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QUASI-APPRAISAL: APPRAISING BREACH OF DUTY OF DISCLOSURE CLAIMS FOLLOWING "CASH-OUT" MERGERS IN DELAWARE

Zachary A. Paiva[*]

ABSTRACT

In recent years, Delaware has served as the hot bed for the dramatic increase in merger appraisal litigation and the proliferation of "appraisal arbitrage" whereby opportunistic shareholders buy into companies following merger announcements and challenge announced deal prices as an investment strategy. While this has not always proved profitable, it has increased scrutiny over the Delaware appraisal regime and the ability for shareholders to avail themselves of the opportunity for a judicial valuation of their shares. Furthermore, it has highlighted information asymmetries in which controlling shareholders, particularly those seeking to cash out their minority shareholders, are incentivized to underpay or mislead minority shareholders who might be reluctant to seek appraisal. This raises questions regarding the accessibility of the appraisal remedy and how closely appraisal should mirror class actions which allow for broader representation with lower barriers to entry. This Note argues that current trends in merger and appraisal litigation, particularly those which have significantly heightened scrutiny over pre- and post-closing disclosure claims, present an opportunity to reexamine quasi-appraisal as a collective form of redress in appraisal actions. This Note calls for the expansion of the quasi-appraisal remedy to provide greater access to appraisal valuations in the most extreme examples of minority shareholder manipulation, which would provide a more equitable form of recovery and discourage manipulation of minority shareholders.

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INTRODUCTION

Sherry Shareholder owns a 2% stake in Controlled Corporation (CC), a Delaware corporation controlled by Matt Majority, who owns a 90% stake. CC is publicly traded and its stock is currently estimated to be worth $10 per share after being worth $20 six months earlier. Majority decides to take the company private by acquiring all of its publicly available shares to capitalize on the current low stock price and reinvest in the corporation to maximize its efficiency and capacity for profits.[1] To do this Majority undergoes a "cash-out merger"[2] under Section 253 of the Delaware General Corporation Law (DGCL). Shareholder is paid $12 per share, a 20% premium, but because her shares were worth $20 just six months earlier, she believes this price unfairly denies her the adequate value of her 2% stake. Does she have a remedy?

The answer depends on the disclosure process and CC's efforts to inform Shareholder of her shares' value. While appraisal is deemed the exclusive remedy for disgruntled shareholders,[3] it does not account for fraudulent or illegal behavior on behalf of the controlling shareholder or material omissions or misstatements that may significantly impact Shareholder's knowledge of the "fair value"[4] of her shares.[5] Is this

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1. This assumes that once private, CC will not issue dividends and Majority will focus on increasing the company's profitability by increasing capital expenditures to improve and expand operations.

2. For purposes of this Note, a "cash-out merger" is a merger whereby a target company is merged into an acquiring company, and the shareholders of the target company are provided with cash as compensation for relinquishing their shares.

3. Appraisal is a statutorily mandated procedure whereby target shareholders who object to the merger price may seek an independent judicial valuation of their shares in a proceeding in a state court of the corporation's state of incorporation. This Note limits its discussion of appraisal to Delaware and proceedings brought before the Delaware Court of Chancery, the state's trial court known for its expertise in commercial litigation. Delaware allows minority shareholders to seek appraisal subject to certain exceptions and procedural requirements. DEL. CODE ANN. tit. 8, § 262 (West 2016). For a discussion of these exceptions and procedural requirements, see *infra* Part I.A.

4. Delaware courts must assess "all relevant factors" when determining the fair value of shares. DEL. CODE ANN. tit. 8, § 262(h) (West 2016). Fair value is a highly contested factor in appraisal proceedings and Delaware courts have "significant discretion" to determine the fair value of shares. Golden Telecom, Inc. v. Glob. GT LP, 11 A.3d 214, 217–18 (Del. 2010). The Delaware Supreme Court has recently clarified that fair value is "fair compensation for [a petitioner's] shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction." DFC Glob. Corp. v. Muirfield Value Partners, L.P., No. 518, 2016, 2017 WL 3261190, at *18 (Del. Aug. 1, 2017).

5. It is generally understood that shareholders who own more than 50% of the company's stock or demonstrate "domination by a minority shareholder through actual control of corporate conduct," are controlling shareholders. Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 70 (Del. 1989) (citations omitted); *see also* Kahn v. Lynch Commc'n Sys., 638 A.2d 1110 (Del. 1994) (finding that a 44% shareholder should be treated as a controlling shareholder based on its ability to control corporate decisions). Controlling shareholders owe fiduciary duties both to the corporation and its minority

equitable to Shareholder? How may she recover the fair value of her shares with limited knowledge of how CC determined the merger or deal price? The answer may not lie within statutory appraisal relief but instead may hinge on a rarely invoked post-closing damages remedy known as quasi-appraisal.[6]

Based on the Delaware Court of Chancery's "fair value" determination,[7] quasi-appraisal damages attempt to compensate minority shareholders for the out-of-pocket damages they suffered following the loss of their shares and the breach of a controlling shareholder's duty of disclosure.[8] Quasi-appraisal damages attempt to rectify inadequate disclosure and an ill-informed decision regarding the exercise of discretionary appraisal rights by allowing plaintiffs post-closing claims when they would otherwise not qualify for the statutory appraisal remedy.[9] However, this remedy is only available if the Court of Chancery determines that a controlling shareholder breached its duty of disclosure and that the breach contributed to a finding that the short-form merger, whereby a 90%+ shareholder acquires the corporation's remaining shares without a minority shareholder vote, cashed out the minority shareholders without properly informing minority shareholders of their appraisal rights.[10] The quasi-appraisal calculation is based on the difference

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shareholders (those holding less than the controlling stake) to prevent actions that benefit controlling shareholders to the detriment of the corporation and its minority shareholders. Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983).

6. Quasi-appraisal is a class-wide equitable remedy to assess the out-of-pocket damages suffered by minority shareholders which compensates them for the loss of their shares following the breach of a controlling shareholder's duty of disclosure. *See generally In re* Orchard Enters., Inc. Stockholder Litig., 88 A.3d 1, 50 (Del. Ch. 2014). For a discussion of quasi-appraisal, see *infra* Part III.

7. *See supra* note 4.

8. *See supra* note 6.

9. *See generally* Berger v. Pubco Corp., 976 A.2d 132, 136–45 (Del. 2009).

10. The duty of disclosure or 'duty of candor' requires directors and controlling shareholders to "disclose fully and fairly all material information within the board's control when it seeks shareholder action." Malone v. Brincat, 722 A.2d 5, 9 (Del. 1998) (quoting Zirn v. VLI Corp., 681 A.2d 1050, 1056 (Del. 1996) (quoting Stroud v. Grace, 606 A.2d 75, 84 (Del. 1992))). The requirement to disclose all material information is not an independent duty "but the application in a specific context of the board's fiduciary duties of care, good faith, and loyalty." Malpiede v. Townson, 780 A.2d 1075, 1086 (Del. 2001). Short-form mergers under DGCL Section 253 are not subjected to entire fairness review; instead, "absent fraud or illegality, the only recourse for a minority stockholder who is dissatisfied with the merger consideration is appraisal." Glassman v. Unocal Expl.

between the merger consideration provided and the fair value of minority shareholders' shares.[11]

Understanding Delaware courts' use of quasi-appraisal requires an overview of several related areas. This Note proceeds as follows. Part I briefly examines the statutory framework for minority shareholders' rights following "cash-out" mergers under the DGCL. Part II discusses current trends in merger litigation that negatively impact minority shareholders' ability to seek appraisal or recover post-closing damages.[12] Part III discusses the history and application of quasi-appraisal as an equitable remedy.[13] Finally, Part IV recommends means of reform, through an expansion of the quasi-appraisal remedy to ensure that minority shareholders are adequately protected following DGCL Section 253 mergers.

I. THE STATUTORY FRAMEWORK

This Part discusses the statutory framework for the quasi-appraisal remedy, namely, the statutory availability of appraisal in Delaware under DGCL Section 262 and the statutory authority for short-form mergers under DGCL Section 253 when a controlling shareholder owns at least ninety percent of a company in a "cash-out" or "going-private" merger.

Corp., 777 A.2d 242, 243 (Del. 2001). However, "[a]lthough fiduciaries are not required to establish entire fairness in a short-form merger, the duty of full disclosure remains, in the context of this request for stockholder action." *Id.* at 248.

11. *See Berger*, 976 A.2d at 137 (discussing Nebel v. Sw. Bancorp, Inc., Civ. A. No. 13618, 1995 WL 405750, at *7 (Del. Ch. July 5, 1995)).

12. For purposes of this Note, post-closing damages are damages which are available to wronged plaintiffs following the consummation of a merger transaction. Short-form mergers under DGCL Section 253 are said to have closed immediately after the parent corporation through the expedited process of filing a certificate of ownership and merger. *See Glassman*, 777 A.2d at 247 (discussing DGCL Section 253).

13. For purposes of this Note, an equitable remedy is a judicially-crafted remedy which is obtained when available legal remedies cannot redress the injury to a non-breaching party following breaches of contract. *See Equitable Remedy*, BLACK'S LAW. DICTIONARY (10th ed. 2014). In this context, it arises as a way in which the Delaware Court of Chancery may craft remedies that provide recoveries to minority shareholders outside of the statutory appraisal process following breaches of the duty of disclosure.

A. SECTION 262: THE STATUTORY APPRAISAL REMEDY

Section 262 of the DGCL permits stockholders of corporations acquired in certain merger or consolidation transactions to exercise appraisal rights, subject to certain exceptions and procedural requirements.[14] DGCL Section 262(g), recently amended by House Bill 371 and applicable to transactions consummated, resolutions adopted and authorizations provided on or after August 1, 2016,[15] provides that the Court of Chancery must dismiss an appraisal proceeding as to all stockholders who assert appraisal rights unless:

> (1) the total number of shares entitled to appraisal exceeds 1% of the outstanding shares of the class or series eligible for appraisal, (2) the value of the consideration provided in the merger or consolidation for such total number of shares exceeds $1 million, or (3) the merger was approved pursuant to § 253 or § 267 [of the DGCL].[16]

Recent amendments limit appraisal demands by including a new *de minimis* exception that restricts appraisal demands where the number or value of shareholders' shares is minimal.[17] However, for this *de minimis* exception to apply, the shares at issue must be listed on a national securities exchange immediately before the merger or consolidation.[18]

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14. DEL. CODE ANN. tit. 8, § 262 (West 2016).

15. Act of June 16, 2016, ch. 265, § 10, 80 Del. Laws (2015–2016) (codified at DEL. CODE ANN. tit. 8, § 262(g) (West 2016)). The bill became effective on August 1, 2016 and applies only to appraisal proceedings arising out of (i) "transactions consummated pursuant to agreements entered into on or after August 1, 2016," (ii) "mergers pursuant to Section 253 [of the DGCL with] resolutions *adopted by [a] board* of directors on or after August 1, 2016 or," (iii) "mergers pursuant to Section 267 [of the DGCL], *authorizations provided* on or after August 1, 2016." *Id.* § 18 (emphasis added).

16. DEL. CODE ANN. tit. 8, § 262(g) (West 2016).

17. *Id.*; Appraisal demands are formal letters written by dissenting shareholders which are "deliver[ed] to the corporation, before the taking of the vote on the merger or consolidation," and "reasonably inform[] the corporation of the identity of the stockholder and that the stockholder intends thereby to demand the appraisal of such stockholder's shares." *Id.* § 262(d)(1).

18. The so called "market out" exception states that "no appraisal rights under this section shall be available for the shares of any class or series of stock, which stock, or depository receipts in respect thereof, at the record date fixed to determine the stockholders entitled to receive notice of and to vote at the meeting of stockholders to act upon the agreement of merger or consolidation, were . . . listed on a national securities exchange." *Id.* § 262(b)(1).

Appraisal awards have a default presumption of accruing interest at a rate of five percent over the Federal Reserve discount rate from the merger's effective date through the actual payment of the appraisal award, and are compounded quarterly unless the Court of Chancery determines otherwise for good cause.[19] Corporations can settle claims with appraisal petitioners prior to the appraisal proceedings.[20]

However, amendments to DGCL Section 262(h) prevent statutory interest from running on the entire amount of damages sought. For example, if a corporation makes a voluntary cash payment to the appraisal petitioners for all or a portion of the merger consideration, then recovery on interest is limited to the difference between the prepaid amount and the final award.[21] Pursuant to DGCL Section 262(h), these agreements permit the corporation to prepay a portion of the merger consideration and avoid accruing a portion of the statutory interest prior to the Court of Chancery's determination of fair value.[22] Any prepayment is at the sole discretion of the corporation and does not influence the Court of

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19. *Id.* § 262(h). While it is unclear how Delaware courts will interpret what constitutes "good cause," some commentators have noted that a "bylaw precluding statutory interest for appraisal arbitrageurs, who did not own their stock prior to the announcement of the merger agreement and who acquired their stock notwithstanding notice of the bylaw" would arguably be "good cause." Berton W. Ashman et al., *Appraisal Practice Tips 1 Year After Prepayment Amendment*, POTTER ANDERSON & CORROON LLP (July 31, 2017), http://www.potteranderson.com/newsroom-publications-Appraisal-Practice-Tips-1-Year-After-Prepayment-Amendment.html [https://perma.cc/4QVT-BRGA].

20. Some commentators have noted that the costs of appraisal litigation are so expensive that in many instances they induce settlement. *See e.g.*, Theodore E. Mirvis et al., *Delaware Appraisal at a Crossroads?*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (June 20, 2017), https://corpgov.law.harvard.edu/2017/06/20/delaware-appraisal-at-a-crossroads/ [https://perma.cc/P83C-WVWC] (noting that recent appraisal litigation has raised fundamental questions regarding structuring appraisal in ways that would reduce settlement).

21. DGCL Section 262(h) provides that "the surviving corporation may pay to each stockholder entitled to appraisal an amount in cash, in which case interest shall accrue thereafter as provided [t]herein only upon the sum of (1) the difference, if any, between the amount so paid and the fair value of the shares as determined by the Court, and (2) interest theretofore accrued, unless paid at that time." DEL. CODE ANN. tit. 8, § 262(h) (West 2016).

22. *Id.*

Chancery's determination of fair value.[23] Some commentators note that these legislative amendments may prevent appraisal arbitrage,[24] and provide less incentive for shareholders to bring appraisal actions.[25]

B. SECTION 253: THE STATUTORY SHORT-FORM MERGER

DGCL Section 253 allows for short-form mergers in which a Delaware parent corporation that owns "at least 90% of the outstanding shares of each class of the stock of a [subsidiary] corporation" can authorize the buy-out of the minority shareholders without a shareholder vote.[26] DGCL Section 253 streamlines the process and does not require a parent or subsidiary shareholder vote, but requires that minority shareholders receive cash, stock, debt, or other securities in return for their shares.[27]

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23. *Id.*; *see also* Ashman et al. *supra* note 19 (noting that "[w]hile no legal inference may be drawn from the prepayment as to whether the amount prepaid represents the fair value of the appraised shares, prepayment may affect the litigation in other ways").

24. "'[A]ppraisal arbitrage' [is] a practice whereby institutional investors invest in a company upon a takeover announcement with the intention of exercising appraisal rights. . . . [to] take advantage of the relatively high default interest rate under the [DGCL] (5% over the Federal Reserve discount rate) earned on the value of shares held by dissenting stockholders pending disposition of an appraisal claim and payable even if the final appraisal award is less than the merger consideration paid to non-dissenting stockholders." Oliver Brahmst & Matthew Hendy, *Appraisal Risk Back in the Spotlight After Dell*, WHITE & CASE LLP (June 6, 2016), https://www.whitecase.com/publications/alert/appraisal-risk-back-spotlight-after-dell [https://perma.cc/24UJ-V7K5].

25. Should corporations prepay appraisal amounts, they may limit investors who seek or prolong appraisal solely for the purpose of accruing the statutorily mandated interest rate as an investment strategy in a near-zero interest economy. *Amendments to Delaware General Corporation Law Will Affect Appraisal Actions and "Intermediate-Form" Mergers*, ROPES & GRAY LLP (June 20, 2016), https://www.ropesgray.com/newsroom/alerts/2016/June/Amendments-to-Delaware-General-Corporation-Law-Will-Affect-Appraisal-Actions.aspx [https://perma.cc/4DQM-7HFD]; *but see* Ashman et al. *supra* note 19 ("For serial acquirers, prepayment could come with the risk that the money will be used to fund an arbitrage investment in the next target of the acquirer, leading to yet more appraisal litigation.").

26. *See* DEL. CODE ANN. tit. 8, § 253 (West 2017).

27. *Id.*

Shareholders of the parent corporation who dissent from the merger are not entitled to statutory appraisal remedies.[28] However, to ensure that they receive the fair value of their shares, dissenting minority shareholders of a subsidiary company can seek appraisal pursuant to DGCL Section 262.[29] In fact, the Delaware Supreme Court established that "absent fraud or illegality, appraisal is the exclusive remedy available to a minority stockholder who objects to a short-form merger" and that "[t]he determination of fair value must be based on *all* relevant factors, including damages and elements of future value, where appropriate."[30] This exception from entire fairness review[31] is based on the notion that if "the corporate fiduciary sets up negotiating committees, hires independent financial and legal experts, etc., then it will have lost the very benefit provided by the statute—a simple, fast and inexpensive process for accomplishing a merger."[32] That being said, the controlling shareholder is only entitled to this form of "limited review" and "exclusive remedy" when "all facts are disclosed that would enable the shareholders to decide whether to accept the merger price or seek appraisal."[33] Since these protections are available to parent corporations conducting DGCL Section 253 mergers, they are an incentive to provide proper disclosure when cashing out minority shareholders.

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28. *Id.* § 253(d) (in the event of a short-form merger involving a Delaware subsidiary not 100% owned by the parent, the stockholders of the Delaware *subsidiary* shall have appraisal rights as set forth in § 262). In this context, dissenting from the merger involves shareholders of the acquiring company voting against the merger at issue.

29. These appraisal rights are available if "all of the stock of a subsidiary Delaware corporation party to a merger effected under § 251(h), § 253 or § 267 . . . is not owned by the parent [corporation] immediately prior to the merger." *Id.* § 262.

30. Glassman v. Unocal Expl. Corp., 777 A.2d 242, 248 (Del. 2001).

31. Entire fairness review is a heightened form of judicial scrutiny applied to transactions where a majority of the board of directors appear interested. *In re* KKR Fin. Holdings LLC S'holder Litig., 101 A.3d 980, 990 (Del. Ch. 2014). In those instances, the transaction must be inherently and objectively fair, both in terms of a fair dealing and a fair price. Weinberger v. UOP, Inc., 457 A.2d 701, 711 (Del. 1983).

32. *Glassman*, 777 A.2d at 247–48.

33. Berger v. Pubco Corp., 976 A.2d 132, 134 (Del. 2009) (discussing *Glassman*, 777 A.2d at 248).

II. CURRENT TRENDS IN MERGER AND APPRAISAL LITIGATION

Significant attention has been drawn to current trends in merger litigation whereby nearly 95% of publicly announced mergers have been challenged in one or more jurisdictions.[34] These lawsuits (often class-action suits) are characterized as frivolous, and have amounted to a trend of "ritualized quasi-litigation" where the plaintiffs' bar brings unmeritorious claims and then grants broad releases of their claims in exchange for supplemental disclosure and attorney's fees.[35] These broad settlements are appropriately named "disclosure-only settlements."[36] This practice is seen as rising to a level of a "deal tax" on mergers that leads to what current Chief Justice Leo E. Strine Jr. of the Delaware Supreme Court characterized as "intergalactic releases" of shareholder claims.[37] These claims often lead to nothing more than supplemental disclosure and attorney's fees and have likely prevented meritorious claims from receiving the appropriate attention that they deserve.

This Part discusses additional trends in merger litigation that affect plaintiff's ability to recover in: (1) disclosure-only settlements, (2) transactions involving uncoerced and fully informed shareholder votes, (3) post-closing damages actions, (4) transactions involving a controlling shareholder conditioned on protections provided *ab initio*, and (5) based on "fair value" determinations in statutory appraisal proceedings under DGCL Section 262(h). These trends establish a framework to better understand quasi-appraisal jurisprudence in Delaware and efforts to ensure that controlling shareholders adhere to their duty of disclosure and

34. Matthew D. Cain & Steven Davidoff Solomon, Takeover Litigation in 2014 2 (Feb. 20, 2015) (unpublished manuscript), https://ssrn.com/abstract=2567902 [https://perma.cc/6PHU-GKEM].

35. *In re* Activision Blizzard, Inc. Stockholder Litig., 124 A.3d 1025, 1067 (Del. Ch. 2015).

36. *Id.*

37. *See* Transcript of Settlement Hearing and Request for Attorneys' Fees and the Court's Rulings at 65, Acevedo v. Aeroflex Holding Corp., No. 7930–VCL (Del. Ch. July 8, 2015). In *Acevedo*, Chief Justice Strine rejected a global release of claims in exchange for a reduced termination fee and a shortening of the matching-rights period by one day because the deal protections had not impeded competing bidders and thus were insufficient to support a global release. *Id.* at 71–73. Further, the additional disclosures were nonsubstantive, immaterial, and insufficient consideration to support the broad "intergalactic release." *Id.* at 73.

provide sufficient information for minority shareholders to assess the fair value of their shares.

A. Increased Scrutiny of Disclosure Only Settlements

In re Trulia, Inc. Stockholder Litigation marked an abrupt shift in the landscape of merger litigation in Delaware by signaling increased skepticism of disclosure-only settlements.[38] In *Trulia*, Chancellor Bouchard rejected a disclosure-only settlement as inadequate, finding that supplemental disclosures were not "plainly material" and therefore insufficient to support the broad release of stockholder claims against the defendants.[39] In doing so, the Court of Chancery articulated a new standard to support heightened judicial scrutiny of disclosure-only settlements. That is, supplemental disclosures must be "plainly material" in a way that "significantly alter[s] the 'total mix' of information made available" to shareholders to address a material misrepresentation or omission at early stages of litigation.[40] However, wary that the plaintiffs' bar would seek disclosure-only settlements in other jurisdictions, the court stated that the proliferation of forum-selection clauses could be combined with the "hope and trust" that other courts would adopt a similar approach to disclosure-only settlements.[41] Some commentators speculate that *Trulia* could increase merger litigation,[42] but early indications suggest that Delaware's heightened standard and attempts to limit frivolous litigation and alleviate the "deal tax" have been partially successful in reducing merger litigation.[43]

B. The "Cleansing" Effect of Corwin

Around the same time as *Trulia*, Delaware courts began to articulate a heightened standard for post-closing damages claims by limiting

38. *In re* Trulia, Inc. Stockholder Litig., 129 A.3d 884 (Del. Ch. 2016).
39. *Id.* at 898–99.
40. *Id.* at 896 (quoting Gantler v. Stephens, 965 A.2d 695, 710 (Del. 2009)).
41. *Id.* at 899.
42. *See* Paul J. Collins & Michael J. Kahn, *Deal Litigation After* Trulia, DEL. BUS. CT. INSIDER (Apr. 27, 2016), http://www.delbizcourt.com/id=1202756113215 [https://perma.cc/8A9H-LKAU].
43. *See, e.g.*, Matthew D. Cain et al., *The Shifting Tides of Merger Litigation*, VAND. L. REV. (forthcoming 2018).

damages available from an alleged breach of fiduciary duty by target company directors following certain merger transactions.[44] This created a "cleansing effect" whereby mergers approved by informed and disinterested shareholders and not otherwise subject to entire fairness review could overcome certain breaches of fiduciary duties and extinguish post-closing damages claims at the motion to dismiss phase.[45] Furthermore, the Delaware Supreme Court held in *Corwin v. KKR Financial Holdings*, that the business judgment rule is the appropriate standard of review if a deal is (1) "approved by the fully informed, uncoerced majority of disinterested stockholders" and (2) "not subject to the entire fairness" standard of review.[46] Shortly after *Corwin*, the Delaware Supreme Court upheld the business judgment rule in light of proper shareholder approval and emphasized that:

> [w]hen the business judgment rule standard of review is invoked because of a vote, dismissal is typically the result. That is because the vestigial waste exception has long had little real-world relevance, [and] because it has been understood that stockholders would be unlikely to approve a transaction that is wasteful.[47]

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44. *See, e.g.*, Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304 (Del. 2015).

45. *See* Joseph O. Larkin & Shaivlini Khemka, *After* Corwin*, Court of Chancery Provides Additional Guidance on Application of Business Judgment Rule to Post-Closing Damages Claims*, INSIGHTS: DEL. EDITION (Nov. 17, 2016), https://www.skadden.com/insights/after-corwin-court-chancery-provides-additional-guidance-application-business-judgment-rule. For purposes of this Note, a disinterested shareholder is one who is not a controlling shareholder an insider of the corporation, or otherwise standing on both sides of the transaction. The underlying logic assumes that the informed and uncoerced vote of disinterested shareholders is able to otherwise overcome certain breaches of fiduciary duties.

46. *Corwin*, 125 A.3d at 305–06. The business judgment rule is a deferential form of judicial review that relies upon the "presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984), *overruled on other grounds by* Brehm v. Eisner, 746 A.2d 244 (Del. 2000). If the business judgment rule applies, Delaware courts "will not substitute [their] own notions of what is or is not sound business judgment." Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971).

47. Singh v. Attenborough, 137 A.3d 151, 151–52 (Del. 2016) (citations omitted).

Thus, *Corwin* and its progeny further emphasize the importance of shareholder approval to "cleanse" transactions, and Delaware courts' skeptical view of post-closing damages claims.

Furthermore, the cleansing effect of a fully informed shareholder vote has been extended to post-closing damages claims following noncoercive first-step tender offers and transactions that do not involve a controlling shareholder.[48] For example, the Court of Chancery found that shareholders' decisions to participate in tender offers has "the same cleansing effect" under *Corwin* as stockholder approval pursuant to a traditional long-form merger.[49] Therefore, Vice Chancellor Tamika Montgomery-Reeves rejected the arguments that (1) tender offers differ from "statutorily required stockholder votes based on the lack of any explicit role in the [DGCL] for a target board of directors responding to a tender offer," and (2) "a first-step tender offer in a two-step merger arguably is more coercive than a stockholder vote in a one-step merger."[50] In *Larkin v. Shah*, the Court of Chancery stated that the entire fairness standard only applies in the controlling shareholder context because those cases involve "inherent coercion"[51] and that the business judgment rule is the "irrebuttable" standard absent a controlling shareholder's

48. *See, e.g.*, *In re* Volcano Corp. Stockholder Litig., 143 A.3d 727, 741 (Del. Ch. 2016), *aff'd*, 156 A.3d 697 (Del. 2017) (unpublished table decision). In this context, a noncoercive tender offer is a controlling shareholder's public offer to purchase securities for consideration where shareholders are not "wrongfully induced by some act of the defendants to sell their shares for reasons unrelated to the economic merits of the sale." Ivanhoe Partners v. Newmont Mining Corp., 533 A.2d 585, 605 (Del. Ch. 1987), *aff'd*, 535 A.2d 1334 (Del. 1987).

49. *Volcano*, 143 A.3d at 741. For purposes of this Note, a long-form merger is a merger by a shareholder who owns less than 90% of the target company's shares and who must receive approval of the merger in the form of a target shareholder vote. *See* DEL. CODE ANN. tit. 8, § 251 (West 2017).

50. *Volcano*, 143 A.3d at 742–43 (alteration in original) (internal quotation marks omitted).

51. *See In re* JCC Holding Co., 843 A.2d 713, 723 (Del. Ch. 2003) ("[C]ontrolling stockholders are reasonably perceived as having such potent retributive powers as to subject minority stockholders to inherent coercion in casting a vote on a squeeze-out merger. This inherent coercion is thought to undermine the fairness-guaranteeing effect of a majority-of-the-minority vote condition because coerced fear or a hopeless acceptance of a dominant power's will, rather than rational self-interest, is deemed likely to be the animating force behind the minority's decision to approve the merger." (applying Kahn v. Lynch Commc'n Sys., Inc., 638 A.2d 1110, 1116–17 (Del. 1994))).

involvement in a conflicted transaction.[52] These cases reaffirm that Delaware courts continue to trust the collective wisdom of shareholders and their voting approval to cleanse the majority of non-conflicted transactions.

C. A "BRAVE NEW WORLD" FOR POST-CLOSING DAMAGES CLAIMS

These trends reflect Delaware courts' continued skepticism regarding the merits of post-closing claims, and the increased deference courts grant corporations that adhere to uncoerced and informed shareholder votes. Due to these shifts in merger litigation, plaintiffs find it increasingly difficult to bring post-closing damages claims.[53]

Furthermore, the permissible window of time to bring post-closing disclosure claims is shorter.[54] This is likely a result of *Corwin* and *Trulia*'s combined effects which—given the number of suits resulting in mootness settlements and the deference granted to shareholder votes—decreased defendants' willingness to voluntarily produce discovery on disclosure and other pre-closing claims.[55] Confronted by these conditions, plaintiffs allege they face a "brave new world" for post-closing damages claims, and challenge limited production on the grounds that "plaintiffs cannot fairly assess whether a disclosure violation occurred, rendering the vote 'uninformed' for *Corwin* purposes."[56] For instance, the plaintiffs in *In re Columbia Pipeline Group, Inc. Stockholder Litigation*, sought a rule denying the defendant corporation's motion to dismiss, staying discovery, and requiring the defendant to produce discovery documents that could

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52. Larkin v. Shah, C.A. No. 10918–VCS, 2016 WL 4485447, at *1 (Del. Ch. Aug. 25, 2016).

53. *See* Larkin & Khemka, *supra* note 45 ("As a practical matter, the *Corwin* case has created a high bar for plaintiff stockholders to pursue a post-closing damages claim.").

54. *Id.* ("[Recent decisions] strongly indicate that disclosure claims should be brought before the stockholder vote when the purported harm of an uninformed vote may still be remedied. Accordingly, stockholder plaintiffs may not be able to seek tactical gain by deferring disclosure claims until after stockholders vote and the disclosures can no longer be supplemented.").

55. *See id.*; *see also* Edward B. Micheletti et al., *Forward Momentum:* Trulia *Continues to Impact Resolution of Deal Litigation in Delaware and Beyond*, INSIGHTS: DEL. EDITION (Nov. 17, 2016), https://www.skadden.com/insights/publications/2016/11/forward-momentum-itruliai-continues-to-impact-reso.

56. *See* Micheletti et al., *supra* note 55.

enable plaintiffs to determine whether a material omission occurred for purposes of a duty of disclosure violation.[57] The omission at issue related to the plaintiffs' contention that Columbia Pipeline Group's directors engineered a spin-off and sold the company to TransCanada Corporation to secure change-in-control bonuses for themselves.[58] In a bench ruling, Vice Chancellor Laster rejected these claims because the plaintiffs bore the burden to plead sufficient facts making it reasonably conceivable that any duty of disclosure violations occurred and that *Corwin* did not apply.[59]

While recently the Court of Chancery found that certain disclosure claims can proceed following a shareholder vote that was neither uncoerced nor uninformed, for purposes of *Corwin*, the unique facts at issue likely indicate the extreme circumstances necessary for post-closing damages claims to overcome a motion to dismiss. In *In re Saba Software, Inc. Stockholder Litigation*, Vice Chancellor Joseph Slights III denied defendant corporation Saba's motion to dismiss after a rushed sales process where plaintiffs were forced to make a "Hobson's choice"[60] of accepting nine dollars in cash or the "recently-deregistered, illiquid stock" when voting on the merger.[61] Finding a "pleading-stage inference of bad faith,"[62] Vice Chancellor Sights agreed that the plaintiffs could plead that Saba acted in bad faith after providing limited financial projections and that they failed to provide information sufficient for shareholders to assess alternatives to the merger consideration.[63] Because these issues occurred in the midst of an accounting restatement that led to the company's deregistration by the Securities and Exchange Commission (SEC) and clear loyalty issues regarding the board's incentive to capitalize on its

57. *In re* Columbia Pipeline Grp., Inc. Stockholder Litig., No. 12152–VCL, 2017 WL 898382, at *1–3 (Del. Ch. Mar. 7, 2017).

58. *Id.* at *2.

59. *See id.* at *1, *5. The court noted that "[t]he duty of disclosure demands that fiduciaries disclose facts. It does not demand that fiduciaries 'engage in "self-flagellation" and draw legal conclusions' as to the inferences to be drawn from those facts." *Id.* at *3 (citation omitted).

60. *In re* Saba Software, Inc. Stockholder Litig., C.A. No. 10697–VCS, 2017 WL 1201108, at *15 (Del. Ch. Mar. 31, 2017).

61. *Id.*

62. *Id.* at *20.

63. *See id.* at *17, *20, *23 (discussing how plaintiffs successfully pled non-exculpated breaches of the duties of care and loyalty).

equity options,[64] the rushed sales process, serious omissions, and clear loyalty issues emphasized the extreme factors needed to amount to materiality.[65] Although the claims could proceed, this case likely reflects the limits of *Corwin* cleansing and the unlikely scenario that plaintiffs will overcome following immaterial omissions.[66]

These challenges reflect judicial reluctance to permit post-closing damages claims and emphasize the rarity of well-pled plaintiffs' disclosure claims. Especially when corporations can provide limited voluntary disclosure and rely upon the protections of the business judgment rule at the pleadings stage. While not insurmountable, *Corwin*'s cleansing remains a serious hurdle for plaintiffs seeking to recover post-closing damages on disclosure claims.

D. CONTROLLING SHAREHOLDERS AND THE *MFW* STANDARD

Furthermore, these trends are not unique to the non-controller context and are also prevalent in controlling shareholder "going private" transactions. In fact, three recent opinions, *In re Chelsea Therapeutics International Ltd. Stockholders Litigation,*[67] *In re Books-A-Million Inc. Stockholders Litigation*,[68] and *Employees Retirement System of St. Louis*

64. *See id.* at *3, *21.

65. *See e.g.*, S. Michael Sirkin & Nick Mozal, Saba Software Inc.—*Eluding* Corwin *Dismissal*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Apr. 5, 2017), https://corpgov.law.harvard.edu/2017/04/05/saba-software-inc-eluding-corwin-dismissal/ [https://perma.cc/26FG-3AWK] (noting that while plaintiffs face a "steep uphill climb" in overcoming the pleadings stages burden of overcoming *Corwin* and a non-exculpated breach of fiduciary, *Saba* emphasizes that these burdens are "not insurmountable in the right case").

66. *See* Paul S. Scrivano & Sarah Young, *Outer Boundaries of* Corwin*, and When a Stockholder Vote Will Cleanse Post-Merger Claims, Are Taking Shape*, ROPES & GRAY LLP (May 1, 2017), https://www.ropesgray.com/newsroom/alerts/2017/05/Outer-Boundaries-of-Corwin-and-When-a-Stockholder-Vote-will-Cleanse-Post-Merger-Claims.aspx [https://perma.cc/5ZAS-3LC3] (discussing *Saba*, and the subsequent Court of Chancery decision *In re* Paramount Gold and Silver Corp. Stockholders Litig., C.A. No. 10499–CB, 2017 WL 1372659 (Del. Ch. Apr. 13, 2017), which "should provide comfort that the failure to include immaterial disclosure will not be usable by plaintiff stockholders as a means to continue spurious claims beyond the motion to dismiss stage").

67. *In re* Chelsea Therapeutics Int'l Ltd. Stockholders Litig., C.A. No. 9640–VCG, 2016 WL 3044721 (Del. Ch. May 20, 2016).

68. *In re* Books-A-Million Inc. Stockholders Litig., C.A. No. 11343–VCL, 2016 WL 5874974 (Del. Ch. Oct. 10, 2016).

v. TC Pipelines GP, Inc.,[69] reflect the Delaware courts' adherence to the "*MFW* standard" which applies the deferential business judgment rule at the pleadings stage of controlling shareholder transactions and prevents post-closing damages claims from proceeding to trial when certain procedural requirements are met.[70]

In *In re Chelsea Therapeutics*, Vice Chancellor Sam Glasscock III dismissed plaintiffs' claims for post-closing damages alleging that Chelsea Therapeutics' board of directors acted in bad faith in selling the company at a price substantially below its standalone value.[71] The plaintiffs originally sought a preliminary injunction to enjoin the transaction on the grounds that the defendants omitted certain projections and study results in the proxy materials which were material to their decision to vote on the merger.[72] However, then Vice Chancellor Parsons denied the motion on the grounds that the disclosure was sufficient and that any additional studies were highly speculative.[73] Following the denial of the motion, the plaintiffs sought post-closing damages alleging that the board's decisions to disregard certain projections and to instruct its financial advisor to ignore a set of financial projections when making a fairness opinion led to the company's undervaluation and were "inconceivable as anything other than actions against the interests of the stockholders, maximizing value for whom was, at that point, the only proper purpose of the Board."[74] Since the case involved the denial of both a pre-closing disclosure claim and post-closing damages claims, it further

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69. Emps. Ret. Sys. of St. Louis v. TC Pipelines GP, Inc., No. 291, 2016, 2016 WL 7338592 (Del. Dec. 19, 2016).

70. The "*MFW* standard" refers to the six procedural requirements needed at the outset of a transaction to invoke the business judgment rule for controlling shareholders: "(i) the controller conditions the procession of the transaction on the approval of both a special committee and a majority of the minority stockholders; (ii) the special committee is independent; (iii) the special committee is empowered to freely select its own advisors and to say no definitely; (iv) the special committee meets its duty of care; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority." *In re* MFW S'holders Litig., 67 A.3d 496, 535 (Del. Ch. 2013). The *MFW* standard was adopted by the Delaware Supreme Court in *Kahn v. M & F Worldwide Corp.*, 88 A.3d 635, 645 (Del. 2014).

71. *See Chelsea Therapeutics*, 2016 WL 3044721, at *1–2.

72. *See id.* at *4. The board had disclosed the existence of the alternative findings and had stated that they were omitted because of their highly speculative nature. *See id.*

73. *Id.* at *4–5.

74. *Id.* at *2.

demonstrates the difficult pleading requirements and the lack of remedies available to challenging "take-private" transactions.

In re Books-A-Million and adherence to the *MFW* standard emphasize the availability of the deferential business judgment rule protection at the motion to dismiss stage of "take-private" transactions involving controlling shareholders.[75] The protection is available so long as the defendants demonstrate their compliance with the *MFW* standard "in a public way suitable for judicial notice, such as board resolutions and a proxy statement" and further, the plaintiffs cannot plead with sufficiency that any conditions of the *MFW* standard were not satisfied.[76] In *In re Books-A-Million*, Vice Chancellor Laster confirmed that the Court of Chancery would dismiss breach of fiduciary duty claims at the pleadings stages when all six procedural requirements of the *MFW* standard were satisfied.[77] Although the plaintiffs alleged that the *MFW* standard should not apply because the special committee of independent directors acted irrationally and in bad faith,[78] Vice Chancellor Laster disagreed, finding that the controlling shareholder, the Anderson family, had no duty to facilitate a third-party offer and did not breach its fiduciary duties by offering to buy the minority shares at a price lower than what a third-party could have offered.[79] For that reason, the Anderson family was able to "freeze-out" the Books-A-Million minority without having to overcome the entire fairness standard or the burden of discovery to prove that the *MFW* standard was satisfied. In *TC Pipelines*, the Delaware

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75. *See e.g.*, Steven Epstein & Gail Weinstein, Books-A-Million *Demonstrates the Power of* MFW, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Nov. 17, 2016), https://corpgov.law.harvard.edu/2016/11/17/books-a-million-demonstrates-the-power-of-mfw/ [https://perma.cc/7U4L-W486] (emphasizing that "MFW and other decisions reflect an evolution of the substantive law to much greater deference than in the past to boards and stockholders in M&A matters").

76. *In re* Books-A-Million, 2016 WL 5874974, at *8 (quoting Transcript of Oral Argument on Defendants' Motion to Dismiss and the Court's Ruling at 21, Swomley v. Schlecht, No. 9355–VCL (Del. Ch. Aug. 27, 2014), 2014 WL 4470947).

77. *See id.* at *7–8.

78. The plaintiffs had sought enhanced scrutiny under *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, for alleged violation of parts ii and iv of the *MFW* standard. *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 180 (Del. 1986).

79. *In re* Books-A-Million, 2016 WL 5874974, at *1, *12, *15.

Supreme Court confirmed that the Court of Chancery properly determined adherence to the *MFW* standard at the pleadings stage.[80]

E. The Weight Granted to the Deal Price in Section 262 "Fair Value" Determinations

Recent decisions by the Court of Chancery expound upon the relative weight of the deal price in appraisal actions under DGCL Section 262(h). These decisions emphasize the significant variations in appraisal valuations based on differing valuation methods and unique case specific factors. These decisions may signal a departure from the recent proliferation of appraisal suits due to the inconsistency of approaches and results.[81] Continued deference to the deal price as a nearly-exclusive indicator of fair value will likely continue to disincentivize minority shareholders from seeking appraisal.

The Court of Chancery recently emphasized that it need not rely on the merger price to assess fair value in management buyouts. For instance, in *In re Appraisal of Dell Inc.*, Vice Chancellor Laster determined that Dell's deal price was an unreliable measure of fair value, and the fair value of Dell's shares was twenty-eight percent higher than the deal price provided.[82] While commentators speculate that the case highlights a trend in heightened appraisal exposure for management,[83] Vice Chancellor Laster noted that the transaction involved a management buyout, rendering the deal price resulting from the public auction less relevant, and that there was a significant "valuation gap" between the long-term value of Dell and its short-term market value.[84] Although the management buyout involved a well-run arms-length sales process, Laster found that like-minded financial bidders made similar financial assumptions based on required internal rates of return in leveraged buyout pricing models

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80. Emps. Ret. Sys. of St. Louis v. TC Pipelines GP, Inc., No. 291, 2016, 2016 WL 7338592, at *2 n.9 (Del. Dec. 19, 2016) (citations omitted).

81. For a discussion of the substantial increase in appraisal proceedings, *see* Charles R. Korsmo & Minor Myers, *Appraisal Arbitrage and the Future of Public Company M&A*, 92 WASH. U. L. REV. 1551, 1567–83 (2015).

82. *See In re* Appraisal of Dell Inc., C.A. No. 9322–VCL, 2016 WL 3186538, at *35–36 (Del. Ch. May 31, 2016).

83. *See e.g.*, Brahmst & Hendy, *supra* note 24.

84. *In re* Appraisal of Dell Inc., 2016 WL 3186538, at *28–29, *32.

which significantly undervalued Dell.[85] While the Dell appraisal involved unique facts, the case serves as a reminder of the significant challenge in determining fair value and the difficulty in weighing various financial theories and models in appraisal cases. As the case is currently pending before the Delaware Supreme Court,[86] the decision will likely be followed closely as it could continue to incentivize appraisal arbitrage as an investment strategy.

Difficult fair value assessments also arise in the context of procedural deficiencies in sales involving controlling shareholders on both sides of the transaction. For instance, *Dunmire v. Farmers and Merchants Bancorp of Western Pennsylvania Inc.* involved a stock-for-stock transaction between two controlling shareholders without a public auction or outside bidders.[87] Noting that the controlling shareholders on both sides set the stock exchange ratio, Chancellor Bouchard "place[d] no weight" on the merger price as an indicator of fair value,[88] and conducted a discounted net income analysis to set the share's fair value at 10% above the merger price.[89] This case strongly emphasizes that judges may make independent assessments of the share's fair value based on their own valuation methods, which may vary from the parties' valuation methods.

Two Court of Chancery opinions from 2017, *ACP Master, Ltd. v. Sprint Corp.* (*Clearwire*)[90] and *In re Appraisal of SWS Group, Inc.*,[91] further muddle fair value determinations and the appeal of seeking appraisal. In fact, both cases found that minority shareholders' shares were worth materially less than the merger price. In *Clearwire*, hedge

85. *See id.* at *29–30.

86. For arguments pending before the Delaware Supreme Court, see Appellant's Opening Brief, Dell Inc. v. Magnetar Glob. Event Driven Master Fund Ltd., No. 565, 2016 (Del. Jan. 17, 2017), 2017 WL 318529, and Appellee's Opening Brief, Dell Inc. v. Magnetar Glob. Event Driven Master Fund Ltd., No. 565, 2016 (Del. Feb. 13, 2017), 2017 WL 825592.

87. Dunmire v. Farmers & Merchs. Bancorp of W. Pa., Inc., C.A. No. 10589–CB, 2016 WL 6651411, at *1, *7 (Del. Ch. Nov. 10, 2016). For purposes of this Note, a stock-for-stock transaction is a transaction whereby shares of the parent company's stock are provided as consideration to the target company in a merger transaction.

88. *Id.* at *7–8.

89. *See id.* at *1, *16.

90. ACP Master, Ltd. v. Sprint Corp. (*Clearwire*), C.A. No. 8508–VCL, 2017 WL 3421142 (Del. Ch. July 21, 2017).

91. *In re* Appraisal of SWS Grp., Inc., C.A. No. 10554–VCG, 2017 WL 2334852 (Del. Ch. May 30, 2017).

fund Aurelius Capital Management sought a fair value determination of $16.08 per share for its 25 million shares of Clearwire Corporation, which Sprint, its 50.2% controlling shareholder, acquired in a take-private transaction.[92] Furthermore, Aurelius claimed that Sprint breached its fiduciary duties as a controlling shareholder by forcing Clearwire to accept its bid.[93] Vice Chancellor Laster not only denied Aurelius' valuation but also ruled that Sprint met its burden of demonstrating entire fairness and overpaid for Clearwire following a highly contested bidding war with DISH.[94] Laster determined that Clearwire's $3.6 billion sale price ($5 per share) was more than twice its fair value of $2.03 per share and maintained that "[t]he deal price also provided an exaggerated picture of Clearwire's value because the transaction generated considerable synergies" with estimates ranging from $1.5 to $2 billion.[95] *In re Appraisal of SWS* also involved a "synergies-driven transaction" whereby Hilltop Holdings, Inc. (Hilltop) acquired SWS Group Inc. (SWS) for a mix of cash and stock worth $6.92 per share.[96] Finding the merger price to be unreliable, Vice Chancellor Glasscock relied on a "discounted cash flow analysis" and determined that the consideration was worth $6.38 per share, 7.8% below the merger consideration provided at closing.[97] Interestingly, neither side argued that the deal price was the best indicator of fair value and instead argued for traditional valuation methods that lead to valuations "50% above and 50% below the deal price" respectively.[98] While some note that the deal price is not the floor of fair value and that "Delaware courts do not guarantee . . . positive . . . appraisal arbitrage[],"[99]

92. *Clearwire*, 2017 WL 3421142, at *1, *31.

93. *Id.* at *16.

94. *Id.* at *27.

95. *Id.* at *31. Interestingly, the court noted that had Clearwire accepted Sprint's earlier bid of $2.97 per share that the transaction likely would not have been entirely fair. Instead, Sprint's earlier "acts of unfair dealing would have resulted in a finding of unfairness and a damages award in the form of a fairer price." *Id.* at *20. However, after shareholders voted down the $2.97 per share bid and DISH entered the bidding, the merger price of $5 overcame any earlier unfair dealing. *See id.* at *26.

96. *In re* Appraisal of SWS Grp., Inc., 2017 WL 2334852, at *1, *5.

97. *Id.* at *1.

98. *Id.* The petitioner relied upon a comparable company's analysis and both parties conducted discounted cash flows analyses. *Id.* at *10.

99. Edward D. Herlihy et al., *Delaware Court of Chancery Appraises Public Company at Nearly 20% Below Merger Price*, WACHTELL, LIPTON, ROSEN & KATZ (May

below-the-deal-price fair value determinations remain rare in appraisal proceedings and may be limited to unique factual situations where it is more difficult to assess fair value.[100] However, *Clearwire* and *In re Appraisal of SWS* may signal the potential for more fair value determinations below the deal price, particularly in cases where the merger price reflects significant synergies.

Nonetheless, the deal price remains an important consideration in otherwise properly run sales processes without significant synergies. For instance, in *Merion Capital L.P. v. Lender Processing Services, Inc.*,[101] Chancellor Laster granted full weight to the deal price and emphasized that if a:

> merger giving rise to appraisal rights resulted from an arms-length process between two independent parties, and if no structural impediments existed that might materially distort the crucible of objective market reality, then a reviewing court should give substantial evidentiary weight to the merger price as an indicator of fair value.[102]

Furthermore, the court focused on the pre-signing period and the "market check" which in tandem with the merger price offered meaningful competition in the absence of additional bidders.[103] Thus, the case reflects the deference the Court of Chancery provides to the deal price in the event of a well-run sales process and absent noteworthy unique facts that could affect a fair value determination.

The Delaware Supreme Court's recent en banc reversal of a Court of Chancery determination that the fair value of shares exceeded the deal price reiterates the significant deference granted to the deal price in

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31, 2017), http://static.reuters.com/resources/media/editorial/20170601/swsappraisal—wachtellmemo.pdf [https://perma.cc/96NQ-HVES].

100. *See, e.g.*, Gail Weinstein & Philip Richter, *Below-The-Merger-Price Appraisal Results and the SWS Decision*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (June 26, 2017), https://corpgov.law.harvard.edu/2017/06/26/below-the-merger-price-appraisal-results-and-the-sws-decision/#more-95410 [https://perma.cc/YFD6-L2SM] (noting that there have only been two other below-the-merger-price determinations since 2010 and that the cases have all involved unusual facts).

101. Merion Capital L.P. v. Lender Processing Servs., Inc., C.A. No. 9320–VCL, 2016 WL 7324170 (Del. Ch. Dec. 16, 2016).

102. *Id.* at *14 (citations omitted) (internal quotations omitted).

103. *Id.* at *21.

appraisal proceedings with competitive sales processes. Additionally, it demonstrates the rarity of favorable rulings for shareholders seeking appraisal and the judicial deference granted to private equity buyers who conduct market checks. In *In re Appraisal of DFC Global Corp.*,[104] private equity buyer, Lone Star, purchased payday lending company DFC Global Corp. for around $9.50 per share, an amount that Chancellor Bouchard found to be an undervaluation of nearly 8%.[105] On appeal, the Delaware Supreme Court rejected Chancellor Bouchard's equal weighing of the deal price, a comparable company's analysis, and discounted cash flow projections in the wake of regulatory uncertainties undermining the projections, and deferred to the deal price as the best indicator of fair value.[106] Writing that the purpose of an appraisal is to ensure that shareholders "receive fair compensation for their shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction,"[107] Chief Justice Strine declined to adopt a presumption that the merger price unequivocally demonstrates fair value, but stated that the Court of Chancery had a proven record of determining that the deal price was the best indicator of fair value and has significant discretion in fair value determinations based on the facts at hand.[108] Recognizing that the market of potential buyers "who had money at stake" could properly account for the regulatory risks necessary to value the company,[109] Strine deferred to market-based evidence of a fair sales process rather than the minority shareholders' contentions that the company had been undervalued based on future performance uncertainties and Lone Star's financial constraints as a financial buyer seeking an internal rate of return.[110] The case reiterates the difficulties minority shareholders face in appraisal proceedings and the

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104. *In re* Appraisal of DFC Glob. Corp., C.A. No. 10107–CB, 2016 WL 3753123 (Del. Ch. July 8, 2016), *rev'd sub nom.* DFC Glob. Corp. v. Muirfield Value Partners, L.P., No. 518, 2016, 2017 WL 3261190 (Del. Aug. 1, 2017) (en banc).

105. *Id.* at *1. Chancellor Bouchard had granted equal weight to a comparable company's analysis, the deal price and discounted cash flow projections to determine the fair value of DFC's shares. *See id.*

106. DFC Glob. Corp. v. Muirfield Value Partners, L.P., C.A. No. 518, 2016, 2017 WL 3261190, at *1 (Del. Aug. 1, 2017) (en banc).

107. *Id.* at *18.

108. *Id.* at *15.

109. *Id.* at *21.

110. *Id.* at *20.

deference Delaware courts give to the deal price in properly run sales processes. The Delaware Supreme Court may not have granted a presumption in favor of the deal price, but reaffirmed that it will continue to be viewed as the most reliable indicator of fair value.

III. QUASI-APPRAISAL

Quasi-appraisal has emerged as a means of measuring class-wide recovery of out-of-pocket damages following a controlling shareholder's violation of its duty of disclosure.[111] This Part discusses the history of the remedy and its current use in short-form mergers where controlling shareholders violate their duty of disclosure and misstate or deprive minority shareholders of material information which could impact their decision regarding whether to seek appraisal or accept the merger consideration. Part III.A discusses the origins and development of quasi-appraisal as an equitable remedy in Delaware. Part III.B discusses Delaware's tailoring of the quasi-appraisal remedy in a class-action fashion and with risk factors like opting-in and escrow requirements for plaintiffs seeking quasi-appraisal. Finally, Part III.C discusses quasi-appraisal as an equitable remedy and not as an independent cause of action, and the requirements plaintiffs must satisfy to avail themselves of the remedy.

A. THE ORIGINS OF POST-CLOSING REMEDIES FOR DUTY OF DISCLOSURE VIOLATIONS

Quasi-appraisal was first introduced in Delaware in *Weinberger v. UOP, Inc.*, when created as an equitable remedy to temporarily allow additional appraisal actions in response to significant adjustments to Delaware law.[112] *Weinberger* involved a "cash-out" merger where minority shareholders of UOP Inc. (UOP) brought suit on behalf of a class of shareholders who did not exchange their shares for the merger price following a cash-out merger where the remaining shares of UOP were acquired by its controlling shareholder, The Signal Companies, Inc.

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111. *See, e.g.*, *In re* Orchard Enters., Inc. Stockholder Litig., 88 A.3d 1 (Del. Ch. 2014).

112. Weinberger v. UOP Inc., 457 A.2d 701 (Del. 1983).

(Signal).[113] The plaintiffs also sought to set the merger aside or, in the alternative, recover monetary damages against UOP, Signal, and Lehman Brothers Kuhn Loeb, Inc., which served as UOP's investment banker and provided a fairness opinion prior to the merger.[114] The plaintiffs did not rely on the statutory appraisal remedies of DGCL Section 262, and yet the Delaware Supreme Court rejected the "Delaware block" method,[115] and allowed for additional appraisal actions to accommodate new "fair value" valuation methods that were previously restricted.[116] The court noted that "[w]hile the present state of these proceedings does not admit the plaintiff to the appraisal remedy per se, the practical effect of the remedy we do grant him will be co-extensive with the liberalized valuation and appraisal methods we herein approve for cases coming after this decision."[117] Thus, *Weinberger* marks an abrupt change in merger law as the court promoted appraisal to curb controlling shareholders' exploitations of the minority in cash-out mergers.[118] For the first time, the court used its equitable powers to artificially simulate an appraisal proceeding and fashioned a remedy not previously available to plaintiffs. While *Weinberger* emphasized the increased importance of appraisal to check majority manipulation of the minority, the specific remedy of quasi-appraisal was largely tailored to accommodate new valuation methods.

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113. *Id.* at 703.

114. *Id.*

115. *Id.* at 712–13 (stating that the Delaware block method or weighted average method "wherein the elements of value, i.e., assets, market price, earnings, etc., were assigned a particular weight and the resulting amounts added to determine the value per share. . . . shall no longer exclusively control such proceedings").

116. *Id.* at 714 (citation omitted) ("On remand the plaintiff will be permitted to test the fairness of the $21 price by the standards we herein establish, in conformity with the principle applicable to an appraisal—that fair value be determined by taking 'into account all relevant factors.' In our view this includes the elements of rescissory damages if the Chancellor considers them susceptible of proof and a remedy appropriate to all the issues of fairness before him.").

117. *Id.* at 704.

118. *See e.g.*, George S. Geis, *An Appraisal Puzzle*, 105 NW. L. REV. 1635, 1644 (2011) (footnotes omitted) ("Among other reforms, *Weinberger* established appraisal as a primary legal framework for checking abusive freezeouts. It also replaced an overly formalistic and outdated judicial valuation methodology with a more flexible and realistic approach. These reforms, perhaps combined with an increase in freezeout mergers, soon led to a new wave of appraisal proceedings.").

Following *Weinberger*, Delaware courts appeared reluctant to invoke quasi-appraisal as an equitable remedy. Yet, Delaware courts continued to clarify the duty of disclosure requirements necessary to avoid quasi-appraisal proceedings. The Delaware Supreme Court noted that when investors face an investment decision such as deciding whether to seek appraisal, the "[t]he directors of a Delaware corporation are required to disclose fully and fairly all material information within the board's control."[119] The materiality standard applies to information if "there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote."[120] In the case of omitted information, there must be "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[121]

Quasi-appraisal found new life in 1991 when the Court of Chancery denied injunctions in *In re Ocean Drilling & Exploration Co. Shareholders Litigation*[122] and *Steiner v. Sizzler Restaurants International, Inc.*[123] but allowed plaintiffs in both cases to seek quasi-appraisal. In both cases, quasi-appraisal was permitted due to the time pressure of expediting decisions on the motions to enjoin the mergers and the findings that neither instance involved material deficits in disclosure which merited an injunction.[124] However, Chancellor Allen noted in *Steiner* that corrective disclosure, if provided prior to corporate action, would be the preferred remedy to "counter-factual determinations (i.e.,

119. Malone v. Brincat, 722 A.2d 5, 12 (Del. 1998).

120. Rosenblatt v. Getty Oil Co., 493 A.2d 929, 944 (Del. 1985) (quoting TSC Industries, Inc. v. North-way, Inc., 426 U.S. 438, 449 (1976)).

121. *Id.*

122. *In re* Ocean Drilling & Expl. Co. S'holders Litig., CIV. A. No. 11898, 1991 WL 70028 (Del. Ch. Apr. 30, 1991).

123. Steiner v. Sizzler Rests. Int'l., Inc., C.A. No. 11994, 1991 WL 40872 (Del. Ch. Mar. 19, 1991).

124. *See, e.g.*, Robert B. Schumer et al., *Quasi-Appraisal: The Unexplored Frontier of Stockholder Litigation*, 12 M&A J., no. 2, at 2. https://www.paulweiss.com/media/103314/7719347_1.pdf [https://perma.cc/Z4GF-FBDA] ("Each merger was a *fait accompli* from the perspective of the stockholder vote. Thus, there was both little practical value in a disclosure-based injunction and too little time to make the close call of whether the marginal disclosure claims presented justified an injunction. . . . [a]s discussed below, these circumstances were unique and do not provide a sufficient basis to expand the doctrine of quasi-appraisal.").

what would have happened if disclosure had been made) and damage or quasi-appraisal calculation."[125] Thus, both cases are noteworthy for their expansion of the quasi-appraisal remedy in post-closing proceedings where the plaintiffs would not suffer significant "irreparable harm"[126] or "irreparable injury."[127] However, they provide limited additional protections or remedies for shareholders based on unique situations where time pressures forced the Court of Chancery to expedite proceedings and avoid deciding on impractical merger injunctions.

While not a quasi-appraisal decision, *Glassman v. Unocal Exploration Corporation* established quasi-appraisal as an appropriate remedy for duty of disclosure violations following short-form mergers. As noted previously,[128] *Glassman* determined that absent fraud or illegality and subject to full disclosure, appraisal is the exclusive remedy for shareholders dissenting from a short-form cash-out merger in Delaware.[129] Therefore, *Glassman* eliminated the need for the controlling shareholder to establish entire fairness in favor of "a simple, fast and inexpensive process for accomplishing a merger" that the Delaware Supreme Court considered to be consistent with "the truncated process authorized by § 253."[130] Yet, because closing would occur at the time of the short-form merger, the decision paved the way for quasi-appraisal as a post-closing remedy for violations of a parent corporation's duty of disclosure.[131] It remains to be seen how quasi-appraisal proceedings

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125. *Steiner*, 1991 WL 40872, at *3.
126. *Ocean Drilling*, 1991 WL 70028, at *7.
127. *Steiner*, 1991 WL 40872, at *2.
128. *See supra* Part I.B.
129. Glassman v. Unocal Expl. Corp., 777 A.2d 242, 248 (Del. 2001).
130. *Id.* at 247–48.
131. *See, e.g.*, Geis, *supra* note 118, at 1648 (emphasizing that quasi-appraisal emerged as a judicial response to problems created by the combination of DGCL Section 253 and the new *Glassman* standard of review). While some have noted that this decision benefited minority shareholders, others have warned of the potential for further manipulation of minority shareholders by the majority. *Compare*, Stanley Onyeador, Note, *The Chancery Bank of Delaware: Appraisal Arbitrageurs Expose Need to Further Reform Defective Appraisal Statute*, 70 VAND. L. REV. 339, 343 (2017) (footnote omitted) ("Target shareholders in short-form mergers retain appraisal as an absolute remedy because such transactions substitute procedural rigor for efficiency, justifying value insurance of minority shares for which the market does not always provide an accurate valuation."), *with* Geis, *supra* note 118, at 1644 (footnotes omitted) ("While freezeout mergers can promote efficient and desirable outcomes, they also forge a

should be structured when a parent corporation violates its duty of full disclosure following a short-form merger.[132]

B. QUASI-APPRAISAL: TO REQUIRE PLAINTIFFS TO OPT-IN OR OUT?

In a notable pre-*Glassman* opinion, quasi-appraisal was invoked as an equitable remedy to alleviate a violation of DGCL Section 262 on an opt-out basis. In *Nebel v. Southwest Bancorp, Inc.*,[133] the Court of Chancery allowed a minority shareholder who had not sought appraisal to challenge a short-form merger on the grounds that the defendant corporation, which owned 91.68% of the target's shares prior to the DGCL Section 253 merger, failed to provide a proper copy of the appraisal statute.[134] The court found this to be a material misdisclosure and a statutory violation and while stopping short of allowing rescissory damages or invalidating the merger, the court determined quasi-appraisal was the appropriate remedy for the minority shareholders.[135] In a parallel appraisal proceeding conducted on an opt-out basis, the court determined that plaintiffs were entitled to the difference between the merger consideration received and the fair value of their shares, an increase from $41 to $85 per share.[136] This provided a significant recovery for the plaintiffs and a formal recognition of the harms that minority plaintiffs could suffer from flawed disclosure and improper appraisal calculations.

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powerful weapon for majority shareholders interested in taking advantage of minority owners.").

132. *See In re* Orchard Enters., Inc. Stockholder Litig., 88 A.3d 1, 49–50 (Del. Ch. 2014) (discussing *Glassman*, 777 A.2d at 248).

133. Nebel v. Sw. Bancorp, Inc., Civ. A. No. 13618, 1995 WL 405750, (Del. Ch. July 5, 1995).

134. *Id.* at *1, *6–7, (stating that although the corporation notified the stockholders of the record date and availability of shares for appraisal, the corporation had violated DGCL Section 262(d)(1) because the last page of the Delaware appraisal statute attached to the notice was in fact a statute from another state).

135. *Id.*; *see also* Nebel v. Sw. Bancorp Inc., No. Civ. A. 13618, 1999 WL 135259, at *8 (Del. Ch. Mar. 9, 1999) (discussing previous ruling and ruling on motions to dismiss claims presented in the second amended complaint).

136. Nebel v. Sw. Bancorp Inc., 1999 WL 135259, at *8. This increase likely reflected a flawed appraisal proceeding which determined the "fair market value" of the minority shares rather than the value of the company as a going concern and the pro-rata percentage owned by the minority shareholders. *Id.* at *2 n.3.

Nearly ten years later, in a post-*Glassman* opinion, the Court of Chancery invoked quasi-appraisal in *Gilliland v. Motorola, Inc.* on an opt-in basis.[137] In *Gilliland*, Motorola, Inc. (Motorola) failed to provide financial information in a short-form merger notice sent to the minority shareholders of Next Level Communications (Next Level), following Motorola's acquisition of Next Level's shares.[138] However, Motorola conducted a first-step tender offer and argued that it met its full duty of disclosure because the "total mix" of recently published financial information, including financial information of Next Level provided during its first-step tender offer, was sufficient so that no additional financial information was necessary in the short-form merger notice.[139] Vice Chancellor Lamb rejected this argument and ruled that a parent corporation must completely disclose all material facts relevant to the minority stockholders' decisions whether to accept the merger consideration or to seek appraisal, including substantive financial information relating to the value of the target company, in the short-form merger notice provided.[140] However, Vice Chancellor Lamb crafted the quasi-appraisal remedy on an opt-in basis for minority shareholders and required the plaintiffs to place $0.14 per share of their merger consideration into escrow to join the class action seeking appraisal.[141] In doing so, Vice Chancellor Lamb distinguished the disclosure violations of *Nebel* and stated that the plaintiffs' opt-out "solution distorts the traditional risk/reward tradeoff found in a statutory appraisal and puts Motorola in an inequitable position not justified by the facts in this case."[142] *Gilliland*, thus, provides further clarification as to the duty of disclosure requirements of controlling shareholders in short-form mergers, but left questions remaining as to when quasi-appraisal should mirror *Gilliland* or *Nebel*, and again how closely a quasi-appraisal remedy should mirror the mandated requirements of DGCL Section 262.

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137. Gilliland v. Motorola, Inc., 873 A.2d 305, 313 (Del. Ch. 2005).

138. *Id.* at 307–08 (explaining how Motorola had initially acquired 88% of Next Level Communications in a first step tender-offer ending on April 2003, and then converted a portion of its preferred stock to common stock prior to completing a short-form merger pursuant to DGCL Section 253).

139. *Id.* (noting how Motorola had met the other statutory requirements of DGCL Section 262).

140. *Id.*

141. *Id.* at 313–14.

142. *Id.* at 315.

The Delaware Supreme Court addresses these issues en banc in *Berger v. Pubco Corp.* when it tailored a *Nebel* style quasi-appraisal remedy and stated that "the quasi-appraisal remedy for a violation of th[e] fiduciary disclosure obligation[]should not be restricted by opt in or escrow requirements."[143] *Berger* involved a "going private" transaction in which Pubco's president, Robert H. Kanner, owned over 90% of Pubco's shares and cashed out its minority shareholders for $20 per share.[144] The Court of Chancery ruled that Kanner committed two separate disclosure violations by: (1) attaching the wrong appraisal statute and (2) not discussing the method used to determine the $20 consideration offered,[145] and ordered Kanner to provide supplemental disclosures while ordering a *Gilliland* style quasi-appraisal remedy.[146] Affirming the separate disclosure violations, the Delaware Supreme Court ruled that the "practicality of implementation and fairness to the litigants" warranted reversal of the Court of Chancery's decision to apply opt-in and escrow requirements for quasi-appraisal.[147] Furthermore, the court stated that "majority stockholders that deprive their minority shareholders of material information should forfeit their statutory right to retain the merger proceeds payable to shareholders who, if fully informed, would have elected appraisal,"[148] and did not require those seeking quasi-appraisal to make a demand through their record holders at the time of the merger.[149]

Berger v. Pubco is particularly noteworthy for the way in which the Delaware Supreme Court justified its remedy. The court specified that quasi-appraisal need not directly replicate DGCL Section 262 statutory protections, and could be adjusted to resemble a statutory appraisal with variations to account for a balancing of the equities.[150] Nevertheless, the court went so far as to say that "where there is a breach of the duty of

143. Berger v. Pubco Corp., 976 A.2d 132, 145 (Del. 2009).

144. *Id.* at 134.

145. *Id.* at 135–36 (discussing Berger v. Pubco Corp., Civil Action No. 3414–CC, 2008 WL 2224107, at *3 (Del. Ch. May 30, 2008)).

146. Berger v. Pubco Corp., Civil Action No. 3414–CC, 2008 WL 2224107, at *5 (Del. Ch. May 30, 2008) (requiring both an opt-in and escrow requirement), *rev'd*, 976 A.2d 132 (Del. 2009).

147. *Berger*, 976 A.2d at 136, 140.

148. *Id.* at 144.

149. *Id.* at 141.

150. *Id.* at 142 n.27, 145.

disclosure in a short form merger, the Gilliland approach does not appropriately balance the equities."[151] The court justified this statement by noting that because the opt-out requirement would be more beneficial to minority shareholders by avoiding the risk of forfeiture, and neither the opt-out nor opt-in requirement would be more burdensome to the majority shareholder,[152] that an opt-in requirement was the proper remedy.[153] Further, while not requiring minority shareholders to escrow a portion of their consideration might confer the "dual benefit" of retaining the merger proceeds while pursuing a class action, that "[t]he appraisal statute should be construed even-handedly" and the majority shareholder should be held accountable for violations of DGCL Section 253.[154] A significant progression from the humble origins of quasi-appraisal, *Berger* emphasized that majority shareholders would be deprived of the benefits of DGCL Section 253 if they materially violated the duty of disclosure in short-form mergers.

C. A Remedy or a Cause of Action?

While *Berger v. Pubco* signaled the potential for an increased risk of litigation following short-form mergers, quasi-appraisal relief remains a rarely invoked equitable remedy. In fact, Delaware courts emphasized that "quasi-appraisal is not itself a cause of action, but is instead a remedy that, where appropriate, awards stockholders damages based on the going-concern value of their previously owned stock upon a finding of a breach of fiduciary duty, such as the duty to disclose."[155] Post-*Berger* opinions provide further elucidations of additional issues that can evade quasi-appraisal proceedings. For instance, in *Houseman v. Sagerman,* the Court of Chancery denied a quasi-appraisal remedy based on the doctrine of laches—which prevents the enforcement of delayed legal claims if they

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151. *Id.* at 145.

152. *Id.* at 143 (noting that the majority shareholders would easily know the members of the plaintiff class at an early stage regardless of an opt-in or opt-out requirement).

153. *Id.*

154. *Id.* at 144. Although the court crafted a *Nebel* style quasi-appraisal remedy, it recognized that a *Gilliland* style quasi-appraisal remedy may still be appropriate in cases involving a "technical and non-prejudicial violation" of DGCL Section 253. *Id.* at 145.

155. Houseman v. Sagerman, C.A. No. 8897–VCG, 2015 WL 7307323, at *4 (Del. Ch. Nov. 19, 2015) (citing *In re* Orchard Enters., Inc. Stockholder Litig., 88 A.3d 1, 42 (Del. Ch. 2014)).

prejudice defendants—and the difficulty of producing information to craft a quasi-appraisal remedy after ruling that the plaintiffs would otherwise be entitled to one.[156] These additional concerns further emphasize the limited opportunity for minority shareholders to avail themselves of the quasi-appraisal remedy. While originally interpreted as a landmark plaintiff-friendly opinion with the potential to change appraisal law, *Berger* likely did not open the floodgates of quasi-appraisal and merely serves as a reminder of the importance of proper disclosure in DGCL Section 253 mergers.

Furthermore, the standard for a breach of the duty of disclosure remains a significant hurdle for plaintiffs to avail themselves of the quasi-appraisal remedy. This is magnified by the increased scrutiny Delaware courts place over post-closing disclosure claims. Recently, *Nguyen v. Barrett*,[157] which involved an alleged omission of information related to unlevered free cash flows and the compensation contingency for a financial advisor who advised the acquiring company prior to a DGCL Section 251(h) merger, reaffirmed the narrowing opportunity for plaintiffs to challenge mergers.[158] In *Nguyen,* the plaintiffs added a "count" of quasi-appraisal to their second amended complaint following a merger pursuant to DGCL Section 251.[159] The court found that "a disclosure that does not include all financial data to make an independent determination of fair value is not . . . per se misleading or omitting a material fact" and would not rise to the level of a material omission which could result in a quasi-appraisal remedy.[160] Since plaintiffs must prove "at trial that the defendants committed a non-exculpated breach of the fiduciary duty of disclosure, then damages can be awarded using a quasi-

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156. *Id.* at *10–12.

157. Nguyen v. Barrett, C.A. No. 11511–VCG, 2016 WL 5404095 (Del. Ch. Sept. 28, 2016).

158. *See, e.g.*, Warren S. de Wied, *Narrow Path for Success of Post-Closing Disclosure Claims*–Nguyen v. Barrett, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (Nov. 2, 2016), https://corpgov.law.harvard.edu/2016/11/02/narrow-path-for-success-of-post-closing-disclosure-claims-nguyen-v-barrett/ [https://perma.cc/27YX-L448] (noting the difficulty plaintiffs face in bringing disclosure claims post-closing and the narrowing window to challenge merger transactions post-closing).

159. *Nguyen*, 2016 WL 5404095, at *2.

160. Nguyen v. Barrett, Civil Action No. 11511–VCG, 2015 WL 5882709, at *4 (Del. Ch. Oct. 8, 2015) (quoting *In re* CheckFree Corp. S'holders Litig., Civil Action No. 31393–CC, 2007 WL 3262188, at *2 (Del. Ch. Nov. 1, 2007)), *appeal denied*, 2015 WL 5924668, at *1 (Del. Oct. 9, 2015).

appraisal measure,"[161] the standard remains significantly burdensome for minority shareholders to present post-closing damages claims following DGCL Section 253 mergers.

The burdensome standard for post-closing damages claims following DGCL Section 253 mergers is apparent in the Court of Chancery's recent denial of a minority shareholder's request for quasi-appraisal in *In re United Capital Corp. Stockholders Litigation*.[162] *In re United Capital* involved a DGCL Section 253 "going private" transaction by a controlling shareholder who appointed an independent special committee that set the merger price at $32, and provided recent financial statements, management's analysis of the financial statements, background information on the merger, and disclosures about potential board conflicts.[163] The plaintiff challenged the merger on the grounds that the merger notice omitted information about the company's reasoning for the merger price, financial valuation protections, the process undertaken by the special committee, and potential conflicts involving the directors.[164] The merger price was noteworthy because it was $7 below the share price on the announcement date and was determined without the use of financial advisors.[165] However, the court dismissed the action because the plaintiff failed to plead that the disclosures were inadequate, and further denied quasi-appraisal on the grounds that "none of [p]laintiff's alleged omissions [we]re material to the decision of whether to seek appraisal in light of the abundant disclosures already provided."[166] Further, the court found that the plaintiff had enough information to determine that he might not be able to "trust the merger price" and therefore "stockholders ha[d] all the information necessary to decide whether to seek appraisal."[167] The case is noteworthy in emphasizing the difficulty for plaintiffs pleading duty of disclosure violations and the rarity of quasi-appraisal equitable relief. While the court noted that the shareholders had enough information

161. Chen v. Howard-Anderson, 87 A.3d 648, 691 (Del. Ch. 2014).

162. *In re* United Capital Corp. Stockholders Litig., C.A. No. 11619–VCMR, 2017 WL 389520 (Del. Ch. Jan. 4, 2017).

163. *Id.* at *2.

164. *Id.* at *1.

165. *Id.* at *2 (noting that the controlling shareholder had originally announced a merger price of $30 per share, but negotiated with the independent special committee and raised the consideration to $32 per share).

166. *Id.* at *4.

167. *Id.* at *8.

to distrust the merger price, the case emphasizes that the controlling shareholder need not provide enough information for an independent assessment of the value of the minority shares.[168]

Creative pleadings that avoid characterizing quasi-appraisal claims as breaches of the fiduciary duty of disclosure face similar challenges in surpassing the pleading stage. Oftentimes these claims have the significant burden of overcoming the threshold exculpatory provision of DGCL Section 102(b)(7) which exculpates director's monetary liability for breaches of the duty of care.[169] For instance, in *In Re Cyan, Inc. Stockholders Litigation*, plaintiffs brought post-closing claims alleging that Cyan's board breached its fiduciary duties by making material omissions and misstatements in proxy materials that were issued prior to being acquired by Ciena Corporation in a mostly stock-for-stock transaction,[170] and sought quasi-appraisal as an independent claim.[171] The plaintiffs argued that their "equitable claim [wa]s for frustration of the statutory right of appraisal, not breach of fiduciary duty" and that because appraisal is statutory, that a failure to provide information sufficient to decide whether to seek appraisal should be evaluated independently from breach of fiduciary duty claims.[172] The plaintiffs also argued that Cyan

168. The court noted that "in a short-form merger, the minority stockholders are not entitled to all facts material to their own valuation assessment." *Id.* at *7, (citing Berger v. Pubco Corp., Civil Action No. 3414–CC, 2008 WL 2224107, at *3 (Del. Ch. May 30, 2008)).

169. DGCL Section 102(b)(7) provides in part that a Delaware certificate of incorporation may contain a "provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision shall not eliminate or limit the liability of a director: (i) For any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law." DEL. CODE ANN. tit. 8, § 102(b)(7) (West 2015).

170. Notably, the plaintiffs alleged that: (1) the board materially misled its shareholders regarding financial advisor Jefferies LLC's potential conflict in providing advice on the transaction as an owner of $5.5 million of Cyan's 8% convertible notes; (2) the board failed to disclose the significance of revenues from its largest customer, Windstream; (3) the board failed to disclose Jefferies LLC's precedent transaction that appeared in the appendix of a PowerPoint presentation Jefferies provided to the board. *In re* Cyan, Inc. Stockholders Litig., C.A. No. 11027–CB, 2017 WL 1956955, at *12–16 (May 11, 2017).

171. *Id.* at *1.

172. *Id.* at *17.

acted in bad faith by not providing a supplement to the proxy materials after receiving a letter from plaintiffs' counsel seeking further information to help determine whether to seek appraisal.[173] Citing *Corwin*'s safe harbor for fully informed, uncoerced votes by a majority of disinterested shareholders, and stating that the plaintiffs failed to plead a non-exculpated breach of fiduciary duty, the court dismissed the breach of fiduciary claims on two independent grounds.[174] Furthermore, the court denied the plaintiffs' request for quasi-appraisal and reinforced the holding from *In re Orchard Enterprises, Inc. Stockholder Litigation* that quasi-appraisal is "simply a form of remedy" and not an independent cause of action that could be assessed separately from the duty of disclosure claims to circumvent DGCL Section 102(b)(7) and *Corwin*.[175] While quasi-appraisal is clearly permitted as a form of remedy and not as a cause of action, *In re Cyan* emphasizes both the difficulty that plaintiffs face in determining whether to seek appraisal and the limited recourse available when challenging disclosure or seeking equitable relief post-closing.

IV. PROPOSALS FOR REFORM

In re United Capital Corp. and current trends in merger litigation—that limit plaintiff's abilities to recover post-closing damages and provide greater deference to controlling shareholders—reflect the significant burdens minority shareholders face in recovering for alleged violations of a controlling shareholder's duty of disclosure. Furthermore, as some commentators note, appraisal is an ineffective mechanism of deterring opportunistic majority shareholder behavior that takes advantage of minority shareholders.[176] This problem is magnified in the context of short-form mergers under DGCL Section 253 because of the difficulties minority shareholders face in assessing the value of their shares, and the

173. *Id.* at *11.

174. *Id.*

175. *Id.* at *17.

176. *See, e.g.*, Charles Korsmo & Minor Myers, *Reforming Modern Appraisal Litigation,* 41 DEL. J. CORP. L. 279, 331 n.196 (2017), (noting that "a basic problem with appraisal as a mechanism of deterrence is that there is a natural limit to the number of shares that can dissent. In a long-form merger or a tender offer, realistically not more than 50% could conceivably demand appraisal, and in a short-form merger not more than 10% could dissent").

likelihood of under-enforcement of opportunistic manipulation by a controlling shareholder.[177] Under DGCL Section 253, short-form mergers are deemed effective before any disclosure is made to minority shareholders and thus must exist in the post-*Trulia* and *Corwin* world where controlling shareholders limit discovery pre-closing and post-closing claims are subjected to heightened scrutiny.[178]

While appraisal arbitrage is a problematic phenomenon, it is likely addressed with the most recent amendments to DGCL Section 262 and the *SWS*, *Clearwire*, and *DFC Global* decisions.[179] For that reason, controlling shareholders can bet on the fact that significantly less than ten percent of the minority shareholders will seek appraisal. Therefore, they are incentivized to offer less of a merger price as the controlling shareholder did in *In re United Capital Corp*.[180] Due to the vague nature of the current materiality standard, shareholders are often forced to decide whether to seek appraisal with limited independent ability to value their shares. Furthermore, controlling shareholders have an incentive to disclose information that portrays the merger price offered in the way

177. Chief Justice Strine of the Delaware Supreme Court recognized that minority shareholders can be inherently disadvantaged by information asymmetries, timing disadvantages, and the potential for coercion and unfairness by controlling shareholders when making decisions to tender or seek appraisal. *See In re* Pure Res., Inc. S'holders Litig., 808 A.2d 421, 450 (Del. Ch. 2002).

178. *See supra* Parts II.A.–B.

179. *See* Jack B. Jacobs, *Pushbacks and Delaware Appraisal Arbitrage*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (June 28, 2016) https://corpgov.law.harvard.edu/2016/06/28/pushbacks-and-delaware-appraisal-arbitrage/ [https://perma.cc/626Q-P4XJ] (noting how the *de minimis* exception and implications from *Dell* that the surviving corporation will be able to ascertain whether a purchased block of shares voted in favor of the merger will decrease the risk for appraisal arbitrage and lessen appraisal claims filed).

180. *See* Jay B. Kesten, *The Uncertain Case for Appraisal Arbitrage*, 52 WAKE FOREST L. REV 89, 129 (2017) (noting that "in most cases it is likely rational and cost effective to offer a lower price to the majority or at least not raise one's bid and set aside an 'appraisal reserve' for any potential dissenters") (citation omitted); *contra* Brian Broughman et al., Merger Negotiations in the Shadow of Judicial Appraisal 19 (Sept. 27, 2017) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3039040 [https://perma.cc/54DN-J56P] (finding that "[b]idders acquiring a Delaware target do not appear to lower their price in response to events that increase the threat of appraisal").

most advantageous to them.[181] This is particularly noticeable when the merger price deal premium is significantly less than average.[182] The *In re United Capital Corp.* case thus serves as an example of an instance where quasi-appraisal should be expanded to ensure that controlling shareholders adhere to their duty of disclosure and do not unfairly disadvantage minority shareholders.

This Part proposes several potential adjustments to the quasi-appraisal remedy, and discusses the implications of (1) recognizing quasi-appraisal as a cause of action after altering disclosure requirements to ensure that quasi-appraisal need only to be invoked in the most egregious forms of duty of disclosure violations, (2) mandating that quasi-appraisal actions be conducted on an opt-out basis, and (3) adding punitive damages to quasi-appraisal actions to deter controlling shareholder opportunism.

A. Reassessing Quasi-Appraisal as an Independent Cause of Action

Recognizing quasi-appraisal damages as an independent post-closing cause of action in DGCL Section 253 mergers would have a significant effect on plaintiffs' abilities to recover from controlling shareholders' violations of their duty of disclosure. Not only would controlling shareholders be required to provide the DGCL Section 262 mandated information to minority shareholders, they would also need to ensure that all provided information permits shareholders to properly consider the alternatives of seeking appraisal for their shares. In this way, the disclosure requirement could be strengthened to require that stockholders "be given all the financial data they would need if they were

181. *See In re* Dole Food Co. Stockholder Litig., C.A. No. 8703–VCL, 2015 WL 5052214, at *1–2, *29–32 (Del. Ch. Aug. 27, 2015) (discussing management earnings manipulation prior to a management buyout and finding that management intentionally undermined projections made in disclosure materials).

182. *See US M&A News and Trends*, FactSet (July 2017), https://www.factset.com/mergerstat_em/monthly/US_Flashwire_Monthly.pdf [https://perma.cc/D63W-XZ3W] (reporting a median deal premium between 24% and 50% between the second quarters of 2015 and 2017); *see also* Broughman et al., *supra* note 180 (manuscript at 2) (finding that "shareholders of Delaware targets receive marginally higher acquisition premiums following events that strengthen the appraisal remedy").

making an independent determination of fair value."[183] Additional disclosure would be easy to provide and would ensure that minority shareholders had an ability to independently determine the value of their shares and decide whether to seek appraisal.[184]

In instances where minority shareholders opted not to seek appraisal and suffered "irreparable harm" from controlling shareholder misrepresentations or omissions, they would have a cause of action which would ensure sufficient discovery and disclosure after the pleadings stage. Since plaintiffs who could plead with particularity that they had suffered "irreparable harm" would avail themselves of an approximation of an appraisal proceeding at earlier stages of litigation, they could avoid discovery restraints and early dismissal of meritorious claims that affected their decision whether to seek appraisal. Although this would likely increase the incentive for disclosure-only settlements, heightened judicial scrutiny in the post-*Trulia* world would ensure that only those supplemental disclosures that remedied previously material omissions or misrepresentations would be appropriate. Thus, these supplemental disclosures would likely qualify as "plainly material" for purposes of the *Trulia* standard. With these additions, quasi-appraisal would rarely need to be invoked and would only be appropriate in the most egregious duty of disclosure violations. Furthermore, Delaware would be able to limit informational asymmetries and the potential for coercive or opportunistic behavior by controlling shareholders in DGCL Section 253 mergers.

B. Mandating that Quasi-Appraisal Be Conducted on an Opt-out Basis

Quasi-appraisal is traditionally invoked as a remedy when a fiduciary breaches its duty of disclosure in a transaction which involves a vote, not one that is statutorily available to expedite proceedings.[185] Although it is

183. *See* Skeen v. Jo-Ann Stores, Inc., 750 A.2d 1170, 1174 (Del. 2000) (expressly rejecting the expanded disclosure standard because it was not sufficient for the plaintiffs to "merely allege that the added information would be helpful in valuing the company").

184. *See* Korsmo & Myers, *supra* note 176, at 336–38 (discussing the standard rejected in *Skeen* as the appropriate disclosure standard to ensure proper disclosure which would be easily facilitated by corporations and would benefit the private enforcement system of duty of disclosure violations).

185. *See, e.g.*, *In re* Orchard Enters., Inc. Stockholder Litig., 88 A.3d 1, 42 (Del. Ch. 2014) ("One cause of action where the Delaware Supreme Court and the Court of

invoked frequently in the DGCL Section 253 short-form merger context, it is applied with limited uniformity. Therefore, in DGCL Section 253 proceedings where minority shareholders are denied the protection of a vote, they should be entitled to opt-out class-certification and lesser demand requirements for quasi-appraisal damages when a controlling shareholder breaches its duty of disclosure. These adjustments would be in line with the Delaware Supreme Court's decision in *Berger v. Pubco Corp.*, and would reflect that minority shareholders should have the opportunity to be compensated for the loss of their equity as a going concern. These remedies would mirror those available after a long-form merger (which similarly do not require an opt-in or an escrow requirement to challenge transactions) and would ensure that plaintiffs recover from controlling shareholders' most egregious duty of disclosure violations.

C. Making Quasi-Appraisal Remedies Punitive

The current use of quasi-appraisal inadequately protects minority shareholders in DGCL Section 253 mergers. This is because a violation of a controlling shareholder's duty of disclosure that results in "irreparable harm" resembles compensatory damages with no deterrent effect. While *Gilliland v. Motorola, Inc.* sought to equate opt-out, no escrow requirement, quasi-appraisal remedies with a procedural windfall to the plaintiffs, the rarity of quasi-appraisal should guarantee that when minority shareholders are "irreparably harmed," controlling shareholders are held accountable for violating their duty of disclosure. As *In re Dole Food Co.* serves as a cautionary tale for management manipulation of minority shareholders in a management buyout, its deterrent effect could be strengthened via the availability of a multiplied factor of damages akin to treble damages in the antitrust context. This damage multiple might only be available in cases like *Berger v. Pubco Corp.* where minority shareholders are blatantly deprived of the ability to determine the value of their shares and there exists a clear violation of the statutorily mandated

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Chancery consistently have held that quasi-appraisal damages are available is when a fiduciary breaches its duty of disclosure in connection with a transaction that requires a stockholder vote. The premise for the award is that without the disclosure of false or misleading information, or the failure to disclose material information, stockholders could have voted down the transaction and retained their proportionate share of the equity in the corporation as a going concern. Quasi-appraisal damages serve as a monetary substitute for the proportionate share of the equity that the stockholders otherwise would have retained.").

requirements under DGCL Section 262. This would ensure that the private enforcement system for violations of the duty of disclosure properly addresses instances where controlling shareholders made material misrepresentations or omissions that significantly impacted minority shareholders' decisions regarding appraisal.

CONCLUSION

This Note analyzes how recent amendments to the DGCL and current trends in merger and appraisal litigation present an apt opportunity to expand the role of quasi-appraisal as an equitable remedy following DGCL Section 253 mergers in Delaware. Because of the challenges associated with minority ownership of corporations and potential abuse by controlling shareholders, this piece addresses making quasi-appraisal an independent cause of action, expanding disclosure requirements to ensure that minority shareholders can conduct independent valuations of their shares, mandating that quasi-appraisal remedies be available on an opt-out basis, and making egregious violations of the duty of disclosure subject to punitive damages. While these proposals are by no means an exhaustive effort to reform appraisal litigation, they provide a baseline to ensure proper disclosure and to deter controlling shareholder misconduct of DGCL Section 253. Minority shareholders who are "cashed out" should have the opportunity to independently assess the value of their shares prior to deciding whether to seek appraisal and should be entitled to appropriate damages if a controlling shareholder violates its duty of disclosure. For that reason, these efforts seek to guarantee that quasi-appraisal be invoked to ensure that minority shareholders are "cashed out" in the most fair and practical way possible.