

## THE “MARKET EXCEPTION” IN APPRAISAL STATUTES

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### **Introduction: Public Shareholders and Appraisal Rights**

Appraisal is a right and a remedy. Available by statute in all states, appraisal provides dissenting shareholders the right “to require the corporation to pay them the ‘fair value’ of their shares upon some mergers or other fundamental changes.”<sup>1</sup> Appraisal statutes provide procedures for dissenting shareholders to receive a judicial hearing in which the court appraises the value of their interests. “A primary purpose of appraisal statutes is to protect minority shareholders.”<sup>2</sup> The intent of appraisal valuations by courts is to compensate dissenting minority shareholders equitably for the unwanted change in their investments. Therefore, courts in most states employ a valuation standard called “fair value,” which is considered to be a fuller measure of value that can result in an assessment higher than market price.<sup>3</sup>

Appraisal rights and fair value assessments are broadly available for shareholders of private companies. However, 38 states now restrict the appraisal rights of shareholders of public companies through a provision in their appraisal statutes called a “market exception” (also called a “market-out” or a “market-out exception”). With varying specifics, these statutes deny shareholders of publicly traded companies the right to the court-awarded assessment to which similarly-situated private company shareholders are entitled.

Although the market exception has been addressed (and criticized) from time to time in legal journals, the author has identified only one article in the past 40 years that discusses the differing requirement in various jurisdictions.<sup>4</sup> This study updates and expands the discussion in that article, describing the current status of the market exception for each state

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<sup>1</sup> Robert B. Thompson, “The Case for Iterative Statutory Reform: Appraisal and the Model Business Corporation Act,” 74 *Law & Contemp. Prob.* 253 (2011).

<sup>2</sup> Shannon P. Pratt, *Valuing a Business: The Analysis and Appraisal of Closely Held Companies*, 5th Ed. (McGraw Hill, 2008), p. 916.

<sup>3</sup> This article deals with appraisal statutes only. The fair value standard also applicable for causes of action other than appraisal in many states. Fair value is frequently the standard of value in shareholder oppression cases. Delaware applies fair value for valuations in “entire fairness” cases involving a breach of fiduciary duty.

<sup>4</sup> Mary Siegel, “An Appraisal of the Model Business Corporation Act’s Appraisal Rights Provisions,” 74 *J. of Law and Contemporary Problems* 231 (2011).

and the District of Columbia. It summarizes, for each jurisdiction, whether a market exception applies, the definition of publicly traded shares, the scope of the exception, and the terms of any exemption that allows public shareholders to have appraisal rights.

The first state to enact a market exception was Delaware in 1967.<sup>5</sup> Within ten years, 20 states had legislated a market exception,<sup>6</sup> and the number rose to 26 by 1999.<sup>7</sup> The 2008 Official Comments on the Model Business Corporation Act (“MBCA”) stated:

Approximately half of the general corporation statutes in the United States provide exceptions to appraisal for publicly-traded shares, on the theory that it is not productive to expose the corporation to the time, expense and cash drain imposed by appraisal demands when shareholders who are dissatisfied with the consideration offered in an appraisal-triggering transaction could sell their shares and obtain cash from the market.<sup>8</sup>

Many states provide specific exemptions from the public shareholder market-out provisions which restore the right to a judicial appraisal at fair value. These varied exemptions are often awkwardly referred to as “exceptions to the market exception”. For purposes of clarity, we refer to these “exceptions to the market exception” as “exemptions.” The principal exemptions are for transactions with interested parties and for receiving consideration other than common stock.

### **The Importance of the Fair Value Standard in Appraisal**

We start with a discussion of the “fair value” standard and its importance. Fair value is the “going-concern value” of the enterprise.<sup>9</sup> Professors Hamermesh and Wachter state that, for accomplishing appraisal statutes’ intent to fairly compensate dissenting shareholders, “[T]he ‘going concern value’ standard adopted by the Delaware courts as the measure of ‘fair value’ in share valuation proceedings is superior, in both fairness and efficiency, to its two main competitors, [fair] market value and third-party sale value.”<sup>10</sup>

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<sup>5</sup> Robert H. Jerry II “A Reconsideration of the Stock Market Exception to the Dissenting Shareholder's Right of Appraisal,” 74 *Mich. L. Rev.* 1023, 1031(1976).

<sup>6</sup> Jerry at 1024, fn. 4.

<sup>7</sup> Siegel at 246.

<sup>8</sup> Official Comments to the MBCA, Chapter 13 (2008).

<sup>9</sup> “Fair value” in appraisals is distinct from (and normally greater than) “fair value” for accounting purposes as defined in FAS 157. The latter is a form of fair market value.

<sup>10</sup> Lawrence A. Hamermesh and Michael L. Wachter, “Rationalizing Appraisal Standards in Compulsory Buyouts,” 50 *B.C. L. Rev.* 1021 (2009).

The fair value standard in appraisal valuations is based on equitable concepts of justice and is used in almost all states.<sup>11</sup> When the unanimous consent requirement for corporate action was abandoned, it was replaced by the right to a judicial appraisal. This process is employed to award minority shareholders a full measure of their interests when a major change in their investment occurs and they have dissented. It serves to compensate objecting investors who are forced out their equity investment in an enterprise or, alternatively, are locked into an investment materially different from the one in which they had invested. “Fair value” affords a fuller measure of the minority’s interest because it excludes discounts for minority status and, in most states, lack of marketability or illiquidity.<sup>12</sup> In addition, fair value includes opportunities for value enhancement that management has anticipated:

[G]oing concern value must include not only the discounted free cash flow to be generated by the corporation’s [existing] assets, but also the discounted free cash flow to be generated by the reinvestment opportunities anticipated by the corporation.<sup>13</sup>

Fair value differs from fair market value and from third-party sale value. It differs from fair market value (the price at which an asset would change hands between a knowledgeable and willing buyer and a knowledgeable and willing seller) because fair market value is often subject to discounts for minority interest and/or lack of marketability. Because of these discounts, fair market value is generally less than fair value.

Third-party sale value (acquisition value) is a standard derived from transactions in which corporate control is acquired.

Under a third-party sale standard, [dissenting] shareholders would receive a value greater than fair value. Third-party sale price includes additional elements of value resulting from the transaction, such as operating control and synergistic values. Most appraisal statutes expressly exclude from fair value any increases in value resulting from the synergies accomplished by the transaction.<sup>14</sup>

If dissenters were to receive acquisition value, they would often receive a windfall above going-concern value.

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<sup>11</sup> The appraisal statutes in California and Ohio specify “fair market value.” Wisconsin uses “fair market value” for business combinations and “fair value” in all other situations. Most states apply definitions of “fair value” that are similar to Delaware’s.

<sup>12</sup> Discounts for lack of marketability are permitted in New York as well as in appraisals of banks in Iowa and by the Controller of the Currency. Some other states permit discounts for lack of marketability in limited circumstances.

<sup>13</sup> Hamermesh & Wachter at 1022.

<sup>14</sup> *Id.*

## **The Model Business Corporation Act and Delaware: Appraisal Trigger Events and Market Exceptions**

Professor Siegel's 2011 thoughtful and comprehensive article discussing appraisal rights in the MBCA contrasts the corporate events that give minority shareholders the right to an appraisal action under the MBCA and under Delaware corporate law:

MBCA section 13.02(a) lists five mandatory appraisal triggers, each of which specifically defines events that require the corporation to offer its shareholders appraisal rights: (1) mergers, (2) share exchanges, (3) dispositions of assets, (4) amendments to the articles, and (5) conversion or domestication. Delaware, in contrast, mandates appraisal rights only for some mergers.<sup>15</sup>

Siegel notes that the MBCA's five appraisal triggers, compared to Delaware's single trigger, results in the MBCA offering "more opportunity for shareholders to demand" their appraisal rights.<sup>16</sup> She points out that "whether increased opportunity to exercise these rights is good corporate policy depends on one's view of appraisal rights and their function."<sup>17</sup>

Although the MBCA offers greater opportunity for appraisal rights, it denies these rights to public shareholders in some circumstances by including market exceptions. The drafters of the MBCA have debated over many years the advisability of denying appraisal rights to shareholders of public companies, and they have in fact changed their position twice. They deleted the market exception in 1978, but then restored it under specific circumstances in 1999. The 1999 Committee on Corporate Laws, cognizant that most dissatisfied public shareholders have a public market in which to dispose of their holdings, agreed that they should be compelled to use it. Acknowledging, however, that market price was not always a valid indication of value, the Committee rationalized its use by pointing out appraisals' defects of high cost (arguably prohibitive for small shareholders) and inability to produce a "perfect price".

The 1999 Committee was troubled, however, by the problems that interested party transactions could cause public shareholders. Siegel points out that after much deliberation, the Committee concluded that an exemption to public shareholders' inability to obtain appraisal should be granted in conflict cases:

The 1999 Committee . . . believed that the market-out exception had great value even if it was not reliable in all circumstances. Specifically, the strengths of the market-out are that it eliminates the uncertainty, large costs, and time commitment involved in any appraisal proceeding. Furthermore, although the market may not always achieve a perfect price, the variables involved in an appraisal proceeding surely do not produce an ideal price either, and are

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<sup>15</sup> Siegel at 232. Siegel's reference to "some mergers" reflects the fact that Delaware offers appraisal to an acquired company's shareholders in mergers other than in stock-for-stock mergers.

<sup>16</sup> *Id.* at 233.

<sup>17</sup> *Id.*

indisputably attendant by large financial and time costs. . . . [T]hrough its additional exception for conflict-of-interest transactions, the Committee reinstated appraisal rights for those transactions when the market is, arguably, unreliable.<sup>18</sup>

When this exemption, referred to above by the MBCA as an “additional exception,” is adopted by a state, it serves the purpose of exempting public shareholders in conflicted transactions from the denial of appraisal rights.

### **Why Many States and the MBCA Choose to Deny Appraisal Rights to Public Shareholders Through the Market Exception**

The states that have market exceptions (with or without exemptions) do so for many of the policy reasons proposed by the MBCA. They recognize the considerable court and legal expenses as well as the procedural difficulties involved in pursuing appraisal, and they are unconvinced that judicial appraisals inevitably result in accurate or “fair” assessments. Recognizing that the courts need to assess fair value for private company shareholders because no established market price for private company shares exists, they note that, in contrast, public shareholders presumptively have an available market. These states prescribe that when a public market exists (or is deemed to exist), public shareholders must employ market price instead of court-appraisal as the measure of their interests.

Proponents of market exceptions argue that because shareholders of publicly traded companies may freely sell their shares, appraisal rights are unnecessary.

[They] argue . . . that the market adequately values stock; valuation through appraisal is unnecessary because dissenting shareholders can sell their shares on the market for the appropriate price. . . . [They] contend that appraisal is redundant for shares of publicly traded companies because the shareholders . . . may obtain the appropriate value by selling on the market.

. . . For minority shareholders of a closely-held company, finding a buyer willing to pay fair value for the shares is usually difficult and often impossible. Appraisal provides a means for these shareholders to exit in an illiquid market; however, appraisal is unnecessary for stockholders of a publicly-traded company because they can easily sell on the market.<sup>19</sup>

In contrast, opponents of denying appraisal rights to public shareholders argue that the market exception is based on the questionable concept that market price necessarily represents the fair value of shares. The case against the market exception was persuasively set forth in Barry Wertheimer’s classic 1998 article on appraisal:

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<sup>18</sup> *Id.* at 247

<sup>19</sup> Jeff Goetz, “A Dissent Dampened by Timing: How the Stock Market Exception Systematically Deprives Public Shareholders of Fair Value,” 15 *Fordham J. of Fin. and Corp. L.* 771, 777-79 (2009).

Legislatures that have enacted appraisal statutes without market exceptions appear to have recognized that the market does not always adequately protect minority shareholders, and that minority shareholders cashed out at a price at or above the market price may require additional protection. [R]eliance on market price does not adequately protect the interests of minority shareholders.<sup>20</sup>

[A] powerful argument that counsels against reliance on market price to determine fair value stems from informational asymmetry. Insiders proposing a cash-out merger are likely to have access to information that is not available to minority shareholders, and that is not reflected in market prices. It is unfair to allow insiders to use such information to their benefit, and unfair to relegate dissenting shareholders to a market price that does not reflect information known only to insiders.<sup>21</sup>

### **The Market Exception – Four Categories**

The states' positions as to the market exception can be grouped in four general categories.

1. First, 11 states have virtually all-inclusive “market out” exceptions denying appraisal rights to shareholders of publicly traded companies. These states deny appraisal rights for public shareholders regardless of interested party involvement or the form of consideration received. In these states, the only options available to dissatisfied shareholders are either to sell in the market or to accept the consideration being paid.
2. A second group of 13 states, including Delaware, base their determination to deny appraisal to public shareholders on the type of consideration received in the transaction. They deny appraisal to shareholders of publicly traded corporations who receive publicly traded common stock in stock-for-stock mergers<sup>22</sup> but permit appraisal for public shareholders who receive cash or debt. They also allow public shareholders to pursue appraisal in the infrequent situations where they receive consideration such as debt, preferred stock or warrants in addition to stock.
3. A third group of 14 states and the District of Columbia align themselves with the MBCA and draw their public market exception somewhat more narrowly. They permit appraisal for public shareholders who receive cash or debt and additionally permit if shareholders receive publicly traded common stock in a

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<sup>20</sup> Barry M. Wertheimer, “The Shareholders’ Appraisal Remedy and How Courts Determine Fair Value,” 47 *Duke L. J.* 613, 635 (1998).

<sup>21</sup> *Id.* at 638.

<sup>22</sup> Some of these states permit appraisals in stock-for-stock mergers with parent companies.

conflicted transaction. This allows publicly-traded companies' shareholders to retain appraisal rights when interested parties are materially involved, regardless of the form of consideration received. In these cases, legislators have recognized that the superior position of controllers or other interested parties may have affected the terms of the transaction.

4. The other 12 states have no market exception, granting public company shareholders appraisal rights and fair value equally with private company shareholders. They make the appraisal remedy comprehensively available to dissenting shareholders, regardless of regardless of interested party involvement or the form of consideration.

The definition of publicly traded or marketable shares varies from state to state. The appended Exhibit A summarizes, for each jurisdiction, whether a market exception applies, the definition of publicly traded shares, the scope of the exception, and the terms of any exemption that allows public shareholders to have appraisal rights. The table below shows the states according to market exception category, as well as a listing of those jurisdictions which allow appraisal to stockholders of publicly traded companies.

<b>1. Appraisal Denied to All Shareholders of Public Companies</b>	<b>2. Appraisal Denied If Publicly Traded Shares Are Sole Consideration</b>	<b>3. Appraisal Denied If Publicly Traded Shares Are Sole Consideration Except in Interested Party Transactions</b>	<b>4. No Market Exception</b>
Alaska Arizona Indiana Michigan New Jersey Oregon Pennsylvania Rhode Island South Carolina Tennessee Wisconsin	California Colorado Delaware Georgia Kansas Minnesota Nevada New York North Dakota Oklahoma Texas Utah Wyoming	Connecticut District of Columbia Florida Idaho Iowa Louisiana Maryland Maine Massachusetts Mississippi New Hampshire North Carolina South Dakota Virginia West Virginia	Alabama Arkansas Hawaii Illinois Kentucky Missouri Montana Nebraska New Mexico Ohio Vermont Washington

## 1. Public Shareholders Denied Appraisal

Eleven states either flatly forbid appraisal for all public shareholders or tightly restrict its availability. All but one of these states deny appraisal to all shareholders of publicly traded companies regardless of the form of consideration. The three most restrictive – Arizona, Pennsylvania and Rhode Island – bar appraisals for shareholders of any company with 2,000 shareholders even if there is *no market whatever* for their shares. This overbroad scope allows such companies to squeeze out illiquid minority holders and deny them the appraisal rights that they would have had their shares not effectively (and inaccurately) been deemed to be marketable.

Michigan permits appraisal in the infrequent situation where shareholders receive consideration that includes anything other than cash and/or stock, (*i.e.* consideration such as debt, preferred stock, warrants, or contingent rights) but it denies appraisal in all other cases. However, Michigan denies appraisal to shareholders of *private* companies who receive shares traded on a national securities exchange as their sole consideration.

## 2. Public Shareholders Denied Appraisal in Stock-for-Stock Transactions for Publicly Traded Shares, Including Most Conflict Transactions

Delaware and 11 other states apply the market exception and deny appraisal rights to public corporation shareholders only if shareholders of publicly traded companies receive nothing but publicly traded common shares in a stock-for-stock transaction.<sup>23</sup> They permit appraisal if any cash or alternate consideration such as debt, preferred stock, or warrants, is included in the consideration paid.<sup>24</sup> Maryland, however, does not require that the shares received be marketable.

One state, New Jersey, applies the market exception not only to receipt of publicly traded shares, but also to receipt of other kinds of publicly traded securities. Shareholders of New Jersey corporations who receive alternative consideration such as low quality debt or preferred stock are harmed, since those securities cease participating in the upside but retain downside risk.

The reasoning in barring appraisal for shareholders of publicly traded companies in stock-for-stock transactions while permitting it for cash transactions is that when shareholders receive publicly traded common stock, the acquired company's shareholders continue as shareholders in the combined public company. Disgruntled shareholders continue to hold marketable stock, so that they can use its liquidity to exit when they choose.

[The exemption] simply recognizes that the shareholder-firm relationship has not been terminated, so appraisal has not been triggered. A pure equity exchange results in a continuing equity relationship, and the shareholder

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<sup>23</sup> As discussed below, there are significant differences in the states' definitions of publicly traded stock.

<sup>24</sup> Generally, if shareholders receive cash for fractional shares in a stock-for-stock merger, the market exception nonetheless applies.



continues to bear the firm's operational risk at a price discounted for expected future agency costs. Further, at the time of merger, the expected agency costs faced by the acquired and acquiring stocks are the same. This explains the cash out exception: if the minority is cashed out, then this relationship is terminated.<sup>25</sup>

A recent criticism argues that barring appraisal in stock-for-stock mergers is counter to the original purpose of statutory appraisal:

[The] market out exception . . . doesn't make much sense. . . . [T]he appraisal remedy was originally adopted at a time when consideration in mergers was mostly stock. Dissenting stockholders who didn't want the stock of the acquirer . . . were given the right . . . to receive the value of their stock in cash money. So, modern appraisal statutes seem to get this exactly backwards. If you receive stock, no appraisal. If you receive cash (something other than stock of the surviving corporation or publicly traded stock), you have rights.<sup>26</sup>

These 13 states deny appraisal in most or all interested party transactions. In eight of these states (California, Colorado, Georgia, Minnesota, Nevada, New Jersey, North Dakota, and Utah), all shareholders of publicly traded companies who are squeezed out in *any* stock-for-stock merger with another public company are denied an appraisal remedy even if it is an interested party transaction. Delaware, Kansas, New York, and Oklahoma permit appraisal when shareholders are squeezed out for stock in a short-form merger – this limited provision serves to protect minority shareholders who are given parent company stock. Texas permits appraisal in any merger with a parent company – but not in a stock-for-stock merger with another company controlled by an interested party.

Denying appraisal in interested party stock-for-stock transactions leaves room for abuse by a controller who uses stock and lowballs the exchange ratio. However, controllers squeezing out minority shareholders most often use cash rather than stock, in which case shareholders remain eligible for appraisal. Most stock-for-stock mergers are arms' length and thus are less likely to result in viable appraisal actions.<sup>27</sup>

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<sup>25</sup> Brett A. Margolin and Samuel J. Kursh, "The Economics of Delaware Fair Value," 30 *Del. J. Corp. L.* 413, 432 (2005).

<sup>26</sup> M&A Law Prof Blog, "The nonsensical market out in appraisal," Sept. 13, 2018, available at <https://lawprofessors.typepad.com/mergers/2018/09/the-nonsensical-market-out-in-appraisal.html>.

<sup>27</sup> Some commentators appear not to have recognized the fact that most stock-for-stock mergers are arms' length. For example, Siegel asserts, "Delaware's market-out exception . . . clearly decrease[s] the frequency of appraisal rights." Siegel at 251.

### 3. Public Shareholders Denied Appraisal in Stock-for-Stock Transactions for Publicly Traded Shares Except in Conflict Transactions

Fourteen states and the District of Columbia base their determination as to whether to permit appraisal for shareholders of public companies on whether the transaction is conflicted. They apply the market exception when the consideration paid to public shareholders consists solely of publicly traded stock *except when the transaction is with an interested party*. “The term ‘interested transaction’ addresses two groups of conflict transactions: those . . . which involve controlling shareholders; and those . . . which involve senior executives and directors.”<sup>28</sup>

The provision allowing appraisal in interested party transactions serves to protect minority shareholders, who are potentially subject to an abusive transaction initiated by a control shareholder:

Where a pre-existing, controlling shareholder squeezes out the minority, . . . the minority shareholders are especially vulnerable to an acquisition at a price that fails to reflect the firm’s going concern value.<sup>29</sup>

Some statutes state that the market exception “shall not be applicable and appraisal rights shall be available . . . where the corporate action is an interested transaction,”<sup>30</sup> The definition of “interested party” varies from state to state. In 1998, Wertheimer expressed concerns about trying to define interested party transactions that remain valid today:

In order to apply the market exception only to non-conflict transactions, it would be necessary to craft a statutory definition of conflict of interest transaction that is broad enough to cover the multitude of potential conflicts. This is a hazardous undertaking, because it creates a risk that a conflict of interest transaction could slip through the cracks of the statutory definition. . . . A merger may appear to be an arm's-length transaction between unrelated parties, but the directors or managers of one corporation may receive a payment on the side, or other consideration, in return for their agreement to support the transaction. This more subtle side payment scenario is a real concern because it negates true arm's-length bargaining.<sup>31</sup>

He concluded that “it is preferable to provide an appraisal remedy to public shareholders in all contexts, rather than only in non-conflict situations.”<sup>32</sup>

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<sup>28</sup> Official Comments to Model Bus. Corp. Act, § 13.01 (2008).

<sup>29</sup> Hamermesh and Wachter at 1021.

<sup>30</sup> *E.g.*, VA. CODE ANN. § 13.1-730 (b)(4).

<sup>31</sup> Wertheimer at 706.

<sup>32</sup> *Id.* at 707.

#### **4. States with No Market Exception**

Only 12 states have no market exception. Their appraisal statutes make no distinction between public and private corporations in granting appraisal rights to shareholders. Also, there is no market exception for appraisals of national banks by the Controller of the Currency. These jurisdictions concur with the views expressed by Wertheimer in 1998, when he wrote, “There is no longer any justification for this exclusion, given the minority shareholder protection rationale for the remedy.”<sup>33</sup>

#### **The Statutory Definition of a Publicly Traded Company Varies Widely**

States use widely varying criteria in determining whether a corporation is to be deemed public (and thus subject to the market exception) or private. Some use a clear and simple definition – shares are deemed publicly traded if they are listed on a national securities exchange.<sup>34</sup> This category has various alternatives: (i) the New York Stock Exchange and the NYSE MKT LLC (formerly the American Stock Exchange), (ii) these two markets plus Nasdaq; or more broadly, (iii) a national securities exchange registered with the SEC.

Some states deem any shares traded on any “organized market” to be publicly traded, and some do not even require that a market actually exists. In some states, the definition of a publicly traded company includes an entity with 2,000 shareholders. Where the 2,000 shareholder requirement creates an presumption of marketability, (a) some states exclude insider shares, (b) some states require 2,000 shareholders *of record*,<sup>35</sup> and (c) some states require a minimum aggregate market value of common stock, usually \$20 million.

The MBCA has modified the wording of its market exception clause. The 2002 MBCA § 13.02(d) said:

- (1) Appraisal rights shall not be available for the holders of shares of any class or series of shares which is:
  - (i) listed on the New York Stock Exchange or the American Stock Exchange or designated as a national market system security on an interdealer quotation system by the National Association of Securities Dealers, Inc.; or
  - (ii) not so listed or designated, but has at least 2,000 shareholders and the outstanding shares of such class or series has a market value of at least \$20 million (exclusive of the value of such shares held by its subsidiaries, senior executives, directors and beneficial shareholders owning more than 10 percent of such shares).

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<sup>33</sup> Wertheimer at 704.

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<sup>35</sup> Counting shareholders of record rather than beneficial owners materially raises the bar for companies traded on a national securities exchange, since it is common for publicly traded shares to be held by a nominee in “street name.”

Clause (ii) does not even require that a market exists. In practice, shares of numerous companies with 2,000 shareholders are clearly illiquid: indeed, some large private companies have shareholder agreements that limit or even prohibit sale of shares to third parties.

The 2008 and 2016 MBCA § 13.02 used different wording:

(1) Appraisal rights shall not be available for the holders of shares of any class or series of shares which is:

(i) a covered security under section 18(b)(1)(A) or (B) of the Securities Act of 1933 [*i.e.*, a national securities exchange];

(ii) traded in an *organized market* [emphasis added] and has at least 2,000 shareholders and a market value of at least \$20 million . . .

However, nowhere in the MBCA is “organized market” defined. Although several states use this language from the MBCA none has defined “organized market.” Many companies that are “listed” in the “pink sheets” (presumably an organized market) have numerous shareholders but minimal trading volume. “Pink sheet” companies are thinly traded and often virtually illiquid. They frequently have inadequate public disclosure – or none at all – and therefore their published bid and asked prices are highly unlikely to reflect a company’s value.

It is difficult to comprehend how, even if a company has more than 2,000 stockholders, its shares can be assumed to be marketable when there is no market in which they can be sold. Deeming shares to be marketable *when there is no active market or no market at all* is a flawed concept. The underlying concept of the market exception is that shareholders have the option of selling in an active and informed market, but shareholders cannot have this option when there is no market into which they can sell.

## **Conclusions**

A market exception limited to stock-for-stock mergers into companies whose shares have a liquid market can be justified by the fact that shareholders in the acquired company continue to be shareholders in the surviving entity. However, it is vulnerable to abuse if the acquirer’s shares lack liquidity or when there is not an exemption for interested party transactions. Granting appraisal rights for dissenters in interested party transactions is beneficial to minority shareholders, provided that the definition of interested party transactions is adequate.

The states that deny appraisal rights for shareholders of publicly traded companies, regardless of interested party involvement, the form of consideration, or the marketability of the shares received, unreasonably deprive abused public company shareholders of the ability to obtain redress through the appraisal remedy.

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## EXHIBIT A

### Terms of the Market Exception \*

	<b>Definition of publicly traded shares</b>	<b>Market exception applies if consideration is:</b>	<b>Exemption from the market exception:</b>
Alabama	[No market exception]	–	–
Alaska	Shares of company listed on a national securities exchange.	Any form of consideration.	–
Arizona	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Any form of consideration.	–
Arkansas	[No market exception]	–	–
California	Shares of company listed on a national securities exchange.	Shares of company listed on a national securities exchange.	If shares have transfer restrictions or if shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
Colorado	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	If shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
Connecticut	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Delaware	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	If shareholder receives anything but marketable shares, as defined, or short-form merger other than 2 <sup>nd</sup> step of a two-step transaction. Cash for fractional shares does not trigger appraisal rights.
District of Columbia	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Florida	Shares of company listed on a national securities exchange or with 2,000 shareholders and market value of \$10 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company listed on a national securities exchange or with 2,000 shareholders and market value of \$10 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.

\* In this Exhibit, a “listed” company is a company traded on the New York Stock Exchange or the NYSE MKT LLC. The term “national securities exchange” also includes Nasdaq and other national securities exchange registered with the SEC. “Marketable shares, as defined” refers to the definition in the center column.

	<b>Definition of publicly traded shares</b>	<b>Market exception applies if consideration is:</b>	<b>Exemption from the market exception:</b>
Georgia	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	If shareholder receives anything but marketable shares, as defined, or if shareholder receives shares different in type or exchange ratio from shares offered to others of same class. Cash for fractional shares does not trigger appraisal rights.
Hawaii	[No market exception]	–	–
Idaho	Shares of company listed on a national securities exchange or with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company listed on a national securities exchange or with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Illinois	[No market exception]	–	–
Indiana	Shares of company listed on a national securities exchange.	Any form of consideration.	–
Iowa	Shares of listed or Nasdaq company or company with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of listed or Nasdaq company or company with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	If acquisition is by beneficial owner of 20% or by party with right to elect 25% of directors, or if shareholder receives anything but cash or marketable shares, as defined.
Kansas	Shares of listed or Nasdaq company or company with 2,000 shareholders of record.	Shares of listed or Nasdaq company or company with 2,000 shareholders of record.	Short-form merger, or if shareholder receives anything marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
Kentucky	[No market exception]	–	–
Louisiana	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Maine	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Maryland	Shares of company listed on a national securities exchange.	Shares of a corporation (but with no marketability requirement).	Merger with interested party, as defined, or if directors and executive officers were the beneficial owners, in the aggregate, of 5%, or if directors and executive officers receive stock on terms not available to all holders. Cash for fractional shares does not trigger appraisal rights.
Massachusetts	Shares of listed or Nasdaq company, or company traded on a regional securities exchange or interdealer quotation system that has least 250,000 outstanding shares and market value of \$5,000,000, excluding shares held by officers, directors and affiliates.	Shares of listed or Nasdaq company, or company traded on a regional securities exchange or interdealer quotation system that has least 250,000 outstanding shares and market value of \$5,000,000, excluding shares held by officers, directors and affiliates.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares.

	<b>Definition of publicly traded shares</b>	<b>Market exception applies if consideration is:</b>	<b>Exemption from the market exception:</b>
Michigan	Shares of company listed on a national securities exchange.	Any form of consideration; also, if shares of company listed on a national securities exchange are sole consideration to private company shareholders.	If shareholder receives anything but cash or marketable shares, as defined.
Minnesota	Shares of listed or Nasdaq company.	Shares of listed or Nasdaq company.	If shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
Mississippi	Shares of listed or Nasdaq company or company with 2,000 shareholders of record and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of listed or Nasdaq company or company with 2,000 shareholders of record and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Missouri	[No market exception]	–	–
Montana	[No market exception]	–	–
Nebraska	[No market exception]	–	–
Nevada	Shares of listed or Nasdaq company or company with 2,000 shareholders.	Shares of listed or Nasdaq company or company with 2,000 shareholders.	If shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
New Hampshire	Shares of company traded in an organized market with 1,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders	Shares of company traded in an organized market with 1,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
New Jersey	Shares of company listed on a national securities exchange or with 1,000 shareholders of record.	Shares, obligations or other securities which will be listed on a national securities exchange or by held 1,000 holders of record.	If shareholder receives any consideration other than shares, obligations or other securities which will be listed on a national securities exchange or by held 1,000 holders of record
New Mexico	[No market exception]	–	–
New York	Shares of company listed on a national securities exchange.	Shares of company listed on a national securities exchange.	Merger with parent company, or if shares are not entitled to vote on transaction, or if shareholder receives anything but marketable shares, as defined.
North Carolina	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
North Dakota	Shares of company listed on a national securities exchange.	Shares of company listed on a national securities exchange.	If shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
Ohio	[No market exception]	–	–
Oklahoma	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Short-form merger, or if shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.

	<b>Definition of publicly traded shares</b>	<b>Market exception applies if consideration is:</b>	<b>Exemption from the market exception:</b>
Oregon	Shares of company listed on a national securities exchange.	Any form of consideration.	–
Pennsylvania	Shares of listed or Nasdaq company or company with 2,000 shareholders.	Any form of consideration, unless other members of the class receive special treatment.	–
Rhode Island	Shares of listed or Nasdaq company or company with 2,000 shareholders of record.	Any form of consideration.	–
South Carolina	Shares of company listed on a national securities exchange.	Any form of consideration.	–
South Dakota	Shares of company listed on a national securities exchange or with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company listed on a national securities exchange or with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Tennessee	Shares of company listed on a national securities exchange.	Any form of consideration.	–
Texas	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Merger with parent, or if shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
Utah	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	Shares of company listed on a national securities exchange or with 2,000 shareholders of record.	If shareholder receives anything but marketable shares, as defined. Cash for fractional shares does not trigger appraisal rights.
Vermont	[No market exception]	–	–
Virginia	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million.	Shares of company listed on a national securities exchange or with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Washington	[No market exception]	–	–
West Virginia	Shares of company listed on a national securities exchange, or with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company listed on a national securities exchange, or with 2,000 shareholders and market value of \$20 million excluding shares held by senior executives, directors and 10% beneficial shareholders.	If transaction is with interested party, as defined, or if shareholder receives anything but cash or marketable shares, as defined.
Wisconsin	Shares of listed or Nasdaq company	Any form of consideration.	–
Wyoming	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	Shares of company traded in an organized market with 2,000 shareholders and market value of \$20 million, excluding shares held by senior executives, directors and 10% beneficial shareholders.	If shareholder receives anything but cash or marketable shares, as defined.



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