

Delaware Court: In Most Cases Appraisal is the Exclusive Remedy With Regard to a Short Form Merger

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Original Title: Delaware Court Reinforces Principle that in Most Circumstances Appraisal is the Exclusive Remedy in Connection With a Short Form Merger

On January 10, 2012, in the case of *In Re Appraisal of the Aristotle Corporation*, the Delaware Court of Chancery addressed an issue of first impression with respect to the standing of stockholders, who dissented to a short form merger under Section 253 of the Delaware General Corporation Law ("DGCL") and perfected their appraisal rights, to bring an additional claim alleging that the directors breached their fiduciary duty to disclose the material facts necessary for the stockholders to determine whether to seek appraisal.

In connection with a short form merger, the petitioners filed an appraisal action under Section 262 of the DGCL seeking the fair value of their shares. Despite the fact that the appraisal action was pending, on the eve of trial and eighteen months into their appraisal case, the petitioners filed a separate complaint for breach of fiduciary duty of disclosure in connection with the merger seeking the difference between the fair value of their shares and the price of the merger. The defendants moved to dismiss the fiduciary complaint for lack of standing.

Because there were no prior cases that squarely addressed this issue, the Court relied on its prior decision of *Andra v. Blount*, 772 A.2d 183 (Del. Ch. 2000) by analogy. There, the Court was faced with an action for breach of the duty of disclosure in connection with a tender offer, which culminated in a cash out of remaining shareholders through a short form merger. The plaintiff initially moved for expedited proceedings to enjoin the consummation of the tender offer until corrective disclosures were issued. Thereafter, the plaintiff withdrew her request to enjoin the tender offer and instead waited to bring a postclosing action for money damages in the form of an appraisal proceeding. After the short form merger was consummated, in which plaintiff refused to accept the merger consideration and preserved her appraisal rights, plaintiff renewed her fiduciary duty challenge to the disclosures. The Court ruled that plaintiff did not have standing to pursue her disclosure claim because she did not tender her shares and thus, could not have been injured by the allegedly misleading disclosures.

Importantly, the *Andra* Court noted that a different result might have been obtained if the plaintiff had timely sought to enjoin her disclosure claim *before* her decision to tender. This would have given the Court an opportunity to order corrective disclosures, a remedy that would inure to the benefit of all the stockholders contemplating the decision to tender. The Court refused to look at the potential injury to the other shareholders because the plaintiff withdrew her injunction motion through which she could have sought to demonstrate collective injury to other investors. Instead, plaintiff chose to press her disclosure claim only after the merger closed. As a result, the Court held plaintiff to the traditional standing requirement that she show individual injury as a result of the misleading disclosures—a burden plaintiff could not satisfy, because she chose not to tender.

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Relying on the reasoning in *Andra*, the Chancellor in the instant case ruled that the petitioners did not have standing to pursue their disclosure claim because the petitioners never sought to represent other investors, did not promptly seek to enjoin the merger and thus, did not suffer any cognizable individual injury that could be redressed by the Court of Chancery. The Court further found this to be particularly true because the relief sought in the fiduciary duty action is the same as the exclusive remedy afforded in a Section 262 appraisal action—a fair value determination.

The Chancellor reasoned that "when a litigant files a new claim that, if proven, would not entitle it to any relief that it does not already have a right to receive, that litigant in my view has no proper standing." In other words, the alleged disclosure inadequacies did not in any way impair the petitioners' ability to seek appraisal, and addressing the fiduciary duty claim could at best result in the petitioners' "right to a 'quasi' version of something they already possess in its actual form." Such a moot court determination, according to the Chancellor, would result in an advisory opinion, against which the Delaware Supreme Court has warned.

The Court further found that there was no need to evaluate the possibility of nominal damages in connection with the fiduciary duty action, because the petitioners' voting interests were not harmed, and they will receive a fair value determination in connection with the appraisal action.

This case is important to shareholders who seek appraisal in connection with a short form merger but also choose to bring a subsequent action for breach of the duty of disclosure in connection with merger. If the stockholder refuses to tender in connection with the short form merger, thereby preserving their appraisal rights, but fails to seek an injunction of the merger, he will not be able to demonstrate cognizable injury to bring a fiduciary action for breach of the directors' duty of disclosure *after* the closing of the short form merger transaction.

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Sheldon K. Rennie is a Partner with the National Firm of Fox Rothschild LLP. Sheldon has more than 10 years of experience representing national and international clients in the areas of Delaware corporate and business litigation and creditor's rights. He regularly practices in the Delaware Court of Chancery, the United States District Court for the District of Delaware and the Delaware Superior Court.

He is experienced in handling disputes among shareholders, members of boards of directors, general partners and members of limited liability companies. He regularly handles matters under the Delaware General Corporation Law involving corporate governance, fiduciary duties, challenges to the election of directors and actions for the inspection of corporate books and records.

Sheldon utilizes his experience in the Delaware Court of Chancery and knowledge of Delaware's entity statutes to provide strategic advice to clients on Delaware law regarding corporations, limited liability companies, limited partnerships and general partnerships.

In addition to his corporate and business litigation practice, Sheldon serves as local counsel in patent matters in the Delaware District Court and engages in title litigation, representing several title insurance companies.

Sheldon's recent representations include the following:

- Negotiated a successful buyout for a partner in a major financial firm where the partner was on the verge of a "squeeze-out".
- Successfully defended a large cosmetic company in a patent infringement trial, saving the client over \$20 Million.
- Successfully represented a board of directors in an action challenging the director's fiduciary duties and the proper constitution of the board.
- Successfully represented a title insurance company at trial where the homeowner asserted fraud in connection with the granting of a mortgage.

Sheldon also serves on the firm's Partner Advancement Committee.

Before Fox Rothschild

Sheldon served as a judicial law clerk for the Hon. William T. Quillen of the Superior Court of Delaware. At Villanova University School of Law, he was the Editor-in-Chief of the Environmental Law Journal. Sheldon was also the 1995 recipient of the Louis L. Redding Fellowship.

Beyond Fox Rothschild

Sheldon is an Adjunct Professor at Villanova University School of Law. He has also been appointed to the Lawyer's Advisory Committee of the Third Circuit Court of Appeals based upon recommendations by the District Court Judges in Delaware.

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