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Case No. 6120-VCN

IN THE COURT OF CHANCERY FOR THE STATE OF DELAWARE

RICHARD FRANK, Plaintiff, v. ZAK W. ELGAMAL, JAIME OLMO-RIVAS, BLAND E. CHAMBERLAIN III, JOSE CHAPA JR., CHARLES BAILEY, MICHAEL KLEINMAN, HENRY Y. L. TOH, GREAT POINT PARTNERS I, LP, AH HOLDINGS INC., AH MERGER SUB, INC., and AMERICAN SURGICAL HOLDINGS, INC., Defendants.	)	**C.A. No. 6120-VCN**

MEMORANDUM OPINION

Date Submitted: December 22, 2011
Date Decided: March 30, 2012

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NOBLE, Vice Chancellor

I. INTRODUCTION

This action arises out of the merger (the "Merger") of American Surgical Holdings, Inc. ("American Surgical" or the "Company") with AH Merger Sub, Inc. ("Merger Sub"), a wholly-owned subsidiary of AH Holdings, Inc. ("Holdings"), which, in turn, is an affiliate of Great Point Partners, I LP ("Great Point" and collectively, with Merger Sub and Holdings, the "Purchasing Entities"). Plaintiff Richard Frank brought this purported class action to challenge the Merger. Frank alleges that American Surgical's Board of Directors (the "Board"), and the Company's control group (the "Control Group" and collectively, with the Purchasing Entities and the Board, the "Defendants") breached their fiduciary duties in connection with the Merger. Frank also alleges that the Purchasing Entities aided and abetted those breaches of fiduciary duty. The Defendants have moved to dismiss all of the claims asserted against them. This is the Court's decision on the Defendants' motion.

II. BACKGROUND[1]

A. *The Parties*

Frank was, at all relevant times, the owner of shares of American Surgical common stock.

[1] Except in noted instances, the factual background is based on the allegations in the Verified Amended Class Action Complaint (the "Complaint" or "Compl.").

Before the Merger, American Surgical was a Delaware corporation with its principal executive offices in Houston, Texas. American Surgical provided professional surgical assistant services to patients, surgeons, and healthcare institutions in Texas, Oklahoma, Virginia, Tennessee, and Georgia. The Company's common stock traded on the Over-the-Counter Bulletin Board.

Defendants Zak W. Elgamal, Jamie Olmo-Rivas, Charles Bailey, Michael Kleinman, and Henry Y.L. Toh were, at all relevant times, the members of the Board. Elgamal also was Chairman of the Board, as well as American Surgical's President and Chief Executive Officer. Before the Merger, Elgamal owned 27.53% of American Surgical's common stock. Olmo-Rivas was the Company's Chief Operating Officer, and, before the Merger, he owned 27.58% of the Company's common stock.

Until the Merger, Defendants Jose Chapa Jr. and Bland E. Chamberlain III were surgical assistants employed with American Surgical. In addition, Chapa was one of the Company's most highly compensated executive officers, and he owned 8.04% of American Surgical's common stock. Chamberlain owned 8.04% of the Company's common stock. Elgamal, Olmo-Rivas, Chapa, and Chamberlain make up the Control Group.[2] Immediately before the Merger, the Control Group held

[2] Early on in this Memorandum Opinion, the phrase "Control Group" is used for convenience. The Defendants question whether the four individuals may fairly be characterized as a "control group."

71.19% of American Surgical's common stock. The Complaint alleges that the members of the Control Group, "as majority shareholders of the Company acting in concert, owed fiduciary duties to the public shareholders of the Company . . . ."[3]

Defendant Great Point is a private-equity fund affiliated with Great Point Partners, an investment firm based in Greenwich, Connecticut that specializes in recapitalization transactions involving middle-market health care companies. Defendant Holdings, an affiliate of Great Point, and Defendant Merger Sub, a wholly-owned subsidiary of Holdings, were created solely to effectuate the Merger.

B. *Factual Background and Procedural History*

On August 12, 2009, the Board created a mergers and acquisitions committee (the "M&A Committee"), consisting of directors Toh, Elgamal, and Olmo-Rivas, to explore strategic opportunities for the Company. Soon after it was formed, the M&A Committee hired the Polaris Group ("Polaris") to serve as the Company's financial advisor. On December 2, 2009, the Board designated directors Bailey and Kleinman as a special committee (the "Special Committee"). The purpose of the Special Committee was to "negotiate the terms and conditions of any potential transaction involving the sale of the Company,"[4] but the

[3] Compl. ¶ 2.
[4] *Id.* at ¶ 44.

Complaint alleges that "the members of the Special Committee engaged in little, if any, negotiations."[5]

From August 2009 through December 2009, Polaris solicited potential business combinations for American Surgical. "After various rounds of information sharing involving many strategic and financial entities, four parties emerged as having a continued interest in discussing a possible transaction."[6] The Complaint alleges that a company, described as Private Equity Firm A, proposed a strategic transaction to American Surgical that was superior to the Merger:

> The proposal from Private Equity Firm A was not a full cash buyout offer but a multi-million dollar investment in the Company that would have allowed the Company to fund its expansion, and also allow the Company's public shareholders to continue their investment in the Company as it continues to expand to other states. . . . Private Equity Firm A's proposal valued the Company at $46 million. However, the proposal from Private Equity Firm A was not as lucrative to the . . . [Control Group]. Accordingly, the . . . [Control Group] pushed forward with the Merger offered by Great Point . . . .[7]

The Special Committee, however, determined that the Merger "represented the most favorable transaction for the Company's shareholders"[8] and "retained a

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[5] *Id.*

[6] *Frank v. Elgamal*, 2011 WL 3300344, at *2 (Del. Ch. July 28, 2011) (the "Letter Opinion" or "Letter Op."). The Court draws certain background facts and aspects of the procedural history from the Letter Opinion. Nothing taken from the Letter Opinion is material to the Court's analysis.

[7] Compl. ¶ 46.

[8] Letter Op., 2011 WL 330344, at *2.

separate financial advisor—Howard Frazier Barker Elliott, Inc. ["HFBE"]—to render a fairness opinion with respect to a possible transaction with Great Point."[9]

On December 20, 2010, after months of negotiations between American Surgical and Great Point, American Surgical entered into an agreement and plan of merger (the "Merger Agreement") with Holdings and Merger Sub. The Merger was structured as a reverse triangular merger—Merger Sub merged with American Surgical, and American Surgical survived as a wholly-owned subsidiary of Holdings. Under the terms of the Merger Agreement, each share of American Surgical common stock was converted into a right to receive $2.87 in cash.[10] The Merger Agreement also provides that "[t]he affirmative vote of the holders of a majority of the outstanding Common Shares on the record date for the Company Meeting is the only vote of holders of securities of the Company which is required to approve and adopt this Agreement . . . [and] the Merger . . . ."[11] Moreover, the Merger Agreement contained several defensive devices, including a termination fee, a matching rights provision, and a no-shop clause.

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[9] *Id.*

[10] "[U]nder the terms of the Merger Agreement, . . . American Surgical's stockholders would [also] receive (a) additional per share merger consideration consisting of a final cash dividend, if any, payable by the Company and computed in accordance with the . . . [Merger Agreement], and (b) an ownership interest in CMC Associates, LLC, a subsidiary of the Company, which will be the beneficial owner of certain pending litigation and litigation rights. The value of the potential dividend and ownership interest in CMC Associate[s], LLC, was not ascertainable prior to the consummation of the Merger." Compl. ¶ 35. American Surgical's shareholders received a dividend of $0.02 per share on March 23, 2011. Letter Op., 2011 WL 3300344, at *2.

[11] Compl. ¶ 43.

On December 20, 2010, three sets of agreements, in addition to the Merger Agreement, were entered into in connection with the Merger.[12] First, each member of the Control Group executed a stockholder voting agreement (the "Voting Agreements") with Holdings. In the Voting Agreements, each member of the Control Group agreed to vote all of the American Surgical common shares he owned in favor of the Merger. At that time, the members of the Control Group owned about 64% of American Surgical's common stock, but by the record date of the Merger, they owned 71.19% of the Company's common stock.

Second, each member of the Control Group entered into an exchange agreement (the "Exchange Agreements") with Holdings. In the Exchange Agreements, each member of the Control Group agreed to exchange, immediately before the effective time of the Merger, some of his American Surgical common shares for shares of Holdings' Series A Preferred Stock. Collectively, the members of the Control Group agreed to, and subsequently did, exchange 2,234,707 shares of American Surgical common stock (about 17.4% of American Surgical's common stock) for a 14.9% ownership interest in Holdings. Thus, although American Surgical's minority shareholders would be cashed-out in the Merger, the Exchange Agreements, which were executed on the same day as the

[12] American Surgical Holdings, Inc., Current Report (Form 8-K) Ex. 10.1-10.12 (Dec. 23, 2010), *available at* http://www.sec.gov/Archives/edgar/data/1257499/000119312510287695/001193125-10-287695-index.htm. The Complaint incorrectly states that several of these agreements were entered into on December 23, 2010. *See* Compl. ¶¶ 8-11. The fact that these agreements were entered into on December 20, as opposed to December 23, is not material to the Court's analysis.

Merger Agreement, provided that the members of the Control Group would retain an interest in the Company following the Merger.

Third, each member of the Control Group signed an employment agreement with Merger Sub (the "Employment Agreements"), which became effective at the effective time of the Merger.

> Elgamal and Olmo-Rivas were each provided with a base annual salary of $386,250, an annual incentive bonus up to 100% of their base salary, and an additional annual bonus of 12.5% of any EBITDA generated in excess of certain set target EBITDA amounts for the 2010 and 2011 calendar year. . . . [Merger Sub] also granted to Defendants Elgamal and Olmo-Rivas performance-based stock options equal to 1.75% of the fully diluted shares of . . . Holdings . . . , which options would vest based on the achievement of certain EBITDA targets. . . . Defendants Chapa and Chamberlain were provided with a base annual salary of $250,000 and $175,000 respectively, [and] with discretionary bonuses of $100,000 and $50,000, respectively.[13]

On December 19, 2010, the day before the Merger Agreement was executed, HFBE stated its opinion that "the [Merger] consideration, without interest, to be received by the Company's stockholders (other than the . . . [Control Group]) was fair, from a financial point of view, to such holders."[14] The Complaint, however, takes issue with HFBE's fairness opinion. The Complaint alleges that the opinion was based, in part, on a flawed comparable company analysis. According to the

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[13] Compl. ¶ 42.

[14] American Surgical Holdings, Inc., Definitive Proxy Statement (Schedule 14A), at 11 (Jan. 21, 2011), *available at* http://www.sec.gov/Archives/edgar/data/1257499/000119312511011660/ddef14a.htm. The Court only relies on American Surgical's Definitive Proxy Statement for the proposition that HFBE gave a fairness opinion on December 19, 2010.

Complaint, HFBE divined a 5-7x EBITDA multiple for American Surgical by comparing it to companies that were not actually comparable. The Complaint argues that companies comparable to American Surgical were actually sold at EBITDA multiples of 11-15x. The Complaint further contends that, even assuming HFBE's comparable company analysis was properly performed, "the $2.87 Merger price was on the very low end of the Implied Per Share Equity Value Reference Ranges for the Company's Common Stock, and well below the midpoint of those ranges."[15] Moreover, the Complaint asserts that not all aspects of the fairness opinion were fairly disclosed to American Surgical's shareholders—"HFBE anticipated that the . . . [Merger] would provide $20-30 million in synergies to Great Point . . . [and that the Control Group, with its ongoing interest in the Company, would benefit from these synergies. But] this fact was not disclosed in the Definitive Proxy."[16]

On January 4, 2011, the Company filed its preliminary proxy statement.[17] On January 11, Frank initiated this action. On January 14, he moved for expedited proceedings and a preliminary injunction.[18] On January 21, American Surgical filed its definitive proxy statement, "which contained supplemental disclosures that effectively mooted the Plaintiff's disclosure claims. For that reason, Frank

[15] Compl. ¶ 59.
[16] *Id.* at ¶ 67.
[17] Letter Op., 2011 WL 3300344, at *2.
[18] *Id.*

withdrew his motions for expedited proceedings and for a preliminary injunction on January 24th."[19] On February 23, 2011, at a special meeting of American Surgical's common stockholders gathered for the purpose of voting on the Merger, 86.6% of the Company's common stock was voted, and 99.9% of those shares voted were cast in favor of the Merger. On March 23, 2011, the Merger closed.[20] On that same day, Toh received a $250,000 fee for his role in negotiating the Merger.

III. CONTENTIONS

The Complaint consists of four causes of action. Cause of Action I alleges that the members of the Control Group "acting in concert and together as a group, were controlling shareholders, and have violated their fiduciary duties of loyalty and care owed to the public shareholders of American Surgical . . . ."[21] More specifically, Cause of Action I alleges that the Merger "is an attempt to deny Plaintiff and the other members of the Class their right to share proportionately in the true value of the Company, while usurping the same for the benefit of the . . . [members of the Control Group] who will maintain an interest in American Surgical on terms that were unfair and inadequate to Plaintiff and the members of

[19] *Id.*
[20] *Id.*
[21] Compl. ¶ 69.

the Class."[22] Cause of Action I also suggests that the members of the Control Group breached their fiduciary duties because they possessed "non-public information concerning the financial condition of American Surgical, . . . which they did not disclose to American Surgical's public stockholders,"[23] Cause of Action II alleges that the members of the Control Group were unjustly enriched as a result of the Merger. Cause of Action III alleges that the members of the Board, as well as Chamberlain and Chapa have breached their duty "to ensure that any transaction where the controlling shareholders of the Company are standing on both sides, is fair to American Surgical's shareholders, and [their duty] to ensure that the Company's shareholders were provided with all material information required by them in order to determine whether or not to seek appraisal."[24] According to the Complaint, the members of the Board, Chamberlain, and Chapa "have violated their fiduciary duties to Plaintiff and the other Class members by acquiescing to an unfair process dictated by conflicted insiders."[25] Cause of Action IV alleges that the Purchasing Entities aided and abetted the breaches of fiduciary duty articulated in Causes of Action I and III. Cause of Action IV offers two reasons why the Purchasing Entities should be liable for aiding and abetting.

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[22] *Id.* at ¶ 72.
[23] *Id.* at ¶ 71.
[24] *Id.* at ¶ 81. In the alternative, Cause of Action III alleges that "in agreeing to the Merger, . . . [the members of the Board, Chamberlain, and Chapa] initiated a process to sell American Surgical that imposes a heightened fiduciary responsibility on them," *id.* at ¶ 85, which they have violated "by failing to maximize shareholder value." *Id.* at ¶ 86.
[25] *Id.* at ¶ 82.

First, the Purchasing Entities were "intimately involved in the negotiations and structuring of the . . . [Merger] and understood that the . . . [Control Group] and the minority shareholders were competing for the consideration that . . . [the Purchasing Entities] would pay to acquire American Surgical."[26] Second, the Purchasing Entities "demanded deal protection measures, including an excessive termination fee, matching rights, and a no-shop clause while enticing American Surgical's management to enter into a deal with them through equity offerings . . . and lucrative salaries and bonuses . . . ."[27] Frank seeks to: (1) certify this action as a class action; (2) rescind the Merger or, in the alternative, recover rescissory damages for the purported class; (3) have the Defendants account for all of the damages they caused the purported class; and (4) recover the costs of this action, including reasonable attorneys' fees.

The Defendants have filed a joint motion to dismiss the Complaint pursuant to Court of Chancery Rule 12(b)(6). The Defendants argue that the arguments made in support of Cause of Action I are insufficient to rebut the presumptions of the business judgment rule. The Defendants admit that a control group may, necessarily, have to show the entire fairness of a transaction that it stands on both

[26] *Id.* at ¶ 89.
[27] *Id.* at ¶ 90.

sides of,[28] but the Defendants argue that here, the Control Group did not stand on both sides of the Merger. The Defendants argue that, the Purchasing Entities, a group of third parties with no affiliation to any member of the Control Group, structured the terms of the Merger, and that "none of the alleged controllers in this case—individually or as a group—negotiated the part of . . . [the Merger] that involved the . . . [minority shareholders'] deal compensation."[29] Moreover, the Defendants argue that the members of the Control Group "were net ***sellers*** of American Surgical's shares in the Merger . . . ."[30]

> The . . . [members of the Control Group] sold 75% of their shares for the same Merger consideration as all of the other stockholders, and "rolled over" only 25% of their shares. Moreover, while the shares they rolled over represented nearly 18% of the outstanding stock of American Surgical, they were exchanged for only 15% of the acquiring company—a correspondingly smaller percentage of the acquiring company's shares. . . . In these circumstances, the Rollover Defendants would ***always*** be better off if a higher price were paid in the Merger.[31]

Because, according to the Defendants, the allegations in Cause of Action I are insufficient to overcome the presumptions of the business judgment rule, the Defendants argue that Cause of Action I fails to state a claim that the members of

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[28] *See* Joint Opening Br. in Supp. of Defs.' Mot. to Dismiss ("Defs.' Opening Br.") at 14 ("While entire fairness may apply *ab initio* where a controlling entity stands on both sides of a transaction (i.e., in a squeeze out merger or a merger between two companies with one shareholder ***controlling both sides***), '[e]ntire fairness is not automatically triggered when a *noncontrolling* shareholder appears on both sides of the challenged transaction.'") (quoting *Orman v. Cullman*, 794 A.2d 5, 20 n.36 (Del. Ch. 2002)).

[29] Joint Reply Br. in Supp. of Defs.' Mot. to Dismiss ("Defs.' Reply Br.") at 9.

[30] Defs.' Opening Br. at 16.

[31] *Id.*

the Control Group breached their fiduciary duties. The Defendants also dispute that Chamberlain and Chapa were part of the Control Group—"[w]ithout allegations that Chapa and Chamberlain were somehow needed to secure dispositive control over the transaction, they are not accused of violating any specific duties to the class shareholders and must be dismissed."[32]

In challenging Cause of Action II, the Defendants argue that a claim that the Control Group was unjustly enriched must fail for at least two reasons. First, the Defendants contend that "the dismissal of Plaintiff's First Cause of Action for Breach of Fiduciary Duty necessarily requires that the Unjust Enrichment claim fail as well."[33] Second, the Defendants contend that Frank's argument that the Control Group was unjustly enriched is based on a flawed interpretation of HFBE's fairness opinion. Specifically, the Defendants argue that Frank failed to consider projected net debt in calculating the enterprise value of American Surgical after the Merger. According to the Defendants, the fairness opinion, properly interpreted, shows that the Control Group was not enriched as a result of the Merger.

As for Cause of Action III, the Defendants argue that because the Control Group was not standing on both sides of the Merger, the decision to enter into the Merger Agreement is entitled to the presumptions of the business judgment rule, unless the Complaint pleads facts to suggest that a majority of the Board was not

[32] *Id.* at 28.
[33] *Id.* at 26.

independent and disinterested when the Board approved the Merger Agreement. The Defendants continue their argument by laying out why a majority of the Board was disinterested and independent. The Defendants concede that "[f]or purposes of this motion, Defendant directors Elgamal and Olmo-Rivas, who owned more than 55% of the Company's stock, and who received post-merger employment, discretionary bonuses, and ownership in the post-merger company may be considered to have had an 'interest' in the Merger."[34] But the Defendants contend that the other three members of the Board, Klienman, Bailey, and Toh, were independent and disinterested. Moreover, the Defendants argue that the terms of the Merger Agreement were negotiated by the Special Committee, and the Special Committee recommended that the Board enter into the Merger Agreement. According to the Defendants, the Special Committee was composed of independent and disinterested directors, Bailey and Kleinman, and therefore, the Defendants contend that the Special Committee's approval of the Merger is another basis upon which the Court should determine that the Board's decision to enter into the Merger Agreement is entitled to the presumptions of the business judgment rule. The Defendants also argue that, if they are correct that the presumptions of the business judgment rule apply to the Board's decision to undertake the Merger, any claim for monetary damages against any member of the

[34] *Id.* at 19-20.

Board, for breach of the duty of care, should be dismissed because American Surgical had adopted an exculpatory provision pursuant to 8 *Del. C.* §102(b)(7) which eliminates director liability for good faith breaches of the duty of care. "If, on the other hand, entire fairness does, or may, apply here, then Defendants are content to have the §102(b)(7) defense decided at trial or further summary disposition."[35]

With respect to Cause of Action IV, the Defendants argue that because Frank has failed to plead an underlying breach of fiduciary duty by the Board or the Control Group, a claim for aiding and abetting fails as a matter of law. Moreover, the Defendants argue that even if Frank has pled a claim for breach of fiduciary duty, he has failed to adequately plead that the Purchasing Entities knowingly participated in that breach.

In opposing the Defendants' motion to dismiss Cause of Action I, Frank argues that the Complaint adequately alleges that Elgamal, Olmo-Rivas, Chapa, and Chamberlain "were, together, majority shareholders of American Surgical, owing a fiduciary duty to the minority public shareholders."[36] Frank also argues that the Complaint adequately alleges that the members of the Control Group stood on both sides of the Merger because "they negotiated for themselves a material

[35] Defs.' Reply Br. at 24.
[36] Pl.'s Br. in Opp. to Defs.' Mot. to Dismiss ("Pl.'s Answering Br.") at 11.

interest in the surviving company,"[37] and therefore, that the Merger is subject to entire fairness review. "Moreover, even if the members of the controlling group did not stand on both sides of the . . . [Merger, Frank contends that] entire fairness might still be the appropriate standard of review at trial because no majority-of-the-minority provision was included as part of the . . . [Merger]."[38]

In support of Cause of Action II, Frank argues that the Complaint adequately pleads a claim for unjust enrichment against the members of the Control Group. Frank contends that the Defendants' argument that the unjust enrichment claim is based on a flawed analysis of HFBE's fairness opinion should not be addressed on a motion to dismiss—"[the Defendants'], or their expert's, disagreement with the analysis in the Complaint is not appropriately the subject for a motion to dismiss, but is a factual question that will be more appropriately answered after the completion of discovery."[39]

In defense of Cause of Action III, Frank argues that the Complaint adequately pleads that all of the Defendants were either interested in the Merger, or not independent, and therefore, that the Merger is subject to entire fairness review. Frank contends that each member of the Control Group was interested in the Merger because each received a material benefit (continued employment) in

[37] *Id.* at 11-12.
[38] *Id.* at 12.
[39] *Id.* at 29.

connection with the Merger. Frank further contends that Toh was interested in the Merger because he was paid $250,000 for his role in negotiating the Merger. According to Frank, "[s]uch a significant payment should, at least for purposes of this Motion, be considered a disabling conflict."[40] Frank argues that Bailey and Kleinman "were not independent because they had business relationships with the Company."[41] Specifically, Bailey and Kleinman, who are surgeons, worked at hospitals which allegedly have contractual relationships with one of American Surgical's subsidiaries.[42]

With regard to Cause of Action IV, Frank argues that the Complaint adequately pleads a claim for aiding and abetting.

IV. ANALYSIS

"Pursuant to [Court of Chancery] Rule 12(b)(6), this Court may grant a motion to dismiss for failure to state a claim if a complaint does not assert sufficient facts that, if proven, would entitle the plaintiff to relief."[43] "[T]he governing pleading standard in Delaware to survive a motion to dismiss is reasonable 'conceivability.'"[44] Thus, when considering a motion to dismiss,

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[40] *Id.* at 27.
[41] *Id.* at 22.
[42] Compl. ¶ 47.
[43] *In re Alloy, Inc. S'holder Litig.*, 2011 WL 4863716, at *6 (Del. Ch. Oct. 13, 2011).
[44] *Central Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings, LLC*, 27 A.3d 531, 537 (Del. 2011) (citation omitted).

> a trial court should accept all well-pleaded factual allegations in the Complaint as true, accept even vague allegations in the Complaint as "well-pleaded" if they provide the defendant notice of the claim, draw all reasonable inferences in favor of the plaintiff, and deny the motion unless the plaintiff could not recover under any reasonably conceivable set of circumstances susceptible of proof.[45]

"The court . . . need not 'accept conclusory allegations unsupported by specific facts or . . . draw unreasonable inferences in favor of the non-moving party,'"[46] but as long as there is a reasonable possibility that a plaintiff could recover, a motion to dismiss will be denied.[47]

A. *Cause of Action I*

Cause of Action I alleges that the members of the Control Group breached the fiduciary duties that they owed to American Surgical's minority stockholders. When a corporation with a controlling stockholder merges with an unaffiliated company, the minority stockholders of the controlled corporation are cashed-out, and the controlling stockholder receives a minority interest in the surviving company, the controlling stockholder does not "stand on both sides" of the merger.[48] Therefore, in that type of transaction, *Kahn v. Lynch Communication*

[45] *Id.* at 536 (citation omitted).
[46] *Alloy*, 2011 WL 4863716, at *6 (citing *Price v. E.I. duPont de Nemours & Co., Inc.*, 26 A.3d 162, 166 (Del. 2011)).
[47] *See id.* ("Delaware's reasonable 'conceivability' standard asks whether there is a 'possibility' of recovery.") (citing *Central Mortg.*, 27 A.3d at 537 n.13).
[48] *In re John Q. Hammons Hotels Inc. S'holder Litig.*, 2009 WL 3165613, at *10 (Del. Ch. Oct. 2, 2009).

Systems, Inc.[49] "does not mandate that the entire fairness standard of review apply notwithstanding any procedural protections that were used."[50]

> [I]t is nonetheless true that . . . [the controlling stockholder] and the minority stockholders . . . [are] in a sense "competing" for portions of the consideration . . . [that the unaffiliated company is] willing to pay to acquire . . . [the corporation] and that . . . [the controlling stockholder], as a result of his controlling position, could effectively veto any transaction. In such a case it is paramount-indeed, necessary in order to invoke business judgment review-that there be robust procedural protections in place to ensure that the minority stockholders have sufficient bargaining power and the ability to make an informed choice of whether to accept the third-party's offer for their shares.[51]

Specifically, "business judgment would be the applicable standard of review if the transaction were (1) recommended by a disinterested and independent special committee, *and* (2) approved by stockholders in a non-waivable vote of the majority of all the minority stockholders."[52] If a transaction is not conditioned on "robust procedural protections," "entire fairness is the appropriate standard of review."[53]

The Complaint sufficiently alleges that the Merger was a *Hammons*-type transaction. The Complaint pleads facts which suggest that the Control Group was American Surgical's controlling stockholder, that the Merger was a transaction between unaffiliated parties, and that the terms of the Merger granted the members

[49] 638 A.2d 1110 (Del. 1994).
[50] *Hammons*, 2009 WL 3165613, at *10.
[51] *Id.* at *12.
[52] *Id.*
[53] *Id.* at *13.

of the Control Group a minority interest in the surviving company while American Surgical's minority stockholders were cashed-out. Therefore, because the Merger was not conditioned on "robust procedural protections," the Merger will be reviewed for entire fairness.

1. The Control Group was American Surgical's Controlling Stockholder

> Although a controlling shareholder is often a single entity or actor, Delaware case law has recognized that a number of shareholders, each of whom individually cannot exert control over the corporation (either through majority ownership or significant voting power coupled with formidable managerial power), can collectively form a control group where those shareholders are connected in some legally significant way-e.g., by contract, common ownership, agreement, or other arrangement-to work together toward a shared goal.[54]

"If such a control group exists, it is accorded controlling shareholder status, and its members owe fiduciary duties to the minority shareholders of the corporation."[55]

Although there was no one person or entity that controlled American Surgical, the Complaint sufficiently alleges that Elgamal, Olmo-Rivas, Chapa, and Chamberlain, the members of the Control Group, were connected in a legally significant way. The Complaint alleges that the members of the Control Group, "as majority shareholders of the Company acting in concert, owed fiduciary duties

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[54] *Dubroff v. Wren Holdings, LLC*, 2009 WL 1478697, at *3 (Del. Ch. May 22, 2009) ("*Dubroff I*") (citing *In re PNB Holding Co. S'holders Litig.*, 2006 WL 2403999, at *9-10 (Del. Ch. Aug. 18, 2006); *Emerson Radio Corp. v. Int'l Jensen Inc.*, 1996 WL 483086, at *17 (Del. Ch. Aug. 20, 1996)).

[55] *Dubroff v. Wren Holdings, LLC*, 2011 WL 5137175, at *7 ("*Dubroff II*") (Del. Ch. Oct. 28, 2011) (citing *Dubroff I*, 2009 WL 1478697, at *3).

to the public shareholders of the Company . . . ."[56] Moreover, the Complaint outlines how all of the members of the Control Group contemporaneously entered into the Voting Agreements, the Exchange Agreements, and the Employment Agreements. Specifically, the Complaint describes that on December 20, 2010, each member of the Control Group (1) agreed to vote his shares of American Surgical common stock in favor of the Merger, (2) exchanged some of his American Surgical common stock for an interest in the post-Merger entity, and (3) accepted employment with the post-Merger entity. It can reasonably be inferred, from that conduct, that the members of the Control Group were acting as American Surgical's controlling stockholder. Therefore, for purposes of a motion to dismiss, the Control Group was American Surgical's controlling stockholder.[57]

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[56] Compl. ¶ 2.

[57] The Defendants argue that even if Elgamal and Olmo-Rivas are considered to be a control group, Chapa and Chamberlain should not be considered to be part of that group because "Elgamal and Olmo-Rivas certainly possessed a majority interest in American Surgical ***without Chapa and Chamberlain***." Defs.' Opening Br. at 28 (emphasis in original). A person is part of a control group when he is connected to the other members of the control group in some "legally significant way." Chapa and Chamberlain are alleged to have entered into Voting Agreements, Exchange Agreements, and Employment Agreements at the same time that Elgamal and Olmo-Rivas entered into those agreements. And the Complaint alleges that Elgamal, Olmo-Rivas, Chapa, and Chamberlain acted together to attain unique benefits for themselves at the expense of American Surgical's other stockholders. Thus, at this procedural stage, the Court will view Chapa and Chamberlain as members of the Control Group. If later in this litigation, Chapa and Chamberlain can show that they were not members of the Control Group, then they will obviously not be liable as controllers. Moreover, even if the Control Group only consisted of Elgamal and Olmo-Rivas, the Court's analysis, at this stage, would not change. Even if the Control Group only consisted of Elgamal and Olmo-Rivas, the Complaint would still allege that a control group agreed to enter into a transaction to benefit itself at the expense of American Surgical's minority stockholders.

2. American Surgical's Minority Stockholders were Cashed-Out in the Merger while the Control Group Retained an Interest in the Surviving Company

Although the Defendants try to distinguish this case from *Hammons* and *In re LNR Property Corp. Shareholders Litigation*,[58] the facts here are strikingly similar to the facts in each of those cases. In *Hammons*, a corporation with a controlling stockholder merged into an unaffiliated company, and the corporation's minority stockholders were cashed-out. The controlling stockholder, however, was not cashed-out. Rather, in return for his shares of the corporation's stock, the controlling stockholder received a 2% interest in the surviving company, as well as certain other benefits.[59] The Court, in *Hammons*, recognized that the unaffiliated purchaser "made an offer to the minority stockholders, who were represented by the disinterested and independent special committee,"[60] but the Court still determined that the merger would be subject to entire fairness review unless it was conditioned on "robust procedural protections."[61]

Similarly, in *LNR*, a corporation with a controlling stockholder merged with an unaffiliated company and the corporation's minority stockholders were cashed-

[58] 896 A.2d 169 (Del. Ch. 2005).
[59] 2009 WL 3165613, at *7.
[60] *Id.* at *10.
[61] *Id.* at *12. *See also Orman*, 794 A.2d at 19-22 (determining that a merger was entitled to the presumptions of the business judgment rule "[d]espite the fact that the Cullman Group possessed voting control over the Company both before and after the proposed transaction, [where] approval of the merger required that a majority of the Unaffiliated Shareholders of Class A stock, voting separately as a class, vote in favor of the transaction," and the merger was recommended by an active special committee with full bargaining power.) (citation omitted).

out. In connection with the merger, however, the controlling stockholder and other members of the corporation's management obtained an ownership stake in the surviving entity. The *LNR* Court, addressing a motion to dismiss, was required to accept the allegation in the complaint that the controlling stockholder sold a portion of his stockholdings "for a significant sum yet still retained the ability to participate in the Company's future profits and growth"[62] by acquiring a 20.4% interest in the surviving entity.[63] The Court determined that that allegation, "if true, could support a reasonable inference that . . . [the controlling stockholder] was sufficiently conflicted at the time he negotiated the sale that he would rationally agree to a lower sale price in order to secure a greater profit from his investment in . . . [the surviving entity]."[64] The Court further stated that "[i]f this is shown to be the case, the transaction will be subject to entire fairness review."[65]

This case, as in *Hammon*s and *LNR*, involves a corporation with a controlling stockholder that entered into a merger with an unaffiliated company, and in the Merger, the minority stockholders were cashed-out while the controlling stockholder retained the ability to participate in the corporation's future profits and growth. Although the Defendants correctly contend that there is no allegation in the Complaint that the Control Group negotiated the compensation that the

[62] *LNR*, 896 A.2d at 173.
[63] *Id.* at 172.
[64] *Id.* at 178.
[65] *Id.* (citations omitted).

minority stockholders received in the Merger, the Court in *Hammons* determined that even when an independent and disinterested special committee negotiates on behalf of the minority, a merger will still be subject to entire fairness review unless it is conditioned on "robust procedural protections."[66] Moreover, although the Defendants contend that the members of the Control Group were "net sellers" in the Merger,[67] the Court, in *LNR*, made clear that when a corporation's minority stockholders are being cashed-out in a transaction, and the corporation's controlling stockholder will have a continued interest in the surviving entity, it is reasonable to infer that the controlling stockholder might "agree to a lower sale price in order to secure a greater profit from his investment in . . . [the surviving entity]."[68] As Frank states:

> It is certainly plausible to conclude from the Complaint's allegations that the . . . [members of the Control Group] were motivated to obtain a substantial amount of cash from the deal but at the same time retain a sizable interest in the surviving Company, which they undoubtedly hoped would, with the help of a private equity firm, continue its planned expansion to become a "nationwide leader in the surgical assistant sector" that the Company strived for in its business plan.[69]

In short, the Merger is analogous to the transactions at issue in *Hammons* and *LNR*, and thus, the Merger is subject to entire fairness review unless it was conditioned on "robust procedural protections."

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[66] *Hammons*, 2009 WL 3165613, at *12.
[67] *See* Defs.' Opening Br. at 16.
[68] *LNR*, 896 A.2d at 178.
[69] Pl.'s Answering Br. at 24.

3. The Merger was not Conditioned on Robust Procedural Protections

The Merger was not conditioned on a non-waivable vote of the majority of all the minority stockholders. Rather, the Merger Agreement provides that "[t]he affirmative vote of the holders of a majority of the outstanding Common Shares on the record date for the Company Meeting is the only vote of holders of securities of the Company which is required to approve and adopt this Agreement . . . [and] the Merger . . . ."[70] Moreover, the Defendants do not argue that the Merger was conditioned on some other shareholder-protective mechanism that would satisfy *Hammons*.[71] Thus, the Merger is subject to entire fairness review.

"[W]hen the entire fairness standard applies, controlling stockholders can never escape entire fairness review, but they may shift the burden of persuasion . . . ."[72] The one way that the Control Group could shift the burden of persuasion is by showing "that the transaction was approved . . . by an independent board majority (or in the alternative, a special committee of independent

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[70] Compl. ¶ 43.

[71] The Defendants do argue that a majority of American Surgical's minority stockholders voted to approve the Merger. Defs.' Reply Br. at 20-22. A majority of the minority vote, however, only serves as a robust procedural protection when it is a non-waivable pre-condition to a transaction. Only when a transaction is conditioned on a vote of the majority of all minority stockholders will the minority stockholders know that they have real power. The fact that a majority of American Surgical's minority stockholders eventually voted to approve the Merger is not a robust procedural protection; it is something that occurred after the Merger was a foregone conclusion. The one actual procedural protection that the Defendants point to is the Special Committee, and under *Hammons*, that is not enough to invoke the presumptions of the business judgment rule in this setting.

[72] *In re Southern Peru Copper Corp. S'holder Deriv. Litig.*, 2011 WL 6440761, at *20 (Del. Ch. Oct. 14, 2011, revised Dec. 20, 2011) (citation omitted).

directors)."[73] The Defendants claim that the Merger was approved by both an independent majority of the Board, and the Special Committee, which, they argue, was composed of independent and disinterested directors. The Defendants might be correct as to one or both of those claims, but a motion to dismiss is not the proper vehicle for deciding whether the burden of proof under entire fairness should be shifted.[74] The Merger will be reviewed for entire fairness, and therefore, the Defendants' motion to dismiss Cause of Action I is denied.[75]

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[73] *Id.*

[74] *See Orman*, 794 A.2d at 20 n.36 ("Once the business judgment rule presumption is rebutted, the burden of proof shifts to the defendant, who must either establish the entire fairness of the transaction or show that the burden of disproving its entire fairness must be shifted to the plaintiff. A determination of whether the defendant has met that burden will normally be impossible by examining only the documents the Court is free to consider on a motion to dismiss—the complaint and any documents it incorporates by reference.").

[75] The Court is aware that purchasers of companies, especially private equity funds, often condition a transaction on the continued employment of critical members of management. Moreover, purchasers will sometimes structure a transaction so that the managers who continue with the company receive an equity stake in the company. Presumably, transactions are structured in this way so that the managers have "skin in the game." Moreover, this Court has suggested that, at least in some circumstances, it is permissible to structure transactions in this way. *See In re OPENLANE, Inc. S'holders Litig.*, 2011 WL 4599662, at *5 (Del. Ch. Sept. 30, 2011) ("A competent executive who will stay on after the transaction may be viewed as value-adding by an acquirer."); *Wayne County Employees' Ret. Sys. v. Corti*, 2009 WL 2219260, at *11 (Del. Ch. July 24, 2009) ("That Kotick and Kelly did not have to pursue the transaction with Vivendi in order to retain their positions as managers significantly alleviates the concern that Kotick and Kelly were acting out of an impermissible 'entrenchment' motive.'"). The problem of applying that reasoning to this case is that when the managers who are being given an on-going interest in the company are also members of the company's control group, it is reasonable for the Court to infer not only that the purchaser wants the managers to have "skin in the game," but that the managers/control group members are using their control to acquire a unique benefit for themselves at the expense of the minority stockholders.

Delaware's corporate law is primarily process-based—"the foundational principle of Delaware corporate law [is] that the directors, and not the court, properly manage the corporation." *Corti*, 2009 WL 2219260, at *15. *Hammons* clearly laid out a process—when a corporation with a controlling stockholder merges with an unaffiliated company, the minority stockholders of the controlled corporation are cashed-out, and the controlling stockholder receives a minority

B. *Cause of Action II*

Cause of Action II alleges that the members of the Control Group were unjustly enriched as a result of the Merger. In order to plead a claim for unjust enrichment, Frank must allege "(1) an enrichment, (2) an impoverishment, (3) a relation between the enrichment and impoverishment, (4) the absence of justification, and (5) the absence of a remedy provided by law."[76] With regard to an enrichment, the Complaint alleges that the Merger allowed the members of the Control Group "to continue to benefit from the Company's ongoing success,"[77] and that the Merger increased the likelihood of that success—the Company is now being run by, Great Point, a sophisticated market participant.[78] With regard to an impoverishment, the Complaint alleges that American Surgical's minority shareholders are not able to participate in the Company's ongoing success because they were cashed-out, at an unfairly low price, in the Merger.[79] Thus, the Control Group's alleged enrichment and the minority shareholders alleged impoverishment are related—the Merger allegedly both cashed out the minority shareholders at an unfair price, and gave Great Point control of American Surgical. Finally, the

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interest in the surviving company, the merger will be subject to entire fairness review unless there are robust procedural protections in place. The Merger Agreement did not contain robust procedural protections. Thus, it is subject to entire fairness review.

[76] *Dubroff II*, 2011 WL 5137175, at *11 (quoting *Latesco, L.P. v. Wayport, Inc.*, 2009 WL 2246793, at *9 n.33 (Del. Ch. July 24, 2009)) (internal quotations omitted).

[77] Compl. ¶ 78.

[78] *Id.* at ¶ 67.

[79] *Id.* at ¶¶ 2, 67.

Complaint alleges that the Control Group's actions in connection with the Merger constituted a breach of fiduciary duty. Actions that constitute a breach of fiduciary duty are remedied in equity, and, at least for purposes of a motion to dismiss, unjustified. Therefore, Frank has adequately pled a claim for unjust enrichment.[80]

Frank's claim for unjust enrichment in Cause of Action II appears, at least to some extent, to be duplicative of his claim for breach of fiduciary duty in Cause of Action I. Delaware law, however, appears to permit a plaintiff to simultaneously assert two equitable claims even if they overlap.[81] A plaintiff will only receive, at most, one recovery,[82] but, at least at this procedural juncture, Frank may simultaneously assert a claim for breach of fiduciary duty and a claim for unjust enrichment against the members of the Control Group. Thus, the Defendants' motion to dismiss Cause of Action II is denied.

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[80] The Defendants' argument that Frank's unjust enrichment claim is based on a flawed interpretation of HFBE's fairness opinion is a factual argument. Therefore, even assuming that the argument is accurate, it would not be a proper basis upon which to grant a motion to dismiss.

[81] S*ee MCG Capital Corp. v. Maginn,* 2010 WL 1782271, at *25 n.147 (Del. Ch. May 5, 2010) ("In this case, then, for all practical purposes, the claims for breach of fiduciary duty and unjust enrichment are redundant. One can imagine, however, factual circumstances in which the proofs for a breach of fiduciary duty claim and an unjust enrichment claim are not identical, so there is no bar to bringing both claims against a director.").

[82] *Id.* ("If MCG is able to prove Maginn breached his duty of loyalty in Count Five then it will also be successful in proving unjust enrichment in Count Six. Both claims hinge on whether Maginn was disloyal to Jenzabar by the manner in which he procured the 2002 Bonus. Of course, in the event MCG makes its case on both claims, Jenzabar will only be entitled to one recovery; return of the 2002 Bonus plus interest.").

C. *Cause of Action III*

Cause of Action III alleges that the members of the Board, as well as Chamberlain and Chapa, have breached their fiduciary duty to ensure that the Merger was fair to American Surgical's minority shareholders, as well as their duty to ensure that the Company's shareholders were provided with all material information relevant to the decision of whether to seek appraisal. Because, as discussed above in Section IV.A, the members of the Control Group have, at this stage, the burden of proving that the Merger was entirely fair, the claims asserted against them in Cause of Action III survive. Moreover, Frank has adequately alleged that Toh was interested in the Merger because he received a $250,000 fee for his role in the transaction.[83] The Defendants may ultimately be correct that Toh earned that fee, and that it was not material to him, but, at this point, the Court can reasonably infer that Toh was interested in the Merger.

As for Bailey and Kleinman, Frank has alleged that they were not independent because they are surgeons who worked at hospitals that have a contractual relationship with one of American Surgical's subsidiaries. That allegation is insufficient as a matter of law to suggest that Bailey and Kleinman were not independent. Thus, if Bailey and Kleinman breached any duty, it was

[83] *See Orman*, 794 A.2d at 30 ("Even though there is no bright-line dollar amount at which consulting fees received by a director become material, at the motion to dismiss stage and on the facts before me, I think it is reasonable to infer that $75,000 would be material to director Bernbach . . . .").

likely their duty of care. The Defendants contend that American Surgical has adopted an exculpatory provision pursuant to 8 *Del. C.* §102(b)(7), and thus, that Bailey and Kleinman cannot be held monetarily liable for any breach of their duty of care. The Defendants recognize, however, that this is not the time to address the effect of a §102(b)(7) exculpatory provision—"[i]f . . . entire fairness does, or may, apply here, then Defendants are content to have the §102(b)(7) defense decided at trial or further summary disposition."[84] Thus, the Defendants' motion to dismiss Cause of Action III is denied.

D. *Cause of Action IV*

Cause of Action IV alleges that the Purchasing Entities aided and abetted the breaches of fiduciary duty committed by the members of the Control Group and the Board. To state a claim that the Purchasing Entities aided and abetted a breach of fiduciary duty, Frank must plead "'(1) the existence of a fiduciary relationship, (2) a breach of the fiduciary's duty, . . . (3) knowing participation in that breach by the . . . [Purchasing Entities],' and (4) damages proximately caused by the

[84] Defs.' Reply Br. at 24. *See also LNR*, 896 A.2d at 178 ("While the independent director defendants may ultimately be able to rely upon the Section 102(b)(7) charter provision, it is premature to dismiss the claims against them on this basis. First, the entire fairness standard of review may be applicable, and, thus, 'the inherently interested nature of those transactions [may be] inextricably intertwined with issues of loyalty.'") (quoting *Emerald Partners v. Berlin*, 787 A.2d 85, 93 (Del. 2001)).

breach."[85] With regard to the requirement of "knowing participation," the Supreme Court has held:

> Knowing participation in a board's fiduciary breach requires that the third party act with the knowledge that the conduct advocated or assisted constitutes such a breach. Under this standard, a bidder's attempts to reduce the sale price through arm's-length negotiations cannot give rise to liability for aiding and abetting, whereas a bidder may be liable to the target's stockholders if the bidder attempts to create or exploit conflicts of interest in the board. Similarly, a bidder may be liable to a target's stockholders for aiding and abetting a fiduciary breach by the target's board where the bidder and the board conspire in or agree to the fiduciary breach.[86]

The Complaint makes two arguments in support of its claim that the Purchasing Entities aided and abetted breaches of fiduciary duty. First, the Purchasing Entities were "intimately involved in the negotiations and structuring of the . . . [Merger] and understood that the . . . [Control Group] and the minority shareholders were competing for the consideration that . . . [the Purchasing Entities] would pay to acquire American Surgical."[87] Second, the Purchasing Entities "demanded deal protection measures, including an excessive termination fee, matching rights, and a no-shop clause while enticing American Surgical's management to enter into a deal with them through equity offerings . . . and lucrative salaries and bonuses . . . ."[88] Neither of those arguments, however,

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[85] *Malpiede v. Townson*, 780 A.2d 1075, 1096 (Del. 2001) (quoting *Penn Mart Realty Co. v. Becker*, 298 A.2d 349, 351 (Del. Ch. 1972) (other citations omitted)).
[86] *Id.* at 1097-98 (citations omitted).
[87] Compl. ¶ 89.
[88] *Id.* at ¶ 90.

suggests that the Merger was anything other than an arm's-length transaction. With regard to the first argument, the Defendants are correct that it "is a tautology: no acquirer can ever complete an acquisition without being involved in the negotiations."[89] Moreover, although the first argument suggests that the Purchasing Entities knew that the Control Group and the minority shareholders were competing for consideration, it does not suggest that the Purchasing Entities attempted to exploit that competition. With regard to the second argument, nearly every third-party bidder seeks deal protection devices, and the fact that the Purchasing Entities were able to get American Surgical to agree to a few does not suggest anything other than that the parties were bargaining at arm's-length. Therefore, the Defendants' motion to dismiss Cause of Action IV is granted.[90]

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[89] Defs.' Reply Br. at 26.

[90] The aiding and abetting claim here is distinguishable from the aiding and abetting claim in *Hammons*. In *Hammons*, the Court explained that the plaintiffs had alleged that the purchaser knew that the target company's shares were trading at a discount because the company's controlling stockholder had engaged in improper self-dealing. Nevertheless, the purchaser allegedly relied on the company's stock price. 2009 WL 3165613, at *18. The *Hammons* Court stressed "that . . . [the controlling stockholder] and the minority stockholders were in a sense 'competing' for the consideration . . . [the purchaser] would pay . . . ," and thus, the Court held that "plaintiffs could prevail at trial on the issue of fair dealing." *Id.* As stated above, here, unlike in *Hammons*, there is no allegation that the Purchasing Entities attempted to exploit the competition between the Control Group and American Surgical's minority stockholders. The Complaint alleges that the Defendants timed the Merger "to take advantage of a recent unexplained decline in the market price of American Surgical's stock," Compl. ¶ 57, but without an allegation that Great Point knew that the stock price was depressed for an improper reason, the fact that Great Point sought to consummate the Merger when American Surgical's stock price was low merely suggests that it was a savvy buyer. Thus, Frank's aiding and abetting claim against the Purchasing Entities fails as a matter of law.

V. CONCLUSION

For the foregoing reasons, the Defendants' motion to dismiss is granted as to Cause of Action IV, but denied as to Causes of Action I, II, and III. An implementing order will be entered.