COURT OF CHANCERY
OF THE
STATE OF DELAWARE

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July 20, 2007

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Re: *Greystone Digital Technology, Inc., et al. v. Robert H. Alvarez*, Civil Action No. 2796-VCP

Dear Counsel:

Plaintiffs, Greystone Digital Technology, Inc. and Gary R. Morris (collectively "Greystone"), have brought this action against Robert H. Alvarez a/k/a Harold R. Alvarez for, among other things, a declaratory judgment pursuant to 8 *Del. C.* § 225 as to who the directors and officers of Greystone are. Greystone now asks this Court to enter a default judgment against Alvarez for his failure to fully participate in this litigation and comply with certain orders of the Court. For the reasons set forth below, Greystone's motion is denied.

I. BACKGROUND AND FACTS

A. Facts

Greystone Digital Technology, Inc. is a Delaware corporation.[1] Gary R. Morris resides in Texas and claims to have been the President and sole director of Greystone since September 15, 2004. Alvarez resides in Florida and has held himself out as the President and a director of Greystone.

In an affidavit accompanying his Complaint, Morris avers that he owns at least 99% of Greystone's outstanding shares, and that as a result, he is the President and sole director of Greystone. Morris also is the President of Kiboga Systems, Inc. ("Kiboga"), headquartered in Dallas, Texas. Until September 15, 2004, Morris was the majority shareholder of Kiboga. Morris then made a tender offer for all of the outstanding shares of Greystone in a stock-for-stock exchange for his own Kiboga shares. Almost all Greystone shareholders tendered their shares to Morris, with the exception of 200,000 to 300,000 shares, making Morris the owner of 99% of Greystone's outstanding stock.

Plaintiffs' Complaint alleges that Alvarez essentially has "hijacked" Greystone by fraudulently misrepresenting that he is the President and a director of Greystone. According to the Complaint, on December 28, 2006, Alvarez applied to the Delaware Secretary of State to reinstate Greystone's charter, which had lapsed. In January 2007, Alvarez used an old shareholder list to solicit proxies from former shareholders of

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[1] Unless otherwise noted, the facts recited are drawn from the Verified Complaint filed on March 14, 2007.

Greystone for a Special Meeting to be held on February 14, 2007. The purpose of the meeting was to consider and vote upon various proposals that Alvarez promulgated. The proposals included: (1) forming a Nevada corporation – Greystone Ltd. – and transferring all of Greystone's assets and liabilities to that corporation; (2) authorizing a distribution of Greystone Ltd. common stock to all Greystone shareholders; and (3) authorizing the directors and officers of Greystone to take whatever actions necessary to register the shares of Greystone Ltd. At the meeting, Morris was not allowed to vote his shares, and Alvarez announced that he previously nominated and elected himself a director of the Corporation. A majority of the shares allowed to vote approved Alvarez's proposals. They also authorized the issuance of a promissory note to Alvarez, convertible into 60 million shares of Greystone stock.

On February 27, 2007, Alvarez formed GreyTech, Ltd. ("GreyTech") and began advising brokers with clients who hold Greystone shares about a purported merger and share exchange between Greystone and GreyTech, the new Nevada entity.

B. Procedural History

Plaintiffs filed this action on March 14, 2007. Counts I and II of the Complaint seek, pursuant to 8 *Del. C.* § 225, a determination that Morris is the President and sole director of Greystone, that the votes taken at the February 14, 2007 meeting were invalid, and that any actions taken in furtherance of those votes are void. Counts III and IV assert

claims against Alvarez for fraud and tortious interference with business relations. Count V seeks preliminary and permanent injunctive relief.

Since the Complaint was filed, the parties have agreed to three Stipulated Temporary Restraining Orders. They were entered on March 23, 2007, April 25, 2007, and May 16, 2007 (referred to collectively as the "TRO"). The last TRO was to expire on June 30, 2007. The Court also granted Plaintiffs' request for a prompt trial and scheduled trial for August 22, and 23, 2007.

Plaintiffs have filed several motions for sanctions and similar relief over the last two months. On May 9, 2007, Greystone filed a Motion for Entry of Default Judgment ("Motion for Default Judgment"). On May 22, Greystone filed a Motion for Sanctions and Rule to Show Cause for Multiple Violations of the Temporary Restraining Order ("Motion for Sanctions"). After hearing argument on May 29, 2007, the Court granted, in part, Greystone's Motion for Sanctions. The same day, Alvarez filed an Answer to the Complaint ("Answer") and a Response to Plaintiffs' Motion for Default Judgment ("Response"). Greystone filed its Reply on June 1, 2007. Thereafter, Greystone filed a Second Motion for Sanctions on June 11, and a Second Motion for Rule to Show Cause on June 26. In both of those motions, Greystone accused Alvarez of further violations of the Court's orders.

On July 19, 2007, the Court heard argument on the Motion for Default Judgment, Second Motion for Sanctions and Second Motion for Rule to Show Cause. Based on the submissions and argument, I granted each of the latter two motions, in part.

Greystone seeks entry of a default judgment against Alvarez for: (1) failing to contest Greystone's allegations of default; (2) failing to demonstrate excusable neglect; and (3) repeatedly disregarding this Court's orders.[2]

II. ANALYSIS

A. Standard

The standard for entry of a default judgment is set forth in Court of Chancery Rule 55(b):

> When a party against whom a judgment for affirmative relief is sought, has failed to appear, plead or otherwise defend as provided by these Rules, and that fact is made to appear, judgment by default *may* be entered . . . . (Emphasis added).

Rule 55(b) is permissive, not mandatory, giving the court the discretion to decide whether to enter a default judgment based on the particular set of facts before it.[3] Entry of a default judgment is an "extreme remedy."[4] As the Delaware Supreme Court recently

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2 Pls.' Reply Mem. in Supp. of Mot. for Entry of Default J. ("PRM") at 2-4.

3 *In re 53.1 Acres of Land in Mispillion Hundred*, 2002 WL 31820972 (Del. Ch. Sept. 19, 2002) (citing *U.S. Surgical Corp. v. Auhull*, 1998 WL 326493, at *2 (Del. Ch. May 28, 1998)).

4 *U.S. Surgical Corp.*, 1998 WL 326493, at *2 (quoting *Sundor Elec., Inc. v. E.J.T. Constr. Co.*, 337 A.2d 651, 652 (Del. 1975)).

noted, there is a trend disfavoring the use of default judgments.[5] This trend, however, is "counterbalanced by consideration of social goals, justice and expediency, a weighing process [that is] largely within the domain of the trial judge's discretion."[6] Moreover, in *U.S. Surgical Corp. v. Auhull*, this Court held that entry of a default judgment requires the existence of "a willful or conscious disregard for the rules of the Court."[7] Default judgment also may be entered when a party blatantly fails to appear or plead for a prolonged period of time.[8]

B. Discussion

Greystone argues that Alvarez admits in his Answer to being in default, and that those admissions are sufficient to justify entry of a default judgment. These admissions alone, however, do not necessarily warrant a default judgment. In his Response, Alvarez does admit to failing to file a timely Answer. That said, Alvarez's counsel participated in

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5 *Apartment Comties. Corp. v. Martinelli*, 859 A.2d 67, 69 (Del. 2004) (quoting *Rogers v. Hartford Life & Accident Ins. Co.*, 167 F.3d 933, 936 (5th Cir. 1999) ("Most courts have adopted a policy in favor of resolving cases on their merits and against the use of default judgments") (internal quotations omitted)).

6 *Apartment Comties. Corp.*, 859 A.2d at 69 (quoting *Pelican Prod. Corp. v. Marino*, 893 F.2d 1143, 1146 (10th Cir. 1990) and *Gomes v. Williams*, 420 F.2d 1364, 1366 (10th Cir. 1970) (internal quotations omitted)).

7 1998 WL 326493, at *2 (citing *Sundor Elec., Inc.*, 337 A.2d at 652).

8 *Stonington Partners, Inc. v. Lernout Hauspie Speech Prods., N.V.*, 2002 WL 31439767, at *4 (Del. Ch. Oct. 23, 2002) (entering default judgment against defendants who made no effort to respond to the complaint until a year after the commencement of the action).

a teleconference with the Court on May 23, 2007 and appeared in court on May 29, 2007 at the hearing on Plaintiffs' Motion for Sanctions. Moreover, Alvarez attended by telephone the May 29 hearing. Although Alvarez and his counsel have been lax in their attention to the Court's deadlines, Alvarez has at least responded to the Complaint and participated, to some extent, in the proceedings. Alvarez's counsel also signed each of the three stipulated TROs, which further evidence Defendant's participation in the case.

Further, Plaintiffs have not presented any evidence or convincing arguments that they have been prejudiced by Alvarez's delay. Alvarez answered the Complaint on May 29, 2007, approximately seven weeks after the 20-day period specified in Rule 12(a) expired. At a May 23, 2007 teleconference, however, the Court had permitted Alvarez to file his Answer by Friday, May 25, 2007. Although Alvarez filed his Answer late by a few calendar days, or one business day, his delay did not prejudice Greystone.

Greystone also argues that Alvarez has not shown that his failure to abide by the Court's deadlines was attributable to any "excusable neglect." Assuming this is the case, the rules only explicitly require a showing of "excusable neglect" in the context of a motion to have a final judgment, by default or otherwise, vacated under Rule 60(b)(1).[9] Furthermore, this Court has analyzed excusable neglect in terms of "how a reasonably prudent person would act under the circumstances."[10] Although I would not call

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[9] Ct. Ch. R. 60(b)(1).

[10] *Stonington Partners*, 2002 WL 31439767, at *5.

Alvarez's conduct prudent, I do not find it inexcusable, especially when viewed in the context of so severe a penalty as a default judgment.

The case Greystone cites as authority for the requirement of excusable neglect, *Pioneer Investment Services Co. v. Brunswick Associates Ltd. Partnership*,[11] is not persuasive. The case is largely inapposite and, in any event, does not support entry of a default judgment in the case at bar. In *Pioneer*, the Supreme Court upheld the Sixth Circuit's finding that a U.S. Bankruptcy Court should have accepted late filings. Under Bankruptcy Rule 3003(c)(2), all creditors holding contingent, unliquidated, or disputed claims, must file a proof of claim with the bankruptcy court before a deadline ("bar date") set by the court. Respondents' counsel in *Pioneer*, who failed to file any proofs of claim by the bar date, asserted that he was unaware of the deadline and had experienced professional difficulties during that time. The Bankruptcy Court did not permit the late filing, finding that respondents could not claim excusable neglect because they had notice of the bar date.[12] The District Court, on appeal, affirmed in part and reversed in part, preferring the Ninth Circuit's test to the Bankruptcy Court's "narrow" reading of

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11 507 U.S. 1489 (1993).

12 *Id.* at 1493 ("Following precedent from the Court of Appeals for the Eleventh Circuit, the court held that a party may claim excusable neglect only if its failure to timely perform a duty was due to circumstances which were beyond [its] reasonable [c]ontrol.") (quoting *In re S. Atl. Fin. Corp.*, 767 F.2d 814, 817 (11th Cir. 1985) (internal quotations omitted)).

excusable neglect.[13] The Bankruptcy Court applied the Ninth Circuit's test, but still denied respondents' request to accept the late filings.[14] On appeal to the Sixth Circuit, the Court of Appeals reversed the Bankruptcy Court's denial, finding that it improperly penalized respondents for the mistakes of their counsel. The Supreme Court concluded that ascertaining whether neglect is excusable requires an equitable determination that "tak[es] account of all relevant circumstances surrounding the party's omission."[15] The Court substantially accepted the test for excusable neglect that the Sixth Circuit used and affirmed the court's decision to reverse the Bankruptcy Court's refusal to accept late filings.[16]

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[13] 507 U.S. at 1493. ("Embracing a test announced by the Court of Appeals for the Ninth Circuit, the District Court remanded with instructions that the Bankruptcy Court evaluate respondents' conduct against several factors, including: (1) whether granting the delay will prejudice the debtor; (2) the length of the delay and its impact on efficient court administration; (3) whether the delay was beyond the reasonable control of the person whose duty it was to perform; (4) whether the creditor acted in good faith; and (5) whether clients should be penalized for their counsel's mistake or neglect.") (quoting *In re Dix*, 95 B.R. 134, 138 (B.A.P. 9th Cir. 1988) (internal quotations omitted)).

[14] 507 U.S. at 1493. ("[T]he Bankruptcy Court found (1) that petitioner would not be prejudiced by the late filing; (2) that the 20-day delay in filing the proofs of claim would have no adverse impact on efficient court administration; (3) that the reason for the delay was not outside respondents' control; (4) that respondents and their counsel acted in good faith; and (5) that, in light of [counsel's] business sophistication and his actual knowledge of the bar date, it would not be improper to penalize respondents for the neglect of their counsel.")

[15] *Id.*

[16] *Id.* at 1498-99 ("With regard to determining whether a party's neglect of a deadline is excusable, we are in substantial agreement with the factors identified

As additional grounds for a default judgment in this case, Greystone relies on Alvarez's refusal to follow the Court's orders on several occasions on and after May 29, 2007. In particular, Greystone emphasizes Alvarez's failure to appear in person at the hearing on May 29, 2007, his violations of the TRO, his failure to appear at a properly noticed deposition, and his alleged lack of respect for this Court.

Alvarez, in fact, has been too lax in his attitude toward this Court and these proceedings. I do not find, however, that Alvarez's conduct has been so egregious as to warrant imposition of the extreme remedy of a default judgment at this relatively early stage of the litigation. While Alvarez did fail to comply with the Court's conditional request that he appear in person at the hearing on May 29, his explanation based on a perceived ambiguity in the Court's statement was not unreasonable. Furthermore, the Court addressed Alvarez's noncompliance by refusing his request to testify via telephone at the May 29 hearing. Similarly, Plaintiffs' complaint about Alvarez's failure to appear for a noticed deposition seems overblown. There is no evidence that Plaintiffs' counsel even conferred with the defense about the date of the deposition, and the notice provided only one week's notice. Having also reviewed Plaintiffs' submissions in support of their other pending motions for sanctions and contempt, I do not find that Alvarez's conduct is

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by the Court of Appeals." The relevant factors to be considered include: "the danger of prejudice to the debtor, the length of the delay and its potential impact on judicial proceedings, the reason for the delay, including whether it was within the reasonable control of the movant, and whether the movant acted in good faith.")

sufficiently egregious or prejudicial to warrant entry of a default judgment. The Court already has sanctioned Alvarez once for violating the TRO and imposed further sanctions, short of a default judgment, at the hearing on July 19.

III. CONCLUSION

For the reasons stated, Plaintiffs' motion for entry of default judgment is hereby denied.

IT IS SO ORDERED.

Sincerely,

/s/Donald F. Parsons, Jr.

Vice Chancellor

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