SINGER v. MAGNAVOX CO. AND SECTION 253

BY ROBERT K. PAYSON*

MR. PAYSON: Much of what Steve Rothschild said provides a background for my focus on 253 [1] and where we now stand in light of *Singer v. Magnavox*.[2] As Steve explained, in 1957 section 253 was amended so as to authorize the acquisition with cash of a 10% or less owned subsidiary's interest, the minority shareholder's interest, by a 90% owned parent.

Let me first, for those of you who aren't familiar with the statute, explain that under section 253 a parent which owns 90% or more of a subsidiary can cash-out minority shareholders according to the terms of the statute, for cash or other consideration without prior notice to the minority shareholders. Unlike section 251,[3] the merger under 253 does not require that the merger be considered either by the directors of the subsidiary or by the shareholders of the subsidiary. Notice under the statute goes to the minority shareholders after the merger has been consummated.

In *Stauffer v. Standard Brands*,[4] a plaintiff attacked the merger on the grounds that the consideration tendered to the minority shareholders was so inadequate as to constitute fraud. The court of chancery dismissed the complaint on a motion to dismiss, holding that appraisal under section 262 [5] was complete, adequate and the exclusive remedy to any charge of a freeze-out under section 253.[6]

The supreme court affirmed that decision, but held back a little bit and said that although they cannot conceive of a type of fraud that would be necessary to successfully mount an attack on a 253 merger, this case doesn't present that. This is only a dispute as to value, and therefore appraisal provides the exclusive remedy.

Two years later in the case of *Braasch v. Goldschmidt* [7] the same chancellor who wrote the lower opinion in *Stauffer v. Standard Brands, Inc.*[8] held that the motion to dismiss would not be granted where there

---

* Admitted to Delaware Bar, 1964. Duke University, A.B. 1961; Duke University, LL.B. 1964. Fraternity: Phi Delta Phi. Deputy Attorney General, State of Delaware, 1965-1966. Member, Delaware State and American Bar Associations.

1. DEL. CODE ANN. tit. 8, § 253 (1975).
2. 380 A.2d 969 (1977).
3. DEL. CODE ANN. tit. 8, § 251 (1975).
4. 41 Del. Ch. 7, 178 A.2d 311 (1962), *aff'd*, 187 A.2d 78 (Del. 1962).
5. DEL. CODE ANN. tit. 8, § 262 (1975).
6. *Id.* § 253.
7. 41 Del. Ch. 519, 199 A.2d 760 (1964).
8. 41 Del. Ch. 7, 178 A.2d 311 (1962), *aff'd*, 187 A.2d 78 (Del. 1962).

were allegations that the parent had acquired its majority interest frauduently, or its 90% interest.

The court in the *Braasch*[9] case looked at it as a two-step transaction. If you had acquired a 90% interest unlawfully or fraudulently, the merger under 253, even though technical compliance with the statute had been accomplished, might present a cause of action assuming that the hearing on the merits of the plaintiff could in fact support the charges of fraud.

Singer[10] may, or may not, have changed the law, but I think most of the lawyers who practice corporate law and litigation thought it was established by the *Stauffer*[11] case.

Steve has indicated that he believes that *Singer* applies to section 253 mergers. It has been argued that since there is no notice required to the minority shareholders prior to the accomplishment of the merger, the legislature has created a conclusive presumption that the merger accomplished in technical compliance with the statute is not subject to attack and that appraisal is the exclusive remedy.

Kemp v. Angel,[12] which was decided after *Singer* and which Steve mentioned in his presentation, involved allegations that the parent had fraudulently acquired its 90% interest from the subsidiary pursuant to a tender offer. The argument was made in that case that because of that fraud the overall transaction should be enjoined and that the merger should not be permitted to be consummated under the short form statute.

Chancellor Marvel went farther than that. He said, "Based on *Singer* I cannot find that the fiduciary obligations of a 90 percent plus parent are any less than the fiduciary obligations of a 50 percent plus parent." Or as Steve pointed out,[13] a parent which has working control and which in fact can garner the votes necessary to accomplish a merger.

Subsequently, in *Najjar v. Roland International Corp.*[14] (and this is the case that Steve and I argued some weeks ago and were hoping that Justice Quillen would present an opinion to us this morning but we haven't seen it yet), Najjar, the plaintiff, once again alleged that under 253 the parent, which had 97.6% of the subsidiary, had accomplished the merger for an improper purpose, namely to freeze-out

9. 41 Del. Ch. 519, 199 A.2d 760 (1964).

10. 380 A.2d 969 (1977).

11. 41 Del. Ch. 7, 178 A.2d 311 (1962), *aff'd,* 187 A.2d 78 (Del. 1962).

12. 381 A.2d 241 (Del. Ch. 1977).

13. *See* address by Steven J. Rothschild, Seminar, Delaware Corporation Law—And Some Federal Considerations (Feb. 16, 1979) (reprinted in this issue, 4 DEL. J. CORP. L. — 1979).

14. 387 A.2d 709 (Del. Ch. 1978).

minority shareholders. That was the allegation, of course, that was sustained in *Singer.*

The defendants made a two-fold argument: number one, that under 253 there was a conclusive presumption of proper purpose, and that therefore appraisal was the exclusive remedy; and the second tactic by the defendants was that since the plaintiffs had not sought recision of the transaction, since it was an action only for money damages, that appraisal was the exclusive remedy.

The argument was based on the proposition that in a direct attack on the fairness of the price offered in the merger, the measure of damages would be the difference between a fair or intrinsic value of the shares and the value offered in the tender offer. That, of course, is exactly, at least according to the defendants in the *Najjar* case, the measure of the damages in an appraisal action. Therefore, it was argued that appraisal provided the exclusive remedy and that the action should be dismissed.

Vice Chancellor Brown rejected both arguments. He said in light of *Singer* that a complaint which alleges with respect to a 253 merger an improper purpose, that is to freeze-out minority shareholders and for no other purpose, may state a causative action, and the allegations are not subject to a motion to dismiss.

The case that Steven and I both indicated is now pending in the Delaware Supreme Court was argued on December 9, and since I argued the case on my birthday, I expect to have a good result.

Shortly after *Singer* and *Tanzer*[15] came down from the supreme court, I received a call from a good friend of mine in Houston, Texas, who practices as a corporate lawyer. He said that he really didn't know where to turn, that he had read the decisions and he obviously knew they applied to section 251, but he didn't know whether or not they would apply to section 253.

He said he had a number of clients going through a number of corporate transactions, and he was afraid to consummate those transactions for his clients because he was afraid that the clients would be sued, and he said that his clients didn't like to be sued. In fact, he said in light of the *Singer* and the *Tanzer* cases he felt kind of like a country dog in the city. I said, "What do you mean by that?" He said, "Well, Bob, I feel like a country dog in the city because if I stand still I get screwed, and if I move they bite me on the rear."

15. Tanzer v. International Gen. Indus., 379 A.2d 1121 (Del. 1977).