

# Delaware Amendments Would Apply 'Market Out' Exception to Section 251(h) Back-End Mergers, Clarify Ratification Procedures

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04 / 26 / 18

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On April 19, 2018, the Executive Committee of the Delaware State Bar Association approved proposed amendments to the Delaware General Corporation Law (DGCL). This year's amendments would provide for the application of the "market out" exception to appraisal rights for Section 251(h) short-form mergers and certain changes to the procedures for ratification of defective corporate acts, among other changes.

## Application of 'Market Out' Exception to Appraisal Rights for Section 251(h) Mergers

The proposed amendments to DGCL Section 262(b) would apply the "market out" exception to the availability of statutory appraisal rights for back-end mergers consummated pursuant to Section 251(h) following an exchange offer without a vote of stockholders. Presently, Section 262(b)(3) provides that appraisal rights are available for mergers effected pursuant to Section 251(h) so long as any shares are held by persons other than the parent. This differs from mergers generally, in which appraisal rights are not available for shares of any class or series of stock of a target corporation that are listed on a national securities exchange or held of record by more than 2,000 holders if the merger consideration for such shares consists solely of (i) stock of the surviving corporation or any other corporation (or depository receipts in respect thereof) that is listed on a national securities exchange or held of record by more than 2,000 holders, (ii) cash in lieu of fractional shares or depository receipts, or (iii) any combination of the foregoing. Presently, this "market out" exception does not apply to mergers effected pursuant to Section 251(h). As a result, Section 251(h) rarely has been utilized in acquisitions where the merger consideration paid to target stockholders is shares of stock.

If the amendments are adopted by the legislature, mergers effected under Section 251(h) following a stock-for-stock exchange offer of publicly traded shares will receive treatment for appraisal rights equal to that afforded to holders in one-step acquisitions where a vote of target stockholders is required to approve the merger.

## Information Required by Appraisal Statement

The amendments to Section 262(e) would modify the information to be included in the statement that must be furnished to dissenting stockholders upon their request in connection with Section 251(h) mergers. In recognition of the fact that no shares are "voted" for the adoption of the merger agreement in a Section 251(h) transaction, the amendments would clarify that the surviving corporation must provide stockholders, upon their request, with the number of shares not purchased in the tender or exchange offer, rather than the number of shares not voted for the merger.

## Ratification of Defective Corporate Acts

Several amendments have been proposed to Section 204, which allows for the ratification of defective corporate acts. First, the amendments would confirm that Section 204 remains available for ratifying defective corporate acts in circumstances where no shares of valid stock are outstanding. This would eliminate the need for any stockholder vote on the ratification of a defective corporate act in such circumstances, even if a vote of stockholders would otherwise be required under Section 204.

Second, the amendments would clarify that, in cases where a vote of stockholders is required for the ratification of a defective corporate act, the notice of the stockholder meeting required to be given to holders of valid or putative stock may be given to such

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holders as of the record date for the defective corporate act if it involved the establishment of a record date. The amendments also would allow public companies to give such notice to such stockholders through disclosure in a proxy statement or other document publicly filed with the Securities and Exchange Commission pursuant to Section 13, 14 or 15(d) of the Securities Exchange Act.

Next, the amendments would clarify and confirm that any act or transaction that a corporation takes that is within its power under the DGCL may be ratified under Section 204 if such act or transaction was void or voidable due to a “failure of authorization.” Such amendment is intended to eliminate any implication arising from *Nguyen v. View, Inc.*, C.A. No. 11138-VCS (Del. Ch. June 6, 2017) that an act or transaction may not be within the power of a corporation — and therefore may not constitute a “defective corporate act” susceptible to cure by ratification — solely on the basis that it was not approved in accordance with the provisions of the DGCL or the corporation’s certificate of incorporation or bylaws. The proposed amendments, however, would not alter the power of the Court of Chancery to decline to validate a defective corporate act that has been ratified under Section 204 on the basis that the failure of authorization that rendered such act void or voidable involved a deliberate withholding of any consent or approval required under the DGCL, the certificate of incorporation or bylaws.

Finally, the amendments would clarify that the failure of an act or transaction to be approved in compliance with disclosures in any proxy statement or consent solicitation statement may constitute a failure of authorization. Thus, an act or transaction alleged to be defective due to deficiencies in the disclosure documents whereby the vote or consent of stockholders to such act or transaction was sought may be cured through ratification pursuant to Section 204.

## Forfeiture of Charter

The amendments also would modify Section 284 to make clear that the Delaware attorney general has the exclusive authority to move for the revocation or forfeiture of a corporation’s charter for abuse, misuse or nonuse of its corporate powers, privileges or franchises by filing a complaint in the Court of Chancery. Furthermore, as amended, Section 284 would provide that the Court of Chancery has the power to appoint a trustee to administer and wind up the affairs of a corporation whose charter has been revoked or forfeited pursuant to Section 284.

A copy of the proposed legislation is [available here](#). The proposed amendments will be introduced in the General Assembly for consideration and, if adopted, would become effective August 1, 2018.