context of a merger, it is clear that this standard also requires that the value of lost opportunities be taken into account.

[11] As I understand plaintiffs' theory of the case, they claim that, but for a breach of fiduciary duty, Hall would have negotiated either a form of transaction which was tax free to the Hall stockholders or a price (above \$27.50) which reflected a premium for there being a recognition of taxable gain by Hall stockholders. Cf. *Shrage v. Bridgeport Oil Co.*, 31 Del.Ch. 805, 71 A.2d 882 (Del.Super.1950). Further, plaintiffs claim that if the proxy statement had not been misleading, they would have been able to stop the merger which in fact occurred and to force the negotiation of a new transaction which would have been either non-taxable or reflect a premium for its taxable character. Cf. *Gould v. American Hawaiian SS. Co.*, 535 F.2d 761 (8d Cir.1970). On either claim, the damages would presumably be the difference between what plaintiffs received in the appraisal action and what they would have received if there had been no wrongdoing. While it is too early in the game to decide precisely what an analysis of the damage issues will entail, it is likely that a determination of the value of what plaintiffs would have received absent any wrongdoing will involve different factors than those considered by the Court of Chancery in determining the appraised value of the plaintiffs' stock in accordance with Section 262 of Delaware's General Corporation Law. It will presumably involve, for example, a consideration of what Mobil was willing to pay for the Hall stock. The value of the stock to Mobil, however, is a factor which the Chancellor could not and did not consider in fixing the appraised value.

It follows that the Chancellor's finding of an appraised value of \$22.22 does not preclude plaintiffs from contending that they are entitled to an award of damages in this action. This does not mean, however, that the determinations of fact in the prior action will have no preclusive effect here. It well may be that some of those determinations will be relevant to the damage issues in this case and, if so, they will be binding on the plaintiffs here.

Plaintiffs argue that nothing in the appraisal action should be given preclusive

effect because they did not wish to litigate that action by the time it got to trial. This fact simply is not relevant. Facts involving the value of Hall shares were put in issue in the appraisal action, plaintiffs were afforded a full and fair opportunity to litigate those issues, and the Court made findings thereon. If facts so found are relevant here, anyone who was a plaintiff in the appraisal action will be precluded from contesting them here.

IV. ELECTION OF REMEDIES AND MOOTNESS

[12, 13] Defendants correctly point out that a stockholder of a Delaware corporation who elects to pursue his appraisal remedy under the Delaware General Corporation Law cannot thereafter sue derivatively on behalf of the corporation. This is so because "the effect of the appraisal action ... [is] to convert the status of the plaintiffs therein from that of stockholders of the corporation to that of creditors thereof." *Braasch v. Goldschmidt*, 41 Del.Ch. 519, 199 A.2d 760, 766 (Del.Ch.1964). Under Delaware law, a stockholder electing appraisal is also foreclosed from attacking the merger through a fraud claim asserted on his own behalf. *Braasch* at 766. This does not mean, however, that defendants are entitled to have plaintiffs' state law claims dismissed at this point.

[14] While no Delaware case has so held, I predict that the Supreme Court of Delaware would hold that a stockholder who elects appraisal in ignorance of fraud in the merger will be entitled to rescind that election upon discovery of the fraud even though his election would otherwise be irrevocable under the appraisal statute. Judge Steel of this Court made a similar prediction in *Voege v. American Sumatra Tobacco Corporation*, 241 F.Supp. 369 (D.Del.1965). This may be relevant here because plaintiffs claim that they were ignorant of the fraud they now assert at the time they elected their appraisal remedy,

My prediction and this claim are sufficient to get plaintiffs past a motion to dismiss.'

[15] Defendants also urge, on the basis of *Bokat v. Getty Oil Co.*, 262 A.2d 246 (Del.Supr.1970), that all derivative claims asserted on behalf of Hall must be dismissed because they are moot. In *Bokat*, the plaintiff instituted suit on behalf of Tidewater Oil Company charging that Tidewater's majority stockholder, Getty Oil Company, had wrongfully exploited Tidewater for Getty's exclusive benefit. The action sought to recover damages for injuries allegedly incurred by Tidewater as a result of Getty's self-dealing. Six years after institution of the suit, the stockholders of Getty and Tidewater approved a merger of the two companies and Getty survived the merger. Thereafter, Getty successfully moved for summary judgment on the derivative claims on the ground that they had been rendered moot as a result of the merger. Chief Justice Wolcott held:

These, then, are derivative actions seeking to recover damages from Getty Oil for the benefit of Tidewater. As such, if the actions had merit, they were assets of Tidewater which, under 8 Del.C. § 259, passed on the merger to Getty Oil along with Tidewater's other assets.

The action against Getty Oil has therefore been made moot by the merger, for if this were not so, the anomalous situation of a corporation suing itself for its own benefit would be presented. *Braasch v. Goldschmidt*, 41 Del.Ch. 519, 199 A.2d 760. This results from the nature of a derivative action which is to be considered as though the injured corporation, itself, was suing the defendants. *Keenan v. Eshleman*, 23 Del.Ch. 234, 2 A.2d 904

262 A.2d at 249.

Bokat is controlling with respect to the derivative claim asserted against Mobil-

7. Plaintiffs appear to have filed their Chancery fraud action substantially before asking the Court of Chancery to relieve them of their election and dismiss the appraisal action. If they had knowledge of the fraud they now assert at the time of their motion to dismiss

Hall. When the merger occurred, Hall, as the surviving corporation, inherited Mobil-Hall's contingent liability on this claim. Since a corporation can not sue itself for its own benefit, the derivative claims asserted on behalf of Hall against Mobil-Hall must be dismissed as moot. The rationale of *Bokat* does not apply, however, to the derivative claims against the other defendants.

V. MATERIALITY

[16] One requirement for a cause of action under Rule 10b-5 and Section 14(a) alleging that a proxy statement was misleading because of an omission or misrepresentation of fact is that the fact must be material. The standard for materiality is that "there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449, 96 S.Ct. 2126, 2132, 48 L.Ed.2d 757 (1976). This does not require proof that disclosure would have caused a reasonable shareholder to change his or her vote; it is only necessary that the omitted facts would have assumed "actual significance in the deliberations of the reasonable shareholder." *TSC* at 499, 96 S.Ct. at 2132. The same definition has been articulated in the context of the Delaware rule requiring disclosure of material facts by a prospective buyer owing a fiduciary duty to a prospective seller. *Lynch v. Vickers Energy Corp.*, 383 A.2d 278, 281 (Del.Supr.1977). Defendants contend that all material facts were fully disclosed. I shall examine separately each of the categories of allegedly omitted or misleading information challenged by defendants as not material.

1. Conflicts of Interest

[17] The plaintiffs' primary argument is that the proxy statement was misleading because it gave the impression that the merger had been negotiated for Hall at

and either could or did urge it as a ground for relief, there may be some preclusion effect here. The parties have not briefed the issue, however, and I express no opinion with respect to it.

arms length by persons sharing a common interest with all Hall stockholders.

The true facts, according to plaintiffs, are as follows: The merger was negotiated by Gordon R. Worley, representing the Mobil interests, Jay Pritzker, representing the Pritzker interests, and J. Ira Harris of Salomon Brothers, Inc. ("Salomon Brothers"), representing Hall and Hall stockholders. Hall management was deliberately and totally excluded from the negotiations. Since Salomon Brothers had substantial and continuing ties to Mobil and the Pritzkers, as well as a financial interest in closing the deal, and since Jay Pritzker had personal interest in having a cash transaction, this meant that the minority stockholders who had an interest in a tax free transaction and a continuing equity interest, or in a premium for a cash transaction, were represented only by persons having a conflict of interest. Moreover, it is charged that a non-cash tax free transaction was never considered by the negotiators or the Hall board because Jay Pritzker ruled it out at the commencement of the negotiations.

In addition to falsely giving the impression that minority stockholders were represented in the negotiation of the merger terms by Hall management, plaintiffs maintain that, in this context, the proxy was misleading in failing to disclose that Salomon Brothers (whose financial interests were disclosed) acted not as an advisor to Hall management but as Hall's sole negotiator, that the Pritzker interests whose stock was being held in Bahamian trusts would not have to recognize gain on a cash transaction,⁸ and that Jay Pritzker had foreclosed the possibility of a tax free transaction.

The defendants dispute significant portions of what plaintiffs claim to be the true facts. Moreover, they stress that there are flaws in plaintiffs' logic. They point out, for example, that plaintiffs recognize the propriety of a cash transaction with a fair premium for Hall stockholders and that Jay Pritzker had no conflict of interest when it came to negotiating for as much cash as

possible in the cash transaction now under attack.

I am unwilling to say on the basis of the current record that plaintiffs will be unable to prove any set of facts entitling them to relief on this "conflict of interest" claim. The current record simply provides an unsatisfactory basis for deciding whether the proxy materials were materially misleading with respect to the negotiation of the merger.

2. The Supermajority By-Law Provision

Section 1.6 of the Hall by-laws requires an 80% supermajority to approve a merger with a "related entity." A "related entity" is defined as the beneficial owner of 10% or more of the voting shares entitled to vote on the merger and a beneficial owner includes any person who (1) has the right to vote or to direct the voting of such stock or (2) has "any agreement, arrangement or understanding with any other person or persons concerning the acquisition, disposition or voting" of such stock.

Hall's proxy statement stated that no party to the transaction held 10% or more of Hall stock or had any agreement, arrangement or understanding with respect to the voting of such stock, and that, therefore, the supermajority provision was inapplicable. Plaintiffs allege that this statement was misleading because they claim that the Pritzker interests in fact had an understanding with Mobil that their Hall shares would be voted in favor of the merger. (Complaint ¶¶ 20(a), 27, 42(c)).

Defendants interpret the by-law to mean that the arrangement or understanding must extend beyond an arrangement as to the vote on the merger and the conversion of the stock pursuant to the merger. I do not agree; if this were the proper interpretation, the clause would merely be repetitive of the prior clause which defined a beneficial owner to include any person with the right to vote the stock. There is a dispute of fact, however, as to whether any such agreement existed. If all that is final-

8. The fact that much of the Pritzker stock was held in Bahamian trusts was disclosed, but this

does not constitute notice of the conflict of interest which plaintiffs allege.

ly shown is that the Pritzkers had expressed an intention to vote in favor of the merger, the by-law is not applicable. Plaintiffs at this time, however, maintain there was more than just an expressed intention to vote in favor of the merger.

Defendants also contend, even assuming the proxy statement erroneously stated that the supermajority provision of the by-laws was not applicable because there was no "arrangement" or "understanding", that the misrepresentation was not material because the by-law is itself invalid under the Delaware Corporation Law. Their position is that a provision requiring a higher vote than that required by statute must be in the certificate of incorporation rather than in the by-laws.⁹ The issue thus posed is clearly a litigable one. This does not mean, however, that the statement in the proxy was not material. The fact that there was a basis for someone to challenge the merger if fewer than 80% of the shareholders approved it would itself appear to be material.

3. The Loeb Rhoades Opinion

As set forth in the proxy statement, the board of directors of Hall engaged Loeb Rhoades, Hornblower & Co. ("Loeb Rhoades"), an investment banking firm, to perform certain financial services for Hall in connection with the proposed merger. In particular, Loeb Rhoades was asked for a preliminary view of the fairness of a \$27.50 per share offer.

Plaintiffs insist that the contents of what it refers to as the "Loeb Rhoades report" should have been disclosed in the proxy statement. The "report" referred to, however, is an internal Loeb Rhoades memorandum written by two analysts to its commitment committee. The memorandum reveals on its face that it represents the ten-

tative views of its authors based upon their preliminary study. Moreover, the tentative conclusion was that the merger terms were fair and the facts concerning Hall which were relied upon in formulating this tentative conclusion were reported in the proxy materials. Under these circumstances defendants had no duty to disclose the contents of the Loeb Rhoades memo under the federal securities laws or under the principles of *Lynch v. Vickers Energy Corp.*, 383 A.2d 278 (Del.Super.1977).

4. The Unfairness of the Merger

The Hall proxy was also allegedly misleading because the directors failed to disclose the unfairness of the merger and the lack of a valid business purpose for the merger.¹⁰ Such allegations have consistently been held not to state a violation of either the federal securities laws or Delaware law. *Biesenbach v. Guenther*, 588 F.2d 400, 402 (3d Cir.1978); *Fisher v. United Technologies Corp.*, 6 Del.J. of Corp.Law, 380, 386 (Del.Ch.1981).

5. The Rights of Hall Shareholders Opposing the Merger

Finally, the complaint contains several allegations that defendants failed to disclose the complete legal picture with respect to shareholders who might wish to oppose the merger. Thus, for example, plaintiffs claim that the proxy statement failed to disclose the burden of proof in any legal controversy over the merger (§ 20(i)) and the "legal or equitable remedies," apart from statutory appraisal (8 Del.C. § 262) "which would also be available to such stockholders, including the right to seek equitable relief and damages arising out of any fraud or illegality...." (§ 20(k)).

It is now well established that such allegations do not state a claim under either

9. Section 251(c) of the Delaware Corporation Law which requires that a merger agreement be submitted for shareholder approval provides that a majority vote is sufficient to adopt the agreement. Section 102(b)(4) permits the certificate to contain "provisions requiring for any corporate action, the vote of a larger portion of the stock ... than is required by this chapter."

10. Complaint, paragraphs 20(d), (h), (j) and (l). For example, paragraph 20(d) alleges that the proxy statement misleadingly "represented that the directors of Hall believed that the proposed merger was in the best interests of Hall and all its stockholders, whereas, in fact, the directors of Hall knew, or should have known, that the merger was grossly detrimental and unfair to Hall and its stockholders, other than the Pritzker interests."

the federal securities laws or Delaware law. The mandate that all material facts of the transaction must be disclosed "does not require that the proxy contain a statement of suggested strategy for those wishing to oppose the transaction." *Gans v. Filmway, Inc.*, 453 F.Supp. 1116, 1121 (E.D.Pa.1978), *aff'd without op.*, 595 F.2d 1212 (3d Cir. 1979); *Accord* with respect to state law, *Fisher v. United Technologies, Inc.*, 6 Del.J. of Corp.Law, 380, 384 (Del.Ch.1981).

VI. THE SALOMON BROTHERS AND J. IRA HARRIS

Salomon Brothers and one of its partners, J. Ira Harris, are named as defendants. The allegations with respect to Salomon Brothers are brief and largely conclusory; the allegations with respect to Mr. Harris are non-existent. These defendants will be dismissed from the suit unless plaintiffs, within thirty days, amend their complaint to state a claim against them under the securities laws or state law. If the claim or claims stated are based solely on state law plaintiffs shall also effect service of process within that period.

[18] Count III of the complaint incorporates most of the other allegations of the complaint and then alleges in conclusory terms that Salomon Brothers "conspired with the other defendants in the planning and execution" of the merger. (Complaint ¶ 29). This allegation, read alone, is insufficient to state a claim under the pleading requirements of Rule 9(b). *DuPont v. Wyly*, 61 F.R.D. 615 (D.Del.1973).

Count III goes on to allege that "it was improper and illegal for Salomon Brothers to ... give its opinion to Hall [on the fairness of the transaction when it was in] ... a position of serious and irreconcilable conflict, because of its ties to the Mobil interests and to the Pritzker interests." (Complaint ¶ 32). The plaintiffs cite nothing in their brief to support this statement and, given the fact that the "ties" to the Mobil and Pritzker interests were fully disclosed in the opinion and proxy statement, I can perceive no theory which might support a claim based upon it. Certainly, it states

no claim under the federal securities acts and the service of process on these defendants is insufficient in the absence of such a claim.

Finally, Count III alleges that the Salomon Brothers' opinion "was not complete, accurate, and objective and could not, to its knowledge have been complete, accurate, and objective." (Complaint ¶ 30). If all that is meant by this is that the firm's view of the transaction was colored by its self-interest so that "it was prejudiced in favor of the acquiring Mobil interests," this allegation adds nothing to those previously discussed. If it is an attempt to allege that Salomon Brothers issued an opinion which it knew to be false and that Hall stockholders would rely upon it, this would be an entirely different matter. It is far from clear that plaintiffs intended to allege the issuance of a deliberately misleading opinion, however, and there is nothing in the complaint which provides a clue as to what might be false or misleading about the opinion. If Salomon Brothers is to be charged with having issued an opinion constituting a device to defraud or with common law misrepresentation, it should be in unambiguous terms and the charge should indicate what rendered the opinion false or misleading.

VII. THE CANADIAN IMPERIAL BANK DEFENDANTS

[19] The Canadian Imperial Bank of Commerce (Bahamas) Limited ("Bahamas") is alleged to have been the owner of 45.2% of the Hall stock as trustee under various trusts for the benefit of the Pritzkers. Read liberally, the complaint alleges that the Canadian Imperial Bank of Commerce ("Canadian") a Canadian bank, exercises control over the actions of Bahamas, thereby sharing its fiduciary duty to Hall's minority stockholders. Bahamas and Canadian (the "Banks") have filed motions to dismiss for failure to state a claim against them and for lack of personal jurisdiction.

The Banks' motions to dismiss for failure to state a claim must be denied. The allegations of control alone are sufficient to state a claim under Section 20(a) of the

Exchange Act which renders controlling parties liable for violations of a controlled party. 15 U.S.C. § 78t(a). Both Canadian and Bahamas have filed affidavits which would support a "good faith non-inducement" defense under that Section, but these can properly be considered only after affording plaintiffs an opportunity for responding in the manner contemplated by Fed.R.Civ.P. 56.

[20, 21] The Banks' motions to dismiss for want of personal jurisdiction over them must also be denied. This Court has personal jurisdiction over foreigners not present in the United States in actions arising under the Securities Exchange Act to the extent permitted by the due process clause of the Fifth Amendment. *Leasco Data Processing Equipment v. Maxwell*, 468 F.2d 1826, 1840 (2d Cir.1972). Under the due process clause, if a defendant's contacts with the forum are so numerous that they reach the "minimum contacts" required by *International Shoe Co. v. Washington*, 326 U.S. 310, 66 S.Ct. 154, 90 L.Ed. 95 (1945), such that "maintenance of the suit does not offend 'traditional notions of fair play and substantial justice,'" *id.* at 316, 66 S.Ct. at 158, citing *Milliken v. Meyer*, 311 U.S. 457, 463, 61 S.Ct. 339, 342, 85 L.Ed. 278 (1940), then personal jurisdiction over the defendant may be asserted consistent with the due process clause. *Texas Trading & Milling Corp. v. Federal Republic of Nigeria*, 647 F.2d 300, 314 (2d Cir.1981), cert. denied, 454 U.S. 1148, 102 S.Ct. 1012, 71 L.Ed.2d 301 (1982).

[22] While it may be, as the Banks suggest, that "the mere ownership and voting of stock in a Delaware company as a trustee" is not enough to meet the "minimum contacts" requirement of *International Shoe*, when the plaintiffs' claim is based on violations of the Securities Exchange Act by a Delaware corporation, I am persuaded that the exercise of control over the offending corporation is a sufficient contact upon which to predicate jurisdiction. *Sun First Nat. Bank of Orlando v. Miller*, 77 F.R.D. 430, 440 (S.D.N.Y.1978).

VIII. CONCLUSION

I thus have concluded: (1) that neither plaintiffs' federal claims nor their state claims are barred by limitations, (2) that the prior appraisal action in the Court of Chancery does not preclude plaintiffs from contending that they are entitled to an award of damages in this action, (3) that the derivative claim asserted on behalf of Hall against Mobil-Hall must be dismissed, (4) that plaintiffs' pursuit of their appraisal remedy does not warrant dismissal of plaintiffs' state law claims, at this stage, (5) that plaintiffs may be able to show a material misrepresentation or omission in Hall's proxy materials, (6) that the claims against Salomon Brothers and J. Ira Harris must be dismissed unless plaintiffs file a curative amendment within thirty (30) days, and (7) that the motion of the Banks to dismiss the claims against them should be denied.



Carolyn BELL and Maryland Welfare Rights Organization (Individually and on behalf of all others similarly situated)

v.

Kalman R. HETTLEMAN, Secretary, Maryland Department of Human Resources (Individually and in his official capacity)

and

Richard S. Schweiker, Secretary of the United States Department of Health and Human Services (In his official capacity).

Civ. No. K-82-2369.

United States District Court,
D. Maryland.

Jan. 31, 1983.

Complaint was filed against the Secretary of the Maryland Department of Hu-

KAUFMAN v. ALBIN

Cite as, Del.Ch., 447 A.2d 761

Del. 761

Samuel KAUFMAN, Plaintiff,
v.
William ALBIN, et al, Defendants.

Court of Chancery of Delaware,
New Castle County.

Submitted March 26, 1982.

Decided May 11, 1982.

3. Pretrial Procedure ⇐644

In stockholder derivative action, where plaintiff offered to amend complaint in order to meet corporation's argument, court would decline to grant dismissal and would grant plaintiff leave to amend complaint so as to plead with more specificity the alleged futility of making demand on corporation's board of directors. Chancery Court Rule 23.1, Del.C. Ann.

In stockholder derivative suit, defendants filed motions to dismiss. The Court of Chancery, New Castle County, Harnett, Vice Chancellor, held that: (1) service of process was properly obtained over certain individual defendants pursuant to directors' implied consent to substituted service of process statute, and (2) plaintiff would be granted leave to amend complaint so as to plead with more specificity the alleged futility of making demand on corporation's board of directors.

Motion denied.

On Defendants' Motions to Dismiss: Denied.

Joseph A. Rosenthal, Morris & Rosenthal, P. A., Wilmington, and Bertram Bronzaft, Garwin, Bronzaft & Gerstein, New York City, for plaintiff.

William T. Allen, Lewis S. Black, Jr., and David A. Jenkins, Morris, Nichols, Arsht & Tunnell, Wilmington, for defendant Philip A. Hunt Chemical Corp.

Jack B. Jacobs, and Bruce M. Stargatt, Young, Conaway, Stargatt & Taylor, Wilmington, and Philip L. Graham, Jr., and William Lucas, Sullivan & Cromwell, New York City, for defendants.

1. Pretrial Procedure ⇐687

In considering motion to dismiss, all well-pleaded allegations must be accepted as true, in order to determine whether plaintiff might recover under any reasonably conceivable set of circumstances susceptible of proof.

2. Corporations ⇐121(3)

Where cancellation of already existing options was subject to number of contingencies including acceptance of tender offer by large number of shareholders, that transaction, which was subject of suit, commenced with adoption of resolution on August 22, 1977, concerning treatment of such options, but was not consummated until October 8, 1977, when tender offer ended, and therefore, alleged wrong was a continuing wrong and any cause of action attacking it arose or accrued after September 1, 1977, the effective date of directors' implied consent to substituted service of process statute, and service of process was properly obtained thereunder. 10 Del.C. § 3114.

HARTNETT, Vice Chancellor.

The defendants filed motions to dismiss this stockholder derivative suit on several grounds, most of which arose from the claim that the Delaware corporate directors consent to substituted service of process statute did not permit valid service of process in this case. The contentions are all without merit and the motions must be denied.

I

[1] As is required in considering a motion to dismiss, all well-pleaded allegations must be accepted as true; *Danby v. Osteopathic Hospital Ass'n of Del.*, Del.Ch., 101 A.2d 308 (1953), *aff'd.*, Del.Sup., 104 A.2d 903 (1954); *Laventhol, Krekstein, Horwath & Horwath v. Tuckman*, Del.Sup., 372 A.2d 168 (1976); in order to determine whether plaintiff might recover under any reasonably conceivable set of circumstances sus-

ceptible of proof. *Klein v. Sunbeam Corp.*, Del.Supr., 94 A.2d 385 (1952).

The well-plead facts are: On August 22, 1977 the Board of Directors of Philip A. Hunt Chemical Corporation ("Hunt") reviewed the terms of a proposed tender offer for the shares of stock of Hunt made by Turner & Newell Industries, Inc. ("Turner"). The Board determined that the offered price was fair and voted unanimously to recommend to all stockholders of Hunt that they accept the offer and tender their shares to Turner. At this same meeting, the Board also considered the ramifications of the proposed tender offer on certain unexercised stock options held by Hunt employees, some of whom were officers, and resolved to accelerate the exercise date of all options held by employees. However, in order to avoid any potential "short-swing profit" charge, the options held by officers were given a different treatment. In consideration for the cancellation of these options, the officer-optionees were to receive the difference between the option price held on their options and the \$20 tender offer price.

Plaintiff contends that the individual defendant-directors wasted the corporation's assets by improperly permitting the officer-optionees to surrender their options in connection with the tender offer.

The resolutions which the Board enacted on August 22, 1977 were contingent upon the actual commencement by Turner of the proposed tender offer and also upon its consummation in compliance with the terms set by Turner. Section 6 of Turner's Office to Purchase listed a number of conditions which, if brought to fruition, could cause the tender offer to abort. Additionally, it was provided that if less than 2,950,000 shares (52% of the outstanding shares) were tendered, Turner could refuse to consummate the tender offer. The tender offer was made by Turner to the stockholders of Hunt commencing on September 12, 1977 and ending on October 3, 1977.

The tender offer was successfully consummated on October 3, 1977 when 98% of the outstanding shares were tendered and

Turner purchased 53.7% of the shares tendered. On that date the options belonging to Hunt's various officers were cancelled in accordance with the August 22, 1977 resolutions of the Board.

II

The first grounds argued in favor of defendants' motion to dismiss is that service of process was improperly obtained over the individual defendants pursuant to 10 Del.C. § 3114 (the directors implied consent to substituted service of process statute).

10 Del.C. § 3114 states in part:

"§ 3114. Service of process on nonresident directors, trustees or members of the governing body of Delaware corporations.

(a) Every nonresident of this State who after September 1, 1977, accepts election or appointment as a director, trustee or member of the governing body of a corporation organized under the laws of this State or who after June 30, 1978, serves in such capacity and every resident of this State who so accepts election or appointment or serves in such capacity and thereafter removes his residence from this State shall, by such acceptance or by such service, be deemed thereby to have consented to the appointment of the registered agent of such corporation (or, if there is none, the Secretary of State) as his agent upon whom service of process may be made in all civil actions or proceedings brought in this State, by or on behalf of, or against such corporation, in which such director, trustee or member is a necessary or proper party, or in any action or proceeding against such director, trustee or member for violation of his duty in such capacity, whether or not he continues to serve as such director, trustee or member at the time suit is commenced. Such acceptance or service as such director, trustee or member shall be a signification of the consent of such director, trustee or member that any process when so served shall be of the same legal force and validity as if served upon such director, trustee or member

within this State and such appointment of the registered agent (or, if there is none, the Secretary of State) shall be irrevocable...."¹

This section was enacted by 61 Del.Laws, Ch. 119 which provided: "This act shall apply only to causes of action arising or accruing subsequent to the effective date of this act," which was September 1, 1977.

Plaintiff concedes that 10 Del.C. § 3114 does not provide a means for service of process on three former directors of Hunt who were elected prior to September 1, 1977 and who resigned on October 6, 1977, because the statute by its terms is only effective as to nonresident directors who were elected after September 1, 1977 or who served as directors after June 30, 1978. Therefore, plaintiff has agreed to dismiss the complaint as to defendants Albin, Towbin and Waldron.

III

The primary issue remaining is whether this cause of action arose or accrued after September 1, 1977—the effective date of 10 Del.C. § 3114. The individual defendants contend that the alleged corporate wrong took place on August 22, 1977, the date of the adoption of the resolutions by Hunt's directors; that on that date the cause of action arose or accrued; and consequently service of process on the nonresident directors could not be accomplished pursuant to 10 Del.C. § 3114. It is conceded that the individual defendants are not amenable to service of process except pursuant to the provisions of that statute. According to the defendants, there was nothing more to be done by them after August 22, 1977, except to perform the ministerial act of receiving and cancelling the options, which had no real effect on the transaction, and therefore this cause of action arose or accrued on August 22, 1977, which was before 10 Del.C. § 3114 became effective.

Plaintiff counters by pointing out that, due to the existence of conditions depend-

ent upon subsequent acts of Hunt and Turner, the alleged wrong did not occur until October 3, 1977, the date the tender offer ended, and there could be no accrual of a cause of action until that date.

[2] No case squarely on point has been cited. The defendants, however, rely heavily on *Elster v. American Airlines*, Del.Ch., 100 A.2d 219 (1953), a case brought to cancel certain options, for the proposition that the alleged wrong occurred on August 22, 1977—the date of the adoption of the resolution. *Elster*, however, is distinguishable from the present case because in *Elster* the option or contract rights were fixed and finally established at the time the options were granted. In the present case the cancellation of already existing options was subject to a number of contingencies including the acceptance of the tender offer by a large number of shareholders.

I must therefore look to the general principles of law relating to the question of when a cause of action arises or accrues.

In 54 C.J.S., *Limitation of Actions* § 110 (p. 15) (1948), it is stated:

"Where a party's right depends on the happening of an event in the future, the cause of action accrues, and the statute of limitations begins to run, only at the time when the event happens."

In 51 Am.Jur.2d, *Limitation of Actions* § 127 (pp. 3 & 6) (1970), it is stated:

"If a right of action depends upon some contingency or a condition precedent, the cause of action does not accrue and the statute of limitations does not begin to run until that contingency occurs or the conditions precedent is complied with."

After August 22, 1977 the tender offer still had to be commenced and Hunt's stockholders had to be advised that the directors of Hunt recommended that the tender offer be accepted. This was done on September 12, 1977. Turner also had available many options which would have enabled it to terminate the tender offer if certain events took place before October 3, 1977.

A.2d 174 (1980).

1. The constitutionality of this statute was upheld in *Armstrong v. Pomerance*, Del.Supr., 423

Even more importantly, the tender offer was contingent upon it being accepted by the tendering of at least 52% of the outstanding shares of Hunt stock.

In *Folk*, *The Delaware General Corporation Law*, 487 (1967) it is stated:

"Accordingly, the circumstances of the case will determine whether the transaction is executed or continuing. If the action complained of requires stockholder approval, the transaction is not considered complete until the stockholders have approved it."

In *Lavine v. Gulf Coast Leaseholds*, Del. Ch., 122 A.2d 550 (1956) it was held that where exchanges of stock are contingent upon shareholder approval, the transaction is not completed until the shareholder vote takes place. In the present case, there was no shareholder vote denominated as such, but the acceptance of the tender offer by the tendering of the requisite number of shares was, for all practical purposes, the same as a vote by the stockholders of Hunt because, until the shareholders tendered the required number of shares (which was over 50% of all the outstanding shares) the transaction was subject to extinction.

I therefore find that the transaction which is the subject of this suit commenced with the adoption of the two resolutions on August 22, 1977 but was not consummated until October 3, 1977. The alleged wrong was therefore a continuing wrong and any cause of action attacking it arose or accrued after September 1, 1977, the effective date of 10 Del.C. § 3114.

IV

The individual defendants also argue that they had no notice, prior to the effective date of 10 Del.C. § 3114, on September 1, 1977, that they could be haled into a Delaware Court to defend the actions which took place on August 22, 1977, and therefore their constitutional rights of due process were violated. They cite *Shaffer v. Heitner*, 433 U.S. 186, 97 S.Ct. 2569, 53 L.Ed.2d 683 (1977), and *Armstrong v. Pomerance*, Del.Super., 423 A.2d 174 (1980). And, they argue that the doctrine of due

process precludes any retrospective application of 10 Del.C. § 3114.

The individual defendants base their argument of a violation of their right of due process on the assumption that, following the August 22, 1977, resolutions, nothing more was needed to be done to consummate the transaction. This was, however, not the case, as defendants well knew, the tender offer still had to be commenced, the stockholders had to be informed of the recommendation of the directors of Hunt that it be accepted, at least 52% of the shareholders of Hunt had to accept the tender offer and various other conditions set by Turner had to be met. The tender offer was not commenced until September 12, 1977, at which time the shareholders of Hunt were first informed of the tender offer, of the proposed treatment of the stock options, and that the directors of Hunt recommended acceptance of the tender offer. The transaction was not completed until October 3, 1977.

The notification of Hunt's stockholders occurred on September 12, 1977, and the tender offer was completed on October 3, 1977, both of which dates were after September 1, 1977, the effective date of 10 Del.C. § 3114, and therefore there was no retroactive application of 10 Del.C. § 3114 or lack of due process.

V

Defendants also argue that certain officers who were not directors but were also optionees and who, it is conceded, are immune from service of process under Delaware law, are indispensable parties to this litigation because rescission of their option contracts is requested. Plaintiff, however, has agreed to amend the complaint to delete as defendants all the officers who were optionees, with the exception of Messrs. Bonniwell and Belmont who were also directors.

Defendant-Hunt has also moved to dismiss the complaint on grounds that plaintiff's failure to make a demand upon the Board of Directors of Hunt prior to the

instigation of this action cannot be legally excused under the circumstances existing when the suit was filed. Hunt points out that Chancery Court Rule 23.1 requires that the complaint allege "with particularity" any efforts a plaintiff has made in order to have the Board of Directors instigate an action and to also specifically plead any reasons for failure to make such a demand.

[3] Plaintiff, while sharply disputing Hunt's allegation that the complaint lacks adequate specificity, has nevertheless offered to amend the complaint in order to meet Hunt's arguments. I therefore decline to grant a dismissal for failure to comply with Rule 23.1 at this time and grant plaintiff leave to amend the complaint so as to plead with more specificity the alleged futility of making a demand on Hunt's Board of Directors.

The individual defendants' motion to dismiss is therefore denied. Hunt's motion to dismiss is also denied conditioned upon the plaintiff's amendment of the complaint in order to more fully comply with Chancery Court Rule 23.1. The complaint should also be amended to exclude as defendants the three former directors who resigned on October 6, 1977, the officers of Hunt who are not directors and also the unnamed officers of Hunt who were originally designated as defendants.



STATE OF SOUTH CAROLINA)

COUNTY OF GREENVILLE)

Brian P. Menezes,)

Plaintiff,)

v.)

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga, Stephen)
B. Duerk, WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P., WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC,)

Defendants.)

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

FILED-CLERK OF COURT
GREENVILLE CO. S.C.
DATE: 8/10/08

2008 AUG - 8 P 4: 53

WL Ross & Co. LLC, Wilbur L. Ross,)
Jr., Michael J. Gibbons, David H. Storper,)
David L. Wax, Joseph L. Gorga,)
WLR Recovery Fund II, L.P.,)
WLR Recovery Fund III, L.P., WLR)
Recovery Associates II LLC, and WLR)
Recovery Associates III LLC;)

Counterclaimants,)

v.)

Brian P. Menezes,)

Counterclaim Defendant.)

**REPLY MEMORANDUM IN SUPPORT OF MOTION FOR JUDGMENT ON THE
PLEADINGS OR, ALTERNATIVELY, MOTION FOR SUMMARY JUDGMENT**

PRELIMINARY STATEMENT

As framed by the parties' briefs and the questions asked by the Court at the end of the July 31, 2008 hearing, Defendants' Motion boils down to a single decisive issue: when did Plaintiff's claims challenging the merger at issue first accrue? See Pl's. Mem. in Opp. to Defs.' Mot. to Dismiss ("Pl's. Mem.") at 1. It is undisputed that this is a question of law for the Court.

Defendants contend that based on well-settled Delaware law, Plaintiff's claims accrued when the defendant board members approved the terms of the merger agreement on August 29, 2006. If so, those claims were released on September 28, 2006 when Plaintiff executed his broad Settlement Agreement and Release of All Claims (the "Release") at the conclusion of a prior dispute between the parties. Plaintiff, on the other hand — relying on non-binding and inapposite authority — contends that his claims accrued when the merger closed on October 20, 2006 and he allegedly suffered damages, and thus fall outside the scope of the September 28, 2006 Release. See, e.g., id. at 1, 8, 9, 12. Plaintiff's contention is flat wrong.

The current binding authorities from the Delaware courts, addressing this "accrual" issue and speaking as clearly as anyone ever could wish, hold that claims accrue "as soon as the wrongful act occurs," regardless of whether or when the plaintiff incurs a loss. See Albert v. Alex. Brown Mgmt. Servs., Inc., Nos. 762-N, 763-N, 2005 Del. Ch. LEXIS 100, at * 58-60 (Del. Ch. June 29, 2005). Indeed, Delaware courts have specifically and emphatically rejected Plaintiff's core argument:

In essence, the plaintiffs argue that they could not have brought suit until they had suffered a harm This is incorrect. **The law in Delaware is crystal clear that a claim accrues as soon as the wrongful act occurs.** This is so because the plaintiffs were harmed as soon as the alleged wrongful acts occurred. **Whether or not the plaintiffs could have sued for damages is not dispositive** as to whether the claim accrued since, as soon as the wrongful acts occurred, the plaintiffs could have sought injunctive relief. ... **The court reiterates that a claim accrues at the time of the alleged wrongdoing, and not when the plaintiff suffered a loss.**

Id. (emphasis added) (attached as Exhibit 1).¹

¹ While the parties agree that Delaware law controls the question of when Plaintiff's Delaware-based claims accrued, Albert is consistent with South Carolina law. See Stephens v. Draffin, 327 S.C. 1, 5, 488 S.E.2d 307, 309 (1997) (holding that "cause of action accrues at the moment when the plaintiff has a legal right to sue on it").

The alleged wrongdoing here occurred when the Defendant board members approved the merger agreement. In re Beatrice Co., Inc. Litig., 522 A.2d 865, 1987 WL 36708 *3 (Del. Mar. 24, 1987) (holding that when a merger is challenged, the claim arises, and hence the plaintiff has standing to sue, “at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged”). The subsequent release therefore covers all of Plaintiff’s claims and requires that the claims be dismissed in their entirety with prejudice.

ARGUMENT

Consistent Delaware authority, including Supreme Court holdings from as recently as this summer, amply confirm that Plaintiff’s alleged claims accrued upon the supposedly wrongful act—the Defendants’ approval of the merger agreement. See, e.g., Int’l Bhd. Teamsters v. Coca-Cola Co., No. 601,2007, 2008 WL 2484587, at *1 (Del. June 20, 2008) (affirming entire opinion of Court of Chancery, filed sub nom. In re Coca-Cola Enters., Inc. S’holders Litig., No. 1927-CC, 2007 Del. Ch. LEXIS 147 (Del. Ch. Oct. 17, 2007), including rationale that “a plaintiff’s cause of action accrues at the moment of the wrongful act—not when the harmful effects of the act are felt”) (Supreme Court and Court of Chancery opinions attached as Exhibit 2).² Nothing in Plaintiff’s arguments manages to avoid this clear teaching.

In fact, likely recognizing the flaws in his “accrual” argument, Plaintiff has resorted to the desperate argument that his own “subjective intent” or “unilateral mistake” could be grounds for avoiding the release. But these arguments too fail as a matter of law.

² Contrary to Plaintiff’s suggestion, there is “no provision under the Delaware Rules of Court restricting the citation of unpublished opinions for precedential value in opinions. To the contrary, rules expressly permit the citation of unpublished opinions in briefs submitted to various Delaware state courts for this purpose.” Wisdom Imp. Sales Co., L.L.C. v. Labatt Brewing Co., 339 F.3d 101, 115 n. 14 (2d Cir. 2003) (citing Del. R. Sup. Ct. 14(g)(ii); Del. R. Com. Pl. Ct. 107(f)); see also New Castle County v. Goodman, 461 A.2d 1012, 1013 & n.1 (Del. 1983) (same).

I. Delaware Law Is “Crystal Clear” That Plaintiff’s Alleged Claims Accrued, Not When Plaintiff Allegedly Suffered Loss But When Defendants’ Approved The Merger.

Plaintiff’s argument hangs on an erroneous assumption that his alleged claims could accrue only when Plaintiff experienced his alleged damages. See, e.g., Pl.’s Mem. at 1 (“Indeed, how could [a claim accrue] since there are not damages until the merger takes place?”), 8 (“a claim for ‘damages’ cannot ‘accrue’ until there are in fact ‘damages’”), 12 (“since plaintiff had no damages until the consummation of the merger ... his claim for damages for breach of fiduciary duty did not accrue until that day.”). The assumption is contrary to Delaware law and, moreover, is not supported by Plaintiff’s cited cases, which are irrelevant, inapposite and overwhelmed by the great weight of clear, current and binding authorities, which consistently hold that an alleged claim accrues upon the accomplishment of the alleged wrongful act and does not wait for any resulting loss or harm.

A. The Delaware Authorities Are Clear And Consistent.

As shown in the Defendants’ opening Memorandum, the Delaware courts have repeatedly and authoritatively held that a cause of action such as Plaintiff’s accrues when the alleged wrongful conduct occurs; accrual does not depend on plaintiff incurring a compensable loss. See, e.g., Wal-Mart Stores, Inc. v. AIG Life Ins. Co., 860 A.2d 312, 319 (Del. 2004) (holding that a cause of action for breach of fiduciary duty accrues “at the time of the wrongful act”). Over and over, the courts have rebuffed—with evident impatience—plaintiffs arguing that a claim could not accrue until there were damages. See Coca-Cola Enters., Inc. S’holder Litig., 2007 WL 3122370, at *5 n. 39 (quoting previous authorities: “The court reiterates that a claim accrues at the time of the alleged wrongdoing, and not when the plaintiff suffered a loss.”), aff’d sub nom. Int’l Bhd. Teamsters v. Coca-Cola Co., 2008 WL 2484587, at *1. The rule is “crystal

clear.” Albert, 2005 Del. Ch. LEXIS 100, at *59. The claims accrue with the misconduct, and “[w]hether or not the plaintiffs could have sued for damages is not dispositive[.]” Id.

Thus, when a plaintiff’s claims challenge the terms of a merger, those claims accrue at the time the board approves the supposedly unfair terms. Contrary to Plaintiff’s argument here, the claims for such alleged misconduct are not somehow put “on hold” until the merger is consummated and its effects can be assessed; rather the claim accrues when the merger terms are fixed. See, e.g., Brown v. Automated Mktg. Sys., Inc., No. 6715, 1982 WL 8782, at *2 (Del. Ch. Mar. 22, 1982) (holding that claim accrued when board approved merger agreement and did not wait for shareholder approval: “it is the fixing of the terms of the transaction which will be finalized by the consummation of the merger which provides the foundation for the suit”); see also Omnicare, Inc. v. NCS Healthcare, Inc., 809 A.2d 1163, 1169 (Del. Ch. 2002) (holding claim for breach of fiduciary duties arose out of the directors’ decision to approve the merger); In re Beatrice Co., 522 A.2d 865, 1987 WL 36708, at *3 (holding that claim challenging merger arose “at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged”).

For this reason, Plaintiff’s argument that supposed conditions or contingencies in the merger agreement might have precluded some of the alleged damages, see Pl’s. Mem. at 7, is irrelevant. The alleged wrongful act here was the fixing of the allegedly unfair merger terms, which was accomplished when the board approved those terms. At that point, all that remained was for the supposedly unfair terms to be carried out.³ Thus, at that point, the claims had accrued. See Brown, 1982 WL 8782, at *2 (rejecting argument that no wrong occurred until the merger was voted on and approved).

³ In fact, Plaintiff’s “contingencies” argument is belied by his own Complaint. The Complaint repeatedly alleges that, once the merger agreement was entered, the approval process was a mere formality. See Compl. at ¶¶ 22, 23, 24.

Additionally, Plaintiff's attempts to distinguish the Delaware authorities cited above are unavailing. Trying to skirt the cases specifically holding that claims accrue as soon as a board approves allegedly unfair merger terms, Plaintiff asserts that these cases sought injunctive relief, not damages. But under the Delaware authorities this is a distinction without a difference. As soon as the wrongful act occurs (e.g. the board action approving a merger), the claims based on that act accrue, whether for an injunction to stop the act's effects or for damages after the effects have been felt. See, e.g., Albert, 2005 Del. Ch. LEXIS 100, at *59 ("Whether or not the plaintiffs could have sued for damages is not dispositive as to whether the claim accrued since, as soon as the wrongful acts occurred, the plaintiffs could have sought injunctive relief."). In short, Plaintiff's supposed grounds for distinguishing these cases hangs on the same misapprehension that plagues Plaintiff's entire argument—namely, Plaintiff's erroneous notion that time of accrual is determined by when damages arise, rather than when the alleged misconduct occurs. Ernest L. Folk, III et al., Folk on Delaware General Corporation Law § 327.3 (5th ed. 2006) ("[T]he determinative issue is when the specific acts of alleged wrongdoing occurred, not when their effect is felt.").

Similarly, Plaintiff incorrectly asks this Court to ignore such controlling authority as Brown and Beatrice because those cases concern issues of shareholder "standing," rather than statute of limitations or release issues. Here as well, Plaintiff's proposed "distinction" is meaningless. In each of those cases, the Delaware court had to identify when alleged wrongdoing occurred in the case of a disputed merger—because the courts recognized that the claim accrued when the alleged wrongdoing occurred, and a plaintiff who purchased stock after the claim accrued would not have standing to press the claim. In each case, the court concluded that the alleged wrongdoing giving rise to the claim was the board's approval of the disputed

merger and not some later effect or result of that approval. These holdings translate directly to this case and mandate that Plaintiff's claims—like the claims in Brown, Beatrice and the other Delaware merger cases—accrued when the Defendants approved the challenged merger terms and no later.

In fact, Plaintiff's supposed "distinction," if it were really the law, would lead to an absurd result. It would mean that someone who purchased shares after a merger was announced, but before it closed, would have standing to claim damages after the merger closed, even though they would not have standing to seek an injunction stopping the merger before closing. This would be illogical, and it is not the law.

Rather, the clear Delaware law holds that the claims accrued when the Defendant board members approved the merger terms. This occurred before Plaintiff signed his broad release. Thus Plaintiff's claims all fail as a matter of law.

B. Plaintiff's Cited Cases Are Irrelevant And Inapposite.

Against the Defendants' crystal clear Delaware authority, Plaintiff hangs his arguments on three non-binding and irrelevant cases. None of them negates the reasoning above or warrants allowing Plaintiff to avoid the effect of his Settlement Agreement and Release.

Plaintiff's reliance on Baron v. Allied Artists Pictures Corp., 717 F.2d 105 (3d Cir. 1983) is misplaced for the simple reason that the case addresses not Delaware law but federal law. The Baron decision concerns a federal cause of action and addresses when, under federal law, that federal cause of action would have accrued. See Baron, 717 F. 2d at 108 ("[W]e agree ... that when the cause of action ... accrued ... is in this case a federal law question."). It does not speak in any way to the accrual of the state-law causes of action in this case, and Plaintiff is therefore mistaken to suggest that Baron has any effect here. Moreover, contrary to Plaintiff's suggestion, a federal case such as Baron would not be controlling here even if it did speak to the issues on

this Motion; the controlling authority here is that of the Delaware state courts. Fiat Motors of N. Am., Inc. v. Wilmington, 619 F. Supp. 29, 32 (D. Del. 1985) (“In the absence of an authoritative pronouncement from the state’s highest court,” the federal court’s duty is merely “to predict how the [state] court would rule.”) (citation omitted; emphasis added).⁴

Likewise, Dofflemeyer v. W. F. Hall Printing Co., 558 F. Supp. 372 (D. Del. 1983), fails to help Plaintiff because, among other reasons, this 25-year old federal case is simply out of step with subsequent Delaware Supreme Court precedent. See, e.g., E.I. DuPont de Nemours & Co. v. Admiral Ins. Co., 711 A.2d 45, 60 (Del. 1995) (disregarding a decision by the Court of Appeals for the Third Circuit where that decision was inconsistent with current Delaware law). In Dofflemeyer, the trial court based its reasoning explicitly on the assumption that the plaintiffs’ claim could not accrue until the plaintiffs had suffered injury. See Dofflemeyer, 558 F. Supp. at 379 (“Until [merger was consummated] the transaction which was the subject of the suit was not accomplished and there had been no injury.”). The assumption is 180 degrees contrary to more recent Delaware Supreme Court and Chancery Court decisions, which provide the controlling law here, and, as shown above, reject any notion that damages are necessary before a claim accrues. See Albert, 2005 Del. Ch. LEXIS 100, at *60 (“The court reiterates that a claim accrues at the time of the alleged wrongdoing, and not when the plaintiff suffered a loss.”).

Finally, Plaintiff’s citation to Kaufman v. Albin, 447 A.2d 761 (Del Ch. 1982) is unavailing because the case did not concern a negotiated merger, as this case does, but rather just a tender offer. As the name suggests, a tender offer is just that—an offer.⁵ Thus, in Kaufman,

⁴ According to West’s KeyCite service, Baron has never been cited in a single Delaware State court opinion.

⁵ Tender offers and negotiated mergers are not equivalents under Delaware law. See, e.g., In re Pure Res., Inc., 808 A.2d 421, 437 (Del. Ch. 2002) (noting that tender offers are not even addressed by the Delaware General Corporation Law); Solomon v. Pathe Commc’ns Corp., 672 A.2d 35, 39 (Del. 1996) (explaining that the fairness of certain tender offers is evaluated by a different standard than that applied to “cash-out mergers”). In Kaufman, because the transaction took the form of a tender offer, the target company’s board did not appoint a special

there was no transaction at all until the tender offer succeeded (i.e., was accepted by the sellers), and the ongoing offer was deemed a “continuing wrong.” Id. at 764 (“The alleged wrong was therefore a continuing wrong.”). Here, by contrast, the complete merger terms were settled by agreement and approved by the Defendants, and, consequently, Delaware law is clear that there is not a continuing wrong. See Brown, 1982 WL 8782, at *2 (holding that, in claims challenging terms of merger, it is the fixing of the merger terms that gives rise to the action, not the consummation of the merger, and “there is no continuing wrong”).

In weighing Plaintiff’s three cited decisions (all from the early 1980s and only one of them actually a Delaware case) against the numerous current decisions that the Defendants have presented, it is telling to examine how the leading Delaware treatise has changed its language over time. The treatise is Folk on Delaware General Corporation Law. In the 1967 edition, as cited by the Kaufman court, Folk maintained that “if the action complained of requires stockholder approval, the transaction is not considered complete until the stockholders have approved.” See Kaufman, 447 A.2d at 764. Today, however, the Folk treatise no longer contains that statement. Rather, keeping up with the Delaware precedents that Defendants have cited, the 2006 edition of Folk holds that (i) it is the specific wrongful acts, and not the effect, that determine when a claim accrues, and (ii) Delaware law has held a proposed merger to be consummated upon the fixing and announcement of its terms, without waiting for subsequent stockholder approval:

Generally, the determinative issue is when the specific acts of alleged wrongdoing occurred, and not when their effect is felt. Therefore the circumstances of the case will determine whether the transaction is executed or

(continued...)

committee or negotiate terms with the acquirer (as here), but rather merely voted to recommend that stockholders accept a tender offer – advice the stockholders were free to follow or ignore. Kaufman, 447 A.2d at 762.

continuing. For instance, an offer made by the corporation to certain of its stockholders to exchange one class of stock for another, which was specifically conditioned on approval by the corporation's other stockholders, was held not to be completed until stockholder approval was obtained. On the other hand, **both a proposed merger and a proposed supermajority voting provision have been held to be consummated when their terms were fixed and announced by the board of directors, and not to be continuing transactions up to the time of stockholder approval.**

Folk on Delaware General Corporation Law § 327.3 (5th ed. 2006)

In short, Folk recognizes what Plaintiff has failed to see. The negotiated merger at issue here was consummated and Plaintiff's alleged claims accrued at the time the merger terms were fixed and approved by the Defendants.

II. Plaintiff's Attempt To Re-Write The Settlement Agreement And Release According To His Own Alleged Subjective Intent Is Impermissible As A Matter Of Law.

In a sign that Plaintiff knows full well the flaws of his "accrual" argument, Plaintiff has resorted to asserting his own personal understanding of the Release—as if his personal thoughts could trump the plain language. For example, without reference to any specific provision in the Release, Plaintiff's Opposition Memorandum claims that the Release "did not" have "anything to do with the merger" of SCI and FITG and that the "Release relates solely to litigation that [P]laintiff commenced in 2006." See Pl's. Mem. at 2. Likewise, Plaintiff tries to explain the phrase "arising prior to the execution of this Confidential Settlement Agreement" appearing in sub-paragraph (6) of § 7 by claiming the "obvious point on [P]laintiff's part was to preserve shareholder claims regarding the upcoming merger in the event it was unfair." Id. at 3. This attempt to re-write the broad Release language cannot succeed. It is the plain language that controls here, and that language clearly and unambiguously releases all of Plaintiff's claims.

A. The Broad Release Language Must Be Construed And Applied By Its Plain Terms And Without Considering Extrinsic Evidence Or Any Party's Subjective Intent.

While it is undisputed that Delaware law governs when Plaintiff's claims accrued, the construction of the Release is governed by South Carolina law. (Release § 29.) The law in South Carolina is well settled that one party's subjective interpretation of a contract is irrelevant when a court is constructing the contract's terms. M & M Group, Inc. v. Holmes, Op. No. 4427 (S.C. Ct. App. filed July 15, 2008) (Shearouse Adv. Sh. No. 30 at 29, 35) (stating "[p]arties are governed by their outward expressions and the court is not free to consider their secret intentions"); Silver v. Abstract Pools & Spas, Inc., 376 S.C. 585, 593, 658 S.E.2d 539, 543 (Ct. App. 2008) (party to contract "is not permitted to reinterpret written contract terms midstream because he is unhappy with the contract he executed"); Ecclesiastes Prod. Ministries v. Outparcel Assocs., 374 S.C. 483, 498, 649 S.E.2d 494, 501 (Ct. App. 2007) ("Parties [to a contract] are governed by their outward expressions and the court is not at liberty to consider their secret intentions."); Bannon v. Knauss, 282 S.C. 589, 593, 320 S.E.2d 470, 472 (Ct. App. 1984) ("Interpretation of the contract is governed by the objective manifestation of the parties' assent at the time the contract was made. It does not depend on the subjective, after the fact meaning one party assigns to it.") (internal citation omitted).⁶

Moreover, this rule applies to releases just as it does to any other type of contract. The South Carolina Federal District Court specifically applied this principle in interpreting the

⁶ To rebut certain serious factual inaccuracies in Plaintiff's Response, the Defendants submitted the Affidavit of Matt Johnson. Mr. Johnson's Affidavit, however, is not relevant to interpreting the unambiguous Release, and should not be considered for that purpose. Now, Plaintiff's attorney, Mr. Herlong, has asked for leave to file his own affidavit. But the lengthy factual rendition provided by Mr. Herlong at the July 31, 2008 Hearing, and presumably in any rebuttal affidavit he might submit, is precisely the type of extrinsic evidence that must not be considered on this Motion. Moreover, to the extent that Mr. Herlong may contend that his testimony is relevant or necessary in construing the Release, Mr. Herlong has made himself a witness, which would violate the witness advocate rule. See Collins Entm't, Inc. v. White, 363 S.C. 546, 563-64, 611 S.E.2d 262, 271 (Ct. App. 2005) (affirming order that attorney could participate as counsel or as witness but not both).

provisions of a general release in Wilson Group, Inc. v. Quorum Health Res., 880 F. Supp. 416 (D.S.C. 1995):

[The plaintiff] argues its representatives who negotiated the 1991 management agreement did not intend to provide a general release. This argument would fail for two reasons. First, the subjective intention of parties to a clear and unambiguous contract do not control its meaning. Any other principle would allow a party to avoid the legal effect of a release by claiming it did not believe it was releasing its rights. Second, both parties were represented by counsel in the negotiation of the release and are presumed to understand its legal ramifications.

880 F. Supp. at 426 n.9; see also S. Glass & Plastics Co. v. Duke, 367 S.C. 421, 428, 626 S.E.2d 19, 22 (Ct. App. 2005) (holding that a “release is a contract, and the scope of a release is gathered by its terms”); Campbell v. Bi-Lo, Inc., 301 S.C. 448, 451, 392 S.E.2d 477, 479 (Ct. App. 1990) (stating that “[i]n determining the nature of the Release, we look first to the instrument itself”).

Therefore, because everyone agrees that the Release language is plain and not ambiguous, see Pl’s. Mem. at 2 (agreeing that the release language is “plain”), it is the language alone that determines the release’s meaning and effect. See Ellis v. Taylor, 316 S.C. 245, 248, 449 S.E.2d 487, 488 (1994) (holding that, where “the language of a contract is plain and capable of legal construction, that language alone determines the instrument’s force and effect”). Construction of the contract is a question of law for the Court and the express language of the Settlement Agreement alone must determine the document’s force and effect. Ellie, Inc. v. Miccichi, 358 S.C. 78, 93, 594 S.E.2d 485, 493 (Ct. App. 2004). As Plaintiff himself has correctly admitted, the circumstances surrounding the Release are irrelevant. See Pl’s. Mem. at 2 (“The circumstances behind the release are not relevant given its plain language.”). The only thing to consider is what the Release actually says.⁷

⁷ See also Bowers v. S.C. Dep’t of Transp., 360 S.C. 149, 153, 600 S.E.2d 543, 545 (Ct. App. 2004) (holding that because “the Release unambiguously sets forth the contracting parties’ intent, we are bound by that

B. The Broad Release Language Covers All Of Plaintiff's Claims.

What the Release says is simply that Plaintiff has released all of his claims in existence as of the Release date. Thus, Plaintiff has released all of the claims at issue here.

Contrary to Plaintiff's argument, the Release is not limited to claims in the original lawsuit. Rather, the Release language found at § 7 of the Settlement Agreement says in italics on the top of each page that it is a "Settlement Agreement and Release of All Claims." The first paragraph of § 7 states that Plaintiff "does hereby release, acquit and forever discharge" the Defendants from "any and all manner of actions, causes of action, suits, claims,...and debts, whatsoever, in law or in equity, whether known or unknown...which Plaintiff either has had or now has against the Released Parties for or related to any matter or thing whatsoever from the beginning of time up to and including the date of execution hereof." No clearer statement could be made as to the broad, all-encompassing aspect of the release.

Use of the term "whatsoever" alone demonstrates the broad and all-encompassing coverage of the releases given by Plaintiff in first paragraph of § 7, without even considering the phrase "from the beginning of time up to and including the date of execution" of the Settlement Agreement. See State v. Holman, 14 S.C.L. 124, 125, 3 McCord 306, 308 (1825) (broadly construing the phrase "any matter or thing whatsoever" appearing in a South Carolina statute); Schuck v. Shook, 10 N.Y.S. 935, 936, 1890 N.Y. Misc. LEXIS 1073 (N.Y. Sup. Ct. 1890) (finding "word 'whatsoever' has a very broad and comprehensive meaning. Among other definitions given to the word by Webster are 'one thing or another,' and 'anything that may be,'

(continued...)

clearly expressed intent without resort to extrinsic evidence"); Gordon Farms, Inc. v. Carolina Cinema Corp., 294 S.C. 158, 160, 363 S.E.2d 235, 236 (Ct. App. 1987) (holding the "[p]arties to a contract have a right to make their own contracts, and when the contracts they make are capable of clear interpretation, the court's province is confined to the enforcement of the contract as written; the court cannot exercise its discretion as to the contents of contract or substitute its own construction for an agreement clearly entered into between the parties").

etc..."); 94 C.J.S. Whatsoever (1956) (stating the word "whatsoever" has a very "broad and comprehensive" meaning and is often defined as "all that," "no matter what" or "anything that may be"). Moreover, the Parties went even further in the first paragraph of § 7, expressly stating that "[i]t is Plaintiff's intention to release all rights and claims that he may lawfully release." (emphasis added).

Additionally, "without in any way limiting the generality" of the release language in the first paragraph of § 7, the second paragraph of § 7 states the release "applies to and waives: ... (6) any claim based upon or as an owner of any stock or interest in any of the Released Parties arising prior to the execution of this Confidential Settlement Agreement." Moreover, contrary to Plaintiff's contention that the Release was limited to claims in Plaintiff's original lawsuit, subparagraph (8) of the second paragraph in § 7 provides that the release "applies to and waives" all claims "made or which may have been made in the Underlying Lawsuit or Amended Complaint." This provision demonstrates that a claim did not have to have been actually made in the underlying lawsuit, to be released, only that the claims existed ("may have been made") at the time the Release was executed.

In short, Plaintiff's contentions regarding his or his lawyer's subjective intent in executing the Release or what they thought the Release meant are completely irrelevant under South Carolina law. The Release covers all claims existing as of the time Plaintiff signed it and, as shown above, that includes all of his claims in this action.

III. Plaintiff's Last-Ditch "Mistake" Argument Also Fails As A Matter Of Law.

As a final attempt to avoid the release, Plaintiff's attorney, at the July 31 hearing, implied that Plaintiff's understanding of the Settlement Agreement and Release was a "mistake." This last-ditch argument fails as well, because (i) there are no grounds here for allowing a supposed "unilateral mistake" to negate Plaintiff's release, and (ii) in any event, Plaintiff could not rescind

without first returning the consideration (\$576,550) that Plaintiff received in exchange for his release, and Plaintiff has not done so.

A. Unilateral Mistake Regarding The Law Or Legal Effect Of A Contract Is Not Grounds For Avoiding Or Rescinding The Contract.

As a general rule, unilateral mistake is not by itself grounds to challenge or rescind a contract. Regions Bank v. Schmauch, 354 S.C. 648, 662, 582 S.E.2d 432, 440 (Ct. App. 2003). Plaintiff has not pled any of the facts necessary to support the only exceptions to this rule, *i.e.*, that his purported mistake in executing the Release (1) was "induced by fraud, deceit, misrepresentation, concealment, or imposition of the party opposed to rescission and without negligence on the part of the party claiming rescission," or (2) that his purported mistake was "accompanied by very strong and extraordinary circumstances which would make it a great wrong to enforce the agreement." Truck S., Inc. v. Patel, 339 S.C. 40, 49, 528 S.E.2d 424, 429 (2000); *see also* Alderman v. Bevin, 233 S.C. 545, 550-56, 106 S.E.2d 385, 388-91 (1958) (holding one party's unilateral mistake cannot be used to rescind or void effect of contract); Richardson's Rests., Inc. v. Nat'l Bank of S.C., 304 S.C. 289, 297, 403 S.E.2d 669, 673 (Ct. App. 1991) (holding that "[a]n erroneous impression taken up from the suggestion of the party's own mind does not relieve him from the contract).

In Smothers v. U.S. Fidelity & Guaranty Co., 322 S.C. 207, 470 S.E.2d 858 (Ct. App. 1996), the Court of Appeals refused to reform or rescind a release where the parties claim to have misunderstood the legal effect of the release under South Carolina law:

It is the general rule that a court of equity will not, where a mistake of law is disclosed, grant relief from the consequences thereof in the absence of fraud or undue influence. Nor will relief be granted where the complaining party took measures to secure knowledge as to the state of the law and, being misinformed, placed himself in the prejudicial situation of which he later complains. Everyone is presumed to have knowledge of the law and must exercise reasonable care to protect his interests.

Id. at 210-11, 470 S.E.2d at 860 (citations omitted). While the courts will “protect those who are unable to protect themselves and those of whom an undue advantage has been taken,” Plaintiff is neither “ignorant [nor] unwary” as the law requires. Id. at 211, 470 S.E.2d at 860. As in Smothers, Plaintiff was “represented by an attorney and had an opportunity to consult with [his] attorney prior to entering into the release.” Id. In short, Plaintiff has not alleged any grounds for finding unilateral mistake—and the simple reason for this is that there are no such grounds. See In re Estate of Holden, 343 S.C. 267, 279, 539 S.E.2d 703, 710 (2000) (holding parties’ contention that “they did not realize the legal consequences of their disclaimers...was a mistake of law and is not subject to equitable relief”).

B. Plaintiff May Not Challenge The Release On The Grounds Of Fraud Or Mistake Because He Has Not Returned All Of The Consideration He Received.

Finally, even if Plaintiff had pled the factual circumstances necessary to create an exception to the general rule against rescission for unilateral mistake, “it is well settled that one who seeks to avoid the effects of a release must first return or tender consideration paid therefore [sic].” State Farm Mut. Auto. Ins. Co. v. Turner, 303 S.C. 99, 102, 399 S.E.2d 22, 23 (Ct. App. 1990); see also Maw v. McAlister, 252 S.C. 280, 289, 166 S.E.2d 203, 207 (1969) (holding that a claim for rescission could not be asserted where “plaintiff failed to tender a return of the cash portion of the consideration for the release before seeking its rescission”); Dunaway v. United Ins. Co. of Am., 239 S.C. 407, 410, 123 S.E.2d 353, 354 (1962) (holding that “one who seeks to avoid the effect of a release must first return or tender the consideration paid therefor . . . ‘this rule obtains even though the contract of settlement was induced by the fraud or false representations of the other party’”) (citation omitted); Green v. Sparks, 232 S.C. 414, 430, 102 S.E.2d 435, 444 (1958) (“Ordinarily, the consideration received for a release should be returned or tendered before an action [seeking rescission] is instituted, or contemporaneously with the

institution thereof.”) (citation omitted). Plaintiff has not tendered or returned (or attempted to tender or return) the nearly \$600,000 that he was paid in exchange for the Release; thus he may not now seek rescission.

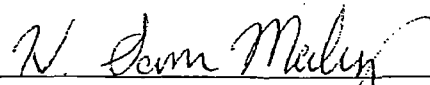
CONCLUSION

Defendants’ Motion frames a threshold issue of law that will either (i) dispose of the Plaintiff’s case entirely or (ii) eliminate as a matter of law the Defendants’ defense of release as well as their counterclaim for breach of the release.⁸ The Delaware courts have spoken clearly to this issue of law, holding that claims such as Plaintiff’s arise when the merger terms are fixed and not when the merger ultimately closes. Plaintiff’s position that claims are deferred until loss or damages arise has been repeatedly and emphatically rejected. The governing law is crystal clear, and under that law Plaintiff’s claims all fail. Thus, for the reasons stated herein, as well as in the Defendants’ opening Memorandum and at the July 31, 2008 Hearing, Defendants respectfully request that their motion be granted and that judgment be entered against Plaintiff and in favor of Defendants.

⁸ Defendants concede that if the Court finds that Plaintiff’s claims accrued after he signed the Release, a ruling denying Defendants’ Motion would mean that the affirmative defense of Release and Defendants’ counterclaim for breach of release should be stricken (stated different, Defendants concede that a denial of their Motion would result in the granting of Plaintiff’s Motion to Dismiss Defendants’ Counterclaim, albeit on grounds different than those raised by Plaintiff). Because the law clearly favors a finding that the Release bars Plaintiff’s claims, however, Defendants’ Motion should be granted and Plaintiff’s case should be dismissed.

Dated: August 8, 2008

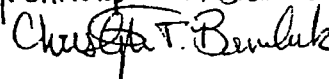
Respectfully submitted,



H. Sam Mabry, III
HAYNSWORTH SINKLER BOYD, P.A.
Two Liberty Square - 11th Floor
75 Beattie Place
Greenville, South Carolina 29601
Telephone: (864) 240-3221
Facsimile: (864) 240-3300

Signed w/ permission by: Christopher T. Brumback

OF COUNSEL:



Michael J. McConnell
Joseph E. Finley
JONES DAY
1420 Peachtree Street, N.E.
Suite 800
Atlanta, GA 30309-3053
Telephone: (404) 521-3939
Facsimile: (404) 581-8330

Counsel for all Defendants and
Counterclaimants

EXHIBIT 1

LEXSEE 2005 DEL. CH. LEXIS 100



Caution

As of: Aug 07, 2008

TODD ALBERT, JOSEPH M. BRYAN, JR., KEVIN CALDERWOOD, KATHERINE D. CROTHALL, SCOTT W. FRAZIER, FU FAMILY REVOCABLE TRUST, ROBERT B. GOERGEN, SR., ROBERT G. GOERGEN, JR., TODD A. GOERGEN, HASAN 1995 LIVING TRUST, WAI YAN HO, WILLIS JAMES HINDMAN, JOHNSON FAMILY LIVING TRUST, MICHAEL R. KIDDER REVOCABLE TRUST, MARK AND ANN KINGTON, JEFFREY A. KOSER, MARLENKO INC., ELAINE MCKAY FAMILY, LP, DAVID MIXER, MRW TRUST, JAMES MURRAY, JIM K. OMURA 1996 TRUST, JENNIFER OWEN AND MICHAEL J. ROSS, NICHOLAS PEAY, DOUGLAS G. SMITH, FREDERICK G. SMITH, JANE VEI-CHUN SUN, MARK WABSCHALL, KAREN L. WALSH, WARMEHNOVEN 1995 CHILDREN'S TRUST, YAN 1996 REVOCABLE TRUST, BARBARA J. ZALE, and CHARLES A. ZIERING, Plaintiffs, v. ALEX. BROWN MANAGEMENT SERVICES, INC.; DEUTSCHE BANK SECURITIES, INC.; DEUTSCHE BANK, AG; RICHARD HALE; GARY FEARNOW; BRUNS GRAYSON; E. ROBERT KENT, JR.; TRUMAN T. SEMANS; DC INVESTMENT PARTNERS, LLC; DOCTOR ROBERT CANTS, III; and MICHAEL W. DEVLIN, Defendants. ELIZABETH J. BAKER, BENDER 1996 REVOCABLE TRUST, DR. STEVEN J. BERLIN, ESTATE OF ROBERT B. BLOW, LUTHER C. BOLIEK, STEPHEN E. COIT, SARA CROWDER, GERALD K. AND TERESA K. FEHR, FU FAMILY REVOCABLE TRUST, RALPH GLASGAL, ROBERT G. GOERGEN, JR. 1985 TRUST, TODD A. GOERGEN 1985 TRUST, PETER O. HAUSMANN, WILLIS JAMES HINDMAN, WILLIAM F. KAISER, MARK AND ANN KINGTON, TIMOTHY K. KRAUSKOPF, WILLIAM T. MCCONNELL, PHILIP R. MCKEE, DAVID MIXER, MRW TRUST, JAMES MURRAY, PAUL D. AND JUDITH F. NEWMAN, W.L. NORTON, GREGORY PACKER, HOWARD E. ROSE, RUBEN FAMILY LIMITED PARTNERSHIP, S S TRUST, SALADRIGAS FAMILY LTD. PARTNERSHIP, RICARDO A. SALAS, JOSE M SANCHEZ, SAMUEL SIEGEL, SILVERMAN 1996 IRREVOCABLE TRUST, DOUGLAS G. SMITH, FREDERICK G. SMITH, RONALD B. STAKLAND, STRAUCH KULHANJAIN FAMILY TRUST, BRUCE E. TOLL, ALEXANDER R. AND MARJORIE L. VACCARO, YANOVER FAMILY LTD. PARTNERSHIP, MICHAEL YOKELL, and JUSTIN A. ZIVIN, Plaintiffs, v. ALEX. BROWN MANAGEMENT SERVICES; DEUTSCHE BANK SECURITIES, INC.; DEUTSCHE BANK, AG; RICHARD HALE; E. ROBERT KENT, JR.; TRUMAN T. SEMANS; DC INVESTMENT PARTNERS, LLC; DOCTOR ROBERT CRANTS, III, and MICHAEL W. DEVLIN, Defendants.

C.A. No. 762-N, C.A. No. 763-N

COURT OF CHANCERY OF DELAWARE, NEW CASTLE

2005 Del. Ch. LEXIS 100

March 21, 2005, Submitted

June 29, 2005, Decided

June 29, 2005, Filed

NOTICE:

[*1] THIS OPINION HAS NOT BEEN RELEASED FOR PUBLICATION. UNTIL RELEASED, IT IS SUBJECT TO REVISION OR WITHDRAWAL.

SUBSEQUENT HISTORY: Motion granted by, in part, Motion denied by, in part *Albert v. Brown*, 2005 Del. Ch. LEXIS 133 (Del. Ch., Aug. 26, 2005)

PRIOR HISTORY: *Albert v. Alex. Brown Mgmt. Servs.*, 2004 Del. Super. LEXIS 303 (Del. Super. Ct., Sept. 15, 2004)

CASE SUMMARY:

PROCEDURAL POSTURE: Plaintiff investors sued defendant fund managers for breach of fiduciary duty and contract, fraud, negligence, unjust enrichment, conspiracy to commit fraud, and aiding and abetting of the preceding. The managers sought to dismiss, arguing that the claims were time-barred, that the investors failed to state a claim upon which relief could be granted, that any claims were derivative, and that they had not pleaded that demand was refused or futile.

OVERVIEW: After the funds' value collapsed, the managers suspended redemptions and communications with the investors. The allegations were set out in 11 counts. The managers argued that the claims were time-barred pursuant to the three-year statute of limitations of *Del. Code Ann. tit. 10, § 8106*. The parties entered into a tolling agreement, effective November 11, 2003, which tolled the statutes of limitations applicable to the investors' claims. Therefore, absent tolling, if the claims accrued before November 11, 2000, they were time-barred. Three of the factual allegations made by the investors occurred after November 11, 2000. Therefore claims based on these factual allegations were not time-barred. These allegations were (1) that the managers failed to provide financial statements and reports as they were required to do under the partnership agreements and Delaware law, (2) that the managers wrongfully allowed withdrawals in December 2000 and 2001, thereby precipitating a liquidity crisis, and (3) that the managers failed to provide active and competent management of the funds. However, the court was uncertain which of the 11 claims remained at issue.

OUTCOME: Before addressing the managers' remaining challenges, the court requested a further submission from the investors addressing the continuing vitality of the claims asserted in the complaints. The court asked that this submission be made no later than July 15, 2005. The managers' response, not to exceed 10 pages, was to

be filed by July 22, 2005. When those additional submissions were received, the court would address the remaining issues.

LexisNexis(R) Headnotes

Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Failures to State Claims
Civil Procedure > Dismissals > Involuntary Dismissals > Failures to State Claims

Evidence > Inferences & Presumptions > General Overview

[HN1] The standard for dismissal pursuant to Del. Ch. Ct. R. 12(b)(6) for failure to state a claim upon which relief can be granted is well established. The motion will be granted if it appears with reasonable certainty that the plaintiff could not prevail on any set of facts that can be inferred from the pleading. In considering a motion to dismiss under Rule 12(b)(6), the court is required to assume the truthfulness of all well-pleaded allegations of fact in the complaint. All facts of the pleadings and inferences that can reasonably be drawn therefrom are accepted as true. However, neither inferences nor conclusions of fact unsupported by allegations of specific facts are accepted as true. That is, a trial court need not blindly accept as true all allegations, nor must it draw all inferences from them in the plaintiffs' favor unless they are reasonable inferences.

Contracts Law > Contract Interpretation > Fiduciary Responsibilities

Governments > Fiduciary Responsibilities

Torts > Procedure > Statutes of Limitations > General Overview

[HN2] The applicable statute of limitations contained in *Del. Code Ann. tit. 10, § 8106* imposes a three-year period of limitations on tort, contract, and fiduciary duty claims, and that three-year period applies by analogy to proceedings in equity. A statute of limitations period at law does not automatically bar an action in equity because actions in equity are time-barred only by the equitable doctrine of laches. However, the statutory period may create a presumptive time period for application of laches to bar a claim. In the absence of unusual or mitigating circumstances, where the analogous statute of limitations at law period has run, a plaintiff is barred from bringing suit without the necessity of the court engaging in a traditional laches analysis.

Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Failures to State Claims

Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Motions to Dismiss

[HN3] The Supreme Court of Delaware has cautioned trial courts to be sparing in resort to documents outside the pleadings in considering a motion to dismiss.

Governments > Legislation > Statutes of Limitations > Time Limitations

[HN4] A cause of action accrues under *Del. Code Ann. tit. 10, § 8106* at the time of the wrongful act, even if the plaintiff is ignorant of the cause of action.

Civil Procedure > Discovery > General Overview

Governments > Legislation > Statutes of Limitations > Time Limitations

Governments > Legislation > Statutes of Limitations > Tolling

[HN5] Under the so-called "discovery rule," the statute of limitations is tolled where the injury is inherently unknowable and the claimant is blamelessly ignorant of the wrongful act and the injury complained of. In such a case, the statute will begin to run only upon the discovery of facts constituting the basis of the cause of action or the existence of facts sufficient to put a person of ordinary intelligence and prudence on inquiry which, if pursued, would lead to the discovery of such facts. The statute of limitations then begins to run upon the discovery of facts constituting the basis of the cause of action or the existence of facts sufficient to put a person on inquiry notice of such facts.

Governments > Legislation > Statutes of Limitations > Tolling

Torts > Business Torts > Fraud & Misrepresentation > Nondisclosure > General Overview

[HN6] The statute of limitations will be tolled if a defendant engaged in fraudulent concealment of the facts necessary to put a plaintiff on notice of the truth. Fraudulent concealment requires an affirmative act of concealment or some misrepresentation by a defendant that prevents a plaintiff from gaining knowledge of the facts. Mere ignorance of the facts by a plaintiff, where there has been no such concealment, is no obstacle to operation of the statute of limitations. Where there has been fraudulent concealment from a plaintiff, the statute of limitations is suspended until his rights are discovered or until they could have been discovered by the exercise of reasonable diligence.

Business & Corporate Law > General Partnerships > Management Duties & Liabilities > Fiduciary Responsibilities > Duty of Good Faith & Loyalty
Governments > Fiduciary Responsibilities
Governments > Legislation > Statutes of Limitations > Tolling

[HN7] Under the theory of equitable tolling, the statute of limitations is tolled for claims of wrongful self-dealing, even in the absence of actual fraudulent concealment, where a plaintiff reasonably relies on the competence and good faith of a fiduciary. Underlying this doctrine is the idea that even an attentive and diligent investor may rely, in complete propriety, upon the good faith of fiduciaries, and may be completely ignorant of transactions that constitute self-interested acts injurious to the partnership. This doctrine tolls the limitations period until an investor knew or had reason to know of the facts constituting the wrong.

Governments > Legislation > Statutes of Limitations > Pleading & Proof

Governments > Legislation > Statutes of Limitations > Time Limitations

Governments > Legislation > Statutes of Limitations > Tolling

[HN8] It is a plaintiff's burden to plead facts to demonstrate that the statute of limitations was, in fact, tolled. Furthermore, if the limitations period is tolled under any of these theories, it is only tolled until a plaintiff discovers, or by exercising reasonable diligence should have discovered, his injury. Thus, the limitations period begins to run when the plaintiff is objectively aware of the facts giving rise to the wrong, i.e. on inquiry notice.

COUNSEL: Attorneys for the Plaintiffs: Jeffrey S. Goddess, Esquire, Jessica Zeldin, Esquire, ROSENTHAL, MONHAIT, GROSS & GODDESS, P.A., Wilmington, Delaware; Steven E. Fineman, Esquire, Hector D. Geribon, Esquire, Daniel P. Chiplock, Esquire, LIEFF, CABRASER, HEIMANN & BERNSTEIN, LLP, New York, New York.

Attorneys for the Defendants: Michael D. Goldman, Esquire, Peter J. Walsh, Esquire, Jr., Melony R. Anderson, Esquire, POTTER ANDERSON & CORROON LLP, Wilmington, Delaware; Christopher P. Hall, Esquire, Kevin Rover, Esquire, Marilyn B. Ampolsk, Esquire, MORGAN LEWIS & BOCKIUS, LLP, New York, New York.

OPINION

MEMORANDUM OPINION AND ORDER

LAMB, Vice Chancellor.

I.

The plaintiffs, investors in two exchange funds, bring these complaints against the managers of the funds for breach of fiduciary duty, breach of contract, fraud, negligence, unjust enrichment, and conspiracy to commit fraud and aiding and abetting of the preceding. Each plaintiff contributed appreciated securities (valued at a million dollars or more) to the funds in the hopes of receiving a diversified [*2] basket of securities, capital appreciation, and tax deferral. After the funds' value collapsed, the funds' managers suspended redemptions and communications with the investors.

The defendants seek to dismiss both complaints, arguing that the plaintiffs' claims are time-barred, that the plaintiffs fail to state a claim upon which relief can be granted, and that any claims that the plaintiffs have made are derivative, and they have not pleaded that demand was refused or futile. The court agrees the majority of claims are untimely. However, because it is unclear which of the plaintiffs' numerous claims are time-barred, the court orders the plaintiffs to file supplemental arguments on this issue.

II.

1 This opinion deals with the disposition of motions in two separate suits, *Albert v. Alex. Brown Mgmt. Serv.*, C.A. No. 762-N, and *Baker v. Alex. Brown Mgmt. Serv.*, C.A. No. 763-N. Even though the named defendants, the attorneys for both parties, and the factual and legal allegations are essentially the same in both, the cases have not been consolidated. The main factual difference between the cases is that C.A. No. 762-N is brought by investors in Fund I and deals with alleged wrongdoing with respect to Fund I, while C.A. No. 763-N is brought by investors in Fund II and deals with allegations of wrongdoing with respect to Fund II. When factually distinguishing the allegations made in the two cases, the court refers to the complaint filed in C.A. No. 762-N as the "Fund I Complaint" and the complaint filed in C.A. No. 763-N as the "Fund II Complaint." Collectively, the court refers to them simply as the complaints. Unless otherwise noted, the facts recited in this opinion are taken from the well-pleaded allegations of the complaints.

[*3] Plaintiffs are limited partners in two investment vehicles known as exchange funds, the DB Alex. Brown Exchange Fund I, L.P. ("Fund I") and the DB Alex. Brown Exchange Fund II, L.P. ("Fund II") (collectively, the "Funds"), managed and operated by the defendants. The plaintiffs made investments in the Funds in 1997 by contributing certain concentrated equity positions, with a minimum value of \$ 1 million, in exchange for interests, or units, in one of the Funds.

Initially, the Funds met with great success. From the initial net asset value ("NAV") of \$ 119.47 per partnership unit for Fund I, and \$ 71.61 for Fund II, the Funds peaked at NAVs of approximately \$ 370 for Fund I and \$ 135 for Fund II, in 2000. However, the Funds suffered from the vicissitudes of the markets, and by mid-2003, the NAVs had fallen to approximately \$ 26 for Fund I and \$ 33 for Fund II. The plaintiffs filed the complaints in this court on October 19, 2004.

The plaintiffs filed two richly detailed complaints, well over a hundred pages each, naming as defendants Alex. Brown Management Services ("Alex. Brown"),² the General Partner of Fund I and the Investment Advisor of Fund II; Alex. Brown's Management Committee; [*4] DC Investment Partners LLC ("DCIP"), the Sub-Advisor of Fund I and the General Partner and Sub-Advisor of Fund II;³ DCIP's managing members;⁴ Deutsche Bank Securities Inc. ("DBSI"), the custodian and placement agent of the Funds; and Deutsche Bank, AG.⁵

2 Alex. Brown was a wholly owned subsidiary of Alex. Brown, Inc. from its creation until on or about September 1, 1997.

3 Collectively, Alex. Brown and DCIP are referred to as the "Managers."

4 Defendants Robert Crants, III and Michael W. Devlin were, at all relevant times, the managing members, and part owners, of DCIP.

5 In September of 1997, Alex. Brown, Inc. was acquired by Bankers Trust New York Corporation and was renamed BT Alex. Brown Incorporated. In June of 1999, Deutsche Bank acquired Bankers Trust, including BT Alex. Brown and its subsidiaries. Effective December 4, 1999, BT Alex. Brown changed its name to DB Alex. Brown, LLC. Effective January 1, 2001, DB Alex. Brown changed its name to Deutsche Banc Alex. Brown. Effective April 1, 2002, Deutsche Banc Alex. Brown changed its name to Deutsche Bank Securities.

[*5] A. Exchange Funds Generally

Generally, an exchange fund is a vehicle that allows investors with substantial holdings of equity securities with large, unrealized capital appreciation to diversify and gain professional management. The investors contribute their appreciated securities and receive an interest in the partnership, thereby diversifying their holding

without incurring immediate capital gains tax. A provision in the Internal Revenue Code (the "Tax Code") allows the exchange to be tax free, as long as the partnership (or fund) holds no more than 80% of its assets in "stocks and securities" at the fund's closing. Since the contributed securities in an exchange fund are generally stock and securities as defined by the Tax Code, the fund's sponsor must insure that, at each exchange fund closing, at least 20% of the fund's assets are held in "qualified investments." These investments consist of a limited range of less liquid investments that fall outside the definition of "stock and securities." To satisfy this requirement, exchange funds usually invest in private preferred stock units; e.g. those issued by real estate operating partnerships.

To achieve the benefits of [*6] a tax-free exchange, partners must generally remain in the partnership (or fund) for a minimum number of years, as specified in the Tax Code (five years at the inception of Fund I, seven years at the inception of Fund II).⁴ At the end of the requisite period, partners may generally redeem all or a portion of their share of the partnership without triggering capital gains tax liability. Redemption policies vary. For example, most exchange funds distribute a *pro rata* portion of the fund's total marketable securities; i.e. investors often receive a diversified basket of securities as a tax-free redemption.

6 The five year anniversary of the inception of Fund I passed in May of 2002. The seven year anniversary of the inception of Fund II passed in October of 2004.

Exchange fund sponsors are generally large investment banks or independent investment management firms. The fiduciary oversight of investors' interests are usually performed by the sponsor or an independent group, such as a management committee [*7] or a board of directors. Exchange fund participants must satisfy financial suitability standards, and the minimum investment is usually \$ 1 million.

Portfolio construction is important to exchange funds. In order to preserve the tax deferral for the investors, the fund's management tries to avoid selling any of the original contributed securities during the life of the fund. Most funds have a clearly-stated investment objective and use sophisticated portfolio construction techniques to determine an appropriate and diversified universe of stocks eligible for inclusion in the fund. Selection criteria generally includes such characteristics as market capitalization, industry sector, trading volume, volatility, and dividends.

When the fund sponsors assemble the proposed portfolio and prospective investors have submitted their

stocks for inclusion in the fund, investors generally receive an "inspection report" listing the contributed securities that have tentatively been accepted. The investor typically has three to five business days to review that report and to withdraw from the fund if desired. Generally, once the deadline has passed, the investment manager reviews the remaining portfolio [*8] to ensure that it is still in keeping with the investment objective and makes any necessary adjustments, after which the fund closes and the partnership is officially formed.

Concurrent with the portfolio construction process, the fund sponsor secures the required 20% qualified investments portion of the portfolio. Many funds use leverage, borrowing money from banks (lines of credit) or brokers (margin accounts) to purchase the qualified investments and other assets for the fund's portfolio.

B. The Marketing Of The Funds

For both Funds, an Alex. Brown Internal Sales Memorandum (the "Sales Memos") was used by Alex. Brown brokers to market and promote the Funds to prospective investors. Both Sales Memos stated that the Funds' objective was to "achieve long-term appreciation in the value of the Fund's assets equal to or better than the appreciation in the broader stock market." The strategy identified in the Sales Memos was to construct a "diversified portfolio," characterized by "flexibility and the ability to accept a broad range of contributed securities." The Sales Memos indicated that the Funds would contain the contributed securities, illiquid securities, and acquired [*9] securities.

The Fund I Sales Memo stated that the securities contributed to the Fund would be "screened by the Sub-Advisor according to liquidity and fundamentals." The Fund I Sales Memo also stated that the Fund's management would use hedging strategies to "liquefy a portion of the contributed securities to provide the funds to purchase the illiquid securities and the acquired securities." According to the Fund I Sales Memo, the contemplated hedging strategies would also facilitate "the acceptance of a broad range of [contributed] securities." The Fund II Sales Memo stated that Fund II's management would hedge the contributed securities "almost immediately with collars. Typically, calls and puts will be purchased approximately 10% out of the money," so there is roughly 10% upside and 10% downside exposure." According to the Fund II Sales Memo, the contemplated hedging would allow a "wider range of securities, as well as larger amounts of a single stock, to be accepted."

The Fund I Sales Memo stated that the illiquid securities would be selected by the sub-advisor and general partner, and would initially be precious metals but would ultimately be invested in "LBO funds, distressed [*10]

real estate funds, merchant banking funds, and other private equity placements." The Fund II Sales Memo indicated that the Fund would have access to "top private equity funds." According to the Fund II Sales Memo, Fund II's illiquid assets would initially be commodities "used as a holding tank" until longer term investments draw down capital commitments" but that private real estate partnerships would become "the primary investment vehicle for the illiquid portfolio."

In addition, the Sales Memos stated that the balance of the Funds' assets would be in "acquired securities," specifically the "Flag Funds" managed by Alex. Brown Investment Management.

7 The Flag Funds were at all relevant times offered and managed by Alex. Brown and its successors, including DBSI. Three members of the Funds' Management Committees also served leading roles with the Flag Funds. Defendants Richard Hale, the Chairman of the Management Committees of both Funds, and Truman T. Semans, a member of the Management Committees of both Funds, were at all relevant times directors of the Flag Funds (at inception of Fund II, Semans was the Chairman of the Flag Funds), and Gary Fearnow, also a member of the Management Committees of both Funds, was a Vice-President of the Flag Funds.

[*11] C. The Terms Of The Funds

The terms and structure of Fund I were set forth in a Private Placement Memorandum dated April 14, 1997 ("Fund I PPM"), an Agreement of Limited Partnership ("Fund I Partnership Agreement") and subscription documents, including a subscription agreement ("Fund I Subscription Agreement"). Likewise, the terms and structure of Fund II were set forth in a Private Placement Memorandum dated October 3, 1997 ("Fund II PPM"), an Agreement of Limited Partnership ("Fund II Partnership Agreement") and subscription documents, including a subscription agreement ("Fund II Subscription Agreement").⁸

8 Both Funds were established as Delaware limited partnerships and are governed by Delaware law.

The PPMs of both Fund I and Fund II state that the Funds were established to "offer diversification and professional investment management to persons who have substantial holdings of publicly traded or privately held equity securities with relatively large unrealized capital appreciation or that [*12] are restricted as to disposition under the *Securities Act of 1933*, as amended." The investment objective of the Funds was to "achieve

long-term appreciation in the value of the Fund's assets, while minimizing the recognition of capital gains by the Fund and Investors with respect to the contributed securities." The PPMs stated that "persons who transfer appreciated securities to the Fund in exchange for Units . . . will not incur federal income tax liability by reason of the exchange."

The PPMs provided that an investment in the Funds could be made by "contributing equity securities acceptable to the Fund in exchange for limited partnership interests in the Fund." The PPMs also provided that in determining which securities would be accepted for contribution to the Funds and in what amounts, "the Sub-Advisor will undertake an extensive screening process to identify the securities eligible for contribution. This screening process will be based upon an analysis of historical levels of risk and returns for securities, liquidity characteristics and forecasts of future returns based on fundamental analysis and quantitative models." However, unlike many exchange funds, the Funds did not [*13] offer prospective limited partners the opportunity to inspect the accepted contributed securities prior to the closing of the Funds. Further, at no time prior to or after the closing of the Funds, were the plaintiffs provided with any analysis of the screening of those securities submitted for inclusion in the Funds.

The PPM represented that the Funds intended to accomplish its objectives and goals through investing in three broad asset classes: (i) equity securities, primarily of publicly traded companies, including restricted securities, that were contributed by Investors; (ii) "illiquid assets," which the PPMs indicated would comprise at least 22% of the Funds' total assets, consisting of real estate and exchange-traded commodities other than precious metals, owned directly or through partnerships or similar entities; and (iii) "acquired assets," which were to "consist of shares of diversified equity and other mutual funds and unit investment trusts . . . including the Flag Investors Equity Partners Fund. . . ."

The PPMs stated that the Funds were to borrow under a credit facility with commercial banks or under margin arrangements with broker-dealers to purchase the illiquid assets [*14] and acquired assets, and to pay placement fees as well as offering, organizational, and borrowing expenses. The PPMs also stated that the Funds could borrow to make additional acquisitions of investments or to meet any short-term liquidity needs of the Funds.

D. Management Of The Funds

The General Partner and Investment Advisor of Fund I is, and at all relevant times was, Alex. Brown. The PPM stated that the General Partner would be "responsible for managing the Fund's investment activities

and for the oversight and management of the business and operations of the Fund." The Fund I PPM also stated that the General Partner would be "responsible for the establishment of investment policy [and] relationships with Investors." The Fund I PPM provided that responsibility for the "supervision of the Fund and monitoring of its investment strategy will reside in the Management Committee of the General Partner." ("Fund I Committee"). In April of 1997, and until about July 2, 2002, the Fund I Committee included Hale, Fearnow, Bruns Grayson, E. Robert Kent, Jr., and Semans.

Likewise, the Investment Advisor of Fund II is, and at all relevant times was, Alex. Brown. The PPM stated that [*15] the Investment Advisor would be responsible for establishment of investment policy, relationships with Investors, and for the oversight and overall management of the business and operations of Fund II. The Investment Advisor was also responsible for convening and conducting all meetings of the investors, distributing annual and other reports to investors and responding to inquiries received from the investors, prospective investors, the general public, and others. In addition, the Investment Advisor was responsible for establishing bank credit facilities and was responsible for Fund II's compliance with its reporting obligations to lending banks.

The Investment Advisor established a management committee (the "Fund II Committee")⁹ to carry out these functions. From the inception of the Fund to the present, the Chairman of the Fund II Committee has been Hale. From October of 1997 until about July 2, 2002, the Fund II Committee included Fearnow, Grayson, Kent, and Semans:

9 Collectively, the Fund I Committee and the Fund II Committee are referred to as the "Management Committees."

[*16] From the inception of Fund I through on/or about September 1, 1997, a subsidiary of Alex. Brown (and its successors) served as the placement agent for Fund I, solicited subscriptions for units in Fund I, and served as the custodian for Fund I's accounts. In addition, either Alex. Brown, Inc. or Alex. Brown & Sons provided Fund I with a margin account. Likewise, from October of 1997 through about June 4, 1999, BT Alex. Brown (and its successors) served as the private placement agent for Fund II, solicited subscriptions for Fund II, and served as the custodian for Fund II's accounts. During that same time period, BT Alex. Brown provided Fund II with a margin account.

DCIP is, and was at all relevant times, the Sub-Advisor for Fund I and the General Partner and Sub-Advisor of Fund II. The PPMs of both funds provide: "DCIP is responsible for the day-to-day management and

administration of the Fund and for providing certain investment management advice to the Fund." DCIP acted principally through its managing members, defendants Crants and Devlin.

As compensation for acting as the Investment Advisor and General Partner of Fund I, and the Investment Advisor of Fund II, and to cover expenses, [*17] Alex. Brown received a monthly fee equivalent to 1.35% annually of the total values of the gross assets of the Funds. A portion of the management fee, equivalent to .55% of gross assets annually, was paid to DCIP monthly for its management services. In addition, the placement agent and accounts custodian -- BT Alex. Brown and its successors, including Deutsche Bank Securities -- received placement and servicing fees.

E. Redemptions

When first established, Fund I's PPM included a five year investment requirement and Fund II's PPM included a seven year investment requirement.¹⁰ However, the PPMs and the Partnership Agreements of the Funds provided for limited redemption rights after the second anniversary of an investor's admission to the Fund."

10 This difference in the length of the investment requirement was due to a change in the Revenue Code that occurred between the formation of Fund I and Fund II.

11 After the second anniversary and on or before the fifth anniversary of Fund I, or the seventh anniversary for Fund II, of an investor's admission to the Funds, an investor could redeem its units as of any quarter-end at their NAV, provided that the redemption would be limited to the investor contributed securities, and to those contributed securities fair market value, at the time of redemption. After the fifth anniversary of one's admission to Fund I, or the seventh anniversary of admission to Fund II, an investor could redeem its units as of any quarter-end at NAV, subject to the General Partner's (Fund I) or the Investment Manager's (Fund II) right to select securities to be distributed.

[*18] Notwithstanding the specific redemption provisions, the Investment Advisor reserved the right, in its sole discretion, to delay or deny redemptions, if such redemption requests imposed significant liquidity costs on the Funds. More specifically, the PPMs provided that no redemption would be made "to the extent the Fund, as determined by the Investment Advisor in its sole discretion, does not have sufficient or appropriate assets to satisfy the redemption."

F. The Closings

Fund I was officially formed and closed on or about May 5, 1997. At its inception, Fund I had 88 limited partners who contributed more than 90 securities valued at approximately \$ 152.5 million. The 33 plaintiffs who have initiated this action are among those limited partners. At the inception of Fund I, the plaintiffs contributed securities worth approximately \$ 59.9 million.

Fund II was officially formed and closed between October of 1997 and April 17, 1998 (the date of the last closing). At its inception, Fund II had 82 limited partners who contributed more than 80 securities valued at approximately \$ 132.7 million. The 42 plaintiffs who have initiated this action are among those limited partners. At [*19] the inception of Fund II, the plaintiffs contributed securities worth approximately \$ 59 million.

G. Removal Of The General Partner

The Partnership Agreement of Fund II provides that, by consent of the limited partners in Fund II, those limited partners "shall be entitled to remove the General Partner" for breaches by the General Partner of any material obligations under the Fund II Partnership Agreement based upon a determination by the limited partners that the General Partner had acted negligently in any material respect, or had engaged in fraud or willful misconduct, or failed or refused to substantially perform its duties as the General Partner. The action of removing the General Partner requires the consent or approval of limited partners whose units represent at least 51% of the aggregate units owned by the limited partners in Fund II. There is no similar provision in the Partnership Agreement of Fund I.

H. The Performance Of The Funds And Management's Reporting

The PPMs and the Partnership Agreements promised the investors that they would "receive unaudited semi-annual and audited annual financial statements and semi-annual reports on the performance of [*20] the Fund." The Partnership Agreement also provided that the "names of the Limited Partners and their addresses are set forth on Schedule A, which shall be amended by the General Partner, from time to time to reflect the withdrawal and substitution of Limited Partners and the change in the number of Units owned by the Limited Partners."

The first Fund I Management Committee meeting took place on May 12, 1997. Present at this meeting were Committee members Hale, Fearnow, Grayson, and Semans. Crants of DCIP also participated in the meeting by telephone. " This first meeting was devoted primarily to a discussion of the illiquid investments for Fund I. Allegedly, the Management Committee did not meet again for more than one year.

12 The plaintiffs allege not to have knowledge of what was discussed or determined during Management Committee meetings until those Committee minutes were obtained in June of 2003.

The Management Committee of Alex. Brown Management and DCIP communicated with the plaintiffs through [*21] semi-annual reports. The first such report for Fund I was dated September 30, 1997, and for Fund II was dated January 20, 1998. These reports were sent to the limited partners sometime thereafter.

According to the financial statement accompanying the September 30, 1997 report, Fund I was composed of "a broadly diversified portfolio of over 90 different securities, aggregating over \$ 160mm and to date have hedged approximately 95% of those holdings using a combination of both short sales against the box' and equity collars." The September 30, 1997 report also noted that in "terms of the illiquid assets, we have now committed approximately 27% of the Fund's total assets to private partnerships" and that Fund I had a NAV of \$ 119.47 per partnership unit.

Likewise, the financial statement accompanying the January 20, 1998 report stated that Fund II was composed of "a diversified portfolio of over 55 different securities, aggregating over \$ 80 million in value, and the Fund expects to enhance these numbers further with additional closings in 1998." The January 20, 1998 financial statement continued: "In spite of the fact that we are still in the marketing period, we have hedged the majority [*22] of those holdings using equity collars, and expect to hedge the remainder in the coming quarter." Also according to these financial statements, Fund II had a NAV of \$ 71.61 per unit as of December 31, 1997.

The January 20, 1998 report for Fund II went on to state:

We expect the illiquid assets that we acquire will represent one of the most important drivers to the long-term performance of the Fund. We are therefore extremely pleased to report that we have already been able to commit approximately 15% of the Fund's assets to two real estate partnerships, and have approximately 22% of the Fund invested in a managed commodity partnership while we look for new real estate investments and await the funding of our current commitments.

In October of 1997, Fund I committed, and eventually invested, \$ 5 million in ABX Fund LP. Fund I was the only limited partner, and only investor, in the ABX Fund. The General Partner of the ABX Fund, Calvert Capital, managed the ABX Fund through defendant Grayson, a member of the Management Committee of Fund I. The ABX Fund was sponsored by BT Alex. Brown. Alex. Brown and Grayson received management fees of approximately \$ 140,000 annually in [*23] addition to the fees charged by Fund I's management on the Fund's assets for the management of the ABX Fund. The plaintiffs were never advised that Fund I was the sole investor in ABX.

The next report from the Management Committee and the Sub-Advisor for Fund I to the limited partners was dated December 31, 1997, and was sent to the limited partners sometime thereafter. The report stated that management's "strategy of hedging the contributed securities (heavily weighted in technology stocks) and acquiring illiquid assets and shares in the Flag Equity Partners Fund and the Flag Value Builders Fund helped mute the markets' volatility meaningfully." According to the report, technology and telecommunications contributed securities represented at least 69% of Fund I's NAV as of the end of 1997. The December 31, 1997 report further noted that management's "hedging approach will continue in 1998, though we may shift more of our short-against-the-box positions over to new equity collars." Approximately 95% of the contributed securities were hedged through collars and short sale transactions by the end of 1997. The December 31, 1997 report stated that, as of December 31, 1997, Fund I had a [*24] NAV of \$ 118.12 per unit. The December 31, 1997 report also stated that, by the end of 1997, Fund I had a line of credit with PNC Bank of approximately \$ 55.8 million.

The first audited financial statement for Fund I is for the fiscal year ending December 31, 1997, is dated February 20, 1998, and was sent to the limited partners sometime thereafter. That audited financial statement included a description of the percentage of contributed securities attributable to industry sectors. More specifically, the December 31, 1997 audited financial statement for Fund I reported that at least 62.3% of the contributed securities were invested in technology and telecommunications stocks. Belying the well-pleaded factual allegations in the Fund I Complaint, the plaintiffs make the conclusory allegation that they were not informed by Fund I's management of this heavy weighting of Fund I in technology and telecommunications stocks.

The December 31, 1997 audited financial statement, also explained that approximately 13% of Fund I's portfolio was invested in the Flag Funds. The Flag Funds held a number of positions in technology and telecommunications stocks, further increasing the Fund's overall

[*25] investment in those sectors. The Fund's investment in investment partnerships and private partnerships (approximately 12% of the overall portfolio at the time) also included stakes in technology and telecommunications companies.

The first audited financial statement for Fund II was for the fiscal year ending December 31, 1997, is dated February 20, 1998, and was sent to the limited partners sometime thereafter. That audited financial statement, like the first audited financial statement for Fund I, included a description of the percentage of contributed securities by industry sectors. It stated that at least 41.3% of the contributed securities were invested in technology and telecommunications stocks. The financial statement identified all individual stocks that made up more than 5% of Fund II's value. In addition, the financial statement identified that, as of December 31, 1997, Fund II had a line of credit with PNC Bank of approximately \$ 35 million. On January 14, 1998, the PNC Bank line of credit was increased to \$ 50 million.

The next communication from Alex. Brown and DCIP regarding Fund I was dated June 30, 1998, and sent to the limited partners sometime thereafter. In that [*26] report, management described large declines in the markets in the first half of 1998, but stated it had "effectively utilized equity collars to limit our downsize exposure in these severe sell-offs." Collars and short sales were being used at the time to hedge over 90% of the contributed securities. The June 30, 1998 report stated that, as of June 25, 1998, Fund I had a NAV of \$ 121.14 per unit and that on or about July 13, 1998 Fund I's line of credit was increased to approximately \$ 86.5 million. In addition to PNC Bank, two other banks, Bank of America and First American National Bank, provided lines of credit.

Likewise, DCIP and Alex. Brown provided a management report regarding Fund II to the limited partners dated June 30, 1998, and sent this report to Fund II's limited partners sometime thereafter. In that report, Fund II's management stated:

Since the end of last year, we have had five additional closings adding 27 more stocks to the portfolio and slightly greater than \$ 48 million in market value of contributed securities. The final closing for the fund was on April 17. . . . With these additional closings, the fund is now comprised of 82 different securities, aggregating [*27] over \$ 120 million of contributed securities.

The June 30, 1998 report represented that management "instituted prudent portfolio hedging with equity collars protecting over 90% of the portfolio." The report went on:

The equity collars that are used as a hedging tool allow some upside participation while limiting our downside risk. The performance of the contributeds [sic] has been generally positive, though the portfolio, which has many small and mid-cap stocks, has lagged the Dow Jones and S&P 500 indices as large-cap stocks have generally outperformed small-cap stocks.

The June 1998 report also stated that Fund II had "already been able to commit approximately 20% of the fund's assets to real estate partnerships, and have approximately 22% of the fund invested in a managed commodity partnership while we look for new real estate investments and await the funding of our current commitments." As of June 25, 1998, Fund II had a NAV of \$ 70.98 per unit.

Thereafter, semi-annual reports for both Funds were sent out to the limited partners by DCIP and Alex. Brown. These reports detailed the rise and fall of the Funds' net asset values.

Date	Fund I's NAV Per Unit
June 30, 1999	\$ 128.34
December 31, 1999	\$ 293.04
February 15, 2000	\$ 370
June 30, 2000	\$ 292.89
December 31, 2000	\$ 194.70
June 30, 2001	\$ 102.11
December 31, 2001	\$ 74.25

[*28] After 2001, Alex. Brown and DCIP stopped reporting to the limited partners and did not provide the limited partners with the 2001 audited financial statement, the June 30, 2002 report, or the December 31, 2002 report for Fund I until the spring of 2003.

The net asset values reported in the semi-annual reports for Fund II show that Fund II also suffered the slings and arrows of the financial markets.

Date	Fund II's NAV Per Unit
December 31, 1998	\$ 74.72
June 30, 1999	\$ 82.83
December 31, 1999	\$ 133.82
June 30, 2000	\$ 134.53
December 31, 2000	\$ 97.54
June 30, 2001	\$ 80.82
December 31, 2001	\$ 66.59

After 2001, Alex. Brown and DCIP stopped reporting to the limited partners and did not provide the limited partners with an audited 2002 financial statement, a June 30, 2002 financial report, a December 31, 2002 financial report, or a June 30, 2003 financial report for Fund II.

The Management Committee of Fund I again met on September 6, 2001. Present at the meeting were Com-

mittee members Hale, Fearnow, and Kent. Also in attendance were Hooker, Crants, Phillips, and Potter. During the September 6, 2001 meeting, Chairman Hale stated "that the recent [*29] sharp market decline was creating liquidity issues for Fund I. Fund I's NAV had fallen to \$.80 at the August 25, 2001 monthly pricing and was about \$.64 today." According to Hale, the "decline was primarily a function [of] the drop in value of the contributed

securities." Hale also stated that "Fund I was facing about \$ 7mm in margin calls over the next week. . . ." In addition, selling "contributed securities was discussed but it generates a taxable gain that must be paid by the Fund so it was not seen as a good solution."

I. The Liquidity Crunch Cometh

Predictability, in early 2001, the Funds ran into a liquidity crunch. The Managers of the Funds had attempted to reduce the risk of the Funds by simultaneously buying a put option and selling a call option on the same security, known in financial jargon as "collaring." This is essentially a wash transaction, since the value of the put option purchased is approximately the same as the value of the call option sold. However, as the value of some securities in the Funds appreciated, the Funds were required to honor the call options. Since the Funds did not want to transfer the securities subject to the calls (as this would [*30] have been a taxable event), the Managers were forced to pay the difference between the strike price and the securities' current price. As the price of certain securities in the Funds (such as Yahoo!) exploded, the Funds were forced to come up with large amounts of cash, quickly. They did so mostly through their lines of credit.

As a result of declining market prices, on three separate occasions between September 27, 2001 and February 1, 2002, Fund I violated a financial covenant in its \$ 40 million bank line of credit agreement, which required Fund I to maintain a ratio of total assets to borrowings of 2.25:1.00. Each time, Bank of America provided two months of relief by reducing the test ratio to 2.0. In or about May of 2002, Fund I entered into a demand loan with Deutsche Bank for \$ 10 million. On or about June 5, 2002, Fund I triggered an "Event of Default" under the credit agreement with Bank of America by failing to repay the loan at maturity (June 5, 2002), among other things. On or about June 21, 2002, Alex. Brown Management sent a letter to Fund I's limited partners, notifying them for the first time of the event of default, the demand loan with Deutsche Bank, and the violation [*31] of the bank covenant.

Fund II also ran into liquidity problems. From September of 2001 to April of 2002, on four separate occasions, Fund II violated similar financial covenant in its \$ 30 million bank line of credit agreement, requiring Fund II to maintain a ratio of total assets to borrowings of 2.25:1.00. Each time, Bank of America provided two months of relief by reducing the test ratio to 2.0 for a short period of time. On or about June 28, 2002, Fund II triggered an "Event of Default" under the credit agreement with Bank of America by failing to repay the loan at maturity, among other things. The limited partners

were not immediately advised of the covenant violations, or of the bank default.

In a letter dated July 11, 2002, the Management Committee advised Fund II's limited partners that Fund II had defaulted on its credit agreement with Bank of America. The letter also advised Fund II's investors of a discontinuation of redemptions and that the Fund's management was discontinuing publishing a NAV for the Fund.

Pursuant to an August 27, 2002 Amendment and Waiver, Bank of America agreed to extend the letter of credit maturity to June 24, 2003, provided that Fund II provide [*32] a perfected second lien on Fund II's margin account, further protection of its collateral, and pay all accrued interest and fees. On or about September 24, 2002, Fund II's management wrote to the limited partners advising them of the renewal of the Bank of America loan through June 30, 2003, the changes in the Management Committee, and indicating that Fund II's NAV had fallen to \$ 35.54 per unit. "

13 The Fund I Complaint alleges both that Bank of America extended the maturity date of the letter of credit until June 24, 2003, and that the Managers informed the limited partners that the Bank of America loan had been renewed until June 30, 2003. Fund I Compl. PP 181-82. There is no explanation in the Fund I Complaint for the apparent discrepancy between these two dates.

J. Management Shakeup

On or about July 2, 2002, officials at Deutsche Bank fired the Management Committee of the Funds, except for Hale, and replaced those Committee members with Leo Grohowski (Managing Director and Chief Investment [*33] Officer for Deutsche Asset Management in the Americas), Ann Doyle (head of Alternative Products for DB Alex. Brown Private Client Division), and Michael Colon (Chief Operating Officer for DB Alex. Brown Private Client Division and Chief Operating Officer for Americas Equities for Deutsche Bank).

In or about May of 2003, the Managers resumed formal communication with the limited partners of Fund I by issuing a report dated April 30, 2003. According to the report, as of April 30, 2003, the Fund had a NAV of \$ 26.01 per unit. In or about July of 2003, the limited partners of Fund I received audited financial statements for Fund I for 2001 and 2002, dated March 14, 2003 and May 9, 2003. These statements, and the accompanying notes, described to the limited partners Fund I's ongoing financial difficulties and a new letter of credit arrangement with Deutsche Bank.

Likewise, in July of 2003, the Managers issued a report, dated April 30, 2003, to the limited partners of Fund II regarding that Fund. According to the report, as of April 30, 2003, the Fund had a NAV of \$ 29.57 per unit. In July of 2003, the plaintiffs received audited financial statements for Fund II for 2001 and 2002, dated [34] March 14, 2003 and June 26, 2003. In October of 2003, Alex. Brown and DCIP sent another report, dated June 30, 2003, in which the management advised the limited partners that Fund II would not honor any redemption requests and that, as of June 30, 2003, the Fund had a NAV of \$ 33.19 per unit.

During the life of the Funds, Alex. Brown and DCIP allowed several redemptions of capital contributions to be made.

K. Procedural Posture

The allegations set out in the two complaints are nearly identical and they are both set out in eleven counts. The first count is for breach of fiduciary duty. The second count is for aiding and abetting a breach of fiduciary duty. The third count is for common law fraud. The fourth claim is for aiding and abetting common law fraud. The fifth count is for breach of contract against Alex. Brown Management (with respect to Fund I) and breach of contract against DCIP (with respect to Fund II). The sixth count is for breach of the covenant of good faith and fair dealing against Alex. Brown (with respect to Fund I) and breach of the covenant of good faith and fair dealing against DCIP (with respect to Fund II). The seventh count is for gross negligence. [35] The eighth count is for unjust enrichment against all defendants. The ninth count is for conspiracy liability. The tenth count is for an accounting. The eleventh count is for agency liability against Deutsche Bank and Deutsche Bank Securities.

On January 24, 2005, the defendants moved to dismiss the amended complaints on the grounds that: (i) the claims are untimely, (ii) the majority of claims are derivative, and the plaintiffs have not pled demand nor that demand was excused, (iii) the plaintiffs' claims for aiding and abetting, conspiracy, and agency liability are improperly pled, (iv) the complaint fails to state a claim for unjust enrichment, and (v) the plaintiffs' request for an accounting is improper. On March 21, 2005, the court heard oral arguments on the motions to dismiss. This is the court's disposition of those motions.¹⁴

¹⁴ For the sake of clarity, the two separate motions will be referred to hereafter collectively as one.

III.

[HN1] The standard for dismissal pursuant to *Rule 12(b)(6)* [36] for failure to state a claim upon which relief can be granted is well established. The motion will be granted if it appears with reasonable certainty that the plaintiff could not prevail on any set of facts that can be inferred from the pleading.¹⁵ In considering a motion to dismiss under *Rule 12(b)(6)*, the court is required to assume the truthfulness of all well-pleaded allegations of fact in the complaint.¹⁶ All facts of the pleadings and inferences that can reasonably be drawn therefrom are accepted as true.¹⁷ However, neither inferences nor conclusions of fact unsupported by allegations of specific facts are accepted as true.¹⁸ That is, a trial court need not blindly accept as true all allegations, nor must it draw all inferences from them in the plaintiffs' favor unless they are reasonable inferences.¹⁹

¹⁵ *Kohls v. Kenetech Corp.*, 791 A.2d 763, 767 (Del. Ch. 2000).

¹⁶ *Grobow v. Perot*, 539 A.2d 180, 187 n.6 (Del. 1988).

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *In re Lukens Inc. S'holders Litig.*, 757 A.2d 720, 727 (Del. Ch. 1999).

[37] IV.

A. Statute Of Limitations

The defendants argue that all claims are time-barred. [HN2] The applicable statute of limitations contained in 10 Del. C. § 8106 imposes a three-year period of limitations on tort, contract, and fiduciary duty claims, and that three-year period applies by analogy to proceedings in equity.²⁰ A statute of limitations period at law does not automatically bar an action in equity because actions in equity are time-barred only by the equitable doctrine of laches. However, the statutory period may create a presumptive time period for application of laches to bar a claim.²¹ In the absence of unusual or mitigating circumstances, where the analogous statute of limitations at law period has run, a plaintiff is barred from bringing suit without the necessity of the court engaging in a traditional laches analysis.²²

²⁰ *Wal-Mart Stores v. AIG Life Ins. Co.*, 860 A.2d 312, 319 (Del. 2004) (per curiam). Likewise, 10 Del. C. § 8106 applies to actions based on gross negligence, *Cincinnati Bell Cellular Sys. Co. v. Ameritech Mobile Phone Serv.*, 1996 Del. Ch. LEXIS 116, at *44 (Del. Ch. Sept. 3, 1996); an accounting, *Artesian Water Co. v. Lynch*, 283 A.2d 690, 692 (Del. Ch. 1971); and conspiracy, aiding and abetting, and agency liability, see *Atlantis Plastics Corp. v. Sammons*, 558 A.2d 1062.

1064 (Del. Ch. 1989) (applying 10 Del. C. § 8106 and holding that a claim for conspiracy was time-barred).

[*38]

21 *United States Cellular Inv. Co. v. Bell Atl. Mobile Sys.*, 677 A.2d 497, 502 (Del. 1996); see also *Atlantis Plastics*, 558 A.2d at 1064 ("An analogous statute of limitations period applicable at law, however, is to be given great weight in determining whether a suit is to be time-barred in equity by laches and will be applied in the absence of unusual or mitigating circumstances.").

22 See *United States Cellular*, 677 A.2d at 502; *Atlantis Plastics*, 558 A.2d at 1064.

In connection with efforts to informally resolve their dispute, the parties entered into a tolling agreement, effective November 11, 2003, which tolled the statutes of limitations applicable to the plaintiffs' claims. Therefore, absent tolling (discussed more fully *infra*), if the claims accrued before November 11, 2000, they are time-barred.

B. Documents Relied Upon In The Motion To Dismiss

In their motion to dismiss, the defendants rely heavily upon documents purportedly demonstrating that the plaintiffs had timely access to the facts [*39] underlying their claims such that they should be deemed to have been given "inquiry notice" and be barred from pursuing their claims on that basis. The court's ability to consider these documents is therefore critical to resolving this motion. [HN3] Our Supreme Court has cautioned trial courts to be sparing in our resort to documents outside the pleadings. ²³ However, as in other cases, ²⁴ it is clear that the documents relied upon by the defendants on this motion (e.g. the audited financial reports and the semi-annual investor reports) were consulted, relied upon, and quoted from extensively by the plaintiffs in drafting the complaints. "By expressly referring to and so heavily relying on these documents in the Amended Complaint, plaintiffs have incorporated them by reference. . . ." ²⁵ Therefore, these documents are properly before the court on the motion to dismiss.

23 See, e.g., *Wal-Mart*, 860 A.2d at 320; *In re Santa Fe Pacific Corp. S'holder Litig.*, 669 A.2d 59, 68-70 (Del. 1995).

24 See, e.g., *In re Dean Witter P'ship Litig.*, 1998 Del. Ch. LEXIS 133, at *27 n.46 (Del. Ch. July 17, 1998), *aff'd*, 725 A.2d 441 (Del. 1999).

[*40]

25 *Id.*; see also *Santa Fe*, 669 A.2d at 69 (holding that, on a 12(b)(6) motion, this court has properly considered documents referred to in complaints when the documents were integral to

a plaintiff's claim and incorporated in the complaint).

C. Accrual Of Claims

[HN4] A cause of action accrues under 10 Del. C. § 8106 at the time of the wrongful act, even if the plaintiff is ignorant of the cause of action. ²⁶ The complaints allege seven different types of wrongdoing by the defendants.

26. *Wal-Mart*, 860 A.2d at 319; *Fike v. Ruger*, 754 A.2d 254, 260 (Del. Ch. 1999) ("A cause of action accrues at the moment of the wrongful act, even if the plaintiff is ignorant of the wrong.") (citing *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *15)).

First, the plaintiffs allege that DCIP failed to properly screen the securities [*41] accepted into the Funds and, instead, accepted essentially all of the securities offered for inclusion in the Funds. ²⁷ Second, the plaintiffs allege that the Managers failed to properly hedge the funds against risk, especially since the Funds were overweighted in technology and telecommunications stocks. ²⁸ Third, the plaintiffs allege that the decisions, or lack thereof, made by the Managers caused a liquidity crisis that caused a virtual collapse of the fund. ²⁹ Fourth, the plaintiffs allege that the Managers failed to provide financial reports and/or annual audited financial statements in violation of Delaware law and the Partnership Agreements. ³⁰ Fifth, the plaintiffs allege that the Managers did not, and were incapable of, providing proper day-to-day management of the funds because the actual managers of the Funds were not sufficiently experienced or capable. ³¹ In addition, the plaintiffs allege that the Managers failed to properly screen the securities for inclusion in the Funds, failed to implement a proper hedging strategy, and failed to manage the funds so to meet their investment goals. ³² Sixth, the plaintiffs allege that the Managers engaged in self-dealing by [*42] receiving millions of dollars in fees and by investing the Funds' money in companies managed and controlled by Alex. Brown Management. ³³ Seventh, the plaintiffs allege that Deutsche Bank aided and abetted the wrongful conduct alleged above, engaged in the illegal activity, and participated in a conspiracy to violate the law. ³⁴ Finally, in addition to these seven alleged wrongful acts, the court infers from the complaints a claim that the redemptions allowed by the Funds' Managers were wrongful. The court addresses each of the factual bases, and the accrual, of these claims in turn.

27 Fund I Compl. PP 170-72, Fund II Compl. PP 188-190.

28 Fund I Compl. PP 185-190, Fund II Compl. PP 204-208.

29 Fund I Compl. P 194, Fund II Compl. P 212.

30 Fund I Compl. P 221, Fund II Compl. P 235.

31 Fund I Compl. P 229, Fund II Compl. P 243.

32 Fund I Compl. P 229, Fund II Compl. P 243.

33 Fund I Compl. PP 234-37, Fund II Compl. PP 248-51.

34 Fund I Compl. P 238, Fund II Compl. P 252.

[*43] 1. Failure To Screen, Diversify, And Properly Design The Funds

The plaintiffs allege that the Managers breached their fiduciary duties in initially screening the stocks allowed into the Funds, failing to properly diversify the Funds, and that, generally, "the entire structure of the Fund[s] was fatally flawed from the outset." ³⁵ Accepting these allegations as true, the plaintiffs' injuries occurred when the Funds closed, at which time the Funds were not (allegedly) properly diversified nor properly screened. This was the time of the wrongful act. Fund I closed on May 5, 1997, ³⁶ and Fund II closed on April 17, 1998. ³⁷ Likewise, claims that the Funds were improperly structured accrued at the time the Funds closed. Therefore, all the claims based on these factual allegations accrued before November 11, 2000 and are presumptively time-barred.

35 Fund I Compl. P 270, Fund II Compl. P 285.

36 Fund I Compl. P 84.

37 Fund II Compl. P 96.

2. Failure To Implement Hedging Strategies

[*44] The plaintiffs allege that Alex. Brown and DCIP breached their fiduciary duties, their contractual duties, and committed fraud by failing to properly implement hedging strategies to protect the Funds from downside risk. According to the complaints, at the time the Funds were formed the Managers of the Funds hedged the majority of the contributed securities using collars and, to a lesser extent, short sales. ³⁸ Beginning in the fall of 1998, the managers began discussing the effect that hedging was having on the Funds. ³⁹ By the fall of 1999, all prior hedges on the Fund I had expired, and the Managers determined not to re-hedge. ⁴⁰ Similarly, the Managers removed all of the hedges on Fund II in the fall of 1999. ⁴¹ The Funds were, therefore, unhedged during the fourth quarter of 1999 and early 2000 when the stock markets boomed. ⁴² This allowed the Funds to

participate in the boom, but also left them exposed to the stock market bust. ⁴³ In the spring of 2001, after the Funds had suffered substantial losses, the Managers reinstated some hedging strategies. ⁴⁴

38 Fund I Compl. P 186, Fund II Compl. P 205.

[*45]

39 Fund I Compl. P 188, Fund II Compl. P 206.

40 Fund I Compl. P 190.

41 Fund II Compl. P 206.

42 Fund I Compl. P 186, Fund II Compl. P 205.

43 Fund I Compl. P 191, Fund II Compl. P 209.

44 Fund I Compl. P 192, Fund II Compl. P 210.

The alleged harm to the plaintiffs occurred when the Managers unhedged the Funds. This was the act that exposed the Funds to the risk of a falling market, and that led to their alleged injury. Thus, any claims arising from the fact that the Funds were not properly hedged accrued at the time the Funds became unhedged. The complaints allege that this occurred in the fall of 1999. ⁴⁵ Therefore, all the claims based on these factual allegations accrued before November 11, 2000 and are presumptively time-barred.

45 Fund I Compl. P 190, Fund II Compl. P 206.

3. The Liquidity Crisis

The complaints allege that the collars used by the **[*46]** Funds' management were specifically designed to settle in cash, rather than by the delivery of the underlying securities. When the strike prices of the calls were exceeded, the Funds repurchased the calls with cash generated from borrowing, instead of liquidating the underlying securities. Beginning in the middle of 1998, as the stock market bubble inflated, the hedged securities blew through their collars. This created millions of dollars in cash liabilities for the Funds. ⁴⁶

46 Fund I Compl. P 187, Fund II Compl. P 205.

The complaints allege that the Funds' "liquidity problem -- and hence its inability to meet its investment objective -- began when the [Managers] failed to evaluate and screen the securities selected for the Fund." ⁴⁷ According to the plaintiffs, these initial "structural flaws" led to the lack of liquidity. ⁴⁸ It was the lack of liquidity, plaintiffs contend, that eventually led to the Funds inability to hedge with equity collars, declining net asset

values, bank defaults, and the [*47] suspension of redemption rights.⁴⁹

47 Fund I Compl. P 198, Fund II Compl. P 216.

48 Fund I Compl. P 194, Fund II Compl. P 212.

49 Fund I Compl. PP 194-219, Fund II Compl. PP 212-33.

However, the wrongful acts the plaintiffs allege are that the Managers failed to diversify and screen the securities admitted into the Funds. As discussed in Section IV.C.1, *supra*, these acts all occurred, and therefore the claims based on them accrued, before November 11, 2000. Thus, they are presumptively time-barred.

4. Failure to Provide Financial Reports And List Of Limited Partners

The complaints allege that, under Section 11.2 of the Partnership Agreements, the Managers were required to deliver semi-annual unaudited financial statements and a report on the financial condition of the Funds' business and the results of its operations to each limited partner. Also, the Partnership Agreements required the Managers to provide annual audits of the Funds, consisting of a balance sheet, a statement [*48] of operations, a statement of cash flows and related notes.⁵⁰ The complaints allege that the Managers failed to produce reports or audited statements during 2002, resumed reporting in the spring of 2003, and this failure to provide reports during that time period violated the Partnership Agreement as well as Delaware law.⁵¹

50 Fund I Compl. P 220, Fund II Compl. P 234.

51 Fund I Compl. P 221, Fund II Compl. P 235.

In addition, management was required to identify in Schedule A to the Partnership Agreements the names and addresses of the Funds' limited partners, and amend such list to reflect the withdrawal and substitution of limited partners and the change in the number of units owned by the limited partners.⁵² The plaintiffs allege that, despite this obligation, the Partnership Agreements did not include the names and addresses of the limited partners and the number of units each held in the Funds, and management never provided to the plaintiffs that information.⁵³

52 Fund I Compl. P 222, Fund II Compl. P 236.

[*49]

53 Fund I Compl. P 222, Fund II Compl. P 236.

With respect to the claims for failing to provide audited financial statements and financial reports, the Managers first failed to provide these reports in 2002. Having occurred after November 11, 2000, these claims are timely.

With respect to the claims for failing to provide lists of the limited partners of the Funds, these claims accrued at the time of the wrongful act, i.e. the time at which the Managers were allegedly obligated to provide the names of the limited partners but failed to do so. This was, according to the complaints, at the time the Managers sent out the Partnership Agreements. This occurred long before November 11, 2000. Therefore, the claims based on these alleged wrongful acts are presumptively untimely.

5. Failure Of Alex. Brown And DCIP To Provide Professional And Active Management And Supervision Of The Funds

The complaints allege that Alex. Brown was charged with managing the investment decisions of the Funds and that Alex. Brown delegated this responsibility to the Management Committees.⁵⁴ The complaints further [*50] allege that the Management Committees devoted such a negligible amount of time to their work that they violated their duties to exercise reasonable care, in good faith, to the manage the Funds.⁵⁵ The complaints also allege that DCIP failed in its duty to manage and administer the Funds on a day-to-day basis. Specifically, the complaints allege that defendants Crants and Devlin, who did the actual managing of the Funds for DCIP, were not sufficiently experienced or qualified to manage the Funds.⁵⁶ The complaints also allege that Crants and Devlin devoted insufficient time to managing the Funds and that, instead, they devoted their time to the creation and management of other investment companies, for which they were investigated for securities fraud.⁵⁷

54 Fund I Compl. P 224, Fund II Compl. P 238.

55 Fund I Compl. P 225, Fund II Compl. P 239.

56 Fund I Compl. P 229, Fund II Compl. P 242.

57 Fund I Compl. PP 230-31, Fund II Compl. PP 244-45.

As opposed to their other claims, [*51] the plaintiffs' allegations of failure to manage the Funds are not a discrete wrong, which occurred at a specific time. Instead, they allege that DCIP and Alex. Brown owed (and owe) a continuing duty to actively manage and supervise the Funds. The wrongful act is the failure to meet that duty. The court cannot say that this wrongful act occurred before November 11, 2000. Therefore, the plaintiffs' claims based on the failure of Alex. Brown and

DCIP to provide active management are *not* barred by the statute of limitations.

6. Self-Dealing And Related Party Transactions

The complaints allege that Alex. Brown and DCIP received millions of dollars in management fees from the Funds and that millions more were paid to Alex. Brown's affiliates and parents over the years in the form of accounts servicing fees, transaction commissions or fees, and interest on margin accounts.⁶³ The complaints further allege that the Funds' management invested the Funds' money in companies and partnerships managed and controlled by Alex. Brown's affiliates and parents (including Deutsche Bank Securities), and members of the Management Committee so that Alex. Brown could collect fees on both sides [*52] of the transaction.⁶⁴ The complaints also allege that the fees that Alex. Brown and DCIP generated through their operation of the Funds and their investment of the Funds' assets in related-party entities, as well as their desire to continue to receive those fees, motivated Alex. Brown and DCIP to engage in the wrongful conduct alleged in the complaints.⁶⁵

58. Fund I Compl. P 233, Fund II Compl. P 247.

59. Fund I Compl. P 234, Fund II Compl. P 248.

60. Fund I Compl. P 232, Fund II Compl. P 251.

The complaints allege four specific related-party transactions that were improper. First, the complaints allege that, in October of 1997, Fund I invested \$ 5 million in a private venture capital partnership, known as the ABX Fund, that was run by Grayson, a member of Fund I's Management Committee. Rather than invest the \$ 5 million directly, Fund I's management allegedly directed the money to a separate entity controlled by a member of the Management Committee, thereby generating fees and commissions [*53] for Grayson and his company, to the detriment of the plaintiffs.⁶⁶

61. Fund I Compl. P 236.

Second, the complaints allege that, in October of 1998, Fund II invested \$ 7.5 million in a private partnership known as the Place Collegiate Properties Fund. Allegedly, Crants and Devlin had ownership interests in the Place Collegiate Properties Fund, and stood to benefit financially from Fund II's investment in that fund.⁶⁷

62. Fund II Compl. P 250.

Third, the complaints allege that the Funds invested in the Flag Funds. The Flag Funds were offered and managed by Alex. Brown and its successors, including

Deutsche Bank Securities, and members of the Management Committees also served leading roles in the Flag Funds.⁶⁸ The complaints further allege that as of December 31, 1997 approximately 13% of Fund I's portfolio was invested in the [*54] Flag Funds,⁶⁹ and that, by November of 1998, Fund II had invested approximately \$ 7 million in the Flag Funds.⁷⁰

63. Fund I Compl. P 75, Fund II Compl. P 86.

64. Fund I Compl. P 94.

65. Fund II Compl. P 121.

Fourth, the Fund I Complaint alleges that from the inception of Fund I, on September 1, 1997, a subsidiary of Alex. Brown (and its successors) served as the placement agent for Fund I, served as the custodian for Fund I's accounts, and provided Fund I with a margin account.⁷¹ Likewise, from October of 1997 through about June 4, 1999, BT Alex. Brown (and its successors) served as the private placement agent for Fund II, solicited subscriptions for Fund II, served as the custodian for Fund II's accounts, and provided Fund II with a margin account.⁷² The self-dealing, apparently, is that an affiliate of the Funds' Managers provided the margin accounts.

66. Fund I Compl. P 78.

67. Fund II Compl. P 89.

[*55] On the face of the complaints, all of these alleged wrongful acts took place, and thus accrued, long before November 11, 2000. As such, the claims based on these allegedly wrongful acts are presumptively time-barred.

7. The Redemptions

The complaints allege that the Managers of the Funds wrongfully allowed several limited partners to withdraw part or all of their interests from the Funds, and failed to advise the plaintiffs of these withdrawals. With respect to Fund I, the plaintiffs allege that on July 7, 1999, seven limited partners withdrew approximately \$ 13.3 million.⁷³ On July 18, 2000, five limited partners withdrew approximately \$ 6.8 million.⁷⁴ By December 2001, the Managers had allowed the additional redemption of approximately \$ 8.0 million.⁷⁵ On June 21, 2002, Alex. Brown Management sent a letter to Fund I's limited partners, including the plaintiffs, stating that they were suspending all redemptions.⁷⁶

68. Fund I Compl. P 122.

69. *Id.* P 133.

70. *Id.* P 210.

71. *Id.* P 162.

[*56] With respect to Fund II, on April 30, 1999, one limited partner withdrew approximately \$ 1.2 mil-

lion. " On July 20, 1999, two limited partners withdrew approximately \$ 1.97 million. " On November 8, 1999, one limited partner withdrew approximately \$ 2.4 million. " On January 31, 2000, one limited partner withdrew approximately \$ 1.6 million. " On April 12, 2000 and July 18, 2000, five limited partners withdrew a total of approximately \$ 41.7 million. " On October 1, 2000, an investor withdrew approximately \$ 3 million. " On January 17, 2001, three investors withdrew approximately \$ 1.8 million. " On October 25, 2001, an investor withdrew approximately \$ 150,000. " On December 31, 2001, two investors withdrew approximately \$ 3.4 million. " In October of 2003, the Managers disseminated a report, dated June 30, 2003, to the plaintiffs, stating that the Fund would not honor any redemption requests. It further stated that "redemptions would increase the Fund leverage," and that the "release of stocks in the case of a redemption is a reduction in the collateral for the margin and bank loans." " 41

72 Fund II Compl. P 130.

[*57]

73 *Id.* P 135.

74 *Id.* P 136.

75 *Id.* P 142.

76 *Id.* P 147.

77 Fund II Compl. P 152.

78 *Id.* P 159.

79 *Id.* P 169.

80 *Id.* P 174.

81 *Id.* P 186.

On the face of the complaints, claims based on the majority of these alleged wrongful acts are untimely. That is because they are alleged to have occurred before November 11, 2000. However, three withdrawals from Fund II are alleged to have occurred after November 11, 2000. These allegedly occurred on January 17, 2001, October 25, 2001, and December 31, 2001 (the "Fund II 2001 Withdrawals"). Additionally, approximately \$ 8.0 million in withdrawals were alleged to have occurred in December of 2000 from Fund I (the "Fund I December 2000 Withdrawals"). Therefore, all claims for allowing withdrawals, except those based on the Fund I December 2000 Withdrawals and the Fund II 2001 Withdrawals, are presumptively time-barred. " 42

82 All alleged wrongful withdrawals, other than the Fund I December 2000 Withdrawals and the Fund II 2001 Withdrawals, are hereinafter referred to as the "Pre-2001 Withdrawals."

[*58] 8. The Plaintiffs' Response

The plaintiffs argue that their claims did not accrue until December 31, 2001, when the Funds' NAVs were

reported to be lower than their first reported level. They argue that "each Plaintiff could not have suffered an injury or damages before he or she actually suffered a loss' relative to his or her initial investment. . . ." " They complain that the NAVs of the Funds did not peak until sometime after the defendants committed most of the alleged wrongful acts. The plaintiffs also claim that the cause of action could not have accrued until December 31, 2001, because they could not have brought suit until then. In essence, the plaintiffs argue that they could not have brought suit until they had suffered a harm, and that they did not suffer a harm until the value of the Funds dropped below the initial NAV.

83 Fund I Pl.'s Answering Br. at 12.; Fund II Pl.'s Answering Br. at 13.

This is incorrect. The law in Delaware is crystal clear that a claim accrues as soon as the [*59] wrongful act occurs. " This is so because the plaintiffs were harmed as soon as the alleged wrongful acts occurred. Whether or not the plaintiffs could have sued for damages is not dispositive as to whether the claim accrued, since, as soon as the alleged wrongful act occurred, the plaintiffs could have sought injunctive relief. They did not. Instead, they waited until the value of the Funds climbed to dizzying heights, and then came crashing down.

84 See *Wal-Mart*, 860 A.2d at 319 ("[A] cause of action accrues' under Section 8106 at the time of the wrongful act, even if the plaintiff is ignorant of the cause of action."); *SmithKline Beecham Pharms. Co. v. Merck & Co.*, 766 A.2d 442, 450 (Del. 2000) ("[The] statute [of] . . . limitations period begins to run from the time the cause of action accrues. This is so even if the plaintiff is ignorant of the cause of action.") (quoting *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *15); *Isaacson, Stolper & Co. v. Artisan's Sav. Bank*, 330 A.2d 130, 132 (Del. 1974) ("The statute of limitations . . . begins to run at the time of the wrongful act, and, ignorance of a cause of action, absent concealment or fraud, does not stop it.").

[*60] The flaw in the plaintiffs' argument is best exemplified by their claims for hedging. The wrongful act the plaintiffs allege is the unhedging of the Funds. However, after the defendants unhedged the Funds, their value skyrocketed. This was due, of course, to the fact that the Funds were exposed to much more risk. Assuming (without deciding) that unhedging the Funds was a wrongful act, it was wrongful because it exposed the Funds to this extra risk. However, under the plaintiffs' theory, they are given the equivalent of a call option. If

the unhedging of the Funds works out, and the value of the Funds goes up, the plaintiffs will have no complaint. But if the hedging (or lack thereof) strategy does not work out, and the value of the Funds falls, the plaintiffs can sue. This clearly is not, and should not be, the law. The plaintiffs made the decision to ride the bubble to the top. They cannot now complain that the bubble burst.

The court reiterates that a claim accrues at the time of the alleged wrongdoing, and not when the plaintiff suffered a loss.

D. Tolling Of The Statute Of Limitations

The plaintiffs allege that their claims are timely because the statute of limitations [*61] was tolled until approximately June of 2002. Even after a cause of action accrues, the running of the limitations period can be tolled in certain limited circumstances.⁸⁵ The plaintiffs assert three separate theories to support a tolling of the statute of limitations in this case: (1) inherently unknowable injuries; (2) fraudulent concealment; and (3) equitable tolling. Each of these doctrines permits tolling of the limitations period where the facts underlying a claim were so hidden that a reasonable plaintiff could not timely discover them.⁸⁶

85 *Wal-Mart*, 860 A.2d at 319.

86 *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *19.

1. Inherently Unknowable Tolling

[HN5] Under the so-called "discovery rule," the statute of limitations is tolled where the injury is inherently unknowable and the claimant is blamelessly ignorant of the wrongful act and the injury complained of.⁸⁷ In such a case, the statute will begin to run only upon the discovery of facts constituting [*62] the basis of the cause of action or the existence of facts sufficient to put a person of ordinary intelligence and prudence on inquiry which, if pursued, would lead to the discovery of such facts. The statute of limitations then begins to run upon the discovery of facts constituting the basis of the cause of action or the existence of facts sufficient to put a person on inquiry notice of such facts.⁸⁸

87 *Wal-Mart*, 860 A.2d at 319 (quoting *Coleman v. PriceWaterhouseCoopers, LLC*, 854 A.2d 838, 842-43 (Del. 2004)).

88 *Wal-Mart*, 860 A.2d at 319 (quoting *Coleman*, 854 A.2d at 842-43).

2. Fraudulent Concealment Tolling

[HN6] The statute of limitations will also be tolled if a defendant engaged in fraudulent concealment of the facts necessary to put a plaintiff on notice of the truth.⁸⁹

Fraudulent concealment requires an affirmative act of concealment or some misrepresentation by a defendant that prevents a plaintiff from gaining knowledge [*63] of the facts.⁹⁰ "Mere ignorance of the facts by a plaintiff, where there has been no such concealment, is no obstacle to operation of the statute [of limitations]."⁹¹ "Where there has been fraudulent concealment from a plaintiff, the statute of limitations is suspended until his rights are discovered or until they could have been discovered by the exercise of reasonable diligence."⁹²

89 *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *20-*21.

90 *Id.* at *21 (citing *Halpern v. Barran*, 313 A.2d 139, 143 (Del. Ch. 1973)).

91 *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *21 (quoting *Halpern*, 313 A.2d at 143).

92 *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *21 (citing *Halpern*, 313 A.2d at 143).

3. Equitable Tolling

[HN7] Under the theory of equitable tolling, the statute of limitations is tolled for claims of wrongful self-dealing, even in the absence of actual fraudulent concealment, [*64] where a plaintiff reasonably relies on the competence and good faith of a fiduciary.⁹³ Underlying this doctrine is the idea that even an attentive and diligent investor may rely, in complete propriety, upon the good faith of fiduciaries, and may be completely ignorant of transactions that constitute self-interested acts injurious to the partnership.⁹⁴ This doctrine tolls the limitations period until an investor knew or had reason to know of the facts constituting the wrong.⁹⁵

93 *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *21.

94 *Id.* at *22 (quoting *Kahn v. Seaboard Corp.*, 625 A.2d 269, 275 (Del. Ch. 1993)).

95 *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *22 (citing *NL Indus. v. MAXXAM, Inc.* (In re MAXXAM, Inc. /Federated Dev. S'holder Litig.), 659 A.2d 760, 769 (Del. Ch. 1995)).

[HN8] It is a plaintiff's burden to plead facts to demonstrate that the statute of limitations was, in fact, tolled.⁹⁶ Furthermore, if the limitations [*65] period is tolled under any of these theories, it is only tolled until a plaintiff discovers, or by exercising reasonable diligence should have discovered, his injury.⁹⁷ Thus, the limitations period begins to run when the plaintiff is objectively aware of the facts giving rise to the wrong, i.e. on inquiry notice.⁹⁸ Therefore, for the plaintiffs to establish that, due to any of these three doctrines, this action is not

time-barred, they must show that they were *not* on inquiry notice of their claims before November 11, 2000.

96 *Dean Witter*, 1998 Del. Ch. LEXIS 133, at *23.

97 *Id.*

98 *Id.*

E. Inquiry Notice

1. Failure To Screen, Diversify, And Properly Design The Funds, And The Liquidity Crisis

The plaintiffs had actual or inquiry notice of the alleged failure to screen the securities and diversify the Funds by the time they received the investor reports and audited financial statements detailing the makeup of the Funds. With respect to Fund I, [*66] the plaintiffs specifically allege that the Fund Managers sent them the December 31, 1997 semi-annual investor report and the February 20, 1998 audited financial statement (for the year ending December 31, 1997) shortly after the date of those documents.⁹⁹ The plaintiffs expressly acknowledge that the December 31, 1997 investor report disclosed that the securities contributed to Fund I were "heavily weighted in technology stocks."¹⁰⁰ Moreover, the December 31, 1997 investor report, like each subsequent semi-annual investor report, included a schedule listing all of Fund I's contributed securities and illiquid assets, and the February 20, 1998 audited financial statement disclosed the value of each category of Fund I's investments, including the percentage of Fund I's net equity and dollar value represented by the contributed securities within each industry sector. Therefore, by the time the plaintiffs received the December 31, 1997 investor report, they knew the securities that made up Fund I, and should have known that Fund I was overweighted in technology and telecommunications stocks, and that the Fund was not diversified.

99 Fund I Compl. P 92.

[*67]

100 *Id.* at P 90.

With respect to Fund II, the plaintiffs specifically allege that "sometime in the late winter or early spring of 1998," they received the first audited financial statement for Fund II; dated February 20, 1998, and for the fiscal year ending December 31, 1997; and that this statement "first informed [the plaintiffs] of how heavily weighted the contributed securities and the overall Fund portfolio were in technology and telecommunications stocks. . . ." ¹⁰¹ The plaintiffs also allege that that the audited financial statement identified the individual technology and telecommunications stocks that made up more than 5% of Fund II's portfolio. ¹⁰² Moreover, like that for Fund I, the February 20, 1998 audited financial statement for Fund II

disclosed the value of each category of Fund II's investments, including the percentage of Fund II's net equity and dollar value represented by the contributed securities within each industry sector. Therefore, again like Fund I, by the time the plaintiffs received the February 20, 1998 audited financial statement for Fund II, they knew [*68] the securities that made up Fund II, and should have known that Fund II was overweighted in technology and telecommunications stocks and that it was not diversified.

101 Fund II Compl. P 101.

102 *Id.*

In addition, the failure to screen and properly diversify the Funds are the factual predicates of the so-called "liquidity crisis." Thus, the above analysis applies equally to this alleged wrongdoing.

For the above reasons, the claims based on the failure to screen, diversify, and properly design the Funds, and the liquidity crisis, are time-barred and must be dismissed.

2. Failure To Implement Hedging Strategies

The plaintiffs had actual or inquiry notice of the alleged failure to implement hedging strategies before November 11, 2000. With respect to Fund I, the plaintiffs had actual or inquiry notice that Fund I was unhedged no later than July or August of 2000, when they received the June 30, 2000 semi-annual report that disclosed that Fund I was no longer hedged. That report stated: [*69]

In order to mute some of the volatility in the market, we evaluated possible hedging strategies for the contributed portfolio, but it became clear that given our current level of diversification, it would be too expensive for the risk trade-off. We will, however, continue to monitor and evaluate potential hedging strategies.¹⁰³

103 *Anderson Aff. Ex. 14 at 2* (emphasis added).

Furthermore, each audited financial report contained lists of the value of each investment category, as a percentage of net assets of the Funds. These included a listing of the call options, put options, and securities sold short. The December 31, 1998 audited financial report listed that 39.7% of the net assets of Fund I (valued at

approximately \$ 62 million) were in call options. It also listed that 18.8% of the net assets of Fund I (valued at approximately \$ 30 million) were in securities sold short. The December 31, 1999 audited financial report shows that, a year later, these numbers had dramatically changed. [*70] The December 31, 1999 audited financial report listed that only 0.8% of the net assets of Fund I (valued at approximately \$ 6 million) were in call options, while 10.0% (valued at approximately \$ 37 million in losses) were in securities sold short.

Likewise, the investors of Fund II had actual or inquiry notice that that Fund was unhedged no later than January or February of 1999, when they received the December 31, 1998 semi-annual investor report. The Fund II Complaint quotes the December 31, 1998 semi-annual investor report and alleges that Fund II removed its hedges in the second half of 1998.¹⁰⁴ The specific passage from the 1998 semi-annual investor report quoted in the Fund II Complaint states:

The use of equity collars throughout the first nine months of the year protected the Fund from losses totaling over \$ 15 million or nine points of net asset value. As valuation fell to unsustainable levels, however, we removed our hedges to participate in the upside we believed could occur. This decision proved beneficial as the markets recovered and several of our holdings generated improved performance toward the end of the year. (Emphasis added.)

104 Fund II Compl. P 120.

[*71] The audited financial reports for Fund II also provided the Fund II investors with a list of the value of each investment category, as a percentage of net assets of the Funds, including a listing of the options used to hedge Fund II. Therefore, for all of the above reasons, the plaintiffs had actual or inquiry notice that the Funds were unhedged.

3. Failure To Provide The Names And Addresses Of The Funds' Limited Partners

The plaintiffs had actual or inquiry notice of the failure to provide a list of the limited partners before November 11, 2000. The complaints allege that the Managers were required to provide the names and addresses of the Funds' limited partners in the Partnership Agreements, and that they failed to do so.¹⁰⁵ The Fund I Partnership Agreement did not contain a list of the lim-

ited partners of that Fund, while the Fund II Partnership Agreement contained a list, but did not contain the addresses and ownership interests of the limited partners.¹⁰⁶

105 Fund I Compl. P 222, Fund II Compl. P 236.

106 See Fund I Partnership Agreement; Fund II Partnership Agreement, Schedule "A."

[*72] However, the plaintiffs should have been aware that the Partnership Agreements did not contain a limited partner list (or that the list was incomplete) as soon as they received the document. Schedule A of the Fund II Partnership Agreement clearly lists the names of limited partners, without any additional information. Schedule A of the Fund I Partnership Agreement is blank. The plaintiffs received these documents long before November 11, 2000. Thus, these claims are untimely.

4. Self-Dealing And Related Party Transactions

The plaintiffs had actual or inquiry notice of the alleged self-dealing and related party transactions before November 11, 2000. The documents that the Managers provided to the plaintiffs disclosed that the Funds would engage in the types of fee arrangements and related party transactions that the plaintiffs now challenge. The Fund I and Fund II Partnership Agreements contain nearly identical provisions that provide:

3.7 Compensation; Reimbursement of Expenses. The Partnership may pay compensation and other fees to the [Managers] or any Affiliated Persons thereof, in such amounts and on such terms as the General Partner, in its sole discretion, shall, [*73] subject to the provisions of Section 3.8, determine. Each Limited Partner, by becoming such, acknowledges and agrees, without limiting the generality of the foregoing, that the General Partner and its Affiliated Persons shall be entitled to receive from the Partnership the fees and commissions described in the [Private Placement] Memorandum, all of which shall be deemed to satisfy the provisions of Section 3.8. ...

3.8 Transactions with Affiliated Persons. The Partnership may enter into transactions with the [Managers] and Affiliated Persons [thereof], but only on terms at least as favorable to the Partnership as may be reasonably expected to be obtained from unrelated third parties, it being agreed that the terms of the ar-

rangements referred to in Section 3.7 satisfy such standard.

The PPMs also made extensive disclosures of the potential conflicts of interest and related party transactions. In the section titled "Conflicts of Interest," the PPMs unambiguously state: "There are inherent and potential conflicts of interest between the General Partner and the Fund and the Sub-Advisor and the Fund."¹⁰⁷ The PPMs also disclose that there were possible conflicts with [*74] respect to fees:

The Fund may invest in investment vehicles sponsored by Alex. Brown or affiliates of Alex. Brown which will increase the funds under management of such other investment vehicles and which may increase, in dollar terms, the amount of fees payable to the investment advisors of such other investment vehicles who may be affiliates of the General Partner or Alex. Brown.¹⁰⁸

¹⁰⁷ Fund I PPM at 36, Fund II PPM at 40.

¹⁰⁸ Fund I PPM at 17, Fund II PPM at 18.

The plaintiffs were also aware (or should have been) of the specific allegations of related-party transactions. First, with respect to Fund I's investment in the ABX Fund, this investment was disclosed to the plaintiffs in the Fund I September 30, 1997 investor report. Furthermore, while the plaintiffs complain that defendant Grayson ran the ABX Fund, they also admit that this fact was disclosed to them.¹⁰⁹

¹⁰⁹ Fund I Compl. P 236.

[*75] Second, with respect to the Funds' investment in the Flag Funds, the PPMs specifically disclosed that the Funds would invest in the Flag Funds. The PPMs state:

The Fund will seek to accomplish its investment objective through investing in securities in three broad asset types. . . . The third class is expected to consist of shares of diversified equity mutual funds and unit investment trusts [collectively, the "Mutual Funds" including the *Flag Investors Equity Partners Fund*. . . .]¹¹⁰

¹¹⁰ Fund I PPM at 1-2 (emphasis added); the Fund II PPM at 1-2 states essentially the same, except it uses a slightly different phraseology.

Thus, the plaintiffs should have been aware that the Funds would invest in the Flag Funds from the time they received the PPMs, long before November 11, 2000.

Third, with respect to Alex. Brown (and/or its successors) providing margin accounts to the Funds, these transactions were disclosed to the plaintiffs in the PPMs. The PPMs state: "The Fund also may . . . [*76] . . . invest Fund cash in short-term investments, such as . . . short-term bank obligations and interest-bearing deposit accounts, including, without limitation, instruments of, and accounts with, Alex. Brown or its affiliates."¹¹¹ Therefore, from the beginning of their investment, the plaintiffs were put on notice that the Funds would have investment accounts with Alex. Brown and/or its affiliates.

¹¹¹ Fund I PPM at 22; Fund II PPM at 23.

Fourth, while the investment of Fund II in the Place Collegiate Properties Fund was not specifically disclosed, it was a type of investment that was well-disclosed. The passages from the Fund II Partnership and Fund II PPM quoted, *supra*, clearly put the plaintiffs on notice that these type of investments would be made by that Fund.

Thus, for the above reasons, the claims based on the alleged self-dealing are time-barred.

5. Pre-2001 Withdrawals

The plaintiffs had actual or inquiry notice of the allegedly wrongful redemptions before November 11, 2000. Under the [*77] Fund I Partnership Agreement, redemptions of the fair market value of contributed stock were allowed after the second anniversary of the investor's admittance into Fund I.¹¹² This was also disclosed in the Fund I PPM.¹¹³ The Fund II Partnership Agreement and the Fund II PPM provided the same.¹¹⁴ Thus, from the very beginning of their investment, the plaintiffs were aware that, after two years, the Funds would allow withdrawals.

¹¹² Fund I Compl. P 81.

¹¹³ *Id.*

¹¹⁴ Fund II Compl. P 93.

In addition, the plaintiffs were on notice (or should have been) of many of the specific redemptions about which they complain. With regard to the withdrawals from Fund I, the plaintiffs specifically admit that they were aware of withdrawal of \$ 13.3 million (occurring on July 7, 1999) in April of 2000 due to the "issuance of the 1999 audited financial statements for Fund I in about

April, 2000." ¹¹⁵ Likewise, with respect to Fund II, the plaintiffs complain that the Managers allowed redemptions [*78] of approximately \$ 5.6 million in 1999. However, the plaintiffs specifically admit that they were made aware of these redemptions by "the issuance of the 1999 audited financial statements for Fund II, date April 25, 2000." ¹¹⁶

115 Fund I Compl. P 208.

116 Fund II Compl. P 219.

Given that the Partnership Agreements and the PPMs specifically informed the plaintiffs that the Funds would allow redemptions, and given that the financial reports disclosed the initial redemptions, the plaintiffs should have been aware that the Funds would allow these redemptions. Therefore, the claims based on the Pre-2001 Withdrawals are time-barred.

V.

Three of the factual allegations made by the plaintiffs occurred after November 11, 2000. Therefore, and to that extent, claims based on these factual allegations are not time-barred. These factual allegations are: (i) the Managers failed to provide financial statements and reports as they are required to under the Partnership

Agreements and Delaware law, (ii) [*79] the Managers wrongfully allowed the Fund I December 2000 Withdrawals and the Fund II 2001 Withdrawals, thereby precipitating (or at least exacerbating) a liquidity crisis, and (iii) the Managers failed to provide active and competent management of the Funds.

Given the limited nature of these matters, the court is uncertain which of the eleven legal claims set forth in both complaints remain at issue. Before addressing the defendants' remaining challenges to those claims, the court concludes that it is advisable to request a further submission from the plaintiffs that addresses the continuing vitality of the claims asserted in the complaints. The court asks that this submission be made no later than July 15, 2005 and should not exceed 10 pages in length. The defendants' response, not to exceed 10 pages, should be filed by July 22, 2005. When those additional submissions are received, the court will address the remaining issues.

VI.

For the foregoing reasons, the motions to dismiss are granted in part, denied in part, and reserved in part. IT IS SO ORDERED.

EXHIBIT 2

Westlaw.

Slip Copy
Slip Copy, 2008 WL 2484587 (Del.Supr.)
(Table, Text in WESTLAW), Unpublished Disposition
2008 WL 2484587 (Del.Supr.)

Page 1

International Broth. Teamsters v. Coca-Cola Co.
Del.Supr.,2008.
Only the Westlaw citation is currently available.

NOTICE: THIS OPINION HAS NOT BEEN
RELEASED FOR PUBLICATION IN THE
PERMANENT LAW REPORTS. UNTIL
RELEASED, IT IS SUBJECT TO REVISION OR
WITHDRAWAL.

NOTE: THIS OPINION WILL NOT BE
PUBLISHED IN A PRINTED VOLUME. THE
DISPOSITION WILL APPEAR IN A REPORTER
TABLE.

Supreme Court of Delaware.
INTERNATIONAL BROTHERHOOD
TEAMSTERS, Robert Lang and Natalie Gordon,
Plaintiff Below, Appellants,
v.

The COCA-COLA COMPANY, Fernando Aguirre,
James E. Copeland, Jr., Calvin Darden, J. Alexander
M. Douglas, J. Trevor Eyton, Gary P. Fayard, Irial
Finan, Marvin J. Herb, L. Phillip Humann, Donna A.
James, Paula R. Reynolds, Howard G. Buffett, John L.
Clendenin, Steven J. Heyer, John E. Jacob,
Jean-Claude Killy, Deval L. Patrick, Summerfield K.
Johnston, Jr., Lowry F. Kline, John R. Alm, E. Liston
Bishop III, Rick L. Engum Patrick J. Mannelly, G.
David Van Houten, Jr., and Coca-Cola Enterprises,
Inc., Defendants Below, Appellees.

No. 601,2007.

Submitted: June 18, 2008.
Decided: June 20, 2008.

Court Below: Court of Chancery of the State of
Delaware, C.A. No.1927-CC.

Before STEELE, Chief Justice, BERGER and
RIDGELY, Justices.

ORDER

MYRON T. STEELE, Chief Justice.

*1 This 20th day of June 2008, upon consideration of
the briefs of the parties, and their contentions in oral
argument, it appears to the Court that the judgment of
the Court of Chancery should be affirmed on the basis

of and for the reasons set forth in its decision dated
October 17,2007.

NOW, THEREFORE, IT IS ORDERED that the
judgment of the Court of Chancery is **AFFIRMED**.

Del.Supr.,2008.
International Broth. Teamsters v. Coca-Cola Co.
Slip Copy, 2008 WL 2484587 (Del.Supr.)

END OF DOCUMENT

LEXSEE 2007 DEL. CH. LEXIS 147

IN RE COCA-COLA ENTERPRISES, INC. SHAREHOLDERS LITIGATION

CONSOLIDATED C.A. NO. 1927-CC

COURT OF CHANCERY OF DELAWARE

2007 Del. Ch. LEXIS 147

August 6, 2007, Submitted
October 17, 2007, Decided

NOTICE:

THIS OPINION HAS NOT BEEN RELEASED FOR PUBLICATION. UNTIL RELEASED, IT IS SUBJECT TO REVISION OR WITHDRAWAL.

SUBSEQUENT HISTORY: Affirmed by *Int'l Bhd. Teamsters v. Coca-Cola Co.*, 2008 Del. LEXIS 274 (Del., June 20, 2008)

CASE SUMMARY:

PROCEDURAL POSTURE: Plaintiff shareholders filed derivative actions against defendants, the soft drink company and the directors of the nominal defendant, a corporation which was the primary bottler and distributor of the soft drink company's products, alleging breaches of fiduciary duty. The shareholders filed an amended, consolidated complaint. The soft drink company and the directors filed motions to dismiss, pursuant to Del. Ch. Ct. R. 12(b)(6).

OVERVIEW: The soft drink company and the corporation which was the primary bottler and distributor of the soft drink company's products entered into a Master Bottle Contract in 1986 to govern their relationship. The shareholders alleged that the soft drink company and the directors worked together to abuse the relationship between the soft drink company and the corporation. The shareholders contended that by maximizing sales volume, the corporation had maximized the soft drink company's profits at the expense of the corporation's profits. The court found that the shareholders railed against particular actions that had occurred in the past three years, but those actions were the foreseeable results of the contract which was formed in 1986. The shareholders' claims were, therefore, time-barred, in accordance with the limitations period under *Del. Code Ann. tit. 10, § 8106*, because each claim hinged upon the allegations that the terms and conditions established by the contract

were unfair to the shareholders. Additionally, the shareholders failed to meet their burden of establishing that the statute of limitations had been tolled.

OUTCOME: The amended complaint was dismissed.

LexisNexis(R) Headnotes

Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Failures to State Claims
[HN1] On a motion to dismiss, a court may consider documents that are integral to the complaint.

Civil Procedure > Pleading & Practice > Pleadings > Complaints > Requirements
[HN2] An allegation is conclusory when it merely states a generalized conclusion with no supporting facts.

Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Failures to State Claims
[HN3] On a motion to dismiss, a court assumes that the well-pleaded allegations in a complaint are true, but does not accept the truthfulness of conclusory allegations.

Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Failures to State Claims
Civil Procedure > Pleading & Practice > Pleadings > Complaints > Requirements
[HN4] Del. Ch. Ct. R. 8(a) requires that pleadings give notice of the claim being asserted through a short and plain statement that shows the pleader is entitled to relief. When a complaint fails to do so, it must be dismissed under Del. Ch. Ct. R. 12(b)(6). In reviewing a motion to dismiss, a court must take as true all well-pleaded factual allegations and make every reasonable

inference in favor of the plaintiff. The court will not, however, give any credence to conclusory allegations or wildly speculative and unreasonable conjecture.

*Business & Corporate Law > Corporations > Directors & Officers > Management Duties & Liabilities > Fiduciary Responsibilities > General Overview
Civil Procedure > Pleading & Practice > Pleadings > Complaints > Requirements
Torts > Intentional Torts > Breach of Fiduciary Duty > Elements*

[HN5] To state a legally sufficient claim for breach of the duty of loyalty, plaintiffs must allege facts showing that a self-interested transaction occurred, and that the transaction was unfair to the plaintiffs.

*Business & Corporate Law > Corporations > Directors & Officers > Management Duties & Liabilities > Fiduciary Responsibilities > General Overview
Civil Procedure > Equity > General Overview
Governments > Courts > Authority to Adjudicate
Governments > Legislation > Statutes of Limitations > Time Limitations
Torts > Intentional Torts > Breach of Fiduciary Duty > Defenses*

[HN6] Courts of equity came into being because universally applicable legal rules are bound to work injustice in certain individual cases. As such, it would be antithetical for a court of equity to blindly apply a statute of limitations to bar equitable claims. Nevertheless, because equity follows the law, it is firmly established that a court of equity can and will apply a statute of limitations by analogy. In fact, the Supreme Court of Delaware has held that absent unusual circumstances, a court of equity will deny a plaintiff relief when suit is brought after the analogous statutory period. Where a plaintiff seeks money damages for breach of fiduciary duties, the claim will be subject to the three-year limitations period of *Del. Code Ann. tit. 10, § 8106* and an equity court need not engage in traditional laches analysis.

*Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Affirmative Defenses
Governments > Legislation > Statutes of Limitations > General Overview
Torts > Procedure > Commencement & Prosecution > General Overview*

[HN7] A statute of limitations sets a strict time period after which a claim, if not made, is barred. The doctrine of laches, on the other hand, bars a particular plaintiff from bringing a claim about which he had knowledge

where the plaintiff's unreasonable delay prejudiced a defendant. Laches is an intensely factual analysis.

*Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Affirmative Defenses
Governments > Legislation > Statutes of Limitations > General Overview
Torts > Procedure > Commencement & Prosecution > General Overview*

[HN8] The time fixed by the analogous statute of limitations is deemed to create a time period beyond which delay is presumptively unreasonable for purposes of laches.

*Civil Procedure > Equity > General Overview
Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Affirmative Defenses
Civil Procedure > Pleading & Practice > Defenses, Demurrers, & Objections > Failures to State Claims
Governments > Legislation > Statutes of Limitations > General Overview
Torts > Procedure > Commencement & Prosecution > General Overview*

[HN9] When the allegations of a complaint show an action was commenced too late, a defendant may properly seek dismissal under the statute of limitations or the doctrine of laches. The statute of limitations is used as a presumptive guide for an equity court.

*Governments > Legislation > Statutes of Limitations > Time Limitations
Torts > Procedure > Statutes of Limitations > Accrual of Actions > Occurrence of Tort*

[HN10] Under Delaware law, a plaintiff's cause of action accrues at the moment of the wrongful act—not when the harmful effects of the act are felt—even if the plaintiff is unaware of the wrong.

*Business & Corporate Law > Corporations > Shareholders > Actions Against Corporations > Derivative Actions > Enforcement of Corporate Rights
Business & Corporate Law > Corporations > Shareholders > Actions Against Corporations > Standing > Claim Presentation*

[HN11] *Del. Code Ann. tit. 8, § 327* requires ownership of stock contemporaneously with the wrongs challenged in a derivative suit.

Civil Procedure > Pleading & Practice > Pleadings > Complaints > Requirements

Governments > Legislation > Statutes of Limitations > Pleading & Proof
Governments > Legislation > Statutes of Limitations > Time Limitations
Governments > Legislation > Statutes of Limitations > Tolling
Torts > Procedure > Statutes of Limitations > Tolling > Equitable Estoppel

[HN12] When a complaint asserts a claim that is on its face barred by the statute of limitations, the plaintiffs bear the burden of pleading specific facts demonstrating that the statute was tolled. Equitable tolling will toll the statute of limitations for claims of wrongful self-dealing, even in the absence of actual fraudulent concealment, where a plaintiff reasonably relies on the competence and good faith of a fiduciary. Nevertheless, neither equitable tolling nor any other theory can toll the statute of limitations beyond the point at which the plaintiff had actual knowledge or should have been aware of the facts giving rise to the wrong.

COUNSEL: [*1] Norman M. Monhait, of ROSENTHAL, MONHAIT & GODDESS, P.A., Wilmington, Delaware; OF COUNSEL: James E. Miller, Patrick A. Klingman, and Karen M. Leser, of SHEPHERD, FINKELMAN, MILLER & SHAH, LLC, Chester, Connecticut; Scott R. Shepherd, James C. Shah, and Nathan Zipperian, of SHEPHERD, FINKELMAN, MILLER & SHAH, LLC, Media, Pennsylvania; Mark C. Gardy and James S. Notis, of GARDY & NOTIS, LLP, Englewood Cliffs, New Jersey; Nadeem Faruqi, of FARUQI & FARUQI, LLP, New York, New York; Craig B. Smith, of SMITH, KATZENSTEIN & FURLOW, LLP, Wilmington, Delaware, Attorneys for Plaintiffs.

Edward P. Welch and Jennifer C. Voss, of SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP, Wilmington, Delaware; OF COUNSEL: Jay B. Kasner, of SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP, New York, New York, Attorneys for Defendants The Coca-Cola Company, J. Alexander M. Douglas, Gary P. Fayard, Irial Finan, Steven J. Heyer, Robert A. Keller, James E. Chestnut, Joseph R. Gladden, Jr., and Deval L. Patrick.

Samuel A. Nolen, Srinivas M. Raju, and Michael R. Robinson, of RICHARDS, LAYTON & FINGER, P.A., Wilmington, Delaware; OF COUNSEL: Todd R. David, John A. Jordak, Jr., and Ambreen A. Delawalla, of ALSTON & BIRD LLP, Atlanta, [*2] Georgia, Attorneys for Nominal Defendant Coca-Cola Enterprises, Inc. and Defendants Fernando Aguirre, John R. Aim, E. Liston Bishop III, Howard G. Buffet, John L. Clendenin, James E. Copeland, Jr., Calvin Darden, Rick L. Engum, J. Trevor Eyton, Marvin J. Herb, L. Phillip Humann,

John E. Jacob, Donna A. James, Summerfield K. Johnston III, Summerfield K. Johnston, Jr., Jean-Claude Killy, Lowry F. Kline, Patrick J. Mannelly, Paula R. Reynolds, and G. David Van Houten.

OPINION

MEMORANDUM OPINION

CHANDLER, Chancellor

While there may never be a decisive victory in the Great American Cola Wars,¹ the plaintiffs in this action seem to think they got the wrong stock, baby--uh huh.² Plaintiffs, who are shareholders in Coca-Cola Enterprises, Inc. ("CCE"), the primary bottler and distributor of Coca-Cola products, conclude their fifty-page complaint with a lengthy and unfavorable comparison between the stock price performance of their company, CCE, with Pepsi Bottlers Group, its counterpart in the world of Pepsi. Dismayed that the Pepsi Bottlers Group has outperformed CCE despite the fact that the Coca-Cola Company ("Coke") has outperformed PepsiCo, plaintiffs have authored a tale of abuse spanning two [*3] decades, in which defendant Coke has, "[s]ince CCE's creation,"³ somehow high jacked the CCE board and forced its members to operate CCE solely to benefit Coke. Stripped of its histrionics, however, the amended complaint essentially alleges claims that challenge the fundamental nature of the relationship between Coke and CCE--a relationship that plaintiffs acknowledge was established over twenty years ago in a perpetual Master Bottle Contract. Sobered from their rhetorical high by defendants' motions to dismiss, plaintiffs have attempted to save their case by showing equitable tolling, but their attempt has not satisfied their burden. Consequently, for the reasons described later, plaintiffs' amended complaint is dismissed as time-barred.

¹ See *Pepsico, Inc. v. The Coca-Cola Co.*, 114 F. Supp. 2d 243, 245 (S.D.N.Y. 2000) (noting the fabled marketing battle between Coke and Pepsi).

² Cf. *The Pepsi Legacy 1990*, http://www.pepsi.com/ads_and_history/legacy/1990/1990.php (last visited Oct. 17, 2007) (recalling the Diet Pepsi Commercial featuring Ray Charles and the "Uh Huh Girls" singing "You've Got the Right One, Baby").

³ Am. Compl. P 1.

I. BACKGROUND

A. Procedural History

On February 7, 2006, [*4] the International Brotherhood of Teamsters filed a derivative action in this Court on behalf of CCE against Coke and current and

former members of the CCE board of directors alleging breaches of fiduciary duty. In March and April of the same year, two substantially similar complaints were filed here by Robert Lang and Natalie Gordon. Lang and Gordon moved to consolidate, and the Teamsters filed a competing consolidation motion. After a brief dispute between the plaintiffs, the three filed an amended, consolidated complaint on September 29, 2006. On October 16, 2006, defendants filed their motions to dismiss. Following briefing and oral argument, this is my decision on the motions.

B. Facts

Nominal defendant CCE is the largest bottler and distributor of Coke beverage products in the world. Initially formed as a wholly owned subsidiary of Coke, CCE was spun off in 1986 as an independent, public company. Its relationship with former parent Coke, of course, continued pursuant to a series of contracts and licensing agreements, the most important of which is the 1986 Master Bottle Contract ("MBC").

The MBC defines the contours of the relationship between CCE and Coke that persists today. ⁴ [*5] In addition to establishing that CCE may buy Coke's syrup and concentrate, bottle, and sell the soda, the MBC grants Coke certain rights and saddles CCE with certain responsibilities. For example, CCE must allow Coke representatives access to CCE facilities to conduct inspections to assure Coke that CCE is "complying with instructions" and other standards. ⁵ The MBC also provides that: (1) Coke has the right to pull the final product if it is not satisfied and can force CCE to recall the product after shipment; ⁶ (2) Coke has the right to set and revise prices of its concentrates and syrups; ⁷ (3) CCE must "develop and stimulate and satisfy fully the demand" for Coke beverages; ⁸ (4) CCE must "cooperate in and vigorously promote" all joint marketing programs with Coke; ⁹ (5) CCE must present for approval to Coke its "plans for the ensuing year" and the plans must be approved by Coke; ¹⁰ (6) CCE must report on its progress to Coke at least quarterly if not more frequently; ¹¹ (7) Coke may give to CCE technology it has or develops; ¹² and (8) CCE must furnish financial or other records to Coke upon request. ¹³

4 The Court may properly consider the contract in deciding this motion to [*6] dismiss because plaintiffs expressly refer to and rely on the contract in their amended complaint. *In re Dean Witter P'ship Litig.*, C.A. No. 14816, 1998 Del. Ch. LEXIS 133, 1998 WL 442456, at *6 n.46 (Del. Ch. July 17, 1998), *aff'd*, 725 A.2d 441 (Del. 1999); see also *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 860 A.2d 312, 320 (Del. 2004) ([HN1]

"On a motion to dismiss, the Court may consider documents that are 'integral' to the complaint"). The amended complaint references the MBC and its terms repeatedly. See Am. Compl. PP 6, 46, 55, 56, 66, 94-97.

5 MBC art. IV, P 11.

6 *Id.* at P 13.

7 *Id.* at art. V., P 14.

8 *Id.* at art. VI, P 17.

9 *Id.* at P 18.

10 *Id.* at P 20(a).

11 *Id.* at P 20(b).

12 *Id.* at art. XII, P 36.

13 *Id.* at P 40(c).

Plaintiffs allege that Coke and the directors of CCE have worked together to abuse the relationship between the two companies. At the heart of the amended complaint is the contention that by maximizing sales volume, CCE has maximized Coke's profits at the expense of CCE's. CCE's decisions to push for increased volume can only be explained, plaintiffs contend, by Coke and the individual defendants' desire to aid Coke's financial future. Connected to this core theme are arterial sections flowing with vitriol [*7] about Coke's domination, channel stuffing, and harmful experimentation in various warehouse delivery systems.

1. Coke's Alleged Domination and Abuse

Despite conceding that Coke has directly named just three of CCE's thirteen directors and that Coke owns just a thirty-six percent share of CCE, plaintiffs maintain that Coke controls and dominates CCE. Plaintiffs trace the history of this domination to CCE's origins in the mid-1980s.

Plaintiffs stuff much of the amended complaint with conclusory allegations of control and abuse. "[HN2] An allegation is conclusory when it merely states a generalized conclusion with no supporting facts. For example, the bald assertion that 'Coke ultimately controls virtually every aspect of CCE's operations and profitability in a manner designed to maximize Coke's own financial condition' is conclusory. That allegation does not explain how Coke controls CCE; it perfunctorily concludes that Coke exerts control without offering any support. Plaintiffs' amended complaint is riddled with similar, conclusory statements. ¹⁴

14 [HN3] On a motion to dismiss, this Court assumes that the well-pleaded allegations in a complaint are true, but does not accept the truthfulness [*8] of conclusory allegations. *In re Gen. Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 168 (Del. 2006).

15 Am. Compl. P 54.

16 See, e.g., Am. Compl. P 50 ("For all practical purposes, Coke controls CCE.").

There are, however, several substantive allegations of control and abuse. First, the MBC provides "Coke with the ability to manipulate its own financial condition from sales to CCE through, among other things, price changes, sales volume changes, financing terms, and other terms of payment and conditions."¹⁷ Second, Coke forces "CCE to pay a higher price for beverage base and concentrate than CCE otherwise would have paid" if the MBC were negotiated at arm's length.¹⁸ Third, a 2002 Sales Growth Initiative Agreement between Coke and CCE incentivized increased sales volume at the expense of profit by providing CCE with payments from Coke if it hit certain sales volume thresholds.¹⁹ Fourth, "Coke is directly involved in CCE's annual business planning process" and can manipulate this process by withholding its approval.²⁰

17 Am. Compl. P 55.

18 *Id.* at P 56.

19 *Id.* at PP 59-64.

20 *Id.* at PP 66-67.

2. Channel Stuffing

The plaintiffs define "channel stuffing" as "last minute forced sales increases," [*9]²¹ and argue that Coke pushed this practice on CCE. Plaintiffs allege that Coke caused CCE to engage in channel stuffing by giving advance warning of future price increases, giving discounts in price for increased orders in volume or other incentives for ordering more, and over-delivery of product. Plaintiffs cite as an example the fact that CCE allegedly parked numerous trailers filled with product in the parking lots of various accounts in the early 1990s. Plaintiffs contend that this practice persisted (albeit to a lesser extent) in 2004 in the Kansas City area and that CCE would count this parked product as having been sold.

21 *Id.* at P 85.

3. Wal-Mart Delivery

Finally, plaintiffs assert that the individual defendants and Coke forced CCE to change the way it delivers products to the Wal-Mart account. Previously, CCE and the other Coke bottlers utilized a direct store delivery distribution method whereby the bottlers could negotiate for the pricing and marketing of the beverages at each individual retail location. For large, national accounts (like Wal-Mart), CCE negotiated on behalf of all Coke's major bottlers. The amended complaint alleges that in 2004 Coke somehow "forced" CCE [*10] to test a new warehouse delivery system for the Wal-Mart account. In 2005, plaintiffs say, "Coke directed that CCE propose [to

the other bottlers] the switch to the Warehouse Delivery system" ²² for delivery of the Powerade energy drink for all Wal-Mart stores. Plaintiffs stress that CCE did so without following the proper notice procedures outlined in its agreement with the other bottlers and that this switch is detrimental to "the long-term best interests of CCE." ²³

22 Pls.' Answering Br. 9.

23 Am. Compl. P 112.

C. Defendants' Motions to Dismiss

Defendants have moved to dismiss the complaint pursuant to Court of Chancery Rule 12(b)(6) for failure to state a claim upon which relief can be granted and Rule 23.1 for failure to adequately plead demand futility. Defendants offer a litany of reasons to dismiss this action. First, defendants argue that the amended complaint is barred by the statute of limitations or the doctrine of laches, because plaintiffs' claims arise out of contractual agreements formed in the mid-1980s. Second, defendants assert that the amended complaint's allegations are factually insufficient to state a claim as a matter of law, because the allegations are conclusory [*11] and speculative. Third, defendants say that the CCE board of directors is comprised of a majority of independent directors and that the decisions challenged in the amended complaint were well informed and made in the exercise of sound business judgment.

D. Plaintiffs' Response

Plaintiffs obviously disagree. They challenge whether a statute of limitations / laches defense can appropriately be raised at this stage in the litigation and argue that, even if such a defense is properly presented now, it is inapplicable in this case. Further, plaintiffs stress that their allegations are legally sufficient and that demand would have been futile.

II. ANALYSIS

A. Standard of Review and Pleading Requirements

[HN4] Court of Chancery Rule 8(a) requires that pleadings give notice of the claim being asserted through a "short and plain statement" that shows "the pleader is entitled to relief." ²⁴ When a complaint fails to do so, it must be dismissed under Rule 12(b)(6). In reviewing a motion to dismiss, this Court must, as noted above, take as true all well-pleaded factual allegations and make every reasonable inference in favor of the plaintiff. The Court will not, however, give any credence to conclusory allegations [*12] or wildly speculative and unreasonable conjecture. ²⁵

24 Ct. Ch. R. 8(a).

25 See *Malpiede v. Townson*, 780 A.2d 1075, 1083 (Del. 2001).

Plaintiffs' amended complaint purports to state a cause of action for breach of the duty of loyalty against Coke²⁶ and the individual defendants. To establish a breach of the fiduciary duty of loyalty, plaintiffs must show that the defendants either (1) "stood on both sides of the transaction and dictated its terms in a self-dealing way," or (2) "received in the transaction a personal benefit that was not enjoyed by the shareholders generally."²⁷

26 Coke strenuously denies that it is a controlling shareholder of CCE and, therefore, denies that it owes any fiduciary duties. Because I have decided to dismiss the complaint on other grounds, I need not address this issue.

27 *Chaffin v. GNI Group, Inc.*, C.A. No. 16211-NC, 1999 Del. Ch. LEXIS 182, 1999 WL 721569, at *5 (Del. Ch. Sept. 3, 1999); see also *Joyce v. Cuccia*, C.A. No. 14953, 1997 Del. Ch. LEXIS 71, 1997 WL 257448, at *5 (Del. Ch. May 14, 1997) ([HN5] "To state a legally sufficient claim for breach of the duty of loyalty, plaintiffs must allege facts showing that a self-interested transaction occurred, and that the transaction was unfair to the plaintiffs.").

Immediately, [*13] the Court may dispose of the claim related to the distribution of beverages to Wal-Mart because the amended complaint manifestly fails to allege facts showing that a breach of the duty of loyalty occurred in connection with that transaction. The switch to a warehouse distribution arrangement with Wal-Mart was effected by an agreement between CCE (on behalf of the consortium of bottlers) and Wal-Mart. Plaintiffs have not alleged that either Coke or any of the individual defendants are somehow on Wal-Mart's side, nor are there any facts that show any of the defendants will derive a personal benefit from the transaction. Plaintiffs have included a conclusory assertion that this distribution arrangement will harm the long-term interests of CCE and will help Coke, but this amorphous allegation is insufficient.²⁸ By failing to allege facts showing the elements of a breach of the fiduciary duty of loyalty with respect to the Wal-Mart distribution arrangement, plaintiffs have failed to state a claim upon which relief can be granted.

28 If a complaint were held sufficient simply because it restates the legal elements of a particular cause of action, Rule 8(a) would be rendered meaningless. [*14] Plaintiffs need not offer prolix tales of abuse belabored by needless details, but plaintiffs must allege facts sufficient to show

that the legal elements of a claim have been satisfied.

Plaintiffs' other claims are supported by more robust factual allegations, but they are ultimately no more successful. Because plaintiffs' other claims are really complaints about the painful effects of the terms of the 1986 MBC, the claims accrued in 1986 and are time-barred.

B. Statute of Limitations and Doctrine of Laches

[HN6] Courts of Equity came into being because universally applicable legal rules are bound to work injustice in certain individual cases.²⁹ As such, it would be antithetical for a court of equity to blindly apply a statute of limitations to bar equitable claims.³⁰ Nevertheless, because "equity follows the law,"³¹ it is firmly established that this Court can and will apply a statute of limitations by analogy.³² In fact, the Supreme Court has held that "[a]bsent unusual circumstances, a court of equity will deny a plaintiff relief when suit is brought after the analogous statutory period."³³ Where, as here, a plaintiff seeks money damages for breach of fiduciary duties, the claim will [*15] "be subject to the three-year limitations period of 10 Del. C. § 8106" and this Court need not "engage in traditional laches analysis."³⁴

29 H. Jefferson Powell, "Cardozo's Foot": *The Chancellor's Conscience and Constructive Trusts*, 56 LAW & CONTEMP. PROBS. 7, 7-8 (1993).

30 [HN7] A statute of limitations sets a strict time period after which a claim, if not made, is barred. The doctrine of laches, on the other hand, bars a particular plaintiff from bringing a claim about which he had knowledge where the plaintiff's unreasonable delay prejudiced a defendant. Laches is an intensely factual analysis. See *Fed. United Corp. v. Havender*, 11 A.2d 331, 343 (Del. 1940) (noting that delays of even as short as two months have been held to constitute laches under Delaware law).

31 E.g., *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 584 (Del. Ch. 2007).

32 *Acierno v. Goldstein*, C.A. No. 20056, 2004 Del. Ch. LEXIS 82, 2004 WL 1488673, at *2 (Del. Ch. June 29, 2004) ([HN8] "The time fixed by the analogous statute of limitations is deemed to create a time period beyond which delay is presumptively unreasonable for purposes of laches."); *Fike v. Ruger*, 754 A.2d 254, 260 (Del. Ch. 1999), *aff'd*, 752 A.2d 112 (Del. 2000); [*16] *In re MAXXAM, Inc.*, 659 A.2d 760, 769 (Del. Ch. 1995); *Bovay v. H. M. Byllesby & Co.*, 27

Del. Ch. 33, 29 A.2d 801, 803 (1943); see also 27A AM. JUR. 2D Equity § 198 (West 2007).

33 *U.S. Cellular Inv. Co. of Allentown v. Bell Atl. Mobile Sys., Inc.*, 677 A.2d 497, 502 (Del. 1996).

34 *Atlantis Plastics Corp. v. Sammons*, 558 A.2d 1062, 1064 (Del. Ch. 1989).

Defendants argue that the claims in the amended complaint all arise from the 1986 MBC. As such, defendants contend, those claims are time-barred under section 8106. Plaintiffs have three responses. First, plaintiffs argue that defendants may not use the statute of limitations or the doctrine of laches as a defense in a motion to dismiss. Second, plaintiffs say their claims are based on discrete actions that occurred within the past three years rather than on the 1986 contract. Third, plaintiffs contend that if the statute of limitations applies, it has been equitably tolled. For the reasons stated below, none of these responses is persuasive and the claims in the amended complaint are barred under section 8106.

1. This Court May Properly Consider the Statute of Limitations and the Doctrine of Laches when Reviewing a Motion to Dismiss.

Plaintiffs devote considerable [*17] energy attempting to persuade this Court that a motion to dismiss is an improper mechanism by which one might determine whether claims are time barred. In so doing, plaintiffs (at best) misunderstand or (at worst) disregard well settled Delaware law. As this Court has stated time and time again, [HN9] when the allegations of a complaint show the action was commenced too late, a defendant may properly seek dismissal under the statute of limitations or the doctrine of laches. Plaintiffs have in fact correctly conceded that the statute of limitations is used as a presumptive guide for this Court, * but plaintiffs have failed to overcome that presumption. The allegations of the amended complaint itself affirmatively establish the plaintiffs' claims are based on the 1986 MBC.

35 *E.g., Tyson Foods*, 919 A.2d at 585; *Kahn v. Seaboard*, 625 A.2d 269, 277 (Del. Ch. 1993); *Boeing Co. v. Shrontz*, C.A. No. 11273, 1992 Del. Ch. LEXIS 84, 1992 WL 81228, at *2 (Del. Ch. Apr. 20, 1992); see also 1 R. FRANKLIN BALLOTTI & JESSE A. FINKELSTEIN, *THE DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS* § 13.8 (3d ed., supp. 2006).

36 Pls.' Answering Br. at 17.

2. The Wrath of Kahn: Claims Accrue at the Moment of Initial Wrongdoing--Not [*18] when their Effects Are Felt.

In *Kahn v. Seaboard Corp.*, Chancellor Allen dismissed a complaint that alleged a breach of fiduciary duty claim against directors who "structure[d] the contract] so as to obtain better terms for Flour than would have been the case had the transactions been negotiated on an arm's length basis." * Specifically, he found that "[t]he wrong attempted to be alleged is the use of control over Seaboard to require it to enter into a contract that was detrimental to it and beneficial, indirectly, to the defendants. Any such wrong occurred at the time that enforceable legal rights against Seaboard were created." * Ultimately, it is that principle that dooms plaintiffs' amended complaint.

37 625 A.2d 269, 270 (Del. Ch. 1993) (quoting complaint).

38 *Id.* at 271.

[HN10] Under Delaware law, a plaintiff's cause of action accrues at the moment of the wrongful act--not when the harmful effects of the act are felt--even if the plaintiff is unaware of the wrong. * Defendants contend plaintiffs' claims of abuse by Coke and so-called "channel stuffing" are really challenges to the 1986 MBC. Plaintiffs, of course, resist this characterization. Instead, plaintiffs counter, their complaint [*19] challenges certain transactions that occurred within the last three years. Specifically, they challenge: (1) a 2002 Sales Growth Initiative Agreement that incentivized increased volume in sales; (2) the revisions to the 2004 Rocky Mountain Division business plan; (3) the use of databases by Coke to track daily CCE sales; and (4) channel-stuffing practices.

39 *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 860 A.2d 312, 319 (Del. 2004) ("This Court has repeatedly held that a cause of action 'accrues' under Section 8106 at the time of the wrongful act, even if the plaintiff is ignorant of the cause of action."); *Albert v. Alex Brown Mgmt. Servs., Inc.*, C.A. No. 762-N, 2005 Del. Ch. LEXIS 100, 2005 WL 1594085, at *18 (Del. Ch. June 29, 2005) ("The court reiterates that a claim accrues at the time of the alleged wrongdoing, and not when the plaintiff suffered a loss."); *Fike v. Ruger*, 754 A.2d 254, 260 (Del. Ch. 1999) ("A cause of action accrues at the moment of the wrongful act, even if the plaintiff is ignorant of the wrong."), *aff'd*, 752 A.2d 112 (Del. 2000); *In re Dean Witter P'ship Litig.*, C.A. No. 14816, 1998 Del. Ch. LEXIS 133, [WL] at *4 (Del. Ch. July 17, 1998) ("The general law in Delaware is that the Statute of Limitations [*20] begins to run, i.e., the cause of action accrues, at the time of the alleged wrongful act, even if the plaintiff is ignorant of the cause of action."), *aff'd*, 725 A.2d

441 (Del. 1999); cf. *Schreiber v. R.G. Bryan*, 396 A.2d 512, 516 (Del. Ch. 1978) ("[W]hat must be decided is when the specific acts of alleged wrongdoing occur, and not when their effect is felt."); 2 EDWARD P. WELCH, ET AL., *FOLK ON THE DELAWARE GENERAL CORPORATION LAW* § 327.3.2 (2007-1 supp.) ("Generally, the determinative issue is when the specific acts of alleged wrongdoing occurred, and not when their effect is felt.").

The claim challenging the 2002 Sales Growth Initiative is clearly time-barred under the three-year statute of limitations. The amended complaint quotes from the agreement itself and challenges actual provisions and terms of the contract. Plaintiffs appear to have conceded as much by abandoning this argument in their answering brief.

The claim challenging the revisions to the 2004 Rocky Mountain Division Business Plan is also time barred. Plaintiffs argue that in 2004 Coke forced CCE to revise the plan to push for an increase in sales volume at the expense of CCE's profits. Under the 1986 MBC, however, [*21] CCE is *obligated* to submit its annual plans to Coke and those plans must be approved by Coke.⁴⁰ The revised plan did not call for a waste of CCE's assets or resources; rather, it called for a 5.5% gross profit gain combined with an increase in projected sales volumes instead of the 7.3% gain combined with a decrease in projected sales called for in the original plan. This was clearly permitted and expected under the terms of the 1986 MBC. If plaintiffs have a valid claim on this point, they had it in 1986.

40 MBC art. VI, P 20(a).

The claim challenging the use of databases by Coke to track sales of CCE also appears to have been abandoned by plaintiffs. Even if it were not, the use of databases provided by Coke to CCE is clearly permitted by and contemplated in the 1986 MBC. "Again, if there is a valid claim, it is a claim that existed in 1986.

41 See *id.* at art. XII, P 36.

Finally, the crux of the claim challenging the alleged channel stuffing is that "Coke routinely has forced CCE to purchase additional beverage base or concentrate beyond CCE's immediate needs, and/or has raised prices on such materials, without adequate notice, all in order to improve Coke's own financial condition [*22] and meet Coke's earnings guidance and sales volume projections." "Coke has every right, however, under the 1986 MBC to "revise at any time, in its sole discretion, the price of any of the Concentrates or Syrups, the terms of payment, and other terms and conditions of supply, any such revision

to be effective immediately upon notice to the Bottler." "Plaintiffs have alleged only that Coke exercised its rights under the contract.

42 Am. Compl. P 85.

43 MBC art. V, P 14(a).

Each one of these claims is, therefore, time-barred because each "hinges upon the allegations that the terms and conditions established by a contract are unfair to the plaintiff[s]." "Plaintiffs attempt to avoid dismissal by claiming that they are challenging the actions taken in the last three years," but concede that the contract "may have provided the means by which the Defendants effectuated their breaches of fiduciary duty." "Plaintiffs took a similar position (and made a similar concession) at oral argument." "This is precisely the argument considered and rejected by Chancellor Allen in *Kahn*" and by the Federal District Court in *Marvel*. "I likewise reject it. The actions challenged in the amended complaint [*23] represent the manifestation of the bargain struck in 1986 between Coke and CCE." "Absent tolling, therefore, these claims are barred by section 8106."

44 *In re Marvel Entm't Group, Inc.*, 273 B.R. 58, 74 (D. Del. 2002) (interpreting Delaware law).

45 Plaintiffs' reliance on *Teachers' Ret. Sys. of La. v. Aidinoff* is misplaced. There, the Court found a claim based on actions taken under a contract was not time-barred because the contract had a provision that granted an annual right of termination. 900 A.2d 654, 666 (Del. Ch. 2006). The Court found that the complaint was actually challenging the decision of the defendants to continue to honor the harmful contract when they could have opted out each year. *Id.* Here, the plaintiffs admit that the MBC is perpetual. Am. Compl. P 95; MBC art. VIII, P 24.

46 Pls.' Answering Br. at 21.

47 Transcript of Oral Argument at 53.

48 *Kahn v. Seaboard Corp.*, 625 A.2d 269, 271 (Del. Ch. 1993).

49 *Marvel*, 273 B.R. at 74.

50 Compare *Kahn*, 625 A.2d at 270 (quoting complaint: "defendants have violated their duty of loyalty by structuring such transaction so as to obtain better terms for Flour than would have been the case had the transaction been negotiated on an arm's-length [*24] basis"), with Am. Compl. P 56 ("Coke also requires CCE to pay a higher price for beverage base and concentrate than CCE otherwise would have paid to Coke if CCE's beverage base agreements with Coke had been negotiated at arms' length").

51 Plaintiffs' claims may also be barred under [HN1] 8 Del. C. § 327, which requires owner-

ship of stock contemporaneously with the wrongs challenged in a derivative suit. Plaintiffs have only alleged that they owned CCE stock from October 15, 2003, to the present, but the wrong actually complained of is the 1986 MBC. See 7547 *Partners v. Beck*, 682 A.2d 160 (Del. 1996) (strictly applying section 327 to bar a derivative suit).

3. Plaintiffs Have Not Met their Burden of Establishing that the Statute has Been Equitably Tolled.

[HN12] When a complaint asserts a claim that is, as here, on its face barred by the statute of limitations, plaintiffs bear the burden of pleading specific facts demonstrating that the statute was tolled. "Equitable tolling will toll the statute of limitations 'for claims of wrongful self-dealing, even in the absence of actual fraudulent concealment, where a plaintiff reasonably relies on the competence and good faith of a fiduciary.'" "Nevertheless, [*25] neither equitable tolling nor any other theory can toll the statute of limitations beyond the point at which the plaintiff had actual knowledge or should have been aware of the facts giving rise to the wrong."

52 *In re Dean Witter P'ship Litig.*, C.A. No. 14816, 1998 Del. Ch. LEXIS 133, [WL] at *6 (Del. Ch. July 17, 1998), *aff'd*, 725 A.2d 441 (Del. 1999); *Yaw v. Talley*, C.A. No. 12882, 1994 Del. Ch. LEXIS 35, [WL] at *6 (Del. Ch. Mar. 2, 1994).

53 *Dean Witter*, 1998 Del. Ch. LEXIS 133, [WL] at *6; see also *Kahn*, 625 A.2d at 275.

54 *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 585 (Del. Ch. 2007) ("Even where a defendant uses every fraudulent device at its disposal to mislead a victim or obfuscate the truth, no sanctuary from the statute will be offered to the dilatory plaintiff who was not or should not have been fooled.").

Plaintiffs summarily state that they "did not know or have reason to know of Defendants' self-interested wrongdoing prior to 2004." "The amended complaint itself, however, belies that assertion by relying on and quoting from documents publicly filed with the SEC prior to 2004." "Moreover, plaintiffs undercut their own argument with the affected rhetoric of the complaint's allegations. In the amended complaint, [*26] plaintiffs conjure images of the long-suffering whipping boy CCE, mistreated "[s]ince [its] creation" "by Coke, whose abuses are recounted by CCE's former employees with

"unanimity." "With respect to the channel stuffing allegations, the amended complaint details practices from the 'early 1990s,' " and it chronicles Coke's alleged domination from the 1980s to the present. "Finally, Coke and CCE have publicly disclosed their agreements with one another and their individual finances in filings under the Federal securities laws. The plaintiffs have railed against particular actions that have occurred in the last three years, but those actions were the foreseeable results of a contract formed in 1986. Intermittently, plaintiffs seem to acknowledge as much. "As in *Tyson*, "[i]f plaintiffs believed that these contracts were unfair, they could reasonably have been aware of their injuries in [1986]." "Consequently, plaintiffs have failed to meet their burden of establishing that the statute of limitations has been tolled.

55 Pls.' Answering Br. at 20.

56 See, e.g., Am. Compl. PP 62-64.

57 *Id.* at P 1.

58 *Id.* at PP 68-73.

59 *Id.* at P 91.

60 *Id.* at PP 46-49.

61 See Pls.' Answering Br. at 21 (admitting [*27] that the MBC "may have provided the means by which the Defendants effectuated their breaches of fiduciary duty"); Transcript of Oral Argument at 53 ("[W]e believe that the control arises as a result of the contractual relationships and the actions taken pursuant to those contractual relations . . .").

62 *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 586 (Del. Ch. 2007).

III. CONCLUSION

CCE's relationship with Coke may not be optimal, but it is guided by a contract formed in 1986. If the plaintiffs in this action or if CCE's shareholders in general believe it is time CCE took a more aggressive, competitive stance vis-a-vis Coke, they ought to put pressure on management; they cannot seek to do so by dressing up their frustration in the guise of fiduciary duty claims. Because the amended complaint objects to so-called wrongs that all rationally flow from Coke and CCE's 1986 agreement, plaintiffs' claims accrued in 1986. Because plaintiffs have alleged facts that show they either were or should have been aware of these claims for far more than three years before filing this action, the amended complaint is dismissed as time-barred.

IT IS SO ORDERED.

STATE OF SOUTH CAROLINA

COUNTY OF GREENVILLE

Brian P. Menezes,

Plaintiff,

v.

WL Ross & Co. LLC, Wilbur L. Ross,
Jr., Michael J. Gibbons, David H. Storper,
David L. Wax, Joseph L. Gorga, Stephen
B. Duerk, WLR Recovery Fund II, L.P.,
WLR Recovery Fund III, L.P., WLR
Recovery Associates II LLC, and WLR
Recovery Associates III LLC,

Defendants.

IN THE COURT OF COMMON PLEAS

C.A. No. 2008-CP-23-2701

**Plaintiff's Second Memorandum In
Opposition To Defendants' Motion To
Dismiss**

Defendants' opening Memorandum neglected to mention the only three cases that actually addressed the question presented here. As previously demonstrated by Plaintiff, those cases hold unequivocally, as one would expect, that a claim like Plaintiff's for breach of fiduciary duty in connection with a merger hold accrues upon the closing of the merger. See Kaufman v. Albin, 447 A.2d 761 (Del. Ch. 1982); Baron v. Allied Artists Pictures Corporation, 717 F.2d 105 (3d Cir. 1983); and Dofflemeyer v. W.F. Hall Printing Co., 558 F. Supp. 372 (D. Del 1983).

Defendants' Reply Memorandum includes further argument in support of its motion and attempts to distinguish those cases. For the reasons set forth below, the arguments are without merit. Plaintiff respectfully submits that Defendants' Motion to Dismiss should be denied.

I. General Delaware Law Regarding Accrual of Tort Claims

There is nothing particularly unusual about Delaware's law on the accrual of tort claims. The long-standing principle is that such claims "accrue at the time of the injury." Nardo v. Guido

DeAscanis & Sons, Inc., 254 A.2d 254, 256 (Del. Super. Ct. 1969) (emphasis added) (“A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of the injury.”). See also, e.g., Kaufman v. C.L. McCabe & Sons, Inc., 603 A.2d 831 (Del. 1992) (“A cause of action in tort accrues at the moment when “an injury, although slight, is sustained in consequence of the wrongful act of another....”); Krahmer v. Christie’s Inc., 903 A.2d 773 (Del. Ch. 2006) (“For tort claims, a cause of action accrues at the time of the injury.”); State ex rel. Secretary of Dept. of Transp. v. Regency Group, Inc., 598 A.2d 1123, 1128 (Del. Super. 1991) (“Tort actions accrue at the time of injury.”); City of Newark v. Edward H. Richardson Associates, Inc. 375 A.2d 475, 476 (Del. Super. 1977) (“It has been held repeatedly that tort actions accrue at the time of the injury and that the statute of limitations begins to run at that time.”); Freedman v. Beneficial Corporation, 406 F. Supp. 917 (D. Del. 1975) (“Causes of action sounding in tort, such as this one, accrue at the time of injury.”); Howmet Corp. v. City of Wilmington, 285 A.2d 423, 425 (Del. Super. 1971) (citing Nardo).

Indeed, while in a contract case it is the “breach” which is the wrongful act, in a tort case it is the “injury” that is the “wrongful act.” Bilinski v. Farmers Bank of State, 1982 WL 172848, *2 (Del. Super. 1982) (“In Delaware it is well settled that the limitations period begins to run at the time of the wrongful act. . . . A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of injury.”)

II. The Coca-Cola Case, Recently Affirmed By The Delaware Supreme Court, Illustrates How These Principles Apply In A Case Involving An Underlying Contract.

On June 20, 2008, the Delaware Supreme Court in Int’l Bhd. Teamsters v. Coca-Cola Co., 2008 WL 2484587 (Del. Sup. 2008), affirmed the decision of the chancery court in In re Coca-Cola Enterprises, Inc., 2007 WL 3122370 (Del. Ch. 2007).

The Coca-Cola case involved a “Master Bottle Contract” between the Coca-Cola Company and one of its distributors that had been entered into in 1986. The plaintiffs were complaining “about the painful effects of the terms of the 1986 MBC” (2007 WL 2484587 *4.) There were apparently no conditions precedent to performance of the contract and thus no “closing” after it was signed. “Execution” and “closing” were one and the same. The court, relying on Kahn v. Seaboard Corporation, 625 A.2d 269 (Del. Ch. 1993), held that the wrong “occurred at the time that enforceable legal rights . . . were created.” 625 A.2d at 271. Accordingly, the plaintiff’s claims accrued [in 1986] when the MBC contract had been entered into since that was when “enforceable legal rights . . . were created.”

To fully understand this, it is helpful to look at the Kahn decision. That case was a derivative action against the controlling stockholder and three members of the board of Seaboard Corporation. The alleged wrong was the defendants’ use of their control over Seaboard to cause it to enter into a ten-year lease contract that was detrimental to it and beneficial to them. As in Coca-Cola, there were apparently no conditions precedent to performance of the contract, no “closing” after it was signed, and “execution” and “closing” were one and the same. The defendants argued that the claims were barred by the statute of limitations. The chancery court held that the wrong “occurred at the time that enforceable legal rights against Seaboard were created.” 625 A.2d at 271. Accordingly, the claims had accrued when the 1986 contract was entered into and were time-barred.

Among other things, it is interesting that under the theory of Defendants here, the claims in Coca-Cola and Kahn (and Wal-Mart¹ which Defendants also cite) would have accrued even earlier, when the defendants there authorized entry into the contracts at issue.

¹ Wal-Mart Stores, Inc. v. AIG Life Ins. Co., 860 A.2d 312 (Del. 2004), involved Wal-Mart’s purchase of various life insurance (“COLI”) policies between 1993 and 1995. The company alleged that the defendants failed to disclose material facts and risks of the plan to purchase the COLI policies. 860 A.2d at 317. As in Coca-Cola and

III. Under The Coca-Cola Case, Plaintiff's Claims Could Not Have Accrued Prior to the Closing of the Merger.

Under Coca-Cola and Kahn (and Wal-Mart) there could not possibly have been a breach of fiduciary duty claim by Plaintiff until FITG had "legal rights" to "enforce[]" the item being complained about, *i.e.*, the merger. A quick look at the Merger Agreement, as noted in Plaintiff's prior memorandum (pp. 4-7), reveals that there were many conditions that had to be satisfied before the Merger could have been enforced:

"Conditions to Each Party's Obligation To Effect the Merger
The respective obligation of each party to effect the merger is subject to the satisfaction or waiver on or prior to the Closing Date of the following conditions . . ."

(Proxy at 82, emphasis added.) Among others, FITG's stockholders had to approve the merger, SCI's stockholders had to approve the amendment to its certification of incorporation, and the escrow agreement had to be duly executed by both companies. These conditions were not satisfied until the Closing Date on October 20, 2006. (Plaintiff's Mem. In Opp. at 7.) Further, FITG's representations and warranties had to be accurate on the Closing Date and there had to be no "material adverse changes" in its business. (Proxy at A-36.²) Those conditions, as alleged at length in the Complaint (*See, e.g.*, ¶¶50-54, 56, 58, 59, 62, 64, & 67-71), were never satisfied and could never have been satisfied. As such, the Merger, like so many other proposed mergers, should have been one that went "bust."³

Kahn, there were apparently no conditions precedent and no "gap" between the "execution" of the contracts and the "closing." The court held that Wal-Mart's claim had accrued when it purchased the COLI policies, which would have been the point at which those contracts were enforceable against it. Again, as in Coca-Cola, it is noteworthy that the court did not hold, as would be expected if Defendants theory in this case were correct, that the claim accrued even earlier when the defendants had received proposals from various insurance companies and recommended that Wal-Mart the purchase the COLI policies of AIG and Hartford. 860 A2d. at 315.

² See list of conditions for FITG alone at note 10 below.

³ It is not uncommon for mergers to go "bust" and not be consummated. The financial press tracks this carefully. *See*, "Buyouts Gone Bust," a six-page report at Exhibit A hereto: www.thedeal.com/dealscape/2008/06/dealwatch_buyouts_gone_bust.php.

Accordingly, FITG could not have had any right to enforce the Merger before October 20, 2006, at the earliest (and only then if the financial conditions were waived, which would have been a breach of fiduciary duty itself). Weiss v. Northwest Broadcasting Inc., 140 F. Supp. 2d 336 (D. Del. 2001) (“As a general matter, a condition precedent is an act or event, other than a lapse of time, which, unless the condition is excused, must occur before a duty to perform a promise in the agreement arises.”), citing Gilbert v. El Paso Co., 575 A.2d 1131, 1142 (Del. 1990).

In this respect, the merger transaction was much like a contract to purchase a house. Such a contract is not “enforceable” until all the conditions to closing are satisfied (financing, home inspection, termite letter, etc.) and the closing date has come and gone.

Under Coke, as under Kahn, Plaintiff could have had no breach of fiduciary duty claim until FITG had “legal rights” to “enforce[]” the Merger Agreement. Since FITG had no such rights before the Closing Date at the earliest, and since the Closing Date was after the date of the Release, plaintiff’s claims could not have accrued prior to the date of the Release. Hence, they were not covered by the Release.

IV. The Only Three Cases To Address The Issue Have Held That Claims Like Plaintiffs’ Accrue Upon The Closing Of The Merger, Just As The Coca-Cola Case Dictates, And Defendants’ Efforts To Distinguish Those Cases Are Ineffectual.

As the discussion of Coca-Cola above shows, under Delaware law, the Plaintiff’s claim could not possibly have arisen prior to the Close Date because the underlying Merger Agreement was not “enforceable” before that time. As shown in Plaintiff’s prior memorandum, the only three cases to address this issue have reached that same conclusion.

As previously pointed out, the Delaware Chancery Court explicitly addressed the issue in Kaufman v. Albin, 447 A.2d 761 (Del.Ch. 1982). The chancery court first looked to general

principles as outlined in CJS and AmJur.⁴ Then it noted that Folk's The Delaware General Corporation Law (1967, page 487), had stated that "if the action complained of requires shareholder approval, the transaction is not complete until the shareholders have approved of it." 447 A.2d at 764. And finally it referred to Lavine v. Gulf Coast Leaseholds, 122 A.2d 550 (Del.Ch. 1956), which held that "where exchanges of stock are contingent upon shareholder approval, the transaction is not completed until the shareholder vote takes place." Based on these principles, Kaufman held that the transaction had "commenced with the adoption of the two resolutions on August 22, 1977 [by the board authorizing the merger], but was not consummated until October 2, 1977 [when sufficient shares were tendered and the merger was successfully concluded]." 447 A.2d at 764 (emphasis added)." Accordingly, it had accrued upon the closing of the merger.

Defendants' only basis for distinguishing Kaufman was that it "did not concern a negotiated merger, as this case does, but rather just a tender offer," and that, unlike in Kaufman, "the complete merger terms [here] were settled by agreement and approved by the Defendants." (Reply at 9.) This argument is wrong in two respects. First, while the merger in Kaufman was in the form of a tender offer, the facts show that in Kaufman, just as here, the merger was agreed to and approved by the defendant-directors. As the court notes, the directors received and "reviewed the terms of a proposed tender offer," "determined that the price was fair and voted unanimously to recommend [it] to all stockholders" 447 A.2d at 762.

Second, the logic of the Kaufman decision is, frankly, even more compelling here than it was there. This is because in Kaufman there was only one condition precedent to the "closing," namely, the tendering of shares by the shareholders. Here, in great contrast, there were pages and pages of

⁴ "Where a party's right depends on the happening of an event in the future, the cause of action accrues, and the statute of limitations begins to run, only at the time when the event happens." C.J.S., Limitation of Actions, §110 (1948).

"If a right of action depends upon some contingency or a condition precedent, the cause of action does not accrue and the statute of limitations does not begin to run until that contingency occurs or the conditions precedent is complied with." Am.Jur., Limitations of Actions, § 127 (1979).

conditions precedent to the closing, including shareholder approval and no material adverse changes. (See Part III above.) If the one condition in Kaufman meant that the claim did not accrue until closing, the myriad conditions here surely mean the same thing.

Accordingly, Kaufman stands as a clear and unchallenged statement from the Delaware Chancery Court that a breach of fiduciary duty claim regarding a merger accrues at the closing of the merger.

To the same effect is the Third Circuit United States Court of Appeals' decision in Baron v. Allied Artists Pictures Corporation, 717 F.2d 105 (3d Cir. 1983), the only appellate decision regarding the issue. The precise question there was whether a shareholder's action based on false and misleading materials effecting a merger accrued when the shareholder had knowledge of the falsity or later when the merger was consummated. The trial court had held that the cause of action accrued when the shareholder knew of the falsity and that, since that was more than three years before he had brought the lawsuit, the lawsuit was time-barred. The court of appeals reversed and held that it accrued when the merger was consummated.

Defendants argue that Baron involves federal law, which they imply is different than Delaware law, and is therefore inapplicable. However, as the court of appeals noted, the claim at issue was "in the nature of" an action for "damages for breach of fiduciary duty" under Delaware law. Id. at 108. Moreover, the court's opinion as to when the claim accrued was premised on a "rule of general application" which, it found, Delaware "adheres to":

It is a rule of general application that a cause of action for the recovery of damages accrues only when it could be prosecuted to a successful conclusion. E.g., United States v. Wurts, 303 U.S. 414, 418, 58 S. Ct. 637, 82 L. Ed. 932 (1938)⁵; Grayson v.

⁵ In Wurts, the United States Supreme Court in wrote: "It would require language so clear as to leave room for no other reasonable construction in order to induce the belief that Congress intended a statute of limitations to begin to run before the right barred by it has accrued. Obviously, the Government had no right to sue this taxpayer to recover money before money had been paid to him. The construction urged by respondent would allowed the statute of limitations to begin to run against recovery on an erroneous payment before any such payment is made." 303 U.S. 414, 418 (1938).

Harris, 279 U.S. 300, 304-05, 49 S. Ct. 306, 73 L. Ed. 700 (1929); City of Philadelphia v. Lieberman, 112 F.2d 424, 428 (3d Cir.1940). Delaware, whose statute of limitations governs, adheres to that rule. "A cause of action for breach of contract accrues at the time of the breach and a cause of action in tort accrues at the time of the injury." Nardo v. Guido DeAscanis & Sons, Inc., 254 A.2d 254, 256 (Del. Super. Ct.1969). The state recognizes "the basic rule that, in general, the statute of limitations begins to run from the date of the injury caused by the defendant "Lembert v. Gilmore, 312 A.2d 335, 337 (Del. Super. Ct. 1973). The United States District Court in Delaware has consistently recognized as much. Rose Hall, Ltd. v. Chase Manhattan Overseas Bank, 494 F. Supp. 1139, 1157 (D. Del.1980); Oliver B. Cannon & Son, Inc. v. Fidelity & Casualty Co., 484 F. Supp. 1375, 1388 (D. Del. 1980); Freedman v. Beneficial Corp., 406 F. Supp. 917, 922 (D. Del.1975).

Id. at 108 (emphasis added). Accordingly, defendants' attempt to distinguish Baron is without merit.

The third case directly on point is Dofflemeyer v. W.F. Hall Printing Company, 558 F. Supp. 372 (D.Del. 1983). It involved a merger which was approved by the defendant directors on November 27, 1978. As here, the approval was followed on January 29, 1979, by the distribution of a Proxy statement to the shareholders. The merger was approved by shareholder vote and became effective on February 21, 1979. Id. at 375. Like Defendants here, the defendants there argued that the breach of fiduciary duty claims accrued when the board approved the merger agreement and not when the merger was consummated. The court of appeals disagreed. It held that the claim accrued when the merger closed since "the merger transaction which is the subject of this suit was not accomplished and no injury occurred until the merger was effected." Id. at 379 (emphasis added). As the court noted, "[i]t is a basic principle of limitations law that a cause of action does not accrue before the right to institute suit arises." Id. at 379 (citing C.J.S., Limitations of Actions, §109.) The court then observed that "[t]he plaintiffs could not have sued for damages until the merger was actually accomplished – until that time, they had suffered no injury by the defendants' acts." Id. (emphasis added). Since they had not suffered any injury until the merger was consummated, their claim did not accrue until then.

Defendants are unable to distinguish Dofflemyer in any respect. Instead, they assert that “this 25-year-old federal case is simply out of step with subsequent Delaware Supreme Court precedent.” (Reply at 8.) Defendants do not, however, cite any “Delaware Supreme Court precedent” to support that assertion. Plaintiff assumes, in light of other parts of Defendants’ papers, that they must be referring to the Coca-Cola case. However, the holding of that case (that the cause of action “accrued” when the underlying contract became “enforceable” – see Part II above) could hardly be more in line with Dofflemyer’s holding that the claims did not accrue until closing since that would be the earliest date the merger agreement would be “enforceable.”

Moreover, contrary to Defendants’ implication, Dofflemyer has not stood alone, un-cited, and ignored for 25 years. It was followed as recently as 1997 in Montgomery v. Aetna Plywood, Inc., 956 F.Supp. 781 (N.D. Ill. 1997), another case which Defendants have ignored. The question there was whether, under Delaware law, a breach of fiduciary duty claim against a company’s directors regarding a stock repurchase accrued at the time of the repurchase or earlier when the board authorized the repurchase. The court, relying on Dofflemyer and Kaufman, held that the claim “accrued” upon the “consummation of the sale,” not at the time of the resolution authorizing it. Id. at 787. In addition, the relevant part of Dofflemyer was recently quoted by the Delaware Court of Chancery as an apparently accurate statement of Delaware law in a case that is not otherwise relevant here. Bren v. Capital Realty Group Senior Housing, Inc., 2004 WL 370214, *4 (Del. Ch. Feb. 27, 2004) (noting that in Dofflemyer, the plaintiffs “could not sue for damages until the merger was consummated. Prior to that time plaintiffs had suffered no injury from the defendants’ acts.” (emphasis added)).

Defendants’ suggestion that Dofflemyer is inconsistent with Albert v. Alex. Brown Mgmt. Servs., Inc., 2005 Del. Ch. LEXIS 100, 2005 WL 1594085 (June 29, 2005), is well off-the-mark. Albert involved two investment funds that the plaintiffs had invested in. The plaintiff

alleged, among other things, that the defendants violated their fiduciary duty by “unhedging” the investment funds. 2005 Del. Ch. LEXIS 100, *44-45. What is quite interesting is that there was obviously a gap between when the defendants decided to stop “hedging” the funds and when they actually did stop.⁶ Under the theory of Defendants here, the claim in Albert would have accrued when the defendants made the decision to stop hedging. The court, however, held that it accrued “at the time the Funds became unhedged.” 2005 Del. Ch. LEXIS 100, *45, 2005 WL 1594085, *14. That’s when there was “harm” or “injury.” As such, it is precisely consistent with Dofflemyer and Coca-Cola.

Albert is even more clearly consistent with Dofflemyer when one looks at how the court treated the first claim in the case. The first claim was that “the Managers breached their fiduciary duties in initially screening the stocks allowed into the Funds, failing to properly diversify the Funds, and that, generally, the entire structure of the Fund[s] was fatally flawed from the outset.” (Id., 2005 Del. Ch. LEXIS 100 at *43.) The court held that plaintiffs’ injuries on this first claim occurred when the “Funds closed,” and that was when the claim “accrued”:

Accepting these allegations as true, the plaintiffs’ injuries occurred when the Funds closed, at which time the Funds were not (allegedly) properly diversified nor properly screened. This was the time of the wrongful act. Fund I closed on May 5, 1997, and Fund II closed on April 17, 1998. Likewise, claims that the Funds were improperly structured accrued at the time the Funds closed.

⁶ The court wrote (2005 Del. Ch. LEXIS 100, *44, 2005 WL 1594085 *13-14, footnotes omitted):

2. Failure To Implement Hedging Strategies

The plaintiffs allege that Alex. Brown and DCIP breached their fiduciary duties, their contractual duties, and committed fraud by failing to properly implement hedging strategies to protect the Funds from downside risk. According to the complaints, at the time the Funds were formed the Managers of the Funds hedged the majority of the contributed securities using collars and, to a lesser extent, short sales. Beginning in the fall of 1998, the managers began discussing the effect that hedging was having on the Funds. By the fall of 1999, all prior hedges on the Fund I had expired, and the Managers determined not to re-hedge. Similarly, the Managers removed all of the hedges on Fund II in the fall of 1999. The Funds were, therefore, unhedged during the fourth quarter of 1999 and early 2000 when the stock markets boomed. This allowed the Funds to participate in the boom, but also left them exposed to the stock market bust. In the spring of 2001, after the Funds had suffered substantial losses, the Managers reinstated some hedging strategies.

(Id., emphasis added, footnotes omitted.) Again, as with the unhedging claim, if Defendants' theory were true, the first claim would have accrued much earlier. It would have accrued well before the closing of the funds, when the plaintiff received the private placement memorandum disclosing how the funds were to be operated (April 14, 1997, for fund I and October 3, 1997, for fund II – Id. at *11), or perhaps when the plaintiff sent in his investment and subscription agreement. That it did not accrue until the funds “closed” is, again, precisely consistent with Dofflemyer (and Baron and Kaufman and Coca-Cola).

The portion of Albert that Defendants specifically rely on simply relates to the argument of the plaintiffs there that their claims had not accrued until their investment collapsed because until then they suffered no “harm.” The court did not hold, as Defendants suggest, that “harm” was unnecessary to claim “accrual.” Indeed, such a holding would be completely inconsistent with Delaware law. Instead, the court (using the language of the plaintiffs there) held that plaintiffs had in fact been “harmed” and the harm had occurred as soon as the “unhedging” occurred and, because of that “harm,” could have brought their claim at that time. Id. at *58-60. This is hardly inconsistent with Dofflemyer since Dofflemyer held that the plaintiff suffered no “injury” “until the merger was accomplished” and that was why his claim “accrued” at that point. 558 F. Supp. at 379 (emphasis added). Basically, Dofflemyer speaks in terms of “injury,” while Albert speaks both in terms of “injuries”⁷ and “harm.” There is no difference.

Moreover, if Albert actually supported accrual of Plaintiff's claims prior to the Closing of the Merger, it would be contrary to the Delaware Supreme Court's decision in Coca-Cola (see Parts II-III above), which it obviously cannot be. This simple fact puts the part of Albert quoted

⁷ See discussion on preceding page of claim in Albert that the funds were not set up properly – “the plaintiffs’ injuries occurred when the Funds closed.” 2005 Del. Ch. LEXIS 100 at *43.

by Defendants⁸ in context. Under Coca-Cola, there is no claim until the underlying contract is “enforceable.” Under Albert, there must be a “harm” but there need not be a “loss” or “damages.” In context, it is clear that Albert is referring to quantifiable financial “losses” or financial “damages” and not to “harm” or “injury” (or non-financial damages). In light of Coca-Cola, Plaintiff was not “harmed” or “injured” (or “damaged” in any sense) until the Merger agreement became enforceable, as also held by Kaufman, Baron, and Dofflemyer.

V. The “Standing” Cases That Defendants’ Cite Do Not Involve (Or Even Mention) Claim Accrual, Notwithstanding Defendants’ Continued Mis-Characterization Of Those Cases, And Are Simply Irrelevant.

In their original memorandum, Defendants asserted that under Delaware law the claim here “accrues when the board [of SCI] pass[ed] the ‘resolution approving the merger’” (Def. Mem. In Supp., at 12.) In support of that contention, Defendants cited Brown v. Automated Mktg. Sys., Inc., 1982 WL 8782, *2 (Del. Ch. Mar. 22, 1982). They further asserted that “when a merger is challenged, the claim arises . . . ‘at the time the terms of the merger were agreed upon’” In support of that statement, they cited In re Beatrice Cos., Inc. Litig., 522 A.2d 865 (Del. 1987). (Def. Mem. In Supp., at 12.) Finally, they asserted that in Omnicare, Inc. v. NCS Healthcare, Inc., 809 A.2d 1163 (Del. Ch. 2002), a claim for breach of fiduciary duty “arose when the directors decided to approve the merger” (Def. Mem. at 13.)

Plaintiff obviously pointed out in response – as anyone who read those cases would – that those cases do not say or hold what Defendants claimed they say and hold. (Pl. Mem. at 12-13.) None of them involves the issue of when claim “accrues” (or “arises”). They relate to “standing,” which is a different issue altogether.

⁸ “In essence, the plaintiffs argue that they could not have brought suit until they had suffered a harm This is incorrect. The law in Delaware is crystal clear that a claim accrues as soon as the wrongful act occurs. This is so because the plaintiffs were harmed as soon as the alleged wrongful acts occurred. Whether or not the plaintiffs could have sued for damages is not dispositive as to whether the claim accrued since, as soon as the wrongful acts occurred, the plaintiffs could have sought injunctive relief. . . . The court reiterates that a claim accrues at the time of the alleged wrongdoing, and not when the plaintiff suffered a loss.” (Reply at 2.)

Defendants continue to seriously mis-characterize these cases. In the Reply, Defendants again refer specifically to Brown as “holding” that the claim “accrued” when “the board approved [the] merger agreement and did not wait for shareholder approval” (Reply at 5.) A simple reading of the case reveals that the opinion does not “hold” that or address claim “accrual.” Indeed, the word “accrual” (or any form of it) is not used anywhere. The holding is simple: plaintiff “lack[ed] standing to maintain the cause of action alleged.” 1982 WL 8782 at *3. Beatrice and Omnicare are to the same effect. Neither of them discusses or deals with claim “accrual” either.

While Defendants obviously wish the issue in those cases was claim “accrual,” if it had been, none of them would have been dismissed. This is because in each case the plaintiff’s claim was well within the statute of limitations period regardless of whether the claim “accrued” at the time transaction was approved or when it later closed. The cases were dismissed only because the plaintiffs lacked “standing” because they had not owned the stock at issue at the time the board approved the transactions. These cases simply do not go to the issue of when the claims “accrued.”

Defendants’ wishful characterization of Brown, Beatrice, and Omnicare has never been accepted by any court.⁹ To the contrary, the characterization of Brown has been expressly rejected by the only court to consider it, the United States District Court for Delaware in Dofflemeyer. The defendants there made the same argument as Defendants here make regarding Brown. The district court rejected it out-of-hand:

Brown is also inapplicable. In that case, the Court of Chancery held that a plaintiff who purchased shares after reading a press release indicating that the board of directors had approved a plan of merger did not have standing to challenge the merger when it was carried out according to the plan. The holding of that case involved a determination of the times when a plaintiff must own stock in a corporation in order to have standing to challenge a merger and is not pertinent to when, if standing had existed, the plaintiff could have sued for damages.

558 F. Supp. at 379 n.5 (emphasis added).

⁹ It has not been endorsed by any commentator either. Defendants imply that the Folk treatise has done so (Reply at 9), but Folk merely reports Brown without comment.

Moreover, to the extent there were any doubt, it should be put to rest by the Delaware Supreme Court's decision in Coca-Cola, affirming the lower court's holding that the wrong there "occurred at the time that enforceable legal rights . . . were created [regarding underlying contract]." 625 A.2d at 271. As discussed in Part III above, under Coca-Cola, there could not possibly have been a breach of fiduciary duty claim by Plaintiff until the merger agreement was "enforceable," and that could not have occurred prior to the Closing Date at the earliest. To the extent Brown (or Omnicare or Beatrice) could be read to support Defendants' argument, it would be violate Coca-Cola.

Finally, Brown, Omnicare, all Beatrice are all pre-merger cases and simply do not go to the issue of when claims relating to consummated mergers accrue. Only Kaufman, Baron, and Dofflemyer address that question. Apart from the "standing" problems in Brown, Omnicare, and Beatrice, the claims at issue there (pre-merger claims for injunctive relief) could only be brought under the teaching of Coca-Cola if all the conditions precedent to closing had been satisfied, at which point the claims would accrue. It is a safe bet, however, that in many such cases not all of the conditions precedent have been satisfied. Since the cases are obviously not dismissable, Coca-Cola and Kahn obviously do not bar them. The reconciliation of (a) the fact that such cases are allowed to proceed with (b) the holdings of Coca-Cola and Kahn is (c) that the pre-merger claims are separate claims from post-merger claims. That being so, post-merger claims obviously accrue (as Kaufman, Baron, and Dofflemyer hold) upon consummation of the merger.

Accordingly, since Brown (and Omnicare and Beatrice) involve pre-merger claims, they are, even apart from the "standing" point, irrelevant to the basic claim here – namely, that it was a breach of fiduciary duty for Defendants to allow the Merger to consummate (see Part VI below). They should have cancelled it or, at minimum, renegotiated the terms as happens in so many mergers.

VI. The Essential Claim Here (Allowing The Merger To Consummate) Obviously Took Place After the Execution Of The Release And Cannot Be Barred By It Even If Defendants' Other Arguments Were Correct.

It cannot be disputed that under Delaware law, Defendants had "continuing" fiduciary duties to Plaintiff, running up and through the Merger and even through today. It was not a one-time, one-and-out thing. Even the Albert case which Defendants cite shows that a claim regarding "continuing" duties continually accrues. One of the claims in Albert was that the defendant fund managers had failed to properly manage the funds. As the court noted defendants "owed (and continue to owe) a continuing duty to actively manage and supervise the Funds." Albert v. Alex. Brown Mgmt. Servs., Inc., 2005 Del. Ch. LEXIS 100, 2005 WL 1594085 (June 29, 2005). The "wrongful act" was the "failure to meet that duty" which was not a "discrete act." Accordingly, it was not barred by the statute of limitations. Id., 2005 Del. Ch. LEXIS 100, *51, 2005 WL 1594085, *16.

And it cannot be seriously disputed, as explained in the proceeding section, that a post-merger claim such as here (allowing the Merger to consummate) is separate and different from a pre-merger claim such as one for injunctive relief. A post-merger claim would obviously not accrue until the Merger consummates.

Hence, it is clear that while the Release might have applied to pre-merger claims (i.e., a claim for injunctive relief or a claim regarding the options plaintiff executed in the summer of 2006 to purchase SCI stock from the company (a claim specifically excluded from this action by Plaintiff because of the Release)), it would not apply to Defendants "continuing [fiduciary] duty." Likewise, it would not apply the post-merger claim that it was a breach of fiduciary to allow the Merger to consummate. As already discussed, the Merger could not possibly have proceeded based on the financial conditions precedent (e.g., as of the Closing date, the representations and warranties shall be true and there shall have been no significant changes in

FITG's business¹⁰) unless those requirements were "waived." And the waiver of those conditions to "allow" the Merger to go forward would obviously have occurred at the time of the Closing (well after the Release). That would be a post-Merger claim, accruing at the time of the Merger.

In point of fact, the pre-Release events in the Complaint are set forth simply as "background." (See Complaint, at 9 and Heading to ¶¶ 34-49.) The central claim (obviously) is that the Merger should not have allowed to consummate. (It is obviously the "central" and "only" claim regarding the Merger since if it had not consummated, Plaintiff would have nothing to complain of regarding the Merger. In this sense, the claim could be described as a "continuing wrong" under another principle set forth in Kahn v. Seaboard Corp., 625 A.2d 269, *135-36 (Del. Ch. 1993), since it can be proved "only by reference to actions within the limitations

¹⁰ See Merger Agreement, §6.2 (Proxy at A-35) (emphasis added):

Section 6.2 Conditions to Obligations of SCI and Merger Sub. The obligations of SCI and Merger Sub to effect the Merger are further subject to satisfaction or waiver of the following conditions:

(a) Representations and Warranties. The representations and warranties of ITG set forth herein (without giving effect to any qualifications contained therein as to materiality or Material Adverse Effect) shall be true and correct as of the Closing Date as if made at and as of such time (except to the extent expressly made as of an earlier date, in which case as of such date), with only such exceptions to be true and correct as would not, individually or in the aggregate, reasonably be expected to result in a Material Adverse Effect with respect to ITG, and ITG shall have delivered to SCI a certificate to such effect signed on behalf of ITG by an executive officer of ITG and dated as of the Closing Date.

(b) Performance of Obligations of ITG. ITG shall have performed in all material respects all obligations required to be performed by it under this Agreement at or prior to the Closing Date, and ITG shall have delivered to SCI a certificate to such effect signed on behalf of ITG by an executive officer of ITG and dated as of the Closing Date.

(c) Financial Advisor Opinion. The opinion of RSM EquiCo, financial advisor to the SCI Special Committee, shall not have been withdrawn or changed in a manner adverse to SCI.

(d) FIRPTA Certificate. SCI shall have received an affidavit of ITG certifying that it is not a United States real property holding corporation under Section 897 of the Code.

(e) No Material Adverse Effect. There shall have been no changes, other than changes contemplated by this Agreement in the business, operations, condition (financial or otherwise), assets or liabilities of ITG and its Subsidiaries (regardless of whether such events or changes are inconsistent with the representations and warranties of ITG set forth herein) that, individually or in the aggregate, has had or would reasonably be expected to have a Material Adverse Effect with respect to ITG.

(f) Escrow Agreement. The Escrow Agreement shall have been duly executed by the parties thereto.

period.”) The simplest way to confirm this is by reference to the breaches of fiduciary duty set forth in Paragraph 99 and 104 of the Complaint:

¶99. WLR and Ross breached their fiduciary duties to the minority stockholders of SCI including Plaintiff in the respects alleged above, and also more specifically as follows:

- (a) by proposing the Merger and then allowing it to close notwithstanding the financial condition of FITG;
- (b) by approving the Merger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders down to 35%, or at all;
- (c) by not providing accurate and complete information regarding FITG to Dr. Tessori and RSM or ensuring that such information was provided to them;
- (d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account, or see that it was taken into account, with regard to the Merger;
- (e) by failing to ensure that proper due diligence was conducted on behalf of SCI on FITG;
- (f) by allowing the representation at the Merger closing that MAC Clause condition was satisfied;
- (g) by failing to call off or renegotiating the Merger (or cause it to be called off or renegotiated) because of the financial condition of FITG;
- (i) by allowing the debt previously held by FITG to be transferred to the Combined Company and/or by allowing that debt to be converted into preferred stock;
- (j) by allowing or causing the renegotiation the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith;

¶104. Each of these defendants breached their fiduciary duties to the minority stockholders of SCI including Plaintiff in one or more of the respects alleged above and also more specifically as follows:

- (a) by proposing the Merger and then allowing it to close notwithstanding the financial condition of FITG;
- (b) by approving the Merger on terms which gave 65% ownership to the FITG stockholders and diluted the minority shareholders down to 35%, or at all;
- (c) by not providing accurate and complete information regarding FITG to Dr. Tessori and RSM or ensuring that such information was provided to them;
- (d) to the extent any one of them was not aware of the financial situation of FITG, by failing to learn of the financial situation of FITG and failing to take it into account, or see that it was taken into account, with regard to the Merger;
- (e) by failing to ensure that proper due diligence was conducted on behalf of SCI on FITG;
- (f) by making or allowing to be made the representation at the Merger closing that MAC Clause condition was satisfied;

- (g) by failing to call off the Merger (or cause it to be called off) because of the financial condition of FITG;
- (h) by allowing the debt previously held by FITG to be transferred to the Combined Company and/or by allowing that debt to be converted into preferred stock;
- (i) by allowing or causing the renegotiation the SCI's credit facility and/or obtaining \$100 million of additional preferred stock in connection therewith; . . .

(Emphasis added).

The essential point here, and the one that resonates through virtually all of the above paragraphs from the Complaint, is that it was a breach of fiduciary duty on the date of the Closing for the Defendants to allow the Merger to Close. To be consistent with the holding of Coca-Cola and Kahn, that has to be a separate claim from a pre-merger claim for injunctive relief. And, as is self-evident, it would not accrue until the Merger had closed.

Since the underlined breaches took place after the Release and/or related to continuing duties of the defendants, they could not be barred by the Release. Beyond that, some of them literally are "discrete" events that come even after the Closing (e.g., items (i) and (j) in the foregoing lists). Obviously, none of these could be barred.

CONCLUSION

Under the Delaware Supreme Court's decision in Coca-Cola, Plaintiff had no claim until the underlying merger agreement was "enforceable." This is the only logical rule since, as widely tracked in the financial press (see note 3 supra and Exhibit A), proposed mergers go "bust" and fail to consummate all the time.

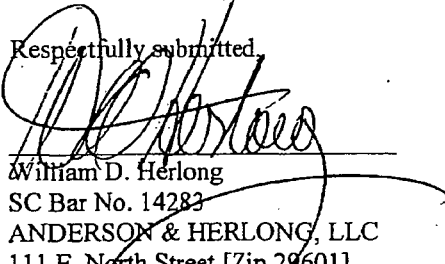
Since the Merger could not have been "enforceable" before the Closing Date, at the earliest, Plaintiff's claims, as common sense would dictate, could not have accrued prior to that date. This conclusion based on Coca-Cola is confirmed by every single case to address claim "accrual" in the context of a merger, each of which has held that the claim accrues when the

merger closes. Kaufman v. Albin, 447 A.2d 761 (Del.Ch. 1982); Baron v. Allied Artists Pictures Corporation, 717 F.2d 105 (3d Cir. 1983); and Dofflemyer v. W.F. Hall Printing Co., 558 F. Supp. 372 (D. Del 1983).

And since Plaintiff's claims could not have accrued before the Closing Date, the Release is inapplicable.

For these reasons, Defendants Motion to Dismiss should be denied.

Respectfully submitted,



William D. Herlong
SC Bar No. 14282
ANDERSON & HERLONG, LLC
111 E. North Street [Zip 29601]
P.O. Box 2105
Greenville, SC 29602-2105
Tel. (864) 255-9255
Fax (864) 752-0820
william@ahlf.us

Attorneys for Brian Menezes

August 20, 2008.

Exhibit A

"Buyouts Gone Bust"

http://www.thedeal.com/dealscape/2008/06/dealwatch_buyouts_gone_bust.php

The Deal.com

Tuesday, August 19, 12:19 pm

[Home](#) [Dealscape](#) [Newsweekly](#) [Tech Confidential](#) [Corporate Dealmaker](#) [Deal Video](#) [Events](#)

• Quality for The Deal Newsweekly
• Subscribe/Login to TheDeal.com

Dealscape

 SYNDICATE

[Dealscape Home](#) [Hedge Clipper](#) [International](#) [M&A](#) [Private Equity](#) [Bankruptcy](#) [Regulatory](#) [The Deal Career Center](#)

Dealwatch: Buyouts gone bust

[Posted on June 10, 2008 at 8:42 AM]

[E-mail](#) | [Leave a Comment](#)[Filed under: Dealwatch](#) | [Law suits](#) | [PE Pipeline](#) | [Private Equity](#)
 [SHARE](#)

Search

Enter keyword

Editor's Choice

- Greenlight's Einhorn fights Natrixis plan
- Could it be the beginning of another Richard Breeden insurgency?
- Wilbur Ross' solution for the credit crisis
- Are labor problems the next cause for bankruptcies?
- Pitt launches Web site to help short sellers



Kicking off the week of May 12, the \$1.3 billion take-private of Cumulus Media Inc. bit the dust after its would-be buyers (chairman, president and CEO Lew Dickey and Merrill Lynch & Co.'s private equity arm) and the Atlanta-based radio broadcaster could not renegotiate terms. Cumulus may be the latest, but SLM Corp. kicked off a wave of terminations based on everything from the credit markets to material adverse changes in a company's business to an inability to renegotiate on favorable terms. So many stalled deals, in fact, have left PE firms excluded from some auctions, sending targets into the arms of strategics. Here's a look at recent buyouts gone bust:

SLM Corp. (Turned sharply south: July 11, 2007)

Kicking things off was student lender Sallie Mae. The Deal's Scott Stuart wrote in a February retrospect:

SLM Corp. on July 11 let it be known that JC Flowers & Co. of New York might not be able to close its \$26 billion buyout of the education lending company known as Sallie Mae because of potential changes in the legislative landscape for federal loan support. JC Flowers was buying Sallie Mae with equity partners J.P. Morgan Chase & Co. and Bank of America Corp. It soon became a topic of conjecture that JC Flowers director J. Christopher Flowers might seek an out because of the rapidly declining credit environment that, seven months later, risk arbitrageurs and dealmakers had become all too familiar with. ...

Although the Sallie Mae buyout is rightly a 2007 deal corpse, the saga over the Reston, Va., company ended only recently, on Jan. 28, when SLM restructured a \$30 billion lending facility that had been part of its merger package with BofA and J.P. Morgan. This time, the new \$31 billion financing was syndicated out to also include Barclays Capital, Deutsche Bank AG, Credit Suisse Group, Royal Bank of Scotland plc and UBS. As part of that transaction, Sallie Mae dropped its lawsuit in Delaware Court of Chancery to compel the partners to the April 15, \$8.8 billion equity commitment to pay the \$900 million termination fee.

The Delaware suit was to determine whether Sallie Mae had suffered a material adverse change in its business as defined by the merger agreement. ... The JC Flowers deal offered \$60 per share for SLM. The buyers did offer a reduced price of \$50 plus a warrant of unknown value in October. The offer was spurned. SLM shares now trade at around \$21.

Harman International Industries Inc. (Fell apart: Sept. 21, 2007)

Despite much pushback from the car stereo maker's founder and chairman Sidney Harman, the would-be buyers walked in September. The Deal's Vyvyan Tenorio wrote:

On Sept. 21, Kohlberg Kravis Roberts & Co. and Goldman Sachs Capital Partners said they would walk from their \$8 billion agreement in April to buy the audio systems maker. The deal opened another front in the material-adverse-change wars. The sponsors had agreed to buy Harman International Industries Inc. for \$120 per share but backed off, claiming the Washington-based company had suffered an unspecified material adverse change. An indignant Sidney Harman, the company's 89-year-old chairman and founder of the company in 1953, and CEO Dinesh Palival fired back, insisting the company had had no serious setbacks. In a conference call Sept. 27, they pointed to the company's growth prospects. In a compromise Oct. 22, KKR and Goldman, which would have been liable to pay a \$225 million breakup fee had Harman taken them to court and won, invested \$400 million in convertible debt, a rare instance of noblesse oblige, perhaps. More likely it was either that or a \$225 million breakup fee.

Acadcom Corp. (Crumbled: Oct. 1, 2007)

And then there was drawn-out fight over Acadcom, as Tenorio noted:

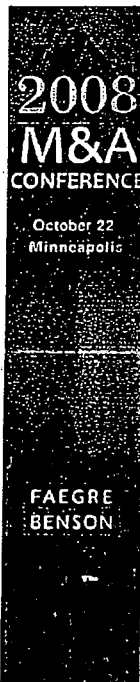
This two-year tussle between the Little Rock, Ark., customer information management company and two would-be buyers, San Francisco- and Boston-based activist fund manager ValueAct Capital Partners LP and technology buyout group Silver Lake, ended with no clear winner and no shortage of losers. On Oct. 1, not long after Acadcom Corp. shareholder MMI Investments LP gave up its fight in mid-August against the proposed \$3 billion, or \$22.10 a share, acquisition, the buyers decided to abort the deal. Neither side gave reasons, but Acadcom stock had been sliding, and the company posted disappointing earnings in the quarter ended June 30. ValueAct lost money on its stock purchase, plus its share of the \$65 million penalty paid to Acadcom. The day the deal was killed, Acadcom chairman Charles Morgan said he would retire once a replacement had been found.

Affiliated Computer Services Inc. (Dried up: Oct. 31, 2007)

Cerberus Capital Management LP pulled out of its ACS buyout in late October. Stuart noted:

Cerberus Capital Management LP and Darwin Deason have dropped their longstanding \$6.2 billion bid for Affiliated Computer Services Inc. because of conditions in the credit markets. ... Deason, ACS's founder and chairman, teamed up with Cerberus on a \$62 per share cash take-private offer. Deason owns roughly 9% of ACS, which provides outsourced business processing and information technology services, but he controls 42% of the vote. Cerberus had an exclusivity agreement with Deason that had received particular scrutiny by the special committee's review.

The buyers expressed frustration at the lengthy review process.



Syndicate

Subscribe to our RSS feed

Recent Entries

- Greenlight's Einhorn fights Natrixis plan
- General Dynamics in \$2.25B Jet Aviation deal
- Lehman moves to sell Neuberger Berman
- Fannie, Freddie drag down the Street
- Could it be the beginning of another Richard Breeden insurgency?
- Lehman may sell real estate assets
- Wilbur Ross' solution for the credit crisis
- Are labor problems the next cause for bankruptcies?

In its termination letter, Cerberus stressed that it would have been able to close the deal had the offer been accepted earlier. But terminating based on credit market conditions makes it seem more that Cerberus does not want to pursue the deal at the \$62 price, or simply could not get acceptable financing in the near term for that deal, rather than that the special committee ignored the \$62 bid. Cerberus also said that, if market conditions change, it may consider proposing another transaction for ACS.

J Sainsbury plc (Second suitor walked: Nov. 5, 2007)

In Europe, one particular stalled buyout commanded much financial media attention and played out in a tragic-comic way, Jonathan Braude argued:

The private equity folks at CVC Capital Partners Ltd. must be rolling in the supermarket aisles at Qatar's decision to walk away from buying J Sainsbury plc. The London buyout shop, after all, hadn't been able to get backing for its own £11.7 billion (\$24.4 billion), 582 pence a share offer for the grocer in April this year. Not only did it face unflinching opposition from the founding Sainsbury family, but its own consortium partners, including Blackstone Group LP and TPG, had also walked. It must have been galling to see the Qatar Investment Authority and its U.K. agent, Paul Taylor of Three Delta LLP, get so close to buying the business with his £11.9 billion, 600 pence a share proposal.

After picking off first the Sainsbury board, then the shareholders and ultimately the company pension fund with a series of concessions, Taylor's fund, Delta (Two) Ltd., fell at the most difficult hurdle of all — raising an extra slab of equity from his own Qatari backers. At the last moment, his lending banks wouldn't play ball...

It will be a while before anyone appears with a third attempt at buying Sainsbury. But whoever tries his luck should be careful not to assume it was only the Qataris and the unfortunate Taylor who got things so badly wrong. Taylor may yet have the last laugh.

United Rentals Inc. (Terminated: Dec. 24, 2007)

And URI, also victim to Cerberus' second-guessing, was the first to sue in Delaware to enforce a merger agreement, David Marcus noted:

As financing markets worsened last summer, the precise language in the merger agreements private equity firms signed became more important to buyers and sellers than it had been in years. ... Many sellers saw their deals close on the original terms. Others, notably Home Depot Inc. in the sale of its HD Supply unit, had to accept a price cut. And SLM Corp. and Harman International Industries Inc. had little recourse when buyers walked.

But only United Rentals Inc. sued in Delaware to enforce a merger agreement. The Greenwich, Conn., construction equipment rental company attempted to force Cerberus Capital Management LP to close the parties' \$6.6 billion agreement, which led to a trial before Chancellor William B. Chandler III. The collapse of the URI buyout highlights the importance of the issue and invites comparisons to the ways parties in other deals—including, in one instance, Cerberus itself—resolved it.

URI, then, in June 2008 did what Cerberus wouldn't, leveraging up to buy as much as \$1.4 billion in equity.

PPG Industries Inc. (Collapsed: Dec. 31, 2007)

Two stalled buyouts rounded out December. As Tenorio noted:

Affiliates of private equity firm Platinum Equity LLC said they are terminating an agreement after Monday, Dec. 31, to buy the automobile glass units of Pittsburgh-based PPG Industries Inc. for about \$500 million and filing a lawsuit in New York claiming the company fraudulently concealed facts material to the leveraged buyout. Unlike other recent LBO blowups stemming from the credit crunch, the Beverly Hills, Calif., firm said the issue isn't over financing, and that it is in fact still interested in buying the assets — at the right price...

On Sept. 13, Platinum agreed to acquire the assets of PPG's glass unit, which supplies glass to automakers and the aftermarket, as well as its auto glass services operation. Platinum, led by financier Tom Gores, has a long history of acquiring financially troubled businesses in technology and other areas and turning them around.

PHH Corp. (Missed deadline: Dec. 31, 2007)

Tenorio also gave the run down on the multifaceted PHH deal:

General Electric Capital Corp., a unit of General Electric Co. agreed in March to buy Mount Laurel, N.J.-based finance company PHH Corp., which specializes in auto leases and residential mortgage loans, for \$1.8 billion plus about \$8 billion of debt. GE Capital wanted PHH's fleet services business, which fit well with GE's operations. But the deal was contingent on GE selling PHH's mortgage business to Blackstone Group LP. Blackstone's financing consisted of \$750 million of equity and the assumption of \$4.26 billion debt for a total of about \$5 billion. J.P. Morgan Chase Bank NA and Lehman Brothers Inc. committed to provide, in a 70-30 split, a package that included up to \$1.6 billion in term loans and revolvers and \$4 billion in a mortgage loan repurchase facility. In September the lenders said they were cutting the financing by as much as \$750 million. Blackstone at first expressed disagreement with the banks, hoping perhaps for a price cut on the buyout of its HD Supply, which involved the same lenders. But no such luck. The parties missed the Dec. 31 deadline, and Blackstone, while laying the blame on the banks, eventually honored the \$50 million termination fee.

NIBC Holding NV (Bit the dust: Jan. 30, 2008)

Flowers found itself on the other side of a stalled buyout Jan. 30, as Renee Cordes noted:

Blaming market turmoil, Iceland's Kaupthing Bank hf on Wednesday, Jan. 30, yanked its planned 2.99 billion euro (\$4.42 billion) purchase of Dutch investment bank NIBC Holding NV from a group led by JC Flowers & Co. LLC.

The collapse of the deal came in the month it was due to complete and led the Dutch investment bank's owners to pledge 300 million euros in fresh equity...

The deal with Kaupthing had excluded NIBC's U.S. subprime portfolio, which sold for \$528 million in August to a nascent company owned by a consortium of NIBC shareholders. Enthoven said Wednesday that NIBC's results were "substantially affected" by the loss of the portfolio.

Reddy Ice Holdings Inc. (Melted: Jan. 31, 2008)

The Reddy Ice buyout finally melted Jan. 31, when the target revealed its \$1.1 billion deal with GSO Capital Partners LP was called off. The Dallas-based packaged ice company was due a \$21 million cash termination fee on Feb. 5 but would have to pay up to \$4 million to New York hedge fund GSO and its consultants for related expenses, according to a statement at the time. The company's chairman and chief executive William F. Brick said the company and GSO had tried for weeks to renegotiate the deal.

- Pitt launches Web site to help short sellers
- HBOS Australian unit looks appetizing to CBA

Video

The Deal Calendar: August 18-22, 2008



Union Square Ventures' Brad Burnham on venture funding and technology deals.

Categories

- 2008 Distressed Investing conference (33)
- ABI Bankruptcy Conference (4)
- ACG InterGrowth Conference (5)
- Advisers (76)
- Airlines (124)
- Antitrust (67)
- Argyle Executive Forum's 2007 Leadership in VC Conference (3)
- Auction (479)
- Autos (210)
- Banking (612)
- Bankruptcy (361)
- Better know a Democrat (8)
- Breaking News (80)
- CVCA Annual Meeting (4)
- Calendar (19)
- Chronicle (149)
- Closing Bell (100)
- Corporate restructuring (754)
- Deal Calendar (14)
- Deal Digest (65)
- Deal International (316)
- Deal Life (16)
- Deal Stocks (215)
- Deal preview (85)
- Dealmakers (556)
- Dealmakers on the stump (12)
- Dealwatch (123)
- Distressed (427)
- Earnings (80)
- Economics (33)
- Editor's Choice (1228)
- Energy (18)
- Exclusive (9)
- Executive Summary (4)
- Executive changes (110)
- Garbithage (4)
- Healthcare (13)
- Healthcare Dealmaking Symposium (26)
- Hedge Clipper (331)
- History (194)
- Hostile takeover (75)
- IBF VC conference 2007 (3)
- IPO (91)
- Innovative Financing (11)
- International (5)
- Law (144)
- Law suits (122)
- Layoffs (43)
- M&A (1775)
- Media (578)
- Media Maneuvers (132)
- Mergers & Acquisitions Institute (3)
- Microsoft/Yahoo (27)
- Middle Market (108)
- Morning roll call (92)
- NVCA Annual Meeting (3)
- PC Symposium (84)
- PE Pipeline (49)
- PE Fund-raising (54)
- Police Blotter (11)
- Politics (262)
- Post-merger (123)
- Private Equity (1075)
- Proxy Fight (60)
- Rabble Rattle (15)
- Ratings Review (62)
- Real Estate (169)
- Regulatory (217)
- Retail (261)
- Roll Call (99)
- Scandal (74)
- Soapbox (71)
- Sovereign wealth fund (36)
- Spinoff (25)
- Sports (45)
- Sun Valley (7)

3Com Corp. (Canceled: March 20, 2008)

3Com Corp. was the last buyout to go bust March 20 when a Bain Capital LLC affiliate pulled out of its \$2.2 billion deal for the company one month after saying it was unlikely to gain clearance from the federal panel that vets foreign investment in U.S. assets. 3Com unveiled a major blow Feb. 20, as Bill McConnell and Andrea Ott noted:

The proposed \$2.2 billion buyout of 3Com Corp. by a Bain Capital LLC-led investor group has run into a roadblock after a national security review panel told the parties the deal would not be approved as currently structured, 3Com and Bain said, however, they had not given up hope of reaching a new merger proposal and they "remain committed to continuing discussions."

To that end, Donna Block wrote days later, they went back to the drawing board:

Shares of network gear maker 3Com Corp. jumped in early trading Friday, Feb. 29, after the company announced it will adjourn its scheduled shareholder meeting without a vote on the proposed \$2.2 billion buyout by private equity firm Bain Capital LLC and China's Huawei Technologies Co.

In a statement announcing the merger's termination March 20, Bain said: "Bain Capital made several alternative proposals to 3Com that we believe could have satisfied the concerns raised by CFIUS. ... We regret that we were unable to agree upon an alternative transaction."

Myers Industries Inc. (Kaput: April 4, 2008)

Myers Industries' buyout went bust April 4, when Goldman Sachs Capital Partners pulled out of its \$1.1 billion deal for Akron, Ohio-based rubber and plastics maker. Myers Industries said its split with GS Capital was mutual, but didn't give a reason. The deal looked iffy for months, Dealscape's George White noted, particularly after a December 2007 extension to afford GS Capital time to assess its target's prospects.

Alliance Data Systems Corp. (Dunzo: April 21, 2008)

Closing out the week of April 14, Alliance Data Systems Corp. said April 18 its \$6.4 billion sale to Blackstone Group was off and the credit card processor was suing the firm to collect its \$170 million breakup fee. The Deal's Donna Block noted:

The Dallas-based company cited Blackstone's "refusing to accept reasonable and customary regulatory requirements and prolonging negotiations with regulators" as evidence it did not honor its agreement.

Alliance Data accused the Blackstone affiliates last month of trying to back out of the deal in what it said was a case of "buyer's remorse."

Under the deal's terms, Blackstone could walk away from the buyout by 11:59 p.m. on Thursday, as long as it was not in breach of the merger agreement.

In January the buyout ran into trouble. Blackstone said it did not envision gaining regulatory clearance from the Office of the Comptroller of the Currency necessary to close the deal. But if the deal was to come to fruition, the clock was ticking, Stuart noted:

The \$81.75 per share deal has been in limbo since Alliance moved in early February to jump start the stalled talks between bank regulators and Blackstone.

The Office of the Comptroller of the Currency must approve the change of control of Alliance Data's credit card bank subsidiary, World Financial Network National Bank, which has about 100 million cardholder accounts and \$4 billion in receivables. Negotiations with the OCC broke down, in Blackstone's view, after the regulator sought \$400 million in "source of strength" assurances from Blackstone funds to support the bank.

Alliance Data had sued Blackstone, but withdrew the suit, saying it thought it had found a solution. This was assumed to involve Alliance Data shareholders funding an entity that would issue a guaranty in lieu of commitment from Blackstone.

Cumulus Media Inc. (Busted: May 12, 2008)

Cumulus' \$1.3 billion buyout bit the dust May 12 after its buyers, chairman, president and CEO Lew Dickey and Merrill Lynch's private equity arm tried and failed to amend terms of their agreement. Shares of the Atlanta-based radio broadcaster closed Friday May 9 at \$5.81 — nearly half off the \$11.75 buyout price. In late 2007, tighter credit markets, a looming recession and the subsequent likely impact on radio advertising seemed to weigh on the company and the deal.

For the latest on buyouts we're watching as they market debt, fight law suits, renegotiate terms and try to eek their way through, stay tuned to Dealscape and the PE Pipeline. — Carolyn Murphy

Dealwatch executive summary

The Date	The Action
6.10.08	URI does what Cerberus wouldn't.
5.12.08	Cumulus buyout is scrapped.
4.18.08	ADS deal is dead.
4.20.08	Alliance Data deadline looms.
2.20.08	3Com, Bain withdraw CFIUS proposal. But all hope was not lost.
2.20.08	A 2007 retrospect: Sallie Mae kicked off a wave of failed buyouts. Others followed like a ton of bricks. URI sued in Delaware to enforce its merger agreement.
1.31.08	Reddy Ice finally melts.
1.30.08	NIBC deal goes bust.
12.27.07	PPG deal stalls.
11.20.07	J Sainsbury is done.
10.31.07	Cerberus drops ACS.
9.21.07	KKR, Goldman Sachs plan to walk from Harman.

Source: The Deal

Tags:

- ADS
- busted buyout

- The Corporation (225)
- The Deal's Alternative Energy Symposium (5)
- The Deal's M&A Outlook 2008 (31)
- Today's deals (230)
- Venture Capital (100)
- debt markets (67)

Monthly Archives

- August 2008 (174)
- July 2008 (418)
- June 2008 (439)
- May 2008 (404)
- April 2008 (434)
- March 2008 (369)
- February 2008 (324)
- January 2008 (275)
- December 2007 (121)
- November 2007 (195)
- October 2007 (191)
- September 2007 (95)
- August 2007 (79)
- July 2007 (99)
- June 2007 (88)
- May 2007 (125)
- April 2007 (98)
- March 2007 (126)
- February 2007 (78)
- January 2007 (60)
- December 2006 (43)
- November 2006 (58)
- October 2006 (61)
- September 2006 (52)
- August 2006 (67)
- July 2006 (66)
- June 2006 (103)
- May 2006 (119)
- April 2006 (93)
- March 2006 (99)
- February 2006 (80)
- January 2006 (111)
- December 2005 (34)

Blog Roll

- BloggingBuyouts
- BloggingStocks
- Dealback
- DealBreaker
- Deal Journal
- FT Alphaville
- footnoted.org
- Going Private
- peHUB
- Reuters Dealzone
- SEC Investor
- Prince Of Wall Street

- Cerberus
- Cumulus Media
- KKR
- private equity
- Sallic Mac
- URI

Also From Dealscape

- Greenlight's Einhorn fights Nativis plan
- General Dynamics in \$2.25B Jet Aviation deal
- Lehman moves to sell Neuberger Berman
- Fannie, Freddie drag down the Street
- Could it be the beginning of another Richard Breeden insurgency?

[Dealscape Home Page](#)

From The Deal Blogs Network

- Google going geothermal
- Venezuela wrests control of Cemex operations
- Indian firms are the most active emerging market acquirers, says KPMG
- Refiner Alon reassigned execs as it integrates acquisition
- Applied Materials/ASM talks may not be dead yet

[The Deal Blogs Home](#)

Post a comment

Name:

Email Address:

URL:

☐ Remember personal info?

Comments: (you may use HTML tags for style)

Please only click "Post" once. It may take a few moments to process.

The Deal.com

- Sitemap
- About Us
- Contact Us
- Advertise
- Privacy Policy
- Terms & Conditions

Dealscape

- Hedge Clipper
- International
- M&A
- Private Equity
- Bankruptcy
- Regulatory

Newsweekly

- Features
- Insights
- Dealwatch
- Community
- Dealmakers
- The Magazine

Corporate Dealmaker

- Topics
- CD Events
- The Magazine
- Resource Center

Tech Confidential

- Behind The Money
- Money Out
- VC Ratings
- The Note

Deal Video

- Deal Calendar
- Behind The Money
- PC Symposium
- Healthcare Symposium

©Copyright 2008, The Deal, LLC. All rights reserved. Please send all technical questions, comments or concerns to the Webmaster.