The appraisal remedy under US law

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INTRODUCTION

The State of Delaware is well-known for being the place of incorporation of most American and many international corporations. Nowadays, more than 1 million legal entities are incorporated in Delaware, including approximately 66% of all publicly-traded companies in the United States of America. Corporations choose Delaware for the place of their incorporation as this state is generally recognized as a state with a flexible and business-friendly corporate statute, an experienced and deeply rooted into America’s corporate case law business court and a business-friendly administration. Therefore, there is no more illustrative and suitable corporate law to be analyzed and discussed with regard to the appraisal remedy under US law.

Delaware’s outstanding reputation in the area of corporate statutes developed naturally at the end of the 19th century, during the industrial revolution. American corporations, evolved from entities pursuing public activities which the states were not able to provide by themselves, began to grow and had to adapt to the new economic reality and new requirements of the market. To be able to function in this new reality corporations had to introduce many changes into their structures and functioning. It was not so easy because at that time the generally recognized and acceptable rule was a rule of unanimous will of shareholders. In this way, a single shareholder was able to block any decision or change by using his veto power. To enable corporations an adaptation to the new reality, the rule of unanimity was replaced by majority rule. Granting the decision right to majority shareholders resulted in the necessity of protecting minority shareholders against majority’s decisions. That was a time when first appraisal statutes were provided for in US corporate law.

The appraisal remedy is a remedy at law granted to shareholders enabling them, under defined conditions (prerequisites), to dissent from consolidation, merger or other fundamental changes in a corporation accepted by a majority of shareholders and to receive a fair value of their shares of stock determined by a court. Thereby, minority shareholders are protected against fundamental changes in a corporation approved by a majority and are not forced to continue their investment in a corporation, considering they can leave a corporation in return for a fair value of their shares. At the same time, majority shareholders are not restricted from introducing changes to a corporation by dissenting minority. Nowadays, all fifty states provide for appraisal statutes to protect minority shareholders.
In this paper, titled “The appraisal remedy under US law” I will analyze appraisal rights as an instrument of protecting of minority shareholders in American law and I will answer the following research questions:

1. What is the nature and the goal of the appraisal remedy?
2. Will the newest amendment of the Delaware General Corporate Law change the application of appraisal rights?
3. Is the development of appraisal rights in the European Union necessary or rather redundant?

Chapter I focuses on theoretical deliberations about the appraisal remedy. In this part of the paper I will analyze the historical development of appraisal rights and discuss the reasons for which this remedy at law was introduced into American corporate law. Then, I will present several theories concerning a potential goal of appraisal rights and try to indicate the most accurate one.

In Chapter II, I will present and analyze Delaware’s appraisal statutes. I will focus on the scope of the appraisal remedy’s application, on eligible shares and on the appraisal procedure. I will also indicate the problem of fair valuation of dissenting shareholders’ shares and the exclusivity of the appraisal remedy.

Chapter III addresses appraisal arbitrage as an investment strategy. I will present the concept of appraisal arbitrage and the causes of the abuse of appraisal rights. Then, I will answer the second research question, whether the newest amendments to Delaware’s statute may address appraisal arbitrage and in which way.

Finally, in Chapter IV, I will analyze the European Union legislation paying special attention to appraisal rights and their forms in European company law itself and in Member States’ national legislation. Eventually, I will answer the question whether the introduction of appraisal rights, as regulated in the United States, is necessary or rather redundant.
Chapter I Appraisal rights as a shareholders’ remedy

1. Historical development of appraisal rights

The United States’ corporate law originates from contract rights, especially from those that arose from joint stock associations and partnerships. In one of its landmark decisions concerning corporate law in the United States, namely in the case Dartmouth College v. Woodward, the United States Supreme Court noted that shareholders’ rights are property rights in their nature and that legislative measures cannot undermine or vary those rights. The United States Supreme Court admitted the constitutional value of the rights of shareholders by directly saying that any right granted to a dissenting shareholder by a contract is protected by the United States Constitution.

The development of corporations in the United States and thereby corporate law began when the first corporations were chartered by legislative acts, as at that time were no statutes providing a procedure of incorporation of an entity. Those corporations were created in order to pursue activities of a public nature as the states did not have adequate resources to perform all their functions. The grants were given by the states to, among others, bridges, canals, mills and railroad companies. Although the companies were set up by the states to provide and develop public facilities for the general interest and they were, without any doubts, “the creatures of public policy”, the charters sometimes were considered as granting a privilege of monopoly or the power of indisputable province. The grants given to the companies by states explicitly specified the conditions under which construction would have had to be carried out, including the conditions concerning the maintenance of a finished facility ready to be used by a public (e.g. guarantee, terms of repair, etc.).

According to William J. Carney, the main factor contributing to enacting corporation statutes, which were supposed to provide an incorporation procedure, thereby to replace establishing companies by charters, was the development of the notion that states were entitled to make a reservation of their power to alter the contracts with the companies considered to be private enterprises. This notion was delivered by Justice Story in his

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4 Carney, supra note 1, at 83.
5 Id., at 83-84.
concurring opinion in the case Dartmouth College v. Woodward mentioned above. As the result of this judgment the process of adopting corporate statutes had begun. The first general corporation statute was adopted in 1837 in the state of Connecticut. The corporate statutes were generally widespread in the 1870s.

The first appraisal rights were granted to shareholders by statutory provisions at the end of the 19th century simultaneously with the enactment of first corporate statutes in general. Before the appearance of the corporate statutes the common rule in the most of the states was the requirement of unanimous consent of the shareholders of a company in order to consolidate or merge with another company. The shareholders’ power to veto any amendment of a charter, consolidation, merger and sale of assets was protected by courts. The protection given by courts to minority shareholders was similar to the appraisal remedy, meaning that in cases when a company sold its assets or entered into consolidation or merger only by an approval of majority shareholders, then minority shareholders (those voting against consummated transactions) were entitled to sue a company for payment of the fair value of their shares or they could bring an action before a court in order to have this transaction set aside in proportion to them. Thereby, providing an appraisal remedy, the requirement of unanimous will of the shareholders was replaced by the rule of a consent of the majority of the shareholders. In other words the minority shareholders received a right to dissent from the decisions made by the majority and to give back their shares for the fair price (value), while the majority of the shareholders got a possibility to make decisions in a company in a larger extent than at the time when an unanimous consent was required. Some scholars see the

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7 Wertheimer, supra note 6, at 619; Wertheimer points out that there was a possibility to bind minority of shareholders by a decision of the majority (providing the corporations more centralized process of decision-making than in the partnership were decisions were made only by consensus) but this flexibility did not apply to mergers and consolidations.
8 Mary Siegel, “Back to the Future: Appraisal Rights in the Twenty-First Century”, 32 Harv. J. on Legis. 79 1995, at 86. As an example Siegel points at the case Mason v. Pewabic Mining Co., 133 U.S. 50, 58 (1890) in which the court declared the forcing minority shareholders to become shareholders of a new company by a sale of assets for shares as injustice). See Carney, supra note 1, at 79 note 34, for the list of cases in which the courts relieved the minority shareholders from corporations attempting to make changes the company without unanimous consent of shareholders.
9 Lattin Norman D., “Remedies of Dissenting Stockholders under Appraisal Statutes”, 45 Harv. L. Rev. 233 (1931), at 234, listing the cases in which a remedy similar to the appraisal right was awarded by courts.
adoption of appraisal rights simply as a compensation for the eradication of the shareholders’ ability to use their veto power\textsuperscript{11}.

The time when the first appraisal rights were given by the corporation statutes was not casual. The end of the 19\textsuperscript{th} century was a time when the industrial revolution took place. The corporations needed to adapt themselves to a new reality and to new requirements of the market. In those circumstances the condition of unanimous consent became an obstacle for the companies wishing to change in order to grow. Under the unanimity provision every shareholder was able either to block changes from which a company could potentially benefit or either to force a company to convince investors to set up a new enterprise that would generate indispensable extra costs\textsuperscript{12}.

The introduction of appraisal rights into corporate statutes is considered to be tantamount with abolishing the requirement of shareholders’ unanimous approval of merger or consolidation of a corporation replaced by the simple majority of the shareholders’ votes. However, as stated by Robert B. Thompson, these two statutory provisions should not be considered equivalent as they were spread across the United States in a significantly different time and pace. As already mentioned, the unanimity requirement with regard to mergers and consolidations was replaced by the majority voting in the late 19\textsuperscript{th} century. However among the first twelve states that enacted such provisions, only five of them provided appraisal rights at that time (Ohio, Wyoming, Alabama, South Carolina and Nebraska)\textsuperscript{13}. While half of the states stipulated the majority voting for mergers and consolidations of corporations by 1909, the appraisal remedies were generally introduced across the United States only between the second and the third decade of the 20\textsuperscript{th} century\textsuperscript{14}. Mary Siegel points out that at least twenty states enacted appraisal rights in their corporation statutes by 1927\textsuperscript{15}. As of today all fifty states provide appraisal rights in their corporation statutes.

Considerations on the evolution and the development of appraisal rights have the significant importance for a few reasons and are crucial for the further analysis and elaboration of this remedy at law. In the first place, the enactment of appraisal rights into

\begin{itemize}
  \item Thompson, supra note 9, at 13.
  \item Id., at 14 referring to Walter C. Noyes, A Treatise on the Law of Intercorporate Relations, §57 no. 4 (1902), listing the first twelve states enacting new rules concerning mergers and consolidations and these five states which at the same time provided appraisal rights.
  \item Thomson, supra note 9, at 14.
  \item Siegel, supra note 8, at 90-91.
\end{itemize}
corporate statutes changed the position of shareholders as their rights were not based anymore on contract rights which could possibly be easily breached. At the same time the rule of majority voting evolved from being considered as wrongful to a generally accepted principle. Appraisal rights have from the very beginning not been perceived as a shareholder’s damage remedy based on a breach of contract but, instead, it aimed to entitle shareholders to receive a payment which corresponds to the fair value of their shares (stocks)\textsuperscript{16}.

Second of all, the analysis of the historical development of the appraisal remedy enables to fully understand the different approaches to appraisal rights in corporation statutes in different states as to conditions entitling a shareholder to use his appraisal remedy. When the American corporations and corporation law firstly appeared, the common link between shareholders’ decisions concerning mergers, sales of assets or amendments of a charter was obvious and clear. All these actions required unanimous consent of all shareholders to be validly taken. At the moment when that requirement was replaced by the majority voting, it was not clear anymore which transactions of corporations involving shareholders’ voting should be a subject of appraisal rights and which should not\textsuperscript{17}.

Finally, the analysis of the history of the evolution of appraisal rights is an essential element to understand and explain the goal of the development and the introduction of appraisal rights into corporation statutes. A historical overview of the appraisal remedy also helps to formulate and analyze the role of appraisal rights in modern statutes and contemporary appraisal litigation (proceedings).

2. The concept and the role of the appraisal remedy

2.1 First theories and Manning’s critique

As already mentioned, the analysis of the historical development of appraisal rights enables to understand their primary goals and nature. American scholars tried to understand and to explain the role of the appraisal remedy in corporate law and its implications on corporations and shareholders from the very beginning of the existence of that legal concept. From today’s perspective, we could divide those attempts into three groups, namely traditional views, first developed and comprehensive critique presented by Bayless Manning in his famous article from 1962, and post-Manning approaches either concurring Manning’s point of view or arguing with it and presenting their own arguments.

\textsuperscript{16} Carney, supra note 1, at 70; Siegel supra note 8, at 91.

\textsuperscript{17} Joseph L. Weiner, “Payment of Dissenting Stockholders”, 27 Colum. L. Rev. (1927) No. 5, at 548.
The appraisal remedy is a remedy at law granted to shareholders enabling them, under defined conditions (prerequisites), to dissent from consolidation, merger or other fundamental changes in a corporation\(^{18}\) accepted by a majority of shareholders and to receive a fair value of their shares of stock determined by a court.

The first theories concerning the purpose and the role of appraisal rights, representing traditional point of view on that issue, stated that the appraisal remedy is a protection of both the majority and the minority shareholders. According to these theories the former should not be prevented from introducing changes in a corporation, from making decisions considered by them as advantageous for a company and the latter should not be forced to remain in a corporation complete different to the corporation they involved to by investing\(^{19}\). The appraisal remedy from this point of view is seen as a relief to dissenting shareholders who are not able any longer to prevent or to block the will of the majority and is seen as a substitute of minority shareholders’ previous right to veto majority’s decisions\(^{20}\). As pointed out by Irving J. Levy “The right to payment is regarded as an alternative one with the right of going along on the new venture or preventing it if improper. Payment is not regarded as validating unauthorized action; nor as rendering constitutional acts which, in its absence, would be held to violate due process.”\(^{21}\). The protection of minority shareholders provided for by the appraisal remedy was seen by scholars as ex post fairness as minority shareholders should have a possibility to leave a company when changes were introduced by a decision of a majority\(^{22}\).

Such an approach to the role of the appraisal remedy was confirmed, among others, in the comment to the Uniform Business Incorporation Act from 1928 which stated that: “The majority ought to be able to carry out the policies which seem to them best, but the minority ought not to have to bear the consequences of the majority’s adoption of those rather

\(^{18}\) Circumstances, occurences and transactions upon which the appraisal right may be based differ across states’ jurisdictions. Apart from merger which is granted as transaction triggering the appraisal remedy by all states some of them grant this remedy at law in case of consolidation, a corporation selling its all assets or even amending a corporate articles. George G. Geis, “Internal Poison Pills”, 84 N.Y.U. L. Rev. 1169 (2009) at 1186; Thompson, supra note 10 at 7, 9.


\(^{21}\) Levy supra note 19, at 427.

\(^{22}\) Levmore, Kanda supra note 20, at 431.
extraordinary and unexpected measures. The traditional point of view was also supported by the courts which held that the minority shareholders had a right to disassociate, to leave, to retire or to refuse to go along. Consequently appraisal rights were considered to be a remedy at law which gives the minority shareholders a choice between continuing in a changed corporation or exercising their appraisal right.

This traditional point of view was widely spread and generally accepted by courts and scholars until 1962 when Bayless Manning published his essay criticizing appraisal rights as such and also criticizing and arguing with the traditional theory dealing with the goals of the appraisal remedy.

First of all, Manning argues that the appraisal remedy does not mainly serve to protect the outvoted shareholders against changes and decisions made by a majority against their will but actually it enables majority shareholders, or even more precise, the management of a corporation acting on behalf of majority shareholders, to take actions easier, with a “greater mobility.” It happens with a help of courts which prefer minority shareholders to revoke and exercise their appraisal rights rather than to accede to dissenting shareholder’s application for the injunction of a transaction at stake. He notices that the supporters of appraisal rights and their traditional function could not take into account that granting minority shareholders’ right for appraisal would not help them but it would help majority shareholders, so actually a corporation itself and its management body, to avoid injunction. Manning wonders whether introducing the appraisal remedy was an expression of a concern about dissenting shareholders or if it was rather just good politics. He states that “It is a nice question whether the early appraisal statutes were promoted by perspicacious legislative agents of management, who saw in these statutes a way to consolidate and liberate their own condition. But this has been a consequence.” Analyzing the appraisal remedy Manning points out the fact that the development of this remedy at law took place at the same time as the development of American corporate law in the direction of the will of majority and greater mobility, meaning that introducing this legal concept into statutes was just an expression of a general trend in

23 Thompson supra note 10, at 18.
24 Id., citing the cases in which the courts held those rights of the minority shareholders; e.g. Morely Bros. v. Clark, 361 N.W.2d 763, 764 (Mich. Ct. App. 1984); Cole v. National Cash Credit Ass'n, 156 A. 183, 187 (Del. Ch. 1931); Johnson v. Baldwin, 69 S.E.2d 585, 591 (S.C. 1952).
25 Thompson supra note 10, at 19.
27 Id., at 227
28 Id., at 229
American corporate law. He finds that even without the statutory appraisal rights, courts probably would have supported the will of majority over a dissenting minority as “It no longer seems feasible (or, it is significant to note, moral) to permit the objecting individual to stand in the way of a transaction approved (or at least not objected to) by a majority (or those acting in their name).”

Furthermore, Manning points out burdens that are borne by exercising the appraisal remedy by dissenting shareholders. In the first place, a shareholder exercising his appraisal rights must incur the costs of the procedure even if those costs are not significant. Secondly, such a shareholder also remains in uncertainty as to the result of the proceedings often for a very long time. These two aspects, the expensive and long judicial procedure, might make using the statutory appraisal remedy not worth it, especially when simple selling shares can be an easier, less complicated way to leave a company. Manning spotlights the meaning of efficiency of a procedure is a key for the usefulness of this remedy at law. Moreover, the application of appraisal rights may be hindered by complicated and long statutory provisions constituting the remedy and may also be hindered by courts which are prone to a rather strict interpretation and application of those statutory provisions. Generally, Manning takes a position that the appraisal remedy is overestimated as a legal instrument protecting minority shareholders. When a market value of shares of dissenting shareholders in a company is not known, the estimation of this value by a court becomes unpredictable and appraisal proceedings are delayed, expensive and their outcomes are highly uncertain.

The author also pays attention to problems and restraints which the appraisal remedy brings to corporations. For instance, at the moment of taking an activity or entering into a transaction which possibly may trigger appraisal rights, corporations, or more precisely their managements, do not know and are not able to estimate how many potential dissenters can occur. Such a situation creates a lot of uncertainty. Another problematic aspect of appraisal rights for corporations is an economic perspective. Namely, when there are many dissenting shareholders (but obviously still remaining minority shareholders) paid out in cash the aggregated sum of the value of their shares may create a liquidity problems of a corporation.

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29 Id., at 229-230.
30 Id., at 230.
31 Manning explains that statutes became far longer and more complex to compare to early ones because of the latter did not provide answers for key and significant questions about the appraisal remedy and procedure (such as how long the procedure will be, who should pay expenses of that procedure, what are the legal grounds of a judicial review, where a dissenting shareholder cease to be a shareholder, etc.) and the current statutes want to provide all these answers in advance. See id., at 231.
which carries serious consequences such as for instance consternation of company’s creditors and their race for a cash which still is in a corporation. Financial problems (e.g. illiquidity) caused by dissenting shareholders exercising the appraisal remedy, may also hinder the decision taken by the majority. For instance, a corporation that decided to merge with another corporation does not know at the time of making that decision how many dissenting shareholders will apply their appraisal act, nor how much money the corporation will be required to contribute.

Those situations are completely contrary to the main function attributed to the appraisal remedy, which is not only the protection of minority shareholders but also the protection of majority shareholders, so a corporation itself, from being unable to take, in their view advantageous actions which could be blocked by a veto of dissenting shareholders. Referring to that goal of the appraisal remedy Manning states that “In such a situation, the appraisal statutes have obviously failed in the job of providing simultaneously for a protection to the dissidents and an avenue of mobility for the majority.”

Manning looks at the appraisal remedy from a very wide perspective, he analyzes every aspect of this remedy at law and its exercising by entitled shareholders and he finds many disadvantages, real problems attached to appraisal rights both from the perspective of a dissenting shareholder and from the perspective of an involved corporation. As a consequence, in his opinion, the appraisal remedy provides for little fairness bearing high costs.

2.2 Post-Manning approaches

Bayless Manning’s critique of the appraisal remedy aroused wide and complex discussion about the usefulness of this legal concept or its lack and the scholars also have attempted to try to define the goals and the function of this remedy at law in American corporate law once again, taking into account different perspectives and circumstances than it was done by the representatives of the traditional theory. The most popular and the most significant post-Manning theories are those developed by Daniel R. Fishel, Saul Levmore and Hideki Kanda and by Peter V. Letsou and which will be discussed in this part of the paper.

32 Id., at 234.
33 Id., at 235.
34 Id., at 236.
Daniel R. Fishel regards the appraisal remedy as an implied contractual term. He finds that the traditional point of view focuses only on the protection of minority shareholders at the moment a transaction (usually merger) already took place and that it does not take into account how the appraisal remedy influences entering into a transaction, its terms and the agency costs borne by a management of a corporation in the case where a transaction does not occur. As the result, the author sees that the remedy has consequences on those issues and the interest of not only minority shareholders dissenting from a transaction but the interest of shareholders as a whole.

Generally Fishel considers the appraisal remedy to be an implied contractual term which “sets the minimum price at which the firm, or a part thereof, can be sold in situations where certain groups are more likely to attempt to appropriate wealth from other groups than to maximize the value of the firm.” By setting this minimal price for shares of a corporation the appraisal remedy protects all shareholders from entering into a transaction where a value of their shares is reduced by a bidder and as a result all shares being a subject of a transaction are traded at a higher price. Therefore, appraisal rights have a significant influence on the consummation of a certain transaction and its terms.

The author argues that every shareholder is affected by the concept and the role of the appraisal remedy as “The higher the consideration likely to be received in an appraisal proceeding, the higher the price the bidder will have to pay to convince shareholders to tender.” The appraisal remedy also affects a process of negotiations of a transaction by a management of a corporation as it sets a price which will be approved by shareholders, thus shareholders will vote for a transaction itself. According to Fishel’s theory, shareholders are willing to support a transaction if they know in advance, ex ante, that shares will not be sold below a certain price level, therefore a higher price for those shares will be a consequence of the appraisal remedy.

According to Fishel, however, it cannot be assumed that the appraisal remedy increases the value of a transaction in every case. He points out that appraisal rights are costly instruments. In the terms of costs attached to the appraisal remedy Fishel invokes the

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36 Fishel, supra note 35, at 876.
37 Id., at 879.
38 Id.
39 Id.
same arguments as Bayless Manning. He finds that purchasing shares of dissenting shareholders by a company results in withdrawing capital from it and therefore there is a high risk of liquidity problems in a company and as a consequence a company is likely to sell its assets at much lower price than it normally could be done and is likely to bear extra costs connected with organizing and collecting new capital. Moreover, the appraisal proceeding is expensive and provides for a significant uncertainty for both parties.

Another approach to the purpose of the appraisal remedy was developed by Saul Levmore and Hideki Kanda. In their article the authors present three different theories explaining the goal of the appraisal remedy which they call inframarginality, reckoning and discovery theories.

The theory of inframarginality is based on the assumption that not all shareholders consider their shares and a value of their shares identically, that “the marginal, or market, price therefore understates their average valuation of these shares, and that appraisal may serve to protect these inframarginal valuations.” In other words, the appraisal remedy gives a protection for shareholders in case these inframarginal values are lost.

To illustrate the application of the theory of inframarginality the authors refer to the appraisal remedy provided by the Delaware General Corporation Law. According to §262 of this statute if shares possessed by a shareholder are listed on a national securities exchange and if this shareholder receives such shares or shares of an acquiring corporation then no appraisal rights are available to such a shareholder. In Levmore and Kanda’s view in these kind of transactions shareholders are less likely to lose inframarginal value than in transactions where shareholders’ shares are thinly traded. That is why appraisal rights are granted to the latter in order to achieve this inframarginality goal. In the case of a transaction where a shareholder holds widely traded shares and he receives the same kind of shares or shares of an acquiring company “it may well be that no net loss of inframarginal value occurs; this is because that which is received is also not valued identically by all recipients so that inframarginal value may take the place of lost inframarginal value.”

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40 Id., at 881.
41 Levmore, Kanda, supra note 20.
42 Id., at 438
43 Del. Code Ann. tit. 8, §262 (b) (2016)
44 Levmore, Kanda, supra note 20, at 440.
45 Id.
Another goal of appraisal rights considered by Levmore and Kanda is reckoning. The authors point out that shareholders must monitor a corporation whose shares they possess in order to evaluate its management. One of the main tools of this monitoring is measuring the income made by the management of a corporation from a disposable capital. However, in the cases where a corporation is being a subject of fundamental changes this monitoring is more difficult to perform than in usual circumstances as such changes may make unclear the performance of management. An entity that is a result of such fundamental changes may be so different from an entity it was before “that much information about managers will be lost if the two experiences are evaluated as one.”46. If this kind of situation occurs in a company then the appraisal remedy may be considered as a point of reckoning as a future performance may be assessed from a point of reference determined at appraisal47.

The final theory presented by Levmore and Kanda is the theory of discovery. According to the authors, appraisal rights should be able to help shareholders to prevent and uncover wrongful behaviour of management of a corporation. Such wrongful behaviour of management may be magnified especially while a company undergoes some fundamental changes or is being a subject of a merger or consolidation48. That is because instead of negotiating in the best interest of a company and its shareholders, management may be tempted to accept deal less attractive as such but more attractive for management, for instance with regard to its remuneration or other incentives. Thus, in some situations the fear of shareholders for legitimacy of a transaction of a change and for real motivations of management for taking these actions.

In Levmore and Kanda’s point of view, in the situations where a transaction or a fundamental change decided by management seems not clearly justified or dubious for shareholders, the appraisal remedy may “serve as a useful discovery tool for uncovering suspiciously non-arm’s-length bargains or side payments to the target’s managers, guiding future fiduciary suits, and, generally deterring misbehaviour.”49. In the authors’ opinion appraisal rights can effectively serve this goal because the appraisal proceeding is relatively quick, the costs of the proceeding are usually shared by the parties and, above all, the appraisal proceeding delivers information about a corporation and its plans and assets necessary for shareholders envisaging a fiduciary suit. Moreover, the scholars state that the

46 Id., at 441.
47 Id., at 442.
48 Id.
49 Id., at 444.
The appraisal procedure will “threaten to drain the corporation’s funds and therefore may deter misbehaviour by managers whose plans require the presence of these funds. [...] shareholders, managers, and legislators are likely ex ante to agree on such a system because it may contribute to corporate performance and help attract capital.”

The last theory concerning the potential goals and role of the appraisal remedy in corporate law was introduced by Peter V. Letsou. In his article the author firstly discusses and argues with traditional view on the appraisal remedy, with Manning’s critique and with some post-Manning approaches. Then he provides for his own theory which is based on the assumption that appraisal rights are capable of reconciliation of different shareholders’ preferences as to transactions that result in a changed risk of a company’s shares.

Letsou explains that transactions that change market risk of a corporation, in the situation where shareholders do not have enough access to capital markets, are likely to make some shareholders more and the other less wealthy. In such cases the appraisal remedy provides for a compensation by a company to those shareholders who are worse off by a transaction while the costs of the compensation are born by shareholders made better off by that transaction. Thereof, shareholders will prefer to accept transactions which bring them more than costs of compensating of dissenting shareholders. As a consequence, the appraisal remedy can be seen as a factor decreasing the probability of entering by a company in risk changing transactions which could cause net losses for shareholders, thus all shares being a subject of a transaction are traded at a higher price. It must be noticed, what is emphasized by Letsou, that the theory of reconciliation is applicable, pursuits its goal, only if shareholders do not have an effective access to capital markets and where shareholders’ risk preferences differ.

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50 Id.
51 Id., supra note 20.
52 Id., at 1140.
53 Id., at 1140-1141.
Chapter II The appraisal remedy under the Delaware General Corporation Law

1. The substantial prerequisites of appraisal rights

1.1 Merger or consolidation

The State of Delaware is the leading state in the United States with regard to the place of incorporation of American and international corporations. Nowadays more than 1 million entities is incorporated in Delaware. The state is a domicile for more than 66% of all publicly-traded companies in the United States, including 66% of companies being listed in the Fortune 500 list. The Division of Corporations of the State of Delaware delivers following reasons as choosing Delaware for a place of incorporation by corporations: (a) providing a complete package of incorporation services by the division itself, (b) the most flexible, advanced and business friendly statute in the United States concerning a formation of business (the Delaware General Corporation Law), (c) the old and unique business court that has written most of the modern American corporate law cases (the Delaware Court of Chancery) and (d) the Delaware’s State Government that is accessible and business-friendly. For all these reasons the Delaware General Corporation Law and its provisions regulating appraisal rights are the most relevant and the most suitable for the detailed analysis of the appraisal procedure in the United States.

The Delaware General Corporation Law provides for appraisal rights in §262. This provision regulates events triggering appraisal rights, obligations of a dissenting shareholder and a corporation, and a judicial appraisal proceeding.

Under Delaware law appraisal rights are granted to dissenting shareholders only in a case of merger or consolidation (hereinafter referred as merger as consolidations are merger-like transactions resulting in a creation of a new entity). The grounds for the appraisal remedy are very limited, especially compared to the Model Business Corporation Act (adopted by numerous states) which provides for five appraisal triggers: merger, share exchange, disposition of assets, amendment of the articles of incorporation, domestication and conversion of a corporation. A merger is a recognized trigger for appraisal rights by all states, but only two of them recognize a merger as the only event triggering appraisal rights,

54 https://corp.delaware.gov/aboutagency.shtml
55 Id.
as Delaware does. Other grounds of the appraisal remedy mentioned in the Model Business Corporation Act are widely recognized by U.S. jurisdictions (69% of all American jurisdictions follow the Model Business Corporation Act’s approach of providing for multiple events triggering appraisal rights). Forty seven states provide for appraisal rights in the case of a significant disposition of assets, forty four jurisdictions in the case of share exchange, thirty nine states for particular amendments of the articles of association and nineteen jurisdictions for certain domestications and conversions. In its judgment in the case *Cede & Co. v. Technicolor, Inc.*, the Court of Chancery of the State of Delaware explaining the limited scope of appraisal rights under Delaware law stated that “the legislature has narrowed the issues involved in order to provide a fair and economical remedy for a specific problem”.

Although Delaware law entitles shareholders to appraisal rights only in case of a merger, it actually includes many mergers. According to §262(b) appraisal rights shall be available for shareholders of a constituent corporation in case of (a) a merger of domestic corporations, except for mergers where a vote of shareholders is not necessary for an authorization of such a merger, (b) a merger of domestic and foreign corporations, (c) a merger of a domestic corporation and a joint-stock or other association, (d) mergers of domestic non-stock corporations, (e) mergers of domestic and foreign non-stock corporations, (f) mergers of domestic stock and non-stock corporations, (g) mergers of domestic and foreign stock and non-stock corporations, (h) mergers of domestic corporations and

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59 Id., at 235.
60 These jurisdictions are: Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, and Wyoming; Siegel, supra note 58, at 234.
62 These jurisdictions are: Arkansas, California, Colorado, Florida, Hawaii, Iowa, Kentucky, Maine, Massachusetts, Michigan, Minnesota, New Hampshire, North Dakota, Oregon, Pennsylvania, South Carolina, South Dakota, Texas, and Wyoming; Siegel supra note 58, at 235.
64 Although there is no definition of a constituent corporation in the Delaware General Corporation Law, it is clear from the provisions of this statute that every corporation involved in a merger of a consolidation is a constituent corporation, regardless of being a surviving or disappearing corporation; Welch, Turezyn, Saunders, supra note 63, at. 734.
partnerships and (i) a merger of a domestic corporation and a limited liability company. However, some merger transactions are excluded from the scope of appraisal rights. These are called “market exceptions”, “market-out exceptions” or “market exemptions” and as they concern certain types of shares being traded they will be discussed in the 1.2 part of this chapter.

Additionally, the Delaware General Corporation Law enables a corporation to recognize an additional event that trigger appraisal rights by a private ordering. According to §262(c) any corporation may provide, through its certification of incorporation, that appraisal rights governed by §262, are available “for the shares of any class or series of its stock” in the cases of (a) an amendment of the corporation’s articles of association, (b) any merger or consolidation in which the corporation is involved or (c) in the case of a sale of all or substantially all assets of the corporation. If the certificate of incorporation of a corporation contains such a provision, then the provisions of §262, including provisions concerning the perfection of appraisal rights, are applicable as nearly as it is practicable. For a comparison, under the Model Business Corporation Act such additional events triggering appraisal rights do not have to be necessarily provided by the articles of incorporations, they may also be introduced by bylaws or by a resolution of the board of the directors.

The Delaware Law’s provision for a merger being the only event triggering appraisal rights seems to be a very restrictive approach. Such an approach, compared to the provisions offered by the Model Business Corporation Act and by numerous states that adopted it, is less attractive for shareholders, as they have very limited grounds for exercising their appraisal rights and, at the same time, is more attractive for a corporation itself, as granting shareholders multiple triggers for the appraisal remedy could cause much more difficulties and restraints on its functioning and introduce fundamental changes in a company. As explained in the previous part of the paper, a corporation could face significant financial problems if many shareholders exercise their appraisal rights in many situations. However, providing for many types of merger that entitle shareholders to invoke their appraisal rights significantly broaden the scope of the application of the appraisal remedy, being very limited

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65 Del. Code Ann. tit. 8, § 262 (c) (2016); Delaware is not the only state recognizing private ordering, the other jurisdictions are: Alabama, Arizona, Arkansas, Colorado, Connecticut, Florida, Georgia, Hawaiii, Idaho, Illinois, Indiana, Iowa, Kentucky, Maine, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Mexico, North Carolina, North Dakota, Oregon, South Carolina, South Dakota, Tennessee, Utah, Virginia, Washington, West Virginia, and Wyoming; Siegel, supra note 58, at 234.
and strict at the first sight. Moreover, enabling corporations to offer additional events to which appraisal rights apply, makes exercising this remedy more flexible and allows to find the most suitable solution for both, shareholders and corporations.

1.2 Shares of stock and their types

In principle §262(b) of the Delaware General Corporation Law grants appraisal rights to shares of any class or series of stock of a constituent corporation in mergers falling into the scope of this provision. However, §262(b)(1) provides for market-out exceptions from this principle. Such exceptions are based on the type of shares being subject of a merger.

In the first place, appraisal rights are not available for the shares of any class or series of stock that are either listed on a national securities exchange or are held of record by more than 2000 holders at the date on which the shareholders are entitled to receive a notice of the meeting of stockholders to vote on a merger. The application of this provision is not limited to shares issued by a surviving corporation, but it also applies to shares of an acquired corporation. Similarly, the exceptions are applicable regardless of the form in which a merger was approved, namely whether it was done by shareholders voting at a general meeting or by their written consent.

These exceptions are justified by the goal of appraisal rights, that is providing an effective market, judicially created, for dissenting shareholders. Consequently, there is no need for such a remedy “where there is already a substantial trading market, either through a securities exchange or other national market” where shareholders can easily sell their shares at a fair price. The rationale for introducing such exceptions in Mary Siegel’s opinion is that “at the announcement of an appraisal-triggering transaction, the market for that corporation’s stock is operating with maximum efficiency and serves as a reliable determination of the fair value of the corporation’s shares.” According to Marco Ventoruzzo these exceptions “clearly reflects the liquidity goal of early appraisal statutes”. Although the justification of the market-out exception seems to be reasonable and generally accepted, the opponents of this solution can be found in the doctrine as well. They argue that fair value and market value are

67 Welch, Turezyn, Saunders, supra note 63, at 735.
68 Id.
69 Siegel, supra note 58, at 245.
not always synonymous, as “the market may be demoralized, be reflective only of publicly available information, or only a mirror of the transaction price.”

Moreover, under §262(b)(1) no appraisal rights are available for holders of any shares of stock of the surviving corporation in the case of a merger that did not require approval by voting of the stockholders according to §251(f). An analogous exception to appraisal rights regulated by Delaware law can be found in the Model Business Corporation Act. §13.02 (b)(1) provides that appraisal rights are not available for shares which can be easily sold in a liquid market, namely for those shares that are covered by the Securities Act, traded in an organized market and has at least 2000 holders and a market value of at least $20 million or are issued by an open end management investment company.

Secondly, the Delaware General Corporation Law provides for an exception to the exception. The provision §262(b)(2) limits the scope of the exception introduced by §262(b)(1) by granting appraisal rights to shares of any class or series of stock of a constituent corporation only if holders of such shares are required, by the terms of an agreement of merger, to accept consideration in cash, securities “other than stock of a widely held corporation, stock of the surviving corporation, or a mix of the two.” (such as bonds or debentures), or property or rights. In other words, the consideration received by shareholders must be different from the shares they held before a merger. Consequently, the exception to the exception is not applicable to stockholders of a surviving corporation “whose shares are unaffected by the merger.” Providing the exception to the exception was necessary, as the market-out exception does not provide the remedy for dissenting shareholders if they are faced with cash-out. This may result in a situation where “the fair value of the shares might be significantly higher that the cash consideration offered by controlling shareholders. Alternatively, the market price might not reflect the shares’ fair value because it has discounted for the possibility of a majority freeze-out.” These reasons sufficiently explain and justify the exception to the general exception. The Model Business Corporation Act also provides a market-out exception applicable to a transaction that is an “interested

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71 Siegel, supra note 58, at 247, citing Alfred F. Conrad’s and her own opinions.
72 The provision regulates a merger of domestic corporations.
75 Welch, Turezyn, Saunders, supra note 63, at 737.
76 Id., at 736.
77 Ventoruzzo, supra note 70, at 856.
transaction”\textsuperscript{78}, contrary to Delaware law which does not distinguish between interested and disinterested transactions. An interested transaction is defined by the Model Business Corporation Act as a corporate action other than a merger, involving an interested person in which any of the shares or assets of the corporations are converted or acquired. An interested person is a person, or an affiliate of a person, who during one year preceding an approval of a corporate action by the board of directors was the beneficial owner of at least 20\% of the voting power of the corporation (other than as owner of excluded shares), had the power (other than as owner of excluded shares) to cause the election of appointment of at least 25\% of the directors to the board of the directors of the corporation or was a senior executive or director of the corporation or a senior executive of any affiliate corporation and that person will receive a financial benefit not generally available to other shareholders as a result of the corporate action\textsuperscript{79}.

Another situation, in which appraisal rights are granted to all shares is the so called short-form merger. According to §262(b)(3) if all of the stock of a subsidiary Delaware corporation party is not owned by the parent corporation, in case of (a) a merger of a parent entity and a subsidiary corporation or corporations, (b) a merger of a parent corporation and a subsidiary or subsidiaries and (c) a certain variation of merger of domestic corporation, appraisal rights are available for the shares of the subsidiary Delaware corporation.

\textbf{1.3 Pre-judicial phase of appraisal process}

Before the appraisal claim can be brought before a court, some pre-judicial steps must be taken. The initial obligations with regard to the appraisal procedure is imposed on a corporation. According to §262(d)(1), if a proposed merger triggering appraisal rights is to be submitted for approval at a stockholders’ meeting, the corporation is obliged to notify, at least 20 days before the meeting is to be held, each shareholder entitled to the appraisal remedy about the availability of appraisal rights. Such a notice has to include a copy of §262 of the Delaware General Corporate Law. If a corporation fails to fulfil this obligation to include such a copy, then an appropriate remedy will arise on this basis, as the statutory mandate must be strictly observed as a matter of law\textsuperscript{80}.

\textsuperscript{78} Model Bus. Corp. Act § 13.02 (b) (4) (2016).
\textsuperscript{79} Model Bus. Corp. Act § 13.01 (5.1) (2016).
\textsuperscript{80} Welch, Turezyn, Saunders, supra note 63, at 740.
In the case *Raab v. Villager Industries* the Delaware Supreme Court extended the scope of the corporation’s pre-merger notice by imposing on Delaware corporations an obligation to include in its notice an instruction of perfecting appraisal rights by stockholders. Such an instruction should include “the general rule that all such papers should be executed by or for the stockholder of record, fully and correctly, as named in the notice to the stockholder; and (...) the manner in which one may purport to act for a stockholder of record, such as a joint owner, a partnership, a corporation, a trustee, or a guardian.” In the Delaware Supreme Court’s opinion such specific instructions of the appraisal proceeding are required by fairness to stockholders. In its later case, *Enstar Corp. v. Senouf*, the Delaware Supreme Court stated that proper instructions are such instructions which “disclose a material fact necessary to permit a reasonable person to perfect his or her (or a customer’s) appraisal rights.” Moreover, stockholders are entitled to receive a notification of approval of a transaction which has to be delivered by a surviving or resulting corporation within 10 days after the effective date of the merger.

In case of the short-form merger, either a constituent corporation before the effective date of the merger, or a surviving or resulting corporation within 10 day after the effective date of the merger, is obliged to notify each stockholder entitled to appraisal rights of the approval of the merger and of the availability of appraisal rights for such stockholders. Such a notification has to include a copy of the provision §262. If the notification is delivered after the effective date of the merger it also has to include a notification of the effective date of the merger. A shareholder entitled to appraisal rights may, within 20 days after mailing of such a notice, deliver a surviving or resulting corporation a written demand of the appraisal of his shares. Such a demand must fulfil the requirements discussed below. If a notice of a corporation did not notify stockholders of the effective date of the merger then either a constituent corporation has to send a second notice before the effective date of the merger notifying each of the stockholders that are entitled to appraisal rights of the effective date of the merger, or a surviving or resulting corporation has to send a second notice to such stockholders within 10 days after such effective date. If such a notice is sent more than 20

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84. Chapter II, part 2.2
days following the sending of the first notice, the second notice need to be sent only to stockholders who demanded appraisal of their shares.\textsuperscript{85}

Although it is not directly provided by the Delaware’s statute, it is the director’s fiduciary duty to disclose to stockholders “the available material facts that would enable them to make an informed decision, premerger, whether to accept the merger consideration or demand appraisal.”\textsuperscript{86} The material facts are those facts which are considered by shareholders as important in making a decision whether to approve a merger or to seek the appraisal remedy (e.g. providing a financial disclosure).\textsuperscript{87}

In the case of a failure by a corporation to notify stockholders with a pre-merger notice including information about availability of appraisal rights for them, these stockholders may be still permitted by a court to seek a relief thorough a concept of “quasi-appraisal”. The concept assumes that, despite of the fact that the requirements to perfect appraisal rights are not met, a dissenting shareholder is still entitled to claim the fair determination of a value of his shares before a court. The quasi-appraisal remedy may be available for shareholders even if a corporation notified them on time but it failed to disclose all necessary material facts. In the case \textit{Gilliand v. Motorola Inc.} the Court of Chancery of the State of Delaware allowed quasi-appraisal action to proceed, as a corporation did not provide any financial information in its pre-merger notice delivered to stockholders and advising them an approval of a short-term merger.\textsuperscript{88} In the case \textit{Berger v. Pubco Corp.} the Delaware Supreme Court held that where “the material facts are not disclosed (...) the minority shareholders become entitled to participate in “quasi-appraisal” class action to recover the difference between fair value and the merger price”.\textsuperscript{89} By contrast in the very recent case \textit{In re United Capital Corp. Stockholders Litigation}, the Court of Chancery of the State of Delaware held that stockholders were not entitled to quasi-appraisal remedy. Although some facts were omitted by a corporation in its pre-merger notice but these omissions were not material as the notice disclosed the necessary information regarding the determination of a fair price, reasoning behind an offered price, sufficient financial data, including those current and forward-looking,

\textsuperscript{85} Del. Code Ann. tit. 8, § 262 (d) (2) (2016).
\textsuperscript{87} Id.
\textsuperscript{89} Berger v. Pubco Corp., 976 A.2d 132 (Del.2009).
the corporation’s cash, cash equivalence and its future use and certain directors’ potential conflicts.  

2. Preliminary obligations of the dissenting shareholder

2.1 Holding of record of stock and opposition to transaction

To validly claim the appraisal, a dissenting shareholder must be, as provided by §262(a), a stockholder of a corporation. This provision defines a stockholder as a holder of record of stock in a corporation. Such a stockholder, in order to be entitled to appraisal rights, has to hold shares of stock on the date of making a demand for appraisal with respect to those shares and has to continuously hold such shares through the effective date of the merger being a trigger for the appraisal remedy. Consequently, it is in a shareholder’s interest and in its power to obtain record ownership and the advantages attached to that. That is why the requirement of being a stockholder of a corporation to exercise appraisal rights cannot be seen as depriving unregistered stockholders from any rights. Even before introducing the legal definition of a stockholder into the Delaware’s statute, the availability of appraisal rights was limited to the owner holding s record of stock, as “a corporation should, in estimating the number of dissenters, be able to rely exclusively on corporate records of stock ownership and should not become involved in disputes between registered and unregistered stockholders.”

Another essential prerequisite of the appraisal rights is an opposition to a transaction. §262(a) provides for the appraisal rights only to shareholders who have neither voted in favour of a merger nor contested thereto in writing pursuant to §228. This provision requires a stockholder not to vote in favour of a merger, it does not require a stockholder to vote against it. As a result a shareholder may abstain from voting. However, if a stockholder accepts a merger consideration he abandons the appraisal rights although he is still a dissenting shareholder.

92 Welch, Turezyn, Saunders, supra note 63, at 744.
93 Id., giving the examples of the cases which limited the appraisal rights to record owners.
94 Del. Code Ann. tit. 8, § 262(a) (2016); Welch, Turezyn, Saunders, supra note 63, at 743.
95 Welch, Turezyn, Saunders, supra note 63, at 743.
2.2 Demand for appraisal

Besides holding of record of stock and opposition to a transaction, the Delaware General Corporate Law requires dissenting shareholders to make a demand for appraisal. Pursuant to §262(d)(1) such a demand has to be made in a written form and has to be delivered to a corporation before the vote on a merger. The demand for appraisal should inform the corporation about the stockholder’s identity and should express his intention to demand the appraisal of his shares. No other formal requirements of the demand are imposed on dissenting stockholders. The provision explicitly states that voting against the merger or a proxy does not constitute a demand for the appraisal. Only a separate written demand fulfilling the requirements provided by §262(d)(1) is to be considered sufficient for the appraisal procedure. A dissenting stockholder does not have to make the demand by himself, as it is settled in case law, the written demand may be made and delivered to the corporation by an agent acting on the behalf of the stockholder.

As pointed out by the scholars the purpose of such a written demand for the appraisal is “to inform the corporation and its other stockholders of the number of possible dissentients and, as such, potential demands of cash for their shares. This is desirable, since the amount of cash that might be required to pay off dissenting stockholders might have an influence on other stockholders’ votes on the merger.” Such an information may be significant especially for an acquiring corporation, since the acquiring corporation will eventually bear the burden of making a payment for dissenting shareholders. For this reason, in the case of mergers for which appraisal rights are available, merger agreements very often provide a condition under which the transaction will be closed only if the number of shareholders of an acquired corporation demanding the appraisal remain below certain percentage of the total number of shareholders of that corporation. Delivering the demand for the appraisal before the vote on a merger is actually taken is essential for serving this purpose. If there are some incompatibilities between the stockholder and a corporation with regard to the demand of the appraisal, then the stockholder is the one bearing a burden of proof that such a demand was

97 Welch, Turezyn, Saunders, supra note 63, at 742, noticing that in the early cases it was held that such an agent had to present a proof of his agency before the time for delivering the demand for the appraisal was expired, however nowadays the courts held that there is no necessity of providing of the proof of agency while making the demand.
delivered to a corporation on time, so prior to voting on a merger. Submitting the written demand for the appraisal before the deadline provided by §262(d)(1) is essential, because as it was stated by the Court of Chancery of the State of Delaware “time periods under [8 Del. C. §262] are strictly enforced, and the failure to meet a deadline will result in the loss of appraisal rights.”

Although the deadline for making the demand for the appraisal is strictly provided by §262(d)(1) and the justification for such a demand within a certain period seems to be convincing and sufficient, some argue that formal requirements imposed on a dissenting shareholder to exercise his appraisal rights are meaningful burdens imposed on a minority, as it may be difficult for a stockholder to declare his dissent before the vote on a merger is held and that “procedural compliance raises transaction costs for good-faith minority shareholders that are being unfairly cashed-out.” Such an opinion is supported by George G. Geis who states that appraisal rights are complicated remedy and the dissenting shareholders “have to navigate a variety of hurdles to perfect their claims.”

3. Judicial proceeding

3.1 Institution of the proceeding

In order to commence a proceeding, as provided by §262(e) a surviving or resulting corporation or any stockholder entitled to appraisal rights who complied with the preliminary obligations may, within 120 days after the effective date of the merger, file a petition in the Court of Chancery demanding a determination of the value of the stock of all such stockholders. A petition filed after the given period is ineffective. Pursuant to §262(e) it is sufficient if only a surviving or resulting corporation or one stockholder files a petition in order to institute the appraisal proceeding. There is no need to file a separate petition by each dissenting shareholder, as all stockholders are consolidated into one action and as the value of shares is determined by the court not only for a petitioner but for all shareholders entitled to appraisal rights. Thereby, the named petitioners have a fiduciary duty to the dissenting shareholders who are entitled to appraisal rights and who did not file a separate petition for appraisal rights.

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100 Welch, Turezyn, Saunders, supra note 63, at 743.
102 Ventoruzzo, supra note 70, at 857.
105 Welch, Turezyn, Saunders, supra note 63, at 746.
106 Id.
the appraisal\textsuperscript{107}. While filing the petition for appraisal the surviving or resulting corporation is obliged to submit, along with the petition, a duly verified list of the names and addresses of stockholders who have demanded the appraisal\textsuperscript{108}. If the petition is filed by a shareholder, such a list must be filed by the corporation, in the Court of Chancery, within twenty days after receiving a copy of the shareholder’s petition for appraisal which must be served upon the corporation by the shareholder filing the petition for appraisal\textsuperscript{109}. Filing duly verified list does not preclude the corporation from questioning whether the listed shareholders perfected their appraisal rights pursuant to the statute\textsuperscript{110}.

If the petition for appraisal is not filed within 120 days after the effective date of the merger by the corporation or by any dissenting shareholder, appraisal rights cease\textsuperscript{111}. Moreover, appraisal rights cease as the result of the shareholder’s withdrawal. The dissenting shareholders may withdraw their demands for appraisal in two ways. In the first place, a dissenting shareholder who neither has commenced the appraisal proceeding, nor joined that proceeding as a named party, may, within 60 days after the effective date of the merger, withdraw, in the written form, his demand for the appraisal and accept the terms of the merger\textsuperscript{112}. Secondly, a dissenting shareholder may deliver the written withdrawal of his demand of the appraisal, after the given period, then however, such a withdrawal must be accompanied by the written approval of the corporation\textsuperscript{113}.

Any stockholder for whom appraisal rights are available and who complied with the preliminary obligations is entitled to receive, from the surviving or resulting corporation, a statement informing about the total number of shares not voting in favour of merger and with respect to which the written demands for appraisal have been made and the total number of holders of such shares\textsuperscript{114}. A stockholder entitled to such a statement, may submit his written request for the statement within one hundred twenty days after the effective date of the merger and the corporation is obliged to mail the statement to the requesting stockholder within ten days after receiving the stockholder’s written demand or within ten days after the expiration of the period for delivery of written demands for appraisal, whichever is later\textsuperscript{115}. Receiving

\begin{footnotesize}
\begin{enumerate}
\item\textsuperscript{107} Id.
\item\textsuperscript{108} Del. Code Ann. tit. 8, § 262 (f) (2016).
\item\textsuperscript{109} Id.
\item\textsuperscript{10} Welch, Turezyn, Saunders, supra note 63, at 747.
\item\textsuperscript{111} Del. Code Ann. tit. 8, § 262 (k) (2016).
\item\textsuperscript{112} Del. Code Ann. tit. 8, § 262 (e) (2016).
\item\textsuperscript{113} Del. Code Ann. tit. 8, § 262 (k) (2016).
\item\textsuperscript{114} Del. Code Ann. tit. 8, § 262 (e) (2016).
\item\textsuperscript{115} Id.
\end{enumerate}
\end{footnotesize}
such a statement allows the dissenting shareholder to know the number of the shares qualifying for the appraisal and to expect to share the costs of the appraisal proceedings with other dissenting shareholders.\textsuperscript{116}

Once the dissenting shareholders have perfected their appraisal rights by demanding the appraisal, their status as stockholders has been changed. The dissenting shareholders, from and after the effective date of the merger, cannot vote their stock for any purpose and dividends and other distributions on the stock are not paid to them unless dividends or other distributions were payable prior to the effective date of the merger.\textsuperscript{117} As a consequence of the changed statutes, the dissenting shareholders resemble more creditors of the surviving or resulting corporations than its stockholders, as since the effective date of the merger, rather than after submitting their demands for appraisal, they are actually “monetary claimants” against the corporation.\textsuperscript{118}

\textbf{3.2 The appraisal proceeding}

After fulfilling all preliminary obligations by both, the dissenting shareholders and the corporation, and after the proceeding has been lawfully and successfully commenced, the petition demanding a determination of the value of shares of the dissenting shareholders can proceed. The appraisal procedure as provided by §262 of the Delaware General Corporate Law seems to be very rigid and complicated, but the Court of Chancery has a wide discretion in organizing the appraisal proceeding in the most efficient and the most suitable way for the case at stake.\textsuperscript{119}

The first step that is taken in the appraisal proceeding is notifying a hearing. If so ordered by the Court of Chancery, the Register in Chancery gives a notice of the place and time of the hearing of the appraisal petition.\textsuperscript{120} Such a notice shall be given to the surviving or resulting corporation by certified or registered mail and to the dissenting shareholders mentioned on the list delivered by the corporation at the addresses stated on the list. The notice is also given by one or more publications in a newspaper generally circulated in the City of Wilmington not later than one week before the date of the hearing or by publication

\begin{footnotes}
\item[116] Welch, Turezyn, Saunders, supra note 63, at 747.
\item[118] Welch, Turezyn, Saunders, supra note 63, at 753, note 134.
\item[119] Id., Del. Code Ann. tit. 8, § 262 (h) (2016) stating that “the appraisal proceeding shall be conducted in accordance with the rules of the Court of Chancery, including any rules specifically governing appraisal proceedings”.
\end{footnotes}
deemed advisable by the Court. The costs of the notice about the hearing are borne by the corporation\textsuperscript{121}. The shareholders demanding the appraisal of their shares and holding stock represented by certificates may be required by the Court to submit such certificates to the Register in Chancery in order to make a notation of the pendency of the appraisal proceeding on a certificate. The Court is empowered to dismiss the appraisal proceeding towards a shareholder who failed to comply with a request of submitting a certificate of stock\textsuperscript{122}. Furthermore, according to §262(g) the Court is obliged to dismiss the appraisal proceedings under the given conditions. As this provision was introduced to the Delaware General Corporation Law as an amendment in 2016 it will be discussed in the next chapter of the paper.

At the hearing the Court determines the shareholders who complied with the preliminary obligations and therefore became entitled to appraisal rights\textsuperscript{123}. The moment of determining the shareholders entitled to the appraisal is as significant as prior to the determination, in its discretion the Court may proceed to trial upon application by the corporation or by any shareholder entitled to participate in the appraisal proceeding\textsuperscript{124}. Any dissenting shareholder is entitled to participate fully in all proceedings if his name is on the duly verified list provided by the corporation and if he submitted their certificates of stock until the Court determines that such a shareholder is not entitled to appraisal rights\textsuperscript{125}.

During the appraisal proceeding the Court of Chancery determines the fair value of the shares of the dissenting shareholders\textsuperscript{126}. Besides the fair value of the shares determined by the Court, pursuant to §262(h) the dissenting shareholders are entitled to the statutory interest unless otherwise determined by the Court for good cause shown. The statutory interest is compounded quarterly from the effective date of the merger through the date of payment of the judgment and accrue at five percent over the Federal Reserve discount rate. The latest amendments to the Delaware General Corporation Law introduced in 2016 provided for a pre-judgment payment made by the corporation in order to avoid paying the statutory interest. This provision will be discussed in details in the next chapter of the paper.

\textsuperscript{121} Id.
\textsuperscript{122} Id.
\textsuperscript{123} Del. Code Ann. tit. 8, § 262 (g) (2016).
\textsuperscript{124} Del. Code Ann. tit. 8, § 262 (h) (2016).
\textsuperscript{125} Id.
\textsuperscript{126} Id., for the analysis of the issue of the fair valuation of the shares see part 3.3.
Once the fair valuation of the shares is determined by the Court, the Court directs the payment of such a fair value of the shares, together with due interest, by the corporation to the stockholders entitled to the payment. The payment must be made to each entitled shareholder forthwith in the case of the shareholders holding uncertified stock and upon the surrender to the corporation of the certificates representing stock in the case of the shareholders holding shares represented by certificates. The Court’s decree in the appraisal proceeding is enforceable in the same way as other decrees of the Court of Chancery, regardless of the fact whether the corporation is a corporation of the state of Delaware or of any other state.

According to §262(j) the costs of the appraisal proceedings are determined by the Court and taxed upon the parties in the way deemed by the Court equitable in the circumstances of the case. Pursuant to a stockholder’s application, the Court may order that all or a part of the expenses borne by any stockholder with regard the appraisal proceedings, including, but not limited to, the fees and expenses of experts and the reasonable fees of attorneys will be charged pro rata against the value of the shares entitled to the appraisal. As the expenses may be charged pro rata against all of the shares being the subject of the appraisal, the costs of the proceeding, as well as the benefits, may be also shared between the dissenting shareholders that do not participate in the appraisal proceedings. Moreover, as pointed out by the doctrine, the Court usually does not burden the dissenting shareholders with the costs of the litigation, as it would result in cutting down the full value of their shares.

As the result of the appraisal proceedings the shares of the corporation to which the shares of the dissenting shareholders would have been converted if they had approved the merger, have the status of authorized and unissued shares of the corporation.

3.3 Fair valuation of the shares

The purpose of the appraisal proceeding is the fair valuation of the shares of dissenting shareholders by the court. The meaning of the fair value has never been defined by the Delaware’s statute, however such a meaning was clarified by the Delaware Supreme Court in

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128 Id.
130 Welch, Turezyn, Saunders, supra note 63, at 767.
1950. In the case *Tri-Continental Corp. V. Battye*132 the Delaware Supreme Court stated that “The basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him, viz., his proportionate interest in a going concern. By value of the stockholder’s proportionate interest in the corporate enterprise is meant the true intrinsic value of his stock which has been taken by the merger.” In the recent years this concept of the fair value of the shares was expanded by defining “what has been taken from the shareholder” as “the pro rata share of the value of the company as a whole in most jurisdictions.”133 During the determination of the fair value of the shares, the Court takes into account all relevant factors, excluding however elements of value arising from the accomplishment or expectation of the merger134. The Delaware General Corporate Law does not impose on the court any other requirements with regard to fair valuation of the shares in the appraisal proceedings. Therefore, the court has a wide discretion as to the means and methods used for that purpose. Consequently, the court’s approach to the determination of the fair value of the shares is essential for protecting minority shareholders through the appraisal remedy and the appraisal proceedings. If a way in which the court determines the fair value of the shares does not serve this goal, minority shareholders “will ignore the appraisal remedy in favour of other means of challenging fundamental transactions, principally breach of fiduciary duty claims, which may be less efficient and more time consuming to resolve.”135

As mentioned, the method of determining the fair value of the dissenting shareholders’ shares depends on the court’s approach and choice. In the state of Delaware, until 1983 the traditional and exclusive method of the valuation of the shares was the Delaware block method136. To determine the value of the shares using the Delaware block method first several steps must be taken. In the first place, it is necessary to determine the value of a corporation including three different calculations: based on the corporation’s asset value, the corporation’s earnings value and on the corporation’s market value. Secondly, the court as an appraiser

135 Wertheimer, supra note 6, at 626.
must assign a percentage weight for each calculated value. The weight established for each relevant factor is based on the facts of a case. Finally, each value is “multiplied by a weighted factor expressed as a percentage of the whole so that the products of the calculations when added together will equal one hundred percent and represent the total value of each share.” Consequently, the fair value of the corporation is equal to the weighted average of the three separate calculations of the value of each relevant factor. If the value of the corporation determined in this way is considered as a reasonable by the court, the total number of the shares of each dissenting shareholder is multiplied by such value and the result is a sum of money which will be paid to the shareholder for his shares.

The Delaware block method was strongly criticized by scholars and practitioners, especially with regard to its validity and reliability. The first argument of the doctrine against this method was that the Delaware block method takes into account only the value of the corporation’s assets, earnings and market value while ignoring other relevant factors such as post-merger gains or rescissory damages. Furthermore, the Delaware block method was criticized with regard to its formulaic approach to valuation of a corporation and its inflexibility. Others argued that this method always results in an undervalued corporate stock. Another argument raised by the doctrine was that the Delaware block method disadvantages dissenting shareholders as it is based on the assumption that the corporations “will not be operated to achieve its highest valuation. For example, if a corporation’s highest value is based on its asset value, rational owners of the corporation would seek to achieve that value, yet the Delaware block method averages that value with lesser values.” The doubts concerning the Delaware block method as a method of valuation of the shares in the appraisal proceedings were confirmed in 1983, when the Delaware Supreme Court issued one of its

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137 As a particular weight is assigned to each value, the Delaware block method is also called weighted average method or weightening method.
139 Clardy, supra note 136, at 291.
140 Wertheimer, supra note 6, note 66.
141 Clardy, supra note 136, at 291.
142 Allred, supra note 138, at 210.
144 Allred, supra note 138, at 211.
146 Wertheimer, supra note 6, note 67, Schaefer, supra note 145, at 1038-1039.
landmark decisions in the case *Weinberger v. UOP, Inc.* In its decision, the Delaware Supreme Court abandoned the Delaware block method as the exclusive method for determining the fair value of shares. The Delaware Supreme Court stated that the Delaware block method “to the extent it excludes other generally accepted techniques used in the financial community and the courts, it is now clearly outmoded.” In this case the Delaware Supreme Court adopted “a more liberal, less rigid and stylized, approach to the valuation process” and declared that this more liberal approach “must include proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court.” In this decision, the Delaware Supreme Court also supported the findings given in *Tri-Continental Corp. V. Battye* that all relevant factors should be taken into account while determining the fair value by stating that “elements of future value, including the nature of the enterprise, which are known or susceptible of proof as of the date of the merger and not the product of speculation, may be considered. (...) fair value also includes any damages, resulting from the taking, which the stockholders sustain as a class.” Although the Delaware Supreme Court rejected the Delaware block method as the exclusive method of the valuation of shares, courts still used this method arguing that *Weinberger v. UOP* case did not reject this approach as such.

The decision of the Delaware Supreme Court in the *Weinberger v. UOP* case, opened the possibility to adopt other methods of the valuation of the shares in the appraisal proceedings. Since then, the most significant method used in Delaware has been the discounted cash flow method. In this method, the value of a corporation is determined by “the present value of the discounted stream of future free cash flows.” The Delaware Court of Chancery described the discounted cash flow method as “in many situations (...) the single best technique to estimate the value of an economic asset” as it “entails three basic components: an estimation of net cash flows that the firm will generate and when, over some period; a terminal or residual value equal to the future value, as of the end of the projection period, of the firm’s cash flows beyond the projection period; and finally a cost of capital with which to discount to a present value both the projected net cash flows and the estimated

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148 Wertheimer, supra note 6, at 617.
149 *Weinberger v. UOP, Inc.*, 457 A.2d 701 at *712.
150 Id., at *704, *713.
151 Id., at *701.
152 Allred, supra note 138, at 209.
153 Wertheimer, supra note 6, at 627.
154 *Hamermesh, Wachtter, supra note 136, at 125.*
Although the discounted cash flow method has been the most often used method of determination of the fair value of the shares in the appraisal proceedings since Weinberger decision, it has not been considered as the exclusive method. The Delaware’s courts have used various methods in the fair valuation of the shares in the appraisal proceedings. These include: valuation based on asset value, valuation based on earnings value, comparable companies analysis, comparable transactions analysis or valuation based on transaction price.

3.4 Exclusivity of the appraisal remedy

Exclusivity of the appraisal remedy indicates that other potential remedies, such as damage actions or injunctive suits are not available for dissenting shareholders. It means that in case of an event triggering appraisal rights the only remedy available for dissenting shareholders is buy-out of their shares by a corporation at the fair value determined by a court. Consequently, as a result of exclusivity of the appraisal remedy, a court extinguishes the shareholders’ claim other than the appraisal claims (e.g. challenge the directors’ decision making, alleging directors’ misconduct resulting in a devaluation of the shares before an event triggering appraisal rights occurred).

The appraisal statutes’ approach to the exclusivity of appraisal rights is not uniform and is not always clear. Some states provide for appraisal rights as the exclusive remedy, others state that the appraisal remedy is exclusive under certain circumstances or with some exceptions. Finally, some appraisal statutes do not determine the exclusivity of the appraisal remedy at all. The Delaware General Corporation Law is an example of such a statute, as it is silent about the exclusivity of appraisal rights. For that reason, this issue remained a long time controversial in litigations conducted in Delaware’s courts. In early cases Delaware’s courts held that appraisal rights are the exclusive remedy of dissenters, unless cases involving

156 Wertheimer, supra note 6, at 628.
157 Id., at 629, Welch, Turezyn, Saunders, supra note 63, at 760.
158 Welch, Turezyn, Saunders, supra note 63, at 760.
159 McLellan, supra note 86, at 115.
162 Pepin, supra note 161, at 956.
illegality or fraud. In its later judgments, the Delaware Supreme Court stated that dissenting shareholders could claim to enjoin a merger if they showed that the merger was unfair, inadequate and that it did not serve a proper business purpose and that a class action suit is available for dissenting shareholders in order to obtain recisionary damages from an acquiring corporation based on a breach of fiduciary duty or misrepresentation with regard to a tender offer. As the result of these decisions dissenting shareholders could bring a class action suit claiming recissory damages or an injunctive action as a collateral action to the appraisal proceeding. The application of these decisions and pursuing two collateral actions by minority shareholders were unstable and appraisal rights, as a remedy at law, “had lost much, if not all, of its importance.”

The situation, however, changed in 1983 when the Delaware Supreme Court issued a decision in the case Weinberger v. UOP which formed the current application of the exclusivity of appraisal rights in Delaware. In its decision, the Delaware Supreme Court held that the appraisal remedy is the exclusive remedy for a dissenting shareholder, if, in case of a cash-out merger, his only allegation is an inappropriate cash value of his shares determined by the directors. However, the Delaware Supreme Court also held that the appraisal remedy is not the exclusive remedy of a dissenting shareholder in cases “where fraud, misrepresentation, self-dealing, deliberate waste of corporate assets, or gross and palpable overreaching are involved.” Upon the decision of the Delaware Supreme Court several conditions must be met in order to invoke the exclusivity of the appraisal remedy with regard to decision-making triggering appraisal rights. These are: (a) all cash freeze-out merger, (b) a dissenting shareholder’s claim must allege only inappropriate cash value of his shares determined by the directors, (c) a dissenting shareholder’s claim must not concern directors’ other decision-making, and (d) a dissenting shareholder’s claim only seeks cash relief.

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167 Id., at 899.
168 Weinberger v. UOP, Inc., 457 A.2d 701 at *714.
169 Id.
170 Pepin, supra note 161, at 968
171 M. Pepin, however, points out the exception to this condition. She states that the collateral claim is not precluded by appraisal rights, even if a dissenting shareholder challenges only valuation of his shares by directors, if directors’ decision-making “was accompanied by (1) deception by the directors or shareholders (if the shareholders had a choice to make), (2) conflict of interest in decisionmaking by the directors or shareholders, or (3) waste.” Id., at 969.
excluding allegation of facts sufficient to justify non-damage relief\textsuperscript{172}. Some scholars argue that the decision in the \textit{Weinberger v. UOP} case did not clarify whether the appraisal remedy is the exclusive remedy of dissenting shareholders in cash-out mergers and that the Delaware Supreme Court did not intend to state the exclusivity of the appraisal remedy\textsuperscript{173}. They state that the exclusivity of the appraisal remedy is a function of “entire fairness” and this function is reinforced by courts that follow the assumption of the non-exclusivity of the appraisal remedy, unless an appraisal statute provides otherwise\textsuperscript{174}.

The issue of the exclusivity of the appraisal remedy with regard to the short-form mergers is less complicated. It is settled in case law, that, if a controlling shareholder holds at least 90% of shares of a corporation and minority shareholders may be cashed-out without the shareholders’ vote, the appraisal remedy is the exclusive remedy of dissenting shareholders\textsuperscript{175}.

\textsuperscript{172} Id., at 968-972.
\textsuperscript{173} Coleman, supra note 143, at 790-791.
\textsuperscript{174} Id., at 795.
Chapter III Appraisal arbitrage

1. The misuse of appraisal rights

Appraisal arbitrage is a notion used for describing a certain investment strategy that most often involves the misuse or even the abuse of appraisal rights. In recent years shareholder activism and arbitral arbitrage activity has significantly increased the number of appraisal proceedings in the state of Delaware which has not necessarily served the minority shareholders who opposed a merger to have a judicial appraisal of the value of their shares and then to have their shares bought back by a corporation at the appraised value. To address the abuse of appraisal rights and appraisal arbitrage, the state of Delaware introduced in 2016 amendments to the Delaware General Corporation Law limiting appraisal rights by a restriction of stockholders entitled to the appraisal remedy.

Appraisal arbitrage is an investment strategy, usually used by hedge funds, in which an investor purchases shares of a corporation after a cash-out merger was announced, very often just before shareholders’ voting on the merger. The only intention of such a purchase is asserting appraisal rights provided by the statute. If during the proceeding, the court determines that the price of the transaction was lower than the fair value of the shares, then the difference between the value determined by a court and the transactional price represents the return of an investor on his investment. Appraisal arbitrage is a strategy with no risk and with a potentially high-return. In those cases appraisal rights do not serve as a remedy for dissenting shareholders but as an arbitrage for the hedge funds (arbitrageurs) which recently have become the dominant group of players on the appraisal litigation’s field. The hedge funds are very sophisticated entities which developed appraisal arbitrage as a highly specialized form of investment. Such an investment strategy based on appraisal rights “has utterly transformed what may once have been accurately characterized as a sleepy corporate law backwater.” For some of the hedge funds, appraisal arbitrage is the exclusive investment strategy and they have been established for such a purpose.

179 Abigail Pickering Bomba et al., New Activist Weapon— The Rise of Delaware Appraisal Arbitrage: A Survey of Cases and Some Practical Implications, FRIED, FRANK, HARRIS, SHRIVER & JACOBSON LLP, June 18,
Undoubtedly, the investors using appraisal arbitrage as a separate investment strategy abuse a loophole in the appraisal rights system. Appraisal arbitrage activity exploits appraisal rights that are intended to protect minority shareholders exposed to abusive mergers taking advantage of them by providing them a remedy at law. Moreover, appraisal arbitrage “commonly affects the public dynamics surrounding challenges to deals and can have a significant effect on the certainty of and ultimate price paid in a deal.”

The revision of the appraisal mechanism was necessary due two reasons. At the first place, there was a need for restoring a marketplace balance and, secondly, for remedying the negative impact that appraisal arbitrage has on surrounding corporations since they are burdened by unfair economic advantage gained by arbitrageurs.

As the result of increased shareholder activism and appraisal arbitrage activity, the number of filed petitions for appraisal significantly increased in the recent years. During the period between 2004 and 2015, approximately 5% of transactions for which appraisal rights were available resulted in at least one petition for appraisal in the Delaware Court of Chancery. In 2011 the number of appraisal petitions more than doubled and in 2013 appraisal petitions were filed for more than 15% of transactions for which appraisal rights were available. Simultaneously the value of appraisal claims increased. The value of appraisal claims was nearly $1.5 billion in 2013, nearly 1% of the value of all merger activity in that year, and it increased ten times from 2004. Moreover, in the given period, eight appraisal proceedings involved more than $100 million and four of them occurred in 2013, including the case of Dell which involved $654 million worth of dissenting shareholders. As pointed out by Charles R. Korsmo and Minor Myers who studied the appraisal petitions filed in the Delaware Court of Chancery against public corporations in the period between 2004 and 2013, the most remarkable aspect of increased appraisal activity in Delaware is that the number of the appraisal claims increased independently from the number of consummated...
mergers. The authors observe that between 2011 and 2013, in contrary to the period between 2007 and 2008, the increase of the appraisal proceedings and its economic significance did not occur simultaneously with an increase in merger activity as such. From their point of view, the increased number of appraisal proceedings reflects an increasing interest in appraisal rather than “a mere cyclical phenomenon tied to the conditions of the merger market.” Moreover, besides the increased number of appraisal petitions and the increased value of the appraisal claims, during the period 2004 - 2013 the number of repeat petitioners increased. These are petitioners who filed more than one appraisal petitions in the given period. The repeat petitioners were involved in more than 80% of the appraisal proceedings since 2011. These repeat petitioners are typically the hedge funds using appraisal arbitrage as an investment strategy.

Wei Jong, Tao Li, Danquing Mei and Randall Thomas documented that the increased number of the appraisal petitions and the increased value of the appraisal claims in the recent years is the result of the intensified appraisal arbitrage activity taken usually by the hedge funds. Their studies showed that the dominance of the hedge funds in appraisal arbitrage strategy is clear since they represent 75% of the dollar volume involved in all appraisal petitions filed in the recent years. Moreover, the top seven hedge funds filed petitions for more than 50% of the dollar volume of the appraisal petitions and the top seven law firms representing such hedge funds are mentioned in approximately 50% of all the appraisal cases.

The main reason of the increased appraisal arbitrage activity, which is most often invoked by scholars and practitioners, is the decision of the Delaware Court of Chancery taken in 2007 in the case In re Appraisal of Transkaryotic Therapies, Inc. This case is widely recognized as the case that opened the door for appraisal arbitrage activity. According to §262 of the Delaware General Corporate Law, appraisal rights are available for stockholders holding shares of stock at the date of making the demand for appraisal and
opposing a merger triggering appraisal rights by voting against the transaction or abstaining from voting. In the Transkaryotic Therapies, Inc. case, the shareholders, claiming appraisal for all their shares, purchased the major part of their shares after the merger was announced and after the record date for the shareholders’ vote on the merger, but before the effective date of the merger. The issue raised in this proceeding was whether under §262 of the Delaware General Corporation Law, a stockholder who purchased his shares after the record date is obliged to prove that each of his specific shares, for which the appraisal is sought, was not voted in favour of the merger by the previous shareholder.

The Court of Chancery held that appraisal rights are available for shares purchased after the record date. The Court of Chancery reasoned that, as under §262 appraisal rights are available only for a record holder, the perfection of these rights is determined by the actions of a record holder. Consequently, as long as the number of shares seeking appraisal is less than or equal to the number of shares that voted against the merger or abstained from voting, shares purchased after the record date can be used to assert appraisal rights. By its decision the Court of Chancery “created a timing advantage for activist shareholders and hedge funds to delay purchasing a target company’s shares until the very last minute. This timing advantage allows for prospective appraisal investors to make better investment decisions by having more time to consider the most current market, industry and company information.” Scholars and practitioners argue that this decision was a significant reason for the increase of appraisal arbitrage activity, as arbitrageurs “are taking advantage of the flexibility of Transkaryotic.”

However, there can still be found voices dismissing that theory. According to Charles R. Korsmo and Minor Myers Transkaryotic Therapies, Inc. case has a marginal influence on the increase of the time period during which the potential appraisal petitioners may purchase their shares. They argue that appraisal rights have always been available for shares purchased between the time at which a merger was announced and the record date, and that this ruling ensures that corporations may not set the record date, as an opportunistic action, to avoid appraisal claims. Moreover, the authors point out that the decision in Transkaryotic Therapies, Inc. concerns transactions which are voted by a shareholders’

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194 In re Appraisal of Transkaryotic Therapies, Inc., WL 1378345, at *1.
195 Id., at * 4.
196 Mei, supra note 193, at 85.
197 Boyd, supra note 180, at 505.
198 Korsmo, Myers, supra note 178, at 1578.
199 Id., at 1579.
meeting, while many transactions are not voted on by shareholders. Under the Delaware General Corporate Law, mergers can be approved by written consent of majority of shareholders and some mergers, like short-form mergers and, to a certain extent, mergers of domestic corporations can be consummated without a voting of shareholders. Therefore, the decision of the Court of Chancery in Transkaryotic Therapies, Inc. has no impact on those kind of transactions, while their proportion is substantial in M&A activity and even larger in appraisal proceedings.\textsuperscript{200}

To justify their opinion that the ruling in Transkaryotic Therapies, Inc. given by the Delaware Court of Chancery in 2007 has not had an impact on the increase of appraisal petitions, the authors analyzed appraisal petitions filed before and after the decision was issued and analyzed the share of transactions possibly affected by the ruling in all appraisal activity in the given period. Korsmo and Myers found that during the period between 2004 and 2007, the appraisal petitions were filed for approximately 5% of the transactions with a tender offer and for approximately 5% of the transactions voted on by shareholders (so transactions potentially affected by the Transkaryotic Therapies, Inc. ruling). In the period after the decision (2009-2013), the appraisal petitions were filed for 13% of the transactions with a tender offer and for 9% of the transactions voted on by shareholders. This data clearly show that the Transkaryotic Therapies, Inc. has not caused the increase of the appraisal activity related to the transactions potentially affected by it, as one would expect. To the contrary, the significant increase of the appraisal petitions is noticeable with regard to transactions falling outside the scope of the ruling. The authors conclude their analysis by stating that “whatever legal changes were wrought by the Transkarytoic decision do not appear to have moved the needle on appraisal activity.”\textsuperscript{201}

The findings of the Delaware Court of Chancery in the case Transkaryotic Therapies Inc., were not one-time exceptions. The Delaware Court of Chancery reaffirmed them in the more recent cases In re Appraisal of Ancestry.com, Inc.\textsuperscript{202} and Merion Capital LP v. BMC Software, Inc.\textsuperscript{203}. In the Ancestry.com case, the hedge found purchased the shares in Ancestry.com after the record date and filed a petition for appraisal. The corporation argued that appraisal rights were not available for those shares as the petitioner was not able to prove that the shares he purchased did not vote in favour of the merger. The Delaware Court of

\textsuperscript{200} Id.
\textsuperscript{201} Id.
Chancery found, as in the *Transkaryotic Therapies Inc.* case, that “the actions of beneficial holders are irrelevant in appraisal matters” and that the petitioner was able to assert appraisal rights for the shares purchased after the record date as long as he had “at least as many shares not voted in favour of the merger as the number for which demand was made.” In the *BMC Software* case, the Delaware Court of Chancery reaffirmed the previous decisions by stating that the petitioner is not required to demonstrate that the shares were used to vote in favour of the merger by any previous owner. While the position of the Delaware Court of Chancery taken in *Transkaryotic Therapies Inc.* case opened the doors for appraisal arbitrage, the decisions in *Ancestry.com* and *BMC Software* cases supported this practice. It is also worth to mention the very recent case *In re Appraisal of SWS Group, Inc.* decided by the Delaware Court of Chancery in May 2017, in which the court stated that if a petitioner is recognized as arbitrageur, then the appraisal price may be lower than a merger price. Although that case did not deny or restrict appraisal arbitrage, it demonstrated that appraisal arbitrage is not any longer a no-risk investment strategy, as it used to be. It is too soon to say whether this finding will limit appraisal arbitrage activity, but it possibly make the investors to reconsider their investment strategy and their expected profits.

Another reason given by scholars and practitioners as the explanation of the increased appraisal activity is the method of calculating the interest rates for petitioners provided by the Delaware General Corporate Law. Pursuant to §262(h) the shareholders during the appraisal procedure are entitled to “interest from the effective date of the merger through the date the date of the of payment of the judgment” unless good cause is shown and the court decides otherwise. The interest “shall be compounded quarterly and shall accrue at 5% over the Federal Reserve discount rate.” The statutory interest rate provided for the appraisal remedy is significantly higher than the current market rate, which is 1.75% as effective from June 2017. The purpose of the statutory interest is compensating the shareholders asserting appraisal rights while they are waiting for the payment of the appraisal claim and to compensate them the expenses that they may bear with regard to the appraisal proceeding. The dissenting shareholders should be compensated as “the shareholder places the investment

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207 Id.
209 Boyd, supra note 180, at 509.
‘in limbo’ until the court rules on the petitioner’s right to appraisal and determines the fair market value of the shares. As a result, shareholders have no right to receive income from their ownership in the merging corporation while waiting on an uncertain decision by the court system.”211 The interest rate provided by the Delaware General Corporate Law is regarded as a factor that mitigates risk linked to the exercising of appraisal rights as the result of the appraisal proceeding is highly uncertain for dissenting shareholders. In this context the statutory interest rate is a kind of guarantee of a rate of return in the case when, as the result of the appraisal proceeding, a dissenting shareholder receives the amount that is only minimally higher that the merger price or even lower.212 In this way the hedge funds for which the appraisal activity is an investment strategy benefit from the statutory interest rate. This is a clear abuse of appraisal rights as they are provided in order to protect long-term shareholders who do not want to be a part of a changed corporation after merger.213 and not in order to provide some kind of minimum return rate for investors purchasing shares of a corporation in order to file the appraisal petition. Some practitioners argue that even if the statutory interest rate is not used as a separate opportunity for an investment (due to periods of “ultra-low” interest rates), the statutory interest rate being a part of appraisal rights can be “at least a meaningful offset to the extended period of illiquidity and litigation costs imposed on the dissenting shareholders for the duration of the proceedings.”214 While the appraisal activity as such brings almost no risk, providing the statutory interest rate makes appraisal arbitrage an even more attractive and lucrative investment strategy and may be considered as an unquestionable incentive for bringing the appraisal claims by shareholder activists and hedge funds.215 Besides making the abuse of appraisal rights by arbitrageurs more attractive, the statutory interest rate can make corporations enter into unattractive settlements with dissenting shareholders seeking the appraisal, as they are threatened by the huge costs resulting from paying a dissenting shareholder the statutory interest.216 Furthermore, Craig Boyd accurately points out that such a fear of corporations may threaten corporate mergers.

211 Boyd, supra note 180, at 508.
213 Boyd, supra note 180, at 509.
214 Wolf et al., supra note 212, at 2.
215 Mei, supra note 193, at 86.
216 Boyd, supra note 180, at 510.
217 Wolf et al., supra note 212, at 2.
activity as such and enables arbitrageurs to receive “a fair amount of leverage by threatening to impose an extremely large interest payment.”  

Once again, Charles R. Korsmo and Minor Myers do not agree with the theory presented by the doctrine and they state that the statutory interest rate is not a factor increasing the appraisal activity. In the first place, the authors argue that the statutory interest rate, 5% over the Federal Reserve discount rate, is not an attractive return rate for the appraisal petitioners in the light of the risks and uncertainty of the appraisal proceeding. Although the statutory interest rate is better than an amount that dissenting shareholders might get in a money market account, it still, according to Korsmo and Myers, does not compensate them enough for the risk of the appraisal proceedings in terms of costs, length and uncertain result of the court’s determination. The scenario in which, the investors, usually arbitrageurs, invest a significant amount of money (“hundreds of millions of dollars”) in the appraisal proceedings and in their uncertain results, just to obtain a rate of return from the statutory interest rate, even if it is well above the market interest rate, is not credible in the author’s view.

Although Korsmo and Myers argue with both theories potentially explaining the increase in the appraisal activity in the recent years by denying them and presenting counter-arguments, they do not find themselves the explicit factor being the cause of the raised appraisal arbitrage. However, the authors provide one explanation that could be a cause of the increased appraisal activity. They suspect that the raise in appraisal arbitrage is just a result of the activity of a few investors who considered the appraisal activity as a method “for salvaging an investment following a bad merger, became intrigued by the opportunity, and explored it further.” Based on the results, successful from an investor’s point of view, of the appraisal claims brought by those few investors, others simply decided to follow that investment strategy as well what resulted in a significant increase of the appraisal petitions in the recent years.

218 Boyd, supra note 180, at 510.
219 Korsmo, Myers, supra note 178, at 1580.
220 Id.
221 Id., at 1580-1581.
222 Id., at 1582.
223 Id.
2. Delaware General Corporation Law’s 2016 amendments

2.1 Elimination of de minimis appraisal claims

To address the abuse of appraisal rights by appraisal arbitrageurs and thereby to limit the appraisal activity the state of Delaware introduced two significant amendments to the appraisal rights provisions provided by the Delaware General Corporate Law. The amended provisions of §262 came into effect on August 1, 2016.

The first amendment introduced the elimination of de minimis appraisal claims. Pursuant to the amended §262(g) if the shares of the class or series of stock of a constituent corporation for which appraisal rights are available were listed on a national securities exchange immediately before the merger, the Court of Chancery shall dismiss the appraisal proceedings as to all holders of such shares who are otherwise entitled to 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 this title”224, i.e. short-form mergers provided for a merger of parent corporation and subsidiary or subsidiaries and a merger of parent entity and subsidiary corporation or corporations.

According to the synopsis of the Delaware House Bill 371 amending title 8 of the Delaware General Corporate Law225 the limitation of appraisal rights for the shares traded on a national securities exchange reduces the risk “that the petition for appraisal will be used to achieve a settlement because of the nuisance value of discovery and other burdens of litigation.”226 Thereby, the Delaware General Corporate Law limits the appraisal claims for which the valuation dispute is not substantial and which could be used as a mean of achieving a settlement with a corporation that may be, as discussed above, very often threatened with the high costs of payment of the statutory interest and the costs of litigation itself. In other words, the amendments aim to reduce appraisal arbitrage as they limit the type of claims that are usually considered to be equivalent to the activity of appraisal arbitrageurs227. The synopsis also provides for the explanation of excluding short-form mergers from de minimis exception. In the short-form mergers there is no requirement for the board of directors of a

226 Id.
227 Boyd, supra note 180, at 511.
corporation to approve and to recommend the merger, so there is no other remedy at law available for shareholders and the exercising of appraisal rights is the only possibility for dissenting shareholders to remedy.\textsuperscript{228}

The assessment of the impact of de minimis exception on the appraisal activity is unfeasible at the moment, since the amendments came into effect several months ago. However, based on the empirical analysis of appraisal arbitrage presented by Wei Jang, Tao Li, Danqing Mei and Randall Thomas\textsuperscript{229}, the decrease in the appraisal petitions is supposed to be noticeable. The authors documented that the median of the petitioners’ stake size is $1.9 million, while the stakes with a value below $1 million and with the total number of shares not exceeding 1\% of all outstanding shares of a corporation are involved in approximately thirty two percent of the cases. Accordingly, the authors correctly project that due to de minimis exception the number of the appraisal petitions will drop by one quarter. They also conclude that introducing de minimis exception will not have an impact on shareholders’ motivation for exercising their appraisal rights\textsuperscript{230}.

The amendment introducing de minimis exception undoubtedly aims in addressing appraisal arbitrage and in limiting the appraisal activity as such by excluding from the scope of appraisal rights shares that are traded on a national securities exchange unless the shares represent the significant value and the significant part of the total number of shares of a corporation. Based on the given data it is possible to assume that this aim may be achieved to some extent, as the major part of the appraisal claims that may be equivalent to appraisal arbitrage is brought by the big hedge funds which can easily target a significant number of shares in a corporation with a value above $1 million and thereby fall into the scope of de minimis exception.

2.2 Pre-judgment payment

The second amendment to the Delaware General Corporate Law introduced in 2016 enables corporations to avoid a payment of the statutory interest (5\% over the Federal Reserve discount rate) by making a pre-judgment payment to dissenting shareholders. According to the amended §262(h) the surviving corporation may pay, at any time before the entry of judgment in the proceedings, “to each stockholder entitled to appraisal an amount in cash, in

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\textsuperscript{228} DE HB371, 2015-2016, 148th General Assembly. \\
\textsuperscript{229} Jiang, Li, Mei, Thomas, supra note 177, at 700. \\
\textsuperscript{230} Id.
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which case interest shall accrue thereafter as provided 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.” 231 As explained by
the synopsis of the Delaware House Bill 371 the sum of money paid before judgment to
petitioners is to be determined solely by the surviving corporation. There is also no inference
or requirement as to the amount of money paid as pre-judgment payment. Such an amount
may be equal, less than, or greater than the fair value of the shares being the subject matter of
the appraisal proceedings. Moreover, the surviving corporation may decide to make a pre-
judgment payment only to shareholders whose “entitlement to appraisal is uncontested.” 232

As discussed in the previous part of the paper, the relatively high rate of the statutory
interest might be considered as an incentive for the appraisal claims and might be a factor to
the increasing appraisal arbitrage, especially that this statutory interest rate is well above the
market interest rate. By just simply bringing the appraisal claims, the investors could get a
satisfactory rate of return, regardless of the result of the court’s determination of the fair value
of shares. Introducing the amendment enabling the corporations to make pre-judgment
payments in order to avoid paying the statutory interest may discourage the activity of
arbitrageurs as statutory interest will not provide any rate of return anymore. As documented
by Jang, Li, Mei and Thomas, the statutory interest rate triggered, in the period between 2000
and 2014, 6.5 percentage points of “additional appraisal filings” among all eligible mergers or
approximately a 45% increase in the appraisal petitions filed 233. It is reasonable to assume that
this amendment will limit appraisal arbitrage, especially that it is the corporations’ discretion
over an amount paid to dissenting shareholders. Even if the amount of the pre-judgment
payment is lower than the fair value of shares determined by the court, the corporations will
avoid a huge financial burden by paying much lower statutory interest than they would be
supposed to pay without making any pre-judgment payment. As the result the exercising of
appraisal rights simply as an investment strategy based only on the rate of return obtained
from a payment of the statutory interest rate will not be profitable and attractive anymore for
the investors being arbitrageurs.

233 Jiang, Li, Mei, Thomas, supra note 177, at 700.
Chapter IV The perspectives of appraisal rights in Europe

1. Recent legislation within the European Union

The European Union’s legislation does not provide appraisal rights understood directly, as the shareholders’ right to dissent from mergers or other fundamental changes in a company accepted by majority shareholders and to receive a fair value of their shares determined by a court. However, some of the provisions of the EU company law imply the possibility of providing such rights by Member States within their national laws. Thereby, although the EU legislation does not impose on the Member States the general obligation to provide appraisal rights as a remedy at law in their national legal systems, it does not preclude introducing them into the Member States’ national legislations either. Indeed, some Member States, such as Germany, Italy and France, went beyond the EU legislation and provide minority shareholders for the right to challenge the fairness of a price offered for their shares upon merger. However, such rights more resemble the appraisal remedy available under US law in spirit, than in form234.

As to the EU provisions implying appraisal rights, one ought to take notice in the first place of the directive 2017/1132 relating to certain aspects of company law235. Pursuant to article 114, in the case of a merger by acquisition by a company which holds 90% or more of the shares of a company being acquired, the requirements applicable to mergers by acquisitions, such as drawing up a detailed written report and information on a merger by an administrative or management body of a company, examination of the draft terms of merger by experts and availability of documents for inspection by shareholders, shall not be imposed by the Member States if according to Member States’ national laws, the minority shareholders of the acquired company are entitled to have their shares purchased by the acquiring company and to receive consideration corresponding to the value of their shares, which, in the case of disagreement regarding such consideration, is determined by a court or by an administrative authority designated by the Member State. Based on this provision, there is no doubt that Member States may provide for appraisal rights in the case of a merger in their national legislation. The EU directive only provides for such a possibility without imposing any requirements concerning the scope or the form of such rights.

A similar provision may be found in the regulation 2157/2001 on the Statute for a European company (SE)\textsuperscript{236}. According to article 25(3), if the law of a Member State of a merging company provides for a procedure scrutinizing and amending the share-exchange ratio or a procedure compensating minority shareholders, without preventing the registration of the merger, such a procedure may apply to a formation of SE by merger if the other merging companies of Member States which do not provide for a such procedure explicitly accept the possibility for the shareholders of that merging company to be entitled to such a procedure. The analogous provision with regard to cross-border mergers of limited liability companies is provided by article 127 of the directive relating to certain aspects of company law\textsuperscript{237}. Once again, the European legislator permits for the procedure similar to the appraisal remedy but only in the case when a Member States already provides for such a remedy in its national legal system.

In the view of the foregoing EU provisions the Member States are free to adopt the rights entitling minority shareholders to appraise their shares. As mentioned above, some Member States indeed provide for such rights. As there are no uniform rules or requirements with regard to the appraisal remedy the scope of application, the procedure and the forms of such a remedy significantly differ from state to state. To illustrate the possible legal solutions regarding appraisal rights in Europe, the examples of national regulations in Germany, Italy and France will be discussed.

German law, in the first place, provides for appraisal rights in the Transformation Act\textsuperscript{238}. In case of a merger, if the exchange ratio has been determined at a too low a value, or if the membership in an acquiring company is not a sufficient consideration for the share of an acquired company, shareholders of an acquired company who are not entitled to bring an action against the entry into force of a merger resolution may demand from an acquiring company additional cash compensation which may amount to one tenth of the amount of the nominal capital or share capital allocated to the shares allotted. Such an additional payment is determined, as appropriate, by a court pursuant to the Act on Valuation Proceedings under Corporate Law and upon to shareholders’ petition\textsuperscript{239}. Under the Transformation Act appraisal rights are available for minority shareholder also in case of a

\textsuperscript{236}C\textsuperscript{ouncil Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE), OJ L 294, 10.11.2001, p. 1–21

237\textsuperscript{Supra note 235.}


239\textsuperscript{Section 15 (1) of the Transformation Act.}
merger upon which a company absorbs a company having a different legal form, or a merger upon which a stock company listed on the stock exchange merges onto an unlisted stock company and where a cash compensation is offered by an acquiring company to shareholders, objecting against a merger resolution of an acquired company, in return for their shares or memberships. If such shareholders assert that the offered cash compensation is too low, an appropriate cash compensation is determined by a court, upon those shareholders’ petition. The appropriate cash compensation is determined by a court also if a cash compensation was not offered by an acquiring company or was not offered in a proper way. The same provisions apply in case of a merger of companies having the same legal form but where restrictions to a disposition over the shares in an acquiring company are applicable and in case of an acquiring company being unable to acquire its own shares and where shareholders declare their withdrawal from the company. Additionally, the German legislator followed the article 25(3) of the regulation on the Statute for a European company (SE) and provided appraisal rights for minority shareholders in case of the formation of SE by a merger and the formation of a holding-SE.

In Italy, shareholders are entitled to withdraw from a company and to receive the value of their shares. Article 2437 of the Italian Civil Code explicitly provides a list of events triggering withdrawal rights. According to the provision, withdrawal rights are granted to shareholders who have not taken part in resolutions concerning (a) a change of a corporate purpose through a significant change of a company’s business, (b) a transformation of a company into a different legal entity, (c) a cross-border transfer of a company’s registered office, (d) a revocation of a winding up of a company, (e) a suppression of an enabling withdrawal right, (f) a change of criteria used for shares’ valuation in case of a shareholder’s withdrawal, and (g) amendments of the bylaws with regard to shareholders’ participation and voting rights. Withdrawal rights are also granted to shareholders who have not approved a resolution extending a company’s term or, establishing or removing limitations to the free

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240 Section 29(1) of the Transformation Act.
241 Section 34 of the Transformation Act.
242 Section 29(1) of the Transformation Act.
245 The scope of the expression “have not taken part” includes: not voting in favour of a resolution, an absence at a meeting, an explicit dissent and an abstention from voting. Ventoruzzo, supra note 244, at 64.
246 Ventoruzzo, supra note 244, at 62; Carone, supra note 244, at 326.
circulation of the shares, unless such withdrawal rights are excluded by the bylaws\textsuperscript{247}. Moreover, if a company is not established for an indefinite term and its shares are not listed on a regulated market, shareholders may withdraw from such a company by giving notice 180 days in advance\textsuperscript{248}. Additionally, article 2497 of the Italian Civil Code provides withdrawal right for shareholders of a company directed or coordinated by a different company, in case of (a) a change of a business purpose of a holding company if such a change directly affects an economic condition of a subsidiary, (b) a judgment ordering a payment of damages caused to a subsidiary by a holding company as a result of abusing its power of coordination and direction, and (c) a direction and coordination by a holding company being a circumstance modifying “the risk associated with the investment”, at the beginning or at the end such a direction and coordination\textsuperscript{249}. The criteria of evaluation of withdrawing shareholders’ shares are different in case of listed and non-listed shares. The valuation of the former is based on “the calculation of the arithmetic average of the closing prices of every negotiation day in the six months preceding the publication of the shareholders’ meeting’s call.”\textsuperscript{250} The value of the latter is determined by a company’s directors, supported by a non-binding opinion of an external auditor and of a board of auditors and taking into account “the fair value of the company’s assets and liabilities, its earning perspectives and the possible market value of the shares.”\textsuperscript{251} Article 2437 of the Italian Civil Code also provides a possibility of imposing different valuation criteria by the bylaws\textsuperscript{252}.

In France, an example of the regulation resembling appraisal rights may be found in article 236-6 of General Regulation of the AMF (Autorité Des Marchés Financiers)\textsuperscript{253}. Pursuant to that provision, if a company’s shares are listed on a regulated market and such a company is controlled by a shareholder or a group of shareholders, that controlling shareholder or group of shareholders must inform the AMF about their intention to significantly amend a company’s bylaws or articles, “in particular the provisions concerning the company’s legal form or disposal and transfer of equity securities or the rights pertaining thereto”, or about their decision to merge that company into a controlling company, or with another company controlled by a controlling company, to contribute or sell most or all of the

\textsuperscript{247} Article 2437 of the Italian Civil Code; Carone, supra note 244, at 327.
\textsuperscript{248} Id.
\textsuperscript{249} Ventoruzzo, supra note 244, at 63.
\textsuperscript{250} Id., at 66.
\textsuperscript{251} Id., at 66.
\textsuperscript{252} Id., at 66.
company’s assets, to change a company’s business or to suspend dividends for several financial years. Upon such information, the AMF evaluates the consequences of the intended changes with regard to interests and rights of holders of a company’s equity securities and voting rights. Then, based on its evaluation the AMF decides whether a buy-out offer for minority’s shares should be made by a controlling shareholder or a group of shareholders. If a buy-out offer is made, it must be approved by the AMF254.

The foregoing examples of the Member States’ national regulations providing shareholders’ rights resembling appraisal rights illustrate the different approaches of the national legislators to such rights. These national regulations differ in the scope of the rights, in the events triggering them (although fundamental changes in a company may be found as a common ground of these events), in the valuation methods and in the competent authorities.

2. The perspective of the development of appraisal rights in the European Union: necessity or redundancy?

As mentioned above, appraisal rights for minority shareholders are not provided by the European Union’s law and thereby there is no uniform legislative framework for such rights in Europe. However, it does not mean that the European Union does not sufficiently protect minority shareholders. The European company law does provide legal solutions that protect minority shareholders against fundamental changes in a company, especially in case of a merger or a takeover, in an efficient way. An introduction of appraisal rights into the European Union’s legal system, therefore, would be rather redundant because appraisal rights, as regulated under U.S. law, are not superior to the minority shareholders’ protection offered by the European Union255.

In the first place, European company law relies on the shareholders’ decision rights strategy. The directive relating to certain aspects of company law requires a domestic merger (precisely, a draft terms of mergers and any amendments to the articles of association necessitated by a merger) to be approved by the general meeting of each merging companies by a qualified majority of at least 2/3 votes attached to the shares of a company or to the subscribed capital represented. As the directive requires a majority at least 2/3 votes of

254 Article 236-6 of General Regulation of the Autorité Des Marchés Financiers; Kraakman et al., supra note 234, at 191.

255 As all states of the United States of America offer appraisal rights in case of a merger and as the Delaware’s statute provides for appraisal rights only in case of a merger, thus the provisions of European company law will be discussed and analyzed from the perspective of a protection of minority shareholders in case of a merger or a takeover.
shareholders, Member States may provide a higher threshold of majority required to approve a merger (e.g. Poland requires a majority of $\frac{3}{4}$ votes representing at least half of the subscribed capital of a company). Member States may also provide an approval of a merger by a simple majority in case when at least half of the subscribed capital of a company is represented on the general meeting. The same provisions are applicable to an approval of a division of a company by the general meeting of each company involved\(^{256}\). With regard cross-border mergers, the directive requires only an approval of the common draft terms of cross-border merger by the general meeting of each of the merging companies, without providing any further requirements, as each company involved in cross-border merger must comply with the national provisions of a Member State to which it is subject\(^{257}\). Thus, the requirements concerning the approval of a cross-border merger by the general meetings of companies involved are provided by national laws of Member States and usually, Member States require the application of provisions concerning domestic mergers. The protection of minority shareholders through shareholders’ decision rights, with regard to a merger, is stronger and more efficient in the European Union than in the United States, as, for example, the Delaware General Corporation Law requires only a simple majority approval of a merger\(^{258}\). Consequently, a merger that could potentially take advantage of a company and its shareholders is less probable and more difficult to be approved within the European Union as it must be approved by bigger part of each company’s shareholders than in the United States.

Secondly, pursuant to the directive relating to certain aspects of company law, Member States may provide in their national laws rules for a nullity of a merger, which also can be considered as an instrument protecting minority shareholders against changes in a company. However, requirements concerning the rules for a nullity of a merger laid down in article 108 of the directive are very restrictive. Therefore, even if Member States provide a possibility to declare a merger null and void, the right of shareholders to contest a merger is very limited, as there is a high risk of abuse of such rights by shareholders\(^{259}\).

Another legal instrument protecting shareholders as a whole, in case of both domestic and cross-border mergers is a requirement of an examination of the draft terms of a merger by experts. According to article 96 and article 125 of the directive relating to certain aspects of

\(^{256}\) Art. 93 (1) and art. 139 (1) of the directive relating to certain aspects of company law.

\(^{257}\) Art. 121 (1) (b) and art. 126 (1) of the directive relating to certain aspects of company law.

\(^{258}\) e.g. Del. Code Ann., tit. 8, §251 (c) (2016).

company law, an independent expert, acting on behalf of each company involved in a merger and approved or appointed by a competent administrative or judicial authority, examines the draft terms of a merger and draws up a written report to the shareholders. An independent expert may also be appointed by a competent authority for all companies involved at the joint request of those companies, if Member States provide for such an option. In his written report an independent expert is obliged to state whether the share exchange ratio proposed in the draft terms of a merger is fair and reasonable. He must also indicate the methods of valuation used for determining the share exchange ratio, state whether such methods are adequate while considering the specificity of a merger and if applicable, explain valuation difficulties. Consequently, an independent expert serves the same goal as a judge in an appraisal proceedings, he makes sure that the shareholders will receive a fair value of their shares. The examination of the draft terms of a merger by an independent expert is even more efficient than the appraisal remedy as it takes place before the shareholders’ vote on a merger, is a less expensive and quicker procedure, and, most importantly, it is an obligatory procedure applicable to every domestic merger of public limited liability companies in the European Union. In the United States, a minority shareholder must demand an appraisal, whereas the terms of a merger, notably the share exchange ratio, are examined automatically in the European Union, without a need to fulfil any obligatory prerequisites. Additionally, independent experts bear a civil liability towards the shareholders of an acquired company, in respect of their misconduct in the performance of their duties relating to an examination of the draft terms of a merger.\textsuperscript{260}

It is also worth to mention the position of shareholders in case of takeover bids. To protect minority shareholders, the directive on takeover bids\textsuperscript{261} provides two solutions: a so-called mandatory bid (article 5) and a sell-out right (article 16). The former requires a holder of a specified percentage of voting rights in a company, giving him control of that company, to make a bid to minority shareholders at the earliest opportunity and at the equitable price, which is considered as the highest price paid for the same securities by a bidder or by persons acting in concert with a bidder, over a period not less than six months and not more than twelve months before the bid. The latter enables holders of remaining securities to require a bidder to buy their securities at a fair price, where a bidder holds securities representing at least 90% of the capital to which voting rights are attached and 90% of the voting rights in the

\textsuperscript{260} Art. 107 of the directive relating to certain aspects of company law.

bidding company, or where a bidder, as the result of an accepted bid, acquired securities representing at least 90% of the bidding company’s capital carrying voting rights and 90% of the voting rights comprised in the bid. The analogous right is granted to a bidder, which is entitled to require holders of remaining securities to sell him their securities at a fair price under the same circumstances (squeeze-out right).

It is clear from the foregoing that European company law provides several legal solutions protecting minority shareholders against changes in a company as a result of a merger or a takeover. The protection granted to minority shareholders by the European Union’s legislation is sufficient and even more efficient than the protection of minority shareholders provided by appraisal rights under US law. The European approach provides this protection on each stage of a merger, is less expensive, quicker and applicable, in principle, to every merger or takeover that takes place within the European Union, without any further requirements. The European Union provides for a protection comparable to appraisal rights, especially through an obligation of an examination of the draft terms of a merger by an independent expert who examines and assesses the share exchange ratio, its fairness and reasonableness, and valuation methods. Therefore, an introduction of appraisal rights in the European Union legal system is redundant and not a necessity.
CONCLUSION

Appraisal rights are generally recognized within the United States of America. All fifty states provide appraisal statutes, however to a different extent. Some of the states recognize multiple events triggering appraisal rights, while others, like the state of Delaware, limit the scope the appraisal remedy’s application. Nevertheless, a merger is a common trigger of this remedy at law in all appraisal statutes in the United States. Despite of different approaches and theories concerning the purpose of appraisal rights developed over the years by scholars and practitioners, the main goal of providing appraisal remedy in a corporate law is protecting minority shareholders against fundamental changes in a corporation. The legal concept of appraisal enables minority shareholders to leave a changed corporation in return for a fair value of their shares, and allows majority shareholders and a corporation as such to introduce advantageous, from their point of view, changes in a corporation and its functioning without being hindered by minority shareholders. That is also a reason for which a traditional rule of unanimous will of shareholders with a single shareholder’s veto power was replaced by a rule of a majority consent at the end of 19th century when corporations began to grow and had to adapt themselves to altered economic activities.

Although the main purpose of appraisal remedy is protecting of minority shareholders, many argue that appraisal rights bring a little fairness for a high cost. Undoubtedly, perfecting appraisal rights is an elaborate procedure burdening dissenting shareholders with many formalities and prerequisites that must be fulfilled in order to bring an appraisal action. The asserting of appraisal rights is an expensive procedure with a lengthy duration and with an uncertain result. The dissenting shareholders and the corporation must not only bear the burden of costs of appraisal proceedings, but they also remain in uncertainty as to the result of a court’s determination. The judicial determination of a fair value of dissenting shareholders’ shares and the valuation methods used for this purpose are at a court’s wide discretion. The appraisal statutes state that a judicially determined value of shares must be a fair value, however they do not provide any guidance or requirements concerning specific valuation methods or their elements. That is the main element of an uncertainty of appraisal proceedings.

The number of filed appraisal petitions increased significantly in the recent years. The main reason of this increased appraisal activity is a development of appraisal arbitrage as an investment strategy. Investors, mainly hedge funds, discerned in asserting appraisal rights a
good investment opportunity, with almost no risk and a potential high return, and started to buy significant number of shares in corporations involved in a merger, after a public announcement of a merger but before an effective date of a merger, only in order to initiate appraisal proceeding. As the result, arbitrageurs were able to get a high return of their investment without bearing any risk, especially that besides a fair value of their shares, they were entitled to a statutory interest rate of 5% over the Federal Reserve discount rate. The provision of statutory interest made appraisal arbitrage an unusually attractive investment strategy based on taking advantage of appraisal rights providing a protection of minority shareholders. To address appraisal arbitrage, the state of Delaware introduced in 2016 amendments to the Delaware General Corporation Law limiting the scope of application of appraisal rights and entitling corporations to pre-judgment payments allowing to avoid a payment of statutory interest to dissenting shareholders. The introduction of these changes in Delaware’s appraisal statute made appraisal arbitrage less attractive because the payment of statutory interest is not guaranteed anymore and is less available as it limits the scope of shareholders for whom appraisal rights are available.

Even though appraisal rights may be an efficient instrument of protecting minority shareholders, the introduction of this legal concept into the legal system of the European Union is redundant. European company law does not provide for appraisal rights but at the same time it does not restrict Member States from including appraisal remedy into their national laws. Some Member States went beyond the uniform European standards and decided to provide appraisal or withdrawal rights for shareholders in their national legislation although European company law provides sufficient protection of minority shareholders. The European Union’s legislation relies on shareholders’ decision rights, on an examination of the draft terms of a merger by an independent expert, the possibility of a nullity of a merger and, in case of a takeover, on a mandatory bid and sell-out right. All these legal instruments provided by European company law efficiently protect shareholders as a whole and appraisal rights, as regulated in the United States of America, are not superior to these European solutions. Therefore, the introduction of appraisal remedy into the European Union’s legal system would be rather redundant than necessary.
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