

Client Alert

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Delaware Deal Planning: No Appraisal Rights for the Legal Acquiror's Stockholders Despite Extraordinary Dividend

The Delaware Court of Chancery recently rejected a stockholder's attempt to seek appraisal rights in a change-of-control transaction in which the stockholders were to receive an extraordinary dividend but retain their stock ownership. The court's decision confirms a straightforward application of the Delaware General Corporation Law, thus giving more certainty to transaction planners.

The Transaction

The litigation, *City of North Miami Beach General Employees' Retirement Plan v. Dr Pepper Snapple Group, Inc.*, was brought by stockholders of Dr Pepper Snapple Group, Inc. ("Dr Pepper") to challenge its pending merger with Keurig Green Mountain, Inc. ("Keurig"). From a legal perspective, Dr Pepper was the acquiring entity. As a result of the merger, however, Keurig's owners would own a majority of Dr Pepper's outstanding shares. Thus, Dr Pepper's public stockholders would retain their equity interest, but control of the company would be held by Keurig's owners.

The transaction was structured as a traditional reverse triangular merger in which Dr Pepper would use a newly formed merger subsidiary to merge with and into Keurig's holding company, which would survive the merger as a wholly owned subsidiary of Dr Pepper. At the effective time of the merger, the owners of Keurig's holding company would receive shares of Dr Pepper constituting 87% of Dr Pepper's outstanding stock, while Dr Pepper's pre-merger stockholders would own the remaining 13%. On the day before the merger, however, Dr Pepper would declare an extraordinary dividend of \$103.75 per share payable to its shareholders.

Thus, Dr Pepper's shareholders would receive a significant cash payment through the extraordinary dividend, but their shares would remain outstanding and they would continue to hold their interest in Dr Pepper after the transaction. To complete the merger, Dr Pepper's stockholders had to vote to approve (i) the share issuance to Keurig's owners as required by stock exchange rules and (ii) an amendment to Dr Pepper's certificate of incorporation to increase the number of authorized and unissued shares, which vote was required by Delaware law. Dr Pepper's proxy statement informed the stockholders that they were not entitled to appraisal rights.

The Court's Opinion

The Court of Chancery rejected the plaintiffs' argument that Dr Pepper's stockholders were entitled to appraisal rights in connection with the transaction. First, the court said that under the Delaware General Corporation Law, appraisal rights are only available to a "constituent corporation" in the merger, which means a party being merged (whether the survivor or non-survivor). Because Dr Pepper used a reverse triangular merger structure, its merger subsidiary was the "constituent corporation." Second, the court held that even if Dr Pepper had been a "constituent corporation" to the merger, appraisal rights were still unavailable because Dr Pepper's stockholders did not relinquish their shares in the transaction.

Transactional planners often resort to creative structures driven by tax, finance, and other reasons. The court's opinion, therefore, provides increased certainty to deal parties in how Delaware courts will examine transactions under the relevant merger and appraisal statutes.

It bears noting, however, that the court distinguished the 2007 decision in *Louisiana Municipal Police Employees' Retirement System v. Crawford*. There, a target company's stockholders received merger consideration consisting of shares of the publicly traded acquiror. Normally, that would not trigger appraisal rights in Delaware. The court focused, however, on the fact that the target stockholders would also receive a cash dividend payable in connection with the merger closing. Under the Delaware General Corporation Law, appraisal rights are available if stockholders are required to accept cash in a merger (other than in lieu of fractional shares). The *Crawford* court thus treated the dividend as part of the merger consideration and indicated that appraisal rights were available.

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