IN THE SUPREME COURT OF THE STATE OF DELAWARE

LONGPOINT INVESTMENTS TRUST and ALEXIS LARGE CAP EQUITY FUND LP,	:	
	:	No. 31, 2016
Petitioners-Below, Appellants,	:	
v.	:	On Appeal from the Court of Chancery of the State of Delaware
PRELIX THERAPEUTICS, INC., a Delaware corporation	:	
	:	C.A. No. 10342-CM
Respondent-Below, Appellee.	:	

APPELLEE'S ANSWERING BRIEF

/s/ TEAM G

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NATURE OF PROCEEDINGS

Petitioners brought this action on May 6, 2015. Under Delaware General Corporation Law ("DGCL") *8 Del. C.* § 262(e), the action was filed in the petitioners' names. But, the petitioners acknowledge that the registered holder changed between when the appraisal demand was submitted, when the shares voted on the transaction and when the merger was completed.

On January 13, 2016, the Chancery Court found petitioners' shares were not eligible for an appraisal remedy. To enumerate, the court first held in *Merion Capital LP vs. BMC Software, Inc.* and *In re Appraisal of Ancestry.Com* precluded Prelix's assertion that petitioners must demonstrate their shares voted in compliance with § 262(a). At the same time, the court found petitioners did not demonstrate standing to bring an appraisal action because, under § 262(a) and *In re Appraisal of Dell, Inc.*, they failed to "continuously hold[] such shares through the effective date of the merger." On January 13, 2016, Petitioners appealed to the Supreme Court of the State of Delaware from the order of Chancery Court. On January 15, 2016, the appeal was granted.

SUMMARY OF ARGUMENT

It is well-established under Delaware law that appraisal rights are created by statute, and entitlement to those rights requires strict compliance with statutory standards. *Alabama By-Products v. Cede & Co.*, 657 A.2d 254, 257 (Del. 1995). Under Section 262(a) of the Delaware General Corporation Law ("DGCL"), stockholders must meet four requirements in order to pursue appraisal of their shares. Appraisal rights are conferred only to a stockholder who (1) held the shares for which it seeks appraisal on the date of making the demands; (2) continuously held those shares through the effective date of the merger; (3) has otherwise complied with Section 262(d) concerning the form and timing of the appraisal demands; and (4) has not voted in favor of or consented to the merger with regard to those shares. *8 Del. C.* § 262(a).

In this appeal, Longpoint Investments Trust and Alexis Large Cap Equity Fund LP (together "Appellants") argue they are entitled to an appraisal remedy, under § 262(a), despite noncompliance with the second and fourth factors.

First, Appellants have not produced any evidence indicating how the shares were voted, either by themselves or by the prior shareholder. Instead, Appellants rely on earlier holdings that fail to enforce the voting requirement when shareholders acquire stock after the record date. This proposition of law, created out of dicta, is not only contrary to the statutory requirements, but also fails to address the inevitable dilemma that will arise when dissenters are not required to comply with the voting requirement in 262(a).

Secondly, Cede & Co. did not continuously hold Appellants' shares as the stockholder of record through the effective date of the merger, thus barring Appellants from seeking appraisal of their shares. Because Appellants failed to comply with the statutory requirements of § 262(a), this Court must invalidate their appraisal demands.

STATEMENT OF FACTS

On October 15, 2014, Radius Health Systems Corp. ("Radius") announced its proposed acquisition of Prelix Therapeutics, Inc. ("Prelix"). (Op. 2). Both the proposed acquisition and initial price were negatively received by shareholders. (Op. 2). As a result, the constituent corporations announced a marked up purchase price. (Op. 2). But the marketplace remained resentful. (Op. 2). While the date remains uncertain, petitioners Longpoint Investments Trust ("Longpoint") and Alexis Large Cap Equity Fund LP ("Alexis") acquired common stock in Prelix between the record date—to determine the shareholder who will vote the shares—December 4, 2014 and the increased price announcement on December 18, 2014. (Op. 3). Even after the price announcement, Cede & Co. ("Cede"), the record holder of the shares, acted on behalf of the petitioners and submitted written demands for appraisal of the newly acquired shares. (Op. 3).

Shortly after submitting their demand for appraisal, the Depository Trust Company ("DTC") moved the matching amount of shares from the fungible bulk of shares into the Fast Automated Securities Account ("FAST"), with certificates assigned with corresponding numbers for those shares. (Op. 3). On January 23, 2015, the new certificates were issued in the name of Cede and delivered to the petitioners' DTC participants, herein after the custodial banks. (Op. 3). However, both of the petitioners' DTC participants requested the certificates be reissued in the name of the different, depository nominees. (Op. 3). On February 5, 2015, the certificates representing the petitioners' shares were endorsed to include their DTC

participants' nominees. (Op. 3). As a result, the record holder who submitted the appraisal demand, Cede, was no longer the record holder of the shares when the merger was voted on and ultimately transpired. (Op. 4). The merger was approved by 53% of the Prelix shareholders on February 17, 2015, and completed on April 16, 2015. (Op. 3-4). Petitioners then brought this appraisal action on May 6, 2015. (Op. 4).

ARGUMENT

I. APPELLANTS FAILED TO ESTABLISH THAT THEIR SHARES WERE NOT VOTED IN FAVOR OF THE MERGER THEREBY BARRING THEIR APPRAISAL RIGHTS UNDER § 262(a).

A. Question Presented

Whether Appellants are entitled to an appraisal remedy under §262(a) when they failed to establish that their shares were not voted in favor of the merger.

B. Scope Of Review

To the extent the Court of Chancery's decision implicates the statutory construction of DGCL § 262, this Court's standard of review is *de novo*. *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214, 219 (Del. 2010). Petitioners' appeal is based on whether they fulfilled the requirements of § 262(a). Thus, the *de novo* standard applies.

C. Merits Of Argument

While the Chancery Court has bound itself to precedent, the Supreme Court must interpret Section 262 to better reflect current reality. Longpoint and Alexis argue they are entitled to appraisal rights despite no evidence indicating the shares were voted in favor of the merger as required by statute. *Longpoint Investments Trust and Alexis Large Cap Equity Fund LP v. Prelix Therapeutics, Inc.*, Del. CCP, C.A. No. 10342-CM (Del. Ch. Jan. 15, 2015).

1. Petitioners Are Not Entitled To Appraisal Because They Have Not Demonstrated Compliance With The Voting Requirement In §262(a).

To be eligible for an appraisal remedy, a record shareholder cannot vote in favor of the merger. *See 8 Del. C.* § 262(a). However,

when a beneficial shareholder acquires shares after the record date but before the merger vote, that beneficial owner may still claim and perfect appraisal rights. *In re Appraisal of Transkaryotic Therapies, Inc.*, 2007 WL 1378345, at *3 (Del. Ch. May 2, 2007). But this is contingent on the record holder voting a number of shares against the merger sufficient to cover the appraisal demand. *In re Appraisal of Transkaryotic Therapies, Inc.*, 2015 WL 1378345, at *3 (May 2, 2007).

In *Transkaryotic*, the court concluded that under "the statutory text [of Section 262] as well as the […] longstanding Delaware Supreme Court precedent […] only the record holder's actions determine perfection of the right to seek appraisal." This relieved claimants who purchased shares after a record date, but before a merger vote, of the burden to demonstrate their newly acquired shares were not voted in favor of the merger by the previous beneficial owner. As a result, appraisal arbitrage has become an increasing popular investment strategy when Delaware companies announce mergers. To enumerate, "'[a]ppraisal arbitrage' is […] an investment strategy whereby an investor acquires [shares] in a cash-out merger target with the specific intention of exercising the statutory stockholder appraisal right found in [Section 262]."

In *Ancestry.Com*, the court continued to facilitate appraisal arbitrage and deviate further from the text and intent of Section 262. In *Ancestry.Com*, a private equity firm purchased shares in the respondent after the record date, but filed the necessary documentation to assert its appraisal rights before the merger vote. *Ancestry.Com at *2*. Despite purchasing the shares from anonymous

sellers on the open market, no evidence was presented to verify how the shares were voted. *Id.* While acknowledging the growing concern of appraisal arbitrage, the court held a beneficial owner may still perfect an appraisal remedy for shares acquired after a record date, so long as a timely appraisal demand is submitted and the record owner has "sufficient shares […] not voted in favor of the merger to 'cover' its demand." *Id.* at *1.

But what is most perplexing is the court's reasoning when refusing to impose a share-tracing requirement. *Transkaryotic* at *2 (finding shares are held in "an undifferentiated manner, known as 'fungible bulk'" and votes cannot be attributed to a specific share); see also *BMC Software* at *5 (explaining *Transkaryotic* rejected imposing a share-tracing requirement on claimants because the difficulties of modern securities practices and tracing votes to shares); but see *In re Appraisal of Dell Inc.* at *24-25 (explaining if a share-tracing requirement were implemented, "courts [would be able to] apply […] statutory limitations more accurately"). While Delaware jurisprudence has relieved dissenters who acquire shares after a record date to demonstrate how shares were voted, the opposite has been observed in state and federal law. In particular, New York courts have held for more than 50 years that when shareholders acquire shares a record date, they cannot perfect an appraisal remedy. William Davitt, *New York Practice Series – Commercial Litigation in New York State Courts* § 89:38 (2015), *available at* WL. How do we want to cite this? Furthermore, under Section 11(a) or 12(a)(2) of the Securities Act of 1933, the claimant has the burden of proof. *In re Sterling*

Foster & Co., Inc., Securities Litigation, 222 F.Supp. 2d. 216 (E.D.N.Y., June 27, 2002). In addition to complying with other Section 11(a) and 12(a)(2) requirements, secondary market purchasers must trace their shares to demonstrate standing. *Id.*

Appellants argue while every share is voted in favor of a merger, those same shares remain eligible for appraisal rights when they are acquired after the record date. In addition, appellants have conceded they did not vote their shares specifically because the shares were acquired after the record date. Ultimately, appellants' voting requirement argument relies on this Court affirming the Chancery Court's holding in *Transkaryotic*, and subsequent case law observing this interpretation. *See generally BMC Software*, *Ancestry.Com*, and *Dell.* But, this Court has never excused non-compliance with the voting requirement of Section 262(a) when shares were voted in favor of a merger. Furthermore, as seen above, both state and federal law does not permit dissenting shareholders to disregard statutory preconditions simply because their shares were acquired after the record date.

2. Judicial Interpretation Does Not Address The Dilemma That Will Arise When Dissenters, Who Acquire Shares After A Record Date, Are Not Required To Comply With The Vote Requirement In § 262(a).

Despite Delaware's strong commitment to precedent, judicial interpretation of § 262 must change to avoid an appraisal conundrum, analogous to *Dole Food*. To emphasize, appraisal claims have nearly tripled since *Transkaryotic*. Charles R. Korsmo & Minor Myers, Appraisal Arbitrage and the Future of Public Company M&A, 92 WASH. U. L. REV. (forthcoming 2015) (manuscript at 16), available at

http://ssrn.com/abstract=2424935.The substantial increase can largely be attributed to institutional investors, primarily hedge funds, engaging in appraisal arbitrage. FRIED, FRANK, HARRIS, SHRIVER & JACOBSON LLP, New Activist Weapon-- The Rise of Delaware Appraisal Arbitrage: A Survey of Cases and Some Practical Implications 1 (June 18, 2014), http://www.friedfrank.com. While the intention of an appraisal remedy is to ensure dissenting shareholders receive the fair value of their shares, appraisal arbitrage has become a lucrative investment strategy. More than three-quarters of appraisal claims are brought by institutional investors, who have previously filed similar actions. Korsmo & Myers, *supra* note 1, at 18. As mentioned, this can be attributed to the court's holding in *Transkaryotic* which creates a unique opportunity for investors to acquire shares in a target company after the record date, but before the shareholder vote, and utilize the appraisal remedy as an investment strategy. Korsmo & Myers, supra note 1, at 2. This is further illustrated in Delaware case law. While only nine appraisal cases have been decided between 2010 and 2013, seven have granted awards greater than the original merger price. FRIED, FRANK, HARRIS, SHRIVER & JACOBSON LLP, supra note 3, at 3.

In re Appraisal of Dole Food Company, Inc., No. 9079-VCL (August 27, 2015) manifests the concerns articulated in cases after *Transkaryotic*, where beneficial owners who acquired stock after the record date were permitted to perfect appraisal demands. *See generally In Anecstry.Com; Merion Capital LP v. BMC Software, Inc.* There the proceedings revealed while only 50.9% of the shareholders approved the merger, the number of shares demanding an appraisal remedy exceeded

those not voted in favor on for the merger. § 14.10 APPRAISAL AND QUASI-APPRAISAL RIGHTS AND REMEDIES, Takeover Defense: Mergers & Acquisitions (Aspen Publishers).

Affirming the misinterpretation of Section 262(a) would ignore a clear, textual requirement to establish standing. Consequently, this would open the door for future cases, where claimants could exercise an appraisal remedy, despite their shares being voted in favor of the merger.

II. CEDE & CO. DID NOT CONTINUOUSLY HOLD APPELLANTS' SHARES AS THE STOCKHOLDER OF RECORD THROUGH THE EFFECTIVE DATE OF THE MERGER, THEREBY DISQUALIFYING APPELLANTS FROM THE APPRAISAL REMEDY UNDER § 262(a).

A. Question Presented

Whether Appellants satisfied the continuous holder requirement of § 262(a) when the depository nominee, in whose name Appellants' shares were registered at the time they submitted their demands for appraisal, failed to continuously hold those shares as the record stockholder through the effective date of the merger.

B. Scope Of Review

The standard of review for this issue is the same as above, *de novo*.

C. Merits Of Argument

An appraisal claimant's failure to strictly comply with the requirements of § 262(a) is not excusable, irrespective of the equities. *See Berger v. Pubco Corp.*, 976 A.2d 132, 144 (Del. 2009). As such, this Court must reject Appellants' appraisal demands if they did

not continuously hold their shares through the effective date of the merger. For the reasons below, they did not.

1. The Retitling Of Appellants' Shares From Cede & Co. To The Custodial Banks' Nominees After The Demands For Appraisal But Before The Effective Date Of The Merger Constituted A Change In Record Ownership For Purposes Of The Continuous Holder Requirement Under § 262(a).

Appellants lost their right to appraisal when certificates representing their Prelix shares were reissued to their custodial banks' nominees prior to the merger date. Under § 262(a), a "stockholder" is barred from seeking appraisal of his or her shares if, after making the demands, he or she does not continuously hold those shares through the effective date of the merger. *8 Del. C.* § 262(a). The statute expressly defines the term "stockholder" as "a holder of record of stock in a corporation." *Id.*; *Salt Dome Oil Corp. v. Schenck*, 41 A.2d 583, 589 (Del. 1945) (holding that "only the registered holder of stock is a 'stockholder' within the sense of the word" as it appears in the appraisal statute). Thus, it is the record holder, not the beneficial holder, that is subject to the statutory requirements for showing entitlement to appraisal rights under § 262(a) and (d). *In re Appraisal of Ancestry.com, Inc.*, 2015 WL 66825, at *8 (Del. Ch. Jan. 5, 2015) (holding that under a plain reading § 262(a), it remains the record holder who must comply with the statutory requirements for appraisal); *In re Appraisal of Transkaryotic Therapies, Inc.*, 2007 WL 1378345, at *4 (Del. Ch. May 2, 2007) ("[T]he actions of the beneficial holders are irrelevant in appraisal matters, [and] the inquiry ends" if the record holder does not fulfill the requirements of § 262(a)). Accordingly, the relevant

inquiry here is whether Cede, the depository nominee in whose name Appellants' shares were registered at the time their demands for appraisal were submitted, remained the record holder of those shares through the effective date of the merger.

Delaware courts have consistently held that transfers of title from a depository nominee to a custodial bank's nominee constitute a change in record ownership under § 262(a). *In re Appraisal of Dell Inc.*, 2015 WL 4313206, at *25 (Del. Ch. July 13, 2015) (holding that the petitioning funds did not satisfy the continuous holder requirement of § 262 when record title of their shares—held by Cede at the time they submitted their demands for appraisal—were transferred to the nominees of their brokers' custodial banks prior to the merger date); *see Nelson v. Frank E. Best Inc.*, 768 A.2d 473, 477 (Del. Ch. 2000) (Strine, V.C.) (noting that a transfer of title shortly after Cede's demands for appraisal invalidated that request because Cede would no longer be the "continuous holder of record" between the date of the demands and the effective date of the merger). Therefore, a change in record ownership as a result of custodial arrangements bars a beneficial stockholder from seeking appraisal of its shares. *Dell*, 2015 WL 4313206, at *10.

Here, Appellants did not continuously hold their shares through the effective date of the merger as required under § 262(a). It is immaterial that they remained the beneficial holders through the merger date. DTC's nominee, Cede, was the stockholder of record on January 13, 2015 when it made the demands for appraisal on behalf of Appellants. After those demands were submitted, DTC directed Prelix's

transfer agent to issue uniquely numbered share certificates representing Appellants' shares—still registered in Cede's name—to Appellants' respective custodial firms, J.P Morgan Chase and Bank of New York Mellon. Those banks subsequently reissued Appellants' share certificates in the names of its own nominees, Cudd & Co. and Mac & Co., on February 15, 2015, prior to Prelix's acquisition on April 16, 2015.

The foregoing events are indistinguishable from those described in *Dell*. There, the court held that the nominee-level transfers prior to the merger date constituted a change in record ownership, thus barring the claimant funds from seeking appraisal of their shares. Here too, Appellants' custodial banks transferred record title of Appellants' shares, initially held by Cede, to their own nominees prior to the effective date of the merger. Therefore, the reasoning in *Dell* applies equally to the case at bar. Because Cede was no longer the record holder of Appellants shares when Radius acquired Prelix, this Court must invalidate Appellants' demands for appraisal under § 262(a).

2. Appellants' Lack Of Knowledge Concerning The Changes In Record Ownership Does Not Excuse Non-Compliance With § 262(a).

It is immaterial that Appellants played no role in bringing about the nominee-level transfers of record ownership. The fact that shares may be surrendered by the broker or record owner without the consent or knowledge of the beneficial owner is irrelevant to the corporation. *Salt Dome Oil*, 41 A.2d 583, 585-89. With respect to share appraisal, a corporation deals exclusively with the stockholder of record, and

should not be forced to inquire into the "possible misunderstandings…between the non-registered and registered holder of shares." *Id.* at 589.

This Court has long held that when investors hold shares in street name or through one or more custodial firms, they assume the risk that the intermediaries will fail to properly exercise their appraisal rights. *See, e.g.*, *Enstar Corp. v. Senouf*, 535 A.2d 1351, 1353 n.2 (Del. 1987) (disqualifying shares from appraisal remedy where broker failed to deliver demand signed by or on behalf of stockholder of record); *Am. Hardware Corp. v. Savage Arms Co.*, 136 A.2d 690, 692 (Del. 1957) ("If an owner of stock chooses to register his shares in the name of a nominee, he takes the risks attendant upon such an arrangement...."). More recently, the Chancery Court rejected the argument that § 262(a)'s continuous holder requirement should apply differently when beneficial owners are unaware of nominee-level transfers that would otherwise invalidate their appraisal demands. *Dell*, 2015 WL 4313206, at *25. There, the court explained that because a stockholder's agreement with its custodial banks permits the retitling its shares, ownership changes driven by the depository system are considered voluntary transfers. *Id.*

That reasoning applies with equal force here. Yes, it is undisputed that Appellants played no role in the reissuance of their share certificates in the names of Cudd & Co. and Mac & Co. But this Court has made it clear that Appellants nonetheless assumed the risk of such a transfer via their agreement with J.P Morgan Chase and Bank of New York Mellon. *See Am. Hardware*, 136 A.2d at 692. As in *Dell*, the

nominee-level changes of record ownership prior to the merger date invalidated Appellants' demands for appraisal, regardless of whether or not they approved or even knew about those transfers. As such, this Court should reject any argument that § 262(a)'s continuous holder requirement might operate differently depending on whether Appellants knew about the changes in record ownership.

3. This Court Should Not Expand The Meaning Of "Record Holder" As It Appears In § 262(a) To Include Custodial Banks And Brokers On The DTC Participant List.

In anticipation of Appellants' argument for an alternative reading of "a holder of record" for purposes of § 262(a)'s continuous holder requirement, this Court should adhere to the same principles of strict statutory interpretation that have guided its decisions in the past. As discussed, a stockholder's entitlement to appraisal is contingent on complying with the precise standards of § 262(a). *Alabama By-Products*, 657 A.2d at 257. Although the DGCL does not expressly define what it means to be a "holder of record," this Court has made it clear that "[a corporation] may rightfully look to the corporate books as the sole evidence of membership." *Salt Dome Oil*, 41 A.2d at 589 (Del. 1945). Thus, the record holder for purposes of the DGCL is the person that appears on the stock ledger.

Appellants will likely argue that this Court should "look through" Cede to the custodial banks and brokers as record owners, such that nominee-level transfers would not constitute changes in record ownership for purposes of the continuous holder requirement. That approach was articulated in great length by Vice Chancellor Laster in his *Dell* decision. "Attempt[ing] only to present the reasons

why one trial judge believes that a different approach would be superior," the Vice Chancellor suggested that the Supreme Court treat DTC participants as "record holders" for the purposes of § 262(a). *Dell*, 2015 WL 4313206, at *25.

It would not be the first time that the Delaware Supreme Court has addressed this sort of proposal. Indeed, in *Crown EMAK Partners, LLC v. Kurz*, this Court refused to entertain the Vice Chancellor's suggestion that DTC participants be treated as holders of record, albeit for a different, but similar purpose. 992 A.2d 377, 397 (Del. 2010). Characterizing the Vice Chancellor's proposal as *obiter dictum*, this Court emphasized that the because the DGCL is carefully crafted and periodically reviewed by the General Assembly, any adjustments to that statutory scheme should be accomplished *by* the General Assembly through a coordinated amendment process. *Id.* at 398 (emphasis added). As such, any redefining of a "holder of record" as it appears in § 262(a) should be deferred to the legislature. *Id.*

Granted, § 262(a) might better address the intricacies of the DTC and preemptively resolve issues like the matter at hand here if, for instance, the statute expressly referred to the DTC participants and properly defined their role in the appraisal process. But that is a matter for the legislature to resolve, for only the General Assembly is properly equipped to address it. *See id.* Because the Delaware Supreme Court has long enforced a principle of strict statutory interpretation, regardless of the equities or public policy considerations involved, this Court must adhere to those same

principles and enforce § 262(a)'s record holder requirement as currently interpreted.

CONCLUSION

For the foregoing reasons, Appellants are not entitled to appraisal of their Prelix shares, and the decision of the Delaware Court of Chancery should be affirmed.