IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

MARYLYNN HARTSEL and DEANNA PARKER, individually, derivatively and on behalf of all others similarly situated, Plaintiffs, - against - THE VANGUARD GROUP, INC., GEORGE U. SAUTER, DUANE F. KELLY, JOHN J. BRENNAN, CHARLES D. ELLIS, RAJIV L. GUPTA, AMY GUTMANN, JOANN HEFFERNAN HEISEN, ANDRÉ F. PEROLD, ALFRED M. RANKIN, JR., and J. LAWRENCE WILSON; ACADIAN ASSET MANAGEMENT, LLC, RONALD D. FRASHURE, JOHN R. CHISHOLM, and BRIAN K. WOLAHAN; MARATHON ASSET MANAGEMENT, LLP, and NEIL M. OSTRER, Defendants, - and - VANGUARD INTERNATIONAL EQUITY INDEX FUNDS, d/b/a VANGUARD EUROPEAN STOCK INDEX FUND, and VANGUARD HORIZON FUNDS, d/b/a VANGUARD GLOBAL EQUITY FUND Nominal Defendants.	C.A. NO. 5394-VCP

MEMORANDUM OPINION

Submitted: February 9, 2011
Decided: June 15, 2011

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PARSONS, Vice Chancellor.

This case involves a stockholder challenge to the decision of two funds within the Vanguard mutual fund complex to purchase shares of allegedly illegal foreign online gambling businesses that are publicly traded in overseas capital markets. The plaintiffs allege that various defendants, including the board of trustees overseeing the two Vanguard Delaware statutory trusts whose funds purchased such shares, as well as various financial advisory firms that serviced the funds and certain of their employees, conspired to cause the funds at issue to purchase and hold the challenged securities in violation of 18 U.S.C. § 1955, which makes it a crime to "own" any part of an illegal gambling business. The plaintiffs further allege that, despite indications by the mid 2000s that U.S. law enforcement and regulatory agencies would begin to crack down on foreign online gambling businesses that targeted U.S. citizens, the defendants failed to cause the relevant mutual funds to sell the challenged securities. As a result of the step up in enforcement actions, according to the plaintiffs, the value of the shares held by the mutual funds dropped precipitously in recent years, thereby causing the funds and their stockholders to lose millions of dollars.

The plaintiffs' complaint asserts both derivative and direct claims based on their allegations that the defendants' actions constituted a violation of their fiduciary duties, negligence, and waste. All of the many defendants in this action have moved to dismiss the complaint on the grounds that: (1) this Court may not assert personal jurisdiction over the individual defendants named in the complaint; (2) all of the plaintiffs' claims are derivative in nature and, therefore, the complaint must be dismissed for the plaintiffs'

failure to make demand on the board of trustees or demonstrate why a demand would be futile; and (3) the complaint fails to state a claim.

For the reasons discussed in this Opinion, I grant the defendants' motions and dismiss with prejudice all of the claims in the complaint based on the first two grounds stated above. Consequently, I do not address Defendants' additional argument that the complaint fails to state a claim.

I. BACKGROUND

A. The Parties

Plaintiffs, Marylynn Hartsel and Deanna Parker, are stockholders of certain funds offered by Vanguard Horizon Funds ("VHF") and Vanguard International Equity Index Funds ("VIEIF"), respectively.[1] As discussed in greater detail below, they purport to bring this action against the various Defendants in both direct and derivative manners.

For the sake of clarity, I introduce the numerous defendants in this action by summarizing the basic structure of the mutual fund complex involved.[2] I begin with the two nominal defendants: VHF and VIEIF are Delaware statutory trusts based in Wayne, Pennsylvania, which are registered under the Investment Company Act of 1940 (the "ICA")[3] as open-ended investment management companies. Each of these trusts contains

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1 Verified Compl. (the "Complaint") ¶¶ 17-20. Unless otherwise noted, all facts recited in this Opinion are drawn from the Complaint and accepted as true for purposes of Defendants' motions to dismiss.

2 I refer to VHF and VIEIF as "Nominal Defendants." At times, I refer to the remaining Defendants collectively as "Defendants" but differentiate among them when necessary.

3 15. U.S.C. § 80a-1-64.

multiple mutual funds, for each of which a separate class of stock is offered to public investors. VHF, for example, offers four different series of shares representing four different mutual funds, one of which is the Vanguard Global Equity Fund ("Vanguard Global"). Similarly, VIEIF offers six different mutual funds, including the Vanguard European Stock Index ("Vanguard European") (together with Vanguard Global, the "Affected Funds" or "Funds"). Importantly, the different mutual funds held by Nominal Defendants are not separate legal entities; rather, they are separate mutual funds which form part of a series of mutual funds held by each Nominal Defendant. As such, investors in each of the mutual funds within a specific Nominal Defendant hold different series of shares in the same legal entity.[4] Indeed, the purpose of the trust structure of Nominal Defendants is to serve as an "umbrella" entity that registers as an investment company with the SEC so that each mutual fund within the trust can enjoy its trust's registration and avoid the costs and burdens of separately registering.

Nominal Defendants are part of a larger mutual fund complex in which there are thirty-four other separate registered investment companies like them (the "Vanguard

[4] As discussed in the Complaint, each Nominal Defendant contains separate mutual fund series, with each series representing a different portfolio of securities. Compl. ¶ 25. Each portfolio represents a single "mutual fund," which has distinct investment objectives, policies, and risks. By investing in a single portfolio of VHF, for example, a stockholder does not participate in the investment results of any other mutual fund within VHF and must look solely to the assets of its mutual fund for earnings and the like. Therefore, each mutual fund represents a different group of stockholders of VHF with an interest in only one portfolio of securities among the several portfolios managed by VHF. *Id.*

Complex").[5] Each such entity has a board of trustees, which oversees that trust or investment company's series of funds. Defendants John J. Brennan, Charles D. Ellis, Rajiv L. Gupta, Amy Guttman, JoAnn Heffernan Heisen, Andre F. Perold, Alfred M. Rankin, Jr., and J. Lawrence Wilson (collectively, "Trustee Defendants" or "Trustees") were members of the Board of Trustees of both VHF and VIEIF (the "Board of Trustees" or the "Board") at times relevant to this action.[6] In fact, the thirty-six investment companies within the Vanguard Complex all share a single board of trustees.

Defendant the Vanguard Group, Inc. ("Vanguard") is an investment management company organized under the laws of and headquartered in Pennsylvania. It is owned by the investment companies it manages and, importantly, the same board of trustees that oversees each separate mutual fund series in the Vanguard Complex also serves as Vanguard's board of directors. Vanguard serves as an investment adviser to approximately thirty-six investment companies, including VHF and VIEIF.[7] As such,

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5 The thirty-six entities in the Vanguard Complex offer approximately 130 separate mutual fund series.

6 Plaintiffs assert that the Trustee Defendants served in that capacity when the Affected Funds invested in the gambling businesses described below. Compl. ¶ 151. They further allege, on information and belief, that Brennan and Wilson no longer serve on the Board of each Nominal Defendant, but that the remaining six Trustee Defendants still constitute a majority of the Board, which now includes four additional nonparty Trustees. *Id.* ¶ 47.

7 In particular, Vanguard provides corporate management, administrative, marketing, and distribution services. As it explains, for example, "[i]nvestment advisors [like Vanguard] make the investment decisions for the Funds, subject to the supervision and oversight of . . . the Trustees." Op. Br. of Vanguard, Sauter, and Kelly ("VOB") 5. Similarly, I refer to Vanguard's reply brief as "VRB"; Plaintiffs' answering brief as "PAB"; Acadian, Frashure, Chisholm, Wolahan,

Vanguard provided certain advisory services to Nominal Defendants' mutual fund series, including Vanguard Global and Vanguard European. Specifically, it provided such services to Vanguard Global through one of Vanguard's principals, Defendant Duane F. Kelly, who Plaintiffs allege exercised operational or managerial oversight over that fund. Plaintiffs further allege on information or belief that Kelly also had operational or managerial responsibility for implementing Vanguard Global's challenged investment strategy. Vanguard offered such services to Vanguard European through its Quantitative Equity Group ("VQEG") division. Specifically, Defendant George U. Sauter (together with Kelly, the "Vanguard Individual Defendants"), VQEG's chief investment officer as well as a managing director of Vanguard and chief investment officer of other Vanguard mutual funds, oversaw VQEG's management of Vanguard European. According to Plaintiffs, Sauter was responsible for developing the Affected Funds' challenged investment strategies. In addition, Plaintiffs allege that Kelly was responsible for the day-to-day management of Vanguard European and its implementation of Sauter's investment strategy.

Besides Kelly, two additional Defendant-entities and certain of their employees provided investment advisory services to Vanguard Global. At all relevant times, Defendant Acadian Asset Management, LLC ("Acadian") exercised managerial or operational oversight concerning Vanguard Global's investment strategy. Acadian is a

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Marathon, and Ostrer's opening and reply briefs as "AOB" and "ARB," respectively; and the Trustee Defendants' opening and reply briefs as "TOB" and "TRB," respectively.

Delaware LLC with its principal place of business in Boston, Massachusetts. Defendants Ronald D. Frashure, John R. Chisholm, and Brian K. Wolahan allegedly are Acadian portfolio managers who were responsible for Vanguard Global's complained-of investment strategy (the "Acadian Individual Defendants").[8]

Defendant Marathon Asset Management, LLP ("Marathon") is an investment advisory firm organized under the laws of the United Kingdom, which maintains an office in Mt. Kisco, New York. According to Plaintiffs, Marathon also provided investment advisory services to Vanguard Global and exercised managerial or operational control over its investments beginning around April 2006. Plaintiffs allege that, like his counterparts at Acadian, Defendant Neil M. Ostrer, a Marathon portfolio manager, was responsible for implementing certain of Vanguard Global's complained-of investment decisions.[9]

B. Facts

1. 18 U.S.C. § 1955

At the heart of Plaintiffs' Complaint is 18 U.S.C. § 1955 ("§ 1955"), which, among other things, prohibits a person or entity from owning all or part of an "illegal

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[8] According to affidavits filed contemporaneously with Defendants' motions to dismiss, Frashure is the president and chief executive officer, Chisholm is an executive vice president and chief investment officer, and Wolahan is a senior vice president and co-director of alternative strategies at Acadian. *See* Aff. of Ronald D. Frashure ("Frashure Aff.") ¶ 3; Aff. of John R. Chisholm ("Chisholm Aff.") ¶ 3; Aff. of Brian K. Wolahan ("Wolahan Aff.") ¶ 3.

[9] I refer to the nonentity Defendants, Frashure, Chisholm, Wolahan, Ostrer, Sauter, and Kelly, as "Individual Defendants."

gambling business."[10] In relevant part, § 1955 states that "[w]hoever conducts, finances, manages, supervises, directs, or *owns* all or part of an illegal gambling business shall be fined under this title or imprisoned not more than five years, or both."[11] The statute defines "illegal gambling business" as "a gambling business which[:] (i) is a violation of the law of a State or political subdivision in which it is conducted; (ii) involves five or more persons who conduct, finance, manage, supervise, direct, or own all or part of such business; and (iii) has been or remains in substantially continuous operation for a period in excess of thirty days or has a gross revenue of $2,000 in any single day."[12] It further defines "gambling" as acts including, but not limited to, "pool-selling, bookmaking, maintaining slot machines, roulette wheels or dice tables, and conducting lotteries, policy, bolita or numbers games, or selling chances therein."[13]

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10 *See* 18 U.S.C. § 1955. The Complaint further asserts that a violation of § 1955 constitutes a predicate crime under the Federal Racketeer Influenced and Corrupt Organizations Act ("RICO") and, thus, amounts to "racketeering activity." Compl. ¶¶ 12, 59; *see also* 18 U.S.C. § 1961(1)(B).

11 18 U.S.C. § 1955(a) (emphasis added).

12 *See id*. § 1955(b)(1). "State" is defined as any "State of the United States, the District of Columbia, the Commonwealth of Puerto Rico, and any territory or possession of the United States." *Id*. § 1955(b)(3).

13 *Id*. § 1955(b)(2). Section 1955 does not criminalize, however, "any bingo game, lottery, or similar game of chance conducted by an organization exempt from tax under paragraph (3) of subsection (c) of section 501 of the Internal Revenue Code of 1986, as amended, if no part of the gross receipts derived from such activity inures to the benefit of any private shareholder, member, or employee of such organization except as compensation for actual expenses incurred by him in the conduct of such activity." *Id*. § 1955(e).

2. The Affected Funds invest in the Gambling Enterprises

Plaintiffs' chief contention is that various Defendants, as fiduciaries responsible for managing and advising the Vanguard Funds, knowingly caused the Affected Funds to purchase shares of four allegedly illegal off-shore internet gambling businesses that accepted and processed wagers from U.S. citizens (the "Challenged Securities").[14] Specifically, Plaintiffs contend that the following businesses are "illegal gambling businesses" under § 1955: (1) Sportingbet PLC ("Sportingbet"); (2) PartyGaming PLC ("PartyGaming"); (3) Bwin Interactive Entertainment AG ("Bwin"); and (4)NETeller PLC ("NETeller") (collectively, the "Gambling Enterprises").[15]

As is discussed further below, Plaintiffs argue that Defendants caused Nominal Defendants, VHF and VIEIF, through their respective Affected Funds, to violate § 1955 and breach their fiduciary duties by purchasing and continuing to own shares in the Gambling Enterprises. Plaintiffs further allege that Defendants took these actions despite being aware of the illegality of their investments.

Next, I briefly summarize the details of the Affected Funds' purchases of the Challenged Securities.

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[14] The Complaint alleges that when Defendants made or caused to be made the investments at issue, they knew or were reckless in not knowing that U.S. law enforcement agencies considered off-shore gambling businesses that were taking or processing bets from U.S. gamblers to be illegal gambling businesses under § 1955 and certain states' laws. Compl. ¶¶ 73, 81, 83-86.

[15] To support their assertion that U.S. authorities considered the Gambling Enterprises' operations illegal, Plaintiffs cite a public letter from the Department of Justice, media reports, and filings by certain of the Enterprises. They also contend that these gambling entities derive substantial revenue from gambling operations involving individuals in U.S. markets.

a. Sportingbet

During the period from April 1, 2006 until at least November 1, 2006, VIEIF, through the Vanguard European fund, purchased millions of dollars worth of Sportingbet shares.[16] VIEIF purchased approximately 150,000 of these shares in the second quarter of 2006. It increased its Sportingbet holdings to over 974,082 by July 31, 2006 and purchased another 41,640 shares from August 1 to October 31 of that same year.

Similarly, from January 1, 2006 and until at least January 1, 2007, VHF, through the Vanguard Global fund, purchased incrementally 68,624 Sportingbet shares.

b. PartyGaming

Between May 1, 2006 and May 1, 2008, VIEIF, through the Vanguard European fund, purchased millions of dollars worth of PartyGaming shares.[17] VIEIF's annual report filed with the SEC on December 27, 2006, for example, disclosed that its holdings included approximately 281,089 PartyGaming shares it had acquired sometime after July 2006.

Similarly, VHF, through the Vanguard Global fund, purchased 607,500 shares of PartyGaming in 2006. In particular, Plaintiffs allege that Ostrer caused Vanguard Global to purchase PartyGaming shares in approximately seven trades between April and

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[16] Citing reports VIEIF filed with the SEC, Plaintiffs assert that VIEIF purchased approximately 1,015,722 shares of Sportingbet from April 1, 2006 to October 31, 2006.

[17] The Complaint cites an SEC filing, for example, in which VIEIF reported that it accumulated 3,018,542 shares of PartyGaming between May 1, 2006 and January 31, 2007.

December 2006. It continued to hold these securities until approximately the end of 2006.

c. Bwin

VIEIF, through the Vanguard European fund, purchased tens of thousands of shares of Bwin from April 1, 2006 through at least May 1, 2008.[18] Vanguard allegedly accumulated its Bwin shares incrementally, including a purchase of 10,287 shares in the months following July 2006.

d. NETeller

Finally, from July 1, 2005 until at least July 1, 2006, VHF, through the Vanguard Global fund, purchased 64,859 NETeller shares, allegedly in several separate transactions.

3. The U.S. heightens its law enforcement focus on internet gambling businesses

Plaintiffs allege that by mid-2006, authorities in the U.S. began to crackdown, so to speak, on internet gambling website companies which accepted wagers from U.S. bettors in violation of U.S. law. The number of criminal and civil prosecutions increased with regard to such entities. For example, a U.S. grand jury in Missouri indicted the London-based BetOnSports PLC ("BetOnSports"), an entity in which the Nominal Defendants did not invest, for racketeering, mail fraud, and running an illegal gambling enterprise based on its operations in U.S. markets. The same grand jury indicted BetOnSports's founder, CEO, and twelve others. Additionally, Sportingbet's chairman,

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[18] VIEIF reportedly acquired 70,600 Bwin shares between April 1, 2006 and January 31, 2007.

Peter Dicks, was arrested on a Louisiana state warrant on gambling-related charges. Moreover, federal prosecutors charged NETeller's founder, Stephen Lawrence, with conspiracy to violate certain gambling-related laws, including § 1955.[19] News of these prosecutions, and others, allegedly caused shares of such internet gambling businesses to decline in off-shore markets.

In another manifestation of this crackdown, Congress enacted the Unlawful Internet Gambling Enforcement Act of 2006 ("UIGEA") in October 2006.[20] This statute was designed, in part, to make it more difficult for internet gambling businesses to circumvent existing U.S. anti-gambling laws by making it unlawful to transfer funds to or from such entities.[21]

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19 NETeller also was charged with conspiracy and forfeited $136 million in criminal proceeds as part of a deferred prosecution agreement.

20 31 U.S.C. §§ 5361-67; *see also* Compl. ¶¶ 104, 114-15.

21 Specifically, 31 U.S.C. § 5363 provides that "[n]o person engaged in the business of betting or wagering may knowingly accept, in connection with the participation of another person in unlawful Internet gambling (1) credit, or the proceeds of credit, extended to or on behalf of such other person (including credit extended through the use of a credit card); (2) an electronic fund transfer, or funds transmitted by or through a money transmitting business, or the proceeds of an electronic fund transfer or money transmitting service, from or on behalf of such other person; (3) any check, draft, or similar instrument which is drawn by or on behalf of such other person and is drawn on or payable at or through any financial institution; or (4) the proceeds of any other form of financial transaction, as the Secretary and the Board of Governors of the Federal Reserve System may jointly prescribe by regulation, which involves a financial institution as a payor or financial intermediary on behalf of or for the benefit of such other person."

4. The Gambling Enterprises' share prices drop

The Complaint alleges that "[s]oon after passage of the [UIGEA], PartyGaming, Sportingbet, and Bwin withdrew from the U.S. market completely." This resulted in a precipitous decline in each of the Gambling Enterprises' share prices.[22] When Vanguard European and Vanguard Global first invested in PartyGaming, for example, its shares traded around $2.80, but by the time it withdrew its operations from U.S. markets its share price hovered around $.60, a drop of almost 80%.[23] Similarly, Sportingbet's shares traded around $7.30, but declined to around $3.16 per share after the BetOnSports indictments were announced in July 2006.[24]

Bwin, for its part, took an approximately $685 million impairment charge, based on the applicable exchange ratio, as a result of the increased U.S. law enforcement focus on its industry beginning in 2006. In addition, Bwin's share price, which hovered around $129 per share in May 2006, declined to about $17 by October 2006. Finally, the Complaint alleges that Vanguard Global's last valuation of its NETeller holdings before Lawrence was arrested "implied a per-share price of approximately $11."[25] But, Lawrence's arrest caused a suspension in trading of NETeller's shares and when trading

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22 All of the Gambling Enterprises are listed and traded on European exchanges; Sportingbet, PartyGaming, and NETeller are listed on the London Stock Exchange, and Bwin is listed on the Vienna Stock Exchange.

23 The share price figures averred in the Complaint represent figures calculated after converting foreign currency into U.S. dollars.

24 Sportingbet's share prices later fell even further.

25 Compl. ¶ 124.

resumed, those shares opened at $1.30. Plaintiffs aver that the value of the Gambling Enterprises' shares depended on their revenue streams derived from activities in the U.S. and, therefore, declined sharply after those Enterprises withdrew from U.S. markets.

5. The S.D.N.Y litigation

On August 29, 2008, Plaintiffs filed a substantially identical suit, *McBrearty v. Vanguard Group, Inc.*, against the present Defendants in the Federal District Court for the Southern District of New York ("S.D.N.Y.").[26] In *McBrearty*, Plaintiffs alleged that the same conduct challenged in this case gave rise to state law claims for breach of fiduciary duties, negligence, and waste, as well as for a RICO violation. On April 2, 2009, the court dismissed with prejudice Plaintiffs' RICO claim for lack of proximate causation and, as there was no federal claim left before the court, declined to exercise supplemental jurisdiction over their state law claim.[27] As such, the court dismissed the state claims without prejudice to re-filing in state court. On November 23, 2009, the Second Circuit affirmed the district court's decision.[28] On June 14, 2010, the Supreme Court denied certiorari.[29]

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[26] *McBrearty v. Vanguard Gp., Inc.*, 2009 WL 875220, at *1 (S.D.N.Y. Apr. 2, 2009), *aff'd*, 353 F. App'x 640 (2d Cir. 2009), *cert. denied*, 130 S. Ct. 3411 (2010).

[27] *Id*. at *4.

[28] *McBrearty v. Vanguard Gp., Inc.*, 353 F. App'x 640, 642 (2d Cir. 2009).

[29] *McBrearty v. Vanguard Gp., Inc.*, 130 S. Ct. 3411 (2010).

C. Procedural History

While the *McBrearty* petition for certiorari was pending, Plaintiffs filed their Complaint in this Court on April 7, 2010, alleging three derivative counts (Counts I-III) and two individual and class counts (Counts IV-V). Specifically, Count I asserts that Defendants breached their fiduciary duties by causing Nominal Defendants, through the Affected Funds, to invest in purportedly illegal gambling businesses. Counts II and III accuse Defendants of negligence and waste, respectively, based on the same conduct. Counts IV and V parallel Counts I and II, respectively, but are brought by Plaintiffs individually and on behalf of "a Class of investors in any of the [Affected] Funds who purchased one or more shares in the [Affected] Funds during the Class Period."[30]

On July 30, 2010, all Defendants moved to dismiss the Complaint.[31] After extensive briefing, I heard argument on those motions on February 9, 2011 (the "Argument"). This Opinion constitutes my ruling on Defendants' motions.

D. Parties' Contentions

Defendants raise a myriad of deficiencies with Plaintiffs' Complaint, which fall within three principal categories. First, Defendants Frashure, Chisholm, Wolahan, Ostrer, Sauter, and Kelly contend that there is no basis for this Court to exercise *in personam* jurisdiction over them, either under the Delaware long-arm statute or the Due

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30 Compl. ¶ 169.

31 Defendants filed three separate motions and three separate sets of opening and reply briefs. They joined in and incorporated by reference in their individual filings, however, portions of each other's submissions. *See, e.g.*, TOB 2 n.1; AOB 18; VOB 10.

Process Clause of the Fourteenth Amendment. Next, Defendants assert that all of Plaintiffs' claims are derivative, rather than direct, and, thus, should be dismissed under Rule 23.1 because Plaintiffs were required to, but did not, make a demand on the Board of Trustees. In particular, Defendants aver that Plaintiffs failed to plead particularized facts demonstrating that demand would have been futile. Finally, Defendants argue that the Complaint fails to state a claim on the merits for breach of fiduciary duty, negligence, or waste.

Plaintiffs strenuously dispute virtually all aspects of Defendants' motions to dismiss. I address Defendants' primary arguments and Plaintiffs' counterpoints in the next section.

II. ANALYSIS

A. Defendants' Motions for Dismissal Based on Lack of Personal Jurisdiction over the Individual Defendants

Individual Defendants, all of whom are nonresidents of Delaware, object to this Court's exercise of personal jurisdiction over them, arguing that there is no basis for such jurisdiction under Delaware's long-arm statute, any other statute, or the Due Process Clause of the Fourteenth Amendment.[32] Plaintiffs disagree and argue that all Individual Defendants are subject to jurisdiction under various subsections of the long-arm statute, as well as a conspiracy theory of jurisdiction. In addition, they argue that Frashure, Chisholm, and Wolahan have consented to jurisdiction under 6 *Del. C.* § 18-109(a).

[32] Trustee Defendants, Vanguard, Acadian, and Marathon do not contest personal jurisdiction.

Finally, Plaintiffs contend that this Court's assertion of jurisdiction over the Individual Defendants comports with the Due Process Clause.

1. The applicable standard

Before considering the merits of Defendants' motion to dismiss under Rule 12(b)(6), the Court first must address the Individual Defendants' motions to dismiss for lack of personal jurisdiction under Rule 12(b)(2).[33] This Court applies a two-step analysis to determine whether the exercise of personal jurisdiction over a nonresident defendant is appropriate.[34] First, the Court must determine whether there is a basis for personal jurisdiction under Delaware statutory law, specifically, the Delaware long-arm statute.[35] And second, if a statutory basis for jurisdiction exists, the Court must determine "whether subjecting the nonresident to jurisdiction in Delaware violates the Due Process Clause of the Fourteenth Amendment."[36]

The plaintiff has the burden to offer affirmative proof that these two steps are satisfied as to each defendant.[37] Specifically, when a motion under Rule 12(b)(2) is

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33 *See, e.g.*, *Branson v. Exide Elecs. Corp.*, 625 A.2d 267, 269 (Del. 1993); *Werner v. Miller Tech. Mgmt., L.P.*, 831 A.2d 318, 327 (Del. Ch. 2003).

34 *See, e.g.*, *Maloney-Refaie v. Bridge at Sch., Inc.*, 958 A.2d 871, 877-78 (Del. Ch. 2008); *Fisk Ventures, LLC v. Segal*, 2008 WL 1961156, at *6 (Del. Ch. May 7, 2008), *aff'd*, 984 A.2d 124 (Del. 2009).

35 *Maloney-Refaie*, 958 A.2d at 877-78; *Fisk Ventures, LLC*, 2008 WL 1961156, at *6.

36 *Maloney-Refaie*, 958 A.2d at 877-78 (internal quotation marks omitted); *Ryan v. Gifford*, 935 A.2d 258, 265 (Del. Ch. 2007).

37 *Fisk Ventures, LLC*, 2008 WL 1961156, at *6; *Ryan*, 935 A.2d at 265; *Werner*, 831 A.2d at 329.

presented without an evidentiary hearing, as it is here, the plaintiff's burden is to point to sufficient evidence in the record to support a *prima facie* case that jurisdictional facts exist to support the two elements it must prove.[38] In doing so, the court is not limited to the pleadings and can consider affidavits, briefs of the parties, and the available results of discovery.[39] Still, allegations regarding personal jurisdiction in a complaint are presumed true, unless contradicted by affidavit, and, as with a motion to dismiss under Rule 12(b)(6), the court must construe the record in the light most favorable to the plaintiff.[40]

2. 6 *Del. C.* § 18-109(a)

In addition to Delaware's long-arm statute, discussed *infra*, Plaintiffs argue that Frashure, Chisholm, and Wolahan are subject to this Court's jurisdiction under the Delaware Limited Liability Company Act's implied consent statute, 6 *Del. C.* § 18-109(a), because they serve as officers of a Delaware LLC, Acadian. Plaintiffs contend that because the Individual Acadian Defendants shared responsibility for implementing the challenged investments and such investments involve or relate to Acadian's business, they qualify as LLC managers and, therefore, have consented to this Court's jurisdiction under the statute. Defendants assert that Plaintiffs misapprehend § 18-109(a), and, specifically, its requirement that an action "involve[e] or relat[e] to the business of the

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38 *See, e.g.*, *Maloney-Refaie*, 958 A.2d at 877-78; *Carlton Invs. v. TLC Beatrice Int'l Hldgs., Inc.*, 1995 WL 694397, at *6 (Del. Ch. Nov. 21, 1995).

39 *Vichi v. Koninklijke Philips Elecs. N.V.*, 2009 WL 4345724, at *4 (Del. Ch. Dec. 1, 2009); *Ryan*, 935 A.2d at 265; *Crescent/Mach I P'rs, L.P. v. Turner*, 846 A.2d 963, 974 (Del. Ch. 2000).

40 *See, e.g.*, *Vichi*, 2009 WL 4345724, at *4; *Ryan*, 935 A.2d at 265; *Crescent/Mach I P'rs, L.P.*, 846 A.2d at 974.

[LLC]."[41] According to Defendants, my decision in *Vichi v. Koninklijke Philips Electronics*[42] stands for the proposition that an action involves or relates to the business of an LLC if, among other things, the allegations in the complaint focus on the rights, duties, and obligations the manager owes to his own organization, and not to external entities, such as the stockholders of a client mutual fund.[43] Thus, Defendants contend that even if Frashure, Chisholm, and Wolahan are LLC managers,[44] § 18-109(a) is inapplicable because this action concerns breaches of duties they allegedly owed to Plaintiffs, who are not affiliated with Acadian.

Section 18-109(a) states, in pertinent part:

> A manager . . . of a limited liability company may be served with process . . . in all civil actions . . . brought in the State of Delaware *involving or relating to the business of the limited liability company* or a violation by the manager . . . of a duty to the limited liability company or any member of the limited liability company, whether or not the manager . . . is a manager . . . at the time suit is commenced. A manager's . . . serving as such constitutes such person's consent to the appointment of the registered agent of the limited liability company . . . as such person's agent upon whom service of process may be made as provided in this section. Such service as a manager . . . shall signify the consent of such manager . . . that any process when so served shall be of the same legal

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41 ARB 3-4.

42 2009 WL 4345724 (Del. Ch. Dec. 1, 2009).

43 *Id*.

44 It is not clear from the pleadings that Frashure, Chisholm, and Wolahan would be considered "managers" under Acadian's LLC agreement or § 18-109(a). Having found that Plaintiffs have not satisfied the "involving or relating" requirement of § 18-109(a), however, I need not reach this issue. Instead, I assume without deciding that they are managers for purposes of my analysis.

> force and validity as if served upon such manager . . . within the State of Delaware and such appointment of the registered agent . . . shall be irrevocable. [45]

It, therefore, is an implied consent statute, but it applies only to a manager of an LLC, which is defined as either a manager fixed under the operative LLC agreement or a "person who participates materially in the management of the limited liability company."[46]

The plaintiff in *Vichi* argued that this Court could assert personal jurisdiction over Ho, a businessman who at the time of the actions giving rise to the suit was Vice President and Global Treasurer for LG.Philips Displays Holding B.V. ("LPD"). Pursuant to a financing transaction with the plaintiff, Ho signed notes issued in Delaware on behalf of LG.Philips Displays Finance LLC ("Finance"), a Delaware LLC and subsidiary of LPD. He signed in his capacity as an employee of LG.Philips Displays International Ltd. ("International"), which was the sole member and manager of Finance. After LPD defaulted on notes it had issued to the plaintiff, the plaintiff sued Ho, among others, and asserted that this Court had personal jurisdiction over him pursuant to § 18-109(a).[47]

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45 6 *Del. C.* § 18-109(a) (emphasis added).

46 *Vichi v. Koninklijke Philips Elecs.*, 2009 WL 4345724, at *7 (Del. Ch. Dec. 1, 2009).

47 *Id*. (noting that Ho had never visited, worked in, or otherwise had any connection with Delaware).

In *Vichi*, after holding that Ho did not qualify as a "manager" under the statute, I also found that the plaintiff's lawsuit did not constitute an action "involving or relating to the business" of Finance.[48] I explained that:

> An action involves or relates to the business of an LLC [within the meaning of § 18-109(a)] if: (1) the allegations against [the manager] focus centrally on his rights, duties and obligations as a manager of a Delaware LLC; (2) the resolution of th[e] matter is inextricably bound up in Delaware law; and (3) Delaware has a strong interest in providing a forum for disputes relating to the ability of managers of an LLC formed under its law to properly discharge their respective managerial functions.[49]

Citing several cases, I held that "Delaware courts interpret the 'rights, duties and obligations as a manager of a Delaware LLC' to refer to rights, duties, and obligations a manager owes to his organization."[50] Based on this language, Defendants contend that § 18-109(a) is inapplicable here because Plaintiffs' allegations pertain to duties Frashure, Chisholm, and Wolahan allegedly owed to Nominal Defendants and Plaintiffs, and not to Acadian.

Plaintiffs dispute Defendants' reading of *Vichi* and § 18-109(a). In particular, they argue that § 18-109(a) is drafted in the disjunctive so that it applies in two distinct situations: first, with regard to an LLC manager who breaches a fiduciary duty to the LLC, which Plaintiffs concede is not alleged here; and second, with regard to "any claim

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48 *Id*. at *7-8.

49 *Id*. at *8.

50 *Id*.

that arises out of the business of a Delaware [LLC] for which they work."[51] Plaintiffs contend that the latter situation exists here and provides a basis for jurisdiction, principally because the individual Acadian Defendants worked for a Delaware LLC that was managing investments on behalf of the Nominal Defendants. As such, Plaintiffs assert that Frashure, Chisholm, and Wolahan "had to know and expect" that if litigation regarding those investments arose, it might be brought in Delaware.

The literal language of § 18-109(a) provides some support for Plaintiffs' argument.[52] The statute provides that this Court may assert personal jurisdiction over a manager of a Delaware LLC "in all civil actions . . . involving or relating to the business of the limited liability company *or* a violation by the manager . . . of a duty to the limited liability company . . . ."[53] Based on the use of "or" in this sentence, Plaintiffs argue that each of the two identified scenarios provides an independent basis for jurisdiction, including when an action involves or relates to the business of an LLC.

As the Court in *Assist Stock Management* explained, however, broadly reading the "involving or relating to" language in the clause on which Plaintiffs rely could lead to the assertion of personal jurisdiction in circumstances that do not meet the minimum contacts

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51 Tr. of Feb. 9, 2011 Arg. ("Tr.") 113-14.

52 *See Assist Stock Mgmt. L.L.C. v. Rosheim*, 753 A.2d 974, 979 (Del. Ch. 2000) (noting that if one interpreted the "involving or relating to" language in § 18-109(a) broadly, the mere fact that the defendant, Rosheim, was a manager of a Delaware LLC and that the suit involved or related to its business would provide a basis for jurisdiction).

53 6 *Del. C.* § 18-109(a) (emphasis added).

requirements of the Due Process Clause.[54] Indeed, requiring Delaware LLC managers to submit to the jurisdiction of this Court whenever a suit involves or relates to the LLC's business could be unconstitutional. On the specific facts of the *Assist Stock Management* case, however, the court held that sufficient minimum contacts were present, such that it properly could exercise personal jurisdiction over the defendant. There, the court relied on the three factors referenced in *Vichi* to protect against an unconstitutionally broad application of § 18-109(a).[55]

Thus, for Plaintiffs to invoke the "involving or relating to" clause of § 18-109(a), they must establish that the exercise of personal jurisdiction over the Acadian Individual Defendants would not offend traditional notions of fair play and substantial justice. Due process would not be offended if Plaintiffs can show that (1) the allegations against the defendant-manager focus centrally on his rights, duties and obligations as a manager of a Delaware LLC; (2) the resolution of the matter is inextricably bound up in Delaware law; and (3) Delaware has a strong interest in providing a forum for the resolution of the

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[54] *See Assist Stock Mgmt.*, 753 A.2d at 980 ("Admittedly, the 'involving or relating to' language found in § 18-109 can, too, be susceptible to too broad an application. I believe, however, that '[p]rotection against unconstitutional application of [the] statute[ ] could be provided on a case-by-case basis by applying the minimum-contacts analysis mandated by due process.'"); *see also Cornerstone Techs., LLC v. Conrad*, 2003 WL 1787959, at *12 (Del. Ch. Mar. 31, 2003) ("In [*Assist Stock Management*], Vice Chancellor Lamb respected the General Assembly's decision to write § 18-109 more broadly than § 3114 of the DGCL, by investing this court with personal jurisdiction over managers in disputes 'involving or relating to the business of' their LLCs. He held that this language must be given effect and that protection against an unconstitutional application of the statute can be afforded by the minimum contacts analysis.").

[55] *See Assist Stock Mgmt.*, 753 A.2d at 981; *see supra* note 49.

dispute relating to the manager's ability to discharge his managerial functions.[56] For personal jurisdiction purposes under *Vichi*, the relevant rights, duties and obligations of a defendant-manager of a Delaware LLC are the rights, duties, and obligations of the manager vis-á-vis his organization.[57]

Here, Plaintiffs' claims do relate to Frashure, Chisholm, and Wolahan's involvement in Acadian's business of providing financial advisory services to mutual funds. The allegations do not focus, however, on the duties and obligations those Defendants owed to Acadian. Rather, Plaintiffs allege that these Defendants' actions constituted breaches of fiduciary duties owed to Plaintiffs and Nominal Defendants. As was the case in *Vichi*, and even assuming the Acadian Individual Defendants are "managers" under § 18-109(a), I find that Plaintiffs' claims do not involve or relate to Acadian's business in the sense of its internal business as required by the statute and the

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[56] *See, e.g.*, *Vichi v. Koninklijke Philips Elecs. N.V.*, 2009 WL 4345724, at *8 (Del. Ch. Dec. 1, 2009); *Assist Stock Mgmt.*, 753 A.2d at 981. This test does not render meaningless the "involving or relating to" language in § 18-109(a), as Plaintiffs argue, because it does not require an allegation that a manager breached a duty or violated some other law to obtain jurisdiction over him; rather, it requires an allegation involving or relating to the rights, duties, and obligations he has in relation to his LLC. *See Cornerstone Techs.*, 2003 WL 1787959, at *12 ("In this case, the issue as to who owns what part of Cornerstone and Arastra (*i.e.*, the issue in the Ownership Count) is 'related in some respect' to the management disputes underlying this case - *i.e.*, it relates to the business of the Companies.")

The test articulated in *Assist Stock Management* and *Vichi* may not be exhaustive or exclusive. Plaintiffs, however, have not alleged any facts that suggest they otherwise might satisfy both § 18-109(a) and the Due Process Clause.

[57] *Vichi*, 2009 WL 4345724, at *8.

Due Process Clause.[58] Therefore, § 18-109(a) does not provide a basis for this Court to assert personal jurisdiction over Frashure, Chisholm, and Wolahan.

3. Conspiracy theory

Plaintiffs next argue that the Individual Defendants are subject to jurisdiction in Delaware because they conspired with the entity Defendants in this matter, through their financial advisory services, to cause Nominal Defendants to invest in purportedly illegal gambling businesses, which caused Plaintiffs to suffer resulting losses.[59]

The "conspiracy theory" of personal jurisdiction does not constitute an independent basis for subjecting an out-of-state resident to personal jurisdiction. Rather, it rests upon the notion that, in appropriate circumstances, a defendant's conduct that either occurred or had a substantial effect in Delaware, and thus would make him subject to personal jurisdiction in Delaware, may be attributed to another defendant who would not otherwise be amenable to jurisdiction in this State, if that defendant is a co-conspirator.[60] In *Istituto Bancario*, the Delaware Supreme Court held that:

> [A] conspirator who is absent from the forum state is subject to the jurisdiction of the court . . . if the plaintiff can make a

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58 *See id*. ("all of the counts that Vichi asserts against Ho relate to the Notes transaction between Finance and Vichi or to breaches of fiduciary duties allegedly owed to Vichi personally. None of these counts relate to the rights, duties and responsibilities Ho owes *to Finance*, or in any other way to the internal business affairs of Finance or to the running of Finance's day-to-day operations.").

59 PAB 54, 58-59 (citing Compl. ¶¶ 15, 61, 65, 157-58).

60 *See Istituto Bancario Italiano SpA v. Hunter Eng'g Co.*, 449 A.2d 210, 225 (Del. 1982) ("The conspiracy theory rests in part upon the legal premise that the acts of a conspirator are imputed to all the other co-conspirators."); *Benihana of Tokyo, Inc. v. Benihana, Inc.*, 2005 WL 583828, at *6 n.16 (Del. Ch. Feb. 4, 2005).

> factual showing that: (1) a conspiracy to defraud existed; (2) the defendant was a member of that conspiracy; (3) a substantial act or substantial effect in furtherance of the conspiracy occurred in the forum state; (4) the defendant knew or had reason to know of the act in the forum state or that acts outside the forum state would have an effect in the forum state; and (5) the act in, or effect on, the forum state was a direct and foreseeable result of the conduct in furtherance of the conspiracy.[61]

Delaware courts construe this test narrowly and require a plaintiff to assert specific facts, not conclusory allegations, as to each element.[62]

While Plaintiffs' Complaint mentions the word conspiracy several times,[63] it does so in a conclusory manner and asserts few, if any, facts in support of an alleged conspiracy. Indeed, Plaintiffs have not properly alleged even the first prong of the *Istituto Bancario* test: the existence of a conspiracy to defraud. To meet that requirement of the test, a plaintiff must allege the following elements: (1) two or more persons; (2) some object to be accomplished; (3) a meeting of the minds between or among such

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61 *Istituto Bancario*, 449 A.2d at 225 ("a defendant who has so voluntarily participated in a conspiracy with knowledge of its acts in or effects in the forum state can be said to have purposefully availed himself of the privilege of conducting activities in the forum state, thereby fairly invoking the benefits and burdens of its laws. . . . It can further be said that such participation is a substantial contact with the jurisdiction of a nature and quality that it is reasonable and fair to require the defendant to come and defend an action there."); *see also Werner v. Miller Tech. Mgmt., L.P.*, 831 A.2d 318, 329-30 (Del. Ch. 2003).

62 *Werner*, 831 A.2d at 329-30.

63 Compl. ¶¶ 15, 61, 65, 157-58.

persons relating to the object or a course of action; (4) one or more unlawful acts; and (5) resulting proximate damages.[64]

Because of the paucity of detail about an alleged conspiracy, it is difficult to discern its purported parameters. To the extent Plaintiffs argue that a conspiracy existed between certain Individual Defendants and their respective corporate employers, *e.g.*, between Sauter and Vanguard, these claims are legally deficient because "a corporation generally cannot be deemed to have conspired with its officers and agents for purposes of establishing jurisdiction under the conspiracy theory."[65] It also is unclear from the Complaint whether Plaintiffs allege that certain Individual Defendants conspired with certain other Individual Defendants or other nonemployer entity Defendants to cause the

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64 *See, e.g.*, *Hamilton P'rs, L.P. v. Englard*, 11 A.3d 1180, 1198 (Del. Ch. 2010); *Carlton Invs. v. TLC Beatrice Int'l Hldgs., Inc.*, 1995 WL 694397, at *15 n.11 (Del. Ch. Nov. 21, 1995); *see also Allied Capital Corp. v. GC-Sun Hldgs., L.P.*, 910 A.2d 1020, 1036 (Del. Ch. 2006) ("Under Delaware law, to state a claim for civil conspiracy, a plaintiff must plead facts supporting (1) the existence of a confederation or combination of two or more persons; (2) that an unlawful act was done in furtherance of the conspiracy; and (3) that the conspirators caused actual damage to the plaintiff.").

65 *Amaysing Techs. Corp. v. Cyberair Commc'ns, Inc.*, 2005 WL 578972, at *7 (Del. Ch. Mar. 3, 2005) ("It is basic in the law of conspiracy that you must have two persons or entities to have a conspiracy. A corporation cannot conspire with itself any more than a private individual can, and it is the general rule that the acts of the agent are the acts of the corporation.") (internal quotation marks omitted); *In re Transamerica Airlines, Inc.*, 2006 WL 587846, at *6 (Del. Ch. Feb. 28, 2006). There is an exception to this rule where an agent steps out of his role as an officer or agent and acts pursuant to personal motives. *Amaysing Techs. Corp.*, 2005 WL 578972, at *7. This exception does not apply here, however, because Plaintiffs have not pled facts that would permit the Court reasonably to infer that Individual Defendants caused Nominal Defendants to purchase the Challenged Securities because of "personal animus and/or desire for financial benefit other than [their] corporate salary." *See id.*; *see also* Compl. ¶ 61.

challenged security purchases in issue. Assuming Plaintiffs do allege such a conspiracy, they have failed to assert sufficient facts to permit the Court to infer that there was a meeting of the minds between any Individual Defendants regarding such challenged purchases.[66] Indeed, the Complaint lumps together Vanguard Individual Defendants, Acadian Individual Defendants, and Ostrer, and does not differentiate among them or explain how any two of these Defendants, let alone all of them, came to a common understanding or intent to work toward some common objective to engage in unlawful conduct.[67] The Complaint suggests that the various Individual Defendants played some role in the decision to cause the Affected Funds to invest in the Challenged Securities, which, according to Plaintiffs, violated the law. It does not detail or differentiate the nature of their roles or the degree to which they may have acted in concert.

An important premise of all of Plaintiffs' claims, however, is that it was illegal to purchase or hold the Challenged Securities. Yet, as discussed *infra*, Plaintiffs have not shown that their allegations of illegality are well-founded. Therefore, those allegations

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66 Similarly, I find that Plaintiffs have failed to allege a conspiracy among or between Individual Defendants who work at the same Defendant employer and that employer. *See supra* note 65. Agents of a corporation generally are not subject to civil liability for conspiring among themselves and with their own corporation. *See Allied Capital Corp. v. GC-Sun Hldgs., L.P.*, 910 A.2d 1020, 1045 n.63 (Del. Ch. 2006) (dicta).

67 Paragraphs 15 and 65 of the Complaint, for example, each allege in one sentence that "Defendants" conspired to violate RICO. Paragraph 61 is a general and conclusory statement that "Defendants," without differentiating among them, conspired to cause Nominal Defendants to continue their ownership of allegedly illegal gambling enterprises. In addition, paragraphs 157 and 158 mention a conspiracy, but only in passing in the context of a discussion of the Trustees' actions.

cannot serve as the basis for a conspiracy.[68] Because Plaintiffs have failed to allege a common objective or a meeting of the minds among or between two or more specific Defendants regarding a fraudulent or unlawful objective, I find that Plaintiffs have failed to allege the existence of a conspiracy. Therefore, I need not address the remaining elements of civil conspiracy.

Similarly, because the first two elements of the *Istituto Bancario* test for establishing jurisdiction based on a conspiracy theory are not met here, I need not address the remaining elements of that test.[69] As such, I hold that the conspiracy theory provides no basis for this Court to exercise personal jurisdiction over any of the Individual Defendants in this action.

4. Long-arm statute

Next, Plaintiffs advance several theories in support of their contention that all Individual Defendants are susceptible to the jurisdiction of this Court under the Delaware long-arm statute.[70] Under that statute, this Court may exercise personal jurisdiction over

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68 *See DeBonaventura v. Nationwide Mut. Ins. Co.*, 428 A.2d 1151, 1155 (Del. 1981) (affirming decision to reject a conspiracy claim where "there was no unlawful conduct upon which the conspiracy claim could be grounded").

69 I note, however, that Plaintiffs' conspiracy theory of jurisdiction appears to have at least one additional flaw. Specifically, Plaintiffs have not alleged any qualifying act or effect that allegedly occurred in Delaware. Instead, they appear to rely on their contention that the challenged actions of Defendants caused injury to a Delaware entity to satisfy the requirement of a relevant effect in Delaware. For the reasons discussed *infra* Part II.A.4.c, I find this argument unpersuasive.

70 10 *Del. C.* § 3104(c).

a defendant for a claim that "arises from" an enumerated "jurisdictional act."[71] Furthermore, Delaware courts construe the statute as broadly as permitted under the Due Process Clause.[72]

In particular, this Court may exercise specific jurisdiction

> over any nonresident, or a personal representative, who in person or through an agent . . . (2) Contracts to supply services or things in this State; (3) Causes tortious injury in the State by an act or omission in this State; [or] (4) Causes tortious injury in the State or outside of the State by an act or omission outside the State if the person regularly does or solicits business, engages in any other persistent course of conduct in the State or derives substantial revenue from services, or things used or consumed in the State . . . .[73]

Plaintiffs contend that all three subsections of § 3104(c) quoted above provide a basis for personal jurisdiction over some or all Individual Defendants. I address each of these theories in turn.

a. § 3104(c)(2): contracting to supply services or things in Delaware

Plaintiffs assert that Acadian and Marathon each contracted with VHF to provide advisory services to Vanguard Global and specified in their respective contracts that Delaware law would govern the construction of the contracts. According to Plaintiffs, this Court should infer from those facts and the likelihood that VHF would act on the advice supplied by its investment advisors, that the parties intended Acadian and

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71 *Mobile Diagnostic Gp. Hldgs., LLC v. Suer*, 972 A.2d 799, 804 (Del. Ch. 2009).

72 *See, e.g.*, *Hamilton P'rs, L.P. v. Englard*, 11 A.3d 1180, 1197 (Del. Ch. 2010); *Mobile Diagnostic Gp. Hldgs.*, 972 A.2d at 804.

73 10 *Del. C.* § 3104(c).

Marathon's advisory services to have been supplied in Delaware by Individual Defendants.[74]

Under § 3104(c)(2), this Court may obtain jurisdiction over an out-of-state defendant if that defendant contracted to supply services in Delaware. As Plaintiffs acknowledge, a contractual choice of law provision in favor of Delaware, on its own, generally does not warrant the exercise of personal jurisdiction over an out-of-state defendant for conduct arising from that contract.[75] Nevertheless, Plaintiffs tout the choice of law provision as an important factor favoring jurisdiction here. But, even assuming Plaintiffs are correct, the existence of such a provision would be important only as to whether the out-of-state parties to the contracts at issue, *i.e.*, Acadian and Marathon, may be susceptible to jurisdiction in Delaware. Plaintiffs do not allege that their agents Frashure, Chisholm, Wolahan, and Ostrer were parties to the contracts Acadian and Marathon had with VHF. That is, these Individual Defendants did not "contract" with VHF at all; rather, the Complaint alleges merely that they are employed by the out-of-

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74 *See* PAB 57 (arguing that the parties fully expected any litigation arising out of those contracts to be brought in Delaware).

75 *Mobile Diagnostic Gp. Hldgs.*, 972 A.2d at 805 ("It is well settled law that 'a contract between a Delaware corporation and a nonresident to . . . transact business outside Delaware, which has been negotiated without any contacts with this State, cannot alone serve as a basis for personal jurisdiction over the nonresident for actions arising out of that contract.' It is also well established that a choice of Delaware law provision in a contract is not, of itself, a sufficient transaction of business in the State to confer jurisdiction under (c)(1). . . . Similarly, agreeing to a provision in a contract that provides for service of process by any means permitted under Delaware law is not a jurisdiction-conferring act within this State."); *Werner v. Miller Tech. Mgmt., L.P.*, 831 A.2d 318, 331 (Del. Ch. 2003).

state parties that contracted with VHF. By itself, however, a business relationship between an out-of-state defendant's employer and a company located in Delaware does not provide the necessary contacts to satisfy the Delaware long-arm statute as to the defendant-employee.[76]

Thus, I hold that § 3104(c)(2) provides no basis for asserting personal jurisdiction over Frashure, Chisholm, Wolahan, or Ostrer.

b. § 3104(c)(4): tortious injury and act or omission outside of Delaware

Plaintiffs next argue that Vanguard, Acadian, and Marathon caused a tortious injury in Delaware by providing advisory services regarding the Challenged Securities, discussed further *infra*, and that each regularly does or solicits business in Delaware and derives substantial revenue from their services rendered for the benefit of Delaware entities, including VHF and VIEIF.[77] Although none of those three entities has challenged this Court's jurisdiction, Plaintiffs invite the Court to assume that each of them would be subject to personal jurisdiction based on § 3104(c)(4). Plaintiffs then assert that the Court also may extend that jurisdiction to cover their employees, Individual Defendants, for two derivative reasons.

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[76] *See Binks v. DSL.net, Inc.*, 2010 WL 1713629, at *14 n.118 (Del. Ch. Apr. 29, 2010).

[77] PAB 55-56 (citing multiple statistics regarding revenue). Section 3104(c)(4) applies "when a defendant has had contacts with [Delaware] that are so extensive and continuing that it is fair and consistent with state policy to require that the defendant appear here and defend a claim even when that claim arose outside of this state and causes injury outside of this state." *Red Sail Easter Ltd. P'rs, L.P. v. Radio City Music Hall Prods., Inc.*, 1991 WL 129174, at *3 (Del. Ch. July 10, 1991).

First, Plaintiffs emphasize that their claims arise out of the services rendered by Individual Defendants in their capacity as employees of Vanguard, Acadian, and Marathon, and those entities derive substantial revenue from providing such services. Plaintiffs argue, therefore, that the Court has jurisdiction over Individual Defendants because they conspired with their employers to provide the challenged financial advice to Nominal Defendants. As discussed *supra*, however, the Complaint does not plausibly allege that the Individual Defendants conspired with each other or any other Defendants, including Vanguard, Acadian, or Marathon. Thus, I reject this argument for jurisdiction.

Plaintiffs' second contention is that, even if there was no conspiracy, each Individual Defendant satisfies § 3104(c)(4)'s revenue requirement because Individual Defendants are high-level officers and portfolio managers of their respective Defendant-employers, and "it is reasonable to infer that the Individual Defendants also derive substantial revenue from the fees that the entit[y Defendants] charge Nominal Defendants for their services."[78] Yet, Plaintiffs cite no case law or other authority for the proposition that a defendant-employee's receipt of a salary based on services rendered to a company that allegedly derives substantial revenue from its activities in Delaware is a sufficient contact under § 3104(c)(4) to confer personal jurisdiction over that defendant.

Moreover, Plaintiffs' argument is unpersuasive both as a matter of law generally and as a matter of fact in the circumstances of this case. Analytically, it would be prohibitively difficult for a court to attempt to trace an employee's salary back to each of

[78] PAB 56-57.

its financial and geographic sources based on the customers for which the employee worked.[79] In addition, I do not agree that receiving a salary, part of which might reflect time spent working to generate fees related to services an employer provided in Delaware, would satisfy the Due Process Clause's minimum contacts requirement. In any event, even drawing all inferences in favor of Plaintiffs and assuming that a salary could, on its own, satisfy the substantial revenue requirement of § 3104(c)(4), Plaintiffs' Complaint has not alleged sufficient facts to support a reasonable inference that any of the Individual Defendants' salaries were substantial or were derived from fees charged to Nominal Defendants.[80]

Therefore, Plaintiffs have not shown that § 3104(c)(4) provides a basis for subjecting Individual Defendants to this Court's jurisdiction.

c. § 3104(c)(3): tortious injury in Delaware caused by an act or omission in Delaware

Finally, Plaintiffs argue that Individual Defendants are subject to jurisdiction under § 3104(c)(3), because they caused Nominal Defendants to own allegedly illegal

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79 *See Amhil Enters. Ltd. v. Wawa, Inc.*, 1994 WL 750535, at *4 n.5 (D. Md. Dec. 16, 1994) (citing *Birrane v. Master Collectors, Inc.*, 738 F. Supp. 167, 169 n.2 (D. Md. 1990)) ("It might be argued that a highly-salaried corporate officer or other corporate employee or a shareholder to whom dividends have been paid has personally 'derive[d] substantial revenue from goods . . . [or] . . . services . . . used or consumed in the State' if the corporation has itself derived substantial revenue from such goods or services. . . . However, the factual difficulties presented in tracing the particular source of salaries or dividend payments are virtually insurmountable, and, constitutional considerations aside, there is no legislative history suggesting that the General Assembly intended that courts should embark on such a radical inquiry in deciding jurisdictional issues.").

80 Indeed, the Complaint fails to allege any details about the size, source, or breakdown of any Individual Defendant's salary.

gambling securities in Delaware and Nominal Defendants suffered resulting losses in Delaware. Specifically, they assert that a corporation is "injured," in a metaphysical sense, where it is incorporated and, thus, when share prices declined for securities held by the Affected Funds within Nominal Defendants, those entities suffered an "injury" in Delaware. Plaintiffs also contend that the relevant "acts" required by the statute, which include causing Nominal Defendants to own shares in the allegedly illegal gambling businesses, occurred in Delaware because that is where such shares are owned.

Under § 3104(c)(3), this Court may exercise personal jurisdiction over an out-of-state defendant if the plaintiff demonstrates that the nonresident-defendant has caused a tortious injury in Delaware and such injury was due to an act or omission by the defendant in Delaware.[81] Thus, for jurisdiction to attach, a plaintiff must establish both elements of subsection (c)(3): an injury and an act or omission in Delaware.

As to the "injury" part of the analysis, Plaintiffs contend that Nominal Defendants were injured by the decline in the prices of the Challenged Securities that the Affected Funds held and, because they are Delaware trusts, they incurred that injury in Delaware. Although the concept is somewhat metaphysical, when a Delaware business entity is injured financially by allegedly "faithless conduct of its directors," or in this case trustees, this Court has held that the entity may be said to be injured in its "legal home,"

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[81] *See* 10 *Del. C.* § 3104(c)(3); *Ohrstrom v. Harris Trust Co. of N.Y.*, 1998 WL 8849, at *3 (Del. Ch. Jan. 8, 1998).

Delaware, for purposes of § 3104(c)(3).[82] Hence, Plaintiffs plausibly argue that, if they can state a claim as to the alleged illegal conduct of Individual Defendants and show that such conduct caused the Affected Funds of VHF and VIEIF to suffer declining net asset values ("NAV"),[83] those injuries would have been "suffered" in Delaware, the state under whose law VHF and VIEIF were created and are governed.

Still, plausibly alleging an injury in Delaware is only half of what Plaintiffs must show to satisfy subsection (c)(3). They also must establish that the out-of-state Defendants committed an act or omission *in* Delaware, as well.

Plaintiffs claim that they have made the requisite showing of an act in Delaware here because Individual Defendants provided advisory services which facilitated Vanguard Global and Vanguard European's purchases of the Challenged Securities. While they acknowledge that these Funds purchased the shares in foreign jurisdictions,

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82 *See Sample v. Morgan*, 935 A.2d 1046, 1057-58 & n.44 (Del. Ch. 2007) ("when a Delaware resident-a Delaware corporation-is injured by a breach of fiduciary duty, it is easy to conceive of the corporation as having been injured in its chosen place of legal residence. After all, it is precisely for purposes of internal affairs that corporations-which are not physical beings-choose a legal domicile. When they suffer financial injury, that injury should, consistent with the instruction of *Hercules* and other Delaware public policies favoring a broad construction of § 3104's reach, be deemed to have been suffered in Delaware for purposes of § 3104(c)(3).") (discussing *Hercules Inc. v. Leu Trust & Banking (Bah.) Ltd.*, 611 A.2d 476 (Del. 1992)); *see also Chandler v. Ciccoricco*, 2003 WL 21040185, at *11 n.46 (Del. Ch. 2003).

83 A mutual fund is priced by the NAV method. *Siemers v. Wells Fargo & Co.*, 243 F.R.D. 369, 373-74 (N.D. Cal. 2007). This method is "based on the daily market closing prices for the underlying portfolio (such as portfolio shares in General Motors, Exxon Corporation, etc.). The net asset value of the portfolio as a whole is then divided by the number of shares outstanding in the mutual fund to derive the daily share value." *Id.*

Plaintiffs argue that the Funds' "ownership" of those shares within the meaning of 18 U.S.C. § 1955 occurred in Delaware where the Nominal Defendants are domiciled.

Although this Court has recognized financial harm to a Delaware business entity as a form of *injury* that has occurred in Delaware, it nonetheless has required, consistent with notions of due process, a factual showing that a tangible *act or omission* actually took place in Delaware.[84] Based on the Complaint and the record before me, I am not convinced that Plaintiffs have alleged any such act or acts that have taken place in Delaware.

The Complaint avers that various Individual Defendants provided portfolio management and investment advisory services to Vanguard Global and Vanguard European, which caused those funds to purchase the Challenged Securities. But, these services were provided by nonresident individuals, from their employers' out-of-state locations,[85] to Delaware statutory trusts based in Pennsylvania, and allegedly had the effect of causing certain of the trusts' mutual funds to purchase the Challenged Securities in overseas markets. Plaintiffs do not assert, however, that any Individual Defendant took any tangible action in Delaware, such as physically coming to the State to provide

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84 *See Sample*, 935 A.2d at 1058 (noting that any problems with a metaphysical approach to evaluating whether financial harm to a Delaware business entity constitutes an "injury" in Delaware "are best policed by the minimum contacts tests or by the other aspects of § 3104, which for the most part require that an actual act take place in Delaware."); *see also Ohrstrom*, 1998 WL 8849, at *3.

85 In addition, Vanguard and Marathon are not organized under the laws of Delaware. Acadian is a Delaware LLC, but the mere fact that Frashure, Chisholm, and Wolahan are employed by a Delaware entity does not, without more, provide a basis for jurisdiction under § 3104(c)(3).

advice, filing or helping to file any document in the State, or communicating, in person or through other means, with any person or entity in Delaware. Thus, none of the acts by the Individual Defendants alleged to have caused injury to Plaintiffs and the Affected Funds took place in Delaware.[86] Nor does the fact that an individual's conduct may have had an effect in Delaware establish that an action allegedly causing such effect took place *in* Delaware.[87] Indeed, the record indicates that Individual Defendants provided the challenged advisory services and financial advice from their offices in Pennsylvania, Massachusetts, and the United Kingdom, respectively, and gave such advice to certain mutual funds whose principal places of business were in Pennsylvania.[88]

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[86] *See In re Am. Int'l Gp., Inc.*, 965 A.2d 763, 815 (Del. Ch. 2009); *Ohrstrom*, 1998 WL 8849, at *3 ("Assuming for the sake of argument that Plaintiffs were injured in Delaware as a result of Harris Trust's conduct, Plaintiffs still have failed to demonstrate that their injury occurred as a result of an act or omission *that took place* in Delaware. . . . Therefore, Plaintiffs cannot rely on the third prong of Delaware's long-arm statute to secure personal jurisdiction over Harris Trust.").

[87] *See Ohrstrom*, 1998 WL 8849, at *3; *cf. Iotex Commc'ns, Inc. v. Defries*, 1998 WL 914265, at *8 (Del. Ch. Dec. 21, 1998) ("The second and third arguments are that Defries' alleged breach of his fiduciary duties as one of IOTEX's directors caused a 'substantial effect' in Delaware simply by virtue of IOTEX's incorporation in this State and that Bayendor's alleged breach of fiduciary [duty] while he was President of IOTEX's predecessor . . . caused injury in this State. . . . These alleged 'effects' add nothing to the analysis because they have only a metaphysical connection with this jurisdiction. In my judgment, as a general rule, in the case of Delaware corporations having no substantial physical presence in this State, an allegation that a civil conspiracy caused injury to the corporation by actions wholly outside this State[] will not satisfy the requirement found in the Supreme Court's opinion in *Istituto Bancario* of a "substantial effect . . . in the forum state.")

[88] *Compare Hercules Inc. v. Leu Trust & Banking (Bah.) Ltd.*, 611 A.2d 476, 481 (Del. 1992) (noting that a nonresident investment banker's act of giving allegedly

Therefore, I agree with Defendants that Plaintiffs have failed to allege conduct occurring in Delaware, on behalf of any Individual Defendant, which would satisfy the act or omission requirement of § 3104(c)(3). Accordingly, that statute provides no basis for asserting jurisdiction over any Individual Defendant.

5. Due Process

In addition to demonstrating a statutory basis for personal jurisdiction as to each Individual Defendant, Plaintiffs also must show that the Court's exercise of jurisdiction over them meets the so-called minimum contacts analysis. This analysis "seeks to determine the fairness of subjecting a nonresident defendant to suit in a distant forum by considering all of the connections among the defendant, the forum and the litigation. . . . [and] ensures that 'the States through their courts, do not reach out beyond the limits imposed on them by their status as coequal sovereigns in a federal system.'"[89] The Court must determine whether each nonresident defendant's conduct and connection with Delaware is such that he reasonably would have anticipated being haled into court here.[90]

Having concluded that there is no statutory basis on which to assert personal jurisdiction over any Individual Defendant, I need not reach Plaintiffs' due process

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fraudulent financial advice to a Delaware corporation with its principal place of business in Delaware constituted an act in Delaware for purposes of § 3104(c)(3)).

89 *Werner v. Miller Tech. Mgmt., L.P.*, 831 A.2d 318, 330 (Del. Ch. 2003) (internal quotation marks omitted).

90 *See id.*

arguments.[91] Even assuming, however, that the relevant statutes could be construed sufficiently broadly to confer jurisdiction as to any or all such Defendants here, I am persuaded that asserting jurisdiction over them would offend the Due Process Clause because of their lack of contacts with this State.[92] Sauter and Kelly work for Vanguard, a Pennsylvania corporation based in Pennsylvania. There is no evidence that they reside, conduct business, or own real property in Delaware, or that they have had any other specific and relevant contact with Delaware. Further, while Frashure, Chisholm, and Wolahan work for a Delaware LLC, Acadian, they live and work in Massachusetts, where Acadian's principal place of business is, and do not own real property or any other assets in Delaware.[93] Finally, Ostrer, who lives and works in the UK, works for Marathon, a UK LLP with its principal place of business in London.[94] While he co-advises a Marathon pooled fund that has one Delaware investor, it is unrelated to the mutual funds involved in this action. Ostrer has never worked in or visited this State.[95]

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91 *See Fisk Ventures, LLC v. Segal*, 2008 WL 1961156, at *6 (Del. Ch. May 7, 2008).

92 *See Sample v. Morgan*, 935 A.2d 1046, 1056 (Del. Ch. 2007) ("the Supreme Court has instructed that trial courts should permit service under § 3104 if the statutory language plausibly permits service, and rely upon a Due Process analysis to screen out uses of the statute that sweep too broadly.").

93 *See, e.g.*, Frashure Aff. ¶¶ 1-6; Chisholm Aff. ¶¶ 1-6; Wolahan Aff. ¶¶ 1-6. Wolahan has never visited Delaware, and Frashure and Chisholm have not visited in the last five years. I also note that Acadian has no offices in Delaware. *See* Frashure Aff. ¶ 5.

94 *See* Aff. of Neil M. Ostrer ¶¶ 1-6.

95 *Id*.

In sum, Plaintiffs have not shown that Individual Defendants have the requisite minimum contacts with Delaware to justify haling them into court here. While those Defendants actively may have facilitated the Funds' purchases of the Challenged Securities and overseen their management, Plaintiffs failed to demonstrate that they undertook any action in Delaware or otherwise have sufficient contacts with this State to support the exercise of personal jurisdiction over them.[96] Therefore, I dismiss the Complaint as to all Individual Defendants for want of personal jurisdiction.

6. Jurisdictional discovery

In the alternative, Plaintiffs argue that "if any doubt exists concerning jurisdiction as to any Defendant, Plaintiff[s] should be afforded jurisdictional discovery."[97] Because Plaintiffs have the burden to make a *prima facie* showing of personal jurisdiction, I have the discretion to delay ruling on the issue of jurisdiction to permit them a reasonable opportunity for additional discovery.[98]

In the circumstances of this case, however, I consider Plaintiffs' request for additional time to take jurisdictional discovery unwarranted. First, the Court never stayed discovery in this action and Plaintiffs had over ten weeks between the filing of Defendants' opening briefs in support of their motions to dismiss and the filing of

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96 *See Klita v. Cyclo$_3$pss Corp.*, 1998 WL 749637, at *4 (Del. Super. Aug. 27, 1998) ("While it may well be true that the Brokers actively participated in the conception of the offering, drafted key provisions of the Certificate, and fully anticipated that Cyclo$_3$pss would make the filing, nothing they did constituted an act in this jurisdiction satisfying due process requirements of minimal contacts.").

97 PAB 59.

98 *See Cyclo$_3$pss Corp.*, 1998 WL 749637, at *4.

Plaintiffs' answering brief. Yet, Plaintiffs evidently did not attempt to take any discovery during that time period or the additional period before the motions were argued. Second, Plaintiffs counsel have extensively litigated similar claims in other jurisdictions in the past and are well aware of their potential jurisdictional discovery needs. Finally, the parties do not seriously dispute the nature of Individual Defendants' contacts with Delaware, *i.e.*, they provided advisory services to Delaware trusts whose principal places of business are in Pennsylvania. Instead, their disagreements focus on the legal import of those contacts and are not fact intensive. For all of these reasons, I am not persuaded that additional factual discovery would benefit the parties' jurisdictional dispute or that the attendant delay would be justified. Therefore, I deny Plaintiffs' request for leave to take jurisdictional discovery.

B. Defendants' Motions for Dismissal Based on Plaintiffs' Failure to Make a Pre-suit Demand

The parties next dispute a host of issues relating to whether Plaintiffs needed to make a pre-suit demand regarding some or all of the counts in the Complaint. Specifically, Defendants claim that all of the counts are derivative in nature and subject to a demand requirement. They further assert that Plaintiffs have failed to satisfy the applicable demand requirements as articulated under Delaware statutory and common law. Plaintiffs counter that they properly have stated direct claims in Counts IV and V. Moreover, regarding Counts I-III, Plaintiffs aver that they adequately have pled facts from which the Court reasonably can infer that making a demand on the Board of Trustees would have been futile and, thus, their failure to do so is excusable. I begin by

addressing whether Plaintiffs may proceed on their direct claims for breach of fiduciary duty and negligence arising from Defendants' challenged conduct here. Finding that all of their claims are derivative in nature, I then examine Plaintiffs' arguments for why demand should be excused as to their derivative claims.

1. Plaintiffs have not properly stated direct claims under Counts IV and V

Plaintiffs contend that, under the governing Delaware standard found in *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*,[99] their claims against Defendants are not exclusively derivative.

In *Tooley*, the Supreme Court explained that to determine whether a claim is direct or derivative, a court must look exclusively to (1) who suffered the alleged harm and (2) who would receive the benefit of any recovery or other remedy.[100] The manner in which a plaintiff labels its claim and the form of words used in the complaint are not dispositive; rather, the court must look to the nature of the wrong alleged, taking into account all of the facts alleged in the complaint, and determine for itself whether a direct claim exists.[101] As to the first prong of *Tooley*, the "stockholder's claimed direct injury must be independent of any alleged injury to the corporation. . . . [The stockholder] must demonstrate that the duty breached was owed to [it] and that [it] can prevail without

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99 845 A.2d 1031 (Del. 2004).

100 *Id*. at 1035; *see In re J.P. Morgan Chase & Co. S'holder Litig.*, 906 A.2d 808, 817 (Del. Ch. 2005), *aff'd*, 906 A.2d 766 (Del. 2006).

101 *See In re J.P. Morgan Chase*, 906 A.2d at 817; *In re First Interstate Bancorp Consol. S'holder Litig.*, 729 A.2d 851, 860 (Del. Ch. 1998).

showing an injury to the corporation."[102] If the nature of the injury is such that it falls directly on the business entity as a whole and only secondarily on individual investors "as a function of and in proportion to [their] pro rata investment in the [entity]," then the claim is derivative and may be prosecuted only on behalf of the entity as a derivative action.[103] As to the second prong of *Tooley*, "in order to maintain a direct claim, stockholders must show that they will receive the benefit of any remedy."[104]

Plaintiffs argue that they suffered individual injuries separate and distinct from the injuries suffered by Nominal Defendants. Specifically, they argue that Nominal Defendants did not suffer an actual loss at the time their Affected Funds purchased the Challenged Securities, but rather would suffer one when they sold them and realized a loss. Pointing to the unique structure of series mutual funds and the fact that the NAV of each of the Affected Funds was recalculated on a daily basis, Plaintiffs contend that they suffered an additional, direct harm in that "[e]very day that there was a downward adjustment based on a decline in the market value of the [Challenged Securities], Plaintiffs suffered actual injury – a reduction in the calculated value of their shares – even

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102 *Tooley*, 845 A.2d at 1039; *In re J.P. Morgan Chase*, 906 A.2d at 817.

103 *Kelly v. Blum*, 2010 WL 629850, at *9 n.63 (Del. Ch. Feb. 24, 2010); *In re Triarc Cos.*, 791 A.2d 872, 878 (Del. Ch. 2001).

104 *Albert v. Alex. Brown Mgmt. Servs., Inc.*, 2005 WL 2130607, at *13 (Del. Ch. Aug. 26, 2005); *Big Lots Stores, Inc. v. Bain Capital Fund VII, LLC*, 922 A.2d 1169, 1179 (Del. Ch. 2006) (noting that a direct claim is one in which "no relief flows to the corporation").

though the Funds had not necessarily realized any loss at all."[105] Put simply, Plaintiffs argue that because the NAV of each Affected Fund, and, thus, the contractual redemption price of their shares, was recalculated daily, Plaintiffs suffered a direct injury apart from the injury the Funds themselves would suffer when they eventually sold the securities.

Except for *Gentile v. Rossette*, discussed *infra*, Plaintiffs cited no Delaware authority for this proposition. Instead, they rely on *Strigliabotti v. Franklin Resources, Inc.*, a case from the Federal District Court for the Northern District of California. There, plaintiffs, stockholders in several mutual funds in the Franklin Templeton fund complex, brought suit against various defendant-investment advisors who provided services to such mutual funds. The plaintiffs claimed that, among other things, the defendants had charged the funds excessive fees in violation of § 36(b) of the ICA.[106] Citing to, among other cases, *Tooley*, the court stated that it had to decide whether there was a corporate injury to determine whether the plaintiffs' claims against the defendants were derivative or direct.[107] The court in *Strigliabotti* held that the claims were direct and the plaintiffs had alleged injury to themselves, and not to the funds, because "the financial harm from

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105 PAB 49. Plaintiffs assert that they suffered lost profits, or the "loss in value that their shares would have had if, the Funds' portfolio had been invested in lawful investments." *Id*.

106 *Strigliabotti v. Franklin Res., Inc.*, 2005 WL 645529, at *1 (N.D. Cal. Mar. 7, 2005).

107 *Id*. at *8.

overcharges is harm to the individual investors, who own the Funds' assets and bear its expenses directly on a pro rata basis."[108]

The holding in *Strigliabotti* is not controlling in this case for at least three reasons. First, as a decision from a California federal court, it is not binding on this Court.[109] Second, courts from other jurisdictions have questioned its reasoning[110] and at least one later decision by another California district court held, in a similar context, that the plaintiffs could not state a direct claim.[111] Finally, and most importantly, courts in other

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108 *Id*. In addition to *Strigliabotti*, at least one other case has found that the unique structure of mutual funds and the manner in which their NAVs are calculated permits stockholders to sue directly on claims alleging unlawful conduct that diminishes the value of a fund's portfolio. *See In re Mut. Funds Inv. Litig.*, 590 F. Supp. 2d 741, 746 (D. Md. 2008). As discussed in the text, however, I do not consider the reasoning of these cases on this issue persuasive.

109 *See Meso Scale Diags., LLC v. Roche Diags. GmbH*, 2011 WL 1348438, at *13 (Del. Ch. Apr. 8, 2011).

110 *See, e.g.*, *Hogan v. Baker*, 2005 WL 1949476, at *4 (N.D. Tex. Aug. 12, 2005) ("Plaintiffs point to *Strigliabotti* . . . which allowed an investor to proceed with a direct action based on the 'unique structure' of mutual funds. . . . However, the Court is unpersuaded that the distinction between mutual fund ownership and stock ownership described by Plaintiffs is sufficient to transform their claims from derivative to direct. . . . While *Strigliabotti* is on point, its reasoning is at odds with the overwhelming majority of courts who have addressed this issue. In fact, *Strigliabotti* does not cite any applicable case law in reaching its holding.") (internal citations omitted); *Stegall v. Ladner*, 394 F. Supp. 2d 358, 365 (D. Mass. 2005) ("To the extent *Strigliabotti* stands for the proposition that mutual fund investors enjoy the right to a direct action simply because the value of shares in the fund are computed daily on a pro rata basis, I find it unpersuasive.").

111 *See Mutchka v. Harris*, 373 F. Supp. 2d 1021, 1027-28 (C.D. Cal. 2005); *see also Hogan*, 2005 WL 1949476, at *4 ("Further, the facts in *Mutchka v. Harris*, . . . a conflicting case decided after *Strigliabotti*, are practically identical to the facts in the case at hand. In *Mutchka*, the court quickly rejected the exact argument that Plaintiffs make here. . . . Instead of focusing on the 'unique structure' of mutual funds, the *Mutchka* court focused on whether the investors' injury was distinct

jurisdictions who have considered the issue have determined that the conclusion reached in *Strigliabotti* was inconsistent with Delaware law.[112]

I concur with these courts' interpretations of Delaware law and find, on the facts pled in the Complaint, that Plaintiffs have failed to allege an injury separate and distinct from an injury alleged to have been suffered by the Affected Funds of Nominal Defendants. The unlawful conduct asserted by Plaintiffs in relation to the Trustee Defendants essentially involves Trustee mismanagement in purchasing and then holding the Challenged Securities. Under Delaware law, allegations of trustee or director mismanagement regarding securities portfolio investments generally are considered derivative in nature.[113]

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from that suffered by the corporation. . . . The *Mutchka* court reasoned that an investor, whether investing in stocks or mutual funds, is not injured by a diminution in share value until he sells his shares and 'the fact that the funds' value is calculated daily does not make the alleged injury any more direct.' ").

[112] *See, e.g.*, *In re Goldman Sachs Mut. Funds Fee Litig.*, 2006 WL 126772, at *6 (S.D.N.Y. Jan. 17, 2006) ("We are not persuaded that [*Strigliabotti's*] holding, which applied a similar (though not identical) standard for derivative suits under California law, is consistent with Delaware law. Rather, a pro rata bearing of expenses by individual shareholders seems to fall within the very essence of an injury which is not independent from that suffered by the corporation."); *Hogan*, 2005 WL 1949476, at *4 ("the misconduct alleged by Plaintiffs did not injure Plaintiffs or any other Fundholders directly, but instead injured them indirectly as a result of their investment in the Funds. Further, several courts applying Delaware law have held that if the only injury to an investor is the indirect harm which consists of the diminution in the value of his or her shares, the suit must be derivative.") (internal citations omitted).

[113] *See Albert v. Alex. Brown Mgmt. Servs., Inc.*, 2005 WL 2130607, at *13 (Del. Ch. Aug. 26, 2005) ("The gravamen of these claims is that the Managers devoted inadequate time and effort to the management of the Funds, thereby causing their large losses. Essentially, this is a claim for mismanagement, a paradigmatic

Plaintiffs argue, however, that the "series" structure of the Nominal Defendants makes investors in Vanguard Global and Vanguard European "essentially a minority class of shareholders of Nominal Defendants" who share no common interests with investors in the other seven series of funds offered by Nominal Defendants"[114] Based on this premise, Plaintiffs contend that the injury suffered by the holders of shares in the Affected Funds was not inflicted on holders of the other series of funds or on the Nominal Defendants themselves because each series of securities is segregated from the rest.

The focus of Plaintiffs' argument is wrong and inconsistent with the distinction drawn between direct and derivative claims. I consider it more appropriate to compare the alleged injury suffered by Plaintiff-stockholders with that allegedly suffered by the Affected Fund in which they invested, rather than with the alleged harm to the Nominal Defendants. For one thing, each series within a series mutual fund complex acts as a completely segregated fund in the business of investing in securities.[115] Besides being considered a discrete economic unit, each series often is treated as a separate investment company for various purposes under the ICA, even though it may not have separate legal form and may be covered under the umbrella of a single trust entity, like Nominal

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derivative claim."); *In re Evergreen Mut. Funds Fee Litig.*, 423 F. Supp. 2d 249, 261 (S.D.N.Y. 2006); *Weinstein v. Appelbaum*, 193 F. Supp. 2d 774, 782 (S.D.N.Y. 2002).

114 PAB 50.

115 *See* Joseph R. Fleming, *Regulation of Series Investment Companies Under the Investment Company Act of 1940*, 44 BUS. LAW. 1179, 1181 (1989).

Defendants.[116] For another thing, courts in various jurisdictions have recognized the independent nature of each series within mutual fund trust entities in determining that stockholders who invested in one or a few mutual fund series within a single trust do not have standing to assert claims for purported wrongdoing on behalf of all of the series within that trust.[117] In addition, the fact that Plaintiffs brought suit against Nominal Defendants "d/b/a" the Affected Funds further supports my inclination to compare the alleged injuries of the Affected Funds to the injuries claimed by the stockholder-Plaintiffs. Finally, doing so would comport with the Delaware Statutory Trust Act ("DSTA"), which permits a statutory trust, through its governing instrument, to treat

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116 *See id*. at 1179-81 ("With a few notable exceptions, the [SEC] and its staff have applied the provisions of the [ICA] to a series fund as if the individual portfolios of that fund were separate investment companies.").

117 *See, e.g.*, *Stegall v. Ladner*, 394 F. Supp. 2d 358, 362-63 (D. Mass. 2005) (noting that in certain contexts, each series within a trust is treated as a separate corporate entity with separate management contracts and share distribution plans, which prevents plaintiffs from using the corporate structure of the broader investment company to confer standing across all funds within the same company, even if each series fund is not separately incorporated); *Williams v. Bank One Corp.*, 2003 WL 22964376, at *1 (N.D. Ill. Dec. 15, 2003) ("There is no precise parallel to the described arrangement in the corporate world, but the closest analogy still seems to be that of separate subsidiaries (the various mutual funds) that share a common parent (the Massachusetts business trust). What controls over the other factors identified in counsel's submission is the total separateness of the beneficial interest in the funds, with [the plaintiff] being a shareholder in only two of them. [His] small holdings in those two funds provide no justification for using them as a springboard for him to act on behalf of the umbrella Massachusetts trust . . . ."); *In re Am. Mut. Funds Fee Litig.*, 2005 WL 3989803, at *1-2 (C.D. Cal. Dec. 16, 2005).

different series within the trust as distinct economic entities.[118] Indeed, Nominal Defendants have elected to so treat certain assets and liabilities of each series under their respective declarations of trust (collectively, the "Declarations").[119]

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[118] *See, e.g.*, 12 *Del. C.* §§ 3804(a) ("in the event that the governing instrument of a statutory trust, including a statutory trust which is a registered investment company under the [ICA] . . . creates 1 or more series as provided in § 3806(b)(2) of this title, and if separate and distinct records are maintained for any such series and the assets associated with any such series are held in such separate and distinct records . . . and accounted for in such separate and distinct records separately from the other assets of the statutory trust, or any other series thereof, and if the governing instrument so provides, and notice of the limitation on liabilities of a series as referenced in this sentence is set forth in the certificate of trust of the statutory trust, then the debts, liabilities, obligations and expenses incurred, contracted for or otherwise existing with respect to a particular series shall be enforceable against the assets of such series only, and not against the assets of the statutory trust generally or any other series thereof, and, unless otherwise provided in the governing instrument, none of the debts, liabilities, obligations and expenses incurred, contracted for or otherwise existing with respect to the statutory trust generally or any other series thereof shall be enforceable against the assets of such series."); 3805(h) ("Except to the extent otherwise provided in the governing instrument of the statutory trust, where the statutory trust is a registered investment company under the [ICA] . . . any class, group or series of beneficial interests established by the governing instrument with respect to such statutory trust shall be a class, group or series preferred as to distribution of assets or payment of dividends over all other classes, groups or series in respect to assets specifically allocated to the class, group or series as contemplated by § 18 (or any amendment or successor provision) of the [ICA] . . . provided that this section is not intended to affect in any respect the provisions of § 3804(a) of this title."); 3806(b)(2) ("A governing instrument may contain any provision relating to the management of the business and affairs of the statutory trust . . . [including] establish[ing] or provid[ing] for the establishment of designated series of trustees, beneficial owners, assets or beneficial interests having separate rights, powers or duties with respect to specified property or obligations of the statutory trust or profits and losses associated with specified property or obligations, and, to the extent provided in the governing instrument, any such series may have a separate business purpose or investment objective . . . .").

[119] *See, e.g.*, Aff. of Brian C. Ralston ("Ralston Aff.") Ex. A, Amended and Restated Agreement and Declaration of Trust of Vanguard International Equity Index

Against this background, I find that each stockholder who held shares in Vanguard European and Vanguard Global suffered an alleged injury based on their pro rata ownership of shares in those Funds. The decline in the share prices of the Challenged Securities would have exerted downward pressure on the NAV of each Affected Fund, which, in turn, allegedly caused a concomitant negative effect on the redemption value of each stockholder's Affected Fund investment. Thus, any injury to Plaintiffs based on a diminution of the value of their shares is secondary and derivative to the alleged injury suffered by the Funds themselves.[120]

Funds ("VIEIF Declaration"), Art. III § 6(a)-(b); *id*. Ex. B, Amended and Restated Agreement and Declaration of Trust of Vanguard Horizon Funds ("VHF Declaration"), Art. III § 6(a)-(b).

120 *See Gentile v. Rossette*, 906 A.2d 91, 99 (Del. 2006) ("any dilution in value of the corporation's stock is merely the unavoidable result (from an accounting standpoint) of the reduction in the value of the entire corporate entity, of which each share of equity represents an equal fraction. In the eyes of the law, such equal 'injury' to the shares resulting from a corporate overpayment is not viewed as, or equated with, harm to specific shareholders individually.") Moreover, the manner in which NAVs are recalculated on a daily basis does not change the fact that the harm allegedly suffered by investors in each of the Affected Funds is the same harm allegedly suffered by those Funds. *See*, *e.g.*, *Mutchka v. Harris*, 373 F. Supp. 2d 1021, 1027-28 (C.D. Cal. 2005) ("Furthermore, the fact that the funds' [NAV] is calculated daily does not make the alleged injury any more direct because the injury is not realized until an investor[] sells his or her shares of the fund. In that respect, mutual funds are no different than stock ownership, where the value of shares is calculated by the marketplace with each and every trade. The Court therefore finds that the Mutchkas' negligence and breach of fiduciary claims allege an injury to the funds, and thus must be brought derivatively."); *Stegall v. Ladner*, 394 F. Supp. 2d 358, 366 (D. Mass. 2005) ("I do not see how that calculation is materially different from fluctuating daily prices of shares held by stockholders of publicly traded corporations. The assets remain those of the fund, as the earnings are of a corporation until distributed. The mutual fund participant has a right to those assets, but that right derives from-is derivative of-the fund.").

Even if I compare the alleged injury of investors in the Affected Funds to the alleged injury suffered by Nominal Defendants, and not solely to the relevant Affected Funds, I still would find that Plaintiffs failed to allege an independent injury. Plaintiffs assert that only they, and not stockholders in the other seven series of funds in Nominal Defendants, were harmed by the Challenged Securities purchases here. Nevertheless, the injury of which they complain was caused by a diminution in the Affected Funds' share values unconnected to any violation of voting rights or allegation that the Affected Funds were singled out to have their share values diminished to benefit one or more of the other series. In this situation, harm can be said to have fallen directly on Nominal Defendants, as the umbrella entity controlling the Affected Funds, and only indirectly in pro rata fashion on stockholders who owned shares in those Funds.[121] Therefore, I find that under the first prong of *Tooley*, Plaintiffs have not demonstrated that they suffered an injury independent from that suffered by the Affected Funds or Nominal Defendants.

Turning to the second prong of *Tooley*, I must consider who would receive the benefit of any remedy obtained as a result of Defendants' alleged wrongdoing. Assuming that Plaintiffs succeed in proving that, for example, Defendants breached their fiduciary

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[121] *See Lapidus v. Hecht*, 232 F.3d 679, 683 (9th Cir. 2000) ("A shareholder does not acquire standing to maintain a direct action when the alleged injury is inflicted on the corporation and the only injury to the shareholder is the indirect harm which consists of the diminution in the value of his or her shares. . . . While it is true that only shareholders in the series corresponding to the fund, and not shareholders in the other ten series, were affected by the allegedly improper issuance of senior securities, an injury caused simply by the alleged issuance of senior securities unconnected to any violation of voting rights would be an injury to the trust generally. Therefore, any harm to the fund-series shareholders arising from such an issuance of securities would be only indirect.") (internal citations omitted).

duties to the Affected Funds, it is logical to assume that the remedy for that breach would go to those Funds only, and not the other series within Nominal Defendants. Such a remedy would not be inconsistent with the provisions of the DSTA or Nominal Defendants' respective Declarations. Moreover, Plaintiffs have not cited any case law or other authority or reasoning that would preclude imposition of a remedy that would flow to the Affected Funds only. Such a remedy would support my conclusion that Counts IV and V are not properly pleaded as direct claims.

Plaintiffs posit that perhaps the remedy would flow to Nominal Defendants and, in that case, benefit all of their series of funds, and not just the Affected Funds. Defendants concede, however, that any remedy obtained as a result of injury to the Affected Funds would "flow to the [Affected] Funds directly and only indirectly to [their] shareholders on a pro rata basis."[122] Again, Plaintiffs have not cited any case or provided any analysis as to why a derivative remedy must flow to Nominal Defendants and not the specific funds in them that supposedly were harmed by Defendants' conduct. Therefore, I find this argument unpersuasive.[123]

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122 TRB 25

123 Plaintiffs also make two subsidiary arguments regarding *Tooley's* second prong. First, they contend that proceeding exclusively on their derivative claims would result in only those who owned shares at the time of recovery being able to share in the remedy, which would be an investor population different from the "group that owned shares at the time of the injury." PAB 50. I find no merit in this argument. That certain stockholders no longer own shares of the Affected Funds does not change the derivative nature of the harm alleged by Plaintiffs. Rather, it means that those investors no longer have standing to pursue a derivative claim. Indeed, to proceed derivatively against a Delaware statutory trust, a plaintiff has the burden of satisfying a continuous ownership requirement. 12 *Del. C.* §

Moreover, Plaintiffs do not argue that their claims for breach of fiduciary duty and negligence in Counts IV and V are exclusively direct. Rather, as reflected in the substantively identical claims in Counts I and II, they argue that under *Gentile* those claims are simultaneously both derivative and direct. Plaintiffs' reliance on *Gentile* is misplaced, however. In that case, the Supreme Court identified a situation in which minority stockholders may bring both derivatively and directly a claim for breach of fiduciary duties based on "a species of corporate overpayment claim."[124] Such a claim arises where: "(1) a stockholder having majority or effective control causes the corporation to issue 'excessive' shares of its stock in exchange for assets of the controlling stockholder that have a lesser value; and (2) the exchange causes an increase in the percentage of the outstanding shares owned by the controlling stockholder, and a corresponding decrease in the share percentage owned by the public (minority)

3816(b) ("In a derivative action, the plaintiff must be a beneficial owner at the time of bringing the action . . . ."); *see also Lewis v. Anderson*, 477 A.2d 1040, 1049 (Del. 1984); *Strategic Asset Mgmt., Inc. v. Nicholson*, 2004 WL 2847875, at *1-2 (Del. Ch. Nov. 30, 2004).

Plaintiffs also argue that the "cost of a judgment in favor of Plaintiffs against Vanguard would fall disproportionately on the holders of the other seven series of shares offered by Nominal Defendants." PAB 50. As such, they contend that the interests of stockholders of the Affected Funds are different from the interests of the stockholders of the other series within Nominal Defendants. This argument also is unpersuasive. The relevant inquiry in determining whether a claim is direct or derivative is supplied in *Tooley*, which focuses on who suffered the alleged injury and who would receive the benefit of a remedy for that injury. *See Tooley*, 845 A.2d at 1033. Plaintiffs have cited no authority for shifting the focus to identifying the entities that might have to contribute to a potential remedy for an alleged injury.

[124] *See Gentile v. Rossette*, 906 A.2d 91, 99-100 (Del. 2006).

shareholders."[125] The "limited circumstances involving controlling stockholders" that gave rise to a dual direct and derivative claim in *Gentile* simply do not exist in the circumstances of this case.[126] Plaintiffs have not alleged that the Affected Funds or Nominal Defendants have a controlling stockholder, let alone that a controlling stockholder caused those entities to enter into a transaction that caused, among other things, a redistribution to the controlling stockholder of a portion of the economic value and voting power embodied in minority stockholders' interests.[127] Moreover, Plaintiffs have not alleged that any Defendants sought to confer a benefit on other fund series

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125 *See id.* In holding that this situation gives rise to a derivative claim, the Court observed that "[b]ecause the means used to achieve [the transaction's] result is an overpayment . . . of shares to the controlling stockholder, the corporation is harmed and has a claim to compel the restoration of the value of the overpayment. *Id.* at 100. But, it further explained that such a situation also gives rise to direct claims for the public or minority stockholders of the corporation because "the end result of this type of transaction is an improper transfer . . . of economic value and voting power from the public shareholders to the majority or controlling stockholder. For that reason, the harm resulting from the overpayment is not confined to an equal dilution of the economic value and voting power of each of the corporation's outstanding shares. A separate harm also results: an extraction from the public shareholders, and a redistribution to the controlling shareholder, of a portion of the economic value and voting power embodied in the minority interest." *Id.*

126 *See Feldman v. Cutaia*, 951 A.2d 727, 728-29 (Del. 2008); *see also Dubroff v. Wren Hldgs., LLC*, 2009 WL 1478697, at *3 (Del. Ch. May 22, 2009) (describing the circumstances in which a claim is both direct and derivative under *Gentile* as "unique"); *Green v. LocatePlus Hldgs. Corp.*, 2009 WL 1478553, at *2 (Del. Ch. May 15, 2009) (similarly describing a dual-natured claim under *Gentile* as occurring in a "specific situation.").

127 As discussed *supra*, because of the nature and structure of series mutual funds, I reject Plaintiffs' suggestion that each series within a fund complex should be viewed as containing a series of minority stockholders of a larger entity.

within either Nominal Defendant at the expense of the Affected Funds. On the facts alleged in the Complaint, therefore, *Gentile* is inapposite.

Having carefully considered Plaintiffs' arguments that Counts IV and V of their Complaint qualify as direct claims under *Tooley*, I find they are without merit and hold that Plaintiffs have stated derivative claims only. Thus, I will dismiss with prejudice Counts IV and V of the Complaint.

2. Is demand excused?

Having concluded that Plaintiffs' claims are all derivative, I now address Defendants' argument that Plaintiffs were required to make a demand on the Board of Trustees or demonstrate that such a requirement was excused. Plaintiffs concede that they did not make a demand, but argue that the Complaint pleads sufficient facts from which I may infer that their failure to do so was excused.

Under Court of Chancery Rule 23.1, a derivative complaint must "allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors . . . and the reasons for the plaintiff's failure to obtain the action or for not making the effort."[128] Under this rubric, Delaware courts typically apply one of two tests for determining whether a complaint should be dismissed for failure adequately

[128] Ct. Ch. R. 23.1(a). Like Rule 23.1, § 3816(c) of the DSTA, which applies because Nominal Defendants are Delaware statutory trusts, provides that plaintiffs have the burden to plead with particularity in their complaint the efforts, if any, that they took "to secure initiation of the action by the trustees, or the reasons for not making the effort." 12 *Del. C.* § 3816(c). While plaintiffs do not need to plead evidence, they must do more than offer conclusory statements or mere notice pleading. *See Brehm v. Eisner*, 746 A.2d 244, 254-55 (Del. 2000).

to plead demand futility. First, the *Aronson* test applies to claims involving contested board action with respect to a specific transaction or conscious business decision.[129] It states that demand on a board is excused only if the complaint contains particularized factual allegations that raise a reasonable doubt that either: (1) the board of directors are disinterested and independent; or (2) a challenged transaction or conduct was otherwise the product of a valid exercise of business judgment.[130]

The *Rales* test, on the other hand, applies in lieu of the *Aronson* test where the subject of a derivative suit is not a board decision but rather a board's inaction leading to a violation of its oversight duties.[131] Under this test, to determine whether demand is excused, a court must examine whether the board that would be addressing the plaintiff's demand is capable of impartially considering its merits without being influenced by "improper considerations."[132] Specifically, a court must determine whether "the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint is filed, the board of directors could

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129 *See Aronson v. Lewis*, 473 A.2d 805, 813 (Del. 1984), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000); *Wood v. Baum*, 953 A.2d 136, 140 (Del. 2008).

130 *See, e.g.*, *White v. Panic*, 783 A.2d 543, 551 (Del. 2001); *Aronson v. Lewis*, 473 A.2d at 814.

131 *Wood*, 953 A.2d at 140; *Rales v. Blasband*, 634 A.2d 927, 933-34 (Del. 1993) (noting that the *Aronson* test should not be applied "(1) where a business decision was made by the board of a company, but a majority of the directors making the decision have been replaced; (2) where the subject of the derivative suit is not a business decision of the board; and (3) where . . . the decision being challenged was made by the board of a different corporation.").

132 *Rales*, 634 A.2d at 934.

have properly exercised its independent and disinterested business judgment in responding to a demand."[133] As under the *Aronson* test, *Rales* requires that a majority of the board to which a demand would be made "be able to consider and appropriately to respond to a demand 'free of personal financial interest and improper extraneous influences.'"[134] Under *Rales*, therefore, demand is excused if the Court finds that there is "a reasonable doubt that a majority of the Board would be disinterested or independent in making a decision on demand."[135]

Plaintiffs argue that demand is excused here under *Rales* because the Complaint pleads facts that create a reasonable doubt that a majority of the Trustee Defendants are disinterested or independent. In particular, they point to the fact that the Trustee Defendants failed to take appropriate action after becoming aware of the other Defendants' wrongdoing in causing the Affected Funds to purchase and hold the Challenged Securities. Defendants quibble with Plaintiffs' assertion that *Rales* governs this case and, instead, argue that *Aronson* applies because the Complaint alleges that Trustee Defendants, with the other Defendants, "knowingly caused, and participated in a scheme to cause, the [Affected Funds] to purchase stock in one or more illegal gambling

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133 *Id*.; *Wood*, 953 A.2d at 140-41.

134 *Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart*, 833 A.2d 961, 977 (Del. Ch. 2003), *aff'd*, 845 A.2d 1040 (Del. 2004) (internal citations omitted).

135 *Id*. (internal quotation marks omitted).

businesses," which Defendants characterize as allegations of "affirmative board action."[136]

I need not resolve this dispute, however, because, as discussed below, I find that the Complaint does not allege particularized facts sufficient to cast reasonable doubt on the independence or disinterestedness of Trustee Defendants under either *Aronson* or *Rales*.[137]

a. Statutory independence and disinterestedness

As Nominal Defendants are Delaware trusts and, thus, creatures of statute, I look first to the DSTA for the applicable standard for independence and disinterestedness. A stockholder-plaintiff may bring a derivative action on behalf of the statutory trust in which they own shares without making a pre-suit demand "if an effort to cause [the trust's trustees] to bring the action *is not likely to succeed*."[138] The DSTA is enabling in nature and, as such, permits a trust through its declarations of trust to delineate additional standards and requirements with which a stockholder-plaintiff must comply to proceed derivatively in the name of the trust.[139] The Declarations for both VIEIF and VHF have done just that; they contain identical provisions which provide that:

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136 TRB 9.

137 *See Guttman v. Huang*, 823 A.2d 492, 500 (Del. Ch. 2003) ("the differences between the *Rales* and the *Aronson* tests in the circumstances of this case are only subtly different, because the policy justification for each test points the court toward a similar analysis.").

138 12 *Del. C.* § 3816(a) (emphasis added).

139 *See id*. § 3816(e).

> [A] demand on the Trustees shall only be deemed not likely to succeed and therefore excused if a majority of the Board of Trustees, or a majority of any committee established to consider the merits of such action, is composed of Trustees who are not "independent trustees" (as that term is defined in the [DSTA]).[140]

The DSTA defines "independent trustee" as any trustee who is not an "interested person" of the trust, as that term is defined in the ICA.[141]

In interpreting the interplay between the relevant portions of the DSTA and the ICA, one federal court explained that a trustee is an "interested person" under the ICA if he is an "affiliated person," which means that the trustee is "controlled" by or "controls" its investment advisor.[142] The ICA defines "control" as the "power to exercise a controlling influence over the management or policies of a company, unless such power

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140 *See* VIEIF Declaration Art. VIII § 10(a); VHF Declaration Art. VIII § 10(a). The provisions of Nominal Defendants' Declarations "are not subject to reasonable dispute because they are capable of accurate and ready determination by resort to 'sources whose accuracy cannot reasonably be questioned,'" *i.e.*, SEC documents. *See MicroStrategy Inc. v. Acacia Research Corp.*, 2010 WL 5550455, at *4 (Del. Ch. Dec. 30, 2010). Therefore, I properly may take judicial notice of them.

141 *See* 12 *Del. C.* § 3801(d).

142 *Boyce v. AIM Mgmt. Gp., Inc.*, 2006 WL 4671324, at *5 (S.D. Tex. Sept. 29, 2006); *see also Migdal v. Rowe Price-Fleming Int'l, Inc.*, 248 F.3d 321, 329 (4th Cir. 2001) ("'Disinterested directors are . . . those [] who are not 'affiliated' with the fund's investment adviser-i.e., they are not 'controlled' by the investment adviser"; 15 U.S.C. § 80a-2(a)(3) (defining "affiliated person" to mean, among other things, "(C) any person directly or indirectly controlling, controlled by, or under common control with, such other person; (D) any officer, director, partner, copartner, or employee of such other person; [and] (E) if such other person is an investment company, any investment adviser thereof or any member of an advisory board thereof[.]").

is solely the result of an official position with such company."[143] It further specifies, however, that a natural person will be presumed not to be a controlled person.[144] In addition, pursuant to the DSTA, if a trustee is not an interested person under the ICA, he will be deemed to be independent and disinterested for all purposes.[145] Thus, because the Trustee Defendants to whom Plaintiffs would have needed to make their demand are natural persons, they are presumed to be independent and disinterested for all purposes under Delaware law.[146]

To rebut this presumption, Plaintiffs, again, point the Court to the "unique structure" of series mutual funds as placing the Trustee Defendants in a web of "multiple, serious, actual, and irreconcilable conflicts."[147] They highlight, in particular, two such conflicts as preventing Trustee Defendants from acting as disinterested and independent trustees. First, they focus on the fact that the Trustees constitute the entire Board of Trustees of Nominal Defendants as well as the board of directors of Vanguard, a primary Defendant. As such, Plaintiffs contend that the Trustee Defendants have an irreconcilable conflict because they cannot carry out their fiduciary duties owed to

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143 15 U.S.C. § 80a-2(a)(9).

144 *Id*.; *Boyce*, 2006 WL 4671324, at *5. This presumption is rebuttable. *See* 15 U.S.C. § 80a-2(a)(9).

145 *See* 12 *Del. C.* § 3801(d); *In re Goldman Sachs Mut. Funds Fee Litig.*, 2006 WL 126772, at *11 (S.D.N.Y. Jan. 17, 2006) ("Under Delaware law, trustees who are not 'interested' under the ICA 'shall be deemed independent and disinterested for all purposes.'").

146 *See Boyce*, 2006 WL 4671324, at *5.

147 PAB 35.

Nominal Defendants who are suing Vanguard, when they also owe fiduciary duties to Vanguard. Second, Plaintiffs argue that the Trustee Defendants face another irreconcilable conflict because they also serve as the trustees for every other investment company managed by Vanguard within the Vanguard Complex. Specifically, because each investment company has a financial interest in Vanguard, they contend that a decision to pursue the interests of stockholders in Nominal Defendants against Vanguard would be contrary to the interests of the stockholders in the other investment companies managed by Vanguard.[148]

Preliminarily, I find no merit in Plaintiffs suggestion that the Trustees' service on multiple boards of statutory trusts within the same series mutual fund complex makes them interested persons for purposes of the ICA. First, the ICA makes clear that "no person shall be deemed to be an interested person of an investment company solely by reason of . . . his being a member of its board of directors . . . ."[149] The DSTA further provides that

> the receipt of compensation for service as an independent trustee of the statutory trust and also for service as an independent trustee of 1 or more other investment companies managed by a single investment adviser (or an "affiliated person" (as such term is defined [in the ICA]) of such

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148 Plaintiffs also argue that the Trustees made "'sizeable personal investments' as 'private individuals' in the funds they oversee – and therefore in Vanguard itself," which allegedly demonstrates that they have personal interests in conflict with the interests of Nominal Defendants. *Id*. at 39-40.

149 15 U.S.C. § 80a-2(a)(19)(A).

> investment adviser) shall not affect the status of a trustee as an independent trustee under this chapter.[150]

Moreover, neither the ICA nor the SEC prohibits the use of multi-board membership within mutual fund complexes.[151] Indeed, "membership on the boards of several funds within a mutual fund complex is the prevailing practice in the industry."[152] Thus, as courts in other jurisdictions and in similar contexts have held previously, I hold that trustees who serve on multiple boards within the same mutual fund complex are not *per se* interested persons under the ICA, even though pursuing one fund's interests within the complex might adversely affect the complex's other funds.[153] Thus, service on multiple boards alone is insufficient to cast reasonable doubt on a trustee's ability to exercise his business judgment as to whether to accept a stockholder's demand to bring suit against a board of trustees or others.

Plaintiffs argue, however, that they have pled more than the Trustees' mere service on multiple investment company boards within the same complex. They emphasize that

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150 12 *Del. C.* § 3801(d).

151 *Migdal v. Rowe Price-Fleming Int'l, Inc.*, 248 F.3d 321, 330-31 (4th Cir. 2001).

152 *Id*.

153 *See, e.g.*, *id*.; *Seidl v. Am. Century Cos.*, 713 F. Supp. 2d 249, 261-62 (S.D.N.Y. 2010) ("To hold otherwise would essentially nullify the demand requirement in situations where the corporation is an investment firm with multiple related funds."); *In re Mut. Funds Inv. Litig.*, 384 F. Supp. 2d 873, 878-79 (D. Md. 2005); *Krantz v. Fid. Mgmt. & Research Co.*, 98 F. Supp. 2d 150, 157 (D. Mass. 2000); *see also* IMO The Vanguard Gp., Investment Company Act Release No. 11645, 1981 WL 36522, at *5 n.35, 22 S.E.C. Docket 238 (Feb. 25, 1981) ("Interlocking boards of directors within a[] [mutual fund] investment complex are neither prohibited nor uncommon.") ("SEC Release No. 11645").

the same Board of Trustees that oversees Nominal Defendants and other trusts within the Vanguard Complex also serves as the board of Vanguard itself, a principal Defendant here.

This additional fact, however, does not automatically make the Trustee Defendants interested persons under the ICA. Under § 80a-2a(3)(E), for example, a company that is an "investment advisor," such as Vanguard, generally is an "affiliated person" and, as such, an "interested person" of the company it advises (*i.e.*, Nominal Defendants).[154] But, because Vanguard provides its services to Nominal Defendants at cost,[155] it is excluded from the definition of "investment advisor" and, thus, "affiliated person" in § 80a-2(a)(3)(E) of the ICA.[156] Thus, Trustees' membership on the board of Vanguard does not make them affiliates of Vanguard and, therefore, interested persons under this provision of the ICA.

Another basis on which Plaintiffs arguably might rely to demonstrate an affiliation between Nominal Defendants and Vanguard is § 80a-2(a)(3)(C), which provides that a person is an affiliate of another if he or she directly or indirectly controls, is controlled by, or is under common control with such other person.[157] Control is defined to mean

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154 15 U.S.C. §§ 80a-2(a)(3)(E), 2(a)(20).

155 *See* SEC Release No. 11645, 1981 WL 36522, at *2; *see also* Aff. of Thomas I. Sheridan, III ("Sheridan Aff.") Ex. R at B-19.

156 15 U.S.C. § 80a-2(a)(20) (noting that the definition of "investment advisor" does not include "a company furnishing such services at cost to one or more investment companies, insurance companies, or other financial institutions").

157 *Id*. § 80a-2(a)(3)(C).

"the power to exercise a controlling influence over the management or policies of a company . . . ."[158] Plaintiffs assert that Vanguard controls Nominal Defendants in that it has a "legally enforceable right to prevent Trustees from taking any action that would be contrary to [Vanguard's] interests" and has the "practical ability to prevent any such action[] because it has the ability to remove Trustees."[159] The Complaint, however, does not allege specific facts to support these conclusory assertions. The record indicates that Vanguard does not have the ability to remove the Trustee Defendants from their positions at Nominal Defendants because a Trustee may be removed only by a majority vote of the other Trustees or by a super-majority vote of Nominal Defendants' stockholders.[160] In addition, Vanguard is wholly-owned by the approximately thirty-six statutory trusts comprising the Vanguard Complex, including Nominal Defendants, in proportion to their relative net assets.[161] Thus, if there is any control relationship alleged in the Complaint, it is one where Nominal Defendants control Vanguard.

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158 *Id*. § 80a-2(a)(9).

159 PAB 47-48. The Complaint also alleges that Vanguard exerts control over Trustee Defendants because it has the power to appoint them. Compl. ¶ 163. But, this argument is unpersuasive. *See Verkouteren v. Blackrock Fin. Mgmt., Inc.*, 1999 WL 511411, at *3 (S.D.N.Y. Jul. 20, 1999) ("the fact that the directors are initially appointed by [defendant-advisor] 'merely states a fact common to all funds which has not been deemed problematic by the bodies regulating the industry.'"), *aff'd*, 208 F.3d 204 (2d Cir. 2000).

160 *See* VIEIF Declaration Art. IV § 1; VHF Declaration Art. IV § 1; Sheridan Aff. Ex. R at B-22.

161 Compl. ¶ 39; *see also* SEC Release No. 11645, 1981 WL 36522, at *2; *see also* Sheridan Aff. Ex. R at B-19.

This type of control arguably still qualifies as an affiliation between Nominal Defendants and Vanguard under § 80a-2(a)(3)(C). Having carefully considered the Complaint, however, I find that Plaintiffs have failed to plead particularized facts from which I reasonably could infer that Nominal Defendants have sufficient net assets in relation to the other approximately thirty-four trusts in the Vanguard Complex to be able to exercise a controlling influence over Vanguard's management or policies. In fact, other than a brief mention of Vanguard's wholly-owned status, the Complaint does not address the degree of control, if any, that Nominal Defendants exert over Vanguard. Conclusory allegations that Trustee Defendants were appointed or controlled by, or that they control, a trust's investment advisor, without more, are insufficient to excuse demand under the ICA and, therefore, the DSTA.[162]

Moreover, Plaintiffs have offered little else in the way of particularized factual allegations to create a reasonable doubt as to any of the Trustees' disinterestedness or independence. Under this Court's demand futility jurisprudence, "disinterested" generally means "that directors can neither appear on both sides of a transaction nor expect to derive any personal financial benefit from it in the sense of self-dealing, as opposed to a benefit which devolves upon the corporation or all stockholders generally."[163] "Independence" generally means "that a director's decision is based on the

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162 *See In re Goldman Sachs Mut. Funds Fee Litig.*, 2006 WL 126772, at *11 (S.D.N.Y. Jan. 17, 2006).

163 *In re J.P. Morgan Chase & Co. S'holder Litig.*, 906 A.2d 808, 821 (Del. Ch. 2005), *aff'd*, 906 A.2d 766 (Del. 2006) (internal citations omitted).

corporate merits of the subject before the board rather than extraneous considerations or influences."[164]

The Complaint did not allege that one Trustee dominated the others or that the Trustees collectively were dominated by any other Defendant. It similarly did not allege that any of the Challenged Securities purchases were self-interested transactions for any of the Trustees in that they would receive a financial benefit from such purchases that would not be shared by the Affected Funds or their stockholders. Rather, the Complaint avers that Trustee Defendants are interested persons because of the unusually complicated structure of the series mutual fund complex in which they operate. This structure involves the Trustee Defendants in numerous interlocking relationships. Consequently, a demand by Plaintiffs essentially would ask Trustee Defendants to sue themselves in their capacity as Vanguard directors.

This Court is mindful of the importance of considering the facts alleged to determine whether Trustee Defendants would be able to exercise their business judgment in considering a stockholder demand. Having said that, Delaware law does not excuse demand on grounds of self-interest when a plaintiff's argument essentially boils down to a claim that director defendants generally are not inclined to sue themselves.[165] Thus,

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164 *Id*.

165 *See Aronson v. Lewis*, 473 A.2d 805, 818 (Del. 1984), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000); *In re Citigroup Inc. S'holder Deriv. Litig.*, 964 A.2d 106, 121 (Del. Ch. 2009). Delaware courts focus instead on factors such as whether the director defendants faced a "substantial likelihood" of personal liability. *See* discussion, *infra*, Part II.B.2.b.

Plaintiffs have failed to articulate sufficient grounds based on the structure of the Vanguard Complex for finding that a majority of Trustee Defendants lack independence under the Declarations and, therefore, that demand should be excused as not likely to succeed.

b. Substantial likelihood of liability resulting from the challenged conduct

Plaintiffs also argue that Trustee Defendants lack independence and disinterestedness because they face a substantial likelihood of liability arising from their actions with respect to the Challenged Securities and because the conduct at issue was so egregious that it likely was not the product of an exercise of valid business judgment. Plaintiffs appear to concede that these arguments do not satisfy the terms of Nominal Defendants' Declarations or the ICA.[166] Rather, they suggest that satisfying the "not likely to succeed" requirement in the DSTA is not the exclusive means by which a plaintiff may demonstrate demand futility against a board of trustees of a Delaware statutory trust. That proposition is dubious, but I need not address it here because Plaintiffs' other arguments for demand futility are also without merit.

The first of these arguments wholly depends on Plaintiffs' repeated contentions that § 1955 makes passive minority public ownership of gambling enterprises illegal and that the Trustees committed criminal wrongdoing by permitting the Affected Funds in Nominal Defendants to purchase and continue to own the Challenged Securities. This argument seeks to establish demand excusal under the second prong of *Aronson* as well

166 *See* PAB 46.

as *Rales*.[167] To cast reasonable doubt that board action was other than the product of a valid exercise of business judgment under *Aronson's* second prong, a plaintiff must allege particularized facts sufficient to raise "(1) a reason to doubt that the action was taken honestly and in good faith or (2) a reason to doubt that the board was adequately informed in making the decision."[168]

Under *Rales*, directors who face a "substantial likelihood of personal liability are deemed to be interested and, thus, cannot make an impartial decision regarding demand."[169] But, demand will be excused on this basis "only in the rare case" where a plaintiff can demonstrate director conduct that is "so egregious on its face that board approval cannot meet the test of business judgment, and a substantial likelihood of director liability therefore exists."[170]

Plaintiffs have failed to plead sufficient particularized facts either to permit this Court to infer that Trustee Defendants acted or failed to act with regard to the Challenged

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167 *See Guttman v. Huang*, 823 A.2d 492, 501 (Del. Ch. 2003) ("When, however, there are allegations that a majority of the board that must consider a demand acted wrongfully, the *Rales* test sensibly addresses concerns similar to the second prong of *Aronson*. To wit, if the directors face a "substantial likelihood" of personal liability, their ability to consider a demand impartially is compromised under *Rales*, excusing demand.").

168 *In re J.P. Morgan Chase & Co. S'holder Litig.*, 906 A.2d at 824.

169 *In re Dow Chem. Co. Deriv. Litig.*, 2010 WL 66769, at *12 (Del. Ch. Jan. 11, 2010); *Ryan v. Gifford*, 918 A.2d 341, 355 (Del. Ch. 2007) ("Directors who are sued have a disabling interest for pre-suit demand purposes when 'the potential for liability is not a mere threat but instead may rise to a substantial likelihood.'").

170 *See Aronson*, 473 A.2d at 815; *In re Dow Chem. Co. Deriv. Litig.*, 2010 WL 66769, at *12; *In re Citigroup Inc. S'holder Deriv. Litig.*, 964 A.2d at 121 (internal citations omitted).

Securities in bad faith or that they face a substantial likelihood of liability because of their actions or inactions. Again, Plaintiffs' arguments essentially hinge on whether purchasing or owning the Challenged Securities is a crime under § 1955. Having carefully considered the allegations in the Complaint and the submissions and arguments of the parties, I am not convinced that this conduct is criminal.

I begin with the proposition that for demand to be excused on the ground that challenged corporate actions or inactions constituted illegal conduct, the Complaint must plead particularized facts that raise a reasonable doubt about the legality of the conduct or inaction at issue.[171] Section 1955 makes it illegal to, among other things, "own[] all or part of an illegal gambling business."[172] Plaintiffs assert that the word "own" is "clear and unambiguous" and reflects the intent of Congress to make it illegal to passively own stock in an illegal gambling business.

In its simplicity, Plaintiffs' argument has some superficial appeal. There are no factual allegations, however, that stock in gambling businesses was publicly traded when § 1955 originally was enacted in 1970. Moreover, the history of the application of § 1955 shows that Plaintiffs' interpretation of it is anything but clear and unambiguous. Despite having been enacted more than forty years ago and the fact that U.S. investors have been able to passively invest as stockholders in offshore gambling enterprises since the mid 2000s, the Complaint contains no allegation that any law enforcement authority

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171 *See Litt v. Wycoff*, 2003 WL 1794724, at *7 (Del. Ch. Mar. 28, 2003).

172 18 U.S.C. § 1955(a).

or court has interpreted § 1955 to apply to passive public stockholders.[173] Nor have Plaintiffs directed the Court to any instances where government regulatory or law enforcement agencies have brought charges against passive stockholders under § 1955.

The Complaint does allege that a number of individuals associated with offshore gambling enterprises recently have been arrested, prosecuted, or convicted for their conduct relating to those enterprises. These individuals, however, founded or managed directly such enterprises and none of them was penalized solely because he was a stockholder in those entities.[174] Similarly, the Complaint alleges that a number of corporate entities were sanctioned under § 1955. These entities, however, actively had engaged in gambling operations and were not disciplined solely because they invested in securities of other entities who engaged in illegal gambling operations.[175] Thus, as Plaintiffs admit, this issue is one of first impression for any agency or court[176] and, as such, this Court would be the first to hold that § 1955 makes passive minority stock ownership of illegal gambling businesses a crime. In such unchartered waters, this Court

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173 *See* Tr. 64 ("The Court: I've got 40 years [that] the statute has been out there. 40 years that no one has ever asserted this. Nobody's prosecuted anybody for it. Nobody's prosecuting them now. Nobody's recommending they prosecute them now. Mr. Sheridan: That's right. The Court: And all I have is your reading of the statute. Mr. Sheridan: That's right.").

174 *See* Compl. ¶¶ 82, 110-12, 117, 138-39, 141.

175 *See id*. ¶¶ 85, 109, 118, 138, 140. None of the Complaint's allegations regarding media reports about illegal gambling enterprises appear to relate to passive stockholders who invested in those entities. *See id*. ¶ 79.

176 *See* PAB 22.

must proceed with caution, especially where a federal, as opposed to a Delaware, statute is involved.[177]

For purposes of the pending motions to dismiss, I need not determine definitively whether or not passive public stock ownership in an illegal gambling business violates § 1955. Rather, I hold that the Complaint fails to allege sufficient particularized facts to raise a reasonable doubt about the legality of owning publicly traded securities of offshore gambling enterprises. Based on the evidence in the record at this preliminary stage, I find that Plaintiffs have not shown the existence of a reasonable basis to conclude that the word "own" in § 1955 includes passive public minority stockholders.

Therefore, to the extent Plaintiffs argue that Trustees caused the Affected Funds to purchase the Challenged Securities and consciously decided to continue to own them despite reports of a U.S. crackdown on offshore illegal betting enterprises, I find that Trustees did not act in bad faith or in a way that could not possibly have been a legitimate exercise of business judgment. Similarly, I am not persuaded that, to the extent Plaintiffs argue that because Trustees failed to act to sell the securities once they were apprised of the step up in enforcement actions in the mid-2000s, they face a substantial likelihood of liability. This is so because I am not convinced that purchasing or owning securities in publicly traded gambling enterprises is illegal under § 1955. In that regard, to the extent that Plaintiffs argue the media reports and other news of prosecutions and the like under § 1955 in the mid-2000s constituted red flags that the Trustees ignored, I disagree. As

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[177] *See Litt*, 2003 WL 1794724, at *7 n.46.

previously discussed, these reports and prosecutions did not involve owners of securities in illegal gambling enterprises. As such, they did not make clear that passive stock ownership also was illegal.[178] In the eyes of some, Trustees may have been asleep at the wheel when it came to managing the Affected Funds' losing investments in the purported illegal gambling enterprises or morally challenged in permitting such investments to be made and maintained in ventures that the government considers predatory and illegal. For purposes of Rule 23.1, however, their action or inaction is more aptly characterized as making a poor risk calculation or business decision with regard to these investments. Moreover, even if Trustees' conduct related to purchasing and owning securities in allegedly illegal gambling businesses did violate § 1955, the Complaint fails to allege sufficient facts for the Court to infer that they knew that such ownership was illegal.[179]

For the foregoing reasons, therefore, I hold that demand is not excused in this case under either the second prong of *Aronson* or under *Rales*.

c. Pre-suit inaction

Plaintiffs also argue that demand is excused here because Trustee Defendants not only have failed to take action to prosecute Plaintiffs' claims since they first were served in the *McBrearty* action in 2008, they also asserted and caused Nominal Defendants to

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178 *See Wood v. Baum*, 953 A.2d 136, 143 (Del. 2008) ("Under Delaware law, red flags 'are only useful when they are either waved in one's face or displayed so that they are visible to the careful observer.'").

179 *See id*. at 142 ("the Complaint alleges many violations of federal securities and tax laws but does not plead with particularity the specific conduct in which each defendant 'knowingly' engaged, or that the defendants knew that such conduct was illegal.").

assert in formal court filings in that action that the plaintiffs' complaint should be dismissed with prejudice. This conduct, according to Plaintiffs, demonstrates that Trustee Defendants "have already committed themselves to the position that Nominal Defendants' claims should not be enforced and therefore foreclosed any possibility of acceding to a demand."[180]

Mere inaction on the part of a board after a corporation's claim accrues does not relieve the plaintiffs of the requirement to make demand.[181] But, plaintiffs need not make a demand on a board that already has affirmatively decided to refuse action.[182] Plaintiffs argue that Trustee Defendants' motion to dismiss the complaint in *McBrearty* reflects such an affirmative decision not to act. Thus, they contend that demand is excused here because it would not be likely to succeed.

Preliminarily, the fact that Defendants have moved to dismiss this action does not mean that demand would have been futile.[183] Rather, "futility is gauged by the circumstances existing at the commencement of a derivative suit" and not afterwards with

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180 PAB 40.

181 *See In re INFOUSA, Inc. S'holders Litig.*, 953 A.2d 963, 987 (Del. Ch. 2007).

182 *See id*.

183 *See Aronson v. Lewis*, 473 A.2d 805, 809-10 (Del. 1984) ("The trial judge correctly noted that futility is gauged by the circumstances existing at the commencement of a derivative suit. This disposed of plaintiff's argument that defendants' motion to dismiss established board hostility and the futility of demand."), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

the benefit of hindsight.[184] Moreover, the fact that directors are asked to sue themselves, which might have the effect of placing control over potential derivative claims in "hostile" hands, does not make demand futile under Delaware law.[185]

As such, Plaintiffs' argument that Trustee Defendants' motion to dismiss the related *McBrearty* action establishes that they already had committed themselves to denying a demand before this action is not convincing. Specifically, actions taken in a previous litigation do not establish that the Board of Trustees would have opposed Plaintiffs' claims had demand been made before filing *this action*. Plaintiffs have cited no authority or reasons to find that Defendants' arguments about the merits of the *McBrearty* action are binding on them to such an extent that they could not change their minds about pursuing the claims in the current Complaint. Plaintiffs have not argued, for example, that Trustee Defendants would be judicially estopped by their motion to dismiss the *McBrearty* action on the merits from deciding to allow Plaintiffs to proceed with the claims in this action.[186] I perceive no material difference in terms of potential demand

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184 *Id*.

185 *Brehm*, 746 A.2d at 257 n.34.

186 *See generally Motorola Inc. v. Amkor Tech., Inc.*, 958 A.2d 852, 859-60 (Del. 2008) ("Judicial estoppel acts to preclude a party from asserting a position inconsistent with a position previously taken in the same or earlier legal proceeding. The doctrine is meant to protect the integrity of the judicial proceedings. The primary determination made by the court turns on whether a party is attempting to 'establish an inconsistent or different cause of action arising out of the same occurrence.' However, judicial estoppel also prevents a litigant from advancing an argument that contradicts a position previously taken that the court was persuaded to accept as the basis for its ruling. . . . '[J]udicial estoppel operates only where the litigant's [position] contradicts another position that the

futility in a given action between a motion to dismiss a derivative claim in that action and a motion to dismiss a derivative complaint in a related, earlier action. Under either scenario, the policy underpinning Rule 23.1 is served by requiring a plaintiff to make a demand or show grounds for demand excusal.

Therefore, I reject Plaintiffs' argument that the defensive litigation positions taken by Trustee Defendants in the *McBrearty* action, without more, are sufficient to establish that demand would be futile.

d. Demand is not excused regarding the non-Vanguard Defendants

Plaintiffs' arguments for excusing demand focus exclusively on Trustee Defendants as well as their purported conflicts with Vanguard. As such, the non-Vanguard Defendants, including Sauter, Kelley, Acadian, Frashure, Chisholm, Wolahan, Marathon, and Ostrer, contend that demand is not excused as to them because the Complaint fails to plead particularized facts suggesting that Trustee Defendants would be unable to consider impartially a demand to pursue claims against those other Defendants as third-parties. Plaintiffs' only response is that demand is excused with regard to all Defendants because they "allege a conspiracy in which *all* Defendants were involved."[187]

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litigant previously took *and* that the Court was successfully induced to adopt in a judicial ruling.'") (emphasis in original) (internal citations omitted). Plaintiffs have not alleged that a prior court relied on Trustee Defendants' challenge to the adequacy of the pleadings regarding a state court cause of action. Trustee Defendants' statements and actions in the *McBrearty* action ultimately might be admissible against one or more Defendants as an admission. Such an admission, however, would not preclude Trustee Defendants from later changing their position and arguing that the admission should not be given conclusive effect.

[187] PAB 45 (emphasis in original).

For the reasons discussed *supra* Part II.A.3, Plaintiffs have failed to adequately plead the requisite elements of a conspiracy. As such, this argument fails. Furthermore, in the absence of a conspiracy, Plaintiffs have failed to articulate a basis as to why Trustee Defendants would be unable to consider bringing suit against these third-party companies and their employees. Therefore, the Complaint must be dismissed as to all Defendants based on Plaintiffs' failure to make a pre-suit demand on the Board of Trustees.

C. Merits

Having found that the Complaint is entirely derivative and that Plaintiffs failed adequately to plead demand excusal, I hold that Defendants are entitled to a dismissal with prejudice of all the claims in the Complaint. Accordingly, I need not address Defendants' challenges to the merits of Plaintiffs' claims under Rule 12(b)(6).[188]

III. CONCLUSION

For the reasons stated in this Opinion, I grant Defendants' motions to dismiss the Complaint in its entirety with prejudice.

IT IS SO ORDERED.

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188 *See In re Dow Chem. Co. Deriv. Litig.*, 2010 WL 66769, at *1 n.1 (Del. Ch. Jan. 11, 2010) ("demand futility under Rule 23.1 is 'logically the first issue [for all derivative claims] and if plaintiffs cannot succeed under the heightened pleading requirements of Rule 23.1 . . . there is no need to proceed to an analysis of the merits of the claim' under Rule 12(b)(6).").