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CONTACT: Mary Cheatham
Haynes and Boone, LLP
214.651.5467 (office)
214.929-8837 (cell)
mary.cheatham@haynesboone.com

Haynes and Boone Secures Significant Victory Involving Shareholder Derivative Suits and Demand Letters

DALLAS - The Texas Supreme Court has issued a decision in favor of Lancer Corporation directors, represented by Haynes and Boone, LLP, in a precedent-setting ruling on shareholder derivative suits involving Texas corporations. The decision marks the first ruling by the Texas Supreme Court on the strict statutory prerequisites for commencing shareholder derivative litigation and represents a significant victory for businesses that elect to incorporate under the laws of Texas.

In a unanimous decision (Chief Justice Wallace Jefferson did not participate), the Court ruled that a two-sentence pre-suit demand letter to Lancer directors was inadequate under article 5.14(c) of the Texas Business Corporations Act because it referenced no complaining shareholder, cited no specific wrongdoing by any party, described no specific injury to the corporation and failed to request any specific remedial action be taken by the Lancer board.

The demand letter, sent by the law firm Lerach Coughlin Stoia Geller Rudman & Robbins just three days before the firm filed a shareholder derivative suit against Lancer directors, arose from an announced merger between Lancer and Hoshizaki America at a share acquisition price of \$22 per share. The letter did not identify a client and did not state that the firm represented any Lancer shareholder. The letter noted the existence of a competing offer, gave Lancer's directors one day to "confirm to us, in writing" that the board was "taking no further steps to consummate or in any way facilitate the previously announced sale" and cautioned the directors that "[y]our fiduciary obligations require that you fully and fairly consider all potential offers."

After the derivative suit was filed against the Lancer directors on December 23, 2005, in Bexar County, Texas, no effort was made to enjoin the Lancer/Hoshizaki merger, and the transaction closed as planned in early 2006. After the merger, an amended petition was filed seeking rescission, damages and attorneys' fees.

Texas corporate law makes a pre-suit demand an absolute prerequisite to the commencement of a shareholder derivative suit. The Court's ruling held that in issuing a pre-suit demand letter, a shareholder must be identified and the content of the demand letter must be particular. The Court also held that mandamus review of a challenged pre-suit demand letter was appropriate, stating that "allowing this case to proceed to trial would effectively allow a shareholder to sue for damages connected with a merger without giving the corporation's board an opportunity to make such a decision for itself."

Nicholas Even, a Haynes and Boone litigation partner representing Lancer's directors, said: "We never argued that a shareholder cannot make a demand on directors through an attorney, but we did assert from the outset of this case that some shareholder must be identified as the source of the demand. In addition, directors are not clairvoyant and can't be expected or required to act where a shareholder does not specify what has gone wrong and what actions should be taken. This decision recognizes that

anonymous or generic demand letters are contrary to the language and spirit of Texas corporate law and would defeat the very purpose of the pre-suit demand requirement.”

Haynes and Boone appellate partner Debbie McComas, who argued the matter before the Texas Supreme Court added: "Today's ruling makes clear that mandamus will be available to protect Texas corporations from lengthy, disruptive, and costly litigation brought by shareholders where the statutory demand requirements are not satisfied. When, as was the case here, the very act of proceeding to trial would defeat the substantive right involved, businesses that receive unfavorable interlocutory rulings in Texas state courts should consider seeking mandamus relief."

In addition to Mr. Even and Ms. McComas, the client team representing Lancer Corporation included partners George Bramblett and Lamont Jefferson.

Haynes and Boone, LLP is an international corporate law firm with offices in Texas, New York, California, Washington, D.C., Mexico City and Moscow, providing a full spectrum of legal services. With almost 550 attorneys, Haynes and Boone is ranked among the largest law firms in the nation by *The National Law Journal*. The firm has been recognized as one of the "Best Corporate Law Firms in America" (*Corporate Board Member Magazine*, 2001-2009), as one of "The Best 20 Law Firms to Work For" (*Vault.com*, 2008), and as a Top 100 law firm for both diversity (*MultiCultural Law Magazine*, 2009) and women (*Women 3.0*, 2008).