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Colorado Federal Judge Rejects Plaintiffs' Claim for Separate Class Vote on Merger, Rules that Inadequate Price Does Not Constitute Breach of Duty

In a recent opinion with important implications for Maryland companies, a United States District Judge for the District of Colorado granted summary judgment to a Maryland real estate investment trust and other defendants in a suit filed by former minority unitholders claiming that the conversion of their units into a new series of units in connection with a merger constituted a breach of contract and a breach of duty.

The case, *Stender v. Archstone-Smith Operating Trust*, arose out of the 2007 acquisition of Archstone-Smith Trust, a Maryland real estate investment trust ("Archstone"), and its related operating trust, Archstone-Smith Operating Trust, also a Maryland real estate investment trust (the "Operating Trust"), by Tishman Speyer Development Corp. and Lehman Brothers Holdings Inc. In the transaction, a new limited liability company formed by the acquirers was merged with and into the Operating Trust and the Class A-1 Units of the Operating Trust were converted into the right to receive, at the unitholders' election, either $60.75 in cash or a new Series O Unit for each Class A-1 Unit outstanding. Following the merger of the Operating Trust, Archstone was merged into a new real estate investment trust formed by the acquirers, with the holders of Archstone's common shares receiving $60.75 per share in cash. In between the two mergers, the Declaration of Trust of the Operating Trust was amended to reflect that there were no longer any Class A-1 Units outstanding and that Archstone's successor in the second merger would not be publicly traded.

The Declaration of Trust of the Operating Trust provided that Archstone, as trustee of the Operating Trust, could cause the merger of the Operating Trust with or into another entity if the merger was (a) in connection with a termination transaction in which the unitholders of the Operating Trust received, or had the right to elect to receive, the same per share consideration offered to the common shareholders of Archstone and (b) approved by the holders of a majority of the then outstanding units entitled to vote thereon (including any Class A-2 Units held by the trustee). As the holder of approximately 89% of the combined Class A-1 and Class A-2 Units, Archstone approved the merger of the Operating Trust without the vote of any holders of Class A-1 Units.

Unhappy with the choice of cash, which triggered adverse tax consequences, or Series O Units, which had different economic rights than the Class A-1 Units, certain former holders of Class A-1 Units filed suit against Archstone, the Operating Trust, the individual trustees of Archstone and several other parties alleging that the merger of the Operating Trust violated certain provisions of the Declaration of Trust of the Operating Trust granting the holders of Class A-1 Units a separate class vote on the amendment of specified sections of the Declaration and requiring individual unitholder approval for certain amendments adverse to the particular unitholder. The complaint further alleged that Archstone breached its duty to the holders of Class A-1 Units when it negotiated and approved the merger of the Operating Trust and that the individual trustees of Archstone aided and abetted this breach.

In its opinion, after indicating that "[t]he A-1 units were, functionally speaking, a form of preferred stock [which] brought preferential distribution rights but also limited control over corporate governance," the Court flatly rejected the plaintiffs' argument that the conversion of Class A-1 Units into Series O Units in the merger of the Operating Trust should be viewed as an amendment of the Declaration of Trust of the Operating Trust subject to the class vote and individual unitholder approval requirements contained therein. The Court stated: "Plaintiffs' position on that is clear, but it does not become correct by frequent repetition. The A-1 units were never amended. They were terminated, as Maryland law permitted in the context of a merger." Regarding the plaintiffs' attempt to support their argument by pointing to the post-merger amendments to the Declaration of Trust of the Operating Trust, the Court simply noted that these amendments occurred about 30 minutes after the Class A-1 Units had been eliminated in the merger.

The Court's decision on the plaintiffs' breach of contract claim was consistent with the holding in *Warner Communications, Inc. v. Chris-Craft Industries, Inc.*, the seminal Delaware case on preferred stock voting rights. In that case, the Delaware Court of Chancery determined that a charter provision granting preferred stockholders the right to vote on adverse amendments did not apply to a merger in which the preferred stock was converted into a new security, as it was the conversion that created the adverse effect and the conversion did not depend to any extent upon a charter amendment. (For more discussion in this regard, see James J. Hanks, Jr. and Christopher W. Pate, "Preferred Stock Voting Rights: Toward Greater Certainty," *Insights* (September 2004).)

In rejecting the plaintiffs' breach of duty claim, the Court noted that ownership of stock of a Maryland company entails the possibility of termination of ownership by merger, twice citing an older Maryland case, *American General Corp. v. Camp*, and that the plaintiffs failed to point to anything in the Declaration of Trust of the Operating Trust "creating expectations that differ from those which otherwise exist as a matter of law." (The Court also held that the words "with or into," when used in connection with a merger, include both a forward and a reverse merger.)

The Court further held that "to the extent Plaintiffs' claim reduces to simple dissatisfaction with the negotiated per-share compensation . . . , there is no fiduciary duty claim when 'the plaintiffs' fundamental grievance [is] one of inadequate price.'" Although not mentioned by the Court when it erroneously repeated the plaintiffs' characterization of trustee duties as "fiduciary" under Maryland law, this result is reinforced by (a) the statutory standard of conduct now applicable to trustees of a Maryland real estate investment trust, which requires each trustee to act in good faith, in a manner reasonably believed to be in the best interests of the trust (not individual shareholders or groups of shareholders) and with the care of an ordinarily prudent person in a like position under similar circumstances, and (b) the statutory presumption (which applied even in 2007 during the events in question) that an act of a trustee satisfies the statutory standard of conduct.

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As always, our colleagues and we are available at any time to discuss these or other matters of Maryland law.

Jim Hanks
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