COMPANY OBLIGATIONS TO ITS STOCKHOLDERS ON A SALE OR MERGER OF THE COMPANY

Under the laws of most states, the decision to sell a company requires the approval of owners holding at least a majority of the outstanding stock of the company and sometimes an even higher percentage. For this purpose, the "sale of a company" typically includes a sale of its assets outside the ordinary course of business and a merger or consolidation with another entity that results in a change of control. Even if the required percentage of ownership interests in the company is held by a few, even a single stockholder, the company, acting through its board of directors, still has a fiduciary duty to provide the other owners with certain information. In general terms, a fiduciary duty is a duty imposed by law that requires that a person act fairly and in good faith with the persons entitled to rely upon the fiduciary. This duty includes but is not limited to full and fair disclosure of relevant facts necessary to permit the owners to make an informed business decision.

What Information Should be Provided?

The information to be provided to minority owners depends on a number of factors, including whether the owners are insiders who have access to key information by virtue of their positions as directors or executive officers of the company or they are simply passive investors. As noted above, the information provided must be sufficient to permit the minority stockholders to make an informed business decision. In general terms, this would typically include the proposed purchase price and payment terms; the structure of the transaction (e.g., whether it is taxable or non-taxable), and perhaps most importantly, any additional consideration to be received by stockholders who are on the management team (e.g., stock or options of the acquiring company, consulting fees, etc.), vis-a-vis other stockholders. It is also critically important that the information provided to minority stockholders not omit information that would make the information provided materially misleading.

Appraisal Rights

In order to better protect the minority owners, the corporation laws of most states (though not always the laws governing limited liability companies) include statutory appraisal rights. If a minority owner disagrees with the proposed price, the stockholder has a right to request an appraisal by a qualified appraiser. Appraisal rights may vary from state to state.[1] Therefore, the information provided to minority stockholders should include a detailed description of who may demand appraisal rights and the process for doing so; a copy or a detailed summary of the purchase or merger agreement and any other key documents;[2] financial and other material information regarding the acquiring company, and any potential conflicts of interest.

The failure of the company to comply with its obligations to minority owners may adversely impact the closing of the proposed transaction or result in post-closing litigation.

If you have questions on this issue or other business matters, please contact PLDO Partner William F. Miller at 508- 420-7159 or email wmiller@pldolaw.com.

[1] In a recent and fairly controversial decision, the Delaware Supreme Court ruled that a stockholder may waive its statutory appraisal rights by written agreement.

[2] Because these agreements are usually lengthy and complex, the preferred approach is usually to provide a full copy of the purchase or merger agreement, thereby eliminating the opportunity for a claim that the summary was incomplete or materially misleading.

William F. Miller
Partner

PANNONE LOPES
DEVEREAUX & O'GARA LLC
counselors at law

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