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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

FRANKLIN MIEULI,
Plaintiff,
v.
EDWARD J. DEBARTOLO, JR., et al.,
Defendants.

No. C-00-3225 JCS

**ORDER GRANTING IN PART AND DENYING
IN PART DEFENDANT’S MOTION TO
DISMISS COMPLAINT FOR FAILURE TO
STATE CLAIMS PURSUANT TO FED. R. CIV. P.
12(b)(6)**

Defendant’s Motion To Dismiss Complaint For Failure To State Claims Pursuant To Fed. R. Civ. P. 12(b)(6) came on for hearing on December 22, 2000, at 9:30 a.m. For the reasons stated below, Defendant’s Motion is GRANTED in part and DENIED in part.

I. INTRODUCTION

Plaintiff Frank Mieuli (“Mieuli”) is a limited partner of the San Francisco Forty-Niners Limited (“the Partnership”), a California limited partnership. Mieuli is suing both the Partnership and Edward J. DeBartolo Jr. (“DeBartolo”), individually, based upon news reports that DeBartolo is transferring his interest in the San Francisco Forty-Niner’s to his sister, Denise DeBartolo York, as part of a settlement between DeBartolo and York. Mieuli alleges that DeBartolo has breached both a letter agreement and the limited partnership agreement by failing to honor a tag-along provision in those agreements. Those provisions purportedly require that DeBartolo give Mieuli advance notice of his intent to sell his interest in the Forty-Niners and that Mieuli be given the opportunity to sell his interest in the Forty-Niners to the same buyer and on the same terms. Mieuli also brings claims on his own behalf and on behalf of the partnership

1 alleging that DeBartolo has mismanaged partnership assets. Defendant DeBartolo moves to dismiss all of
2 Plaintiff's claims pursuant to Fed. R. Civ. P. 12(b)(6).

3
4 **II. BACKGROUND¹**

5 On March 15, 1977, DeBartolo and the former owners of the San Francisco Forty-Niners signed a
6 Memorandum of Purchase and Sale ("Memorandum") under which DeBartolo, "or a California
7 Corporation to be formed of which DeBartolo shall be sole shareholder," agreed to purchase 90% of the
8 assets of the Forty-Niners. Plaintiff and the Morabito family trusts each agreed to transfer and contribute
9 their 5% interest in the team to a limited partnership be formed by DeBartolo to operate the team. First
10 Amended Complaint ("FAC") at 2-3, ¶¶ 4, 8; *see also* Memorandum at 1, ¶ 2, Exh. A to Declaration of
11 Peter Obstler in Support of Defendant Edward DeBartolo, Jr.'s Motion to Dismiss Complaint for Failure to
12 State Claims Pursuant to Fed. R. Civ. P. 12(b)(6) ("Obstler Decl.").

13 On the same day, DeBartolo and Mieuli signed a letter agreement setting forth the terms of their
14 agreement "in connection with the limited partnership to be formed for the purposes of purchasing and
15 operating the San Francisco 49ers football team." FAC at 2, ¶ 5; *see also* March 15, 1977 Letter
16 Agreement ("the Letter Agreement"), Exh. B to Obstler Decl. The Letter Agreement gave Mieuli "tag-
17 along" rights in the event that DeBartolo decided to sell his interest in the limited partnership. Specifically,
18 the Letter Agreement contained the following provisions:

19
20 _____
21 ¹ The facts set forth in this section are based on the allegations in Plaintiff's First Amended Complaint,
22 which are assumed to be true for the purposes of this motion. *See During v. First Boston Corp.*, 815 F.2d
23 1265, 1267 (9th Cir. 1987). The Court also relies upon the following documents, which were explicitly
24 referenced in Plaintiff's First Amended Complaint ("FAC"): 1) the March 15, 1977 Letter Agreement
25 (referenced in FAC at 2, ¶ 5); 2) the March 15, 1977 Memorandum of Purchase and Sale (referenced in FAC
26 at 2, ¶ 4); 3) the March 25, 1977 Limited Partnership Agreement (referenced in FAC at 3, ¶ 9). *See Branch*
27 *v. Tunnell*, 14 F.3d 449, 454 (9th Cir. 1994) ("documents whose contents are alleged in the complaint and
28 whose authenticity no party questions, but which are not physically attached to the pleading, may be considered
on a Rule 12(b)(6) motion"). In considering the Partnership Agreement, the Court assumes, without deciding,
that the First Amendment to Limited Partnership Agreement may be considered on this motion as part of the
Partnership Agreement. The Court does not consider the newspaper articles attached to Defendant's motion
to be part of Plaintiff's complaint. The Court may consider newspaper articles referenced in and integral to the
complaint. *Krim v. Coastal Physician Group, Inc.*, 81 F. Supp. 2d 621, 625 n. 2 (M.D.N.C. 1998), *aff'd*,
201 F.3d 436 (4th Cir. 1999). Here, however, Plaintiff's only reference to news reports is the allegation that
"[a]ccording to published reports, on or about March 18, 2000, DeBartolo contracted for the sale of his
interest in the partnership." FAC at 5, ¶ 15 This general reference to "news reports" does not provide a
sufficient basis for incorporating the entire content of these unspecified news reports into Plaintiff's complaint.

1 7. DeBartolo shall give Mieuli formal written notice of his intent to sell his partnership interest
2 in San Francisco 49ers, Limited. . . .

3 8. If DeBartolo, at any time, sells all of his interest in the San Francisco 49ers, Limited, Mieuli
4 may, but need not, sell all of his interest in the San Francisco 49ers, Limited to the same
5 purchaser and on the same terms and conditions.

6 *Id.* at 4. The Letter Agreement also provided that all of the provisions in the Agreement would be binding
7 on “the heirs, personal representatives, successors and assigns of DeBartolo and Mieuli, including, but not
8 limited to, any corporation that acquires any interest in San Francisco 49ers, Limited.” *Id.* at 5.

9 At approximately the same time that DeBartolo signed the Letter Agreement, he formed a
10 corporation, San Francisco Forty-Niners, Inc. (“S.F., Inc.”) and transferred his entire ownership interest in
11 the team to S.F., Inc. FAC at 2-3, ¶ 7. S.F., Inc. rather than DeBartolo was named as the general partner
12 in the limited partnership agreement (“the Partnership Agreement”) creating San Francisco Forty Niners,
13 Limited (the “Partnership”), signed March 25, 1977. *See* San Francisco Forty Niners, Limited: Limited
14 Partnership Agreement, Exh. D to Obstler Decl. DeBartolo signed the Partnership Agreement on behalf of
15 S.F. Inc. *Id.* The Partnership Agreement was also signed by Marshall Leahy, managing partner of the
16 Morabito family trusts. *Id.* Under the Partnership Agreement, S.F. Inc., Franklin Mieuli and the Morabitos
17 contributed their respective ownership interests in the team to the Partnership. In exchange, S.F., Inc. was
18 to have a 90% interest in the Partnership as the general partner. Plaintiff and the Morabitos were to retain a
19 5% interest each as limited partners. Altamonte, Inc., not DeBartolo, executed the First Amendment to
20 Limited Partnership Agreement on July 1, 1992, as shareholder of S.F., Inc. First Amendment to Limited
21 Partnership Agreement, Exh. D to Obstler Decl.²

22 Plaintiff learned from news reports published around March 18, 2000 that DeBartolo had
23 contracted for the sale of his interest in the Partnership. FAC at 5.³

24 ² According to DeBartolo, Altamonte Inc. is wholly owned by Edward J. DeBartolo Corporation, a
25 parent entity jointly owned by Mr. DeBartolo and his sister, Denise DeBartolo York. Motion at 6, n. 3. For
26 the purposes of this motion, the Court does not consider this factual assertion, which is outside the scope of
27 Plaintiff’s pleadings.

28 ³ News reports provided by DeBartolo as exhibits to this motion indicate that the news reports
 referred to by Plaintiff probably concerned the settlement between Edward J. DeBartolo, Jr. and his sister,
 Denise DeBartolo York. *See* Exh. D. to Obstler Decl. According to the reports, DeBartolo and York agreed
 to divide the assets of Edward J. DeBartolo Corporation, with York controlling the San Francisco Forty-
 Niners and DeBartolo controlling the remaining assets of the corporation. *Id.* Again, the Court does not
 consider the contents of these news reports as they are not contained in the pleadings.

1 Plaintiff filed a complaint against DeBartolo and the Partnership on May 19, 2000. *See* Exh. A to
2 Notice of Removal. DeBartolo removed to the Federal District Court for the Northern District of
3 California on September 6, 2000 and filed a motion to dismiss on October 10, 2000. In that motion,
4 Defendant DeBartolo asserted that he was not the proper defendant with respect to any of Plaintiff's
5 claims and therefore, that the complaint should be dismissed. Rather than responding to Defendant's
6 motion, Plaintiff filed a first amended complaint on October 30. Defendant took its original motion off
7 calendar and filed a Motion to Dismiss Plaintiff's First Amended Complaint For Failure to State Claims
8 Pursuant to Fed. R. Civ. P. 12(b)(6) (the "Motion") on November 17.

9 In his First Amended Complaint ("FAC"), Plaintiff alleged the following claims:

10 Claim One: Breach of Letter Agreement;

11 Claim Two: Breach of Limited Partnership Agreement

12 Claim Three: Breach of Fiduciary Duty

13 Claim Four: Derivative Claim for Breach of Fiduciary Duty

14 Claim Five: Derivative Claim for Conversion of Partnership Assets

15 Claim Six: Derivative Claim for an Accounting

16 Claim Seven: Derivative Claim for Unjust Enrichment

17 Claim Eight: Violation of Business and Professions Code Section 17200

18 Plaintiff's first two claims are based upon DeBartolo's alleged failure to give Plaintiff notice of his
19 intent to sell his interest in the Partnership and to afford Plaintiff the opportunity to sell his own interest on
20 the same terms, which Plaintiff says DeBartolo was required to do under both the Letter Agreement and the
21 Partnership Agreement. FAC at 5-6. Plaintiff's third claim is based upon the allegation that "[a]s de facto
22 general partner, DeBartolo owed a fiduciary duty to plaintiff, a limited partner" and that DeBartolo
23 breached that duty "by converting the Partnership's funds and by engaging in other acts of mismanagement
24 and self-dealing." FAC at 6. Claims Four through Seven are derivative claims asserted on behalf of the
25 Partnership based upon DeBartolo's alleged conversion, mismanagement and self-dealing while acting as
26 "de facto general partner." FAC at 8-10. Finally, Claim Eight, for unfair business practices under § 17200
27 of the California Business and Professions Code, is based upon the same conduct alleged in Claims One
28 through Seven. FAC at 10.

1 Defendant makes the following arguments in his Motion:

2 1. Claim One:

3 a. DeBartolo did not breach the tag-along provision in the Letter Agreement because that
4 provision applied only to sale by DeBartolo of his *individual* interest in the limited
5 partnership and DeBartolo never had such an individual interest.

6 b. Under the doctrine of novation, the obligations set forth in the Letter Agreement were
7 completely subsumed by the Partnership Agreement and the Partnership Agreement makes
8 clear that tag-along rights apply only to the general partner and not to DeBartolo as an
9 individual.

10 2. Claims Two, Three, Four and Six: All of these claims are based upon duties owed by the general
11 partner rather than DeBartolo individually. Moreover, there is no justification for imposing alter ego
12 liability because Plaintiff has not shown that there is a unity of interest between S.F., Inc. and
13 DeBartolo and Plaintiff has not shown that inequitable results will follow if corporate separateness is
14 respected.

15 3. Claims Four through Seven:

16 a. These claims are barred because the Uniform Limited Partnership Act, Cal. Corp. Code §
17 15501 *et seq.*, bars limited partners from asserting derivative claims on behalf of the
18 partnership.

19 b. Plaintiff has not pleaded adequate facts to satisfy the requirement under Fed. R. Civ. P.
20 23.1 that plaintiffs bringing derivative claims must “allege with particularity the efforts, if any,
21 made by the plaintiff to obtain the action the plaintiff desires from the directors or
22 comparable authority and . . . the reasons for the plaintiff’s failure to obtain the action or for
23 not making the effort.”

24 4. Claim Eight: Plaintiff’s claim under § 17200 of the Business and Professions Code must be
25 dismissed because the underlying claims upon which it is based are defective.

26 Plaintiff makes the following arguments in his opposition to Defendant’s motion:

27 1. Claim One:

28

- 1 a. Plaintiff has pleaded in the complaint that DeBartolo transferred his interest in the
2 partnership, albeit indirectly, and this allegation must be taken as true on a motion to
3 dismiss. Moreover, because every contract is read to include an implied covenant of good
4 faith and fair dealing, Defendant cannot use the “artifice” of corporate ownership to thwart
5 Plaintiff’s legitimate contractual expectations.
- 6 b. The doctrine of novation does not apply because it does not clearly appear from the Letter
7 Agreement or the Partnership Agreement that the parties intended to extinguish the original
8 agreement. In fact, the Partnership Agreement was intended to supplement the Letter
9 Agreement.
- 10 c. The integration clause does not show that the Letter Agreement was superseded by the
11 Partnership Agreement.
- 12 2. Claim Two: As the de facto general partner, DeBartolo can also be sued under the Partnership
13 Agreement for breach of the tag-along provision in that agreement.
- 14 3. Claim Three, Four and Six:
- 15 a. These claims are valid because DeBartolo was the de facto general partner of the
16 limited partnership and therefore owed fiduciary duties, including the duty to make
17 an accounting, to the Partnership and to Mieuli, even if DeBartolo was not a party
18 to the Partnership Agreement. On this theory, DeBartolo is directly liable on these
19 claims.
- 20 b. DeBartolo is liable on these claims under an alter-ego theory, which Plaintiff has
21 adequately alleged.
- 22 4. Claims Four-Seven:
- 23 a. Cal. Corp. Code § 15526 does not prohibit derivative suits by limited partners.
24 b. Plaintiff has adequately alleged futility by alleging that the Partnership repeatedly
25 informed Plaintiff that it was not willing to participate in this litigation.
- 26 5. Claim Eight: Plaintiff’s claim under § 17200 of the Business and Professions Code should not be
27 dismissed because the underlying claims are sufficiently pleaded.
28

1 **III. ANALYSIS**

2 **A. Legal Standard**

3 A complaint should not be dismissed for failure to state a claim under Fed. R. Civ. P.
4 12(b)(6) “unless it appears beyond doubt that a plaintiff could prove no set of facts in support of his claim
5 which would entitle him to relief.” *During v. First Boston Corp.*, 815 F.2d 1265, 1267 (9th Cir.
6 1987)(quoting *Conley v. Gibson*, 355 U.S. 41 (1957). In ruling on a motion to dismiss, all allegations of
7 material fact are taken as true and construed in the light most favorable to the non-moving party. *Id.*

8
9 **B. Claim One**

10 **1. Breach of the Letter Agreement**

11 Defendant asserts that under the express terms of the Letter Agreement, Plaintiff’s tag-along rights
12 applied to DeBartolo’s individual interest in the yet-to-be formed partnership, the San Francisco Forty-
13 Niners, Limited. Because DeBartolo never held an individual interest in the Partnership (as is evident from
14 the Partnership Agreement) he has not violated the Letter Agreement. Plaintiff, on the other hand, asserts
15 that he has adequately pled a breach of contract claim, and that Defendant’s argument is based upon factual
16 representations that contradict the allegations of the complaint and therefore, should not be considered on a
17 motion to dismiss. In support of this argument, Plaintiff asserts that the complaint alleged that the Letter
18 Agreement covered “both direct and indirect sales” of DeBartolo’s interest. Opposition at 9. Plaintiff
19 points to the following allegation in the FAC in support of this argument:

20 The parties’ purpose in including similar language in both the Letter Agreement and the Limited
21 Partnership Agreement was to ensure that if DeBartolo ever directly or indirectly transferred his
22 interest in the Team or the Partnership for value, plaintiff would be able to transfer his interest on the
23 same terms. Thus, they intended that these rights would be triggered by DeBartolo’s sale of his
interest in the Corporation, the Corporation’s sale of its interest in the Partnership, or any other
mechanism by which DeBartolo parted with his interest in the Partnership or the Team and received
value in return.

24 FAC at 3-4, ¶ 10. Plaintiff further asserts that regardless of whether the Letter Agreement explicitly
25 covered indirect as well as direct sales of DeBartolo’s partnership interest, the implied covenant of good
26 faith and fair dealing that is read into every contract was breached by DeBartolo’s alleged acts.

27 The Court should dismiss Plaintiff’s breach of contract claim based upon the Letter Agreement only
28 if Plaintiff can prove no set of facts which would demonstrate that its interpretation of the Letter Agreement

1 is correct. *See Quigley v. Pennsylvania Higher Education Assistance Agency*, 2000 WL 1721069 at
2 *5 (N.D. Cal. 2000) (denying motion to dismiss breach of contract claim where contract was reasonably
3 susceptible to both plaintiff’s and defendant’s interpretation of the contract)(citing *Barnett v. Centoni*, 31
4 F.3d 813, 816 (9th Cir. 1994)). Interpretation of a written instrument is “solely a judicial function unless
5 the determination turns upon the credibility of extrinsic evidence.” *Powers v. Dickson, Carlson &*
6 *Campillo*, 54 Cal. App. 4th 1102, 1111 (Cal. Ct. App. 1997). Courts interpret the “intent and scope of
7 the agreement by focusing on the usual and ordinary meaning of the language used and the circumstances
8 under which the agreement was made.” *Id.* Where the written instrument is unambiguous, parol evidence
9 to show intent cannot be admitted. *Id.* On the other hand, parol evidence may be admitted to explain the
10 meaning of a writing when the meaning urged is one to which the written contract term is reasonably
11 susceptible or when the contract is ambiguous.” *Id.* Applying these rules, courts have granted motions to
12 dismiss on contract claims where it is clear from the unambiguous terms of the contract that the alleged
13 conduct by the defendant does not constitute a breach of contract. *See, e.g., International Ins. Co. v.*
14 *Red & White Co.*, 1994 WL 706361 at *13 (N.D. Cal.) (dismissing counterclaim for breach of contract
15 where contract was unambiguous under California law); *Campbell v. Allstate Ins. Co.*, 1998 WL 657488
16 at *1 (C.D. Cal.) (dismissing breach of contract claim on basis that the defendant’s acts were consistent
17 with the plain language of the contract and therefore did not breach the contract). On the other hand,
18 where the contract is ambiguous and there is a question of fact concerning the parties’ intent, dismissal of a
19 breach of contract claim pursuant to Rule 12(b)(6) is inappropriate. *See, e.g., Quigley*, 2000 WL
20 1721069 (N.D. Cal. 2000).

21 Here, Defendant DeBartolo asserts that the tag-along provision in the Letter Agreement
22 unambiguously applies only to DeBartolo’s sale of “his partnership interest” in the soon-to-be formed
23 partnership, and that because DeBartolo never had a partnership interest in the San Francisco 49er Limited
24 (because he transferred his interest to S.F., Inc. before the Partnership was formed), he cannot be sued for
25 breach of the Letter Agreement. Motion at 10. Plaintiff, on the other hand, asserts that the Letter
26 Agreement was intended to cover “indirect as well as direct ownership.” Opposition at 8-9.

27 While Defendant may or may not prevail on this point at trial or on summary judgment, the Court
28 cannot say on this motion that, as a matter of law, the Letter Agreement does not cover transfer of an

1 indirect interest by DeBartolo. Rather, because the Letter Agreement does not explicitly address whether
2 the word “interest” was intended to include an indirect interest, there is an ambiguity which cannot be
3 resolved at this point in the proceedings.⁴ See *Oregon RSA No. 6, Inc. v. Castle Rock Cellular of*
4 *Oregon Limited Partnership*, 840 F. Supp. 770 (D. Or. 1993), *aff’d* 76 F.3d 1003 (9th Cir. 1996)
5 (holding that where explicit terms of contract only provided for tag-along rights as to sale or transfer of
6 partnership interest, the contract did not unambiguously provide that there were no tag-along rights with
7 respect to a transfer of ownership of the entity that owned the partnership interest).

8 In addition, the Court cannot conclude that there was no breach of the Letter Agreement based
9 solely on the pleadings because of the implied covenant of good faith and fair dealing that is read into the
10 Letter Agreement. In arguing that Defendant has breached that duty, Plaintiff relies heavily upon the district
11 court’s decision in *Oregon RSA No. 6, Inc. v. Castle Rock Cellular of Oregon Limited Partnership*,
12 840 F.Supp. 770 (D. Or. 1993), *aff’d* 76 F.3d 1003 (9th Cir. 1996). There, the partnership agreement
13 contained a right of first refusal which provided that:

14 Before the General Partner or any Limited Partner sells, transfers or assigns all or any part of its
15 Partnership Interest to a non-affiliate of such Partner, it shall offer by giving written notice to the
16 General Partner, that interest to all of the other Partners for the price at which and the terms under
17 which such non-affiliate has offered in writing to pay for such interest.

17 76 F.3d at 1007. Plaintiff, the general partner, alleged that the right of first refusal was violated when the
18 grandparent company of one of the limited partners secretly agreed with the parent company of another of
19 the limited partners to convey all of its interest in the entities that owned its partnership interest. *Id.* at
20 1005-1006. The defendant asserted that the right of first refusal did not apply because, on its face, the
21 term in the partnership agreement did not cover sale of an entity that held a partnership interest but rather,

22
23 ⁴ In his Reply brief, Defendant makes the further argument that even assuming Plaintiff’s interpretation
24 of the Letter Agreement is correct, Defendant has not breached the Letter Agreement. Reply at 5.
25 Specifically, Defendant points to the fact that “[t]he Partnership Agreement establishes that, at least as of 1992,
26 Mr. DeBartolo had divested himself of any personal interest in the corporate General Partner, which was and
27 is wholly owned by Altamonte, Inc.” *Id.* Defendant goes on to note that on October 10, 1997, “Mr.
28 DeBartolo severed all his ties as an officer or director with the General Partner or Altamonte, Inc.” *Id.* With
respect to the point that Altamonte had become the owner of S.F., Inc. by 1992, even assuming the Court can
consider this fact, which is based on the First Amendment to Limited Partnership Agreement – a document that
is not explicitly referenced in Plaintiff’s complaint – this does not establish as a matter of law that DeBartolo
could not have breached the Letter Agreement. There are no allegations in the complaint concerning the
ownership of Altamonte, Inc. With respect to the assertion that Defendant severed his ties with Altamonte and
S.F., Inc. in 1997, this alleged fact is based upon a news report that the Court may not consider on a motion
to dismiss.

1 was limited to sale of the partnership interest itself. 840 F. Supp. at 773. The district court disagreed,
2 finding that the implied duty of good faith and fair dealing in the contract was breached because the transfer
3 was an “artifice intended to thwart plaintiff’s legitimate contractual expectation that it would have that it
4 would have a right of first refusal” with respect to the transaction in that case. *Id.* at 775. In reaching this
5 conclusion, the court relied in part on the undisputed fact that the corporate entities which owned the
6 partnership interest were themselves shell corporations. *Id.* The Court rejected the defendants’ argument
7 that “the good faith doctrine cannot be used to contradict the express terms of the contract.” *Id.* at 778.
8 The Court noted that the good faith duty read into the contract merely filled a gap where the contract was
9 silent, pointing out that the contract did not expressly permit the transaction in question but rather, failed to
10 prohibit it explicitly. *Id.*

11 Defendant asserts that *Oregon RSA* is inapplicable because the court in that case was applying
12 Oregon law rather than California law, and that California courts have “consistently rejected claims that
13 acquisition of the parent of a partner to a partnership may constitute a transfer of an interest in the
14 partnership sufficient to trigger first refusal provisions under the partnership agreement.” Reply at 6.
15 Defendant cites to *United States Cellular Investment Company of Los Angeles v. Airtouch Cellular*,
16 2000 WL 349002 (C.D. Cal.) in support of this position that California law differs from Oregon law.
17 However, that case does not support Defendant’s position.

18 In *United States Cellular*, the court considered a motion for a temporary restraining order and
19 therefore was required to determine whether the plaintiff had demonstrated probable success on the merits.
20 *Id.* The plaintiff asserted that the defendant had breached the right of first refusal contained in a partnership
21 agreement when it transferred all rights to control the entity that owned its partnership interest to another
22 entity. *Id.* The court rejected the plaintiff’s argument, based upon the decision in *Oregon RSA*, that the
23 defendant had breached the implied covenant of good faith and fair dealing that is read into contracts. *Id.*
24 at * 8. In reaching this conclusion, the court considered *extrinsic evidence* going to the parties’ intent.
25 The court noted that in *Oregon RSA*, the corporate entities whose ownership was transferred were shell
26 corporations, whereas evidence presented by the defendant in *United States Cellular* showed that the
27 corporate entities whose stock was transferred were not shell corporations. *Id.* The court also based its
28 conclusion on the conduct of the plaintiff following execution of the partnership agreement, pointing out that

1 there had been two previous transfers of control of the same entity and Plaintiff had not challenged either
2 transfer, supporting the defendant’s interpretation of the partnership agreement. *Id.* at *8. This
3 consideration of extrinsic evidence distinguishes *United States Cellular* from the instant case, where the
4 Court is bound to assume the truth of the allegations in the FAC. Moreover, the court in *United States*
5 *Cellular* did not reject the underlying principle that a party may not, by artifice, circumvent the parties’
6 legitimate contractual expectations.

7 While *Oregon RSA* and *United States Cellular* reach opposite conclusions with respect to
8 whether the implied duty of good faith and fair dealing was breached, both cases indicate that where an
9 agreement does not specifically state that the right of first refusal applies to transfers of stock ownership, the
10 court must look to extrinsic evidence to determine what the intentions of the parties to the agreement were
11 and whether the defendant were seeking to circumvent that agreement. *See United States Cellular* at *9;
12 *Oregon RSA*, 840 F. Supp. at 776.⁵ Here, the Letter Agreement does not explicitly address whether the
13 tag-along rights apply to transfers of control of the entity that owns a partnership interest. Because Plaintiff
14 may be able to prove some set of facts that will support his interpretation of the Letter Agreement, Plaintiff
15 has adequately pleaded his breach of contract claim based upon the Letter Agreement.

16
17 **2. Novation**

18
19 ⁵ Defendant also relies on *Richardson v. La Rancherita*, 98 Cal. App. 3d 73 (1979) in support of
20 its argument that Claim One should be dismissed because there has been no breach of the Letter Agreement.
21 There, the plaintiff and the defendant were parties to a real estate lease which required that La Rancherita
22 consent to the assignment of the lease to another tenant. 98 Cal. App. 3d at 79. When plaintiff attempted to
23 assign the lease to a new tenant, La Rancherita refused to consent to the assignment, hoping to negotiate a lease
24 with the new tenant on terms more favorable to La Rancherita. *Id.* In order to get around the consent
25 requirement, plaintiff’s shareholders arranged to sell their corporate stock to the new tenant. *Id.* La Rancherita
26 threatened a forfeiture of the lease in response, and plaintiff sought a declaratory judgment that the sale of their
27 stocks did not violate the contract. *Id.* at 78. The court granted summary judgment in favor of the plaintiff,
28 finding on the basis of the language in the contract alone that transfer of stock ownership was not a breach of
the contract. *Id.* at 79. The court noted that La Rancherita had submitted declarations stating that plaintiff’s
actions amounted to “financial blackmail . . . to vitiate the terms of the lease” but that these declarations had
“contribute[d] more fuel than facts to the conflict.” *Id.* It also made clear that although it had relied on the
terms of the lease alone, “many factual issues pertaining to the meaning of the subject lease provision could have
been raised.” *Id.* It was only because the parties did not raise these factual questions that the court did not
address them. *Id.* Given the court’s recognition in *Richardson* that extrinsic evidence might have been
presented on the issue of intent, that case does not support Defendant’s position that Plaintiff’s breach of
contract claim based on the Letter Agreement should be dismissed at this stage of the case.

1 Defendant asserts as an additional ground for dismissing Claim One that Plaintiff cannot allege a
2 breach of contract claim based on the Letter Agreement because the Partnership Agreement extinguished
3 the obligations set forth in the Letter Agreement under the doctrine of novation. Motion at 11. “Novation
4 is the substitution of a new obligation for an existing one.” *Wells Fargo Bank N.A. v. Bank of America*
5 *NT&SA*, 32 Cal. App. 4th 424, 431 (1995). The substitution is by agreement and with the intent of
6 extinguishing the prior obligation. *Id.* “The substitution of a new obligation for an existing one may be either
7 (1) a new obligation between the same parties, or 2) a new obligation arising because of new parties, either
8 a new debtor or a new creditor.” *Id.* In order for the doctrine of novation to apply, “it must clearly
9 appear that the parties intended to extinguish rather than merely modify the original agreement.” *Id.* The
10 intent to release a party from an obligation under the contract may be expressed in advance, in the
11 underlying contract. *Id.* For instance, in *Wells Fargo*, a novation was found where the defendant
12 purchased a lease from a third party. *Id.* at 432. The court found the requisite intent on the part of the
13 plaintiffs to extinguish the obligations of the third party based on the terms of the original lease, which stated
14 that the lessee “shall be relieved of all liability accruing under this lease from and after the date of any
15 assignment.” *Id.*

16 Here, Defendant argues that the anticipatory language of the Letter Agreement indicates the intent
17 of the parties that the Partnership Agreement extinguish the obligations under the Letter Agreement. In
18 particular, Defendant points to the reference in the Letter Agreement to the “limited partnership to be
19 formed.” Motion at 11. Defendant also relies on the Partnership Agreement, which provides for tag-along
20 rights with respect to the General Partner, arguing that this term reflects the intent of the parties to substitute
21 the tag-along rights provision of the Partnership Agreement for the provision in the Letter Agreement.
22 Motion at 12. Finally, Defendant points to the integration clause in the Partnership Agreement, which he
23 says reflects the parties’ intent to extinguish the obligations under the Letter Agreement.

24 Defendant’s argument on novation is unconvincing because the “anticipatory language” in the Letter
25 Agreement does not reflect a clear intent to extinguish the obligation of the Letter Agreement. The Letter
26 Agreement provides that “[a]ll of the provisions in this agreement shall be binding on the heirs, personal
27 representatives, successors and assigns of DeBartolo” but does not include the additional language of the
28 lease in *Wells Fargo*, namely that DeBartolo will be relieved of his obligations under the Letter Agreement

1 upon transfer or assignment of his interest. Nor does the integration clause provide unambiguous evidence
2 of the intent of DeBartolo and Mieuli, as that clause by its terms appears only to apply to the parties to the
3 Partnership Agreement, and DeBartolo as an individual is not a named party to that agreement. *See* § 25
4 to Partnership Agreement.

5
6 **C. Claims Two, Three, Four and Six**

7 Defendant asserts that Claims Two, Three, Four and Six should be dismissed because all of the
8 duties on which these claims are based arise from the Partnership Agreement, and Defendant is not a party
9 to that agreement. Motion at 13. Plaintiff responds that Defendant may be liable on the basis that the
10 general partner, S.F., Inc. acted as DeBartolo’s alter ego. In addition, with respect to Claims Three, Four
11 and Six, Plaintiff asserts that DeBartolo can be held directly liable as the “de facto” general partner of the
12 Partnership.

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14 **1. Alter Ego Liability**

15 In order to determine alter ego liability, California courts require: “1) that there be such unity of
16 interest and ownership that the separate personalities of the corporation and the individual no longer exist,
17 and 2) that if the acts are treated as those of the corporation alone, and inequitable result will follow.”
18 *Associated Vendors, Inc. v. Oakland Meat Co., Inc.*, 210 Cal. App. 2d 825, 837 (1962). The doctrine
19 is designed to prevent fraud or injustice, and thus, “bad faith in one form or another is an underlying
20 consideration.” *Id.* The question of whether or not to pierce the corporate veil is a “peculiarly factual
21 issue.” *Tomaselli v. Transamerica Ins. Co.*, 25 Cal. App. 4th 1269, 1284 (1994). The Court may
22 consider a wide variety of factors, including whether there has been commingling of funds, whether the
23 individual treated assets of the corporation as his own and whether the corporation was adequately
24 capitalized. *Associated Vendors*, 210 Cal. App. 2d at 837.

25 At the pleading stage, conclusory allegations that a corporate entity is the alter ego of the defendant
26 are insufficient to survive a motion to dismiss. *See, e.g., Hockey v. Medhekar*, 30 F. Supp. 2d 1209,
27 1211 n.1 (N.D. Cal. 1998) (dismissing securities fraud claim against individual defendants on basis that
28 allegation that corporations were alter egos for those defendants was insufficient to state a claim); *Hokama*

1 v. *E.F. Hutton & Company, Inc.*, 566 F. Supp. 636, 647 (C.D. Cal. 1983) (holding that plaintiff had
2 failed to state a claim against individual defendant where complaint contained only conclusory allegation of
3 alter ego status without alleging the elements of the doctrine).

4 Here, in contrast to the cases cited by Defendant, Plaintiff has included allegations which go beyond
5 “conclusory allegations” in support of its alter ego theory. See FAC at ¶ 8, 11-14, 33-34. Although
6 Defendant characterizes Plaintiff’s allegation as mere “boilerplate recitation of the various unity factors,”
7 most of the cases on which Defendant relies in support of this argument do not involve motions to dismiss
8 under Rule 12(b)(6), where no evidence outside of the complaint may be considered. *See, e.g., Tomaselli*
9 *v. Transamerica Ins. Co.*, 25 Cal. App. 4th 1269, 1285 (1994) (reversing award of punitive damages
10 against defendant because plaintiff failed to establish “financial condition” of defendant at trial and rejecting
11 argument on appeal that punitive damages could be supported on the basis of parent company’s financial
12 condition because there was no evidence in the record showing unity of interest and inequitable result
13 justifying reliance on alter ego theory); *In re Christian and Porter Aluminum Co. v. Titus*, 584 F.2d 326,
14 337 (9th Cir. 1978) (rejecting findings of bankruptcy judge on alter ego status of defendant because there
15 was no evidence in the record showing unity of interest); *Calvert v. Huckins*, 875 F. Supp. 674, 678
16 (E.D. Ca. 1995) (granting motion to dismiss for lack of personal jurisdiction because plaintiff’s had failed to
17 present sufficient evidence in support of alter ego theory to make a prima facie case of alter ego
18 jurisdiction).

19 In contrast, the court’s decision in *Federal Reserve Bank of San Francisco v. HK Systems*, 1997
20 WL 227995 (N.D. Cal.) – which does involve a Rule 12(b)(6) motion to dismiss – supports Plaintiff’s
21 position that the allegations in the complaint here are sufficient to state a claim based on alter ego liability.
22 In *HK Systems*, the court denied a motion to dismiss for failure to plead adequately alter ego status where
23 the plaintiff alleged that the defendant parent corporation “dominated and controlled” the subsidiary “to
24 such an extent that the individuality and separateness of the subsidiary had ceased,” that the parent
25 disregarded the corporate form of the subsidiary” and that subsidiary was so inadequately capitalized that
26 its capitalization was “illusory.” *Id.* at *5. Similarly, here, Plaintiff has alleged unity of interest, FAC at 7, ¶
27 33 and undercapitalization of the corporate entity, which is sufficient to survive a motion to dismiss on an
28 alter ego theory.

1 behalf of the partnership. Rather, the court held that the basic purpose of § 15526 is served by allowing
2 limited partners to bring a derivative claim against the partnership. *Id.* at 1453.

3 In *Wallner*, the limited partner sued the general partners for breach of fiduciary duty on the basis
4 that the general partners had leased partnership property to themselves and failed to pay rent. *Id.* at 1448.
5 The trial court dismissed the claim under § 15526 and the court of appeal reversed. The court of appeal
6 reasoned that the purpose of § 15526 is to prevent the limited partners from interfering with the right of the
7 general partners to carry on the business of the partnership. *Id.* 1453. Because the basis for the lawsuit
8 was that the general partners had declined to carry on the business of the partnership, the derivative action
9 claims brought by the limited partner did not interfere with that right. *Id.* Similarly, in this action Plaintiff is
10 alleging claims on behalf of the Partnership based on DeBartolo's failure to conduct the business of the
11 partnership in a satisfactory manner. Under *Wallner*, Mieuli is not barred by § 15526 from bring derivative
12 claims on behalf of the Partnership.

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14 **E. Demand Requirement**

15 Defendant asserts that Plaintiff's derivative claims should be dismissed because they do not satisfy
16 the demand requirement under Fed. R. Civ. P. 23.1. That rule provides that where a shareholder brings a
17 derivative claim:

18 The complaint shall . . . allege with particularity the efforts, if an, made by the plaintiff to obtain the
19 action the plaintiff desires from the directors or comparable authority . . . and the reasons for the
20 plaintiff's failure to obtain the action or for not making the effort.

21 Fed. R. Civ. P. 23.1. While Rule 23.1 governs pleading requirements for derivative claims, state
22 substantive law is generally the source of the demand requirement for derivative claims in diversity actions.
23 *Kamen v. Kemper*, 500 U.S. 90, 97 (1991). Therefore, in determining the adequacy of the pleadings,
24 state law governing demand and futility should be applied. *Country National Bank v. Mayer*, 788
25 F.Supp. 1136, 1140 (E.D. Cal. 1992). Because the general partner, S.F. Inc., is a California Corporation,
26 California law should be applied in determining the adequacy of the pleadings on demand and futility.

27 Under California law, a derivative action generally must be brought by the board of directors. *Id.*
28 at 1144. The decision of whether the board shall bring a derivative action falls under the business
judgment rule. *Id.* Under this rule, a director is not liable for a mistake in business judgment which is made

1 in good faith and in what he or she believes to be the best interests of the corporation. *Id.* Further, courts
2 presume that in making a business decision, the directors of a corporation acted on an informed basis, in
3 good faith and in the honest belief that the action was taken in the best interests of the company. *Lamden*
4 *v. LaJolla Shores Clubdominium Homeowners Ass’n*, 72 Cal. Rptr. 2d 906, 915 (1998). Therefore, a
5 plaintiff challenging the board’s decision “has the burden of showing the decision involved a conflict of
6 interest, or was made in bad faith (e.g. fraudulently) or without the requisite degree of care and diligence.”
7 *Id.* (citation omitted).

8 Where a shareholder has made a formal demand and the company has refused to act on that
9 demand, a shareholder, in order to survive a motion to dismiss under Rule 23.1, must allege both that a
10 demand was made and particular facts that create a reasonable doubt that the board’s refusal was in fact
11 made on an informed basis, in good faith, and with the corporation’s best interests in mind. *See Stepak v.*
12 *Addison*, 20 F.3d 398, 403 (11th Cir. 1994); *Findley v. Garrett*, 109 Cal. App. 2d 166, 177-78 (1952);
13 *Levine v. Smith*, 591 A.2d 194, 211 (Del. 1992). Conclusory allegations that the board’s refusal to act
14 was wrongful are insufficient to satisfy the requirements of Rule 23.1. *Stepak*, 20 F.3d at 403.

15 Alternatively, the requirements of Rule 23.1 may be satisfied where a shareholder alleges specific
16 facts showing that it would have been futile to make a demand on the corporation. *Country National Bank*
17 *v. Mayer*, 788 F. Supp. 1136, 1144 (E.D. Cal. 1992). Conclusory allegations of fraud, conspiracy or bad
18 faith on the part of the directors is insufficient to satisfy the futility requirement. *Id.* at n. 16. On the other
19 hand, an allegation that the president of the board dominated the board and that his interests were adverse
20 to that of the plaintiff have been found to suffice. *Id.* A plaintiff may also satisfy the demand requirement by
21 alleging facts showing that a majority of the board were not disinterested and therefore, demand would
22 have been futile. *Id.* at 1145-1146.

23 Here, Plaintiff asserts in his Opposition that he has alleged specific facts showing that demand
24 would have been futile. Opposition at 17-18. Plaintiff points to the allegation in his FAC that “[t]he
25 Corporation has repeatedly informed plaintiff that it is not willing to participate in this litigation. Demand
26 upon the Corporation to do so would therefore be futile.” FAC at 8, ¶ 38. Plaintiff also argues that the
27 current general partner of the limited partnership is the “only authority competent to file suit on behalf of the
28 Partnership.” Opposition at 18. Therefore, Plaintiff asserts, “a clearer case of futility would be difficult to

1 imagine.” However, Plaintiff has failed to plead specific facts which show that the general partner, or at
2 least a majority of the board of directors of the general partner, are not disinterested. *See In re Silicon*
3 *Graphics Inc. Securities Litigation*, 183 F.2d at 990. Therefore, Plaintiff has not adequately pleaded
4 futility.

5 Nor does the case cited by Plaintiff, *Nussbacher v. Continental Nat’l Bank and Trust Co. of*
6 *Chicago*, 518 F.2d 873, 877 (7th Cir. 1975) provide support for Plaintiff’s position. There, the court of
7 appeals found that plaintiff’s allegation of futility was adequate where plaintiff alleged that after she
8 commenced an identical action in another jurisdiction, the board of directors had met to discuss whether
9 they would join in the litigation and decided that it would be contrary to the interests of the corporation to
10 participate. *Id.* at 875. She also alleged that a majority of the board members participated in the illegal
11 acts alleged. *Id.* Finally, the chairman of the board had submitted an affidavit to the district court stating
12 that if the plaintiff had proposed that the corporation commence the action at issue, the board would not
13 have done so, and further stating that he had conferred with the other members of the board and that they
14 were in agreement with him.” *Id.* at 876. Here, no such particular allegations have been made and there is
15 no indication as to whether or not the board of directors of the general partner ever considered whether or
16 not to participate in this action.

17 The Court finds that Plaintiff has failed to comply with the requirements of Rule 23.1 with respect to
18 Claims Four through Seven. These claims are therefore dismissed with leave to amend to plead specific
19 facts showing that either: 1) a formal demand was made upon the board of directors of the general partner
20 and the board wrongfully rejected that demand; or 2) it would have been futile to make a demand upon the
21 board of directors.⁶

22
23 **F. California Business and Professions Code § 17200**

24 Defendant asserts that Plaintiff’s § 17200 claim is predicated upon his other claims and that
25 because Plaintiff has failed to state any valid claims, his § 17200 claim must be dismissed as well. To the
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27 ⁶ Although Plaintiff’s FAC and Opposition indicate that Plaintiff was seeking to comply with Rule 23.1
28 by pleading futility, at oral argument, Plaintiff appeared to take the position that Plaintiff had, in fact, made a
formal demand upon the board of directors and that the demand had been rejected.

1 extent that Plaintiff has stated other valid claims, as indicated above, his § 17200 claim also will not be
2 dismissed on this motion.

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4 **IV. CONCLUSION**

5 Defendant's Motion To Dismiss is therefore DENIED with respect to Claims One, Two, Three and
6 Eight. Defendant's Motion is GRANTED with respect to Claims Four through Seven, with leave to amend
7 within thirty (30) days to plead with particularity that the demand requirement of Fed. R. Civ. P. 23.1 has
8 been met.

9 IT IS SO ORDERED.

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11 Dated: January 16, 2001

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JOSEPH C. SPERO
United States Magistrate Judge

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