

# Structuring Around Stockholders' Appraisal Rights in a Merger

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Stockholders, in connection with certain transactions (for instance, stockholders of a non-surviving corporation in a merger), are often entitled to seek a judicial determination as to the "fair value" of their shares. These rights are known as appraisal rights or dissenters' rights, depending on applicable law. Recently, the Delaware Court of Chancery rejected stockholders' assertions that they were entitled to appraisal rights in a merger where the stockholders gave up control of the corporation in exchange for cash and a minority interest in the post-merger entity.

In January 2018, Company A, Company B, and Merger Sub, a wholly-owned subsidiary of Company B formed to facilitate the transaction, entered into an Agreement and Plan of Merger. The transaction was structured as a reverse triangular merger, as follows:

- Merger Sub merged with and into Company A, with Company A surviving as a wholly owned subsidiary of Company B (the "Merger").
- Each share of Merger Sub common stock was converted into one share of Company A.
- Stockholders of Company A received newly issued shares of Company B common stock in exchange for their shares of Company A common stock.
- Company A declared a \$9B cash dividend to Company B.
- Company B declared a special cash dividend payable to its stockholders of record as of the business day immediately preceding the closing of the Merger.

At the effective time of the Merger, stockholders of Company A prior to the Merger will hold 87% of the common stock of Company B and stockholders of Company B prior to the Merger will hold 13% of the common stock of Company B.

As provided in the preliminary proxy statement, stockholders of Company B were not asked to vote on the Merger, but, rather, were asked to vote on two proposals related to the newly issued common stock of Company B being issued as consideration. Stockholders of Company B sought to enjoin the transaction or,

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alternatively, to be permitted to seek appraisal of their shares from the Court of Chancery, arguing the Board of Directors breached their fiduciary duty by failing to inform stockholders that they had appraisal rights in connection with the Merger and that Company B violated Delaware law by failing to inform stockholders of the availability of appraisal rights in the preliminary proxy statement. The Court of Chancery disagreed, holding (a) only stockholders of a “constituent corporation” have appraisal rights, and Company B was not a “constituent corporation” in the Merger as it was not being merged with another entity; and (b) the stockholders were not required to relinquish their shares in connection with the Merger, which relinquishment is contemplated by Delaware law. In so holding, the Court of Chancery rejected stockholders’ arguments to (y) disregard corporate form and confer Merger Sub’s status on its parent, thereby treating Company B as a de facto “constituent corporation” in the Merger; and (z) focus on the structure and economic reality of the Merger - stockholders of Company B are giving up 100% control for cash and a minority interest in the post-merger entity - rather than the express statutory language. Thus, Company B stockholders were not entitled to appraisal rights.

This structure is certainly not appropriate for all transactions. A Board of Directors must consider a host of legal, financial, and other factors in determining the appropriate structure for their deal. Moreover, there may be potential benefits to granting stockholders appraisal rights - for instance, certain jurisdictions deem appraisal rights to be an exclusive remedy. Nevertheless, it provides a Board of Directors with a proposed structure to consider in structuring a deal and affirms that only stockholders of “constituent corporations” are entitled to appraisal rights under Delaware law.

## Structuring Around Stockholders’ Appraisal Rights in a Merger