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Stockholders of Parent-Target Not Entitled to Appraisal Rights in Merger Involving Transfer of Control

Recently, the Delaware Court of Chancery held that stockholders of Dr Pepper Snapple Group, Inc. were not entitled to appraisal of their shares in connection with a reverse triangular merger involving a subsidiary of Dr Pepper and the parent of Keurig Green Mountain, Inc. Because the transaction was structured so that Dr Pepper was not a “constituent corporation” in the merger and the public stockholders would retain their shares, the court found that the transaction did not satisfy the terms of Delaware’s appraisal rights statute. While the decision by Chancellor Bouchard in *City of North Miami Beach General Employees’ Retirement Plan v. Dr Pepper Snapple Group, Inc.* was notable because appraisal rights were denied even though Dr Pepper stockholders would transfer control of the company in what is effectively a mixed-consideration deal, it is unlikely to prove meaningful from a precedent standpoint except in cases involving the uncommon acquisition structure used in the transaction.

Background

Earlier this year, Dr Pepper and Keurig agreed to combine their companies through a reverse triangular merger that merges a subsidiary of Dr Pepper into the parent of Keurig (“Maple Parent”), resulting in Keurig becoming an indirect wholly owned subsidiary of Dr Pepper. Before the closing of the merger, Maple Parent will declare a \$9 billion cash dividend to Dr Pepper (payable immediately following the closing of the merger). Also before the closing, Dr Pepper will declare a \$103.75 per share special cash dividend to its stockholders of record as of the business day immediately preceding the closing of the merger (payable one business day after the effective time of the merger), funding this dividend with the \$9 billion received from Maple Parent along with funds from third-party sources. The Dr Pepper stockholders will retain their shares of Dr Pepper, and the ultimate owners of Maple Parent/Keurig will receive shares of Dr. Pepper in the transaction. Following the merger, Dr Pepper’s original stockholders will hold 13%, and the owners of Maple Parent/Keurig will hold 87%, of the equity of the combined company.

While not entitled to a vote on the merger, the Dr Pepper stockholders are being asked to approve two proposals necessary to effectuate the transactions: one, to approve the issuance of common stock as merger consideration, and two, to increase authorized shares to permit such issuance. In the proxy statement related to these approvals, the company stated that Dr Pepper stockholders do not have appraisal rights in connection with the transaction. Plaintiffs, stockholders of Dr Pepper, brought suit alleging a violation of Section 262 of the Delaware General Corporation Law (“DGCL”) governing

appraisal rights and breaches of fiduciary duty by the Dr Pepper board stemming from the failure to inform Dr Pepper stockholders that they were entitled to appraisal rights.

Analysis

In granting the defendants' motion for summary judgment, the Court of Chancery concluded that Dr Pepper stockholders were not entitled to appraisal rights for two reasons:

- *Dr Pepper was not a "constituent corporation" in the merger.* DGCL Section 262(b) provides that appraisal rights are available for the shares of "a constituent corporation in a merger or consolidation." While the DGCL does not explicitly define "constituent corporation," the court concluded that various other provisions of the DGCL using the term clearly implied that it only included entities that actually were merged or combined in the transaction and not a parent of such entities. Additionally, the court cited precedent in which "constituent" parties was interpreted to mean only those parties actually merging, with one such precedent case noting that "stockholders of a parent corporation of a merging subsidiary in a triangular merger 'generally do not have the right to vote on the merger, nor are they entitled to appraisal.'"
- *Dr Pepper stockholders retained their shares in connection with the merger.* Under Section 262's "market-out" exception, stockholders of a constituent corporation are not entitled to appraisal rights in a merger if their shares are either listed on a national securities exchange or held of record by more than 2,000 holders. The stockholders' appraisal rights might be restored, however, under an "exception to the exception" if they are required to accept in the merger anything other than: (i) shares of the surviving or resulting corporation in the merger, (ii) stock of a corporation that, at the effective time of the merger or consolidation, is listed on a national securities exchange or held of record by more than 2,000 holders, (iii) cash in lieu of fractional shares, or (iv) any combination of the foregoing.

Under this statutory scheme, the court noted that even if Dr Pepper were considered a constituent corporation, its stockholders would not be entitled to appraisal rights in the merger under the "market-out" exception because Dr Pepper shares are traded on a national securities exchange. Moreover, nothing in the "exception to the exception" would restore their appraisal rights because the stockholders were keeping their Dr Pepper shares in the merger, and therefore were not required to accept *anything* for their shares. The court recognized that the merger constituted a sale of control to Maple Parent, but noted that Section 262 does not grant appraisal rights simply upon a sale of control, but rather when stockholders' shares are "being taken from them in *certain, statutorily specified* types of transactions."

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