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Inadvertent Proxy Voting Instruction Results in Denial of State Law Appraisal Claim

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As reported by Ignites and the Wall Street Journal on June 1, 2016, an inadvertent proxy vote in favor of a buyout proposal for Dell Inc. (Dell), the computer technology company, resulted in the exclusion of certain mutual funds sponsored by T. Rowe Price & Associates, Inc. (T. Rowe) and other T. Rowe clients that relied on T. Rowe to direct the voting of their shares (together, the TR Petitioners) from approximately $190 million in additional sale proceeds, following the appraisal of Dell shares in a ruling by Vice Chancellor J. Travis Laster in Delaware Chancery Court on May 31, 2016 (the Appraisal Decision). In a decision earlier in May (the TR Petitioners Decision), the Delaware Chancery Court held that, because the holder of record of Dell shares for which the TR Petitioners sought appraisal did not dissent to the management-supported merger, the TR Petitioners did not satisfy the dissenter requirement under Delaware law and, consequently, could not pursue an appraisal. According to Ignites, the TR Petitioners held approximately 31 million Dell shares. Based on the evidence presented at trial, the Delaware Chancery Court concluded in the Appraisal Decision that the fair value of Dell's common stock at the effective time of the merger was $17.62 per share, not the $13.75 per share paid by Michael Dell and Silver Lake Management LLC. A discussion of the TR Petitioners Decision follows below:

On May 11, 2016, the Delaware Chancery Court issued an opinion regarding the ability of the TR Petitioners to pursue an appraisal of their Dell shares. As explained in the opinion, the buyout plan favored by Dell management was effected by a merger between Dell and three counterparties (the Merger) that gave rise to appraisal rights. The opinion states that a stockholder can pursue an appraisal only if the stockholder "neither voted in favor of the merger…nor consented thereto in writing." The appraisal statute defines the term "stockholder" as "a holder of record of stock in a corporation." The opinion states that the TR Petitioners were not holders of record for state law purposes. Instead, the TR Petitioners were beneficial owners who held their shares through a custodial bank, State Street Bank & Trust Company (the Custodian).[8] However, as the opinion notes, for purposes of Delaware law, the Custodian was not a holder of record either; it was a participant member of the Depository Trust Company (DTC), the depository institution. DTC, in turn, tracks the number of shares that each participant member holds using an electronic book entry system and, as is its practice, held the TR Petitioners' shares in the name of its nominee, Cede & Co. (Cede)[9] which was the holder of record for purposes of Delaware law and thus, had the legal right under Delaware law to vote the shares and demand appraisal.

Nevertheless, due to competing requirements and practices (including from stock exchange listing standards, federal law and contractual obligations), Cede was required to vote the TR Petitioners' Dell shares as T. Rowe directed. This resulted from what the opinion describes as a "daisy chain of authorizations": first, DTC transferred Cede's state law voting authority to the DTC participants by executing an omnibus proxy in their favor,[3] meaning voting authority for the TR Petitioners rested with the Custodian (as noted, a participant member of DTC). The Custodian, in turn, outsourced to Broadridge Financial Solutions, Inc. (the Proxy Agent), the responsibility for collecting and implementing voting instructions from its account holders, including the TR Petitioners. In order to do so, the opinion states that the Custodian gave the Proxy Agent a power of attorney authorizing the Proxy Agent to execute proxies on the Custodian's behalf, meaning voting authority for the TR Petitioners' Dell shares then rested with the Proxy Agent. The opinion further notes that the Proxy Agent fulfilled its contractual obligations to the Custodian by communicating with the Custodian's account holders and obtaining voting instructions. As to T. Rowe, this process involved an additional party, Institutional Shareholder Services Inc. (the Proxy Advisory Firm) which was retained by T. Rowe to notify the firm about upcoming votes, provide voting recommendations, collect T. Rowe's voting instructions, and convey them to the Proxy Agent.

The opinion explains that when the Proxy Advisory Firm learns that an issuer has scheduled a meeting of stockholders, its web-based delivery platform, part of a computerized system maintained by the Proxy Advisory Firm (the ISS Voting System), would notify T. Rowe by generating a communication called a meeting record. T. Rowe personnel would view the meeting record through its "Proxy Recommendation System" (the TR Voting System), which would pre-populate the meeting record with voting instructions that matched T. Rowe's standard voting policies. When T. Rowe received a meeting record, the TR Voting System would send an e-mail automatically to the portfolio managers of the T. Rowe funds who were invested in that issuer so that they could review the meeting record and determine whether to depart from T. Rowe's standard voting policies. As the opinion explains, in order to vote, a T. Rowe portfolio manager could either leave the pre-populated voting instructions in place or submit different instructions. Thereafter, once finalized, the voting instructions would be sent to the Proxy Advisory Firm. In the next stage of the voting process, the Proxy Advisory Firm conveys the voting instructions to the Proxy Agent. Based on the transfer of voting authority from Cede to the Proxy Agent, the Proxy Agent then votes the shares over which it had received voting authority in accordance with the voting instructions it had received.

The process leading to the vote of Dell shares began when Dell's board of directors approved the Merger on February 5, 2013, scheduled a meeting of stockholders for July 18, 2013 (the July Meeting) and set a record date of June 3, 2013 for the meeting. Dell filed its definitive proxy statement for the July Meeting on May 31, 2013, announcing the meeting date and record date, solicited proxies from Dell's stockholders, and asked them to vote "FOR" the Merger.

For the July Meeting, the opinion notes, the ISS Voting System generated a meeting record on July 9, 2013 (the July Meeting Record) and identified three agenda items, including approval of the merger agreement.[4] For a transaction that is supported by management, the T. Rowe default voting position was to vote "FOR" the transaction. Accordingly, the TR Voting System pre-populated the July Meeting Record with T. Rowe's default voting positions and sent an e-mail to all of the T. Rowe portfolio managers who held Dell stock in actively managed accounts. The opinion states that six of the portfolio managers decided to vote against the Merger and communicated their determinations to a T. Rowe Corporate Governance Specialist. Thereafter, on July 16, 2013, the Corporate Governance Specialist logged into the TR Voting System and changed the voting instructions in the July Meeting Record to vote "AGAINST" the Merger. Then, on the same day, relying on the voting instructions entered into the July Meeting Record by the Corporate Governance Specialist, a T.

Rowe Business Analyst entered the “AGAINST” instructions into the ISS Voting System and transmitted those voting instructions to the Proxy Advisory Firm through its web-based portal. Another T. Rowe employee e-mailed the Proxy Advisory Firm to confirm that it had received the instructions to vote “AGAINST,” which the Proxy Advisory Firm, in turn, confirmed.

The opinion states that on July 18, 2013, Dell convened the July Meeting for the sole purpose of adjourning it until July 24. The Proxy Advisory Firm updated the date of the meeting, but did not send out a new meeting record for the adjourned meeting. Nevertheless, the opinion notes, the T. Rowe Corporate Governance Specialist confirmed that T. Rowe’s instructions to vote “AGAINST” remained operative in both the TR Voting System and the ISS Voting System. Thereafter, the meeting was adjourned again until August 2. Once again, the Proxy Advisory Firm updated the date of the meeting, but did not send out a new meeting record for the adjourned meeting. As with the first adjournment, the Corporate Governance Specialist reconfirmed that T. Rowe’s instructions to vote “AGAINST” remained operative in both the TR Voting System and the ISS Voting System.

The opinion states that on August 2, 2013, Dell convened the adjourned meeting for the sole purpose of adjourning it again until September 12, 2013 (the September Meeting) and set a new record date of August 13 for the September Meeting. On August 12, the Proxy Advisory Firm updated the date of the meeting to September 12, but the ISS Voting System did not generate a new meeting record. As the opinion notes, the T. Rowe Corporate Governance Specialist confirmed for a third time that T. Rowe’s instructions to vote “AGAINST” all three proposals remained operative in both the TR Voting System and the ISS Voting System.

The opinion then notes that on September 4, 2013, the ISS Voting System generated a new meeting record for the re-scheduled meeting (the September Meeting Record). The TR Voting System showed both the July Meeting Record and the September Meeting Record. The opinion explains that in the ISS Voting System, however, the September Meeting Record replaced the July Meeting Record, which had the effect of deleting the voting instructions that had been entered in the ISS Voting System.

The TR Voting System automatically pre-populated the September Meeting Record with the default voting instructions called for by T. Rowe’s voting policies, meaning the TR Voting System populated the September Meeting Record with instructions to vote “FOR” the Merger. The opinion states that no one from T. Rowe’s proxy team logged into the ISS Voting System to check the status of T. Rowe’s voting instructions. Thus, as part of the routine operation of the two systems, the default voting policies in the September Meeting Record, including voting “FOR” the Merger, were transmitted by the Proxy Advisory Firm to the Proxy Agent. The Proxy Agent then delivered its clients’ proxies to Dell’s proxy solicitor. The Merger was approved at the September Meeting.

The opinion explains that in August 2014, in connection with the required SEC filing by eight of the TR Petitioners that are mutual funds of Form N-PX disclosing how they voted their securities during the most recent twelve-month period ended June 30, the Proxy Advisory Firm generated the forms using data pulled from the ISS Voting System. The opinion states that T. Rowe personnel checked the forms for accuracy and filed them. According to the opinion, the forms stated that the eight TR Petitioners had voted “FOR” the Merger. The opinion explains that because T. Rowe had opposed the Merger publicly, “the disclosure that eight of the [TR Petitioners] had voted “FOR” the Merger generated inquiries” and T. Rowe began to investigate what happened.

The Delaware Chancery Court determined that “Dell has proven by a preponderance of the evidence that the [TR Petitioners] shares were voted “FOR” the Merger.” Summarizing the chain of authority

regarding the TR Petitioners' vote on the Merger, the opinion states that "Broadridge [i.e., the Proxy Agent] voted those shares in favor of the Merger through the Broadridge client proxies, which exercised the voting authority that Broadridge received from State Street [i.e., the Custodian] through a power of attorney, and which State Street had received from Cede through the DTC omnibus proxy." Therefore, the Delaware Chancery Court held that because the holder of record did not dissent as to the shares for which the TR Petitioners sought appraisal, the dissenter requirement was not met and the TR Petitioners' shares did not qualify for appraisal.

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1 A footnote to the opinion notes that some of the TR Petitioners used other custodians, but the parties treated this variation as immaterial and briefed the matter as if State Street were the sole custodian, which the Delaware Chancery Court described as a "shared premise [that] simplifies one aspect of a complex situation."

2 As the opinion explains, DTC primarily holds shares on behalf of its participants in fungible bulk, meaning that all of the shares are issued in the name of Cede without any subdivision into separate accounts of the custodian's customers.

3 The opinion explains that the record holders for purposes of federal law are the DTC participants and therefore, DTC cannot simply vote the shares held in Cede's name. Therefore, to transfer its state-law voting rights to the federal-law record holders, DTC executes an omnibus proxy in favor of its participants.

4 The other two items on the agenda were: (1) an advisory vote on golden parachute compensation payable in connection with the Merger; and (2) a proposal giving Dell authority to adjourn the July Meeting. The opinion notes that T. Rowe's default voting positions were to vote "AGAINST" an advisory vote on golden parachute compensation and "FOR" the authority to adjourn.

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