

June 20, 2016

Amendments to Delaware General Corporation Law Will Affect Appraisal Actions and “Intermediate-Form” Mergers

On June 16, 2016, Delaware Governor Jack Markell signed into law House Bill 371, which amends the Delaware General Corporation Law (DGCL) with respect to, among other things, appraisal proceedings and “intermediate-form” mergers.

Specifically, the bill amends Section 262 of the DGCL to limit *de minimis* appraisal claims and to provide surviving corporations with the right to pay stockholders exercising appraisal rights prior to the time the Delaware Court of Chancery makes a final value determination, thereby limiting the amount of interest that would accrue on an appraisal award.

The legislation also clarifies the requirements and procedures relating to “intermediate-form” mergers under Section 251(h) of the DGCL, particularly those involving rollover of target equity.

The amendments will generally become effective on August 1, 2016. The amendments to Section 262 affecting appraisal proceedings will be effective only with respect to appraisal proceedings arising out of transactions consummated pursuant to agreements entered into on or after August 1, 2016 (or, in the case of mergers pursuant to Section 253 of the DGCL, resolutions adopted by a board of directors on or after August 1, 2016 or, in the case of mergers pursuant to Section 267 of the DGCL, authorizations provided on or after August 1, 2016). The amendments to Section 251(h) regarding intermediate-form mergers will be effective only with respect to merger agreements entered into on or after August 1, 2016.

Appraisal Actions

Under Section 262 of the DGCL, stockholders of any corporation that is acquired in certain merger or consolidation transactions may exercise appraisal rights, subject to certain exceptions and to compliance with specified procedural requirements. The new legislation amends Section 262(g) to provide that the Court of Chancery must dismiss an appraisal proceeding as to all stockholders who assert appraisal rights unless (a) the total number of shares entitled to appraisal exceeds 1% of the outstanding shares of the class or series eligible for appraisal, or (b) the value of the consideration provided in the merger or consolidation for such total number of shares seeking appraisal exceeds \$1 million, or (c) the merger was approved pursuant to Section 253 or Section 267 of the DGCL. These provisions thus prevent stockholders from demanding appraisal in cases where the number of their shares or the value of those shares is minimal. This *de minimis* exception applies only to shares that were listed on a national securities exchange immediately before the merger or consolidation.

Section 262(h) of the DGCL provides that, unless the Court of Chancery determines otherwise for good cause, interest on an appraisal award always accrues from the effective date of the merger through the date of payment of the appraisal award at a rate of 5% over the Federal Reserve discount rate, compounded quarterly. Of course, surviving corporations already have the ability to propose agreements with appraisal petitioners to release all or a portion of the merger consideration and thereby to eliminate the running of statutory interest as to the amount released, but surviving corporations previously could not *require* appraisal petitioners to accept such payments. The legislation now amends Section 262(h) to give the surviving corporation the right to make a voluntary cash payment to stockholders seeking appraisal prior to the Court of Chancery’s final judgment regarding fair value, thereby reducing the amount of interest that accrues during the appraisal process. If the surviving corporation makes a prepayment, interest will accrue only on the sum of (i) the difference, if any, between the amount paid and the fair value of the shares as determined by the Court of Chancery and (ii) interest accrued before the prepayment, unless paid at the time of such prepayment. The

amount of any prepayment is in the sole discretion of the surviving corporation, and there is no inference that the amount paid by the surviving corporation is equal to, greater than, or less than the fair value of the shares to be appraised.

By providing surviving corporations the absolute right to prepay appraisal amounts and to cut off statutory interest, Delaware may have, at the margins, lessened the incentive for stockholders to bring or prolong appraisal actions.

Intermediate-Form Mergers

Section 251(h) of the DGCL provides a mechanism for an acquiror to consummate a two-step takeover (i.e., a tender offer to purchase a majority of the shares of a public company followed by a second-step merger to acquire the remaining shares not tendered in the offer) without the need to obtain shareholder approval on the second-step merger, thereby avoiding the cost and delay involved in preparing and distributing a Schedule 14C information statement prior to the shareholder vote on the second-step merger. The amendments implemented by the legislation resolve various interpretive and practical issues that had arisen in connection with implementation of transactions structured to comply with Section 251(h), particularly those involving rollover of target equity.

The legislation clarifies that Section 251(h) is applicable to a corporation that has a class or series of stock listed on a national securities exchange or held of record by more than 2,000 holders immediately prior to the execution of the merger agreement, even if not all classes or series of stock of such corporation are so listed or held. The amendments also clarify that the offer for a target corporation's stock may be consummated pursuant to separate offers for separate classes or series of stock.

In addition, the amendments to Section 251(h)(3) provide that, for purposes of determining whether the acquiror holds sufficient shares to approve the merger, it may include any rollover stock (defined below) and shares of stock of the target corporation held by any person that owns, directly or indirectly, all of the outstanding stock of the offeror, or that is a direct or indirect wholly-owned subsidiary of such person or persons (collectively, offeror affiliates). "Rollover stock" is defined as any shares of stock of the target corporation that are the subject of a written agreement requiring such shares to be transferred, contributed or delivered to the offeror or any offeror affiliate in exchange for stock or other equity interests in the offeror or any offeror affiliate, so long as such shares are in fact so transferred, contributed or delivered before the effective time of the merger. The amendments also clarify the circumstances under which certificated and uncertificated shares of stock of the target corporation are deemed "received" for purposes of Section 251(h)(3).

The amendments to Section 251(h)(5) also provide that rollover stock and shares of the target corporation that are owned at the commencement of the offer by the target corporation, the offeror, and any of their direct or indirect wholly-owned subsidiaries, may be excluded from conversion in the merger into the right to receive the merger consideration.

Other Matters

Section 111 of the DGCL provides that any civil action to interpret, apply, enforce or determine the validity of the provisions of various instruments, documents or agreements may be brought in the Delaware Court of Chancery, except to the extent that a statute confers exclusive jurisdiction on a court, agency or tribunal other than the Court of Chancery. The amendments expand the Court of Chancery's jurisdiction to include civil actions involving any instrument, document or agreement (1) to which a corporation and one or more of its stockholders are parties, and pursuant to which one or more stockholders sells or offers to sell any stock of the corporation, or (2) by which a corporation agrees to sell, lease or exchange any of its property or assets, and which by its terms provides that one or more stockholders approve of or consent to such sale, lease or exchange.

The amendments also include technical changes regarding the quorum and voting requirements for board committees and subcommittees, the execution of stock certificates, and procedures to revoke dissolution or restore or revive a corporation's certificate of incorporation.

If you would like to learn more about the amendments to the DGCL, please contact your usual legal advisor at Ropes & Gray.