

IN THE SUPREME COURT OF THE STATE OF DELAWARE

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

Appellant's Opening Brief

Team P
Attorneys for Appellants

February 5, 2016

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NATURE OF PROCEEDINGS

Appellants, petitioners below, filed petitions seeking appraisal on November 24, 2015. Appellees, respondents below, moved for summary judgment. Chancellor Mosley granted summary judgment for Appellees and dismissed the petition for appraisal on January 13, 2016.

Petitioners filed a timely notice of appeal on January 15, 2016.

Petitioners request that this Court reverse the Court of Chancery's order granting summary judgment for respondents and enforce petitioners' appraisal rights. Petitioners further request this Court clarify current law and announce that the stockholder of record includes those entities listed on the Cede breakdown. This will distinguish the voluntary relationship between a client and its custodial bank from the federally mandated relationship between the custodial bank and Depository Trade Company, thereby allowing shareholders to retain their appraisal rights and not lose them because of changes driven by the depository system.

SUMMARY OF ARGUMENT

1. Appraisal rights should not be forfeited based on a hypertechnical interpretation of the stockholder of record requirement or the application of out of date case law. The decision below limits the definition of stockholder of record to only names appearing on a corporation's stock ledger. This interpretation resulted, and will continue to result, in the unconscionable loss of appraisal rights.

This Court should reverse the decision below because the Cede breakdown is a record of a corporation that should be recognized under Delaware law. This Court should interpret stockholder of record consistent with federal law and recognize that the entities listed on the Cede breakdown are stockholders of record. Any other interpretation would contravene the underlying purpose of Delaware's appraisal statute.

2. Moreover, ownership changes driven by the depository system must be treated as involuntary. The appraisal rights were lost only because of the involuntary transfer caused by the federally mandated depository system. Because participation in the depository system is a *de facto* requirement and the transfer at issue is a direct consequence of this requirement, Longpoint and Alexis did not assume the risk that they may lose their appraisal rights based on a transfer they did not participate in. Therefore, this Court should treat the Cede breakdown as evidence of continuous share ownership, and prohibit corporations from denying appraisal rights to their investors based on a technicality.

STATEMENT OF FACTS

This appeal stems from Delaware law failing to recognize custodial banks as record holders after the federally mandated policy of share immobilization was enacted. The inability of shareholders to retain their appraisal rights is based on impermissible hypertechnicalities that neither the legislature nor the Delaware Supreme Court has yet rectified.

A. The Plaintiffs Ownership Of Prelix Shares.

Plaintiffs, Longpoint Investments Trusts ("Longpoint") and Alexis Large Cap Equity Fund LP ("Alexis"), together owned approximately 5.4 percent of the 49 million outstanding shares of common stock of Respondent Prelix Therapeutics, Inc. ("Prelix") as of April 16, 2015, the date on which Prelix was acquired by Radius Health Systems Corp. ("Radius") through a merger with an acquisition subsidiary of Radius. (Op at 1.)

Section 262 of the Delaware General Corporation Law (the "DGCL") permits "[a]ny stockholder of a corporation" who complies with the statute's requirements to litigate a proceeding that will result in a judicial determination of the "fair value of the shares." *In re Appraisal of Dell Inc.*, 2015 WL 4313206, at *2 (Del. Ch.) (quoting 8 *Del. C.* §§ 262(a), (h)). The word stockholder means a "holder of record of stock in a corporation." 8 *Del. C.* §§ 262(a). The statute also requires that a stockholder who wishes to pursue appraisal must "continuously hold [] such shares though the effective date of the merger." *Id.*

The shares owned by Longpoint and Alexis were initially held in the name of Cede & Co. ("Cede"), DTC's nominee, but were transferred before the date of the merger to nominees of J.P. Morgan Chase and Bank of New York Mellon, the custodial banks for the shares in question. (Op. at 1.) The vast majority of publicly traded shares in the United States are not registered on a corporation's books in the name of beneficial owners, but rather in the name of Cede, the nominee of The Depository Trust Company ("DTC"). *Dell*, 2015 WL 4313206, at *1. The creation of DTC was a federal response to the paperwork crisis on Wall Street during the late 1960s and early 1970s, in which increased trading volume overwhelmed brokerage firms trying to document stock trades using paper certificates. *Id.*

Over 800 custodial banks and brokers are participating members of DTC. *Id.* DTC holds shares on their behalf in fungible bulk, meaning that none of the shares are issued in the names of DTC's participants. *Id.* Instead, all of the shares are issued in the name of Cede. *Id.* DTC uses an electronic book entry system called the Fast Automated Securities Transfer account (the "FAST Account") to track the number of shares that each participant holds. *Id.* With share immobilization, legal title remains with Cede when a transfer is made and no new paper certificates are required. *Id.* This solved the paperwork crisis but complicated other aspects of the legal system. *Id.*

B. The Plaintiffs Seek Appraisal, And DTC Issues Paper Certificates.

On January 13, 2015, Longpoint and Alexis delivered written demands for appraisal of their shares, in conformity with Section 262(d)(1). (Op. at 3.) The demands were made on their behalf by Cede,

DTC's nominee, in whose name the shares were registered at the time. *Id.* When Longpoint and Alexis caused Cede to demand appraisal, DTC removed the shares covered by the demand from the fungible bulk tracked in the FAST Account. *Id.* DTC did this by requesting Prelix's transfer agent to issue uniquely numbered paper certificates representing those shares. *Id.* The issuance of these certificates, in the name of Cede, occurred on January 23, 2015, and the new certificates were delivered to J.P. Morgan Chase and Bank of New York Mellon, DTC participants holding the Prelix shares on behalf of Longpoint and Alexis, respectively. *Id.*

C. DTC Delivers The Certificates To The Custodians, Who Re-Title Them, Before The Merger Closes.

For reasonable business reasons (insurance requirements, recordkeeping for internal audit, mitigating risk of theft, etc.) some banks and brokers only hold stock certificates that are issued in the names of their own nominees. *Dell*, 2015 WL 4313206, at *3. J.P. Morgan Chase and Bank of New York Mellon requested that Cede endorse Longpoint and Alexis' shares in the name of the banks own nominees, Cudd & Co. and Mac & Co., respectively. (Op. at 3.) On February 5, 2015, Prelix's transfer agent issued new certificates in the names of those new nominees. *Id.* Thus, the maker of the demands for appraisal on which this case is premised—Cede—was no longer the registered holder of stock of Plaintiffs' shares by the time the merger closed on April 16, 2015. *Id.* at 3-4.

D. Plaintiffs Seek Appraisal.

Plaintiffs filed their petition on May 6, 2015. *Id.* at 4. As permitted by section 262(e) of the DGCL, they filed in their own names and candidly disclosed that their shares were not registered in the name of Cede, whose name the shares were registered at the time petitioners submitted their written demands for appraisal. *Id.* Although the Court of Chancery has expressed a preference for a different interpretation of the term "stockholder of record"—one that would include the custodial banks and brokers—the Court accepted and applied the determination of law articulated in *Dell*, and concluded that petitioners were not entitled to appraisal of their shares because Cede did not continuously hold the shares through the effective date of the merger, as required by Section 262(a). *Id.* at 5-6.

It is undisputed, however, that Plaintiffs were unaware of the changes in record ownership that occurred on February 5, 2015, and that they played no role in bringing about those changes. *Id.* From the date of making the demand through the effective date of the merger, Plaintiffs remained the beneficial owners. See *id.* at 1-5. The custodians remained the custodians. See *id.* But now, due to technicalities, there were new nominees on Prelix's stock ledger. See *id.*

ARGUMENT

I. THIS COURT SHOULD REVERSE THE DECISION OF THE COURT OF CHANCERY BECAUSE A CUSTODIAL BANK SHOULD BE CONSIDERED A STOCKHOLDER OF RECORD.

A. Question Presented.

Whether the stockholder of record requirement in section 262 of Delaware General Corporation Law includes custodial banks that hold shares of stock on behalf of beneficial owners when those banks are listed on a corporation's Cede breakdown.

B. Standard Of Review.

"Questions of law involving statutory interpretation are reviewable *de novo*." *Freeman v. X-Ray Associates, P.A.*, 3A.3d 224, 227 (Del. 2010) (citing *Dambro v. Meyer*, 974 A.2d 121, 129 (Del. 2009)). No deference should be given to the trial court's determinations, both as to the facts and the law. See *Williams v. Geier*, 671 A.2d 1368, 1375 (Del. 1996).

C. Merits Of Argument.

1. The Term Stockholder Of Record Should Encompass Custodial Banks.

This Court should reverse the decision of the Court of Chancery because the term stockholder of record should include custodial banks and not be limited to simply the nominee of DTC. Section 262 of the DGCL affords a stockholder the opportunity to have his shares appraised and awarded the fair market value provided that certain conditions have been fulfilled. See 8 Del. C. §262 (2016). The condition under review here requires the stockholder seeking appraisal

to continuously hold the shares through the effective date of the merger. *Id.* § 262(a). Under the DGCL, a stockholder is defined as “a holder of record of stock in a corporation.” *Id.* However, the DGCL does not define what record is being referenced.

In *Dell*, the petitioners were the beneficial owners of common stock. 2015 WL 4313206, at *1. As the beneficial owners, the petitioners did not possess legal title to their shares. *Id.* The petitioners’ shares were held through a custodial bank. *Id.* Because of the federal policy of share immobilization, the custodial banks did not possess legal title either. *See id.* The shares were registered in the name of Cede & Co. (“Cede”), DTC’s nominee, which is the name that appeared on the corporation’s stock ledger. *Id.* at *1, *6.

The petitioners sought appraisal of their shares after a merger was announced. *See id.* at *7. When the appraisal proceeding was initiated, DTC obtained a paper stock certificate from the corporation corresponding to the number of shares owned by the petitioners. *Id.* Then, DTC attempted to deliver the certificate to the petitioners’ custodial banks, but the banks had a policy that prevented them from holding paper stocks in the name of DTC’s nominee. *See id.* Therefore, the banks requested that the paper stocks be re-titled in the name of their nominees. *See id.* Subsequently, the transfer of title was performed. *See id.*

Thereafter, the corporation moved for summary judgment, contending that the transfer of title violated the continuous stockholder of record requirement. *See id.* at *8. The Court of

Chancery agreed, stating that “[u]nder existing precedent, Cede was the stockholder of record.” *Id.* at *9. Therefore, “[w]hen the shares were re-titled, the [petitioners] lost their appraisal rights.” *Id.*

Although the present action is analogous to *Dell*, that decision was rendered by the Court of Chancery. Thus, that decision does not govern the outcome of this case. See *Zeeb v. Atlas Powder Co.*, 87 A.2d 123, 126 (Del. 1952) (“The decisions of the trial courts of this state are not binding precedents upon [the Supreme Court] under any principle of *stare decisis*.”). This case presents an issue of first impression for this Court. This Court should reverse the decision of the Court of Chancery because (1) a custodial bank is listed on the Cede breakdown, which is a record of a corporation, (2) the purpose of section 262 is eviscerated by a contrary holding, (3) a custodial bank is a record holder under federal law, and (4) the interest of the public would be better served.

a. The Cede Breakdown Is A Record Of A Corporation.

The record of a corporation should not be limited to its stock ledger. “[I]t is undisputed that when a statute is ambiguous and its meaning may not be clearly ascertained, the Court must rely upon its methods of statutory interpretation and construction to arrive at what the legislature [intended].” *Coastal Barge Corp. v. Coastal Zone Indus. Control Bd.*, 492 A.2d 1242, 1246 (Del. 1985). Because the term “record” is ambiguous, this Court should “consider [the entire statute] as a whole and read each section in light of all others to produce a harmonious [result].” *PHL Variable Inc. Co. v. Price Dawe*

2006 Ins. Trust, 28 A.3d 1059, 1070 (Del. 2011). Section 220 of the DGCL provides that any stockholder has the right to inspect, copy, and extract “[t]he corporation’s stock ledger, a list of its stockholders, and its other books and records.” See 8 Del. C. § 220 (b)(1) (2016) (emphasis added).

It is well settled under Delaware law that a beneficial holder is entitled to the Cede breakdown under section 220. See, e.g., *Wynnefield Partners Small Cap Value L.P. v. Niagara Corp.*, 2006 WL 2521434, at *2 (Del Ch.). The Court of Chancery first considered this issue in *Giovanini v. Horizon Corp.*, 1979 WL 178568 (Del. Ch.). In *Giovanini*, a stockholder sought to acquire the Cede breakdown under section 220 in attempt to solicit proxy votes from other shareholders. *Id.* at *1. Although the plain language of the statute provides for the inspection of the list of stockholders, the court concluded that this list included the Cede breakdown. *Id.* at *2.

In reaching its holding, this Court recognized the dilemma that share immobilization has created. See *id.* at *1 (stating that share immobilization “prevents the stock ledger from revealing to one examining it just which brokerage firms own shares and the number of shares owned by each.”). Because of share immobilization, the corporation’s stock ledger merely reflects the name Cede, which “is thrice removed from the true beneficial owner.” *Id.* Consequently, when a corporation must determine the proper amount of informational material that should be forwarded to brokerage firms that are holding stock through Cede, a corporation must obtain a Cede breakdown. See *id.* at *2.

In the present action, this Court should interpret section 262 in light of section 220 to produce a harmonious result. See *PHL Variable Inc. Co.*, 28 A.3d at 1070. Section 220 is entitled "Inspection of Books and Records." See 8 Del. C. § 220 (2016). Under Delaware law, a stockholder is entitled to inspect the Cede Breakdown pursuant to that section. See *Giovanini*, 1979 WL 178568, at *2. Therefore, the Cede breakdown is a record of the corporation. Accordingly, this Court should not limit the term record in section 262 to only a stock ledger because the term is, in fact, more expansive.

b. To Effectuate The Purpose Of Section 262, This Court Should Reject A Narrow Interpretation.

Another method of statutory interpretation is to determine the legislative intent. When interpreting a statute, "a final determination should not be made until the court has attempted to understand the purposes sought to be achieved by the legislative branch and the words chosen interpreted sympathetically to the achievement of that end." *In re Best Lock Corp. Shareholder Litigation*, 845 A.2d 1057, 1087 (Del. Ch. 2001). The legislative purpose of section 262 "is to provide equitable relief for shareholders dissenting from a merger on grounds of inadequacy of the offering price." *Paskill Corp. v. Alcoma Corp.*, 747 A.2d 549, 552 (Del. 2000).

This Court should not limit the definition of stockholder of record to only the name appearing on the stock ledger because that interpretation would not further the purpose of section 262, especially in light of share immobilization. The stockholder of record

requirement was enacted before share immobilization became necessary in response to increased trading of stocks. See *Dell*, 2015 WL 4313206, at *17-18. Accordingly, the Delaware General Assembly was unable to consider the implications of share immobilization. Even if the General Assembly intended a narrow definition of record, applying that interpretation now would contravene the underlying purpose of appraisal.

The stockholder of record requirement was codified in 1967. See *Dell*, 2015 WL 4313206, at *17. This “made explicit the formerly implicit requirement of record ownership.” Ernest L. Folk, Rodman Ward & Edward P. Welch, *FOLK ON THE DELAWARE GENERAL CORPORATION LAW: A COMMENTARY & ANALYSIS* 144 (2d ed. 1988). In *Salt Dome Oil Corp. v. Schenck*, a decision rendered before codification, this Court limited the appraisal remedy to registered owners because the corporation should be able to rely exclusively on its records of stock ownership when estimating the number of shareholders who oppose the proposed merger. 41 A.2d 583, 589 (Del. 1945). This Court stated that the beneficial holder could have transferred his shares to himself to become a full legal title holder, and any disadvantage suffered is the result of a failure to act. *Id.* However, this Court announced two exceptions to that rule: (1) express reservation of rights and (2) “unavoidable intendment.” *Id.*

Salt Dome does not control the outcome of this case because that decision was rendered before share immobilization. Because of share immobilization, custodial banks are prompted to hold shares through

DTC. Nevertheless, the rationale underlying the record holder requirement continues to prevail because a corporation can rely exclusively on the Cede breakdown to estimate dissenting shareholders. Currently, the record that a corporation relies on is the Cede breakdown, whereas when the record holder requirement was codified, it was the stock ledger. The name that was once reflected on a stock ledger now appears on the Cede breakdown. This is an unavoidable result of share immobilization. A custodial bank cannot choose to bypass DTC. If every custodial bank attempted to bypass DTC, the stock market would crash. Therefore, *Salt Dome* and its progeny are not applicable, and this Court should recognize the changes that have occurred in the trading industry and reconcile those changes with the purpose of the appraisal statute.

Moreover, the purpose of the appraisal statute is "to provide equitable relief for shareholders dissenting from a merger on grounds of inadequacy of the offering price." See *Paskill Corp.*, 747 A.2d at 552. The hypertechnical interpretation requiring a stockholder to be listed on a corporation's stock ledger, rather than a Cede breakdown, results in the unconscionable loss of appraisal rights in circumstances similar to the present action.

c. Under Federal Law, The Cede Breakdown Is A Corporate Record Of Significant Importance.

A corporation could not function without the Cede breakdown, whereas the stock ledger has limited utility in the aftermath of share immobilization. During the 1960s, trading stocks required the physical

delivery of certificates. See David Brooks, Comment, *Depository Trust Company & the Omnibus Proxy: Shareholder Voting in the Era of Share Immobilization*, 52 S. TEX. L. REV. 205, 209 (2014). This system was unsustainable, and by 1968, due to a surge of trading, the New York Stock Exchange ("NYSE") was forced to close every Wednesday in order to keep up with paperwork. See *id.* "In response, Congress amended the Securities Exchange Act of 1934 to adopt a policy immobilizing share certificates." *Id.* Share immobilization is a creature of federal law. See 15 U.S.C § 78q-1 (2015).

Federal law delineates specific obligations that a corporation must comply with when submitting matters to a vote. See 17 C.F.R. § 240.14a-13 (2015). Specifically, a corporation's "list of security holders indicates that some of its securities are registered in the name of [Cede], the corporation is required to inquiry into the participants" of Cede, otherwise known as the Cede breakdown. *Id.* at n. 1. Although Cede is the only entity that has the legal right to vote under Delaware Law, the beneficial owners retain the right to instruct Cede how to vote. See *Crown EMAK Partners, LLC v. Kurz*, 992 A.2d 377, 382 (Del. 2010)

With respect to this federal statute, a record holder is explicitly defined as "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) (2015). In contrast, DTC is not a record holder, it is a clearing agency. See 15

U.S.C § 78c (23) (A) (2015) (defining a clearing agency as "a securities depository [acting] as a custodian of securities").

In addition to the previously mentioned methods of statutory construction, this Court should consider federal law. Federal law clearly provides that a custodial bank is a record holder, and DTC is clearly an agency. Further, federal law recognizes that share immobilization has restricted the stock ledger's usefulness and, consequently, instructs corporations to refer to the Cede breakdown during matters of significant importance, such as voting. Additionally, under the Securities Exchange Act, records are defined as "accounts, correspondence, memorandums, tapes, discs, papers, books, and other documents or transcribed information of any type. 15 U.S.C. § 78c(37) (2015). Undoubtedly, the Cede breakdown is a record that this Court should recognize.

d. As A Matter Of Public Policy, A Corporation Should Not Be Permitted To Use Share Immobilization As Both A Sword And Shield.

The way in which the appraisal rights at issue have been lost is unconscionable and should not be permitted as a matter of public policy. Interpreting the stockholder of record requirement narrowly to include only the nominee listed on a corporation's stock ledger would allow corporations to use share immobilization as both a sword and a shield. Share immobilization shields corporations from the ever-increasing amount of public trading. See *Matter of Enstar Corp.*, 1986 WL 8062, at *2 (Del. Ch.). "[I]t relieves the corporation of the paperwork which would be required if every owner of a share of stock

had his shares listed in his own name on the books of the corporation." *Id.*

Conversely, if a stockholder of record is limited to names appearing on a stock ledger, it would allow corporations to use share immobilization as a sword. Share immobilization is a *de facto* requirement. The stock market would not function without it. *See Dell*, 2015 WL 4313206, at *6 ("In 2014, the NYSE reported average daily volume of approximately 1 billion shares and approximately 4 million separate trades."). Limiting the stockholder of record to the name listed on a corporation's stock ledger results in an unconscionable loss of appraisal rights based on a hypertechnical interpretation. The loss of appraisal rights is even more egregious considering the fact that the corporation did not suffer any prejudice as a result of the retitling. Moreover, a broad definition of stockholder of record would not cause any prejudice to corporations in subsequent appraisal proceedings because the Cede breakdown can be easily obtained at a nominal cost. *See Giovanini*, 1979 WL 178568, at *1 (stating that obtaining a Cede breakdown can be accomplished in a matter of minutes). Based on these reasons, this Court should reverse the decision below.

II. EVEN IF THIS COURT CHOOSES NOT TO ALTER THE INTERPRETATION OF STOCKHOLDER OF RECORD, OWNERSHIP CHANGES DRIVEN BY THE DEPOSITORY SYSTEM MUST BE TREATED AS INVOLUNTARY.

A. Question Presented.

Whether Delaware law should treat ownership changes driven by the depository system as involuntary transfers when federally mandated share immobilization forces changes in title.

B. Standard Of Review.

A trial court's application of the law is subject to *de novo* review. *Cede & Co. v. Technicolor, Inc.*, 884 A.2d 26, 36 (Del. 2005). No deference should be given to the trial court's determinations, both the facts and the law. *LaPoint v. AmerisourceBergen Corp.*, 970 A.2d 185, 191 (Del. 2009).

C. Merits Of Argument.

- 1. But For The Federal Mandate, Custodial Banks And Brokers Would Have Appeared On The Stock Ledger Maintained By The Transfer Agent Through Their Own Nominees, And No Change In Ownership Would Have Occurred Before The Merger Was Finalized.**

Had Congress and the Securities Exchange Commission ("SEC") not mandated the existence of a depository level of ownership, this case would not be in front of the court today because the custodial banks would have appeared on the stock ledger maintained by the corporations transfer agent through their own nominees. Until 1975, securities transactions were conducted using physical certificates; once a buyer and seller agreed on terms, the seller would endorse a physical

certificate and the corporation would be notified of the change in ownership. S. Michael Sirkin, *Who Owns Stock in a Delaware Corporation? The Answer Can Be a Surprise*, 19 No. 8 The M & A Law. NL 1. However, current policy requires that an accumulation of shares be held in central depositories in order to facilitate trade and lessen the burden of these trades on brokers and corporations. *Dell*, 2015 WL 4313206, at *5.

Before the advent of share immobilization, this Court concluded that only a registered stockholder was entitled to exercise legal rights and be treated as a stockholder by the corporation. See *Salt Dome*, 41 A.2d at 585-89. This Court noted in *Salt Dome* that, as a matter of policy, corporations are entitled to know who the objecting stockholders are so that the amount of money to be paid to them may be provided. *Id.* at 589. However, but for the addition of the depository level of ownership, corporations would know who the objecting stockholders are by looking directly at their stock ledger. Today, corporations are only able to obtain this information through a Cede breakdown, but Delaware law has yet to recognized this change in the ownership chain that followed the federal mandate of share immobilization.

Before share immobilization, custodial banks appeared on the corporation's ledger as registered stockholders. See *Dell*, 2015 WL 4313206, at *11. But for the mandate of share immobilization, the shares owned by Longpoint and Alexis would have appeared on Prelix's stock ledger through their custodial banks' chosen nominees: Cudd & Co. and Max & Co. It is only because of the existence of DTC that

Longpoint and Alexis had their shares unknowingly transferred. If Longpoint's and Alexis' firms had not been DTC participants, their shares would never have been held in the name of Cede. Meaning, there would not have been a retitling of their shares once they began the appraisal process and the new certificates were delivered to J.P. Morgan Chase and Bank of New York Mellon. Longpoint and Alexis should not lose their appraisal rights when their shares are involuntarily retitled due to a federally mandated program, especially when it is uncontested that those rights would have been maintained prior to the implementation of share immobilization.

2. Participation In The Depository System Is A De Facto Requirement Established By Congress And The SEC.

Without widespread participation in the depository system, securities markets would break down. Therefore, changes driven by the depository system are not truly voluntary. Under the current policy of share immobilization, stockholders have no real choice in whether they hold their shares through DTC, and therefore, they are not assuming any risk as participants of DTC.

Before the federal policy of share immobilization took effect, the decision to hold shares through an intermediary was a matter of choice. In *Salt Dome*, this Court found that a corporation was only required to rely on its own records to determine who was and was not a stockholder, and if a stockholder chose to complicate its relationship with the corporation by holding its shares through an intermediary, they accepted the risk and the corporation was not required to look through the registered holders of the shares. 41 A.2d at 589. Now,

with the creation of DTC, a required depository level of ownership has been added to the ownership chain. See *Dell*, 2015 WL 4313206, at *16.

Respectfully, this Court incorrectly found in *Enstar Corp. v. Senouf* that, “[t]he decision [to use DTC] is a matter which is strictly between the broker and its clients.” 535 A.2d. 1351, 1354 (Del. 1987). Broker-client relationships affect the entire securities market. See *Dell*, 2015 WL 4313206, at *21. Theoretically, it is true that an investor could choose to hold his shares in his name, however, only a few could do so before the system would break down entirely. *Id.* Without widespread participation in the depository system, securities markets would drown in paperwork. *Id.* It would be inevitable that the system would break down because the market has grown to an average daily trading volume of approximately 1 billion shares and 4 million separate trades, significantly more than that which was processed in the 1970s. *Id.* at *6. The depository system established by Congress and the SEC is the reason that the market is able to process the amount of trades that it does, and its “almost-universal participation is a *de facto* requirement.” *Id.* at *21.

In *Salt Dome*, this Court stated that stockholders assume the risk that intermediaries will act contrary to their best interests because the relationship between the customer and the broker was a voluntary one. 41 A.2d at 589. However, the relationship between the broker and DTC is not voluntary. The creation of the depository system was a necessary response to the paperwork crisis. *Dell*, 2015 WL 4313206, at *21. The necessity of the depository system ensures that the shareholder, realistically, has no choice but to use DTC and therefore

cannot choose to accept the risk that DTC will not act in his best interest.

Longpoint and Alexis chose to hold their shares through their custodial banks, but had no real choice in whether their shares were held through DTC, because the use of this intermediary is a *de facto* requirement. See *Id.* at *21. Therefore, when the title was transferred from Cede to Cudd & Co. and Mac & Co., this transfer was a result of a federally mandated policy and not a result of Longpoint and Alexis voluntary use of intermediaries.

If this Court holds that in order to maintain appraisal rights, an investor must opt-out of the depository system, the securities market will likely collapse and the ambitions of the share immobilization policy created by the SEC and Congress will be thwarted. Further, the use of the depository system benefits corporations as well. *Dell*, 2015 WL 4313206, at *22. It is this system that has allowed public trading of securities to take place and has given issuers the ability to raise capital through public markets while avoiding costly paperwork burdens. *Id.*

Because participation in the depository system is a *de facto* requirement established by Congress and the SEC, changes driven by the depository system are involuntary transfers. This Court must not allow corporations to deprive shareholders their appraisal rights because of involuntary transfers.

3. Because Changes Driven By the Depository System Are Involuntary, This Court Should Treat The Cede Breakdown As Evidence Of Continuous Share Ownership.

Even if this Court chooses not to alter the interpretation of stockholder of record, it should allow a Cede breakdown to be used to establish continuous ownership, despite the involuntary transfers driven by the depository system. A Cede breakdown identifies the custodial banks and brokers that hold shares in fungible bulk on the date that the breakdown is requested, and the amount of shares held. *Dell*, 2015 WL 4313206, at *6. This Court should require Cede breakdowns be used once a shareholder gives notice that they plan to seek appraisal, so that the federally mandated policy of share immobilization does not destroy the stockholder's appraisal rights.

Delaware law, which requires a record holder to assert the rights of a shareholder, "allows the corporation or an inspector of elections to determine from readily available records whether the consent was valid." *Kurz v. Holbrook*, 989 A.2d. 140, 164 (Del Ch. 2010), *aff'd in part, rev'd on other grounds sub nom. Crown EMAK P'rs, LLC v. Kurz*, 992 A.2d 377 (Del. 2010). This policy is appropriately applied to the appraisal process because similarly to voting, a shareholder is exercising a right granted to them by statute. See *id.* To promote efficiency and accuracy in the appraisal process, a corporation should look to readily available records in order to determine whether a request for appraisal is valid, and these records include Cede breakdowns. Additionally, there is no additional burden on the corporation to look to Cede breakdowns in considering the validity of

a request for appraisal. Corporations may express concerns about the uncertainty and practical difficulties they may face in identifying its stockholders if asked to look beyond the stock ledger, however these concerns are misguided.

Federal regulations require DTC to furnish one to "each issuer whose securities are held in the name of the clearing agency of its nominee." 17 C.F.R. § 240.17Ad-8(b) (2015). Cede breakdowns are a necessary part in preparing for a meeting of stockholders or distribution of voting cards and solicitation materials. *Kruz*, 989 A.2d. at 174. The use of Cede breakdowns to determine which investors request appraisal of their shares will not have negative effects on the company's ability to do business efficiently and predictably. See *id.*

The right to appraisal was designed to provide equitable relief for shareholders dissenting from a merger. *Cede & Co. v. Technicolor, Inc.*, 542 A.2d 1182, 1186 (Del. 1988). Under the current regime, shareholders are stripped of their statutory right to fair market value of their shares for fear of causing an inconvenience to corporations by requiring them to check the Cede breakdown to see which investor is actually seeking appraisal of their shares. See *Enstar Corp.*, 535 A.2d. at 1354. However, because corporations are forced by federal law to frequently request Cede breakdowns, and these breakdowns can be provided in a matter of minutes, the inconvenience placed on corporations. See *Dell*, 2015 WL 4313205, at *6.

In addition to protecting shareholders' appraisal rights, using a Cede breakdown also promotes order and certainty and provides a sure

source of information for corporations. *Id.* at *16. 75 percent of all publicly traded shares are held through Cede. *Dell*, 2015 WL 4313206, at *6. Thus, a corporation's stock ledger shows jumbo stock certificates held in the name of Cede. *Id.* All of Cede's holdings are held for brokers, banks, or other entities that participate in the federal policy of share immobilization, negating the effectiveness of stock ledgers. *Id.* When submitting a matter for a stockholder vote, a corporation must look to the Cede breakdown and cannot treat Cede as one single holder on record. *Id.* This policy has proven to be the most effective way for corporations to obtain a realistic picture of their stockholders, but has yet been expanded to apply to appraisal litigation.

Following the implementation of share immobilization, the use of a Cede breakdown to show continuous ownership is the best way to restore the appraisal process to what it was before, and to meet the goals outlined in *Salt Dome*. This will increase reliability and continuity for both corporations and their shareholders, and will ensure that shareholders are not stripped of their appraisal rights based on a technicality. Even if this court chooses not to alter the interpretation of stockholder of record, it should allow Cede breakdowns to be used to show continuous ownership, despite the involuntary transfers driven by the depository system.

Conclusion

For the foregoing reasons, this Court should vacate the Court of Chancery's order granting respondents motion for summary judgment.

Respectfully submitted,

 /s/ Team P

Team P, Counsel for

Appellants, Plaintiffs Below

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