

## Pleading Failures Doom Disclosure Claims in Short-Form Merger Case

### Delaware Law Update

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Vice Chancellor Tamika R. Montgomery-Reeves of the Delaware Court of Chancery (the “Court”) issued a Memorandum Opinion on January 4, 2017, dismissing a lawsuit arising from a short-form merger involving United Capital Corporation (“United Capital” or the “Company”). A.F. Petrocelli, chairman of the board of directors (the “Board”), president, CEO of the Company, and owner of 94 percent of United Capital’s outstanding shares, offered to purchase the Company’s minority shares through a short-form merger. The Company’s Board formed a Special Committee that approved the transaction, and stockholders received written notice of the transaction (the “Notice”), which included “financial statements, management’s analysis of the Company’s financial status, the background of the merger, and potential Board and Special Committee conflicts.” In the consolidated class action lawsuit, the lead stockholder-plaintiff alleged that deficiencies with the Notice gave rise to breaches of the duty of disclosure.

The Court began by reciting the standards applicable to short-form mergers under 8 *Del. C.* § 253. “Although fiduciaries are not required to establish entire fairness in a short-form merger,” the Court explained, “the company must notify the minority of the availability of appraisal rights,” provide a copy of the appraisal statute, and disclose “information material to the decision of whether or not to seek appraisal . . .”

The Court determined that the Notice “contained sufficient information for stockholders to decide whether to seek appraisal,” but the plaintiff argued that various material facts had been omitted. Among other things, the plaintiff asked for an inference that undisclosed financial projections existed because of forward-looking information contained in the Notice. The Court rejected this argument because the plaintiff failed to identify specific facts to support the allegation.

The plaintiff also argued that the Notice failed to specifically disclose that two of the three independent members of the Special Committee had “long personal, professional, and financial ties with Petrocelli.” The Court rejected this argument as well because the Notice “reveal[ed] the Special Committee’s existence, outline[d] its negotiation process, disclose[d] . . . potential conflicts, provide[d] financial and business information necessary to inform stockholders about whether to seek appraisal, and [did] not deceive stockholders into relying primarily on the Special Committee.”

This decision provides at least two insights. First, while Delaware is a “notice pleading” jurisdiction, and the Court of Chancery will generally deny a motion to dismiss if a complaint presents a “reasonably conceivable set of circumstances” upon which the plaintiff may prevail, plaintiffs cannot rely on conclusory, unsupported allegations to support their claims. Instead, and even though the Court will give the plaintiff the benefit of all reasonable inferences, claims must be supported by specific allegations of fact. Second, *United Capital* serves as a reminder that appraisal is generally the only remedy available to stockholders in a short-form merger, and that even where potentially significant facts have not been disclosed (such as the specifics of personal relationships underlying disclosed conflicts), pleading disclosure violations can be difficult.