



**COURT OF CHANCERY
OF THE
STATE OF DELAWARE**

STEPHEN P. LAMB
VICE CHANCELLOR

New Castle County Court House
500 N. King Street, Suite 11400
Wilmington, Delaware 19801

Submitted: March 28, 2005
Decided: March 30, 2005

C. Barr Flinn, Esquire
Young Conaway Stargatt & Taylor, LLP
1000 West Street, 17th Floor
Wilmington, DE 19801

Daniel B. Rath, Esquire
Rebecca L. Butcher, Esquire
James S. Green, Jr., Esquire
Landis Rath & Cobb LLP
919 Market Street, Suite 600
Wilmington, DE 19801

***RE: U.S. Bank National Association v.
U.S. Timberlands Klamath Falls, L.L.C., et al.
C.A. No. 112-N***

Dear Counsel:

Counsel for U.S. Bank National Association seeks to file a third amendment to its complaint. The proposed amended complaint does not name any new parties to this action, but does seek to add the following claims: breach of contract against defendant U.S. Timberlands Yakima, L.L.C. (“Yakima”) (Count I and VI); injunctive relief (Count V); tortious interference with contract against defendants John M. Rudey, George R. Hornig, and Yakima (Count VII); aiding and abetting a breach of fiduciary duties against defendants Rudey and Hornig (Count X); and

piercing the corporate veil against defendants Rudey, Hornig, Yakima, and all of the U.S. Timberlands companies¹ (Count IX).

The defendants object to the proposed amendment on the grounds that U.S. Bank waited too long to bring these claims and that this delay is prejudicial to them. The defendants also argue that the claims are baseless and, therefore, allowing amendment would be futile.

This court freely grants leave to amend pleadings. Court of Chancery Rule 15(a) provides that “[a] party may amend the party’s pleading . . . by leave of [the] Court . . . and leave shall be freely given when justice so requires.” “A party should be granted leave freely to amend its complaint, unless there is evidence of bad faith, undue delay, dilatory motive, undue prejudice or futility of amendment.”²

With respect to all of the claims, except the claim for piercing the corporate veil, the prejudice to the defendants is negligible. As a result of the need for the court to consider several motions to dismiss, discovery on the complaint is only just getting under way. Document production is in the early stages and only one deposition has been started. Moreover, the factual basis for the new claims (with

¹ The U.S. Timberland companies include U.S. Timberlands Klamath Falls, L.L.C. (n/k/a Inland Fiber Group, L.L.C.), U.S. Timberlands Services Company, L.L.C. (n/k/a Timber Resource Services, L.L.C.), U.S. Timberlands Finance Corp. (n/k/a Fiber Finance Corp.), U.S. Timberlands Holdings Group, L.L.C. (n/k/a Cascade Resource Holding Group, L.L.C.).

² *Fox v. Christina Square Assoc.*, 1995 Del. Ch. LEXIS 89, at *5 (Del. Ch. June 19, 1995).

insignificant exception) is the same as the existing complaint and has been known to the defendants for some time. Given that trial is not scheduled until late June of this year, it seems that the defendants have ample time to discover any incidental, additional facts raised by these claims.

The court is, frankly, more concerned with the legal basis for one or more of the claims, in particular the claim for breach of contract that U.S. Bank now wants to assert against Yakima, which is not a signatory to the contract in question.

Nevertheless, while the legal sufficiency of some of these claims may be in doubt, the court will defer consideration of the question until the conclusion of discovery, at which point other motions will, no doubt, be presented. The court perceives no prejudice to the defendants in proceeding this way, since the dubious claims do not raise additional matters for discovery.

However, with respect to the claim for piercing the corporate veil, the assessment of prejudice is different. This claim involves factual allegations well beyond any other claim brought by U.S. Bank. To state a veil-piercing claim in Delaware, the plaintiff must plead facts supporting an inference that the company created a sham entity designed to defraud investors and creditors.³ Some of the factors that a court must consider when being asked to disregard the corporate form

³ See, e.g., *Crosse v. BCBSD, Inc.*, 836 A.2d 492, 497 (Del. 2003).

include: (1) whether the company was adequately capitalized for the undertaking; (2) whether the company was solvent; (3) whether corporate formalities were observed; (4) whether the dominant shareholder siphoned company funds; and (5) whether, in general, the company simply functioned as a facade for the dominant shareholder.⁴ This is a fact-intensive inquiry that goes well beyond any factual allegations that U.S. Bank has made to this point and would undoubtedly involve substantial discovery. For example, for U.S. Bank to prove that the U.S. Timberlands companies did not observe corporate formalities (or for the defendants to prove that the U.S. Timberlands companies *did* observe corporate formalities), the defendants will have to produce company books and records that go back several years, for several different companies. Such a production is obviously quite burdensome. In addition, the defendants were not put on notice that they would have to make such a production. Given the relatively late stage of this proceeding and the nearness of trial, the court finds it would unreasonably prejudice the defendants to permit the injection of veil-piercing issues into the case at this time. Of course, this ruling is without prejudice to the assertion of those claims in a later proceeding, if necessary.

⁴ *Harco Nat'l Ins. Co. v. Green Farms, Inc.*, 1989 Del. Ch. LEXIS 114, at *11 (Del. Ch. Sept. 19, 1989) (quoting *United States v. Golden Acres, Inc.*, 702 F. Supp. 1097, 1104 (D. Del. 1988)).

U.S. Bank Nat'l Assoc. v. U.S. Timberlands, et al.

C.A. No. 112-N

March 30, 2005

Page 5

In conclusion, to the extent that U.S. Bank seeks to add a claim for piercing the corporate veil, its motion to amend its complaint is denied. In all other respects, U.S. Bank's motion to amend its complaint is granted. U.S. Bank shall file its Third Amended Complaint in conformity with this order within 5 days.

IT IS SO ORDERED.

/s/ Stephen P. Lamb
Vice Chancellor