

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

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Re: *Beal Bank, S.S.B., et al., v. WestPoint Int'l, Inc., et al.*  
Civil Action No. 2617-CC

Dear Counsel:

For the reasons set forth below, after carefully examining the arguments presented by counsel, I am denying defendants' motions to dismiss without prejudice.

## I. BACKGROUND FACTS

In 1998, WestPoint Stevens Inc. (Stevens) obtained operating financing through a \$480 million credit agreement with numerous lenders. Stevens granted a first lien on certain of Stevens' real and personal property to those lenders.<sup>1</sup> Among the pledged collateral was all the capital shares of each domestic subsidiary as Stevens then owned or after acquired. As additional security for its First Lien Lenders, Stevens executed a Stock Pledge Agreement. This agreement further provided that:

Any or all of the Pledged Shares held by Pledgee [Beal Bank] may, if an Actionable Default has occurred and is continuing, without notice to Pledgor [International], be registered in the name of Pledgee or its nominee, and Pledgee or its nominee may thereafter without notice to Pledgor exercise all voting and corporate rights at any meeting with respect to the issuer of the Pledged Shares and exercise any and all rights of conversion, exchange, subscription or any other rights, privileges or options pertaining to any of the Pledged Shares as if it were the absolute owner thereof....<sup>2</sup>

On June 1, 2003, Stevens filed for bankruptcy. By no later than November 30, 2004, Stevens defaulted on its payment obligations. An automatic stay under 11 U.S.C. § 362, which applies in every bankruptcy case, prevented Beal Bank from exercising its right to register the pledged stock in Beal Bank's name or to foreclose on the property. An auction later ensued, and on July 8, 2005, the Bankruptcy Court entered a Sale Order authorizing the sale of substantially all of the assets of Stevens to WestPoint International, Inc. ("International").<sup>3</sup>

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<sup>1</sup> On June 6, 2005, Beal Bank was appointed to serve as the Administrative Agent under the credit agreement, the successor Collateral Trustee under the Collateral Trust Agreement, and the successor "Pledgee" under the Stock Pledge Agreement.

<sup>2</sup> WestPoint Int'l Inc. Defs.' Opening Br. in Supp. of Mot. to Dismiss Ex. 1 at 5.

<sup>3</sup> Neither the Asset Purchase Agreement nor the Sale Order specifically mentions International as the purchaser. Instead, the Asset Purchase Agreement refers to WS Textile Co., Inc. as the parent and Textile Co., Inc. as the purchaser. Further, the Sale Order refers to Textile Co., Inc. as the purchaser. The plaintiffs in their complaint and both parties in all briefs, however, refer to WestPoint International, Inc., through WestPoint Homes, Inc., as the purchaser. More importantly, all parties agree that WestPoint International, Inc. issued its shares as consideration, and it is against WestPoint International, Inc.'s securities that Beal Bank currently holds a replacement lien.

International, through its subsidiary WestPoint Home, Inc., agreed to pay cash to Stevens' Debtor in Possession. International further agreed to issue securities in International to First Lien Lenders and Second Lien Lenders of Stevens. To protect the value of these shares, International agreed to prepare a registration statement under the Securities Act as soon as reasonably practicable after the distribution date. Pursuant to the Sale Order and Asset Purchase Agreement, and after the entry of the Escrow Stipulation, the transaction closed on August 8, 2005.

Beal Bank appealed many of the provisions of the Sale Order, including those related to the purported release of their replacement liens and satisfaction of their claims. On November 16, 2005, the District Court vacated all portions of the Sale Order that purported to release liens or to satisfy claims of the objecting First Lien Lenders. Specifically, the court found that Beal Bank possessed replacement liens granted to the same extent, validity, and priority as the original liens. Thus, the replacement lien of the objecting First Lien Lenders attached to 73% of International's common stock.

While details of the asset purchase were being litigated, the directors of International proceeded with business as they saw fit. In November 2005, International took steps to restructure its corporate organization. By way of board resolutions and stockholder consents, the board effected the following changes: removing and reappointing the entire board; expanding the board and adding two new directors; staggering the directors' terms of office; requiring a two-thirds supermajority stockholder vote to remove any director—even for cause; requiring a two-thirds supermajority vote to amend any bylaw; and eliminating the stockholders' right to take action by written consent absent unanimous consent.

Further, on December 8, 2006, Beal Bank received notice that International had formed a special committee to determine whether it should issue preferred stock and, if so, on what terms. This committee recommended that International issue \$200 million of preferred stock to raise funds principally for acquisition of a foreign manufacturing facility. A shareholder vote for approval of the issuance was scheduled to take place at the annual meeting on December 20, 2006. Upon shareholder approval, the Icahn Group agreed to purchase half of the preferred shares, and the other First Lien Lenders were offered the opportunity to purchase the other \$100 million in preferred stock. Beal Bank moved for a temporary restraining order, which was denied, requesting that the meeting be postponed until this Court's adjudication of the right of Beal Bank to vote the pledged shares. Members of Beal Bank attended the meeting and attempted to vote, but were denied access. Voting shareholders approved the share issuance. Beal Bank and

other First Lien Lenders rejected the offer to purchase \$100 million in shares and, as a result, Icahn purchased all \$200 million preferred shares.<sup>4</sup>

The amended complaint states five claims. Count I alleges that the directors owe fiduciary duties to lienholders that should be recognized as equitable shareholders. Further, International's refusal to register the pledged shares in Beal Bank's name and Textile's refusal to deliver International proxies so that Beal Bank could vote and protect itself forced the objecting First Lien Lenders into a minority shareholder position. Thus, the Icahn controlling group owed a duty not to cause International to effect transactions that would benefit themselves at the expense of other shareholders. Defendants allegedly breached these duties by approving the 2005 amendments to International's certificate of incorporation and bylaws and by approving the share sale at the December 20, 2006 annual meeting. These actions entrenched the current directors, gave the controlling Icahn group power to elect six of ten directors, and diluted the value of Beal Bank's collateral. Count II further contends that all other defendants aided and abetted in breaches of fiduciary duties. Count III asserts a claim that International breached the Asset Purchase Agreement and the related Registration Rights Agreement by failing to register the International securities with the SEC. Count IV alleges that Textile converted plaintiffs' voting rights by declining to record the securities in Beal Bank's name and by declining to grant Beal Bank a proxy to vote Textile's shares. Finally, Count V declares that International's failure to record Beal Bank as record owner violated 6 *Del. C.* § 8-401(a).

## II. ANALYSIS

Delaware law is well-settled as to the standard applicable to a motion to dismiss under Court of Chancery Rule 12(b)(6). This Court must assume the truthfulness of all well-pled allegations of fact in the complaint and draw all reasonable inferences that flow from the face of the complaint in favor of the plaintiffs. In applying the standard, this Court "may consider the unambiguous terms of documents incorporated by reference in the complaint when the documents are integral to the plaintiff's claims."<sup>5</sup> "[C]onclusory statements without supporting factual averments [however] will not be accepted as true for the purposes of a motion to dismiss."<sup>6</sup> The motion will be granted if "it appears with

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<sup>4</sup> Holders of the new preferred stock would be granted the right to elect six of ten members of the board of directors.

<sup>5</sup> *Morgan v. Sample*, 914 A.2d 647, 662 (Del. Ch. 2007).

<sup>6</sup> *Grimes v. Donald*, 673 A.2d 1207, 1214 (Del. 1996).

reasonable certainty that, under any set of facts that could be proven to support the claims asserted, the plaintiffs would not be entitled to relief.”<sup>7</sup>

#### A. *WestPoint International Defendants*

As stated earlier, WestPoint International defendants assert numerous theories for dismissal. They contend: (1) that the asset sale failed to trigger Beal Bank’s right to record; (2) that defendant directors owed no fiduciary duties to Beal Bank because Beal Bank was a lienholder, not an “equitable shareholder;” and (3) that International never breached the Registration Rights Agreement by failing to register its securities with the SEC because the condition precedent to registration has not yet occurred.

The record before me lacks sufficient development to warrant dismissal at this stage. Neither party disputes that the Collateral Trust Agreement and the Stock Pledge Agreement provide that Beal Bank may register pledged shares of Stevens’ subsidiaries in Beal Bank’s name in the event of an actionable default. Likewise, neither party disputes that an actionable default occurred no later than 2004. Thus, it seems to me that the 2004 default should have triggered Beal Bank’s ability to exercise its right to have the shares registered in its name. Exercise of this right, however, seems to have been hindered by the automatic stay. In 2005, the Bankruptcy Court approved the sale of Steven’s assets to International and issued a Sale Order, which Beal Bank challenged. Through a series of orders from the Bankruptcy Court and the District Court, Beal Bank finally received a replacement lien on International securities “to the same extent, validity, and priority that they attached to the Purchased Assets immediately prior to the Closing.”<sup>8</sup> Neither Court, however, expressly explains what constitutes a replacement lien to the same extent, validity, and priority as Beal Bank possessed immediately before the closing. For example, does Beal Bank hold a lien against International securities with a conditional right to vote in the event of breach by International? That is, do the rights that Beal Bank had pursuant to the Stock Pledge Agreement transfer? Does Beal Bank hold a lien with a vested entitlement to have shares registered in its name and to vote those shares at International’s meetings? After all, at the time the Bankruptcy Court issued the Sale Order, an actionable default had occurred triggering Beal Banks right to record any of the pledged stock in its name and, but for the stay, Beal Bank could have registered the

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<sup>7</sup> *Morgan*, 914 A.2d at 662 (quoting *VLIW Tech., LLC v. Hewlett-Packard Co.*, 840 A.2d 606, 610-11 (Del. 2003)).

<sup>8</sup> WestPoint Int’l Inc. Defs.’ Opening Br. in Supp. of Mot. to Dismiss Ex. 5 at ¶ 5.

securities in its name. Or are both of these propositions incorrect, and instead Beal Bank only received a replacement lien that is the monetary equivalent of the previous lien?

The question of exactly what rights Beal Bank possessed in its replacement lien is best answered by the Bankruptcy Court and the District Court that originally determined Beal Bank's rights pursuant to the agreements and the bankruptcy sale. The answer to this question, however, directly influences my consideration of whether Beal Bank had the right to be listed as record shareholder, whether 6 *Del. C.* § 8-401 applies, and whether equity requires that International directors owe duties to Beal Bank. Without explicit knowledge of exactly what right plaintiffs possessed as a result of the Bankruptcy Sale Order and subsequent amendments, I am unable to adequately consider WestPoint International defendants' motion to dismiss. The motion to dismiss is denied in its entirety without prejudice.

#### *B. Special Committee Defendants*

The special committee defendants join in WestPoint International defendants' averments and further contend that the complaint should be dismissed as to them for additional reasons. First, defendants reiterate that the special committee directors do not owe any fiduciary duty to Beal Bank who is a lienholder, not a stockholder. Second, defendants allege that the amended complaint fails to give notice of an entire fairness claim, and that the director defendants, lacking a duty to plaintiffs, cannot be required to prove the entire fairness of the transaction. Instead, the committee's actions are protected by the business judgment rule. Plaintiffs, however, fail to allege any facts that suggest that defendants were interested or lacked independence or that the business decisions fell outside the realm of business judgment. Thus, only a duty of care claim remains. An exculpatory clause, however, protects the committee from personal liability as a result of breaches of the duty of care. As such, the argument goes, all claims against the special committee director defendants should be denied with prejudice.

For the reasons stated above, I deny, without prejudice, the special committee director defendants' motion to dismiss Count I based on their claim that they owe no fiduciary duty to Beal Bank. I am unable to determine whether the directors owed any fiduciary duties without first knowing what position or rights Beal Bank possesses as a result of the bankruptcy sale.

Second, I cannot agree with the special committee director defendants that the complaint fails to give notice of an entire fairness claim. This Court has previously held that “[a]ll that is required is that the complaint give ‘fair notice’ of [entire fairness] claims. A court undertaking that analysis must afford a liberal construction to the language of the pleading.”<sup>9</sup> The amended complaint provides such notice. Count 1 specifically alleges that the board made governance changes that “would entrench the current Board of Directors, cement the Icahn Controlling Shareholders’ control over [International], and depress the value of the [International] common stock to enhance the value of their own interests in [International].”<sup>10</sup> The complaint further alleges that “[n]o ‘compelling justification’ existed for the Directors and the Icahn Controlling Shareholders’ actions, nor were the corporate restructurings alleged above fair to the other shareholders of [International].”<sup>11</sup> Finally, the complaint alleges that “Directors and Icahn Controlling Shareholders were not acting in good faith, were not acting with honest belief that their actions were in the best interest the company or its shareholders other than themselves, wholly disregarded the best interest of [International] and the other shareholders in taking these actions, and acted disloyally to the other shareholders including Plaintiffs as equitable shareholders.”<sup>12</sup> Based on these and other statements throughout the complaint, I find that defendants had sufficient notice of the existence of an entire fairness claim. Again, the motion to dismiss is denied without prejudice.

IT IS SO ORDERED.

Very truly yours,

A handwritten signature in cursive script that reads "William B. Chandler III". The signature is written in black ink and is positioned above the printed name of the signatory.

William B. Chandler III

WBCIII:trm

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<sup>9</sup> *In re New Valley*, 2001 Del. Ch. LEXIS 13, at \*21 (Jan. 11, 2001) (quoting *Emerald Partners v. Berlin*, 726 A.2d 1215, 1220 (Del. 1999)).

<sup>10</sup> Compl. at ¶ 87.

<sup>11</sup> Compl. at ¶ 89.

<sup>12</sup> Compl. at ¶ 90.