

Why Delaware Appraisal Awards Exceed the Merger Price— The Gap Between What the Delaware Chancery Court Says and Does

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As has been widely noted, the number of post-merger appraisal petitions in Delaware has increased significantly in recent years, due primarily to the rise of appraisal arbitrage as a weapon of shareholder activists seeking alternative methods of influence and value creation in the M&A sphere.¹ The phenomenon of appraisal arbitrage² is to a great extent a product of the frequency with which the Delaware Chancery Court has appraised dissenting shares at “fair values” that are higher (often, far higher) than the merger consideration in the transactions from which the shareholders are dissenting.³ Our analysis of the post-trial appraisal decisions issued in Delaware since 2010⁴ indicates that the court’s appraisal determinations have exceeded the

¹ Through 2010, the number of appraisal petitions filed in Delaware roughly paralleled overall merger activity, with appraisal rights being asserted in about 5% of the transactions for which they were available. In 2011, the rate of petitions doubled to 10%. In 2013, 28 petitions were filed in Delaware, representing 17% of appraisal-eligible transactions. This data has been reported by Charles Korsmo and Minor Meyers, professors at Case Western University School of Law and Brooklyn Law School, respectively, in their study, *Appraisal Arbitrage and the Future of Public Company M&A*, publication forthcoming in 92 *Washington University Law Review* __ (2015) (draft April 14, 2014), 14-18. The amounts at stake have increased as well, with the value of dissenting shares seeking appraisal in 2013 (\$1.5 billion) being ten times the value of dissenting shares in 2004, and more than five times the value of dissenting shares at their highest point in the last five years. In 2014, 20 appraisal claims have been filed in Delaware through August.

² “Appraisal arbitrage” refers to the acquisition of target shares, typically by hedge funds and activist investors, after announcement of a merger, with the purpose of seeking appraisal rights (often accompanied by a call to other stockholders not to vote for the merger and to join in seeking appraisal rights for their shares). For further discussion of “appraisal arbitrage”, please see our recent Memoranda: *New Activist Weapon—The Rise of Delaware Appraisal Arbitrage: A Survey of Cases and Some Practical Implications* (June 18, 2014); *The Rise of Appraisal Arbitrage*, published in *Insights Corporate & Securities Law Advisor* (July 2014); *Perspective on Appraisal Arbitrage—and a Look at Delaware’s Most Recent Appraisal Cases*, *Fried Frank M&A Quarterly* (2nd Quarter 2014); and *New Activist Weapon—A Look at Appraisal Arbitrage Cases*, published in *Law360* (August 7, 2014).

³ The well above market statutory interest, which accrues from the date of filing of an appraisal petition to the date of payment of the appraised amount (after an appraisal proceeding that typically takes two years or longer), has further encouraged appraisal arbitrage. Given the considerable recent attention to and criticism of the interest rate, some believe that the Delaware Legislature may consider changing the statutory interest rate when, in January 2015, as has been requested by the Governor of Delaware, the Legislature will be considering a variety of corporate governance and corporate law issues.

⁴ Our findings are summarized in the chart that follows this article.

merger price in all but two cases—with the appraisal determinations representing premiums over the merger price ranging from 8.5% to 149% (with an average of 61%).

There has been understandable concern. Practitioners and academics have commented on the uncertainty created for deals from an unknowable and potentially significant post-closing appraisal liability,⁵ and have questioned the logic underlying the court’s almost invariable determination that the “going concern” value of a target company just prior to a merger was significantly higher than the merger price.⁶ Because the Delaware appraisal statute prescribes that the “fair value” of dissenting shares for appraisal purposes must be based on the *going concern value* of the company just prior to the merger, but *excluding* any value relating to the merger (such as merger synergies and a control premium)⁷-- and because a merger price is essentially the going concern value of a target company *plus* expected merger synergies and a control premium-- as a matter of simple logic, going concern value should generally be *well below* the merger price, not far above it.

Why do the court’s appraisal awards exceed the merger price so often and by so much? And who is affected?

Based on our analysis of the Delaware appraisal decisions since 2010, we have concluded as follows:

- First, the extent of the problem has been overstated. Appraisal cases, while more prevalent than ever, still are not common. Moreover, appraisal cases are largely self-selecting for transactions in which the apparent facts provide a basis for believing that the merger price seriously undervalues the target company.

⁵ For example, noted Delaware corporate law expert Professor Stephen Bainbridge has called the process “a crap shoot”; has stated that the appraisal cases leave the “unavoidable impression” that the Delaware courts “are just sort of making this stuff up as they go along”; and has concluded that “the best thing to do would be to toss out current law in its entirety and start over with a blank piece of paper.” Stephen Bainbridge, *Elements of Value Arising from the Accomplishment or Expectation of the Merger*, StephenBainbridge.com, posted 5/25/12.

⁶ For example, Lawrence Hammermesch, a professor of corporate finance, has expressed his “doubt that efficient markets [i.e., which underlie the merger price] necessarily and systematically yield prices below [going concern value]” (which is the valuation required in appraisal cases). Lawrence Hammermesch and Michael Wachter, *The Fair Value of Cornfields in Delaware Appraisal Law*, Delaware Journal of Corporate Law, Vol. 31 (2005), at 119.

⁷ The premise is that a stockholder is entitled to be compensated for the value of the shares that the stockholder has been involuntarily deprived of—in other words, the value of the company as a going concern as if the merger had not occurred.

- Second, rather than indicating an illogical or highly uncertain approach by the court, the *actual results* of the appraisal cases (as opposed to the court’s expressed jurisprudence) indicate a deep-- and rational-- skepticism by the court, not of merger prices generally but of merger prices in “interested” transactions (that is, mergers involving a controlling stockholder, parent-subsiary, or management buyout) that did not include a meaningful market check as part of the sale process.
- Third, the court’s virtually exclusive reliance in appraisal cases on the discounted cash flow (DCF) valuation methodology—an analysis that is subject to significant uncertainty, particularly in terms of the discount rate used (which involves a high degree of subjectivity and as to which even a small change will produce a significant impact on the result) – readily permits higher valuations in connection with interested transactions that do not include a market check.
- Finally, notwithstanding the court’s continuing reference to the irrelevance of the merger price in appraisal proceedings, it would appear that the merger price would always be relevant as a benchmark in determining going concern value and that its use would not be inconsistent with the prescriptions of the appraisal statute. Moreover, consideration of the merger price, rather than its irrelevance, would appear to reflect the reality of what the court has done in appraisal cases (albeit contrary to what it has said in appraisal decisions).

The extent of the problem has been overstated.

It should be noted that, despite the significant increase in the filing of appraisal petitions over the last several years, the large majority of appraisal-eligible transactions still do not attract appraisal petitions. In 2013, appraisal petitions were filed in 17% of appraisal-eligible transactions. By contrast, almost *all* strategic transactions now attract breach of fiduciary duty litigation. Moreover, most appraisal petitions are withdrawn or the cases settled (although often for significant sums). Thus, there have been only nine Delaware post-trial appraisal decisions since the beginning of 2010.

In addition, appraisal cases are largely self-selecting for transactions in which the merger price does not fairly value the company. Because appraisal proceedings are complicated, lengthy, expensive and risky, and because the expenses are shared by the dissenting stockholders

(and cannot be shifted to all shareholders as a group or to the target company), generally appraisal cases that are brought and decided are those in which, from the apparent facts, there is a likelihood that the merger price does not fairly value the company. For example, Andrew Barroway, founder and CEO of Merion Investment Management, one of the most prolific of the hedge funds dedicated to filing appraisal petitions, has said that Merion looks for deals that appear to be undervalued by at least 30% and focuses on management-led buyouts. “The vast majority of deals are fair. We’re looking for the outliers,” he has said.⁸ In effect, virtually every appraisal decision relates to a transaction that is an outlier.

The actual results of the appraisal cases indicate a deep-- and rational-- skepticism by the court, not of merger prices generally, but of merger prices in “interested” transactions that did not include a market check.

Rather than indicating an illogical or highly uncertain approach by the court, the *actual results* of the appraisal cases (while belying the jurisprudence and the court’s assertions in its opinions) indicate a deep and rational skepticism by the court of merger prices in “interested” transactions that do not include a market check-- as well as skepticism about the range of fairness established by the target company’s investment bankers in connection with their fairness opinions and the financial analyses of the target company’s experts in the appraisal proceedings in these transactions. While the court espouses the traditional Delaware jurisprudence that holds that the merger price and sale process are irrelevant to an appraisal determination of going concern value⁹, the pattern of the court’s appraisal determinations appears to reflect an elemental

⁸ See Liz Hoffman, *Risky Legal Ploy Seeks to Milk Buyouts*, Wall St. Journal (April 15, 2014).

⁹ For example, in *Golden Telecom*, Chief Justice Steele wrote:

[The statute] unambiguously calls upon the Court of Chancery to perform an independent evaluation of ‘fair value’ at the time of a transaction. It vests the Chancellor with significant discretion to consider ‘all relevant factors’ and determine the going concern value of the underlying company. Requiring the Court of Chancery to defer—conclusively or presumptively—to the merger price, even in the face of a pristine, unchallenged transactional process, would contravene the unambiguous language of the statute and the reasoned holdings of our precedent. It would inappropriately shift the responsibility to determine ‘fair value’ from the court to the private parties.

Similarly, in *Orchard*, then Chancellor (now Supreme Court Justice) Strine, refusing to consider the merger price in determining the appraisal amount, wrote:

[Respondent] makes some rhetorical hay out of its search for other buyers. But this is an appraisal action, not a fiduciary duty case, and although I have little reason to doubt [Respondent’s] assertion [as to there having been no buyer who would pay \$25 million for the company’s preferred stock and an attractive price for the common stock], an appraisal must be focused on [Respondent’s] going concern value. Given the

distrust by the court of the fairness of the merger price in the case of interested transactions where there has not been a market check. The data is consistent in supporting the inverse conclusion as well—that, in the context of a transaction *with* a meaningful market check, the court will tend to rely on the merger price as a significant factor in determining going concern value.

In the cases we have reviewed (from 2010 to date), *the appraisal determinations representing the highest premiums over the merger price were all in “interested” transactions, and in none of those transactions was there a meaningful market check as part of the sale process.*¹⁰ The premiums over the merger price in these interested transaction cases ranged from 19.5% to 148.8% (averaging 80.5%). By contrast, in the four cases that involved “disinterested” transactions (i.e., third party mergers), two of the appraisal determinations were at a premium above the merger price, but at lower premiums than in the interested cases-- 8.5%¹¹ and 15.6%¹², respectively; one of the determinations was equal to the merger price (where there was a full market check with competing bidders in an open auction)¹³; and one was below the merger price,

relevant legal standard, the trial court did not focus extensively on the quality of marketing [of Respondent].... Instead, the testimony at trial focused mostly on the question that is relevant, which is the going concern value of [Respondent] as of the date of the merger.

¹⁰ The *Orchard* case appears to be an exception, as it included a post-signing go-shop period (albeit that produced no competing proposal), as well as a majority-of-the-minority vote condition. However, first, the appraisal determination was made based largely on the court’s determination that the liquidation preference in Orchard’s preferred stock had not been triggered by the merger (contrary to the board’s assumption when agreeing to the merger). Second, notably, in the separate fiduciary duty litigation (decided in 2014), the court was critical of the sale process, concluding that there was evidence of “substantive and procedural” unfairness in the process and price, and declining to apply business judgment review—or even to shift the burden of proof under the entire fairness review—in light of its conclusion that the features of the process purportedly intended to ensure fairness may have failed to operate effectively. Thus, although there were some features of a market check and other procedural protections in *Orchard*, the court’s high appraisal determination was made in largely the same context as in the other interested transactions, all of which had no market check whatsoever.

¹¹ In this case, *Merion v. 3M Cogent*, there was a sale process with a reasonable market check-- but the court’s appraisal opinion suggests that the court did not take the sale process and merger price into account *only* because the respondent itself had not taken it into account in its own argument to the court on valuation (relying instead solely on its expert’s DCF analysis). “Respondent asks this Court to rely on a merger price that it has not relied on itself and that is not adjusted to produce the going concern value of Cogent. *Those deficiencies* render the merger price largely irrelevant to this case,” Vice Chancellor Parsons wrote (emphasis added).

¹² In this case, *IQ Holdings v. American Commercial Lines*, there had been a relatively weak market check (a post-signing go-shop that produced no competing proposal).

¹³ In this case, *Huff v. CKx*, for the first and only time since the 2010 the Delaware Supreme Court decision in the *Golden Telecom* case (which had rejected a presumption in favor of the merger price in appraisal cases), the court

reflecting a 14.4% discount to the merger price¹⁴. One may predict that for the cases that fall between these extremes—that is, interested transactions *with* meaningful market checks and disinterested transactions *without* full market checks—the court is likely to be guided, in the former cases, by the extent to which it has confidence that the market check was sufficient to overcome the skepticism engendered by the interested nature of the transaction and, in the latter cases, by the extent to which the disinterested arm’s length nature of the transaction may overcome the skepticism arising from the absence of a meaningful market check.

The court’s reliance on the DCF valuation methodology readily permits higher valuations in interested transactions without a market check.

Pursuant to the Delaware appraisal statute, the court may use any financial analyses that are generally accepted by the financial community to determine going concern value. In

determined to defer to the merger price as the basis for determining the appraisal amount. Vice Chancellor Glasscock went to great lengths in the opinion, however, to emphasize: first, that no other valuation methodology would be reliable because of the unique fact situation that precluded development of reasonable projections, and, second, critically, that the merger price *would* be reliable because of the robust sale process that had included third party bidders competing in a full, open auction. (The unique situation that convinced the court that reliable projections could not be produced was that approximately 75% of the company’s cash flow came from its rights to the television show “American Idol”; the network distribution agreement for the show was set to expire; and it was impossible to form any reasonable view as to whether the rights would be extended or, if so, on what terms. Glasscock distinguished the situation from the usual uncertainty involved in projections, characterizing the result of the upcoming negotiations as a “one-time, unpredictable, irreversible, and immitigable increase or decrease” in revenue, based on “a single superseding event beyond the company’s control involving [decisions by] idiosyncratic actors....” He also determined that there were no comparable companies or transactions sufficiently comparable for comparables analyses to be reliable. He concluded that, in the absence of other possible valuation analyses, the “merger price [was] the best and most reliable indication of CKx’s value.” The court requested that the parties submit evidence as to what adjustments should be made to the merger price to reflect going concern value (such as excluding merger synergies). While acknowledging that logically adjustments should be made, the court found that the parties had not submitted sufficient evidence to do so; therefore, no adjustments were made—reflecting the difficulties involved in the process of backing out merger synergies and a control premium from the merger price (which maybe one reason the court has not more directly adopted this approach).

¹⁴ This case, *Gearrald v. Just Care*, is an anomaly. The minority stockholders dissenting from the merger were a) the target company’s founder and former CEO of the target company (who, as a director of the company, had voted for the merger) and b) the former CFO. They themselves had prepared the company projections that had provided the basis for the acquiror’s determination of the merger price and the petitioner’s DCF analysis in the appraisal case. The court’s determination that the merger price was higher than going concern value was based primarily on their testimony that they had not prepared the projections in the ordinary course of business or with a view to reflecting their realistic opinion about future cash flows, but, rather, that they had artificially inflated the projections in order to attract the highest possible price from the buyer.

appraisal proceedings, both parties' financial experts generally submit discounted cash flow (DCF) analyses, sometimes along with comparable company or comparable transaction analyses. The court has almost invariably used a DCF analysis, alone, to determine going concern value.¹⁵

Notably, determination of what discount rate to use in a DCF analysis is highly subjective. In addition, even a slight change in the discount rate used will have a significant impact on the result. Thus, a dissenting stockholder who can convince the court to lower the discount rate used by the company in its DCF analysis stands to achieve an appraisal determination that is significantly higher than the merger price. A look at the *Sunbelt Beverage* appraisal case is instructive.¹⁶

The price paid in the Sunbelt merger was \$45.83 per share. Both parties' experts in the appraisal proceeding agreed that the DCF methodology should be used; agreed to use management's projections in the analysis; agreed on the basic discount rate to be used; agreed that a small-company risk premium should be applied to increase the discount rate; and agreed that the small-company risk premium should be derived from the Ibbotson risk premium table.¹⁷

¹⁵ It is generally accepted practice in the financial community to use a DCF analysis in conjunction with other analyses, such as comparable company and comparable transaction analyses, as each method has its own inherent flaws. The Chancery Court has acknowledged a preference to rely on comparables analyses in addition to the DCF analysis, in order to "triangulate" going concern value, whenever possible (*see, e.g., Merion v. 3M Cogent*, at 13). However, in all the cases we reviewed, the court relied solely on the DCF analysis (even though in almost every case the target company's investment bankers had relied on comparables analyses in determining the range of fairness for the company, and the target company's (and, often, the petitioner's) financial experts in the appraisal proceeding also relied on comparables analyses along with the DCF analysis). In each case, the court found that the comparables analyses were based on companies and transactions that were not sufficiently comparable to lead to a reliable result. The only exceptions to the court's use of a DCF analysis were in the *CKx* case (discussed above); and in *Laidler v. Hesco*, where the court used a variation of the DCF analysis—namely, a DCCF (discounted capitalization of cash flow) analysis.

¹⁶ The appraisal determination in *Sunbelt* reflects the largest premium over the merger price of any case in our review. The backdrop to the consolidated appraisal-fiduciary duty litigation was an arbitration panel determination that the only reason for the merger was to eliminate the petitioner—"without notice and without legal justification"—as the sole remaining minority stockholder. The panel had found that the respondent's assertions that the petitioner had verbally agreed to sell her shares at a formula price that had been set forth in an agreement that had been negotiated and applicable three years earlier were patently false. The court characterized the controller's actions as "strong-arm tactics," noted that the process was "anything but fair," and found the investment banker's fairness opinion provided to the Sunbelt board to have been "highly suspect" and "merely window dressing". While not discussed in the opinion, the court also may have been influenced by the fact that the company's value increased dramatically after the merger.

¹⁷ The Ibbotson table assigns a "small company risk premium" based on a company's market capitalization. The "premium" is an addition to the discount rate (i.e., a discount to the overall value), reflecting the increased overall risk for a company associated with small size. The premium amounts are assigned based on which of ten "deciles" the company falls within. The smallest market cap companies fall within the 10th decile and the largest fall within

The only areas of disagreement between the experts with respect to the DCF analysis related to two factors that affected the discount rate—first, whether the company’s market capitalization placed it in the 9th or the 10th decile of companies in the Ibbotson table; and, second, whether a company-specific risk premium¹⁸ should also be applied to the discount rate.

The DCF analysis by the company’s expert (which used the small company premium applicable to companies in the 10th decile of the table—5.78%; and which also applied a company-specific risk premium of 3%) yielded a fair value of **\$36.30** per share. The DCF analysis by the petitioner’s expert (which used the premium applicable to companies that were close to the line between the 9th and 10th decile in the table—3.47%; and did not apply a company-specific premium) resulted in a fair value of **\$114.04**. The critical difference between the two analyses, which led to these vastly different amounts, was simply the relatively small effect of the two different risk premiums on the discount rate. The court accepted the petitioner’s expert’s view on these two factors¹⁹ and determined fair value to be \$114.04 (significantly above the respondent’s determination of \$36.30 and the merger price of \$45.83).

Consideration of the merger price, rather than its irrelevance, would appear to reflect the reality of what the court has done in appraisal cases (albeit contrary to what it has said), and would appear to be not inconsistent with the prescriptions of the appraisal statute.

As noted, it appears that the court harbors a deep skepticism that the merger price in an interested transaction without a meaningful market check will fairly value a company. This conclusion is not self-evident, as the court goes to considerable length in its appraisal opinions to assert that any consideration of the merger price is not appropriate in an appraisal case.

the 1st decile. Thus, companies in the 10th decile are assigned the highest risk premium (thus, the largest amount will be added to the discount rate, reducing the value that would otherwise be determined for the company).

¹⁸ A “company-specific risk premium” is another premium that can be added to the discount rate. It reflects increased risk that relates to *unique* circumstances of the specific company being valued (and that is not otherwise reflected in the discount rate, as adjusted by other risk premiums). Its use is only infrequently appropriate.

¹⁹ As to the small company risk premium, the court preferred the rate that reflected that the company’s market cap was close to the line between the 9th and 10th deciles, rather than the rate that placed the company within the 10th decile (even though there was evidence that the company actually fell within the 10th decile). With respect to the three risks “unique” to the company that the Respondent’s expert had identified as justifying a company-specific risk premium, the court viewed two of the risks (the company’s supplier contracts being subject to at will termination, and intense competition from certain other companies) as being industry-wide risks that were not specific to the company, and viewed the third risk (that the company’s projections were too optimistic) as not having been supported by any evidence submitted and, in any event, not giving rise to a company-specific risk premium.

However, based on an analysis of the actual results of the cases, as discussed above, there is an almost complete correlation between the extent to which the sale process lends confidence to the merger price as not undervaluing the company, on the one hand, and the amount by which the court's appraisal determination exceeds the merger price, on the other hand.

In our view, the statutory language does not command disregard of the merger price in an appraisal proceeding. In fact, the statute's direction to the court that, in determining going concern value, it must consider "all relevant factors" may be seen as expressly permitting (if not even possibly *requiring*) that the merger price be considered as one, among other, relevant factors. In *CKx*, the sole case (since the seminal *Golden Telecom* decision) in which the court expressly relied on the merger price to determine going concern value, Vice Chancellor Glasscock expressed his view that the court's rejection of consideration of the merger price in *Golden Telecom* was only a rejection of an *automatic presumption* in favor of the merger price as itself establishing going concern value. Consideration of the merger price as one relevant factor—or even, as Glasscock found it to be in *CKx*, the most relevant factor—would not be inconsistent with that holding, he reasoned.²⁰

²⁰ The question arises: Why has the court—which appears to take the merger price into account while claiming that it does not-- been so reluctant to expressly consider merger price as a relevant factor in going concern value. (Certain academicians have taken the question further and ask why the appraisal statute does not call for a market-oriented approach (in lieu of going concern value) in appraisal cases. The critical issue in appraisal cases, Professor Bainbridge has suggested, should be whether the dissenting stockholders received a fair premium above market price—an analysis that requires "start[ing] with the price paid in the merger and, if appropriate, work[ing] up from there.") Important considerations for the court in not conceding to use of the merger price as a relevant factor may include the following: Interested transactions often arise in a context where there is *not* an efficient, liquid market for the target company's shares against which the merger price can be considered. Also, as discussed in this article, in an interested transaction without a market check, the court does not have confidence in the merger price—because of the control factor and the inherent conflict of interest. Finally, even if the court could have confidence in the merger price in any given transaction, the court may not have confidence that merger synergies can be backed out from the merger price appropriately. The *CKx* case indicates the difficulties in determining even what a merger-specific synergy *is* for appraisal purposes. Is an acquiror's plan to cut back on staff a merger-specific synergy or a cost-saving that could have (wholly or partly) been accomplished by the target company itself? Is the key whether the post-merger improvement was being considered by the target company prior to the merger, as opposed to the idea having been thought up only by the acquiror? In *CKx*, in which the court relied on the merger price in the appraisal because of the unavailability of other methodologies, the court requested that the parties submit evidence as to what adjustments should be made to the merger price to reflect going concern value (such as excluding merger synergies). While acknowledging that logically adjustments should be made, the court found that the parties had not submitted sufficient evidence to do so; therefore, no adjustments were made—perhaps reflecting the difficulties involved.

Conclusion.

Despite the court's record in consistently determining appraisal awards that significantly exceed the merger price, for a disinterested transaction with a meaningful market check, there should be little concern. For an interested transaction without a market check, there will be a meaningful risk of an appraisal award above the merger price. For the transactions that fall between these two extremes, appraisal risk should approximate the extent to which the transaction is interested or disinterested and has or has not included a meaningful market check.

Accordingly, parties to transactions, when considering merger price and sale process issues, will want to factor into that calculus the risk associated with appraisal. Target company stockholders, when deciding whether or not to seek appraisal, will want to consider the nature of the transaction and the reasonableness of the price and process—including the range of fairness determined by the target company's investment bankers in connection with their fairness opinion, the investment bankers' underlying financial analyses (in particular, the DCF analysis) supporting their range of fairness, the nature and extent of the market check in the sale process, the presence of any other features lending credibility to the merger price (such as a majority-of-the-minority stockholder vote requirement), and the reaction of the market and analysts.

Despite much ado about the court's appraisal decisions, it appears that the court's results have a reasonable foundation, although the court's process is opaque. In addition, it appears that, for at least certain types of transactions, the court's results are reasonably predictable—the court is unlikely to make an appraisal determination that significantly exceeds the merger price in a transaction that has been subjected to a meaningful market check.²¹

²¹ Arguably, appraisal rights as currently conceived relate to a broader category of transactions than may be necessary for the protection of shareholders. As a general matter, appraisal is available for transactions in which the target company shares are not publicly traded and widely held or any part of the merger consideration consists of securities that are not publicly traded and widely held. This framework is based on the theory of efficient markets and the principle of substitutability of investments—i.e., that if there is an efficient, liquid market for shares, then appraisal is not necessary because the holders can sell the shares and use the proceeds to make an equivalent investment in other shares. The anomaly is that appraisal is also available if the merger consideration is cash—even though the cash (like publicly traded and widely held shares) could be used to make a different, equivalent investment. The transactions that appear to require appraisal rights for the protection of shareholders are those that give rise to doubt about the efficiency and liquidity of the market for the target shares or any stock merger consideration. In controlling stockholder, parent-subsiidiary, and management buyout transactions, there is an inherent risk that the control factor, conflict of interest, and heightened risk of less than full disclosure will diminish

the efficiency and liquidity of the market for the target shares. A legislative change that would equalize the treatment of cash and stock deals, providing for appraisal rights only in the case of interested transactions, would eliminate the uncertainty of appraisal for transactions for which it appears to be unnecessary, while maintaining protection for transactions where it is needed. Alternatively, a judicial change establishing deference to the merger price as a basis for determining going concern value in transactions other than the transactions that raise these doubts would have a similar effect. Limiting appraisal rights in this way would be consistent with the courts' recent narrowing of the "entire fairness" standard of review to apply only to those interested transactions for which the court thinks it is necessary because certain procedural protections that would allay those doubts are not included—and would reflect the underlying reality of the pattern of the court's appraisal decisions, bridging the gap between what the court has been saying and what it has been doing in these cases.