

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

RICHARD A. WILLIAMSON, on behalf of)
and as trustee for, the Bondholders' Liquidating)
Trust of At Home Corporation and in the name)
of At Home Corporation,)

Plaintiff,)

v.)

COX COMMUNICATIONS, INC., COX)
@HOME, INC., COMCAST CORPORATION,)
COMCAST ONLINE COMMUNICATIONS,)
INC., COMCAST PC INVESTMENTS, INC.,)
DAVID M. WOODROW,)
and BRIAN L. ROBERTS,)

Defendants.)

C.A. No. 1663-N

MEMORANDUM OPINION

Date Submitted: March 27, 2006

Date Decided: June 5, 2006

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CHANDLER, Chancellor

Two cable companies shared joint control over an Internet service provider (“ISP”) in which they held minority equity stakes. The ISP was in the business of providing Internet services to customers of the cable companies. The cable companies sold their joint control to a third cable company through a transaction that is alleged to have been unfair to the ISP. At issue in this litigation is whether the cable companies were actually “controlling shareholders” for the purposes of this transaction and whether the transaction was unfair to the minority shareholders?

Plaintiff—the court appointed representative of the bondholders of At Home Corporation (“At Home” or the “Company”)—challenges the fairness of agreements At Home entered into in March 2000 with its three cable partners: defendant Comcast Corporation (“Comcast”), defendant Cox Communications (“Cox”), and non-party AT&T Corp. (“AT&T”).¹ These three cable partners were At Home’s largest and, plaintiff alleges, controlling shareholders. Plaintiff alleges that Cox and Comcast, together with their two designees to the At Home Board of directors—individual defendants David Woodrow and Brian Roberts—breached fiduciary duties to At Home by causing the Company to enter into the March 2000 Transactions.

¹ Plaintiff brought suit in California against AT&T for breaches of fiduciary duty and for theft of trade secrets. That case settled in May 2005.

I. FACTS

A. *The Formation of At Home*

Telecommunications Inc. (“TCI”), a cable company, founded At Home in March 1995.² At Home, a Delaware corporation, was founded to provide high-speed Internet access to customers through cable television lines.³ In August 1996, Cox and Comcast, also cable companies, acquired minority stockholdings in the Company.⁴ Following the investment by Cox and Comcast, At Home sold stocks and bonds to public investors.⁵

B. *TCI’s Initial Control Over At Home*

At the outset, TCI controlled At Home through its ownership of the At Home series B super-voting common stock.⁶ Ownership of these shares provided TCI with in excess of 70% of the voting power of At Home stock.⁷

TCI’s representatives on the At Home board had the power to control board decisions. At Home’s board of directors was divided into six series A directors and five series B directors. At Home’s certificate of incorporation required that board decisions be approved by a majority of the five series B

² Compl. ¶ 19.

³ Compl. ¶ 19.

⁴ Compl. ¶¶ 12, 14, 15 and 20 (Cox acquired 29,114,600 shares of At Home series A common stock, representing 8.3% of the outstanding series A shares. Comcast acquired 31,118,924 shares of At Home series A common stock, representing 8.8% of the outstanding series A shares.)

⁵ Compl. ¶ 20.

⁶ Compl. ¶ 29.

⁷ Compl. ¶ 26.

directors.⁸ Appointment of the series B directors was governed by a stockholders' agreement between TCI, Cox and Comcast (the "Stockholders' Agreement").⁹ The Stockholders' Agreement provided Cox and Comcast with the right to each designate one series B director, with the remaining three being appointed by TCI.¹⁰

C. The Original Master Distribution Agreements

At Home was in the business of providing high-speed Internet access to cable subscribers of TCI, Cox and Comcast (collectively, the "Cable Companies"). The partnership between At Home, on the one hand, and the Cable Companies, on the other, was governed by agreements called Master Distribution Agreements ("MDAs").¹¹ The first set of MDAs (the "Original MDAs") provided that At Home would provide Internet services to cable customers. In return, At Home would be entitled to a 35% share of the subscription revenues paid by the cable company subscribers to the Cable Companies for high-speed Internet access provided by At Home.¹² The MDAs also provided that the Cable Companies would use At Home as their

⁸ Compl. ¶ 27.

⁹ Compl. ¶ 27.

¹⁰ Compl. ¶ 27. Pursuant to the stockholders' agreement, Cox appointed defendant David M. Woodrow (a senior executive of Cox) and Comcast appointed defendant Brian L. Roberts (the President of Comcast) to the At Home board as two of At Home's five Series B directors.

¹¹ Compl. ¶ 21.

¹² Compl. ¶ 21.

exclusive provider of high-speed Internet access (the “Exclusivity Obligation”).

D. AT&T’s Acquisition of TCI and AT&T’s Breach of the MDAs

AT&T acquired TCI in June 1998.¹³ AT&T stepped into TCI’s shoes with regard to the MDAs and the ownership and control of At Home. Soon after its acquisition of TCI, AT&T breached the MDAs.¹⁴ The MDAs provided that if AT&T (formerly TCI) was unable to sign-up a certain number of At Home high-speed Internet customers by a specified date, Cox and Comcast could terminate the Exclusivity Obligation.¹⁵ AT&T failed to sign up the required number of subscribers by the specified date.

To induce Cox and Comcast not to terminate the Exclusivity Obligation, AT&T agreed to amend At Home’s Certificate of Incorporation to provide that At Home board action required approval by four of the five Series B directors.¹⁶ Because Cox and Comcast had the right to appoint one series B director each, this amendment to the Certificate of Incorporation effectively gave Cox and Comcast the power to veto board decisions if their board designees voted together.

¹³ Compl. ¶ 29.

¹⁴ Compl. ¶ 30.

¹⁵ Compl. ¶ 30.

¹⁶ Compl. ¶ 31.

E. The March 2000 Agreements

The complaint alleges that AT&T quickly realized that splitting up control over board decisions among the three Cable Companies had been a mistake. On March 28, 2000, AT&T, Cox, and Comcast entered into a series of agreements (the “March 2000 Agreements”) that transferred complete control back to AT&T and that, the complaint alleges, greatly benefited each of the Cable Companies at the expense of At Home.¹⁷ The complaint further alleges that the Cable Companies *actually* exerted their control over At Home in order to cause At Home to take steps that were necessary to implement the March 2000 Agreements. In order to facilitate the transfer of control back to AT&T, defendants Woodrow and Roberts voted to amend At Home’s Certificate of Incorporation to provide that AT&T would thereafter have the right to appoint all five of the At Home series B directors.¹⁸ Woodrow and Roberts then resigned from the At Home board of directors.¹⁹

Defendants also allegedly caused At Home to enter into new Master Distribution Agreements (the “March 2000 MDAs”). In their final form, the March 2000 MDAs gave Cox and Comcast the right to break the Exclusivity Obligation and to demand “exit services” from At Home when they exited

¹⁷ Compl. ¶ 34.

¹⁸ Compl. ¶ 34.

¹⁹ Compl. ¶ 34(a).

the business. These “exit services” included technical assistance to be provided by At Home, as well as the transfer of certain At Home assets to Cox and Comcast.²⁰ Defendants also allegedly used their control over At Home to cause the Company to enter into one-sided service level agreements.²¹ These agreements obligated At Home to pay Cox and Comcast penalties in the event that At Home failed to maintain minimum service level requirements.²²

At Home created a special committee to consider the March 2000 Transactions.²³ The special committee, however, was not created until *twenty-four hours* before the full At Home board was scheduled to meet to vote on the March 2000 Transactions. Moreover, the special committee’s review occurred *after* all of the terms of the March 2000 Transactions had already been negotiated and reduced to writing and the review occurred without the benefit of independent legal or financial advisors.²⁴ Additionally, the special committee lacked the power or authority to negotiate better terms because it was merely asked to recommend the March 2000 Transactions to the full board of directors.²⁵ Finally, the full board of

²⁰ Compl. ¶ 41(d).

²¹ Compl. ¶ 41(e).

²² Compl. ¶ 41(e).

²³ Compl. ¶ 39. The special committee consisted of two independent, Series A directors: William R. Hearst, III and John Doerr.

²⁴ Compl. ¶ 39.

²⁵ Compl. ¶ 39.

directors did not have the power to approve or disapprove the transaction because that power was entirely in the hands of the series B directors. When the At Home board met to vote on the March 2000 Agreements, each of the five series B directors (including defendants Woodrow and Roberts) voted in favor of the March 2000 Transactions.²⁶

The March 2000 Transactions were conditioned on approval by At Home's stockholders of the proposed amendments to At Home's Certificate of Incorporation.²⁷ At Home shareholders voted in favor of the proposed amendments to the Certificate of Incorporation.²⁸ The vote was not conditioned on approval by a majority of the minority shareholders. Cox, Comcast and AT&T controlled more than 63% of the vote.²⁹

F. At Home's Bankruptcy Filing

At Home filed for bankruptcy in September 2001 and ceased commercial operations in early 2002.³⁰ As of the filing of the complaint, At Home's assets were in the process of being sold, liquidated or transferred pursuant to a plan of reorganization.³¹ Plaintiff brings this action pursuant to an order issued by the United States Bankruptcy Court for the Northern District of California transferring to the Bondholders Liquidating Trust the

²⁶ Compl. ¶ 40.

²⁷ Compl. ¶ 44.

²⁸ Compl. ¶¶ 45 and 47.

²⁹ Compl. ¶ 45.

³⁰ Compl. ¶ 11.

³¹ Compl. ¶ 11.

Company's causes of action against Cox and Comcast and the individual defendants.³² Plaintiff asserts a single cause of action for breach of fiduciary duty against Cox, Comcast, Woodrow and Roberts. Defendants Cox and Comcast, together with their board designees, have each filed motions to dismiss.³³

At Home first filed a breach of fiduciary duty claim against defendants in connection with the March 2000 Transactions on September 24, 2002 in the United States District Court for the District of Delaware.³⁴ This breach of fiduciary duty claim was asserted as a pendent claim (the third cause of action) to At Home's federal claims (the first and second causes of action) for illegal "short swing profits" arising out of the March 2000 Transactions.³⁵ After transfer of the case to the Southern District of New York, defendants filed motions to dismiss plaintiff's federal claims on the basis of statute of limitations and failure to state a claim.³⁶ The Federal Court granted defendants' motions to dismiss the short swing profits claims and, with the parties' agreement, dismissed the breach of fiduciary duty claim without prejudice pursuant to 28 § U.S.C. 1367(c)(3).³⁷ The parties

³² Compl. ¶ 10.

³³ Cox brings its motion to dismiss together with individual defendant Woodrow. Comcast brings its motion to dismiss together with individual defendant Roberts.

³⁴ Compl. ¶ 10.

³⁵ Compl. ¶ 10.

³⁶ Pl.'s Reply Br. at 42.

³⁷ Compl. ¶ 10.

signed a tolling agreement (“Tolling Agreement”) that tolled the statute of limitations for the breach of fiduciary duty claim, the third cause of action in the previously filed federal action.

II. LEGAL STANDARD

Dismissal pursuant to Chancery Court Rule 12(b)(6) is appropriate “only when it appears with reasonable certainty that the plaintiff would not be entitled to relief under any set of facts that can be inferred from the pleadings.”³⁸ This Court “must assume the truthfulness of all well-pled allegations in the complaint and view those facts, and all reasonable inferences drawn from them, in the light most favorable to the plaintiff.”³⁹ Conclusory allegations unsupported by factual averments will not be considered for purposes of this motion.⁴⁰

III. ANALYSIS

A. Plaintiff’s Fiduciary Duty Claim Against Cox and Comcast

A shareholder does not owe a fiduciary duty to the company’s other shareholders unless she is a “controlling shareholder.”⁴¹ The test for control has two prongs: A shareholder is a “controlling” one if she owns more than 50% of the voting power in a corporation *or* if she “exercises control over

³⁸ *Tooley v. AXA Fin., Inc.*, 2005 WL 1252378, at *3 (Del. Ch. May 13, 2005).

³⁹ *Id.* (citing *Anglo. Am. Sec. Fund, L.P. v. S.R. Global Int’l Fund, L.P.*, 829 A.2d 143, 148-149 (Del. Ch. 2003)).

⁴⁰ *Grimes v. Donald*, 673 A.2d 1207, 1214 (Del. 1996).

⁴¹ *Kahn v. Lynch Commc’n Sys., Inc.*, 638 A.2d 1110, 1113-14 (Del. 1994).

the business and affairs of the corporation.”⁴² Where a shareholder stands on both sides of a transaction and is found to be a controlling shareholder, the transaction will be viewed under the entire fairness standard as opposed to the more deferential business judgment standard.⁴³

To survive defendants’ motions to dismiss, plaintiff must allege domination and control by Cox and Comcast through *actual* control of corporate conduct.⁴⁴ Simply alleging that they had the *potential* ability to exercise control is not sufficient.⁴⁵ It is not necessary, however, for plaintiff to plead actual control by Cox and Comcast over the day-to-day operations of At Home. Plaintiff can survive the motion to dismiss by alleging actual control with regard to the particular transaction that is being challenged.⁴⁶

Based on the particular facts of this case as alleged in the complaint, together with all the reasonable inferences granted at this stage of the litigation, I conclude that the complaint contains facts that do support, at a minimum, the *inference* that Cox and Comcast were controlling

⁴² *Id.*

⁴³ *Id.* at 1116.

⁴⁴ *O’Reilly v. Transworld Healthcare, Inc.*, 745 A.2d 902, 912 (Del. Ch. 1999).

⁴⁵ *In re Sea-Land Corp. S’holders Litig.*, 1987 WL 11283, at *5 (Del. Ch. May 22, 1987) (citing *Gilbert v. El Paso Co.*, 490 A.2d 1050, 1055-56 (Del. Ch. 1984)).

⁴⁶ *In re Western Nat’l Corp. S’holders Litig.*, 2000 WL 710192, at *20 (Del. Ch. May 22, 2000) (“[A] significant stockholder that does not, as a general matter, exercise actual control over the investee’s business and affairs or over the investee’s board of directors but does, in fact, exercise actual control over the board of directors during the course of a particular transaction, can assume fiduciary duties for purposes of that transaction.”) (citing *Kahn v. Lynch*, 638 A.2d at 1114-15).

shareholders.⁴⁷ I summarize the well-plead facts that support this inference below.

1. Cox and Comcast's Designees to the At Home Board of Directors

The fact that an allegedly controlling shareholder appointed its affiliates to the board of directors is one of many factors Delaware courts have considered in analyzing whether a shareholder is controlling.⁴⁸ Cox and Comcast each appointed a designee to be one of the five At Home series B directors. AT&T appointed the remaining three series B directors. The net effect of this arrangement was that control of the At Home board was split between the representatives of the three Cable Companies. Cox appointed Woodrow, a senior Cox executive, and Comcast appointed Roberts, who was at all relevant times the President of Comcast Corporation and one of its directors. Woodrow and Roberts could not be considered, in any sense of the word, independent of Cox and Comcast, and at this stage of

⁴⁷ *O'Reilly v. Transworld Healthcare, Inc.*, 745 A.2d 902, 912 (Del. Ch. 1999) (a plaintiff “can plead sufficiently that a stockholder has actual control of corporate conduct by alleging facts from which a stockholder’s exercise of corporate control can be inferred....”)

⁴⁸ *See, e.g., Kahn v. Lynch*, 638 A.2d 1110 (Del. 1994) (46% shareholder found to be controlling on the basis of several facts, including that shareholder designated directors to five of the eleven board seats). *See also In re Western Nat'l Corp. S'holders Litig.*, 2000 WL 710192, at *20 (Del. Ch. May 22, 2000) (finding a shareholder to be non-controlling on the basis of several factors, including that none of the shareholder’s “managers, employees, agents, or even nominees sat on [the allegedly controlled entity’s] board of directors”); *O'Reilly v. Transworld Healthcare, Inc.*, 745 A.2d 902, 913 (Del. Ch. 1999) (finding a 49% shareholder to be a controlling shareholder on the basis of several facts, including that two of the controlled entities four directors had conflicts of interest in the challenged transaction.)

the litigation I must infer that they acted as the representatives of their employer's interests.⁴⁹

The fact that Cox and Comcast nominated directors to the At Home board does not, without more, establish actual domination or control.⁵⁰ To hold otherwise would have a chilling effect on transactions that depend on a particular shareholder being able to appoint representatives to an investee's board of directors.⁵¹ But this is not a case where plaintiff alleges control based solely, or even primarily, on the fact that defendants appointed two directors. As discussed below, plaintiff also points to Cox and Comcast's business relationship with At Home and their control over At Home board decisions.

⁴⁹ As directors of At Home, the individual defendants owed fiduciary duties to the Company. Plaintiff alleges that the individual defendants breached their duties by voting in favor of the March 2000 Transactions. The individual defendants allegedly voted in favor of the March 2000 Agreements in order to further Cox and Comcast's interests, not At Home's. Plaintiff also alleges the individual defendants voted to approve the March 2000 Agreements even though they knew that AT&T planned to use its control position to plunder the assets of the Company. These allegations (which are accepted as true at this stage) are sufficient to support a claim for breach of the duty of loyalty against the individual defendants.

⁵⁰ *In re Sea-Land Corp. S'holders Litig.*, 1987 WL 11283, at *5 (Del. Ch. May 22, 1987) ("Even if Simmons had caused its nominees to be elected to the Sea-Land board... that fact, without more, does not establish actual domination or control.") (citing *Kaplan v. Centex Corp.*, 284 A.2d 119, 123 (Del. Ch. 1971).

⁵¹ *See Emerson Radio Corp. v. Int'l Jensen Inc.*, 1996 WL 483086, at n.18 (Del. Ch. Aug. 20, 1996) ("If plaintiffs' argument were the law, then whenever a director is affiliated with a significant stockholder, that stockholder automatically would acquire the fiduciary obligations of the director by reason of that affiliation alone. The notion that a stockholder could become a fiduciary by attribution (analogous to the result under the tort law doctrine of respondeat superior) would work an unprecedented, revolutionary change in our law, and would give investors in a corporation reason for second thoughts about seeking representation on the corporation's board of directors.")

2. The Business Relationship Between At Home and Cox and Comcast

The Cable Companies were At Home's only significant customers and At Home depended on their cooperation as customers if it was going to operate its business profitably. Plaintiff alleges that, under the revenue sharing agreement between At Home and the Cable Companies, the Cable Companies were able to (and did) exert control over At Home by influencing the flow of revenue to At Home. These allegations support the inference that the Cable Companies had significant leverage over At Home and were able to dictate to At Home the terms of the March 2000 Agreements.

3. Cox and Comcast's "Veto" Power

There is no case law in Delaware, nor in any other jurisdiction that this Court is aware of, holding that board veto power *in and of itself* gives rise to a shareholder's controlling status. Delaware law requires actual control, not merely the potential to control, and in this case plaintiff makes no allegation that Cox and Comcast ever affirmatively vetoed any At Home board decisions.

Cox and Comcast's potential veto power is significant for analysis of the control issue, however, because it supports plaintiff's allegation that Cox and Comcast had coercive leverage over At Home. Cox and Comcast had

the ability to shut down the effective operation of the At Home board of directors by vetoing board actions. Plaintiff may be able to prove facts showing that this leverage (together with the special business relationships and other circumstances mentioned above) was enough for Cox and Comcast to obtain a far better deal than they would have in an arm's-length transaction.⁵²

B. The Tolling Agreement

In the Tolling Agreement, the parties agreed “to toll the statute of limitations ... for the Third Cause of Action” asserted in the plaintiff’s federal securities action complaint. The third cause of action in the federal securities action asserted a claim for “breach of fiduciary duties against all defendants” and sought compensatory damages.

Defendants contend that plaintiff’s breach of fiduciary duty claim should be dismissed as time-barred because the current breach of fiduciary duty claim is not the same as the previously asserted cause of action in the federal complaint. The Third Cause of Action in the earlier federal action

⁵² Given that plaintiff alleges the March 2000 Agreements were a way for AT&T to acquire sole control of At Home, it is tempting to conclude that AT&T effectively represented At Home’s interests in the negotiations with Cox and Comcast. From this, one might conclude that At Home enjoyed the benefit of AT&T’s negotiating leverage, which even the complaint alleges to have been substantial. The reason this is not persuasive at this stage of the case is that the complaint also alleges that AT&T’s interests were *not* aligned with At Home’s. According to plaintiff, the March 2000 Agreements were the culmination of a process by which AT&T, Cox and Comcast agreed to carve-up the assets of At Home amongst themselves, with no regard for the interests of At Home’s other shareholders.

was captioned “breach of fiduciary duties against all defendants” and asserted that defendants owed fiduciary duties to At Home and breached those duties in connection with the March 2000 Transactions.⁵³ Applying standard principles of contract interpretation, I conclude that the claim in this case is exactly the same cause of action as the tolled cause of action, i.e., a claim for breach of fiduciary duty against Cox, Comcast, Woodrow and Roberts arising out of the March 2000 Transactions. I also conclude that what defendants characterize as plaintiff’s alleged “control premium claim” is really just a theory of damages. Accordingly, it does not change the nature of the claim in a manner that would remove it from the scope of the tolling agreement. For these reasons, I conclude that the Tolling Agreement tolled the statute of limitations for the claim asserted in this case.

IV. CONCLUSION

The question whether a shareholder is a controlling one is highly contextualized and is difficult to resolve based solely on the complaint.⁵⁴ No single allegation in plaintiff’s complaint is sufficient on its own to defeat defendants’ motions to dismiss. Designating directors to the board of directors or entering into business agreements with an investee is not sufficient to trigger a finding of “controlling” status. Nor is the allegation

⁵³ See Cox Appendix, at Ex. 10, at ¶¶ 77-84.

⁵⁴ *In re Cysive, Inc. S’holders Litig.*, 836 A.2d 531, 550-551 (Del. Ch. Aug. 15, 2003.)

that Cox, Comcast and AT&T had parallel interests sufficient to allege that the Cable Companies were part of a “controlling group.”⁵⁵

The complaint succeeds because it pleads a nexus of facts all suggesting that the Cable Companies were in a controlling position and that they exploited that control for their own benefit. The well-plead facts taken together give rise to the inference that the March 2000 Agreements were the culmination of a process by which AT&T, Cox and Comcast agreed to carve-up the assets of At Home among themselves, with no regard for the interests of At Home’s other shareholders. The complaint’s allegations, therefore, are sufficient to withstand a motion to dismiss. The motion to dismiss is denied.

IT IS SO ORDERED.

⁵⁵ *Kennedy v. Venrock*, 348 F.3d 584, 590-91 (7th Cir. 2003).