

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

ROGER B. SMITH,)
a Georgia resident,)
)
Plaintiff,)
)
v.) C.A. No. 15442
)
NU-WEST INDUSTRIES, INC.,)
a Delaware corporation, AGRIMUM)
U.S., INC., a Colorado corporation,)
AGRIUM, INC., a Canadian)
corporation, DALE W. MASSIE,)
DOROTHY E. A. BOWER and)
LARRY A. COLLINS,)
)
Defendants.)

MEMORANDUM OPINION

Date Submitted: October 3, 2000
Date Decided: October 25, 2000

Craig B. Smith, David A. Jenkins, and Michele C. Gott, of SMITH, KATZENSTEIN & FURLOW LLP, Wilmington, Delaware, Attorneys for Plaintiff.

Daniel A. Dreisbach and Srinivas M. Raju, of RICHARDS, LAYTON & FINGER, Wilmington, Delaware; OF COUNSEL: Jonathon D. Bergman, of DAVIS, GRAHAM & STUBBS LLP, Denver, Colorado, Attorneys for Defendants.

CHANDLER, Chancellor

Plaintiff Roger B. Smith, and the class of Nu-West Class A preferred shareholders he represents, seeks a summary judgment determination on Count I of the complaint, alleging that Nu-West Industries (“defendant” or “Nu-West”) failed to pay the proper redemption price for all outstanding shares of Nu-West’s Class A preferred shares. Nu-West and the other named defendants also moved for summary judgment on Count I. Plaintiff alleges that defendants miscalculated the amount of allegedly accrued but unpaid dividends owed on the Class A preferred stock. Defendants claim that Nu-West’s certificate of incorporation plainly states that dividends were not payable for the period in question and, hence, were also not accruing during this period and should be excluded from the redemption price. For the reasons I set forth below, I grant plaintiffs motion for summary judgment.

I .

The following procedural background and factual history are relevant to the pending motion. Andrew E. Shapiro, formerly the named plaintiff, filed this class action on December 20, 1996, against defendants Nu-West Industries, Inc., Agrium U.S., Inc., Agrium, Inc., Dale W. Massie, Dorothy E. A. Bower and Larry A. Collins. In Count I of the complaint, Shapiro sought damages on behalf of the former holders of Class A preferred stock of Nu-West arising from Nu-West’s alleged failure to pay the proper redemption price when it redeemed all outstanding shares of the preferred stock on December 13, 1996. A second count, alleging

breaches of fiduciary duty, was voluntarily dismissed in early 1998. As Count I presented a purely legal issue—the proper calculation of the redemption price for the Class A preferred stock pursuant to Nu-West’s certificate of incorporation—Shapiro moved for summary judgment. Defendants moved to strike the motion for summary judgment, arguing that it was premature because the action had not been certified as a class action. On September 29, 2000, I ruled that this action should be certified under Rule 23(b)(1)(B).¹

Prior to the redemption of its Class A preferred stock, Nu-West, a Delaware corporation, had approximately 290,000 shares of Class A preferred shares issued and outstanding. About 100,000 shares of the Class A preferred stock were publicly held, while Nu-West’s controlling shareholder, Agriurn U.S., held the other 190,000 Class A preferred shares. According to Nu-West’s certificate of incorporation, Nu-West has the right to redeem its Class A preferred at a redemption price of \$100 per share plus (according to the complaint) an amount equal to all accrued and unpaid dividends to the date of redemption.

On December 13, 1996, Nu-West redeemed its Class A preferred stock at a price of \$100 per share plus accrued and unpaid dividends of \$71 SO per share, for a total of \$171 SO per share. It is undisputed that dividends on Nu-West Class A

¹ *Shapiro v. Nu- West Indus., Inc.*, Del. Ch., C.A. No. 15442, Chandler, C. (Sept. 29, 2000), *let. op.*

preferred accumulated at the annual rate of \$11 per share. To calculate the redemption price, Nu-West included \$66 per share for dividends accrued during each of the six fiscal years ending June 30, 1990, through June 30, 1995, together with \$5.50 per share for dividends accrued during the last six months of calendar year 1995. The redemption price did not include any payment for the dividend allegedly accruing during the period from January 1, 1996, through December 13, 1996.

On the redemption date, former plaintiff Shapiro was the record and beneficial owner of 1,126 shares of Class A preferred stock. When he received notice of Nu-West's intent to redeem the Class A preferred shares at \$171.50, Shapiro questioned Nu-West's failure to include in the redemption price dividends accrued from January 1, 1996, through December 13, 1996. Nu-West responded that dividends do not accrue daily, but rather, accrue in full only at the end of each full fiscal year according to its interpretation of its certificate of incorporation. Shapiro believed that the redemption price should have included an additional \$10.43 per share to account for the dividends accruing from January 1, 1996, through the date of redemption, December 13, 1996.² In his complaint, Shapiro

² The time period in question amounts to 347 out of the 366 days of 1996. Multiplying the annual dividend rate of \$11 by .948 (the fraction resulting from dividing 347 by 366), yields the \$10.43 per share figure.

asked the Court to award all Class A preferred shareholders as of December 13, 1996, an additional \$10.43 per share for each redeemed share. Ultimately, as noted above, Smith, the beneficial owner of 18,500 Class A preferred shares as of the redemption date, was substituted for Shapiro as the named plaintiff and the class of Class A preferred shareholders was certified.

II.

With this procedural history and factual background in mind, I turn to both parties' pending motions for summary judgment.

The Court appropriately grants summary judgment only where the moving party demonstrates the absence of genuine issues of material fact and that it is entitled to judgment as a matter of law. On any application for summary judgment, the Court must view the evidence in the light most favorable to the non-moving party. The fact that the parties have filed cross motions for summary judgment does not alter that standard. The court also recognizes that the parties do not concede an absence of factual disputes simply because they have filed cross-motions for summary judgment.³

Summary judgment is particularly appropriate where the issue is the construction of a legal document such as a certificate of incorporation.⁴

The issue the parties present for decision is the question of whether the provisions of NuWest's certificate of incorporation provide for daily accrual of

³ *Continental ins. Co. v. Rutledge & Co., Inc.*, Del. Ch., 750 A.2d 1219, 1227 (2000) (citations omitted).

⁴ See, e.g., *Citadel Holding Corp. v. Roven*, Del. Supr., 603 A.2d 818,822 (1992).

preferred dividends or annual accrual of preferred dividends. I find that there are no disputes of material fact and that the class of plaintiffs are, as a matter of law, entitled to an additional \$10.43 per share. Thus, plaintiffs motion for summary judgment on the Count I of the complaint is granted. As discussed more fully below, Nu-West's certificate of incorporation' clearly, and unambiguously, mandates a finding that dividends accrue daily and are *payable* at the time of redemption.

A. *The Certificate of Incorporation*

As to the dividends associated with the Class A preferred shares, the relevant certificate sections provide:

(B) Dividends and Distributions

- (a) From the issuance date of the Class A Preferred Stock(the "Class A Preferred Issuance Date") until the end of the first full fiscal year of the Corporation, dividends shall begin to accrue and shall be payable only to the extent of Excess Cash Flow (as hereinafter defined) for such period, and unpaid dividends for such period shall not be cumulative.
- (b) For the second full fiscal year of the Corporation after the Class A Preferred Issuance Date, cash dividends shall be payable only to the extent of Excess Cash Flow for such period and shall be cumulative only to the extent of the Adjusted Net Income (as hereinafter defined) for such period.

⁵ See Art. IV, §§ 2(1)(B)(1)(a-c), 2(I)(D)(5), 2(I)(E)(I), 2(1)(E)(2)(iii), 2(I)(E)(5), and 2(I)(G)(I).

- (c) For the third and each subsequent full fiscal year of the Corporation after the Class A Preferred Issuance Date, cash dividends shall be payable only to the extent of Excess Cash Flow for each such period and unpaid dividends for each such period shall be cumulative.⁶

In the event of redemption, the certificate expressly provides that “dividends shall cease to accrue from and after the Class A Redemption Date designated in the notice of redemption.”⁷

Several other certificate provisions also address the treatment of Class A preferred shares. Article IV, § 2(1)(E)(1) notes that the Class A preferred is subject to being exchanged, at the option of Nu-West, for Nu-West’s 11% Subordinated Debentures due June 1, 2002. In that event, the notice of exchange was required to state, among other things, “that dividends on the shares of Class A preferred Stock to be exchanged *will cease to accrue on such Exchange date.*”⁸ Moreover, the certificate provides that from, and after, the Exchange Date “*the right to receive dividends [on Class A preferred] shall cease to accrue.*”⁹ Similarly, on the dissolution, liquidation, and winding up of Nu-West, holders of Class A preferred are entitled to receive \$100 per share “plus a sum equal to all

⁶ Certificate, Art. IV, § 2(1)(B)(1)(a-c).

⁷ Certificate, Art. IV, § 2(1)(D)(5).

⁸ Certificate, Art. IV, § 2(1)(E)(2)(iii)(emphasis added).

⁹ Certificate, Art. IV, § 2(1)(E)(5)(emphasis added).

cumulative dividends on such shares *accrued and unpaid thereon to the date of final distribution.*”¹⁰

B. Summary of the Arguments

Plaintiff, in supporting his motion, argues that the certificate of incorporation, when read as a whole, clearly indicates that dividends for the preferred stock accrue on a daily basis. Moreover, in advancing this argument in both his brief and at the presentation of his motion, the plaintiff emphasized the distinction between the concepts of when dividends “accrue” and when they are “payable.”

Defendants oppose plaintiffs motion and seek summary judgment in their favor. The gist of their argument is that the certificate of incorporation provides that dividends for preferred shares accrue to, and are payable to, shareholders at the end of the fiscal year only. In other words, defendants argue that when the certificate says “payable” it means both payable and accrued.

C. Application of the Law to the Undisputed Facts

The parties’ motions ask the Court to interpret the provisions of Nu-West’s Certificate of Incorporation related to preferred stock dividends.

The Certificate is interpreted using standard rules of contract interpretation which require a court to determine **from** the language of the contract the intent of the parties. In discerning the intent of the

¹⁰ Certificate, Art. IV, § 2(1)(G)(1)(**emphasis** added).

parties, the Certificate should be read as a whole and, if possible, interpreted to reconcile all of the provisions of the document.

If no ambiguity is present, the court must give effect to the clear language of the Certificate. A contract is not rendered ambiguous simply because the parties do not agree upon its proper construction. Rather, a contract is ambiguous only when the provisions in controversy are reasonably or fairly susceptible of different interpretations or may have two or more different meanings [T]he true test is not what the parties to the contract intended it to mean, but what a reasonable person in the position of the parties would have thought it meant.’¹

At the very root of this controversy is the distinction between when, and how, dividends accrue and when they are **payable**. **The** defendants argue that the concepts are one and the same. I do not agree. Three concepts are important when discussing dividends for preferred stock.¹² First, there is the concept of when these dividends are **payable**. Generally, preferred shareholders benefit from a stated and fixed dividend rate, annual or otherwise, which is payable (**i.e., the** shareholder actually receives the dividend) only when the corporation has a stated level of earnings to pay the dividend. Often, a corporation’s articles of incorporation will provide that where there are insufficient earnings or other funds to actually pay a preferred dividend, that dividend will **accumulate**. In the simplest of terms, this means the fixed dividend from the prior period is added to that of the current

¹¹ *Kaiser Aluminum Corp. v. Matheson*, Del. Supr., 681 A.2d 392,395 (1996) (internal citations and quotations omitted).

¹² See *Penington v. Commonwealth Hotel Const. Corp.*, Del. Supr., 155 A. 514 (1931) and *Garrett v. Edge Moor Iron Co.*, Del. Ch., 194 A. 15 (1937).

period. This cumulating will continue until there are funds to pay the dividends. Finally, there is the separate question of when does the shareholder's rights to a dividend accrue? A shareholder's rights to receive a dividend will vest at a particular time. At the time the rights vest, the corporation may, or may not, have the funds to pay the dividend. These are distinct concepts in the area of preferred stock dividends and care should be taken not to confuse them. This case thus reduces to a single question: When did Nu-West's shareholders' rights to a preferred dividend vest or accrue?

To answer this question, I must look to the terms of the certificate. First, I know when the preferred dividends are **payable**. **Article IV**, § 2(1)(B)(1)(a-c) provides that dividends are only payable to the extent of excess cash flow during the fiscal year. To the extent the excess cash flow at the end of the fiscal year is insufficient, the \$11.00 dividend is not paid in that period and cumulates, or rolls forward, into the next year. This section establishes an annual system where at the end of each fiscal year either the dividend is paid or it cumulates.

The difficulty arises where there is an extraordinary event that disrupts the annual cycle. Here we are faced with the redemption of an entire class of preferred stock before the completion of a full annual cycle. The question now becomes whether, and to what extent, the shareholders' rights to that fixed \$11.00 dividend have vested or accrued. If the rights do not accrue until the end of the fiscal year,

as urged by the defendants, then the shareholders are not entitled to any part of the dividend. If the rights accrue daily from the first day of the fiscal year, as argued by the plaintiffs, then the shareholder will be entitled to a portion of the dividend.

While Nu-West's certificate is clear on when these preferred dividends are payable and that they cumulate if unpaid, the certificate is silent on whether the shareholders' rights to the dividends accrue daily up to the date of redemption. Mindful of this Court's duty to seek the intent of the parties from reading the contract as a whole, I find that other provisions of the certificate would lead a "reasonable person in the position of the parties" to conclude that the parties' intended the preferred dividends to accrue daily.

First, Article IV, § 2(1)(D)(5) clearly states that "dividends shall cease to accrue from and after the Class A Redemption Date designated in the notice of redemption." Logically, dividends can only cease to accrue "from and after the Class A Redemption Date" if they have been accruing continuously up to that date.

Second, Article IV, § 2(1)(E)(2)(iii) states that dividends will "cease to accrue" on the Exchange Date when preferred shares are exchanged for debt. This Exchange Date is an "extraordinary" event and not altogether different conceptually from a redemption. Likewise, Article IV, § 2(1)(G)(1) provides that upon dissolution, liquidation, and winding up, Class A preferred shareholders are entitled to receive "all cumulative dividends ... accrued and unpaid thereon to the

date of final distribution.” The date of final distribution may or may not occur at the end of a fiscal year.

III.

Reading the certificate of incorporation as a whole, I conclude that a reasonable person in the position of the parties would conclude that the preferred dividend accrues daily until the occurrence of an extraordinary event stops the accrual—here the redemption of the shares. I do not find that the certificate is ambiguous, nor do I find the terms in conflict. Rather, the provisions are quite clear on their face and act in concert to compel this result. It is only in applying those provisions to this specific fact situation—redemption—that a problem in interpretation arises. While the drafters were, quite simply, less clear than they could have been, the certificate as a whole fills in any minor gaps.

The facts in this case are undisputed and clear. The parties do not contest any fact, so they are entitled to a ruling, as a matter of law, as to whether dividends accrue daily or annually. Nu-West’s certificate of incorporation clearly, and unambiguously, mandates a finding that dividends **accrue** daily and are **payable** at the time of redemption.

I grant plaintiffs motion for summary judgment and deny defendants’ motion for summary judgment. The defendants are directed to pay an additional \$10.43 per share for each Class A preferred share redeemed.

I have entered an Order consistent with this decision.

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Defendants.)

CA. No. 15442

ORDER

For the reasons set forth in this Court's Memorandum Opinion entered in this case on this date, it is

ORDERED that summary judgment is entered in favor of plaintiff and against the defendants, and defendant Nu-West Industries is ordered to pay an additional \$10.43 per share for each Class A preferred share redeemed on December 13, 1996.

FURTHER ORDERED that defendant shall pay the costs of this proceeding, pursuant to Court of Chancery Rule 54(d).

William S. Chandler
Chancellor

Dated: October 25, 2000