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2018]

GET BACK: THE DELAWARE SUPREME COURT DISCOURAGES
APPRAISAL ARBITRAGE IN *DFC GLOBAL CORPORATION V.*
MUIRFIELD VALUE PARTNERS, L.P.

ABRAHAM SCHNEIDER*

“In economics, the value of something is what it will fetch in the market. That is true of corporations, just as it is true of gold.”¹

I. I ME MINE: AN INTRODUCTION TO THE “PROBLEM” OF
APPRAISAL ARBITRAGE

For ten years, investors have been eating a free lunch in the Delaware courts through the practice of “appraisal arbitration.”² Delaware originally established protection for a corporation’s minority shareholders 118 years ago by granting them appraisal rights: if a company undergoes a merger or a consolidation, and shareholders dissent, they can take their shares to the court and have the court decide on a fair value.³ It was not until 2007, however, that savvy investors realized the opportunity appraisal provided and began the practice of appraisal arbitration.⁴ In a single decade, arbi-

* J.D. Candidate, 2019, Villanova University Charles Widger School of Law. All titles and headings in this Casebrief are inspired by Beatles song titles. This Casebrief is dedicated to my generous and loving wife, Katie (and her whole generous and loving family); to my law school Virgil, Doug Baker, who has found me wandering in too many dark woods to count; to the Honorable Mark A. Kearney, who pointed my Roman nose south toward the First State; and, finally, to my dear father, Dave Schneider, who threatened to have me shot when he heard I was going to law school, but who was probably kidding.

1. See *DFC Glob. Corp. v. Muirfield Value Partners, L.P.*, 172 A.3d 346, 368–69 (Del. 2017) (emphasizing fairness of market price).

2. See W. Schachermayer, *The Notion of Arbitrage and Free Lunch in Mathematical Finance*, in *ASPECTS OF MATHEMATICAL FINANCE* 15 (Marc Yor, ed. 2008) (describing financial arbitrage as equivalent to “picking up money that is lying around”).

3. See DEL. CODE ANN. tit. 8, § 262 (West 2017) (granting appraisal rights to dissenting shareholders); see also Charlotte K. Newell, *The Legislative Origins of Today’s Appraisal Debate: A Look Back at the Evolution of the DGCL and the Origins of the Explosive Rise in “Appraisal Arbitration” Filings*, 35 DEL. LAW. 12, 13 (Summer 2017) (explaining history of appraisal rights); Jay W. Eisenhofer & John L. Reed, *Valuation Litigation*, 22 DEL. J. CORP. L. 37, 41 n.9 (1997) (noting that Delaware granted appraisal rights when it enacted its law of corporations in 1899).

4. See generally Stanley Onyeador, *The Chancery Bank of Delaware: Appraisal Arbitrageurs Expose Need to Further Reform Defective Appraisal Statute*, 70 VAND. L. REV. 339, 348–49 (2017) (noting surge in both number of appraisal litigation cases brought and in value of appraisals between 2004–2014). For a discussion of arbitrage’s incipient 2007 case, *In re Appraisal of Transkaryotic Therapies, Inc.*, No. CIV.A. 1554-CC, 2007 WL 1378345 (Del. Ch. May 2, 2007), see *infra* note 48 and accompanying text.

trage turned appraisal rights into the hottest issue in Delaware corporate law.⁵

Arbitrage means profiting by purchasing assets in one market and immediately selling them for a higher price in a different market.⁶ In appraisal arbitrage, an investor purchases shares in a company just before a merger, then, immediately after the merger finalizes, the investor sues for appraisal, hoping the courts will value the shares at a price higher than the deal.⁷ If the court finds the shares are worth more than the deal price, the surviving corporation in the merger must pay the dissenting shareholders the court's appraisal price.⁸ Though not entirely risk free, appraisal arbitrage has become a popular, profitable, and safe investment strategy.⁹

The "problem" with appraisal arbitrage is that Delaware's appraisal statute was intended to vindicate the rights of oppressed minority shareholders, not to provide an investment vehicle for hedge funds.¹⁰ Some see "arbitrageurs" as filing strike suits that can add a price tag of hundreds of millions of dollars onto a merger.¹¹ Others see the practice as positive: some studies suggest that appraisal arbitrage is more likely to target mergers that are vulnerable to minority shareholder exploitation.¹² While the

5. See Newell, *supra* note 3, at 12 ("Appraisal is now a hot topic at corporate law conferences and the subject of more than half the M&A cases Law360 has identified as the 'most important to watch' in 2017."); see also Charles R. Korsmo & Minor Myers, *Appraisal Arbitrage and the Future of Public Company M&A*, 92 WASH. U.L. REV. 1551, 1612 (2015) ("Until now, the academic consensus has been that appraisal litigation is a peripheral sideshow. This view, which may have been accurate as recently as 2009, must now be radically revised.").

6. See *Arbitrage*, DICTIONARY.COM, www.dictionary.com/browse/arbitrage [<https://perma.cc/FU2S-EYEF>] (last visited Sep. 27, 2018) (defining arbitrage).

7. See Jay B. Kesten, *The Uncertain Case for Appraisal Arbitrage*, 52 WAKE FOREST L. REV. 89, 102 (2017) (describing strategy behind appraisal arbitrage). Kesten points out that in traditional merger arbitrage, an arbitrageur buys a large number of shares at a slight discount due to the uncertainty of the merger finalizing, then votes in favor of the merger and profits from the increased price of the consummated merger. See *id.* (explaining traditional arbitrage). Appraisal arbitrage does the opposite, buying shares and voting against the merger despite profiting from its consummation. See *id.* at 89–90 (comparing traditional and appraisal arbitrage approaches).

8. See DEL. CODE ANN. tit. 8, § 262(i) (requiring payment of court's appraisal price).

9. See Kesten, *supra* note 7, at 89–90 (describing popularity and profitability of arbitrage). Kesten states that "[h]edge funds specializing in appraisal arbitrage have raised billions of dollars in recent years." *Id.* at 89 (evaluating increasing activity in appraisal arbitrage). Because of the profitability, "appraisal claims have surged in both number and economic significance." *Id.* at 90 (noting increase in appraisal arbitrage).

10. For an in-depth discussion of appraisal arbitrage's contravention of the intent of § 262, see *infra* note 48 and accompanying text.

11. See Korsmo, *supra* note 5, at 1571 (describing value of arbitrage claims). For a discussion of appraisal arbitrage as strike suits, see *infra* note 49 and accompanying text.

12. See Wei Jiang, Tao Li, Danqing Mei & Randall Thomas, *Appraisal: Shareholder Remedy or Litigation Arbitrage?*, 59 J.L. & ECON. 697, 699–700 (2016) (explain-

possibility of arbitrage may keep companies honest when the merger price is low or the deal is suspicious, the practice itself can seem dubious when the merger is entirely fair—a so-called “clean” merger.¹³ In a clean merger, where the company is put up for auction and there is no conflict of interest in the sale, the market has already decided on a fair price for the company.¹⁴ Should it be acceptable for arbitrageurs to get more than other shareholders because a judge disagrees with the market’s price?¹⁵

Although appraisal arbitrage is legal, the Delaware courts and legislature have recently executed a pincer movement to discourage arbitrage in clean mergers.¹⁶ The profit in arbitrage comes from two sources, roughly in equal proportions: half comes from the award of a higher share price by the Court of Chancery, and half comes from pre-judgment interest accrued during litigation.¹⁷ On one side of the pincer, the Delaware legislature has allowed companies to avoid interest payments through statutory amendment, and on the other side, the Delaware Supreme Court, in *DFC*

ing data showing appraisal litigation, including arbitrage, is most likely where there are conflicts of interest or low takeover premium, as well as in going-private deals, minority squeeze outs, and short-form mergers after tender offers); Korsmo, *supra* note 5, at 1595 (concluding that arbitrageurs “appear to target transactions with, all else equal, lower merger premia.”). *But see* Kesten, *supra* note 7, at 92 (contending that empirical studies “cast doubt on whether appraisal arbitrageurs systematically target underpriced deals”).

13. *See* Onyeador, *supra* note 4, at 352 (“[B]y challenging many mergers that do not have characteristics of unfair merger pricing, arbitrageurs do not use the appraisal remedy to ensure fairness to minority shareholders as the remedy intends.”). *See generally* Hon. Sam Glasscock III, *Ruminations on Appraisal: What Are the Policy Implications of A Dissenter’s Right to Appraisal in A “Clean” Transaction?*, 35 DEL. LAW. 8, 8 (Summer 2017) (dubbing mergers “clean” when “the stock is readily transferable, approved by a disinterested board independent of any controller or other conflict, and where the sale is consummated after an exposure to the market”). To avoid repeating the conditions of a fair market transaction, this Casebrief will also utilize the term “clean” to describe unconflicted and market-tested transactions.

14. *See* *DFC Global Corp. v. Muirfield Value Partners, L.P.*, 172 A.3d 346, 369–70 (Del. 2017) (emphasizing fairness of market price in clean mergers).

15. *See id.* at 367 (warning that judges “should have little confidence [they] can be the special one[s] able to outwit the larger universe of equally avid capitalists”); *see also* Jiang, *supra* note 12, at 700 (explaining that arbitrageurs receive premiums because acquiring companies “are always better off paying the appraisal award to the dissenters rather than trying to preempt the petitions by offering a more generous premium in the transaction to all shareholders”); Kesten, *supra* note 7, at 127–28 (arguing that appraisal arbitrage does more than realize premium; it “perniciously redistributes value from acquirers and ordinary shareholders to the arbitrageurs”).

16. *Cf.* Kesten, *supra* note 7, at 91–92 (describing string of Court of Chancery cases finding deal price was fair value and describing amendments to § 262).

17. *See* Jiang, *supra* note 12, at 700 (“Among the cases that go to trial, judicially ordered valuation improvements and prejudgment interest accruals constitute roughly equal proportions of the total gain.”). Data shows interest accrual accounts for slightly more than half, or 53.4% of the awards in appraisal cases. *See id.* at 726–27 (examining appraisal case outcomes).

Global Corporation v. Muirfield Value Partners, L.P.,¹⁸ has ruled that in a clean merger, the deal price is the best indicator of fair value, except in extreme circumstances.¹⁹ Taken together, the statutory amendments and *DFC Global* are likely to starve arbitrageurs by making the practice unprofitable in clean mergers.²⁰

This Casebrief asserts that the Supreme Court of Delaware navigated this controversial topic by following the legislature's lead in starving arbitrage in clean mergers while preserving judicial discretion to allow appraisal when there is a danger of minority shareholder exploitation.²¹ Part II provides background information regarding appraisal rights, appraisal arbitrage, and Delaware's legislative and judicial reactions to the practice.²² Part III discusses the facts of *DFC Global*, including the merger, the appraisal, and the appeal, and provides an analysis of the court's reasoning.²³ Part IV analyzes the court's decision and comments on the future of appraisal arbitrage for practicing attorneys.²⁴ Finally, Part V assesses the potential impact of *DFC Global* for arbitrageurs, companies, and shareholders.²⁵

II. MAXWELL'S SILVER HAMMER: THE ORIGINS AND EVOLUTION OF APPRAISAL ARBITRAGE

Appraisal rights emerged a century and a half ago to protect dissenting shareholders while allowing corporations to make decisions without unanimous consent.²⁶ More recently, investors introduced appraisal arbitrage by purchasing shares in a corporation prior to a merger solely to profit from the appraisal rights that came with the shares.²⁷ Arbitrage

18. 172 A.3d 346 (Del. 2017).

19. For an in-depth discussion of Delaware's legislative amendments, see *infra* notes 59–62 and accompanying text. For an in-depth discussion of the holding in *DFC Global*, see *infra* notes 99–142 and accompanying text.

20. For an in-depth discussion of the potential effects of *DFC Global*, see *infra* notes 143–80 and accompanying text.

21. For an in-depth analysis of the Delaware Supreme Court's opinion, see *infra* notes 143–56 and accompanying text.

22. For a further discussion of the origin and development of appraisal rights, arbitrage, and the response to arbitrage, see *infra* notes 26–66 and accompanying text.

23. For a further discussion of the facts of *DFC Global*, see *infra* notes 67–98 and accompanying text. For a narrative analysis of the *DFC Global* decision, see *infra* notes 99–142 and accompanying text.

24. For a critical analysis of the *DFC Global* decision and its potential effect on practicing attorneys, see *infra* notes 144–74 and accompanying text.

25. For a discussion of the impact of the *DFC Global* decision, see *infra* notes 175–84 and accompanying text.

26. See Korsmo, *supra* note 5, at 1558 (explaining origins of appraisal rights' role in transition from unanimity to majority voting requirements in corporate law).

27. See Tom Hals, *Court Reverses Dell Buyout Ruling that Alarmed Dealmakers*, REUTERS TECH. NEWS (Dec. 14, 2017, 12:10 PM), <https://www.metro.us/news/reuters/court-reverses-dell-buyout-ruling-alarmed-dealmakers> [https://perma.cc/

works because the courts often value shares higher than the deal price, and the corporation pays interest to the dissenting shareholders until the appraisal is complete.²⁸ Delaware courts have showed increasing skepticism of the practice, and both the courts and the legislature have taken steps to discourage appraisal arbitrage in clean mergers.²⁹

A. *Everybody's Got Something to Hide Except Me and My Monkey: A Brief History of Appraisal Rights*

The Delaware appraisal remedy was born out of corporate necessity.³⁰ Until the late 1800s, a unanimous quorum of the corporation's shareholders had to approve every corporate decision.³¹ Appraisal rights emerged when corporations realized not every decision could be unanimous if the corporations were to continue to expand.³² Appraisal rights resolved this problem by allowing corporations to take action despite some shareholder dissent by providing the dissenters a mechanism to petition the courts for redress.³³

V35N-AHJ9] (“[A]ppraisal has become an investment strategy for sophisticated hedge funds, which buy shares just before a deal closes then seek to profit in court.”).

28. For an in-depth discussion of the profitability of arbitrage through appraisal award and interest, see *infra* notes 41–45 and accompanying text.

29. See, e.g., Victor Lewkow, Meredith E. Kotler & Mark E. McDonald, *Delaware Supreme Court's Dell Decision Further Reduces Appraisal Risks for Buyers*, CLEARY M&A & CORP. GOVERNANCE WATCH (Dec. 18, 2017), <https://www.clearymawatch.com/2017/12/delaware-supreme-courts-dell-decision-reduces-appraisal-risks-buyers/> [<https://perma.cc/5GQN-93YD>] (suggesting Delaware Supreme Court is increasingly limiting arbitrage practice); Anne Tucker, *Tides May Be Slowly Turning in Delaware Appraisal Arbitrage*, LAW PROFESSOR BLOGS NETWORK (Aug. 17, 2016), http://lawprofessors.typepad.com/business_law/2016/08/guest-post-tides-may-be-slowly-turning-in-delaware-appraisal-arbitrage.html [<https://perma.cc/CVN3-AF6R>] (suggesting Delaware intends to shut down arbitrage practice). For an in-depth discussion of the legislative and judicial reactions to the practice of appraisal arbitrage, see *infra* notes 54–62 and accompanying text.

30. See 4 JAMES D. COX & THOMAS LEE HAZEN, *TREATISE ON THE LAW OF CORPORATIONS* § 22:24 (3d ed. 2017) (explaining that appraisal remedies arose because of “expansion of commerce in the nineteenth century,” which “created a need for bigger and more complex corporations” that could make decisions without unanimous approval).

31. See Newell, *supra* note 3, at 13 (describing early corporation law).

32. See COX & HAZEN, *supra* note 30 (“The rule of unanimity impeded corporate growth because any shareholder could prevent a corporate combination if he did not agree.”). The first state to introduce appraisal rights was Pennsylvania in 1858, when shareholders dissented from a railroad merger. See *Lauman v. Lebanon Valley R.R.*, 30 Pa. 42, 45–48 (1858) (introducing appraisal rights).

33. See COX & HAZEN, *supra* note 30 (explaining how appraisal rights solved the lack of contract and property rights that occurred when corporations overrode dissenting shareholders). But see Korsmo, *supra* note 5, at 1560 (noting “[a]ppraisal has long been regarded in the corporate law literature as an almost useless remedy” because individual shareholders have little motivation to bring suits, and corporations can easily circumvent appraisal rights).

Section 262 of the Delaware General Corporation Law codifies appraisal rights and requires the Court of Chancery to determine a “fair value” for the shares.³⁴ The statute also sets out several requirements shareholders must meet before they may invoke appraisal rights, including owning the shares at the date of the merger and “perfecting” their appraisal rights by dissenting from the merger.³⁵ Originally instituted in the late 1800s, Delaware’s appraisal statute “enjoyed a relatively sleepy history.”³⁶ Ten years ago, this “sleepy” statute suddenly became the hottest topic in Delaware corporate law because of the practice known as appraisal arbitrage.³⁷

B. *Taxman: What Appraisal Arbitrage is and How It Developed*

Appraisal arbitrage is an investment model centered around appraisal litigation.³⁸ It occurs when an investor, usually a hedge fund or capital equity firm, purchases shares in a company after it has announced a

34. See DEL. CODE ANN. tit. 8, § 262 (West 2017) (granting appraisal rights). Today, “fair value” generally requires “proof of value by any techniques or methods which are generally considered acceptable in the financial community.” See *Laidler v. Hesco Bastion Envtl., Inc.*, Civil Action No. 7561-VCG, 2014 WL 1877536, at *6 (Del. Ch. May 12, 2014) (explaining requirements for and meaning of fair value) (quoting *Doft & Co. v. Travelocity.com, Inc.*, No. Civ. A. 19734, 2004 WL 1152338, at *5 (Del. Ch. May 21, 2004)). For an in-depth discussion of the history of “fair value,” see *infra* note 57 and accompanying text.

35. See DEL. CODE ANN. tit. 8, § 262 (providing requirements to invoke appraisal rights). Section 262(a) describes the basic requirements:

(a) Any stockholder of a corporation of this State who holds shares of stock on the date of the making of a demand pursuant to subsection (d) of this section [subsection (d) requires a shareholder to perfect appraisal rights by dissenting from the merger] with respect to such shares, who continuously holds such shares through the effective date of the merger or consolidation, who has otherwise complied with subsection (d) of this section and who has neither voted in favor of the merger or consolidation nor consented thereto in writing pursuant to § 228 of this title shall be entitled to an appraisal by the Court of Chancery of the fair value of the stockholder’s shares of stock. . . .

Id. Section 262(d) requires the shareholder to perfect appraisal rights by dissenting from the merger and suing for appraisal within a restricted time frame. See § 262(d) (requiring perfection of appraisal rights).

36. See Jiang, *supra* note 12, at 701 (“[F]rom 1977 to 1997 only an average of 14 appraisal petitions were filed annually in Delaware, many by individual shareholders acting without legal counsel, which were quickly dismissed” (citing Randall S. Thomas, *Revising the Delaware Appraisal Statute*, DEL. L. REV. 3:1-35 (2000))); Newell, *supra* note 3, at 15 (noting appraisal remedy is seldom utilized).

37. See Newell, *supra* note 3, at 12 (“Appraisal is now a hot topic at corporate law conferences and the subject of more than half the M&A cases Law360 has identified as the ‘most important to watch’ in 2017.”); see also Korsmo, *supra* note 5, at 1612 (“Until now, the academic consensus has been that appraisal litigation is a peripheral sideshow. This view, which may have been accurate as recently as 2009, must now be radically revised.”).

38. See Craig Boyd, Comment, *Appraisal Arbitrage: Closing the Floodgates on Hedge Funds and Activist Shareholders*, 65 U. KAN. L. REV. 497, 497–98 (2016) (describing appraisal arbitrage).

merger but before the merger occurs.³⁹ The investor purchases the shares for the sole purpose of dissenting from the merger and taking the shares to court to have them appraised.⁴⁰

Appraisal arbitrage works as an investing technique for two reasons.⁴¹ First, the surviving company in the merger must pay the dissenting shareholders the court's appraisal price.⁴² The Court of Chancery often finds the company undervalued—meaning the dissenting shareholders make the difference as profit.⁴³ Second, Section 262 requires the surviving corporation to pay dissenting shareholders the federal interest rate, plus five percent, on the price of their dissenting shares while the appraisal action is underway.⁴⁴ Because appraisal actions often take up to three years to complete, arbitrageurs earn a healthy and predictable rate of return on the shares and realize a profit even if the court ultimately finds the deal price was fair.⁴⁵ Appraisal arbitrage has become a powerful force, “utterly

39. See Glasscock, *supra* note 13, at 11 (describing appraisal arbitrage as “a phenomenon facilitated by our appraisal statute, as written: the statute permits stockholders who have purchased stock after announcement of the merger to perfect the right to an appraisal”); Jiang, *supra* note 12, at 701 (explaining that hedge funds are “the main driving force” behind appraisal arbitrage); Korsmo, *supra* note 5, at 1573 (“[S]pecialized appraisal petitioners . . . typically . . . invest in the target company after the announcement of the transaction they challenge.”); *id.* at 1572–73 (discussing trend of appraisal litigation increasingly brought by “specialized and sophisticated” investment firms that specialize in appraisal arbitrage).

40. See Korsmo, *supra* note 5, at 1573 (“The decision to invest . . . is based on a calculation that the amount they will be able to recover in an appraisal proceeding in Delaware . . . will exceed the merger price by enough to offer an attractive return.”).

41. See Gardner Davis & Victoria Matese, *Delaware High Court Says a Fair Deal Price Should Get the Most Weight in Appraisal Valuation*, 33 WESTLAW J. CORP. OFFICERS & DIRECTOR LIABILITY, Sep. 5, 2017, at 1 (describing reliability of profit in appraisal arbitrage actions prior to *DFC Global*); Jiang, *supra* note 12, at 699 (describing high average rate of return on appraisal actions when viewed as investment).

42. See DEL. CODE ANN. tit. 8, § 262(i) (West 2017) (requiring payment of court's evaluation of fair value).

43. See Claudia H. Allen, Holly J. Gregory, Gregory V. Varallo & Susan M. Hannigan, *Proceedings of the 2016 Delaware Business Law Forum: A Review and Debate of the Public Policy Implications of Delaware Law*, 72 BUS. L. 755, 760 (2017) (“[A]ppraisal arbitrageurs may be motivated by decisions from the Court of Chancery awarding fair values in excess of transactions prices” (citing Gaurav Jetley & Xinyu Ji, *Appraisal Arbitrage—Is There a Delaware Advantage?*, 71 BUS. L. 427, 429 (2016))).

44. See DEL. CODE ANN. tit. 8, § 262(h) (outlining requirements for interest payments). See generally Jiang, *supra* note 12, at 701 (explaining award of statutory interest of federal rate plus five percent). As Jiang points out, appraisal arbitrage works as an investment strategy because “[t]his interest rate is significantly higher than that available on many fixed-income investments.” *Id.* (explaining profitability of appraisal arbitrage). Additionally, Kesten writes that “a favorable interest rate is at least one important determinant of appraisal claims.” See Kesten, *supra* note 7, at 116 (explaining role of interest rate in viability of appraisal arbitrage).

45. See Jiang, *supra* note 12, at 725 (“[T]he interest accrual essentially ensures that the appraisal arbitrageurs never receive negative raw returnsFalse”). But see Korsmo, *supra* note 5, at 1554 (suggesting “the idea that interest rates are driving sophisticated parties to target appraisal is implausible” because of risks of using

transform[ing] what may once have been accurately characterized as a sleepy corporate law backwater.”⁴⁶

It is not difficult to see why appraisal arbitration is a controversial topic: the legislature instituted Section 262 to vindicate the rights of oppressed minority shareholders who could not make their voices heard in corporate decisions.⁴⁷ Arbitrators are hardly oppressed shareholders; they are savvy investors, and some see them as parasites on mergers and acquisitions for which they otherwise have no concern.⁴⁸ Arbitration is a business tactic based on a statute that was not enacted to defend the rights of arbitrators.⁴⁹ Further, arbitration is sometimes seen as adding a tax that com-

illiquid and unsecured legal claim as investment tool). Korsmo argues the rise in appraisal litigation is a phenomenon attached to the general rise in fiduciary litigation related to mergers. *See id.* (offering alternate explanation for rise in appraisal arbitration). Regarding length of appraisal arbitration claim and prejudgment interest, see Jiang, *supra* note 12, at 697 (explaining that appraisal litigation ordinarily reaches judgment “1-3 years after completion of the merger,” and that dissenting shareholders receive “appraised value with accrued prejudgment interest”).

46. *See* Korsmo, *supra* note 12, at 1553 (describing transformative effect of arbitration on appraisal law).

47. For a discussion on the origins of Section 262, see *supra* note 30, and accompanying text.

48. *See, e.g.*, Boyd, *supra* note 38, at 497 (“[C]laims are not being brought by the dissenting minority shareholders that Section 262 was designed to protect. The surge of new plaintiffs has primarily been hedge funds and activist shareholders attempting to take advantage of an unjust investment strategy”); *see also In re Appraisal of Transkaryotic Therapies, Inc.*, No. Civ. A. 1554-CC, 2007 WL 1378345, at *5 (Del. Ch. May 2, 2007) (voicing concern that appraisal arbitration would “pervert the goals of the appraisal statute by allowing it to be used as an investment tool”). *But see* Jiang, *supra* note 12, at 697 (“Appraisal petitions are more likely to be filed against mergers with perceived conflicts of interest, including going-private deals, minority squeeze outs, and acquisitions with low premiums, which makes them a potentially important governance mechanism.”); Korsmo, *supra* note 5, at 1555 (arguing “that the rise of appraisal arbitration is, on balance, a beneficial development” because arbitrators “target transactions with lower deal premia and also going-private transactions, where minority shareholders are most likely to face expropriation.”). Korsmo argues that the motivation of appraisal arbitrators and exploited minority shareholders are aligned, because transactions vulnerable to exploitation tend to prove the most beneficial to arbitrators, and therefore appraisal arbitration generally produces meritorious, rather than nuisance claims. *See id.* at 1596–97 (arguing that appraisal arbitration generally benefits shareholders). Moreover, there is some evidence that appraisal arbitration has increased deal premiums across the board, benefiting all shareholders, not just dissenting shareholders. *See* Chas Kidwell & Kyle Schrod, *Delaware Limits Appraisal Rights, but at What Cost?*, LEXOLOGY (Oct. 2, 2017) <https://www.lexology.com/library/detail.aspx?g=9d07424b-5770-4b46-a3b8-1236d2c66bd6> [<https://perma.cc/H5S6-R2GR>] (arguing appraisal arbitration is beneficial because it increases deal prices).

49. *See, e.g.*, George S. Geis, *An Appraisal Puzzle*, 105 NW. L. REV. 1635, 1664 (2011) (suggesting appraisal is “a back-end cesspool for strike suits.”); Glasscock, *supra* note 13, at 29 (“The dissenting stockholder in solicitude for whom the statute was ostensibly designed is absent in this scenario.”); Jiang, *supra* note 12, at 698 (“The sharp increase of appraisal arbitration has stoked concerns that a new form of strike suit has been born.”). Taking a milder tone than Geis, Vice Chancellor

panies must now consider when approaching a sale or purchase, and sometimes the tax can be large enough to prevent a deal from happening.⁵⁰ Nevertheless, despite some scholars suggesting the practice may be “antithetical to policy goals of the appraisal remedy,” appraisal arbitrage is legal.⁵¹

Glasscock notes that “arbitrageurs are hardly dissenters.” See Glasscock, *supra* note 13, at 29 (examining motivations of arbitrageurs). In fact, though arbitrageurs dissent from a merger to perfect their appraisal rights, the situation they “most fear” is that the merger will not be approved. See *id.* (explaining arbitrageurs’ interests in mergers). This puts arbitrageurs in an ironic position: to perfect appraisal rights, they must dissent from the merger, but if their voices are heard and the dissent prevails, they stand to lose a great deal of money because the share price will revert to its level from before the merger announcement bolstered its value. See *id.* (explaining contradiction between arbitrageurs’ votes and desired outcome). This situation demonstrates that arbitrageurs are only technically dissenters, not true minority shareholders attempting to prevent a merger and seeking redress when their attempts fail. See *id.* (emphasizing that arbitrageurs do not vindicate rights protected by Delaware’s appraisal statute).

50. See Desiree M. Baca, *Curbing Arbitrage: The Case for Reappraisal of Delaware’s Appraisal Rights*, 13 N.Y.U. J.L. & BUS. 425, 443 (2017) (describing appraisal arbitrage as “value-reducing because it essentially imposes an appraisal tax on transactions.”) (citing Abigail Pickering Bomba, *Shareholder Activism in M&A—Checklists . . . and the Future*, FRIED FRANK M&A BRIEFING (July 7, 2014), www.friedfrank.com/siteFiles/Publications/Final%20-%207-10-2014%20TOC%20Memo%20-%20Shareholder%20Activism%20in%20MA%20Checklists1.pdf [https://perma.cc/9YH4-4U9G]); *id.* at 444 (contending that threat of appraisal arbitrage creates risk of preventing deal); see also Korsmo, *supra* note 5, at 1571–72 (showing that appraisal claims have increased not only in number but in value of each claim); *id.* at 1600 (citing concern that “acquirers will come to view the risk of appraisal as essentially a tax that raises the costs of acquiring a company”); Onyeador, *supra* note 4, at 356 (suggesting that arbitrage creates liquidity and litigation risks in scale large enough to gridlock some mergers). Appraisal arbitrage, because it has not traditionally differentiated between clean and interested or conflicted transactions, may discourage counsel from attempting the extra work necessary to have a clean transaction. See Adam B. Frankel, *Reflections on Appraisal: Litigation As New Technologies Disrupt Traditional Markets, Discounted Cash Flow Valuations May Be Inadequate in Determining Fair Deal Values*, 35 DEL. L. 20, 20 (Summer 2017) (suggesting mergers and acquisitions lawyers lack motivation to pursue clean mergers because of arbitrage). Appraisal arbitrage has been a great enough force to significantly increase deal prices and even gridlock deals. See Steven Epstein, *Delaware Appraisal: Practical Considerations*, BUS. L. TODAY (Oct. 2014), http://www.americanbar.org/publications/blt/2014/10/keeping_current_epstein.html [https://perma.cc/K9D9-3TDV] (describing deals that were drastically altered or gridlocked because of appraisal arbitrage).

51. See Onyeador, *supra* note 4, at 356 (suggesting arbitrage is antithetical to appraisal rights because risk of appraisal causes merger price to decline, “stripping value from long-term target stockholders and placing it in the hands of predatory arbitrageurs”). For a discussion of the legality of appraisal arbitrage, see Newell, *supra* note 3, at 12 (explaining appraisal arbitrage “was first challenged 10 years ago and found to comply with the statute”). The Delaware Court of Chancery originally found the investment strategy complied with Delaware’s appraisal statute in 2007. See *In re Appraisal of Transkaryotic Therapies, Inc.*, No. Civ.A. 1554-CC, 2007 WL 1378345, at *3 (Del. Ch. May 2, 2007) (approving legality of appraisal arbitrage practice).

C. *I Want to Hold Your Hand: The Delaware Courts and Legislature Get Together to Curb Appraisal Arbitrage*

The number of appraisal cases in Delaware has spiked in the past decade.⁵² Part of this influx occurred because the Delaware Court of Chancery consistently appraised the share value higher than the deal price, increasing the profitability of the arbitrage practice.⁵³ Recent years, however, have seen an increasing backlash against appraisal arbitrage.⁵⁴ The Court of Chancery has discouraged it by repeatedly capping the value of the shares at the deal price unless there is reason to question the fairness of the deal.⁵⁵ Recently, the Court of Chancery has even broken the deal

52. See Korsmo, *supra* note 5, at 1553 (“Appraisal activity involving public companies is undergoing explosive growth in Delaware, driven by sophisticated parties who specialize in bringing appraisal claims” and showing tenfold increase in appraisal claim value since 2004); Newell, *supra* note 3, at 12 (describing “exponential rise in appraisal filings in the last decade” attributable to appraisal arbitrage).

53. See Jiang, *supra* note 12, at 699 (demonstrating that appraisal litigation accrues “an average (median) annualized return of 32.9 percent” on investment); see also Boyd, *supra* note 38, at 498 (arguing that *Transkaryotic* encouraged arbitrage by allowing shareholders who purchased after merger announcement to dissent).

54. See Daniel E. Meyer, *Maybe Publius Was Right: Relying on Merger Price to Determine Fair Value in Delaware Appraisal Cases*, 165 U. PA. L. REV. 153, 166-67 (2016) (describing backlash and resistance against practice of appraisal arbitrage); Onyeador, *supra* note 4, at 345-55 (describing backlash by corporate defense and other backlash against arbitrage practice). The backlash has in some cases been extreme: when a hedge fund threatened the Dole Company with arbitrage, Dole in turn threatened to reincorporate in a different state unless the legislature amends the appraisal statute. See Onyeador, *supra* note 4, at 355 (describing corporate reaction to arbitrage).

55. See Huff Fund Inv. P’ship v. CKx, Inc., Civil Action No. 6844-VCG, 2013 WL 5878807, at *11 (Del. Ch. Nov. 1, 2013) (giving weight to deal price because transaction was clean), *aff’d*, 2015 WL 631586 (Del. 2015). The Huff case was the first in the trend giving the greatest weight to the deal price in a clean transaction. See Boyd, *supra* note 38, at 514 (explaining arbitrage case history). For a further discussion of cases in the Chancery Court following this trend of granting deference to merger price in clean transaction, compare *In re PetSmart, Inc.*, C.A. No. 10782-VCS, 2017 WL 2303599, at *2 (Del. Ch. May 26, 2017) (setting fair value at deal price because deal price was “‘forged in the crucible of objective market reality’” and is therefore “the best indicator of the fair value of PetSmart as of the closing of the Merger” (quoting *Van de Walle v. Unimation, Inc.*, Civ. A. No. 7046, 1991 WL 29303, at *17 (Del. Ch. Mar. 7, 1991))), and *Merion Capital L.P. v. Lender Processing Servs., Inc.*, C.A. No. 9320-VCL, 2016 WL 7324170, at *26-33 (Del. Ch. Dec. 16, 2016) (finding deal price reflected fair value exactly), and *Merlin Partners LP v. AutoInfo, Inc.*, C.A. No. 8509-VCN, 2015 WL 2069417, at *12-14 (Del. Ch. Apr. 30, 2015) (adopting deal price because company was “‘shopped quite a bit’” and sale was “at arm’s length, without compulsion, and with adequate information”), and *In re Appraisal of Ancestry.com, Inc.*, Consolidated Civil Action No. 8173-VCG, 2015 WL 399726, at *23-24 (Del. Ch. Jan. 30, 2015) (finding deal price represented fair price), and *Merion Capital L.P.*, 2016 WL 7324170, at *18 (adopting deal price because of bidding process that “created credible competition among heterogeneous bidders during the pre-signing phase”), with *In re Dole Food Co.*, C.A. No. 8703-VCL, 2017 WL 624843, at *5 (Del. Ch. Feb. 15, 2017) (refusing deference to merger price when special committee was misinformed and lacked negotiating power), and *Dunmire v. Farmers & Merchs. Bancorp of W. Pa., Inc.*, C.A. No. 10589-CB, 2016 WL 6651411, at *7-8 (Del. Ch. Nov. 10, 2016) (de-

price floor and appraised the shares at less than the deal price.⁵⁶ Delaware courts have, however, stopped short of creating a “presumption” that the market value is the fair value.⁵⁷ From the beginning of the appraisal arbitration practice, the courts have held that arbitration is authorized by the statute; therefore, it is the legislature, not the courts, who must ultimately resolve the issue.⁵⁸

Appraisal arbitration became such a popular (and controversial) practice that in 2016, the Delaware legislature, in an attempt to reduce arbitration, revised Section 262 in two important ways.⁵⁹ First, it added a

clining deference to merger price when there was controlling shareholder and no auction).

56. See *In re Appraisal of AOL Inc.*, C.A. No. 11204-VCG, 2018 WL 1037450, at *21 (Del. Ch. Feb. 23, 2018) (valuing shares at less than deal price); *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*, C.A. No. 11448-VCL, 2018 WL 922139, at *30 (Del. Ch. Feb. 15, 2018) (valuing shares at trading price prior to merger announcement); *LongPath Capital, LLC v. Ramtron Int’l Corp.*, C.A. No. 8094-VCP, 2015 WL 4540443, at *1 (Del. Ch. June 30, 2015) (reducing merger price by value of synergies related to acquisition, leading to valuation of shares below merger price); see also Alison Frankel, *New Chancery Court Opinion Shows Real Risk for Arbitrators in Appraisal Litigation*, REUTERS (June 1, 2017 4:34 PM), <https://www.reuters.com/article/us-otc-appraisal/new-chancery-court-opinion-shows-real-risk-for-arbitrators-in-appraisal-litigation-idUSKBN18S6F0> [<https://perma.cc/AH9P-SMLW>] (noting Court of Chancery’s valuations at less than deal price).

57. See 1 F. HODGE O’NEILL & ROBERT B. THOMPSON, 1 OPPRESSION OF MIN. SHAREHOLDERS AND LLC MEMBERS § 5:45 (“While recognizing the price in an arm’s-length negotiated merger is a strong indication of fair value, the Delaware Supreme Court has said that such a price is not the overriding consideration under its appraisal statute and does not need to be considered if unsupported by evidence that it represents an accurate going concern value.” (citing *M.P.M. Enter. v. Gilbert*, 731 A.2d 790, 796–97 (Del. 1999))); see also *Chicago Corp. v. Munds*, 172 A.452, 454 (Del. Ch. 1934) (describing Delaware’s rejection of New Jersey’s “full market value” standard in favor of “value” standard, which rejects market’s control of appraisal value); Newell, *supra* note 3, at 13–14 (describing recommendations to Delaware General Assembly’s revision committees in support of abandoning appraisal for fair market value and General Assembly’s rejection of those recommendations). The Delaware legislature has made one important concession to the market: in 1967, it added § 262(k), the “market out” provision that denied appraisal when shareholders of public companies boasting at least 2,000 shareholders were given stock-for-stock compensation. See *id.* (describing “market out” provision).

58. See generally *In re Appraisal of Transkaryotic Therapies, Inc.*, No. Civ.A. 1554-CC, 2007 WL 1378345, at *5 (Del. Ch. May 2, 2007) (“To the extent that this concern [over appraisal arbitration] has validity, relief more properly lies with the Legislature. . . . The Legislature, not this Court, possesses the power to modify § 262 to avoid the evil [of appraisal arbitration], if it is an evil. . . .”). *Transkaryotic* shows that the tension between legislative and judicial resolution of the issue has existed since appraisal arbitration first became a practice. See *id.* (advocating for judicial resolution).

59. See Jiang, *supra* note 12, at 699 (explaining dual revisions to § 262 appraisal statute). Jiang’s empirical study suggests the Delaware legislative amendments have been successful not only in reducing arbitration in general but in targeting and eliminating strike suits. See *id.* at 700 (“[T]he Delaware statutory reforms will significantly reduce the number of small appraisal cases filed, which are the cases most likely to constitute strike suits. . . .”). Meanwhile, the amend-

minimum share ownership requirement before the owner could seek appraisal.⁶⁰ Second, it allowed the surviving corporation to prepay the dissenting shareholders the deal price and thus avoid the bulk of interest payments that make arbitrage a predictably profitable endeavor.⁶¹ Together, these revisions “starve” the practice by (1) ensuring that investors own a sufficiently large block of shares to make the litigation worthwhile, and (2) discouraging investors from suing for appraisal when a company can “prepay” for the dissenting shares and thus avoid interest charges.⁶²

Given the legislature’s discouragement of the practice and the trend in the Court of Chancery to limit appraisal at the deal price, the Delaware Supreme Court was primed to weigh in on the issue.⁶³ It did so in *DFC*

ment has preserved arbitrage in the settings where it can do the most good. *See id.* (“However, these statutory changes should not affect the agency-cost-reduction effects of appraisal: these cases target transactions with higher indicia of managerial conflicts of interest and result in some large verdicts in favor of plaintiffs in big cases.”). Given these effects, Jiang concludes that “the revised Delaware appraisal statute should have a positive role as a shareholder remedy.” *Id.* (evaluating Delaware statutory revisions). *But see* Onyeador, *supra* note 4, at 357 (suggesting the amendments are “insufficient” and may inadvertently make appraisal remedy available only to hedge funds and other major investors).

60. *See* Jiang, *supra* note 12, at 699 (describing “de minimis exception”). As Jiang describes the legislative amendment, “the law now requires petitioners to collectively hold a minimum stake of \$1 million in, or 1 percent of, the outstanding stock of the company for which the petitioner is seeking appraisal. . . .” *Id.* (same). Some believe the de minimis requirement “may impair the appraisal rights of those stockholders who do qualify” because only shareholders with a substantial stake, such as hedge funds and activist investors, will meet the requirement. *See* Allen, *supra* note 43, at 762 (speculating on effect of statutory revisions). The de minimis requirement may also be advantageous to corporations because the corporation can “settle with a subset of stockholders until the threshold is no longer met, causing dismissal of the remaining dissenter’s appraisal petitions.” *Id.* (describing possible negative effects of legislative amendment).

61. *See* Jiang, *supra* note 12, at 699 (describing interest prepayment revision). Jiang outlines the interest provision amendment: “companies [may] reduce the amount of statutory prejudgment interest they pay on awards in an appraisal proceeding by tendering some or all of the merger consideration to the appraisal plaintiff early in the litigation. . . .” *Id.* (same); *see also* Onyeador, *supra* note 4, at 358 (noting that “lucrative 12%” average interest rate “incentiviz[es] arbitrageurs to continue targeting fair transactions despite low probabilities of getting a higher judicially awarded premium”).

62. *See* Jiang, *supra* note 12, at 700 (evaluating effects of legislative amendments to appraisal statute). Jiang’s study suggests the legislative amendment to § 262(h) will be an effective curb on appraisal arbitrage. *See id.* (finding “the amendment is likely to significantly reduce the motive for seeking appraisal,” and finding that “Delaware’s reforms [are] a way of discouraging strike suits and interest-rate-driven appraisal cases”). *But see* Onyeador, *supra* note 4, at 358 (arguing that interest prepayment “may perversely encourage arbitrage activity” because it funds arbitrageur’s appraisal proceeding, allowing arbitrageur to bring appraisal suit without attendant liquidity and funding hardships).

63. *See generally* Steve Hecht, *Delaware Supreme Court Decides DFC Global Appeal*, LOWENSTEIN SANDLER APPRAISAL RIGHTS LITIGATION BLOG (Aug. 1, 2017), <https://www.appraisalrightslitigation.com/2017/08/01/delaware-supreme-court-decides-dfc-global-appeal/> [https://perma.cc/S24H-8N8C] (describing *DFC Global* as “highly watched” because of its likely effect upon appraisal arbitrage industry).

Global, answering two salient questions.⁶⁴ First, what will the judiciary's role be in the legislative attempt to curb the practice?⁶⁵ Second, if the court wishes to discourage arbitrage, how can it do so without taking away the dissenting shareholder rights that Section 262 was designed to protect?⁶⁶

III. BABY YOU'RE A RICH MAN: THE COURT OF CHANCERY AWARDS
ARBITRAGEURS A HIGHER PRICE IN *IN RE APPRAISAL OF DFC*
GLOBAL CORPORATION, AND THE DELAWARE
SUPREME COURT REVERSES

In 2014, Lone Star Capital purchased DFC Global for \$9.50 per share, and several dissenting shareholders sued for appraisal.⁶⁷ The Court of Chancery found three factors relevant in determining a fair price for the shares: (1) a discounted cash flow valuation, (2) a comparable companies analysis, and (3) the deal price.⁶⁸ The Court of Chancery weighed these three factors equally and determined a fair appraisal price of \$10.21.⁶⁹ Both parties appealed.⁷⁰ On appeal, the Delaware Supreme Court held that the Court of Chancery did not give sufficient weight to the deal price.⁷¹ It found the Court of Chancery had inflated the future value of DFC Global without support from the record.⁷² It also found that the

The Delaware Supreme Court has already returned to the appraisal arbitrage issue since *DFC Global*, reaffirming the importance of deal price even in management led buyouts in *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd*, 177 A.3d 1, 44 (Del. 2017) (remanding to Court of Chancery to give greater weight to deal price).

64. See Gail Weinstein & Scott Luftglass, *DFC Global: Delaware Supreme Court Strongly Endorses Reliance on Merger Price*, HARV. L. SCH. FORUM ON CORP. GOVERNANCE & FIN. REG. (Aug. 4, 2017), <https://corpgov.law.harvard.edu/2017/08/04/dfc-global-delaware-supreme-court-strongly-endorses-reliance-on-merger-price/> [<https://perma.cc/4F99-BRGR>] (addressing questions answered and left unanswered by *DFC Global* opinion).

65. For a discussion of *DFC Global*'s effect on the court's role in curbing arbitrage, see *infra* notes 143–56 and accompanying text.

66. For a discussion of the Supreme Court's preservation of appraisal, see *infra* notes 143–56 and accompanying text.

67. See *In re Appraisal of DFC Glob. Corp.*, C.A. No. 10107-CB, 2016 WL 3753123, at *1 (Del. Ch. July 8, 2016) (describing purchase of DFC Global Corporation), *rev'd sub nom.* *DFC Glob. Corp. v. Muirfield Value Partners, L.P.*, 172 A.3d 346 (Del. 2017).

68. See *id.* at *5 (describing factors Court of Chancery considers in appraisal evaluation).

69. See *id.* at *23 (concluding \$10.21 constituted fair value of shares).

70. See *DFC Glob. Corp. v. Muirfield Partners, L.P.*, 172 A.3d 346, 348 (Del. 2017) (noting parties' cross-appeals).

71. See *id.* at 366 (concluding Court of Chancery gave insufficient weight to deal price).

72. See *id.* at 375–85 (finding Court of Chancery's conclusions unsupported by record).

Court of Chancery properly used a comparable companies analysis.⁷³ Finally, it found that the Court of Chancery had failed to explain why it weighted each factor in its appraisal equally.⁷⁴ Ultimately, the Delaware Supreme Court reversed and remanded for a new appraisal of the fair value of DFC Global's shares.⁷⁵

A. *Money Can't Buy Me Love: The Sale of a Troubled Payday Lending Company*

DFC Global is a payday lender.⁷⁶ In 2012, DFC Global engaged Houlihan Lokey Capital to search for a potential buyer.⁷⁷ The future of DFC Global was uncertain: increased regulatory restrictions threatened to decrease profits, the company was highly leveraged, and leadership was uncertain.⁷⁸ In 2013, the company began to suffer from increased regulations in the financial industry in the U.K. and Canada, as well as impending regulatory restrictions in the U.S.⁷⁹ Houlihan Lokey Capital searched diligently for a buyer for two years, and though it engaged the interest of multiple companies, most declined to make an offer because of the uncertain regulatory future and the company's highly leveraged status.⁸⁰ DFC Global ultimately received two offers: one from Lone Star Capital, who made a nonbinding offer of \$12.16 per share, and the other from J.C. Flowers & Co, LLC, who made a nonbinding offer of \$13.50 per share.⁸¹

Following these offers, DFC Global's efforts at compliance with the new and impending regulations caused its stock prices and earnings projections to fall precipitously starting in early 2014.⁸² J.C. Flowers & Co. withdrew its bid.⁸³ As DFC revised its earnings projections downward, Lone Star Capital correspondingly lowered its offer, until it made a final offer in late March 2014 of \$9.50 per share.⁸⁴ DFC Global accepted this

73. See *id.* at 386–87 (approving Court of Chancery's use of comparable companies analysis).

74. See *id.* at 388 (requiring Court of Chancery to give rationale for weight attributed to factors and finding it failed to do so).

75. See *id.* at 388–89 (reversing and remanding for new appraisal).

76. See *In re Appraisal of DFC Glob. Corp.*, No. CV 10107-CB, 2016 WL 3753123, at *1 (Del. Ch. July 8, 2016) ("DFC's business focuses on alternative consumer financial services, colloquially known as payday lending."), *rev'd sub nom.* *DFC Glob. Corp. v. Muirfield Value Partners, L.P.*, 172 A.3d 346 (Del. 2017).

77. See *id.* at *3 (describing origination of sales process).

78. See *id.* at *2–3 (describing uncertainty of DFC Global Corporation's future).

79. See *id.* (describing regulatory restriction and effects on DFC Global Corporation).

80. See *id.* (describing initial search for buyer).

81. See *id.* at *4 (describing initial nonbinding offers).

82. See *id.* (describing falling prospective value of company).

83. See *id.* (describing withdrawal of offer).

84. See *id.* (describing Lone Star Capital's declining offer price).

offer, and the merger finalized.⁸⁵ However, several shareholders dissented from that finalized merger.⁸⁶ Shortly after the transaction closed in June 2014, these dissenting shareholders filed for appraisal under Section 262 of the Delaware Code.⁸⁷

B. *You Keep All Your Money in a Big Brown Bag: The Court of Chancery's Appraisal Action and Appeal*

The Court of Chancery found that the parties should be granted appraisal under Section 262 of the Delaware Code.⁸⁸ In the ensuing appraisal litigation, the parties presented different methods of appraising the shares, resulting in greatly disparate values.⁸⁹ The dissenting shareholders relied exclusively on the discounted cash flow model to appraise the share value at \$17.90 per share.⁹⁰ DFC Global relied on the discounted cash flow model, a comparable companies analysis, and the deal price to appraise the share value at \$7.94 per share.⁹¹

The Court of Chancery combined three valuation methods to appraise the fair value of the DFC Global shares at \$10.21.⁹² First, it embarked on its own discounted cash flow model, utilizing various elements from each party's expert, to reach a share value of \$13.07.⁹³ Second, it adopted DFC Global's comparable companies analysis, which valued DFC Global's shares at \$8.07.⁹⁴ Third, it included the deal price as a factor.⁹⁵

85. *See id.* (describing finalization of merger).

86. *See id.* at *1 (describing dissenting shareholders). The dissenting shareholders collectively owned 4,604,683 shares in DFC Global. *See id.* (describing dissenting shareholders stake in company). These shareholders were hedge funds—Muirfield Value Partners, LP, Candlewood Special Situations Master Fund, Ltd., CWD OC 522 Master Fund, Ltd., and Oasis Investments II Master Fund Ltd.—suggesting the dissenting action was classic appraisal arbitrage. *See id.* (identifying dissenting shareholders seeking appraisal).

87. *See id.* at *5 (describing appraisal action filed by dissenting shareholders).

88. *See id.* (granting appraisal remedy).

89. *See id.* (outlining parties' valuation methods and results).

90. *See id.* at *6 (reviewing dissenting shareholder's valuation methodology).

91. *See id.* at *6 (reviewing DFC Global's valuation methodology). As the Court of Chancery noted, the parties' disparate valuation methods create a gap between the appraisals of \$10.09, which is larger than the deal price itself. *See id.* (noting disparity in parties' expert valuations).

92. *See id.* at *23 (establishing final appraisal value).

93. *See id.* at *6–19 (describing court's discounted cash flow analysis using elements from each party's expert). Discounted Cash Flow analysis, or DCF, values a company based on the present value of its future cash flow projections. *See Discounted Cash Flow Definition*, WALL STREET OASIS, <https://www.wallstreetoasis.com/finance-dictionary/what-is-a-discounted-cash-flow-DCF> [<https://perma.cc/HH8B-KSGQ>] (defining discounted cash flow analysis).

94. *See id.* at *19–20 (describing court's adoption of comparable companies analysis). A comparable companies analysis creates a "peer group" of similar companies and values the company based on an averaging of those companies' valuations. *See id.* (describing method for comparable companies analysis).

95. *See id.* at *20–21 (including deal price as factor in valuation). The deal price is the simplest valuation method: it plainly adopts the market's valuation as

The Court of Chancery found the deal price could not be given exclusive weight because (1) DFC Global was navigating turbulent regulatory issues at the time of the sale, which may have obscured its true future value and (2) Lone Star Capital was a financial sponsor rather than a business operator, and may have based its offer price on “achieving a certain internal rate of return and on reaching a deal within its financing constraints, rather than on DFC’s fair value.”⁹⁶ The Court of Chancery gave each appraisal method equal weight.⁹⁷ On appeal from both parties, the Delaware Supreme Court reversed the Court of Chancery and remanded for a new appraisal.⁹⁸

C. *You Never Give Me Your Money: The Delaware Supreme Court Finds Deal Price Deserves More Weight*

The Delaware Supreme Court began by reviewing the gloomy landscape for DFC Global surrounding the sale.⁹⁹ It noted that DFC Global had experienced explosive growth over the last twenty years, but had shrunk in the years leading up to the sale.¹⁰⁰ In addition, DFC Global was highly leveraged with a debt load almost four times its equity.¹⁰¹ Also, the company faced “regulatory headwinds” that rendered the future uncertain.¹⁰² The court also noted further negative signs surrounding the sale itself.¹⁰³ For instance, DFC Global had tried to refinance some of its senior debt and failed because its credit rating had recently been down-

represented by the price offered and accepted for the sale of the company. *See id.* (describing deal price as valuation method).

96. *See id.* at *22 (offering reasons for declining to give deal price prevalent weight).

97. *See id.* at *21 (dividing weight equally among three factors). As the Court of Chancery pointed out, Delaware has used multiple factors to determine a fair appraisal price in the past. *See id.* n.235 (identifying various appraisal factors used by Delaware courts). The court cites *Hanover Direct, Inc. S’holders Litig.*, Civil Action Nos. 1969–CC, 3047–CC, 3291–CC, 2010 WL 3959399, at *2–3 (Del. Ch. Sept. 24, 2010) (adopting valuation of expert who applied multiple valuation techniques, noting that Court has more confidence in accuracy of multiple valuation methods when results support each other, and criticizing other expert’s use of only one technique rather than blend of valuation methods) and *Andaloro v. PFPC Worldwide, Inc.*, No. Civ.A. 20336, Civ.A. 20289, 2005 WL 2045640, at *20 (Del. Ch. Aug. 19, 2005) (attributing 75% weight to discounted cash flow because management projections were reliable, and 25% weight to comparable companies analysis because of good peer group and benefit of additional insight provided by approach).

98. *See* DFC Glob. Corp. v. Muirfield Partners, L.P., 172 A.3d 346, 388–89 (Del. 2017) (reversing and remanding Court of Chancery).

99. *See id.* at 353–54 (describing leveraged status of DFC Global Corporation and regulatory headwinds that created bleak business future).

100. *See id.* at 351–53 (tracking DFC Global Corporation’s historic growth rates).

101. *See id.* at 353 (noting DFC Global Corporation’s debt problems).

102. *See id.* at 353–54 (noting presence of potentially upsetting regulations before merger).

103. *See id.* at 355–56 (noting negative financial indicators related to sale).

graded.¹⁰⁴ Leading up to the sale, DFC Global had revised its projected earnings downward each month, but despite these revisions, the company still failed to meet its target earnings after the sale.¹⁰⁵

After summarizing the Court of Chancery's appraisal, the Delaware Supreme Court moved to the parties' cross-appeals.¹⁰⁶ DFC Global raised three issues on appeal.¹⁰⁷ First, it asked the court to adopt a "judicial presumption" setting the appraisal at the deal price where there was a robust sale process in an arm's-length transaction (i.e. a clean merger).¹⁰⁸ Second, absent a judicial presumption, DFC Global argued the Court of Chancery gave insufficient weight to the deal price.¹⁰⁹ Third, DFC Global argued the Court of Chancery made errors of assumption in its discounted cash flow analysis.¹¹⁰ On cross-appeal, the dissenting shareholders argued the Court of Chancery should not have given weight to a comparable companies analysis and should have relied exclusively on the discounted cash flow analysis.¹¹¹ Finally, the Delaware Supreme Court itself raised the "implied argument" that the Court of Chancery lacked a rationale for giving all three factors in the appraisal equal weight.¹¹²

The Delaware Supreme Court denied DFC Global's first appeal arguing for a "judicial presumption" of the deal price because creating a presumption would contravene the clear statutory language in Delaware's

104. *See id.* (noting credit downgrading leading up to sale).

105. *See id.* (noting failure to meet income projections).

106. *See id.* at 357–61 (summarizing Court of Chancery appraisal).

107. *See id.* at 362–63 (introducing DFC Global's three appeal issues).

108. *See id.* at 362 (describing DFC Global's argument that presumption be given to deal price "in appraisal cases where the transaction was the product of certain market conditions"). Additionally, as the Supreme Court noted, "DFC argues that those conditions pertain to this case and the Court of Chancery erred by not giving presumptive and exclusive weight to the deal price." *Id.* (acknowledging DFC Global's argument for presumptive fairness of deal price).

109. *See id.* (describing DFC's "more case-specific" appeal arguing Court of Chancery's reasons for diminishing weight given to deal price "not rationally supported by the record").

110. *See id.* at 362–63 (describing DFC Global's appeal regarding Court of Chancery's discounted cash flow analysis). DFC Global's appeal on this point regarded the re-argument after the original Court of Chancery appraisal trial. *See id.* (describing post-trial re-argument). During that re-argument, the Court of Chancery admitted a clerical error that revised its discounted cash flow model from well above the deal price—\$13.07—to well below—\$7.70. *See id.* at 361–62 (identifying clerical error in valuation). The Court of Chancery, however, also revised its estimation of the working capital available to DFC, and as a result revised its projections of future profits upward so that its discounted cash flow analysis ultimately returned to almost exactly its previous level. *See id.* (describing Court of Chancery's revision of other factors in valuation).

111. *See id.* at 362–63 (describing petitioners' cross-appeal).

112. *See id.* at 363 (noting that "DFC's overall argument raises another implied argument, which is that the Court of Chancery's decision to afford equal weight to the [three factors] was arbitrary and not based on any reasoned explanation of why that weighting was appropriate").

appraisal statute.¹¹³ The court noted it had already rejected this judicial presumption in *Golden Telecom Inc. v. Global GT LP*,¹¹⁴ finding in that case that Delaware's appraisal statute allowed the Court of Chancery to use its discretion and entertain "all relevant factors" in determining a fair price.¹¹⁵ Creating a judicial presumption would also require the court to "craft . . . the precise pre-conditions that would be necessary to invoke a presumption of that kind."¹¹⁶ Creating these pre-conditions, however, would create a rigid framework that might prevent judicial discretion in the instances when it would be needed most.¹¹⁷ Finally, the court held there is no need for a judicial presumption because the Court of Chancery has shown that in clean transactions, it already gives great deference to the deal price, rendering an explicit presumption unnecessary.¹¹⁸

The high court in Delaware granted DFC Global's second appeal, holding that the deal price should have been given greater weight in the

113. *See id.* (rejecting judicial presumption because presumption would go against § 262, which requires judges to consider "all relevant factors" in appraisal trial).

114. 11 A.3d 214 (Del. 2010).

115. *See DFC Glob. Corp.*, 172 A.3d at 363–64 (explaining reasoning in *Golden Telecom*). The court noted the key statutory provision is found in § 262(h):

Through such proceeding the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account *all relevant factors*.

DEL. CODE ANN. tit. 8 § 262(h) (requiring Court of Chancery to account for all relevant factors) (emphasis added). In *Golden Telecom*, the Delaware Supreme Court found § 262(h) "unambiguously calls upon the Court of Chancery to perform an independent evaluation of 'fair value' and 'vests the Chancellor and Vice Chancellors with significant discretion to consider 'all relevant factors' and determine the going concern value of the underlying company.'" *Golden Telecom Inc.*, 11 A.3d at 217–18 (describing statutory requirements for evaluation in § 262(h)). Given this statutory mandate, requiring the Court of Chancery to defer to the deal price "would inappropriately shift the responsibility to determine 'fair value' from the court to the private parties." *Id.* (assessing appropriateness of presumption for deal price). Rejecting a judicial presumption is necessary to preserve the judicial discretion the statute specifically authorizes. *See id.* (explaining rejection of judicial presumption for deal price).

116. *See DFC Glob. Corp.*, 172 A.3d at 366 (highlighting that creation of presumption of deal price as fair value would require court to outline in detail what conditions sale must meet to invoke presumption). The Delaware Supreme Court's underlying thrust in rejecting a presumption is that this is work for the legislature, not the judiciary. *See id.* ("DFC would have us put a judicial gloss on the broad 'all relevant factors' language . . . [w]e do not, however, view the statutory language as inviting us to do so.").

117. *See id.* (warning against hazards of creating judicial presumption).

118. *See id.* (explaining there is no need for presumption because of "the proven record of our Court of Chancery in exercising its discretion to give the deal price predominant, and *indeed exclusive weight*, when it determines, based on the precise facts before it that led to the transaction, that the deal price is the most reliable evidence of fair value." (emphasis added)).

appraisal.¹¹⁹ The court spent its greatest focus on this issue.¹²⁰ It indicated in clear terms that when there is a robust sale process and the sale is free of the suspicion of self-dealing—as was the case in the DFC Global sale—“[w]e can take the market’s word for it.”¹²¹ The court pointed out that the DFC Global sale was particularly poised to receive a fair market price: it was a publicly traded company, it was actively traded, it was actively examined by debt markets and credit agencies, and during the sale process “numerous strategic and financial buyers” were given access to privileged company information to make their assessments and offers.¹²²

In diminishing the weight it gave to the deal price, the Court of Chancery relied on two factors, which the Delaware Supreme Court rejected.¹²³ First, the Court of Chancery found that DFC Global had been undervalued because regulatory concerns had put it in a “trough” from which it might successfully emerge.¹²⁴ The Delaware Supreme Court found the market had already accounted for this possibility in the sale price.¹²⁵ Second, the Court of Chancery held that because the purchaser, Lone Star

119. *See id.* at 376. (agreeing with DFC Global’s argument on appeal that Court of Chancery should have given deal price greater weight).

120. *See id.* at 366–76 (addressing weight given to deal price). With almost ten pages dedicated to addressing this appeal, the Delaware Supreme Court affords it nearly as much space as the other four appeal issues combined. *See id.* at 363–88 (emphasizing importance of appeal regarding deference to deal price).

121. *See id.* at 370 (emphasizing fairness of market price (quoting RICHARD A. BREALEY, *PRINCIPLES OF CORPORATE FINANCE* 214 (9th ed. 2008))). The Delaware Supreme Court strongly emphasizes the trustworthiness of the market: while the deal price may not *always* be right, a Court of Chancery judge “should have little confidence she can be the special one able to outwit the larger universe of equally avid capitalists with an incentive to reap rewards by buying the asset if it is too cheaply priced.” *See id.* at 367 (addressing proper weight to give to deal price). Further, in a fair, arm’s-length bidding process, “the resulting collective judgment as to value is likely to be highly informative and that, all estimators having equal access to information, the likelihood of outguessing the market over time and building a portfolio of stocks beating it is slight.” *See id.* at 370 (indicating completeness of market price).

122. *See id.* at 372 (describing factors accounting for trustworthy fair market sale price).

123. *See id.* (describing Court of Chancery’s factors for lack of deference to deal price).

124. *See id.* at 372–75 (explaining Court of Chancery’s reasoning in holding DFC Global to be undervalued in sale).

125. *See id.* (positing that market already accounted for regulatory risks in sale price). The Delaware Supreme Court’s rebuttal to the Court of Chancery’s argument is that risk is a part of value: given the facts surrounding the sale, DFC Global seemed to have an equal chance of either emerging from the new regulations as the industry leader or ceasing to be a going concern. *See id.* (evaluating DFC Global’s future prospects). The market observed the same company potential as the Court of Chancery and, based on numerous factors, did not accept DFC Global’s “growth story.” *See id.* at 375 (explaining market’s reasoning in deal price). This did not mean, as the Court of Chancery suggested, that the market ignored these risk factors; rather, “the record demonstrates that the markets factored regulatory risk into DFC’s pricing.” *See id.* (describing effect of regulatory risks on market price).

Capital, was a private equity firm, it purchased DFC Global based on financial reasons—to meet a required rate of return—rather than on strategic reasons, and strategic reasons may have given greater value to the company’s potential.¹²⁶ The Delaware Supreme Court also rejected this factor because “all disciplined buyers,” whether companies or financiers, have required rates of return, and without evidence of an unfair deal, the motivation for purchase should not affect the valuation.¹²⁷

The Delaware Supreme Court granted DFC Global’s third appeal, which argued that the Court of Chancery had erred in its discounted cash flow analysis, because the record did not support a rapid growth prediction for the company.¹²⁸ The Court of Chancery assumed DFC Global would expand at a rate significantly higher than ordinary mature, stable companies.¹²⁹ The Delaware Supreme Court found the Court of Chancery accepted DFC Global’s “unbroken, sunny sky assumptions” about the company’s future without support from the record.¹³⁰ DFC Global’s projections for its future were suspect, and economic principles cast serious doubt on the ability of any company to sustain the growth the Court of Chancery credited to DFC Global’s future.¹³¹

126. *See id.* at 375–76 (explaining Court of Chancery’s reasoning regarding its second factor in lack of deference to deal price).

127. *See id.* (rejecting Court of Chancery’s contention that Lone Star’s status as private equity firm caused it to undervalue DFC Global). The Delaware Supreme Court pointed out that the fair deal price was especially evident in the case of DFC Global because of several reasons:

i) there was no conflict of interest; ii) Houlihan had approached every logical buyer; iii) no one was willing to bid more in the months leading up to the transaction before management significantly adjusted downward its projections; and iv) management continued to miss its targets after Lone Star was the only buyer remaining.

Id. at 376 (noting aspects of clean merger in DFC Global sale process).

128. *See id.* at 376–85 (rejecting Court of Chancery’s assumptions in its discounted cash flow analysis).

129. *See id.* at 377–78 (summarizing Court of Chancery’s upward revisions of its “perpetuity growth rate”).

130. *See id.* at 378 (finding Court of Chancery’s assumptions about DFC’s future earnings not supported by record). The Supreme Court found that “despite . . . risks and rather gloomy outlook [for DFC Global], the Court of Chancery swallowed the March Projections whole, generously giving DFC credit for a period of projected growth until 2018.” *See id.* at 382–83 (evaluating Court of Chancery’s valuation methodology).

131. *See id.* at 381–85 (disagreeing with Court of Chancery’s assumptions about DFC Global’s future potential). The Delaware Supreme Court named five factors that discredit the growth rates the Court of Chancery used in its discounted cash flow analysis: (1) the growth rates were being used by DFC in an attempt to sell the company, and so they were too optimistic; (2) DFC had experienced nearly 20 years of rapid growth, and then stabilized and shrunk in the years prior to the sale, indicating it had reached maturity; (3) the future growth was not grounded in any testimony; (4) the regulatory pushback against the entire payday lending industry suggested that growth could never be sustained at previous rates; and (5) the dissenting shareholders’ own expert testified that DFC had reached a stable growth rate. *See id.* (explaining factors on record contrary to Court of Chancery’s evaluation of potential future growth).

The Delaware Supreme Court denied the dissenting shareholders' appeal because it found allowing a comparable companies analysis was reasonable.¹³² The dissenting shareholders argued that DFC Global, unlike comparable companies, was poised to take market control, and therefore comparing it to other companies' values detracted from its market potential.¹³³ The Delaware Supreme Court rejected this argument because although DFC had potential for growth, it also had potential for collapse under regulatory pressure—these balanced risks provided no reason to value it higher than similar, competing companies.¹³⁴ The Delaware Supreme Court also found the Court of Chancery was right not to rely exclusively on the discounted cash flow analysis.¹³⁵

Finally, the Delaware Supreme Court granted DFC Global's "implied argument" that the Court of Chancery was required to offer a rationale for the weight it gave each factor in the appraisal.¹³⁶ The court found that not only the valuation methods, but the weight accorded to each must be grounded in the record.¹³⁷ The court reiterated that there was no presumption of how to weigh factors, and the Court of Chancery was obligated to exercise its discretion in doing so.¹³⁸

132. *See id.* at 386–88 (addressing petitioners' cross-appeal).

133. *See id.* at 386 (summarizing petitioners' first argument in cross-appeal).

134. *See id.* at 386–87 (explaining reasons for rejecting cross-appeal). The dissenting shareholders' arguments were threefold: (1) the Court of Chancery relied on "trough years," or bad earning years to compare DFC Global's earnings to competing companies; (2) the results would have been different if a single year rather than a spread had been used; and (3) the companies used in the comparable companies analysis were not comparable to DFC Global. *See id.* (explaining dissenting shareholders' arguments for higher valuation price). The Delaware Supreme Court rejected all these arguments, finding there was no evidence that DFC Global was primed for a surge in growth, that a spread of years was more reasonable than a single year's comparison, and that the dissenting shareholders' own expert had compared DFC Global to the same six companies as DFC Global's expert. *See id.* at 386–88 (rejecting petitioners' arguments and approving comparable companies analysis).

135. *See id.* at 388 (finding no abuse of discretion in Court of Chancery for relying on multiple valuation methods). Given the large disparity yielded by the discounted cash flow models used by the two parties' experts and given the inherent instability of that method of valuation, the Delaware Supreme Court reasoned that using such a method exclusively would have been improper. *See id.* (rejecting dissenting shareholders' argument that discounted cash flow analysis should have been sole valuation method).

136. *See id.* at 388 (addressing "implied argument" that Court of Chancery was required to offer rationale for weight accorded to each valuation method).

137. *See id.* (finding weight granted each method must be grounded in record and explained).

138. *See id.* at 388–89 (holding Court of Chancery had discretion in weighing appraisal factors). The Delaware Supreme Court blocked a "back door" judicial presumption in this instance that would have allowed the Court of Chancery discretion in selecting appraisal factors but enforced a presumption regarding the weight to accord to each. *See id.* at 388 ("[I]n keeping with our refusal to establish a 'presumption' in favor of the deal price because of the statute's broad mandate, we also conclude that the Court of Chancery must exercise its considerable discretion" in weighing factors).

In summary, the Delaware Supreme Court held that the Court of Chancery needed to give additional weight to the deal price, and indicated that under fair market conditions, in an arm's-length sale, the market truly can account for nearly every factor, requiring strong evidence to find the deal price unfair.¹³⁹ Despite this strong deference to the deal price, the Supreme Court declined to establish a presumption that the deal price *must* be the appraisal price in a clean transaction.¹⁴⁰ Although it found the Court of Chancery's calculations unsupported by the record, the Delaware Supreme Court did not prohibit the Court of Chancery from entertaining other factors besides the deal price on remand.¹⁴¹ By reversing and remanding, the Delaware Supreme Court ensured the Court of Chancery would give additional weight to the deal price, and that it would fully explain the weight it gave each factor in its new reappraisal.¹⁴²

IV. FIXING A HOLE: *DFC GLOBAL* HELPS REHABILITATE THE DELAWARE APPRAISAL STATUTE

By reversing and remanding the Court of Chancery, the Delaware Supreme Court accomplished three important goals that will help contain the practice of appraisal arbitration.¹⁴³ First, it followed the legislature's clear intent to curb arbitrage in clean transactions.¹⁴⁴ Second, it preserved judicial discretion to appraise at a value other than the deal price, a discretion not only required by the statute but also necessary for the court's ability to vindicate minority shareholder rights.¹⁴⁵ Third, it sent a clear message to arbitrageurs that the practice will not be given a warm welcome in clean mergers.¹⁴⁶

139. For an in-depth discussion of the Supreme Court's holding regarding the weight to be given the deal price, see *supra* notes 119–22 and accompanying text.

140. For an in-depth discussion of the Supreme Court's rejection of a judicial presumption in favor of the deal price, see *supra* notes 113–18 and accompanying text.

141. For an in-depth discussion of the Delaware Supreme Court's allowance of a comparable company analysis and the discounted cash flow analysis as appraisal valuation techniques, see *supra* notes 132–35 and accompanying text.

142. See *DFC Glob. Corp.*, 172 A.3d at 388–89 (remanding to Court of Chancery). The Delaware Supreme Court stated the remand was for “the Chancellor to reassess his conclusion as to fair value in light of our decision,” and that it would “leave the Chancellor with the discretion to address the open issues using procedures he finds the most helpful.” See *id.* at 389 (providing instructions for appraisal on remand).

143. See Weinstein, *supra* note 64 (describing limiting effect of *DFC Global*).

144. See Onyeador, *supra* note 4, at 357 (identifying amendments to § 262 as legislature's “effort to curb appraisal arbitrage.”).

145. See *DFC Glob. Corp.*, 172 A.3d at 363–66 (declining to adopt judicial presumption that market price in clean merger is fair value).

146. For an in-depth discussion of the effect of the *DFC Global* opinion on practitioners, see *infra* notes 156–74 and accompanying text.

A. *Power to the People: The Delaware Supreme Court Follows the Legislature's Lead While Preserving Judicial Discretion in Appraisal Rights*

The *DFC Global* opinion effectively furthers the legislature's intent in its amendments to Section 262.¹⁴⁷ The legislative amendments of 2016 will likely reduce arbitrage cases that constitute strike suits.¹⁴⁸ *DFC Global* has the same effect; it virtually ensures an arbitrageur will be unable to bring shares from a clean transaction to the court and profit from a higher appraisal.¹⁴⁹ Though the opinion does not limit arbitrage in any other merger context, this is a severe blow to the practice because the great majority of arbitrage claims are filed in clean mergers.¹⁵⁰

Because appraisal arbitrage generates money through both the judicial appraisal award and the statutory interest earned on that award, the courts and the legislature both have power over the practice—in order for any effort to stymie arbitrage to succeed, both these branches of government must cooperate.¹⁵¹ In this case, they have done so, allowing the judiciary to maintain its discretion and allowing the legislature to avoid legislation that could unnecessarily and harmfully limit shareholder appraisal rights.¹⁵²

By declining to create a judicial presumption that the deal price is the fair value in a clean merger, the Supreme Court avoided the pitfalls of legislating from the bench.¹⁵³ Creating a judicial presumption would, as the court noted, require it to state in detail the criteria for meeting that

147. See Allen, *supra* note 43, at 761 (describing legislative intent of amendments to § 262).

148. See Jiang, *supra* note 12, at 727 (“[B]oth the de minimis exception and the interest reduction amendment reforms . . . are very likely to reduce the incidence of strike suits.”).

149. See *DFC Glob. Corp.*, 172 A.3d at 370–71 (emphasizing importance and trustworthiness of deal price). The Delaware Supreme Court emphasized the trustworthiness of the deal price even more in a subsequent case, where it gave “the vice chancellor the discretion on remand to enter judgment at the deal price if he so chooses, with no further proceedings.” See *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*, No. 565, 2016, 2017 WL 6375829, at *34 (Del. Dec. 14, 2017) (giving instructions for remand).

150. See Kesten, *supra* note 7, at 92 (“[O]ver 93% of appraisal petitions filed against public companies during 2015 and 2016 challenged arm’s length transactions.”).

151. See Meyer, *supra* note 54, at 192 (arguing both Court of Chancery and legislature have role in reforming appraisal litigation). Meyer argues that the Court of Chancery is “better suited to solve this problem than the legislature is,” because deferring to the merger price, which is the court’s prerogative, “has the institutional capacity to deter these unwanted, speculative, and potentially abusive appraisal claims,” while the effect of the legislative amendments will be limited. See *id.* (describing role of government branches in preventing meritless arbitrage).

152. For a further discussion of the restrictive effects of the legislative amendments, including an argument that it may be a detriment to shareholder rights, see *supra* note 60.

153. See *DFC Glob. Corp.*, 172 A.3d at 348 (declining to adopt judicial presumption because presumption “has no basis in the statutory text” and therefore “until the General Assembly wishes to narrow the prism through which the Court of

presumption.¹⁵⁴ A court cannot foresee all possible future cases, and *DFC Global* allows for the possibility that an otherwise clean merger might contain extraordinary facts that require a fair value different from the deal price.¹⁵⁵

B. *The Long and Winding Road: Attorneys Should Understand that Appraisal Arbitrage is Being Starved in Clean Mergers*

Attorneys representing arbitrageurs should understand the risks of exercising appraisal rights in a clean merger.¹⁵⁶ Arbitrage no longer “resembles buying a lottery ticket with a guaranteed minimum payout equal to the purchase price.”¹⁵⁷ The risks for any client in a clean merger are now heightened because outside of extraordinary circumstances, the Court of Chancery will not appraise fair value above the deal price.¹⁵⁸ Even if it does, there is now strong Delaware Supreme Court precedent to reverse such an appraisal.¹⁵⁹ Combined with the ability of the surviving corporation to avoid interest payments, any appraisal filed in a clean merger runs the risk of racking up fees and costs that will turn the investment into a loss for the client.¹⁶⁰ A still more dismal prospect is that the Court of Chancery will appraise at less than the deal price, exposing the client to serious losses.¹⁶¹ In the case of a clean merger, the courts have

Chancery looks at appraisal value in specific classes of mergers, this Court must give deference”).

154. *See id.* at 366 (“[W]e do not share DFC’s confidence in our ability to craft, on a general basis, the precise pre-conditions that would be necessary to invoke a presumption of that kind.”).

155. *See id.* at 388 (“In some cases, it may be that a single valuation metric [besides deal price] is the most reliable evidence of fair value and that giving weight to another factor will do nothing but distort that best estimate.”).

156. *See Meyer*, *supra* note 54, at 191 (“Increased use of merger price as the best evidence of fair value could have a dramatic effect on appraisal arbitrageurs’ investment strategy.”).

157. *See Davis*, *supra* note 41, at 1 (describing predictability of profit from appraisal arbitrage prior to *DFC Global*).

158. *See id.* (noting Delaware Supreme Court’s requirement that “substantial record-based evidence must support a judicial decision that other factors outweigh a fairly negotiated deal price in an appraisal valuation.”). Davis writes that “absent unusual circumstances, such as a conflict of interest or related party transaction,” the deal price will function as “the lodestar for appraisal proceedings.” *See id.* at 2 (arguing that deal price is best indicator of fair value).

159. *See, e.g., Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*, No. 565, 2016, 2017 WL 6375829 (Del. Dec. 14, 2017) (remanding to Court of Chancery to give greater or exclusive weight to deal price).

160. *See Onyeador*, *supra* note 4, at 357 (noting that “appraisal proceedings usually cost millions of dollars to litigate”). Offsetting this risk to a degree, § 262(j) allows for equitable fee shifting. *See DEL. CODE ANN.* tit. 8, § 262(j) (West 2017) (allowing equitable fee shifting in appraisal litigation).

161. *See Frankel*, *supra* note 56 (noting Court of Chancery’s valuations at less than deal price creates risk for arbitrageurs); *see also LongPath Capital, LLC v. Ramtron Int’l Corp.*, No. CV 8094-VCP, 2015 WL 4540443 (Del. Ch. June 30, 2015) (valuing company at deal price and subtracting synergies to arrive at appraisal

simply not found that meritorious litigation is likely.¹⁶² This opens the possibility that the attorney or law firm bringing the appraisal could be seen as filing strike suits, and the attorney's and law firm's reputation could suffer as a result.¹⁶³

Attorneys should not deter clients from practicing arbitrage, but should be sophisticated in picking the mergers to target.¹⁶⁴ Evidence suggests that appraisal arbitrage can be an effective tool to solve a collective action problem by litigating where individual and unsophisticated shareholders would have little motivation to vindicate their rights.¹⁶⁵ In these situations, the courts do not discourage arbitrage, and the practice will likely continue.¹⁶⁶ Even the advocates of appraisal arbitrage, however, agree that the practice is less effective and perhaps unneeded where the market has determined a price in a fair sale process.¹⁶⁷ Appraisal litigants

value below deal price); Meyer, *supra* note 54, at 178 (noting that "policy motivations may have also been at play in the court's decision" in *LongPath*).

162. See, e.g., Glasscock, *supra* note 13, at 10 (arguing that believing in appraisal rights in clean transaction requires believing in several "unlikely" propositions). Vice Chancellor Glasscock suggests that anyone who believes that fair value should not be set at the deal price in a clean transaction must also believe that (1) there is an inherent value to an entity independent of the market, (2) the inherent value can be higher than that developed by a clean sale, and (3) the inherent value is higher than determined by a disinterested board. See *id.* (arguing for deal price as best indicator of fair value). "These propositions are, to my mind," Vice Chancellor Glasscock writes, "more or less unlikely." See *id.* (evaluating extra-market factors incorporated into value).

163. Cf. Kesten, *supra* note 7, at 114–15 (describing interest rate arbitrage as nuisance suit and "rent seeking").

164. See Tucker, *supra* note 29 (suggesting investors should actively pursue appraisal arbitrage while it is still allowed in Delaware).

165. See Boca, *supra* note 50, at 446 (describing arbitrage's ability to solve collective action problem by decreasing costs for smaller shareholders to dissent). Appraisal actions often suffer from an acute collective action problem because, with some exceptions, class action litigation is prohibited, so plaintiffs must bring claims individually. See *id.* (describing requirements for bringing appraisal arbitrage claim). "[I]t is often cost prohibitive for small shareholders to pursue this remedy." See Kesten, *supra* note 7, at 100 (describing restrictions on appraisal process). Arbitrage creates sufficient motivation to make it more feasible to bring a claim without creating the agency problems brought by class action. See Boca, *supra* note 50, at 446 (describing benefits of arbitrage).

166. See Onyeador, *supra* note 4, at 357 (noting that neither amendment of § 262 prevents arbitrage, and in fact amendments may discourage individual shareholder appraisal while continuing to allow appraisal by arbitrageurs).

167. See Korsmo, *supra* note 5, at 1557 (arguing "a genuine market test of the target company will necessarily provide a superior valuation of the stockholders' interest, and in such circumstances an appraisal proceeding can only cause mischief"). Korsmo argues in favor of appraisal arbitrage to the extent that it targets deals vulnerable to minority shareholder exploitation. See *id.* at 1556 (arguing for benefits of appraisal arbitrage). Korsmo goes so far as to argue the practice should be encouraged and used as a model for other areas of corporate litigation. See *id.* (suggesting arbitrage could be model for corporate litigation). Despite this strong position in favor of arbitrage, when it comes to a fair and robust sale process, Korsmo suggests going further than the Delaware Supreme Court or the Delaware Legislature and creating a "safe harbor" to freeze appraisal at the deal price in

should listen to the message from the Delaware courts and legislature: appraisal arbitrage “ought to lead to litigation that bears markers of litigation merit.”¹⁶⁸ This means targeting cases for arbitrage where minority shareholders are most likely to be exploited.¹⁶⁹ Attorneys should counsel arbitrageurs toward controlled, conflicted, or low premium mergers, where arbitrage is most likely to be profitable and will also benefit other minority shareholders.¹⁷⁰

Finally, after *DFC Global*, it is no longer the case that appraisal arbitrage looms “regardless of how hard seasoned M&A advisors and corporate fiduciaries work to ensure a process that is robust and pristine.”¹⁷¹ Attorneys who advise clients on mergers and acquisitions can now work positively to avoid the price tag of appraisal arbitrage by encouraging robust auctions, fair prices, and arm’s-length transactions.¹⁷² Limiting the fair value in an appraisal arbitrage action to the deal price could save a client hundreds of millions of dollars, an amount worth considering in making every effort to conduct a clean merger.¹⁷³

such transactions. *See id.* at 1557 (“[W]e would support the development of a safe harbor to eliminate appraisal where the transaction has undergone a true auction.”).

168. *See id.* at 1583 (arguing appraisal arbitrage ought to target limited set of “right transactions”).

169. *Cf. Onyeador, supra* note 4, at 353 (noting that “[t]heoretically, appraisal arbitrageurs should want to target deals with a high probability of underpricing”). The “theoretical” transactions that arbitrageurs should be targeting are the exact transactions the Delaware courts and legislature are now effectively constraining them to target. *See supra* notes 178-80 for a discussion of the probable effects of the legislative amendments combined with *DFC Global*.

170. *See Kesten, supra* note 7, at 112–13 (claiming there is lack of evidence that threat of appraisal increases deal premiums offered in all situations (citing Paul G. Mahoney & Mark Weinstein, *The Appraisal Remedy and Merger Premiums*, 1 AM. L. & ECON. REV. 239, 242–43 (1999))).

171. *See Frankel, supra* note 50, at 20 (discussing motivation of mergers and acquisitions attorneys to conduct clean mergers).

172. *Cf. id.* (suggesting lack of motivation to conduct clean merger because of ubiquity of appraisal arbitrage). Frankel’s comments are particularly illuminating, as they were written just before the *DFC Global* opinion was released. *See id.* Citing the Delaware Supreme Court’s *Golden Telecom* case from 2010, he notes that “the Court of Chancery will not be bound by the deal price as the sole determinant of fair value in an appraisal action,” and that “[a]s a result, the potential for significant cost uncertainty looms on the Delaware transaction landscape, regardless of how hard seasoned M&A advisors and corporate fiduciaries work to ensure a process that is robust and pristine.” *See id.* (noting effects of *Golden Telecom* on mergers and acquisitions advisors). With the issuance of *DFC Global*—and now *Dell*—Frankel’s advisory warning is no longer the case: those same mergers and acquisitions advisors and corporate fiduciaries have a great deal of certainty that if they create a robust and pristine sale, the deal price will be given deference. *See DFC Glob. Corp v. Muirfield Partners, L.P.*, 172 A.3d 346, 370–71 (Del. 2017) (emphasizing deference to market price).

173. *See, e.g., Epstein, supra* note 50 (describing how Carl Icahn’s threat of appraisal action successfully blocked deal and raised price 400 million dollars).

V. CARRY THAT WEIGHT: *DFC GLOBAL* WILL CONTINUE TO CURB
ARBITRAGE IN CLEAN MERGERS

In December 2017, the Delaware Supreme Court issued *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*,¹⁷⁴ the first “progeny” of *DFC Global*.¹⁷⁵ In *Dell*, the Delaware Supreme Court reversed an appraisal when the Court of Chancery ruled that the sale price severely undervalued the computer giant.¹⁷⁶ *Dell* demonstrates the Delaware Supreme Court doubled-down on the principle it set forth in *DFC Global*: in a clean sale, there must be an extraordinary reason to depart from the deal price.¹⁷⁷ Though cases in recent years show that the Court of Chancery generally adheres to this principle, *DFC Global* sets a strong standard in case law for the lower court to look to when it refuses to appraise above the deal price.¹⁷⁸ The ultimate effect will be to severely limit the arbitrage practice in clean transactions.¹⁷⁹

While the precedent *DFC Global* set is clear, the effect on shareholders and on the market is less so.¹⁸⁰ Studies conducted on appraisal arbitrage

174. No. 565, 2016, 2017 WL 6375829, at *1 (Del. 2017).

175. See Lewkow, *supra* note 29 (“Dell builds on the Court’s DFC decision earlier this year in which the Court held that the merger price will generally be entitled to significant, if not dispositive, weight in an appraisal action involving the sale of a public company pursuant to an open, competitive, and arm’s-length bidding process.”). As Lewkow notes, *Dell* expands on *DFC Global* by applying the same principles even when there is “a limited pre-signing bidding process” and in non-controlling management buyouts. See *id.* (noting *Dell*’s expansion on *DFC Global* holding).

176. See *Dell, Inc.*, 2017 WL 6375829, at *1–2 (reversing and remanding to Court of Chancery for reappraisal).

177. See *id.* at *34 (allowing Court of Chancery to reappraise at deal price without further review).

178. See *DFC Glob. v. Muirfield Value Partners, L.P.*, 172 A.3d 346, 366 (Del. 2017) (noting that judicial presumption of deal price as fair value would be largely superfluous because Court of Chancery already consistently exercises this standard).

179. See, e.g., Glasscock, *supra* note 13, at 10 (finding “little to recommend extending an appraisal right to dissenters in the case of a ‘clean’ merger” because “efficiency of capital markets, not fairness, is the proper goal of the appraisal statute”); Meyer, *supra* note 54, at 191 (predicting outcome of limiting appraisal to deal price “could be the death knell for appraisal as a speculative investment strategy”).

180. See Kidwell, *supra* note 48 (analyzing effect of Delaware’s legislative and judicial amendments limiting arbitrage and suggesting it caused deal premiums to decline). Kidwell cites a Harvard Law study that shows “the decrease in deal premiums from 2016 to 2017 resulted in target shareholders losing around \$77.4 billion.” See *id.* (describing effects of Delaware’s statutory amendments (citing Matthew Schoenfeld, *The High Cost of Fewer Appraisal Claims in 2017: Premia Down, Agency Costs Up*, HARVARD L. SCH. FORUM ON CORP. GOVERNANCE & FIN. REG. (Sep. 8, 2017), <https://corpgov.law.harvard.edu/2017/09/08/the-high-cost-of-fewer-appraisal-claims-in-2017-premia-down-agency-costs-up/> [https://perma.cc/8QY2-NKU5])). Kidwell suggests these findings may demonstrate that arbitrage did not have a dampening effect on mergers and acquisitions. See *id.* (suggesting arbitrage may not have had negative market effect).

suggest it may benefit shareholders regardless of whether the transaction is clean.¹⁸¹ The threat of appraisal drives up sale prices, even if the deal is clean.¹⁸² If present trends continue, however, arbitrage will be contained to those transactions where it can help provide meaningful appraisal rights to minority shareholders.¹⁸³

181. *See id.* (suggesting Delaware's starvation of arbitrage practice has lowered deal prices). *But see* Kesten, *supra* note 7, at 92 ("If appraisal litigation is increasingly an exercise in rent seeking or interest rate arbitrage, it threatens to impose an inefficient transaction tax on certain mergers and may deter some worthwhile transactions altogether.").

182. *See, e.g.,* Cox, *supra* note 30 (indicating that "directors will be less sanguine about a proposal they submit to the shareholders for approval if they believe there is an efficient mechanism for shareholders to realize an alternatively determined value for their shares than that being recommended by the board of directors."); Korsmo, *supra* note 5, at 1556 ("A highly developed appraisal arbitrage market would aid minority shareholders . . . by deterring abusive mergers and by causing shares traded post-announcement to be bid up to the expected value of an appraisal claim.").

183. *See* Geis, *supra* note 49, at 1639 (describing possibility of minority shareholders using increased appraisal activity created by arbitrage to gain more meaningful appraisal rights).