

Chancery Court Clarifies “Constituent Corporation”

Friday, July 13, 2018

In *City of North Miami Beach General Employees’ Retirement Plan, et al. v. Dr Pepper Snapple Group, Inc., et al.*, (C.A. No. 2018-0227-AGB (Del. Ch. June 1, 2018)), the Court of Chancery held that the term “constituent corporation” as used in Section 262 of the Delaware General Corporation Law means only an entity that actually is being merged or combined with another entity in a merger or consolidation and does not include a parent of such entities. Thus, the Court ruled that the Dr Pepper stockholder plaintiffs are not entitled to appraisal rights because Dr Pepper is not a constituent corporation, but rather the parent of one of two corporations to be merged in connection with the proposed transaction.

City of North Miami Beach General Employees’ Retirement Plan, and Maitland Police Officers and Firefighters Retirement Trust (collectively, the “Plaintiffs”), hold an undisclosed number of shares of Dr Pepper common stock. Dr Pepper Snapple Group, Inc. (“Dr Pepper”), Salt Merger Sub Inc. (“Merger Sub”), Dr Pepper’s Board of Directors, and Maple Parent Holdings Corp. (“Maple Parent”) are collectively (the “Defendants”).

On January 29, 2018, Defendants entered into an Agreement and Plan of Merger (the “Merger Agreement”). The transaction was structured as a reverse triangular merger, in which parent Dr Pepper caused its subsidiary Merger Sub to merge with and into Maple Parent, resulting in Maple Parent becoming a wholly-owned subsidiary of Dr Pepper (the “Merger”). The Merger contemplated that each share of Merger Sub common stock would convert into one share of the surviving corporation, Maple Parent. Each share of Maple Parent common stock would convert into the right to receive shares of Dr Pepper’s newly issued common stock. Additionally, Maple Parent would declare a special cash dividend payable to Dr Pepper.

Dr Pepper’s stockholders were not asked to vote on approving the Merger. Instead, Dr Pepper’s stockholders were asked to approve the requisite share issuance and a charter amendment proposal to increase the number of authorized shares. On March 8, 2018, Dr Pepper, in a preliminary proxy statement, informed Dr Pepper stockholders that they would not be given appraisal rights under Section 262 of the Delaware General Corporation Law (the “DGCL”) in connection with the Merger. On March 28, 2018, Plaintiffs filed a complaint asserting that “the individual defendants breached their fiduciary duties by failing to inform Dr Pepper’s stockholders that they have appraisal rights in connection with the Merger” and that 8 *Del. C.* § 262(d)(1) was violated because Defendants “did not inform stockholders of the availability of appraisal rights.” On cross-motions for summary judgment, the Court ruled for the Defendants.

“This action boils down to the purely legal question of whether Dr Pepper’s stockholders have appraisal rights in connection with the Merger under 8 *Del. C.* § 262.” In concluding that Dr Pepper’s stockholders are not entitled to appraisal rights under 8 *Del. C.* § 262, the Court held that Dr Pepper is not a “constituent corporation” in the Merger, and further that Dr Pepper’s stockholders are not entitled to appraisal rights because they are retaining their shares.

The Court approached this decision as a statutory matter, stating that “appraisal is available in a merger or consolidation governed by Section 262(b) only for the stock of a ‘constituent corporation.’” Although “constituent corporation” is not explicitly defined in the DGCL, the Court noted that the surrounding provisions gave a plain meaning to the term. Together, “they clearly imply that ‘constituent corporations’ are entities that were merged or combined in the transaction and *not* a parent of such entities.” For example, Section 251(a) references an



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entity surviving a merger as being either a “new resulting” entity or one of two or more “constituent corporations” to a merger. From this provision, the Court explains, the term “constituent corporations” must be referencing the corporations actually being merged or consolidated. Section 262(b)(1)(ii) also references the constituent corporation as surviving the merger. “Logically, for a constituent corporation to ‘survive’ a merger, the constituent corporation must be an entity pre-existing the merger that was combined with another entity in the transaction.”

Typically triangular mergers are structured so that the parent corporation does not become a constituent to the merger. As a result, the stockholders of a parent corporation of a merging subsidiary “generally do not have the right to vote on the merger, nor are they entitled to appraisal.” Therefore, the Court concluded, the interpretation in this case is in line with existing precedent.

The Court’s reason for denying appraisal rights under Section 262(b) is because Dr Pepper’s stockholders are not being forced to relinquish their shares as a result of the Merger. Section 262 does not grant appraisal rights for stockholders simply upon a sale of control. Rather, the Court stated that the three step process set forth in Section 262(b) for determining a stockholder’s entitlement to appraisal demonstrates that stockholders are only entitled to appraisal of their shares when those shares are being taken from them in certain, statutorily specified, types of transactions.

In conclusion, the Court found that Dr Pepper’s stockholders are not entitled to appraisal rights under Section 262(b) in connection with the Merger because the statutory requirements have not been met for two reasons: (i) the term “constituent corporation” does not include the parent of the subsidiaries involved in the Merger, and (ii) Dr Pepper’s stockholders retained their shares in connection with the Merger.

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