IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

GENERAL VIDEO CORPORATION, a Delaware corporation, and AUDEO LLC, a Delaware limited liability company,	)	
Plaintiffs,	)	
v.	)	C.A. No. 1922-VCL
EMERY KERTESZ, DANIEL R. SOLIN, PRO ACOUSTICS, LLP, a Delaware limited liability partnership, and PRO ACOUSTICS, LTD., a Delaware corporation,	)	
Defendants.	)	

MEMORANDUM OPINION AND ORDER

Submitted: August 25, 2008
Decided: December 17, 2008

J. Travis Laster, Esquire, Matthew F. Davis, Esquire, ABRAMS & LASTER, LLP, Wilmington, Delaware, *Attorneys for the Plaintiffs.*

Peter J. Walsh, Jr., Esquire, POTTER ANDERSON & CORROON, LLP, Wilmington, Delaware, *Attorneys for the Defendants.*

LAMB, Vice Chancellor.

Two men engaged over a period of years in a business venture that was profitable for a time but ended in insolvency and disagreement. One of them (who was the minority owner) finally quit in order to start a similar venture at a far distant location. Several years later, the majority owner, and the insolvent entity began a series of lawsuits, claiming rights in the new venture and breach of a number of alleged agreements. Because the claims raised in this action presented factual issues that could not be resolved short, the court was required to try this case for three full days.

In this post-trial opinion, the court finds that the plaintiffs' claims factually and legally baseless and enters judgment in favor of the defendants.

I.

A. The Parties

Plaintiff General Video Corporation ("GVC") is an insolvent Delaware corporation, formed on October 7, 1991. GVC's charter was voided for failure to pay franchise taxes in 2002, and revived by the filing of a Certificate of Renewal on July 8, 2005, apparently in order to pursue suit on these claims.

Plaintiff Audeo, LLC is an insolvent Delaware limited liability company, originally formed on September 11, 2002 by Justin Korn, apparently as a means to pursue what remained of GVC's defunct business without interference by GVC's creditors. Audeo's charter had likewise been rendered void, but was revived by the

filing of a Certificate of Revival on July 8, 2005, apparently in order to pursue suit on these claims.

Justin Korn, although not a party, is the controlling stockholder of GVC and its sole remaining director, as well as the sole member and manager of Audeo. He has been involved as either a party or controlling stockholder of a party in 75 legal proceedings.[1]

Defendant Emery Kertesz is a resident of Harker Heights, Texas. He is an electrical engineer, and a stockholder and former director and officer of GVC, which was formed by Korn in order to enter the video and audio equipment business with Kertesz. Kertesz is a principal of Pro Acoustics, LLP and Pro Acoustics, Ltd.

Defendant Daniel Solin is a resident of Bonita Springs, Florida, and is a licensed attorney specializing in securities arbitrations. He is also a Senior Vice President of Index Fund Advisors, and has authored a number of books on investing. Solin formerly represented GVC in a commercial arbitration, and is a principal of Pro Acoustics, LLP and Pro Acoustics, Ltd.

Defendant Pro Acoustics, LLP is a Delaware limited liability partnership, engaged in audio equipment sales over the internet. It is largely a Kertesz family-

[1] JX 292.

run business managed out of Harker Heights, Texas. Defendant Pro Acoustics, Ltd. is a Delaware corporation and the general partner of Pro Acoustics, LLP.

B. Facts

The fact history surrounding the present controversy is, unfortunately, lengthy and tortuous. It begins in the mid-1980s. At that time Korn owned and operated Videobox Networks, Inc., a business involving the sale and distribution of laser video jukeboxes, and Kertesz was employed by LA East, a Lansdale, Pennsylvania based business that sold and installed video and entertainment systems. LA East distributed and installed video jukeboxes from Videobox. As a technician for LA East, Kertesz became intimately familiar with the workings of the Videobox laser jukebox product. Some time in 1988, Videobox was having technical difficulties with its product and ultimately engaged Kertesz (via LA East) as a consultant.

In 1990, while employed by LA East, Kertesz developed the design for a ceiling speaker system providing greater omnidirectional coverage than existing designs (the "SD Speaker"). An attorney retained by and representing LA East, submitted a patent application for the SD Speaker, and a patent was issued in 1992. The patent identified Kertesz as the inventor and that attorney as the addressee "for fee purposes."[2]

[2] JX 239.

1. The 1991 Letter Agreement And The Formation Of GVC

In 1991, with the Videobox business winding down, Korn was looking for a new business venture. At the same time, Kertesz was considering leaving LA East to start a business. After some discussion, the two men agreed to go into business together, focusing on the sale and distribution of "video wall" displays, the same types of products both men were familiar with from Videobox installations. Korn had his attorney draft, and both men signed, a letter agreement dated September 24, 1991 (the "1991 Letter Agreement"), in which they agreed to enter into a "proposed venture."[3] The 1991 Letter Agreement called for the creation of a Delaware corporation, to be owned 65% by Korn, and 30% by Kertesz.[4] Korn was to provide a cash investment pursuant to a referenced "break-even analysis."[5] Kertesz was to provide the technical expertise and run the business day-to-day. Korn claims the parties "lived by this agreement."[6]

Nevertheless, key aspects of this agreement were never fulfilled. Paragraph 3 of the agreement obligates the parties to enter into an employment agreement between the newly formed corporation and Kertesz, providing for a salary of $50,000 per year and health benefits; the agreement also obligates the parties to

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[3] JX 1.
[4] The remaining 5% was designated for employee ownership. Korn and Kertesz later agreed to split the 5% interest originally designated for employees pro rata with their existing ownership stakes, such that their resulting respective ownership interests became 68.42% and 31.58%.
[5] JX 1 ¶ 2. The referenced analysis is not attached and not in the record.
[6] Trial. Tr. vol. 1, 13.

enter into a stockholder agreement containing provisions typically found in stockholder agreements of close corporations. Neither of these follow-on agreements were ever prepared or executed, and Kertesz, for the duration of his employment at GVC, remained an at-will employee. Similarly, although paragraph 3 of the 1991 Letter Agreement states that "Kertesz and all future employees of the [new corporation] shall sign a confidentiality/non-compete agreement in the same form executed by Korn, VNI, LA East and Kertesz dated September 16, 1988,"[7] it appears that Kertesz never signed any such non-compete agreement. Paragraph 7 of the 1991 Letter Agreement also contains a provision purporting to grant a 25-year non-exclusive license to distribute the SD Speaker system to the new corporation in exchange for a 7.5% royalty on net revenues from the sale of the SD Speaker. The same paragraph also contemplates the later grant of an exclusive 99-year license to the new corporation to distribute the SD Speaker system should the corporation engage an attorney to represent Kertesz in any dispute with LA East over the rights to the SD Speaker patent. GVC ultimately did engage an attorney to represent Kertesz in an arbitration with LA East over the rights to the SD Speaker patent, but no agreement implementing the 99-year exclusive license was signed. It was, in fact, 10 years later, after GVC was already

[7] JX 1 ¶ 3. A copy of the September 16, 1998 Videobox non-compete agreement was attached as Exhibit D.

failing, that GVC first entered into a license agreement with Kertesz with respect to the SD Speaker system.

In November 1992, GVC, by unanimous written consent of the directors of the corporation, "ratified, confirmed, and approved in all respects" the 1991 Letter Agreement.[8] Sometime in the mid-1990s, GVC acquired, subject to several mortgages, a 13-acre parcel on which its facility was located in Quakertown, Pennsylvania ("GVC Plaza"). From its beginning, GVC was primarily a video products business, deriving only a very small portion of its income from sales of the SD Speakers. At no point did GVC engage in an internet sales business.

2. Management Of GVC

Pursuant to the 1991 Letter Agreement, Korn and Kertesz agreed to serve as the initial directors of GVC. Kertesz's responsibilities, as President, included the day-to-day management of GVC's operations, which he ran from the offices and warehouse at GVC Plaza. Korn and Kertesz disagree as to the degree of autonomy Kertesz enjoyed in operating GVC. Korn claims that as Chairman and CEO he was involved in only the most important management decisions, while Kertesz, supported by the testimony of long-time GVC employee Margaret Baltrus, testified that Korn made all of the financial decisions and that he had to clear anything he did with Korn. Despite Korn's control over the affairs of GVC, he rarely visited

[8] JX 7.

the company's facilities at GVC Plaza and had little understanding of the daily operations of the business. Nevertheless, once the business was established, and despite no provision for such in the 1991 Letter Agreement, Korn received a salary from GVC commensurate to Kertesz's salary, and caused GVC to pay his health insurance and to reimburse him for claimed business expenses, including an automobile.

Korn also claims that he loaned more than $2 million to GVC (including accrued interest) during the course of the business. He was never able to substantiate this claim. When asked at trial on cross-examination whether he had put into evidence any wire transfers or checks evidencing the money he alleges was loaned to the company, Korn answered: "Except for, I think, a few checks, no."[9]

3. The Purported 1995 Non-Compete Agreement

In this litigation, Korn produced a facsimile copy of what he claims is a non-compete agreement with GVC signed by Kertesz in 1995 (the "1995 Non-Compete Agreement"). Korn was unable to produce an original of the document, and his testimony about the origin of the document is highly suspect. According to Korn, he asked Kertesz to sign the agreement (which he claims GVC required of every

[9] Trial Tr. vol. 1, 195.

employee and officer[10]) in May 1995, in anticipation of GVC developing a new video projection product (which never came to fruition). Korn testified that at his request, Kertesz printed out this form agreement on GVC's computer in Pennsylvania, signed it, and then faxed the signed copy to him in New York. Korn testified that he countersigned the faxed copy on May 25, 1995, and faxed the countersigned document back to Kertesz. He claims he later delivered the original to Kertesz when he next visited GVC Plaza. Notwithstanding the apparent importance Korn attached to this document, he testified that he left the original signed copies of the non-compete agreement in the possession of the party against whom the agreement would be enforced.

Kertesz flatly denies ever having signed such an agreement. In support of his position, Kertesz points out that he had expressed serious concerns about his employment with GVC in an email to Korn a month earlier, leaving him indisposed to enter into a non-compete with GVC. In this, as in other contested factual matters, the court found Kertesz's testimony to be forthright and believable.[11]

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[10] On rebuttal, Korn testified that it was GVC's policy that *all* employees and executives sign non-compete agreements. When asked by the court whether he had signed a non-compete agreement, Korn admitted he had not. According to Korn, he had "set that policy to protect myself, frankly . . . ." Trial Tr. vol. 3, 811.

[11] Kertesz's denial was supported at trial by testimony given by Solin. Solin testified at trial that when he asked Kertesz (prior to entering into the Pro Acoustics business) whether he had signed any kind of non-compete agreement that would restrict his ability to enter into the contemplated business, Kertesz told him "I never signed one. Justin wanted me to sign one, but I always made

Considering all the foregoing evidence, and the suspicious history of the document, the court concludes that Korn's version of events is a fabrication, and that the 1995 Non-Compete Agreement is therefore not authentic. The document did not surface until July 2007, almost two years after the litigation began. When the defendants subpoenaed documents in the earlier-filed New York action, Korn's counsel was unable to produce a copy. Korn insists that the document was provided to his New York counsel, but she was unable to produce it because she had "her computer stolen."[12]

4. The Patent For The SD Speaker System Expires

In 1996, unbeknownst to Kertesz or Korn, the patent on the SD Speaker expired for failure to pay the maintenance fee. The lawyer for Kertesz's former employer, LA East, who handled the application, was unsure whether the U.S. Patent and Trademark Office had sent a notice that the fee was due. Because he was listed on the patent as the addressee for fee purposes, the Patent and Trademark Office would have sent such notice to him. That lawyer also did not recall receiving any notice that the patent had lapsed, though it was his practice to send such notice, upon receipt, to the client (which would have been LA East in

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it clear that I would not sign a covenant not to compete, because if I did and left, then all I can do is be an engineer. What would I do for 18 months? Not like I have a big safety net." Trial Tr. vol. 3, 782.

[12] Trial Tr. vol. 1, 210. The court notes the troubling frequency with which Korn attributed the his inability to produce important documents to data loss.

this case). In any event, he is certain he never advised Kertesz of the expiration of the patent. The court is convinced that given his strong feelings about the patent's value,[13] Kertesz would have paid the fee if he had ever received notice of it.

5. The Toshiba Distribution Agreement, The Bank Loans, And The Indemnity Agreement

In early 1997, with the video wall business healthy and growing, GVC entered into a preliminary agreement (later formalized in September 1997) with Toshiba America Consumer Products, Inc. to act as a distributor of Toshiba video wall products. On the basis of its understanding that its contract granted it sole and exclusive distributorship for Toshiba video wall displays in North America,[14] GVC expanded its sales force and dramatically increased its inventory.

To obtain capital for expansion, GVC turned to Lafayette Bank. Korn and Kertesz met with a vice-president of the bank to secure a new line of credit for over $1 million. At this meeting, they were told that they would both have to sign personal guarantees in order to obtain the loan for GVC. Concerned, Kertesz pulled Korn aside and explained that he was in no position to sign a personal guarantee for that amount of money. Korn, angry that Kertesz might jeopardize the loan, warned Kertesz not to make a big deal of it at the meeting. Kertesz

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[13] Kertesz characterized the patent as the "only commercially valuable thing [he had] in the world that is solely [his]." JX 27.

[14] This understanding later proved to be mistaken.

insisted that he did not wish to enter into such a guarantee, but relented after Korn repeatedly assured him that he would "back him up"[15]—that is, indemnify him—if Lafayette ever looked to Kertesz for satisfaction of his guarantee. On that basis, Kertesz signed the guarantees on May 8, 1998. Kertesz made repeated requests for a written indemnity agreement. Korn provided Kertesz with an agreement on November 12, 1998.

6. The Purported Loans From GVC To Kertesz

By 1998, GVC's video wall business was going well. Kertesz, whose salary for most of his tenure to that point at GVC had been only $50,000,[16] asked the corporation for an advance against his share of future distributions of profits in order to fund the construction of a house. The advance was agreed to and was memorialized in a resolution of the board of directors on April 26, 1999. The resolution provided that GVC "advance against future distributions of profits to Emery Kertesz, as a stockholder of the Company, an aggregate amount of $65,000 as follows: (a) $22,800 advanced on or about July 14, 1998, (b) $10,000 advanced on or about April 19, 1999 and (c) $32,200 advanced on or before May 31, 1999 on the date mutually agreed to by Emery Kertesz and the Board of Directors . . . ."[17]

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[15] *See* Trial Tr. vol. 2, 458-59; *see also* Trial Tr. vol. 3, 646.
[16] Kertesz's salary had remained at $50,000 per year until late in 1997, when it increased to $75,000.
[17] JX 24 at 2.

Korn now characterizes these advances as loans. At the time the advances were made, it was never suggested that the advances constituted loans or that they would have to be repaid. The resolution authorizing the advancement makes no mention of a rate of interest or any repayment requirement, and no promissory note was every given by Kertesz to GVC evidencing any such obligation. Notably, when Korn made loans to GVC, it was his practice to obtain a promissory note from the corporation evidencing the indebtedness.

7. GVC's Business And Kertesz's Health Both Take Negative Turns

Sometime in 1998, reports began to filter in to GVC from its customers and clients that Toshiba was approaching them directly to sell its video wall products at prices below those of GVC. GVC believed it had an exclusive dealer agreement with Toshiba. Although Toshiba repeatedly denied the activity, the rumors were eventually confirmed that Toshiba was shutting down its U.S. video wall operations and dumping its inventory. As a result of Toshiba's direct underselling of video wall equipment, GVC's business began to spiral downward.

GVC had amassed somewhere between $2.5 million and $3 million worth of Toshiba video wall inventory. Toshiba was now selling the exact same equipment into the market direct to dealers and end-users at prices between 20% and 30% of GVC's cost. Toshiba also hired away a key sales executive from GVC (in violation of that executive's non-compete agreement with GVC), in order to obtain

GVC's existing relationships with video wall dealers. Over the course of the next several years, GVC posted net losses of $976,765 (1999), $641,856 (2000), $624,000 (2001), and $707,092 (2002).[18]

In June 1999, Kertesz fell ill and, in April 2000, was diagnosed with Wegener's granulomatosis, a life-threatening chronic auto-immune disease. Most notably, this disease can be exacerbated by stress, and Kertesz and his wife were concerned that the stressful circumstances at GVC would aggravate his illness. In 2000, with Korn's reluctant approval and Kertesz's commitment to be at the company offices in Pennsylvania seven to ten days a month, Kertesz and his family moved to Harker Heights, Texas where his wife's family lived. At around this same time, because of GVC's worsening financial condition, Kertesz's salary was reduced to $24,000 a year.

8. The Second License Agreement

At this time, Kertesz began to focus on protecting his rights in the SD Speaker patent in the event that GVC was to go out of business or enter bankruptcy. If either were to occur, Kertesz feared he would lose the modest royalties he received from SD Speaker sales. Combined with the loss of his salary and health benefits from GVC, Kertesz was concerned about financial ruin, particularly in light of his expected medical expenses. Accordingly, Kertesz asked

[18] JX 37, 74, 82.

Korn to agree to revise the licensing terms by which GVC distributed the SD Speaker system, so as to protect his royalty stream in the event that GVC failed. Korn assented, and retained Simon Cices, an attorney at Kaye Scholer in New York who had represented Korn and occasionally GVC in the past, to draft a new licensing agreement. With Korn's input and at his direction, Cices prepared a letter agreement (the "Second License Agreement") among Korn, GVC, and Kertesz, which, according to Korn, was intended to amend whatever license may have been granted by the 1991 Letter Agreement. The Second License Agreement once again purported to grant a 99-year exclusive license to GVC to distribute the SD Speaker system, and provided for a 7.5% royalty on GVC's net revenues from the sale of the SD Speaker system. The document also contained a representation and warranty by Kertesz that he was the owner of the SD Speaker patent and that no one other than GVC had the right to distribute the speaker system. Most important for purposes of this litigation, the document also contains the following provision:

> If (a) GVC ceases to actively operate as a distributor of electronic products, or (b) [Korn], [Korn]'s nominee and/or members of [Korn]'s family cease to own directly or indirectly, at least 50% of the ownership interests in GVC, then [Kertesz] may enter into a license agreement substantially similar to this letter with a corporation, limited liability company or other legal entity designated by [Korn] (provided that 70% or more of the ownership interests in the new license [sic] are owned directly or indirectly by [Korn] and/or a member of his family and [Kertesz] is offered ownership of 30% of

> the ownership interests in the new licensee for an amount not to exceed $100), in which event immediately after the execution of such new license agreement, this letter agreement shall terminate.[19]

Kertesz executed the agreement in January 2001, at which time both he and Korn (mistakenly) believed Kertesz still held a valid patent on the SD Speaker system.[20] Although signed in January 2001, this agreement is dated on its face "as of November 1, 1991."[21] Korn testified this was done in order to obfuscate the effect of the agreement upon cursory examination by GVC's creditors.

9. The Toshiba Arbitration

By 2000, Korn and Kertesz saw only one path remaining to save GVC: suit (by way of arbitration, as required by the distributor agreement) against Toshiba for breach of the distribution agreement. To represent GVC, Korn turned to Jeffrey Weisenfeld, a New York sole practitioner who had represented Korn in the past. Weisenfeld, who had little experience in commercial arbitration, suggested they engage another lawyer he was familiar with, Daniel Solin, an attorney more experienced in arbitration proceedings.

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[19] JX 3, ¶ 4.

[20] Kertesz did not learn that the patent had expired until 2005, when his Texas counsel (Stuart Smith) placed him in contact with a Baylor professor (David Henry) who looked up the patent in Kertesz's presence and informed him that the patent was no longer in force because it had expired. Korn did not learn of the expiration of the patent until the issue was raised in the pleadings during the Texas litigation.

[21] This sort of back-dating of agreements appears to be a troublingly common practice by Korn. See, for example, the discussion *infra* of the Audeo Resolution dated September 12, 2002, but actually prepared in February 2003, purporting to set the conditions under which Korn would convey a 30% interest in Audeo to Kertesz.

Solin knew nothing about GVC, Korn, or Kertesz. At Weisenfeld's request, Solin agreed to meet with Weisenfeld, Korn, and Cices at Cices' Manhattan office to listen to a discussion of the case. Immediately after that meeting, Solin told Weisenfeld that he was not interested. Later on, Solin explained to Weisenfeld that he was uninterested in accepting the representation because he had "an unsettling feeling about Mr. Korn."[22]

Weisenfeld persisted and offered Solin an arrangement in which Weisenfeld would be responsible for all of the direct contact with Korn. Accordingly, Solin agreed to be retained by Weisenfeld, on GVC's behalf, to assist him in the representation of GVC against Toshiba. The arrangement included a $30,000 retainer to be divided between the two attorneys, plus a contingency fee based on the outcome.

On April 4, 2001, GVC filed a demand for arbitration against Toshiba. Weisenfeld and Solin set out to prepare the case in anticipation of the arbitration hearings. As the time for the hearings approached, it became apparent to all involved that Solin was the best-suited of the two attorneys to act as lead counsel, and at the urging of Korn and Kertesz, Solin agreed to take on that additional responsibility. Weisenfeld testified that Solin worked very hard on the matter, was

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[22] Trial Tr. vol. 3, 659.

effective at the hearings, and delivered an excellent summation. Solin estimated that he spent over a thousand hours preparing and arbitrating the matter.

Although the plaintiffs claim that Solin gained knowledge of GVC's or Audeo's[23] proprietary information about its audio and speaker business in the course of the arbitration, and used that information to his own advantage to the detriment of GVC and Audeo, the Toshiba matter was entirely unrelated to speakers or audio equipment. Also, despite the plaintiffs' claims to the contrary, there is no reason to believe that Solin had any knowledge, before the commencement of this litigation and the earlier actions in New York and Texas, of the 1991 Letter Agreement or the Second License Agreement. Indeed, Weisenfeld, who was co-counsel with Solin in the Toshiba matter, testified at trial that, as of the date of his deposition in this action, he had never heard of either the SD Speaker or Audeo.

On December 12, 2002, the Toshiba arbitration panel issued a "Partial Final Award," essentially denying GVC's claims except as to a minor matter. At this point, GVC had no further hope of paying off its creditors. Any further operation of its business was pointless. GVC lacked sufficient capital to operate, and Korn had no interest in injecting additional capital to benefit GVC's creditors. A request

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[23] It is worth noting that Audeo was not a party to the Toshiba arbitration, was not even formed until the arbitration was virtually over, and was never represented at any time or in any capacity by Solin.

by GVC to modify the award was denied by the panel in late January 2003 and received by GVC and counsel on February 3, 2003. All that remained in the arbitration was for GVC to negotiate a settlement of the minor matter in which it had prevailed.

Shortly after receiving the arbitration panel's decision, Korn asked Weisenfeld whether there was any basis to bring a malpractice claim against Solin, apparently because Solin had refused to employ a tactic which Korn had championed. Weisenfeld replied, "[a]bsolutely not, and I would have to be a witness against you, Justin, if you ever brought such an action."[24]

10. The Creditors Begin To Close In On GVC

On January 5, 2001, nearly two years before the arbitration panel's partial award, Lafayette Bank advised GVC that the scheduled December 31, 2000 payment was in default, but agreed to extend both the line of credit and the quarterly payment to January 31, 2001. On February 16, 2001, the bank agreed to extend the maturity on GVC's line of credit to June 30, 2001.

On or about June 13, 2001, GVC and Lafayette Bank entered into a "Collateral Pledge of Proceeds" agreement, whereby GVC pledged the net

[24] Trial Tr. vol. 2, 428. On his redirect testimony, before Weisenfeld took the stand, Korn testified it was Kertesz's idea to sue Solin, prefacing his remarks with, "[i]t's going to be hard for anybody to accept . . . ." *Id.* at 317. Indeed, in light of Weisenfeld's testimony, Korn's testimony in this regard (as in others) is hard to accept.

proceeds of the Toshiba arbitration (after subtracting litigation and attorneys' costs) to Lafayette Bank as additional collateral on its debt. On August 1, 2001, the bank declared GVC in default on its loans and expressed its intent to pursue its remedies, including enforcement of the personal guarantees of Korn and Kertesz. On August 31, 2001, the bank confessed judgment against Korn on his personal guarantee in the amount of $831,461.59 and initiated litigation against him in New York seeking to enforce its judgment. The bank likewise confessed judgment against Kertesz on his guarantee in the amount of $531,465.59.

By this time, creditors were hounding GVC demanding payment. Baltrus testified that creditors called constantly and frequently appeared at GVC Plaza in person, either in an attempt to collect or to serve papers toward that end. She testified that she was also frequently served by the sheriff with suit papers. After GVC moved Baltrus out of its main offices and into its former service area, conditions became deplorable by her description. The GVC office area's roof leaked, and the space had no climate control, no working restroom facilities, no potable tap water, and was frequently without electricity. On a number of occasions, employees, including Kertesz, could not get prescription medications or were delayed in doing so because GVC was unable to keep up with the premiums on its insurance plan.

As Kertesz and Baltrus were struggling to keep GVC afloat, Korn was focused on perfecting his priority status as a secured creditor of GVC. In August 2001, Korn filed an assumpsit against GVC in Bucks County, Pennsylvania. At about this same time, Korn also notified Kertesz that he would not honor his agreement to indemnify Kertesz against the personal guarantee to Lafayette Bank. Shortly after GVC received notice of a March 29, 2002 sheriff's sale, Korn filed a UCC-1 financing statement in an effort to secure rights in all of GVC's property. On April 15, 2002, with the bank closing in, Korn called his November 30, 1995 promissory note to GVC.

On June 11, 2002, Korn entered into a forbearance agreement with Lafayette Bank. Under that agreement, Lafayette Bank agreed to cancel the sheriff's sale, then scheduled for June 13, 2002, in exchange for a payment by GVC of $150,000 no later than June 12, 2002, a payment of at least $50,000 in real estate taxes then owed by GVC, and the execution of a non-contestability agreement by Korn of his personal guarantee, which would be reduced to $400,000. Shortly thereafter, Korn caused GVC to transfer equipment and property, in apparent violation of the security agreement with the bank, to a warehouse in Allentown, Pennsylvania where it passed into the control of Birddog Capital Corporation, an entity wholly-owned by Korn.

11. The Formation Of Audeo

As GVC's business wound down, Kertesz periodically complained to Korn that GVC's problems were causing the SD Speaker business to suffer, reducing his royalty income. By the spring of 2002, Kertesz suggested forming a new company focused on selling audio products.

In early September 2002, Korn asked Cices to file a Certificate of Formation for Audeo. Cices prepared the Limited Liability Company Agreement of Audeo LLC (the "Audeo LLC Agreement"), designating Korn the sole member and manager of the company. As the sole member, Korn would have complete control over the business and affairs of Audeo and its assets, would be entitled to 100% of its profits and losses, and would be entitled to unilaterally amend or modify the LLC Agreement. Korn capitalized Audeo with $100. Although Korn informed Kertesz of his formation of Audeo, he never told Kertesz of the steps he took to ensure his control of Audeo, nor did he provide Kertesz with a copy of the LLC Agreement. Rather, Kertesz believed that "whatever [he] had in GVC [he] was going to get in Audeo."[25]

Korn also directed Cices to prepare a letter agreement (the "Audeo Letter Agreement") that would condition Kertesz's 30% membership interest

[25] Trial Tr. vol. 2, 474.

contemplated in the Second License Agreement on several added control-related conditions:

> (a) [Korn] will be the managing member of the Company. All decisions relating to the Company (inlcuding, without limitation, whether the Company should acquire or sell any assets, whether the Company needs additional funds and whether the Company should incur debt) will be made solely by [Korn].
>
> (b) [Korn] may admit additional members to the Company provided that their membership interests are diluted on a pro rata basis.[26]
>
> (c) All additional monies required by the Company as determined by [Korn] in [his] sole discretion will be advanced by [Korn] as a loan to the Company.[27]

This draft letter also contemplated a payment by Kertesz of $300 (not $100 as specified in the Second License Agreement) in exchange for his 30% share of Audeo. In other words, Kertesz would provide 75% of the nominal equity capital in the new company, and would be expected to manage the day-to-day operations of the business, and in exchange would receive a 30% share of the profits of the company, which share could be diluted at will by Korn. Korn, on the other hand, would provide 25% of the initial equity capital, would have no involvement in the day-to-day operations of the business, would retain complete management control of the company, and would receive a 70% share of the profits of the company.

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[26] The court notes that under this provision, Korn could, for example, admit his wife to a 50% membership share in the company so long as his and Kertesz's interests were diluted pro rata, in that hypothetical case leaving Kertesz with a 15% interest and giving Korn an effective 85% share. Likewise, Korn could create a new entity, wholly owned by himself, and admit it to membership in like manner.

[27] JX 69.

At trial, Korn tried to explain the variances between the terms of the Second License Agreement and the draft Audeo arrangement by saying that he had made himself the sole member of Audeo initially for convenience, and in order to prevent creditors from becoming suspicious. On cross-examination, Korn was forced to concede that nothing prevented him from making Kertesz a manager or member of Audeo. Similarly, although Korn claims that he faxed the draft Audeo Letter Agreement to Kertesz, Kertesz testified credibly at trial that he never saw the agreement, and there is no record of any such fax. As was the case with the claimed 1995 Non-Compete Agreement, the court finds Korn's testimony in this regard unreliable.

By the end of 2002, GVC was effectively out of business, and was no longer selling audio products or any of its video inventory.[28] Audeo, meanwhile, had begun to sell GVC's leftover inventory of SD Speakers. By January 30, 2003, Kertesz, concerned about Korn's persistent failure to convey to him his expected 30% interest in Audeo, wrote to Korn: "I am not a stockholder, partner or anything with AUDEO. I was hoping we would have something worked out by now, (like you said before) following suit with GVC's set up."[29]

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[28] Korn, in an email to a former employee, stated that no sales of inventory had occurred from before Thanksgiving 2002 through January 19, 2003. JX 99. Korn further stated on January 30, 2003, in an email to Kertesz, that GVC was "effectively dead," and suggested to him that he make GVC's next tax return filing its "last and final return." JX 110.

[29] JX 108.

Korn did not respond to Kertesz's inquiry. Instead, in February 2003, Korn created a document dated September 12, 2002 (the "Audeo Resolution") that purports to memorialize the terms of an agreement between GVC and Audeo and to reflect the terms of Kertesz's admission to Audeo. Several paragraphs of the Audeo Resolution are of interest:

> 1. The Company shall manufacture and distribute certain Super Dispersion speakers and other audio products (the "GVC Speaker Products") on behalf and as agent for GVC, in consideration for which the Company shall receive from GVC:
>   a. After all costs, a net management fee equal to $3,000 per month for six months; and
>   b. All profits, after payment of royalties, from the manufacture, sale and distribution of the GVC Speaker Products for a period of two years.
>
> 2. None of the Company's activities on behalf of or for GVC shall constitute an assignment of GVC's intellectual property or distribution license rights, in part or in whole, to the Company.
>
> 3. The Company hereby appoints Justin Korn as its Chairman and Emery Kertesz as its President.
>
> 4. Before the earlier of the formal launch of its new website or May 5, 2003, the Company will issue to Kertesz a 30% (thirty percent) ownership interest in the Company upon (1) the execution of Kertesz and Korn of an agreement that is in substantial accordance with the terms of the draft letter agreement prepared by Simon Cices, and (2) the execution by Kertesz and Korn of a limited liability company agreement reflecting all of the foregoing.[30]

[30] JX 72.

The legal consequences of paragraphs 1 and 2 above are questionable, and will be discussed further below. To the extent they do anything at all, they clearly constitute a self-dealing transaction with GVC for Korn's benefit, at the expense of GVC, its other stockholders (Kertesz), and, particularly, given the company's insolvent state, its creditors.[31] At trial, Korn testified that no written agreement memorializing this resolution was ever executed between GVC and Audeo, in order to avoid alerting GVC's creditors.

Korn claims he mailed the Audeo Resolution with an original signature to Kertesz around the time it was drafted. Kertesz denies ever having received it or even seeing it before it surfaced in the New York litigation. When pressed on cross-examination as to whether he ever told Kertesz about any of the conditions contained in the Audeo Resolution, Korn testified "I think I did. Maybe not exactly. I can't recall exactly."[32] When asked by the court if any metadata was recovered from his computer that would tend to prove when the Audeo Resolution was actually drafted, Korn replied that the resolution was not recovered on his computer because shortly before he began litigation on the various claims now before this court, the hard drive containing these documents on his computer crashed.

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[31] Because the contemplated relationship between GVC and Audeo confers no benefit whatsoever to GVC, and transfers significant value from GVC (of which Korn owned less than 70%) to Audeo (of which Korn owned 100%), it serves merely to expropriate to Korn value from GVC's creditors and Kertesz.

[32] Trial Tr. vol. 1, 227.

As of March 21, 2003, Audeo's balance sheet showed total equity of $10,101.96, a $2,372.46 net deficit in its checking and savings accounts, and $9.31 of inventory. The Audeo financial statements also show that Audeo suffered a net loss of $12,633.90 in the first quarter of 2003 on sales of approximately $20,000 to $30,000, a performance that if repeated would have rendered Audeo insolvent. Korn testified at trial that he would have been willing to invest over $125,000 (the amount Solin actually invested in the Pro Acoustics business), but he never did so. And, by this time Kertesz and Baltrus had begun to develop a website for Audeo at www.ProAcoustics.com. That effort was shut down shortly after soft-launching because Audeo was unable to pay its web hosting bills. In the brief time the ProAcoustics.com website was up, Audeo never had any web-based sales.

12. Baltrus Resigns And Korn Offers A Partnership Interest To The Exclusion Of Kertesz

On February 28, 2003, Baltrus, who was the last remaining employee of GVC other than Kertesz, resigned effective March 21, 2003. Korn responded on March 11, 2003 by offering Baltrus a 25% interest in an audio business with him, stating that Kertesz would have nothing to do with the business other than a possible consulting role. Korn repeated this offer to Baltrus several times in the following weeks.

13. The Trip To Florida

GVC Plaza was on the verge of being forfeited to the banks. The question arose where to operate the new audio business. Kertesz, who had by then been living in Texas for three years, advocated moving the operations to Texas. Korn adamantly opposed this idea. Instead, Korn urged that the new business operate out of Florida. Kertesz, while preferring to stay in Texas, was willing to entertain the idea, and the two agreed to travel to Florida to look at possible locations.

Korn and Kertesz spent the week of March 10, 2003 looking at properties in and around Naples, Florida. Kertesz quickly realized that the property costs were far higher in Florida than in Texas, and far more than the audio business could sustain. Korn nevertheless remained enthusiastic about Florida. Meanwhile, the two argued about how the small Toshiba settlement would be divided. The two men knew that the settlement would be in the vicinity of $75,000 to $80,000. Kertesz believed that he was entitled to one-third of the proceeds based on his ownership interest in GVC and his major role in the arbitration preparations. Korn disagreed. Eventually, Korn agreed to pay Kertesz $12,500 on a $75,000 recovery, half of the one-third to which Kertesz believed he was entitled. When Kertesz sought assurances from Korn that Audeo would be adequately capitalized, Korn refused to make any commitment.

Kertesz also sought assurances from Korn that he would honor his indemnity agreement. Korn said he had no intention of indemnifying Kertesz. This was the last straw for Kertesz, who realized he could no longer trust Korn and could not continue as his business partner. On the morning of March 15, 2003, Kertesz told Korn that he wanted out, was terminating their business relationship, and was returning to Texas to sell speakers on his own. Korn expressed his dismay and spent the majority of the day trying to convince Kertesz to change his mind. When he failed, Korn insisted on trying to lay out deal points concerning the split. Korn dictated to Kertesz various points he wanted in a separation agreement. Notably absent from Korn's list of demands was any mention of Kertesz's purported obligation to repay any "loans" made to him by GVC. Korn's parting words to Kertesz were that it was appropriate that Kertesz be ruined financially because he had also lost money in their venture.

The night before this meeting, Kertesz had dinner with Solin and his wife at a restaurant in Naples. Kertesz made the initial contact, following up on an open invitation Solin had extended during the course of the arbitration. The discussion centered around Kertesz's poor health and precarious financial situation, as well as the reason he and Korn were in Florida. Kertesz told Solin that he was through with Korn, and was thinking about going back to Texas to run an audio business on his own. Solin advised Kertesz that, given his health situation and need for

medical insurance, he should get a job, preferably with a large company. Solin offered to put Kertesz in touch with a friend in the human resources department at the Home Depot in Atlanta. Kertesz also told Solin he was in danger of losing his house in Texas due to his unpaid mortgage and bills, and conveyed the general dire nature of his financial condition. Solin asked Kertesz how much money he would require to get by while he looked for a job. Kertesz told Solin he would think about it and get back to him.

The next day, Kertesz told Solin that he would need approximately $5,000 while he looked for work. Solin told Kertesz he would think about it, and invited him to meet later for a walk on the beach near his home. Solin met Kertesz at the beach, and after a discussion, Solin gave Kertesz a check for $5,400 and a promissory note to sign. Solin told Kertesz to consider the money a loan, but that "it's not going to hurt us if you don't pay it back."[33]

14. The Attempt To Negotiate An Amicable Split

On March 17, 2003, upon returning from Florida, Kertesz emailed Solin thanking him for dinner in Florida and for his kindness. Solin responded by wishing Kertesz well and asking to be kept posted as to Kertesz's decision process. That same day, Kertesz advised Steve Kinney, a former employee of GVC who

[33] Trial Tr. vol. 3, 675.

was owed money, that "[t]he operations for GVC have thus ceased and the bank is acting to foreclose on its security."[34]

In furtherance of their plan to divide up what was left of GVC, Korn and Kertesz contacted Baltrus to ask for her help with listing the remaining inventory and equipment still housed at GVC Plaza. Although March 21st was Baltrus' last official day of work at GVC, she agreed. Korn and Kertesz agreed to split GVC's SD Speaker inventory, tools, and parts 75% to Korn and 25% to Kertesz.[35] Over the next few days, Kertesz, with Baltrus' assistance, prepared a spreadsheet contemplating the agreed 75/25 split. Included in Kertesz's share was the tooling for the manufacture of the SD Speakers.

15. Kertesz And Solin Go Into Business Together

On or about March 20, 2003, Kertesz sent Solin an email asking him to examine a proposed business plan. Solin felt unqualified to evaluate the plan, and passed it on to his regular accountant and another accountant he was acquainted with for evaluation. At Solin's request, both accountants spoke to Kertesz about the plan. After talking to Kertesz, the accountants told Solin they were skeptical of the viability of the plan.

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[34] JX 137.

[35] Although Kertesz's share of GVC's equity was over 30%, Korn insisted that Kertesz receive only 25% because he blamed the Toshiba loss on Kertesz.

Within a couple of days of sending the plan to Solin, Kertesz asked Solin if he would be interested in the proposed business. Already aware that Kertesz had only recently terminated his relationship with Korn, Solin first asked whether he had ever signed any agreements with Korn or GVC which would prevent him from entering into the audio business. Kertesz assured him that he had not. Solin decided to back Kertesz in the business, telling him on March 24, 2003 that he would invest up to $100,000. Solin testified at trial that the decision was based more on a personal assessment of Kertesz's character than a belief in the business plan.

16. Division Of Assets

On March 24, 2003, Kertesz sent Korn a letter resigning as the President and Manager of GVC and its subsidiaries. Korn denies having received the letter.

On March 26, 2003, Baltrus sent Korn and Kertesz a spreadsheet showing the goods to be shipped to Kertesz in Texas and to Korn's warehouse in Pennsylvania in accordance with the agreed upon 75/25 split. Baltrus had already marked and inventoried the items that were to be sent to each, had them placed on pallets for shipping, and had scheduled Yellow Freight Services to pickup the shipments the next day. When the trucks did not arrive as scheduled, Baltrus called Yellow Freight and learned that Korn had cancelled the shipment. Later that day, Korn arrived and gave instructions that the pallets marked for Kertesz be

unloaded and many of the items repacked and sent to a storage facility (Neu Logistics) under Korn's control. Korn did, however, allow Baltrus to send a few unfinished speaker production parts to Kertesz. Baltrus called Kertesz who, although surprised, told her to do what she was instructed. Korn again offered Baltrus an interest in a partnership with him. Baltrus declined.

Also in late March, Korn put a hold on all of Audeo's bank accounts. When Baltrus told Korn that there were outstanding checks on those accounts, including payroll checks for Kertesz, Korn told her the bank was instructed not to pay them. Korn eventually transferred all of Audeo's remaining funds to his personal account.

Because Korn had initially agreed to send the speaker housing molds ("tooling") to Kertesz as part of their split of the property of GVC, Kertesz asked Baltrus to arrange to pick-up the tooling from Analytics Plastics and send it to him in Texas. Analytics told Baltrus that it needed approximately two weeks to prepare the tooling for shipment. On April 1, 2003, Baltrus took custody of the tooling from Analytics and on April 4, 2003, shipped it to Kertesz in Texas by FedEx. Despite Korn's initial agreement that Kertesz should take the tooling as part of his split, Korn tried to stop this shipment as well. He wrote a letter to Analytics dated March 27, 2003 (which he claims he sent on or soon after that date) instructing Analytics that he was the only person authorized to act on behalf of GVC with

respect to the property. A representative of Analytics testified at deposition that Analytics did not receive Korn's letter until April 3, two days after it had delivered the tooling to Baltrus. Baltrus testified that she was not aware at that time that Korn meant to prevent the shipment of the tooling to Kertesz.

Sometime in early April 2003, Weisenfeld received the Toshiba settlement proceeds of approximately $80,000. On April 8, 2003, Korn accused Kertesz by email of illegally taking the tooling and informed him that the Audeo bank account had been closed. Kertesz replied that Korn's allegations were untrue and offered to work out an amicable agreement, but warned that he could not be strong armed. On April 29, 2003, Korn wrote to Weisenfeld and told him to hold payment of Kertesz's previously agreed to $12,500 share of the Toshiba settlement proceeds until he received further written instructions. Weisenfeld told Korn that, unless an agreement with Kertesz was reached, he would interplead the settlement proceeds with a court. Knowing that the proceeds had been pledged to the bank as collateral, Korn relented, but forced Kertesz to take far less ($5,203) than Korn had originally promised.[36] Korn received almost $69,000 of the Toshiba settlement, as well as all of GVC's remaining video inventory. During all of this negotiation,

[36] The final payment of $9,160 that Kertesz received reflected the $5,203 Toshiba proceeds net of the cost of the shipped GVC inventory, plus various outstanding payroll and expense amounts owed to Kertesz. Kertesz and Korn both understood that Kertesz's share reflected the above offsets and credits. *See* JX 204.

Korn made no mention of any loans he now claims are owed by Kertesz to GVC, nor did he mention any potential non-compete obligations he believed Kertesz to be under.

The next day, Korn wrote to Kertesz and told him he must return the tooling or else make an acceptable offer about the SD Speaker business. Kertesz responded by phone that he felt they already had a deal and that he was not going to return the tooling or make any additional payments.

On the same day he sent the email to Kertesz, Korn sent Kinney an outline of a proposal of a partnership with him in the SD Speaker business. As part of the deal, Korn offered Kinney 30% of the equity in the new business. Kinney declined the offer.

At the time Korn and Kertesz asked Baltrus to do some additional work for them in winding-up the GVC business, they also asked her to take her GVC computer to her home so that she would have it available to her. In late April 2003, Korn asked Baltrus to send him the QuickBooks accounting files from her computer. He then directed her to wipe the hard drive clean of any information so that when the computer was returned to GVC there would be no information on it the sheriff or bank could use to trace assets. When, during discovery, the defendants in this case asked the plaintiffs to produce the accounting files, the

plaintiffs were unable to produce them, claiming the files had been lost after being sent to counsel.

On or about May 6, 2003, GVC, Korn, and Kertesz agreed to a settlement with Lafayette Bank whereby the bank would take title to the GVC real property at GVC Plaza in exchange for a release of GVC's loan obligations and the obligations of Korn and Kertesz under the personal guarantees.

17. Korn Slumbers On His "Rights"

On May 14, 2003, Solin called Weisenfeld to say that he and Kertesz were going into business together. Solin testified that he called Weisenfeld because he knew of Weisenfeld's personal and attorney-client relationship with Korn. He believed that a call to Weisenfeld was the most forthright and transparent way to let Korn know of his business relationship with Kertesz. Solin further testified that if he called Korn directly, he feared Korn would later deny the occurrence of the call if it suited his purposes.

Weisenfeld testified that Solin told him that Kertesz had terminated his relationship with Korn. Solin asked whether he saw any problem with going into business with Kertesz. Weisenfeld responded that he did not see any conflict. In a later conversation with Kertesz, Weisenfeld wished him good luck in the business with Solin.

On May 27, 2003, Kertesz's lawyer, Ariel Berschadsky, wrote to Korn's lawyer, Walter Weir, in an effort to resolve whatever loose ends Kertesz thought remained and to then sever all ties between Kertesz and Korn. The letter advised, among other things, that (1) Kertesz had GVC records and tax information he wished to turn over to Korn; (2) Kertesz had no need for the ProAcoustics.com website or URL and asked what information Korn would like concerning the website; (3) Kertesz had $6,686.62 in customer checks mistakenly mailed to him that he wished to turn over to Korn, along with GVC records and documents relating to the Toshiba arbitration. Lastly, the letter advised that Kertesz "want[ed] nothing from Mr. Korn, other than to have nothing to do with him in the future."[37]

Korn received the letter the same day, and had Weir prepare a response. Weir's response requested accounting and other information already largely available to Korn on GVC's computer, and demanded the return of the checks.[38] Korn's counsel advised that as to the website and URL, a response would be provided under separate cover. No separate letter was ever sent.

Later in the summer of 2003, Korn raised with Weisenfeld the subject of Solin's having gone into business with Kertesz. Weisenfeld related to Korn his telephone conversation with Solin from May. By then fully aware that Kertesz was

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[37] JX 212.
[38] Kertesz returned the checks to Korn.

operating the speaker business with Solin's backing, Korn took no action to either stop Kertesz from selling SD Speakers or to put him on notice that he believed Kertesz to be in violation of his or GVC's rights. Instead, Korn began monitoring the Pro Acoustics business activity. In July 2003, Korn accessed the Pro Acoustics website. For the rest of 2003 and 2004, Korn did nothing. When asked at trial why he did nothing for so long, Korn tried to suggest he was too shocked and surprised by Kertesz's actions to be able to respond to them properly during that nearly two year period.

In February 2005, Korn had his attorney write a letter to Kertesz demanding payment of "certain demand loans" owed to GVC and threatening suit if such "loans" were not repaid.[39] Even then, the attorney's letter was silent as to many of the numerous other claims Korn later raised in litigation.

18. The New York, Texas, And Pennsylvania Actions And The Appearance Of The 1995 Non-Compete Agreement

In May 2005, Korn, GVC, and Audeo sued Kertesz, Solin, and Pro Acoustics in New York state court, alleging various claims relating to the winding-up operations of GVC. The New York complaint generally alleged the conversion of GVC's assets by Kertesz, including misappropriation of the SD Speaker design, but did not seek either injunctive relief or rescissory damages. Notably, this action

[39] JX 228.

made no mention whatsoever of the purported 1995 Non-Compete Agreement. The action was dismissed for lack of personal jurisdiction over the defendants.

In June 2005, Korn filed a second complaint against Kertesz and his wife in New York state court seeking contribution for payments Korn allegedly made to Lafayette Bank on behalf of GVC. Korn voluntarily dismissed this action when confronted with a jurisdictional challenge.

In July 2005, Kertesz filed a Texas state court action against Korn seeking, among other things, declaratory relief from the claims made by Korn in the second New York action. Korn moved to dismiss the Texas action for lack of personal jurisdiction, and his motion was granted.

On October 14, 2005, Kertesz and his wife, along with the Pro Acoustics entities, filed an action in federal court in Texas asserting a number of claims, including a plea for a declaration that Kertesz had the exclusive right to the SD Speaker and a declaration that neither Kertesz nor his wife was liable to Korn for contribution on payments made by Korn on GVC's bank debt. Korn moved to dismiss this action for lack of personal jurisdiction, and his motion was granted.

On February 3, 2006, while the Texas actions were still pending, Korn caused the filing of the original complaint in this court. The complaint failed to make any mention of the purported 1995 Non-Compete Agreement.

On December 12, 2006, Korn filed an action in federal court in Pennsylvania seeking contribution from Kertesz and his wife. On December 20, 2007, the Pennsylvania federal court granted the defendant's motion for summary judgment. Korn has appealed that decision to the Third Circuit.

C. Procedural History

On February 3, 2006, the original compliant was filed in this action. The defendants moved to dismiss or stay the case in favor of the two actions then pending in Texas. By memorandum opinion and order dated July 19, 2006, this court granted the defendants' motion to stay.[40] The stay was lifted once the Texas actions were dismissed and, on July 6, 2007, the plaintiffs amended their complaint in this action as of right.[41]

On July 26, 2007, the defendants moved to dismiss Counts III, XIII, and XIV of the amended complaint, and filed an answer as to the remaining claims. The plaintiffs then timely notified the defendants of their intention to amend the complaint pursuant to Court of Chancery Rule 15(aaa). On October 2, 2007, the plaintiffs filed a second amended complaint. The defendants again moved to dismiss Counts III, XIII, and XIV of the second amended complaint. At the conclusion of oral argument on November 26, 2007, this court denied the motion

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[40] *Gen. Video Corp. v. Kertesz*, 2006 WL 2051023 (Del. Ch.).
[41] Ct. Ch. R. 15(a).

to dismiss with respect to Count III, and reserved decision as to Counts XIII and XIV. On February 25, 2008, those counts were dismissed with prejudice.[42]

Trial on all the remaining counts was held from June 30 through July 2, 2008. Count I alleges various breaches by Kertesz of the fiduciary duty of loyalty to GVC and/or Audeo. Count II alleges usurpation by Kertesz of corporate opportunities belonging to GVC and/or Audeo. Count III alleges a breach by Kertesz of the 1995 Non-Compete Agreement. Count IV alleges breaches by all the defendants of the 1991 Letter Agreement (which the plaintiffs cast as an exclusive license agreement) and the Second License Agreement. Count V alleges conversion by all defendants in the taking of certain property by Kertesz from GVC and/or Audeo and its use by the Pro Acoustics defendants. Count VI alleges misappropriation of trade secrets by all defendants in the use of certain documents relating to the SD Speakers, certain customer and supplier lists of GVC and/or Audeo, the web design for the ProAcoustics.com website, and the "new business plan" for the online audio distribution business. Count VII alleges deceptive business practices by all defendants in the use of the "Super Dispersion" and "Pro Acoustics" trade names. Count VIII is a claim for repayment of various outstanding demand loans Kertesz is alleged to owe to GVC. Count IX alleges tortious interference with business relations by all defendants by virtue of various

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[42] *Gen. Video Corp. v. Kertesz*, 2008 WL 509816 (Del. Ch.).

complained of acts, including Solin's alleged interference with the business relationship between GVC and/or Audeo, Korn, and Kertesz, as well as all of the defendants' alleged interference with GVC and/or Audeo's relationship with its customers and suppliers. Count X alleges tortious interference with contract by Solin and the Pro Acoustics entities for allegedly interfering with Kertesz's performance of his purported obligations under the 1991 Letter Agreement, the 1995 Non-Compete Agreement, and the Second License Agreement. Count XI alleges a breach of the fiduciary duty of loyalty owed by Solin to GVC as GVC's counsel in allegedly usurping the new audio business and using purportedly confidential information about GVC, which he allegedly obtained while acting as counsel to GVC, for personal gain. Count XII alleges that Solin aided and abetted Kertesz's purported breach of his fiduciary duties, or, in the alternative, that Kertesz aided and abetted Solin's purported breach of his fiduciary duties.

II.

The plaintiffs bring a number of claims rooted in alleged breaches of fiduciary duty by Kertesz or Solin. Because a common nucleus of findings of fact and conclusions of law dispose of the majority of these claims, these counts (Counts I, II, XI, and XII) will be dealt with together.

Before proceeding further, two important findings of fact bear repeating: (1) by the end of 2002, GVC was hopelessly insolvent and, for all intents and

purposes, out of business; (2) Audeo was a shell entity, created by Korn primarily as a means to defraud GVC's creditors. Audeo was never properly capitalized and never engaged in any significant operations outside of selling GVC's remaining inventory pursuant to the so-called Audeo Resolution.

In addition, the court finds that Kertesz ceased to be an officer or director of GVC or Audeo on March 15, 2003, the date he told Korn that he "wanted out." Sections 141(b) and 142(b) of the Delaware General Corporation Law ("DGCL") deal with the resignation of corporate officers and directors. Section 141(b) states, in pertinent part:

> Each director shall hold office until such director's successor is elected and qualified or until such director's earlier resignation or removal. Any director may resign at any time upon notice given in writing or by electronic transmission to the corporation.

Section 142(b) contains substantially the same language relating to officer resignations, providing, in pertinent part:

> Each officer shall hold office until such officer's successor is elected and qualified or until such officer's earlier resignation or removal. Any officer may resign at any time upon written notice to the corporation.

The question then is whether these statutory provisions require written notice to the corporation before a resignation can take effect. They do not. Chancellor Brown first considered (without deciding) the question in *Bachman v. Ontell*.[43] Presented

[43] 1984 WL 8245 (Del. Ch.).

squarely with the question in *Dionisi v. DeCampli*, then-Vice Chancellor Steele quoted *Bachman* approvingly as the rule in the case:

> Were I required to rule on the point in order to decide this case, my inclination would be to hold against the plaintiffs [and not require that a director must offer his resignation in a written document]. This is because the statutory language [of § 141(b)] can be construed as permissive rather than mandatory (it is said that the purpose of this language is to provide a means for a director's resignation to become effective at his election as opposed to requiring acceptance by the corporation, which was the former status of our law) and because *I can conceive of circumstances where a completely illogical result would follow from the refusal of the law to recognize an oral resignation clearly given.*[44]

In *Dionisi*, the court faced a set of facts very similar to those presented here: one of the two principals of a closely held corporation (who was a 50% stockholder, CEO, Secretary, and director of the corporation) announced to the other principal that he was quitting the business on January 5, 1987, but did not deliver a written notice of resignation until February 1, 1987.[45] The court found that both parties clearly understood the withdrawing principal was "resigning from the corporation and abdicating all authority of office in the corporation upon his clear and unequivocal announcement," and that the resignation was therefore effective as of that date.[46] The court accordingly held that:

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[44] 1995 WL 398536, at *8 (Del. Ch.), *amended on other grounds*, 1996 WL 39680 (Del. Ch.) (quoting *Bachman*, 1984 WL 8245, at *2) (emphasis added in *Dionisi*).
[45] 1995 WL 398536, at *3.
[46] *Id.* at *9.

> The joint venture ended January 5, 1987. Neither individual retained any rational expectation it would or could continue after Dionisi resigned. . . . I will not entertain a legal fiction and create abstract duties and speculate about breaches and consequential damages where the parties knew then and must know now their business relationship terminated on that fateful day. The relationship continued simply to wind up the affairs of the venture in a manner serving the best interests of [the parties] under the admittedly strained circumstances confronting them. . . . While joint venturers in fact owe each other and the enterprise a fiduciary duty of utmost good faith, fairness and honesty, that duty ends with the death of the joint venture.[47]

On March 15, 2003, Kertesz unequivocally told Korn that he "couldn't do it anymore, . . . wanted out, . . . was all done,"[48] and that he intended to go back to Texas "and have his own speaker business there."[49] Nine days later Kertesz memorialized his resignation by mailing to Korn a letter of resignation as director and/or officer from GVC and all of its subsidiaries. As in *Dionisi*, it is the overwhelming conclusion of this court that, as of March 15, 2003, both parties knew and understood that their venture in GVC and Audeo was at an end. Thus, any claims for breach of fiduciary duty by Kertesz to GVC or Audeo predicated on acts after March 15, 2003 must fail.

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[47] *Id.* (citing *In re Arthur Treacher's Fish & Chips of Ft. Lauderdale, Inc.*, 386 A.2d 1162, 1166 (1978); 3 BETH BUDAY & GAIL O'GRADNEY, FLETCHER CYCLOPEDIA CORPORATIONS § 860, at 275 (Perm. Ed. 1994 Rev. Vol.)).
[48] Trial Tr. vol. 2, 493, 496.
[49] Trial Tr. vol. 1, 243.

A. Counts I And II

After boiling down the repetitive claims in counts I and II, the following unique claims are essentially alleged:

> 1. Kertesz breached his fiduciary duty of loyalty to GVC by usurping the Pro Acoustics business;
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> 2. Kertesz breached his fiduciary duty of loyalty to Audeo by usurping the Pro Acoustics business;
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> 3. Kertesz breached his fiduciary duty of loyalty by usurping the goodwill of GVC and Audeo by using the "Pro Acoustics" and "Super Dispersion" trade names;
>
> 4. Kertesz breached his fiduciary duty to GVC by allowing the patent on the Super Dispersion system to expire;
>
> 5. Kertesz breached his fiduciary duty of loyalty by sharing confidential information about GVC and Audeo with Solin for the personal benefit of Kertesz and Solin and to the detriment of GVC and Audeo.

The court will address each of these claims.

1. Usurpation Of The Corporate Opportunity Of GVC

The best known statement of the corporate opportunity doctrine is taken from the venerable case of *Guth v. Loft, Inc.*[50] As recently summarized:

> The corporate opportunity doctrine, as delineated by *Guth* and its progeny, holds that a corporate officer or director may not take a business opportunity for his own if: (1) the corporation is financially able to exploit the opportunity; (2) the opportunity is within the corporation's line of business; (3) the corporation has an interest or

[50] 5 A.2d 503 (Del. 1939).

> expectancy in the opportunity; and (4) by taking the opportunity for his own, the corporate fiduciary will thereby be placed in a position inimicable to his duties to the corporation.[51]

Chancellor Chandler, in considering the necessary criteria for a corporation to be financially unable to exploit an opportunity, has noted:

> It has been said, however, that such financial inability must amount to insolvency to the point where the corporation is practically defunct. Mere technical insolvency, such as inability to pay current bills when due or mere inability to secure credit, will not suffice. The corporation must be actually insolvent.[52]

In this case, there is no question that GVC was irremediably insolvent by the spring of 2003. Its liabilities exceeded its assets by over $3 million on a $4.6 million balance sheet. By the plaintiffs' own admission, GVC was defunct by the end of 2002. Thus, the Pro Acoustics business was not an opportunity to GVC. Even if this were not the case, the Audeo Resolution Korn prepared required GVC to *pay* Audeo for the "privilege" of having Audeo operate the Pro Acoustics business ostensibly on its behalf, while simultaneously allowing Audeo to retain all of the profits of operating the business. Thus, GVC cannot possibly have had a legitimate interest in pursuing the business through Audeo.

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[51] *Broz v. Cellular Info. Sys., Inc*, 673 A.2d 148, 154-55 (Del. 1996) (citing *Guth*, 5 A.2d at 509.)
[52] *Sterianou ex rel. Stephanis v. Yiannatsis*, 1993 WL 437487, at *4 (Del. Ch.) (quoting 18B AM.JUR.2D *Corporations* § 1790 at 642-43 (1985) (footnotes omitted) and citing *CST, Inc. v. Mark*, 520 A.2d 469, 472 (Pa. Super. 1987); Annotation, *Financial Inability of Corporation to Take Advantage of Business Opportunity as Affecting Determination of Whether "Corporate Opportunity" was Presented*, 16 A.L.R.4TH 185, § 4[b] (1982)).

In addition, the acts complained of by the plaintiffs that allegedly usurped the audio business from GVC—building the Pro Acoustics website, forming the Pro Acoustics entities, and selling the Super Dispersion speakers—all occurred after March 15, 2003. As set forth earlier, acts taken after that date cannot form the basis of claims of breach of the fiduciary duty of loyalty by Kertesz, since he was no longer in a fiduciary relationship with GVC.

2. Usurpation Of The Corporate Opportunity Of Audeo

Because the same acts are complained of, this claim can also be disposed of on the basis that all of those acts occurred after March 15, 2003. Moreover, Audeo had no legitimate interest or expectation in any opportunity in the Pro Acoustics business to the extent it grew out of the Super Dispersion speaker business. Audeo's only connection to the Super Dispersion speaker business was via the self-dealing Audeo Resolution. As was discussed above, the Audeo Resolution simply acted as a means for Korn, through Audeo, to expropriate value from GVC. Because Korn stood on both sides of the transaction as director and controlling stockholder of GVC and as sole member and manager of Audeo, in order for the transaction to not be voidable it would have to meet the entire fairness test.[53] The egregious deal contemplated by the Audeo Resolution could only serve to expropriate value from GVC and its creditors, and could not possibly survive such

[53] *See Kahn v. Tremont Corp.*, 694 A.2d 422, 428 (Del. 1997).

an exacting analysis. As the holder of at most a voidable interest in the Super Dispersion speaker business that the plaintiffs claim was the core of their business plan, Audeo cannot have had the necessary interest or expectancy in the Pro Acoustics business opportunity to bring a claim under the corporate opportunity doctrine.

3. Usurpation Of The Goodwill Of GVC Or Audeo By Use Of The Pro Acoustics Or Super Dispersion Trade Names

Neither GVC nor Audeo had engaged in any significant business operations under the Pro Acoustics name, and there could therefore be no goodwill with respect to that name. Although Audeo had very briefly soft-launched a ProAcoustics.com website, that site was taken down within days for failure to pay the web design and hosting business, and no sales ever took place through that portal.

It was equally clear from the trial testimony that, by the end of 2002, GVC had no "specialty audio business" and was no longer actively promoting the Super Dispersion speaker system or engaging in any sales or marketing efforts whatsoever. Audeo likewise operated merely as a means to sell off GVC's inventory and made no efforts at marketing the Super Dispersion speaker system. There was, therefore, no goodwill to usurp in that trade name.

Additionally, because all of the complained of acts in purportedly usurping the Pro Acoustics and Super Dispersion trade names occurred after March 15, 2003, those acts cannot form the basis of a claim for breach of the fiduciary duty of loyalty.

4. Allowing The SD Speaker Patent To Expire

This claim is the fiduciary duty analog of the claim that was dismissed when the court granted summary judgment on Counts XIII and XIV on the basis of the statute of limitations. Even if it did not fail for that reason, the claim fails for lack of proof. The trial evidence completely failed to prove that Kertesz had any knowledge of or responsibility for the failure to pay the maintenance fee on the SD Speaker patent. Thus, he could not have knowingly misrepresented the status of that patent in the Second License Agreement.

5. Sharing Of Confidential Information

The plaintiffs also utterly failed to meet their burden of proof that Pro Acoustics ever utilized any of the plaintiffs' confidential information in starting or operating its business. Although the plaintiffs point to the customer and supplier lists of GVC as the key confidential information, GVC's customer list had always largely been public as part of its marketing. In addition, GVC's customer list was of no particular use in operating the Pro Acoustics business, which focuses on direct online sales as opposed to GVC's model of sales to dealers. As for GVC's

supplier list, Kertesz testified that he had simply obtained the list of Asian suppliers he uses from an audio trade industry website. Because that list was based entirely on public domain material, it cannot possibly be proprietary confidential information of GVC.

B. Count XI - Breach Of Fiduciary Duty By Solin

In count XI, GVC claims that Solin breached his fiduciary duty of loyalty, owed to GVC in his capacity as attorney to the corporation, by going into business with Kertesz, allegedly to GVC's detriment. In support of this claim, GVC alleges that Solin obtained a variety of confidential information related to the SD Speaker systems, the existence of Audeo, and the plans for the revitalized audio business. GVC further contends that Solin used that information to GVC's detriment by usurping the audio business opportunity and convincing Kertesz to leave GVC and join with him to pursue the audio business.

This entire claim fails as a matter of fact. There is no evidence that Solin ever learned anything about the SD Speakers or Audeo in his capacity as attorney for GVC. In fact, the evidence is quite the opposite. Weisenfeld, for instance, testified that he had never heard of either the SD Speakers or Audeo before his deposition. Solin was not general outside counsel to GVC. He was retained for the specific purpose of assisting Weisenfeld in the Toshiba arbitration, which bore no relation to the audio products business.

Furthermore, there is no evidence that Solin convinced Kertesz to go into business with him. Instead, the evidence shows that Kertesz sought out Solin's help with funding to form his new audio business in Texas, and Solin agreed as much out of compassion for Kertesz as out of any profit motive.

Finally, the contours of the duty of loyalty as between an attorney and client must relate to the matter for which the attorney has been retained to represent or advise the client. While the duty of confidentiality extends to *any* information the attorney learns from the client in his representative capacity, there are no restrictions on how the attorney may act in his individual capacity, so long as his actions are not affected by any confidential information he obtained.[54] Here, there is no evidence that Solin obtained any confidential information during his representation of GVC that would be relevant to Kertesz's audio business. He was thus free to act in his individual capacity as he saw fit with respect to Kertesz's offer of a partnership in the audio business.

C. Count XII - Aiding And Abetting Breach Of Fiduciary Duty

To succeed in a claim for aiding and abetting breach of fiduciary duty, a plaintiff must show: "(1) the existence of a fiduciary relationship, (2) a breach of

[54] *See* Del. Lawyers' Rules of Prof'l Conduct R. 1.7-1.9.

the fiduciary's duty, . . . (3) knowing participation in that breach by the defendants, and (4) damages proximately caused by the breach."[55]

The court finds no breach of fiduciary duty by either Kertesz or Solin. Therefore, it is not possible for the plaintiffs to make out their claim under count XII.

III.

The second amended complaint also contains three counts relating to breaches of various contracts purported to exist between Kertesz and GVC. Count III alleges breach by Kertesz of the 1995 Non-Compete Agreement. Count IV alleges breach by all defendants of the 1991 Letter Agreement (referred to as the "First License Agreement") and the Second License Agreement. Count X claims tortious interference with contract by Solin and the Pro Acoustics entities in allegedly interfering with Kertesz's performance of the First and Second License Agreements and the 1995 Non-Compete Agreement.

A. Count III - Breach Of The 1995 Non-Compete Agreement

As a threshold matter, the court concludes from all of the evidence that Kertesz never signed a non-compete agreement while he was employed at GVC and that the document Korn and the plaintiffs claimed to have been signed by

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[55] *Malpiede v. Townson*, 780 A.2d 1075 (Del. 2001) (quoting *Penn Mart Realty Co. v. Becker*, 298 A.2d 349, 351 (Del. Ch. 1972) (internal quotation marks omitted).

Kertesz is not authentic. Therefore, purely as a matter of fact, the claim predicated on the alleged 1995 Non-Compete Agreement fails. For completeness, however, the court will address the issue of enforceability, assuming *arguendo* the existence of the agreement had been proven.

The 1995 Non-Compete Agreement, according to its terms, is governed by New York law. Under New York law, a covenant not to compete will be enforced only when it meets the following criteria:

> (1) [T]he time and geographical scope of the restriction must be reasonable; (2) the burden on the employee must not be unreasonable; (3) the general public must not be harmed; and (4) the restriction must be necessary for the employer's protection.[56]

Moreover, "an otherwise valid covenant will not be enforced if it would operate in a harsh or oppressive manner. There is, in short, general judicial disfavor of anticompetitive covenants contained in employment contracts."[57]

Although the 1995 Non-Compete Agreement limits itself by its terms to 18 months, it is without limitation on geographical scope. It would thus prevent Kertesz from operating or working in an audio products business in Texas as a result of his former services to GVC in Pennsylvania. Kertesz worked in one capacity or another in audio and video equipment sales and distribution for more

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[56] *Mallory Factor Inc. v. Schwartz*, 536 N.Y.S.2d 752, 753 (App. Div. 1989) (citing *ABC v. Wolf*, 420 N.E.2d 363 (N.Y. 1981)).
[57] *Wolf*, 420 N.E.2d at 367-68 (internal citations omitted).

than 20 years. To prohibit him from engaging in work of that sort anywhere for 18 months would effectively prevent him from earning a living without abandoning his career field and would greatly limit his earning potential. Given the general disfavor shown by New York law to such agreements, this court could likewise find such an agreement to place an unreasonable burden on Kertesz.

More important, "such covenants are enforceable only to the extent that they afford an employer demonstrably necessary protection against unfair competition stemming from the use or disclosure of trade secrets."[58] Because GVC was completely insolvent and out of business when Kertesz left, there is no reason to think that the restrictions in the non-compete agreement could have operated to protect GVC. As a matter of law, therefore, even if the 1995 Non-Compete Agreement was authentic, it could not be enforced in this case, and any claim either in contract or in tort predicated on the enforceability of that agreement must fail.

B. Count IV - Breach Of The First And Second License Agreements By All Defendants

The plaintiffs allege that in manufacturing and distributing the SD Speaker system, the defendants violated the 1991 Letter Agreement and the Second License Agreement. To arrive at this claim, the plaintiffs characterize the 1991 Letter

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[58] *Primo Enters. v. Bachner*, 539 N.Y.S.2d 320, 321 (App. Div. 1989).

Agreement as a license agreement, at least insofar as it contemplates the grant of an exclusive license to a new corporation to be formed to distribute the SD Speakers. Because the Second License Agreement, dated as of November 1, 1991 (a month after the 1991 Letter Agreement), purports to "confirm the agreement among [Kertesz], General Video Corporation, and [Korn] with respect to the Speaker System," and because it is unclear to what extent the 1991 Letter Agreement actually created any license at all, the Second License Agreement will be deemed to supersede the 1991 Letter Agreement. Thus, the Second License Agreement alone need be considered.

Typically, an exclusive license can last no longer than the patent upon which the license is based.[59] The plaintiffs contend that while that may be true as to the world, as a matter of contract Kertesz could still have signed away his personal right to participate in the distribution of the SD Speaker system for some longer term in exchange for the consideration of the agreement. Ultimately, the court need not consider this issue. Moreover, since the only claim the plaintiffs could possibly assert as to the Second License Agreement sounds in contract, only those who are parties to the contract—in this case, only Kertesz—may be liable under it.

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[59] *See Cutter Labs. v. Lyophile-Cryochem Corp.*, 179 F.2d 80, 93 (9th Cir. 1949).

Paragraph 1 of the Second License Agreement purports to grant GVC an exclusive license to distribute the SD Speaker system for 99 years, subject to the provisions of paragraph 4. Paragraph 4 reads as follows:

> If (a) GVC ceases to actively operate as a distributor of electronic products, or (b) [Korn], [Korn]'s nominee and/or members of [Korn]'s family cease to own directly or indirectly, at least 50% of the ownership interests in GVC, then [Kertesz] may enter into a license agreement substantially similar to this letter with a corporation, limited liability company or other legal entity designated by [Korn] (provided that 70% or more of the ownership interests in the new license [sic] are owned directly or indirectly by [Korn] and/or a member of his family and [Kertesz] is offered ownership of 30% of the ownership interests in the new licensee for an amount not to exceed $100), in which event immediately after the execution of such new license agreement, this letter agreement shall terminate.

The plaintiffs assert this paragraph means that for the license to terminate GVC must not only "cease actively operat[ing] as a distributor of electronic products," but Kertesz must then enter into a new license agreement with a legal entity controlled by Korn in which Kertesz is offered a 30% stake in exchange for no more than $100. The defendants contend that paragraph 4 means that the license terminates automatically if GVC ceases operation, without more. The plaintiffs are closer to the truth.

An exclusive license in exchange for a royalty is normally not assignable.[60]

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[60] *See Waterman v. Shipman*, 55 F. 982, 986 (2d Cir. 1893) ("No license is assignable by the licensee to another unless it contains words which show that it was intended to be assignable."). *Cf. Johnson v. Uprite Mfg. Co.*, 161 N.E. 26, 27 (Ohio Ct. App. 1927) ("The grant is of the sole and exclusive license to manufacture, sell, and use devices made according to any and all

Because any such exclusive license in exchange for a royalty contains within it an implied duty on the part of the licensee to use its reasonable best efforts to generate sales under the license,[61] and because the business could not sell the license to another, the license would normally terminate when the licensee ceased operations.

Paragraph 4 operates to modify this rule. Under the Second License Agreement, Korn is effectively given an option—a right to offer Kertesz a 30% interest in a new entity, for an amount not to exceed $100, in exchange for a grant of an exclusive license to the new company. But such a right, like any other contractual term, is subject to the implied duty of good faith and fair dealing. Good faith would require Korn, as the holder of the right, to exercise such right in a timely manner or else waive it forever. The alternative rule would allow GVC, as the licensee, to fail to fulfill its duty to use its reasonable best efforts under the license, but simultaneously prevent the termination of the license based solely on a suggestion that Korn might exercise the right to shift the license to a new party at some time in the future.

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patents, etc. There is no language intimating that there was to be a sale or an assignment of the patent. The devices manufactured under the terms of this instrument must be made according to the patent, which the grantor owns or may hereafter obtain. This language is inconsistent with the idea that there was to be an assignment, or a sale of the patent. The use was limited to the corporation. It was not made to the company and its successors or assigns. So that the company named would only have the right to manufacture, sell, and use the devices. It follows that if it ceased business, all rights under the instrument would terminate.").

[61] *Wood v. Lucy, Lady Duff-Gordon*, 118 N.E. 214, 214-15 (N.Y. 1917) (Cardozo, J.).

The plaintiffs contend that Korn attempted to exercise that right by creating Audeo with the intention to offer to Kertesz a 30% interest. However, despite Kertesz's repeated complaints and demands, Korn never actually offered the required interest in Audeo to Kertesz on the required terms. In this regard, the Audeo Letter Agreement does not show Korn's intent to properly exercise his option. The Audeo Letter Agreement contemplates that Kertesz would get a 30% interest in Audeo only if he agreed to additional and oppressive terms. According to those terms, Kertesz's interest could be diluted at will and would generally be subject to domination by Korn, to a degree exceeding even that which GVC's corporate structure would allow.[62] Moreover, directly contrary to the terms of paragraph 4 of the Second License Agreement, the Audeo Letter Agreement offered the 30% interest in Audeo to Kertesz for consideration of $300—triple the $100 payment set forth by the Second License Agreement.

Because Korn failed to offer a 30% interest to Kertesz in Audeo in a timely fashion after the cessation of business by GVC, the license terminated. While Korn is not a party to this litigation, there is no doubt he is the real party in interest here. Assuming the dubious proposition that Audeo might have some rights by virtue of Korn's rights under the Second License Agreement, to the extent Korn's

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[62] *See* JX 69.

rights were waived, they were *a fortiori* waived as to Audeo. Therefore, Audeo's claim must fail.

Moreover, as to GVC, the asserted right to nominate a new entity in which to vest the license was never for the benefit of GVC. GVC therefore can have no claim under the agreement by virtue of any purported failure to honor that nomination right. GVC had already ceased doing business before the defendants began distributing the SD Speaker system. Thus, it no longer had the expectancy of any benefit from the license and could not have been harmed by the defendants' actions. Therefore, GVC's claim also must fail.

C. Count X - Tortious Interference With Contract By Solin And The Pro Acoustics Entities

The plaintiffs contend that Solin tortiously interfered with GVC's contract rights under the 1991 Letter Agreement, the 1995 Non-Compete Agreement, and the Second License Agreement. Additionally, the plaintiffs contend that Solin's allegedly tortious conduct should be imputed to the Pro Acoustics entities. Because the court finds that Solin did not engage in conduct constituting tortious interference, it is not necessary to reach the issue of imputation of Solin's conduct to Pro Acoustics.

In a claim for tortious interference with contract there must be "(1) a valid contract, (2) about which the defendants have knowledge, (3) an intentional act by

defendants that is a significant factor in causing the breach of the [contract], (4) done without justification, and (5) which causes injury."[63]

The court has already concluded that the 1995 Non-Compete Agreement is not a valid agreement, so it need not be considered any further here. As to the second element to be considered, there is no evidence that Solin was aware, at the time Pro Acoustics was formed, or in fact at any time prior to the filing of this litigation or one of its predecessor suits, of the existence of any of the agreements with which he is alleged to have interfered. None of the agreements relate to the matter for which he was retained to act for GVC—the arbitration with Toshiba regarding video wall systems and the Toshiba distribution agreement. There was no reason for him to have ever learned of the 1991 Letter Agreement or the Second License Agreement during that arbitration, for the simple reason that both agreements relate to the SD Speaker systems and not to video products or the Toshiba relationship.

Furthermore, because (as discussed earlier) Kertesz did not breach the Second License Agreement, which superceded the 1991 Letter Agreement with respect to licensing rights, the third element of the court's inquiry cannot possibly be satisfied. An inescapable logical requirement of the contention that the

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[63] *Wallace ex rel. Cencom Cable Income Partners II, Inc., L.P. v. Wood*, 752 A.2d 1175, 1182 (Del. Ch. 1999).

defendants committed an "intentional act . . . that [was] a significant factor in causing the breach of the [contract]"[64] is that a breach of contract must in fact have occurred. Here, there was no breach, and, therefore, no interference.

IV.

GVC contends in count VIII that certain advances made to Kertesz in 1998 and 1999 constituted demand loans which Kertesz has failed to repay. Having made demand in early 2005, GVC now seeks an order that Kertesz repay the purported loans, or a judgment against Kertesz for damages in the amount of the unpaid loans. Kertesz responds that the advances he received were not loans, that he never anticipated repaying the advances, that there was never any understanding with GVC that he would do so, and that he is therefore not liable to make repayment. Because the court concludes that the plaintiffs have not met their burden of proving the advances were loans, this claim fails.

"Established authority holds that the intention of the parties is the controlling factor in determining whether or not advances should be termed loans."[65] It is thus necessary for the court, in determining the proper characterization of stockholder advances, to determine whether the intent of the

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[64] *Id.*

[65] *Berthold v. Comm'r*, 404 F.2d 119, 122 (6th Cir. 1968); *see also Chism's Estate v. Comm'r*, 322 F.2d 956, 960 (9th Cir. 1963) ("Whether the withdrawals were loans or dividends depends upon petitioners' intent at the time that they were made. And intent, to repay or to retain, is a question of fact, to be determined upon a consideration of all the circumstances in each case.").

parties (the stockholder and the corporation) was that the advances be later repaid or if instead they were merely distributions of retained earnings.

Because GVC seeks to recover on these advances as loans, the burden is on GVC to prove that the parties intended at the time the advances were made that they be repaid. GVC offers in support of its claim its 2002 income tax return, which purports to show an existing balance on loans to stockholders in the amount of $117,161 at the end of the 2002 tax year.[66] This is far from compelling evidence. The tax return, beyond the bald assertion of the existence of such indebtedness to the corporation, does not actually speak to the critical question of who owes that money to the corporation. Moreover, without seeing the tax returns for GVC from 1998 and 1999, the years in which the advances were initially made, and which were conspicuously absent from the record, it is impossible for the court to attempt to correlate the creation of these entries regarding loans to shareholders with the advances made to Kertesz. The plaintiffs attempt in a table in their pretrial opening brief (the "Loan Table") to undertake such correlation. This, too, makes little sense. According to the Loan Table—the source of which information is not provided in the record—in 1999, when Kertesz is purported to have borrowed $42,200, the increase in net debt owed by stockholders is a mere $11,799. Even if this table were evidence (which it is not), it offers no explanation

[66] JX 82 at 4 (GVC's 2002 Form 1120S).

for this discrepancy. It may be that Korn paid back a loan from GVC to himself during that year, or perhaps there is some other explanation for this variance. But the plaintiffs have offered no evidence as to that issue, and the court will not speculate. GVC further argues that if the advances had not properly been loans, they would have constituted taxable income to Kertesz which both GVC and Kertesz would have had to declare on their respective tax returns. Because, the plaintiffs urge, neither Kertesz nor GVC noted any taxable income to Kertesz in their 1998 or 1999 returns in these amounts, it must be true that either these amounts were loans, or else Kertesz is a tax cheat. This is simply incorrect as a matter of law. GVC elected taxation under Subchapter S of the Internal Revenue Code, which implements partnership-like taxation for small business corporations.[67] As such, corporate earnings are not taxed at the corporate level, but are rather allocated to the stockholders each year in accordance to their pro rata share in the ownership of the corporation. The stockholders are then taxed on their allocated share each year regardless of whether or not any distribution is made to the stockholders. Thus, a distribution of retained earnings from GVC to Kertesz above and beyond his annual salary (at least so long as it was not in excess of his

[67] *See* I.R.C. § 1361 *et seq.*

pro rata share of retained earnings) would have had no tax consequences for Kertesz, since he would have already paid taxes on those funds.[68]

The cases plaintiffs cite in support of their position that an advance is the general equivalent of a loan are entirely inapposite. *Thompson v. Williams Companies*,[69] *Fasciana v. Electronic Data Systems Corp.*,[70] and *Advanced Mining Systems, Inc. v. Fricke*[71] are cases where directors or officers seek advancement under section 145 of the Delaware General Corporation Law. Advancement under section 145 is completely different from an "advance" on future distributions of profits made to a stockholder. As the cases all state, an advance to a director or officer under section 145 is simply a loan against the indemnification right the director or officer anticipates. Here, a stockholder has taken a distribution from the profits of the corporation in "advance" of when the corporation may "normally" distribute its profits to its stockholders.

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[68] The only places such distributions would have appeared in GVC's tax return is in the aggregate on line 20 of page 3 of its 1120S ("Total property distributions (including cash) other than dividends reported on line 22 below") and the corresponding line 7 of Schedule M-2 to the same form ("Distributions other than dividend distributions"). Not having those returns for the relevant years, it is impossible to determine what they might have said. The court notes, however, that in GVC's 1996 income tax return (the only return prior to GVC's insolvency included in the record), GVC made aggregate distributions to its stockholders of $236,837. It is thus reasonable to conclude, at the very least, that distributions to corporate stockholders were made in GVC's better economic times.

[69] 2007 WL 2215953 (Del. Ch.).

[70] 829 A.2d 160 (Del. Ch. 2003).

[71] 623 A.2d 82 (Del. Ch. 1992).

The plaintiff has thus proffered no meaningful evidence, other than the self-serving testimony of Korn, in support of its claim that the advances to Kertesz were loans requiring repayment. Kertesz points out two facts that make the plaintiffs' claim all the more dubious: (1) in April and May 2003, when Korn was dickering with Kertesz over a few thousand dollars worth of speaker parts, he made no mention of the over $100,000 loan Kertesz allegedly owed GVC at that time; and (2) Korn made no mention at all of these supposed demand loans until February 2005, when his attorney sent the demand letters to Kertesz, by which point Korn was almost certainly preparing for the first New York action.

Because GVC fails to prove that the advances to Kertesz were intended at the time they were made to be treated as loans requiring repayment, GVC's claim fails.

V.

The plaintiffs also assert numerous claims grounded in tort. In Count V, the plaintiffs allege conversion by all defendants in the taking of GVC's assets. According to the plaintiffs, this conversion destroyed GVC and Audeo. In Count VI, the plaintiffs allege misappropriation of trade secrets of GVC and/or Audeo by all defendants. In Count VII, the plaintiffs allege that the defendants engaged in deceptive business practices in their use of the names "Pro Acoustics" and "Super Dispersion." Count IX claims tortious interference with business relations in

allegedly preventing GVC's use of its "established relationships" with its low-cost overseas suppliers and inhibiting GVC's and Audeo's future sales to their customers, distributors, suppliers, and representatives.

A. Count V - Conversion By All Defendants

In Count V, the plaintiffs claim that the defendants converted the property and assets—namely, the production tooling for the SD Speakers—of GVC to their own use, thus destroying GVC's and Audeo's business. "One who uses a chattel in a manner which is a serious violation of the right of another to control its use is subject to liability to the other for conversion."[72] In other words, conversion is the "wrongful possession or disposition of another's property as if it were one's own . . . ."[73]

The plaintiffs fail to prove that Kertesz wrongfully took the production tooling. Based on the evidence offered at trial, including in particular the testimony of non-party Baltrus, the court concludes that Kertesz had an agreement with Korn to take the tooling and some of the other inventory. Korn breached that agreement by reallocating most of the equipment and inventory to himself. However, Korn did not tell Baltrus that she should send him the tooling (although he claims he tried to tell her by sending an email to a defunct email address in her

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[72] RESTATEMENT (SECOND) OF TORTS § 227 (2008).
[73] BLACK'S LAW DICTIONARY 356 (8th ed. 2004).

name). Baltrus shipped the tooling to Kertesz in accordance with her prior understanding with Korn. Kertesz claims that he was in fact entitled to possess the tooling. The court concludes that Kertesz was correct. The plaintiffs have therefore not carried their burden of proof as to the elements of conversion.[74]

B. Count VI - Misappropriation Of Trade Secrets By All Defendants

In Count VI, the plaintiffs allege that Kertesz and Solin each misappropriated trade secrets of GVC and/or Audeo. As to Solin, this count is easily addressed—he never obtained any audio business trade secrets in the course of his representation of GVC. As discussed earlier in this opinion, Solin's representation was limited to an arbitration with respect to the Toshiba distribution agreement for video wall equipment. He never had any access to or knowledge of any trade secrets with respect to the small audio products business. The same is even more true in the case of Audeo, with which Solin had no contact or relationship.

As to Kertesz, the claim is only slightly more complicated. A trade secret is defined as "information . . . [that] [d]erives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable

[74] The plaintiffs' claim for damages on this claim are, in any case, grossly excessive. The record suggests that (1) the older, used tooling sent to Kertesz was worth as little as $2,000; and (2) the plaintiffs could have obtained new tooling from Analytical Plastics in a few weeks' time for $10,000 or less.

by proper means by, other persons who can obtain economic value from its disclosure or use."[75] The plaintiffs claim that Kertesz misappropriated the following classes of trade secrets from GVC and/or Audeo: (1) specifications for the design and manufacture of the SD Speakers; (2) contracts and distribution agreements for the SD Speakers; (3) pricing related to the overseas manufacture of speakers and audio components; (4) the web interface pages and designs for the stillborn ProAcoustics.com website; and (5) the new business plan for the Pro Acoustics business.

In connection with technical specifications and know-how with respect to the SD Speakers, as discussed earlier, GVC's and Audeo's interest in the Second License Agreement terminated. As to any particular trade secret with regard to the production of the SD Speakers, the plaintiffs have offered no evidence about what that might be beyond their conclusory allegations. Kertesz was the original designer of the speakers, and the speakers had been in production at LA East before GVC ever became involved. Thus, without evidence to the contrary, there is no reason to believe that GVC or Audeo owned any technical know-how or other trade secrets regarding the SD Speaker production.

The plaintiffs also failed to offer evidence that Kertesz misappropriated any contracts or distribution agreements for the SD Speakers. While GVC had largely

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[75] 6 *Del. C.* § 2001(4).

sold the SD Speakers through distributors, the Pro Acoustics business formed by Kertesz and Solin primarily sells via the internet.

With respect to the pricing for overseas manufacture of the speakers or audio components, Kertesz explained that he obtained the contact information for the various inexpensive Asian manufacturers he uses from an audio industry web page, and that there was nothing proprietary about any of those relationships. The plaintiffs have done nothing to rebut this testimony. The evidence also shows that the Pro Acoustics business did not misuse the ProAcoustics.com website. Instead, that website underwent a redesign almost as soon as Pro Acoustics was formed in accordance with Kertesz's new specifications. Finally, the record shows that Kertesz offered the code for the original web pages to Korn, but Korn and his attorney never followed up on the matter.

C. Count VII - Deceptive Business Practices By All Defendants

The plaintiffs allege that by the use of the Super Dispersion and Pro Acoustics trade names, the defendants have violated the Deceptive Trade Practices Act.[76] With regard to the Deceptive Trade Practices Act, then-Vice Chancellor Steele said the following in *Dionisi*:

> A party seeking to recover under this Act must have a basis for injunctive relief. The Act is designed to encourage immediate or at least timely enforcement of its provisions to halt unfair or deceptive

[76] 6 *Del. C.* § 2532.

> trade practices between businesses with "horizontal relationships." The public policy underlying the Act benefits both the businesses involved and presumably, at least inferentially, the public in general. Injunctive relief coupled with the possibility of treble damages and counsel fees looms as a powerful deterrent against wrongdoers and an incentive to litigate for the wronged. It is not a vehicle for damages long after the immediacy of the grievance dissipates. When the press for instant action eases, so does the basis for possible concomitant damages. *The DTPA is not a platform for an independent common law damage suit. "[T]he Act was not intended to create a new cause of action distinct from the common law protections designed to secure businesses against the deceptive trade practices of others."*[77]

The plaintiffs here did not bring suit for injunctive relief in a timely manner. As discussed later in this opinion, any claim with regard to the "taking" of Audeo's potential Pro Acoustics business is by now time-barred by the doctrine of laches. It would be most unjust, after the plaintiffs waited two years to file their first action, and five years after the business began operating, to now enjoin the defendants from using either trade name. With respect to the Super Dispersion trade name, the defendants have stopped using it altogether already, as Pro Acoustics has ceased selling the SD Speaker system. In addition, the audio business was never a significant part of GVC's business, so that to the extent it could have had any goodwill attached to the Pro Acoustics name, that goodwill would have been *de minimis* compared to the goodwill the defendants have now

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[77] 1995 WL 398536, at *13 (quoting *Grand Ventures, Inc. v. Whaley*, 632 A.2d 63, 68 (Del. 1993)) (emphasis added).

developed in the name. As this court stated in *Dionisi*, without a valid claim for injunctive relief, there can be no claim for damages under the Deceptive Trade Practices Act. An injunction is extraordinary equitable relief that will not be awarded where it would work injustice. Because the plaintiffs would not be entitled to injunctive relief if they sought it, they cannot be entitled to damages. The plaintiffs' claim for relief therefore must fail.

D. Count IX - Tortious Interference With Business Relations By All Defendants

The plaintiffs allege that Solin tortiously interfered with the "business expectancy" of GVC and Audeo by "inducing Kertesz to abandon GVC and Audeo and instead form [the Pro Acoustics entities] to conduct the Pro Acoustics Business and distribute the Super Dispersion System for their own benefit."[78] The plaintiffs further allege that Kertesz, Solin, and the Pro Acoustics entities "tortiously interfered with the business relations of GVC and Audeo by preventing GVC and Audeo from continuing its existing Pro Acoustics Business with its customers, distributors, suppliers, and representatives,"[79] thus "destroy[ing] the ability of GVC and Audeo to conduct the Pro Acoustics Business."[80]

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[78] Second Am. Compl. 43 ¶¶ 171-72.
[79] *Id.* 43 ¶ 173.
[80] *Id.* 44 ¶ 176.

In order to prove a claim for tortious interference with business relations, a plaintiff must demonstrate "'(a) the reasonable probability of a business opportunity, (b) the intentional interference by defendant with that opportunity, (c) proximate causation, and (d) damages.' [The court applies] these elements to a particular case 'in light of a defendant's privilege to compete or protect his business interests in a fair and lawful manner.'"[81]

To begin with, the charge of tortious interference against Solin fails for the simple reason that Solin did not engage in any wrongful conduct. Rather than convincing Kertesz to abandon GVC and Audeo, as the plaintiffs claim, it is the finding of the court that Kertesz quit GVC and Audeo of his own volition, and only then sought out Solin's aid in funding his new venture. Solin's acts thus fail to meet (at the very least) the second element of the claim for tortious interference with business relations.

With respect to the second charge of tortious interference, leveled against all the defendants, that Kertesz, Solin, and the Pro Acoustics entities somehow interfered with GVC's and/or Audeo's ability to continue its Pro Acoustics business with customers, suppliers, distributors, and representatives, the plaintiffs have offered no evidence to prove their claim. They have not proven the existence

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[81] *Malpiede*, 780 A.2d 1075, 1099 (Del. 2001) (quoting *DeBonaventura v. Nationwide Mut. Ins. Co.*, 428 A.2d 1151, 1153 (1981)).

of any supplier relationship that the defendants prevented the plaintiffs from continuing, any distributor relationship which was harmed, or any customer relationship that was blocked. GVC and Audeo did not cease to deal with these parties because the defendants interfered with their relationships with them. Rather, GVC and Audeo stopped dealing with these parties because GVC was insolvent and Audeo was an uncapitalized entity. After Kertesz left, there was no one other than Korn left working at either entity, and Korn admitted he had no idea how to run an audio business. There is no sense in which Kertesz's decision to stop using his talents to run an audio business for Korn's benefit constitutes tortious interference. At most, Kertesz simply ceased aiding the plaintiffs and Korn in running their venture—he did not affirmatively interfere with their doing so. To conclude otherwise would be to treat Kertesz as an indentured servant to GVC and Audeo, once a "reasonable probability of a business opportunity"[82] had developed. The plaintiffs' claim for tortious interference with business relations must therefore fail.

VI.

Finally, the court holds that the plaintiffs delayed unreasonably in asserting their equitable claims to recover the profits of the Pro Acoustics entities and, thus,

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[82] *Malpiede*, 780 A.2d 1075, 1099 (Del. 2001) (quoting *DeBonaventura v. Nationwide Mut. Ins. Co.*, 428 A.2d 1151, 1153 (1981)).

are guilty of laches. "Laches is an equitable principle that operates to prevent the enforcement of a claim in equity where a plaintiff has delayed unreasonably in bringing suit to the detriment of the defendant or third parties."[83] Delaware courts have variously characterized laches as "[d]elay in the assertion of a right under circumstances that make it unconscionable for a court of equity to lend aid to its enforcement,"[84] "negligent and unreasonable delay,"[85] and "inexcusable delay."[86] It is a maxim of equity that "[e]quity aids the vigilant, not those who slumber on their rights."[87]

"The Supreme Court of Delaware has identified the following factors as important in determining whether a party is guilty of laches: (1) knowledge of a claim, (2) unreasonable delay, (3) change of position on the part of those affected by the plaintiff's nonaction, and (4) the intervention of rights of those affected."[88] Here, despite having full knowledge of these claims by the middle of 2003, the plaintiffs did not bring them until the middle of 2005. The plaintiffs have offered no coherent explanation of this delay, simply a statement by Korn that he was too

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[83] Donald J. Wolfe, Jr. & Michael A. Pittenger, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 11.05, at 11-55 (2008).
[84] *Scotton v. Wright*, 117 A. 131, 136 (Del. Ch. 1922).
[85] *Bovay v. H.M. Byllesby & Col*, 12 A.2d 178, 190 (Del. Ch. 1940).
[86] *Wright v. Scotton*, 121 A. 69, 72 (Del. 1923).
[87] *Adams v. Jankouskas*, 452 A.2d 148, 157 (Del. 1982); *see also Hutchinson v. Fish Eng'g Corp.,* 203 A.2d 53, 63 (Del. Ch. 1964) ("One of the firmest of equitable principles is that one may not slumber on his rights to the detriment of another and later attempt to assert them.").
[88] Donald J. Wolfe, Jr. & Michael A. Pittenger, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 11.05[b], at 11-56 to -57 (2008).

shocked by Kertesz's actions to know what to do. This delay undoubtedly led to a change in position by Kertesz and Solin, who have invested money and time into the Pro Acoustics enterprise reasonably believing that they would reap the rewards of their endeavor if it should prove successful. In the circumstances, even if the plaintiffs had proven any of their claims, and they have not, they would not be entitled to any equitable relief, including any award of damages predicated on the fiduciary misconduct alleged.

VII.

For all the reasons herein, judgment is awarded to the defendants and against the plaintiffs on all counts. IT IS SO ORDERED.