IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

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| EUGENE M. JULIAN,<br><br>Plaintiff/<br>Counterclaim Defendant,<br><br>v.<br><br>EASTERN STATES CONSTRUCTION SERVICE, INC., a Delaware corporation, and STEVEN BOMBERGER,<br><br>Defendants,<br><br>and<br><br>RICHARD J. JULIAN and FRANCIS R. JULIAN,<br><br>Defendants/<br>Counterclaim Plaintiffs,<br><br>and<br><br>EASTERN STATES DEVELOPMENT COMPANY, INC. and BENCHMARK BUILDERS, INC.,<br><br>Nominal Defendants. | Civil Action No. 1892-VCP |

**MEMORANDUM OPINION**

Submitted: January 18, 2008
Decided: July 8, 2008

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**PARSONS, Vice Chancellor.**

This action involves a dispute among three brothers, Eugene Julian, Francis Julian, and Richard Julian (collectively, the "Julian Brothers") who were in business together from the late 1960's until the end of 2005, when Gene precipitously purported to "retire." As of 2005, the Julian Brothers owned three separate, but related, businesses—Eastern States Construction Service, Inc. ("ESCS"), Benchmark Builders, Inc. ("Benchmark"), and Eastern States Development Company, Inc. ("ESDC"). Each of these businesses had its own stockholders agreement to which Gene, Francis, and Richard were all parties. By 2001, relations among the Julian Brothers were becoming strained and they deteriorated over the next several years, culminating in Gene's retirement. None of the three stockholders agreements clearly gave Gene the right to retire before age sixty-two. Nevertheless, in December 2005, Gene purported to do just that and claims to have the right to retain his stock in ESCS, Benchmark, and ESDC until he reaches age seventy-two, when the various agreements all mandate retirement and resale of a stockholder's stock to the company. Francis and Richard contend the companies had the right to redeem all of Gene's stock as of December 31, 2005, when he ceased to be employed by any of them.

After a full trial, I have concluded Plaintiff, Gene, did not have the right voluntarily to "retire" before he reached his sixty-second birthday and retain his stock. Consequently, Gene must sell his ESCS stock back to the company at its net book value as of December 31, 2005. Gene must do the same as to his stock in ESDC, although the price specified for that stock in the relevant stockholder agreement, referred to as the adjusted net book value, is to be calculated slightly differently. Technically, Gene would

have had to sell back his stock in Benchmark even earlier, because Francis and Richard effectively terminated his employment at Benchmark in 2003. The evidence shows, however, that Francis and Richard waived their right to insist upon such a resale by knowingly failing to try to enforce that right until December 2005 or later. Accordingly, Gene may retain his stock in Benchmark, but has no right to demand that Benchmark redeem it before his seventy-second birthday.

The other major claim advanced by Gene is for breach of fiduciary duty against Francis, Richard, and Steven Bomberger, a director of Benchmark, for approving bonuses to themselves from Benchmark in 2005, totaling $1.3 million. I conclude that Francis, Richard, and Bomberger, as directors of Benchmark, breached their fiduciary duties in granting those bonuses. To remedy that breach of duty I am ordering Francis, Richard, and Bomberger to disgorge the bonus amounts they received back to Benchmark with interest and to reimburse Gene for his reasonable attorneys' fees in prosecuting this aspect of his complaint.

## I. FACTS

These are the facts as I find them after trial.

Plaintiff is Gene Julian who currently owns stock in ESCS, Benchmark, and ESDC, but no longer works for any of the companies.

Defendant ESCS is a Delaware corporation formed on September 14, 1983.[1] Nominal Defendant Benchmark is a Delaware corporation formed on November 28,

[1] Pretrial Stip. ("PT Stip.") ¶ II.1.

1988. Defendant Steven Bomberger is the President of Benchmark and serves as a director of Benchmark, along with Defendants Francis and Richard Julian.[2] Nominal Defendant ESDC is a Delaware corporation formed on June 2, 1958. Eastern States Group Management Company, Inc. is a Delaware corporation formed on December 13, 2004 (together with ESCS, Benchmark, and ESDC, the "Julian Businesses").[3]

**A. The Early Years**

In the early 1970's, Gene, Francis, and Richard worked for Eastern States Construction Company and First State Enterprises.[4] Eastern States Construction Company was owned by the Julian Brothers' father and their uncle, James Julian, along with several minority shareholders. First State Enterprises was owned by the brothers' father and a company owned by their Uncle James, in equal shares.[5] In 1976 the brothers' father died and the Julian Brothers took on increasing responsibilities in the companies. By the mid-1980's the brothers wanted to buy Eastern States Construction Company, which by that time they ran. Among other things, they objected to the continuing need to pay dividends to Uncle James, who had no active role in the company.[6] The brothers successfully bought out all of the minority interests in the

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2 *Id.* ¶ II.2.

3 *Id.* ¶ II.4.

4 T. Tr. at 5-6 (Gene). Citations in this format are to the trial transcript. Where the identity of the testifying witness is not clear from the text, it is indicated parenthetically.

5 *Id.* at 5 (Gene).

6 *Id.* at 109-10 (Gene).

company, except for Uncle James. The brothers attempted to purchase Uncle James' shares, but could not come to terms with him. Consequently, they liquidated Eastern States Construction Company and formed ESCS.[7]

### B. The ESCS Agreements

The Julian Brothers formed ESCS in the mid-1980s to continue in the construction business.[8] On October 14, 1985, the brothers entered into an Agreement of Stockholders of Eastern States Construction Service, Inc. (the "1985 ESCS Agreement").[9] The brothers wanted such an agreement because of the difficulties they experienced without an agreement with Eastern States Construction Company. In forming the agreement, the brothers had two key principles: only people who work for the company could own stock in the company; and there had to be an established mechanism for determining the price of the stock if a shareholder left or died.[10]

In 1986 the brothers allowed ESCS employees to purchase stock in the business as an incentive to retain employees.[11] ESCS employees Rex Gibson and Stephen Trainer, among others, entered into an Agreement of Stockholders of ESCS on March 1, 1986 (the "Employee Agreement"),[12] which was similar to the 1985 ESCS Agreement. At various

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7 *Id.* at 8-9 (Gene).

8 *Id.* at 9-10 (Gene); *id.* at 202-03 (Francis).

9 Joint Trial Ex. ("JX") 2, the 1985 ESCS Agreement.

10 T. Tr. at 115, 117 (Gene); *id.* at 203-04 (Francis).

11 *Id.* at 11-12 (Gene).

12 PT Stip. ¶ II.6.

times from 1986 to 2001, a few other ESCS employees also signed Employment Agreements.[13]

On November 5, 1991, Gene, Francis, and Richard, together with ESCS, replaced the 1985 ESCS Agreement by entering into an Agreement of the Principal Shareholders of Eastern States Construction Service, Inc. (the "1991 ESCS Agreement").[14]

Article 5 of the 1991 ESCS Agreement governs retirement or total disability of a Principal Shareholder. It provides that if a Principal Shareholder retires from ESCS or ceases to be employed due to total disability, the Principal Shareholder must offer to sell his ESCS stock to the other Principal Shareholders in the manner provided in Article 2. To retire a Principal Shareholder must provide at least three years notice of his intent to retire and sell his stock so that the other Principal Shareholders can prepare for payment. Article 5 defines retirement as, "a voluntary termination on or after a Shareholder's sixty-second birthday." Further, Article 5 provides "[a]ny termination, other than one due to death or total disability, prior to a Principal Shareholder's sixty-second birthday shall result in a resale on termination in accordance with ARTICLE 4."

Article 4 of the 1991 ESCS Agreement deals with the resale of stock upon a termination of employment other than due to death, total disability, or retirement. Upon such a termination, Article 4 requires an employee to sell his stock to the corporation forthwith, and obligates the corporation to purchase those shares at the lower of: "(1) the

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[13] *See* JX 1, several ESCS Stockholder Employee Agreements.

[14] PT Stip. ¶ II.5; JX 3, the 1991 ESCS Agreement.

sale price at which they (the shares) were originally sold pursuant to this agreement by corporation to employee, . . . or (2) the then current book value of the shares."[15] Before January 1, 2006, Gene, Francis, and Richard each owned 250 shares of ESCS stock.[16]

### C. The Benchmark Agreement

In 1988, the Julian Brothers, together with Bomberger, started a home building business, Benchmark Builders, Inc.[17] On March 2, 1994, Gene, Francis, Richard, and Bomberger, together with Benchmark, entered into an Agreement of the Principal Shareholders of Benchmark Builders, Inc. (the "Benchmark Agreement").[18] The terms of the Benchmark Agreement resemble those of the 1991 ESCS Agreement. In particular, the terms of the two agreements track nearly identically as regards a Principal Shareholder's termination of employment, retirement, total disability, and the resulting obligation to offer to sell his stock to the other Principal Shareholders. The agreements even use the same article numbers and titles. A proposed amended and restated agreement among the principal shareholders of Benchmark was drafted in 2005 but never executed because Gene, a principal shareholder, refused to sign the amended agreement.[19]

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15 As explained *infra*, Defendants no longer seek to force Gene to sell any of his stock at the first of the two potential prices.

16 PT Stip. ¶ II.7.

17 T. Tr. at 306-10 (Bomberger).

18 PT Stip. ¶ II.8; JX 4.

19 PT Stip. ¶ II.8.

## D. The ESDC Agreement

After buying out their Uncle James and other investors in First State Enterprises, the Julian Brothers and their father changed the name to Eastern States Development Company.[20] On June 15, 2001, Gene, Francis, Richard, and their sister, Janis Julian, together with ESDC entered into an Agreement of Stockholders of Eastern States Development Company, Inc.[21]

On August 24, 2005, the same parties and two new ESDC stockholders, Amelia Julian and Richard J. Julian, Jr., entered into a First Amendment to Agreement of Stockholders of Eastern States Development Company, Inc.[22] The ESDC Agreement, as amended, differs in several respects from the ESCS and Benchmark Agreements. The preamble to the ESDC Agreement recites the following purposes: "(i) to provide for the purchase by the Company of the shares of any Stockholder in the event of such Stockholder's death, and (ii) to provide for the purchase of the shares of a Stockholder who during his lifetime desires to dispose of any of his interest, retires, becomes permanently and totally disabled or voluntarily or involuntarily terminates employment with the Company or any affiliated entity."[23]

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[20] T. Tr. at 51 (Gene).

[21] PT Stip. ¶ II.9.

[22] JX 5, the ESDC Agreement. For convenience, I refer to the 2001 agreement as so amended as the "ESDC Agreement."

[23] *Id.* at 1.

Paragraph 5 provides that upon "the termination of employment, whether voluntary or involuntary, with a member of the Eastern States Group (except for voluntary termination by retirement) . . . the Company shall purchase, and the terminated Stockholder. . . shall sell all of the terminated Stockholder's . . . stock in the Company owned at the time of such Stockholder's termination . . . ."[24] Paragraph 6, entitled "Retirement and Notice of Intent to Retire," states:

> Any Stockholder may retire at any time after attaining age sixty-two (62), provided such Stockholder has notified the Company at least three (3) years prior to the Stockholder's intended date of retirement. Any Stockholder must retire upon attaining age seventy-two (72) and shall be deemed to have provided the notice required by this Paragraph 6 on his or her sixty-ninth birthday.

### E. Changes in the Operations of the Julian Businesses

Gene, Francis, and Richard for many years divided the responsibility for running each of the Julian Businesses among themselves, with one of them managing each business. In terms of the day-to-day operations, Gene was in charge of ESDC, Francis was in charge of Benchmark, Eastern States Leasing LLC, and Sentinel Self Storage LLC, and Richard was in charge of ESCS. ESDC, ESCS, Benchmark, Eastern States Leasing, and Sentinel Self Storage are part of a family of related business entities owned at some time by Gene, Francis, and Richard, either as the sole stockholders or in conjunction with others. Although each of the Julian Businesses generally related to

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[24] *Id.* ¶ 5(a).

construction, real estate development, and leasing activities, they involved distinct operations and were run as separate businesses.[25]

At a meeting of the ESCS board on October 12, 2000, Gene was removed from his role as President of ESCS and made Vice President. In addition to his continuing role as an officer, Gene also served as a director, and received his *pro rata* share of ESCS stock distributions until his resignation on December 31, 2005.[26] Gene also retained check writing authority for ESCS, signing signature cards for ESCS's Wilmington Trust Account as late as November 2005.[27] As Francis and Richard removed Gene from any active role in ESCS, Gene's relationship with his brothers soured. In November 2001, Gene moved out of the building ESCS occupied,[28] and by August 19, 2002, had stopped attending ESCS board meetings.[29] Neither Francis nor Richard requested that Gene sell his stock in ESCS at any time before December 30, 2005.[30]

At a meeting of the Benchmark board of directors held on April 22, 2003, the directors present, Francis, Richard, and Bomberger, passed a resolution removing Gene as a director of Benchmark and providing that Gene would not be considered for re-election as an officer at the next board meeting scheduled for October 2003.

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25 PT Stip. ¶ II.10.

26 T. Tr. at 34-35 (Gene); PT Stip. ¶ II.11.

27 JX 15, copies of ESCS checks; JX 16, memo re ESCS check signers.

28 JX 16; T. Tr. at 36-38 (Gene).

29 JX 12; T. Tr. at 34-36 (Gene).

30 PT Stip. ¶ II.12.

Nevertheless, Gene continued to receive his *pro rata* share of Benchmark stock distributions until December 31, 2005.[31] As in the case of ESCS, neither Francis nor Richard requested that Gene sell his Benchmark stock back to the company until December 30, 2005.[32]

By letter dated December 9, 2005, Gene notified Richard and Francis of his resignation as an officer and director of ESCS and ESDC effective December 31, 2005. The letter also announced Gene's retirement from ESDC as of December 31, 2005.[33] Gene was 61 at that time.[34] After Gene tendered his resignation as an officer and director of ESCS, Richard (on behalf of ESCS) sent a letter on December 30, 2005, informing Gene he would have to sell his stock back to ESCS pursuant to Article 4 of the 1991 ESCS Agreement for a sale price of $18,433.34.[35] I infer from the evidence that this number represents the price at which Gene originally acquired his ESCS shares.

At a February 10, 2006 Benchmark board of directors meeting, the board decided by a vote of 2-1, with Bomberger dissenting, to waive enforcement of the final sentence in Article 5 of the Benchmark Agreement. That sentence provides: "Any termination, other than one due to death or total disability, prior to a Principal Shareholder's sixty-

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[31] *Id.* ¶ II.13.

[32] *Id.* ¶ II.14.

[33] *Id.* ¶ II.15.

[34] T. Tr. at 105 (Gene). Gene was born on May 23, 1944. *Id.*

[35] PT Stip. ¶ II.16.

second birthday shall result in a resale on termination in accordance with Article 4."[36] Likewise, ESCS's counsel stated during the course of this litigation that ESCS also waived enforcement of the final sentence of Article 5 of the ESCS Agreement, which is substantially identical to Article 5 of the Benchmark Agreement. The latter waiver moots the December 30, 2005 letter from Richard to Gene demanding resale of Gene's ESCS stock for just over $18,000.[37]

ESCS, Benchmark, and ESDC are each subchapter S corporations whose income is treated for tax purposes as if it has been received by their stockholders.[38] Before June 2006, Richard and Francis, as the controlling stockholders and directors of ESCS, Benchmark, and ESDC, caused each of those entities to make regular distributions of income to, *inter alia*, permit their stockholders to pay the taxes imputed to each of them based on the income of those entities (the "Tax Distributions").[39] Before Gene's December 9, 2005 letter, Gene regularly received Tax Distributions because Richard and Francis properly recognized Gene as a stockholder in ESCS, Benchmark, and ESDC.[40] There is no evidence Gene received any Tax Distributions after June 2006.

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36 *Id.* ¶ II.17.

37 *Id.* ¶ II.18.

38 *Id.* ¶ II.19.

39 *Id.* ¶ II.20. In September 2004, an advisory board for Eastern States Group was assembled to advise the Julian Businesses. The board includes three independent members. *Id.* ¶ II.22.

40 PT Stip. ¶ II.21.

### F. Benchmark Bonuses

At a meeting of the Benchmark board of directors on December 20, 2005, the board approved a $1,000,000 bonus to Eastern States Group Management Company (the "Management Group Bonus") and a $300,000 bonus to Bomberger (the "Bomberger Bonus," collectively the "Benchmark Bonuses") for calendar year 2005. Defendants allege the board discussed two business reasons for the bonuses – to reward management for a good year and to reduce retained earnings so that fewer assets would be at risk in the event of a lawsuit.[41] The meeting took less than half an hour and no legal or financial advisors attended.[42]

Before the December 20, 2005 meeting, Francis discussed the possibility of awarding bonuses with Richard for approximately fifteen minutes.[43] Both Francis and Richard recognized that payment of any bonuses would decrease the net book value of Benchmark, and thereby benefit Benchmark in the event of a buyback of Gene's shares.[44] Yet, the Benchmark directors did not consult anyone else before deciding to pay the bonuses.[45] Several days after the board meeting, Benchmark issued a check to Eastern

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[41] T. Tr. at 319 (Bomberger).

[42] *Id.* at 333 (Bomberger); JX 20, Minutes of the Benchmark Board of Directors, 12/20/05. The length of the meeting and the absence of outside advisors were typical for Benchmark. *See* T. Tr. at 187 (Gene); *id.* at 314-15 (Bomberger).

[43] *Id.* at 269 (Richard).

[44] *Id.* 243-44 (Francis).

[45] *Id.* at 269 (Richard).

States Management Group for $1,000,000, which then distributed the bonus in equal shares to Francis and Richard.[46] Benchmark paid the Bomberger Bonus in 2006.[47]

The Benchmark Bonuses constituted 22.28% of Benchmark's adjusted income in 2005. For historical context, from 1996 to 1998, Benchmark paid no bonuses. Between 1999 and 2004, Benchmark's bonuses ranged from 3.30% to 3.36% of its adjusted income.[48] Further, the Bomberger Bonus was the first bonus Bomberger received during his career at Benchmark beyond the compensation provided for in his Employment Agreement. A portion of Bomberger's contractual compensation in 2005 and earlier years was based on a percentage of Benchmark's gross profit or income before taxes.

Additionally, the portion of the Benchmark Bonuses paid to Francis, Richard, and Bomberger directly correlates to their respective stock ownership in Benchmark. Specifically, Francis and Richard each own 250 shares of Benchmark stock and Bomberger owns 150 shares. Their respective bonuses each translate into a payment to them of $2,000 per share.[49]

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46 Francis and Richard knew before the Management Group Bonus was paid it would be split equally between them. T. Tr. at 268 (Richard); JX 24. Historically, the Julian Brothers pooled any bonus money from the Julian Businesses and distributed the money equally among them. Gene, however, received none of the Management Group Bonus, even though he worked for the Julian Businesses in 2005. *See* T. Tr. at 210-11 (Francis).

47 PT Stip. ¶ II.24; JX 20.

48 Although the record regarding Benchmark's bonuses lacks precision, the big picture is readily discernible.

49 T. Tr. at 323-25 (Bomberger). In addition to Gene, who owned 250 shares, Benchmark had at least one other shareholder, Frank T. Fortunato, who received

### G. McMullen Square

On July 25, 2005, ESDC and Eastlawn Associates, LLC entered into an Agreement of Purchase and Sale for a tract of land, the "McMullen Square" property. On April 12, 2006, ESDC assigned all of its interests in the agreement to McMullen Square Associates, LLC.[50] The members of McMullen Square Associates were Francis, Richard, and Bomberger. On August 17, 2006, Gene amended his complaint to add a claim of diversion of corporate opportunity for the transfer of ESDC's rights in the McMullen Square property. After that amendment, Defendants transferred the rights back to ESDC, backdated the relevant agreements, and thereby mooted Gene's claim regarding the McMullen Square property.[51]

## II. PROCEDURAL HISTORY

Plaintiff Gene Julian filed this action on January 18, 2006, seeking a judgment declaring him the rightful owner of 250 shares of ESCS stock. On August 17, 2006, Gene filed an amended complaint adding a breach of fiduciary duty count against Defendants Richard and Francis Julian—the directors and majority shareholders of ESCS, ESDC, and Benchmark—for withholding Gene's shareholder distributions from

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distributions between 2000 and 2006. JX's 89-95, Form 1120 S of Benchmark for Fiscal Years 2000-2006. There is no evidence Gene or Fortunato received any payments in connection with the Benchmark Bonuses.

[50] *See* JX 48, Agreement of Purchase and Sale between ESDC and Eastlawn, 7/25/05, and Amendment, 9/2/05; JX 51, Settlement Statement between McMullen Square Associates and Eastlawn Associates, 4/12/06.

[51] PT Stip. ¶ II.25.

these companies after June 2006.[52] The amended complaint also added a diversion of corporate opportunity count on behalf of ESDC against Francis and Richard for acquiring the McMullen Square property Gene claimed rightfully belonged to ESDC.

Defendants filed an answer to the amended complaint and a counterclaim on September 20, 2006, asserting claims for specific performance, breach of contract, and breach of fiduciary duties that challenged the validity of Gene's "retirement" in December 2005. On September 28, 2006, Gene replied to the counterclaim.

On March 23, 2007, Gene filed a second amended complaint (the "Complaint") adding a sixth cause of action for breach of fiduciary duties by the directors of Benchmark based on the $1.3 million in bonuses paid by Benchmark for 2005. The Complaint also added Bomberger as a defendant and Benchmark as a nominal defendant. On April 30, 2007, Francis and Richard answered the Complaint and re-filed their counterclaim without revisions. Bomberger filed his answer on May 2, 2007.

Trial was held on September 12 and 14, 2007. After extensive briefing, the Court also heard post-trial argument.

## III. ANALYSIS

### A. Gene's Stock in ESCS, Benchmark, and ESDC

Gene seeks a declaratory judgment that he has the right to continue to own his stock, and Defendants seek a declaratory judgment that Gene must sell back his stock in

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[52] Gene alleges Francis and Richard began to withhold from him the regular distributions of income when he declined to resolve the litigation on the terms they demanded.

ESCS, Benchmark, and ESDC. The purpose of the statute on declaratory judgments "is to settle and to afford relief from uncertainty and insecurity with respect to rights, status and other legal relations."[53] Declaratory judgment is appropriate when there is an actual controversy between the parties.[54] In this case, an actual controversy exists regarding Gene's status as a shareholder in each of ESCS, Benchmark, and ESDC. A declaratory judgment, therefore, would settle the uncertainty regarding Gene's rights and status.

**1. Contract interpretation principles**

To resolve the parties' dispute, this Court must construe the relevant shareholder agreements. Under Delaware law, contract construction is a question of law.[55] When interpreting a contract, the court strives to determine the parties' shared intent, "looking first at the relevant document, read as a whole, in order to divine that intent."[56] If the contractual language is "clear and unambiguous," the ordinary meaning of the language generally will establish the parties' intent.[57] Therefore, where there is an unambiguous

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[53] 10 *Del. C.* § 6512.

[54] *Dana Corp. v. LTV Corp.*, 668 A.2d 752, 755 (Del. Ch.), *aff'd*, 670 A.2d 1337 (Del. 1995).

[55] *Rhone-Poulenc Basic Chems. Co. v. Amer. Motorists Ins. Co.*, 616 A.2d 1192, 1195 (Del. 1992).

[56] *Matulich v. Aegis Comm'ns Group, Inc.*, 2007 WL 1662667, at *4 (Del. Ch. May 31, 2007) (citing *Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 395 (Del. 1996)); *Brandywine River Prop., Inc. v. Maffet*, 2007 WL 4327780, at *3 (Del. Ch. Dec. 5, 2007).

[57] *Brandywine River*, 2007 WL 4327780, at *3; *Comrie v. Enterasys Networks, Inc.*, 837 A.2d 1, 13 (Del. Ch. 2003).

integrated written contract, the language of that contract will control.[58] Additionally, when interpreting a contractual provision, a court attempts to reconcile all of the agreement's provisions when read as a whole, giving effect to each and every term.[59] In doing so, courts apply the well settled principle that "contracts must be interpreted in a manner that does not render any provision 'illusory or meaningless.'"[60]

A contract is ambiguous, however, when the language "in controversy [is] reasonably or fairly susceptible of different interpretations or may have two or more different meanings."[61] If a contract is ambiguous, "the court may consider extrinsic evidence to uphold, to the extent possible, the reasonable shared expectations of the parties at the time of contracting."[62] In considering extrinsic evidence, the court may consider "'overt statements and acts of the parties, the business context, prior dealings between the parties, [and] business custom and usage in the industry.'"[63] Review of the

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58 *Am. Legacy Found. v. Lorillard Tobacco Co.*, 886 A.2d 1, 19 (Del. Ch. 2005).

59 *See, e.g.*, *Council of the Dorset Condo. Apartments v. Gordon*, 801 A.2d 1, 7 (Del. 2002); *W. Willow-Bay Court, LLC v. Robino-Bay Court Plaza, LLC*, 2007 WL 3317551, at *11 (Del. Ch. Nov. 2, 2007) ("Delaware courts do prefer to interpret contracts to give effect to each term rather than to construe them in a way that renders some terms repetitive or mere surplusage.").

60 *Delta & Pine Land Co. v. Monsanto Co.*, 2006 WL 1510417, at *4 (Del. Ch. May 24, 2006).

61 *Rhone-Poulenc*, 616 A.2d at 1196. Ambiguity does not exist simply because the parties do not agree on a contract's proper construction. *United Rentals, Inc. v. Ram Holdings, Inc.*, 2007 WL 4496338, at *15 (Del. Ch. Dec. 21, 2007).

62 *Comrie*, 837 A.2d at 13.

63 *Id.* (quoting *Supermex Trading Co. v. Strategic Solutions Group*, 1998 WL 229530, at *3 (Del. Ch. May 1, 1998)).

extrinsic evidence "may render an ambiguous contract clear so that an 'objectively reasonable party in the position of either bargainer would have understood the nature of the contractual rights and duties to be.' In such a case, the court would enforce the objectively reasonable interpretation that emerges."[64]

When examining the shared intent of the parties to an ambiguous agreement, if review of the extrinsic evidence does not lead the court to an obvious conclusion, the court may apply the "forthright negotiator principle."[65] Under that principle, "in cases where the extrinsic evidence does not lead to a single, commonly held understanding of a contract's meaning, a court may consider the subjective understanding of one party that has been objectively manifested and is known or should be known by the other party."[66]

Before examining the agreements at issue here, I note that each of the three Julian Brothers is a successful business person. Consequently, I consider them all sophisticated parties. Additionally, the three primary agreements at issue are not entirely consistent and are difficult to harmonize, as is the conduct of the parties in reference to them. The failure of the Julian Brothers, individually and collectively, to pay more attention to these agreements and to confront and resolve differences regarding the nature of their business relationships, when they arose, has complicated significantly the issues before me.

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64 *United Rentals, Inc.*, 937 A.2d at 835 (quoting *U.S. West, Inc. v. Time Warner, Inc.*, 1996 WL 307455, at *10 (Del. Ch. June 6, 1996)). In considering extrinsic evidence, the court adheres to the objective theory of contracts; the subjective understandings of the negotiators are unhelpful in interpreting the contract. *Id.*

65 *Comrie*, 837 A.2d at 13.

66 *United Rentals, Inc.*, 937 A.2d at 836.

Because Gene, Francis, and Richard are sophisticated parties, however, the Court's function is to determine what it is they agreed to and to implement those agreements as closely as possible in the factual circumstances of this case.

No material differences exist between the ESCS and Benchmark Agreements for purposes of the current dispute, but the ESDC Agreement differs markedly from those earlier agreements. Additionally, Gene's involvement in each of the three companies and Francis and Richard's interactions with Gene in terms of the specific companies varied during the relevant period before Gene delivered his December 9, 2005 letter announcing his retirement from ESDC. I therefore analyze Gene's claimed rights to continue owning his stock in each company separately. I begin by addressing a few material issues of contract interpretation.

### 2. The 1991 ESCS Agreement and the Benchmark Agreement[67]

Gene argues the terms "employee," "employed," and "employment" as they appear in Articles 4 and 5 of the 1991 ESCS Agreement are unambiguous and must be given their plain and ordinary meaning. Because the terms are not defined in the agreements, Gene cites Black's Law Dictionary, which defines "employee" as: "A person who works in the service of another person (the employer) under an express or implied contract for hire, under which the employer has the right to control the details of

[67] Because the relevant provisions of the 1991 ESCS Agreement and the Benchmark Agreement are essentially identical, I discuss primarily the 1991 ESCS Agreement. Unless otherwise noted, my interpretation of the disputed terms in that agreement applies equally to the Benchmark Agreement.

work performance."[68] "Employment" is defined as: "Work for which one has been hired and is being paid by an employer."[69] Gene further argues the case law confirms his position that individuals who do not receive compensation and who do not perform any duties other than holding the title of an officer are not "employees." According to Gene, he was not under the direct control of an employer and did not receive a salary. Thus, he contends he was not an employee and cannot be forced to sell his shares pursuant to the 1991 ESCS Agreement or the Benchmark Agreement.

Francis and Richard assert the terms employee, employed, and employment, as used in the agreements, are ambiguous. They therefore urge this Court to look to extrinsic evidence to determine the parties' shared intent as to those terms. Francis and Richard point, for example, to the historical catalyst for the operating agreements. The underlying purpose in creating the first operating agreements, the 1985 ESCS Agreement and the Employee Agreements, was to ensure that only people who work for ESCS could own stock in ESCS and to establish a mechanism to determine the price upon a sale of stock to avoid any disputes. Hence, according to Francis and Richard, Gene is subject to the shareholder agreement provisions that compel the resale of stock upon termination of employment or retirement.

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68 BLACK'S LAW DICTIONARY 564 (8th ed. 2004). Gene cited to the seventh edition, but the eighth edition is the most current and contains the same definition as the seventh.

69 *Id.* at 566.

Turning to the language of the 1991 ESCS Agreement, Article 5, entitled "Retirement or Total Disability," states in pertinent part:

> *In the event a Principal Shareholder ceases to be employed by the corporation* by reason of retirement or total disability, he must offer to sell his shares to the other Principal Shareholders in the manner provided in Article 2 hereof . . . . Principal Shareholders must give at least three years notice of intent to sell stock in order for the other Principal Shareholders to prepare for payment, except that, in the event of total disability, an employee must notify the corporation of his total disability and of his intent to sell his stock six months prior to the date of sale. Retirement is defined as a voluntary termination on or after a Shareholder's sixty-second birthday. Any termination, other than one due to death or total disability, prior to a Principal Shareholder's sixty-second birthday shall result in a resale on termination in accordance with ARTICLE 4.[70]

Article 2, which applies in the case of retirement, provides for valuing each Principal Shareholder's stock in ESCS at current net book value. In contrast, for any termination before a Principal Shareholder's sixty-second birthday, other than for death or total disability, Article 5 refers back to Article 4, which calls for a resale of the shareholder's stock for as low as the price he originally paid for it.[71]

Article 4, entitled "Resale on Termination of Employment," provides:

> *If the employment of an employee with the corporation is terminated* (a) from the date of this agreement by employee's resignation, discharge, with or without cause, disability, or

[70] The 1991 ESCS Agreement Art. 5 (emphasis added).

[71] As discussed *infra*, Defendants do not seek to compel Gene to resell his stock in any of the three companies for what he paid for it. Instead, they essentially would set the price at the net book value, although the determination of that value is slightly more involved in the case of ESDC.

> any other reasons except the employee's death or total disability, or (b) at any time, if employee has committed acts of dishonesty or disloyalty or acts substantially detrimental to the welfare of corporation, then in either case, if such termination occurs while employee is the registered owner of the shares, employee shall be bound to sell to corporation forthwith, and corporation shall be bound to purchase from employee, the shares at the lower of (1) the sale price at which they were originally sold pursuant to this agreement by corporation to employee, . . . or (2) the then current book value of the shares.[72]

The validity of Gene's claim to a contract right to continue to hold his stock in ESCS turns largely on the proper interpretation of the references to "employment" in Articles 4 and 5 of the 1991 ESCS Agreement.

I conclude the language of Article 5 is dispositive. That Article deals with the situation in which a "Principal Shareholder ceases to be employed by the corporation [ESCS] by reason of retirement or total disability" or is subject to "termination, other than one due to death or total disability, prior to a Principal Shareholder's sixty-second birthday." The plain language of Article 5 makes clear the signatories to the 1991 ESCS Agreement, Gene, Francis, and Richard, considered themselves to be "employed by" ESCS in the ordinary, colloquial sense of working for the company in some gainful capacity. As I understand Gene's argument, he contends he was an owner or Principal Shareholder of ESCS, but never an "employee," in the legal sense of that term for purposes of employment law, for example. That begs the question, however, of whether Gene was "employed by" ESCS within the meaning of Article 5. The 1991 ESCS

[72] The 1991 ESCS Agreement Art. 4 (emphasis added).

Agreement he signed plainly indicates he was. Nothing in that agreement suggests the parties intended the word "employed" in Article 5 to have the more narrow legal meaning Gene now attempts to ascribe to it. Thus, the agreement is not ambiguous in that regard.

Even assuming the terms "employee," "employed," and "employment" in the 1991 ESCS Agreement are ambiguous, however, I reach the same conclusion that Gene was "employed by" ESCS at least until 2001 and more likely until he resigned as an officer and director of ESCS effective December 31, 2005.[73]

Assuming the employment related terms are ambiguous, I look to the ordinary meaning of the contract language and attempt to reconcile all of the agreement's provisions when read as a whole. First, the agreement is a Principal Shareholder Agreement, and, as is also true for the Benchmark Agreement, the signatories are all the Principal Shareholders, namely Gene, Francis, and Richard (each with 250 shares).[74] Gene denies ever being an "employee" in ESCS or Benchmark. Further, in Gene's view, under the terms of the Principal Shareholder Agreements, Gene's ties with ESCS could never be severed in a manner that would require him to sell back his stock, other than through mandatory retirement when he reached his seventy-second birthday. Before

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[73] The exact date as of which Gene ceased to be employed by ESCS arguably could be relevant to Gene's waiver argument discussed *infra* Part III.A.4. I need not address that issue further, however, in view of my resolution of the waiver issue and the fact that Defendants do not contend Gene ceased to be employed by ESCS before December 31, 2005.

[74] Similarly, the Benchmark Agreement's signatories are its Principal Shareholders, namely Francis, Richard, Gene, and Bomberger (the brothers owning 250 shares each and Bomberger owning 150 shares).

reaching that age, Gene could retire at any time, he contends, and either hold onto his stock or, by complying with the notice and age requirements of Article 5, compel the company to buy it back.

Other provisions of the 1991 ESCS Agreement, however, reflect the parties' intention that only people who work for the company can own stock in the company. For example, Article 1 restricts a Principal Shareholder's ability to transfer his stock to an immediate family member by requiring that the family member be "employed in a full-time position by" ESCS. This reflects the Julian Brothers' intent that only people who work for the company can be stockholders in the company and supports the conclusion that the parties intended the term "employee" of the company to include one who works for ESCS, such as an officer.

Assuming arguendo the concept of employment is ambiguous in both the 1991 ESCS and Benchmark Agreements, the Court may consider extrinsic evidence to determine the reasonable expectations of the parties at the time of contracting. Here, the parties' overt acts and prior dealings help to clarify any perceived ambiguities. Specifically, the facts surrounding the creation of the operating agreements shed light on the parties' shared intent. From the 1970's through the mid-1980's the Julian Brothers ran businesses in which they lacked total ownership. The brothers therefore paid dividends to passive shareholders, who in their minds did not contribute to the business, chiefly Uncle James. To remedy this situation, the brothers sought complete control, and when they could not reach a mutually acceptable buy-out arrangement with Uncle James, they liquidated the company. Around the same time, Gene, Francis, and Richard formed

ESCS. Wanting to avoid another Uncle James scenario, the brothers entered into a stockholders agreement in 1985, which they later amended in 1991. A key purpose of those agreements was to ensure that only people who worked for the company could own stock in the company.

In this context, I find nothing in the existing evidence to support Gene's hypertechnical argument that he was never "employed" by ESCS. On the contrary, the evidence confirms the parties understood Gene was a Principal Shareholder employed by ESCS when they entered into the 1991 ESCS Agreement.

Because Gene was a Principal Shareholder, I look to Article 5 of the 1991 ESCS Agreement to determine what rights, if any, he has to continued stock ownership. Article 5 explicitly defines retirement as "a voluntary termination on or after a Shareholder's sixty-second birthday." Gene was not yet sixty-two when he resigned in December 2005 as an officer and director of ESCS. Thus, Gene's resignation cannot be considered a "retirement" under the 1991 ESCS or Benchmark Agreements. Rather, under Article 5, Gene's departure qualifies as a "termination," other than one due to death or total disability, prior to his sixty-second birthday. Under the 1991 ESCS Agreement, therefore, Gene's voluntary termination would give rise to an obligation on his part to resell his stock in accordance with Article 4. That Article required Gene to sell his shares to ESCS "forthwith" after the date of his termination, and ESCS was bound to purchase those shares. While under the agreement, ESCS was only required to buy Gene's shares at the sale price at which they were originally sold to Gene, a value lower than the shares'

then current book value, Defendants here seek only a declaration that Gene must sell his ESCS shares back at their current book value as of December 31, 2005.

Although I interpret the Benchmark Agreement the same way as the 1991 ESCS Agreement, the facts regarding Gene's involvement with Benchmark are different. At a meeting of the Benchmark board of directors on April 22, 2003, Francis, Richard, and Bomberger passed a resolution removing Gene as a director of Benchmark. Later in 2003, they also caused Gene not to be reelected as an officer of Benchmark. From that time until December 31, 2005, Gene had little, if any, involvement with Benchmark. To the extent Gene ceased to be employed by Benchmark sometime before December 31, 2005, I conclude for the same reasons as for ESCS, that Benchmark would have had the right to require Gene to sell back his stock forthwith. Benchmark did not demand such a resale of stock until after Gene purported to retire in December 2005, by which time he admittedly had severed all working ties with the Julian Businesses. Moreover, in February 2006, the Benchmark board waived the final sentence in Article 5 of the Benchmark Agreement in favor of "mak[ing] arrangement for the Company to purchase Eugene's shares of stock in the Company based on the year end 2005 net book value as defined in Article 2" of the Benchmark Agreement.[75]

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[75] JX 21.

### 3. The ESDC Agreement[76]

There are significant differences in form and substance between the 1991 ESCS and Benchmark Agreements, on one hand, and the ESDC Agreement, on the other hand. I therefore turn next to the ESDC Agreement.

Gene contends the ESDC Agreement gives each stockholder three options: (1) voluntarily retire before sixty-two with the right to keep your stock but no right to demand the company purchase your interest; (2) retire at sixty-two with the option of retaining your stock or demanding the company acquire your interest, provided the stockholder provides three years notice; or (3) continue working for the company until age seventy-two, at which time retirement is mandatory and the company must buy out your interest. Gene argues he voluntarily retired before sixty-two and is therefore entitled to hold his stock until mandatory retirement.

Francis and Richard respond that when Gene departed ESDC, the company had the option to enforce the age sixty-two retirement limit, the three year notice requirement, or both. Alternatively, they argue Gene did not "retire" under Paragraph 6 of the ESDC Agreement, and therefore Paragraph 5 applies and requires that Gene sell his stock to the company. Francis and Richard also challenge Gene's interpretation of the agreement, because it would permit a stockholder, who works for none of the Julian Businesses, to retain stock in those entities. Such a result, they contend, would violate the parties' key

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[76] Unlike the situation with ESCS and Benchmark, Gene makes no waiver argument as to the ESDC Agreement.

principle in drafting the operating agreements – people who do not work at the company cannot own stock.

In determining whether or not Gene is entitled to hold his ESDC stock, the ESDC Agreement controls. Like the operating agreements for ESCS and Benchmark previously discussed, the ESDC Agreement uses the term employment in a broad sense. When the agreement is construed as a whole and giving effect to all of its provisions, Paragraphs 5 and 6 are the relevant provisions because they cover the situations in which a stockholder is required to sell his stock.

In a letter dated December 9, 2005, Gene notified Francis, in his capacity as Chairman of ESDC, of his self-styled retirement. Gene wrote: "This is to provide formal written notice that I will retire from Eastern States Development Company on December 31, 2005. Effective on that date I will also resign as an Officer and Director of Eastern States Development Company and Eastern States Construction Service."[77] The procedure for retirement appears in Paragraph 6 of the ESDC Agreement.

Paragraph 6, entitled "Retirement and Notice of Intent to Retire," provides:

> (a) Any Stockholder may retire at any time after attaining age sixty-two (62), provided such Stockholder has notified the Company at least three (3) years prior to the Stockholder's intended date of retirement. Any Stockholder must retire upon attaining age seventy-two (72) and shall be deemed to have provided the notice required by this Paragraph 6 on his or her sixty-ninth birthday.

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[77] JX 8.

The agreement's language confines the concept of "retirement" to two circumstances, one permissive and one mandatory. First, a stockholder, who is sixty-two years old or older, may opt to retire provided the stockholder notified ESDC at least three years before the intended date of retirement. Second, all stockholders who still hold stock on their seventy-second birthday must retire, and are deemed to have provided proper notice. In both cases, the stockholder would have the right to require ESDC to redeem his shares for their adjusted net book value.

Here, Gene did not "retire" under Paragraph 6 of the ESDC Agreement. Gene was not yet sixty-two when he departed; he was only sixty-one. Therefore, he was not eligible to retire under the permissive retirement provision. Moreover, permissive retirement under Paragraph 6 requires three years prior notice and Gene only provided several weeks notice. Therefore, Gene's voluntary departure does not fall under Paragraph 6. Further, although Gene claims he had a right under the ESDC Agreement to "retire" voluntarily before age sixty-two and simply retain his stock until he reached the mandatory retirement age of seventy-two, nothing in Paragraph 6 supports that claim. Rather, it appears his situation would come within Paragraph 5.

Paragraph 5 addresses the ramifications of a stockholder's death or termination of employment on her stock ownership. In pertinent part, Paragraph 5 states:

> (a) Upon (i) the termination of employment, whether voluntary or involuntary, with a member of the Eastern States Group[78] (except for voluntary termination by retirement) . . .

[78] Paragraph 1 of the ESDC Agreement defines "Eastern States Group" as including Benchmark, ESCS, ESDC, Eastern States Leasing, L.L.C., and Sentinel Self Storage L.L.C.

> the Company shall purchase, and the terminated Stockholder, . . . shall sell all of the terminated Stockholder's . . . stock in the Company owned at the time of such Stockholder's termination . . . .

Paragraph 5 further provides that the purchase price for the stock shall be its adjusted net book value, and specifies the procedures under which ESDC can pay the amount due over time with interest.

According to Francis and Richard, Gene's December 9, 2005 letter provided notice of his voluntary termination of employment effective December 31, 2005. Thus, they contend that as of December 31, 2005, ESDC was required to purchase and Gene was required to sell all of his stock in ESDC. Gene disagrees and proffers a different interpretation of the ESDC Agreement.

Gene places great weight on the parenthetical language in Paragraph 5, "except for voluntary termination by retirement." Gene alleges he insisted that language be included in the ESDC Agreement to make clear that a Stockholder could voluntarily retire before age sixty-two and not be required to sell back his stock. In addition, Gene acknowledges that, in that circumstance, a stockholder could not require the company to redeem his stock before he reached his seventy-second birthday. There is no evidence, however, that Gene or his counsel ever conveyed that understanding to Francis or Richard during the negotiation of the ESDC Agreement in 2001 or the August 2005 First Amendment to it. Nor does anything in the record suggest Francis or Richard themselves shared Gene's understanding. In fact, they deny ever thinking that a stockholder of ESDC could cease

to be employed by at least one member of the Eastern States Group and still continue to hold stock in ESDC.

The reference to "voluntary retirement" in the parenthetical itself has at least one other plausible interpretation. Paragraph 6 of the ESDC Agreement deals with retirement, whether permissive or mandatory. Conceivably, voluntary retirement refers to the concept I have called "permissive" retirement under Paragraph 6. Otherwise, the ESDC Agreement makes no mention of the term "voluntary retirement," except for the parenthetical reference in Paragraph 5.

In particular, by the parenthetical "except for voluntary termination by retirement" the parties may have meant only to carve out the situation covered explicitly in Paragraph 6 regarding "Retirement and Notice of Intent to Retire." Yet, such a reading arguably would render the parenthetical little more than mere surplusage, a result courts try to avoid, if possible, in construing contract terms. In the absence of any evidence that Gene or his representatives ever fairly conveyed his purported understanding of the importance of the parenthetical to Francis, Richard, or anyone acting on their behalf in negotiating or drafting the original ESDC Agreement or the First Amendment to it, I consider the carve out construction discussed above to be the only reasonable interpretation of the disputed language. In that regard, I also note the parties slightly modified the language of the parenthetical to delete the reference to total disability in the First Amendment, which they entered into only a few months before Gene "voluntarily retired." By that time, the hostility and distrust among the brothers in terms of their business dealings was high. In those circumstances, Gene acted at his own risk by

relying on a particular understanding he had of an arguably ambiguous phrase, when he knew or should have known his brothers did not share that understanding.[79]

In reaching this conclusion, I also find the ESDC Agreement, like the other operating agreements, to be less than a model of clarity. For example, the agreement does not expressly address whether or not a stockholder could "retire" before sixty-two and retain his stock. In construing the agreement as a whole, I read the contract as equating a voluntary "retirement" before a stockholder's sixty-second birthday to a voluntary termination under Paragraph 5, requiring the stockholder to sell his stock to the company. Not only the agreement's language, but also the extrinsic evidence supports this interpretation. Gene's argument that a stockholder can retire before sixty-two and retain his stock in ESDC runs afoul of the brothers understanding that to own stock in the Julian Businesses one must work for the businesses. Under Gene's interpretation, a stockholder hypothetically in his forties could decide unilaterally to stop working for ESDC and any of the other Eastern States Group companies and yet continue to own stock in ESDC. I find that result would violate the intent of the Julian Brothers when they entered into the ESDC Agreement, and that Gene knew it would.

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[79] *See United Rentals, Inc.*, 937 A.2d at 835-36 (quoting *Seidensticker v. Gasparilla Inn, Inc.*, 2007 WL 4054473, at *1 (Del. Ch. Nov. 8, 2007)) (stating where an examination of extrinsic evidence does not lead to an obvious, objectively reasonable conclusion, the Court may employ the forthright negotiator principle and consider "the evidence of what one party *subjectively* 'believed the obligation to be, coupled with evidence that the other party knew or should have known of such belief.'").

There is no dispute Gene ceased to be employed by any company in the Eastern States Group as of December 31, 2005.[80] Thus, I hold Gene was required to sell his stock in ESDC to the company promptly after that date.

**4. Waiver**

Gene argues Francis and Richard waived their right to demand the resale of his stock in ESCS and Benchmark. According to Gene, when Francis and Richard forced him out of ESCS and Benchmark, they did not attempt to enforce any specific buy-back provisions in the shareholder agreements and should be estopped from doing so now. Gene asserts he was terminated from any active role in ESCS in October 2000, and that between then and December 2005 neither Francis nor Richard attempted to acquire his ESCS stock. Similarly, Gene contends he was removed as a director and officer of Benchmark in 2003, ending any work he did for that company. Further, Gene disputes Francis and Richard's argument that so long as he continued to work for ESDC, he could retain his stock in ESCS and Benchmark. According to Gene, Francis and Richard incorrectly base that argument on language in the Employee Agreements and the ESDC Agreement that refers, respectively, to employment with ESCS or an affiliate and with

[80] It is not clear whether Gene bases his argument for maintaining his ESDC stock on his not having been in the "employment" of ESDC within the meaning of the ESDC Agreement. To the extent Gene does make that argument, I reject it as unconvincing. The agreement indicates the parties proceeded on the premise that stockholders such as Gene and his brothers were "employed" by ESDC or another member of the Eastern States Group at the time they signed both the original ESDC Agreement and the First Amendment.

the Eastern States Group. Similar cross-employment language does not appear, however, in the ESCS or Benchmark Agreements.

Francis and Richard respond that Gene has failed to meet the exacting standards for proving waiver. First, they argue that until December 31, 2005, Gene still played roles in both ESCS and Benchmark. Regarding ESCS, while Gene was removed as President in 2001, he was elected Vice President at the same time. Therefore, although Gene was no longer involved in the day-to-day management of ESCS, Francis and Richard allege ESCS still consulted Gene and that Gene retained check writing authority and executed signature cards for ESCS's Wilmington Trust Account. Further, Francis and Richard assert that despite Gene's removal as an officer of Benchmark in April 2003 and lack of any formal association with the company thereafter, Benchmark still consulted Gene occasionally.

Moreover, Francis and Richard allege the parties all understood that so long as a stockholder was working for one of the Julian Businesses, he could retain his stock in all of the entities, but once the stockholder no longer worked for any of the Julian Businesses, he or she had to sell their stock back to the respective companies. To support their position, Francis and Richard point to the ESDC Agreement, which expressly contains such a provision, noting Gene admitted at trial that the ESDC Agreement was a further refinement of the earlier shareholder agreements. Francis and Richard also cite to the example of Rex Gibson, an employee who worked for ESCS, obtained shares in ESCS, and retained those shares when he left ESCS to work solely for ESDC.

Under Delaware law, "[a] contractual requirement or condition may be waived where (1) there is a requirement or condition to be waived, (2) the waiving party must know of the requirement or condition, and (3) the waiving party must intend to waive the requirement or condition."[81] Gene bears the burden of proving the existence of those elements.

**a. The cross-employment argument**

Francis and Richard purportedly understood that a Principal Stockholder in ESCS or Benchmark did not have to sell his stock in that entity until he ceased to be employed by any of the Julian Businesses. Because that circumstance applies to both ESCS and Benchmark, I initially address the merits of Francis and Richard's alleged understanding. I then address whether such a subjective belief, if plainly mistaken, would negate Gene's claim of waiver.

There is no question the Julian Brothers could have written the ESCS and Benchmark Agreements to include the concept that so long as a stockholder works for one of the Julian Businesses, he could retain his stock in all of the companies. The fact is, however, they did not include language to that effect. The absence of any cross-employment language is striking, given the brothers used such language in other contemporaneous agreements, suggesting they intentionally left it out of the ESCS and Benchmark Agreements. For example, the Julian Brothers, at various times from 1986 through 2001, entered into several Employee Agreements that contained cross-

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[81] *AeroGlobal Capital Mgmt., LLC v. Cirrus Indus., Inc.*, 871 A.2d 428, 444 (Del. 2005).

employment language.[82] Specifically, the Employee Agreements provided for the resale of stock upon termination of "employment of a minority Shareholder employee with the corporation or with a corporation affiliated with the corporation."[83] Additionally, the initial 1985 ESCS Agreement contained identical cross-employment language, not found in the current 1991 ESCS Agreement.[84] Further, the ESDC Agreement, which all Julian Brothers acknowledge is a further refinement of their earlier shareholder agreements, expressly provides that, with the exception of Janis Julian, stock in ESDC could only be held by individuals who continued to be employed by "a member of the Eastern States Group" -- *i.e.*, Benchmark, ESCS, ESDC, Eastern States Leasing, L.L.C., or Sentinel Self Storage L.L.C.[85] The operative ESCS and Benchmark Agreements, however, do not include any such language. Rather, the agreements provide for the resale of stock "[i]f the employment of an employee with the corporation is terminated . . . ."[86] Therefore, I reject the argument that so long as Gene worked for one of the other Julian Businesses he had a contractual right to retain his stock in ESCS and Benchmark. To the extent Francis

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82 JX 1, several ESCS Stockholder Employee Agreements. Indeed, Rex Gibson entered into one of these agreements with cross-employment language. This explains why he could leave ESCS to work for ESDC and still hold his ESCS stock. Similar cross-employment language, however, is not included in either the ESCS or Benchmark Agreements.

83 Although even this language is not a model of clarity, the parties seem to agree that it should be read to mean a stockholder is under no obligation to sell stock so long as he continues to be employed by at least one Julian company.

84 *See* JX 2.

85 *See* JX 5 ¶¶ 1, 4.

86 *See* JX 3 Art. 4.

and Richard attempt to rebut Gene's waiver argument by contending they acted on the premise that cross-employment was sufficient, their argument is unpersuasive.[87]

**b. Was there a waiver as to ESCS?**

Turning to waiver regarding Gene's ESCS stock, I look to the extent and duration of Gene's role in ESCS. Beginning in 1985, Gene served as President of ESCS. On October 12, 2000, however, the ESCS board removed Gene as President, demoting him to Vice President. As Francis and Richard stripped away Gene's responsibilities in ESCS, Gene's relationship with his brothers soured. In November 2001, Gene moved out of the building ESCS occupied, and as of August 19, 2002, he stopped attending ESCS board meetings. Although Gene's involvement with ESCS waned over the years, he retained check writing authority. Further, Gene continued to serve as both an officer and a director of ESCS, and receive his *pro rata* share of ESCS stock distributions, until his resignation on December 31, 2005.

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87 The parties did not address whether waiver examines a party's intent from an objective or subjective perspective. For purposes of this dispute, the issue is immaterial. Based on the facts of this case, I find Francis and Richard's claimed reliance on a cross-employment theory to be objectively unreasonable. Further, as discussed *infra*, I find Francis did not subjectively hold this belief. Rather, he acknowledged that in April 2003, when Gene left Benchmark, Benchmark at least arguably had a basis to insist upon the reacquisition of Gene's Benchmark stock. At that time, however, Gene was still "employed" by ESDC and ESCS. Therefore, I find that even if Francis and Richard subjectively held the belief that as long as a shareholder worked for one of the Julian Businesses, he could retain his stock in all of the companies, they also knew that belief was subject to question in terms of the ESCS and Benchmark Agreements and chose to ignore that problem.

To demonstrate Francis and Richard waived their ability to require Gene to sell his shares in ESCS back to the company, Gene would have to show that there was a requirement he sell his shares back before December 2005, Francis and Richard knew of that requirement, and they intentionally waived it. Although Gene's role in ESCS greatly diminished in the period after October 2000, when he ceased being its President, he continued to be an officer and director and have check writing authority until he resigned in 2005. In these circumstances, Gene has not shown that his employment with ESCS terminated before December 2005. Moreover, even if it did in a legal sense, Francis and Richard reasonably could have believed otherwise. Indeed, Gene's December 2005 letter in which he resigned as an officer and director of ESCS supports an inference that he continued to be employed by the company up until that time. Therefore, I conclude that Gene has not proven Francis or Richard waived their right to demand that Gene sell his ESCS stock back to the company as of December 31, 2005.

**c. Was there a waiver as to Benchmark?**

Next, similar to the ESCS waiver analysis, the possibility of a waiver as to Benchmark largely turns on Gene's role at Benchmark. On April 22, 2003, the Benchmark board removed Gene as a director. In addition, the board resolved that Gene would not be considered for re-election as an officer at the next board meeting in October.[88] Thus, by the end of 2003, Gene no longer had a formal relationship with Benchmark other than as a stockholder. Francis and Richard allege, however, that

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[88] JX 19, Minutes of the Benchmark Board of Directors, 4/22/03.

Benchmark continued to consult Gene from time to time. The record contains no details of that activity, however. Further, even assuming the truth of the consulting allegations, under my construction of the Benchmark Agreement, that kind of informal, unstructured relationship would not fall within the concept of "employment," as used in the Benchmark Agreement. Thus, by the end of 2003, Gene's employment with Benchmark had terminated and Benchmark had the right to demand the reacquisition of Gene's Benchmark shares.

Additionally, the evidence shows Benchmark knew of, and intentionally chose not to enforce, this right. For example, on cross-examination, Francis acknowledged that in April 2003, Benchmark decided not to exercise its right to demand the buy-back of Gene's stock:

> Q: Now, the reason you did not ask for Mr. [Gene] Julian's Benchmark stock at that point [April 2003] is because you wanted to carry out what you understand was the general intention of the three of you: that so long as you were working in the Eastern States group that you could retain your stock in any of the companies in that group; correct?
>
> A: Yes.
>
> Q: And also you thought that by not asking him for his stock that you would continue to "make good relations." Isn't that what you testified to?
>
> A: Yes.
>
> Q: And so you understood that, to the extent that the Benchmark Builders' agreement could be read to provide for the mandatory sale of a terminated person's stock, you decided not to enforce that agreement. Isn't that fair?
>
> A: We decided to keep Gene as a stockholder - - I said – because I didn't want to get into more lawsuits. Okay?

> Whatever. I said I don't want another argument. It's easy to leave the guy in. Okay? We're part of a group. We're all working together. I said, "What do I gain if we get rid of him? Nothing."[89]

Based on the evidence, I find Benchmark knew it had at least an arguable basis to insist upon the reacquisition of Gene's Benchmark stock as of the end of 2003 and intentionally chose not to enforce that right. If Benchmark had attempted to force Gene to sell back his Benchmark stock in 2003, the subsequent events regarding ESCS and ESDC might not have transpired as they did. In any event, I hold that Benchmark, Francis, and Richard waived the right to insist upon the resale of Gene's stock upon his termination from the company by failing to enforce that claimed right in a timely fashion.

**B. Benchmark Bonuses**

Gene asserts that the Benchmark Bonuses represent self-interested transactions, and therefore Defendants must establish that the bonuses were entirely fair. According to Gene, the Benchmark Bonuses resulted from unfair dealing and reflect an unfair price. Regarding fair dealing, Gene questions the timing of the bonuses, noting Defendants approved them shortly after Gene resigned from ESCS and ESDC, and most of the bonuses were paid shortly before the end of 2005, thereby intentionally causing a reduction in Benchmark's net asset value (the metric to be used for the purchase price of Gene's stock). Gene criticizes the process used as involving three interested directors of Benchmark who approved self-compensation, without any independent protections. According to Gene, Francis dominated the process and Richard and Bomberger went

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[89] T. Tr. at 252-53.

along, spending no more than half an hour considering the bonuses and failing to seek any review by an independent consultant or other disinterested person before approving them. Finally, Gene contends the amount of the Benchmark Bonuses, $1.3 million, was unfair and not commensurate with past practices of the Julian Businesses. In terms of relief, Gene seeks damages for the alleged breach of fiduciary duty, including disgorgement by Francis, Richard, and Bomberger of the bonuses they received and reimbursement for his attorneys' fees.

Francis and Richard respond by defending the entire fairness of the Benchmark Bonuses. They stress that the Julian Businesses are family run companies with three to four member boards of directors and very few shareholders. The length and nature of the December 20, 2005 Benchmark board meeting at issue matched the procedures attendant to other Benchmark director actions. Thus, Defendants contend the Benchmark Bonuses resulted from fair dealing. Additionally, according to Francis and Richard, the amount or "price" of the bonuses, given the circumstances, was historically comparable and fair.[90]

Bomberger also defends the Benchmark Bonuses as entirely fair. In particular, Bomberger denies having breached his fiduciary duty when he voted in favor of those bonuses. Bomberger argues that as one of three directors his vote was not necessary to authorize the $1 million paid to Eastern States Management Group. According to

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[90] Francis and Richard also raise an unclean hands defense, alleging Gene arranged for another of the Julian Businesses to pay him disproportionate compensation in 2003. The evidence indicates that purportedly unequal treatment was rectified in the compensation paid to Francis and Richard the following year. JX 36. In any event, Defendants failed to prove any basis for applying the defense of unclean hands to bar Gene's challenge to the Benchmark Bonuses.

Bomberger, he had not discussed the prospect of paying any bonuses before the December 20 meeting. Additionally, Bomberger contends that after the meeting he confirmed that the Julian Businesses had paid similar bonuses in the past. Moreover, Bomberger relies on an expert, Trey Stevens, who testified Bomberger's bonus was fair and comported with the "Independent Investor Test."[91]

Self-interested directorial compensation decisions made without independent protections, like other interested transactions, are subject to entire fairness review.[92] Directors of a Delaware corporation who stand on both sides of a transaction have "the burden of establishing its entire fairness, sufficient to pass the test of careful scrutiny by the courts."[93] They "are required to demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain."[94] The two components of entire fairness are fair dealing and fair price. Fair dealing "embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained."[95] Fair price "assures the

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[91] In summary, under the Independent Investor Test Stevens referred to, if the managers of a business produce economic income that exceeds the amount necessary to provide a fair return to shareholders and to compensate management for their labor, all excess profits may be allocated to management as a reward for their superior performance. JX 26, Expert Report of Trey Stevens, 7/17/07, at 11.

[92] *Valeant Pharms. Int'l v. Jerney*, 921 A.2d 732, 745 (Del. Ch. 2007).

[93] *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983).

[94] *Id.*

[95] *Id.* at 711.

transaction was substantively fair by examining 'the economic and financial considerations.'"[96]

The two aspects of entire fairness are not independent. Rather, "the fair dealing prong informs the court as to the fairness of the price obtained through the process. The court does not focus on the components individually, but determines the entire fairness based on all aspects of the entire transaction."[97]

The circumstances of the Benchmark Bonuses give rise to suspicion about their fairness. Eleven days after Gene submitted his letter of retirement and resignation from ESDC and ESCS, the Benchmark board approved the Benchmark Bonuses. Francis initiated the process just days after Gene's notice of retirement. He approached Richard before the December 20, 2005 board meeting and proposed making the bonuses. The brothers discussed the concept for fifteen minutes, and consulted no one else. Francis and Richard concede that they knew any bonus would decrease the net book value of Benchmark, consequently decreasing the value of the shares they contemporaneously were trying to force Gene to sell back.

The size of the bonuses, given their historical context, also raises questions. Before the December 20, 2005 meeting, the Benchmark board had not approved bonuses near the magnitude of $1.3 million. While the record is imperfect, it suggests Benchmark paid no bonuses from 1996 through 1998. From 1999 through 2004, Benchmark's

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96 *Valeant Pharms.*, 921 A.2d at 746 (quoting *Weinberger*, 457 A.2d at 711).

97 *Id.*

bonuses as a percentage of adjusted income hovered between 3.30% and 3.36%. In contrast, the challenged 2005 bonuses constituted 22.28% of adjusted income. Additionally, 2005 marked the first time Bomberger received a bonus beyond the performance-based compensation set forth in his Employment Agreement.

I do not find credible Defendants' argument that the board approved the Benchmark Bonuses as a reward for a good year in 2005 or to reduce retained earnings in the event of a lawsuit. Regarding the reward for a good year, Benchmark had a better year in 2004 than 2005, and the bonuses in 2004 were still only 3.36% of adjusted income. Moreover, when asked about the discrepancy between the bonuses in 2004 and 2005, Richard responded:

> He [Gene] didn't leave, either [in 2004]. We were in shock when he left, to tell you the truth. . . . We were in shock. You know, here's somebody you sweat with and be successful with for 30 years -- 30-plus years -- gives you not as much notice as most of your good truck drivers give us when they decide to retire.[98]

In other words, more than anything else, the bonuses represented a knee-jerk reaction to Gene's precipitous retirement, which Francis and Richard considered a betrayal.

To summarize, the Benchmark Bonuses were the product of an unfair process. The record indicates no coherent, credible reason for the bonuses other than in reaction to Gene's retirement. Additionally, there was no notice, meaningful deliberation, or independent advice or research before the board's action. In fact, as to the Management Group Bonus, Bomberger had no clear idea what he was approving. In addition, the price

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[98] T. Tr. at 270.

was also unfair. There was no historical precedent for the size of the bonus. For example, Gene, who worked for the Eastern States Group through nearly all of 2005, received nothing.[99] Finally, I do not find Stevens' expert testimony persuasive. His "Independent Investor Test" is so subjective and unsupported by work of other experts in the relevant field, that I find it unreliable and unhelpful in the circumstances of this case. I also note Bomberger could not cite any Delaware law that has adopted or supported Stevens' theory. Therefore, I conclude Francis, Richard, and Bomberger failed to demonstrate the Benchmark Bonuses were entirely fair and breached their fiduciary duty of loyalty to Benchmark when they approved them.[100]

When a transaction does not meet the entire fairness standard, the Court of Chancery may fashion any form of equitable and monetary relief as may be appropriate.[101] Disgorgement is one such form of relief.[102] In this case, Francis, Richard,

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[99] By 2005, the Julian Brothers had created a common family paymaster, Eastern States Management Group. At the close of each year, the different Julian Businesses would contribute money to Eastern States Management Group which, in turn, would make distributions to the brothers. The Julian Brothers chose this system, knowing specific businesses would contribute more or less in a given year, but overall it would balance out, stabilizing the flow of distributions.

[100] In making a business decision, Delaware law presumes "'the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company.'" *See, e.g.*, *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 52 (Del. 2006) (quoting *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984)). Bomberger's individual defenses that his vote was not necessary to approve the bonuses and that he did not discuss the bonuses before the meeting, do not excuse his approval of a plainly self-interested transaction. If anything, they work against him as evidence that he did not make a business decision in good faith on an informed basis.

[101] *Weinberger*, 457 A.2d at 714.

and Bomberger have no right to retain any of the Benchmark Bonuses. Therefore, I order Francis, Richard, and Bomberger to disgorge those bonuses and return the amounts they received with interest, to Benchmark. I also will order those Defendants to reimburse Gene for the reasonable attorneys' fees and costs he incurred in prosecuting the Benchmark Bonuses claim.[103]

### C. McMullen Square

Gene contends that as a result of this litigation, Defendants returned the McMullen Square property to ESDC. Gene therefore seeks to recover the attorneys' fees he incurred in producing that benefit. Francis and Richard respond that they had legitimate business reasons for the actions they took regarding the McMullen Square property. Francis and Richard also deny that the return of the McMullen Square property produced any benefit to ESDC, because they allege the project resulted in nothing but losses.

Generally, Delaware follows the American Rule and litigants must pay their own attorneys fees and costs.[104] Under the "mootness" exception to the general rule, a court may award attorneys' fees where the fee applicant demonstrates: "(1) the litigation was meritorious when filed, (2) the action rendering the litigation moot produced the same or a similar benefit sought by the litigation, and (3) there was a causal relationship between

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102 *Valeant Pharms.*, 921 A.2d at 752.

103 *See Carlson v. Hallinan*, 925 A.2d 506, 546-48 (Del. Ch. 2006).

104 *Dover Historical Soc'y, Inc. v. City of Dover Planning Comm'n*, 902 A.2d 1084, 1089 (Del. 2006).

the litigation and the action taken producing the benefit."[105] Further, Delaware law presumes a causal connection between the initiation of litigation and a later arising benefit in cases where the defendant's actions after the filing of the complaint render the claims asserted moot.[106]

In this case, both parties acknowledge Defendants returned the McMullen Square property to ESDC as a result of this litigation. Defendants also do not question the presumption that the litigation caused any resulting benefit. Rather, Defendants contend the return of the McMullen Square property to ESDC did not provide a benefit to the company. Based on the evidence presented, I find Defendants' argument unconvincing. The evidence supports a reasonable inference that the return of the McMullen Square property produced at least some benefit to ESDC. Thus, I will award Gene his reasonable attorneys' fees associated with the McMullen Square property claim. I expect, however, that these fees will be relatively minor.[107]

## IV. CONCLUSION

For the reasons stated, the Court makes the following rulings.

The Court has determined that Gene is entitled to continue as the owner of his Benchmark shares, and that Defendants Francis, Richard, and ESCS are entitled to a

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[105] *Id.* at 1092.

[106] *United Vanguard Fund, Inc. v. TakeCare, Inc.*, 693 A.2d 1076, 1080 (Del. 1997).

[107] Indeed, Gene's counsel represented at argument that the attorneys' fees are less than five figures. PT Tr. at 7.

declaratory judgment that Gene must sell his stock in ESCS and ESDC back to each of those companies.[108]

As to the claims regarding the Benchmark Bonuses, the Court has concluded that Francis, Richard, and Bomberger have breached their fiduciary duties in approving and accepting those bonuses. To remedy that breach, the Court will require Francis, Richard, and Bomberger (1) to disgorge the total of $1.3 million in Benchmark Bonuses they received and return that money to Benchmark with interest at the legal rate, compounded quarterly, and (2) to reimburse Gene for his reasonable attorneys' fees and costs incurred in the prosecution of the Benchmark Bonuses claim.

The Court also will require Francis and Richard to reimburse Gene for his reasonable attorneys' fees and costs incurred in prosecuting his claim for the return of the McMullen Square property to ESDC.

In all other respects, I deny the claims of Gene and the counterclaims of Francis and Richard, and those claims will be dismissed with prejudice. Except for any costs associated with the claims regarding the Benchmark Bonuses and the return of the McMullen Square property payable to Gene, each party shall bear its own costs under Court of Chancery Rule 54(d).

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[108] Some limited additional proceedings may be necessary to reduce these rulings to a final judgment in terms of, for example, the precise value of the stock to be resold. I would expect the ESCS and ESDC shares to be valued as of December 31, 2005, and that value to be converted to a present value as of the date of judgment based on the interest rate prescribed in the 1991 ESCS Agreement of 8% for Gene's ESCS stock and in the First Amendment to the ESDC Agreement of "the prime rate of interest then charged by banks in Wilmington, Delaware" for Gene's ESDC stock.

Plaintiff's counsel shall prepare and circulate for comment an appropriate form of order to implement these rulings and submit it, on notice, within fourteen days of the date of this opinion.