UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

U.S. BANK NATIONAL ASSOCIATION, Litigation Trustee of the Idearc Inc. et al. Litigation Trust,	§	
Plaintiff,	§	
v.	§	CIVIL ACTION NO. 3:10-CV-1842-G
VERIZON COMMUNICATIONS INC., et al.,	§	
Defendants.	§	

MOTION AND BRIEF FOR ENTRY OF JUDGMENT ON ADMISSIONS AND STIPULATED FACTS

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as Litigation Trustee on Behalf of the
Idearc Inc. et al. Litigation Trust

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

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Comes now the Plaintiff, and pursuant to Rules 52 and 56, FED. R. CIV. P., prays that this Court enter judgment against Defendant Verizon Communications, Inc. ("Verizon") for Promoter Liability and Breach of Fiduciary Duty (Count 9) and Alter Ego (Count 11). In the alternative, Plaintiff prays for judgment against Defendants Verizon and Diercksen under Count 8 (Unlawful Dividend under Delaware Code §§ 170, 173, 174).

I. PREFACE

Plaintiff makes this Motion preserving its objections to the order of separate trial and the Court's decision not to empanel a jury. Since this motion rests on stipulated facts, admissions and other matters not genuinely in dispute, Plaintiff believes the Court may enter judgment for Plaintiff as a matter of law without making any additional findings of fact. If the Court cannot grant the full relief requested herein as a matter of law, Plaintiff again requests a trial before a jury as to all claims not resolved. If the Court will not empanel a jury, Plaintiff requests that all

of the remaining claims and issues in this civil action be tried to the Court at the earliest possible date convenient with the Court.

Rule 52(c), FED. R. CIV. P. permits a court to enter judgment after a partial trial if the court finds against a party on that issue. Our case is unique. Here, the Court did not set a claim or defense for trial. Nor did the Court set for trial any ultimate issue of fact that would prove dispositive of a claim or defense. The Court found that Idearc was worth more than $12 billion on November 17. This finding cannot be seen as clearly "for" or "against" any claim or defense. It helps the Defendants defend Plaintiff's claim for constructive fraudulent transfer, but the finding is not inconsistent with Plaintiff's contention that Verizon was the alter ego of Idearc. If Idearc was the alter ego of Verizon, then clearly Idearc was worth far more than $12 billion on November 17. Recognizing that Rule 52(c) may not perfectly fit, the Plaintiff prays the Court also treat this as a motion for summary judgment under Rule 56.

During the separate trial conducted to the bench, Plaintiff introduced into evidence PX 2018, a stipulation as to the contents of Idearc's minute book. The Court makes no mention of the exhibit or the contents of the minute book in its Memorandum of Decision (ECF 647), but a "finding" is not needed. This is because a stipulation of fact is binding on the Court. *Safeco Ins. Co. of America v. Rehabilitation Specialists*, 20 F.3d 1170, 1194 WL 144778 at *5 (5th Cir. 1994), *cert. denied*, 513 U.S. 929 (1994). This stipulation has been filed with the Clerk of the Court in compliance with Rule 11 of the TEXAS RULES OF CIVIL PROCEDURE. (ECF 633) *See*, *Safeco*, 1994 WL 144778 at *5.

The official minute book reveals the following:

1. The bylaws require a two person board and nothing less may constitute a quorum. Ex. A-2 (PX 2018), App. at 28 (citations to "App. __" are to Plaintiff's Appendix to Motion and Brief for Entry of Judgment on

Admissions and Stipulated Facts, which Plaintiff filed contemporaneously with this brief).

2. The incorporator appointed Defendant John Diercksen as a director on June 20, 2006. Ex. A-2 (PX 2018), App. at 47. There is no evidence in the minute book that the incorporator appointed a second director.

3. The bylaws provide that the board elects all officers, including the president. Ex. A-2 (PX 2018), App. at 33-34.

4. The bylaws forbid any corporate indebtedness unless authorized by the board of directors or the president. Ex. A-2 (PX 2018), App. at 43.

5. The minute book reveals a resolution by John Diercksen as a sole director purporting to authorize the issuance of one share of VDDC stock to Verizon, but this resolution does not set a price for the stock. Ex. A-2 (PX 2018), App. at 48.

6. There is no evidence of a sale of Idearc or VDDC securities to Verizon.

7. There is no evidence that Diercksen revalued the assets before purporting to declare a dividend on October 31, 2006.

The admissions by Defendants state no portion of what was received by Verizon on the spin date constitutes sales proceeds. For ease of reference the admissions and the stipulation appear in the Appendix at A-1 and A-2, respectively. Substantially all references to the evidence herein tie to testimony and exhibits adduced at trial. In some instances, Plaintiff refers to evidence not offered at trial. This evidence is reproduced in the Appendix. Plaintiff believes there is no issue of fact as to the genuineness of the attached evidence.

II. ISSUES OF LAW

1. Under Section 107 of the Delaware Code, what are the duties and limitations on the promoter after the charter is filed but before corporate formation is "perfected" through the appointment of a board?

2. Prior to the appointment of the board, may the promoter appoint officers?

3. Prior to the appointment of the board, may the promoter issue stock to itself or others?

4. What is the liability of a promoter on corporate contracts entered into after the articles are filed but before corporate formation is perfected through the appointment of a board?

5. Is it legally possible for a Delaware corporation to ratify or adopt the promoter's contracts if corporate formation is never "perfected?"

a. Was Diercksen or the New Board a *de facto* board under Delaware law?

b. Was Verizon an equitable shareholder under Delaware law?

6. Putting aside all issues concerning the formation of Idearc and the issuance of stock, was Defendant Diercksen required as a matter of law to revalue assets before declaring a dividend?

7. Was Diercksen able to declare a dividend even though there was no board approval?

III. STATEMENT OF FACTS

The Court is generally aware of the facts and the contentions of the parties. No lengthy recitation is needed here.

Verizon engaged Debevoise & Plimpton, LLP ("Debevoise") to form VDDC, a/k/a Idearc. The legal existence of Idearc commenced when Debevoise associate Greg Feldman, the incorporator, filed the Articles of Incorporation on June 20, 2006. Mr. Feldman also adopted original bylaws. The bylaws set a two person board. A quorum required two board members. Mr. Feldman appointed Defendant Diercksen as one of two directors. Mr. Feldman never appointed a second board member.

Verizon directed Defendant Diercksen to appoint Kathy Harless as the putative[1] President of Idearc. Defendant Diercksen did so without a quorum. Without a quorum, Defendant Diercksen purported to authorize Ms. Harless to sell Verizon one share of stock. The resolution he signed established no price for the stock. Ex. A-2 (PX 2018), App. at 48. Thereafter, and again without a quorum, Diercksen appointed Mr. Coticchio as putative CFO and Mr. Mundy, the putative Secretary of Idearc. Ex. A-2 (PX 2018), App. at 49.

Without a quorum, on October 31, Diercksen, at Verizon's direction, signed a resolution purporting to authorize the spin. PX 893. On November 13, Verizon caused Mr. Coticchio, to sign the Distribution Agreement as a putative officer of Idearc, purporting to obligate Idearc to borrow over $9 billion and transfer cash, debt and shares of Idearc stock to Verizon. PX 985. Those shares were to be passed down to Verizon's shareholders.

For the spin to close on November 17, the lawyers had to furnish opinion letters, including letters attesting to the lawful issuance of shares. In particular, the NYSE needed an opinion from a lawyer that the millions of Idearc shares to be passed to Verizon shareholders were lawfully authorized and issued. Computershare, the stock transfer agent, needed a similar opinion. Initially both Fulbright and Debevoise were to provide those opinions. *See, e.g.*, Fulbright's draft opinion letter, *see* Ex. A-3 (FJ0097588-90), App. at 103-106.

Fulbright's due diligence for the opinion letters began on or about November 8, 2006, with the spin set for just nine days later. *See* Ex. A-4 (FJ0043378, Grossman e-mail to Agrons dated November 8, 2006), App. at 107. Debevoise was the keeper of the Idearc minute book and the corporate records. On November 13, Fulbright's Seth Wexler expressed frustration over his inability to locate the minute book. It appeared the minute book of Idearc was not in Texas

[1] Plaintiff uses the term "putative" to denote that which is supposed or alleged, as distinguished from an actual, lawful or *de jure* officer.

where Idearc was located. *See* Ex. A-5 (FJ0005143), App. at 108; A-19, App. at 387-89. He pressed Debevoise lawyers Mr. Dix and Mr. Wickland for the rest of the corporate records. Ex. A-19, App. at 387-89; Ex. A-18, App. at 384-86. On November 13 or 14, Mr. Wexler emailed the Fulbright team that he did not see why Fulbright's opinions were needed because it would duplicate the opinion being given by Debevoise. Ex. A-17, App. at 377; Ex. A-7, App. at 350. Finally, on or just before November 15, 2006, Mr. Dix sent the minute book, such as it was, including the original charter, original bylaws, and resolutions that, if read and understood, would have revealed that the board was never fully constituted and that no stock had ever been authorized or issued. *See* Ex. A-6 (FJ0004130), App. at 109. Fulbright ultimately decided not to furnish opinions concerning stock issuance. On November 17, Debevoise furnished an opinion to the NYSE that all Idearc stock would be lawfully issued. PX 1092. Debevoise also gave comfort to the stock transfer agent. Ex. A-8, App. at 357.

In an effort to fix the corporate books before the closing in New York, resolutions appointing officers were created. Ex. A-9 (FJ 39661-39663), App. at 358-60. Stock certificates were created in favor of Verizon—one by VDDC and one by Idearc. Both were backdated. *See, generally,* PX 1944[2] and Ex. A-16, App. at 376. Harless and Mundy signed the VDDC stock certificates, presumably as putative officers of VDDC. *See* PX 428.

Diercksen resigned his directorship of Idearc just before the spin, but before then he purported to appoint successor board members selected by Verizon. Again, Diercksen acted without a quorum.[3]

[2] Ex. 1944 was excluded at trial on objection that it did not relate to Phase One. There is no objection as to authenticity.

[3] Plaintiff shall refer to these appointees as the "New Board" even though they were not lawfully appointed.

Verizon asked the New Board to ratify Diercksen's conduct as a director of Idearc. They refused. PX 953. Later they purported to ratify the authority of Idearc's putative officers to sign the spin documents. Without reaching the question of whether the New Board was ever lawfully appointed, this Court ruled as a matter of law that the ratification was ineffective. Aug. 8, 2012 Memorandum Opinion and Order [ECF no. 485] at 8.

After the spin, Verizon learned in 2007 that Kathy Harless was at war with the putative CFO over the books and accounting for Idearc. Information was being concealed from the New Board. Diercksen had seen this movie before. *See* PX 1313. Verizon did nothing with the information. Mr. Coticchio left his putative position with Idearc shortly thereafter in 2007. *See* Tr. Vol. 5B, 14:24-15:13. Ms. Harless stayed on until Valentine's Day, 2008. *See* Tr. Vol. 5B, 16:16-22. Throughout that time the New Board made five quarterly transfers of cash of $50 million, for a total of $250 million. *See* Ex. A-10 (March 2009 Idearc Form 10-K at 45), App at 362; Tr. Vol. 5B 13:6-14. These transfers were called "dividends" and paid to putative shareholders of Idearc.

Later, Reed, a member of the New Board, approached Verizon for help to stave off bankruptcy. *See* Ex. A-11, App. at 363; Ex. A-12, App. at 364. In particular, he needed Verizon's help on the Tax Sharing Agreement to refinance the debt. *See* Ex. A-11, App. at 363; Ex. A-12, App. at 364. Verizon refused and let Idearc file bankruptcy ignorant that the debt was Veizon's obligation.

IV. SUMMARY OF ARGUMENT

Verizon was a promoter. A promoter is a fiduciary. That fiduciary duty continues until such time as an independent board is established.

Verizon directed its agent, Greg Feldman, to act as incorporator. Mr. Feldman filed articles but these articles did not identify any board members. Where the articles of incorporation fail to identify the initial board of directors, the incorporator must nominate a board to completely form or "perfect" corporate formation within the meaning of Section 107 of the Delaware Code. Mr. Feldman appointed Diercksen, but he ever appointed a second board member.

Without a second board member, it was impossible for Idearc's board to function because there was no quorum. A corporation has legal existence once the articles are filed, but it does not have the ability to think, understand, or act until it has a board. It cannot appoint officers, issue stock or make contracts. Mr. Feldman is presumed under the law to have read and understood what he signed. Since Mr. Feldman acted as Verizon's agent, his knowledge is imputed as a matter of law to Verizon. *Garcia v. City of New York*, 951 N.Y.S.2d 2, 3 n. 1 (N.Y. App. 2012).

Where the initial board is not identified in the articles, an incorporator has very limited power to manage the affairs of the corporation before the board is appointed. For example, the law allows the incorporator to adopt the original bylaws. The promoter/incorporator may also arrange financing. The promoter/incorporator cannot start the business. *Kenyon v. Holbrook Microfilming Svc., Inc.*, 155 F.2d 913 (2nd Cir. 1946). Delaware law does not permit promoters/incorporators to supplant the board by appointing officers, issuing stock or making contracts. Were the law otherwise the corporate form would be a total sham. The promoter could simply issue himself stock, appoint putative officers to sign and deliver the stock to him, and generally conduct the business of the corporation without ever giving the corporation a brain. Since promoters have a fiduciary duty to the corporation until an independent board is in

place, *a fortiori* the promoter must at a minimum fully constitute a board rather than simply conduct the affairs of the business as though he, the promoter, were the board.

No officer or agent of Verizon could manage Idearc's affairs, not even Verizon's officer, Defendant Diercksen. Diercksen was not the "board." He was simply one member, and a board member has no power to conduct corporate business other than as part of some board action. 2 WILLIAM MEADE FLETCHER, *Fletcher Cyclopedia of the Law of Corporations* § 392 (2012). He could not lawfully sign resolutions, issue stock, or elect officers. He had no power to amend the original bylaws adopted by the incorporator.

As both a practical and legal matter, Diercksen functioned as the arm of Verizon; not as a voting member of a board. His name may appear on resolutions electing putative officers of Idearc, but Seidenberg, Verizon's CEO, not Diercksen, made all the decisions. *See* Tr. Vol. 6A 36:19-37:1. Even the resolutions signed by Diercksen as "sole director" were served up by the promoter's in-house counsel staff for signature. Ex. A-15, App. at 370-75. In short, the promoter through its officers, employees and agents managed the affairs of the company without a board in place in clear violation of well settled corporate law.

Verizon has tried in this case to rewrite Delaware law by arguing it was not a promoter—it was a shareholder—the sole shareholder, and as such waived all corporate irregularities. Verizon was never a legal or equitable shareholder of Idearc. Only boards can issue shares of stock or appoint officers to sign them, and there was never a board. Even if Verizon could stand well-established law on its head, the putative board resolution signed by Diercksen authorizing Kathy Harless to sell a share of VDDC stock to Verizon did not set a price for the stock as the law requires.

In fact, no shares of Idearc were ever issued to anyone. Verizon's theory of stock ownership is that it purchased stock in VDDC, and then exchanged one share of VDDC for one share of Idearc stock. That one share of Idearc stock was then supposedly exchanged or cancelled for the millions of Idearc shares passed to Verizon shareholders on the date of the spin. Since there was never a board, there could be never be any lawful issuance of shares to anyone. Debevoise may choose to write opinion letters at its peril to the NYSE that shares were lawfully issued, but saying so does not make it so.

Money or assets distributed to a promoter who issued himself a stock certificate cannot possibly be a lawful dividend. Verizon arranged to have itself named in a stock certificate before the dividend was paid at closing, but that simply does not work. If a promoter cannot appoint officers or declare dividends, it certainly cannot benefit from fake officers and fake stock certificates. There was no corporate resolution by Idearc authorizing disbursement of funds or the creation of debt. Verizon breached its fiduciary duty in issuing itself stock and in receiving an illegal "dividend" or unauthorized distribution and is liable in damages for the amount it received.

Verizon may argue to no avail that what it conveyed to Idearc exceeded what it received. Verizon's remedy, if any, is a claim in the bankruptcy court in *quantum meruit* as an unsecured creditor. A fiduciary may not use an alleged benefit bestowed to his beneficiary to set-off his liability for breach of trust. *See, e.g., Western Dealer Mgmt., Inc. v. England*, 473 F.2d 262, 265 (9th Cir. 1973), *cert. denied*, 412 U.S. 919 (1973).

Verizon also breached its duty by allowing the New Board to pay illegal and unauthorized "dividends" of $250 million between the date of the spin and the bankruptcy. Only *de jure* boards may authorize dividends, and the New Board was not a *de jure* board. Only

shareholders may receive dividends. The beneficiaries of the New Board's generosity were not shareholders. Verizon's duty to empanel a lawful board, and empanel one that was disinterested, was a continuing duty. Therefore, Verizon's duty to Idearc continued at least until Idearc's bankruptcy, when Idearc became subject to judicial supervision.

A promoter is liable as a principal for unauthorized contracts made in the name of the corporation. As a matter of law, Verizon, not Idearc, was obligated on the high yield notes and the credit facility. In violation of its continuing, fiduciary duty, Verizon let Idearc service the unauthorized spin debt after the spin. Verizon knew or should have known that the debt was Verizon's debt, not Idearc's debt.

There are at least two other instances post-spin where Verizon breached its fiduciary duty. The first was when Defendant Diercksen and Seidenberg became aware that Kathy Harless and Coticchio were at war and Ms. Harless was not being candid with the New Board. *See* PX 1313. Verizon said and did nothing. Then, shortly before Idearc's bankruptcy, Defendant Diercksen and Seidenberg became aware that Idearc was on the verge of bankruptcy because of the debt and failed to install a board and disclose the truth to that board.

A fiduciary may not profit from his breach of duty. Verizon's basis in the Yellow Pages business was $300 million. Verizon received assets on November 17 north of $9 billion. Verizon must disgorge its profit.

Plaintiff is entitled to a judgment of alter ego. This Court must declare as a matter of law that Verizon acted as Idearc's alter ego and is liable for all the Idearc debts for which Idearc allegedly contracted.

Finally, even were one to assume that Verizon was a shareholder when it received the "dividend" on November 17, Diercksen could not legally pay a dividend. He was not the board.

Nor did he revalue the assets as required by law. *See* Plaintiff's Motion for Summary Judgment filed April 23, 2012 [ECF nos. 332-334], which is incorporated herein by reference for all purposes. Both Diercksen and Verizon are liable for a wrongful dividend.

V. ARGUMENT AND AUTHORITIES

A. Corporate Formation And Share Issuance.

1. The Role of Promoter/Incorporator: The Kenyon Decision.

A promoter is one who forms a corporation and provides or arranges for it the instrumentalities and capital with which to conduct business. *See U.S. Bank Nat'l Ass'n v. Verizon Comm., Inc.*, 2012 WL 3100778 at *13 (N.D. Tex. 2012). An incorporator is a natural person who acts on behalf of the promoter to file the articles of incorporation and install the initial board. By law, the incorporator is not required to disclose the identity of the promoter, 8 DEL. C. § 103(a)(1), and promoters often use their lawyers or sometimes "dummies" who file articles of incorporation without disclosing the promoter's identity. *See, e.g., Kenyon,* 155 F.2d at 914. Since *de jure* formation of the corporation is one of the many tasks undertaken by the promoter, one often sees in case authority the term "promoter" and "incorporator" used interchangeably. To be more precise, the promoter and incorporator may be the same person, but more often than not they are different beings, and one is the agent of the other.

Corporate existence is commenced by filing of articles of incorporation. 8 DEL. C. § 106. However, one must distinguish the "commencement" of corporate existence from its "perfection." Just as a child is born and given life, the child has no legal ability to contract or conduct business. A *de jure* corporation exists once the charter is filed with the state, but without a board, corporate formation is not "perfected." Without a board, the corporation cannot issue stock or approve and direct the foot soldiers of commercial activity – its corporate officers.

Where, as here, the charter does not name a board, the incorporator is granted the power under Section 107 of the Code to "perfect" corporate existence by electing a board. 8 DEL. C. § 107. Once the board is established, the promoter's role as incorporator comes to an end, even though his role as promoter may continue long afterwards – until such time as the scheme of promotion is complete and an independent board is in place. *In re Bailes*, 444 F.2d 1241, 1244 (5th Cir. 1971); *Pub Inv. Ltd. v. Bandeirante Corp.*, 740 F.2d 1222, 1234-1235 n. 72 (D.C. Cir. 1983); *Bovay v. H.M. Byllesby & Co.*, 12 A.2d 178, 186 (Del. Ch. 1940). Only after an initial board is in place may the corporation elect officers, and issue and sell stock. *See, generally*, subchapters 4 and 5 of the DELAWARE CODE. Only the board has the power to issue stock. *See* 8 DEL. C. § 141. If the board issues stock, then the board must also set the method and amount of consideration to be paid. *See* 8 DEL. C. §§ 152 and 153.

The Articles filed by Mr. Feldman did not identify any board members. As permitted by statute, Mr. Feldman adopted the Original Bylaws[4] but he failed to "perfect" the corporate formation because he never appointed the second board member.

As to any stock ownership in Idearc, that issue begins and ends with the failure of the promoter/incorporator to "perfect" the formation of Idearc. There is no reason to analyze the issue beyond this one, powerful, irrefutable fact. But even if one were to disregard all Delaware law concerning the perfection of corporate existence, it is still clear that Verizon never owned any stock. Mr. Diercksen's resolution purporting to issue one share of VDDC stock and to authorize Kathy Harless to sell it to Verizon does not set a price. *See* Ex. A-2 (PX 2018), App. at 48.

[4] The use of the term "original bylaws" in Section 107 is not accidental. Once the "original bylaws" are in place, the incorporator cannot amend or modify the bylaws. That is the role of the board – not the promoter or incorporator.

The real question for this Court is what effect, if any, are actions taken by a promoter before the board is in place. Here, before the board was in place, Verizon appointed officers, adopted resolutions, hired lawyers and issued stock. Did this have legal significance?

The language of Section 107 would seem to permit the incorporator to "manage the affairs" of the corporation until such time as the initial board is in place.[5] Feldman did nothing after June of 2006 to manage the affairs of Idearc. Plaintiff anticipates Verizon will argue that if its agent could manage the affairs of Idearc, so could it. So the question becomes, what does Section 107 authorize?

The *Kenyon* case is directly on point. *Kenyon*, 155 F.2d at 914-916. Justice Hand, writing for the Second Circuit and construing Delaware law, had before him facts much like those before this Court. Kathleen Hogan and Fred Lloyd were the promoters of Holbrook, a Delaware corporation formed in November 1942. As in the case at bar, Hogan and Lloyd did not sign the articles as "incorporators." They directed three others (called "dummies") to actually sign the articles, much like Verizon employed Feldman here. After the articles were filed but before a board was in place, the promoters set about a plan of raising capital for the new company. Originally, a loan was investigated to fund operations. When that failed, the promoters located an equity investor. After the passage of some time, in July, 1943, a board was finally installed and stock issued to the investor. During the considerable time that elapsed between when the corporation was formed and when the board was installed, the promoters entered into an employment contract with the plaintiff, Kenyon, employing him as president of the corporation for a term of 5 years. The contract was not ratified by the board, raising full square the issue of a promoter's authority.

[5] Obviously, to literally apply this language would allow an incorporator to manage the affairs of the corporation forever by forever postponing the appointment of a board.

The Second Circuit construed Section 107 of the Code, which existed then in much the same form as it does today. The Second Circuit disregarded the "dummies" and treated the promoters as the real incorporators. The issue was whether the language allowing incorporators to manage or direct the affairs of the corporation until a board was in place allowed the promoters to appoint officers. In ruling it did not, the Second Circuit held that the incorporators had no power to appoint officers before a board was appointed. *Kenyon*, 155 F.2d at 916. Moreover, the statutory grant of power to the promoter did not extend to starting the business-just arranging for financing and electing the board. The appointment of Kenyon as an officer was not binding on the corporation absent ratification by the board, which had not occurred. *Id*. Though this case was decided in 1946, it is still regarded as a correct statement of Delaware law. *See, e.g.*, BALOTTI AND FINKELSTEIN, *Delaware Law of Corporations and Business Organizations*, § 1.6 (2012); WELCH, TUREZYN & SAUNDERS, *Folk on the Delaware General Corporation Law*, § 107.1 (2012).

Verizon has attempted to point to its mythical ownership in Idearc as somehow justifying or ratifying the unauthorized actions taken by the Diercksen as "sole board member." However, Verizon was never an owner of Idearc stock. It was only a promoter.

A case in point is *Brandner Corporation v. Stelnick*, 1996 WL 82461 (Del. Ch. 1996). There, the promoter had, allegedly, fraudulently induced investors to grant him rights in stock giving him control over the corporation. Though articles had been filed, no board was put in place before the grant of rights. The promoter ran the business and had those working with him issue stock certificates even though there was no board. The investors, upon learning of the unsavory character of the promoter, located the incorporator, and had him appoint a board. That board then appointed officers, disenfranchising the promoter. In a fight for control with the

promoter, the promoter relied on the control over the corporation granted by the investors. The investors in turn claimed they were defrauded into granting power over their stock to him. *Brandner*, 1996 WL 82461 at *2 - *5. The Delaware court did not need to reach the issue of fraud to affirm new management. Instead, the court concluded that the promoter's control of operations and issuance of stock certificates was a nullity. Relying on Sections 107, 141, 152, and 153 of the Delaware Code, the court held that nothing predating the establishment of the board had any effect. *Id*. at *6 - *7. There were investors in the enterprise, but no shareholders. Only the board had the power to issue stock, and the board was not in place at the time the stock certificates were issued. *Brandner* has been frequently cited for the proposition that only a duly constituted board may issue stock. *See, e.g., Linton v. Everett*, 1997 WL 441189 at *8 n. 43 (Del. Ch. 1997); *Balin v. Amerimar Realty Co.*, 1996 WL 684377 at *5 (Del. Ch. 1996).

The facts in *Brandner* are not unlike the facts here. Here, Verizon's lawyers and agents created share certificates on November 15 out of whole cloth. Harless and Mundy, though never elected as officers by any board, signed the stock certificates. Mundy, though never lawfully appointed as a secretary, signed a false secretary certificate that purported to establish Verizon as a shareholder of Idearc. *See* Ex. A-2 (PX 2018), App. at 54. Then Debevoise opined to the NYSE and Idearc's transfer agent that all shares to be distributed in the spin would be lawfully issued. *See* PX 1092.

To grant Plaintiff relief, this Court need not reach the issue of whether Verizon acted knowingly or with fraudulent intent when it took steps to "fix" the corporate records before closing. Intent is not relevant to whether Verizon had the power to issue stock to itself. It did not.

2. Promoter Liability On Corporate Contracts And Alter Ego.

There is no issue of fact as to whether Verizon acted as a promoter. The following testimony from trial establishes this:

BY MR. POWERS:

Q: In the examination before my cross began, remember you talked about Mr. Feldman, right?

A: Yes.

Q: Mr. Feldman filed the articles of incorporation for whom?

A: Idearc or then called Verizon Directories Disposition Corporation.

Q: He did that at the direction of whom?

A: You mean what person?

Q: No. You remember your testimony of a moment ago. What company directed that?

A: Verizon.

Q: So Verizon had the company formed, right?

A: Correct.

Q: And also directed the plan of capitalization, correct?

A: Correct.

Tr. Vol. 8B, 40:2-18.

It is black letter law that a promoter is liable on contracts made in the name of the corporation before the charter is filed and corporate existence commences. 1A WILLIAM MEAD FLETCHER, *Cyclopedia of the Law of Corporation*, § 215 (2012). *See also Fish v. Tandy Corp.*, 948 S.W.2d 886, 897 (Tex. App. – Fort Worth 1997, writ denied); *Stringer v. Electronics Supply Co.*, 2 A.2d 78, 79-80 (Del. Ch. 1938). This rule is based on the common law that a putative agent who enters into a contract in the name of a non-existent principal is liable on the contract

as a principal. 1A WILLIAM MEAD FLETCHER, *Cyclopedia of the Law of Corporation*, § 205 (2012); *Fish*, 948 S.W.2d at 897-898. Until such time as a disinterested board is installed and adopts or ratifies the contract, it is the promoter's contract. *Fish*, 948 S.W.2d at 898. *See also Lorillard Tobacco Co. v. American Legacy Found.*, 903 A.2d 728, 745 (Del. 2006). Here, Idearc was incorporated, and it came into existence once Feldman filed the articles. However, the incorporator failed to "perfect" the organization of the corporation because the initial two person board was never appointed. The issue before this Court is whether a promoter is liable on contracts made in the name of the corporation after the charter is filed but before organization of the corporation is perfected.

As a promoter, Verizon is liable on the high yield notes and the credit facility as the maker of the contracts. Just as a putative agent of a non-existent principal is liable on a contract made in the principal's name, so also is the putative agent liable on a contract where the contract is not authorized by the putative principal even though the principal exists. *See, e.g., Walsh v. America's Tele-Network Corp.*, 195 F.Supp.2d 840, 849 (E.D. Tex. 2002); *Warden v. Bank of Mingo*, 341 S.E.2d 679, 682 (W. Va. App. 1986); *Vulcan Corp. v. Cobden Machine Works*, 84 N.E.2d 173, 177 (Ill. App. 1949); *Finsilver, Still & Moss, Inc. v. Cohn*, 181 N.Y.S. 903, 905 (N.Y. Sup. Ct. 1920). *See also* RICHARD A. LORD, *Williston on Contracts* § 35:40 (4th Ed. 2012) (and cases cited therein). Here Verizon's employees or agents signed the high yield notes and the credit facility in the name of Idearc as directed by Verizon and its officer, Defendant Diercksen. *See, e.g.*, the indenture on the high yield notes signed by Mr. Coticchio. PX 1084. Idearc did not and could not have authorized those contracts because it never had a board and was, therefore, incapable of granting assent to the contracts. Further, the bylaws expressly state

that only the board or the president may authorize corporate indebtedness. Ex. A-2 (PX 2018), App. at 43. Here, there was no board and no president.

Diercksen had no authority to act on behalf of Idearc as an Idearc board member, but he did have authority as an officer of Verizon to represent Verizon's interest in the spin. So, when Diercksen appointed Coticchio as the putative CFO of Idearc, that appointment came from Verizon, not Idearc. And when Diercksen instructed Coticchio to sign the high yield notes, that instruction came from Verizon not Idearc. And when Coticchio followed that instruction and signed Idearc's name to the high yield notes and credit facility, he did so as the sub-agent of Verizon, not Idearc. Therefore, since Idearc did not authorize the contracts, the maker of the contracts is Verizon, whose agent directed the subagent to sign the contracts. The credit facility and indenture for the high yield notes are in evidence, signed by Coticchio. *See* PX 1084.

Count Nine of the Amended Complaint alleges promoter liability and breach of duty. Count 11 alleges alter ego in that, *inter alia*, Verizon was the alter ego of Idearc on the Idearc debt. This Court has ruled that this count survives as a remedy. Plaintiff is entitled to judgment decreeing that Verizon as a promoter acted as the alter ego of Idearc in issuing the Idearc debt and is liable on the debt as a principal.

Plaintiff anticipates that Verizon may argue that there was ratification by a *de facto* board or by *de facto* officers. Those concepts have no application here. A *de facto* board is one that is in possession of and exercising the powers of the board under color of an election, but is not a *de jure* board because of some irregularity in its election. *Hockessin Cmty. Ctr., Inc. v. Swift*, ___ A.3d __, 2012 WL 6634007 at *21 (Del Ch. 2012). The same is true of *de facto* officers. *In re Walt Disney Co. Derivative Lit.*, 906 A.2d 27, 48 (Del. 2006). No court has ever applied these concepts to a promoter liability case where the promoter failed to "perfect" the organization of

the corporation by not installing a board. To apply *de facto* board and officer concepts here to these facts would undo Section 107 and the *Kenyon* decision. Indeed, in *Kenyon* the promoters acted like a *de facto* board and purported to appoint a president. This was struck down by the Second Circuit. Until an initial board is installed, there can be no *de facto* board or *de facto* officers.

Plaintiff anticipates Verizon may argue that it was an equitable shareholder of Idearc and ratified the spin and the spin debt. This argument fails because Delaware law only recognizes equitable ownership of stock when (i) the contested stock has been issued and (ii) someone other than the person or entity seeking equitable stockholder rights holds legal title to the stock. *FleetBoston Fin. Corp. v. Alt*, 668 F.Supp.2d 277, 282 (D. Mass. 2009), *aff'd*, 638 F.3d 70 (1st Cir.), *cert. denied*, 132 S.Ct. 415 (2011). Verizon is not an equitable shareholder here because no board was ever formed, there were no shares and Verizon had no right to compel issuance of shares. *FleetBoston*, 668 F.Supp.2d at 282. Verizon was no more a shareholder than Stelnick and the other investors were in *Brandner*. *Brandner*, 1996 WL 82461 at *4, *7.

Verizon will argue again that these rules of law are unfair legal technicalities, and that Verizon contributed the yellow pages business to Idearc and should be compensated for that. The law applies equally to Fortune 50 companies like Verizon as it does to someone like Stelnick in the *Brandner* case. Verizon issued false, back dated certificates to itself to document ownership that did not exist. Verizon created secretary certificates that falsely depicted it as owner and sent false opinions to the NYSE that said the stock to be passed down in the spin was authorized, when it was not. Even if Verizon can somehow distance itself from the acts of its agents, surely Verizon was under some duty to read and understand the articles and the bylaws before embarking on a nine billion dollar transaction. Verizon does not have clean hands here.

Nor is the result inequitable. The putative Idearc debt was repackaged Verizon debt. All benefits of the debt went to Verizon, who has judicially admitted the proceeds were not part of any sale. And if Verizon has some viable claim off the contract for benefits bestowed to Idearc, it has or had the right to file a claim in the bankruptcy court for *quantum meruit*.

This Court has found that Idearc was worth more than the debt on November 17. The Court did not expressly find the value of what Verizon contributed to Idearc. Assuming that what Verizon contributed was worth at least $12 billion, Verizon cannot "set off" this benefit against its liability for breach of duty. *Western*, 473 F.2d at 265. Its recourse is to file a claim in the bankruptcy court as an unsecured creditor.

3. Verizon's Breach Of Duty And Liability For Damages.

A fiduciary breaches his duty where he takes assets of the trust without authority. *See, e.g., Lofland v. Cahall*, 118 A. 1, 5 (Del. 1922); *Wyndham, Inc. v. Wilmington Trust Co.*, 59 A.2d 456, 459 (Del. Ch. 1948). The measure of damages is at least the amount of assets converted by the fiduciary to his personal use or benefit. *Wyndham*, 59 A.2d at 459; *Cahall v. Burbage*, 121 A. 646, 648-649 (Del. Ch. 1923).

Tranche A ($2 billion) of the unauthorized loan was deposited into Idearc's bank account on November 17, 2006. This sum and another $500 million was transferred to Verizon without authority. Idearc was damaged at that point in the amount of the transfer. While the Tranche A debt was unauthorized, the payment by lenders to Idearc gave rise to an implied obligation by Idearc in assumpsit to repay. *See, e.g., Gaines v. Miller*, 111 U.S. 395, 397 (1884) ("Whenever one person has in his hands money equitably belonging to another, that other person may recover it by assumpsit or money had and received."). Verizon breached its duty by taking these funds for its own use.

Also on November 17, Verizon took possession of more than $7 billion in unauthorized debt and used the sale of that debt to discharge its own debt. Thus, Verizon wrongfully benefitted from its breach of trust by the amount of the unauthorized debt.

Verizon knew that the debt – its debt – would be serviced with funds of Idearc after the spin. Still no board was installed. Still the truth was concealed. Verizon breached its duty of loyalty and candor by saying and doing nothing to "perfect" the organization of Idearc – installing a board, and informing the board of the truth. Verizon is liable for the full sum paid on Idearc's debt.

Similarly, Verizon knew that dividends would likely be paid by the New Board post-spin to persons who were not shareholders. Again, Verizon did nothing and is liable for damages of $250 million in wrongful transfers of funds – putative dividends. *See* Ex. A-10 (March 2009 Idearc Form 10-K at 45), App at 362; Tr. Vol. 5B 13:6-14.

Verizon became aware after the spin that the incompetent management it had installed was concealing the real financial condition of Idearc from the New Board. The New Board had already decided that Harless was incapable of bringing Idearc into the digital era. Ex. A-14 (April 27, 2012 deposition testimony of Thomas Rogers at 25:11-19, 27:23-29:9), App. at 366-67. Verizon said and did nothing. Verizon is liable for damages resulting from Idearc's failure to secure competent management sooner than it did.

Verizon became aware that Idearc was near bankruptcy because it was having difficulty servicing the Verizon debt. Ex. A-11, App. at 363; Ex. A-12, App. at 364. A New Board member approached Verizon and sought assistance as regards the Tax Sharing Agreement so it could refinance the debt and stave off bankruptcy. Ex. A-11, App. at 363; Ex. A-12, App. at 364. Verizon did nothing. Moreover, Verizon continued to allow Idearc to service Verizon debt

and force it to abide by a Tax Service Agreement it knew was unauthorized and unenforceable. Verizon effectively forced Idearc into bankruptcy and is liable for the damages that caused.

4. Disgorgement.

A fiduciary who without knowledge and consent deals with the object of his trust must disgorge all profit. *See Harris Trust & Sav. Bank v. Salomon Smith Barney, Inc.*, 530 U.S. 238, 250 (2000). This remedy applies to promoters who transact business with the corporation without the prior approval or ratification of a disinterested board. *Frick v. Howard,* 126 N.W.2d 619, 622-623 (Wi. 1964).

Verizon's basis in the yellow pages was $300 million. PX 52. Verizon received $9.15 billion in exchange for the transfer of the yellow pages business, representing a profit of $8.85 billion. Plaintiff is entitled to damages in that amount representing the profit Verizon wrongfully enjoyed.

B. Liability Under Count 8.

Count 8 is an alternative count that assumes, *arguendo*, that Verizon was a shareholder. Plaintiff moved for summary judgment on the Count. Plaintiff adopts all arguments in that motion. ECF nos. 332, 333.

The Court overruled the motion. Whether a cross-motion was filed is procedurally unclear. Verizon did file a motion that the wrongful dividend was barred by 564(e), and the Court granted that motion in part, saying that 546(e) applied to the cash, but not to the debt. *See* Sept. 14, 2012 Memorandum Opinion and Order [ECF no. 523] at 40-48. Diercksen never plead 546(e) (nor could he). To the extent Diercksen moved for summary judgment as to Count 8, that motion was denied. *Id*.

Procedurally, Count 8 must be tried unless Plaintiff establishes its right here as a matter of law. The minute book establishes that Diercksen was never a director and could not declare a dividend. Whether a dividend is lawful is a two-step process. First, it cannot violate the articles, and, second, it cannot exceed earnings and surplus. *See In re Privacy Infrastructure, Inc.*, 329 B.R. 580, 586-588 (N.D. Tex. 2005). Here, the VDDC articles said that the number of directors was as fixed in the bylaws and that the power of the corporation (including the power to declare dividends) was in the board. Diercksen violated the articles when he approved a dividend without board consent. The minute book establishes no revaluation of assets occurred before a dividend was declared on October 31, 2006. Therefore, as a matter of law, Plaintiff should recover under this Count the entire amount of the dividend from Defendant Diercksen, and joint and several judgment against Diercksen and Verizon for the debt component of the dividend.

VI. PRAYER

Plaintiff prays for judgment as described herein. If the Court chooses not to exercise discretion under Rules 52(a) or 56, FED. R. CIV. P. to enter judgment for Plaintiff, Plaintiff prays that Counts 8, 9 and 11 be set for trial along with all other unresolved claims for relief.

Respectfully Submitted,

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ATTORNEYS FOR U.S. BANK NATIONAL ASSOCIATION
as Litigation Trustee on Behalf of the
Idearc Inc. et al. Litigation Trust

CERTIFICATE OF SERVICE

On February 8, 2013, the undersigned electronically submitted the foregoing document with the Clerk of Court for the U.S. District Court, Northern District of Texas, using the electronic case filing system of the Court. The undersigned hereby certifies that all counsel and/or *pro se* parties of record have been electronically served in accordance with Federal Rule of Civil Procedure 5(b)(2).

/s/ Werner A. Powers