IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

FLETCHER INTERNATIONAL, LTD., Plaintiff, v. ION GEOPHYSICAL CORPORATION, f/k/a INPUT/OUTPUT, INC., ION INTERNATIONAL S.àr.l., JAMES M. LAPEYRE, BRUCE S. APPELBAUM, THEODORE H. ELLIOTT, JR., FRANKLIN MYERS, S. JAMES NELSON, JR., ROBERT P. PEEBLER, JOHN SEITZ, G. THOMAS MARSH and NICHOLAS G. VLAHAKIS, Defendants.	)	Civil Action No. 5109-VCP

MEMORANDUM OPINION

Submitted: January 19, 2010
Decided: May 28, 2010

Edward P. Welch, Esquire, Paul J. Lockwood, Esquire, SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP, Wilmington, Delaware; *Attorneys for Plaintiff*

Kenneth J. Nachbar, Esquire, R. Judson Scaggs, Jr., Esquire, Samuel T. Hirzel, Esquire, Albert J. Carroll, Esquire, MORRIS, NICHOLS, ARSHT & TUNNELL LLP, Wilmington, Delaware; *Attorneys for Defendants*

PARSONS, Vice Chancellor.

In a letter opinion issued on March 24, 2010, I examined part of Fletcher International, Ltd.'s ("Fletcher") motion for partial summary judgment relating to the issuance of a convertible promissory note (the "ION S.àr.l. Note") by ION Geophysical Corporation ("ION") through its wholly-owned subsidiary ION International S.àr.l. ("ION S.àr.l.").[1] In that opinion, I denied Fletcher's motion "insofar as it could be construed as a request for a preliminary injunction effectively invalidating ION's issuance of the ION S.àr.l. Note or requiring that ION repay funds borrowed under that Note," but reserved judgment on certain other issues raised by Fletcher's motion.[2] This Memorandum Opinion addresses those issues.

Specifically, this Court now must determine (1) whether Fletcher has a contractual right to consent to the issuance of any security by a subsidiary of ION, (2) whether the ION S.àr.l. Note is such a security and, if it is, whether ION violated Fletcher's rights by issuing it without first seeking Fletcher's consent, and (3) whether ION's board of directors breached their fiduciary duty to Fletcher by failing to seek Fletcher's timely consent to issuance of the ION S.àr.l. Note or disclose material facts to Fletcher in connection with that Note.

Having examined the language of the relevant documents and finding no ambiguity, I hold that Fletcher does have a contractual right to consent to the issuance of

---

1 *See Fletcher Int'l, Ltd. v. ION Geophysical Corp.*, 2010 WL 1223782 (Del. Ch. Mar. 24, 2010).

2 *Id.* at *2.

any security—as that term is defined under Delaware and federal law—by a subsidiary of ION. Additionally, after examining the features of the ION S.àr.l. Note, particularly its convertibility feature, I conclude that it is a security of ION S.àr.l. that was issued by ION S.àr.l. Therefore, I hold that ION violated the terms of Section 5(B)(ii) of the Certificates of Rights and Preferences governing Fletcher's preferred stock by issuing the Note without Fletcher's consent. Finally, because Fletcher's claims against ION's board of directors for breach of fiduciary duty in connection with the issuance of the ION S.àr.l. Note seek to remedy the same conduct complained of in Fletcher's claim for breach of contract, I grant summary judgment for Defendants on that claim.

I. BACKGROUND

A. The Parties

Plaintiff, Fletcher, is a Bermuda corporation and the beneficial owner of all outstanding Series D Preferred Stock of ION.

Defendant ION is a technology-focused seismic solutions company organized in Delaware.[3] Defendant ION S.àr.l. is a Luxembourg private company. Defendants also include members of ION's board of directors, namely, James M. Lapeyre, Bruce S. Appelbaum, Theodore H. Elliott, Jr., Franklin Myers, S. James Nelson, Jr., Robert P.

---

[3] ION provides advanced seismic data acquisition equipment, seismic software and seismic planning, processing, and interpretations services to the global energy industry. Pl.'s Op. Br. ("POB") 3. Similarly, I refer to Defendants' Answering Brief as "DAB."

Peebler, John Seitz, G. Thomas Marsh, and Nicholas G. Vlahakis (collectively, the "Director Defendants").

B. Facts

Beginning on February 15, 2005, and pursuant to the terms of an agreement between Fletcher and ION on that date, Fletcher purchased 30,000 shares of Series D-1, 5,000 shares of Series D-2, and 35,000 shares of Series D-3 Cumulative Convertible Preferred Stock of ION.[4] Fletcher completed its last purchase in February 2008 and remains the sole holder of all outstanding Series D Preferred Stock.[5]

The Certificates of Rights and Preferences for the Series D-1, D-2, and D-3 Preferred Stock (the "Certificates") establish the rights, preferences, privileges, and restrictions of holders of that stock. Section 5(B)(ii) of the Certificates provides, in pertinent part, that:

> The Holders shall have the following voting rights . . . The consent of Holders of at least a Majority of the Series [D-1, D-2, and D-3] Preferred Stock [respectively], voting separately as a single class with one vote per share, in person or by proxy, either in writing without a meeting or at an annual or a special meeting of such Holders called for the purpose, shall be necessary to: . . . *permit any Subsidiary of [ION] to issue or sell, or obligate itself to issue or sell, except to [ION] or any wholly owned Subsidiary, any security of such Subsidiaries*.[6]

---

4 *See* POB Ex. B at 36.

5 *Id*.

6 POB Ex. A § 5(B)(ii) (emphasis added).

On October 23, 2009, ION issued a press release announcing, among other things, that ION had caused the issuance of two convertible promissory notes to BGP, Inc. ("BGP"), including the ION S.àr.l. Note, under its amended credit facility as one of several transactions intended to lead to the formation of a joint venture between ION and BGP (the "BGP Transactions").[7] Before the BGP Transactions closed on March 25, 2010, the amount of money drawn down under the ION S.àr.l. Note was convertible into shares of ION common stock at the discretion of the holder of the Note.[8] After closing, however, the then-outstanding principal amounts due under the Note were to be converted automatically into shares of ION common stock unless the holder elected otherwise.[9]

---

[7] *See* POB Exs. G, H. Under the terms of ION's amended credit facility, the loans of all lenders party thereto must be repaid *pro rata*. DAB Ex. 7 at Ex. 10.1 §§ 2.10 & 2.16. Unanimous approval of all of the lenders under that credit facility would have been required to amend the provision to permit the repayment of only the ION S.àr.l. Note. *Id.* at Ex. 10.1 § 10.02(b)(iv).

The sixth and most recent amendment to the credit facility added up to $40 million of additional borrowing capacity and allowed the Bank of China to join that facility. DAB Ex. 16. Following this amendment, and in connection with the BGP Transactions, ION issued a $30 million note to the Bank of China, secured by its assets and those of its domestic subsidiaries, and ION S.àr.l. received the remaining $10 million available under the credit facility in exchange for the ION S.àr.l. Note, which is secured by assets owned by it, ION, and ION's other subsidiaries. Aff. of David L. Roland, Esq. ¶ 12.

[8] *See* POB Ex. I at Ex. 4.3 § 6. When the BGP Transactions closed, the Bank of China had advanced $10 million to ION S.àr.l. under the Note. *See* DAB 11, Ex. 18.

[9] *See* POB Ex. I at Ex. 4.3 § 6(e). In connection with the ION S.àr.l. Note, ION "granted warrants . . . that are exercisable to purchase ION shares of common

C. Procedural History

Fletcher filed a complaint on November 25, 2009. On December 23, 2009, it moved for partial summary judgment on Counts I and II of the complaint. Fletcher amended the complaint on January 14, 2010.[10] After briefing, I heard argument on Fletcher's motion for partial summary judgment on January 19, 2010.

Due to the impending closing of the BGP Transactions, I issued a letter opinion on March 24, 2010, denying Fletcher's motion for summary judgment insofar as it sought to invalidate the issuance of the ION S.àr.l. Note or require ION to repay funds borrowed under that Note.

D. Parties' Contentions

The Complaint asserts eight counts against ION, ION S.àr.l., and the Director Defendants, including claims for breaches of contract and fiduciary duty.[11] The pending motion, however, deals only with the first two of those counts.

---

stock at $2.80 per share." DAB 11, Ex. 16. The warrants were issued in the money and have remained in the money since that time. Tr. 68-69.

[10] The Verified Amended Complaint (the "Complaint") is, thus, the operative complaint in this action. Though the Complaint was amended after Fletcher moved for partial summary judgment, Counts I and II were not affected.

[11] Specifically, the Complaint seeks declarative, injunctive, and monetary relief for ION's breach of the Certificates (Count I), Director Defendants' breach of their fiduciary duties (Count II), ION S.àr.l.'s aiding and abetting Director Defendants' breach of fiduciary duties (Count III), ION S.àr.l.'s tortious interference with ION's Certificates (Count IV), ION's tortious interference with Fletcher's contractual or prospective business relations (Count V), ION's breach of the Certificates regarding the ARAM transaction (Count VI), Director Defendants' breach of fiduciary duty regarding the ARAM transaction (Count VII), and ION's breach of contract requiring indemnification (Count VIII).

In Count I, Fletcher avers that, under Section 5(B)(ii) of the Certificates, ION cannot issue securities of its subsidiaries through any of those subsidiaries without Fletcher's consent and that ION violated that provision by unilaterally permitting ION S.àr.l. to issue the Note. In Count II, Fletcher argues that the Director Defendants breached their fiduciary duties of loyalty by failing to (1) provide Fletcher with a timely and meaningful vote on the issuance of the Note and (2) disclose all material facts concerning the ION S.àr.l. Note.[12]

Defendants contend that Fletcher's motion must be denied as to Count I because the ION S.àr.l. Note is not a security as that term is used in Section 5(B)(ii) of the Certificates. In this regard, Defendants first argue that the parties intended "security" to include only equity securities. Second, they claim that, when analyzed under the *Reves* "family resemblance" test and viewed in the context in which it was issued, the Note represents nothing more than a commercial loan.[13] Third, Defendants suggest the motion for summary judgment should be denied because Fletcher did not provide the only reasonable interpretation of "security." Defendants also urge denial of summary judgment on Count II because there is no difference between Fletcher's breach of contract and breach of fiduciary duty claims.

---

[12] Fletcher contends that the undisclosed facts include, "at a minimum, the material facts regarding the BGP Transactions, of which the ION S.àr.l. Note is a part." Compl. ¶ 68.

[13] *See Reves v. Ernst & Young*, 494 U.S. 56 (1990).

II. ANALYSIS

A. Standard for Summary Judgment

The standard for summary judgment is well-known. To succeed on such a motion, the moving party must show that there is "no genuine issue as to any material fact" and that it is entitled to judgment as a matter of law.[14] When the issue involves interpretation of a contract, "summary judgment is appropriate only if the contract in question is unambiguous."[15] Because "the threshold inquiry . . . is whether the contract is ambiguous," the Court generally will grant summary judgment if the moving party establishes that its construction "is the *only* reasonable interpretation."[16]

With this standard in mind, I first analyze Fletcher's claim as it relates to Count I by examining Section 5(B)(ii) of the Certificates to determine if the meaning of "any security" in that provision is ambiguous and, if it is not, whether the ION S.àr.l. Note fits within the meaning of that term.

B. Did ION Violate Fletcher's Rights by Issuing the ION S.àr.l. Note Without Seeking Fletcher's Consent (Count I)?

Fletcher contends that, under Section 5(B)(ii) of the Certificates, ION must obtain Fletcher's consent before an ION subsidiary may issue "any security" of that subsidiary.

---

[14] *See* Ct. Ch. R. 56; *see also Judah v. Del. Trust Co.*, 378 A.2d 624, 632 (Del. 1977); *Twin Bridges Ltd. P'ship v. Draper*, 2007 WL 2744609, at *8 (Del. Ch. Sept. 14, 2007) (citing Ct. Ch. R. 56(c)); *Schick Inc. v. Amalgamated Clothing & Textile Workers Union*, 533 A.2d 1235, 1239 n.3 (Del. Ch. 1987) (citing *Kennedy v. Silas Mason Co.*, 334 U.S. 249, 257 (1948)).

[15] *United Rentals, Inc. v. RAM Hldgs., Inc.*, 937 A.2d 810, 830 (Del. Ch. 2007).

[16] *Id*.

There is no dispute that ION S.àr.l. is a subsidiary of ION.[17] The parties do contest, however, whether the ION S.àr.l. Note fits within the ambit of a "security" as that term is used in the Certificates. A preferred stockholder's rights are primarily contractual in nature, and the "construction of preferred stock provisions are matters of contract interpretation for the courts."[18] Thus, before determining what "any security" means, I review briefly some pertinent principles of contract interpretation.

While the ultimate goal of contract interpretation is to give effect to the parties' shared intent,[19] Delaware adheres to the "objective" theory of contracts and its courts interpret the language of a contract as it "would be understood by an objective, reasonable third party."[20] As such, I must endeavor to determine not only what "the parties to the contract intended it to mean, but what a reasonable person in the position of the parties would have thought it meant."[21]

---

17 Tr. 4 ("[I]t is a stipulated fact between the parties that [ION S.àr.l.] is a subsidiary for purposes of [Section 5(B)(ii) of the Certificates].").

18 *Matulich v. Aegis Commc'ns Gp., Inc.*, 942 A.2d 596, 600 (Del. 2008).

19 *Sassano v. CIBC World Mkts. Corp.*, 948 A.2d 453, 462 (Del. Ch. 2008) (citing *Matulich v. Aegis Commc'ns Gp., Inc.*, 2007 WL 1662667, at *4 (Del. Ch. May 31, 2007)).

20 *NBC Universal, Inc. v. Paxson Commc'ns Corp.*, 2005 WL 1038997, at *5 (Del. Ch. Apr. 29, 2005).

21 *Rhone-Poulenc Basic Chems. Co. v. Am. Motorists Ins. Co.*, 616 A.2d 1192, 1196 (Del. 1992) (citing *Hallowell v. State Farm Mut. Auto. Ins. Co.*, 443 A.2d 925, 926 (Del. 1982)); *see also Eagle Indus., Inc. v. DeVilbiss Health Care, Inc.*, 702 A.2d 1228, 1232 (Del. 1997) ("Contract terms themselves will be controlling when they establish the parties' common meaning so that a reasonable person in the position

Because "[l]anguage in a vacuum may take on any number of meanings,"[22] the Court examines contractual language in the context of the document "as a whole" and "give[s] each provision and term effect, so as not to render any part of the contract mere surplusage."[23] Indeed, a court will "more readily assign contract language its intended meaning if it reads the language at issue within the context of the agreement in which it is located."[24]

This Court ordinarily allows the plain meaning of a contract to control, unless it is ambiguous.[25] Importantly, "the language of an agreement . . . is not rendered ambiguous simply because the parties in litigation differ concerning its meaning."[26] The Court need only find ambiguity where the contested provisions are "reasonably or fairly susceptible

---

of either party would have no expectations inconsistent with the contract language.").

22 *USA Cable v. World Wrestling Fed'n Entm't, Inc.*, 2000 WL 875682, at *8 (Del. Ch. June 27, 2000).

23 *Kuhn Constr., Inc. v. Diamond State Port Corp.*, 2010 WL 779992, at *2 (Del. Mar. 8, 2010).

24 *USA Cable*, 2000 WL 875682, at *8 ("Accordingly, while the canons of contract interpretation instruct an examination of the explicit contract language in order to determine the clause's meaning, one must simultaneously read that language within the context of the contract surrounding that language in order to best elicit the most appropriate meaning.").

25 *Chambers v. Genesee & Wyo., Inc.*, 2005 WL 2000765, at *5 (Del. Ch. Aug. 11, 2005).

26 *City Investing Co. Liquid. Trust v. Cont'l Cas. Co.*, 624 A.2d 1191, 1198 (Del. 1993).

of different interpretations or may have two or more different meanings."[27] Thus, unambiguous words in a contract, though undefined, typically are given their ordinary meaning unless multiple, reasonable interpretations exist.[28] With these principles in mind, I turn to the language of the Certificates at issue here.

1. Is the phrase "any security" in Section 5(B)(ii) ambiguous?

The Certificates do not define "any security," as that phrase is used in Section 5(B)(ii), nor did the parties discuss the meaning of that phrase during negotiations.[29] Nevertheless, Fletcher argues that the term is unambiguous and must be viewed as co-extensive with the statutory definition of security under Delaware and federal law. To support this interpretation of "any security," Fletcher notes that, in their respective definition sections, the Certificates define "Other Securities" as "any *stock . . . and other securities* of" ION.[30] While not directly applicable to Section 5(B)(ii), that definition, according to Fletcher, reflects an understanding that "the term 'securities' [as used in that Section, encompasses] something beyond stock because the definition includes the phrase

---

27 *Rhone-Poulenc*, 616 A.2d at 1196; *see also E.I. du Pont de Nemours & Co., Inc. v. Allstate Ins. Co.*, 693 A.2d 1059, 1061 (Del. 1997) ("Contract language is not ambiguous simply because the parties disagree on its meaning."); *Chambers*, 2005 WL 2000765, at *5.

28 *See Rhone-Poulenc*, 616 A.2d at 1196; *Gildor v. Optical Solutions, Inc.*, 2006 WL 4782348, at *5 (Del. Ch. June 5, 2006).

29 *See* Tr. 7; DAB Ex. 1 at 70-72.

30 POB Ex. A § 5(B)(ii) (emphasis added).

'and other securities' in addition to any stock."[31] I find Fletcher's interpretation reasonable because the disputed term "security" is used in the context of a contract prescribing the rights of holders of preferred stock in a publicly-traded corporation, over which the securities laws cast a long shadow.

Defendants initially countered Fletcher's argument by asserting that, based on the parties' course of conduct and the business context in which the Certificates were drafted, "any security" must be interpreted to mean only "equity securities." Specifically, Defendants argued that Section 5(B)(ii) was intended to address only the sale of equity of an ION subsidiary (which could dilute the value of Fletcher's investment), not debt (which would not). Defendants did not, however, point to any cases or evidence indicating that their narrow, idiosyncratic interpretation is reasonable, consistent with the plain meaning of the phrase "any security," or in line with Fletcher's understanding of that phrase at the time the parties entered into the Certificates. Moreover, the definition of "Other Securities" in the Certificates contradicts even Defendants' subjective interpretation by indicating that the parties understood that term to encompass more than simply equity securities when they drafted those documents.[32]

---

31 POB 17.

32 Defendants do acknowledge that the parties "broadly [defined the phrase 'Other Securities'] to capture any type of . . . securities." DAB 26. Indeed, by the time of the argument on Fletcher's motion, Defendants effectively abandoned their contention that "any security" means "any *equity* security."

But, even if I accepted Defendants' unsupported claim that they subjectively understood Section 5(B)(ii) to include only equity securities, it would be immaterial because I must interpret "any security" objectively. In that regard, the evidence suggests that a reasonable person in the position of the parties likely would have understood the term "any security" to include instruments generally recognized to be securities under federal and state securities statutes and regulations. Defendants did not present any reasonable, alternative definition. Therefore, I hold that "security" is not ambiguous and must be afforded its ordinary meaning as it has developed under federal and state law.

2. Is the ION S.àr.l. Note a "security"?

Even under this definition, however, the question remains whether a convertible promissory note, like the ION S.àr.l. Note, is indeed a security. Fletcher acknowledges that certain classes of notes are not securities, but contends that notes that are convertible into stock unquestionably meet the definition of a "security" under both Delaware and federal law. In response, Defendants claim that, under the *Reves* "family resemblance" test, the ION S.àr.l. Note is not a security because the commercial context in which the Note was issued indicates that it was, in reality, nothing more than a commercial bank loan.[33] In this regard, Defendants minimize the importance of the Note's convertibility feature as "simply a mechanism designed" to allow this "loan" to be more conveniently

---

[33] *See Reves v. Ernst & Young*, 494 U.S. 56, 63 (1990).

unwound if the BGP Transactions failed to close.[34] For the reasons addressed below, I find Defendants' argument unpersuasive and hold that, as a debt instrument convertible into equity securities, the ION S.àr.l. Note qualifies as a "security" under Section 5(B)(ii) of the Certificates.

The United States Supreme Court held in *Reves v. Ernst & Young* that all notes presumptively fall within the definition of a "security."[35] This presumption can be rebutted only by showing that a particular note bears a strong resemblance to one of a judicially crafted list of categories of instruments that are not securities.[36] To determine if a strong resemblance exists, a court must examine (1) the motivations that would prompt a reasonable seller and buyer to enter into the transaction, (2) the plan of distribution of the instrument, (3) the reasonable expectations of the investing public, and (4) the existence of some factor that significantly reduces the risk of the instrument, thus

---

[34] DAB 20. Specifically, Defendants claim that the ION S.àr.l. Note was made convertible into ION stock to protect ION from any *pro rata* repayment requirements that might arise under the Amended Credit Facility if the BGP Transactions did not close. Roland Aff. ¶ 13.

[35] 494 U.S. 56, 65 (1990). The *Reves* test was adopted by the Delaware Supreme Court in *Boo'ze v. State*, 2004 WL 691903, at *2-3 (Del. 2004).

[36] The types of notes generally not considered securities include [1] a "note delivered in consumer financing, [2] [a] note secured by a mortgage on a home, [3] [a] short-term note secured by a lien on a small business or some of its assets, [4] [a] note evidencing a 'character' loan to a bank customer, [5] short-term notes secured by an assignment of accounts receivable, or [6] a note which simply formalizes an open-account debt incurred in the ordinary course of business (particularly if, as in the case of the customer of a broker, it is collateralized)." 494 U.S. at 65 (quoting *Exch. Nat'l Bank v. Touche Ross & Co.*, 544 F.2d 1126, 1138 (2d Cir. 1976)).

rendering application of the securities statutes unnecessary.[37] *Reves* emphasized, however, that when examining these four factors, courts should remember that the "fundamental essence of a 'security' [is] its character as an 'investment.'"[38]

Though *Reves* clearly applies to instruments solely evidencing debt, the convertibility feature of the ION S.àr.l. Note may eliminate the need to examine that instrument under the "family resemblance" test. Indeed, some courts have held convertible notes to be securities without any apparent examination under *Reves*.[39] Other courts have applied the *Reves* factors and, predictably, found a convertible note to be a security.[40]

In this case, the hybrid nature of the ION S.àr.l. Note, which its holder could convert at any time into common stock of ION, strongly supports finding it to be a security under Delaware and federal securities law.[41] Moreover, even considering the

---

37 *Id*. at 66-67.

38 *Id.* at 68-69.

39 *See In re Juniper Networks, Inc. Secs. Litig.*, 542 F. Supp. 2d 1037, 1053 (N.D. Cal. 2008); *Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 395 (Del. 1996).

40 *See Leemon v. Burns*, 175 F. Supp. 2d 551, 559 (S.D.N.Y. 2001) ("The fact that the Note's original principal could be converted into . . . common stock is a strong factor for holding that the Note is a security.").

41 The investment in the ION S.àr.l. Note apparently was conceived initially as a bridge loan from the Bank of China to ION S.àr.l. in connection with the BGP Transactions. According to the terms of ION's amended credit facility, under which the Note was issued, however, the anticipated repayment of the Note at closing would have triggered certain *pro rata* repayment requirements. *See supra* note 7. Considering that option undesirable, the parties to the BGP Transaction included a convertibility function in the Note to avoid the repayment requirement.

ION S.àr.l. Note under the "family resemblance" test, I hold it to be a security because the Note is most naturally understood as an investment in ION, rather than a purely commercial or consumer transaction. The Note is "freely assignable and transferable" by its holder, convertible into common shares of a publicly traded company, and subject to an investment risk, even if that risk is arguably small.[42] These factors all support the conclusion that the ION S.àr.l. Note is an "investment," as that term is used in *Reves*, and, thus, a security.[43] Furthermore, when I compare it to the judicially crafted list of notes that are clearly not securities, I find that the ION S.àr.l. Note "neither fits into . . . nor bears a strong family resemblance to any of those categories."[44] Thus, I hold that the Note is a security as that term is used in Section 5(B)(ii) of the Certificates.[45]

When the Note was issued, it was understood that, as the Note's holder, the Bank of China almost certainly would exercise its right to convert it into ION common stock because the option to convert was issued in the money. *See supra* note 9. As Brian Hanson, CFO of ION, stated in his deposition: "I think absolutely the Chinese . . . will exercise their conversion rights [to convert the Note into shares of ION common stock] . . . prior to having their . . . rights expire." Tr. 68-69. Hanson further declared that "the intent behind the bridge loan . . . was to advance the equity investment" reflected in the BGP Transactions. *Id*. at 69-70.

42 *See Reves*, 494 U.S. at 68-69; DAB Ex. 17 at Ex. 4.3 § 4.

43 *See supra* note 38.

44 *Leemon*, 175 F. Supp. 2d at 559.

45 This conclusion is buttressed by the fact that the ION S.àr.l. Note was issued with a legend that begins: "THE SECURITIES REPRESENTED BY THIS CONVERTIBLE PROMISSORY NOTE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933 . . . ." DAB Ex. 17 at Ex. 4.3. Such a legend is required whenever a security is sold pursuant to an exception to the registration requirements of the Securities Act of 1933 ("Securities Act"). *See* 17 C.F.R. § 230.144A(d)(2) ("The seller and any person acting on its behalf [must

Defendants add another wrinkle to this analysis, however. Specifically, they argue that issuance of the ION S.àr.l. Note does not violate Section 5(B)(ii) because the Note is convertible into shares of ION, not ION S.àr.l.[46] According to this argument, because the Note is convertible into ION's common stock, it must be considered a security of ION, and because ION did not need Fletcher's consent to issue its own securities under the Certificates, Fletcher's voting rights were not violated. Fletcher responds that, even though the ION S.àr.1 Note contains an option allowing it to be converted into shares of ION stock, the Note is still a security of ION S.àr.l. because it issued the Note. I agree with Fletcher in this regard.

By its terms, the ION S.àr.l. Note closely resembles an option contract whereby ION S.àr.l. grants the holder of the Note an option to voluntarily convert the amount drawn down under that Note into shares of ION common stock. Generally, an option to

---

take] reasonable steps to ensure that the purchaser is aware that the seller may rely on the exemption from the provisions of section 5 of the Act provided by this section" in order for the exemption to apply). The Note also states that "[i]n the event of any proposed transfer . . . the Issuer may require . . . that it receive reasonable transfer documentation that is sufficient to evidence that such proposed transfer complies with the Securities Act and other applicable state and foreign securities laws." DAB Ex. 17 at Ex. 4.3. While it may be true, as Defendants suggest, that the legend was added by the lawyers negotiating the terms of the ION S.àr.l. Note simply out of "an abundance of caution," *see* Tr. 54-55, its inclusion nevertheless evidences Defendants' own recognition that the Note could be viewed by investors and regulators as a security subject to the Securities Act.

[46] Defendants base this argument on the facts that, according to the Certificates, ION does not need Fletcher's consent to issue its own securities and need only seek such consent when one of its subsidiaries issues "any security *of such Subsidiaries*." POB Ex. A § 5(B)(ii) (emphasis added).

purchase an equity security—like the ION S.àr.l. Note—is itself a security.[47] Additionally, at least some courts have held that options should be considered securities of the entity issuing them.[48] One basis for treating options as a security of the entity issuing them, as opposed to the entity issuing the underlying securities, is that options and their underlying securities are frequently sold on different markets and constitute separate financial products.

Here, the ION S.àr.l. Note, though convertible into securities of ION, was issued by ION S.àr.l., which received the benefit and bore the burden of issuing that Note. I, therefore, find that the Note is a security of ION S.àr.l. and hold that ION violated Fletcher's consent rights when it allowed its subsidiary to issue such a security without first seeking Fletcher's consent.

---

47 *See, e.g.*, 15 U.S.C. § 78c; *Fry v. UAL Corp.*, 84 F.3d 936, 938 (7th Cir. 1996) (citing *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 750-51 (1975) ("A contract to purchase or sell securities is expressly defined . . . as a purchase or sale of securities for the purposes of [the Securities Act].")); *United States v. Nacchio*, 573 F.3d 1062, 1065 n.2 (10th Cir. 2009); *S.E.C. v. Am. Commodity Exch., Inc.*, 546 F.2d 1361, 1366 (10th Cir. 1976).

48 *See Fry*, 84 F.3d at 938 ("Puts and other stock options are securities within the meaning of the Securities Exchange Act, but they are not necessarily (or in this case) securities issued by the corporation that issued the underlying securities, the subject of the option contracts.") (internal citations omitted). *But see Gudmundsson v. United States*, 665 F. Supp. 2d 227, 235-36 (W.D.N.Y. 2009) (deeming the purchase of a plain vanilla stock option to be a purchase of the underlying security for purposes of section 16(b) of the Securities Exchange Act).

C. Did the Director Defendants Breach Their Duty of Disclosure (Count II)?

Having determined that ION violated Fletcher's consent rights by issuing the ION S.àr.l. Note, I next turn to Fletcher's motion for summary judgment on Count II.

Fletcher claims that the Director Defendants breached their fiduciary duties to Fletcher as a preferred stockholder by failing to (1) provide Fletcher with a timely, meaningful, and informed vote in connection with the issuance of the ION S.àr.l. Note or (2) disclose fully and fairly all material information within the board's control in connection with issuance of the ION S.àr.l. Note. Defendants urge the Court to deny summary judgment on Count II, claiming that there is no difference between Fletcher's contractual and fiduciary duty claims, all of which stem from Section 5(B)(ii) of the Certificates and the same alleged wrongdoing.[49] I agree with Defendants' contention.

The Director Defendants' failure to seek Fletcher's consent before issuing the ION S.àr.l. Note implicates rights defined by the Certificates as opposed to those that may be defined by fiduciary duty principles. Also, the Director Defendants premised their decision not to disclose material information in connection with issuance of the ION S.àr.l. Note on their belief that Fletcher was not entitled to vote on that transaction. Whether that decision was right or wrong, the Director Defendants acted on the basis of their interpretation of Section 5(B)(ii) of the Certificates. Therefore, any fiduciary duty

---

[49] Defendants also argue that, to the extent the meaning of "security" in Section 5(B)(ii) of the Certificates is ambiguous, Fletcher's motion for partial summary judgment as to Count II must be denied. Based on my holding *supra* Part II.B, I reject this argument.

claims asserted by Fletcher based on an alleged violation of either the duty of loyalty or the "duty of disclosure" arise out of and are superfluous to the breach of contract claims raised in Count I.[50] As such, I grant summary judgment in favor of Defendants as to Count II.[51]

---

[50] The so-called "duty of disclosure" is not a distinct fiduciary duty but is "a specific application of the general fiduciary duty owed by directors." *Malone v. Brincat*, 722 A.2d 5, 10 (Del. 1998). It has been characterized as a "combination of" or "derivative of" the fiduciary duties of care and loyalty. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1163, 1166 (Del. 1995). *But see Jackson Nat. Life Ins. Co. v. Kennedy*, 741 A.2d 377, 388-89 (Del. Ch. 1999) ("The duty of disclosure is merely a specific application of the more general fiduciary duty of loyalty that applies only in the setting of a transaction or other corporate event that is being presented to the stockholders for action.").

[51] *Sun-Times Media Gp., Inc. v. Black*, 954 A.2d 380, 388 (Del. Ch. 2008) ("The reality of filing a motion for summary judgment is that the moving party is asking the court to make a judgment and if 'the court concludes that the moving party is not entitled to summary judgment, and the state of the record is such that the nonmoving party clearly is entitled to such relief, the [court] may grant final judgment in favor of the nonmoving party.'") (quoting *Bank of Del. v. Claymont Fire Co. No. 1*, 528 A.2d 1196, 1199 (Del. 1987)).

The rights of preferred stockholders are primarily contractual in nature.[52] Yet, while a board of directors does not owe fiduciary duties to preferred stockholders to the same extent as common stockholders, that is not to say that such duties are nonexistent or that preferred stockholders only may seek to hold directors liable for violation of explicit contractual duties. Indeed, "it has been recognized that directors may owe duties of loyalty and care" to preferred stockholders, particularly in cases where nonexistent contractual rights leave "the holder of preferred stock [in an] exposed and vulnerable position vis-à-vis the board of directors."[53] Thus, if preferred stockholders "share a right

---

[52] *See HB Korenvaes Invs., L.P. v. Marriott Corp.*, 1993 WL 205040, at *5 (Del. Ch. June 9, 1993) ("The special rights, limitations, etc. of preferred stock are created by the corporate charter or certificate of designation which acts as an amendment to a certificate of incorporation. Thus, to a very large extent, to ask what are the rights of the preferred stock is to ask what are the rights and obligations created contractually by the certificate of designation. In most instances, given the nature of the acts alleged and the terms of the certificate, this contractual level of analysis will exhaust the judicial review of corporate action challenged as a wrong to preferred stock.") (citing *Rothschild Int'l Corp. v. Liggett Gp., Inc.*, 474 A.2d 133, 136 (Del. 1984); *Ellingwood v. Wolf's Head Oil Refining Co.*, 38 A.2d 743, 747 (Del. 1944); *In re Appraisal of Metromedia Int'l Gp., Inc.*, 971 A.2d 893, 899 (Del. Ch. 2009); *Shanghai Power Co. v. Del. Trust Co.*, 316 A.2d 589, 593 (Del. Ch. 1974); *Judah v. Del. Trust Co.*, 401 A.2d 932 (Del. 1979)).

[53] *See LC Capital Master Fund, Ltd. v. James*, 2010 WL 892065, at *10 (Del. Ch. Mar. 8, 2010) (citing *HB Korenvaes*, 1993 WL 205040, at *5; *Harbinger Capital P'rs Master Fund I, Ltd. v. Granite Broad. Corp., DS*, 906 A.2d 218, 224 (Del. Ch. 2006)).

There is, however, no established rule clearly answering whether a board of directors "does or does not owe fiduciary duties of loyalty to the holders of preferred stock." *HB Korenvaes*, 1993 WL 205040, at *6. As such, answering that question "demands reference to the particularities of context to fashion a sound reply." *Id.* (citing *Porges v. Vadsco Sales Corp.*, 32 A.2d 148 (Del. Ch. 1943); *MacFarlane v. N. Am. Cement Corp.*, 157 A. 396 (Del. Ch. 1928)); *see also*

equally with the common shareholders the directors owe the preferred shareholders the same fiduciary duties they owe the common shareholders *with respect to those rights*."[54] For instance, directors owe preferred stockholders a duty to disclose material information in connection with common voting rights.[55] But, rights arising from documents governing a preferred class of stock, such as the Certificates, that are enjoyed solely by that preferred class, do not give rise to fiduciary duties because such rights are purely contractual in nature.[56]

Even when directors do owe fiduciary duties to preferred stockholders, however, if claims for breach of such duties are based on the same facts underlying a breach of contract claim and relate to "rights and obligations expressly provided by contract," then

---

LC Capital Master Fund, 2010 WL 892065, at *11 (noting that, as with the common stockholders, directors owe preferred stockholders fiduciary duties as applied in *Revlon* and its progeny); *Jackson Nat. Life Ins. Co.*, 741 A.2d at 387 ("[T]he right to a fair allocation of proceeds is one shared by the common and preferred stockholders and is a right that implicates the fiduciary duty of loyalty.").

54 *MCG Capital Corp. v. Maginn*, 2010 WL 1782271, at *15 (Del. Ch. May 5, 2010) (citing *Jedwab v. MGM Grand Hotels, Inc.*, 509 A.2d 584, 594 (Del. Ch. 1986)).

55 *HB Korenvaes*, 1993 WL 205040, at *5. Generally, "[a] board of directors seeking stockholder approval of a specific corporate action must disclose all material facts relating to the requested action so that stockholders can make an informed decision." *Jackson Nat. Life Ins. Co.*, 741 A.2d at 389 n.19 (citing *Zirn v. VLI Corp.*, 621 A.2d 773 (Del. 1993)); *Gantler v. Stephens*, 965 A.2d 695, 703 (Del. 2009) ("It is well-settled law that 'directors of Delaware corporations [have] a fiduciary duty to disclose fully and fairly all material information within the board's control when it seeks shareholder action.'") (citing *Stroud v. Grace*, 606 A.2d 75, 84 (Del. 1992); *In re Staples, Inc., S'holders Litig.*, 792 A.2d 934, 953-54 (Del. Ch. 2001)).

56 *MCG Capital*, 2010 WL 1782271, at *15.

such claims are "superfluous."[57] As a result, unless the fiduciary duty claims are based on duties and rights *not* provided for by contract, a plaintiff cannot maintain both contractual and fiduciary duty claims arising out of the same alleged wrongdoing.[58]

In this case, Fletcher's right to vote on an ION subsidiary's issuance of securities is provided for in Section 5(B)(ii) of the Certificates and, as a result, is "essentially contractual" in nature.[59] Because Fletcher can remedy the violation of that voting right through its breach of contract claim, it has no need to assert a fiduciary duty claim based on the same contractual consent rights. Additionally, the duty to disclose material information to preferred stockholders in connection with the right to vote is premised on there actually being a vote. Here, the Director Defendants determined that Fletcher was

---

57 *See Blue Chip Capital Fund II Ltd. P'ship v. Tubergen*, 906 A.2d 827, 833 (Del. Ch. Aug. 22, 2006); *MCG Capital*, 2010 WL 1782271, at *15 ("[W]hen preferred shareholders assert fiduciary claims that relate to obligations expressly treated by their unique contractual rights with the corporation, the Court will review those claims as breach of contract claims and the claims for breach of fiduciary duty will be dismissed as superfluous.") (citing *Nemec v. Shrader*, 2009 WL 1204346, at *4 (Del. Ch., Apr. 30, 2009), *aff'd*, 2010 WL 1320918 (Del. 2010)); *Gale v. Bershad*, 1998 WL 118022, at *1 (Del. Ch. Mar. 4, 1998) ("[B]ecause the contract claim addresses the alleged wrongdoing by the board, any fiduciary duty claim arising out of the same conduct is superfluous."); *see also Madison Realty P'rs 7, LLC v. Ag ISA, LLC*, 2001 WL 406268, at *6 (Del. Ch. Apr. 17, 2001) (dismissing fiduciary duty claim because it overlapped completely with plaintiff's contract claim, asserting identical conduct as the basis for both claims).

58 *Madison Realty*, 2001 WL 406268, at *6; *Gale*, 1998 WL 118022, at *5 ("To allow a fiduciary duty claim to coexist in parallel with [a contractual] claim, would undermine the primacy of contract law over fiduciary law in matters involving . . . contractual rights and obligations.").

59 *See Gale*, 1998 WL 118022, at *5.

not entitled to vote based on their interpretation of the Certificates and, not surprisingly, saw no need to disclose information to Fletcher in connection with the BGP Transactions. But whether or not that decision was correct, it is inextricably intertwined with Fletcher's claim that Defendants breached the Certificates. Any remedy for Defendants' conduct may thus be obtained under Count I, and there is no need for an overlapping breach of fiduciary duty claim. Therefore, I grant summary judgment on Count II in favor of Defendants.

III. CONCLUSION

For the foregoing reasons, I grant Fletcher's motion for summary judgment on Count I to the extent it seeks declaratory judgment that Section 5(B)(ii) of the Certificates is valid and binding on ION and that ION breached its obligations under that section by permitting ION S.àr.l. to issue the ION S.àr.l. Note without first obtaining Fletcher's consent.[60] Additionally, I deny Fletcher's motion on Count II and, instead, grant summary judgment on that claim in favor of Defendants.

IT IS SO ORDERED.

---

[60] For the reasons stated in the letter opinion issued on March 24, 2010, I denied various other forms of relief Fletcher sought based on Count I. *See Fletcher Int'l, Ltd. v. ION Geophysical Corp.*, 2010 WL 1223782, at *2 (Del. Ch. Mar. 24, 2010). The Complaint also seeks damages and a permanent injunction based on the breach of the Certificates alleged in Count I. Those aspects of Fletcher's claims were not the subject of its motion for partial summary judgment, however, and I express no opinion regarding them.