

IN THE SUPERIOR COURT OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

RICH REALTY, INC., CARSON M.)
GRAY, ADELIA H. GRAY, RICHARD)
E. GRAY, JR., and JOSSLYN GRAY,)
) C.A. No. 09C-12-273 MMJ
Plaintiffs,)
)
v.)
)
POTTER ANDERSON & CORROON)
LLP, and HAROLD I. SALMONS III,)
Esquire,)
)
Defendants.)

Submitted: December 16, 2010

Decided: February 21, 2011

Defendants' Amended Motion to Dismiss the Amended Complaint

OPINION

Gilbert F. Shelsby, Jr., Esquire, Shelsby & Leoni, P.A., Stanton, DE, Of
Counsel: Jack Meyerson, Esquire, (Argued) Meyerson & O'Neill,
Philadelphia, PA, Attorneys for Plaintiff

Joseph Scott Shannon, Esquire, John L. Slimm, Esquire (Argued), Dante C.
Rohr, Esquire, Marshall Dennehey Warner Coleman & Goggin,
Wilmington, DE, Attorneys for Defendants

JOHNSTON, J.

Defendants Potter Anderson & Corroon LLP and Harold I. Salmons III, Esquire (together “Potter Anderson”) move to dismiss plaintiffs Rich Realty, Inc. (“RRI”), Carson M. Gray, Adelia H. Gray, Richard E. Gray, Jr., and Josslyn Gray’s legal malpractice claims and breach of fiduciary duty claims. Pursuant to Superior Court Rule of Civil Procedure 12(b)(6), Potter Anderson asserts that plaintiffs fail to state claims upon which relief can be granted. Plaintiffs’ claims stem from legal services Potter Anderson provided to them; specifically, Potter Anderson drafted corporate documents that created RRI and drafted a lease agreement between RRI and B. F. Rich & Co. (“BFR”). Plaintiffs contend that Potter Anderson committed legal malpractice and breached its fiduciary duties by issuing RRI stock to minors who could not exercise the voting rights of their shares, and by representing plaintiffs with conflicting interests.

For the following reasons, Potter Anderson’s motion to dismiss is granted in part and denied in part. Additionally, the Court dismisses plaintiffs’ breach of fiduciary duty claims pursuant to Rule 12(b)(1) for lack of subject matter jurisdiction.

FACTUAL AND PROCEDURAL CONTEXT

RRI is a Delaware corporation with its principal place of business in Newark, Delaware. RRI was created on July 3, 1997 for the purpose of

acquiring a Newark, Delaware property, where it subsequently constructed a manufacturing facility. Plaintiffs retained Potter Anderson to draft corporate documents relating to the creation of RRI. Potter Anderson drafted the stock subscription and purchase agreement for the issuance of RRI's common stock. 102.61 shares—approximately 93.5%—of RRI's common stock, were issued to Carson, Adelia, Richard, and Josslyn Gray (collectively “Individual Plaintiffs”).

At all relevant times, Carson was of the age of majority. At all relevant times, Adelia, Richard, and Josslyn were minors (without Carson, Individual Plaintiffs are referred to as “Minor Plaintiffs”). Plaintiffs allege that Potter Anderson was aware that Minor Plaintiffs were minors. Plaintiffs aver that they instructed Potter Anderson assign a custodian to exercise the voting rights of the shares issued to Minor Plaintiffs pursuant to the Uniform Transfer to Minors Act (“UTMA”), but Potter Anderson neglected to create such an arrangement.

Potter Anderson also represented BFR, which received 2.61 shares—approximately 2.5%—of RRI's common stock.¹

Allegedly, because Minor Plaintiffs were minors, they could not exercise the voting rights of their shares. As a result, 2.5% shareholder BFR

¹ The remaining shares were issued to a third party.

assumed control over the affairs of RRI. Additionally, BFR exercised control over RRI because BFR directors and officers also served as directors and officers of RRI. Allegedly, the documents prepared by Potter Anderson enabled this assumption of control.

Plaintiffs allege that their inability to direct the affairs of RRI resulted in substantial financial loss. On August 1, 1997, while RRI was under the control of BFR, Potter Anderson drafted a lease agreement between RRI and BFR for the manufacturing facility. Plaintiffs allege that the terms of the lease were “substantially beneath the applicable fair market values at the time in and around Newark, Delaware.” Plaintiffs claim that Potter Anderson did not address or attempt to obtain a waiver of, what plaintiffs characterize as, a “clear conflict of interest.” Ultimately, in December 2008, RRI sold the manufacturing facility for a significantly discounted price.

In 2004, Individual Plaintiffs’ father, Richard E. Gray, Sr. (“Gray, Sr.”), attempted to obtain and exercise the power to vote Minor Plaintiffs’ shares. Gray, Sr. voted Minor Plaintiffs’ shares in a 2005 shareholder consent action designed to return control of RRI to Individual Plaintiffs. BFR responded by bringing an action under 8 *Del. C.* § 225 in the Delaware Court of Chancery, challenging the validity of the shareholder consent vote.

Chancery Court upheld the validity of the action by shareholder consent.² On appeal, the Delaware Supreme Court reversed. The Court held that Gray, Sr. could not vote Minor Plaintiffs' shares because he was not a court-appointed guardian of their shares.³ Therefore, the Supreme Court declared the shareholder consent action invalid.

On December 30, 2009, plaintiffs brought this action, asserting four claims⁴: (Claim 1) Potter Anderson committed legal malpractice by drafting documents issuing common stock directly to Minor Plaintiffs, rather than pursuant to the UTMA; (Claim 2) Potter Anderson breached its fiduciary duties by drafting documents issuing common stock directly to Minor Plaintiffs, rather than pursuant to the UTMA; (Claim 3) Potter Anderson committed legal malpractice by representing both plaintiffs and BFR without obtaining a waiver of a conflict of interest among clients; and (Claim 4) Potter Anderson breached its fiduciary duties by representing both plaintiffs and BFR without obtaining a waiver of a conflict of interest among clients.⁵

² *B.F. Rich Co., Inc. v. Gray*, 2006 WL 3337163 (Del. Ch.).

³ *B.F. Rich & Co., Inc. v. Gray*, 933 A.2d 1231, 1248 (Del. 2007).

⁴ For purposes of this opinion, plaintiffs claims have been organized by substance, rather than combined into 2 Counts as in the Amended Complaint.

⁵ Because there are five plaintiffs and plaintiff sub-groups (Individual Plaintiffs and Minor Plaintiffs) each asserting four claims, the Court identifies which particular plaintiffs are bringing the claim when determining whether that claim survives Potter Anderson's motion to dismiss (e.g., "RRI's Claim 1" or "Minor Plaintiffs' Claim 3"). If the Court generally refers to a claim, the analysis and holding apply to all plaintiffs.

On December 3, 2010, Potter Anderson filed a Rule 12(b)(6) motion to dismiss plaintiffs' claims. Potter Anderson claims that the three-year statute of limitations has run on all of plaintiffs' claims. Additionally, as to the legal malpractice claims, Potter Anderson argues that plaintiffs failed to state claims upon which relief can be granted because issuing stock to minors is permissible under Delaware law. Potter Anderson asserts that Minor Plaintiffs' voting rights could have been exercised by a court-appointed guardian. Moreover, with respect to the breach of fiduciary duty claims, Potter Anderson asserts that it did not have a "special relationship" with plaintiffs, and therefore, it did not owe them fiduciary duties.

DISCUSSION

Breach of Fiduciary Duty Claims—Subject Matter Jurisdiction

This Court's jurisdiction lies in matters of law, and therefore, the Court will dismiss pursuant to Rule 12(b)(1) when it lacks jurisdiction over the subject matter of a complaint.⁶ This Court has held that the Delaware Court of Chancery has exclusive jurisdiction over breach of fiduciary duty claims even where money damages are sought.⁷ "Chancery takes

⁶ *Reybold Venture Group XI-A, LLC v. Atlantic Meridian Crossing, LLC*, 2009 WL 143107, at *2 (Del. Super.); Del. Const. Art. IV, § 7; 10 Del. C. § 541.

⁷ *Reybold*, 2009 WL 143107, at *2-3; see also *Estate of Buonamici v. Morici*, 2009 WL 792390, at *1 (Del. Super.); *McMahon v. New Castle Assoc.*, 532 A.2d 601, 602 (Del. Ch. 1987).

jurisdiction over ‘fiduciary’ relationships because equity, not law, is the source of the right asserted.”⁸

Because Claim 2 and Claim 4 allege breaches of fiduciary duty, the Court dismisses them for lack of subject matter jurisdiction.

Although the Court lacks subject matter jurisdiction to consider Claim 2 and Claim 4, it appears that Potter Anderson did not owe plaintiffs fiduciary duties. Fiduciary relationships arise where “one person reposes special trust in another or where a special duty exists on the part of one person to protect the interests of another.”⁹ “[A] fiduciary is typically one who is entrusted with the power to manage and control the property of another.”¹⁰ The typical relationships that carry fiduciary duties are trusts, corporations, partnerships, and estates.¹¹ There are narrow circumstances where an attorney takes on fiduciary duties, “such as in the case of client trust accounts or when an attorney is acting in a second capacity like a trustee or corporate manager”¹² Indeed, attorneys are colloquially

⁸ *McMahon*, 532 A.2d at 604; 10 *Del. C.* § 341 (“The Court of Chancery shall have jurisdiction to hear and determine all matters and causes in equity.”).

⁹ *Wal-Mart Stores v. AIG Life Ins. Co.*, 901 A.2d 106, 113 (Del. 2006) (quoting *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 872 A.2d 611, 624 (Del. Ch. 2005)).

¹⁰ *Bond Purchase, L.L.C. v. Patriot Tax Credit Props., L.P.*, 746 A.2d 842, 864 (Del. Ch. 1999); *Wilm. Leasing, Inc. v. Parrish Leasing Co.*, 1996 WL 752364, at *14 (Del. Ch.).

¹¹ *Sokol Holdings, Inc. v. Dorsey & Whitney, LLP*, 2009 WL 2501542, at *3 (Del. Ch.) (citing DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 2.03[b][I] (2008)).

¹² *Id.* at *4.

referred to as “fiduciaries,” but an attorney must act in some capacity beyond the mere provision of legal services to owe actionable fiduciary duties.¹³

Plaintiffs have not alleged that Potter Anderson acted in a capacity beyond providing legal services. Plaintiffs have not raised any issue of fact as to the existence of a special trust or relationship. Representation of a minor plaintiff does not, in and of itself, create a fiduciary relationship between attorney and client. Therefore, plaintiffs have not established that Potter Anderson owed them fiduciary duties that could form the basis for an actionable claim.

Rule 12(b)(6) Standard of Review

When reviewing a motion to dismiss, the Court must determine whether plaintiffs have a viable cause of action.¹⁴ Plaintiffs’ complaint may not be dismissed “unless it appears to a certainty that under no set of facts which could be proved to support the claim asserted would the plaintiff[s] be entitled to relief.”¹⁵ When applying this standard, the Court will accept as

¹³ *Id.*

¹⁴ *Proctor v. Taylor*, 2006 WL 1520085, at *1 (Del. Super.).

¹⁵ *Lord v. Souder*, 748 A.2d 393, 398 (Del. 2000).

true all well-pleaded allegations.¹⁶ If plaintiffs may recover, the Court must deny the motion to dismiss.¹⁷

Individual Plaintiffs' Claims—Direct or Derivative

As a preliminary matter, the Court must determine whether Individual Plaintiffs' claims are direct or derivative to resolve whether their claims are barred by the statute of limitations. If any of Individual Plaintiffs' claims are wholly derivative, then RRI, alone, is the appropriate plaintiff for those claims. In that circumstance, the Court need only consider whether RRI is barred by the statute of limitations for that claim. If any of Individual Plaintiffs' claims are wholly direct, the Court must consider whether Individual Plaintiffs are barred by the statute of limitations for that claim, in addition to determining whether RRI is barred.

Therefore, the Court considers whether Individual Plaintiffs' Claim 1 and Claim 3 are direct or derivative.

Parties' Contentions

Potter Anderson argues that Individual Plaintiffs' claims are wholly derivative. Potter Anderson contends that only RRI was allegedly harmed and would benefit from a judgment. By leasing and selling the manufacturing facility for substantially less than market value, Potter

¹⁶ *Spence v. Funk*, 396 A.2d 967, 968 (Del. 1978).

¹⁷ *Id.*

Anderson asserts, RRI suffered financial loss. Potter Anderson claims that Individual Plaintiffs did not suffer injury beyond the loss they incurred as RRI shareholders.

Plaintiffs respond that Individual Plaintiffs' claims are direct because they suffered injuries separate from RRI. As a result of Potter Anderson's legal services, plaintiffs contend that Individual Plaintiffs were deprived of their voting rights while BFR assumed control of RRI. Consequently, plaintiffs argue that Individual Plaintiffs suffered substantial financial loss while BFR benefitted.

Analysis

In *Tooley v. Donaldson*,¹⁸ the Delaware Supreme Court held that whether a claim is direct or derivative is based solely on two questions: "(1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of the recovery or other remedy (the corporation or the stockholders, individually)?"¹⁹ If the corporation, rather than the individual stockholder, suffered the alleged harm, the corporation alone is entitled to recover, and the claim in question is derivative.²⁰ If stockholders suffered harm independent of any injury to

¹⁸ 845 A.2d 1031 (Del. 2004).

¹⁹ *Id.* at 1033.

²⁰ *Id.* at 1036 (citing *Agostino v. Hicks*, 2004 WL 443987, at *7 (Del. Ch.)).

the corporation that would entitle them to individualized recovery, the cause of action is direct.²¹ “To set out an individual action, the plaintiff must allege either ‘an injury which is separate and distinct from that suffered by other shareholders,’ or a wrong involving a contractual right of a shareholder . . . which exists independently of any right of the corporation.”²²

The Court finds that Individual Plaintiffs’ Claim 1 is wholly direct. Individual Plaintiffs have a claim separate from RRI regarding the voting rights of their shares. Individual Plaintiffs’ alleged inability to vote is an injury distinct from any injury suffered by BFR or RRI. A shareholder’s right to vote is contractual and independent of any right of the corporation.²³

The Court finds that Individual Plaintiffs’ Claim 3 is wholly derivative. Plaintiffs allege that the lease and sale terms for the manufacturing facility were substantially below market value, and, as a result, RRI was not fairly compensated. This alleged injury affected all RRI shareholders equally, reducing the value of RRI’s common stock across the board. While BFR allegedly benefitted from a reduced lease rate and sale

²¹ *Id.* at 1039 (“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 the stockholder and that he or she can prevail without showing an injury to the corporation.”).

²² *Moran v. Household Int’l, Inc.*, 490 A.2d 1059, 1070 (Del. Ch. 1985), *aff’d*, 500 A.2d 1346 (Del. 1985); *see also Ruffalo v. Transtech Service Partners, Inc.*, 2010 WL 3307487, at *9 (Del. Ch.) (“Claims based upon contractual rights of the shareholder which exist separately from any right of the corporation are direct claims.”).

²³ *See Moran*, 490 A.2d at 1070.

price, BFR received that benefit outside of its capacity as a RRI shareholder. The value of BFR's common stock, like Individual Plaintiffs' common stock, was diminished.

Accordingly, with respect to Individual Plaintiffs' Claim 1, they have a direct claim. With respect to Individual Plaintiffs' Claim 3, they are nominal plaintiffs because the claim is derivative. Therefore, the Court engages in two separate analyses to determine whether plaintiffs' claims are barred by the statute of limitations: whether Individual Plaintiffs' Claim 1 is barred; and whether RRI's Claim 1 and Claim 3 are barred.

Statute of Limitations

Parties' Contentions

Potter Anderson argues that the three-year statute of limitations has run on plaintiffs' claims because Potter Anderson drafted the documents that created RRI in July 1997 and represented plaintiffs during the lease transaction in August 1997. Potter Anderson contends that plaintiffs have not established that they were "blamelessly ignorant" of the alleged malpractice. Therefore, Potter Anderson asserts, the statute of limitations is not tolled.

Plaintiffs respond that they were blamelessly ignorant of Potter Anderson's alleged malpractice. Regarding Minor Plaintiffs, plaintiffs argue

that, because they were minors, the statute of limitations is tolled until they reach the age of majority. Further, plaintiffs contend that whether they were on inquiry notice of Potter Anderson's alleged malpractice presents a factual issue. Therefore, plaintiffs assert, so long as their complaint sets forth well-pleaded allegations that they were blamelessly ignorant, the Court cannot dismiss their claims.

Analysis

The 10 *Del. C.* § 8106(a) three-year statute of limitations applies to legal malpractice claims.²⁴ “The statute begins to run at the time of the alleged malpractice and even ignorance of the facts constituting a cause of action is no obstacle to the operation of the statute.”²⁵ The exceptions to this rule are “cases of infancy, incapacity, and fraud, and where there are no observable factors that would place a layman on notice of the problem.”²⁶ If an exception applies, the statute of limitations begins to run when the alleged malpractice is discovered.²⁷

²⁴ *Conaway v. Griffin*, 2009 WL 562617, at *2 (Del. Super.) (TABLE); 10 *Del. C.* § 8106 provides, in pertinent part: “no action to recover damages caused by an injury unaccompanied with force or resulting indirectly from the act of the defendant shall be brought after the expiration of 3 years from the accruing of the cause of such action.”

²⁵ *Id.* at *2 (citing *Mastellone v. Argo Oil Corp.*, 82 A.2d 379, 383 (Del. 1951)).

²⁶ *Id.* (citing *Mastellone*, 82 A.2d at 383; *Pioneer Nat'l Title Ins. Co. v. Child, Inc.*, 401 A.2d 68, 71-72 (Del. 1979)).

²⁷ *Id.*

The Court must accept as true any well-pleaded allegations that plaintiffs were blamelessly ignorant. “Where allegations are merely conclusory, however, (*i.e.*, without specific allegations of fact to support them) they may be deemed insufficient to withstand a motion to dismiss.”²⁸

Carson’s claims are barred by the statute of limitations; Minor Plaintiffs’ claims are not.

The Court finds that Carson’s claims are barred by the section 8106(a) statute of limitations because it has been more than three years since Potter Anderson drafted the corporate documents and lease agreement in 1997. Carson was of the age of majority at all relevant times, and therefore, the infancy exception does not apply.

Plaintiffs did not provide well-pleaded allegations that Carson was otherwise blamelessly ignorant of Potter Anderson’s alleged malpractice. In paragraph 39 of their Amended Complaint, plaintiffs state that “[t]he Individual Plaintiffs, prior to December 2008, remained blamelessly ignorant of the acts and circumstances surrounding the negotiation of the lease and its terms, as drafted by [Potter Anderson].”²⁹ In paragraph 40, plaintiffs allege:

Although aware of the lease from its inception, RRI remained controlled by individuals aligned with BFR as installed by

²⁸ *Id.* (citing *In re Tri-Star Pictures, Inc. Litig.*, 634 A.2d 319, 326 (Del. 1993)).

²⁹ Am. Compl. at ¶ 39 (Tr. Id. 31995479).

defendants and could not address the inequities in the lease prior to the time that non-BFR aligned persons obtained absolute control of RRI in December 2008. Control and continuing misconduct by the defendants and BFR prevented plaintiffs and RRI from taking any action as to the lease until December 2008.³⁰

The Court finds that the allegations in paragraphs 39 and 40 are conclusory. The Amended Complaint fails to set forth particularized factual contentions as to why plaintiffs were blamelessly ignorant. Control of RRI by BFR and unspecified “continuing misconduct” are bare-bones allegations insufficient to excuse filing suit within the three-year statute of limitations.

As to Minor Plaintiffs, the Court finds that their claims are not barred by the statute of limitations. Minor Plaintiffs’ infancy, at all relevant times, tolls the statute of limitations.³¹

RRI’s claims are barred by the statute of limitations.

The Court finds that RRI’s Claim 1 and Claim 3 are barred by the section 8106(a) statute of limitations because it has been more than three years since Potter Anderson drafted the corporate documents and lease agreement in 1997. Plaintiffs did not provide well-pleaded allegations that RRI was blamelessly ignorant of Potter Anderson’s alleged malpractice. Paragraph 40 alleges that RRI could not bring an action against Potter

³⁰ *Id.* at ¶ 40.

³¹ *See Conaway*, 2009 WL 562617, at *2.

Anderson within the statute of limitations because RRI was under BFR's control. This allegation is insufficient to toll the statute of limitations. Assuming that BFR controlled RRI, there was no specifically-pled impediment to Individual Plaintiffs bringing a derivative claim on behalf of RRI within the three-year statute of limitations.

Claim 1—Minor Plaintiffs Stock Issuance Malpractice Claim

Parties' Contentions

Potter Anderson argues that Claim 1 fails to state a claim upon which relief can be granted because issuing stock to minors does not violate Delaware law. Potter Anderson contends that, although they did not issue the stock to Minor Plaintiffs pursuant to the UTMA, Minor Plaintiffs could have voted their shares through a court-appointed guardian.

Plaintiffs respond that whether Minor Plaintiffs could have voted their shares through a court-appointed guardian is not dispositive of their malpractice claim. Rather, plaintiffs assert, the issue is whether Potter Anderson committed legal malpractice by issuing stock to Minor Plaintiffs without an UTMA custodian after plaintiffs instructed Potter Anderson to create such an arrangement.

Analysis

The Court finds that Claim 1 states a claim upon which relief can be granted. The Amended Complaint raises questions of fact as to whether plaintiffs instructed Potter Anderson to issue the stock to Minor Plaintiffs with a UTMA custodian; what instructions were given to Potter Anderson regarding who would control RRI and how RRI should be controlled; whether Potter Anderson negligently disregarded plaintiffs' instructions; and whether Minor Plaintiffs suffered injury as a result of the alleged legal malpractice.

CONCLUSION

The Court dismisses plaintiffs' breach of fiduciary duty claims pursuant to Rule 12(b)(1) for lack of subject matter jurisdiction. The Court of Chancery has exclusive jurisdiction over such claims. In any event, plaintiffs have failed to allege facts sufficient to create the special trust or relationship requisite to an actionable fiduciary duty claim.

Individual Plaintiffs' legal malpractice claims regarding the lease transaction are wholly derivative, and therefore, Individual Plaintiffs do not have a cause of action separate from RRI.

RRI's claims and Carson's claims are barred by the three-year statute of limitations established by 10 *Del. C.* § 8106(a). Plaintiffs have failed to

allege with sufficient specificity that RRI or Carson were blamelessly ignorant of Potter Anderson's alleged malpractice, in such a manner that would toll the statute of limitations.

The statute of limitations is tolled as to Minor Plaintiffs' claim that Potter Anderson committed legal malpractice by drafting documents issuing common stock directly to Minor Plaintiffs, rather than pursuant to the UTMA. The Court finds that this contention states a claim upon which relief may be granted for purposes of Rule 12(b)(6).

THEREFORE, Defendants' Amended Motion to Dismiss is hereby **GRANTED IN PART**. All claims except Minor Plaintiffs' claim that Potter Anderson committed legal malpractice by drafting documents issuing common stock directly to Minor Plaintiffs, rather than pursuant to the UTMA, are hereby **DISMISSED**.

IT IS SO ORDERED.

/s/ Mary M. Johnston
The Honorable Mary M. Johnston