

12TH ANNUAL

Mergers and Acquisitions Institute

Developments in Drag-Alongs and Other Minority Stockholder Squeeze-Out Techniques

Moderator

Larry E. Glasgow, Gardere Wynne Sewell LLP, Dallas, TX

Panelists

Gemma L. Descoteaux, Polsinelli PC, Dallas, TX

Darren C. Hauck, Alston & Bird LLP, Dallas, TX

Robert B. Little, Gibson, Dunn & Crutcher LLP, Dallas, TX

Patricia O. Vella, Morris, Nichols, Arsht & Tunnell LLP, Wilmington, DE

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Before the kicking and screaming starts ...

- How did we end up here?
 - Transactions/circumstances that result in a company with multiple equity owners
 - Rounds/series of equity funding (e.g., venture capital)
 - Family businesses (through the generations)
 - Management/co-investors in private equity portfolio companies
 - Joint ventures
 - Relevant documentation
 - Shareholders' agreement, LLC operating agreement, partnership agreement, etc.
 - Other organizational documents
- Why did we end up here ...
 - Exit

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What defines the field of play?

- Required corporate authorization (if any)
 - Depending on the type of transaction and relevant documentation, board or equity holder approval rights may be required
 - Supermajority/blocking rights
 - Fiduciary duties
- Contractual prohibitions on transfer
- Contractual tools for exit (and terminology):
 - Right of first refusal (ROFR)
 - Right of first offer (ROFO)
 - Drag along rights
 - Tag along rights
 - Call rights
 - Force sale/marketing of the company
 - Buy/sell options
- Statutory tools
 - Merger

Private Company M&A - *Halpin*

Halpin v. Riverstone National, Inc., 2015 WL 854724 (Del. Ch. Feb. 26, 2015) (Glasscock, V.C.)

- Stockholders agreement required stockholders to tender and/or vote their shares in favor of certain change-of-control transactions that were approved by a majority of the company's stockholders (the "**drag-along**").
- Majority stockholder (91%) approved the merger by written consent and the merger closed.
- Company notified stockholders *after* closing of its exercise of the drag-along and the availability of appraisal rights, but disclosed that exercise of such appraisal rights would be a breach of the agreement.
- Minority stockholders exercised appraisal rights.
- Company sought specific performance of the drag-along, i.e., requiring stockholders to vote in favor of the merger, thereby waiving appraisal.

Private Company M&A - *Halpin*

Terms of Drag-Along

- If the majority stockholder “propose[d]” to enter into a change-of-control transaction, the Company could require the minority holders to vote and/or tender their shares in favor of the transaction so long as the minority stockholders were provided advance notice thereof.
- The agreement also gave the company a proxy to vote the minority shares.

Holding

- Drag-along not specifically enforceable because the Company did not follow the procedures set forth in the stockholders agreement.
- Drag-along operated prospectively. That is, the minority holders agreed to vote or tender in favor of a “propose[d]” merger upon advance notice thereof. **The minority holders did not agree to consent to a consummated merger after the fact.**
- Thus, the minority holders were not bound to vote or consent in favor of the merger agreement and could exercise appraisal rights without breach of the stockholders agreement.

Private Company M&A - *Halpin*

Undecided Issue

- Because the Court’s interpretation of the drag-along permitted the stockholders to exercise their appraisal rights, the Court did not need to address the argument, raised by the minority stockholders, that common holders could not waive their appraisal rights *ex ante* by contract under Delaware law.
- The Court characterized the issue as “more nuanced than is the case with preferred stockholders” and noted that no Delaware case law has decided the issue.
- The Delaware courts, however, have historically upheld common stock voting agreements and, under Delaware law, a stockholder who votes in favor of a merger agreement will not be entitled to seek appraisal rights.

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