

Delaware Supreme Court Affirms the Use of Stockholders Agreements to Waive Appraisal Rights

A Practical Guidance® Article by
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Introduction

This First Analysis article discusses the recent opinion by the Delaware Supreme Court in *Manti Holdings, LLC v. Authentix Acquisition Co.*, 2021 Del. LEXIS 286 (Del. Sept. 13, 2021), affirming the use of stockholders agreements by and among Delaware corporations and its stockholders to waive stockholders' rights of appraisal under Section 262 of the Delaware General Corporation Law. 8 Del. C. § 262. The *Manti Holdings* decision further solidifies Delaware's strong policy preference of freedom of contract and private ordering, and confirms that Delaware corporations can have its stockholders waive appraisal rights. Note, however, that not every appraisal waiver may be valid. It also raises the question of what other seemingly "mandatory" stockholder rights may be waived in documents that are not a charter or bylaw.

For practical guidance on stockholder appraisal rights under Delaware law, see [Appraisal Rights \(DE Corporation\)](#).

Initial Guidance

The case arises from a 2017 merger transaction with Authentix Acquisition Co., Inc. (the Company). In 2008, the Company became the parent company of Authentix, Inc., with Carlyle becoming the majority stockholder. Before the 2008 transaction, the Petitioners held a majority of the outstanding shares of Authentix, Inc. In connection with the 2008 transaction, the Petitioners received rollover equity in the Company, became minority stockholders, and were required to enter into a stockholders agreement (the Stockholders Agreement). Importantly, the Stockholders Agreement contained the following provision:

In the event that . . . a Company Sale is approved by the Board and . . . the Carlyle Majority, each Other Holder shall consent to and raise no objections against such transaction . . . , and . . . shall refrain from the exercise of appraisal rights with respect to such transaction.

The Petitioners, the Company and Carlyle were all represented by counsel in negotiating the Stockholders Agreement. Carlyle received preferred stock in a subsequent transaction and the Stockholders Agreement was amended to accommodate.

In 2017, the Company's board recommended a merger with a third party, and Carlyle approved the merger. The merger consideration was paid out through a waterfall

provision which allocated nearly all of the proceeds to the holders of preferred stock. The Petitioners, holding common stock that stood to receive little to no consideration, timely demanded appraisal. The Court of Chancery, however, denied Petitioners' demand and held they had waived their appraisal rights.

A majority of the Supreme Court affirmed the Court of Chancery's holding on appeal. Disagreeing with Petitioners' contractual arguments, the Court held that Petitioners had waived their Section 262 rights in the Stockholders Agreement. Notably, the Court found that the waiver applied post-merger when the Stockholders Agreement self-terminated because, reading the agreement holistically, it made little sense that stockholders were to refrain from exercising appraisal rights not ripe to exercise pre-termination. The Court also held that the post-merger Company could enforce the Stockholders Agreement because it is an entity capable of forming a contract, the change of control did not alter the Company's status as a party to the Stockholders Agreement, and if anyone is to be an intended beneficiary, it would be the surviving company.

The Court then determined that the appraisal waiver was permissible as a matter of Delaware law and policy. Echoing its 2020 decision in *Salzberg v. Sciabacucchi*, 227 A.3d 102 (Del. 2020), the Court reiterated that the DGCL is a broad, enabling act that allows immense freedom for private ordering, only limited by certain mandatory terms (e.g., a charter eliminating or limiting the liability of a director for breaches of loyalty) and public policy. Because "the Petitioners were sophisticated and informed investors, represented by counsel, that used their bargaining power to negotiate for funding from Carlyle in exchange for waiving their appraisal rights . . . [a]nd the [appraisal waiver] was not a 'midstream amendment' that was forced upon the Petitioners without their express consent," it did not have the qualities of an essential feature of the corporate form that cannot be waived (as described in *In re Appraisal of Ford Holdings, Inc. Preferred Stock*, 698 A.2d 973 (Del. Ch. 1997)). The Court held so despite Section 262 saying that qualifying stockholders "shall" be entitled to appraisal. Further, the Court held that the waiver is not a stock restriction that had to be included in the certificate of incorporation under Section 151(a), 8 Del. C. § 151(a), "because the Stockholders Agreement imposed personal obligations on the stockholders rather than encumbrances on the property rights that run with the stock" (as opposed to issuing stock without appraisal rights, which the Court clarifies is not the holding of the case). The Court then rejected Petitioner's argument that Section 218(c), 8 Del.

C. § 218(c), which authorizes two or more stockholders to enter into a voting agreement, prohibited the Company from entering into the Stockholders Agreement. It clarified that "[f]orming contracts is a core corporate power," nothing in Section 218(c) prohibits corporations from entering into stockholders agreements, and there were no reasons provided to support otherwise.

In a lengthy dissenting opinion, Justice Valihura found such ex ante waiver problematic and largely disagreed with the Majority. Expressing concern for diluting the corporate "brand" with that of alternative entities, the Justice interpreted Section 262 to be un-waivable and an important provision for regulating the balance of power between corporate constituencies. In her view, even if the DGCL is amended to permit such waiver, it should be in the certificate of incorporation. As it now stands, stockholders of Delaware corporations may waive their Section 262 rights through a stockholders agreement.

Key Takeaways

- It is now settled that stockholders of a Delaware corporation, whether holding common or preferred stock, may ex ante waive their rights to statutory appraisal under Section 262 of the DCGL in a stockholders agreement. Query, however, if a distinction remains between waivers by preferred versus common stockholders. See, e.g., *Halpin v. Riverstone Nat'l, Inc.*, 2015 Del. Ch. LEXIS 49, at *1 (Del. Ch. Feb. 26, 2015) (identifying that preferred stockholder rights are largely contractual, and noting whether common stockholders can waive the right to seek statutory appraisal in the case of a squeeze-out merger is a more nuanced question than with preferred stockholders).
- It is yet to be determined whether other statutory rights, such as books and records demand rights under Section 220, 8 Del. C. § 220, can be waived.
- Whether an appraisal waiver is valid may vary case-by-case. Expect Delaware courts to at least consider whether the parties to the agreement were sophisticated and represented by counsel.
- Delaware law makes clear that a contractual waiver of a statutory right must be clear to be enforceable, and the facts relied upon to prove waiver must be unequivocal:
 - Thus, a stockholder agreement should require minority shareholders to explicitly acknowledge that they are knowingly waiving their appraisal rights if the drag-along provision is invoked.

- o Be sure to make clear with a savings clause that such appraisal waiver (or some other provision) is intended to survive termination of the stockholders agreement, especially if the agreement is self-terminating. Consider the following savings clause from the NVCA model agreement: *“provided that the provisions of Section 3 hereof will continue after the closing of any Sale of the Company to the extent necessary to enforce the provisions of Section 3 with respect to such Sale of the Company”* Though it ultimately did not matter in this case, it may make the difference under a different agreement and a different set of facts.
- o Further, the exercise of a drag-along right should be made precisely in accordance with its terms, including all of the prescribed time periods and other requirements of the drag-along provision.

Related Content

Practice Notes

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[Stockholder Approval and Appraisal Rights in M&A Deals](#)

[Market Trends 2020: Appraisal Rights Closing Conditions](#)

Form

[Appraisal Demand Letter \(DE\)](#)

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