COURT OF CHANCERY
OF THE
STATE OF DELAWARE

DONALD F. PARSONS, JR.
VICE CHANCELLOR

New Castle County CourtHouse
500 N. King Street, Suite 11400
Wilmington, Delaware 19801-3734

Submitted: July 28, 2005
Decided: November 4, 2005

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Re: *Diane Romero v. Career Education Corporation*,
Civil Action No. 793-N

Dear Counsel:

Pending before the Court is Defendant Career Education Corporation's ("CEC") Motion for Reargument of Its Motion to Dismiss Plaintiff Diane Romero's Complaint filed pursuant to 8 *Del. C.* § 220. For the following reasons, Defendant's motion is denied.

I. BACKGROUND

CEC, a Delaware Corporation, provides private, post-secondary education at 81 schools located primarily in North America and Europe.[1] Romero has been a stockholder of CEC since November 25, 2003.

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[1] *Romero v. Career Educ. Corp.*, 2005 WL 1798042, at *1 (Del. Ch. July 19, 2005).

Romero served a written demand to inspect the books and records of CEC on January 6, 2004 ("January 6 Demand"). Contending that the demand was too broad, CEC asked Romero to narrow her request. Romero complied, and on May 26, 2004, provided CEC with a more narrowly-tailored demand ("May 26 Demand"). In the May 26 Demand, Romero's stated purpose was to investigate possible breaches of fiduciary duties by CEC's board of directors and executives.[2] As a result, CEC agreed to produce all the documents Romero set forth in the May 26 Demand so long as the parties entered into a confidentiality agreement.

Among other things, Romero requested a variety of documents relating to both student enrollment and retention and the company's Ethics Codes.[3] CEC responded by producing only 152 documents, which consisted primarily of publicly filed 10-K's.[4] Unsatisfied with CEC's production, Romero filed a complaint on November 3, 2004 under 8 *Del. C.* § 220.

CEC moved to dismiss Romero's complaint for two reasons. First, CEC claimed that Romero did not have a proper purpose as defined by § 220(b). In addition, CEC

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[2] The alleged breaches of fiduciary duty stem from directors and executives "actively participating in, or failing to make a good faith effort to detect, investigate, prevent and correct, violations of the Ethics Codes, particularly with regard to falsification of, or other wrongdoing or impropriety with respect to, records of student enrollment, retention, and graduation." *Id.*

[3] *Id.*

[4] *Id.*

argued that Romero's complaint contravened the Private Securities Litigation Reform Act of 1995 ("PSLRA")[5] and was preempted by the Securities Litigation Uniform Standards Act of 1998 ("SLUSA").[6] CEC argued that these federal statutes prohibit discovery while other securities related actions are pending and therefore preempt any § 220 demand. While CEC's Motion to Dismiss Romero's § 220 action was pending, Romero filed a derivative action against CEC on June 3, 2005.[7]

In a memorandum opinion entered on July 19, 2005 ("July 19 Opinion"), this Court rejected both of CEC's arguments. In denying CEC's motion to dismiss, the Court held that (1) Romero alleged a proper purpose under § 220, and (2) the stay of discovery in the securities litigation did not preclude her § 220 demand.[8]

On July 28, 2005, CEC moved for reargument on two grounds. First, CEC claims that by filing a derivative complaint Romero has conceded that she has no need for relief in this § 220 action. Second, CEC argues that Romero's more recent filing of a Motion to Unseal the Amended Complaint in the derivative action proves Defendant's contention that Plaintiff is using the § 220 action merely as a means to circumvent the stay in the pending federal securities action.

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5 Pub. L. No. 104-67, 109 Stat. 737 (1995).

6 Pub. L. No. 105-353, 112 Stat. 3227 (1998).

7 *Romero v. Dowdell, et al.*, C.A. No. 1398-N (Del. Ch.) (filed under seal).

8 *Romero*, 2005 WL 1798042, at *2-3.

II. ANALYSIS

The standard applied for a motion for reargument under Court of Chancery Rule 59(f) is well settled: "[T]he moving party [must] demonstrate that the Court's decision was predicated upon a misunderstanding of a material fact or a misapplication of the law."[9]

In addition, Court of Chancery Rule 59(f) is only available to re-examine the existing record; therefore, new evidence should not be considered on a motion for reargument.[10] Further, a motion for reargument will not be granted when a party merely restates its prior arguments.[11]

The Court did not misunderstand any material facts in considering CEC's motion to dismiss. While CEC argues that there has been a "change in circumstances"[12] since the Motion to Dismiss was considered, the only "change" referred to by CEC is Romero's filing of her derivative complaint. The derivative suit, however, was filed approximately six weeks before this Court decided CEC's Motion to Dismiss. Indeed, as noted in the July 19 Opinion, the Court knew about the derivative action when it decided

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9 *Goldman v. Pogo.com Inc.*, 2002 WL 1824910, at *1 (Del. Ch. July 16, 2002).

10 *Miles, Inc. v. Cookson America, Inc.*, 677 A.2d 505, 506 (Del. Ch. 1995) (citing *Maldonado v. Flynn*, 1980 WL 272822 (Del. Ch. July 7, 1980)).

11 *Id.*

12 Def.'s Mot. for Reargument of its Mot. to Dismiss at ¶ 4.

CEC's Motion.[13] CEC could have addressed the pertinence of Romero's derivative suit to this § 220 action while its Motion to Dismiss was still pending, but it failed to do so.

The Court also did not misapply the law when it denied CEC's Motion to Dismiss. CEC argues that the filing of the derivative suit constitutes a concession by Romero that she has received sufficient documents from CEC to plead demand futility. Therefore, the argument continues, Romero can no longer demonstrate a proper purpose for her § 220 demand. Defendant further contends that the only remaining purpose for continuing with the § 220 action is to obtain general discovery, which is not a proper purpose.

The filing of a derivative suit during the pendency of a § 220 action does not necessarily extinguish all proper purposes. This court rejected an argument similar to CEC's in *Khanna v. Covad Commc'n Group, Inc.*[14] In *Khanna*, the defendant alleged that the filing of a derivative claim after the commencement of a § 220 action was a concession that the plaintiff had sufficient information to justify the filing of their derivative claim, and therefore destroyed any proper purpose that might have existed before the filing of the derivative suit.[15] The court disagreed.

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13 *See Romero*, 2005 WL 1798042, at *2 n.8 ("On June 3, 2005, Romero herself filed a derivative action, which is currently the subject of a motion to dismiss.").

14 2004 WL 187274 (Del. Ch. Jan. 23, 2004).

15 *Id.* at *4.

When the overlap in suits results from a defendant's failure to comply with its § 220 obligations, the filing of a derivative complaint will not make an otherwise proper purpose improper. In *Khanna* the court noted that, if the defendant had complied with the plaintiff's demands, the plaintiff would not have filed the § 220 complaint and there would have been no overlap. More importantly, a rule such as CEC urges would encourage corporations to avoid complying with their § 220 obligations. That is, corporations could stall long enough to force plaintiffs to file their substantive claims before the statute of limitations expires even though their § 220 demands remained pending. Further, the mere fact that a party has concluded that it has sufficient information to file a derivative complaint does not mean that additional information the plaintiff otherwise would be entitled to would not be helpful in responding to a motion to dismiss under Court of Chancery Rule 12(b)(6) or 23.1.[16]

For the same reasons stated in *Khanna*, I find unpersuasive CEC's argument that the filing of a derivative claim extinguishes any proper purpose for a § 220 demand. In the July 19 Opinion, I concluded that CEC failed to comply with its § 220 obligations. In fact, the majority of the documents CEC produced were already available to the public. Romero's filing of a derivative action in June 2005 did not relieve CEC of its duties

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[16] *Id.*

under § 220. Thus, the Court did not misapply the law when it denied Defendant's Motion to Dismiss.

In a letter to the Court filed within the last few weeks, CEC points to an additional "change in circumstances."[17] On October 17, 2005, Plaintiff filed a Motion to Unseal the Amended Derivative Complaint in the related action. According to CEC, that motion demonstrates that Plaintiff is using this § 220 action to circumvent the stay of discovery in the federal securities litigation, and therefore lacks a proper purpose.[18]

The fact that Romero has moved to unseal the amended derivative complaint does not convince me that she is trying to circumvent the discovery stay in the federal securities litigation. Under the parties confidentiality agreement, Romero has the right to challenge in this Court the propriety of Defendant's confidentiality designations. Romero's Motion to Unseal currently is being briefed in the derivative action. The Court expresses no opinion about the merits of that motion at this time. The issue will be dealt with in the context of the derivative action.

Furthermore, while the existence of a confidentiality agreement in this action supported the denial of Defendant's motion to dismiss, it was not determinative.[19] In the July 19 Opinion, the Court also made reference to the facts that Romero's demand was

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17 Def.'s Letter to Court filed October 17, 2005, at 1.

18 *Id.* at 2.

19 *Romero*, 2005 WL 1798042, at *4.

more narrow than discovery in general litigation and that her attorneys represented to the Court that they no longer were involved in the securities litigation.[20]

III. CONCLUSION

For the foregoing reasons, Defendant's motion for reargument is denied.

IT IS SO ORDERED.

Sincerely,

/s/Donald F. Parsons, Jr.

Vice Chancellor

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20 *Id*.