

Bouchard Addresses Nature of Derivative Claims in Decision Tossing Challenge to Design Within Reach Merger

By Tom McParland

The Delaware Court of Chancery on Friday rejected a “novel theory” to expand the state’s narrow doctrine allowing some claims to be treated as both derivative and direct. The rejection comes in a decision that nixed an investor lawsuit seeking to undue the \$124 million merger of Herman Miller Inc. and Design Within Reach Inc.

The **post-trial ruling** from Chancellor Andre G. Bouchard rebuffed one set of claims from former DWR stockholders Charles Almond and Andrew Franklin, who alleged in a 2014 lawsuit that a series of technical flaws had prevented the merger of two of the biggest names in the modern furniture industry from taking effect.

The opinion was also the latest to address the Delaware Supreme Court’s 2006 decision in ***Gentile v. Rosette***, which held that certain claims for corporate



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overpayment are direct and derivative when a controlling stockholder extracts money and voting power at the expense of minority investors.

Under a new “control group” argument, Almond and Franklin argued that DWR’s chief executive and chief operating officer had teamed up with majority stockholder Glenhill to unfairly profit from the transaction. The argument represented a threshold issue

for the plaintiffs’ derivative claims because, under Delaware law, such claims belong to a corporation and transfer to the acquiring company in a merger.

In an 81-page opinion, Bouchard ruled that the case did not fit the “narrowly prescribed circumstances” in which purely derivative claims can survive a merger. Bouchard said he was aware of no case where the analysis for determining the existence of a control

group had ever been applied “to glom on to a pre-existing controlling stockholder additional stockholders to give them the status of a ‘control group’ for *Gentile* purposes or otherwise.”

Bouchard said that in order for the argument to succeed, plaintiffs would need to point to an agreement Glenhill had in place with other stockholders to limit its own control, or to share it with the investors.

“In other words, the pre-existing controlling stockholder would have to agree to limit its ability to act in its own self-interest as a controller in some material way; otherwise the pre-existing controlling stockholder would retain the ability to wield control by itself, and the power of control would not reside in the hands of a ‘group,’ he wrote. “Nothing of this nature exists in the trial record.”

Attorneys for both sides did not return calls Friday seeking comment on the decision.

Friday’s ruling comes as the Delaware courts are reassessing the underlying reasoning of *Gentile*. Vice Chancellor J. Travis Laster in December questioned “whether *Gentile* is still good law” in a

decision that found energy company Kinder Morgan liable for the bulk of a \$171 million damages award related to its acquisition of El Paso Corp. and its affiliates.

In December, the state’s high court **overturned** *Laster*, ruling in the “troubling case” that the claims at issue were derivative and the plaintiff’s standing had thus been extinguished in the merger. In a concurring opinion, Chief Justice Leo E. Strine even suggested that it may be time for *Gentile* to be overruled.

“*Gentile* cannot be reconciled with the strong weight of our precedent and it ought to be overruled, to the extent that it allows for a direct claim in the dilution context when the issuance of stock does not involve subjecting an entity whose voting power was held by a diversified group of public equity holders to the control of a particular interest,” Strine said at the time.

Almond is represented in the DWR case by David H. Wollmuth and Michael C. Ledley of Wollmuth Maher & Deutsch in New York and Peter B. Ladig of Bayard P.A. in Wilmington. Franklin is represented by Thomas A. Brown

of Morea Schwartz Bradham Friedman & Brown and Scott J. Watnik of Wilk Auslander in New York and Norman M. Monhait of Rosenthal Monhait & Goddess in Wilmington.

Glenhill is represented by Adrienne M. Ward and Brian Katz of Olshan Frome Wolosky and John B. Horgan of Ellenoff Grossman & Schole in New York and Andrew D. Cordo and F. Troupe Mickler IV of Ashby & Geddes in Wilmington.

The case is captioned *Almond v. Glenhill*.

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