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IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

TEACHERS' RETIREMENT SYSTEM OF LOUISIANA, derivatively and on behalf of all those similarly situated, Plaintiffs, v. RICHARD M. SCRUSHY, WILLIAM T. OWENS, JOHN S. CHAMBERLIN, JOEL C. GORDON, C. SAGE GIVENS, JON F. HANSON, CHARLES W. NEWHALL, III, LARRY D. STRIPLIN, JR., GEORGE H. STRONG, AARON BEAM, JR., JAMES P. BENNETT, P. DARYL BROWN, THOMAS W. CARMAN, RICHARD F. CELESTE, EDWIN M. CRAWFORD, RAYMOND J. DUNN, III, PATRICK A. FOSTER, WILLIAM W. HORTON, LARRY R. HOUSE, JAN L. JONES, MICHAEL D. MARTIN, MALCOLM E. MCVAY, WESTON L. SMITH, ANTHONY J. TANNER, LARRY D. TAYLOR, ROBERT E. THOMSON, PHILIP C. WATKINS, ERNST & YOUNG LLP, UBS WARBURG, LLC, SOURCE MEDICAL SOLUTIONS, INC., MEDCENTERDIRECT.COM, INC., COMPHEALTH, INC., and G.G. ENTERPRISES, INC., Defendants, and HEALTHSOUTH CORPORATION, a Delaware Corporation, Nominal Defendant.	)	C.A. No. 20529

MEMORANDUM OPINION

Date Submitted: February 11, 2004
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Stuart M. Grant, Esquire, John C. Kairis, Esquire, and Marlon Q. Paz, Esquire, GRANT & EISENHOFER, P.A., Wilmington, Delaware, *Attorneys for Plaintiff.*

William D. Johnston, Esquire, SaraBeth Reyburn, Esquire, and Dawn M. Jones, Esquire, YOUNG CONAWAY STARGATT & TAYLOR, LLP, Wilmington, Delaware; Thomas J. Hall, Esquire, Thomas V. Sjoblom, Esquire, and Scott S. Balber, Esquire, CHADBOURNE & PARKE LLP, New York, New York, *Attorneys for Defendant Richard M. Scrushy.*

Richard M. Donaldson, Esquire, MONTGOMERY, McCRACKEN, WALKER & RHOADS, LLP, Wilmington, Delaware, *Attorneys for Defendant Edwin M. Crawford.*

Michael A. Weidinger, Esquire, MORRIS JAMES HITCHENS & WILLIAMS LLP, Wilmington, Delaware, *Attorneys for Defendant Michael D. Martin.*

Robert J. Katzenstein, Esquire and Joelle E. Polesky, Esquire, SMITH, KATZENSTEIN & FURLOW LLP, Wilmington, Delaware, *Attorneys for Defendant Aaron Beam, Jr.*

Henry E. Gallagher, Jr., Esquire and Christos T. Adamopoulos, Esquire, CONNOLLY BOVE LODGE & HUTZ LLP, Wilmington, Delaware; Don B. Long, Jr., Esquire and James F. Henry, Esquire, JOHNSTON BARTON PROCTOR & POWELL LLP, Birmingham, Alabama, *Attorneys for Defendant James P. Bennett.*

John C. Phillips, Jr., Esquire, PHILLIPS, GOLDMAN & SPENCE, P.A., Wilmington, Delaware; James C. Huckaby, Jr., Esquire, John W. Scott, Esquire, and Julie N. Ehinger, Esquire, HUCKABY SCOTT & DUKES, PC., Birmingham, Alabama, *Attorneys for Defendant Source Medical Solutions, Inc.*

Richard L. Horwitz, Esquire, Stephen C. Norman, Esquire, and Erica L. Niezgoda, Esquire, POTTER ANDERSON & CORROON LLP, Wilmington, Delaware, *Attorneys for Defendants Chamberlin, Givens, Gordon, Newhall, Striplin, Strong, Car-man, Celeste, Foster, Horton, Jones, Taylor, and Watkins.*

Martin P. Tully, Esquire, MORRIS, NICHOLS, ARSHT & TUNNELL, Wilmington, Delaware; Robert J. Giuffra, Jr., Esquire and Thomas R. Leuba, Esquire, SULLIVAN & CROMWELL LLP, New York, New York, *Attorneys for Defendant UBS Securities LLC.*

Edward P. Welch, Esquire, Stephen D. Dargitz, Esquire, Julie A. Tostrup, Esquire, Michael A. Barlow, Esquire, Kay Lawson, Esquire, and Katherine J. Neikirk, Esquire, SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP, Wilmington, Delaware, *Attorneys for Nominal Defendant HealthSouth Corporation.*

Kurt M. Heyman, Esquire and Patricia L. Enerio, Esquire, THE BAYARD FIRM, Wilmington, Delaware; Frederick G. Helmsing, Esquire and Patrick C. Finnegan, Equire, HELMSING, LEACH, HERLONG, NEWMAN & ROUSE, P.C., Mobile, Alabama, *Attorneys for Defendant William T. Owens.*

Lawrence C. Ashby, Esquire, ASHBY & GEDDES, Wilmington, Delaware; Brendan V. Sullivan, Jr., Esquire, Steven M. Farina, Esquire, and Michael K. Stem, Esquire, WILLIAMS & CONNOLLY LLP, Washington, D.C., *Attorneys for Defendant Ernst & Young LLP.*

Gary W. Aber, Esquire, ABER, GOLDLUST, BARER & OVER, Wilmington, Delaware, *Attorneys for Defendant Larry R. House.*

STRINE, Vice Chancellor

This is one of the many lawsuits involving alleged wrongdoing at HealthSouth Corporation. This case happens to be a derivative action. In this opinion, I address the motions brought by a multitude of defendants to stay this action in deference to a prior-filed derivative action in Alabama. The plaintiff in this action, the Teachers' Retirement System of Louisiana ("Teachers"), resists this motion, essentially on the grounds that it believes itself to be best positioned to represent HealthSouth as a derivative plaintiff and that this court, rather than an Alabama court, should address the derivative claims because those claims arise under Delaware law.

For many reasons, I grant the defendants' motion to stay this action. In another prior-tiled derivative action involving HealthSouth that remains pending in this court, I initially refused to grant a motion to stay in favor of the prior-filed Alabama action. At that time, it was not at all clear that the Alabama plaintiffs would adequately represent HealthSouth or that their slight timing advantage should give them a decisive edge over Delaware plaintiffs who had filed a superior complaint a few weeks later. But, at the same time, I recognized that it would become necessary in the future to determine the forum in which the derivative claims should proceed and encouraged the Delaware plaintiffs to work with the Alabama plaintiffs towards a mutually satisfactory resolution of that question.

Simultaneously, judges in the Alabama state and federal courts also were encouraging rationality and cooperative action by the Alabama derivative plaintiffs, as well as on the part of plaintiffs in related federal securities actions pending in the Alabama federal court. These judicial efforts ultimately involved, among other things,

the appointment of steering committees to coordinate discovery, the appointment of lead counsel, and judicially supervised settlement discussions. With urging from all the affected courts, the derivative plaintiffs in all the then-pending actions forged an agreement on where the derivative claims should be prosecuted, with this court being the forum for a particular claim, and the rest to be litigated in state court in Alabama. The Delaware derivative plaintiffs — as they existed at that time — were parties to that accord and supported it fully.

Only after all this progress was achieved did Teachers file its complaint. It now seeks to disrupt all this progress by being permitted to proceed with a derivative action in this court that is largely co-extensive with the derivative claims pending in Alabama state court and to thereby disrupt the harmony that has been achieved by plaintiffs' counsel and the various courts involved in the HealthSouth cases. Notably, Teachers has made no attempt to intervene in the Alabama state court actions or to work with counsel in those actions, despite admonitions from this court to do so.

In view of these realities, a stay of this action is clearly in order. Through their active handling of the cases before them, the Alabama state and federal judges have displayed great concern over the HealthSouth cases. Their involvement gives me confidence that HealthSouth's stockholders will be adequately represented by the lead counsel who have been appointed in the Alabama state derivative actions, especially because the operative complaint in that forum has been greatly improved and a number of qualified firms are working together to prosecute the derivative claims there. Their number includes the respected Delaware counsel who filed the first derivative actions in

this court and who won an important summary judgment motion in this court on behalf of HealthSouth.

Given the need for the derivative claims involving HealthSouth to proceed in one forum first and the obvious convenience of Alabama state court as a forum, it would be inefficient, unjust, and injurious to comity among the States to deny the defendants' motion to stay. The good work of various courts to coordinate their efforts should not be tossed aside simply because a late-filing plaintiff believes itself to be superior to all others. The plaintiffs high regard for itself and its lawyers may be justified but the presence of effective, experienced plaintiffs' lawyers in the prior-filed actions renders their pride an insufficient ground upon which to rest the denial of a stay. Furthermore, although this court takes pride in its ability to interpret our state's law, it also recognizes that other courts — such as the Alabama state courts — also are equipped to perform that task competently, particularly when, as in the HealthSouth cases, most of the claims mm on the application of settled principles of Delaware law to a factual record.

I. Factual Background

A. This Action

The plaintiff in this action is the Teachers' Retirement System of Louisiana. Teachers used to own a very large block of stock in HealthSouth but sold the bulk of its position. It retains control over 69,400 Healthsouth shares.

Teachers first became a litigant against HealthSouth when it filed an action in this court seeking books and records. That action under 8 *Del. C.* § 220 was filed on November 27, 2002. The trial in the books and records case was completed on March 18,

2003 and Teachers prevailed. The books and records the court ordered be produced to Teachers were received by mid-April 2003, consistent with this court's order.

Nearly five months later, Teachers brought this action by filing a detailed and lengthy complaint. In the "Teachers' Complaint," a wide variety of transactions, expenditures, and stock sales were challenged. It is unnecessary to summarize all the claims here, except to observe that the Teachers Complaint essentially alleges that HealthSouth was run corruptly, with its Chairman and CEO, defendant Richard Scrushy, using the company as a personal candy store by which he and other high-level HealthSouth officials could satisfy their personal hunger for lucre and prestige at the expense of the company's public stockholders. As part of this improper course of self-dealing, the insider defendants are alleged to have falsified HealthSouth's financial statements in order to prop up the company's stock price. The defendants from outside HealthSouth are alleged to have been complicit in various transactions that formed part of the massive tapestry of fiduciary misconduct weaved by the HealthSouth insiders sued in the complaint.

Consistent with this description, the defendants in this action include current and former directors and officers of HealthSouth. Several of these defendants are former HealthSouth officers who never served on the board of directors and over whom the maintenance of personal jurisdiction in this court is doubtful, to put it mildly.

The remaining defendants are various entities that transacted business with HealthSouth. Some of them provided services to HealthSouth — such as audit and investment banking services — and supposedly facilitated wrongdoing by HealthSouth

insiders. Others were on the other side of transactions with HealthSouth that Teachers alleges were unfair to HealthSouth.

The Teachers' Complaint contained one count that was different in focus than the other counts in that it was not filed primarily with the objective of obtaining remedial relief for past wrongdoing. That count was brought under 8 *Del. C.* § *211* and sought an order requiring an annual meeting of the HealthSouth stockholders.

Litigation on that count was expedited by this court last autumn. The case was tried. At the request of the parties, this court did not issue its decision in order to give Teachers and HealthSouth a chance to resolve their dispute over this issue amicably. They soon did so, with Teachers withdrawing its request for an annual meeting in exchange for an agreement whereby most of the HealthSouth directors who were in office during the past periods for which the company has been forced to withdraw its financial statements and during which the transactions challenged in the Teachers' Complaint transpired would resign, to be replaced by independent directors through a process that Teachers found trustworthy. The § 211 count was dismissed by agreement of the parties.

Thus, the only counts of the Teachers' Complaint that remain are those that seek remedial relief for the pattern of fiduciary misconduct briefly described above. As we will now see, the Teachers' Complaint was preceded by several others filed in various courts that seek virtually indistinguishable relief.

B. The Prior Pending Actions

As discussed in prior opinions of this and other courts, public scrutiny of HealthSouth's financial integrity first became intense in the summer of 2002. At that time, HealthSouth announced that a new policy regarding reimbursement issued by the federal Centers for Medicare and Medicaid Services (the "CMS Policy") would have a large, detrimental effect on the company's revenues. Put simply, many stockholders — and their attorneys — were deeply suspicious about HealthSouth's announcement, given that the CMS Policy had, according to them, been expected for some time. In particular, they suspected that HealthSouth insiders — many of whom had engaged in large transactions involving sales of HealthSouth stock earlier that year — had concealed the effect of the CMS Policy in order to keep HealthSouth's stock price artificially high.

The expected two types of filings were soon made. Less relevant here was the spate of federal securities suits filed on August 28, 2002 alleging violations of Sections 10(b) and 20(b) of the Securities Exchange Act. For ease of reference, I call these the "Federal Securities Actions."

The second and more relevant kind of case was also filed. On August 28, 2002, the first of several derivative actions was filed in the state courts of Alabama (the "Alabama Derivative Actions"). The first complaint, the "Tucker Complaint," challenged a wide array of transactions entered into by HealthSouth insiders over the course of several years. Many of these transactions eventually also became the subject of the Teachers' Complaint. As a last minute add-on, the Tucker Complaint also briefly challenged certain conduct relating to the CMS Policy; namely, the Tucker Complaint

alleged that HealthSouth's then-CEO, Richard Scrushy, had sold a large block of stock back to the company shortly before HealthSouth disclosed the adverse impact of the CMS Policy. As this court noted in an earlier opinion, the original Tucker Complaint was hardly a model of good pleading practice.[1] It barely addressed the need to plead demand excusal, a major problem in a derivative case. Moreover, many of the counts in the Tucker Complaint were alleged against placeholder defendants, who were named as fictitious defendants, but who were not identified.

On September 13, 2002 and October 8, 2002, two additional derivative actions were filed in this court (the "Delaware Derivative Actions"). The Delaware Derivative Actions were focused more narrowly than the Alabama Derivative Actions, centering primarily on recouping improper trading and contract profits HealthSouth insiders had allegedly reaped while HealthSouth was inflating its results by not disclosing more promptly the adverse effects of the CMS Policy. Unlike the Tucker Complaint, which is the key complaint in the Alabama Derivative Actions, the complaints in the Delaware Derivative Actions also asserted that HealthSouth insiders other than Scrushy had sold HealthSouth stock into a market inflated by its ignorance of the effect of the CMS Policy on HealthSouth. In comparison to the Tucker Complaint, the complaints in the Delaware Deriviative Actions reflected, as a prior opinion of this court indicates, much greater research and a proper understanding of the need to plead demand excusal.[2]

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[1] *See Biondi v. Scrushy*, 820 A.2d 1148, 1153-54 (Del. Ch. 2003).

[2] Ronald Brown of Prickett, Jones & Elliott is Delaware counsel in the Delaware Derivative Actions, and worked with Frank P. DiPrima, a New Jersey lawyer, to bring those Actions.

On October 18, 2002, the first of two derivative suits was filed in the United States District Court for the Northern District of Alabama (those and later suits filed in that court being referred to hereafter as the "Federal Derivative Actions"). The claims in the Federal Derivative Actions overlapped with claims already asserted in the Alabama and Delaware Derivative Actions with immaterial exceptions.

C. The Previous Motion To Dismiss Or Stav

Early in one of the Delaware Derivative Actions, HealthSouth and the defendants moved to dismiss or stay that case. There were two primary bases for that motion, which the plaintiffs in the Delaware Derivative Actions adamantly opposed. The first was that a special litigation committee ("SLC") had been established by HealthSouth to investigate the wrongdoing challenged in the Delaware Derivative Actions and that that Action should therefore be stayed, per the line of cases beginning with *Zapata v. Maldonado*.[3] That argument — which is routinely a winning one — was rejected by this court because the HealthSouth SLC, due to its own conduct and composition, could never have made a decision to terminate the litigation that would have commanded respect.[4]

The defendants' second argument was that this court should defer to the prior-filed Alabama Derivative Actions. That argument was rejected for the following reasons:

> The application of the *McWane* doctrine to representative actions — i.e., class and derivative actions — is troublesome. In that context, the *McWane* doctrine is both most useful and most difficult to apply. Representative actions present the greatest chance for identical claims to be presented to multiple courts at the same time. Hence, there is utility to a legal rule of decision that promotes comity and judicial economy by

[3] 430 A.2d. 779 (Del. 1981).
[4] *Biondi, 820* A.2d at 1165-66.

reducing the likelihood for duplicative effort and unseemly wrestling over which forum should take hold of a matter. At the same time, representative actions pose certain dangers — in particular, the potential divergence in the best interests of the plaintiffs' attorneys and the plaintiffs they are purporting to represent — that are not addressed, and indeed may be exacerbated, by a legal rule that places determinative weight on which complaint was filed first.

Because of these competing considerations, this court has proceeded cautiously when facing the question of whether to defer to a first-filed representative action and has given much less weight to first-tiled status than is required in the non-representation action context. In particular, that caution has been motivated by a concern that the underlying client in interest in a representative action — the class or, in the case of a derivative action, the corporation — be represented effectively and faithfully. The mere fact that a lawyer filed first for a representative client is scant evidence of his adequacy and may, in fact, support the contrary inference. For those reasons, this court will not grant a stay simply because there is a prior-filed representative action in a court capable of doing prompt and complete justice. Instead, the, court will examine more closely the relevant factors bearing on where the case should best proceed, using something akin to a ***forum non conveniens*** analysis.

This does not mean that the question of first-filed status is irrelevant. Rather, it means that the first-filed factor typically becomes decisively important only when: (1) a consideration of other relevant factors does not tilt heavily in either direction and there is a need for an objective tie-breaker to promote comity and assure litigative efficiency or (2) the court is assured by virtue of a judicial finding in the first-filed representative action (through a class certification ruling under Rule 23 or selection of lead counsel under the Private Securities Litigation Reform Act of 1995) or other record evidence that the plaintiffs in the action for which a stay was sought are adequately represented in the first-filed action.

In this case, the SLC has not convinced me that first-filed status, without more, counsels in favor of an immediate stay. Read charitably, the original Tucker Complaint pled but one of the claims, as to only one of the transactions, addressed in the Delaware Complaint. Even that one claim was pled cursorily and as an aside to a host of other broad-ranging and thinly-pled complaints about Scrushy's compensation from and management of **HealthSouth.** The Tucker Complaint did not even attempt to plead demand excusal with particularity.

By contrast, the Delaware Complaint dealt comprehensively with a series of trades and transactions by **HealthSouth** directors that the plaintiffs allege were consummated when the directors knew of the adverse effect the [CMS Policy] would have on **HealthSouth,** but the market did not. As important, the Delaware Complaint pled demand excusal with particularity.

Although I do not doubt the competence of the Alabama Circuit Court to handle the claims pled in the Delaware Complaint with skillful dispatch, the reality is that deferring to the Tucker Action requires me to give determinative weight to a pleading that evidenced far more concern for speed in filing than adequacy of content. This is demonstrated by the original failure of Tucker to even **identify** the directors of **HealthSouth** other than Scrushy, to attack any of the sales in **HealthSouth** stock made by other **HealthSouth** directors, or to challenge the **Buyback** [by **HealthSouth** of Scrushy's shares in summer **2002]** on grounds other than corporate waste. By contrast, the Delaware Complaint, although — or perhaps more accurately, ***because*** — it was filed two weeks later, is thorough and **fact-**laden, demonstrating that the plaintiffs' lawyers used the time between the announcement by **HealthSouth** of the [CMS Policy's] effect and the filing of their complaint to perform diligent research.

Indeed, because the Tucker Action focused largely on other transactions and did not address most of the transactions contained in the Delaware Complaint, it is difficult to say that the original complaint in that case raised claims that were functionally identical to those raised in the Delaware Complaint, nor is it apparent that the parties are substantially the same, given the failure of the original Tucker Complaint to plead claims against the other **HealthSouth** directors. For those same reasons, it is not apparent why it should be influential in the representative action context that that the later amended complaint in the Tucker Action added challenges to some, but not all, of the other sales attacked in the Delaware Complaint. The only transaction relevant to the Delaware Action that was challenged specifically in the original Tucker Complaint is the **Buyback** [of Scrushy's shares by **HealthSouth** in summer **2002].** Because the amended Tucker Complaint alleged wholly new claims against defendants who were not even named in the original complaint in that case, the "what" and "who" of those claims were not presaged in any way by the text of the earlier complaint. Even as to **Scrushy,** the amended Tucker Complaint challenges an earlier stock sale that was not even mentioned in the original complaint, despite the practical requirement under Delaware law that derivative claims be pled with particularity.

In concluding that it would be inappropriate to stay the Delaware Action at this time, I am particularly mindful of the Delaware Supreme Court's repeated admonitions to derivative counsel to undertake diligent research before tiling their complaints. These admonitions reflect the important value our state places on the enforcement of the legal and equitable duties of directors of Delaware corporations. By investing in a corporation chartered in Delaware, stockholders seek out and are entitled to the protections afforded by our law. As a practical matter, these protections are often assured by the filing of representative actions like this one, making it important that the quality of representation afforded by plaintiffs' counsel in these cases be high. The importance of quality lawyering at the pleading stage of derivative cases is obvious, given the higher pleading burdens applicable to derivative complaints. For this reason, Delaware law places more emphasis on quality than speed when assessing derivative complaints.

The public policy interest favoring the submission of thoughtful, well-researched complaints — rather than ones regurgitating the morning's financial press — would be disserved by granting a stay in this case.

That said, I am equally mindful of the need for comity with our sister state and federal courts, as well as the practical reality that identical derivative claims should not be **tried in** separate forums. At **a** later stage, the question of where the claims raised in the Delaware Action should proceed can be revisited, and I am confident that an **efficient** and fair resolution to the forum issue can be forged, with cooperation among the litigating parties and among the affected courts. In this respect, one **final** note is advisable.

In its opening papers, the SLC did not ask me to stay the Delaware Action in favor of the Federal **Securities Actions. Because the Delaware** Action largely involves claims that are substantively indistinguishable from federal insider trading claims, it may well be that the federal adjudications should precede the determination of the state law issues and that any schedule in this case should reflect that consideration. Although in one important respect there are state law issues that diverge to some extent **from** the basis for the federal suits — ***i.e.,*** **the question of whether the Buyback** was an unfair interested transaction under state law — in most respects it would seem to be helpful to have a prior federal adjudication of whether the trading directors possessed material, non-public information at the time of their trades and acted with ***scienter.***

For now, however, I simply deny the **SLC's** application for a stay in deference to the Tucker Action, without prejudice to a later, similar **motion.**[5]

D. The Corporate Cataclysm At **HealthSouth**

Shortly after this court denied the motion to dismiss or stay, **HealthSouth's** predicament went from bad to **awful.** In March 2003, federal civil and criminal authorities went public with concerns they had about the integrity of **HealthSouth's** financial statements. To summarize a complicated situation simply, the federal government believed that the corporate books of **HealthSouth** had been intentionally manipulated to overstate the company's health. Within the coming weeks, the SEC had filed a civil suit against **HealthSouth** and former senior executives of **HealthSouth** began pleading guilty to financial crimes. The company's founder and largest stockholder, Richard Scrushy, was tired as CEO but insisted on remaining on the board, which formed a special committee excluding Scrushy. The committee has largely governed the company since new outside advisors were brought in to replace the company's former advisors.

After **HealthSouth's** stock was **delisted** and its trading price became measured in pennies, the company began the difficult task of rebuilding. This process obviously was complicated by an ever-growing number of lawsuits. As the additional revelations of possible accounting fraud became public, the complaints in the various pending suits

[5] *Id.* at 1158-63 (footnotes omitted).

were amended and new suits were filed. Meanwhile, Congress also held hearings into the company's financial practices.

As of the time of these developments, the Teachers' Complaint still had not been filed.

E. The Courts Involved In The Various Suits Encourage Coordination

As the prior opinion denying the motion to stay or dismiss the Delaware Derivative Actions indicated, this court was sensitive to the eventual need to sort out where the fiduciary duty claims, and claims related to those claims, would ultimately be litigated. To that end, this court, among other efforts towards this end, encouraged counsel in the Delaware Derivative Actions to engage in discussions with their colleagues in the Alabama and Federal Derivative Actions with the hope that they could agree on a division of labor and of forums that would make sense.

At the same time, Judge Karon 0. Bowdre of the U.S. District Court for the Northern District of Alabama was also urging efficiency and cooperation among counsel in the various actions. Among other efforts to rationalize the process, Judge Bowdre appointed a steering committee comprised of representatives of counsel from the various actions, including representatives of the Federal Derivative Actions. The federal committee was responsible for coordinating discovery in all the actions involving stockholders of HealthSouth from 1998 until 2002 that were then pending in her court. Importantly, this federal committee was also charged with coordinating discovery with a committee to be appointed by Judge Allwin E. Horn III, the Alabama Circuit Court Judge who was handling the Alabama Derivative Actions. On August 24, 2003, Judge Horn

appointed the state committee, which included derivative counsel from the Alabama Derivative Actions.

By this time, several notable developments had already occurred. In Alabama state court, the Tucker Complaint, as amended, became the focal point of the Alabama Derivative Actions. Several other cases were "abated" in favor of the Tucker Complaint, the functional equivalent of consolidation.

The encouragement to counsel in the Delaware, Alabama and Federal Derivative Actions from all the affected courts eventually paid off. In orders entered by Judge Horn, Judge Bowdre, and me, the following division of labor was agreed upon by the then-existing derivative plaintiffs: 1) the Federal Derivative Actions would be stayed in favor of the Alabama Derivative Actions and the Delaware Derivative Actions; 2) the plaintiffs in the Delaware Derivative Actions would prosecute claims relating to Scrushy's sale of HealthSouth stock back to the company in summer 2000 (the so-called "Buyback") in this court; and 3) the remainder of the derivative claims would be prosecuted before Judge Horn in the Alabama Derivative Actions under the aegis of the Tucker Complaint. By this time, the counsel in the Delaware Derivative Actions were participating and conferring with counsel in the Alabama Derivative Actions and developing joint plans for prosecution of all the derivative claims. To that end, the Tucker Complaint was amended a third time in August 2003 to add yet more claims. By this time, the Tucker Complaint covered all the claims raised in the Delaware Derivative Actions and purported to state a wide variety of other claims that are largely co-extensive with the claims raised in the Teachers' Complaint.

Furthermore, Judges Bowdre and Horn had already personally worked together to bring the parties to the various actions together for confidential settlement discussions. They also worked together to coordinate the timing and scope of discovery, in view of the PSLRA[6] and the desirability of avoiding duplicative discovery that could tax HealthSouth's already strained resources. By autumn 2003, each Judge had put in place an order identifying lead counsel in the actions pending before them,' and their appointees continued to work together on the discovery steering committees they previously established. In December 2003, Judge Horn denied a motion by counsel for another derivative plaintiff to be appointed to the HealthSouth steering committee,' finding that "it is in the best interests of all parties to this action to continue forward with the current plan and method of administering and handling this complex litigation."[9] His ruling was based, in part, on objections made by lead counsel in the Alabama Derivative Actions, objections which were joined by counsel in the Delaware Derivative Actions. That objection stated in part that:

> The courts of three jurisdictions — this one, the U.S. District Court for the Northern District of Alabama, and the Delaware Chancery Court, all urged various derivative plaintiffs to work together. They have done so,

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[6] See 15 U.S.C. § 78u-4(b)(3)(B)-(D) (PSLRA provisions governing discovery).
[7] In an order entered July 14, 2003, Judge Horn indicated that lead counsel already had been appointed in the Alabama Derivative Actions as of that date. Def s Supp. Submission Ex. 16. Additional co-lead counsel were appointed by Judge Horn in an order entered January 8, 2004. Def s Supp. Submission Ex. 3.
[8] That counsel represented derivative plaintiffs who first filed a suit in 1998. They then asked that their suit be placed on ice. When events at HealthSouth became a focus of public attention in 2002, these plaintiffs attempted to defrost their action. I do not focus on that action because the other actions I mention were all filed before the Teachers' Complaint and do not involve the indolence of the action filed in 1998.
[9] Dargitz Reply Aff. Ex. 22.

and we have formed a highly co-operative unit with mutual respect among all counsel. We do not want to put this at risk.[10]

F. The Teachers' Comnlaint Is Finally Filed

Only after a large amount of effort had been expended by Judge Bowdre, Judge Horn, this court, and the parties to the various HealthSouth actions to secure a rational approach to the procession of those actions did the Teachers' Complaint get filed. That occurred on September 8, 2003. Rather than dilate on that Complaint's quality, it suffices to say that the Teachers' Complaint is a high-quality effort that reflects a great deal of work. But it also bears noting that the Complaint largely covers the same ground already trod by the Tucker Complaint, as amended. Although Teachers pokes at the Tucker Complaint, as amended that pleading is much improved from on its original form and is a substantial, fact-laden document that also reflects a good deal of work.

More problematic, of course, was the timing of the filing of the Teachers' Complaint. By that time, the judges of three different courts had successfully encouraged a wide array of counsel to come up with a plan for the rational procession of the various cases affecting HealthSouth. The advisability of that goal for stockholder-plaintiffs is rather obvious but I suppose needs explicit recitation: It was in the interests of all those plaintiffs that HealthSouth's resources be preserved and that the company's financial health be nurtured. A restoration of HealthSouth's strength would help the derivative plaintiffs. A bankruptcy was not in their interest and that was not an unrealistic possibility.

[10] Dargitz Reply Aff. Ex. 15.

Fortunately, by the late summer of 2003, HealthSouth — led by new management and advisors — had made major strides in stabilizing its finances and instilling confidence in its creditors. Although the company's previous financial statements were so materially inaccurate that the company had to withdraw them and could not estimate when accurate financials for those periods could be tiled, HealthSouth was able to provide prospective information. The stock price of the company began to trade in dollars rather than pennies and has remained at that level.

On the litigation front, important events had also transpired. By autumn 2003, fifteen former HealthSouth executives had pled guilty to financial crimes committed in their official capacities at the company. Those crimes principally involved what was allegedly a widespread conspiracy by top-ranking HealthSouth management to manipulate the company's financial statements in order to paint an unrealistically rosy picture of HealthSouth's financial performance. HealthSouth's former Chairman and CEO, Richard Scrushy, was indicted on numerous counts alleging that he was the primary leader of that conspiracy.

On the civil front, the plaintiffs in the Delaware Derivative Actions prosecuted and won a grant of summary judgment against Scrushy as to the Buyback, using theories that did not depend on Scrnshy's knowing participation in the preparation of false financial statements." That order was reduced to an enforceable judgment under Rule 54(b). Soon thereafter, the plaintiffs in the Alabama Derivative Actions began prosecuting a

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[11] *In re Healthsouth Cop. S'holders Litig., 2003 WL 22769045* (Del. Ch. Nov. 24, 2003) (holding Scrushy liable for unjust enrichment and equitable fraud).

similar motion addressing' other transactions involving Scrushy and using the theories advanced in the Delaware Derivative Actions. Counsel for the plaintiffs in the Delaware Derivative Actions worked with counsel in the Alabama Derivative Actions in preparing this motion.

Meanwhile, Teachers made progress of its own. After a trial on its § 211 claim, Teachers extracted a settlement from HealthSouth that resulted in an agreement requiring a majority of the HealthSouth board to resign within the next year, with the resigning directors to be replaced by new independent directors. The resigning directors were those directors who had been in office during the time of the alleged financial fraud. Director Scrushy refused to resign.

II. Legal Analvsis

The defendants premise their motion on the *Mc Wane* doctrine.[12] That doctrine requires that Delaware trial courts exercise their discretion "freely in favor of a stay when there is a prior action pending elsewhere, in a court capable of doing prompt and complete justice, involving the same parties, and the same issues."[13] The purpose of the *Mc Wane* doctrine is to avoid "the wasteful duplication of time, effort, and expense that occurs when judges, lawyers, parties, and witnesses are simultaneously engaged in the adjudication of the same cause of action in two courts."[14]

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[12] *Mc Wane Cast Iron Pipe Corp. v. McDowell- Wellman Eng 'g Co., 263* A.2d 281 (Del. 1970).
[13] *Id.* at 283.
[14] *Id.*

Here, there is no question that the Teachers' Complaint raises claims that, for purposes of applying *Mc Wane,* involve substantially the same parties and same issues as the prior-tiled Alabama Derivative Actions, the Federal Derivative Actions, and the Delaware Derivative Actions. Most pertinently, the Teachers' Complaint and the Tucker Complaint are largely overlapping documents, with exceptions that are immaterial for *Mc Wane* purposes.[15] Furthermore, to the extent that the Teachers' Complaint attempts to raise certain disclosure claims on behalf of HealthSouth stockholders, it also overlaps with the Federal Securities Actions, which were first-filed.

There also is no question that the prior-filed cases are all pending in courts of competent jurisdiction. This court has repeatedly acknowledged that in most circumstances, federal courts and the courts of sister states can apply Delaware law competently.[16] The Delaware law claims raised in the Teachers' Complaint and the prior-filed actions are not so novel as to preclude the Alabama state and federal courts from adjudicating them expertly.

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[15] Under *Mc Wane,* all that is required is substantial identity of the claims and the parties, and the mere fact, for example, that Teachers has styled certain of its claims as "class claims" does not destroy the identity that exists between this case and the other pending derivative actions. See, e.g., *AT & T Corp. v. Prime Sec. Distribs., Inc.,* 1996 WL 633300, at *2 (Del. Ch. Oct. 24, 1996) ("To grant a stay, it is not required that the parties and issues in both actions be identical. Substantial or functional identity is sufficient."); *Schnell v. Porta Sys.* Corp., 1994 WL 148276, at *4 (Del. Ch. Apr. 12, 1994) (stating that "all claims arising from a common nucleus of operative facts [should] be brought at the same time whenever possible" and finding that fiduciary duty claims were functionally similar to prior-pending federal securities claims); *In re Westell Techs., Inc. Deriv. Litig.,* 2001 WL 755134, at *2 (Del. Ch. June 28, 2001) (concluding that claims for breach of fiduciary duty were functionally similar to prior-filed federal securities claims).

[16] *E.g., Corwin v. Silverman, 1999 WL 499456,* at *6 (Del. Ch. June 30, 1999).

Likewise, to the extent that *forum non **conveniens*** factors are relevant, it is evident that Alabama is a convenient place to litigate the claims raised in the Teachers' Complaint given that **HealthSouth's** headquarters are in Birmingham, Alabama. Indeed, it is worth noting that the Teachers' Complaint seeks relief against a number of former **HealthSouth officers** who never served on the company's board. Yet, the Teachers' Complaint alleges no acts that these former officers undertook in Delaware and they are sued for conduct that pre-dates our state's new service of process statute addressing corporate officers."[17] It is probable, therefore, that this court cannot exercise personal jurisdiction over these defendants. By contrast, each of these defendants worked at **HealthSouth's** headquarters in Alabama at relevant times and many are Alabama residents, giving the Alabama courts easy access to jurisdiction over their persons.

In view of these factors, the only genuine issue of concern regarding a stay is whether there is some basis to conclude that **HealthSouth** and its stockholders are not adequately represented in the prior-pending cases, most notably the Alabama Derivative Actions. At an earlier time, it is clear that I harbored doubt on that score, as my prior decision denying the previous motion to stay or dismiss indicates.

Despite Teachers' attempts to pretend that circumstances are the same as when I denied the earlier motion for a stay, they are not. The defendants have submitted "record evidence that the plaintiffs" in this action "are adequately represented" in the Alabama

[17] See 10 *Del.* C. § 3 114(b) (providing that persons who accept positions as officers of Delaware corporations after January **1, 2004** are thereby deemed to consent to service of process in Delaware as to suits against them in their official capacities).

Derivative Actions — as well as the Federal Securities Actions." For that reason, it becomes appropriate for me to give full force to the fact that the Teachers' Complaint was filed long after the Alabama Derivative Actions, the Delaware Derivative Actions, the Federal Derivative Actions, and the Federal Securities Actions.[19] This record evidence indicates that: 1) Judges Horn and Bowdre have actively coordinated and supervised the various actions pending in Alabama, including all the derivative actions pending in their courts; 2) lead counsel has been appointed in the relevant Alabama Derivative Actions; 3) respected Delaware counsel are participating in the prosecution of the Alabama Derivative Actions and consented to the procession of the remainder of their derivative claims in the Alabama state courts; and 4) a number of other qualified plaintiffs' firms are working together to prosecute the Alabama Derivative Actions.

In the face of this record, Teachers has mostly pointed out relatively minor foibles on the part of counsel in the Alabama Derivative Actions, complained about the pace at which the prior-filed Actions have proceeded, and proclaimed its own superiority — and that of its counsel — as champions for the HealthSouth stockholders. Put simply, Teachers' arguments are not convincing.

It may be true that counsel in the Alabama Derivative Actions got off to a bit of a rocky start. But, by now, the Tucker Complaint is vastly improved and Delaware counsel are working with lead counsel in the Alabama Derivative Actions to prosecute a motion for summary judgment. Moreover, Teachers seems to ignore the obvious, which is that

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[18] *Biondi, 820* A.2d at 1159.
[19] *Id.*

the criminal charges pending against many of the defendants in the derivative actions necessarily complicate the procession of the lawsuits, as does the relation of the derivative suits to the Federal Securities Actions. In view of the need for rationality in discovery, the speed at which the prior-filed cases have proceeded is not a reason to deny a stay. Perhaps most importantly, it is clear that the plaintiffs in the prior-filed Actions made a great deal of progress *as derivative plaintiffs* before Teachers even became a derivative plaintiff.[20]

This is especially the case when one considers the pace with which Teachers acted. Although this court does encourage the tiling of well-researched complaints — like the ones filed in the Delaware Derivative Actions — this court must also recognize that timely filings have value, too. In this regard, Teachers did not even file its § 220 action until **after** the Alabama and Delaware Derivative Actions were filed. Even after it received books and records, Teachers took several months to file its Complaint. Notably, Teachers sat idly by while three courts worked together with litigants in pending actions to forge a rational path forward. Those efforts succeeded and were reflected in orders of

[20] The letter from Ronald A. Brown of the Prickett, Jones firm opposing Teachers' desire to prosecute its claims here — a wish Mr. Brown rightly believes would upset the prior coordination order this court entered in the Delaware Derivative Actions as well as the similar orders entered by Judges Bowdre and Horn — succinctly details the numerous productive actions taken by the plaintiffs in the prior-filed Actions and persuasively contrasts that progress with the relatively leisurely schedule by which Teachers simply filed its initial pleading in this action. See Brown Letter, dated Dec. 22, 2003. As Mr. Brown shows, Teachers? timing cannot be compared with that of the plaintiffs in the Delaware Derivative Actions, who successfully balanced the need for careful research with the utility of responsible alacrity in filing. Teachers did not even file its books and records action until over a month after the Delaware Derivative Actions were commenced.

each of those courts, indicating where derivative claims involving HealthSouth would proceed. While Teachers was free to set its own schedule, it cannot be surprised if this court refuses to disrupt the settled expectation of the parties to the prior-filed Actions and to undo the good work of Judges Bowdre and Horn at its tardy instance.

In this respect, it bears noting that this court encouraged Teachers to file suit in Alabama and to attempt to join in the prosecution of the derivative claims in the Alabama Derivative Actions. Teachers refused to do so.

Apparently, its reluctance to do so rests on its desire to be the sole captain of the ship and to proceed in this court, or no other. In support of that desire, Teachers trumpets its prosecution of its $2 11 claim, claiming (with justification) that this victory produced a valuable benefit for HealthSouth's stockholders.[21] Less attractively, however, Teachers has denigrated the efforts and capability of counsel in the prior-filed Actions. Without belaboring the point, I simply note that I do not share Teachers' view that counsel in the Alabama Derivative Actions are inadequate to the task. Among their number are experienced lawyers from many states. These lawyers include Delaware counsel — Prickett, Jones & Elliott[22] -from the Delaware Derivative Actions — a firm with a well-

[21] Teachers also claims that it is a very sophisticated institutional investor, whose savvy will benefit HealthSouth. Although its counsel might be indulged some self-congratulatory comments, the record in the § 220 action does not demonstrate that Teachers' own staff were unusually diligent observers of HealthSouth.

[22] Mr. Brown's corresponding counsel in the Delaware Derivative Actions, Mr. Frank DiPrima, signed the transmittal affidavits supporting the summary judgment motions filed in the Alabama Derivative Actions. These motions, as noted, seek to build on success achieved in the Delaware Derivative Actions and demonstrate the coordination that is now being displayed among counsel for the various derivative plaintiffs.

deserved reputation as effective plaintiffs? counsel, which has already achieved a substantial judgment against defendant Richard Scrushy in this court. Given this reality, and Judge Horn's active oversight of the Alabama Derivative Actions, I am satisfied that the interests of **HealthSouth's** stockholders will be competently championed in Alabama. If Teachers wishes to make sure that is so, its able counsel should intervene in the Alabama Derivative Actions and engage their fellow plaintiffs' lawyers in discussions with a view toward helping with the effective prosecution of the derivative claims in that forum.

III. Conclusion

For the foregoing reasons, the defendants' motion for a stay is hereby **GRANTED.**[23] IT IS SO ORDERED.

[23] Even if *Mc Wane were* not to require a stay, the various considerations I have outlined would justify a stay under a *forum non **conveniens*** analysis.