IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE TRADOS INCORPORATED SHAREHOLDER LITIGATION	))	Civil Action No. 1512-CC

MEMORANDUM OPINION

Date Submitted: July 7, 2009
Date Decided: July 24, 2009

David A. Jenkins, Michele C. Gott, and Robert K. Beste, of SMITH, KATZENSTEIN & FURLOW LLP, Wilmington, Delaware, Attorneys for Plaintiff.

Raymond J. DiCamillo and Scott W. Perkins, of RICHARDS, LAYTON & FINGER, P.A., Wilmington, Delaware; OF COUNSEL: David J. Berger, Elizabeth M. Saunders, and Luke A. Liss, of WILSON SONSINI GOODRICH & ROSATI, PROFESSIONAL CORPORATION, Palo Alto, California, Attorneys for Defendants.

CHANDLER, Chancellor

This is a purported class action brought by a former stockholder of Trados Incorporated ("Trados," or the "Company") for breach of fiduciary duty arising out of a transaction whereby Trados became a wholly owned subsidiary of SDL, plc ("SDL"). Of the $60 million contributed by SDL, Trados' preferred stockholders received approximately $52 million. The remainder was distributed to the Company's executive officers pursuant to a previously approved bonus plan. Trados' common stockholders received nothing for their common shares.

Plaintiff contends that this transaction was undertaken at the behest of certain preferred stockholders that desired a transaction that would trigger their large liquidation preference and allow them to exit their investment in Trados. Plaintiff alleges that the Trados board favored the interests of the preferred stockholders, either at the expense of the common stockholders or without properly considering the effect of the merger on the common stockholders. Specifically, plaintiff alleges that the four directors designated by preferred stockholders had other relationships with preferred stockholders and were incapable of exercising disinterested and independent business judgment. Plaintiff further alleges that the two Trados directors who were also employees of the Company received material personal benefits as a result of the merger and were therefore also incapable of exercising disinterested and independent business judgment. Finally, plaintiff alleges that SDL and certain of its executive officers conspired with certain Trados directors to defer revenue until after the merger.

As explained below, plaintiff has alleged facts sufficient, at this preliminary stage, to demonstrate that at least a majority of the members of Trados' seven member board were unable to exercise independent and disinterested business judgment in deciding whether to approve the merger. Accordingly, I decline to dismiss the breach of fiduciary duty claims arising out of the board's approval of the merger. Plaintiff has failed, however, to state a claim based on the alleged revenue manipulation. Accordingly, I dismiss the breach of duty and aiding and abetting claims based on the alleged revenue manipulation.

I. BACKGROUND

A. The Parties

Before the merger, Trados developed software and services used by businesses to make the translation of text and material into other languages more efficient. Founded in 1984 as a German entity, Trados moved to the United States in the mid-1990s with the hope of going public, and became a Delaware corporation in March 2000. To better position itself for the possibility of going public, Trados accepted investments from venture capital firms and other entities. As a result, preferred stockholders had a total of four designees on Trados' seven member board. Each of the seven members of Trados' board at the time of the board's approval of the merger is named as a defendant in this action.

David Scanlan was the board designee of, and a partner in, Wachovia Capital Partners, LLC ("Wachovia"). At the time of the merger, Wachovia owned 3,640,000 shares of Trados' Series A preferred stock (100% of that series) and 1,007,151 shares of Trados' Series BB preferred stock (approximately 24% of that series).

Lisa Stone was the board designee of Rowan Entities Limited and Rowan Nominees Limited RR (together, the "Rowan Entities"), transferees of Trados' preferred stock held by Hg Investment Managers Limited (collectively, "Hg"). Stone was a director and employee of both Hg Investment Managers Limited and the Rowan Entities.[1] At the time of the merger, Hg owned 1,379,039 shares of Trados' common stock (approximately 4.3%), 2,014,302 shares of Trados' Series BB preferred stock (approximately 48.3% of that series), 5,333,330 shares of Trados' Series C preferred shares (all of that series), and 862,976 shares of Trados' Series D preferred stock (approximately 28.6% of that series).

[1] Plaintiff also alleges that Stone was a part owner of Hg, and that Stone had a personal financial interest in Hg's investment in Trados. Plaintiff further alleges that Hg Investment Managers Limited continued to be the beneficial owners of all shares owned by Hg, and that both Rowan Entities were affiliates of Hg Investment Managers Limited. First Am. Verified Compl. ("Compl.") ¶ 8.

Sameer Gandhi was a board designee of, and a partner in, several entities known as Sequoia. Sequoia owned 5,255,913 shares of Trados' Series E preferred stock (approximately 32% of that series).

Joseph Prang was also a board designee of Sequoia. Prang owned Mentor Capital Group LLC ("Mentor Capital"), which owned 263,810 shares of Trados' Series E preferred stock (approximately 1% of that series).

Wachovia, Hg, Sequoia, and Mentor combined owned approximately 51% of Trados' outstanding preferred stock. Plaintiff alleges that these preferred stockholders desired to exit their investment in Trados.[2]

Two of the three remaining director defendants were employees of Trados. Jochen Hummel was acting President of Trados from April 2004 until September or October 2004, and was also the Company's chief technology officer. Joseph Campbell was Trados' CEO from August 23, 2004 until the merger. The remaining Trados director was Klaus-Dieter Laidig.

[2] Compl. ¶¶ 30, 35-37, 44, 51, 79, 84, 101-102. Plaintiff alleges, for example, that in January 2003 Gandhi wrote that Sequoia's "only real opportunity is to capture a fraction of our 13m investment," and that in June 2003 Gandhi acknowledged that Trados' long term prospects were improving, but wrote that Sequoia "d[id] not own enough of the company to make a meaningful return." *Id.* ¶ 30. Plaintiff further alleges that by mid-2004 Wachovia wanted to exit its investment in Trados because Scanlan felt that the investment was underperforming and consuming too much of his time relative to the size of the investment. *Id.* ¶ 35. Plaintiff also contends that Hg and Mentor wanted to exit their investments in Trados.

B. The Negotiations

In April 2004, the Trados board began to discuss a potential sale of the Company, and later formed a mergers and acquisitions committee, consisting of Stone, Gandhi, and Scanlan, to explore a sale or merger of Trados. Around the same time, the Company's President and CEO was terminated due to, among other issues, a perception by the rest of the board that Trados was underperforming. The board appointed Hummel as an interim President, but instructed him to consult with Gandhi and Scanlan before taking material action on behalf of the Company. In July 2004, Campbell was hired as the Company's CEO, effective August 23, 2004. Gandhi described Campbell as "a hard-nosed CEO whose task is to grow the company profitably or sell it."[3] At the time Campbell joined Trados, however, the Company was losing money and had little cash to fund continuing operations.[4] At a July 7, 2004 meeting, Trados' board determined that the fair market value of Trados' common stock was $0.10 per share.

In June 2004, Trados engaged JMP Securities, LLC, an investment bank, to assist in identifying potential alternatives for a merger or sale of the Company. By July 2004, JMP Securities had identified twenty seven potential buyers of Trados,

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[3] Compl. ¶ 40. In June 2004, Gandhi also reported to Sequoia that a "banker has also been retained to explore the M&A options for the business. I would expect that the company is sold within the next 18 months (perhaps sooner)." *Id.*

[4] Plaintiff alleges that Campbell believed that his "mission on joining TRADOS was to help the company understand its future path, which in the mind of the outside board members at that time was some type of either merger or acquisition event due to the company's performance that year and prior years." Compl. ¶ 44.

and contacted seven of them, including SDL. By August 2004, JMP Securities had conducted discussions with SDL CEO Mark Lancaster, who made an acquisition proposal in the $40 million range. Trados informed Lancaster that it was not interested in a deal at that price, and Campbell formally terminated JMP Securities in September 2004.

In July 2004, Scanlan expressed concern that the executive officers of the Company might not have sufficient incentives to remain with the Company or pursue a potential acquisition of the Company, due to the high liquidation preference of the Company's preferred stock. The board instructed Scanlan to develop a bonus plan to address these concerns. This led to the December 2004 board approval of the Management Incentive Plan (the "MIP"), which set a graduated compensation scale for the Company's management based on the price obtained for the Company in an acquisition.[5]

Trados' financial condition improved markedly during the fourth quarter of 2004, in part due to Campbell's efforts to reduce spending and bring in additional cash through debt financing. By the time of the December 2004 board meeting,

[5] Under the MIP, management would receive 6% of the acquisition price for an acquisition between $30-40 million; 11% for an acquisition between $40-50 million; 13% for an acquisition between $50-90 million; 14% for an acquisition between $90-120 million; and 15% for an acquisition at or above $120 million. From that pool, Campbell would be entitled to 30%, Hummel to 12%, and James Budge to 10%. Plaintiff alleges that an investor described the MIP as "protection for the management team in case [some] shareholders want to sell [the company] at a price where the options/common shares are worthless." Compl. ¶ 52.

Trados had arranged to borrow $2.5 million from Western Technology Investment, with the right to borrow an additional $1.5 million.

Despite the Company's improved performance, the board continued to work toward a sale of the Company. In December 2004, Gandhi reported to Sequoia Capital that the Company's performance was improving, but that Campbell's "mission is to architect an M&A event as soon as practicable."[6] At a February 2, 2005 board meeting, Campbell presented positive financial results from the fourth quarter of 2004, including record revenue and profit from operations. As a result of its improved performance and the lack of an immediate need for cash, the board extended by six months the period during which it could obtain additional cash from Western Technology Investment.

In January 2005, SDL initiated renewed merger discussions with Campbell. Upon learning of SDL's interest, the Trados board expressed that it was not interested in any transaction involving less than a "60-plus" million dollar purchase price. Lancaster first discussed a transaction at $50 million, but later offered $60 million. At the February 2, 2005 meeting, the board instructed Campbell to continue negotiating with Lancaster under the general terms SDL proposed, including the $60 million price. In mid-February 2005, Campbell made inquiries

[6] *Id.* ¶ 51.

with two other potential acquirers of Trados, but neither expressed any substantive interest.

In a theme that runs throughout his allegations, plaintiff alleges that there was no need to sell Trados at the time because the Company was well financed and experiencing improved performance under Campbell's leadership. For example, plaintiff contends that by February 2005 Trados was beating its revenue budget for the year, a trend that continued as Trados beat its revenue projections for the first quarter of 2005 and through the end of May 2005.

By February 2005, Campbell and Lancaster agreed to the basic terms of a merger at $60 million. Trados then re-engaged JMP securities, which plaintiff alleges acted as little more than a "go-between." In April 2005, SDL and Trados signed the letter of intent for the merger at the $60 million price.

C. The Alleged Revenue Manipulation

Plaintiff alleges that SDL, Lancaster, and Alastair Gordon (the "SDL Defendants") conspired with Campbell, Budge, and Hummel to change Trados' normal business practices with respect to the receipt and recognition of revenue. These changes allegedly served no proper purpose for Trados, but would benefit SDL financially by increasing its post-merger revenues. Specifically, plaintiff alleges that Trados management and SDL agreed to (1) delay the recognition of at least $2,046,000 of Trados' revenues until after the merger closed; (2) delay the release of Desktop 7.0, Trados' newest version of its desktop translation software, until after the merger closed, and (3) allow deals representing approximately $1 million of Trados' revenues to "slip" until after the merger.[7]

D. The Merger

The director defendants unanimously approved the merger, and on June 19, 2005 Trados and SDL entered into an Agreement and Plan of Merger. Of the $60 million merger price, approximately $7.8 million would go to management pursuant to the MIP, and the remainder would go to the preferred stockholders in partial satisfaction of their $57.9 million liquidation preference. Plaintiff alleges that the directors know both of these facts, and thus knew that the common shareholders would receive nothing in the merger.[8] The merger was consummated on July 7, 2005.

Plaintiff alleges that Campbell and Hummel received benefits as a result of the merger. Campbell became a director of SDL and received $775,000 through

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[7] In support of these allegations, plaintiff cites to several emails that allegedly evidence the revenue manipulation. For example, by e-mail of May 18, 2005, a Trados attorney told Campbell that he was using a section of the merger agreement to reflect restrictions that SDL was imposing, such as delaying revenue and the release of Desktop 7. Compl. ¶ 68. On June 30, 2005, Budge reported to Campbell that they would have at least $1.9 million in deferred revenue to deliver to SDL, "close to the $2m we promised." *Id.* ¶ 71. On July 6, 2005, Campbell advised Lancaster that "$2,046k in business will be shipped after the deal is substantially closed which is hopefully today and the result will be $2m+ of revenue and profit immediately for SDL." *Id.* ¶ 72. On July 19, 2005, Budge advised Lancaster, Gordon and Campbell that shipping on certain deals had been pushed off until after the Merger "such that SDL could have all the revenue post acquisition." *Id.* ¶ 75.

[8] Plaintiff alleges that, based on advice from Kevin Passarello, Trados' vice president and general counsel, the board believed that the common stockholders did not have the right to seek appraisal of their shares. *Id.* ¶ 85.

the MIP, $1,315,000 in exchange for a non-compete agreement, and a $250,000 bonus. Campbell took $702,000 of his MIP compensation in SDL stock, and $73,000 in cash. Hummel became "SDL's general manager of Europe, the Middle East, and Asia (technology division)," and received $1,092,000 under the MIP, of which he took $436,800 in SDL stock and $655,200 in cash.[9]

On July 21, 2005, plaintiff filed a petition for appraisal, seeking payment of the fair value of his stock as of the date of the merger. Almost three years later, on July 3, 2008, plaintiff commenced a second action, both individually and purportedly on behalf of a class of former stockholders of Trados, against the director defendants. On December 12, 2008, plaintiff filed the First Amended Verified Complaint (the "Complaint"), which includes new facts allegedly discovered by plaintiff in discovery conducted as part of the appraisal action. Defendants have moved for dismissal of the Complaint for failure to state a claim upon which relief may be granted.

II. ANALYSIS

A. The Legal Standard

This Court may grant a motion to dismiss for failure to state a claim under Rule 12(b)(6) if the Court can determine with reasonable certainty that the plaintiff would not be entitled to relief under any set of facts that could be reasonably

[9] *Id.* ¶ 64.

inferred from the well-pleaded allegations in the complaint.[10] In considering a motion to dismiss, the court must accept the well-pleaded allegations of fact in the complaint as true and draw all reasonable inferences that logically flow from those allegations in the plaintiff's favor.[11] Of course, the court is not required to accept mere conclusory allegations as true or make inferences that are not supported by well-pleaded factual allegations.[12] Moreover, the court "is not required to accept every strained interpretation of the allegations proposed by the plaintiff."[13]

B. Laches

Defendants contend that plaintiff's claims for breach of fiduciary duty against the director defendants are barred by the equitable doctrine of laches and should therefore be dismissed.[14] It is well established that "equity follows the law and will apply a statute of limitations by analogy in appropriate circumstances."[15] This Court, however, is not bound by the analogous statute, and, "as the equities require, may apply a period either shorter or longer than that fixed by statute."[16]

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[10] *Malpiede v. Townson*, 780 A.2d 1075, 1082-83 (Del. 2001).
[11] *In re Gen. Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 168 (Del. 2006).
[12] *In re Lukens Inc. S'holders Litig.*, 757 A.2d 720, 727 (Del. Ch. 1999).
[13] *Gen. Motors*, 897 A.2d at 168 (quoting *Malpiede*, 780 A.2d at 1083).
[14] Defendants also contend that the claims against the SDL Defendants are time-barred. As a result of the holdings explained below, however, I need not reach that issue. Moreover, plaintiff made clear in his answering brief that he is not seeking relief based on the approval of the MIP, and merely refers to the MIP as evidence of the alleged incentive for the director defendants to approve the merger. Pl.'s Answering Br. in Opp'n to the Director Defs.' Mot. to Dismiss ("Pl.'s Answering Br.") 2. Accordingly, I need not address defendants' argument that the Court should apply the statute of limitations to bar plaintiff's claims based on the MIP.
[15] *In re Dean Witter P'ship Litig.*, 1998 WL 442456, at *3 (Del. Ch. July 17, 1998).
[16] *Elster v. Am. Airlines, Inc.*, 128 A.2d 801, 805 (Del. Ch. 1957).

Generally, this Court will only apply "a shorter period if, in terms of equity, the plaintiff should have acted with greater alacrity, and when the plaintiff's failure to seek equitable relief with alacrity threatens prejudice to the other party."[17]

The statute of limitations applied to actions for breach of fiduciary duty is three years.[18] Defendants concede that plaintiff filed the fiduciary duty claims within three years of the close of the merger, but argue that the Court should exercise its discretion to apply a shorter period to bar the action. Even accepting defendants' argument that plaintiff had knowledge of the facts underlying the claim, defendants have not shown a threat of undue prejudice as a result of plaintiff's choice to bring the fiduciary duty claims nearly three years after consummation of the merger.

Simply put, I am not convinced that the prejudice defendants allege is the kind of prejudice that would allow this Court, on grounds of equity, to shorten the three year limitation period. Plaintiff is seeking monetary damages, rather than injunctive relief or specific performance. Accordingly, this is not a case in which plaintiff must "act with dispatch" or lose the right to seek relief, even before the end of the analogous limitations period.[19] Moreover, I see no indication of

[17] *U.S. Virgin Islands v. Goldman, Sachs & Co.*, 937 A.2d 760, 808 (Del. Ch. 2007).
[18] 10 *Del. C.* § 8106.
[19] *See CertainTeed Corp. v. Celotex Corp.*, 2005 WL 217032, at *6 (Del. Ch. Jan. 24, 2005); *State ex rel. Brady v. Pettinaro Enters.*, 870 A.2d 513, 527 (Del. Ch. 2005) ("[I]t is understood that the bar of laches will typically arise earlier than the end of the limitations period when a plaintiff seeks a judicial order involving compulsions such as an injunction or an order of

prejudice to defendants because witnesses or other evidence have become unavailable, or because defendants suffered financial detriment by relying on plaintiff's failure to seek relief in a timely manner.[20]

Defendants argue that plaintiff's delay in bringing the fiduciary duty claims has caused them prejudice because "[t]he parties have been embroiled in the Appraisal Action for three years and have engaged in discovery battles, depositions and other motions."[21] Defendants fail, however, to explain how litigating the appraisal action has caused them material and undue prejudice. Defendants also argue that plaintiff has used "misleading excerpts" from depositions of certain of the director defendants who were deposed in the appraisal action and, according to defendants, were not represented by counsel because they were not then

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specific performance. Remedies of this kind will only issue if the plaintiff acts with dispatch, and are normally foreclosed to a plaintiff who sits on its hands until near the end of the analogous limitations period.").

[20] *See Whittington v. Dragon Group L.L.C.*, 2008 WL 4419075, at *7 (Del. Ch. June 6, 2008) ("For purposes of laches, prejudice may occur in different ways. There might be procedural prejudice where, for example, the delay prevents a party from calling crucial witnesses who have become unavailable because of intervening disappearance, illness, or death. Prejudice can also be substantive, such as where a party suffers a financial detriment by relying on the plaintiffs' failure to seek relief in a timely manner.") (footnotes omitted). During oral argument, defendants suggested that they have suffered prejudice because, as in any litigation, memories may fade with the passage of time. As an initial matter, such an assertion, of itself, is not sufficient to establish prejudice for purposes of laches. Moreover, as plaintiff pointed out at oral argument, on January 26, 2009, defendants moved to stay discovery, and the Court granted that motion on February 26, 2009. Defendants' own request that this Court delay discovery seriously undercuts their assertion at oral argument that fading memories or the loss of other evidence threatens them with prejudice.

[21] Opening Br. of Director Defs. in Supp. of their Mot. to Dismiss ("Defs.' Opening Br.") 36.

defendants.[22] Again, defendants fail to establish how this fact would cause them material and undue prejudice. If defendants believe that plaintiff has used "misleading excerpts" from these depositions, then they can conduct discovery of their own and rebut plaintiff's assertions in their defense of this action.

Because defendants have failed to establish that they have suffered or are threatened with any material and undue prejudice as a result of plaintiff's delay in bringing the fiduciary duty claims against the director defendants, I am unable and unwilling to shorten the analogous limitations period. Accordingly, at this stage, I decline to dismiss the claims asserted against the director defendants on grounds of laches.

C. Fiduciary Duty Claims

Count I of the Complaint asserts a claim that the director defendants breached their fiduciary duty of loyalty to Trados' common stockholders by approving the merger. Plaintiff alleges that there was no need to sell Trados at the time because the Company was well-financed, profitable, and beating revenue projections. Further, plaintiff contends, "in approving the Merger, the Director Defendants never considered the interest of the common stockholders in continuing Trados as a going concern, even though they were obliged to give

[22] *Id.*

priority to that interest over the preferred stockholders' interest in exiting their investment."[23]

Directors of Delaware corporations are protected in their decision-making by the business judgment rule, which "is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."[24] The rule reflects and promotes the role of the board of directors as the proper body to manage the business and affairs of the corporation.[25]

The party challenging the directors' decision bears the burden of rebutting the presumption of the rule.[26] If the presumption of the rule is not rebutted, then the Court will not second-guess the business decisions of the board.[27] If the presumption of the rule is rebutted, then the burden of proving entire fairness shifts to the director defendants.[28] A plaintiff can survive a motion to dismiss under Rule 12(b)(6) by pleading facts from which a reasonable inference can be drawn that a majority of the board was interested or lacked independence with respect to the relevant decision.[29]

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[23] Pl.'s Answering Br. 11-12.
[24] *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).
[25] 8 *Del. C.* § 141(a); *In re CompuCom Sys., Inc. Stockholders Litig.*, 2005 WL 2481325, at *5 (Del. Ch. Sept. 29, 2005).
[26] *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993).
[27] *Id.*
[28] *Id.*
[29] *Orman v. Cullman*, 794 A.2d 5, 22-23 (Del. Ch. 2002).

A director is interested in a transaction if "he or she will receive a personal financial benefit from a transaction that is not equally shared by the stockholders" or if "a corporate decision will have a materially detrimental impact on a director, but not on the corporation and the stockholders."[30] The receipt of any benefit is not sufficient to cause a director to be interested in a transaction. Rather, the benefit received by the director and not shared with stockholders must be "of a sufficiently material importance, in the context of the director's economic circumstances, as to have made it improbable that the director could perform her fiduciary duties ... without being influenced by her overriding personal interest . . . ."[31]

"Independence means that a director's decision is based on the corporate merits of the subject before the board rather than extraneous considerations or influences."[32] At this stage, a lack of independence can be shown by pleading facts that support a reasonable inference that the director is beholden to a controlling person or "so under their influence that their discretion would be sterilized."[33]

Plaintiff's theory of the case is based on the proposition that, for purposes of the merger, the preferred stockholders' interests diverged from the interests of the

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[30] *Rales v. Blasband*, 634 A.2d 927, 936 (Del. 1993).
[31] *In re Gen. Motors Class H S'holders Litig.*, 734 A.2d 611, 617 (Del. Ch. 1999); *see Orman*, 794 A.2d at 23.
[32] *Aronson*, 473 A.2d at 816.
[33] *Rales*, 634 A.2d at 936.

common stockholders. Plaintiff contends that the merger took place at the behest of certain preferred stockholders, who wanted to exit their investment. Defendants contend that plaintiff ignores the "obvious alignment" of the interest of the preferred and common stockholders in obtaining the highest price available for the company.[34] Defendants assert that because the preferred stockholders would not receive their entire liquidation preference in the merger, they would benefit if a higher price were obtained for the Company.[35] Even accepting this proposition as true, however, it is not the case that the interests of the preferred and common stockholders were aligned with respect to the decision of whether to pursue a sale of the company or continue to operate the Company without pursuing a transaction at the time.

The merger triggered the $57.9 million liquidation preference of the preferred stockholders, and the preferred stockholders received approximately $52 million dollars as a result of the merger. In contrast, the common stockholders received nothing as a result of the merger, and lost the ability to ever receive anything of value in the future for their ownership interest in Trados. It would not

[34] Defs.' Opening Br. 18-20.

[35] Defendants also contend that the preferred stockholders would receive payment on an as converted basis with the common stockholders. *Id.* at 12-13 ("[T]he preferred would receive the first $57.9 million of any transaction, and would thereafter receive payment on an as converted basis with the common stockholders."); *see* Compl. ¶ 37 ("[O]nce the Liquidation Preferences of Sequoia Capital and Mentor Capital's preferred stock were satisfied in a sale or acquisition of Trados, those entities would not share in any further consideration, which *mostly* would go to Trados' common stockholders.") (emphasis added); Pl.'s Answering Br. 22-23.

stretch reason to say that this is the worst possible outcome for the common stockholders. The common stockholders would certainly be no worse off had the merger not occurred.

Taking, as I must, the well-pleaded facts in the Complaint in the light most favorable to plaintiff, it is reasonable to infer that the common stockholders would have been able to receive some consideration for their Trados shares at some point in the future had the merger not occurred.[36] This inference is supported by plaintiff's allegations that the Company's performance had significantly improved and that the Company had secured additional capital through debt financing.[37] Thus, it is reasonable to infer from the factual allegations in the Complaint that the interests of the preferred and common stockholders were not aligned with respect to the decision to pursue a transaction that would trigger the liquidation preference of the preferred and result in no consideration for the common stockholders.[38]

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[36] On a motion to dismiss for failure to state a claim, I am required to draw all reasonable inferences in favor of the non-moving party. As a result, there are sometimes reasonable (even, potentially, more likely) inferences that must be passed over at this stage of the proceedings. For example, it would be reasonable to infer from the allegations in the Complaint that pursing the transaction with SDL was in the best interest of the Company because it secured the best value reasonably available for the Company's stakeholders and did not harm the common shareholders because, in fact, there was no reasonable chance that they would ever obtain any value for their stock even absent the transaction. Nothing in this Opinion is intended to suggest that it would necessarily be a breach of fiduciary duty for a board to approve a transaction that, as a result of liquidation preferences, does not provide any consideration to the common stockholders.

[37] *See, e.g.*, Compl. ¶¶ 53, 61, 84.

[38] Defendants do not argue that the board had an obligation to the preferred stockholders to pursue a transaction that would trigger the large liquidation preference of the preferred stock. Thus, it is reasonable to infer, at this stage, that one option would be for the Company to continue to operate without paying the large liquidation preference to the preferred, subject of

Generally, the rights and preferences of preferred stock are contractual in nature.[39] This Court has held that directors owe fiduciary duties to preferred stockholders as well as common stockholders where the right claimed by the preferred "is not to a preference as against the common stock but rather a right shared equally with the common."[40] Where this is not the case, however, "generally it will be the duty of the board, where discretionary judgment is to be exercised, to prefer the interests of common stock—as the good faith judgment of the board sees them to be—to the interests created by the special rights, preferences, *etc.,* of preferred stock, where there is a conflict."[41] Thus, in circumstances where the interests of the common stockholders diverge from those of the preferred stockholders, it is *possible* that a director could breach her duty by improperly favoring the interests of the preferred stockholders over those of the

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course, to any other contractual rights the preferred stockholders may have had. Indeed, in a situation in which the liquidation preference of the preferred exceeded the consideration that could be achieved in a transaction, it would arguably be in the interest of the common stockholders not to pursue any transaction that would trigger the liquidation preference. It is also reasonable to infer that the preferred stockholders would benefit from a transaction that allowed them to exit the investment while also triggering their liquidation preference, something they did not have a contractual right to force the Company to do. Again, at this stage, I am required to make reasonable inferences in plaintiff's favor, even if there are other reasonable inferences that can be drawn from the alleged facts and that would result in dismissal of the Complaint.

[39] *Jedwab v. MGM Grand Hotels, Inc.*, 509 A.2d 584, 594 (Del. Ch. 1986) ("[W]ith respect to matters relating to preferences or limitations that distinguish preferred stock from common, the duty of the corporation and its directors is essentially contractual and the scope of the duty is appropriately defined by reference to the specific words evidencing that contract . . . ."); *see Matulich v. Aegis Commc'ns Group, Inc.*, 942 A.2d 596, 599-600 (Del. 2008).

[40] *Jedwab*, 509 A.2d at 594.

[41] *Equity-Linked Investors, L.P. v. Adams*, 705 A.2d 1040, 1042 (Del. Ch. 1997) (citing *Katz v. Oak Indus., Inc.*, 508 A.2d 873, 879 (Del. Ch. 1986)).

common stockholders.[42] As explained above, the factual allegations in the Complaint support a reasonable inference that the interests of the preferred and common stockholders diverged with respect to the decision of whether to pursue

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[42] *See Blackmore Partners, L.P. v. Link Energy LLC*, 864 A.2d 80, 85-86 (Del. Ch. 2004) ("[T]he allegation that the Defendant Directors approved a sale of substantially all of [the company's] assets and a resultant distribution of proceeds that went exclusively to the company's creditors raises a reasonable inference of disloyalty or intentional misconduct. Of course, it is also possible to infer (and the record at a later stage may well show) that the Director Defendants made a good faith judgment, after reasonable investigation, that there was no future for the business and no better alternative for the unit holders. Nevertheless, based only the facts alleged and the reasonable inferences that the court must draw from them, it would appear that no transaction could have been worse for the unit holders and reasonable to infer, as the plaintiff argues, that a properly motivated board of directors would not have agreed to a proposal that wiped out the value of the common equity and surrendered all of that value to the company's creditors."). Defendants contend that *Blackmore Partners* can be distinguished from this case because "the Court in *Blackmore Partners* found that defendants favored creditors to whom they did not owe fiduciary duties over unit holders to whom they did owe fiduciary duties" and that plaintiff "does not, and cannot, allege that the Director Defendants favored anyone to whom they did not owe a fiduciary duty." Reply Br. of Director Defendants in Further Support of their Mot. to Dismiss ("Defs.' Reply Br.") 23. As explained above, however, preferred stockholders are owed the same fiduciary duties as common stockholders when the right claimed by the preferred is "a right shared equally with the common." *Jedwab*, 509 A.2d at 594. If and when the interests of the preferred stockholders diverge from those of the common stockholders, the directors generally must "prefer the interests of common stock—as the good faith judgment of the board sees them to be—to the interests created by the special rights, preferences, *etc.,* of preferred stock." *Equity-Linked Investors*, 705 A.2d at 1042. Based on the allegations in the Complaint, it does not appear that the preferred stockholders had any contractual right to force a transaction that would trigger their liquidation preference. Moreover, the transaction with SDL was, under at least one reasonable inference that can be drawn from the Complaint, not in the best interest of Trados' common stockholders.

Defendants may be correct that the facts in *Blackmore Partners* are somewhat more "extreme" than those alleged in the complaint because the Court in *Blackmore Partners* found "a basis in the complaint to infer that the value of [the company's] assets exceeded its liabilities by least $25 million." *Blackmore Partners*, 864 A.2d at 85. The Court in *Blackmore Partners*, however, concluded, even in the absence of factual allegations that supported an inference of interest or lack of independence by the directors, that "the allegation that the Defendant Directors approved a sale of substantially all of [the company's] assets and a resultant distribution of proceeds that went exclusively to the company's creditors raises a reasonable inference of disloyalty or intentional misconduct." *Id.* at 86. Here, in contrast, there is an allegation that a majority of the board was interested in the decision to pursue the transaction; accordingly, the Court need not conclude that the decision to approve the transaction, of itself, raises "a reasonable inference of disloyalty or intentional misconduct."

the merger. Given this reasonable inference, plaintiff can avoid dismissal if the Complaint contains well-pleaded facts that demonstrate that the director defendants were interested or lacked independence with respect to this decision.

1. The Director Defendants' Approval of the Merger

Plaintiff has alleged facts that support a reasonable inference that Scanlan, Stone, Gandhi, and Prang, the four board designees of preferred stockholders, were interested in the decision to pursue the merger with SDL, which had the effect of triggering the large liquidation preference of the preferred stockholders and resulted in no consideration to the common stockholders for their common shares. Each of these four directors was designated to the Trados board by a holder of a significant number of preferred shares. While this, alone, may not be enough to rebut the presumption of the business judgment rule,[43] plaintiff has alleged more. Plaintiff has alleged that Scanlan, Stone, Gandhi, and Prang each had an ownership or employment relationship with an entity that owned Trados preferred stock.

[43] *See Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 65 (Del. 1989) (stating that a director's representation of one of the corporations largest shareholders "alone did not make him an interested director."). *But see Goldman v. Pogo.com, Inc.*, 2002 WL 1358760, at *3 (Del. Ch. June 14, 2002) ("Because Khosla and Wu were the representatives of shareholders which, in their institutional capacities, are both alleged to have had a direct financial interest in this transaction, a reasonable doubt is raised as to Khosla and Wu's disinterestedness in having voted to approve the First Bridge Loan."). Defendants contend that *Goldman* is distinguishable because "the 'interest' in *Goldman* was far greater and obviously distinct in nature from simply being corporate designees as Christen attempts to posit." Defs.' Reply Br. 13-14. Given the inferences the Court must draw at this stage, it is my inclination that *Goldman* would have some persuasive value in this case. I need not rely on such inclination, however, because plaintiff does not rely merely on the allegation that Scanlan, Stone, Gandhi, and Prang were designees of the preferred. Rather, plaintiff alleges that each of these directors had additional significant relationships to preferred stockholders.

Scanlan was a partner in Wachovia; Stone was a director, employee and part owner of Hg; Gandhi was a partner in several entities referred to as Sequoia; and Prang owned Mentor Capital. Plaintiff further alleges that each of these directors was dependent on the preferred stockholders for their livelihood.[44] As detailed above, each of these entities owned a significant number of Trados' preferred shares, and together these entities owned approximately 51% of Trados' outstanding preferred stock. The allegations of the ownership and other relationships of each of Scanlan, Stone, Gandhi, and Prang to preferred stockholders, combined with the fact that each was a board designee of one of these entities, is sufficient, under the plaintiff-friendly pleading standard on a motion to dismiss, to rebut the business judgment presumption with respect to the decision to approve the merger with SDL.[45]

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[44] Compl. ¶ 79.

[45] *See Orman*, 794 A.2d at 30-31 ("Because director Solomon's principal occupation is that of 'Chairman of Peter J. Solomon Company Limited and Peter J. Solomon Securities Company Limited,' it is reasonable to assume that director Solomon would personally benefit from the $3.3 million *his* company would receive if the challenged transaction closed. I think it would be naïve to say, as a matter of law, that $3.3 million is immaterial. In my opinion, therefore, it is reasonable to infer that director Solomon suffered a disabling interest when considering how to cast his vote in connection with the challenged merger when the Board's decision on that matter could determine whether or not his firm would receive $3.3 million.") (footnote omitted). Defendants attempt to distinguish *Orman* by arguing that, unlike the fees earned by the director's company in *Orman*, the only consideration received by the preferred stockholders was consideration for their shares. Defendants cite *In re Ply Gem Indus., Inc. S'holders Litig.*, 2001 WL 755133, at *9 (Del. Ch. June 26, 2001) for the proposition that directors were not interested where there was no allegation that they "obtained any improper benefit whatsoever from the merger other than from their entitlement, as shareholders, to receive the merger consideration." As explained above, however, the preferred stockholders were not "entitled" to a transaction that would trigger their liquidation preference. Under at least one reasonable inference that can be drawn from the Complaint, the interests of the common and preferred stockholders diverged on that very issue. Indeed, those divergent interests are what led to the present dispute. Accordingly, *In re Anderson, Clayton S'holders Litig.*, 519 A.2d 680 (Del. Ch. 1986), also does

At oral argument, defendants relied on *Dubroff v. Wren Holdings, LLC*[46] for support of the argument that plaintiff had failed to state a claim because he had not alleged that the preferred stockholders were acting in concert or had otherwise formed a controlling group. The discussion of a "control group" in *Wren Holdings* was in connection with the general rule that "equity dilution" claims are derivative, rather than direct. As explained in *Wren Holdings*, there is an exception to this general rule "where a controlling shareholder causes the corporate entity to issue more equity to the controlling shareholder at the expense of the minority shareholders."[47] The emphasis on a control group in *Wren Holdings* arose from the plaintiffs' attempt to establish that certain of the defendants had collectively formed a controlling shareholder group so that plaintiffs would be able to bring a direct claim for the alleged equity dilution.[48] Here, in contrast, there is no need for

not counsel in favor of dismissal here. In *Anderson, Clayton* the Court held that directors "affiliated" with certain trusts would not be considered interested for purposes of the motion for preliminary injunction because the trusts only had an interest as shareholders in the Company and thus were not interested "in a transaction that will treat all shareholders equally." *Id.* at 687. Unlike in *Anderson, Clayton*, the Complaint in this case raises a reasonable inference that the interest of the common and preferred stockholders diverged with respect to the decision to enter into a transaction that triggered the liquidation preference of the preferred and resulted in no consideration to the common stockholders. It is this decision that the four designees of preferred stockholders were allegedly interested in.

[46] 2009 WL 1478697 (Del. Ch. May 22, 2009).

[47] *Id.* at *3.

[48] *Id.* at *3-5.

plaintiff to allege that there was a controlling shareholder or control group in order to establish that individual director defendants were interested.[49]

Defendants also rely on *Orban v. Field*,[50] but that decision does not counsel in favor of dismissal at this stage of the litigation. In *Orban*, the Court was evaluating whether a board breached its duties where it "deploy[ed] corporate power against its own shareholders" by "eliminating the leverage of the common stockholders by diluting their ownership interest below 10%" in order to prevent the common stockholder from using his ability to block a transaction to extract value for his shares.[51] The Court, in deciding to grant summary judgment in favor of defendants, asked whether defendants had met their burden "to show that their conduct was taken in good faith pursuit of valid ends and was reasonable in the circumstances."[52] Although this inquiry was "inevitably one that must be applied in the rich particularity of context," the Court was still able to conclude, based on the evidence in the record, that the plaintiff's "threat to impede the realization of th[e] transaction by the corporation was thwarted by legally permissible action that was measured and appropriate in the circumstances."[53] In making this

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[49] While it is true that an individual stockholder that is not a controlling stockholder can generally vote in its individual interest, the same cannot be said of directors designated to the board by such a stockholder.
[50] 1997 WL 153831 (Del. Ch. Apr. 1, 1997).
[51] *Id.* at *8.
[52] *Id.*
[53] *Id.* at *9.

determination, the Court assumed that the business judgment rule did not apply to the challenged actions.[54]

Here, in contrast, the issue on the motion to dismiss is whether plaintiff has rebutted the presumption of the business judgment rule. Unlike on a motion for summary judgment, I must accept the well-pleaded factual allegations in the Complaint as true. As explained above, those allegations, with the benefit of reasonable inferences, are sufficient, at this stage, to rebut the presumption of the business judgment rule. Unlike in *Orban*, I am unable, at this stage, to make determinations based on the record, such as that the board acted "both in good faith and reasonably."[55] Those determinations must wait for another day.[56]

Plaintiff has alleged facts that support a reasonable inference that a majority of the board was interested or lacked independence with respect to the decision to approve the merger. Accordingly, plaintiff has alleged sufficient facts to survive defendants' motion to dismiss the fiduciary duty claims based on the board's decision to approve the merger.[57]

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[54] *Id.* at *8.

[55] *Id.*

[56] Plaintiff is not entitled to relief merely by rebutting the presumption of the business judgment rule; rather, even if the plaintiff ultimately rebuts the presumption of the rule, the burden shifts to the director defendants to demonstrate the entire fairness of the transaction. *Cede*, 634 A.2d at 361.

[57] Because, at this stage, plaintiff has rebutted the business judgment presumption for a majority of the board, I need not reach plaintiff's allegations as to the remaining director defendants.

2. The Alleged Revenue Shifting

Count I of the Complaint asserts a claim that Campbell and Hummel breached their duty of loyalty to the common stockholders by agreeing "to manipulate Trados' ordinary business practices to benefit SDL by artificially increasing its post-merger revenue."[58] Plaintiff's theory of liability based on the alleged revenue shifting requires inferences that the Court is not required to make, even under the plaintiff-friendly standard on a motion to dismiss.[59] Accordingly, I grant defendants' motion to dismiss as to those claims.

Plaintiff alleges that Campbell, Budge, and Hummel agreed to make certain changes that resulted in revenue being delayed or "shifted" until after the close of the merger. Plaintiff alleges that this action "served no proper purpose for Trados."[60] Plaintiff fails, however, to specify what accounting rule or other requirement was violated by these actions or how the actions would directly cause harm to Trados. Instead, plaintiff contends that the revenue shifting caused the price of SDL stock to increase after the merger, and that any such increase would benefit SDL and holders of SDL stock. Plaintiff further contends that any benefit to SDL stockholders would also benefit Trados managers who received SDL stock as a result of the merger, including Campbell and Hummel. Plaintiff's theory,

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[58] Pl.'s Answering Br. 12.
[59] *Malpiede*, 780 A.2d at 1083 ("Of course, the trial court is not required to accept every strained interpretation of the allegations proposed by the plaintiff . . . .").
[60] Compl. ¶ 66.

however, is still not complete, as it does not yet connect the alleged revenue shifting to any harm to Trados or the common stockholders, or any breach of duty by any defendants. In an attempt to make such a connection, plaintiff alleges that the alleged revenue manipulation resulted in a breach of duty because the increase in the price of SDL stock gave Campbell and Hummel an improper incentive to approve the merger because they would own SDL stock after the merger.

It appears that plaintiff's theory is that Campbell and Hummel wrongfully agreed with the SDL Defendants that Campbell and Hummel would defer certain revenue until after the close, and that this agreement was wrongful because of the possibility that a higher SDL stock price would provide a material benefit to Campbell and Hummel that would wrongfully give them an incentive to approve the merger. Thus, plaintiff alleges that Campbell and Hummel breached their fiduciary duties by agreeing to give themselves an improper incentive to approve the merger. Even at this plaintiff-friendly stage, I am not required to make the inferences necessary to complete this theory of liability. Moreover, plaintiff has not alleged facts that reasonably suggest than any benefit to Campbell and Hummel as a result of the increase in SDL's stock price caused by the alleged revenue shifting would be material to them.[61] Accordingly, plaintiff has failed to

[61] Indeed, there are no factual allegations in the Complaint that suggest that the alleged revenue shifting would result in anything more than a very small increase in the price of SDL stock, at most.

state a claim based on the theory that Campbell and Hummel breached their fiduciary duty by allegedly agreeing to defer revenue.

D. Aiding and Abetting

Count II of the Complaint alleges that the SDL Defendants aided and abetted a breach of fiduciary duty "[b]y conspiring with Messrs. Campbell and Hummel to improperly shift Trados' revenue to SDL."[62] As explained above, the Complaint fails to state a claim for breach of duty based on the alleged revenue deferral or based on an agreement to defer revenue. Accordingly, the Complaint fails to state a claim that the SDL defendants aided and abetted such a breach.[63]

III. CONCLUSION

For the reasons set forth above, defendants' motion to dismiss is granted in part and denied in part. The motion to dismiss is denied with respect to the claim in Count I for breach of fiduciary duty arising out of the board's approval of the merger. The motion to dismiss is granted with respect to the claims based on the alleged revenue shifting. Accordingly, the claim in Count I for breach of fiduciary duty based on the alleged revenue shifting is dismissed. Count II's claim for aiding and abetting is dismissed in its entirety.

IT IS SO ORDERED.

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[62] Compl. ¶ 111.

[63] *See Globis Partners, L.P. v. Plumtree Software, Inc.*, 2007 WL 4292024, at *15 (Del. Ch. Nov. 30, 2007).