IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNT

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OMNICARE, INC.,	)	
	)	
Plaintiff,	)	
	)	
v.	)	C.A. No. 19800
	)	
NCS HEALTHCARE, INC., JON H. OUTCALT, KEVIN B. SHAW, BOAKE A. SELLS, RICHARD L. OSBOURNE, GENESIS HEALTH VENTURES, INC., and GENEVA SUB, INC.,	)	
	)	
Defendants.	)	

MEMORANDUM OPINION AND ORDER

Submitted: October 24, 2002
Decided: October 25, 2002

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LAMB, Vice Chancellor

The Merger Agreement provides that the Board may not terminate the Merger before the NCS stockholders have an opportunity to vote on it. Relatedly, in connection with and shortly after the NCS directors voted to approve the Merger Agreement, Genesis and NCS entered into voting agreements with Outcalt and Shaw whereby those individuals (1) granted Genesis an irrevocable proxy to vote all of their shares of NCS common stock in favor of the Merger Agreement and against any other proposal, (2) agreed to vote all such shares in a like manner, and (3) agreed to avoid disposing of or otherwise encumbering their shares of NCS common stock before consummation of the merger with Genesis ("Voting Agreements").

NCS has a dual class voting structure consisting of Class A Common Stock, which entitles the holder to one (1) vote per share, and Class B Common Stock, which entitles the holder to ten (10) votes per share. The Voting

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> We would also consider a stock transaction in order to allow NCS stockholders to share in the upside of the combined companies. With respect to structure, we would be willing to discuss acquiring the securities of NCS in a tender offer. We wish, and are prepared, to meet immediately with you and your directors, management and advisors to answer any questions about our proposal and to proceed with negotiations leading to the execution of a definitive merger agreement.

Second Am. Compl., at 11.

Omnicare purchased 1,000 shares of NCS Class A Common Stock.[3] Omnicare did not hold any stock in NCS before this purchase. Omnicare has since commenced a tender offer for NCS shares at $3.50 per share.

III.

On August 1, 2002, Omnicare initiated this lawsuit. On September 23, 2002, Omnicare filed a Second Amended Complaint. In its Second Amended Complaint, Omnicare alleges that: (1) the voting agreements between Genesis, Outcalt, and Shaw violated NCS's charter and thus automatically converted Outcalt's and Shaw's Class B shares into Class A shares (Count I); (2) the Board violated 8 *Del. C.* § 141(a) by entering into an exclusivity agreement with Genesis on July 3, 2002, and approving the Voting Agreements and the Merger Agreement on July 28, 2002 in violation of their fiduciary duties (Count II); (3) the Board breached their fiduciary duties by approving the Genesis merger and by refusing to consider Omnicare's July 26, 2002 indication of interest (Count III); (4) Genesis aided and abetted these alleged breaches of fiduciary duties

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[3] This fact is evidenced in Omnicare's Schedule TO filed with the Securities and Exchange Commission on August 8, 2002. The court may take judicial notice of facts publicly available in filings with the SEC. *See, e.g., In re Santa Fe Pacific S'holder Litig.*, 669 A.2d 59, 69-70 (Del. 1995).

relationship between the plaintiff and the defendants at the time of the alleged breach. Nevertheless, Omnicare invites the court to recognize an exception to this rule to allow it standing on the basis of its current status as a competing bidder for control of NCS. It argues, with some force, that a realistic assessment of its position reveals both that the alleged fiduciary misconduct adversely affects its chances of succeeding in its takeover bid and that its interest in obtaining injunctive relief to remedy that alleged misconduct is largely congruent with the interests of NCS stockholders in receiving a better offer for their shares. For the reasons discussed below, the court declines to permit an entity that could not sue in its own right to sue directors for breach of a fiduciary duty owed to others.

1. Public Policy Detests The "Purchase" Of A Lawsuit

It is undisputed that Omnicare was not a stockholder at the time of the alleged misconduct stated in its complaint.[11] Omnicare purchased NCS stock

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[11] A plaintiff is barred from bringing claims when a stockholder purchases stock after the board of directors has approved a transaction and the transaction has been publicly disclosed. *See In re Beatrice Cos., Inc. Litig.*, 1987 WL 36708, at *3 (Feb. 20, 1987) ("In the case of a proposed merger, the plaintiff must have been a stockholder at the time the terms of the merger were agreed upon because it is the terms of the merger, rather than the technicality of its consummation, which are challenged.") (citing *Newkirk v. W.J. Rainey, Inc.*, 76 A.2d 121, 123 (Del. Ch. 1950); *Brown v. Automated Mktg. Sys., Inc.*, 1982 WL 8782, at *2 (Mar. 22, 1982) ("[I]t is not the merger itself that constitutes the wrongful act of which plaintiff complains, but rather it is the fixing of the terms of the transaction") (citation omitted).

principles"[15] and has been applied to preclude stockholders who later acquire their shares from prosecuting direct claims as well.[16] Similarly, our courts have held that plaintiffs who purchase stock after disclosures have been made cannot pursue claims for breaches of the duty of disclosure.[17]

Delaware's policy against allowing plaintiffs to purchase stock and then challenge transactions agreed upon before the purchase "might easily be frustrated if individuals could place orders to purchase stock on the same day the challenged transaction occurred."[18] Delaware courts enforce this policy by denying standing to after-the-fact purchasers and dismissing their complaints.[19] Thus, it would appear that because there is such a strong policy against the

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[15] *See Brown*, 1982 WL 8782, at *2 (citing *Home Fire Ins. Co. v. Barber*, 93 N.W. 1024, 1029 (Neb. 1903)); *see also Bangor Punta Operations, Inc. v. Bangor & A.R. Co.*, 417 U.S. 703, 711 (1974) (noting the basic equitable principle that plaintiffs who acquire shares after disputed transactions occur are barred from recovery).

[16] *See In re Gaylord Container Corp. S'holders Litig.*, 747 A.2d 71, 82 & n.15 (Del. Ch. 1999) (noting that plaintiffs "who buy stock and challenge the earlier adoption of properly disclosed defensive measure" should be "barred from recovery").

[17] *See Thorpe v. CERBCO, Inc.*, 1993 WL 35967, at *3 (Del. Ch. Jan. 26, 1993) ("[W]hile plaintiffs may have standing to complain about breach of duty that occurs while they are shareholders. They have no direct right to be awarded judicial relief for [acts that occurred before they purchased stock]."); *Sanders v. Devine*, 1997 WL 599539, at *5 (Del. Ch. Sept. 24, 1997) ("In the present case, plaintiff was not a stockholder at the time the prospectus was issued, therefore, as a matter of law, there can be no liability under any fiduciary duty theories for the disclosures made in connection with the offering.").

[18] *Avacus Partners, L.P. v. Brian*, 1990 WL 161909, at *6 (Del. Ch. Oct. 24, 1990).

[19] *See, e.g., IM2 Merchandising*, 2000 WL 1664168, at *6.

stockholder, not whether that status sufficed to create standing where there was none before. Finally, it must be observed that, in every case that found standing to sue cited by Omnicare, the plaintiffs owned stock at the time of the alleged fiduciary breach.[23]

Omnicare cites only one case, *Emerson Radio Corp. v. International Jenson, Inc.*,[24] to support its argument that a bidder-plaintiff can bring a breach of fiduciary duty claim without regard to the bidder's ownership of shares.[25] A careful reading of *Emerson*, however, shows that it does not support Omnicare's argument. The court in *Emerson* clearly held that the plaintiff bidder had no standing:

> In its capacity as a bidder, Emerson has no claims to raise, because neither Jensen nor its Board owes a duty to an interested potential acquirer to deal with that acquirer. As the Chancellor has aptly put it:
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> > [I]t is a simple and I would have thought well understood fact that one [in the position of a tender offeror] possesses no legal right to have an owner of an asset supply him with information

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[23] *See Lipton v. News Int'l*, 514 A.2d 1075, 1076 (Del. 1986); *Williams v. Geier*, 1987 WL 11285, at *3 (Del. Ch. May 20, 1987); *Moran v. Household Int'l, Inc.*, 490 A.2d 1059, 1064 (Del. Ch. 1985), *aff'd*, 500 A.2d 1346 (Del. 1985); *Condec Corp. v. Lunkenheimer Co.*, 230 A.2d 769, 772 (Del. Ch. 1967); *GM Sub Corp. v. Liggett Group, Inc.*, 1980 WL 6430, at *1 (Del. Ch. Apr. 25, 1980); *Packer v. Yampol*, 1986 WL 4748, at *5 (Del. Ch. Apr. 18, 1986); *In re Tri-Star Pictures, Inc., Litig.*, 634 A.2d at 321.

[24] 1996 WL 483086.

[25] *Id.*, at *16.

> or negotiate with him. Thus, it simply is not a legal wrong to a would-be buyer for an owner to ignore or reject an offer of sale.
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> *Gagliardi v. Trifoods Int'l Inc.*, Del. Ch., C.A. No. 14725, Mem. Op. at 21, Allen, C. (July 19, 1996). Rather, any duty Jenson's board may have to deal with Emerson as a potential buyer was owed solely to Jensen's stockholders, as a corollary of the Board's fiduciary duty to achieve the highest available value for shareholders. That is why plaintiffs who seek to assert breach of fiduciary duty claims of this kind have been persons to whom such fiduciary duties were owed, i.e., stockholders of the target corporation.[26]

The court in *Emerson* specifically noted, "no Delaware court has recognized the standing of a non-stockholder bidder for a target company."[27] Although the court acknowledged the argument that the bidder-plaintiff should be denied standing, the court found it was not necessary to decide the point, which was raised only at the preliminary injunction hearing itself:

> This question need not be decided to resolve Emerson's motion. That motion can be determined on other grounds with no different result. Moreover, a refusal by this Court to entertain the fiduciary duty claims on this threshold ground would disserve the interests of the parties and the public. Although the Shareholder Plaintiffs do not advance the same claims as Emerson, they do own Jensen stock and have joined in Emerson's position. And, importantly, the merits of the defendants' conduct have now been the subject of discovery, briefing and argument (albeit expedited). For this Court now to refuse to review that conduct would be wasteful of

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[26] *Id.*, at *13.

[27] *Id.*

> the parties' considerable investment of effort and resources, and deprive Jensen's shareholders and the public of such benefit that this Court's (and any reviewing Court's) determinations might have.
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> Accordingly, the Court will proceed on the assumption, *but without deciding*, that Emerson has standing to assert its claims.[28]

The court then went on to deny the preliminary injunction sought by the plaintiff-bidders. Therefore, *Emerson* does not provide support for Omnicare's "bidder standing" argument. Moreover, even if the court were to consider the other factors enumerated in *Emerson*, there would be no compelling reason to allow Omnicare to proceed on its fiduciary duty claims. The time, effort, and resources expended in *Emerson* have not been similarly spent in this controversy. The standing issue was raised well before any deposition discovery was taken and also before the preliminary injunction hearing now scheduled to be heard in three weeks' time.

Finally, addressing Omnicare's policy arguments, the court concludes that they are not sufficiently compelling to permit a person who is not in any respect a participant in the corporation to sue on claims relating to the internal affairs of that enterprise. Delaware courts have shown considerable latitude in entertaining

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[28] *Id.*, at *14 (emphasis added).

fiduciary duty litigation brought by stockholders who are also themselves bidders for control. The only consistent limitation placed on those persons is that they also be stockholders at all relevant times and, thus, among those to whom a duty was owed, even if they only own one share. Of course, this rule is not based on the economic significance of such a bidder's investment, which often is immaterial. Instead, it is based on a purely legal or equitable notion that limits to those having a relationship with the corporation the right to sue over its internal affairs.[29]

Therefore, the court will dismiss Counts II through V of Omnicare's complaint for lack of standing.

B. Omnicare's Count I "Voting Rights" Argument

Omnicare's claim relating to the effect of the Voting Agreements on the Class B shares held by Outcalt and Shaw stands on a different footing. Count I is not a fiduciary duty based claim and does not seek any coercive remedy against either the corporation or its directors. Instead, in Count I, Omnicare seeks a declaration that the Voting Agreements resulted in the automatic conversion of

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[29] If, as Omnicare suggests, persons external to those relationships are acknowledged to have standing to sue to enforce them, it is not immediately apparent why competing bidders are the only ones to whom such standing might be accorded. *See Laster, supra,* note 20.

those Class B shares into Class A shares, pursuant to the terms of the NCS certificate of incorporation. If Omnicare prevails on this claim, the voting power of the shares of common stock that are subject to the Voting Agreements will be diminished from more than 65% to approximately 20% of the total voting power of NCS.

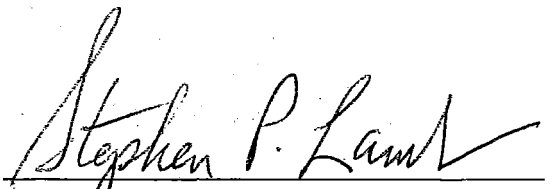
As distinguished from the balance of Omnicare's complaint, the relief sought in Count I does not relate to or seek to remediate any alleged fiduciary misconduct that preceded Omnicare's ownership of NCS stock. Rather than seek to undo anything or remedy any wrong committed in the past, Count I of the complaint merely demands to know whether Outcalt and Shaw continue to own high-voting Class B shares or, instead, whether those shares have been converted into Class A shares.

This is a question of immediate and continuing interest to all stockholders of NCS. It is also a question to which Omnicare, as the owner of 1,000 Class A shares will eventually be entitled to an answer. If Omnicare were to wait until after the vote to approve the Merger takes place, there is no dispute that it would have standing to challenge the result of that vote by bringing a claim under

and fully prepared to litigate this issue. If it is successful, there is a substantial likelihood that the NCS stockholders will be able to achieve a superior transaction in the sale of their corporation.[34] Considering all of these circumstances, the policy against purchasing a claim should give way to permit the prompt, efficient and effective litigation of the issues asserted in Count I. Therefore, the court finds that Omnicare has standing to pursue Count I of its complaint.

VI.

For the foregoing reasons the motion to dismiss Omnicare's claims is granted as to Counts II through V. The motion to dismiss Count I is denied. **IT IS SO ORDERED.**



Vice Chancellor

[34] The merger consideration is currently valued at approximately $1.30 per share in NCS stock. Omnicare's tender offer is priced at $3.50 per share in cash.