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Case No. 4948-VCL

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

UNIVERSAL ENTERPRISE GROUP, L.P.; 617 NORTH SALISBURY BOULEVARD, LLC; 176 FLATLANDS ROAD, LLC; 106 CEDAR STREET, LLC; 102 WEST CENTRAL AVENUE, LLC; 326 EAST DOVER STREET, LLC; 101 MAPLE AVENUE, LLC; 241 CYPRESS STREET, LLC; 28768 OCEAN GATEWAY HIGHWAY, LLC; 610 SNOW HILL ROAD, LLC; 5318 SNOW HILL ROAD, LLC; 302 MAPLE AVENUE, LLC; 177 OLD CAMDEN ROAD, LLC; 111 SOUTH WEST STREET, LLC; 1272 SOUTH GOVERNORS AVENUE, LLC; 505 BRIDGEVILLE HIGHWAY, LLC; 323 WEST STEIN HIGHWAY, LLC; 100 SOUTH MAIN STREET, LLC; 1104 SOUTH STATE STREET, LLC; 133 SALISBURY ROAD, LLC; UNIVERSAL DELAWARE, INC.; and DANIEL SINGH a/k/a DAMINDER S. BATRA;	)	
Plaintiffs,	)	
v.	)	C.A. No. 4948-VCL
DUNCAN PETROLEUM CORPORATION and ROBERT M. DUNCAN;	)	
Defendants.	)	

MEMORANDUM OPINION

Date Submitted: April 4, 2013
Date Decided: July 1, 2013

John V. Fiorella, Jennifer L. Dering, ARCHER & GREINER, P.C., Wilmington, Delaware; Alan. S. Fellheimer, John J. Jacko, III, Susan M. O, FELLHEIMER & EICHEN LLP, Philadelphia, Pennsylvania; *Attorneys for Plaintiffs*.

Daniel F. Wolcott, Jr., Ryan M. Murphy, Janine L. Hochberg, POTTER ANDERSON & CORROON LLP, Wilmington, Delaware; *Attorneys for Defendants*.

LASTER, Vice Chancellor.

The plaintiffs contend that the defendants made factual representations in a written agreement for the sale of a business that turned out to be wrong. They sued for fraud and breach of contract. At trial, the plaintiffs proved that the defendants knew their representations were false, but the plaintiffs failed to prove reliance and therefore could not establish fraud. Judgment consequently is entered in favor of defendants on Counts I, II, III, and V.

The plaintiffs did not need to establish reliance for their breach of contract claim. Rather, such a claim is governed by the terms of the contract itself. The plaintiffs proved that the defendants' false representations breached the contract and resulted in actual damages of $1,497,429. Judgment is therefore entered in their favor on Count VI. Because of pending bankruptcies involving certain of the plaintiffs, judgment is reserved on Count IV and defendants' counterclaims.

I. FACTUAL BACKGROUND

Over the course of four trial days, the parties adduced live testimony from five fact witnesses and five expert witnesses, submitted deposition testimony from seven witnesses, and introduced over 500 exhibits. The plaintiffs bore the burden of proof. Having evaluated the testimony, weighed credibility, and considered the evidence as a whole, I make the following factual findings.

A. Duncan Petroleum

Defendant Robert M. Duncan started out in the soda bottling and distribution business. Beginning in 1971, Duncan began assembling a network of gasoline service stations and convenience stores to complement his soda business. He later formed and

served as President and sole stockholder of defendant Duncan Petroleum Corp. ("Duncan Petroleum" or the "Company"). During the following decades, Duncan Petroleum assembled a portfolio of nineteen gas stations and associated real estate located in Delaware and the eastern shore of Maryland (the "Properties").

B. Regulatory Difficulties

When Duncan first entered the petroleum business, it was not heavily regulated. Over time, the extent of federal and state oversight expanded dramatically to include extensive recordkeeping requirements, routine agency inspections, and the mandated use of safety and compliance equipment, particularly for underground storage tanks ("USTs") used to store gasoline. The eight Delaware Properties had to comply with the Delaware Regulations Governing Underground Storage Tanks, which were enforceable by both the Delaware Department of Natural Resources and Environmental Control ("DNREC") and the U.S. Environmental Protection Agency ("EPA"). The eleven Maryland Properties had to comply with similar Maryland regulations, which were enforceable by both the Maryland Department of the Environment ("MDE") and the EPA. Among other things, the governing regulations required that Duncan Petroleum maintain a functioning automatic tank gauge ("ATG") system for the USTs that monitored the level of gasoline in the tanks and detected leaks.

During the years leading up to the sale of his business, Duncan managed his regulatory responsibilities poorly. He kept spotty records, and his relations with regulators often became confrontational. Although his inadequacies in these areas do not appear to have translated into unsafe operations or environmental spills, Duncan's

regulatory shortcomings resulted in the Properties receiving numerous citations and adverse reports. The following examples provide a sense of the pervasiveness of the problems.

1. Property No. 1: 102 West Central Avenue

Between January 2003 and April 2005, MDE inspection reports noted violations on at least six occasions at the Property at 102 West Central Avenue, Federalsburg, Maryland. Violations included failed ATG results, nonfunctioning ATG equipment, lack of an ATG probe, unavailable leak detection records, torn fuel hoses, and spill catch basins containing liquid product. In March 2007, MDE performed a follow-up compliance check and found that although inventory records were being maintained, the ATG system was not functioning properly, and the station operator indicated that the ATG system had not been operational for approximately three to four months.

2. Property No. 2: 241 Cypress Street

In June 2003, MDE issued a notice of violation for the Property at 241 Cypress Street, Salisbury, Maryland. A case summary report dated July 17, 2003, stated:

> This site does not perform proper leak detection records. The Federal EPA [is] also involved with the owner, Mr. Bob Duncan. Mr. Duncan ignores the regulations and does what he feels like doing. Duncan Petroleum should not be allowed to operate in the State of Maryland due to the large number of violations at his facilities.

JX 233. MDE issued two additional notices of violation for the Property in December 2005.

3. Property No. 3: 617 North Salisbury Boulevard

In August 2007, ATS Environmental Services, an MDE Certified Inspector,

examined the Property at 617 North Salisbury Boulevard, Salisbury, Maryland. The report noted the following violations: failure to install an emergency stop button, failure to test catch basins, sumps, and dispenser pans, failure to protect vent pipes from traffic, and failure to maintain monitoring site wells.

4. Property No. 4: 610 Snow Hill Road

In September 2006, MDE identified eleven violations at the Property at 610 Snow Hill Road, Salisbury, Maryland. The problems included a broken pipe seal, cracked and worn hoses, non-functional hose retractors, the existence of petroleum vapors, and lack of maintenance records.

5. Property No. 5: 106 Cedar Street

During 2006 and 2007, MDE cited the Property at 106 Cedar Street, Cambridge, Maryland on multiple occasions for improperly abandoning two USTs. MDE declined to pursue the violations only after Duncan agreed to sell the Property.

6. Property No. 7: 302 Maple Avenue

In 2005 and 2006, MDE cited the Property at 302 Maple Avenue, Chestertown, Maryland for violations including a lack of monitoring wells, functioning ATG system, and safety equipment, and failure to document overfill devices and release detection systems. In May 2007, MDE noted that inventory records were not being properly reconciled, the ATG system was still not operating, and certain requested records had not been received.

7. Property No. 8: 176 Flatlands Road

In February 2007 and again in August 2007, MDE noted compliance violations for

the Property at 176 Flatlands Road, Chestertown, Maryland. Violations included problems with the ATG system.

8. Property No. 9: 1272 Governor Avenue

In April 2003, DNREC issued a Compliance Inspection Warning Letter for the Property at 1272 Governor Avenue, Dover, Delaware. In June 2004, DNREC issued an additional warning letter. In June 2007, DNREC inspected the Property and cited issues including cracked piping and problems with the ATG system.

9. Property No. 11: 326 East Dover Street

In 2003, MDE noted that monthly inventory records were not being maintained for the Property at 326 East Dover Street, Easton, Maryland. In February 2007, MDE found that the ATG system was out of paper and therefore not generating records.

10. Property No. 12: 101 Maple Avenue

During 2004, MDE cited the Property at 101 Maple Avenue, Preston, Maryland for violations on three occasions. Problems included a failure to maintain the ATG system, piping, and catch basins, and a failure to maintain release detection records.

11. Property No. 13: 323 West Stein Highway

In 2001, DNREC notified Duncan that he needed to install two monitoring wells at the Property at 323 West Stein Highway, Seaford, Delaware. The wells were never installed.

12. Property No. 14: 1104 South State Street

In March 2004, DNREC inspected the Property at 1104 South State Street, Dover, Delaware and noted numerous violations. In March 2007, DNREC noted that the USTs

had been out of service since October 2006 and that leak detection records had not been maintained.

13. Property No. 15: 133 Salisbury Road

In March 2004, DNREC inspected the Property at 133 Salisbury Road, Dover, Delaware and noted numerous violations. In March 2007, DNREC inspected the Property and identified a slow leak from a dispenser.

14. Property No. 16: 111 South West Street

In 2003 and 2006, DNREC inspected the Property at 111 South West Street, Dover, Delaware and noted numerous violations. In June 2007, DNREC noted problems with the method of overfill protection.

15. Property No. 17: 505 Bridgeville Highway

In 2002 and 2003, DNREC inspected the Property at 505 Bridgeville Avenue, Seaford, Delaware and noted multiple violations.

16. Property No. 19: 100 South Main Street

In April 2002, Duncan was fined $2,500 for operating the Property at 100 South Main Street, Bridgeville, Delaware without a permit. An additional fine of $2,500 was suspended on the condition that Duncan not have any DNREC enforcement actions for a year. In April 2003, DNREC cited numerous violations relating to spill buckets, adaptors, annual vapor leak testing, and recordkeeping. In June 2007, DNREC cited the Property for problems with its sumps, a missing UST sensor, and non-functioning ATG equipment.

17. Property No. 20: 5318 Snow Hill Road

In 2005, MDE cited the Property at 5318 Snow Hill Road, Snow Hill, Maryland for improperly abandoning USTs. In February 2007, MDE again cited the Property for failure to maintain proper inventory records and failure to perform proper leak detection tests.

18. Federal Violations

In September 2004, the EPA filed an administrative complaint against Duncan because of compliance issues at five Properties. The EPA and Duncan resolved the action by entering into a Consent Agreement and Final Order in February 2006 (the "CAFO"). Under its terms, Duncan agreed to pay a $65,000 fine, conduct regular inspections and tests of the USTs at the five Properties, and submit periodic reports and records to the EPA.

Duncan initially attempted to comply with the CAFO by sending informal notes to the EPA. By letter dated April 7, 2006, the EPA informed Duncan that his submissions did not comply with the CAFO's requirements, that he had to make formal submissions that adhered to the specific procedures set forth in the CAFO, that his cathodic protection testing report was insufficient, that the covered USTs must be inspected by a certified corrosion expert, and that he was required to conduct the tightness testing called for by the CAFO. The EPA noted that "[g]iven [Duncan Petroleum's] poor record of compliance with the release detection requirements, it [was] necessary to use this more sensitive testing to assure [the] EPA and the public that none of [Duncan Petroleum's] tanks [were] leaking," and that Duncan had to conduct the testing "whether or not [he]

agree[d] with the wisdom behind it." JX 162 at 2. The EPA warned Duncan of "potentially severe consequences if [Duncan Petroleum did] not comply with the [CAFO]," including possible penalties of up to $32,500 per day of noncompliance. *Id.* at 3.

By letter dated November 1, 2006, the EPA again wrote Duncan, this time copying the Department of Justice, and notified him that Duncan Petroleum had "not complied with all of [the] Compliance Tasks" set forth in the CAFO, that the violations were "serious and inexcusable," and that Duncan Petroleum could face "civil penalties of up to $32,500 per day of continued noncompliance." JX 178 at 1, 5. The EPA insisted that Duncan "take *immediate* measures to comply with the [CAFO]," including the required tightness testing. *Id.* at 6.

In response, Duncan told the EPA that he had hired Coastal Pump and Tank to perform the tightness testing. He also represented that he had arranged for the Properties to be certified by INCON, a petroleum monitoring systems provider. During his deposition, Duncan admitted that he never conducted tightness testing for any of the required tanks. Although Duncan claimed that he explained to the EPA that he could not perform the tightness testing because it was physically and economically impossible, he testified at trial that such tests were performed at one of the other Properties. Duncan also admitted that none of the Properties were certified.

Because of Duncan's inadequate compliance with the CAFO, the EPA began investigating twelve other Properties. Between February and August 2007, the EPA issued Requests for Information about numerous compliance violations and equipment

problems found during inspections. Duncan gave cursory answers and did not provide the requested documentary support.

C. Duncan Decides To Sell.

In early 2007, contemporaneously with the increasing regulatory interest in his business, Duncan decided to sell the Properties and retire from the petroleum industry. He hired John Sartory of PetroProperties & Finance LLC, a broker for gas station assets, to market the Properties. Sartory prepared a prospectus, advertised the Properties, and fielded inquiries.

The language of the prospectus informed any interested party that the Properties were not exactly pristine, stating:

> While the Duncan Petroleum Corporation's sites include numerous positive investment highlights, the retail network and Company as a whole is [sic] deficient in certain critical organizational, marketing and design areas . . . . These deficiencies have led to a marketing situation in which total network motor fuel volume has declined by almost 2.5 million gallons over the last three years.

JX 23 at 5. Among other things, the prospectus noted that "the Company has never established standards of appearance or operational guidelines for its dealers and lacks the internal staff to properly supervise its network." *Id.* The prospectus advised that "[g]iven the various operational requirements of the chain, it is recommended that offers be formulated based upon a purely real estate assessment and valuation." *Id.* at 4. To emphasize the latter point, the prospectus noted that the sellers would not share any cash flow or profit and loss data and that "[t]hese units are being marketed purely as a real estate purchase and lease opportunity." *Id.* at 6.

At several points, the prospectus stressed that Duncan would be "very flexible" as to the structure of a transaction and would consider a sale, a long-term lease of certain Properties, and seller financing for a portion of the purchase price. JX 23 at 4, 6. But, Duncan was not willing to retain any aspect of the business involving environmental oversight: "[U]nder all circumstances, any lease or purchase offer should include a provision in which the Buyer/Tenant will purchase all of the existing petroleum dispensing and underground tank storage equipment at each location." *Id.* at 6.

One of the interested parties was plaintiff Universal Enterprise Group, L.P., which operated gas stations and convenience stores in Pennsylvania, Delaware, and New Jersey. Plaintiff Daniel Singh a/k/a Daminder S. Batra ("Batra") controlled Universal Enterprise Group, L.P. and a network of related entities (collectively, "Universal"). Universal Marketing, Inc., one of Universal's affiliates, distributed gasoline to approximately 500 service stations.

In spring 2007, Batra discussed the Properties with Sartory. Batra was exploring various opportunities, but he liked the Properties because they were close to Universal's other retail operations. Before submitting an offer, Batra personally visited the Properties. He evaluated the Properties, assessed their competition, estimated the volume of customer traffic, and considered whether they could be improved. Batra concluded that the Properties had been neglected. They were located in heavily trafficked areas, and Batra thought he could generate substantial returns by enhancing the customer experience and making basic improvements in lighting, roofing, and signage. Batra also anticipated margin growth because of economies of scale from being part of Universal. He thought

the deal offered "tremendous upside." Tr. 76.

D. The Sale Agreement

Batra initially offered to purchase the Properties for $8 million. After negotiations, Batra and Duncan agreed on a price of $16 million. On July 31, 2007, Duncan and Batra signed an agreement for the sale of the Properties. *See* JX 27 (the "Sale Agreement" or "SA"). Universal was designated as the "Buyer," and Duncan Petroleum and Duncan were defined jointly as the "Seller." *Id.* at 1. For simplicity, I will refer only to Duncan. Each side was represented by counsel of its choice: R. Brandon Jones of Hudson, Jones, Jaywork & Fisher, LLC represented Duncan, and Gary A. Zlotnick of Zarwin, Baum, DeVito, Kaplan, Schaer, Toddy, P.C. and Robert D. Fox of Manko, Gold, Katcher & Fox, LLP ("Manko Gold") represented Universal. Jones and Zlotnick were traditional business lawyers; Fox specialized in transactions involving real estate and petroleum marketing.

Under the terms of the Sale Agreement, Universal paid $500,000 in earnest money at signing and would pay another $7.5 million in cash at closing, to be financed through a loan from TD Bank. SA at 4-6. The remaining $8 million would take the form of seller financing. Universal would acquire each Property through a separate special purpose entity ("SPE"), and each SPE would sign a promissory note in favor of Duncan for its allocated portion of the outstanding $8 million balance (collectively, the "Notes"). Each Note would bear interest at 7% and provide for monthly payments of principal and interest based on a twenty-year amortization schedule, with a balloon payment after five years. *Id.* at 5. Batra would personally guarantee the Notes. *Id.* The Notes would be

subordinated to the financing provided by TD Bank.

The Sale Agreement contemplated a sixty-day due diligence period during which Universal would have the opportunity to conduct a comprehensive investigation of the Properties. SA at 7. Duncan agreed to permit Universal to inspect the Properties and conduct site visits and take environmental samples. *See id.* at 8. Duncan also agreed that "[i]n response to Buyer's reasonable request, Seller shall supply such documentation as Seller has or can readily obtain from third parties, to permit Buyer to complete such inspections and review in a timely manner." *Id.* Duncan further committed to provide Universal with his environmental files and disclosed the CAFO:

> (d) *Copies of Seller's Files*. In connection with the preparation of any environmental assessment report desired by Buyer, during the sixty (60) day Due Diligence Period, Seller shall allow the Buyer, its employees, consultants or agents to inspect the Seller's environmental books and records and make available copies of the same.
>
> (1) Seller shall supply Buyer with a copy of previously completed phase II reports, analyses or studies of any of the subject Properties. . . .
>
> (2) Seller hereby discloses unto the Buyer that on or about February 14, 2006 Duncan Petroleum Corp. entered into a consent agreement with the [EPA] resolving an administrative enforcement matter and in regard thereto paid a $65,000.00 fine.

Id. at 9 (the "Seller Files Covenant"). To back up the Seller Files Covenant, a representation in the Sale Agreement stated:

> The Seller has made its environmental files relating to the Property available to the Buyer, including without limitation existing phase I and phase II environmental studies and those additional file materials in its possession which the Seller

> believes in good faith accurately reveal the known environmental condition of the Property.

Id. at 18. The Sale Agreement provided that if Universal's due diligence revealed problems such that "in Buyer's sole discretion . . . Buyer's intended purchase and use of the Propert[y] would not be economically feasible or otherwise desirable," then Duncan would have an opportunity to "cure same to Buyer's satisfaction within thirty (30) days . . . ." *Id.* at 7. Absent cure, Universal could terminate the Sale Agreement. *Id.*

In addition to granting Universal the right to conduct due diligence, Duncan made certain representations about the condition of the Properties. For environmental matters, Duncan represented that except as disclosed in documents provided pursuant to the Seller Files Covenant, the following statement was true:

> To the best of the Seller's knowledge, the Seller has received no notice as of the Effective Date of the Agreement from DNREC or MDE requiring the Seller to undertake environmental corrective or remedial actions . . . and to the best of the Seller's actual knowledge, the Property is in compliance with all applicable Environmental Laws.[1]

SA at 23 (the "Environmental Compliance Representation"). This representation was followed by a cautionary acknowledgement:

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[1] The Sale Agreement defined "Environmental Laws" to mean "all federal, state or local laws, statutes, ordinances, codes, rules, regulations, directives or polices and common law relating to the environment and protection of health in the broadest sense, including but not limited to those governing or otherwise relating to land, water, erosion and sedimentation, air, health and safety to humans and animals, natural resources, or the use, handling, generation, treatment, storage, recycling, transportation, Release or disposal of any Hazardous Materials, including without limitation, CERCLA, RCRA, the Tank Act, HSCA, the CWA, ECLS, HWMA, SWAA, Delaware Storage Tank Act, EHSRMA, HSCA, EPCRKA, WPCA, WMHA, and WISF." SA at 27.

> Notwithstanding any of the Seller's representations contained herein, the Buyer acknowledges the Property has for many years been used as retail motor fuel and convenience store facilities, with underground petroleum storage systems. As such, there is [sic] existing Hazardous Materials under the Real Estate Properties and the Buyer should conduct its own investigation of the condition of the subsurface, soil and groundwater beneath the Real Estate Properties.

Id. at 18. Despite this caution, Duncan represented via the Environmental Compliance Representation that to his knowledge, except as shown in the documents he would provide to Universal, the Properties were "in compliance with all applicable Environmental Laws." *Id.*

Duncan also made other representations that potentially touched on environmental issues. One was the absence of litigation, including investigations: "There are no actions, suits, proceedings or investigations pending or, to the knowledge of Seller, threatened at law or in equity . . . which affect any portion of the Property." SA at 20. Another was that the Properties were operated and maintained in compliance with the law:

> To the best of the Seller's knowledge, information and belief, all laws, ordinances, rules, regulations and orders (including, without limitation, to [sic] those relating to . . . environmental control protection) of any government or any agency, body or subdivision . . . bearing on construction, operations or use of the Property . . . have been and . . . will be complied with by Seller; Seller has received no notice and has no knowledge that any such government, agency, body or subdivision . . . or any employee or official thereof considers the construction or completion of the Property or the operation or use of the same to have violated any such law, ordinance, rule, regulation, order, standard of regulation, [sic] that any investigation has been commenced or is contemplated respecting any such possible violation; that all notices, licenses, permits,

> certificates and authority required in connection with the construction, completion, use or occupancy of the Property or any part thereof have been obtained and are, and on the date of Closing will be, in effect, and in good standing.

Id. at 23.

The Sale Agreement backstopped Duncan's specific representations by warranting that the sell-side representations were true and not materially misleading.

- Section 11(t): "To the best of the Seller's knowledge, information and belief, neither this Agreement . . . or any other information, report or statement furnished or delivered to Buyer by Seller contains any untrue statement or omits to state a material fact necessary to make the statements herein or therein not misleading. Seller has disclosed all material facts which are known to the Seller relating to ownership, operation and maintenance of the Property." SA at 20.

- Section 11(ii): "No representation or warranty by Seller contained in this Agreement . . . or other instrument furnished or to be furnished to Buyer . . . shall contain, any untrue statement of material fact to the best of the Seller's knowledge, information and belief." *Id.* at 26.

In substance, these representations built into the Sale Agreement the standard for a false representation under common law.

Section 13 of the Sale Agreement added specific provisions addressing how the parties would achieve "Closure" on any environmental matters identified during due diligence. SA at 29. It stated:

> Seller acknowledges during the Buyer's Due Diligence Period that there are or may be Hazardous Materials discovered on, under or migrating from one or more of the Real Estate Properties that was caused or created by the prior use and occupancy of the Property by the Seller and/or its operators ("Existing Contamination"), and that current applicable Environmental Law may require monitoring, well

> installations, tests, inspections, borings, remediation operations and/or other activities hereinafter referred to as environmental "Corrective Action." Seller agrees to conduct such Corrective Action on those Real Estate Properties identified during the Due Diligence Period as requiring Corrective Action in accordance with existing Environmental Laws or regulations. The Seller's obligation to complete said Corrective Action shall be limited to the Existing Contamination.

Id. If there was a need for Corrective Action, Duncan would select an environmental consulting company that would develop a Corrective Action plan and offer Universal an opportunity to comment or obtain consideration for the plan from DNREC or MDE. *Id.* at 30. At closing, Duncan would place in escrow an agreed-upon amount of funds sufficient to cover any Corrective Action, and those funds would be "used to reimburse the environmental consultant . . . for costs necessary to complete all post closing Corrective Action activities identified prior to closing." *Id.* If there was a determination by DNREC or MDE that no further Corrective Action was required, that determination would be "conclusive and binding." *Id.* at 29. Once the Corrective Action was complete at a given Property, then "except for Claims resulting from the breach of this Agreement and Seller's indemnity obligation hereunder," Duncan would have "no further obligation or liability to the Buyer for any Claim, demand or cause for action related to or arising out of, any and all Existing Contamination at said Real Estate Property." *Id.*

E. Universal Conducts Due Diligence.

On August 3, 2007, Universal retained Delta Environmental Consultants, Inc. ("Delta") to perform Phase I Environmental Site Assessments ("Phase I ESAs") and UST System Compliance Evaluations ("UST Evaluations") at the Properties. The purpose of

the Phase I ESAs was to determine whether any of the Properties had a recognized environmental condition ("REC"), defined as

> the presence or likely presence of any hazardous substances or petroleum products on a property under conditions that indicate an existing release, a past release, or a material threat of a release of any hazardous substances or petroleum products into structures on the property or into the ground, ground water, or surface water of the property.

JX 8 at 4. The purpose of the UST Evaluations was to "evaluat[e] [Duncan's] compliance with applicable state and federal requirements related to leak detection, corrosive protection, overfill prevention and spill prevention." *Id.* at 33.

The same day, Delta provided Universal with an engagement letter that identified the four components of the Phase I ESAs: (i) a review of records, (ii) site reconnaissance, (iii) interviews with personnel, and (iv) preparation of a report. Delta understood that depending on the conclusions of the Phase I ESAs, Universal would decide whether to proceed with further investigation. The UST Evaluations consisted only of "an office review of available [UST] system records provided by the current owners . . . ." JX 8 at 33. On August 4, Universal returned the executed engagement letter. Universal's environmental counsel, Manko Gold, supervised Delta's efforts.

On August 6, 2007, Universal instructed Delta to fully exercise Universal's information rights under the Sale Agreement, including inspecting Duncan's existing environmental records and any historical phase II reports. Universal's email noted that Duncan had disclosed a consent agreement with the EPA, namely the CAFO, and told Delta to "get a copy" of it along with "any other information" reasonably related to

environmental matters. JX 33 at 1. Delta gave Universal a due diligence request list and questionnaire, which Universal forwarded to Duncan on August 7. While waiting to receive documents and responses to the questionnaires, Delta began planning internally to conduct site visits. Duncan eventually returned the questionnaires and produced five or six boxes of documents.

F. Missing Documents

On August 16, 2007, Universal noted that they only had leases for four of the nineteen Properties. Delta identified other gaps in the production:

> We have some environmental reports for [one Property], but it appears there may be recent work . . . , which is not in the file.
>
> There are two Maple Ave. sites; neither file has any environmental reports or data. . . .
>
> The files we got from Duncan are pretty thin. I asked [Duncan] if we had the environmental files, too, and he said they hadn't had any releases or environmental issues (!).

JX 39 at 1. When Universal followed up with Duncan, he said he provided Delta "with copies 'of all that he ha[d].'" *Id.* at 2.

Shortly thereafter, Delta learned that MDE was investigating eight of the Properties. On August 23, 2007, MDE suggested that Delta request state records, but Delta never made the request. Delta also never visited Duncan's offices to physically search for or collect additional documents.

On August 24, 2007, before completing the Phase I ESAs, Delta recommended expanding the scope of due diligence to include Phase II Environmental Study

Assessments ("Phase II ESAs"). Delta argued that the more extensive Phase II ESAs were necessary, in part, because of Duncan's limited records. In the Phase II ESAs, Delta would "reasonably investigate current soil and ground water conditions" at each Property "for evidence of environmental conditions that indicate the presence or release of hazardous substances or petroleum." JX 1 at 3.

Expert testimony at trial established that it is not customary for an environmental consultant to begin a Phase II ESA before completing a Phase I ESA. Nevertheless, Delta made its recommendation, Universal agreed to it, and Delta proceeded to conduct its Phase I and Phase II ESAs simultaneously. As part of the Phase II ESAs, Delta conducted soil and groundwater testing at seventeen of the nineteen Properties.

Delta's preliminary work indicated potential environmental problems. For example, on September 4, 2007, Delta reported that its soil drillings at one of the Properties in Delaware yielded potentially hazardous material. Delta recommended that Duncan report the information to DNREC.

On September 14, 2007, Duncan supplemented his earlier production by providing nineteen additional sheets of paper, one for each Property. On each sheet, Duncan addressed in cursory bullet-points (i) whether the lease was written or oral, (ii) what the monthly rent was, (iii) what the approximate dealer margins were, and (iv) whether other tenants leased the Property.

On September 21, 2007, Delta produced drafts of the Phase I ESAs. Delta had not requested or reviewed any files from DNREC or MDE. Universal was not happy and believed that Delta had agreed to conduct "File Reviews," whereby Delta would ask for,

obtain, and review records from DNREC and MDE. JX 59 at 5. Delta disagreed and claimed that File Reviews were "out of the scope" of a Phase I ESA. *Id.* at 4. Delta blamed Duncan's poor recordkeeping for the disagreement and suggested that if Duncan had kept better records, no one would be asking for the File Reviews.

> [T]he current owner had very spotty records, and there was no historic data provided for the majority of sites. I don't think the current owner deliberately withheld data, his records were just poor. He sent us his original files for the sites, and it appeared he has simply removed the hanging folders from the cabinets and put them in boxes.

Id. at 3.

The evidence at trial established that in the ordinary course of business, a typical operator of multiple gas stations engages in extensive regulatory and compliance efforts. Duncan's compliance efforts were less formal and fell short of Delta and Universal's expectations. The evidence at trial also established that Delta regarded Phase I ESAs as relatively low-margin, low-risk work and had taken steps internally to maximize profits by cutting corners and minimizing costs. Delta's desire to do as little as possible and preferably only what was absolutely necessary to conduct a Phase I ESA explains Delta's resistance to conducting the File Reviews, its failure to follow-up on red flags at the Properties, and its recommendation to move immediately to the more intensive and lucrative Phase II ESAs and conduct them in parallel with the Phase I ESAs.

To resolve the dispute over the File Reviews, Delta agreed to request documents from DNREC and MDE and address the results in a supplement, which would mitigate the problem of Duncan's limited records. On September 27, 2007, Delta mailed

information requests to the state agencies.

The holes in Duncan's records, snags in the document collection process, and Delta's recommendation to proceed immediately to Phase II ESAs delayed the completion of the due diligence process. To give Universal additional time, the parties amended the Sale Agreement to extend the due diligence deadline to October 31, 2007.

G. Delta Delivers Its Reports.

On September 27, 2007, before completing either the Phase I ESAs or conducting the File Reviews, Delta delivered the Phase II ESAs. In the Phase II ESAs, Delta identified soil or groundwater contamination at all seventeen Properties examined (the "Contaminated Sites"). Section 13 of the Sale Agreement obligated Duncan to take Corrective Action at each of the Contaminated Sites. Delta recommended that Duncan notify DNREC and MDE about the results of its tests.

On October 10, 2007, Delta delivered its Phase I ESAs and UST Evaluations. The Phase I ESAs identified RECs at all nineteen Properties. The Phase I ESAs also identified numerous "data gaps," which Delta blamed on Duncan's recordkeeping. The data gaps included missing records relating to:

- the existence of partially-buried drums and how Duncan historically handled petroleum and hazardous products;
- soil and groundwater conditions during removal and replacement of USTs;
- post-excavation samples for six of eight permanently out of use tanks;
- the condition of USTs and any soil testing data during removals in 1976 and 1996;
- two removed USTs named in state records; and

- the potential for environmental liens on several of the Properties.

See JX 1-20. The Phase I ESAs noted that Delta had sent records requests to DNREC and MDE, stated that Delta would supplement the Phase I ESAs "at a later date," but noted Delta only would do so to the extent that information received from DNREC or MDE indicated any RECs. *See, e.g.*, JX 8 at 11. The Phase I ESAs identified extensive weakness in Duncan's regulatory compliance procedures and noted that Duncan was not in compliance in several areas, including tank leak detection records, piping leak detection records, and cathodic protection test records.

In the UST Evaluations, Delta offered specific assessments and individual recommendations for each Property. The following UST Evaluation for a Property in Salisbury, Maryland is illustrative:

> The lack of maintenance, current testing, and monitoring system records is a concern. It is recommended that tank and spill bucket testing be conducted to maintain compliance with applicable MDE regulations.
>
> Due to the age of the original steel tanks (1974) [and] not having cathodic protection installed until 1997 (23 years) a more intrusive investigation of the tanks may be warranted.

JX 4 at 36.

H. The Parties Renegotiate The Transaction.

On October 12, 2007, Universal authorized Delta to provide the Phase I and II ESAs to Duncan, letting him know that Corrective Action would be needed and that he would have to escrow sufficient funds. Universal and Delta began modeling the cost. During that process, Manko Gold pointed out that Universal did not know everything

about the Properties:

> Please keep in mind that the clean up costs which are being developed by Delta are based upon the relatively limited information that we have today. As you know, information on former USTs, which existed at many of the locations, was not provided by Duncan, and will not be accessed from MDE and DNREC files until later this month. . . . Additionally, based upon the information contained in the [UST Evaluations], there will be some costs to document compliance (again because of a lack of information available from Duncan), and in some cases make station repairs to be able to demonstrate compliance, with environmental laws and regulations on a going forward basis.

JX 78 at 1. Part of what Universal and its advisors had to address was how to proceed in the face of both known unknowns and unknown unknowns.

On October 23, 2007, Delta produced a median estimate for environmental liability of $3.0 million, with a high figure of $3.7 million. On October 31, the day that the due diligence period expired, Universal told Duncan that it would proceed with the transaction only with the following modifications to the deal (the "October Modification"):

- Duncan would remediate the environmental conditions which existed at seventeen Properties investigated in the Phase II ESAs to the point where the Properties received either a "Notice of Compliance" or a "No Further Action" letter from DNREC or MDE, whichever was applicable. JX 87 at 2.

- Duncan would escrow $1.6 million of the purchase consideration to fund any Corrective Action. *Id.*

- If Duncan did not fully undertake the Corrective Action, then Universal could perform the repairs itself and offset the costs against the Notes. *Id.* at 4.

- If Duncan were found to have breached any of the "obligations, representations, indemnities, covenants, and agreements" in the transaction, Universal would have the right to offset any resulting damages against the

Notes. JX 93 at 2.

Duncan agreed. On November 15, 2007, the transaction closed.

I. Duncan Begins Corrective Action, And Delta Delivers The File Reviews.

After closing, Duncan notified DNREC and MDE of the Corrective Action planned for each Property. On January 7, 2008, DNREC informed Duncan that he would need to perform a "hydrogeologic investigation" at one of the Properties in Dover, Delaware. JX 103 at 1. Under the terms of the Sale Agreement, the hydrogeologic investigation qualified as Corrective Action to be paid for with the escrowed funds. At a second Property in Dover, Delaware, DNREC informed Duncan that no further remedial action would be necessary. Under the terms of the Sale Agreement, DNREC's determination meant Duncan had fulfilled his obligations for that Property. On January 24, DNREC approved Duncan's plan for Corrective Action involving a hydrogeologic investigation at a Property in Camden, Delaware.

Meanwhile, Delta still had not supplemented its Phase I ESAs to reflect the results of the File Reviews. When Universal followed up, Delta took the position that the closing of the transaction rendered the File Reviews superfluous. Universal insisted that Delta obtain documents from DNREC and MDE and complete its work. On February 22, 2008, Delta finally provided the supplements. They detailed a history of compliance violations at nearly all of the Properties but did not reveal any new issues.

J. The Clayton Reports

In January 2008, Universal hired a new environmental consulting firm, Clayton Services Co. ("Clayton"), to inspect the Properties. In February 2008, Clayton visited the

Properties, reviewed their environmental compliance, and produced reports (the "Clayton Reports").

On February 28, 2008, Universal gave Duncan the Clayton Reports for two Properties where Clayton had determined that USTs were non-compliant and needed to be repaired or improved. Universal contended that Duncan had failed to disclose the problems, thereby breaching representations found in the Sale Agreement. Universal demanded that Duncan fix the tanks or otherwise Universal would fix them and exercise the right of setoff against the Notes.

On April 29, 2008, Universal provided Duncan with the Clayton Reports for the remaining Properties. Universal claimed that Duncan had breached the Sale Agreement by failing to disclose a history of DNREC and MDE investigations and by having non-compliant equipment. Duncan denied knowing about any agency enforcement actions and claimed that any compliance issues arose post-closing.

For more than a year, the parties engaged in a letter writing campaign about the claims of breach. By letter dated June 2, 2009, Universal finally took the position that it would fix the compliance issues and exercise the right of setoff against the Notes. Universal claimed the cost would be approximately $1.3 million. At trial, Universal established that it actually spent $533,239, consisting of $406,293 in inspection and repair costs and $126,946 in legal fees. Universal also demonstrated that DNREC required the removal of three USTs at an estimated cost of $964,190. Universal never exercised its right to offset these amounts against the Notes.

Universal also reiterated its claim that Duncan breached the Sale Agreement by

failing to disclose a history of regulatory investigations and actions. Universal emphasized the existence of the EPA investigation and CAFO that the Sale Agreement referenced obliquely in Section 3(d)(2). Universal also argued that Duncan failed to produce his extensive correspondence with the EPA, documents relating to his significant history of DNREC and MDE investigations, or otherwise disclose those matters.

K. Universal Files For Bankruptcy.

In July 2009, one of Universal's lenders called a loan of approximately $8 million. Universal could not pay the loan and filed for bankruptcy on July 23.

After the filing, Universal's gasoline suppliers stopped delivering product to the Properties. Without product, the stations could not survive. The SPEs were consolidated into Universal's bankruptcy, and the bankruptcy estate thereby gained control over the Notes and any claims against Duncan relating to the purchase of the Properties. At this point, Universal stopped making payment on the Notes. The bankruptcy was converted into a liquidation, and Charles R. Goldstein became trustee. The trustee entered into a settlement with Batra, who assigned to the trustee his interests in Universal and any claims against Duncan.

L. The Plaintiffs Sue.

On October 5, 2009, the trustee filed this litigation against Duncan Petroleum, Duncan, and Delta. In 2010 and 2011, the Properties were sold for $8 million. In January 2011, Batra filed for personal bankruptcy. During trial, the claims against Delta were settled for $2.3 million.

II. LEGAL ANALYSIS

A party who believes that its contractual counterparty has made a false representation in a written agreement can sue for common law fraud. *Abry P'rs V, L.P. v. F & W Acq. LLC,* 891 A.2d 1032, 1057 (Del. Ch. 2006). The plaintiffs asserted claims for common law fraud in the form of fraudulent inducement (Count I) and fraudulent concealment (Count II). In Count III of the complaint, the plaintiffs asserted a separate count for equitable fraud.

To the extent their fraud claims failed, the plaintiffs sought to recover for breach of contract. In Count VI of the Complaint, the plaintiffs asserted a claim for breach of the Sale Agreement.

In Count IV of the complaint, Batra sought a declaration reducing his obligations under the Personal Guaranty Agreements that secure the Notes. Count V sought "rescission" of the Sale Agreement and related documents, which is a remedy, not a claim. The defendants' counterclaimed for amounts owed under the Notes.

These claims were tried. Judgment is entered in favor of the plaintiffs and against the defendants on Count VI, the breach of contract claim, in the amount of $1,497,429. Judgment is entered in favor of defendants on Counts I, II, III, and V. Judgment is reserved on Count IV and defendants' counterclaims pending supplemental briefing.

A. Common Law Fraud

To establish a claim for common law fraud, a plaintiff must prove (i) a false representation, (ii) a defendant's knowledge or belief of its falsity or his reckless indifference to its truth, (iii) a defendant's intention to induce action, (iv) reasonable

reliance, and (v) causally related damages. *See Stephenson v. Capano Dev., Inc.*, 462 A.2d 1069, 1074 (Del. 1983). The plaintiffs failed to prove reasonable reliance.

1. Knowingly False Representations To Induce Action

Universal proved that Duncan knowingly made a series of false representations in the Sale Agreement, including both the Environmental Compliance Representation and the more general representations about compliance with laws, the absence of litigation, and the providing of all material information. Because of the clarity and specificity of the Environmental Compliance Representation, I will not engage in duplicative analysis of the falsity of the other representations.

In the Environmental Compliance Representation, Duncan represented that

> [t]o the best of the Seller's knowledge, the Seller has received no notice as of the Effective Date of the Agreement from DNREC or MDE requiring the Seller to undertake environmental corrective or remedial actions . . . and to the best of the Seller's actual knowledge, the Property is in compliance with all applicable Environmental Laws.

SA at 23. While operating the Properties, Duncan received multiple notices from the EPA, DNREC, and MDE demonstrating Duncan's noncompliance and requiring him to undertake environmental corrective or remedial actions at the Properties.

Under the CAFO, Duncan agreed to numerous compliance tasks, including the performance of precision tank tightness testing. Duncan attempted to comply, but on April 7, 2006, the EPA informed Duncan that he was not in compliance. On November 1, the EPA reaffirmed its position that Duncan was not in compliance. Between February and August 2007, the EPA issued formal Requests for Information that noted instances of

non-compliance with environmental law. *See, e.g.*, JX 208 at 5-6 (noting "fail[ure] to provide release detection," inactive or non-functioning "sump sensor alarms," and failure to provide "line leak detector testing results").

During this same period, DNREC and MDE likewise provided several notices that plainly contemplated "corrective or remedial actions" or noncompliance with Environmental Laws. *See* JX 224 (MDE report noting ATG system not operating properly); JX 246 (MDE report noting failure to test equipment); JX 264 (MDE report noting failure to properly abandon tanks and requiring testing for reuse); JX 289 (DNREC report noting failure to provide documentation and verify the presence of safety devices). Other examples are summarized in the Factual Background, *supra*. Because of the obvious nature of these violations, I need not consider whether the Clayton Reports uncovered additional violations that occurred on Duncan's watch.

Duncan received notices from the EPA, DNREC, and MDE. He knew about them and about the ongoing environmental violations at the Properties. The existence of these notices and violations rendered the Environmental Compliance Representation false unless Duncan provided Universal with documents relating to these issues. During trial, Duncan admitted that during due diligence, he did not provide Universal with multiple documents reflecting his history of problems with DNREC and MDE, including violations that those agencies identified just months before the sale. *See* Tr. 444-50. Other than disclosing the CAFO in the Sale Agreement, Duncan did not provide Universal with any documents or information relating to the CAFO or his history of interaction with the EPA.

Duncan made these false representations and failed to provide records or otherwise inform Universal about the condition of the Properties because he wanted to induce Universal to buy. By early 2007, Duncan was under substantial pressure from environmental regulators. He wanted to retire and leave the petroleum industry, and he wanted to obtain the best price possible for the business that he had built over thirty years. Duncan knew that if he did not represent that the Properties complied with all environmental regulations and revealed his extensive record of violations, then either Universal would decline to buy or the price he negotiated would be jeopardized. Duncan therefore knowingly made the false Environmental Compliance Representation among others in the Sale Agreement.

2. Reliance

Although Universal proved that Duncan made knowingly false representations to induce Universal to enter into the Sale Agreement, Universal did not prove that it relied upon Duncan's false representations. To prove common law fraud, the recipient of the false representation "must in fact have acted or not acted in justifiable reliance" upon it. *NACCO Indus., Inc. v. Applica Inc.*, 997 A.2d 1, 29 (Del. Ch. 2009) (internal quotation marks omitted). "[J]ustifiable reliance requires that the representations relied upon involve matters which a reasonable person would consider important in determining his course of action . . . ." *Craft v. Bariglio*, 1984 WL 8207, at *8 (Del. Ch. Mar. 1, 1984). "Generally, a party dealing on equal terms with another is not justified in relying on representations where the means of knowledge are readily within his or her reach . . . ." 37 C.J.S. Fraud § 56. *A fortiori* a party who gains actual knowledge of the falsity of a

representation, structures a contract to address the risk of loss associated with the false representation, and proceeds to closing cannot claim justifiable reliance. *See S.C. Johnson & Son, Inc. v. Dowbrands, Inc.*, 111 F. App'x 100, 108 (3d Cir. 2004) (applying Delaware law and denying recovery under fraud theory where purchaser "agreed to rely only upon its own due diligence," "reviewed" and "specifically noted" activities allegedly later considered fraudulently withheld, and "proceed[ed] to closing without waiting for answers").

On the facts of this case, Universal did not prove that it justifiably relied on Duncan's representations in the Sale Agreement relating to legal and environmental compliance, production of documents, and disclosure of all material facts. In the Sale Agreement, Universal bargained for an unfettered due diligence right. Universal then retained Delta and Manko Gold as its experts to conduct due diligence and evaluate the results. Through due diligence, Universal learned about Duncan's poor environmental record, limited document production, and problems with regulatory compliance. *See, e.g.*, JX 1-20 (Phase I ESAs noting absence of records relating to tank leak detection, piping leak detection, and cathodic protection testing); JX 27 (Sale Agreement disclosing EPA, DNREC, and MDE actions); JX 33 (Universal directing Delta to obtain and review the CAFO); JX 39 (email where Delta indicates that Duncan's records are "pretty thin"); JX 40 (email where Delta denies receipt of Duncan's historical phase II reports); JX 42 (email where MDE recommends that Delta request state agency files). To gain more information, Universal instructed Delta to perform the File Reviews.

Universal originally claimed that Delta did not perform its investigations

competently, and those claims were settled in the midst of trial. Essential to Universal's claims against Delta was the fact that Universal relied on Delta's assessments. The trial record established that Universal indeed relied on both Delta and Manko Gold, its environmental counsel. Batra and other Universal representatives received reports from Delta and Manko Gold, accepted their assessments, and followed their advice. Having previously purchased gas stations, Batra was understandably concerned about environmental issues and skeptical about Duncan's claims. So was Fox of Manko Gold, an attorney with extensive experience evaluating environmental risk.

Universal treated Duncan's representations with healthy skepticism. Universal relied on the representations in the sense that they contractually allocated to Duncan the risk that the representations would be incorrect, but Universal did not rely on the representations in the sense of being fraudulently induced by them to close the transaction. Universal instead relied on its advisors and the improved terms it extracted from Duncan in the October Modification.

When they negotiated the October Modification, Universal, Manko Gold, and Delta knew about the gaps in Duncan's records. They also knew that Delta had not conducted the File Reviews to fill the gaps. At the time, Delta estimated that the environmental liability at the Properties would likely cost $3.0 million, with a high figure of $3.7 million. Based on this amount, Universal told Duncan that it would close only if the agreement were modified to provide that (i) Duncan would remediate the environmental conditions to the satisfaction of DNREC and MDE, (ii) Duncan would escrow $1.6 million of the purchase consideration to fund any Corrective Action, (iii) if

Duncan did not fully remediate a Property, then Universal could complete the effort and offset the costs against the Notes, and (iv) if Duncan were found to have breached any "obligations, representations, indemnities, covenants, and agreements" in the Sale Agreement, then Universal would have the right to offset any damages against the Notes. JX 93 at 2. Duncan agreed, and the parties closed the deal.

Through the October Modification, Universal specifically addressed the risks it faced, including the known risks that Duncan's files were incomplete and that there were additional, as yet unknown, problems at the Properties. "When parties have ordered their affairs voluntarily through a binding contract, Delaware law is strongly inclined to respect their agreement, and will only interfere upon a strong showing that dishonoring the contract is required to vindicate a public policy interest even stronger than freedom of contract." *Libeau v. Fox*, 880 A.2d 1049, 1056 (Del. Ch. 2005), *aff'd in part, rev'd in part*, 892 A.2d 1068 (Del. 2006). Requiring parties to live with "the language of the contracts they negotiate holds even greater force when, as here, the parties are sophisticated entities that bargained at arm's length." *Progressive Int'l Corp. v. E.I. Du Pont de Nemours & Co.*, 2002 WL 1558382, at *7 (Del. Ch. July 9, 2002). Because Universal addressed the uncertainties surrounding the accuracy of Duncan's contractual representations through due diligence and the October Modification, Universal cannot now seek a different remedy under the guise of common law fraud.

Based on the evidence presented at trial, Universal did not in fact rely on the representations of the Sale Agreement in a manner sufficient to support common law fraud. Universal instead relied on (i) the assessments and evaluations made by Delta and

Manko Gold and (ii) the October Modification. Because Universal recognized the likely falsity of certain representations in the Sale Agreement and structured its affairs to manage that risk, Universal must take solace in the contractual remedies that it obtained.

3. Rescission And Rescissory Damages

Assuming *arguendo* that Universal could establish reliance and prove common law fraud, Universal would not be entitled to rescission or rescissory damages as a remedy. "Rescission requires that all parties to the transaction be restored to the *status quo ante, i.e.*, to the position they occupied before the challenged transaction." *Strassburger v. Earley*, 752 A.2d 557, 578 (Del. Ch. 2000). Rescission is not feasible here because the Properties were sold to third parties in 2010 and 2011.

The plaintiffs alternatively seek rescissory damages. Delaware courts have been "extremely reluctant" to award rescissory damages. Donald J. Wolfe, Jr. & Michael A. Pittenger, *Corporate and Commercial Practice in the Delaware Court of Chancery* § 12.04[b], at 12-71 (2012). As then-Vice Chancellor Jacobs noted in *Strassburger*, rescissory damages are the "exception to the normal out-of-pocket measure" of compensatory damages. 752 A.2d at 579.

> They are exceptional, because such damages are measured as of a point in time *after* the transaction, whereas compensatory damages are determined at the time *of* the transaction. As a consequence, rescissory damages may be significantly higher than the conventional out-of-pocket damages, because rescissory damages could include post-transaction incremental value elements that would not be captured in an "out-of-pocket" recovery.

Id. Vice Chancellor Jacobs noted that calculating damages in this fashion risked

conflating damages caused by misconduct with changes in valuation arising from other phenomena. *See id.* at 580 (providing scholarly discussion of macroeconomic factors affecting calculation of rescissory damages).

To be actionable, a "fraudulent misrepresentation must actually cause harm." *In re Wayport, Inc. Litig.*, 2013 WL 1811873, at *25 (Del. Ch. May 1, 2013); *accord* Restatement (Second) of Torts § 548A, cmt. a (1977) ("Not all losses that in fact result from the reliance are, however, legally caused by the representation."). Consistent with the requirement of proving causation, this Court has declined to award rescissory damages where a plaintiff proffered insufficient expert evidence and his damages calculation was "speculative." *Gaffin v. Teledyne, Inc.*, 1990 WL 195914, at *17 (Del. Ch. Dec. 4, 1990), *aff'd in part, rev'd in part*, 611 A.2d 467 (Del. 1992).

On the facts of this case, Universal did not prove that its rescissory damages calculation would be causally related to Duncan's alleged fraud. The Properties were acquired in 2007 and sold in the bankruptcy liquidation during 2010 and 2011. Universal's expert made no attempt to disaggregate the macroeconomic and contextual variables affecting the damages calculation. *Compare* Tr. 289 (failing to consider whether bankruptcy liquidation affected value), *with* Fletcher Corporate Bankruptcy, Reorganization & Dissolution §16.03, at 5 (1992) ("Although [Chapter 7] proceedings in bankruptcy are essentially for the benefit of the creditors, there may be serious drawbacks . . . . There is the loss of value sustained as a consequence of the forced sale of assets. Frequently, the liquidation value of business assets will be substantially less than the going concern value . . . ." (footnote omitted)). More significantly, he did not

convincingly rebut the rather obvious fact that Universal bought the Properties at an economic peak and sold them shortly after an economic trough. It would confer an unfair windfall on Universal and penalize Duncan to award a remedy that ignores the manifold independent causes leading to the rescissory damages calculation proffered by Universal. *See Sunrise Ventures, LLC v. Rehoboth Canal Ventures, LLC*, 2010 WL 363845, at *8 (Del. Ch. Jan. 27, 2010), *aff'd*, 7 A.3d 485 (Del. 2010) ("It would be impossible more than four years after the fact for this court fairly and equitably to rescind a complex real estate deal where value has doubtlessly been affected by the intervening events of nearly a half-decade and rapidly churning real estate markets."). Therefore, even assuming the plaintiffs succeeded in proving reliance, rescissory damages would not be an appropriate remedy.

B. Equitable Fraud

The equitable fraud claim fails because Universal failed to prove any type of special relationship with Duncan that would support a claim for equitable fraud. *See U.S. W., Inc. v. Time Warner Inc.*, 1996 WL 307445, at *26 (Del. Ch. June 6, 1996) (Allen, C.). In addition, reliance is an element of equitable fraud, so the claim fails for lack of reliance on the same basis as the common law fraud claim. *See Zirn v. VLI Corp.*, 681 A.2d 1050, 1061 (Del. 1996) (explaining that equitable fraud "provides a remedy for negligent or innocent misrepresentations").

C. Breach Of Contract

Under Delaware law, the elements of a breach of contract claim are "first, the existence of the contract, whether express or implied; second, the breach of an obligation

imposed by that contract; and third, the resultant damage to the plaintiff." *VLIW Tech., LLC v. Hewlett-Packard Co.*, 840 A.2d 606, 612 (Del. 2003). The existence of the Sale Agreement is undisputed. At trial, Universal proved that Duncan breached the Sale Agreement and that Universal is entitled to actual damages. Universal is not, however, entitled to rescissory or diminution-in-value damages.

1. The Breach And Duncan's Reliance Defense

As discussed in Part II.A.1, *supra*, Universal proved that the Environmental Compliance Representation was incorrect. Universal thereby established that Duncan breached the Sale Agreement. Universal also proved that Duncan breached the Seller Files Covenant by failing to produce his extensive correspondence with the EPA, documents relating to his significant history of DNREC and MDE investigations, or otherwise disclose those matters.

To defend against the breach of contract claim, Duncan makes the same non-reliance arguments that were successful against the common law fraud claim. But under Delaware law,

> [a] breach of contract claim is not dependent on a showing of justifiable reliance. That is for a good reason. Due diligence is expensive and parties to contracts in the mergers and acquisitions arena often negotiate for contractual representations that minimize a buyer's need to verify every minute aspect of a seller's business. In other words, representations like the ones made in [the agreement] serve an important risk allocation function. By obtaining the representations it did, [the buyer] placed the risk that [the seller's] financial statements were false and that [the seller] was operating in an illegal manner on [the seller]. Its need then, as a practical business matter, to independently verify those things was lessened because it had the assurance of

> legal recourse against [the seller] in the event the representations turned out to be false.
>
> . . . [H]aving given the representations it gave, [the seller] cannot now be heard to claim that it need not be held to them because [the buyer's] due diligence did not uncover their falsity. . . . Having contractually promised [the buyer] that it could rely on certain representations, [the seller] is in no position to contend that [the buyer] was unreasonable in relying on [the seller's] own binding words.

Cobalt Operating, LLC v. James Crystal Enters., LLC, 2007 WL 2142926, at *28 (Del. Ch. July 20, 2007) (footnote omitted), *aff'd*, 945 A.2d 594 (Del. 2008); *accord Interim Healthcare, Inc. v. Spherion Corp.*, 884 A.2d 513, 548 (Del. Super. 2005), *aff'd*, 886 A.2d 1278 (Del. 2005) ("No such reasonable reliance is required to make a *prima facie* claim for breach."); *Gloucester Hldg. Corp. v. U.S. Tape & Sticky Prods., LLC*, 832 A.2d 116, 127 (Del. Ch. 2003) (rejecting contention that justifiable reliance was an element of breach of contract as "simply incorrect"). *See generally* Charles K. Whitehead, *Sandbagging: Default Rules and Acquisition Agreements*, 36 Del. J. Corp. L. 1081 (2011).

Duncan therefore cannot avoid contract liability by using the same reliance defense he used to escape tort liability. Duncan breached the Sale Agreement. The question is the appropriate remedy.

2. Contract Damages

As a remedy for Duncan's breach of contract, Universal seeks rescissory damages of approximately $15 million, calculated as Universal's upfront investment plus costs incurred to remediate the Properties less the aggregate proceeds from the sale of the

Properties in the bankruptcy liquidation.[2] Alternatively, Universal seeks diminution-in-value damages of approximately $12 million, calculated as Universal's upfront investment less the aggregate proceeds from the sale of the Properties in the bankruptcy liquidation. Duncan argues that Universal is entitled only to actual damages. Duncan is correct.

a. Rescissory Damages

This decision previously discussed rescission as a tort remedy. *See* Part II.A.3. Similar considerations make rescission inappropriate as a contract remedy, but with some additional contractual twists.

"The primary if not the only remedy for injuries caused by the nonperformance of most contracts is an action for damages for the breach . . . ." 24 Williston on Contracts § 64:1 (4th ed.). Rescissory damages may be an appropriate remedy for breach of contract in limited circumstances, such as "if the breach is evidence of an intention no longer to be bound by the agreed terms of the contract, or if the breach may be said to go to the root of the agreement between the parties." Wolfe & Pittenger, *supra*, § 12.04[a], at 12-62 (footnote and internal quotation marks omitted). Where an "agreement or transaction involves multiple obligations," the Court must analyze whether "a party's breach . . . justifies rescission of the entire agreement or transaction . . . ." *Id.* § 12.04[a], at 12-62 to

[2] Universal's upfront investment consisted of approximately $20 million. Universal subsequently incurred costs of $3 million in fees, interest, and principal payments, yielding a total investment in the transaction of $23 million. The Properties were sold in the bankruptcy liquidation for $8 million, resulting in Universal's requested rescissory damages figure of $15 million.

12-63. The Court can also examine other available contractual remedies when considering whether to order rescission. *See, e.g.*, *Cobalt*, 2007 WL 2142926, at *29 (considering whether to grant rescission in light of indemnification language). The Court has "discretion not to grant rescission where delay allows the plaintiff to sit back and test the waters, waiting to assert a claim for rescission until" his venture has failed. *Gotham P'rs, L.P. v. Hallwood Realty P'rs, L.P.*, 817 A.2d 160, 174 (Del. 2002) (internal quotation marks omitted).

On the facts of this case, Universal is not entitled to rescissory damages as a breach of contract remedy. Rescissory damages are not appropriate because Universal's conduct demonstrated that the breaches did not go to the heart of the transaction. Universal understood that Duncan likely breached the Environmental Compliance Representation, negotiated the October Modification to address this risk, and elected to close. Universal may not now change tack and seek to unwind the transaction on the basis of information it was sufficiently aware of prior to closing.

The evidence also shows that after closing, Universal did not originally seek to escape the transaction but rather relied on its contractual rights to ameliorate the harm that Duncan's breaches caused. After learning about the extent of the breaches from the Clayton Reports and File Reviews, Universal did not seek rescission. Instead, Universal asked Duncan to cure or threatened to take Corrective Action and offset the Notes for the cost. In doing so, Universal affirmed the contract.

Furthermore, Universal delayed in seeking rescission. By April 29, 2008, the Clayton Reports were complete. Over the next year and a half, the parties haggled over

the alleged breaches. All the while, Universal continued operating the Properties. In July 2009, Universal filed for bankruptcy for reasons unrelated to its operation of the Properties. Only then did Universal seek rescission. By doing so, Universal "tested the waters," sought to make a go of the venture, and then resorted to its request for rescissory damages as a form of business insurance. Rescissory damages are therefore unavailable for the contract breach.

b. Diminution-in-value Damages

"[T]he standard remedy for breach of contract is based upon the reasonable *expectations* of the parties . . . ." *Duncan v. Theratx, Inc.*, 775 A.2d 1019, 1022 (Del. 2001) (emphasis added). "Expectation damages . . . require the breaching promisor to compensate the promisee for the promisee's reasonable expectation of the value of the breached contract, and, hence, what the promisee lost." *Id.* Expectation damages should "be measured as of the time of the breach." *Comrie v. Enterasys Networks, Inc.*, 837 A.2d 1, 17 (Del. Ch. 2003). They "should not act as a windfall." *Paul v. Deloitte & Touche, LLP*, 974 A.2d 140, 146 (Del. 2009).

The "diminution in the market price of the property caused by the breach," can be used as an alternative to expectation damages in particular contexts. Restatement (Second) of Contracts § 348(2)(a) (1981). For example, when a party performs defectively under a construction or engineering contract, the proper damages remedy is generally the cost to render compliant or complete performance, in other words,

expectation damages.[3] If, however, "there is a tremendous disparity between restoration cost and the diminished value of the property," then diminution-in-value damages "may be an appropriate measure of damages." *Leary v. Oswald*, 2006 WL 3587249, at *1 (Del. Super. Oct. 25, 2006); *accord Shipman*, 1995 WL 109009, at *5 ("If the [cost of completion] remedy is disproportionate to the probable loss in value or if it constitutes economic waste, then the proper measure of damages may be diminution in value."); Restatement (Second) of Contracts § 348, cmt. c (1981) ("Sometimes, however, such a large part of the cost to remedy the defects consists of the cost to undo what has been improperly done that the cost to remedy the defects will be clearly disproportionate to the probable loss in value to the injured party. Damages based on the cost to remedy the defects would then give the injured party a recovery greatly in excess of the loss in value to him and result in a substantial windfall. Such an award will not be made."). The goal when using diminution-in-value damages is to fulfill the policy of awarding contract damages that provide the disappointed promisee with "an amount reasonably calculated to make him or her whole and *neither more nor less* . . . ." Williston, *supra*, § 64:1

[3] *See Shipman v. Hudson*, 1995 WL 109009, at *5 (Del. Super. Feb. 17, 1995) ("The basic measure of damages for a breach of a contract involving improvements to real property is the amount required to remedy the defect by replacement or repair . . . ."); *Council of Unit Owners of Sea Colony E., Phase III Condo., on Behalf of Ass'n of Owners v. Carl M. Freeman Assocs., Inc.*, 564 A.2d 357, 361 (Del. Super. 1989) ("[U]nder Delaware law the cost of repairs is the appropriate measure not only in tort cases but also in contract cases [involving construction defects]."); *Farny v. Bestfield Builders, Inc.*, 391 A.2d 212, 214 (Del. Super. 1978) ("If a party to a construction contract fails to perform its obligations under the contract, the aggrieved party is entitled to damages measured by the amount required to remedy the defective performance unless it is not reasonable or practical to do so.").

(emphasis added).

On the facts of this case, Universal seeks diminution-in-value damages, but such an award would not be appropriate. First, the default approach of awarding damages based on the terms of the contract places Universal in the position it bargained for. Either Duncan will pay for the Corrective Action, or Universal can offset the cost of compliance against the Notes. Second, Universal's request for diminution-in-value damages has it backward. A court will substitute diminution-in-value damages where it is a more efficient means of remedying harm because complete performance would be (i) "disproportionate to the probable loss in value," (ii) constitute "economic waste," or (iii) bestow a windfall on the plaintiff. *Shipman*, 1995 WL 109009, at *5. Universal reverses the tables by seeking a diminution-in-value award of approximately $12 million, an order of magnitude greater than an award based on expectation damages. In this context, it is the diminution-in-value award that would be disproportionate, constitute economic waste, and bestow a windfall.

Universal also is not entitled to its damages calculation because it was not reasonably certain. *See* Restatement (Second) of Contracts § 352 (1981) ("Damages are not recoverable for loss beyond an amount that the evidence permits to be established with reasonable certainty.").

> Although as a general rule the vendor's loss is measured by the market value of the property at the time of the purchaser's breach, the price obtained on a resale of the property at a later date may be sufficient evidence of the market value at the date of breach provided that market conditions are similar and the time lapse between the date of breach and the resale is not great.

Long v. Nealon, 2002 WL 264460, at *1 (Del. Super. Feb. 22, 2002) (quoting 77 Am.Jur.2d Vendor and Purchaser § 482). Universal contends that the bankruptcy sale prices achieved at least two years post-closing reflected the market value of the Properties in light of Duncan's breaches. Universal's argument and proof were unconvincing. Universal's expert did not consider that selling an asset out of bankruptcy affected the value achieved, relied unconvincingly on revenue multiples without explaining why this metric was an appropriate choice for valuing gas stations, and admitted double counting roughly $900,000 in purported damages. *See* Tr. at 281. Most significantly, as discussed, *supra*, in Part II.A.3, he did not convincingly establish which portion of his damages calculation was causally attributable to Duncan's breaches. Thus, Universal is not entitled to diminution-in-value damages which were not reasonably certain.

c. Actual Damages

On the facts of this case, Universal is entitled to actual damages incurred by the breaches of the Sale Agreement. Beyond its prayer for rescissory or diminution-in-value damages, Universal did not attempt to prove causal damages arising from Duncan's failure to produce or disclose dated documents and correspondence relating to violations of the Environmental Compliance Representation. While these nondisclosures were breaches, Universal suffered no damages.

This leaves Duncan's breaches of the Environmental Compliance Representation related to the actual condition of the Properties at closing. Universal proved at trial that

they incurred actual damages in remediating the Properties, including $406,293 to inspect and repair certain USTs, $964,190 to remove three USTs as required by DNREC, and $126,946 in legal fees, yielding total actual damages of $1,497,429.

3. Count IV And Duncan's Counterclaims

In Count IV of the complaint, Batra seeks a declaration reducing his obligations under the Personal Guaranty Agreements that secure the Notes. Through his counterclaims, Duncan contends that any damages owed to Universal should offset the unpaid balance of the Notes, leaving Universal without a net recovery. The parties did not elaborate on whether Batra is entitled to a corresponding offset or whether he remains liable for the unfulfilled obligations underlying the Notes. Moreover, in light of the pending bankruptcies involving both the SPEs and Batra personally, it is not clear that this Court has the power to grant the relief requested by the parties. The parties shall provide supplemental briefs addressing these issues.

III. CONCLUSION

Judgment is entered in favor of plaintiffs on Count VI. Duncan is liable for damages in accordance with this opinion. Judgment is entered in favor of defendants on Counts I, II, III, and V. Judgment is reserved on Count IV and defendants' counterclaims pending supplemental briefing. Enforcement of the judgment in favor of plaintiffs on Count VI is stayed pending resolution of Count IV and defendants' counterclaims. All parties will bear their own costs.