

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE  
IN AND FOR NEW CASTLE COUNTY

ATR-KIM ENG FINANCIAL CORPORATION, )  
and ATR-KIM ENG CAPITAL PARTNERS, )  
INC., )

Plaintiffs, )

v. )

C.A. No. 489-N

CARLOS R. ARANETA, HUGO BONILLA, )  
LIZA BERENGUER and MARITES VICENTE, )

Defendants, )

and )

PMHI HOLDINGS CORPORATION, )  
(f/k/a LBC GLOBAL CORPORATION), a )  
Delaware corporation, )

Nominal Defendant. )

MEMORANDUM OPINION

Date Submitted: October 9, 2006  
Date Decided: December 21, 2006

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**STRINE, Vice Chancellor.**

## I. Introduction

Plaintiffs ATR-Kim Eng Financial Corp. (“ATR Financial”) and ATR-Kim Eng Capital Partners, Inc. (“ATR Capital”) (collectively, “ATR”) own 10% of the shares of a holding company — PMHI Holdings Corp. (f/k/a LBC Global Corp.) (the “Delaware Holding Company”). ATR claims that defendant Carlos Araneta, who controlled the remaining 90% of the Delaware Holding Company’s equity and served as chairman of its board, caused the corporation to transfer its key assets — its ownership of several businesses worth over \$35 million (the “LBC Operating Companies”) — to members of his family in violation of his fiduciary duties. The Delaware Holding Company was formed precisely to enable ATR to share with Araneta in the benefits of owning the LBC Operating Companies. But, after Araneta denuded the Delaware Holding Company of those assets, ATR was left with only a minority stock ownership position in a floundering joint venture that it had undertaken with Araneta, a position that is worth very little. Meanwhile, Araneta and his family were left with sole control of the LBC Operating Companies, which, from the record, appear to be thriving.

Furthermore, ATR claims that the other members of the board of directors of the Delaware Holding Company, defendants Hugo Bonilla and Liza Berenguer, are jointly and severally liable for this harm because they failed to take any steps to monitor Araneta and prevent his self-dealing. Bonilla was the head of Araneta’s operations in the United States, and Berenguer served as the Chief Financial Officer of his worldwide enterprise. They essentially admit that they regarded themselves as mere employees of Araneta and failed to take any steps to fulfill their fiduciary duties to the Delaware Holding Company.

As directors, they were charged with protecting the interests of their corporation and its stockholders. Yet, Bonilla and Berenguer allowed Araneta to do whatever he wanted, without any examination of whether his conduct benefited the Delaware Holding Company and all of its stockholders, rather than simply Araneta personally.

In this post-trial opinion, I find that Araneta breached his duty of loyalty by impoverishing the Delaware Holding Company for his own personal enrichment. Bonilla and Berenguer also breached their duty of loyalty. Having assumed the important fiduciary duties that come with a directorship in a Delaware corporation, Bonilla and Berenguer acted as — no other word captures it so accurately — stooges for Araneta, seeking to please him and only him, and having no regard for their obligations to act loyally towards the corporation and all of its stockholders. Such behavior is not indicative of a good faith error in judgment; it reflects a conscious decision to approach one's role in a faithless manner by acting as a tool of a particular stockholder rather than an independent and impartial fiduciary honestly seeking to make decisions for the best interests of the corporation. Although it is clearly the case that Araneta is the most culpable of the defendants, Bonilla and Berenguer are accountable for their complicity in his wrongful endeavors.

To the point of Araneta's misconduct, the sad reality is that his behavior as a director of the Delaware Holding Company and as a defendant in this litigation clearly manifests: (1) an intent on his part to defraud and injure ATR by consummating a de facto liquidation of the Delaware Holding Company in which its value was siphoned out entirely to the Araneta family, to the exclusion of ATR; (2) a willingness to put an

innocent administrative employee of his at risk by falsely suggesting that she alone (rather than Araneta, Bonilla, and Berenguer as a group) comprised the board of directors of the Delaware Holding Company at the time Araneta impoverished it, all in a cynical attempt to avoid this court's jurisdiction and accountability for his own actions; (3) a contempt for the judicial process by providing a false and incomplete response to a legitimate demand for books and records under 8 *Del. C.* § 220; (4) a desire to obstruct the efficient procession of this litigation by making the discovery process unduly expensive and by failing to promptly produce required discovery; and (5) a shamelessness about telling lies so extreme as to make it impossible to address all of the numerous false statements and assertions he made both from his own lips and through theories he provided to his counsel.

Because of the difficulty of implementing a remedy that would undo the de facto liquidation of the Delaware Holding Company that Araneta effected, I enter an order requiring Araneta to pay to ATR a judgment based on the price ATR originally paid for its 10% equity stake in the Delaware Holding Company, plus pre-judgment and post-judgment interest pegged to a cost of capital determined by reference to an agreement between Araneta and ATR that provides the most reliable benchmark of the interest rate required to make ATR whole and to avoid unjustly enriching Araneta. This judgment may well understate the relief due ATR, as it appears that the LBC Operating Companies are booming. But ATR is willing to accept this more limited remedy and it is the most efficient means of providing it fair recourse.

Given Araneta's egregious misconduct both before and during this litigation, fee shifting under the bad faith exception to the American Rule is in order. Only through such an award will ATR be made whole for the excessive costs it had to incur in order to address Araneta's faithless acts, and only through such an award will Araneta's misuse of a Delaware corporation be rectified. The fee shifting award will also extend to any collection efforts ATR must expend in attempting to collect on this judgment.

Bonilla and Berenguer will be held jointly and severally liable for the monetary judgment but not for the fee-shifting award.

## II. Factual Background

These are the facts as I find them after trial.<sup>1</sup>

### A. Overview Of The Key Arrangements Between Araneta And ATR

Before describing the origins of the current dispute between ATR and Araneta in more detail, it is useful to provide a basic overview of the parties and how they came to form the Delaware Holding Company.

Araneta first met ATR's chairman Ramon Arnaiz when they were in kindergarten in the Philippines. During their school days, Araneta and Arnaiz became close friends. After many years of friendship, the two fell out of touch as each embarked on his own career.

Araneta left the Philippines to attend college in the United States. After completing his studies, Araneta returned home to work in his family's business — an

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<sup>1</sup> Citations to plaintiffs' exhibits ("PX \_\_"), defendants' exhibits ("DX \_\_"), or the trial transcript ("Tr. at \_\_") are illustrative. Other portions of the record often support the same findings.

empire of companies run from the Philippines that share the initials LBC in their names (collectively, “LBC”).<sup>2</sup> Araneta gained prominence by developing LBC Express, Inc. (f/k/a LBC Air Cargo), a Philippine version of Federal Express, into an international money remittance business that facilitates and profits from wire transfers made by Filipino expatriates who have gone abroad to make a living but continue to support their families still living in the Philippines. As a result of his efforts, Araneta came to dominate and control LBC and is the ultimate manager for the thousands of employees working for LBC and the hundreds of locations owned by LBC around the globe.<sup>3</sup>

Meanwhile, Arnaiz went into the financial services field. He gained prominence by spearheading the revitalization of a major financial firm’s Hong Kong office. Following that success, Arnaiz (“A”), along with Manuel Tordesillas (“T”) and Lorenzo Roxas (“R”), founded ATR, a Philippine corporation licensed to provide investment and financial services. From its creation, ATR has been essentially a capital provider, helping businesses raise capital and investing its own funds (and those of its investors) in various enterprises.

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<sup>2</sup> LBC Development Corp., a corporation organized and existing under the laws of the Philippines, was the primary holding company for the Araneta family businesses before the events giving rise to this dispute. Through this entity, the Aranetas owned the non-U.S. LBC Operating Companies that provided courier and money remittance services in the Philippines and to Filipino expatriates working in other nations. These entities include the following companies and their subsidiaries: LBC Domestic Franchise Co., Inc., LBC Express, Inc., LBC Mabuhay Development Philippine Corp., LBC International, Inc., and LBC Development Bank. The Aranetas also own LBC Holdings USA Corp. (overseen by defendant Bonilla), which serves Filipinos working in the United States.

<sup>3</sup> Although Araneta has at various times used his children to directly hold stock in the LBC Operating Companies, his children are subject to his will as to these matters. Araneta exercises de facto and clear control over his family’s worldwide holdings.

In the late 1990s, Araneta and Arnaiz reunited. At that time, Araneta turned to Arnaiz and ATR for investment banking assistance on behalf of his LBC enterprise. Initially, Araneta engaged ATR to search for capital and to prepare LBC for a public offering. After a while, however, the relationship changed.

In 1999, ATR began investigating an opportunity to purchase a controlling interest in The Professional Group Plans, Inc., a corporation that sold “pre-need” insurance policies designed to cover expenses (such as educational and health costs) that buyers expected to face in the future (the “Pre-Need Company”).<sup>4</sup> Seeing potential synergies in this industry between ATR’s financial acumen and LBC’s logistical network, which was well-positioned to attract Filipino customers who had traditionally purchased these policies, Arnaiz offered to structure the investment in the Pre-Need Company as a joint enterprise with Araneta. After some negotiation, Araneta agreed to participate in the deal ATR proposed.

Based on this understanding, ATR and Araneta executed two contracts — an “Undertaking Agreement”<sup>5</sup> and a “Joint Venture Agreement”<sup>6</sup> — that set out the terms of their relationship and laid the groundwork for the Delaware Holding Company’s incorporation. Through the Joint Venture Agreement, ATR and Araneta bought a controlling interest in the Pre-Need Company, and as part of this transaction, ATR

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<sup>4</sup> According to Araneta, “A pre-need company is like . . . an insurance plan except that an insurance plan is something that you sell but you don’t know when the event will happen. In the case of the pre-need, it’s the same thing but a date is set.” Tr. at 20. “In other words, you keep on paying monthly maybe for 20 years; and if anything happens to you within that 20-year period you can make a claim for your health or for your education.” *Id.*

<sup>5</sup> PX 1.

<sup>6</sup> PX 2.

advanced \$3.922 million on Araneta's behalf (the "Advances").<sup>7</sup> In exchange for the Advances, Araneta pledged, in the Undertaking Agreement, to contribute the LBC Operating Companies along with his newly acquired interest in the Pre-Need Company to a new holding company and to issue to ATR a 10% minority interest in that entity.<sup>8</sup>

To protect ATR's investment in the LBC Operating Companies, the Undertaking Agreement granted ATR contractual protections, including the right to a seat on the board of directors of any holding company that Araneta ultimately formed as well as a five-year put option, which, when exercised, required Araneta to buy out ATR's interest at the higher of (i) the issue price of ATR's shares plus a premium of between 22% and 25% per year, or (ii) the adjusted book value of ATR's shares.<sup>9</sup> Likewise, to safeguard their joint investment in the Pre-Need Company, ATR and Araneta executed a Stockholders

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<sup>7</sup> The joint investment in the Pre-Need Company was made through one of ATR's subsidiaries, Professional Mutual Holdings, Inc. ("Professional Holdings") in which both Araneta and ATR had acquired 50% interests at a price of 37.5 million pesos (about \$937,500) each. Using its 75 million pesos in contributed capital as well as an additional 239 million pesos nominally contributed on equal terms by ATR and Araneta (119.5 million pesos each), Professional Holdings purchased 80% of the Pre-Need Company. In this transaction, ATR advanced Araneta's portion as well as its own. As a result, Araneta owed ATR 157 million pesos (approximately \$3.922 million).

<sup>8</sup> The Undertaking Agreement specifically provided that Araneta would transfer the following assets to the Delaware Holding Company:

- (i) LBC Domestic Franchise Co., Inc. and its subsidiaries;
- (ii) LBC Express, Inc. and its subsidiaries;
- (iii) LBC Mabuhay Development Philippine Corp. and its subsidiaries;
- (iv) LBC Holdings USA Corp. and its subsidiaries;
- (v) LBC International, Inc. and its subsidiaries (including all remittance businesses outside of LBC Holdings USA Corp.);
- (vi) LBC Development Bank;
- (vii) the foreign exchange business arising from the remittance transactions involving any and all of the above companies.

PX 1 at 2. For simplicity's sake, I refer to these as the LBC Operating Companies.

<sup>9</sup> ATR also had an option to require Araneta to cede the shares the Advances had purchased as well as all rights and interests secured by the Advances if within a period of three months from the closing of the Joint Venture Agreement the LBC Operating Companies were not transferred into the holding company. Although it is undisputed that the holding company was not formed or funded within three months, ATR chose not to exercise this option.



Agreement which they attached to their Joint Venture Agreement (the “Stockholders Agreement”)<sup>10</sup>. The Stockholders Agreement evenly divided the eight (out of ten) board seats secured by ATR’s and Araneta’s joint 80% interest in the Pre-Need Company, and unanimously appointed Topax Colayco, the residual 20% shareholder in the Pre-Need Company, to be its President and CEO.

Although the Undertaking Agreement did not require that the holding company it contemplated be a Delaware, or even an American, entity, Araneta perceived the United States as a favorable jurisdiction in which to raise capital and viewed Delaware as a tax haven. In particular, Araneta viewed a Delaware entity as a vehicle that could be used to access the American capital markets through an initial public offering of stock. As a result, in January 2000, Araneta incorporated the Delaware Holding Company and presented ATR with 3,000 of its shares (10%) while personally retaining control over the residual 27,000 shares (90%). Likewise, Araneta appointed and dominated the Delaware Holding Company’s board of directors, which consisted of himself, defendant Berenguer (Araneta’s niece and the CFO of the LBC group of companies), and defendant Bonilla (the head of LBC’s U.S. operations).<sup>11</sup>

Thus, after 1999, ATR and Araneta were entwined in several ways: (1) they were contractually linked through the Undertaking Agreement, the Joint Venture Agreement, and the Shareholders Agreement; (2) they shared equal shareholder and directorial

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<sup>10</sup> DX 1 at Annex “A”.

<sup>11</sup> Tr. at 109-15. I also note that ATR was not permitted to exercise its contractual right to appoint a director. By letter dated June 24, 2003, Arnaiz explained, “We were never provided regular, updated financials and a board seat . . . in spite of our repeated request[s].” PX 51.

interests in the Pre-Need Company; (3) they possessed inverse majority and minority shareholder interests in the Delaware Holding Company; and perhaps most importantly, (4) Araneta and ATR were tied together through Araneta's friendship with Arnaiz.

#### B. The Personal Nature Of This Dispute

ATR's claims against Araneta boil down to an allegation that he abused his position of control over the Delaware Holding Company. Specifically, ATR claims that Araneta transferred the LBC Operating Companies from the Delaware Holding Company to his children for no consideration without notice to ATR and without following the process required by Delaware law.

Araneta does not dispute that the LBC Operating Companies are now owned by his family or that ATR has no interest in those assets through its minority ownership of the Delaware Holding Company. He merely claims never to have transferred ownership of the LBC Operating Companies to the Delaware Holding Company in the first place. He says that ATR knew that. What he never says is why ATR would have made a nearly \$4 million payment to acquire 10% of an entity with no valuable assets. Further, in the event that I conclude that he is lying when he says that the Delaware Holding Company never owned the LBC Operating Companies, Araneta offers only the half-hearted and wholly-illogical defense that he was permitted to reclaim the LBC Operating Companies without payment through an accounting "offset" because he was the one who initially contributed the LBC Operating Companies to the Delaware Holding Company.

To understand how a case as stark as this actually resulted in a trial, rather than a voluntary settlement by Araneta, it is useful to return to Araneta's relationship with his old friend, Ramon Arnaiz. That's right, this case is personal.

Araneta has known Arnaiz since they were five years old. As Araneta testified, he and Arnaiz were "very, very close friends, buddy buddies" who sat next to each other in classes and had parents who played mahjong together several times a week while they were growing up.<sup>12</sup> Although Araneta and Arnaiz went to different colleges, and ultimately into different careers, "whenever [they] saw each other [before this dispute], it was really a warm[] meeting."<sup>13</sup>

But, as a result of their business dealings, Araneta's friendship with Arnaiz has ended. Araneta testified that he considers this case a "personal fight" between himself and Ramon Arnaiz.<sup>14</sup> He stated in his deposition and confirmed at trial that he did not think his co-directors had "anything to do with this tie-up with ATR."<sup>15</sup> And, perhaps most tellingly, he admitted on cross examination that at least "to some extent" this litigation was "over the disintegration of [his] friendship" with Arnaiz.<sup>16</sup>

That disintegration began in November 2002 when ATR sold its 50% interest in Professional Holdings, the corporation that owned 80% of the Pre-Need Company. Having closely aligned himself with Arnaiz and ATR, Araneta felt betrayed by that action. In compliance with the Shareholders Agreement, which secured ATR's right to

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<sup>12</sup> Tr. at 16.

<sup>13</sup> Tr. at 17.

<sup>14</sup> Tr. at 104.

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

sell its Professional Holdings shares as long as Araneta was given a right of first refusal, ATR offered its shares to Araneta, but he refused to purchase them.<sup>17</sup> After Araneta declined, ATR sold its interest to Topax Colayco (the “Colayco Sale”) giving Colayco co-equal control with Araneta over Professional Holdings and thus over Professional Holdings’s 80% control bloc in the Pre-Need Company. But, because Colayco already directly owned the residual 20% of the Pre-Need Company that Professional Holdings did not, Araneta understandably viewed himself as having less leverage than Colayco in this dynamic.

Notwithstanding ATR’s contractual right to sell its interest in Professional Holdings and Araneta’s own failure to exercise his right of first refusal, Araneta felt victimized by Arnaiz and ATR and blamed them for subjugating him to the role of a minority investor under Colayco’s de facto control. Even though Colayco had been a longstanding 20% shareholder in the Pre-Need Company, had managed its day-to-day operations as its President and CEO with Araneta’s consent, and had served on the board of the Pre-Need Company with Araneta from the time Araneta first invested in the Pre-Need Company, Araneta testified that he felt as though he was “stuck running this company with a stranger.”<sup>18</sup> Most important, he felt that ATR had done the sticking.<sup>19</sup>

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<sup>17</sup> See PX 44 (offering shares); Tr. at 59 (rejecting offer); *see also* DX 1 at Annex “A” § 5 (describing rights and restrictions regarding transfers of Professional Holdings shares).

<sup>18</sup> Tr. at 86-90; DX 1 at Annex “A” § 3.03.

<sup>19</sup> Araneta testified, “When [ATR] decided to get out of the business, I said ‘My God, that’s the very essence why I got involved in this business. . . . I don’t understand the pre-need business . . . . The very person you’re selling it to, I don’t even know. I came to know him because of you . . . . How can you do this to me?’” Tr. at 60-61.

Araneta allowed this hostility to affect his management of the Delaware Holding Company. After the Colayco Sale, Araneta withheld information, effectively closed the lines of communication with ATR, and eventually transferred all of the LBC Operating Companies out of the Delaware Holding Company.

### C. The Discovery Of Araneta's Misconduct

Araneta began to exact his revenge soon after the Colayco Sale was completed. In the months that followed, ATR repeatedly requested information on the condition of the Delaware Holding Company in which it still had nearly \$4 million invested. But Araneta summarily rebuffed those requests. Araneta testified that any request ATR made for information during the entire 2003 calendar year went ignored because he was “no longer talking to them because [he was] upset with Mr. Arnaiz.”<sup>20</sup> Throughout the first half of that year, lawyers in the Philippines exchanged letters regarding the “ongoing fight” between Araneta and Arnaiz, but were unable to resolve the matter.<sup>21</sup>

Fed up, ATR, through its attorneys, sent a formal books and records demand letter to Araneta on July 18, 2003.<sup>22</sup> In that letter, ATR exercised its right as a stockholder of a Delaware corporation to request financial statements of the Delaware Holding Company as well as documents showing the Delaware Holding Company's ownership of the LBC Operating Companies and Araneta's interest in the Pre-Need Company.<sup>23</sup> In hopes of a response, ATR sent additional demand letters to the Delaware Holding Company's

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<sup>20</sup> Tr. at 235.

<sup>21</sup> Tr. at 233.

<sup>22</sup> PX 53 at 1-3. ATR copied Araneta's son, his lawyer, and the head of LBC's U.S. operations, defendant Bonilla, on this demand. *Id.* at 3.

<sup>23</sup> *Id.* at 4-9.

corporate secretary at its registered address and to Araneta's attorney in the Philippines on the same day as it sent its letter to Araneta.<sup>24</sup> These additional demand letters sought to review the Delaware Holding Company's stock ledger, the records of all business transactions of the corporation, and the minutes of every meeting of the stockholders and directors of the Delaware Holding Corporation since its incorporation.<sup>25</sup>

Each of ATR's demand letters warned that ATR would file suit to protect its interests if its demands were denied.<sup>26</sup> Yet, even knowing legal action was imminent, Araneta testified that he was "so angry with Mr. Arnaiz" that he "ignored these letters" and prevented ATR from gaining the information it sought.<sup>27</sup> Starved for information, ATR filed an action under 8 *Del. C.* § 220 in this court on October 27, 2003. But still irked by ATR's decision to sell its interest in Professional Holdings, Araneta "deliberately ignored" that lawsuit and instructed Bonilla not to provide the requested information.<sup>28</sup>

Only after being ordered by this court to turn over the records requested by ATR did Araneta do so. On January 14, 2004, Araneta produced a "Compliance"<sup>29</sup> that purported to include all available documents but totaled only nine pages and failed to

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<sup>24</sup> *Id.* (copying Araneta, his son, and Bonilla on each).

<sup>25</sup> *Id.*

<sup>26</sup> *See* PX 53 at 2 ("If we do not receive any response from you within ten (10) days . . . we shall be constrained to initiate the appropriate legal actions . . . to protect our client's interests."); *id.* at 5, 8 (providing similar warnings).

<sup>27</sup> *Id.* at 238.

<sup>28</sup> *Id.* at 239. Specifically, when discussing the § 220 litigation with Bonilla, Araneta told him, "Don't mind it." *Id.*

<sup>29</sup> PX 54.

include many essential corporate papers.<sup>30</sup> The nine pages that Araneta did produce, however, included three documents that caused ATR great concern. Those documents — two balance sheets and a purported resolution of the board of directors — led ATR to believe that Araneta had conducted a de facto (and non-pro rata) liquidation of the Delaware Holding Company’s assets and that Araneta was attempting to escape responsibility for that act.

The two balance sheets that manifest the de facto liquidation are dated March 2003 and December 2003, respectively. Under Philippine accounting conventions, as adopted by the parties, both balance sheets reflect “investments” and “liabilities” in an unusual way. On the Delaware Holding Company’s books, “investments” referred to the LBC Operating Companies and the Professional Holdings shares purchased for Araneta by ATR’s Advances, which were to be owned by the Delaware Holding Company under the terms of the Undertaking Agreement. “Liabilities” represented the pro rata amounts due to Araneta and ATR as a result of the equity positions that each gained for their capital contributions. As of March, the Delaware Holding Company’s balance sheet reflected approximately \$36 million in “investments” and approximately \$39 million in

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<sup>30</sup> In response to the pithy Compliance, ATR was permitted to depose Mr. Bonilla under 10 *Del. C.* § 368. That deposition uncovered several documents that had not been previously disclosed including the bylaws of the corporation, the corporate kit, and various financial and tax-related working papers. Finding that the corporation had not complied with its December 22 order, the court awarded ATR its attorneys’ fees in prosecuting the § 220 action. Araneta’s inappropriate behavior continued throughout the present litigation wherein he was repeatedly non-responsive, delayed the proceeding, and had to be admonished for exhibiting “close to contemptuous behavior” and having committed a “clear violation” of applicable rules by engaging in a “persistent pattern [of] flouting obligations that he owes under the rules of this Court and, frankly, under the Delaware General Corporation Law.” See 4/20/04 Hearing Tr. at 10, 57, 59, 61, 67 (noting that “the horsing around, the inappropriate behavior, began long ago”).

“liabilities.” But, by December, the balance sheet showed only \$937,500 in “investments” and \$3.922 million in “liabilities.” These financial statements indicated that during the last nine months of 2003 Araneta stripped the Delaware Holding Company of the LBC Operating Companies. The only operating asset he left in the Delaware Holding Company was ownership of the de facto minority position in the Pre-Need Company.

A board of directors resolution Araneta produced in the Compliance is relevant to considering Araneta’s intentions. In that document, dated May 22, 2003, Araneta putatively resigns his directorship along with Berenguer and Bonilla effective that day. In their stead, Araneta’s secretary, Vicente, was supposedly appointed that day as the President and sole director of the Delaware Holding Company. As I discuss later, Vicente never assumed those positions and Araneta, Bonilla and Berenguer never left the Delaware Holding Company board. Araneta seems to have created this fiction in order to set up a phony defense to this court’s jurisdiction and to claim that Vicente was responsible for any misfeasance at the Delaware Holding Company after May 22, 2003 — a futile exercise in “plausible deniability.”

#### D. The Parties’ Claims

Based on the balance sheets unearthed in the § 220 action, ATR filed this lawsuit on June 3, 2004. ATR’s complaint alleges direct and derivative injuries caused by the removal of the LBC Operating Companies, which were valued at nearly \$36 million, from the Delaware Holding Company between March and December 2003. ATR claims that it was harmed as a stockholder of the Delaware Holding Company when Araneta



effectively made a \$36 million liquidation payment to his family without following the required process and without distributing to ATR its pro rata portion thereof. ATR also alleges that the corporation itself was injured by this transaction because it received no substantial consideration for the transfer of substantially all of its assets to the Araneta family.

In response, Araneta mounted three shifting defenses. First, he raised a “scapegoat” jurisdictional defense based on his purported resignation from the board of directors.<sup>31</sup> Further, in the event his jurisdictional argument proved unpersuasive, Araneta attempted to explain that contrary to his own contemporaneous admissions in e-mails, letters, and financial statements — and, yes, even tax filings — the LBC Operating Companies were never transferred into the Delaware Holding Company in the first instance because of tax issues.<sup>32</sup> Ultimately, in his deposition and at trial, perhaps recognizing the difficulties inherent in this “believe-me-now-I-was-lying-then” tax defense, Araneta proffered a half-hearted justification for the transfer of assets as an “offset” against the “liability” his family was owed for having contributed those assets.<sup>33</sup> If his implausible excuses were not expending ATR’s and this court’s limited resources and impeding ATR’s just claim for recompense, Araneta’s brazen and abundant falsehoods might be amusing. Because they have these costs, they are appalling.

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<sup>31</sup> Araneta raised this defense in his very first pleading, a Motion to Dismiss or Stay filed in July 6, 2004. Araneta also made this argument as his first affirmative defense in his Answer dated August 2, 2004.

<sup>32</sup> This “tax defense” first appeared with along with the jurisdictional defense in Araneta’s Motion to Dismiss or Stay. Over the two years since then, this argument gained prominence, becoming the focus of Araneta’s pre-trial briefing.

<sup>33</sup> *See* Tr. at 253-58 (referencing deposition testimony).

## 1. Araneta's Scapegoat Defense

In May 2003, Araneta claims that the composition of the board of directors of the Delaware Holding Company changed. Araneta asserts, based on a purported board resolution dated May 22, 2003 (the "May 2003 Resolution"), that he, Bonilla and Berenguer resigned as directors, and were replaced by one of his employees at LBC in the Philippines, Marites Vicente.

Vicente is the assistant to the executive secretary to the chairman at LBC, which means that she reports directly to Araneta's secretary and ultimately to Araneta himself.<sup>34</sup> In this position, Vicente did the typing and filing for Araneta and his in-house attorneys, who included Ronaldo Tugonon, and sat at a desk just outside Araneta's office.<sup>35</sup> As part of her responsibilities, Vicente testified that she was regularly called upon to sign documents, many of which she did not understand, at the request of her bosses — Araneta and his attorneys.<sup>36</sup> For her work, Vicente earned a salary of 11,500 pesos (less than \$300) per month. Valuing her job, Vicente never refused to perform the tasks her superiors asked her to perform, and in the three years she had worked for LBC, she never mustered the courage to ask Araneta for a raise even though she believed she deserved one.<sup>37</sup> In this light, Vicente admits that her signature appears on the Compliance, the May 2003 Resolution, and other corporate documents, but she denies that she understood

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<sup>34</sup> Vicente at 5-6.

<sup>35</sup> Vicente at 4-5.

<sup>36</sup> *See, e.g.*, Vicente at 43-45, 47, 50, 58.

<sup>37</sup> Vicente at 3-4, 23-24.

those documents or ever knowingly became a director and officer of the Delaware Holding Company as Araneta has suggested.<sup>38</sup>

Araneta's contention that Vicente was appointed as a director and officer of the Delaware Holding Company is likewise without support in the record. Neither the actions nor testimony of Araneta, Bonilla, Berenguer or Vicente are consistent with a complete overhaul of the board of directors of the Delaware Holding Company in May 2003. Vicente testified that she was never a director or officer of the Delaware Holding Company and that she was "surprised" to learn that she was listed as having those positions.<sup>39</sup> In fact, Vicente did not even know the name of the Delaware Holding Company and did not have any idea what the May 2003 Resolution was when it was shown to her.<sup>40</sup> Perhaps this should have been unsurprising because at his deposition, Araneta testified that he had appointed Vicente to those roles because "[s]he was there" and "[s]he looked timid."<sup>41</sup> Bonilla and Berenguer were likewise unaware of Vicente's appointment to the board. Berenguer testified that she did not learn of Vicente's apparent appointment until October or November of 2004.<sup>42</sup> Bonilla agreed that it was "news to [him] upon receiving [the Compliance containing the May 2003 Resolution while testifying] that [Vicente] was the president and director of the company."<sup>43</sup> Even Araneta

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<sup>38</sup> *See, e.g.*, Vicente at 42-50, 57-58

<sup>39</sup> Vicente at 56.

<sup>40</sup> Vicente at 37-38, 46-47.

<sup>41</sup> Araneta Dep. at 264.

<sup>42</sup> Berenguer at 193.

<sup>43</sup> Bonilla I at 85.

did not acknowledge the role he purportedly assigned to Vicente — failing to name her as one of his co-directors at his deposition.<sup>44</sup>

The actions of Araneta, Bonilla, and Berenguer further manifested their ongoing service as directors after May 22, 2003. On May 23, 2003, the very day after he claims to have resigned, Araneta himself approved a board resolution — which he signed as a director! — to change the name of the Delaware Holding Company (the “Name Change”).<sup>45</sup> Soon thereafter, Bonilla received a copy of the Name Change, and proceeded to prepare, sign, and file a certificate amending the Delaware Holding Company’s charter on June 17, 2003, in accordance with the Name Change.<sup>46</sup> Moreover, in his mind, Bonilla continued to serve as a director of the Delaware Holding Company until December 2003.<sup>47</sup> Consistent with the notion that the leadership of the Delaware Holding Company remained unchanged until late 2003 or early 2004, Berenguer testified that she was still acting in her fiduciary capacity in January 2004.<sup>48</sup> Finally, even Araneta supported this notion when he stated that his co-directors at the time he prepared a balance sheet dated December 31, 2003 were Berenguer and Bonilla, but not Vicente.<sup>49</sup>

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<sup>44</sup> Tr. at 259-60.

<sup>45</sup> PX 54 at 7.

<sup>46</sup> PX 54 at 6.

<sup>47</sup> Bonilla I at 44-45.

<sup>48</sup> See Berenguer at 139-45; Berenguer Ex. 2, at 21 (establishing that Berenguer signed a stock certificate as an officer of the Delaware Holding Company on January 9, 2004). I do note that Berenguer’s testimony regarding her board service was a bit uncertain. She testified that she resigned from the boards of all companies except LBC Development and LBC Development Bank sometime during the period from April or May 2003 through December 2003. But, she was unable to be more specific about her resignation from the Delaware Holding Company’s board than to agree that she believed she resigned “at some point after May 2003,” and that she thought it might have been “[a]ny time from May . . . to August.” Berenguer at 82-83.

<sup>49</sup> Tr. at 259-60.

Thus, only the date on the May 2003 Resolution itself seems to indicate that a transition of the board of directors occurred at the Delaware Holding Company on May 22, 2003. Yet, even this resolution is suspect. At trial, ATR presented evidence that the substance, format, and notary stamps used in preparing this resolution were consistent with it being created in January 2004 — at the same time as the Compliance — rather than in May 2003 — a day before the Name Change.<sup>50</sup> Specifically, the Name Change refers to the Delaware Holding Company as “LBC Global Corporation,” uses a type-written fill-in-the-blank format, and bears a notary stamp from Ronaldo Tugonon in a bolded, sans-serif font.<sup>51</sup> Meanwhile, both the certification of share ownership submitted in the Compliance and dated January 9, 2004 (the “Certification”) and the May 2003 Resolution employ a fully-completed word-processed format, refer to the Delaware Holding Company as “PMHI Holdings Corporation (formerly LBC Global Corporation),” and carry a faded notary stamp from Tugonon in a serif typeface.<sup>52</sup>

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<sup>50</sup> In his post-trial briefing, Araneta submitted the affidavit of Ronaldo Tugonon, the LBC in-house attorney who notarized each of the documents in question, which asserts that Tugonon maintained two offices and two notary stamps, and that his notary logs support the contemporaneous notarization of the May 2003 Resolution, rather than it being back-dated. Def. Post-Trial Br. Ex. 3. I do not consider this post-trial affidavit or its exhibits because it was submitted after the close of evidence at a time when ATR was unable to cross-examine Tugonon or test the merits of his affidavit. *See Stigliano v. Anchor Packing Co.*, 2006 WL 3026168, \*1 (Del. Super. Ct. 2006) (concluding that a post-deposition affidavit was hearsay and “not sufficiently trustworthy to allow its admission” when it had not been “tested by cross-examination”). I further note that the two-cities-two-stamps position Tugonon advances is hardly unassailable given that the “PTR” lines at the end of each notary stamp list the city of Pasay. *See* PX 59. Moreover, Tugonon’s credibility is also suspect because he was likely involved, at the very least, in having Vicente sign documents in a capacity to which she was never properly appointed, which she did not understand, and which she never knowingly assumed.

<sup>51</sup> PX 59.

<sup>52</sup> *Id.*

Perhaps most striking is that when confronted with these documents Araneta did not vehemently deny a charge of fabrication; instead, he claimed a convenient lack of memory.<sup>53</sup>

The timing of the May 2003 Resolution and the date of its appearance in this case also support ATR's claim of fabrication because this chronology establishes a motive for the creation of such a document. The May 2003 Resolution first appeared in the January 2004 Compliance — nearly six months after ATR's July 2003 demand letters put Araneta on notice of impending litigation and nearly three months after the § 220 action was filed — at a time when Araneta must have realized that this court would not permit him to ignore ATR's demands. Moreover, when the May 2003 Resolution was produced in the Compliance, it was accompanied by balance sheets indicating that the removal of the LBC Operating Companies occurred between May 31, 2003 and December 31, 2003 — after Araneta's purported resignation.<sup>54</sup> On that basis, Araneta asserted jurisdictional defenses and attempted to shift responsibility to Vicente.

In light of all the evidence presented, it is possible that the May 2003 Resolution is a back-dated fabrication. Regardless, it is clear that none of the actual Delaware Holding Company directors stood behind it. Each continued to act as a Delaware Holding Company officer and director after that date. As important, it is undisputed that Vicente never accepted appointment to the Delaware Holding Company board and was not properly appointed at any board meeting, by any stockholder vote, or by any other

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<sup>53</sup> Tr. at 142.

<sup>54</sup> See PX 54.

recognized corporate procedure.<sup>55</sup> As such, I find the board of the Delaware Holding Company at all relevant times consisted of Araneta, Bonilla, and Berenguer.

Consequently, I hold that as a factual matter Vicente was never a director of the Delaware Holding Company.

## 2. Araneta's Tax Defense

Araneta's assertion that the Delaware Holding Company was never fully funded or operational is also one I reject as false. Araneta states that he never transferred the LBC Operating Companies to the Delaware Holding Company and that certain post-registration requirements necessary to commence business operations were never completed. As such, he contends that the plan to create and utilize the Delaware Holding Company to implement the Undertaking Agreement was abandoned in May 2000 as a result of certain adverse tax consequences of that proposal. But, these tax issues were resolved by December 2000 — before the Delaware Holding Company was incorporated, before Araneta confirmed the Delaware Holding Company's ownership of the LBC Operating Companies, and before Araneta caused the Delaware Holding Company to file tax returns containing that same information.

Araneta bases his tax argument on the receipt of an opinion letter from a tax specialist that identified material tax obligations that would arise if the LBC Operating Companies were transferred into the Delaware Holding Company. That letter dated May 10, 2000 expressed the opinion that:

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<sup>55</sup> See Berenguer at 200-01 (confirming that the Delaware Holding Company did not have board meetings after January 2001, when its incorporation and funding were completed, and that there was never a formal meeting of the stockholders of the Delaware Holding Company at any time).

The proposal to make [LBC], a Philippine corporation, into a subsidiary of [the Delaware Holding Company] (a US corporation) by an exchange of shares raises a number of concerns . . . [because] corporations formed in the US are taxed by the US on their worldwide income, generally at a 34% or 35% rate on income above \$100,000, though with limited crediting of the foreign tax they pay on foreign income. . . . On the other hand, the US generally has no tax claim on the profits of non-US subsidiaries of non-US corporations.<sup>56</sup>

As a result of these adverse tax consequences, Araneta testified that the Delaware Holding Company was abandoned as the implementation device and his focus shifted towards creating a holding company in Hong Kong.<sup>57</sup>

ATR contends that any tax issue Araneta had with the use of the Delaware Holding Company in the months surrounding May 2000 was resolved before the end of that year. Manuel Tordesillas, ATR's chief executive officer and one of the parties who signed the Undertaking Agreement, testified that he was not made aware of any tax issues that prevented the transfer of assets to the Delaware Holding Company until the start of this litigation.<sup>58</sup> Further, because the Undertaking Agreement placed the responsibility on Araneta and LBC to organize and fund the Delaware Holding Company, Tordesillas explained that ATR was not involved in these implementation issues.<sup>59</sup>

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<sup>56</sup> DX 21 at 4. Araneta also testified that he was informed that the initial transfer of assets into Delaware would create a tax liability in excess of \$7.4 million. Tr. at 35 (“[T]here was a big mistake in incorporating — in putting assets in Delaware because of a very exorbitant or huge tax problem that my family or LBC was going to absorb. At some point, the amount . . . was, in the tune of 7.4 to \$8 million, rough estimates.”).

<sup>57</sup> Tr. at 222.

<sup>58</sup> Tr. at 289.

<sup>59</sup> Tr. at 299-300, 383. This is unsurprising because the primary funding for the Delaware Holding Company was the transfer of assets controlled by Araneta, not ATR.



Moreover, by December 2000, ATR solicited and obtained Araneta's confirmation that he had incorporated and funded the Delaware Holding Company as part of ATR's negotiation of the sale of its 10% interest in the Delaware Holding Company to Philtread Tire & Rubber Company ("Philtread"). In connection with this sale, ATR informed Araneta of the need to complete the transactions required by the Undertaking Agreement. On December 8, 2000, Arnaiz emailed Araneta saying, "[T]o date, LBC is not in compliance with our agreement that requires LBC to set up a holding company incorporating under it all its subsidiaries."<sup>60</sup> That same day, Araneta responded:

PLEASE BE INFORMED THAT WE HAVE ALREADY INCORPORATED THE HOLDING COMPANY FOR YOUR ENTRY AS PER OUR PREVIOUS AGREEMENTS . . . . . WE HAVE ALSO RESOLVED WITH OUR TAX CONSULTANTS THE MANNER OF THE TRANSFER OF SOME ASSETS TO THE HOLDING CO[.], WE SHOULD WITHIN A WEEK OR TWO BE ABLE TO ISSUE IN THE NAME OF ATR [ITS] TEN PERCENT OWNERSHIP AND TOGETHER WITH IT THE STOCK CERTIFICATE CORRESPONDING TO THE TEN PERCENT.<sup>61</sup>

Three days later, on December 11, 2000, Araneta reiterated:

THE HOLDING COMPANY THAT WILL OWN THE "ARANETA" INTERESTS IN 100% LBC HOLDINGS USA, 100% LBC DEVELOPMENT AND 50% OF PROFESSIONAL MUTUAL HOLDINGS INC. IS LBC GLOBAL. . . . WE [ARE] REQUIRING LBC HOLDINGS USA AND LBC DEVELOPMENT TO ISSUE THE NECESSARY CERTIFICATES IN FAVOR OF LBC GLOBAL CORPORATION.<sup>62</sup>

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<sup>60</sup> PX 7 at 2.

<sup>61</sup> PX 7 at 1 (capitals and ellipses in original).

<sup>62</sup> PX 8 at 1.

These emails are devastating to Araneta's claims that tax problems forced the abandonment of the Delaware Holding Company in early-to-mid 2000 and that as a result of those alleged tax problems, no assets were ever transferred to the Delaware Holding Company. Rather than demonstrate a continuing reluctance or refusal to transfer assets, the emails indicate that by December 11, 2000, any tax problems relating to the transfer of the LBC Operating Companies to the Delaware Holding Company had been resolved such that Araneta was issuing the necessary certificates to effect this transfer.<sup>63</sup>

In addition to his December 2000 emails, Araneta personally confirmed that the Delaware Holding Company owned the LBC Operating Companies on two separate occasions in 2001. On January 22, 2001, Araneta signed a deed of adherence letter (the "Deed of Adherence") in both his personal capacity and as chairman of LBC Development attesting to the transfer of the LBC Operating Companies to the Delaware Holding Company.<sup>64</sup> Six months later, on July 26, 2001, Araneta executed, in his personal capacity and on behalf of the Delaware Holding Company, a confirmation letter (the "Confirmation Letter") clarifying the Deed of Adherence and providing a balance sheet indicating that assets were owned by the Delaware Holding Company as of March 31, 2001.<sup>65</sup>

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<sup>63</sup> See PX 7, 8.

<sup>64</sup> PX 20.

<sup>65</sup> PX 27.

The Deed of Adherence explicitly confirmed the formation and funding of the Delaware Holding Company. It verified that:

[T]he holding company referred to as LBC HoldCo [the Delaware Holding Company] in the Undertaking Agreement has now been duly incorporated under the laws of the State of Delaware, U.S.A. and is named “LBC Global Corporation” which now owns, directly or indirectly, the Professional Holdings Shares, the Professional Holdings Advances, all the shares and interest in LBC and all the shares and interests in the companies and businesses which are owned and controlled by [Araneta], as follows:

- (i) LBC Domestic Franchise Co., Inc. and its subsidiaries;
- (ii) LBC Express, Inc. and its subsidiaries;
- (iii) LBC Mabuhay Development Philippine Corporation and its subsidiaries;
- (iv) LBC Holdings USA Corp. and its subsidiaries;
- (v) LBC International, Inc. and its subsidiaries (including all remittance businesses outside of LBC Holdings USA Corporation);
- (vi) LBC Development Bank;
- (vii) the foreign exchange business arising from the remittance transactions involving any and all of the above companies.<sup>66</sup>

Likewise, the Deed of Adherence included Araneta’s consent to ATR’s transfer of its interest in the Delaware Holding Company to Philtread and ATR’s affiliation with Philtread going forward.

The drafting history of the Deed of Adherence reinforces Araneta’s contemporaneous representations. Araneta originally agreed to provide the Deed of Adherence in the Undertaking Agreement, and confirmed that intention on January 9,

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<sup>66</sup> PX 20 at 1-2.

2001 in an email to ATR.<sup>67</sup> He received an initial draft of the Deed of Adherence on January 10, 2001, and an electronic version the following day.<sup>68</sup> Araneta and his attorneys revised the Deed of Adherence and sent it back to ATR for comments.<sup>69</sup> ATR further revised the document to provide for ownership “directly or indirectly” of the assets by the Delaware Holding Company and to clarify language allowing the transfer of the assets to a Hong Kong entity only “provided, that all the assets . . . shall *remain* owned and held by a single holding company, and that ATR shall in any event own and hold 10% of the capital stock of the same holding company.”<sup>70</sup> Neither Araneta nor his attorneys amended or renounced the claim that the LBC Operating Companies had, in fact, been transferred to the Delaware Holding Company, and Araneta executed the final version of the Deed of Adherence guaranteeing ATR’s right to 10% of those assets.

The Confirmation Letter signed six months later reaffirmed the formation of the Delaware Holding Company and its ownership of the assets in both its text and in the balance sheet it incorporated as an attachment. The Confirmation Letter clearly stated:

As contemplated in the Undertaking Agreement and the [Deed of Adherence], LBC Global Corporation [i.e., the Delaware Holding Company] . . . now owns directly or indirectly, the Professional Holdings Shares, the Professional Holdings Advances, all the shares and interest in LBC Development Corporation and the companies and businesses listed in the Undertaking Agreement which are owned and controlled by Mr. Carlos R. Araneta.<sup>71</sup>

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<sup>67</sup> Tr. at 170-71.

<sup>68</sup> PX 15.

<sup>69</sup> PX 18.

<sup>70</sup> PX 19 at 1-2 (emphasis added).

<sup>71</sup> PX 27 at 1.

Likewise, the balance sheet dated March 31, 2001 that was attached to the Confirmation Letter illustrated the Delaware Holding Company's recognition of both its ownership of the LBC Operating Companies as assets and its pro rata liabilities to the Araneta family and ATR as described in the text of the letter.<sup>72</sup> On the balance sheet, LBC Holdings USA, LBC Development, and Araneta's Professional Holdings shares are all listed under assets as "Investments" having a value of \$36,235,500 at cost.<sup>73</sup> Likewise, the balance sheet shows "Liabilities" of \$39,220,000, represented as \$3,922,000 "due to" ATR as well as a \$35,298,000 "accounts payable" entry for the Araneta family.<sup>74</sup> These "Liabilities" correspond exactly to the relative ownership of the Delaware Holding Company — 10% to ATR and the remaining 90% to Araneta.

In addition to Araneta's representations of the Delaware Holding Company's ownership of the assets, disclosures and financial statements by others affiliated with the Delaware Holding Company confirm that the corporation held controlling interests in the LBC Operating Companies from 2001 through 2003. Berenguer created a balance sheet identical to the one discussed above on July 19, 2001 in preparation for its inclusion in

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<sup>72</sup> The Confirmation Letter explained the unique accounting methods used for the contribution of the assets. ATR and Araneta's contributions, although infusions of cash generating equity ownership interests, were recognized as liabilities due to the shareholders under a Philippine accounting practice. The Confirmation Letter clarified that the liabilities reflected on the balance sheet as a result of this transaction were payable pro rata based on percentage share ownership, much like dividends would be paid on equity. Specifically, the Confirmation Letter explained that "[a]ny conversion of all or any portion of the liabilities into equity shall be effected by LBC Global pro rata in proportion to the outstanding amount owed to each of the holders thereof," and "[a]ny full or partial payment or prepayment by LBC Global of the liabilities shall be made to all holders thereof pro rata in proportion to the amount owed to them respectively." PX 27 at 1-2.

<sup>73</sup> *Id.* at Annex "A."

<sup>74</sup> *Id.*

the Confirmation Letter.<sup>75</sup> Victor Marquez, the Delaware Holding Company's accountant, distributed another copy of that very same balance sheet in the corporation's financial statements dated March 2001 and March 2002<sup>76</sup> and proffered it under the pains and penalties of perjury to the State of Delaware and the federal government as part of the corporation's tax returns filed for 2001 and 2002.<sup>77</sup> In fact, no financial statement prepared between the balance sheet incorporated in the July 2001 Confirmation Letter — which Berenguer testified to have double checked before submitting<sup>78</sup> — and the balance sheet dated May 31, 2003 prepared by Araneta and submitted in connection with his Compliance in the § 220 action that preceded this dispute ever showed any combination of assets, liabilities, and equity inconsistent with the Delaware Holding Company's ownership of the LBC Operating Companies.

On the basis of this contemporaneous record and as a predicate to my ultimate decision in this case, I conclude that the Delaware Holding Company owned the LBC Operating Companies. Correspondingly, I find that Araneta's testimony to the contrary was self-serving and untruthful.

### 3. Araneta's Offset Defense

Araneta's final defense is a semantic attempt to disguise the unfairness of his removal of the LBC Operating Companies. To explain the differences in the March 2003

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<sup>75</sup> PX 23. Berenguer also testified to the Delaware Holding Company's ownership of the LBC Operating Companies on at least seven different occasions during her testimony. *See* Berenguer at 88-89, 155, 174, 177, 186, 201, 281.

<sup>76</sup> *See* PX 25; PX 47.

<sup>77</sup> *See* PX 41; PX 50.

<sup>78</sup> Berenguer testified that she was "double careful" in reviewing the figures on the balance sheet, and that she "cross-checked them against the letter" before she or Araneta signed off on them. Berenguer at 153-55.

and December 2003 balance sheets, Araneta testified that he had “offset” the roughly \$36 million in assets he had removed from the Delaware Holding Company, i.e., the LBC Operating Companies, against the liability the Delaware Holding Company showed as “payable” to his family in the same amount.<sup>79</sup> He maintains that the Delaware Holding Company is better off as a result of this transaction because of this decrease in its liabilities.<sup>80</sup> But, Araneta still claims control over 90% of the equity in the Delaware Holding Company and never indicated that the assets had been transferred to any other holding company in which ATR would have a minority interest.<sup>81</sup>

This “offset” defense does not withstand even minimal scrutiny. Despite the nomenclature on the financial statements, which characterize the contributions of the Advances and the LBC Operating Companies as “liabilities” rather than “equity,” there is no dispute that the LBC Operating Companies were contributed in exchange for Araneta’s 90% equity interest. Moreover, the Deed of Adherence and Confirmation Letter explain that any distributions out of the Delaware Holding Company would be paid pro rata on the majority and minority equity investments. No pro rata payment was made to ATR, and Araneta did not forfeit his equity position in the Delaware Holding Company when he cashed out the assets that he initially contributed. Thus, this scenario is even further removed than a non-pro rata exchange accompanying the retirement of the

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<sup>79</sup> When asked whether he had “offset the LBC assets — LBC Holdings and LBC Development — which added up to roughly 36 million . . . against the Araneta advance liability that equaled the same 36 million,” Araneta answered, “Yes. I think so, yes.” Tr. at 253-54. Moreover, Araneta agreed that he “didn’t consult with anyone when [he] did that.” *Id.* at 254.

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

majority equity stake, which would liquidate one investor's stake and leave the remaining investor in complete control of the remaining assets. Here, the majority investor claims not to have given up his equity position even though it withdrew the entirety of its investment.

It is illogical that ATR would be in a better position owning 10% of what had essentially become a shell corporation than it had been in while indirectly owning a share of the LBC Operating Companies. After the removal of the LBC Operating Companies, ATR's interest in the Delaware Holding Company was essentially a 10% stake in Araneta's minority position in the Pre-Need Company.<sup>82</sup> If such a result were permitted to stand, it would unjustly enrich Araneta because after removing the same assets that he initially contributed he would have gained an indirect interest in the Pre-Need Company for nothing. That result is untenable, especially because ATR paid the costs of acquiring the Pre-Need Company out of its coffers in 1999. Thus, no legitimate offset could have taken place.

Factually, then, Araneta's "offset" argument is without basis. Unlike some scenarios in which there may be a dispute as to the values given or received, this is a straightforward self-dealing case in which Araneta took something for nothing. His secretive conduct reinforces this point.<sup>83</sup> Thus, I find the factual predicate for Araneta's "offset" argument has not been satisfied.

#### E. The Philippine Litigation Front

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<sup>82</sup> Tr. at 256-58.

<sup>83</sup> Araneta admitted that he alone decided to carry out this transaction without consulting with anyone, without notifying the other directors, and without informing ATR. Tr. at 254, 260.



After ATR filed its § 220 action in Delaware and was met with Araneta's first instance of litigation abuse, it was sued by Araneta in the Philippines. In that action, Araneta sought, among other relief, the annulment of the Undertaking Agreement and Joint Venture Agreements on the grounds that ATR fraudulently concealed the implications, risks and consequences involved in the acquisition of the Pre-Need Company.<sup>84</sup> In response, ATR sought a declaration of validity and judicial approval of the Colayco Sale.

In the end, Araneta lost his case in the Philippines decisively. The Regional Trial Court refused to annul any of the contracts between the parties.<sup>85</sup> In upholding the validity of the Joint Venture Agreement and the Undertaking Agreement, the Regional Trial Court found that "there was no incident present in the case that would destroy the freedom of Araneta to enter in the agreements" and described Araneta's grounds for annulment to be "sham and contrived."<sup>86</sup> It dismissed Araneta's complaint and entered judgment for ATR on January 24, 2006.

Following that decision, Araneta moved for reconsideration and ATR moved to enforce its rights under § 5 of the Undertaking Agreement, which granted ATR a put option whereby ATR could require Araneta to purchase its interest in the Delaware Holding Company. After reviewing the claims, on May 8, 2006, the Regional Trial Court

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<sup>84</sup> Def. Post-Trial Br. Ex. 1 at 1. Jurisdiction for this contractual dispute was established in the Philippines based on forum selection clauses in both the Joint Venture Agreement and Undertaking Agreement providing: "Each of the parties irrevocably consents to the exclusive jurisdiction of the courts of the National Capital Judicial Region with respect to any action or proceeding relating to this Agreement." PX 1 at 5; DX 1 at 8.

<sup>85</sup> Def. Post-Trial Br. Ex. 1 at 4.

<sup>86</sup> *Id.* at 3-4.

reaffirmed the validity of the Undertaking Agreement and amended its previous decision to include the implementation of the provisions of § 5 of the Undertaking Agreement.<sup>87</sup>

As such, the court found Araneta “liable for the aggregate subscription or issue price of the [Delaware Holding Company] shares and the premium of 25% per annum.”<sup>88</sup>

Araneta, of course, appealed that judgment. The parties indicate that the appellate process in the Philippines could take many years to complete.

### III. Legal Analysis

With this backdrop in mind, I begin my analysis with Araneta’s suggestion that this court is not the proper forum for ATR’s claims. I next turn to Araneta’s disloyal conduct and false disclosures while serving as the dominant director and controlling stockholder of the Delaware Holding Company. Then, I focus on the other directors — Bonilla and Berenguer — and take up the questions regarding their responsibility to monitor Araneta’s conduct. Finally, I address the appropriate relief to be awarded, including whether to grant ATR’s request for an award of imposition of attorneys’ fees and costs.

#### A. Delaware Is The Proper Forum For ATR’s Claims

Araneta contends that the entirety of his dispute with ATR should have been resolved in the Philippines under the terms of the forum selection clauses of the Joint Venture Agreement and the Undertaking Agreement. But, in this court, ATR has premised its claims entirely on the fiduciary duties Araneta, Berenguer, and Bonilla owed

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<sup>87</sup> Def. Post-Trial Br. Ex. 2 at 2.

<sup>88</sup> *Id.* at 3.

to it as directors of a Delaware corporation, not on any other contractual duties that may exist between the parties. As such, this court may properly decide ATR's Delaware law claims.

Under the teaching of *Parfi Holding AB v. Mirror Image Internet, Inc.*,<sup>89</sup> ATR was not required to press its Delaware law claims in the Philippines, as they do not “depend on the existence” of the Undertaking Agreement or Joint Venture Agreement for their viability.<sup>90</sup> When sued by Araneta in the Philippines, ATR had no practical choice but to invoke its contractual remedies as defenses. By doing so, ATR did not waive claims it had against Araneta that are grounded in other legal and equitable duties Araneta owed to it that were not contractual in nature.

Here, ATR simply seeks to finish the process it began in July 2003, before Araneta filed his action in the Philippines, when it first began to pursue Araneta for breaching his duties as the director of a Delaware corporation. The existence of the Philippine litigation provides Araneta no defense. If he wished to escape this court's jurisdiction in responding to claims against him as a Delaware director, he needed to secure an explicit right to that effect. He did not do so and this court is available to ATR for it to seek redress as a stockholder of a Delaware corporation. Because ATR's claims alleging breaches of fiduciary duty by Araneta — as well as his co-directors Bonilla and

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<sup>89</sup> 817 A.2d 149 (Del. 2002).

<sup>90</sup> *See id.* at 155-57 (explaining that “fiduciary duties . . . consist of a set of rights and obligations that are independent of any contract” and can only be limited in their assertion by contractual provisions when “the claims based on fiduciary duties touch on the obligations created in the [contract]”).

Berenguer — arise independently of the parties' contracts, ATR does not seek an impermissible double recovery.

B. Araneta Breached His Duty Of Loyalty By Stripping The Delaware Holding Company Of Its Major Assets For No Consideration

ATR's allegations against Araneta are clear-cut claims of self-dealing by a controlling shareholder and director of a Delaware corporation. Araneta does not contest that he was the controlling shareholder of the Delaware Holding Company, and I have already found that his factual argument that he was not a director at all relevant times is without merit. Similarly, I have found as a fact that Araneta removed from the Delaware Holding Company its primary assets — its ownership of the LBC Operating Companies. In its financial statements and tax filings, the Delaware Holding Company had valued this ownership interest at over \$36 million.<sup>91</sup> Yet, by the end of 2003, this value had disappeared from the Delaware Holding Company's books. To where did Araneta remove the assets? To his family. What did the Delaware Holding Company receive in exchange? Effectively nothing. Araneta did not even reduce his 90% interest in the Delaware Holding Company when he repossessed the very assets that had secured that interest in the first place. Araneta simply took the LBC Operating Companies back in a fit of pique.

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<sup>91</sup> See Tr. at 254.

The standard of review to evaluate this self-dealing is, of course, the entire fairness standard.<sup>92</sup> As a director, Araneta had a duty of loyalty to the Delaware Holding Company to act in the best interests of the corporation and its shareholders and in a manner such that there would be “no conflict between [his] duty and [his] self-interest.”<sup>93</sup> Thus, as the director who conceived of and carried out the transfer of the LBC Operating Companies from the Delaware Holding Company to members of his family for no value, Araneta bore the burden of establishing the fairness of this transaction.<sup>94</sup>

Likewise, as the majority stockholder of the Delaware Holding Company, Araneta owed fiduciary duties to the minority shareholders of the corporation when dealing with the corporation’s property.<sup>95</sup> In this role, Araneta was prohibited from using his position of control to extract value from the corporation to the exclusion of, and detriment to, the minority stockholders.<sup>96</sup> Consequently, in this capacity as well, the law imposed upon Araneta the obligation to prove that the transfer he structured using his total dominion over the Delaware Holding Company’s affairs was fair to the minority rather than an extraction of value to their detriment.<sup>97</sup> Araneta did not do that.<sup>98</sup>

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<sup>92</sup> *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983) (“When directors of a Delaware corporation are on both sides of a transaction, they are required to demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain.”).

<sup>93</sup> *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939).

<sup>94</sup> *See Chaffin v. GNI Group, Inc.*, 1999 WL 721569, at \*5 (Del. Ch. 1999) (finding that a father “must be deemed ‘interested’ in a transaction from which his child stood to benefit substantially in career and economic terms” and that “the entire fairness standard would apply”).

<sup>95</sup> *Sterling v. Mayflower Hotel Corp.*, 93 A.2d 107, 109-10 (Del. 1952).

<sup>96</sup> *See Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971).

<sup>97</sup> *See id.* at 721 (explaining that where a parent corporation “would be receiving something from [its] subsidiary to the exclusion of and detrimental to [the subsidiary’s] minority stockholders” the combination of that “self-dealing, coupled with the parent’s fiduciary duty, would make intrinsic fairness the proper standard”).

In this case, Araneta has not disputed these principles or even advanced an argument under the entire fairness rubric. Indeed, quite obviously, what Araneta did was not fair to the Delaware Holding Company or its minority stockholder, ATR. Araneta's only major defense is his factual claim that the assets were never transferred into the Delaware Holding Company. On this basis, Araneta asserts, without citation to any legal authority, that entire fairness review cannot attach to his transfer of the LBC Operating Companies. That is, Araneta rests his entire case on a factual claim which I reject.<sup>99</sup>

That factual claim is ridiculous. Araneta asserts that for tax reasons he never did what he and his allies said he had done in numerous documents — including the corporation's tax filings! — that is, transfer control of the LBC Operating Companies to

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<sup>98</sup> This fraudulent transfer also involved a sale of substantially all of the Delaware Holding Company's assets and had to be performed consistently with 8 *Del. C.* § 271, which sets forth the procedures required to complete such a transaction. ATR has asserted, without contradiction from Araneta, that these procedures were not followed, and specifically that no shareholder vote took place. For his part, Araneta testified that he did not even inform ATR or his fellow directors about his removal of the LBC Operating Companies. Tr. at 254-55.

<sup>99</sup> Because I reject the factual underpinning of Araneta's argument, I need not decide the legal issue he presents. But, I doubt that Delaware law would permit a fiduciary who contracted to convey assets to a corporation when soliciting a minority shareholder's investment and who later confirmed the corporation's ownership of those assets while serving as a director of that corporation to escape liability for redirecting those assets away from the corporation merely because the fiduciary "cut out the middleman" and never honored his obligation to place the assets into the corporation's accounts in the first place. Fiduciary duties do not attach only when assets are transferred but rather arise "where one person reposes special confidence in another, or where a special duty exists on the part of one person to protect the interests of another, or where there is a reposing of faith, confidence, and trust, and the placing of reliance by one person on the judgment and advice of another." *Lank v. Steiner*, 213 A.2d 848, 852 (Del. Ch. 1965), *aff'd*, 224 A.2d 242 (Del. 1966). From the moment Araneta became a director of, and ATR became a stockholder of, the Delaware Holding Company, Araneta had an obligation to enforce the Delaware Holding Company's right to ownership of the LBC Operating Companies for the benefit of the corporation and its shareholders that paralleled but existed independently from his contractual duty to cause the same transfer to occur. See *Legatski v. Bethany Forest Assoc., Inc.*, 2006 WL 1229689, at \*6 (Del. Super. Ct. 2006) (recognizing that contractual and fiduciary duties are not mutually exclusive).

the Delaware Holding Company. Araneta says he was pondering using a Hong Kong company instead. But a written agreement with ATR indicates that if Araneta wished to transfer the LBC Operating Companies to a Hong Kong entity, it could only do so on specific contractual terms. No evidence of such a transfer exists. Most important of all, it is preposterous to believe that ATR was willing to allow Araneta to keep the LBC Operating Companies for himself, rather than transferring them into some other corporation, whether located in the Philippines, Hong Kong, or elsewhere, in which ATR would have a 10% interest.

Recognizing that this claim might well be found ludicrous, Araneta and his counsel propounded an equally unpersuasive defense. They try to claim that the LBC Operating Companies were transferred to Araneta's family to extinguish a \$36 million debt owed to the Aranetas by the Delaware Holding Company. On cross-examination, Araneta opined that the Delaware Holding Company was better off following the transaction because he "offset" these assets against a "liability" that the corporation owed to his family.<sup>100</sup>

Nothing in the record supports this position. The liability that Araneta purported to offset arose as a result of his contribution of the LBC Operating Companies and was valued based on Araneta's 90% ownership stake. But, following his so-called offset, Araneta testified that he maintained his 90% ownership.<sup>101</sup> Thus, ATR was left with a 10% stake in what is now effectively a shell corporation devoid of its primary operating

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<sup>100</sup> Tr. at 256-57.

<sup>101</sup> Tr. at 258.

assets, while Araneta and his family gained a windfall by retaining a 90% interest in the Delaware Holding Company's remaining assets — primarily the minority interest in the Pre-Need Company — without giving any substantial value in exchange. Suffice it to say that Araneta could not point to any fairness-enforcing procedures that he used to come up with this blatantly unfair transaction. Rather plainly, any director, officer, or advisor acting in good faith would have protested that the transaction was fraudulent.

The evidence in this case is clear, and Araneta's attempts to distort that reality only make his conduct less tolerable. Araneta used his majority control and effective dominion over the Delaware Holding Company and its board of directors to engage in a course of unfair dealing that resulted in a de facto liquidation of corporate assets that enriched the Araneta family at the expense of the Delaware Holding Company and ATR.

C. If The Delaware Holding Company Never Owned The LBC Operating Companies, Araneta Breached His Duty Of Loyalty By Knowingly Disclosing False Information

In order to dispute his self-interested transfer of the LBC Operating Companies, Araneta testified that the Deed of Adherence and Confirmation Letter he signed and sent to ATR while he was a director of the Delaware Holding Company were false. These documents confirmed, both in express representations of fact and through financial statements showing the corporation's assets, that the Delaware Holding Company owned the LBC Operating Companies. But, Araneta testified at trial that he and ATR knew the ownership representations to be false at the time he signed the documents containing them. As I have explained, I find this "believe-me-now-I-was-lying-then" defense to be



without merit. Yet, even if I were to accept the factual predicate to Araneta's argument, it would not aid Araneta in escaping liability.

As a corporate fiduciary, Araneta was required to be candid in all of his communications concerning the Delaware Holding Company's financial condition. As our Supreme Court explained in *Malone v. Brincat*, the fiduciary duty of loyalty prohibits a director from lying to the stockholders.<sup>102</sup> Thus, "[i]t necessarily follows from *Malone* that when directors communicate with stockholders, they must recognize their duty of loyalty to do so with honesty and fairness."<sup>103</sup> As such, a stockholder may carry its burden by establishing that a director breached his or her "fiduciary duty of loyalty . . . by knowingly disseminating to the stockholders false information about the financial condition of the company."<sup>104</sup>

ATR has met its burden here. If Araneta's testimony in court is to be believed, he himself admits that his statements in the Deed of Adherence and in the Confirmation Letter were lies. Araneta testified: "The truth is, I signed these documents. And when I signed these documents they were not true. I signed these documents, but the assets were not transferred to Delaware."<sup>105</sup> Moreover, Araneta confirmed that he understood that he was signing the Confirmation Letter "at the request of ATR for [the] Filipino Stock Exchange" and that he knew public shareholders would be seeing this information in

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<sup>102</sup> 722 A.2d 5, 12 (Del. 1998).

<sup>103</sup> *Jackson Nat'l Life Ins. Co. v. Kennedy*, 741 A.2d 377, 390 (Del. Ch. 1999).

<sup>104</sup> *Malone*, 722 A.2d at 10.

<sup>105</sup> Tr. at 206-07.

some form.<sup>106</sup> Thus, in Araneta's own words, neither the representations in the Deed of Adherence, the Confirmation Letter, nor the financial statements attached thereto provided an accurate picture of the Delaware Holding Company, and he knew it.

Araneta's defense to these admissions — that ATR should have known the falsity of the statements — is without merit. According to Araneta's tale, told for the first time at trial, Arnaiz pressured him to sign these documents and he gave in to that pressure to support his friend and to curry favor with the Philippine government because the brother of the Philippine President was involved with ATR.<sup>107</sup> Although in Araneta's story ATR requested the letters, that fact does not establish that ATR knew the information therein to be untrue. Only Araneta's claim that he told Arnaiz that those statements were false purports to do that.<sup>108</sup> Based on the ever-shifting positions taken by Araneta throughout this litigation, the conflict between his testimony on the witness stand and the contemporaneous emails he sent in December 2000, and the lack of any records indicating ATR's knowledge that the assets were not owned by the Delaware Holding Company after Araneta stated that the tax issues had been resolved, I do not credit Araneta's testimony.

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<sup>106</sup> Tr. at 200.

<sup>107</sup> Tr. at 42-47.

<sup>108</sup> Araneta also argues that various communications sent to ATR regarding the purported tax and other hurdles to making the Delaware Holding Company operational between November 1999 and April 2000 provided notice to ATR that the assets had not been transferred to the Delaware Holding Company. *See* DX 5-21. But, the timing of these communications undercuts their value. Following these communications, Araneta sent an e-mail in December 2000 expressly stating that "WE HAVE ALSO RESOLVED WITH OUR TAX CONSULTANTS THE MANNER OF THE TRANSFER OF SOME ASSETS TO THE HOLDING CO." PX 7 at 1 (capitals in original). The only communication on this topic that Araneta sent after this date, an e-mail dated January 3, 2001, does not list anyone at ATR as a recipient. DX 22.

Consequently, I find that even if Araneta did not transfer the LBC Operating Companies to the Delaware Holding Company, he still violated his fiduciary duties to ATR on an alternate basis. Specifically, I hold that if the LBC Operating Companies were never owned by the Delaware Holding Company, Araneta breached his duty of loyalty to ATR by knowingly disclosing false information concerning the Delaware Holding Company, including false financial statements indicating its ownership of the LBC Operating Companies.<sup>109</sup>

ATR has also brought a fraud claim against Araneta. Given that this claim is identical to ATR's *Malone* claim but would arguably involve more stringent standards,<sup>110</sup> and because I have already found that the transfer occurred and was substantially unfair, I need not reach it. Insofar as reasonable reliance is required, ATR has shown that after being informed that the Delaware Holding Company owned the LBC Operating Companies, it acted on that information.

In a transaction that closed in November 2001, ATR sold its 10% interest in the Delaware Holding Company to Philtread, reinvesting the entire proceeds of the sale as well as roughly \$1.2 million in additional capital back into Philtread to create an Internet

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<sup>109</sup> Moreover, as a director of the Delaware Holding Company, Araneta had a duty to seek recourse against himself — odd, but true — if he failed to deliver the stock of the LBC Operating Companies to the Delaware Holding Company. Of course, I find that his breach occurred later, when he stripped the Delaware Holding Company of those Companies' stock. But either way, Araneta breached his fiduciary duties.

<sup>110</sup> Delaware's standards of fiduciary disclosure are specialized applications of fraud standards. As a result, a plaintiff is rarely better off pressing garden-variety common law fraud claims when a more tailored fiduciary disclosure claim can be pursued. See *Metro Communication Corp. BVI v. Advanced Mobilecomm Technologies Inc.*, 854 A.2d 121, 156 (Del.Ch. 2004) (“[T]he standards that a fiduciary faces are tougher than the common law and equitable fraud standards, which always require proof of reasonable reliance.”).

service and fulfillment business. ATR intended to use the LBC Operating Companies as part of the fulfillment side of its business model for Philtread. More importantly, because Philtread was publicly listed on the Philippine Stock Exchange, ATR made representations to the Philippine equivalent of the U.S. Securities and Exchange Commission and to outside investors that the Delaware Holding Company was “the ultimate holding company for all the LBC operations,” including the LBC Operating Companies, among others, based on Araneta’s express confirmation of those facts in the Deed of Adherence and Confirmation Letter he signed while a director of the Delaware Holding Company.<sup>111</sup> As such, to the extent that ATR cannot hold Araneta accountable by receiving a remedy for his actions in never giving up ownership of the LBC Operating Companies, ATR has exposed itself to liability by endorsing and disseminating Araneta’s false statements.

Of course, I ultimately conclude that Araneta did originally hand over the LBC Operating Companies to the Delaware Holding Company and that the Delaware Holding Company did own those assets for over two years — from at least January 22, 2001, when Araneta attested to that fact in the Deed of Adherence, to May 31, 2003, the date of the last balance sheet showing ownership of those assets — before Araneta stripped them away for no value. But, either way, Araneta has caused harm to ATR.

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<sup>111</sup> PX 32 at 33 (describing the Delaware Holding Company in Philtread’s public disclosures); *see also* PX 20 (Deed of Adherence); PX 27 (Confirmation Letter) (containing Araneta’s express representations).

D. Bonilla And Berenguer Acted As Stooges For Araneta And Failed To Take Any Steps To Perform Their Duties As Fiduciaries

I now come to a slightly more difficult issue. Namely, to what extent should Araneta's fellow directors, Bonilla and Berenguer, share responsibility for harming the Delaware Holding Company and ATR?

Making this more challenging is that ATR does not allege that either Berenguer or Bonilla participated in, approved of, or directly profited from Araneta's removal of the LBC Operating Companies. Rather, ATR claims that Bonilla and Berenguer consciously breached the important duties articulated in this court's *Caremark*<sup>112</sup> decision and recently reaffirmed by our Supreme Court in *Stone v. Ritter*.<sup>113</sup> Specifically, ATR alleges that Bonilla and Berenguer failed to monitor Araneta's conduct thereby allowing his self-dealing to continue.

Under Delaware law, it is fundamental that a director cannot act loyally towards the corporation unless she tries — i.e., makes a genuine, good faith effort — to do her job as a director.<sup>114</sup> One cannot accept the important role of director in a Delaware corporation and thereafter consciously avoid any attempt to carry out one's duties.

One of the most important duties of a corporate director is to monitor the potential that others within the organization will violate their duties. Thus, "a director's obligation includes a duty to attempt in good faith to assure that a corporate information and

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<sup>112</sup> *In re Caremark Int'l, Inc. Deriv. Litig.*, 698 A.2d 959 (Del. Ch. 1996).

<sup>113</sup> --- A.2d ---, 2006 WL 3169168 (Del. 2006).

<sup>114</sup> *See Guttman v. Huang*, 823 A.2d 492, 506 & n.34 (Del. Ch. 2003).

reporting system, which the board considers to be adequate, exists.”<sup>115</sup> Obviously, such a reporting system will not remove the possibility of illegal or improper acts, but it is the directors’ charge to “exercise a good faith judgment that the corporation’s information and reporting system is in concept and design adequate to assure the board that appropriate information will come to its attention in a timely manner as a matter of ordinary questions, so that it may satisfy its responsibility.”<sup>116</sup> Thus, as the Supreme Court recently stated:

*Caremark* articulates the necessary conditions predicate for director oversight liability: (a) the directors utterly failed to implement any reporting or information system or controls; or (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention. In either case, imposition of liability requires a showing that the directors knew that they were not discharging their fiduciary obligations. Where directors fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith.<sup>117</sup>

From the testimony of the directors of the Delaware Holding Company, it is apparent that no reporting system was in place and that no other information systems or controls were ever considered, let alone implemented, by the Delaware Holding Company’s board of directors. They did not even have regular board meetings. As a result, the directors were often unaware of corporate activities — despite how easy that would have been given the Delaware Holding Company’s modest size. Berenguer

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<sup>115</sup> *Caremark*, 698 A.2d at 970.

<sup>116</sup> *Id.*

<sup>117</sup> *Stone*, --- A.2d ---, 2006 WL 3169168, at \*17.

testified that although there had been meetings regarding the Delaware Holding Company before the LBC Operating Companies were transferred into the corporation in January 2001, she did not remember any meetings of the board of directors or of the shareholders after that time.<sup>118</sup> Bonilla confirmed this fact, explaining that when the Delaware Holding Company's name was changed from LBC Global, Corp. to PMHI Holdings, Corp., he was never informed about the change, never voted to approve it, and did not even know what the initials PMHI in the new corporate name stood for at the time he signed the certificate of amendment as the corporation's authorized agent.<sup>119</sup> Even when corporate activities involved them directly — as in the case of their supposed resignations from the board of directors — neither Berenguer nor Bonilla questioned the wisdom of Araneta's actions nor insisted that corporate procedures be followed.<sup>120</sup>

Moreover, both Berenguer and Bonilla testified that they entirely deferred to Araneta in matters relating to the Delaware Holding Company. Berenguer is, as mentioned, Araneta's niece and served as the CFO for the LBC group of companies worldwide.<sup>121</sup> She testified that she would not insert herself into a disagreement between ATR and Araneta about how the Delaware Holding Company should proceed on an issue because such a disagreement would be between those parties and would not affect her as

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<sup>118</sup> Berenguer at 201.

<sup>119</sup> Bonilla I at 175-76; *see also* PX 54 at 6-7.

<sup>120</sup> Notwithstanding the issues regarding the date of their resignation as directors, the process by which Berenguer and Bonilla were removed by Araneta is telling. Bonilla testified that he received a phone call from Araneta informing them that he was no longer a director of the Delaware Holding Company. Bonilla I at 47. Berenguer explained that she did not give formal written notice of her resignation; instead, Araneta just "took it [she] wanted to resign" from the Delaware Holding Company based on her general "verbal intention" to "resign in all LBC" and eventually "replaced" her. Berenguer at 83-84, 195.

<sup>121</sup> Berenguer at 47-48.

a director of the Delaware Holding Company.<sup>122</sup> Similarly, she stated that she would take Araneta's word as authoritative if he claimed that he had agreed with ATR to take certain actions.<sup>123</sup> Bonilla, the head of Araneta's U.S. operations, was more explicit — explaining that to him Araneta and the Delaware Holding Company were basically one and the same and that he took the word of Araneta as being the word of the company.<sup>124</sup> Moreover, when pressed regarding whether he would undertake an independent inquiry if told to act by Araneta, Bonilla responded, "Why should I ask him all these questions? He's telling me they have already agreed . . . . It's not like I'm going to go out there and check on him, doesn't make sense."<sup>125</sup>

Based on these failures, neither Berenguer nor Bonilla can be said to have upheld their fiduciary obligations. Although it was Araneta who ran amok by emptying the Delaware Holding Company of its major assets, the other directors did nothing to make themselves aware of this blatant misconduct or to stop it.

Put in plain terms, it is no safe harbor to claim that one was a paid stooge for a controlling stockholder. Berenguer and Bonilla voluntarily assumed the fiduciary roles of directors of the Delaware Holding Company. For them to say that they never bothered to check whether the Delaware Holding Company retained its primary assets and never took any steps to recover the LBC Operating Companies once they realized that those assets were gone is not a defense. To the contrary, it is a confession that they consciously

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<sup>122</sup> Berenguer at 68.

<sup>123</sup> Berenguer at 197.

<sup>124</sup> Bonilla I at 63.

<sup>125</sup> Bonilla I at 180-81.



abandoned any attempt to perform their duties independently and impartially, as they were required to do by law. Their behavior was not the product of a lapse in attention or judgment; it was the product of a willingness to serve the needs of their employer, Araneta, even when that meant intentionally abandoning the important obligations they had taken on to the Delaware Holding Company and its minority stockholder, ATR.

When required by their office to be loyal to the Delaware Holding Company, Bonilla and Berenguer chose total fealty to Araneta's conflicting interests instead. Consequently, I find them jointly liable for Araneta's fiduciary violations.

#### E. The Core Remedy

The major breach of fiduciary duty in this case is one that injured the Delaware Holding Company in the first instance and ATR secondarily as a minority stockholder. The obvious remedy for this wrongdoing would be to require Araneta to return control of the LBC Operating Companies to the Delaware Holding Company.

ATR is practical, however. It recognizes that it would likely take years and years to chase Araneta and his family around the nation (Araneta has a house in California) and across the globe to get that type of order implemented. Thus, ATR is willing to forsake a full remedy (in the sense that it appears the LBC Operating Companies have done very well) and to accept a direct award of damages.

A direct award to ATR is justified here. Araneta's behavior worked a de facto liquidation of the Delaware Holding Company. It would be unreal to require a monetary award to the Delaware Holding Company by Araneta and his blindly subservient subordinates, Bonilla and Berenguer. Even if such a payment were made, it would be

foolhardy to believe that Araneta and his servants could be trusted to allow ATR to benefit from the grant of that relief to the Delaware Holding Company.

Rather, because Araneta's conduct had the effect of liquidating the Delaware Holding Company, it is appropriate to premise relief on the need to make ATR whole for the injury it suffered by entrusting its capital to the Delaware Holding Company, only to see that corporation impoverished by the defendants. The best way to shape that award is to require Araneta and the defendants to pay back to ATR the cost of acquiring its equity in the Delaware Holding Company — \$3.922 million — plus pre-judgment interest at a rate that fairly compensates ATR for its loss of the upside inherent in the LBC Operating Companies' profit and growth. In determining that rate, I am aided by the parties' dealings and Araneta's admittedly high cost of debt and equity capital. Araneta's cost of debt was as high as 18%.<sup>126</sup> This high (equity-level) rate supports the fairness of a very high rate of interest, as it suggests an even higher cost of equity. That conclusion is confirmed by § 5 of the Undertaking Agreement. In that section, ATR secured a put option at a premium of 25% per annum over the issue price of ATR's shares in the Delaware Holding Company if exercised after the first two years of the investment. Using this contractual estimate of Araneta's cost of equity is the best way to do justice, even though it likely still leaves Araneta with a windfall.<sup>127</sup> I will compound this interest

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<sup>126</sup> See *Bonilla II* at 44-45 (confirming that LBC's cost of private debt is 15%-18%).

<sup>127</sup> See *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 817 A.2d 160, 175 (Del. 2002) (permitting the Court of Chancery to fashion "broad, discretionary, and equitable remedies" in cases involving a breach of the duty of loyalty); *Int'l Telecharge, Inc. v. Bomarko, Inc.*, 766 A.2d 437, 440 (Del. 2000) ("[T]he powers of the Court of Chancery are very broad in fashioning equitable and monetary relief under the entire fairness standard as may be appropriate.");

rate monthly in accordance with my understanding of prevailing commercial practices and in order to better ensure that ATR is made whole.<sup>128</sup>

It is worth noting that ATR requested monthly compounding in their opening brief. The defendants did not respond to this request except insofar as they argued that no damage award of any amount should be entered. Suffice it to say, the defendants are therefore in no position to quibble about the interest rate I now award, having forsaken their chance to respond.

All of the defendants will be jointly and severally liable for the amount of the judgment. Nonetheless, I find that in any action as between Araneta, on the one hand, and Bonilla and Berenguer, on the other, Araneta should be deemed responsible to pay the entire judgment. In other words, to the extent it is later important, if Bonilla and

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*Weinberger v. UOP, Inc.*, 457 A.2d 701, 715 (Del. 1983) (holding that when the entire fairness standard is not met, the Court of Chancery's "powers are complete to fashion any form of equitable and monetary relief as may be appropriate"). In fashioning a remedy, I err on the side of generosity to the plaintiffs because "Delaware law dictates that the scope of recovery for a breach of the duty of loyalty is not to be determined narrowly" and because "strict imposition of penalties under Delaware law are designed to discourage disloyalty." *Bomarko*, 766 A.2d at 441 (quoting *Thorpe by Castleman v. CERBCO, Inc.*, 676 A.2d 436, 445 (Del. 1996)); *see also Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 855 A.2d 1059, n.20 (Del. Ch. 2003).<sup>128</sup> *See Brandin v. Gottlieb*, 2000 WL 1005954, at \*29 (Del. Ch. 2000) (explaining that this court has "broad discretion, subject to principles of fairness, in fixing the rate [of interest] to be applied"); *Gotham Partners*, 817 A.2d at 173 (finding that the Court of Chancery's "uncontested 'discretion to select a rate of interest higher than the statutory rate . . . include[s] the lesser authority to award compounding.'"); *see also Henke v. Trilithic, Inc.*, 2005 WL 2899677, at \*13 (Del. Ch. 2005) (explaining that awarding interest compounded on a monthly basis because doing so better "comports with the fundamental economic reality" that investors and "companies neither borrow nor lend at simple interest rates"); *Smith v. Nu-West Indus.*, 2001 WL 50206, at \*1 (Del. Ch. 2001) (awarding interest compounded monthly), *aff'd*, 781 A.2d 695 (Del. 2001).

Berenguer pay any or all of the judgment, Araneta should be required to make them whole, to the extent that is consistent with applicable law.<sup>129</sup>

#### F. Attorneys' Fees

Finally, I consider ATR's request for an award of attorneys' fees. Delaware follows the American Rule under which parties to litigation normally bear their own costs regardless of the outcome of their case.<sup>130</sup> Yet, the American Rule, and correspondingly Delaware's application thereof, provide for fee awards in exceptional circumstances in order to deter abusive litigation, avoid harassment, and protect the integrity of the judicial process.<sup>131</sup> These circumstances include fraud, bad faith, or other outrageous conduct from which the claim arose and bad faith behavior in the course of subsequent litigation.<sup>132</sup> Here, ATR claims that the egregious nature of Araneta's fiduciary breaches coupled with the implausibility of his defenses and his bad faith in defending this litigation necessitate a fee-shifting award. I agree.

The U.S. Supreme Court has explained that "bad faith may be found, not only in the actions that led to the lawsuit, but also in the conduct of the litigation."<sup>133</sup> Delaware courts have awarded attorneys' fees when defendants "had no valid defense and knew it," when "they unnecessarily required the institution of litigation, delayed the litigation, asserted frivolous motions, falsified evidence and changed their testimony to suit their needs," and when, in short, they "constructed their entire defense in bad faith."<sup>134</sup>

Although any one of these findings alone would be sufficient to justify a shifting of fees;

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<sup>129</sup> In qualifying this statement, I simply recognize that when persons act as mere tools for malefactors and contribute to harm to others, public policy might limit their ability to seek indemnification from their "boss," so to speak. That might be an occupational hazard.

in this case, there is ample evidence to establish transgressions in each of these categories by Araneta.

Here, Araneta's bad faith was pervasive. Araneta's basic duties as a fiduciary of the Delaware Holding Company were well-established. But, by transferring the LBC Operating Companies from the Delaware Holding Company to his family for no value, Araneta flouted his obligations to the minority shareholders and profited at their expense. Moreover, when served with the § 220 suit, this lawsuit, and confronted with his conduct, Araneta engaged in a deliberate pattern of obfuscation ranging from the obstruction of legitimate discovery requests, to the presentation of baseless and shifting defenses, and ultimately to the telling of outright lies under oath and the submission of a phony defense in an attempt to escape this court's jurisdiction by exposing his own secretary to legal risk on the pretense that she was the sole director of the Delaware Holding Company during the period when Araneta denuded it of the LBC Operating Companies.<sup>135</sup>

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<sup>130</sup> *Johnston v. Arbitrium (Cayman Islands) Handels*, 720 A.2d 542, 545-46 (Del. 1998); *see also* John F. Vargo, *The American Rule on Attorney Fee Allocation: The Injured Person's Access to Justice*, 42 AM. U. L. REV. 1567 (1993) (contrasting the American Rule with the English Rule whereby the losing party must pay the victor's litigation expenses).

<sup>131</sup> *Kaung v. Cole National Corp.*, 884 A.2d 500, 506 (Del. 2005).

<sup>132</sup> *See Gans v. MDR Liquidating Corp.*, 1998 WL 294006, at \*3 (Del. Ch. 1998) ("Delaware courts have recognized the following as meriting an award of fees: (i) statutory authority; (ii) a class representative's litigation costs on behalf of the class; (iii) bad faith conduct in litigation; and (iv) fraud, bad faith, or other outrageous conduct from which the claim arose.").

<sup>133</sup> *Roadway Express, Inc. v. Piper*, 447 U.S. 752, 766 (1980) (citations and quotations omitted).

<sup>134</sup> *Arbitrium (Cayman Islands) Handels*, 702 A.2d at 546; *see also Jacobson v. Dryson Acceptance Corp.*, 2002 WL 31521109, at \*16 (Del. Ch. 2002) (stating that fee awards "may be appropriate where a party misleads the court, alters his testimony or changes his position."), *aff'd*, 826 A.2d 298 (Del. 2003).

<sup>135</sup> *See H&H Brand Farms, Inc. v. Simpler*, 1994 WL 374308, at \*5-6 (Del. Ch. June 10, 1994) (imposing fee award for "acts of bad faith and wanton disregard for the rights of others").

Certainly, not all breaches of the fiduciary duty of loyalty warrant the imposition of attorneys' fees.<sup>136</sup> But, where an "untenable conflict should have been perfectly obvious," a director's "effrontery in going forward nonetheless is reprehensible" and those "seeking to censor this outrageous conduct should have their attorneys' fees paid."<sup>137</sup> Thus, as an initial matter, I may award fees if I find that Araneta's conduct giving rise to this litigation constituted "an egregious breach" of his duty to ATR.<sup>138</sup> His conduct involved such an egregious breach. It was a fraudulent transfer that Araneta sought, by later fraud, to conceal.

Likewise, Araneta's misconduct during the litigation process was extensive. He obstructed legitimate requests for discovery. He proffered false testimony in order to avoid this court's jurisdiction and liability. In sum, he made the procession of the case unduly complicated and expensive.

Chancellor Allen well captured the traditional reluctance of this court to shift fees under the bad faith exception to the American Rule, by stating that the bad faith exception only applied when the party in question displayed "unusually deplorable behavior."<sup>139</sup> Even under that standard, which is more stringent than that articulated recently by our Supreme Court in *Kaung v. Cole National Corp.*,<sup>140</sup> Araneta easily qualifies for an order requiring him to pay ATR's attorneys' fees and expenses. Because

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<sup>136</sup> See, e.g., *Weinberger v. UOP, Inc.*, 517 A.2d 653, 656 (Del. Ch. 1986) (refusing to award fees for breach of fiduciary duty absent unjustifiable or bad faith conduct).

<sup>137</sup> *Gans*, 1998 WL 294006, at \*4.

<sup>138</sup> *Id.*

<sup>139</sup> *Barrows v. Bowen*, 1994 WL 514868, at \*2 (Del. Ch. 1994).

<sup>140</sup> 884 A.2d 500, 506 (Del. 2005).

of Araneta's bad faith, I also will enter an order requiring him to bear any additional attorneys' fees and expenses ATR is forced to bear in seeking to collect on this judgment. This will ensure that ATR obtains full relief if it is forced to expend even more resources to obtain redress from Araneta.

On this score, however, Bonilla and Berenguer are in a different position than Araneta. Their regrettable, if all too historically traditional, role as instruments of a controller's will rightly exposes them to damages liability, but they have not engaged in conduct that satisfies the exacting bad faith standard required for fee shifting.

#### IV. Conclusion

Based on the foregoing, I find in favor of ATR on each of its claims and award ATR \$3,922,000 in damages plus pre-judgment as well as post-judgment interest on this amount. Pre-judgment interest shall accrue at an annual rate of 25% with monthly compounding from the date of ATR's investment in the Delaware Holding Company through the date a final judgment is entered. Post-judgment interest at the statutory rate will accrue thereafter until payment is made. Araneta shall also pay ATR's attorneys' fees, costs, and expenses incurred in prosecuting this action and shall pay any future costs expended by ATR in enforcing this judgment. Counsel for the parties shall craft a final order implementing this decision within 20 days.