IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

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HERBERT BEHRENS, Plaintiff,	)	
v.	)	Civil Action No. 17436
AERIAL COMMUNICATIONS INC., TELEPHONE & DATA SYSTEMS INC., LEROY T. CARLSON, JR., DONALD W. WARKENTIN, J. CLARKE SMITH, RUDOLPH E. HORNACEK, JAMES BARR III, WALTER C.D. CARLSON, THOMAS W. WILSON, JR., JOHN D. FOSTER, PERTTI MIETTUNEN and VOICESTREAM WIRELESS CORP., Defendants.	)	

MEMORANDUM OPINION

Date Submitted: January 3 1,200 1
Date Decided: May 18.2001

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JACOBS, VICE CHANCELLOR

A minority shareholder, who sues individually and on behalf of a class of stockholders similarly situated, claims that the corporation and its directors and officers (who are the defendants), entered into an unfair, self-dealing transaction that diluted the minority shareholders' equity stake in the company. The defendants move to dismiss on the basis that after the action was filed, the corporation was merged into another entity and the shareholders no longer own stock in the original corporation. As a result, the defendants argue, the plaintiff lost its standing to maintain this lawsuit which, though styled as a class action, is actually derivative.

For the reasons next discussed, I conclude that this motion is well-founded and must be granted.

I. FACTS

The plaintiff is a former shareholder of Aerial Communications, Inc. ("Aerial" or "the Company"), a Delaware corporation. Aerial's largest stockholder, Telephone and Data Systems Inc. ("TDS"), held 82.5% of Aerial's outstanding common stock. TDS was controlled by a voting trust of which defendlants Leroy T. Carlson, Jr., Walter C.D. Carlson, and other members of the Carlson family are the trustees.

On or about September 20, 1999, Aerial and VoiceStream Wireless Corporation ("VoiceStream") entered into an agreement whereby

VoiceStream would acquire Aerial in a merger in which 0.455 shares of VoiceStream would be exchanged for each Aerial share. Based upon the September 17, 1999 market price of Voice&-earn stock, the implied value of that merger exchange ratio was approximately $25.50 per Aerial share.

This action involves a related but separate transaction that immediately preceded the merger. In that transaction, TDS and Aerial agreed to exchange $420 million of Aerial debt being held by TDS, for Aerial stock that was valued at $22 per Aerial share (the "debt replacement transaction"). The effect of the debt replacement transaction was to increase significantly the number of Aerial shares that TDS owned and would exchange for Voice&-earn stock in the merger. As a result of the combined debt replacement transaction and the Aerial-VoiceStream merger, TDS received for each of its Aerial shares, a profit equivalent in value to $3.50 worth of VoiceStream stock.'

The Aerial board that approved both the merger and the debt replacement transaction consisted of eleven members. Eight of those directors—*i.e.*, a majority--were either affiliated with TDS or were full time employees of Aerial.

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[1] The $25.50 per share merger price less the $22.00 per share value ascribed to each Aerial share in the debt replacement transaction.

As earlier noted, the plaintiff brought this action both individually and on behalf of Aerial's other minority shareholders. The plaintiffs claim is that the -minority shareholders were damaged by the debt replacement transaction, and that the Aerial directors' approval of that transaction constituted a breach of the directors' fiduciary duties to the Aerial minority. The defendants have moved to dismiss the complaint on two grounds. The first is that the plaintiff has no standing to assert his claims; the second is that the complaint fails to state a claim upon which relief may be granted under Court of Chancery Rule 12(b)(6). This is the Opinion of the Court on that motion. Because the Court concludes that the plaintiff no longer has standing to maintain this action, it does not reach the issue of whether the complaint states cognizable legal claims.

II. THE CONTENTIONS AND APPLICABLE PROCEDURAL STANDARD

The defendants argue that the plaintiff lacks standing to challenge the debt replacement transaction because (i) the plaintiffs challenge is necessarily derivative in nature and (ii) as a result of the Aerial-VoiceStream merger, the plaintiff is no longer a shareholder of Aerial and, accordingly, no longer satisfies the "continuous stock ownership" requirement that is a condition precedent to maintaining a derivative action.[2]

The plaintiff responds that it has standing to challenge the debt replacement transaction, because its claim for stock dilution is not a derivative claim to redress damage caused to Aerial. Rather, plaintiff contends, it is asserting a direct claim which the merger could not and did not extinguish.

The essence of the plaintiffs direct claim is that the debt replacement transaction amounted to wrongful self-dealing because at the time TDS agreed to that transaction, TDS, as an Aerial insider, knew that (i) Aerial and VoiceStream would be merging, and that (ii) the merger exchange ratio would provide TDS with an immediate $3.50 per share profit not enjoyed by Aerial's minority stockholders. The plaintiff alleges that TDS controlled Aerial's board and that a majority of Aerial's board of directors had disabling conflicts of interest. Therefore (plaintiff contends), it is inferable that TDS dictated the terms of the debt replacement transaction, and in particular, the $22 per share valuation of the Aerial stock: being issued to TDS in that exchange. That price, which is said to be less than Aerial's fair

[2] *Parnes v. Bally Entertainment Corporation,* Del., Supr., 722 A.2d 1243, 1245 (1999) ("the stockholder must maintain his or her status as a stockholder in order to continue the litigation"). As a result of the merger, the plaintiff ceased being a shareholder of Aerial, instead becoming a shareholder of VoiceStream.

value, would favor TDS at the expense of Aerial, because it would result in TDS receiving more Aerial stock than would be the case had the Aerial stock been fairly valued. As a consequence, the debt replacement transaction must be reviewed under the entire fairness standard, a standard the defendants allegedly cannot satisfy because the debt replacement transaction was not entirely fair to the Aerial minority shareholders.[3]

On a Rule 12(b)(6) motion to dismiss, the Court will assume the truth of all well pleaded allegations of the complaint,[4] and will draw all reasonable inferences in favor of the non-moving party.[5] While the "truthfulness of all well-pleaded allegations in the complaint is to be assumed," conclusions and cursory statements are not accepted unless they are supported by specific allegations of fact.[6] To grant the defendants' dismissal motion, the Court must find that the plaintiff would not be entitled to relief under any set of facts reasonably presented by the complaint.[7] The

[3] The plaintiff also argues that the defendants impermissibly refer to facts outside the complaint which, for that reason, the Court should not consider.

[4] *Grobow v. Perot,* Del. Supr., 539 A.2d 180, 187 n.6 (1988).

[5] *In re USA Cafes, L.P. Litig.*, Del. Ch., 600 A.2d 43, 47 (1991).

[6] *Solomon v. Pathe Communications Corp.,* Del. Supr., 672 A.2d 35, 38-39 (1996) (citing *Grobow v. Perot, supra, 539* A.2d at 187 n.6.

[7] *Rabkin v. Phillip A. Hunt Chemical Corp.,* Del. Supr., 498 A.2d 1099, 1104 (1985).

complaint-and specifically the “standing issue”-are analyzed under this standard.

III. ANALYSIS

Preliminarily, all parties agree that as a legal matter any claims of Aerial were extinguished by the Aerial-VoiceStream merger. Accordingly, for the plaintiffs claim to survive dismissal, that claim must be direct, and not derivative.’ The defendants contend that because any challenge to the debt replacement transaction would necessarily be a derivative claim brought on behalf of Aerial, the plaintiff lacks standing to challenge that transaction. Moreover, defendants urge, even if the plaintiffs claim is direct, for the: claim to survive a dismissal motion the complaint must allege a resulting “special injury” caused to the class of shareholders that is distinct from, and independent of, any injury caused to the corporation. Because the complaint alleges no such special injury, the defendants conclude that the complaint must be dismissed on that basis as well.”

The plaintiff responds that it has standing to maintain the claim notwithstanding the merger, because it is asserting a direct claim on behalf of the minority shareholders for wrongful dilution of their Aerial stock, a

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[8] *See Lewis* v. *Anderson*, Del. Supr., 477 A.2d 1040, 1049(1984).

[9] *Kramer v. W. Pac. Indus., Inc.*, Del. Supr., 546 A.2d 348, 351 (1998).

claim that under Delaware case law is inherently "direct."[10] Moreover (the plaintiff argues) the complaint alleges a "special injury" to the minority shareholders, in that (i) the debt replacement transaction, which was accomplished specifically in contemplation of the merger, increased TDS's equity position in Aerial in relation to the position of the minority stockholders; and (ii) as a consequence, the equity position of Aerial's minority shareholders-in Aerial before the merger and in VoiceStream after the merger-was improperly diluted.

In evaluating these colliding positions, it must be kept in mind that although Aerial entered into these two major transactions in rapid succession, only the first-the debt replacement transaction—is challenged in this action. Shorn of all its trimmings, the challenge is that TDS, using inside information, exchanged its $420 million in Aerial debt in a self-dealing and unfair transaction for a greater number of Aerial shares than TDS would have received had the Aerial stock been fairly valued. For the reasons next discussed, I conclude first that these alleged wrongs are not individual in character, because if there was any resulting injury, it was not to the minority shareholders but only to the corporation.

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[10] *In re Tri-Star Pictures, Inc., Litigation,* Del. Supr., *634* A.2d 31'3 (1993) *("Tri-Star").*

The distinction between a direct and a derivative claim, which sometimes is difficult to apply in specific circumstances, "turns on the existence of direct or 'special' injury to the plaintiff stockholder."" Special injury is established "where there is a wrong suffered by a plaintiff that was not suffered by all stockholders generally, or where the wrong involves a contractual right of the stockholders, such as the right to vote."[12]

The complaint describes the special injury to the minority stockholders as follows:

> [t]he debt replacement transaction increased TDS's equity position in Aerial incident to or in anticipation of the merger. As a direct consequence of the debt replacement transaction, the equity position of Aerial's minority shareholders in Aerial before the merger and in VoiceStream after the merger was diluted.[13]

Thus, the "special injury" is claimed to be a dilution of the pre-merger equity value of the shares held by Aerial's minority stockholders. An equity

[11] *Turner v. Bernstein,* Del. Ch., C.A. No. 16190, Jacobs, V.C., Mem. Op. at ? (Feb. 9, 1999) (citing *First Interstate* at 18).

[12] *Tri-Star, 634* A.2d at 330.

[13] Plaintiffs Sur-Reply Brief at 2. Although the defendants claim that the plaintiff did not allege special injury in the complaint, I find that the special injury detailed in the complaint and quoted herein can be inferred from the allegations of the complaint.

value dilution claim is difficult to maintain directly (as opposed to derivatively),, because such a claim:

> . . . arises only in transactions where a significant stockholder sells its assets to the corporation in exchange for the corporation's stock, and influences the transaction terms so that the result is (i) a decrease (or "dilution") of the asset value and voting power of the stock held by the public stockholders and (ii) a corresponding increase (or benefit) to the shares held by the significant stockholder.[14]

Although at first glance the relevant allegations of the complaint appear to satisfy these criteria, a closer scrutiny reveals tlhat the plaintiff has failed to articulate a "special injury" to the minority shareholders that is a *sine qua non* for a direct claim to arise.

As the complaint alleges, TDS sold an asset ($420 million of Aerial debt) to Aerial in exchange for additional Aerial shares."' The pled facts make it reasonably inferable that TDS, as Aerial's majority stockholde whose director-designees controlled the board, dictated tlhe terms of that transaction. [16] The question becomes: does the complaint allege facts which show that the value of the stock held by Aerial's public stockholder

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[14] *Turner v. Bernstein, supra,* Mem. Op. at 44-45 (Feb. 9, 1999).

[15] Complaint, at ¶ 3; ¶¶ 22 & 23.

[16] *Id.,* at ¶¶ 22-27.

minority-but not its other shareholders--was wrongfully diluted? I conclude that the answer is no.

The complaint does not allege that the merger consideration—$25.50 (stock) per Aerial share was unfair. What it does allege is that TDS used its power as Aerial's majority stockholder to effect a transaction that enabled TDS to buy Aerial stock at $22 per share, knowing that the forthcoming merger would guarantee TDS a profit of $3.50 per share. Although such conduct may constitute a breach of the duty of loyalty, there is no basis, in the complaint to conclude that any harm caused by that breach affected the minority shareholders' stock *exclusively.* That is, the pled facts do not show that the share dilution suffered by the minority shareholders differed in any significant way from the "dilution" suffered by the entire body of Aerial's stockholders collectively.[17] Indeed, the complaint does not even articulate a direct economic injury to the minority's shares, since it does not indicate that but for the debt replacement transaction, Aerial's minority shareholders would have received more than $25 .50 in value of VoiceStream stock for

[17] Even if the number of shares issued by Aerial to TDS was excessive, the injury would be to the corporation, not to any individual shareholder. Each shareholder would suffer a proportionate diminution in the value of the corporation, as a whole. An indirect injury of that kind is an earmark of a claim that is classically derivative, even when asserted in conjunction with a merger. *See, In re First Interstate Bancorp Consol. Shareholder Litig.,* Del. Ch., 729 A.2d 851 (1998) (*aff'd sub nom., Bradley v. First Interstate Bancorp.,* Del. Supr., 748 A.2d 913 (2000)).

each of their Aerial shares. Insofar as the complaint reveals, the minority shareholders would have received the same $25.50 per share merger consideration, with or without the debt replacement transaction.

To support its position, the plaintiff relies heavily on *Tri-Star,* where the Supreme Court, on different pled facts, recognized a direct claim for stock value dilution. The transactional facts alleged in this complaint, however, differ significantly from those which led to that result in *Tri-Star.* In *Tri-Star,* a shareholder increased its stock interest in the corporation from 36.8% to 80%, in a series of transactions designed to gain absolute control." Thereafter, the corporation (Tri-Star) was acquired by Sony Corporation in a merger. Reversing this Court's grant of a motion to dismiss, the Supreme Court held that the minority shareholder plaintiffs' claims were not derivative, and accordingly survived the merger. The basis for that conclusion was that the complaint alleged facts showing that the defendants wrongful conduct had diluted both the economic value and the voting power

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[18] Coca-Cola Company, which held 36.8% of Tri-Star's stock, entered into a voting agreement with HBO, which held 9%. In addition, two other large shareholders, Technicolor, Inc. and Rank American, Inc., which held 9.8% of Tri-Star's common stock, entered into a voting agreement which required them to vote their shares the same way as Coca-Cola and HBO. Through those agreements, therefore, Coca-Cola had effective control of 56.6% of Tri-Star's common stock before the alleged wrongful transactions took place. The proxy materials, however, disclosed that Coca-Cola would not vote its shares (or cause: its affiliates to vote their shares) in favor of the wrongful transaction unless a majority of the minority first approved it, thereby making the minority's approval necessary.

of the minority stockholders' shares, but not the stock owned by the majority shareholder(s). The Supreme Court in *Tri-Star* held that the complaint stated a claim that the defendants had wrongfully manipulated the voting process to induce the minority shareholders to approve the transaction, and that as a result, the minority shareholders had suffered a proportionate loss of voting power, and thereby became powerless to prevent the subsequent merger.

The facts alleged here are materially different. Here, there is no allegation, and no inference can be drawn, that TDS manipulated the Aerial voting process. TDS already had 80% voting control of Aerial at the time of the debt replacement transaction, and thus (unlike the controlling stockholder(s) in *Tri-Star)* had no need to secure an approving vote of the minority stockholders. Moreover, the challenged transaction in *Tri-Star* gave Coca-Cola "total voting control" and diminished the minority's 43.4% interest to below 20%. That "diluted to the point of virtual oblivion" the minority shareholders' ability to oppose the subsequent merger.[19] Here, by way of contrast, the minority-which owned only 20% of Aerial's stock-

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" Although the *Tri-Star* minority had the contractual power to block the wrongful transactions, they were effectively stripped of that right because their approving vote was procured by the controlling majority's non-disclosure of material facts.

already inhabited the region of "virtual [voting power] oblivion," and thus never had voting power sufficient to block any transaction involving Aerial.

In short, the Aerial minority shareholders did not suffer, as a result of the debt replacement transaction, the unique dilution that was inflicted on the minority in *Tri-Star,* nor did the Aerial minority suffer any "special injury" distinct from that inflicted upon all of Aerial's shareholders collectively. Here, there is no cognizable dilution because the complaint does not disclose any meaningful direct injury to Aerial's minority shareholders. The minority suffered no injury to their voting power because they had no voting control or veto power before the debt replacement transaction. Nor did they suffer a distinct economic injury, because there is no claim that the wrongful increase in TDS's holdings of Aerial affected the merger exchange ratio. Essentially, all that is claimed is that TDS wrongfully caused Aerial to "overpay" to repurchase its own debt-a classic claim for waste of corporate assets where the resulting injury is a diminution in the value of the corporation as a whole, rather than an injury unique to any specific shareholder group. By their nature, claims for corporate waste are derivative.

Being (derivative, the plaintiffs claim did not survive the merger. For that reason, the plaintiff no longer has standing to maintain this action.“’

IV. CONCLUSION

The defendants’ motion to dismiss the complaint is granted. IT IS SO ORDERED.

[20] As noted, because the Court concludes that the plaintiff does not have standing to sue, the question of whether a claim is stated in the complaint upon which relief may be granted will not be addressed.