IN THE SUPREME COURT OF THE STATE OF DELAWARE

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

Appellants' Opening Brief

Team N
Attorneys for the Appellants
February 5, 2016

Table of Contents

TABLE OF CITATIONS

DELAWARE SUPREME COURT CASES

DELAWARE CHANCERY COURT CASES

STATUTES

LAW REVIEW ARTICLES

ELECTRONIC SOURCES

NATURE OF PROCEEDINGS

On May 6, 2015, appraisal petitioners Longpoint Investments Trust and Alexis Large Cap Equity Fund LP (hereafter "Appellants") filed an appraisal petition in the Court of Chancery seeking the appraisal of jointly owned shares (the "shares") of common stock in Prelix Therapeutics, Inc. (hereafter "Appellee"). Appellants owned the shares as of the date Appellee was acquired by Radius Health Systems Corp. On January 13, 2016, in case number 10342-CM, the Court of Chancery granted a motion for summary judgment in the matter, in favor of Appellee. The court found that Appellants were not required to prove how each share to be appraised was voted in the merger, but that Appellants did not have standing to pursue an appraisal remedy because the stockholder of record designation changed between the date of demand and the date of the merger. Therefore, the Court of Chancery found that Appellants did not continuously hold the shares through the effective date of the merger, and Appellants had lost their appraisal rights.

Appellants filed notice of appeal in the Supreme Court of Delaware on January 15, 2016, and respectfully request that this Court review and reverse the decision of the Court of Chancery to dismiss the appraisal petition on summary judgment and allow the appraisal action to proceed.

SUMMARY OF ARGUMENT

1. This Court should affirm the decision of the Court of Chancery, that Appellee was precluded from arguing that DGCL section 262(e) imposes an additional "share-tracing" standing requirement for a

beneficial owner that files an appraisal petition on its own behalf. Subsection (e) does not imply a requirement that a post-record date purchaser prove how each specific share was voted by its previous owner, and Appellants carried their burden of proving that they themselves did not participate in the merger vote. A share-tracing requirement of this kind is not only impossible, but would also effectively terminate the appraisal rights of an entire class of important minority shareholders.

2. The appraisal statute's continuous holder requirement should not preclude Appellants from pursuing an appraisal remedy following arbitrary transfers of record at the depository level. In light of the realities of the modern, centralized stock depository system, this Court should adopt an interpretation of shareholder of record that includes DTC participants and their nominees. DTC, through its own nominee Cede & Co., simply acts as a placeholder of record for stocks held centrally in bulk in order to promote more efficient transfers in the high frequency transfer market. This Court should embrace the federal definition of record holder, which includes DTC participants, in order to promote certainty in the transfer market and prevent a recurrent loss of minority appraisal rights.

STATEMENT OF FACTS

On October 15, 2014, Radius' proposed acquisition of Prelix was announced at $14.50 per share, slightly above the pre-announcement trading price on NASDAQ. Op. at 2. December 4, 2014 was the date for determining entitlement to vote on the merger (the "record date").

After the record date, but before the vote on the merger, Appellants together purchased 5.4% of the outstanding Prelix shares ("the shares"). Op. at 1, 3. In line with common trading practices, the shares were held by the Depository Trust Company[1] ("DTC") in the name of DTC's nominee Cede & Co ("Cede"), who became the holder of record upon purchase. Op. at 3, 5.

At this point, the shares were held at DTC in fungible bulk,[2] and Appellants' ownership interest was not assigned to any specific shares. Op. at 5. Since Appellants purchased their shares after the record date, "it is impossible to attribute to [Appellants'] shares any voting behavior" by the previous stockholders who owned the shares as of the record date. Op. at 3, n.4. On January 13, 2015, Appellants delivered written demands for the appraisal of their shares "in conformity with Section 262(d)(1)." Op. at 3. At that point, Cede still held legal title to the shares, and made demand for appraisal on

[1] DTC is a stock-clearing agency that administers ownership transfers on behalf of its participants. It was created in the 1970's in response to a new national policy of "share immobilization," which ended the physical transfer of stock certificates and consolidated stock ownership in a centralized depository system. *In re* Appraisal of Dell, Inc., No. 9322-VCL, 2015 Del. Ch. LEXIS 184, at *14 (Jul. 13, 2015). Presently, DTC holds approximately "three-quarters of [all] shares in publicly traded companies." *Id.* at *15. As such, a "publicly traded corporation cannot avoid going through DTC." *Id.* at *19. DTC is owned by participating custodial banks and brokers. *Id.* at *15 (citations omitted).

[2] "DTC holds the deposited securities in "fungible bulk," meaning that there are no specifically identifiable shares directly owned by DTC participants. Rather, each participant owns a pro rata interest in the aggregate number of shares of a particular issuer held at DTC." Investor Bulletin, Securities and Exchange Commission, DTC Chills and Freezes (May 2012), *available at* https://www.sec.gov/investor/alerts/dtcfreezes.pdf.

Appellants' behalf. Op. at 3. The shareholder vote on the merger was ultimately convened on February 17, 2015, and the merger was approved with just over 53% of the outstanding shares voting in its favor. Op. at 2-3. It is conceded that Appellants did not participate in the merger vote. Op. at 5.

Subsequent to Appellants' demand for appraisal, but before the merger on April 16, 2015, a transfer of record occurred at the depository level without Appellants' knowledge. Op. at 3-4. This process was initiated on January 23, 2015, when DTC used its electronic Fast Automated Securities Transfer program[3] ("FAST") to direct the Prelix transfer agent to issue uniquely numbered paper certificates representing Appellants' shares, initially titled in the name of Cede, so that Appellants' specific shares could be appraised. Op. at 3. Next, the newly issued paper certificates were delivered to participant custodial banks J.P. Morgan Chase ("J.P. Morgan") and Bank of New York Mellon ("BONY") for safekeeping. Op. at 3.

After the paper certificates were delivered to the custodians, another back-office administrative procedure kicked in. Op. at 3. For various "understandable business reasons,"[4] and unbeknownst to Appellants, J.P. Morgan and BONY then instructed Cede to endorse the

[3] DTC inventories ownership interests and negotiates with securities transfer agents using its FAST program. This program is essentially an electronic ledger system that administers ownership transfers between DTC and transfer agents without the need for the physical transportation of paper stock certificates. S.E.C. Rel. No. 60196 at 1-2 (2009).

[4] Including "insurance requirements, recordkeeping for internal audit, mitigating risk of theft, etc." *Dell*, 2015 Del. Ch. LEXIS 184, at *7.

stock certificates so that the shares could be retitled in the names of the banks' own nominees, Cudd & Co. and Mac & Co., respectively. Op. at 3, 5. Although the beneficial owners and the custodians of the shares remained the same throughout this process, the record holder had now changed. Op. at 5. Thus, the Court of Chancery found that a single stockholder of record did not continuously hold the shares through the effective date of the merger. Op. at 5-6. These types of transfers are common business practice, and the Opinion does not reflect whether the firms using these back-office procedures have established policies to avoid transfers that will result in the loss of appraisal rights for their beneficiaries. Op. at 3 n.5.

ARGUMENT

I. THE COURT OF CHANCERY CORRECTLY BARRED APPELLEE FROM ARGUING THAT DGCL SECTION 262(e) CREATES AN ADDITIONAL "SHARE-TRACING" REQUIREMENT FOR STANDING UNDER SECTION 262(a)

A. Question Presented

Does section 262(e) imply an additional share-tracing requirement for a beneficial owner that buy shares after the record date and then files an appraisal petition in its own name, when (1) the plain language of the statute provides no such requirement and the General Assembly's intent in incorporating section 262(e) was clearly to enable minority shareholders with tools to make seeking appraisal a more efficient endeavor, and (2) tracing how previously owned shares were voted is currently impossible when stocks are held of record through the central depository system?

B. Scope of Review

A motion for summary judgment is granted when there is no genuine issue of material fact and the moving party is entitled to a judgment as a matter of law. *In re* Krafft-Murphy Co., Inc., 82 A.3d 696, 702 (Del. 2013). A trial court's decision to grant summary judgment is reviewed *de novo*. *Id.*

C. Merits of Argument

Delaware's statutory appraisal remedy was created to "compensate dissenting shareholders for their loss of the ability to block mergers" at common law. *In re* Appraisal of Ancestry.com, Inc., No. 8173-VCG, 2015 Del. Ch. LEXIS 2, at *8 (January 5, 2015). Shareholders of a corporation have a statutory right to dissent from "fundamental or structural changes in the life of the corporation." Kanda & Levmore, *The Appraisal Remedy and the Goals of Corporate Law*, 32 UCLA L. REV. 429, 429 (1985). Today, a dissenting shareholder's right to an appraisal of the fair market value of their shares "remains firmly embedded in American corporate law," and is available in every jurisdiction in some form. *Id.* at 431. The appraisal remedy protects shareholders and provides a check on majority opportunism and negligence, offering an avenue for meaningful compensation when such conduct persists. Korsmo & Myers, *Appraisal Arbitrage and the Future of Public Company M&A*, 92 WASH. U. L. REV. 1551, 1555 (2015).

A dissenting shareholder has an absolute right to an appraisal. Felder v. Anderson, Clayton & Co., 159 A.2d 278, 286 (Del. Ch. 1960); Kaye v. Pantone, Inc., 395 A.2d 369, 375 (Del. Ch. 1978). To perfect the statutory appraisal remedy under the Delaware General Corporation

Law ("DGCL"), an appraisal petitioner must show that the stockholder of the shares, defined as the "holder of record:"(1) held the shares on the date it made demand for appraisal to the corporation; (2) continuously held the shares from the date of demand through the effective date of the merger; (3) has complied with the form and timeliness requirements of subsection (d); and (4) has not voted in favor of the merger. DEL. CODE ANN. tit 8, § 262 (West 2013); Merion Capital LP v. BMC Software, Inc., No. 8900-VCG, 2015 Del. Ch. LEXIS 3, at *4 (January 5, 2015).

Strict compliance with these requirements is essential. Konfirst v. Willow CSN Inc., No. 1737-N, 2006 Del. Ch. LEXIS 211, at *11 (December 14, 2006). However, DGCL's appraisal remedy was clearly "enacted for the benefit of minority shareholders." Salt Dome Oil Corp. v. Schenck, 41 A.2d 583, 587 (Del. 1945). Additionally, the requirements of the appraisal statute must be "liberally construed" to protect dissenting shareholders, "within the boundaries of orderly corporate procedures and the purpose of the requirement." Raab v. Villager Industries, Inc., 355 A.2d 888, 891 (Del. 1976); *See also*, Schneyer v. Shenandoah Oil Corp., 316 A.2d 570, 573 (Del. Ch. 1974).

In the current case, the Opinion clearly indicates that Appellants delivered written demand for appraisal of their shares in conformity with section 262(d)(1), on January 13, 2015. Op. at 3. Cede made demand on Appellants' behalf. *Id.* The relevant inquiry in this appeal, then, is whether section 262(e) creates an additional standing requirement for an appraisal petitioner that files in its own name, and whether Appellants were required to show how each previously owned

share was voted. The Court of Chancery correctly precluded Appellee from raising this argument.

1. Cede & Co. as Holder of Record Bears the Burden of Perfecting the Voting Prerequisite of Section 262(a)

To pursue DGCL's appraisal remedy, a record holder must make written demand for appraisal before the shareholder vote on the merger, and must not vote in favor of the merger nor consent to it in writing. § 262(a). It is the record holder, rather than the beneficial owner, that must "comply with the statutory requirements in order for [a] petition to be viable." *In re* Appraisal of Ancestry.com, Inc., 2015 Del. Ch. LEXIS 2, at *23-24. Subsection (e) enables a beneficial owner to file an appraisal petition in its own name, but opens with a preface: subsection (e) is only applicable to "any *stockholder* who has complied with subsections (a) and (d) of this section hereof and who is otherwise entitled to appraisal rights." § 262(e)(emphasis added). Thus, it is the stockholder, defined as the record holder, that must make demand for appraisal, and that must perfect § 262(a)'s standing requirements. *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *17; *BMC Software*, 2015 Del. Ch. LEXIS 3, at *11; *In re* Appraisal of Transkaryotic Therapies, Inc., No. 1554-CC, 2007 Del. Ch. LEXIS 57, at *9 (May 2, 2007).

The record holder bears the burden of showing "that it did not vote in favor of the merger with respect to the shares for which appraisal is sought." *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *22. The appraisal statute does not require that a post-record date purchaser that dissents prove how each previously owned share was voted; it merely requires that a self-filing beneficiary show the beneficiary

itself did not vote in favor of the merger, which is always true of a post-record date purchaser. *BMC Software*, 2015 Del. Ch. LEXIS 3, at *17; *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *15.

Beneficially owned shares are often held in "street name" at DTC, meaning that the shares are held in fungible bulk with Cede as the holder of record. *See generally*, *In re* Appraisal of Dell, Inc., No. 9322-VCL, 2015 Del. Ch. LEXIS 184 (July 13, 2015). This presents a unique dilemma when a dissenter has purchased after the record date. *Id.* In this scenario, it is impossible to decipher how each previously owned share was voted. *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *24. Cede votes an aggregate block of shares for and against the merger based on the preferences of those entitled to an interest in a cumulative share pool, and a stockholder identity is not associated with specific shares. *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *16 (citing *Transkaryotic Therapies*, 2007 Del. Ch. LEXIS 57, at *6). For this reason, Delaware precedent provides that Cede, as the record holder, must only verify that it voted against the merger or abstained with enough votes to cover the number of shares for the appraisal demand. *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *21; *BMC Software*, 2015 Del. Ch. LEXIS 3, at *22.

In this case, it is conceded that Appellants did not vote in favor of the merger, nor were they entitled to vote at all as purchasers after the record date. Op. at 5. Furthermore, the court correctly rejected the argument that Appellants must show how each previously owned share was voted. Op. at 1. Whether Cede voted enough shares against the merger to cover Appellants' 5.4% ownership interest

is not discernable from the facts provided in the Opinion. Op. at 1. The Opinion simply states the overall percentage of votes for and against the merger, and does not state the amount of shares that were held by Cede, nor the amount of shares voted for and against the merger by Cede on behalf of its participants. Op. at 2-3. This information is necessary to determine if Cede voted enough shares to cover Appellants' demand, but that burden remains with Cede as the record holder, and Appellants did not have the extreme burden of proving how each previously owned share was voted. Op. at 1.

2. The Appraisal Statute is Unambiguous and the Plain Statutory Language Does Not Imply Any Additional Share-Tracing Requirement

For issues of statutory interpretation, Delaware courts must identify the intent of the legislature and defer to that purpose. *In re* Krafft-Murphy Co., Inc., 82 A.3d at 702. If the statute is clear and unambiguous, the plain meaning controls. *Id.* For a statute to be deemed ambiguous, it must be "reasonably susceptible" of multiple interpretations, or a literal reading must lead to "an unreasonable or absurd result not contemplated by the legislature." *Id.* If ambiguity is found, "courts should consider the statute as a whole, rather than in parts, and read each section in light of all others to produce a harmonious whole." *Id.* Additionally, when a provision is included in one section but omitted from another, "it is reasonable to assume that the [l]egislature was aware of the omission and intended it." Giurichich v. Emtrol Corp., 449 A.2d 232, 238 (Del. 1982).

The primary purpose of DGCL's appraisal statute is "to protect the contractual rights of the shareholders who object to a merger and

to fully compensate shareholders for any loss they may suffer as a result of a merger." *Transkaryotic Therapies*, 2007 Del. Ch. LEXIS 57, at *9. The standing requirement of subsection (a) focuses on the stockholder, rather than the shares. *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *24. In response to a 2007 decision holding in part that, as non-record holders, a beneficial owner was devoid of any right to pursue the appraisal remedy on its own behalf, the General Assembly revised section 262(e) to expand the rights of a beneficial owner that seeks appraisal by allowing it to file an appraisal petition in its own name. *BMC Software*, 2015 Del. Ch. LEXIS 3, at *18; § 262(e). Subsection (e) provides that, notwithstanding the prerequisites of section 262(a), a "beneficial owner of shares ... held ... by a nominee on behalf of such person may, in such person's own name, file a petition...." § 262(e).

Additionally, the amendment served an important informational function and enabled potential dissenters to obtain a statement of "the aggregate number of shares not voted in favor of the merger" and the holders of those shares. *BMC Software*, 2015 Del. Ch. LEXIS 3, at *14. This information allows potential dissenters to better understand the task of pursing appraisal litigation and to "share the costs of the appraisal action." *Id.* While section 262(e) enables beneficial owners with tools to make the appraisal remedy a more efficient endeavor, the burden remains with the record holder to perfect section 262(a)'s standing requirements by showing that it did not vote in favor of the merger with respect to the shares to be appraised. *Ancestry.com*, 2015 Del. Ch. LEXIS 2 at *22.

In two similar cases, decided by Vice Chancellor Glasscock on the same day in 2015, the Court of Chancery clarified that the language of the appraisal statute is unambiguous, and that section 262(e) neither explicitly, nor implicitly, adds any additional standing requirement to those enumerated in section 262(a). *BMC Software*, 2015 Del. Ch. LEXIS 3, at *20, *23; *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *21. In both *BMC Software* and *Ancestry.com*, corporations seeking summary judgment against an appraisal petition argued that the section 262(e) amendment created ambiguity because it could lead to a theoretical glitch: post-record date purchasers could potentially demand appraisal for more shares than were voted against the merger, or could theoretically dissent with a majority of shares when a merger has been approved by a majority of shareholders. *BMC Software*, 2015 Del. Ch. LEXIS 3, at *12. Additionally, the concern was raised in *BMC Software* that, without requiring an appraisal petitioner to show how its shares were voted by their previous owners, the informational component of section 262(e) would be "entirely superfluous," and would not show the actual number of shares qualifying for appraisal. *Id.* at *15 n.31 (citations omitted).

Glasscock was firm in his position that the statute was clear and unambiguous, and that the "theoretical concern" of over appraisal did "not render the statute absurd or inoperable." *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *23. At most, it "indicates that the General Assembly may not have picked a fail-safe method to achieve its goals." *BMC Software*, 2015 Del. Ch. LEXIS 3, at *25. Glasscock rejected the argument that the General Assembly intended the amendment to impose

"an additional standing requirement." *Ancestry.com*, 2015 Del. Ch. 2 at *27. With regard to the increased availability of information intended to facilitate a more informed decision on dissention, the *BMC Software* court held that "it is antithetical to that intention to interpret the language of subsection (e) to impose, on the statute as a whole, an additional hurdle for appraisal petitioners." *BMC Software*, 2015 Del. Ch. LEXIS 3, at *24. The reference to "shares not voted in favor of the merger" in section 262(e) does not operate to change the standing requirements of section 262(a); the breadth of that reference is "limited to defining the scope of the petitioner's informational right, in which that language is found." *Id.* at *25.

While it remains theoretically possible for post-record date purchasers to demand appraisal for more shares than were voted against the merger, this does not make the appraisal statute capable of multiple interpretations, nor does a literal reading lead to unreasonable results except for under extreme hypothetical circumstances. The purpose of the DGCL's appraisal statute is to protect the minority, and the amendment to section 262(e) was aimed at expanding that protection, not limiting it by creating a burdensome share-tracing requirement for self-filing beneficial owners. In line with the reasoning in *BMC Software* and *Ancestry.com*, the appraisal statute is clear and unambiguous, and it remains a firmly embedded central tenant of the statute that only a record holder may perfect section 262(a)'s prerequisites for demanding appraisal.

When considering the appraisal remedy as a whole, implying an additional burdensome standing requirement does not yield a harmonious

result, but instead undermines the very purpose of the remedy: to protect and empower the minority. Such a requirement would produce uncertainty in the transfer market, and would greatly overcomplicate the process of filing a successful appraisal petition. Because Cede votes a pro-rata percentage of the share pool for and against the merger, tracing how previously owned shares were voted is currently impossible. Op. at 3 n.4. Therefore, imposing an additional share-tracing requirement would create an absurd burden for dissenters that purchase after the record date. Ultimately, over-appraisal will remain a looming theoretical possibility, embedded within the very structure of the modern central stock depository system, but to deprive the rights of an entire class of minority shareholders in light of a far-fetched hypothetical projects a net negative.

a. The Addition of an Extra Standing Requirement is a Concern Best Suited for Resolution Through the Legislature

The Delaware judiciary plays a vital role in interpreting the statutory language adopted by the General Assembly. It is this Court's role to interpret that language and if unclear, "explain what [it] ascertain[s] to be the legislative intent without rewriting the statute to fit a particular policy position." Taylor v. Diamond State Port Corp., 14 A.3d 536, 542 (Del. 2011). Furthermore, any imperfection of the legislature's intent embodied in the appraisal statute "does not give a judge license to rewrite clear statutory language." *Ancestry.com*, 2015 Del. Ch. LEXIS 2, at *26. Thus, to add an additional share-tracing requirement "would be to exercise a legislative, not a judicial, function." *Id.* at *28.

The potential issue of over-appraisal is better suited for resolution through the legislature, and reading in an additional standing requirement for a self-filing beneficial owner would effectively encompass a rewrite of the General Assembly's clear language and intent. Subsection (e) of the appraisal statute is designed to empower beneficial owners that seek appraisal, not to create additional burdensome standing requirements.

b. A Share-Tracing Requirement of This Kind is Against Public Policy and Would Eliminate the Appraisal Rights of an Important Class of Dissenting Shareholders

Recently, there has been a rise in institutional investment after the record date in order to seek appraisal for profit. *See generally*, Korsmo & Myers, 92 WASH. U. L. REV 1551 (2015). These investors, known as "appraisal arbitragers," serve an important function in the corporate realm. They aid the minority as a whole "by deterring abusive mergers and by causing shares traded post-announcement to be bid up to the expected value of an appraisal claim." *Id.* at 1556. Appraisal arbitragers pursue appraisal litigation based on merit; i.e., these last minute investors target corporations that plan to merge at a price perceived to be lower than fair market value. See generally, *id.* In the long run, this protects minority shareholders from corporate opportunism, and also aids the economy at large; "[i]f appraisal arbitrage reduces the risk of expropriation faced by minority shareholders, it will increase the value of minority stakes and thus reduce the costs of capital for companies and increase the allocative efficiency of capital markets as a whole." *Id.* at 1556.

To adopt an additional standing requirement is not only against the General Assembly's clear intent, but will produce negative results for dissenting shareholders and needlessly encumber the transfer market as a whole. The addition of this new share-tracing requirement will restrict liquidity in the transfer market because buying after the record date will become less attractive to potential investors. As a result, shareholders that wish to sell shares after the record date for whatever reason will be presented with a smaller market for the shares. This will have an overall chilling effect on the market for shares while a merger is pending. Furthermore, this impossible burden would effectively terminate the appraisal rights of dissenting shareholders that purchase after the record date. Therefore, this additional standing requirement will end the practice of appraisal arbitrage, which plays a critical role in protecting the minority against corporate opportunism and encourages mergers at a price that reflects a more sincere fair market value.

II. THE CUSTODIANS HELD THE SHARES CONTINUOUSLY AND THIS COURT SHOULD INCLUDE DTC PATICIPANTS AS RECORD HOLDERS TO AVOID A RECCURENT LOSS OF MINORITY APPRAISAL RIGHTS

A. Question Presented

Does the continuous record holder requirement in section 262(a) preclude a dissenting shareholder from pursuing an appraisal remedy following standard, back-office transfers at the depository level that occur without the knowledge of the beneficial owner, when those transfers simply reflect the realities of the modern stock depository system in which ownership is administered centrally, and participating banks and brokers own an interest in a bulk share pool?

B. Scope of Review

A motion for summary judgment is granted when there is no genuine issue of material fact and the movant is entitled to a judgment as a matter of law. *In re* Krafft-Murphy Co., Inc., 82 A.3d at 702. A trial court's decision to grant summary judgment is reviewed *de novo*. *Id.*

C. Merits of the Argument

In addition to DGCL's voting prerequisite, the appraisal statute requires that a single holder of record keep legal title to the shares from the date of demand, through the effective date of the merger. § 262(a). However, "holder of record" is not defined in the statute, and Delaware's understanding of the term stems from case law decided long before the era of central depositories and electronic transfers.

This Court first distinguished a beneficial owner from a stockholder in *Salt Dome Oil Corp. v. Schenck*. 41 A.2d at 585. In *Salt Dome*, the Court defined "stockholder" to mean "the holder of legal title to shares of stock." *Id.* Although a record holder often plays the role of trustee on behalf of another beneficiary, "legally he is the stockholder and may be treated as the stockholder by the corporation." *Id.* This clear definition promotes certainty, and ensures that corporations are not burdened with drawing distinctions between registered and beneficial owners. Abraham & Co. v. Olivetti Underwood Corp., 204 A.2d 740, 741 (Del. Ch. 1964)(citing *Salt Dome*, 41 A.2d at 589). *Salt Dome's* progeny has affirmed that it is the record holder that must meet DGCL's prerequisites for perfection of the appraisal remedy. Enstar Corp. v. Senouf, 535 A.2d 1351, 1352

(Del. 1987); *Abraham*, 204 A.2d at 741; *In re* Engle v. Magnavox Co., No. 4896, 1976 Del. Ch. LEXIS 165, at *3 (April 21, 1976).

The judiciary's traditional understanding of DGCL's record holder requirement does not account for the complexities and sheer mass of modern securities markets, and Delaware courts have "largely ignored" the implementation of the federal policy of share immobilization.[5] *In re* Appraisal of Dell, Inc., 2015 Del. Ch. LEXIS 184 at *54. To date, Delaware courts have not distinguished between transfers at the stock depository level, controlled by the federally mandated relationship between DTC and its participants, from transfers between traditional brokers. *Id.* As such, little consideration has been given to DGCL's continuous record holder requirement as applied to depository level transfers and protocols. *Id.* The absence of any resolution on the matter has led to inevitable uncertainties in the transfer market, particularly with regard to a dissenting shareholder's ability to perfect DGCL's appraisal remedy.

The uncertainty created by Delaware's outdated application of the continuous record holder requirement was highlighted in *Dell*, where the Court of Chancery contemplated a novel issue of law. The court considered whether the continuous holder requirement barred several

[5] Prior to 1970, stock transfers were facilitated using paper certificates. An owner would endorse a stock certificate and the transfer would be recorded on a corporation's books. *In re Appraisal of Dell, Inc.*, 2015 Del. Ch. LEXIS 184 at *11. As the frequency and volume of trading in the markets increased, brokers became overwhelmed with paperwork, creating burdensome inefficiencies on the markets. Katsuro Kanzaki, *Immobilization of Stock Certificates: Position of the Beneficial Stockholder*, 3 J. INT'L L. 115, 115 (2014). The SEC's solution was a national policy of "share immobilization." *Dell*, 2015 Del. Ch. LEXIS 184 at *14.

investment funds from pursing appraisal of their shares following administrative transfers of record at the depository level. *Dell*, 2015 Del. Ch. LEXIS 184, at *24. The technical change occurred following demand for appraisal, when DTC participant banks J.P. Morgan and BONY requested that Cede endorse the stock certificates so they could be retitled in the names of the banks' own nominees. *Id.* at *6-8. The banks required this change to protect against the liabilities associated with holding a hugely valuable stock certificate in a name other than the banks' own nominees. *Id.* at *7. The investment funds remained the beneficial owners and the custodial banks remained the same, but a transfer at the depository level from Cede to the custodial banks' nominees was a technical change of record that broke the chain of continuous ownership. *Id.* at *7-8. For this reason, a single record holder had not perfected the continuous holder requirement. *Id.* at *5-9. The investment funds did not request these transfers, but they were considered to be voluntary on the funds' behalf, and the funds were forced to assume the risk that this type of transfer could result in the loss of their absolute appraisal right. *Id.* at *32; *see also*, American Hardware Corp. v. Savage Arms Corp., 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.").

The same awkward dilemma played out in the case at bar, and Appellants lost the ability to pursue an appraisal remedy for the reasons articulated in *Dell*. Op. at 5. Appellants did not choose to retitle the shares in the names of the custodians' nominees, yet they

were forced to assume the risk that these administrative transfers would result in a loss of their absolute appraisal right. Op. at 4. The custodians had not changed, and the transfers reflected the banks' own policies designed to protect themselves "for the reasons described in *Dell*." Op. at 3. Appellants had no knowledge of the transfers and "played no role in bringing about those changes." Op. at. 4. Consistent with the intent of DGCL's appraisal remedy, designed to protect shareholders and empower the minority, a unknowing beneficiary should not be forced to assume the risk that an administrative depository level transfer will forfeit the appraisal remedy. Moreover, this Court should include DTC participants as record holders in order to promote certainty in the transfer market, and protect future dissenting shareholders from this recurrent dilemma.

1. This Court Should Consider Federal Law and Include DTC Participants as Record Holders to Promote Certainty in the Transfer Market

In the *Dell* opinion, Vice Chancellor Laster keenly noted that since the SEC created the central depository system, Delaware courts have "not distinguish[ed] the voluntary relationship between a client and its custodial bank or broker (the "broker level" of ownership) from the federally mandated relationship between the custodial bank or broker and DTC (the "depository level" of ownership.") *Dell*, 2015 Del. Ch. LEXIS 184, at *8. Laster acknowledged that a colloquy on this distinction should be left to this Court, and for this reason used a traditional application of the record holder requirement in line with principles of *stare decisis*. *Id.* at *9, *78. However, in the opinion, he raised an alarm and signified that it is time for this Court to

reevaluate the continuous holder requirement as it relates to ownership transfers at the depository level. *Id.* at *78.

Laster called for a new approach, consistent with federal law, that sees through the transparent ownership designation held by Cede, and recognizes DTC's participants as record holders. *Id.* at *16-19. Under this approach, appraisal petitioners presented with a *Dell* scenario would "retain their appraisal rights, because ownership by the relevant DTC participants never changed." *Id.* at *8-9. Looking to federal law to solve this hiccup makes sense, because transfers from DTC to its participants are a function of the federal policy of share immobilization. Upon implementing this policy, the SEC clarified that "for purposes of federal law, the custodial banks and brokers remain the record holders." *Id.* at *17. Under Federal law, the term "record holder" means "any broker, dealer, voting trustee, bank, association or other entity that exercises fiduciary powers which holds securities of record in nominee name or otherwise or as a participant in a clearing agency...." 17 C.F.R. § 240.14c-1(i)(2016). When the depository system was created, DTC was added at the bottom of the ownership chain, and the custodial banks and brokers continued to appear on the participant list as record holders. *Dell*, 2015 Del. Ch. LEXIS 184, at *33.

Federal law "looks through DTC" and understands Cede for what it really is: a necessary placeholder of record. *Id.* at *17. "For example, when determining whether an issuer has 500 or more record holders ... DTC does not count as a single holder of record. Each DTC participant counts as a holder of record." *Id.* (citing Michael

Molitor, *Will More Sunlight Fade the Pink Sheets?*, 39 IND. L. REV. 309, 314-6 (2006)). In this example, federal law understands that although Cede is the single holder of bulk stock, DTC's participants are an "integral part of the federally mandated ownership scheme," and DTC's constituent custodial banks and brokers continue to appear on the stock ledger while the shares are held centrally at DTC. *Id.* at *33. Therefore, DTC participants are record holders under the federal scheme. 17 C.F.R. § 240.14c-1(i). "Cede is not a record holder." *Dell*, 2015 Del. Ch. LEXIS 184 at, *33.

Federal regulations also enable corporations to easily discover the identities of the banks and brokers holding positions through DTC by the issuance of a "Cede breakdown," which identifies the number of shares of a given issuer held by each DTC participant on a given date. *Dell*, 2015 Del. Ch. LEXIS 184, at *18. This information can be obtained in a matter of minutes through DTC's website. *Id.* When matters are submitted for a stockholder vote, an issuer must obtain a Cede breakdown and send that information to all DTC participants, and "[a]n issuer cannot look only at its own record and treat Cede as a single, monolithic owner." *Id.* at *19. Delaware has similar requirements, and the Cede breakdown is part of the stock ledger for purposes of DGCL section 220(b), which enables shareholders to obtain a list of DTC participants under appropriate circumstances. Crown EMAK Partners, LLC v. Kurz, 992 A.2d 377, 395 (Del. 2010)(citing Kurz v. Holbrook, 989 A.2d 140, 167 (Del. Ch. 2010)). This is evidence that the Delaware judiciary is at least aware of and willing to consider DTC participants and their vital role in the ownership scheme.

In this case, under the federal approach, DGCL's continuous record holder requirement did not bar Appellants from perfecting their appraisal rights because the federal standard includes DTC participants as record holders. Appellants did not lose their appraisal rights when the banks retitled the shares in the names of their own nominees; the custodians remained the same from the date that demand was made through the effective date of the merger. Op. at 3. To hold otherwise would create a recurrent loophole that will see a loss of dissenting shareholders' absolute appraisal right, often without knowledge. When DTC issued the unique certificates following demand, no real change in ownership occurred because the custodians did not change. Op. at 3. The certificates were housed at the custodial banks when they were retitled in the names of the banks' nominees, showing that it was the custodians who were the true holders following demand. *Id.* For this reason, the technical change of record did not break the continuous chain of ownership. The transfers were an arbitrary function of the banks' own policies, designed to protect themselves. Furthermore, it is not equitable to force Appellants to forfeit the appraisal remedy in light of a procedural transfer that occurred without their knowledge. Additionally, the Opinion does not reflect whether steps have been taken by the custodians to solve this problem to protect their beneficiaries. Op. at 3 n.5.

2. This Court has the Authority to Define DTC Participants as Record Holders

The DGCL is broadly enabling and "[t]he design of [the appraisal statute] requires the avoidance of complexities in proceedings under

it." Lichtman v. Recognition Equip., Inc., 295 A.2d 771, 772 (Del. Ch. 1972); *see also*, Kaye v. Pantone, Inc., 395 A.2d 369, 375 (Del. Ch. 1978). The continuous record holder requirement promotes certainty in the transfer market, yet Delaware's current application of the requirement leads to uncertainties, and in a *Dell* scenario it strips the absolute appraisal right of unknowing dissenters. Recognizing DTC participants as record holders would not push this Court into the realm of the legislature, nor would it involve any complex reinterpretation of the continuous holder requirement. The determination of who is a record holder "is a quintessential issue of statutory interpretation" - an interpretation that the courts have not addressed since 1945 in *Salt Dome*. *In re* Appraisal of *Dell*, Inc., 2015 Del. Ch. LEXIS 184, at *36.

A parallel issue to the *Dell* scenario was contemplated in *Kurz*, which considered voting authority under the central depository system. *Kurz*, 992 A.2d 377. DTC (as legal title holder) has the authority to cast votes, and DTC transfers that authority to its participants. *Id.* at 396. In *Kurz*, DTC participants attempted to subvert the clearing agency and transfer voting authority on their own. *Id.* at 382-3. In the lower court's opinion in Kurz, authored by Vice Chancellor Laster, the Vice Chancellor argued that because the DTC participant list is recognized as part of the stock ledger (via the Cede breakdown) for purposes of DGCL section 220, it should also be recognized for purposes of section 219, which grants voting authority. *Id.* at 397. On appeal, this Court did not find it necessary to address the issue directly, but in dictum indicated that such a determination required a

legislative cure because it would alter the structure of the voting process and change the meaning of section 219. *Id.* at 379.

Kurz is distinguishable from the case at bar. Here, recognizing DTC participants as record holders would not grant power to anyone who did not already have it. This change would merely reflect the realities of the contemporary securities market, and recognize that the *Dell* scenario deprives beneficial shareholders of their absolute appraisal rights. The recognition of DTC participants as record holders simply preserves the appraisal right for dissenting shareholders that are already entitled to that right, in line with the legislature's intent to protect the minority. Each day, billions of shares of stock are traded over millions of individual trades.[6] And while centralization at DTC is essential to keep the market moving forward, it should not diminish the rights of market participants who cannot avoid transacting through the depository system.

CONCLUSION

In conclusion, Appellants were not required to prove how each share was voted by its previous owner, and the custodians continuously held the shares from the date of demand through the date of the merger. For these reasons, Appellants respectfully request that this Court overturn the summary judgment so that Appellants may pursue an appraisal remedy.

[6] Dan Strumph, *Wall Street Adjusts to the New Trading Normal*, WALL STREET JOURNAL (June 6, 2016), http://www.wsj.com/articles/wall-street-adjusts-to-the-new-trading-normal-1401910990.