

HARRY C. NEEL, MICHAEL JENKINS,
and LEE CAVANAUGH, Individually and
Derivatively on Behalf of THE
STONYCREEK VALLEY
DEVELOPMENT CORPORATION,

Plaintiffs,

v.

DANIEL DIVELY, and THE
STONYCREEK VALLEY
DEVELOPMENT CORPORATION,

Defendants.

IN THE COURT OF COMMON PLEAS OF
SOMERSET COUNTY, PENNSYLVANIA

NO. 275 Civil 2019

PRELIMINARY OBJECTIONS
TO PLAINTIFFS' FIRST
AMENDED COMPLAINT

For Plaintiffs: John Paul Regan, Esq.
Brian T. Must, Esq.
For Defendant Dively: David T. Leake, Esq.
Andrew Snyder, Esq.
For Defendant Stonycreek
Valley Development
Corporation: James R. Cascio, Esq.
Argument: December 5, 2019

RECEIVED
FEB 28 2020

2020 FEB 27 AM 11:38
PROthonotary
RECORD

MEMORANDUM

This matter comes before us on Defendants' Preliminary Objections to Plaintiffs' First Amended Complaint, which are overruled in part and sustained in part for the reasons detailed in the following memorandum.

Factual and Procedural History

Plaintiffs Harry C. Neel, Michael W. Jenkins, and Lee E. Cavanaugh, individually and on behalf of the Stonycreek Valley Development Corporation ("SVDC"), initiated the instant action

Certified to be true and
correct copy of the original
Document on file in
this office.
[Signature]
Prothonotary

by filing a complaint on April 17, 2019.¹ SVDC is a Non-Profit Cooperative Corporation that oversaw the construction of Lake Stonycreek and currently governs the surrounding residential community. See, Amend. Compl. ¶¶ 6, 12-13. Prior to its re-incorporation as a non-profit, SVDC was a stock-share basis for-profit corporation permitting shareholders a right to vote on a one-vote-per-share basis. Id. ¶ 59. That basis was retained after re-incorporation in 2005, and shares were available for purchase for \$10.00 per share. Id. ¶¶ 60, 73.

Plaintiffs contend that in 2018, the Board, including Defendant Daniel Dively (“Dively”) misused proxy-voting by distributing the majority shareholder’s shares to themselves, ensuring that they retained their seats on the Board. Id. ¶ 68. After entrenching their positions, Plaintiffs allege that in February of 2019, the Board proposed an amendment to SVDC’s By-Laws that would replace the shareholders’ *one-vote-per-share* with cumulative voting rights with a *one-vote-per-shareholder* voting system without cumulative voting. Id. ¶ 71. After attempting to purchase shares during the week of March 8, 2019, Plaintiffs Neel and Jenkins were informed for the first time that the Board passed a moratorium on the sale of shares. Id. ¶¶ 74-79. Plaintiffs allege that SVDC’s By-Laws prohibited the Board from ceasing the transfer of shares more than 50 days prior to the vote on the proposed amendment on April 27, 2019 and without giving shareholders 10 days notice. Id. at ¶¶ 81-86; Pls.’ Ex. C, Art. VIII, § 4. Plaintiffs contend that the Board instituted such a moratorium to ensure that its’ proposed amendment passed. Id. at ¶ 79.

Nevertheless, the proposed amendment was ultimately denied during the April 27, 2019 special meeting. Id. ¶¶ 87-88. After the vote, however, a family member of a director motioned to vote on a new and separate amendment to the Bylaws that would replace the *one-vote-per-share*

¹ We granted Plaintiffs’ Consented Motion for Leave of Court to Amend Complaint on July 2, 2019. Plaintiffs filed their Amended Complaint on July 11, 2019.

with cumulative voting system with a *one-vote-per-lot-owner* without cumulative voting system. Id. ¶¶ 89-90. Plaintiffs allege that the Board did not provide prior notice that the motion would be discussed at the special meeting, that the motion was not proposed by the adoption of the Board or proposed by a member entitled to cast at least 10 percent of the votes, and that the motion was not filed with the secretary of the corporation. Id. ¶¶ 91-95. Nonetheless, the motion was included among a list of amendments, collectively entitled “Enclosure A,” to be voted on in the annual meeting on May 24, 2019. Id. at ¶ 99. According to Plaintiffs, Enclosure A was ultimately passed because it provided that SVDC would redeem its shares at \$10 per share. Id. ¶¶ 101, 105. Plaintiffs allege that the amendment was not properly proposed pursuant to SVDC’s By-Laws and Pennsylvania statutory law, and that the amendment was not filed with the Pennsylvania Department of State after it was approved. Id. ¶¶ 97, 109. In addition, Plaintiffs also aver that the new one-vote-per-lot-owner voting system discriminates against shareholders who are not lot owners. Id. ¶ 110.

Plaintiffs also allege that Dively, as a member of SVDC’s Board of Directors and owner of Dirt Bottom Excavating, Inc. (“Dirt Bottom”), engaged in self-dealing by rendering Dirt Bottom’s services to SVDC for a fee. Id. ¶¶ 27-31. In order to obtain the service contracts, Plaintiffs allege that Dively manipulated SVDC’s bidding process either “by drafting requested scopes of service favorably to his business, by undercutting known bids, or by discussing the splitting of a contract for his services into amounts that fall below SVDC’s threshold that triggers automatic sealed bidding for contracts.” Id. ¶ 37. Plaintiffs further aver that Dively threatened and intimidated residents and shareholders who questioned his conduct. Id. ¶ 39. Plaintiffs contend that such self-interested dealings harmed SVDC and deprived its shareholders of the right to obtain the lowest-priced services. Id. ¶ 40.

On March 20, 2019, Plaintiffs voiced their concerns in a letter to the Board about certain actions taken in violation of SVDC's By-Laws and the Nonprofit Corporation Law of 1988 ("NPCL"). Id. ¶ 19; Ex. A. After receiving no response, shareholders made a demand on the Board requesting that they appoint a Special Litigation Committee to investigate the allegations contained in the letter. Amend. Compl. ¶ 21; Ex. B. The Board again did not respond. Amend. Compl. ¶ 24. In addition, Plaintiffs allege that over a two-year period, the Board ignored over two dozen written demands to inspect corporate records. Id. at ¶ 48. If the Board did respond to a request, the shareholders were provided incomplete and outdated information. Id. at ¶ 49.

Plaintiffs' Amended Complaint asserts direct and derivative claims for breach of fiduciary duties and direct and derivative claims for violations of the NPCL. Both SVDC and Dively filed preliminary objections to the Amended Complaint.² We find that based on Plaintiffs' averments, Defendants' Preliminary Objections shall be sustained in part and overruled in part. We consider these objections in seriatim.

Standard of Review

The standard for preliminary objections in the nature of a demurrer is as follows:

Preliminary objections in the nature of a demurrer test the legal sufficiency of the complaint. When considering preliminary objections, all material facts set forth in the challenged pleadings are admitted as true, as well as all inferences reasonably deducible therefrom. Preliminary objections which seek the dismissal of a cause of action should be sustained only in cases in which it is clear and free from doubt that the pleader will be unable to prove facts legally sufficient to establish the right to relief. If any doubt exists as to whether a demurrer should be sustained, it should be resolved in favor of overruling the preliminary objections.

² Defendant Daniel Dively's Preliminary Objections to Plaintiffs' First Amended Complaint was filed on July 31, 2019. Stonycreek Valley Development Corporation's Preliminary Objections under Pa.R.C.P. 1028 was filed on November 1, 2019.

Defendant Dively's Preliminary Objections

- I. Preliminary Objection Pursuant to Rule 1028(a)(4) – Count III of Plaintiff's Amended Complaint must be dismissed for legal insufficiency (Demurrer) as to Dively individually.

Count III is a direct and derivative claim for alleged “Violations of the Nonprofit Corporation Law of 1988.” Amend. Compl. at 20. Without any supporting case law or analysis, Dively argues for the dismissal of Count III pursuant to Pa.R.C.P. 1028(a)(4) because: (1) Count III does not contain averments against him individually; (2) it is unclear what cause of action is being brought; and (3) Plaintiffs lack standing. Dively Brief at 4. We address the standing issue first.

Standing

The NPCL provides that a director owes a fiduciary relation to the corporation and shall perform his duties “in good faith, in a manner he reasonably believes to be in the best interest of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances.” 15 Pa.C.S.A. § 5712(a). Because a director’s duty is owed to the corporation, it may only be enforced by the corporation or in a derivative action on behalf of the corporation. 15 Pa.C.S.A. § 5717.

However, the protection afforded to officers and directors against direct suits under section 5717 does not apply where another section of the NPCL dealing with parties suing to enforce their own rights is involved. White v. Assocs. in Counseling & Child Guidance, Inc., 767 A.2d 638, 643 (Pa. Commw. Ct. 2001). Specifically, section 5793(a) provides that “[u]pon application of any person aggrieved by any corporate action, the court may hear and determine the validity of the corporate action.” 15 Pa.C.S.A. § 5793(a). “Corporate action” includes “[t]he taking of any action

on any matter that is required under this subpart or under any other provision of law to be, or that under the bylaws may be, submitted for action to the members, directors, members of an other body or officers of a nonprofit corporation.” 15 Pa.C.S.A. § 5791(a). “Act” or “action” includes the failure to act. 15 Pa.C.S.A §§ 102, 5103. “A litigant can establish that he or she has been ‘aggrieved’ by such a corporate action by showing a substantial, direct, and immediate interest in the outcome of the litigation in order to be deemed to have standing.” Petty v. Hosp. Serv. Ass’n of Ne. Pennsylvania, 967 A.2d 439, 448 (Pa. Commw. Ct. 2009), affd., 611 Pa. 119, 23 A.3d 1004 (2011).

A. Inspection of Corporate Records

Plaintiffs first argue that the Board, including Dively, violated Section 5508 of the NPCL when it refused to answer dozens of written demands to inspect SVDC’s corporate Records. Pls.’ Brief at 8. Section 5508 of the NPCL provides that any member of a nonprofit corporation has a right to examine, upon request, certain corporate records for any proper purpose. 15 Pa.C.S.A. § 5508(b). The inspection of corporate records in order to ascertain whether a corporation is being properly managed is a reasonable purpose. Hurst v. Shaw, 121 Pa. Cmwlth. 1, 9, 549 A.2d 1349, 1352 (1988). “If the corporation, or an officer or agent thereof, refuses to permit an inspection sought by a member... the member may apply to the court for an order to compel the inspection.” 15 Pa.C.S.A. § 5508(c). SVDC’s By-laws also state that “[e]very shareholder shall have a right to examine...the share register, books or records of account, and records of the proceedings of the shareholders and directors, and make extracts there from.” Pls.’ Ex. C.

Taking the allegations in the Amended Complaint as true, there is no question that Plaintiffs have standing to ask this Court to compel the inspection of SVDC’s corporate records. See, 15 Pa.C.S.A. § 5508(c). Here, Plaintiffs made over two-dozen written demands on the Board to

inspect corporate records and information regarding the management, accounting, operation, voting audits, and voting records of SVDC. Compl. ¶ 48. Such demands are indeed a proper purpose under section 5508. See, Hurst, 549 A.2d at 1352. The Board did not honor many of those demands, and when it did, it provided incomplete information. Id. ¶ 49. Therefore, Plaintiffs have established that they have a substantial, direct, and immediate interest in the inspection of corporate records in which they are entitled under section 5508 of the NPCL and SVDC's Bylaws. See, 15 Pa.C.S.A. § 5793(a).

B. Discrimination in the Sale of Shares

Plaintiffs' next argue that the Board, including Dively, violated sections 5505 and 5751 by failing to provide a ten-day notice of its moratorium on the sale of shares during the fifty-day period preceding the Special Meeting and by implementing the discriminatory practice of allowing some people to purchase shares, but not others. Pls.' Brief at 8. Section 5505, entitled "persons bound by bylaws," provides that:

Except as otherwise provided by section 5713 (relating to personal liability of directors) or any similar provision of law, bylaws of a nonprofit corporation shall operate only as regulations among the members, directors, members of an other body and officers of the corporation, and shall not affect contracts or other dealings with other persons, unless those persons have actual knowledge of the bylaws.

15 Pa.C.S.A. § 5505. SVDC's Bylaws provide that the Board "may fix a time, not more than fifty days, prior to the date of any meeting of shareholders...or the date when any change or conversion or exchange of shares will be made or go into effect, as a record date for the determination of the shareholders entitled to notice of, or vote at, any such meeting...or to exercise such rights as the case may be...." Pl.s Ex. C, Art. VIII, § 4. The Bylaws further provide that the Board must give shareholders ten days notice before ceasing the sale of shares. Id.

In this case, fifty-days prior to the Special Meeting, scheduled for April 27, 2019, would have been March 8, 2019. Amend. Compl. ¶ 84. Plaintiffs allege that they attempted to purchase additional shares during the following week of March 11, 2019. Id. ¶¶ 74, 76. At that point, they were informed for the first time that a moratorium on the sale of shares had been passed, except for individuals owning no shares. Id. ¶¶ 75-76. Plaintiffs never received written notice of the moratorium. Id. ¶ 84.

In addition to never receiving written notice, Plaintiffs allege that the Board's moratorium on the sale of shares violated section 5751 by discriminating between current shareholders and potential-future shareholders. Id. ¶ 86. Pls.' Brief at 8. Section 5751 provides that, "[u]nless otherwise provided by a bylaw adopted by the members: [t]here shall be one class of members whose voting and other rights and interests shall be equal..." 15 Pa.C.S.A. § 5751(a). We find that Plaintiffs have alleged sufficient facts to support the inference that they have been aggrieved by the Board's decision to institute a moratorium on the sale of shares in violation of section 5751 and SVDC's Bylaws.

Improper Amendment of the By-laws/Discriminatory Voting

Finally, Plaintiffs argue that the amendment implementing a *one-vote-per-lot-owner* voting system was not proposed consistent with section 5912 of the NPCL, nor was it filed with the Department of State pursuant to section 5916. Pls.' Brief at 8. In addition, Plaintiffs allege that the current voting system likewise violates section 5751 by treating shareholders of the same class disparately by permitting shareholders who are lot owners a right to vote while denying that right to shareholders who are not lot owners. Id.

Section 5912, entitled “[p]roposal of amendments,” provides in relevant part:

(a) General rule.--Every amendment of the articles of a nonprofit corporation shall be proposed:

- (1) by the adoption by the board of directors or other body of a resolution setting forth the proposed amendment;
- (2) unless otherwise provided in the articles, by petition of members entitled to cast at least 10% of the votes that all members are entitled to cast thereon, setting forth the proposed amendment, which petition shall be directed to the board of directors and filed with the secretary of the corporation; or
- (3) by such other method as may be provided in the bylaws.

15 Pa.C.S.A. § 5912(a). That section also provides that the articles proposed to be amended must set forth the existing text with brackets around language that is to be deleted and underscoring language that is to be added, or provide that the articles be amended as fully set forth therein. 15 Pa.C.S.A. § 5912(c).

As discussed supra, following the vote to deny the Proposed Amendment on April 27, 2019, a family member of a current Board member motioned to vote on a new amendment that would implement a one-vote-per-lot owner voting system without cumulative voting. Amend. Compl. ¶ 89. That motion was not proposed by a petition of members entitled to cast at least 10-percent of the votes, was not adopted by the Board, and there was no prior notice that the motion would be discussed. Id. ¶¶ 91-95. Nevertheless, the motion was included in a list of amendments, entitled “Enclosure A,” voted on, and approved at an Annual Meeting on May 24, 2019. Id. ¶ 89, 99, 105. Enclosure A did not contain the language of the proposed amendment, the existing text that it proposed to be amended, or the proposed articles, as amended, set forth in full. Id. ¶ 98. In addition, the amendment was never filed with the Pennsylvania Department of State. Id. ¶ 109.

Keeping the stringent standard for sustaining a demurrer in mind, we read the Amended Complaint to support the showing that, among other things, Dively is a member of the SVDC Board of Directors, the Board improperly used proxy votes, knew of the demands to inspect corporate records but voted to ignore them, instituted a discriminatory practice of selling shares, and used a one-vote-per-lot-owner voting system in violation of the NPCL. See, Amend. Compl. at ¶¶ 5, 27, 49, 69, 149, 152. The allegations, if taken as true, support the inference that the Board's actions or inactions were inconsistent with the NPCL and SVDC's Bylaws. Therefore, the Board, including Dively, is not entitled to the protection against direct suits afforded to it by section 5717. See, White, 767 A.2d at 643. Accordingly, Dively's first preliminary objection is overruled.

II. Preliminary Objection Pursuant to Rule 1028(a)(4) – Plaintiff's requests for punitive damages, attorney's fees, and expenses should be dismissed for legal insufficiency (Demurrer).

Dively next argues for the dismissal of Plaintiffs' request for punitive damages, attorney's fees, and expenses in Counts I through III and at the end of the Amended Complaint because "there is no statutory authority authorizing Plaintiffs to seek said damages." Dively Brief. at 5. Plaintiffs argue that both the NPCL and the common-law provide for an award of punitive damages, attorney's fees, costs, and expenses. Pls.' Brief. at 9.

Attorney's Fees, Costs, and Expenses

The bedrock principle known as the "American Rule" provides that each litigant pays his own attorney's fees unless a statute or contract provides otherwise. Hardt v. Reliance Standard Life Ins. Co., 560 U.S. 242, 252–53 (2010); Trizechahn Gateway LLC v. Titus, 601 Pa. 637, 652, 976 A.2d 474, 482 (2009). Section 5742 of the NPCL provides that:

Unless otherwise restricted in its bylaws, a nonprofit corporation shall have power to indemnify any person who was or is a party... to any threatened, pending or completed action by or in the right of

the corporation to procure a judgment in its favor... against expenses (including attorneys' fees) actually and reasonably incurred by him in connection with the defense or settlement of the action if he acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the corporation.

15 Pa.C.S.A. § 5742. Furthermore, section 5784 provides, in relevant part, that if “a derivative action is successful in whole or in part, *the court* may award the plaintiff reasonable expenses, including reasonable attorney fees and costs, from the recovery of the nonprofit corporation...” 15 Pa.C.S.A. § 5784 (emphasis added). Contrary to Dively’s assertion, there is clearly statutory authority authorizing Plaintiffs’ claim for attorney’s fees, costs, and expenses.

Punitive damages

Additionally, “[p]unitive damages may be awarded for conduct that is outrageous, because of the defendant's evil motive or his reckless indifference to the rights of others.” Feld v. Merriam, 506 Pa. 383, 485 A.2d 742, 747 (1984) (quoting Restatement (Second) of Torts § 908(2) (1979)). In other words, punitive damages may be awarded only when the act(s) perpetrated by the defendant is/are so outrageous as to demonstrate malicious, willful, or wanton conduct. Hutchison v. Luddy, 582 Pa. 114, 124, 870 A.2d 766, 772 (2005). See also, Viener v. Jacobs, 2003 PA Super 324, 834 A.2d 546 (2003) (holding that it was proper to award punitive damages against majority shareholder in closely-held corporation on underlying claim for breach of fiduciary duty).

Here, Plaintiffs allege, inter alia, that Dively “intimidated and threatened residents and shareholders who spoke out against his misconduct.” Amend. Compl. ¶ 39. As discussed infra, it is also alleged that the Board, including Dively, effectively usurped Plaintiffs’ right to participate in the corporation. The “freezing out” of minority shareholders can give rise to punitive damages, since such individuals are particularly vulnerable to wanton neglect and bad faith. Viener, 834 A.2d at 561. Thus, at this time, we are unable to conclude that Plaintiffs will be unable to prove

facts legally sufficient to establish the damages sought. Dively's second preliminary objection is therefore overruled.

III. Preliminary Objection Pursuant to Rule 1028(a)(4) – Counts I and II of the Amended Complaint should be dismissed since neither contain any averments of facts which, if proven, would establish liability against Defendant Dively individually.

Dively seeks dismissal of Counts I and II of the Amended Complaint because they are “void of any allegations that support piercing the corporate veil of SVDC in order to hold Dively individually liable” and because Plaintiffs lack standing to sue Dively directly. Dively Brief. at 6. Plaintiffs respond that there is no need for allegations of piercing the corporate veil because section 5713 of the NPCL authorizes the personal liability of directors in instances of self-dealing. Pls.’ Brief. at 11.

Standing

Section 5713 of the NPCL provides, in relevant part:

(a) General rule.--If a bylaw adopted by the members of a nonprofit corporation so provides, *a director shall not be personally liable*, as such, for monetary damages for any action taken *unless*:

(1) the director has breached or failed to perform the duties of his office under this subchapter; and

(2) the breach or failure to perform constitutes *self-dealing, willful misconduct or recklessness*.

15 Pa.C.S.A. § 5713 (emphasis added). However, as discussed supra, section 5717, entitled “[l]imitation on standing,” prohibits the enforcement of the board’s statutory duty by a member directly. 15 Pa.C.S.A. § 5717.

Although a shareholder generally cannot pursue a direct cause of action, a shareholder does have common-law individual standing (as opposed to statutory standing discussed above) to sue if

they allege a direct, personal injury independent of any injury to the corporation, and they are entitled to receive the benefit of any recovery. Hill v. Ofalt, 2014 PA Super 17, 85 A.3d 540, 548 (2014); Fishkin v. Hi-Acres, Inc., 462 Pa. 309, 316, 341 A.2d 95, 98 (1975) (“If the injury is one to the plaintiff as a stockholder and to him individually, and not to the corporation...it is an individual action”); White v. First Nat’l Bank, 252 Pa. 205, 97 A. 403, 405 (1916) (“a stockholder can maintain a [direct] action where the act of which complaint is made is not only a wrong against the corporation, but is also in violation of duties arising from contract or otherwise, and owing to him directly”).

A court must therefore undertake an independent inquiry, considering the nature of the injury alleged, to determine whether the action is direct or derivative. See, Reifsnnyder v. Pittsburgh Outdoor Advert. Co., 405 Pa. 142, 149, 173 A.2d 319, 322 (1961) (determining whether plaintiff’s alleged direct injury as an individual shareholder was “merely a subterfuge attempting to disguise a harm to the corporation”). In Hill, the Superior Court outlined the manner in which to approach this inquiry:

As is hornbook law:

If the injury is one to the plaintiff as a shareholder as an individual, and not to the corporation, for example, where the action is based on a contract to which the shareholder is a party, *or on a right belonging severally to the shareholder*, or on a fraud affecting the shareholder directly, or where there is a duty owed to the individual independent of the person's status as a shareholder, it is an individual action. If the wrong is primarily against the corporation, the redress for it must be sought by the corporation, except where a derivative action by a shareholder is allowable, and a shareholder cannot sue as an individual.... Whether a cause of action is individual or derivative must be determined from the nature of the wrong alleged and the relief, if any, that could result if the plaintiff were to prevail.

In determining the nature of the wrong alleged, the court must look to the body of the complaint, not to the plaintiff's designation or stated intention. The action is derivative if the gravamen of the complaint is injury to the corporation, or to the whole body of its stock or property without any severance or distribution among individual holders, or if it seeks to recover assets for the corporation or to prevent dissipation of its assets.... If damages to a shareholder result indirectly, as the result of an injury to the corporation, and not directly, the shareholder cannot sue as an individual.

12B FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 5911 (2013)); See also, ALI Principles of Corporate Governance § 7.01(a) (“[a]n action in which the holder can prevail only by showing an injury or breach of duty to the corporation should be treated as a derivative action”).

85 A.3d at 549 (emphasis added).

There is no question that a shareholder may bring a direct action to protect his voting rights. Reifsnyder, 405 Pa. at 149 (holding that the right to vote is basic and fundamental to most shares of stock and is independent of any right that the corporate entity possesses and the shareholder could enforce and protect such rights by bringing a direct action). Indeed, as previously discussed, section 5751 of the NPCL provides that “[t]here shall be one class of members whose voting and other rights and interests shall be equal...” 15 Pa.C.S.A. § 5751(a). A shareholder may also bring an action personally to enforce his or her right to inspect the corporate books. Shaw v. Hurst, 135 Pa. Cmwlth. 635, 639, 582 A.2d 87, 89 (1990). Section 5508 of the NPCL provides that any member of a nonprofit corporation has a right to examine, upon request, certain corporate records for any proper purpose. 15 Pa.C.S.A. § 5508.

Moreover, “an attempt by a group of majority shareholders to ‘freeze out’ minority shareholders for the purpose of continuing the enterprise for the benefit of the majority

shareholders constitutes a breach of the majority shareholders' fiduciary duty to the minority shareholders.” Viener v. Jacobs, 2003 PA Super 324, 834 A.2d 546 (2003).

In this case, Count I is a derivative claim and Count II is a direct claim against the SVDC’s Board of Directors, including Dively, for alleged breach of fiduciary duties. Amend. Compl. at ¶¶ 15, 17. Although the Amended Complaint contains allegations of self-dealing,³ the majority of the factual allegations, as incorporated into both Counts I and II, involve the Board’s failure to respond to shareholder requests to inspect corporate records, the improper use of voting proxies, and discrimination in the sale of shares. Amend. Compl. at ¶¶ 5-15.

Specifically, Plaintiffs allege that during the 2018 Board election, the Board, rather than splitting the majority shareholder’s votes equally among all candidates, distributed a portion of the votes to themselves to safeguard their seats on the Board. Id. ¶ 68. Because of the alleged improper distribution, Plaintiffs aver that the Board undermined and entirely devalued the value of the shares owned by non-Board members, including Plaintiffs. Id. ¶ 69. In addition, it is alleged that the Board instituted a moratorium on the sale of shares to ensure its proposed amendments were passed; included in the packet of amendments was the one-vote-per-lot-owner without cumulative voting system. Id. ¶ 79. That system now effectively freezes out members who do not own property. Id. ¶ 110.

As to Count II, the rights discussed above are not merely incidental to the allegations of corporate injury, but rather are fundamental and owed directly to the shareholders. See, Reifsnyder, 405 Pa. at 149. Plaintiffs have supported their breach of fiduciary duty claim with allegations that they were effectively “frozen out” by the Board. Consequently, Count II is more appropriately

³ We note that self-dealing constitutes paradigmatic injuries to the corporation, not to the Plaintiffs individually. See, Hill v. Ofalt, 2014 PA Super 17, 85 A.3d 540, 548 (2014).

characterized as direct. However, being that allegations of self-dealing do not give rise to individual standing, those averments must be stricken from Count II.

As to Count I, “[i]t is Hornbook law that a corporation has a cause of action against its officers and directors for breach of fiduciary duty.” Vill. at Camelback Prop. Owners Assn. Inc. v. Carr, 371 Pa. Super. 452, 468, 538 A.2d 528, 536 (1988), aff’d sub nom. Vill. at Camelback Prop. Owners Ass’n, Inc. v. Carr, 524 Pa. 330, 572 A.2d 1 (1990). Here, there is no issue of piercing the corporate veil and therefore Dively’s demurrer with respect to Count I cannot be sustained. Id.

Accordingly, Dively’s third preliminary objection is sustained only to the extent that Count II contains allegations of self-dealing. See, ALI Principles of Corporate Governance § 7.01(c) (noting that “[i]f a transaction gives rise to both direct and derivative claims, a holder may commence and maintain direct and derivative actions simultaneously, and any special restrictions or defenses pertaining to the maintenance, settlement, or dismissal of either action should not apply to the other”).

IV. Preliminary Objection Pursuant to Rule 1028(a)(3) – In the alternative, Plaintiffs should be required to file a more specific amended complaint as to Counts I and II.

Dively’s preliminary objections also contain a motion for more specific pleading asserting that the Amended Complaint does not enable him to prepare a response to any of the allegations contained in Counts I and II. The test for determining whether a complaint is sufficiently specific under rule 1028(a)(3) is whether its averments are sufficiently clear and set forth sufficient facts that allow the defendant to prepare his defense. Commonwealth by Shapiro v. Golden Gate Nat’l Senior Care LLC, 194 A.3d 1010, 1029 (Pa. 2018). In Pennsylvania, officers and directors of a corporation are deemed to stand in a fiduciary relation to the corporation. Seaboard Indus., Inc. v. Monaco, 442 Pa. 256, 261, 276 A.2d 305, 308 (1971). Indeed, Section 5712 of the NPCL provides:

Directors.--A director of a nonprofit corporation shall stand in a fiduciary relation to the corporation and shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith, in a manner he reasonably believes to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances...

15 Pa.C.S.A. § 5712(a). “A director has breached a duty or engaged in illegal self-dealing and is personally liable for any harm to the corporation if, presumably, the transaction was palpably unfair, or constitutes willful misconduct or recklessness.” Commonwealth by Kane v. New Foundations, Inc., 182 A.3d 1059, 1069 (Pa. Commw. Ct. 2018), reconsideration denied (Mar. 27, 2018). 15 Pa.C.S.A. § 5713(a).

Here, Plaintiffs aver that Dively is a member of the SVDC Board of Directors. Amend. Compl. ¶¶ 5, 112. The Amended Complaint also alleges, inter alia, that Dively owns Dirt Bottom Excavating, Inc. and that Dirt Bottom provides services to SVDC for a fee. Id. ¶¶ 28, 31. Plaintiffs also allege that Dively used his position on the Board of SVDC to engage in self-dealing by steering SVDC contracts for services to Dirt Bottom. Id. ¶¶ 34, 35. The Amended Complaint further avers that Dively’s alleged self-dealing was in violation of the NPCL and his traditional fiduciary duties of care and loyalty to SVDC, causing direct harm to the corporation. Id. ¶¶ 42, 114, 116.

In addition to the averments relating to self-dealing, both Counts I and II allege that the Board, including Dively, breached their fiduciary duties owed to Plaintiffs individually by actively refusing to honor written demands to inspect corporate books, misusing proxy votes, and by instituting discriminatory voting practices. Amend. Compl. ¶¶ 136-140. We find that Plaintiffs have set forth sufficient facts to enable Dively to prepare a defense to both Counts I and II. Dively’s fourth preliminary objection is therefore overruled.

V. Preliminary Objection Pursuant to Rule 1028(a)(3) – In the alternative, Plaintiffs should be required to file a more specific amended complaint as to Count III.

Finally, Dively argues that to the extent Count III is not dismissed, Plaintiffs should be required to “plead count III with more specificity to include allegations supporting a claim against Dively individually i.e. why the corporate veil of both SVDC and Dirt Bottom Excavating, Inc. should be pierced....” Dively Brief. at 8. As discussed in our analysis of Dively’s first preliminary objection, Plaintiffs have alleged sufficient facts to support their assertion that the Board’s actions were inconsistent with statutory law and SVDC’s Bylaws. We find that those facts are sufficient to put Dively, *a member of the Board*, on notice of the claims against him. Dively’s fifth preliminary objection is therefore overruled.

Defendant SVDC’s Preliminary Objections

I. Preliminary Objection Pursuant to Rule 1028(a)(4) – Failure to Plead Pursuant to the Business Judgment Rule.

SVDC argues that this Court should dismiss the Amended Complaint with respect to the Board’s decision not to pursue a derivative claim under the business judgment rule. SVDC Brief. at 1-2.⁴ See, Cuker v. Mikalauskas, 547 Pa. 600, 606, 692 A.2d 1042, 1045 (1997). Plaintiffs argue that the rule does not apply to cases involving self-dealing and where a corporation does not make an informed decision in good faith. Pls.’ Brief. at 7-8.⁵ In the alternative, Plaintiffs argue that even if the rule does apply, Defendants have not taken the necessary actions required to avail itself of the rule’s protections. Pls.’ Brief. at 7. We agree with Plaintiffs on this issue.

In Cuker, Our Supreme Court has explained that:

The business judgment rule reflects a policy of judicial noninterference with business decisions of corporate managers,

⁴ Stonycreek Valley Development Corporation’s Brief in Support of Preliminary Objections under P.A.R.C.P. 1028 will hereinafter be cited as “SVDC Brief.”

⁵ Plaintiffs’ Brief in Support of Response to Defendant Stonycreek Valley Development Corporation’s Preliminary Objections to Amended Complaint will hereinafter be cited as “Pls.’ Brief.”

presuming that they pursue the best interests of their corporations, insulating such managers from second-guessing or liability for their *business decisions in the absence of fraud or self-dealing or other misconduct* or malfeasance.

Cuker, 547 Pa. at 606 (emphasis added); 15 Pa.C.S.A. § 5713 (a); See also, Pittsburgh History & Landmarks Found. v. Ziegler, 200 A.3d 58, 61 (Pa. 2019). Decisions regarding litigation by or on behalf of a corporation, including shareholder derivative actions, are business decisions within the province of the board of directors. Cuker, 547 Pa. at 611. “Such business decisions of a board of directors are, unless taken in violation of a common law or statutory duty, within the scope of the business judgment rule.” Id.

In determining whether the business judgment rule applies, the relevant factors to be considered include: whether the board or committee refusing to sue was disinterested,⁶ whether it was assisted by counsel, whether it prepared a written report, whether it was independent, whether it conducted an adequate investigation, and whether it rationally believed its decision was in the best interests of the corporation (i.e., acted in good faith). Cuker, 547 Pa. at 612. “If *all* of these criteria are satisfied, the business judgment rule applies and the court should dismiss the action.” Id. (emphasis added).

In this case, the Amended Complaint alleges that Dively, as a member of SVDC and owner of Dirt Bottom Excavation, engaged in self-dealing to the detriment of SVDC by rendering Dirt Bottom’s services to SVDC for a fee. Amend. Compl. at ¶¶ 27-35, 116. Plaintiffs aver that Dively further used his position on the Board to manipulate the bidding process, ensuring that other bidders were unable to bid against Dirt Bottom, and to draft the scope of services favorably to his

⁶ A defendant director is not interested in the disputed conduct if the plaintiff “does not otherwise allege with particularity facts that, if true, raise a significant prospect that the director would be adjudged liable to the corporation or its shareholders.” Braun on Behalf of USA Techs., Inc. v. Herbert, 2018 PA Super 41, 180 A.3d 482, 488 (2018).

business. Amend. Compl. at ¶¶ 37, 117. Plaintiffs also allege that, in addition to condoning Dively's self-dealings by allowing him to discuss and vote on the transactions, the Board also misused proxy-votes to entrench their own positions and violated several provisions of the NPCL by ignoring corporate records requests and discriminating in the sale of shares. Amend. Compl. at ¶¶ 124, 144, 152. We find that such business decisions involving self-dealing and statutory violations are clearly beyond the scope of the business judgment rule. See, Cuker, 547 Pa. at 611.

In addition, the Board did not take all of the steps necessary to avail itself of the business judgment rule. Plaintiffs allege that the Board ignored their demand to appoint a Special Litigation Committee to investigate suspected instances of self-dealing. Amend. Compl. at ¶¶ 21-24. The Plaintiffs further allege that to date, the Board has not responded to either the Plaintiffs' Demand Letter or formed a Special Litigation Committee. Id. at ¶ 25. Plaintiffs have also pled with particularity facts that, if true, raise a significant prospect that Dively was not disinterested and therefore liable to the corporation. Id. at ¶¶ 116-120. For these reasons, SVDC's first preliminary objection is overruled.

II. Preliminary Objection Pursuant to Rule 1028(a)(4) and 1028(a)(5)—Misjoinder of Causes of Action and Failure to State a Direct Cause of Action Against SVDC in Count II.

SVDC next argues that Count II of the Amended Complaint is legally insufficient to state a viable cause of action against it and its Board of Directors. SVDC's Brief at 3. Specifically, SVDC argues that Plaintiffs do not have standing under either section 5717 of the NPCL or individually. Id. To the contrary, Plaintiffs argue that they do have individual standing because the Board of Directors owed "at least two duties to Plaintiffs as shareholders and as members of the corporation." Pls.' Brief. at 13. Plaintiffs aver in Count II that the Board had both a duty to honor

corporate records requests and to treat all shareholders equally. *Id.*; Amend. Compl. at ¶¶ 136-140.

We agree with Plaintiffs on this issue.

As discussed in our analysis of Dively’s preliminary objection with respect to Count II, *supra*, we find that Plaintiffs have alleged independent injuries apart from any injury to the corporation. However, the allegations relating to Dively’s alleged self-dealing must be stricken, since self-dealing constitutes paradigmatic injuries to the corporation, and therefore does not give rise to independent standing. *See, Hill v. Ofalt*, 2014 PA Super 17, 85 A.3d 540, 548 (2014). Accordingly, SVDC’s preliminary objection is sustained to the extent that Count II contains allegations of self-dealing, but otherwise is overruled.

- III. Preliminary Objection Pursuant to PA.R.C.P 1028(a)(3)—Insufficiently Specific Averment of Damages.
- IV. Preliminary Objection Pursuant to PA.R.C.P 1028(a)(3)—Insufficiently Specific Averment of References to the Non-Profit Corporation Law, Robert’s Rules, and “Corporate Formalities.”

Damages

SVDC next argues that Plaintiffs’ requests for damages “in an amount to be proven at trial in excess of the mandatory amount of arbitration” fails to identify the facts upon which the claim is based and the measure of damages. SVDC’s Brief at 7. Plaintiffs respond that their allegations are limited to the knowledge and information at their disposal and are not required to provide a more detailed summary of damages. Pls.’ Brief.⁷ at 15. We agree with Plaintiffs on this issue.

Pennsylvania Rule of Civil Procedure 1019(a) provides that “[t]he material facts on which a cause of action or defense is based shall be stated in a concise and summary form.” Pa.R.C.P. No. 1019(a). The purpose of this rule is to require the pleader to disclose material facts sufficient

⁷ Plaintiffs’ Brief in Support of Response to Defendant Stonycreek Valley Development Corporation’s Preliminary Objections to Amended Complaint will hereinafter be cited as “Pls.’ Brief.”

to notify the adverse party of the claims it will have to defend against. Commonwealth by Shapiro v. Golden Gate Nat'l Senior Care LLC, 194 A.3d 1010, 1029 (Pa. 2018). “While our rules require the pleading of all material facts upon which claims are based, there is no requirement to plead the evidence upon which the pleader will rely to establish those facts.” Id. In addition, a party will generally not be required to furnish information peculiarly within the demanding party's knowledge. Georges Twp. v. Union Tr. Co. of Uniontown, 293 Pa. 364, 143 A. 10 (1928); Retina Assocs. of Greater Philadelphia, Ltd. v. Retinovitreal Assocs., Ltd., 2017 PA Super 380, 176 A.3d 263, 281 (2017). A more specific pleading is therefore not required for matters where an objecting party has, or should have, as much or more knowledge than the pleader. Hock v. L. B. Smith, Inc., 69 Pa. D. & C.2d 420, 423 (Pa. Com. Pl. 1974).

With respect to damages, any pleading demanding relief for unliquidated damages *cannot* claim or demand any specific sum, but must merely state whether the amount claimed does, or does not, exceed the jurisdictional amount of arbitration in that county. Pa.R.C.P. 1021.

Here, the Amended Complaint outlines the material facts necessary for the relief sought. We agree with Plaintiffs that any other documentary evidence required to establish those facts as to “the specific basis upon which damages are claimed” would require additional discovery. SVDC’s Brief at 7; Amend. Compl. ¶¶ 48-49. Moreover, contrary to SVDC’s assertion, Plaintiffs are not required to—and indeed must not—demand a specific sum; they need only state whether the amount claimed exceeds the jurisdictional amount of arbitration. Plaintiff’s request for relief “in an amount to be proven at trial *in excess of the mandatory amount for arbitration*” meets the requirements of Rule 1021. See, Amend. Compl. ¶¶ 125, 140, 154. Accordingly, SVDC’s third preliminary objection is overruled.

General Averments of Violations of NPCL, Robert's Rules, and Corporate Formalities

Finally, SVDC argues that the Amended Complaint's general averments to violations of the NPCL, Robert's Rules, and corporate formalities leave it to guesswork as to the provisions and formalities relied upon by Plaintiffs. SVDC's Brief. at 7. Plaintiffs again argue that the Amended Complaint provides SVDC with sufficient notice of the alleged violations of the NPCL and Bylaws. Pls.' Brief at 16.

In this case, we find that the Amended Complaint sufficiently puts SVDC on notice of the claims in which it has to defend itself. "The purpose of the pleadings is to place the defendants on notice of the claims upon which they will have to defend." Yacoub v. Lehigh Valley Med. Assocs., P.C., 2002 PA Super 251, ¶ 16, 805 A.2d 579, 588 (2002). To assess whether a claim has been pled with the requisite specificity, the allegations must be viewed in the context of the pleading as a whole. Commonwealth by Shapiro v. Golden Gate Nat'l Senior Care LLC, 194 A.3d 1010, 1030 (Pa. 2018).

Here, the Amended Complaint refers to various provisions of the NPCL and SVDC's By-Laws that Plaintiffs believe were violated. Specifically, the Amended Complaint alleges, *inter alia*, that "[u]nder *Section 5508 of the N[P]CL*, and *Article VII, Paragraph 2 of SVDC's By-Laws*...the shareholders and other members of SVDC have a right, upon written demand, to inspect the Corporation's records." Amend. Compl. ¶ 8. Additionally, "[u]nder *Article VIII, Paragraph 4 of the By-Laws*, the Board of Directors may only cease the transfer of shares not more than fifty days prior to the date of any meeting effecting the rights of shareholders." *Id.* ¶ 80. Although several averments are made, particularly within Count III, where the NPCL is referenced but no specific section is provided, we find that the Amended Complaint as a whole adequately sets forth the

nature of the claims in order to permit SVDC to prepare a defense. Accordingly, SVDC's fourth preliminary objection is overruled.

We enter the following order:

HARRY C. NEEL, MICHAEL JENKINS,
 and LEE CAVANAUGH, Individually and
 Derivatively on Behalf of THE
 STONYCREEK VALLEY
 DEVELOPMENT CORPORATION,
 Plaintiffs,
 v.
 DANIEL DIVELY, and THE
 STONYCREEK VALLEY
 DEVELOPMENT CORPORATION,
 Defendants.


) IN THE COURT OF COMMON PLEAS OF
) SOMERSET COUNTY, PENNSYLVANIA
)
)
) NO. 275 Civil 2019
)
)
) PRELIMINARY OBJECTIONS
) TO PLAINTIFFS' FIRST
) AMENDED COMPLAINT
)
)
)

ORDER

AND NOW THIS 26th day of February, 2020, upon consideration of Defendants' Preliminary Objections to Plaintiffs' Amended Complaint, it is hereby **ORDERED** that Defendants' Preliminary Objections are **SUSTAINED IN PART**, and **OVERRULED IN PART**.

We find that the averments relating to Defendant Daniel Dively's alleged self-dealing in Count II of Plaintiffs' Amended Complaint, including those incorporated by reference, do not give rise to individual standing. Accordingly, Defendants' Preliminary Objections are **SUSTAINED** with regard to those specific allegations, and therefore those allegations are stricken from Count II of the Amended Complaint.

All other preliminary objections are **OVERRULED**.

BY THE COURT:


 SCOTT P. BITTNER, J.