

IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
20TH JUDICIAL DISTRICT, DAVIDSON COUNTY

KATHY HOLT WEEDMAN,)
JACK SANDERS HOLT, JANELLE)
HOLT, JUDY BAUMAN and)
DONNA ETHERIDGE,)

Plaintiffs,)

vs.)

No. 16-464-BC

SANDERS MANUFACTURING)
COMPANY, OWEN SANDERS,)
JAMES J. SANDERS III, ERIC)
O. SANDERS, and LOREN G.)
KIRKPATRICK,)

Defendants.)

**MEMORANDUM AND ORDER OF 12/11/17-12/13/17 TRIAL OF
FINDINGS OF FACT AND CONCLUSIONS OF LAW: (1) DISMISSING
PLAINTIFFS' REMAINING CLAIMS, AND (2) AWARDING SOME
INDEMNITY TO PLAINTIFFS AND TO DEFENDANT DIRECTORS**

This lawsuit was filed by five shareholders holding a minority interest in an approximately 20-shareholder corporation. The Plaintiffs' lawsuit is asserted to have been brought on behalf of the Defendant Corporation, Sanders Manufacturing Company, as a derivative claim. The Plaintiffs have sued the Corporation, and, as Individual Defendants, the chairman of the Corporation's board and two directors. These Individual Defendants/Officers are also shareholders.

By the time of trial the remaining relief sought by the Plaintiffs to be determined was

— whether a receiver should be appointed for the dissolution voluntarily underway by the Corporation, and

- recovery of attorneys fees and expenses the Plaintiffs have expended in this lawsuit.

The Defendants opposed appointment of a receiver and sought recovery of their attorneys' fees.

After considering the law and the evidence, it is ORDERED that the Plaintiffs' claim for appointment of a receiver is denied as unnecessary.

As to the attorneys' fees, it is ORDERED that the Plaintiffs' recovery of their attorneys fees pursuant to Tennessee Code Annotated 48-17-401 is, with one exception, denied on the grounds that the Plaintiffs' lawsuit has not conferred a benefit on the Defendant Corporation. The exception is that the Plaintiffs shall be awarded their attorneys fees for work performed by Plaintiffs' Counsel in filing and prevailing on the June 13, 2017 *Plaintiffs' Motion For Summary Judgment*.

It is further ORDERED that the claim of the Individual Defendants to recover attorneys' fees is granted, and the Defendant Company, pursuant to Tennessee Code Annotated section 48-18-503, shall indemnify the Defendant Directors for reasonable attorneys fees they incurred from June 13, 2017 through the December 13, 2017 conclusion of the trial of this case in defending against this lawsuit.

It is additionally ORDERED that to quantify the respective fees awarded above, by February 23, 2018, Counsel for each side shall file an affidavit, as required by Local Rule 5.05, stating the amount of fees they seek limited to the tasks and times for which attorneys fees are ordered above. Any opposition to the amount of the fees sought shall

be filed by March 9, 2018. A reply, if any, shall be filed March 16, 2018. Following that, the Court shall rule on the amounts on the papers.

The findings of fact and conclusions of law, on which the above orders are based are as follows.

Claims Tried

As noted at the outset, by the time of the December 11, 2017 trial, the lawsuit had been narrowed by motions for summary judgment to the issues of appointment of a receiver and each side seeking recovery of attorneys fees.¹ To obtain appointment of a receiver and recover attorneys' fees the wrongful conduct of the Defendants asserted by the Plaintiffs was twofold: (1) the Defendants had engaged in a conflict of interest transaction by adopting a February 11, 2016 Resolution and (2) Corporate Controller, Eric Sanders, had the Corporation pay the Individual Defendants' attorneys fees in connection with this litigation. The Defendants sought recovery of their attorneys fees as indemnification. Here is an outline of the claims.

¹ The Plaintiffs, the Defendant Company, and the Defendant Directors each filed motions for summary judgment. They were granted in part in three separate rulings denominated A, B and C as follows: **(A)** *Memorandum And Order: (1) Granting In Part And Denying In Part Defendants' Motion For Summary Judgment, And Denying Plaintiffs' Request For Judgment As A Matter Of Law; (2) Denying Defendants' 11/30/16 Motion To Recover Subpoena Costs; And (3) Setting 2/10/17 Deadline To Schedule Telephone Conference, February 2, 2017; (B)* *Memorandum And Order: (1) Granting Plaintiffs' Summary Judgment Motion That Defendants Have Not Complied With T.C.A. § 48-18-504(c) And 506 And Enjoining Advanced Fees; And (2) Setting 6/23/17 Deadline To Schedule Rule 16 Conference To Select Trial Date, June 13, 2017; and (C)* *Memorandum And Order Ruling On Defendant Company's Motion For Summary Judgment Seeking To Dismiss All Claims Of March 29, 2017 First Amended Complaint, October 30, 2017.*

1. Conflicting Interest Transaction – Plaintiffs’ claim for a declaratory judgment nullifying a February 11, 2016 Resolution adopted by the Defendant Company on the grounds that the Resolution constituted a director’s conflicting interest transaction (paragraphs 1, 10 and 12 of the Prayer For Relief of the March 29, 2017 *First Amended Complaint*);
2. Judicial Supervision of Dissolution – Plaintiffs’ claim for voluntary dissolution of the Defendant Company to proceed with the appointment of a receiver as provided in Tennessee Code Annotated section 48-24-301(4) and 303 (paragraph 4 of the Prayer For Relief of the Dissolution Action of the March 29, 2017 *First Amended Complaint*); and
3. Competing Claims For Attorneys Fees – Each side, Plaintiffs and Defendants, asserted they were entitled to recovery of attorneys fees because the other side’s claims lacked merit and prosecution of the claims did not confer a benefit on the Company.

At the conclusion of the presentation of Plaintiffs’ evidence, the conflicting interest transaction claim, item 1 above, was dismissed under Tennessee Civil Procedure Rule 41.02. The December 13, 2017 *Memorandum And Order Granting In Part Defendants’ Rule 41.02 Motion For Involuntary Dismissal* and the January 3, 2018 *Memorandum And Order Denying Oral Motion At Trial To Reconsider Rule 41.02 Dismissal Of Paragraphs 1, 10, & 12 Of The First Amended Complaint Pertaining To Conflicting Interest Transaction Claims* are incorporated herein by reference.

A full trial was then conducted on items 2 and 3 above – appointment of a receiver and recovery of attorneys fees. At the conclusion of the evidence, the Court took the matter under advisement. On these claims provided below are the findings of fact and conclusions of law.

Findings of Fact and Conclusions of Law

Appointment of a Receiver Denied

The Plaintiffs' claim at trial for appointment of a receiver during voluntary dissolution pursuant to Tennessee Code Annotated sections 48-24-301(4) and 303 consisted of two alleged bad acts taken by the Defendant Directors. One of the alleged bad acts was the February 2016 Resolution adopted by the Defendant Company. This was the claim the Court dismissed under Rule 41.02 at the conclusion of Plaintiffs' presentation of evidence. This alleged bad act, having been dismissed, furnishes no basis for appointment of a receiver.

The other bad act alleged by Plaintiffs to justify appointment of a receiver was payment by Eric Sanders, the Company Comptroller until July 2017 and now the President of the Defendant Company, of the attorneys fees being incurred by the Defendant Directors in this litigation. A ruling in part had already been granted on this claim prior to trial on summary judgment. The Court found that the Defendants had not complied with the statutory requirements to advance fees but reserved for trial a determination of intent and remedy, quoting the summary judgment ruling as follows.

It is therefore ORDERED that the Plaintiffs' motion for summary judgment is granted with respect to items 2 and 5 above to the extent that the Court concludes as a matter of law that the Defendants have not complied with Tennessee Code Annotated sections 48-18-504(c) and 48-18-506.

With respect to the remedy for failing to comply with the requirements of Tennessee Code Annotated section 48-18-504(c) and 48-18-506, it is ORDERED that the Defendant Corporation is enjoined and prohibited from advancing fees and expenses to pay the defense of the Individual Defendant Directors in this case until further order of the Court.

With respect to the remainder of 2 above, asserting personal liability of the Individual Defendant Directors for damages to the Corporation and seeking recovery of damages for fraudulent concealment, and with respect to the relief sought in requests 3, 4, and 7(a) above, for summary judgment on personal liability of the Individual Defendant Directors, fraudulent concealment, conversion, Eric Sanders breach of office and receipt of an improper benefit, all of these requests for relief concern conduct involving wrongful intent. Whether such intent exists in this case presents genuine issues of material fact precluding entry of summary judgment. Further precluding entry of summary judgment at this time is that because the degree of culpability can not be determined on summary judgment nor can the scope and kind of reimbursement remedy be determined. That is, the nature of the remedy depends on the degree of culpability. Additionally, the outcome of the other aspects of the case, not before the Court on summary judgment, affect whether damages are recoverable or a set-off. It is therefore ORDERED that Plaintiffs' motion for summary judgment on personal liability of the Individual Defendant Directors, fraudulent concealment, conversion, Eric Sanders breach of office and receipt of an improper benefit is denied.

Memorandum And Order: (1) Granting Plaintiffs' Summary Judgment Motion That Defendants Have Not Complied With T.C.A. § 48-18-504(c) And 506 And Enjoining Advanced Fees; And (2) Setting 6/23/17 Deadline To Schedule Rule 16 Conference To Select Trial Date, pp. 8-9 (June 13, 2017).

At trial the Defendant's evidence consisted of the testimony of Eric Sanders. He was the Company Comptroller until July 2017 and then President. The Court finds Mr. Eric Sanders' testimony to have been forthright, reasonable and credible.

Additionally, these facts were established at trial, in general, about Mr. Eric Sanders' competent conduct as Controller and President, which distinguishes this case from *May v. Scott*, 388 F. Supp. 2d 828 (W. D. Tenn. 2005) cited by Plaintiffs. There also was Mr. Eric Sanders' testimony specifically about the Corporation advancing payment to the Defendants of their attorneys' fees.

As to Mr. Eric Sanders' conduct in general the Court finds the proof demonstrated that he acted in a number of instances in the best interests of the Company and competently in:

- interviewing and selecting a broker to market the Company real estate,
- obtaining \$3.5 million for the real estate, a higher price than expected,
- investing \$2.5 million in 10 different CD ladders with different maturity dates for flexibility with the dissolution,
- negotiating with the new buyer staying at the location rent-free until June 2017,
- obtaining an assumption of the 3-year lease that had to be entered into to operate marketing division until sold,
- accounts payable and payroll of marketing division paid off,
- providing monthly financial statements to shareholders by mail,
- providing to shareholders on all sales of Company assets, LOIs, meetings, votes, settlement statements,
- spending as little as possible to attend trade shows,

- not seeking to be paid a noncompete fee from buyers of Company assets.

With respect to the specific act of not complying with Tennessee Code Annotated sections 48-18-504 and 506 in authorizing the Company to pay the litigation costs of the Defendant Directors, the Court accredits Mr. Eric Sanders' testimony that he believed, upon advice of Counsel, that his execution of a guarantee/written affirmation, pursuant to Tennessee Code Annotated section 48-18-504(a) that he was acting in good faith and would repay the advance if ultimately it was determined he was not to be indemnified, was all that was required. Upon advice of Counsel, he was unaware of the incorporation in section 48-18-504(c) of the requirements of section 48-18-506.

In addition the Court finds that the evidence presented by the Plaintiffs of the testimony of shareholder/Plaintiff Judy Bauman and board of director's member Sam Weedman did not undercut or detract from Mr. Eric Sanders' testimony. The testimony of Ms. Bauman and Mr. Weedman corroborated the previous June 13, 2017 summary judgment that the Company advancing attorneys fees to the Defendant Directors did not comply with section 48-18-506. Their testimony, however, did not overcome Mr. Eric Sanders' credibility that he acted upon advice of Counsel, without malice, design or bad faith, in authorizing the Company to advance payment of attorneys' fees to the Defendant Directors, because he believed all that was required to do this was execution under section 48-18-504(a) of a written affirmation/guarantee.

Further, as to Mr. Sam Weedman's testimony that a receiver during dissolution is needed because Mr. Eric Sanders wants to delay dissolution, hold onto the Company so

funding of the retirement plan (the “SERP”) can be delayed for Mr. Eric Sanders (age 57) to come of age to participate in the SERP was denied by Mr. Eric Sanders. Such a delay is inconsistent with the above findings on Mr. Sanders, and the delay is not accredited by the Court.

Based upon these findings, the Court concludes that the then Comptroller Eric Sanders’ payment of the Directors’ attorneys fees in the litigation from May 4, 2016, to June 23, 2017, without complying with Tennessee Code Annotated sections 48-18-504(c) and 48-18-506, does not constitute fraudulent concealment or conversion,² was not done maliciously or in bad faith and was based upon advice of Counsel. Under these circumstances and with the Rule 41.02 dismissal of the other alleged wrongful conduct of Defendants, appointment of a receiver is not warranted. Instead a procedure, earlier instituted,³ where the Defendant must give 21 days’ notice of funding the SERP is sufficient.

Indemnification to Plaintiffs

Based upon the foregoing findings of fact and conclusions of law, and the June 13, 2017 summary judgment, the Court concludes that it is appropriate under Tennessee

² The causes of action of fraudulent concealment or conversion are not listed as a cause of action in the First Amended Complaint, and Plaintiffs were denied filing a Second Amended Complaint. The causes of action are referred to in Plaintiffs’ briefing and, therefore, are dealt with in this ruling.

³ On February 27, 2017, the Court Ordered, “Nevertheless, to maintain the status quo on the pending retirement plan issues in this case and so as not to render the Plaintiffs’ claims ineffectual prior to their disposition, it is ORDERED that 21 days prior to funding the retirement with proceeds from the sale of the company’s real estate, the Defendants shall file a notice with the Court and opposing Counsel of their intention to fund the retirement plan with the sale proceeds. This will provide the Plaintiffs an opportunity to seek extraordinary relief if they need to do so with respect to the funding of the retirement plan.”

Code Annotated section 48-17-401(d)(1) for the Defendant Company to reimburse the Plaintiffs for the attorneys fees they expended in support of the June 13, 2017 summary judgment that resulted in the determination that the Defendant Company was not complying with Tennessee Code Annotated section 48-18-506 in advancing fees.

Indemnification to Defendants

Additionally, the Court concludes that it is appropriate under Tennessee Code Annotated section 48-18-505(2) for the Defendant Company to indemnify the Defendant Directors for the reasonable attorneys fees they incurred, from June 14, 2017 through the December 13, 2017 conclusion of the trial, in defending against this lawsuit. This conclusion is based upon the foregoing findings; the December 13, 2017 Rule 41.02 dismissal and the subsequent January 3, 2018 *Memorandum And Order Denying Oral Motion At Trial To Reconsider Rule 41.02 Dismissal Of Paragraphs 1, 10, & 12 Of The First Amended Complaint Pertaining To Conflicting Interest Transaction Claims*; and the February 2, 2017 and October 30, 2017 summary judgments.

As succinctly outlined in the October 30, 2017 summary judgment ruling, the great majority of Plaintiffs' claims were dismissed on summary judgment in February 2017. Further, Plaintiffs' motion to amend was futile, failed to state a claim and moot. *See Memorandum And Order Denying Plaintiffs' Amended Motion To Amend* (Nov. 13, 2017). Of the two remaining issues for trial, the alleged February 2016 Conflict of Interest transaction was dismissed on a Rule 41.02 motion. Further, a less drastic and narrowly tailored alternative then proceeding to trial on the alleged February 2016

Conflict of Interest transaction would have been, instead, for Plaintiffs' Counsel at the commencement of the litigation to seek a mandatory temporary injunction, along the lines ordered by the Court *sua sponte*, for notice to be given to the shareholders if there was to be funding of the SERP.

On the other legal issue – Company advancement of attorneys fees to the Individual Defendants – the Court has found the Plaintiffs did not entirely prevail because the advancement was done based upon advice of Counsel and that the harm of noncompliance with section 48-18-506 was mitigated by the guarantees executed by the Defendant Directors. In sum, except for halting the Company advancement of the litigation fees being incurred by the Defendant Directors without complying with section 48-18-506, the derivative litigation of the Plaintiffs has conferred no benefit on the Company.

/s/ Ellen Hobbs Lyle
ELLEN HOBBS LYLE
CHANCELLOR
TENNESSEE BUSINESS COURT
PILOT PROJECT

cc by U.S. Mail, email, or efile as applicable to:

William B. Hawkins III
Eric G. Evans
Ronald H. Pursell
Edward Hadley
James P. Catalano