

Updates

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Washington Court Reaffirms Appraisal as Remedy for Shareholders Challenging a Merger

In an unpublished decision issued on January 3, 2023, Division I of the Washington Court of Appeals strongly reaffirmed Washington law providing that, absent a showing of fraudulent corporate conduct or certain procedural irregularities, appraisal is the exclusive remedy for a shareholder of a Washington corporation seeking to challenge a corporate merger transaction. *Allentoff v. Red Lion Hotels Corp., et al.*, No. 83576-0-I, 2023 WL 21338 (Wash. Ct. App. Jan. 3, 2023). In reaching its decision, the court of appeals closely followed the important precedent established by the Washington Supreme Court in *Sound Infiniti, Inc. ex rel. Pisheyar v. Snyder*, 169 Wn.2d 199, 237 P.3d 241 (2010).[\[1\]](#)

Facts

The *Allentoff* case arose out of the merger of Red Lion Hotels Corporation (RLH) into Sonesta International Hotels Corporation. Two former RLH shareholders filed class-action complaints alleging that RLH, its directors, and its CEO had breached fiduciary duties by providing incomplete and misleading financial disclosures in the proxy statement issued in support of the merger vote. RLH responded by issuing supplemental disclosures designed to cure the alleged misrepresentations and omissions. More than 92% of the voting RLH shareholders approved the transaction. The merger transaction closed, and the RLH shareholders received \$3.50 per share, which was an 88% premium to the price of the stock before the proposed transaction was announced.

Contending that the proxy statement, even with the supplemental disclosures, was false and misleading, the shareholder plaintiffs filed amended complaints seeking "post-closing" damages. After consolidation of the two actions, the defendants moved to dismiss the amended complaints, asserting that the shareholders could not seek damages challenging the merger transaction because their sole remedy under the Washington Business Corporation Act (WBCA) is a statutory appraisal proceeding to obtain the "fair value" of their shares. The trial court granted the motion to dismiss; the court of appeals affirmed.

Washington's Statutory Appraisal Remedy

A shareholder of a Washington corporation who contends that they would not receive adequate consideration for the shares involuntarily lost as the result of a major corporate reorganization transaction, such as a merger, may challenge the transaction through a statutory appraisal process. Revised Code of Washington (RCW) 23B.13.020(1). The statutory appraisal process is the only means by which a complaining shareholder can challenge the amount of consideration for their shares. Through the appraisal process, the dissenting shareholder is entitled to receive cash value equivalent to the "fair value" of their shares immediately prior to the effective date of the challenged corporate action, excluding any appreciation or depreciation in anticipation of the corporate action.

Appraisal is the exclusive remedy available to a dissenting shareholder "unless the action fails to comply with the procedural requirements imposed by RCW title 23B, RCW 25.120.831 through 25.10.886, the [corporation's] articles of incorporation, or the bylaws, or is fraudulent with respect to the shareholder or the corporation." RCW 23B.13.020(2). In *Sound Infiniti*, the Supreme Court held that "the appraisal proceeding in RCW 23B.13.020 is a dissenting shareholder's exclusive remedy unless a corporate action is procedurally defective or fraudulent." 169 Wn.2d at 202. The Supreme Court provided examples of the limited circumstances under which a shareholder who objects to a major corporate action may pursue remedies outside the appraisal process:

If the corporation attempts an action in violation of the corporation law on voting, in violation of clauses in articles of incorporation prohibiting it, by deception of shareholders, or in violation of a fiduciary duty—to take some examples—the court's freedom to intervene should be unaffected by the presence or absence of dissenters' rights under this chapter. *Id.* at 208.

While the Supreme Court in *Sound Infiniti* did not limit to common-law actual fraud, the type of fraudulent conduct that would allow a dissenting shareholder to seek relief outside the appraisal process, it made clear that such claims must contain more than *allegations* of fraudulent conduct: a "dissenting shareholder cannot seek identical relief outside of the appraisal proceeding by merely *alleging* fraudulent conduct." *Id.* at 209 (emphasis in original). Instead, "there must still be *some* showing that the corporate action itself . . . is 'fraudulent with respect to the shareholder or the corporation.'" *Id.* (quoting RCW 23B.13.020(2) (emphasis in original)). In *Sound Infiniti*, the Supreme Court recognized that evidence of alleged fiduciary breaches by officers and directors, even if not amounting to fraud, could be considered in an appraisal proceeding if such evidence affects fair value. *Id.* at 211.

Reaffirmation of *Sound Infiniti*

Plaintiff shareholders fail to overcome the statutory presumption that appraisal is a dissenting shareholder's exclusive remedy.

In affirming that appraisal is the sole remedy for challenging an authorized corporate transaction, the court of appeals rejected the plaintiffs' contention that they only needed to allege breach of fiduciary duty or fraud by the defendants in order to pursue an action outside the appraisal process. Rather, the court "must look at the actual facts of the case to determine whether the corporate action was fraudulent." *Allentoff*, 2023 WL 21338, at *4 (citing *Sound Infiniti*, 169 Wn.2d at 209). Here, the court of appeals concluded that the shareholders' complaints presented only conclusory statements that the defendants were "dishonest," had "misled shareholders regarding critical facts," and engaged in "bad faith conduct." These allegations, the court held, "do not present facts that show fraudulent action." *Id.* at *5.

Not only did the court of appeals find that the shareholders' allegations did not present *facts* that demonstrated fraudulent conduct, but it concluded that other facts alleged in the amended complaints contradicted the shareholders' conclusory allegations of fraud. Thus, while the shareholders claimed that revenue forecasts in the proxy statement issued in support of the planned merger omitted essential information related to RLH's revenue, the court found that this information, in fact, was disclosed to RLH's shareholders in proxy materials issued before the vote on the merger proposal took place. *Id.* at *5.

Plaintiff shareholders fail to overcome the presumption that appraisal is the dissenting shareholders' exclusive remedy when the only relief they seek is monetary damages.

In addition to deciding that the plaintiff shareholders had failed to plead sufficient facts to demonstrate that RCW 23B.13.020(2)'s fraud exception applied, the court concluded that the shareholders were limited to an appraisal proceeding for the additional reason that they sought only monetary damages. The court explained: "An action for damages alone will not lie, since this would allow a dissenting shareholder, by merely alleging fraudulent or unlawful corporate conduct, to seek therein the identical relief available to him in appraisal proceedings." *Allentoff*, 2023 WL 21338, at *6 (quoting *Sound Infiniti*, 169 Wn.2d at 210-11). The court thus concluded that:

The crux of the shareholders' complaint is that they disagree with how the company was valued and the respondents' role in allowing that to happen caused shareholders to suffer a loss by not receiving a fair value for their shares. This is the classic case the appraisal process was designed to address.

Id. at *6.

Denial of Leave to Amend

Finally, the court of appeals affirmed the trial court's decision to deny the shareholders leave to amend. The shareholders' only argument in support of leave to amend was that the trial court had not stated its reason for denying leave to amend. The court held that this was insufficient, and that to obtain a reversal of the trial court's denial of leave to amend, it was incumbent on the shareholders to argue how amendment of the complaints would allow them to show a fraudulent exception to the appraisal proceeding statute—which they had not done. Under these circumstances, the court held, amendment would have been futile, a situation in which the trial court has no obligation to provide an explicit explanation for its decision to deny amendment of the complaint. *Id.* at *6.

Takeaway

Allentoff is a strong endorsement of the *Sound Infiniti* precedent that an appraisal proceeding is the exclusive remedy for a shareholder of a Washington corporation who is unhappy with a merger or similar corporate action. *Allentoff* builds on *Sound Infiniti* by providing a strong statement that a shareholder's complaint containing conclusory allegations of fraud will not suffice to get around the exclusive appraisal remedy.

Endnote

[1] Perkins Coie represented the defendants and the nominal defendant (Sound Infiniti, d/b/a/ Infiniti of Kirkland; now known as Infiniti of Bellevue) in *Sound Infiniti* and was local counsel for the defendants in *Allentoff*.

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