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No. 368A20 TWENTY-FIRST DISTRICT

SUPREME COURT OF NORTH CAROLINA

****

REYNOLDS AMERICAN INC.,

Plaintiff-Appellee,

v.

THIRD MOTION EQUITIES
MASTER FUND LTD, MAGNETAR
CAPITAL MASTER FUND, LTD.,
SPECTRUM OPPORTUNITIES
MASTER FUND LTD, MAGNETAR
FUNDAMENTAL STRATEGIES
MASTER FUNDS LTD, MAGNETAR
MSW MASTER FUND LTD, MASON
CAPITAL MASTER FUND, L.P.,
BLUE MOUNTAIN CREDIT
ALTERNATIVES FUND L.P.,
BLUEMOUNTAIN FOINAVEN
MASTERFUND L.P.,
BLUEMOUNTAIN GUADALUPE
PEAK FUND L.P.,
BLUEMOUNTAIN SUMMIT
TRADING L.P., BLUEMOUNTAIN
MONTENVERS MASTER FUND
SCA SICAV-SIF, and BARRY W.
BLANK TRUST,

Defendants-Appellants, and

From Forsyth County
No. 17 CVS 7086

ANTON S. KAWALSKY, trustee for the)
benefit of Anton S. Kawalsky Trust UA)
9/17/2015, CANYON BLUE CREDIT)
INVESTMENT FUND L.P., THE)
CANYONVALUE REALIZATION)
MASTER FUND, L.P., CANYON)
VALUE REALIZATION FUND, L.P.,)
AMUNDI ABSOLUTE RETURN)
CANYON FUND P.L.C., CANYON-SL)
VALUE FUND, L.P., PERMAL)
CANYON IO LTD., and CANYON)
VALUE REALIZATION MAC 18 LTD.,)
)
Defendants.)
)

****

PLAINTIFF-APPELLEE'S BRIEF

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VALUE FUND, L.P., PERMAL)
CANYON IO LTD., and CANYON)
VALUE REALIZATION MAC 18 LTD.,)
)
Defendants.)
)

****

PLAINTIFF-APPELLEE'S BRIEF

****

PRELIMINARY STATEMENT

On 16 January 2017, British American Tobacco p.l.c. ("BAT") and Reynolds American Inc. ("RAI") entered into a merger agreement, subject to the approval of a majority of the RAI shareholders other than BAT (the "Merger"). That agreement provided for RAI's shareholders to receive a combination of cash and BAT stock that, at the time the merger agreement was signed, was worth $59.64 per share—a 26.4% premium over the $47.17 per share trading price of RAI before BAT's first merger offer became public. The Merger resulted from three months of arm's-length negotiations between BAT and a committee of independent RAI directors (the "Transaction Committee") empowered by RAI's Board of Directors (the "RAI Board"). During the negotiations, the Transaction Committee rejected several BAT offers, and BAT raised its offer four times, resulting in approximately $4 billion in additional consideration for RAI's shareholders. RAI's shareholders, including those unaffiliated with BAT, voted overwhelmingly in favor of the deal. The Merger closed on 25 July 2017 (the "Transaction Date").

This appeal arises out of demands by certain former RAI shareholders ("Dissenters") for payment of what they contend to be the "fair value" of their RAI shares. Most of the Dissenters are hedge funds that first acquired RAI stock after BAT's offer to buy the company became public. Rather than accept the merger consideration paid to other RAI shareholders, Dissenters demanded substantially higher payments. When the parties were unable to reach agreement, RAI paid each Dissenter $59.64 per share, plus interest from the closing of the Merger, and this litigation followed.

By statute, the Business Court below was charged with determining the fair value of the shares owned by Dissenters on the Transaction Date. N.C.G.S. § 55-13-30(a). After full consideration of the evidence presented at a nine-day trial, the Business Court concluded that the $59.64 per share that RAI had already paid was equal to or greater than the fair value of RAI shares as of the Transaction Date, such that no further payment was due.

The Business Court's decision that Dissenters received fair value, if not more, for their shares of RAI is supported by a mountain of mutually reinforcing evidence. All evidence of value presented at trial, including the stock market's contemporaneous assessment of RAI's value; the deal price negotiated by an independent, sophisticated and properly motivated Transaction Committee and approved by 99% of the shares voted by shareholders other than BAT; the contemporaneous judgments of analysts and even one of the Dissenters themselves; the real-time discounted cash flow ("DCF") valuations performed by three independent and experienced financial advisors; various other real-time and expert valuations to cross-check the reasonableness of the DCFs—all of it lined up to establish that the fair value of RAI at the time the

Merger closed was no more than the $59.64 that Dissenters already received.

The only outlier was Dissenters' valuation of $92.17 per share—which, if accepted, would imply that RAI's Board, RAI's management team, three independent financial advisors, numerous stock market analysts, and the market at large all mispriced RAI stock by approximately ***$50 billion***. To support this extraordinary valuation, Dissenters asked the Business Court to ignore all other evidence of value in the record and rely *exclusively* on a DCF model prepared for this litigation by their expert. The Business Court's decision to reject Dissenters' valuation and instead credit the contemporaneous evidence was well justified and should be affirmed.

To begin with, Dissenters do not challenge the Business Court's findings of fact. Instead, on appeal, Dissenters proceed largely as if trial had not happened. Their brief presents the same version of the facts that they offered at trial, notwithstanding that the Business Court authored over 100 pages of detailed factual findings expressly rejecting Dissenters' factual narrative. Rather than challenge the Business Court's findings as clearly erroneous or insufficiently supported, Dissenters barely acknowledge that the Business Court's findings exist. Dissenters do not get a do-over of the facts. The Business Court's factual findings are well-supported and conclusive on appeal.

Those findings definitively preclude Dissenters' valuation. The Business Court found that each of the inputs into Dissenters' analysis was not supported by the record. Most critically, their expert's DCF relies on a set of financial projections that the Business Court found to be based on simple straight-line extrapolations of existing business trends, and on a growth rate that assumes there would be no material adverse developments in the future. As the Business Court aptly observed, "[a] valuation predicated upon the theory that a tobacco company like RAI will suffer no significant adverse regulatory, tax, or competitive effects in the future is simply not credible or reliable".[1] (R p 256 ¶ 254.)

Rather than simply accept Dissenters' made-for-litigation DCF, the Business Court properly recognized that there is no single path to determine fair value. It is common and appropriate for courts to use multiple valuation concepts and techniques in appraisal proceedings.

[1] Citations to "R p [ ]" are citations to the Record on Appeal and citations to "T p [ ]" are citations to the trial transcript. Citations to "DB [ ]" are citations to Defendants-Appellants' Brief, dated 21 September 2020.

When multiple methods are considered, each can serve as a sanity check on the other. That is what the Business Court did here, finding that all contemporaneous evidence of value pointed in the same direction. The Business Court was not required to jettison all of this evidence in favor of what it determined to be a flawed DCF model based on unreliable inputs put together by Dissenters' expert after the fact, solely for litigation purposes. Doing so would conflict with North Carolina cases, appraisal cases in other jurisdictions and the Official Comments to the Model Business Corporation Act ("Model Act") on which the North Carolina statute is based—not to mention plain common sense.

Dissenters' other criticisms of the Business Court and its opinion are meritless. Dissenters claim incorrectly that the Business Court failed to value RAI as of the closing date of the Merger, despite the Business Court's clear explanation that it did just that. Dissenters claim incorrectly that the Business Court's fair value opinion relied solely on the deal price, despite extensive factual findings regarding the numerous other valuation concepts and techniques previously described—market evidence, DCF analyses, precedent transactions, and even one of the Dissenters' own valuations—that support the Business Court's conclusion. Dissenters' request to be awarded a "control premium" is based on long-discredited cases from Delaware and contrary to their own expert's testimony. And Dissenters' various evidentiary challenges fare no better; they rely on legal rules of their own invention seemingly designed to strip the record of all evidence of value, except their expert's outlier calculation. The Business Court was right to reject those arguments.

The Business Court's judgment is thoughtful, comprehensive and legally sound. Dissenters have offered no basis to disturb it.

STATEMENT OF FACTS

I. GOVERNING STATUTE

This is an appeal from an appraisal proceeding governed by N.C.G.S. §§ 55-13-01 through 55-13-31. When a corporation is acquired, these statutory provisions allow shareholders that do not support the transaction to assert appraisal rights and to seek payment of fair value for their shares. The current appraisal statute was enacted in 1989 as part of an overall revision to the North Carolina Business Corporation Act, which used the Model Act as its basis. *See Beam v. Worldway Corp.*, 1997 NCBC 3, 1997 WL 33463602, at *5 (N.C. Super. Ct. Oct. 23, 1997) ("The use of the Model Act as a basis for the revisions to the Business

Corporation Act was purposeful. It helped to bring North Carolina's corporation law in closer conformity with the majority of other states.").

The statute lays out a detailed set of procedures that shareholders and corporations must follow in connection with an assertion of appraisal rights. To initiate the process, a shareholder must: (i) "[d]eliver to the corporation, before the vote [on the merger] is taken, written notice of the shareholder's intent to demand payment if the proposed action is effectuated"; and (ii) "[n]ot vote, or cause or permit to be voted, any shares of any class or series in favor of the proposed action". N.C.G.S. § 55-13-21(a)(1)-(2).

The next step in the process is assigned to the corporation. Within 10 days after the merger becomes effective, the corporation "must deliver a written appraisal notice and form [meeting certain requirements] to all shareholders who satisfied the requirements of G.S. 55-13-21". *Id.* § 55-13-22(a). If the shareholder signs and returns the appraisal form certifying "that the shareholder did not vote for or consent to the transaction", the corporation must pay the shareholder within 30 days "the amount the corporation estimates to be the fair value of their shares, plus interest". *Id.* §§ 55-13-22(b)(1), 55-13-25(a).

A shareholder dissatisfied with the amount the corporation has paid "must notify the corporation in writing of that shareholder's estimate of the fair value of the shares and demand payment of that estimate plus interest", less any payment the corporation has already made. *Id.* § 55-13-28(a). A corporation that receives such a demand must either pay the additional amount demanded or file a complaint against the shareholder within 60 days, asking the court "to determine the fair value of the shares and accrued interest". *Id.* § 55-13-30(a). A shareholder made a party to such a proceeding is entitled to judgment "for the amount, if any, by which the court finds the fair value of the shareholder's shares, plus interest, exceeds the amount paid by the corporation to the shareholder for the shareholder's shares". *Id.* § 55-13-30(e).

II. PROCEDURAL HISTORY

Dissenters are former RAI shareholders consisting primarily of hedge funds in the appraisal arbitrage business[2] who acquired their RAI stock following the public announcement of BAT's offer to acquire the company. Prior to the Transaction Date, Dissenters notified RAI that they did not wish to accept the Merger consideration and instead asserted appraisal rights under N.C.G.S. § 55-13-21 for payment of what they contended to be the "fair value" of their RAI shares. (R pp 5-7 ¶¶ 3-25, 11 ¶ 40.) In compliance with N.C.G.S. § 55-13-22, RAI sent a written appraisal notice and form to each Dissenter on the Transaction Date, 25 July 2017. (R p 11 ¶ 41.) The appraisal notice stated that RAI estimated the fair value of each share of RAI common stock to be $59.64. (*Id.*) In

[2] The practice of "appraisal arbitrage" involves "a strategy in which investors purchase shares in order to pursue appraisal". *In re Appraisal of Dell Inc.*, Consol. C.A. No. 9322-VCL, 2015 WL 4313206, at *23 (Del. Ch. July 13, 2015). Many of the appellants here are repeat appraisal dissenters. *See, e.g.*, *In re Appraisal of Solera Holdings, Inc.*, Consol. C.A. No. 12080-CB, 2018 WL 3625644, at *2 (Del. Ch. July 30, 2018) (appellants Blue Mountain Credit Alternatives Master Fund, L.P., BlueMountain Summit Trading, L.P. and BlueMountain Foinaven Master Fund, L.P.); *In re ExamWorks Grp. S'holder Appraisal Litig.*, Consol. C.A. No. 12688-VCL, 2018 WL 1008439, at *2 (Del. Ch. Feb. 21, 2018) (appellants Magnetar Capital Master Fund Ltd. and Third Motion Equities Master Fund Ltd.); *In re Dole Food Co. S'holder Litig.*, 110 A.3d 1257, 1259 (Del. Ch. 2015) (appellants Magnetar Capital Master Fund Ltd. and Spectrum Opportunities Master Fund Ltd.); *Merion Cap., L.P. v. 3M Cogent, Inc.*, C.A. No. 6247-VCP, 2013 WL 3793896, at *1 (Del. Ch. July 8, 2013) (appellant Magnetar Capital Master Fund Ltd).

September 2017, in compliance with N.C.G.S. § 55-13-25, RAI paid each Dissenter $59.64 per share, plus statutory interest that had accrued since the Transaction Date. (R pp 136-37 ¶¶ 20-25.) Dissenters thereafter notified RAI pursuant to N.C.G.S. § 55-13-28(a) that they were dissatisfied with the amount paid and demanded amounts ranging from $81.21 to $94.33 per share. (R pp 32 ¶ 46, 61 ¶ 48.)

On 29 November 2017, RAI filed a Complaint for Judicial Appraisal pursuant to N.C.G.S. § 55-13-30, seeking a determination that the fair value of RAI shares as of the Transaction Date was no more than the $59.64 per share that it already paid each Dissenter. (R pp 144 ¶ 4, 146 ¶ 9.) The case was designated as a mandatory complex business case and assigned to the North Carolina Business Court on 1 December 2017. (R pp 23-24.)

After extensive discovery, including the production to Dissenters by RAI of over 30,000 documents consisting of over 280,000 pages and the depositions of 13 current and former RAI employees, the matter was tried to the Business Court, sitting without a jury, over nine days from 10 June 2019 through 25 June 2019. (R p 145 ¶ 5.) The Business Court admitted into evidence 177 exhibits and received testimony from witnesses appearing at trial—including nine fact witnesses and four experts—as well as from additional fact witnesses appearing by video deposition testimony. (*Id.*) The parties submitted voluminous post-trial briefs and proposed findings of fact and conclusions of law, and the Business Court heard a full day of post-trial oral argument on 2 October 2019. (*Id.*)

After 130 pages of factual findings, the Business Court ultimately determined that "[t]he evidence at trial of all 'valuation concepts and techniques', 'excluding any appreciation or depreciation in anticipation of the' merger and 'without discounting for lack of marketability or minority status', establishes the fair value of RAI's shares as of the Transaction Date to be no more than $59.64 per share". (R p 313 ¶ 382 (quoting N.C.G.S. § 55-13-01(5)).) On appeal, Dissenters' lengthy Statement of Facts substantially disregards the Business Court's findings and seeks to substitute their own alternative version of the facts, which is often unsupported or even directly contradicted by the Business Court's findings. A summary of the Business Court's findings relevant to this appeal, which clarifies Dissenters' many misstatements of fact, follows.

III. TOBACCO INDUSTRY BACKGROUND

At the time of the Merger, RAI was a predominantly domestic tobacco company whose primary product was cigarettes. (R pp 147-48 ¶¶ 12-13.) The U.S. cigarette market and RAI's cigarette sales were in "structural decline", with cigarette demand and the number of cigarette consumers decreasing steadily for over 30 years. (R pp 150-52 ¶¶ 19-22.) Through price increases, acquisitions and divestitures, cost-cutting, and sound financial management, RAI "weathered the decline of the U.S. tobacco industry reasonably well". (R p 150 ¶ 17; *see also* R p 159 ¶ 33.) "The evidence showed, however, that, at the time of the Merger, the mechanisms RAI had previously employed to increase profitability and meet its [earnings per share] targets were less likely to be available in the future." (R pp 153-54 ¶ 24; *see also* R p 162 ¶ 40.)

In addition to the cigarette industry's structural decline, RAI's limited opportunities for growth and constraints on RAI's ability to increase prices and profits, "extensive evidence was introduced showing that RAI faced a number of other serious risks that had the potential to undermine the Company's future profitability or, depending on their nature and magnitude, have devastating effects on RAI's future business prospects". (R p 166 ¶ 50.) Among these risks were heightened regulation of tobacco products, increased taxation, and the threat of costly litigation. (R pp 166-75 ¶¶ 51-74.) The Business Court found that the "evidence shows that the existing and future regulation of tobacco products had the potential to substantially affect RAI's ability to increase future profits". (R p 166 ¶ 51.) For example, both sides introduced testimony regarding the potential impact of heightened regulation of menthol cigarettes on RAI's business, after which the Business Court found that "RAI's fears of future regulation were well-founded" (R p 169 ¶ 57), and that Dissenters' arguments and proffered evidence on menthol regulation (*see* DB 33-34) were unpersuasive. (R p 169 ¶¶ 58-59.) The Business Court also found that potential increases in taxation and the potential for increased litigation and settlement costs posed meaningful risks to RAI. (R pp 172-75 ¶¶ 68-74.)

IV. RAI'S PRE-MERGER TRANSACTIONS

Prior to the Merger, RAI was involved in several significant corporate transactions, most notably with Brown & Williamson Tobacco Corporation ("B&W") in 2004 and Lorillard Tobacco Company ("Lorillard") in 2015. (R pp 175-76 ¶¶ 75-78.)

In the 2004 B&W transaction, RAI was formed as a holding company for the newly combined assets of R.J. Reynolds Tobacco Company and the U.S. assets, liabilities and operations of B&W, a wholly owned subsidiary of BAT. (R pp 175-76 ¶¶ 76-77.) Through the B&W transaction, BAT became a beneficial holder of approximately 42% of RAI's common stock. (R pp 175-76 ¶ 77.) Contemporaneously with that transaction, RAI and BAT negotiated a set of contractual restrictions appearing in a "Governance Agreement" that were "designed, among other things, to maintain RAI's independence and strictly limit the influence BAT and its subsidiaries could exert over RAI". (R p 176 ¶ 79.) These restrictions included BAT's being allowed to nominate a maximum of five out of RAI's 13 directors, three of whom were required to be independent of BAT. (R p 177 ¶ 80.) For the remaining eight seats, BAT had no say on how to vote; it was required to vote its shares as directed by the RAI Board's Corporate Governance and Nominating Committee. (*Id.*) The Governance Agreement also prevented BAT from engaging in any material transaction with RAI without the approval of a majority of the independent directors on the RAI Board not nominated by BAT. (R pp 177-78 ¶ 82.) RAI also instituted a "Related Person Policy" "to foster transparency and proper governance which required various levels of review before RAI could enter into any transaction with BAT". (R p 180 ¶ 88.) This Court previously has observed, in a divided pleading-stage decision, that "the Governance Agreement placed 'contractual handcuffs' on BAT that prevented it from controlling the Reynolds board". *Corwin v. British Am. Tobacco PLC*, 371 N.C. 605, 619, 821 S.E.2d 729, 739 (2018). Here, following a full trial, the Business Court found that "notwithstanding BAT's substantial holdings in the Company, RAI had the freedom to make decisions independently from BAT". (R p 180 ¶ 87.)

Dissenters nevertheless state that in the present Merger, BAT exerted "substantial influence over RAI". (DB 23.) As support for this claim, Dissenters cite documents and testimony suggesting merely that BAT's shareholdings in RAI "could" influence matters submitted to a vote by RAI shareholders. (*Id.*) Dissenters' theorizing about possible influence by BAT is flatly contradicted by the Business Court's post-trial finding of fact that, in actuality, based on the evidence, "RAI's ability to act independently of BAT, and even in a manner contrary to BAT's wishes, was demonstrated in practice". (R p 180 ¶ 89.)

In the Lorillard transaction in 2015, RAI acquired Lorillard, including its largest brand, the menthol cigarette Newport, and simultaneously divested certain other cigarette and vapor products to a third party. (R p 176 ¶ 78.) In support of their valuation of RAI, Dissenters place great emphasis on the idea that the Lorillard transaction had a "transformational" impact on RAI's business. (DB 25-28.) The effect of the Lorillard transaction was not lost on the Business Court. Its findings took account of the Lorillard transaction's effect on RAI from a valuation perspective. In the period of time *after* the Lorillard transaction and before BAT's 20 October 2016 offer, RAI's weighted average stock price was still only $46.26, substantially below the $59.64 deal price. (R p 230 ¶ 198.) Additionally, "[b]y the time of the Merger negotiations in October 2016 . . . it appeared that RAI would no longer be able to rely on meaningful future mergers and acquisitions to overcome the effect of declining cigarette sales volumes and to increase its profitability and [earnings per share]". (R p 155 ¶ 27.)

The investment bank Lazard Ltd. ("Lazard"), which served as a financial advisor to RAI in connection with the Merger, also represented RAI in the Lorillard transaction. (R p 151 ¶ 19 n.10.) At trial, Dissenters argued that the valuation work Lazard had done during the Lorillard transaction supported their proposed fair value. (R p 272 ¶ 297.) Specifically, Lazard conducted a valuation of the combined post-transaction RAI/Lorillard entity using a DCF analysis that resulted in a valuation ranging from $60.15 to $93.39 per share. (R p 272 ¶ 296.) However, after this analysis was done, in August 2015, RAI effected a two-for-one stock split (R pp 272-73 ¶ 297)—so if a single share of RAI was worth (hypothetically) $80 before the split, it was converted to two shares worth $40 each. Accordingly, taking the split into account, Lazard's pre-split valuation actually equated to a range of $30.08 to $46.70 per share by the time of the BAT Merger. (*Id.*) Further, in performing this DCF analysis, Lazard used a projected long-term growth rate range for the combined RAI/Lorillard entity of negative 0.50% to positive 0.50%. (R p 272 ¶ 296.) Although RAI was a buyer in the Lorillard transaction but a seller in the BAT Merger, Lazard stayed consistent; its valuation work for the BAT Merger continued to use the same projected perpetual growth rate range of negative 0.50% to positive 0.50% for the same RAI/Lorillard entity (R p 262 ¶ 270)—

demonstrating that those projected growth rates were based on Lazard's best judgment rather than a desired valuation result.

Prior to the Merger, RAI met periodically with several investment banks, including the three investment banks that would eventually serve as its financial advisors in connection with the Merger. (R pp 182-83 ¶¶ 92-95.) The investment banks included Lazard, Goldman Sachs Group, Inc. ("Goldman") and JPMorgan Chase and Co. ("JPMorgan") (collectively, the "Financial Advisors"). These meetings covered topics including, among other things, potential transactions involving BAT. (R p 182 ¶ 92.) Contrary to Dissenters' suggestions otherwise (DB 36-37, 40-41), the Business Court found that "there was nothing sinister nor nefarious concerning these meetings" (R p 182 ¶ 93) and that "[t]here is no evidence anyone at RAI acted to further his or her own personal interest ahead of the Company's in the time period prior to the Merger and, in particular, in RAI's pre-Merger meetings with Lazard, Goldman, and JPMorgan" (R p 183 ¶ 96). For example, the Business Court found specifically that "[n]o credible evidence" was offered to support Dissenters' claim that RAI's CFO, Andrew Gilchrist, had "sought the investment bankers' perspectives on the amount BAT might be willing to pay in an acquisition of RAI to manipulate a potential future valuation of RAI to a value within BAT's perceived price range". (R p 184 ¶ 98.)

Ultimately, the Business Court found that:

> "RAI's separate pre-Merger meetings with Lazard, Goldman, and JPMorgan were a prudent step taken by RAI management to be better prepared for a potential offer from BAT and to be better positioned to advocate for a higher price if such an offer materialized. Rather than evidence a conspiracy to facilitate acceptance of an artificially low price, these meetings between the Financial Advisors and a variety of individuals from RAI reflect prudent scenario planning on the part of RAI's management and routine business development efforts on the part of these investment banks."

(R pp 185-86 ¶ 101.) Dissenters' claims to the contrary ignore the well-supported factual findings of the Business Court, which rejected the key narrative advanced by Dissenters at trial (and reasserted in their brief on appeal) as untrue and unsupported by the evidence.

V. THE MERGER PROCESS

The Business Court found that, together with a variety of other corroborating evidence of value, the $59.64 deal price was entitled to "substantial" weight in its fair value determination based on extensive evidence, including:

- "months of arm's-length negotiations between sophisticated parties";
- "a fully independent and well-informed transaction committee, which showed a willingness to walk away from a deal entirely and continue operating as an independent company if a fair price could not be obtained";
- "[t]hree highly respected financial advisors [that] separately concluded that the deal price was fair to RAI's shareholders"; and
- "RAI's non-BAT shareholders voted overwhelmingly in favor of the Merger".

(R p 186 ¶ 102; *see also* R pp 297-98 ¶ 347.)

A. BAT's Initial Offer

On 20 October 2016, BAT made its initial offer of a mix of cash and stock then worth $56.50 per share of RAI common stock, a nearly 20% premium to RAI's closing stock price on that day (R p 186 ¶ 103) and exceeding RAI's all-time high trading price (R p 187 ¶ 104). Dissenters state that BAT timed its offer opportunistically after a drop in RAI's stock price, based on "material non-public, value-relevant information." (DB 36-37.) However, RAI's stock had been trading "at a peak multiple in the marketplace" prior to BAT's October 20 offer, and its stock price as of that date "did not represent a substantial deviation" from its 52-week trading average and exceeded its volume-weighted average price since the closing of the Lorillard transaction. (R pp 229-30 ¶¶ 197-98.) The

Business Court also found that the supposedly "non-public, value-relevant" information identified by Dissenters either was already publicly available or otherwise would not have meaningfully affected RAI's stock price if made public. (R pp 233-35 ¶¶ 203-07.) Even Dissenters' own expert admitted that he did not have an opinion whether this information "on balance, was more negative or more positive". (R p 234 ¶ 203.) Contemporaneous commentary from financial research analysts viewed the proposed transaction positively for RAI's shareholders. (R p 189 ¶ 109.)

The letter containing BAT's 20 October 2016 offer acknowledged that any transaction would require approval by a majority of RAI's independent board members and a majority of the votes cast by non-BAT shareholders. (R p 187 ¶ 106.) Despite BAT's statement that it would not support an alternative transaction, the Business Court was satisfied that RAI's Board did not feel constrained by BAT from seeking alternatives. (R p 188 ¶ 108.) The RAI Transaction Committee and Board "reviewed alternatives to negotiating a merger with BAT" with their Financial Advisors (R p 219 ¶ 176) and "seriously considered strategic alternatives, including remaining independent from BAT"

(R p 220 ¶ 177). Among other things, the RAI Board believed that a sufficiently attractive offer from another buyer would persuade BAT to change its mind. (R p 188 ¶ 108.)

In response to BAT's offer, the RAI Board created the Transaction Committee, comprised solely of fully independent, non-BAT-affiliated directors with full authority to evaluate, negotiate and, ultimately, accept or reject the proposed BAT transaction, or any other strategic alternative. (R pp 189-90 ¶ 111.) The Transaction Committee appointed Goldman as its financial advisor (R p 191 ¶ 115), while JPMorgan and Lazard were hired as RAI's financial advisors (R p 192 ¶ 117). Dissenters suggest that the Financial Advisors' compensation structure, in which the bulk of their payment was a percentage of deal price payable on the consummation of a transaction, incented them to support the sale of RAI at a price below fair value. (DB 39-40.) The Business Court's findings directly reject this, stating that the format of the Financial Advisors' compensation "was typical in the industry" and that "there is no credible evidence that any of the Financial Advisors took any action in connection with the Merger to cause a transaction with BAT at less than fair value".

(R p 193 ¶ 119.) Once again, Dissenters ignore this well-supported finding of the Business Court that rejects their version of the facts.

B. The Information Provided to the Financial Advisors

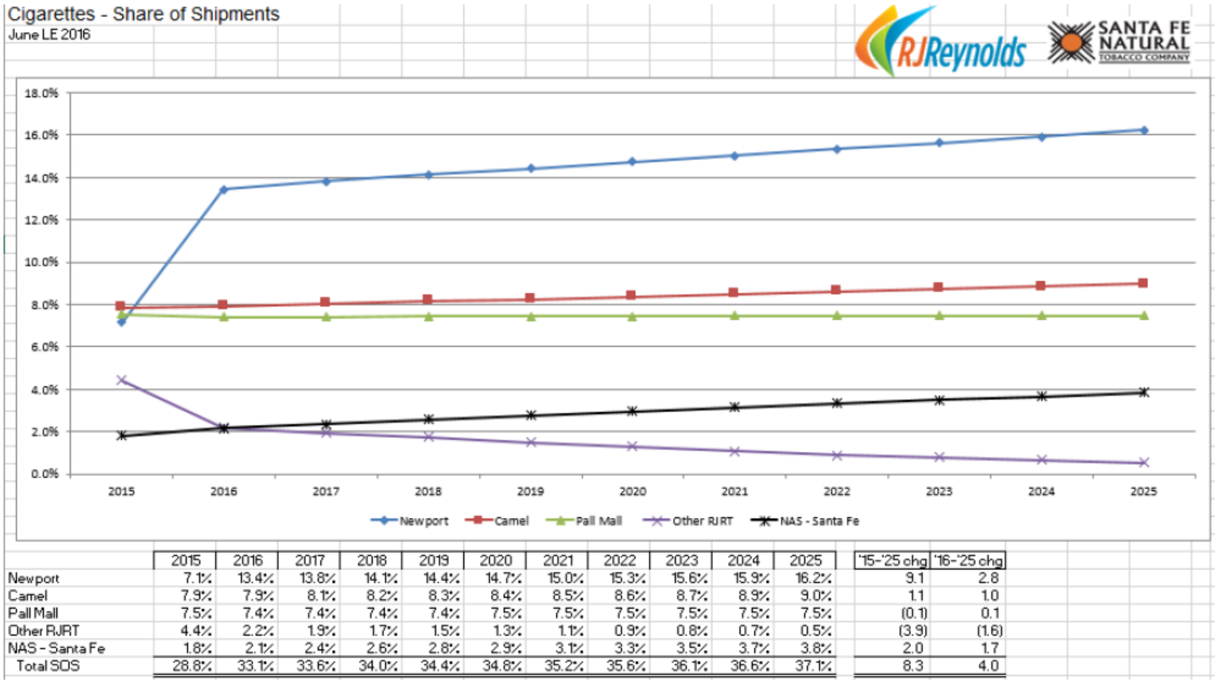
Dissenters' statement of the facts surrounding the information RAI provided to the Financial Advisors has little in common with the Business Court's findings. Instead, Dissenters spend many pages reiterating the same conspiracy theory and unsubstantiated assertions that the Business Court rejected expressly. Dissenters do not challenge the Business Court's findings as insufficiently supported by the evidence; rather, they act as if the Business Court's findings on this central issue do not exist. Because Dissenters' valuation arguments depend entirely on the information that RAI supposedly withheld from the Financial Advisors, Dissenters' misstatements must be addressed.

After BAT's 20 October 2016 offer, RAI management spent several weeks conducting diligence calls and sending information to the Financial Advisors (*see, e.g.*, R pp 207 ¶ 147, 216 ¶ 170), providing them with "whatever information they requested" (R p 223 ¶ 186). Among the information provided were projections of RAI's future financial performance. (R pp 205-06 ¶ 145.) On a monthly basis, RAI management created financial projections. (R pp 195 ¶ 124, 198 ¶ 130.) These financial projections were "assumption-based" (R p 196 ¶ 126), meaning that they were "not designed to take into account the large looming risks to the industry" (R p 196 ¶ 127) and "expressly assumed that the risks would not occur during the projection period" (R p 197 ¶ 128). Assumptions that were unknown or unquantifiable were identified as "risks" or "sensitivities", consideration of which was "critical in determining whether the projections could be reasonably relied upon". (R p 197 ¶ 129.)

Dissenters' assertion that "RAI attempted to disown its projections at trial" (DB 33) is baseless and was rejected by the Business Court. Dissenters' statement disregards the contemporaneous documentary evidence and extensive trial testimony establishing that the forecasts did not attempt to quantify the risks and sensitivities facing RAI's business. (R pp 200-01 ¶ 135.) For example, when RAI management presented the forecasts to the RAI Board, it expressly identified in writing and orally "the key assumptions underlying" the forecasts and it included a detailed set of "[p]lan risks & sensitivities". (*Id.*) The Business Court found that the exclusion of these risks and sensitivities from the projected numbers rendered the forecasts optimistic, and that ignoring those risks and sensitivities when valuing RAI would be unreasonable. (R p 197 ¶ 129.) For example, Dissenters state that the threat to RAI's business of increased regulation of menthol cigarettes (including RAI's best-selling brand) should be disregarded because RAI's ordinary course financial projections did not attempt to quantify that risk for purposes of the company's day-to-day business operations. (DB 33-35.) The Business Court found otherwise, stating that "it is not credible for a valuation of RAI to assume that a menthol ban is impossible or that such a ban would have no effect on RAI's future cash flows". (R p 266 ¶ 278.)

For some of the year, RAI's monthly projections focused on the current year plus the two subsequent years. (R p 198 ¶ 131.) In October of each year, as part of creating an "operating plan", the projections extended out for five years. (R p 199 ¶ 133.) The latter three years were not used to set RAI's budget or to set financial performance and marketplace objectives. (R p 199 ¶ 134.) Instead, they were "generally used 'as a check to make sure things are still on track'". (R p 200 ¶ 134.) Every year in June, in preparation for an annual "Strategy Day" held by the Board, RAI management prepared a set of ten-year projections.

(R p 202 ¶ 138.) In preparing these projections, “the finance team applied a ‘broad brush approach’ [and] used a ‘much higher’ materiality threshold for forecasting years three through ten”. (*Id.*) In fact, “the very foundational elements of the forecast . . . were generally extrapolations in years six through ten”. (R p 203 ¶ 141.) The projections themselves show “straight-line extrapolations” of key data:



Cigarettes - Share of Shipments
June LE 2016

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	'15-'25 chg	'16-'25 chg
Newport	7.1%	13.4%	13.8%	14.1%	14.4%	14.7%	15.0%	15.3%	15.6%	15.9%	16.2%	9.1	2.8
Camel	7.9%	7.9%	8.1%	8.2%	8.3%	8.4%	8.5%	8.6%	8.7%	8.9%	9.0%	1.1	1.0
Pall Mall	7.5%	7.4%	7.4%	7.4%	7.4%	7.5%	7.5%	7.5%	7.5%	7.5%	7.5%	(0.1)	0.1
Other RJRT	4.4%	2.2%	1.9%	1.7%	1.5%	1.3%	1.1%	0.9%	0.8%	0.7%	0.5%	(3.9)	(1.6)
NAS - Santa Fe	1.8%	2.1%	2.4%	2.6%	2.8%	2.9%	3.1%	3.3%	3.5%	3.7%	3.8%	2.0	1.7
Total SOS	28.8%	33.1%	33.6%	34.0%	34.4%	34.8%	35.2%	35.6%	36.1%	36.6%	37.1%	8.3	4.0

(*Id.*) Indeed, “[t]he fact that extrapolations provided the most fundamental inputs to years six through ten of the ten-year projections was not contradicted”. (R p 204 ¶ 142.) “RAI management and the Board considered the forecasts for years three through five to be of ever-decreasing reliability and years six through ten to be extrapolations intended to provide information about whether a continuation of existing trends would allow the Company to meet its [earnings per share] targets." (R p 203 ¶ 140.) RAI used the ten-year projections only for very limited purposes. (R p 202 ¶ 138.)

For the Financial Advisors' valuation analyses, RAI management provided the Financial Advisors with its most recent financial projections. Because BAT's offer came in October, the most recent projections available were the five-year "operating plan" projections from October 2016. (R p 206 ¶ 145.) RAI management also made adjustments to the October 2016 projections to account for events that had transpired since the projections had been prepared, as well as certain management decisions about restructuring part of the business that had not yet been made known within RAI (the "Top-Side Adjustments"). (R pp 206-07 ¶ 146.) The Top-Side Adjustments had the effect of *increasing* RAI's projected performance and therefore *increasing* any resulting valuation the Financial Advisors might reach. (R p 258 ¶ 259.)

The core of Dissenters' factual narrative—indeed, the core of Dissenters' entire case—relates to the ten-year financial projections created in June of 2016. (DB 29-31.) Dissenters contend that RAI management deliberately withheld the ten-year projections from the Financial Advisors as part of a scheme to ensure that RAI's valuation would be low enough for BAT to afford. (DB 40-41, 44-50.) In particular, Dissenters contend that the Financial Advisors were not provided with sufficiently detailed cash flow information regarding the ten-year projections that showed 7-8% growth in years six through ten, and that this knowledge would have changed the Financial Advisors' valuations. (DB 46-48.) The Business Court found this conspiracy theory "contrary to the evidence" (R p 207 ¶ 148), explaining that:

> "[L]ess than two weeks after the October 20 Offer, RAI management provided each of the Financial Advisors with the financial information given to the Board at the July 2016 Strategy Day, *including projections of operating income and growth rates for years six through ten of the June 2016 Strategic Plan*. (DX0069.0021; DX0169.0040; DX0234.0021.) The Financial Advisors were thus aware of the forecasted compound annual growth rates of 7% to 8% for the out years of those projections. A management team intent on hiding the ten-year projections would not have provided the Strategy Day presentation with the ten-year operating income and growth rates. At that point, the supposed conspiracy would have been exposed because all three Financial Advisors knew the projected trajectory and could have insisted on further detail if they believed it was necessary. *That simply did not happen here*."

(R pp 207-08 ¶ 149 (emphasis added).) What *did* happen was that, rather than providing its Financial Advisors with outdated ten-year projections from June, RAI provided them what they asked for: RAI's most recent and most reliable projections. (R pp 205-06 ¶ 145, 208 ¶ 150, 222 ¶ 185.) Because BAT's offer came in October, management provided the October projections, which were the most up-to-date projections at the time.

Dissenters' statement that the June 2016 ten-year projections ought to have been provided because they were RAI's "most recent *ten-year* projections" (DB 46-47 & n.14) was also rejected by the Business Court, which found that the Financial Advisors were comfortable using the five years of projections provided by RAI management, and that there was "no magic to ten years, seven years, five years as long as it forms a reasonable and best view". (R p 209 ¶ 153.) The Business Court also found that years six through ten of RAI's June 2016 financial projections "were less informative than the projections in the October 2016 Projections because the later years, based in large part on extrapolations of existing trends, were developed with a 'broad brush approach[,]' and used a 'much higher' materiality threshold". (R p 208 ¶ 151.) Finally, the Business Court found that "the evidence does not indicate that the Financial Advisors needed detailed ten-year projections to adequately perform their valuation analyses" (R p 208 ¶ 152) and that it was "typical when performing valuation work to receive and use five-year projections from management". (R p 210 ¶ 155.)

Dissenters' conspiracy theory also is rendered implausible by the fact that RAI management included the Top-Side Adjustments in the projections provided to the Financial Advisors. These adjustments increased RAI's projected cash flows by a total of approximately $1.4 billion. (R pp 206-07 ¶ 146, 234 ¶ 204.) This runs counter to Dissenters' conspiracy theory that RAI management sought to withhold favorable information in order to *depress* RAI's valuation so that BAT could afford to buy RAI. If that theory were true, why would RAI management include adjustments that added $1.4 billion to RAI's cash flows? Dissenters offer no explanation. (DB 41.)

Dissenters' characterization of the Financial Advisors' requests for ten-year projections from RAI management is based on cherry-picked portions of the record that, again, disregard the Business Court's findings. (R pp 207-12 ¶¶ 148-59.) Indeed, the Business Court specifically found that Dissenters' cited evidence "does not warrant a conclusion that the Financial Advisors' use of five-year projections was unreasonable; it indicates only that the Financial Advisors considered whether ten years of projections were available." (R p 257 ¶ 258.) Nonetheless, Dissenters state that Lazard and JPMorgan requested ten years of financial projections and expected RAI to provide them, only for RAI management to mysteriously withhold them, with the end result being that the Financial Advisors undervalued RAI by tens of billions of dollars. (DB 43-50.) However, as previously stated, RAI's Board and the Financial Advisors *were* provided with materials showing the 7-8% projected annual growth rate from RAI's June 2016 ten-year projections that Dissenters emphasize; the Financial Advisors could have insisted on receiving further information if they felt it was needed—but they did not make any such request. (R pp 207-10 ¶¶ 148-55.)

To summarize, the Business Court found that:

> "Considering all of the evidence, including the credibility of the relevant witnesses, the Court cannot conclude that RAI's decision to provide the Financial Advisors with the five-year October 2016 Projections rather than the ten-year projections from the June 2016 LE was calculated to deprive the Financial Advisors of important information to drive down their valuations of RAI to a range affordable to BAT. All credible evidence is to the contrary. Ultimately, the record is clear that the Financial Advisors received all the information they believed they needed for their valuation work . . . and no credible evidence was offered at trial supporting any effort by RAI management to hide information to depress the resulting valuation of the Company."

(R pp 211-12 ¶ 159.)[3]

C. RAI's Deliberations and Negotiations

After receiving BAT's 20 October 2016 offer, the Transaction Committee met numerous times with its lawyers and Financial Advisors and reviewed strategic alternatives to the BAT transaction, including whether potential alternative buyers existed (R p 219 ¶ 176), and the pros and cons of remaining independent from BAT (R p 220 ¶ 177). In November 2016, the Transaction Committee rejected BAT's offer without making a counterproposal. (R pp 217 ¶ 173, 220 ¶177.) In December 2016, BAT submitted an increased offer, which RAI again rejected without a counterproposal. (R p 217 ¶ 173.) Ultimately, BAT raised its offer four times before a final deal was reached in January 2017, after months of negotiations. (*Id.*) The final agreement provided for RAI's shareholders to receive a combination of cash and BAT stock that, at the

[3] In their brief, Dissenters hypothesize that the Business Court would have reached a different conclusion if it had been able to review BAT's internal valuations of RAI, but that Dissenters were somehow thwarted in obtaining this discovery. (DB 13.) They cite nothing in the record to support this speculation. To the contrary, Dissenters sought and obtained the Business Court's permission to take discovery of BAT in the UK. (R pp 109-14.) Having failed to pursue the opportunity the Business Court granted them, Dissenters cannot now challenge the Business Court's findings based on unsubstantiated guesses about what documents not in the record might show.

time the merger agreement was signed, was worth $59.64 per share. (R p 221 ¶ 181.) The negotiations by RAI's Transaction Committee achieved approximately $4.5 billion in additional consideration for RAI's shareholders, and a 26.4% premium over RAI's 20 October 2016 stock price. (*Id.*) Dissenters' characterization of these negotiations as "tepid back-and-forth" (DB 39) is not founded on the facts.

Dissenters emphasize that RAI's Transaction Committee did not conduct an auction or actively solicit bids from third parties. (DB 38.) However, the Business Court found that "there were few (if any) companies in the world" that could have made an offer for RAI (R p 218 ¶ 175), and that "there was no admissible evidence at trial from any source that any third party was interested in purchasing RAI with or without BAT's support". (R p 218 ¶ 174.) While Dissenters state vaguely that one company, Japan Tobacco International, had interest in acquiring RAI (DB 38), the Business Court found that Dissenters' lone hearsay statement "reporting what an unnamed person at Japan Tobacco allegedly said" was "hardly persuasive" evidence of the company's willingness to pay tens of billions of dollars to acquire RAI. (R p 294 ¶ 340.) In contrast, the Business Court identified evidence indicating that Japan Tobacco was *not* interested in acquiring RAI (R pp 219 ¶ 176, 293-94 ¶¶ 339-40), none of which Dissenters acknowledge in their brief.

Prior to the RAI Board's vote on the Merger, each of the Financial Advisors separately evaluated BAT's final offer of $59.64 and determined that price was fair from a financial point of view to the holders of RAI stock other than BAT. (R p 222 ¶ 183.) Lazard stated that it was a "landmark price", and JPMorgan described it as a "homerun transaction". (R p 226 ¶ 187.) Within the financial analyst community, there was no indication that RAI was substantially undervalued; to the contrary, some analysts "expressed concern that BAT was overpaying". (*Id.*)

The Financial Advisors' fairness opinions were supported by numerous valuation techniques that were meant to be examined together. (R pp 221-22 ¶¶ 182-84.) As illustrated by the "football field" slides that were presented by each of the Financial Advisors to the Transaction Committee and/or Board in January 2017 and are reproduced in the Business Court's opinion (R pp 223-26 ¶ 186), these mutually reinforcing valuation techniques included, among others:

- comparable companies analysis, which "involves comparing a company's valuation multiples to those of its peers" (R p 237 ¶ 212);

- precedent transactions analysis, which "involves comparing a company's multiple to the multiples of the prices paid for selected peer companies" (R p 243 ¶ 225); and

- discounted cash flow analysis, which involves estimating the present day value of RAI's future free cash flows (R p 250 ¶240).

RAI's shareholders overwhelmingly approved the deal reached by RAI's Transaction Committee. Of the non-BAT-owned shares that voted, 99% were in favor of the Merger. (R p 227 ¶ 189.) The Merger closed on 25 July 2017. (R p 227 ¶ 191.)

VI. ADDITIONAL EVIDENCE OF VALUE

The Business Court found that there was a wide variety of mutually corroborating evidence demonstrating that the $59.64 per share that RAI already paid Dissenters equaled or exceeded the fair value of RAI shares as of the date of the Merger. (R p 228 ¶ 193.) It also found that Dissenters' proposed valuation—which rested entirely on their expert's litigation-driven work—was a $50 billion outlier, and that Dissenters' proffered reasons for ignoring *all* contemporaneous evidence of value were unsupported by the record. (R pp 228-29 ¶ 195.)

A. RAI's Unaffected Stock Price

The Business Court found that RAI's stock price prior to BAT's 20 October 2016 offer was "persuasive evidence of underlying fair value". (R p 229 ¶ 196.) On 20 October 2016, RAI's common stock closed at $47.17 per share (the "Unaffected Stock Price"). (R p 229 ¶ 197.) RAI's Unaffected Stock Price "did not represent a substantial deviation" from its 52-week trading average of approximately $49.00, and represented a significant gain from the years leading up to BAT's offer. (R pp 229-30 ¶ 197.)

The Business Court also found that the evidence indicated that RAI's stock traded in an efficient market, and that there was no material non-public information that would cause RAI's fair value to differ significantly from its stock price. (R pp 232-35 ¶¶ 202-07.) As discussed further below (*see* Part II.D.2), the Business Court's market efficiency finding was based on a substantial factual record and the testimony of both sides' experts. (R pp 231-33 ¶¶ 199-202.) No evidence was introduced indicating that RAI's stock possessed characteristics indicating that it did not trade efficiently. (R pp 231-32 ¶ 201.) The Business Court's factual findings supporting market efficiency included:

- RAI's stock being publicly traded in high volumes and with high liquidity on the New York Stock Exchange;
- RAI's very large ($67.3 billion) market capitalization;
- Wide availability of information about RAI;
- RAI's stock price moving in response to the release of new information and market-wide trends;
- Coverage by 16 well-informed analysts who frequently published information about RAI; and
- The absence of a controlling shareholder.

(R pp 232-33 ¶ 202.)

B. RAI's Adjusted Unaffected Stock Price

To account for developments occurring between the Unaffected Stock Price date of 20 October 2016, when BAT made its first offer, and the 25 July 2017 closing of the Merger on the Transaction Date, RAI's expert, Professor Paul Gompers, calculated an "Adjusted Unaffected Stock Price".[4] He started with RAI's stock price on 20 October 2016, and indexed it to the performance of RAI's closest competitor, Altria, from that date through 24 July 2017. (R pp 236-37 ¶ 210.) Given the increase

[4] It would not have been appropriate to use RAI's actual trading price in July 2017, because the stock was at that point trading based largely on the price of the Merger. (R pp 235-36 ¶ 208.)

in Altria stock over that period, that analysis led to an implied Transaction Date trading price of RAI stock of $55.33 per share. (*Id.*) Gompers also indexed RAI's 20 October 2016 stock price to the performance of the S&P 500, which led to an implied Transaction Date trading price of $53.78 per share. (*Id.*) These analyses were reasonable proxies for how RAI stock would have traded because "no evidence was offered of a material, value-relevant event between October 20, 2016 and July 25, 2017 that affected RAI separately from the tobacco industry or the market as a whole". (R p 236 ¶ 210 n.38.) The Business Court found that Gompers's Adjusted Unaffected Stock Price analysis provided evidence that "while RAI's stock price may have appreciated to some degree in the time between the October 20 Offer and the Transaction Date, RAI's stock would still have traded 7% to 10% below the deal price as of July 24, 2017" and thus persuasively "suggests that the deal price is consistent with, and Dissenters' proposed valuation is inconsistent with, RAI's fair value on the Transaction Date". (R p 237 ¶ 211.)

C. Comparable Companies Analysis

The Business Court found that comparable companies analyses performed by Lazard and JPMorgan, and by RAI's expert Gompers, provided helpful context in checking the results of other valuation techniques. (R pp 242-43 ¶ 224.) Comparable companies analysis involves comparing RAI's trading multiple to those of its peers. (R p 237 ¶ 212.) Lazard's and JPMorgan's comparable companies analyses resulted in valuation ranges below $59.64 (R p 238 ¶ 215), and Gompers demonstrated that Dissenters' proposed $92.17 valuation implied an unrealistic multiple for RAI that was double its closest peer, Altria (R p 242 ¶ 223). The Business Court ultimately found that "comparable companies analyses performed by RAI's Financial Advisors and by Gompers provide relevant information that, when considered in connection with other valuation concepts and techniques, support a conclusion that [Dissenters'] $92.17 per share valuation is excessive". (R pp 242-43 ¶ 224.)

D. Precedent Transactions Analysis

The Business Court also considered precedent transactions analyses conducted by the Financial Advisors. (R p 247 ¶ 233.) Precedent transactions analysis "involves comparing a company's multiple to the multiples of the prices paid for selected peer companies". (R p 243 ¶ 225.) Each Financial Advisor independently performed a precedent transaction analysis that resulted in a valuation range consistent with the $59.64 deal price. (R pp 243-44 ¶ 226.) Indeed, Lazard found that the price RAI received from BAT was at a higher multiple than any other prior transaction involving a U.S. tobacco company. (R pp 246-47 ¶ 233.) While the Business Court ultimately determined that, for purposes of its valuation, precedent transactions analyses performed by the Financial Advisors and Gompers were of limited value due to "differences in the selected transactions", it nonetheless found that these analyses "provide[d] support that the deal price of $59.64 was at or above RAI's fair value and that [Dissenters'] valuation was clearly excessive". (R p 247 ¶ 233.)

E. Financial Analyst Price Targets

The Business Court found that financial analysts' price targets for RAI's stock supported the $59.64 deal price; no analyst indicated that BAT was "getting a steal" at that price. (R p 247 ¶ 234.)

F. Mason Capital's Valuation

Absent from Dissenters' Statement of Facts is a valuation that one of the Dissenters, Mason Capital, sent—twice—to RAI's Transaction Committee in November 2016. (R p 248 ¶¶ 235-36.) At that time, Mason Capital valued RAI at $54.44 per share. (R p 248 ¶ 236.) A representative from Mason Capital testified at trial that this $54.44 valuation represented its best view of the actual value of a share of RAI's stock (R p 249 ¶ 237) and that this valuation was not depressed on account of any overhang or minority discount (R p 249 ¶ 238). The Business Court found that "[t]he substantial discrepancy in Mason Capital's contemporaneous and litigation-driven valuations of RAI's shares undermine[s] the credibility and reliability of the latter". (R pp 249-50 ¶ 239.)

STANDARD OF REVIEW

"When a trial court sits without a jury, findings of fact are conclusive on appeal if supported by any substantial evidence." *Farm Bureau Mut. Ins. Co. v. Cully's Motorcross Park, Inc.*, 366 N.C. 505, 512, 742 S.E.2d 781, 786 (2013) (internal quotation marks omitted); *see also Winston Affordable Hous., LLC v. Roberts*, 374 N.C. 395, 402, 841 S.E.2d 267, 273 (2020) ("When reviewing a judgment entered following a bench trial, 'the trial court's findings of fact have the force and effect of a jury verdict and are conclusive on appeal if there is competent evidence to support them.'" (quoting *Bailey v. State*, 348 N.C. 130, 146, 500 S.E.2d 54, 63 (1998))). That is true even where "the evidence could be viewed as supporting a different finding". *Winston*, 374 N.C. at 402, 841 S.E.2d at 273. When a party has failed to challenge the findings of fact, the findings are binding on the appellate court. *See Scarborough v. Dillard's, Inc.*, 363 N.C. 715, 722, 693 S.E.2d 640, 644 (2009). "The trial court's legal conclusions are reviewed de novo." *Winston*, 374 N.C. at 403, 841 S.E.2d at 273.

As recognized by other appellate courts reviewing fair value determinations under appraisal statutes that, like North Carolina's, are patterned on the Model Act, "[a] fair value determination is necessarily a fact-specific process", *HMO-W Inc. v. SSM Health Care Sys.*, 234 Wis. 2d 707, 729, 611 N.W.2d 250, 260 (Wis. 2000), and "[a]n appellate court does not substitute its judgment for that of the trial court in a factual dispute over the valuation of property", *EagleView Techs., Inc. v. Pikover*, 192 Wash. App. 299, 309, 365 P.3d 1264, 1270 (Wash. App. 2015). Accordingly, while "the determination of whether a given fact or circumstance is relevant to fair value . . . is a question of law" reviewed de novo, "the ultimate determination of fair value is a question of fact" subject to deference on appeal. *Swope v. Siegel-Robert, Inc.*, 243 F.3d

486, 491, 494 (8th Cir. 2001) (reviewing fair value determination under Missouri's appraisal law).

ARGUMENT

The Business Court determined, based on an extensive evidentiary record, that the fair value of RAI shares as of the Transaction Date was "no more than" the $59.64 that RAI had already paid Dissenters (plus interest) in September 2017 pursuant to N.C.G.S. § 55-13-25. The Business Court's detailed factual findings powerfully support its fair value determination and show Dissenters' $92.17 valuation—an approximately ***$50 billion*** increase over the transaction price—to be entirely unrealistic.

Rather than challenge the Business Court's factual findings, Dissenters largely ignore them. They instead base their appeal on their own alternative version of the facts, without any acknowledgement that they presented the same factual contentions at trial and that the Business Court repeatedly found Dissenters' view to be unsupported or contradicted by the evidence. As one key example, Dissenters' valuation rests entirely on their expert's discounted cash flow ("DCF") model, which uses a perpetuity growth rate derived from the ten-year projections from

RAI's 2016 Strategy Day. But the Business Court expressly found those ten-year projections to be unsuitable for use in valuing RAI, based on exhaustive findings as to the manner in which those projections were prepared and the limited purpose for which they were intended to be used. Dissenters' failure to challenge those factual findings, which are amply supported in the record, dooms Dissenters' DCF model and by extension dooms their case. Dissenters cannot sidestep the Business Court's factual findings by pretending they do not exist. (*See* Part I below.)

Dissenters' other main strategy on appeal is to mischaracterize the Business Court's analysis. They repeatedly accuse the Court of doing things it did not do. For example, as shown below, the Business Court did not value RAI as of the wrong date, did not "defer[] entirely" to the negotiated deal price and did not "confuse" fiduciary duty law with appraisal law. (DB 4, 16.) These unfounded criticisms of the Business Court's analysis should be rejected. What remains are an assortment of arguments about economic theory and challenges to evidentiary rulings, none of which warrants disturbing the judgment below. (*See* Parts II-III below.) Dissenters also advance a truly frivolous claim for a windfall of over $100 million in supposed "interest", which they say they are owed even if (as the Business Court found) RAI paid them, in a timely fashion, an amount equal to or exceeding the fair value of their shares. (*See* Part IV below.)

I. THE BUSINESS COURT MADE A WELL-SUPPORTED DETERMINATION OF FAIR VALUE USING CUSTOMARY AND CURRENT VALUATION CONCEPTS AND TECHNIQUES.

The careful and thorough opinion that the Business Court issued—as contrasted with the caricature of that opinion depicted in Dissenters' brief—is firmly grounded in the North Carolina appraisal statute, customary and current valuation concepts and techniques and the trial record.

A. The Appraisal Statute Does Not Limit the Customary and Current Valuation Concepts and Techniques a Court May Use.

Appraisal is, by design, a flexible process. Under N.C.G.S. § 55-13-01(5), fair value is to be assessed as of the closing of the transaction (i) "excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable"; (ii) "using customary and current valuation concepts and techniques"; and (iii) "without discounting for lack of marketability or minority status".

As noted by the Business Court, the statute "does not limit or prescribe the specific 'valuation concepts and techniques' that the Court may use, and requires only that they be 'customary and current' and 'generally employed for similar business in the context of the transaction requiring appraisal'". (R p 283 ¶ 321 (quoting N.C.G.S. § 55-13-01(5)).) In the words of the Supreme Court of another state with an appraisal statute that, like North Carolina's, is patterned on the Model Act: "As we have observed on prior occasions, there is no predominant formula for arriving at fair value." *Sieg Co. v. Kelly*, 568 N.W.2d 794, 798 (Iowa 1997). The notes to the Model Act expressly recognize this flexible approach to valuation:

> "Clause (ii) of the definition of 'fair value' . . . adopts the view that different transactions and different contexts may warrant different valuation methodologies. Customary valuation concepts and techniques will typically take into account numerous relevant factors, and will normally result in a range of values, not a particular single value."

Model Bus. Corp. Act § 13.01 cmt. 2 (1969) (Am. Bar Ass'n, amended 2016).

Given the capacious definition of "fair value" and the absence of binding North Carolina authority determining fair value under N.C.G.S.

§ 55-13-30,[5] the Business Court sensibly considered case law from other states that have adopted appraisal statutes patterned on the Model Act, as well as Delaware, which has a large body of appraisal law and to which North Carolina courts often look for guidance in the corporate law context,[6] to survey "customary and current" valuation concepts and techniques:

> "In the merger context, courts, economists, and valuation professionals customarily and currently use a wide range of valuation concepts and techniques, including but not limited to assessing market evidence of the value of the shares, assessing whether the transaction process was one in which the resulting deal price is a reliable indicator of value, reviewing internal valuations performed by the company prior to consideration of the merger, estimating the net present value of the company's expected future cash flows (a DCF analysis), comparing the company's trading multiples to the trading multiples of similar firms, and comparing the multiples paid in the merger to the multiples paid in similar transactions."

[5] (*See* R p 277 ¶ 312 (citing Russell M. Robinson, II, *Robinson on North Carolina Corporation Law* § 27.04 (7th ed. 2017) ("There is no reported appellate North Carolina decision determining the fair value of shares in an appraisal proceeding.")).)

[6] *See, e.g.*, *Energy Invs. Fund, L.P. v. Metric Constructors, Inc.*, 351 N.C. 331, 334-35, 525 S.E.2d 441, 443 (2000) (noting that the Chancery Court of Delaware is "generally recognized as an authority in the interpretation of business law"); *Corwin v. British Am. Tobacco PLC*, 371 N.C. 605, 613, 821 S.E.2d 729, 735 (2018) (finding Delaware caselaw to be persuasive).

(R pp 283-84 ¶ 322 (citing *Sieg* 568 N.W.2d at 798, and *In re Appraisal of Dole Food Co.*, 114 A.3d 541, 550 (Del. Ch. 2014)).)

The Business Court's conclusion as to what constitutes "customary and current valuation concepts and techniques" was well grounded in the factual record and in the law. In terms of the factual record, both the Financial Advisors and the parties' experts testified as to the valuation analyses and methods that are used in the ordinary course of business by practitioners. For example, there was evidence that valuation professionals and financial economists regularly consider market-based metrics, such as the trading price of a company's stock and the value an asset receives in an arm's-length transaction. (*See, e.g.*, T p 784:3-6 ("if the market is efficient and there's no material, nonpublic information, then the market price will be the best estimate of a firm's . . . intrinsic or fundamental value"); *see also* R pp 228 ¶¶ 193-94, 229 ¶ 196.) There was also evidence that valuation professionals and financial economists regularly consider more theoretical approaches, such as DCF valuations, comparable companies analyses and precedent transactions analyses. (*See, e.g.*, T pp 227:25-229:14, 771:7-24, 779:25-780:16, 1287:8-21; *see also* R pp 237 ¶ 212, 243 ¶ 225, 250 ¶ 240.) The evidence showed that properly conducted valuations require consideration of *multiple* approaches. (*See, e.g.*, T pp 813:22-814:4 (expert testimony that a DCF valuation is "only as good as the inputs" and "without doing an analysis of checks [on those DCF inputs], you can't be certain that your inputs are correct"); T p 1449:3-8 (JPMorgan representative's testimony that JPMorgan conducted valuations of RAI using a DCF valuation, comparable companies and precedent transactions "as a means of being complete and looking at as many accepted valuation methodologies in the context of looking at the value of a publicly-traded company" and that "it would be atypical for us to do anything but look at all three of those valuation methodologies in the context of providing an opinion"); *see also* R p 222 ¶ 184.) There are "various sanity checks that *Dissenters' experts agree* are a typical part of the valuation process". (R pp 274-75 ¶ 302 (emphasis added).)

As a legal matter, there is extensive support for considering, as part of an appraisal proceeding, valuation methods other than the expert-driven DCF that Dissenters tout as the *only* permissible means of conducting an appraisal. For example, appraisal courts consider the trading price of a corporation's stock. *See, e.g.*, *Verition Partners Master*

Fund Ltd. v. Aruba Networks, Inc., 210 A.3d 128, 138 (Del. 2019) ("[T]he price a stock trades at in an efficient market is an important indicator of its economic value that should be given weight."); *In re Appraisal of Jarden Corp.*, Consol. C.A. No. 12456-VCS, 2019 WL 3244085, at *27 (Del. Ch. July 19, 2019) ("When the market is efficient, the trading price of a company's stock can be a proxy for fair value."), *aff'd*, 236 A.3d 313 (Del. 2020). As discussed further below (*see* Part II.C), appraisal courts also consider the deal price arrived at by an independent, diligent and properly motivated board of directors. *See Dole*, 114 A.3d at 559 ("[T]he fact that a transaction price was forged in the crucible of objective market reality (as distinguished from the unavoidably subjective thought process of a valuation expert) is viewed as strong evidence that the price is fair.").

While Dissenters contend that the structure of the North Carolina appraisal statute makes it inappropriate to consider a negotiated deal price (DB 9-10, 73-74), the notes to the Model Act, on which North Carolina's appraisal statute is based, state otherwise. The notes provide that "[a] court determining fair value . . . should give *great deference* to the aggregate consideration accepted or approved by a disinterested board of directors for an appraisal-triggering transaction". (R p 285 ¶ 324 (quoting Model Bus. Corp. Act § 13.01 cmt. 2 (1969) (Am. Bar Ass'n, amended 2016)) (emphasis added).) The Business Court was correct to reject Dissenters' contention that an assessment of deal price in determining fair value is not a "customary and current valuation concept technique" under § 55-13-01(5), finding that argument "has no support in North Carolina case law and is squarely refuted by the legislative history reflected in the Model Business Corporation Act commentary". (R p 285 ¶ 324 n.46.) Dissenters acknowledge the relevance of the Model Act commentary as a general matter, because they rely on it for other purposes elsewhere in their brief on appeal (*see* DB 62), but they ignore it here. Their insistence that deal price is categorically irrelevant in North Carolina cannot be reconciled with this legislative history. In fact, Dissenters have not identified *any* authorities supporting their novel interpretation of the statute.[7]

Courts may also consider more theoretical "valuation concepts and techniques" such as analyses of comparable companies, comparable

[7] Dissenters' broadside challenge to the relevance of deal price is also contradicted by appraisal cases from other Model Act states in which deal price was given substantial if not dispositive weight. *See, e.g.*, *TWC I, LLC v. Damos*, 870 N.W.2d 274, at *3 (Iowa Ct. App. 2015) (finding no error in the trial court's consideration of the deal price); *see also Ely, Inc. v. Wiley*, 587 N.W.2d 465, 469 (Iowa 1998).

precedent transactions and DCF analyses, but the weight and utility of these methodologies will depend on the specific circumstances of the case. They are generally given less weight in cases like this one where there was an active public market for the stock and a robust deal process. *See, e.g.*, *DFC Glob. Corp. v. Muirfield Value Partners, L.P.*, 172 A.3d 346, 370 (Del. 2017) ("[A] singular discounted cash flow model is often most helpful when there isn't an observable market price."); *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*, 177 A.3d 1, 37-38 (Del. 2017) ("Although widely considered the best tool for valuing companies when there is no credible market information and no market check, DCF valuations involve many inputs—all subject to disagreement by well-compensated and highly credentialed experts—and even slight differences in these inputs can produce large valuation gaps."); *In re Appraisal of Columbia Pipeline Grp.*, Consol. C.A. No. 12736-VCL, 2019 WL 3778370, at *51-52 (Del. Ch. Aug. 12, 2019) ("*Dell* and *DFC* teach that a trial court should have greater confidence in market indicators and less confidence in a divergent expert determination . . . . Consistent with the Delaware Supreme Court's observations in *Dell* and *DFC*, [petitioners' expert's] DCF valuation had many inputs, and [the company's expert] questioned a number of them. The proper choices were matters of legitimate debate, and the outcome of those debates generated large swings in the valuation output. . . . The wide swings in output that result from legitimate debate over reasonable inputs undermine the reliability of [petitioners' expert's] DCF model."); *Union Ill. 1995 Inv. Ltd. P'ship v. Union Fin. Grp., Ltd.*, 847 A.2d 340, 359 (Del. Ch. 2004) ("In view of the market's opportunity to price UFG directly as an entity, the use of alternative valuation techniques like a DCF analysis is necessarily a second-best method to derive value.").

Moreover, "those knowledgeable about valuation recognize that the field is as much art as science". *Dole*, 114 A.3d at 553 n.7. It is therefore appropriate to cast a skeptical eye on the use of any one approach to the exclusion of all others, particularly when that approach purports to identify with precision a value that is far out of line with all other evidence. *Id.* at 557 ("Rather than supporting the petitioners' idealized depiction of valuation as a scientific process that should be reserved exclusively for neutral opiners, the martial metaphor suggests the need to consider other evidence as a check on the warring experts' models."). Even where the parties have retained credible experts, the court should consider "factual evidence relating to valuation as a cross-check, or reality-check, on the litigation-driven figures generated by [those] experts." *Id.* at 550. That is all the more important here, where Dissenters' DCF model produces a valuation that is so out of line with all other evidence of value in the record and implies a mispricing of RAI that—so far as either side has been able to determine—would be larger than in any other reported appraisal case, anywhere in the country, ever. (*See* R p 274 ¶ 302.)

Dissenters' interpretation of the statute, which would limit the contemporaneous information the Court can consider and would force it to rely exclusively on expert calculations performed after the fact for litigation, is formalistic, wooden and divorced from the reality of valuation. There is no single scientific way to get to one number when assessing fair value. As the Business Court properly concluded, there are multiple "customary and current valuation concepts and techniques" that a reviewing court can and should consider.

B. Substantial Evidence Supports the Business Court's Factual Findings Relevant to Value.

As the Business Court found, every credible indicator of value in the record supported RAI's valuation and showed Dissenters' valuation to be an "extreme outlier". (R pp 274-75 ¶ 302.) The evidence on this score is overwhelming and described at length in the Business Court's opinion, which includes nearly 300 paragraphs of comprehensive and meticulously cited factual findings. Rather than grapple with these findings, Dissenters attempt to discredit the indicators of value on which the Business Court relied by rehashing factual contentions that the Court squarely rejected. But the Business Court's post-trial "findings of fact . . . are conclusive on appeal if there is competent evidence to support them". *Winston*, 374 N.C. at 402 (quoting *Bailey*, 348 N.C. at 146). In this case, there is a wealth of such competent evidence to support each of the indicators of value identified by the Business Court.

At trial, RAI introduced evidence using several customary and current valuation concepts and techniques, including:

- the real-time discounted cash flow ("DCF") valuations performed by three independent and experienced sets of financial advisors, along with various other real-time and expert analyses to cross-check the reasonableness of the DCFs;

- the stock market's contemporaneous assessment of RAI's value, taking into account the events between the signing of the deal and the Transaction Date;

- the deal price negotiated by an independent, sophisticated and properly motivated Transaction Committee; and

- the contemporaneous judgments of analysts, shareholders and even one of the Dissenters.

In arriving at its conclusion, the Business Court evaluated all of this evidence carefully and found it to be consistent and mutually reinforcing, with Dissenters' litigation-driven analysis the sole and clear outlier.

1. Discounted Cash Flow Analyses and Cross-Checks

The parties agree that a DCF valuation is an appropriate method for valuing a company's shares. (R p 250 ¶ 240.) The parties likewise agree that the primary inputs into a DCF valuation are (i) projections of the company's financial performance for a period of years, (ii) an estimated rate of growth for the period of time following the years covered by the projections, and (iii) a discount rate to bring the projected future cash flows back to a net present value. (*Id.*; DB 107 n.30.) Where they disagree is on the appropriate inputs to use in valuing RAI—an issue that was the subject of extensive factual development at trial and detailed findings by the Business Court. On each input, the Business Court made factual findings that support the contemporaneous DCF analyses relied on by RAI and dismantle the supposed reliability of the made-for-litigation DCF presented by Dissenters' expert—which is the *only* basis for their valuation.

This alone should be dispositive of Dissenters' appeal. Their sole valuation method is based on inputs that the Business Court found to lack factual support, and they do not challenge the Court's factual findings on that score. By contrast, RAI presented at trial the contemporaneous DCF analyses conducted by its three Financial Advisors, which in one case yielded per-share value ranges of $45.16 to $72.17, with a midpoint of $55.74; in another case yielded per-share value ranges of $47.54 to $68.63, with a midpoint of $56.26; and in the third case yielded per-share range values of $50.03 to $73.38, with a midpoint of $59.59. (R p 251 ¶ 243.) The Business Court found that the inputs into these DCFs were well-supported by the record and that the analyses are "reliable and constitute persuasive evidence that the fair value of RAI's shares as of the Transaction Date was at or below the deal price of $59.64 per share". (R p 305 ¶ 363.) There was ample evidence for that finding, as shown below with respect to each of the inputs into the Financial Advisors' DCFs.

(i) The Business Court's Factual Findings Support the Financial Advisors' Use of the October 2016 Projections.

The first input into a DCF analysis is a set of projections of the company's future financial performance. The Financial Advisors' DCFs used five-year management projections prepared in October 2016, as supplemented by additional "Top-Side Adjustments" that had the effect of increasing the projections by approximately $300 million per year and therefore increasing the DCF value. (R p 253 ¶ 247; R pp 205-06 ¶¶ 145-46.) The Business Court found that "the Financial Advisors' use of the October 2016 Projections as an input in their DCF calculations was reasonable". (R p 259 ¶ 262.) Those projections "were RAI's most current financial projections at the time, and RAI management supplemented those projections with a wealth of additional information for the Financial Advisors' consideration". (*Id.*)

Indeed, the evidence showed that, if anything, the October 2016 Projections were optimistic. The financial projections "used in a DCF analysis must be probability-weighted, or risk-adjusted, to reflect the expected value of the future cash flows". (R p 251 ¶ 244.) As the Business Court found, however, "RAI's regular financial projection process was not intended to create a probability-weighted value of future cash flows, but instead expressly assumed that current industry trends and dynamics would continue without substantial change". (R p 252 ¶ 245.) RAI's projections "were subject to specifically identified sensitivities that were not reflected in the numerical forecasts. These sensitivities included major competitive, regulatory, litigation, or other exogenous shocks." (R p 254 ¶ 250.) While some of these sensitivities might have led to increased cash flow, "the evidence was clear that the upside and the downside to the management forecasts do not 'offset each other', because the downside was much more serious, meaning that the forecasts are more optimistic than the expected cash flows". (R p 256 ¶ 255.) "For these reasons, the RAI Board and management recognized that the projections were optimistic and biased upwards." (R p 255 ¶ 251.)

On appeal, Dissenters respond with a series of factual contentions already rejected by the Business Court's findings. *First*, they argue that the Financial Advisors wanted and needed ten years of projections to do their DCFs, but that RAI management "withheld" that information in order to cause the Financial Advisors to arrive at a lower valuation. (DB 40-50.) The Business Court definitively rejected this outlandish conspiracy theory. "[T]here is no evidence to support Dissenters' contention that RAI deliberately withheld ten-year projections to drive a lower valuation within BAT's price range." (R p 256 ¶ 256.) On the contrary, "the evidence shows that RAI management was actually advocating for a *higher* valuation and the *highest* possible purchase price for the Company". (R p 258 ¶ 259 (emphases in original).) For example, not only did management provide the Financial Advisors with the value-increasing Top-Side Adjustments, but "when negotiations between RAI and BAT had reached an impasse in December 2016, RAI management assisted the Financial Advisors in providing information to BAT intended to support a higher valuation than BAT's models showed". (R p 258 ¶ 261.)

Moreover, "[d]espite Dissenters' arguments to the contrary, the record is clear that the Financial Advisors received all the information they believed they needed for their work". (R p 257 ¶ 258.) "[E]ach Financial Advisor testified unequivocally that the information it received from RAI management, including the five-year October 2016 Projections, was entirely sufficient to adequately and competently perform the Advisor's valuation analysis." (R pp 256-57 ¶ 256.) In addition, contrary to Dissenters' repeated assertions that the Financial Advisors were unaware of the growth reflected in the ten-year Strategy Day projections, the Business Court found the exact opposite: "[L]ess than two weeks after the October 20 Offer, RAI management provided each of the Financial Advisors with the financial information given to the Board at the July 2016 Strategy Day." (R p 207 ¶ 149.) On this basis, the Business Court concluded that the Financial Advisors "were . . . aware of the forecasted compound annual growth rates of 7% to 8% of the out years of those projections" and they "could have insisted on further detail if they believed it was necessary". (R pp 207-08 ¶ 149.) Instead, "the evidence does not indicate that the Financial Advisors needed detailed ten-year projections to adequately perform their valuation analyses. Indeed, representatives from Goldman, Lazard, and JPMorgan each testified that such information was unnecessary." (R pp 208-09 ¶ 152.) Dissenters' brief does not challenge or even mention any of these factual findings.

There is yet another fundamental problem with Dissenters' insistence that the Financial Advisors should have used the June 2016 ten-year projections: the factual findings of the Business Court demonstrate that the ten-year projections were "unsuited for valuation analysis". (R p 305 ¶ 364.) This point bears repeating. Dissenters repeatedly characterize the ten-year projections as "*critical* value-relevant information" that should have been used in valuing RAI. (DB 49 (emphasis in original); *see also* DB 11.) Dissenters' valuation depends on accepting those ten-year projections as reliable estimates of RAI's future cash flows. Argument after argument in Dissenters' brief hinges on the ten-year projections. (*See, e.g.*, DB 90 (claiming that "the unaffected market price of RAI stock could never have been a fair measure of inherent value because it failed to incorporate" the growth projections in years six through ten of the ten-year projections); DB 114 (asserting that Dissenters' expert used the most appropriate long-term growth rate because it was based on the ten-year projections).)

But after hearing the evidence at trial, the Business Court made a series of factual findings that render Dissenters' reliance on the ten-year projections unsustainable. "In preparing the June LE [the ten-year projections], the finance team applied a 'broad brush approach'" (R p 202 ¶ 138), and "RAI management and the Board considered the forecasts for years three through five to be of ever-decreasing reliability and years six through ten to be *extrapolations* intended to provide information about whether a continuation of existing trends would allow the Company to meet its [earnings per share] targets" (R p 203 ¶ 140 (emphasis added)). Indeed, "[t]he fact that extrapolations provided the most fundamental inputs to years six through ten of the ten-year projections was not contradicted". (R p 204 ¶ 142.) Nor could it have been contradicted; as shown above (p 28), simple straight-line extrapolations of key metrics like share of cigarette shipments are easily visible in the graphs included in the projections themselves. (R p 204 ¶ 141.)

Moreover, like the five-year projections, the ten-year projections "were based on certain identified assumptions that there would be no significant changes from the status quo". (R p 205 ¶ 144.) They "assumed business as usual without accounting for major downside risks". (R p 253 ¶ 248 (internal quotation marks omitted).) They were therefore unduly optimistic. As the Business Court found, "[a] valuation predicated upon the theory that a tobacco company like RAI will suffer no significant adverse regulatory, tax, or competitive effects in the future is simply not credible or reliable". (R p 256 ¶ 254.)

Second, Dissenters argue that the October 2016 projections were no longer current as of the Transaction Date in July 2017, and that any DCF valuation for appraisal purposes would need to be based on RAI's July 2017 projections. But the Business Court found that "for the periods that overlapped, the October 2016 Projections were a bit more *optimistic* than the July 2017" projections used by Dissenters' expert (R p 254 ¶ 249 (emphasis added))—meaning that the July 2017 five-year projections that Dissenters prefer would lead to a *lower* DCF value.

Third, Dissenters dispute the idea that the RAI projections (whether five-year or ten-year) had an upward bias, arguing that the various risks facing RAI, such as increased menthol regulation or increased excise taxes, were "both unknown and unquantifiable". (DB 112 (emphasis omitted).) Dissenters' expert made the same argument at trial, and the Business Court found that his "approach disregards the expressly stated assumptions and sensitivities to RAI's financial projections. . . . The evidence indicates that if one or more of these risks were to materialize, it would have a dramatic, negative effect on the Company's growth and profitability." (R pp 255-56 ¶ 254.) Although these risks "were not incorporated into the numerical projections . . . , that does not mean that they can be ignored when valuing the Company".[8] (*Id.*)

Dissenters' challenges to the Financial Advisors' use of the October 2016 five-year projections (and to the optimistic nature of those projections) are squarely foreclosed by the Business Court's factual findings.

(ii) The Business Court's Factual Findings Support the Financial Advisors' Growth Rate Ranges.

The second input into both sides' DCF analyses is a perpetuity growth rate ("PGR"), which is "the rate at which a company's expected free cash flows are assumed to grow indefinitely after the period for which there are year-by-year forecasts". (R p 259 ¶ 263.) Two of the Financial Advisors' contemporaneous DCF analyses used PGRs that ranged from -0.5% to 0.5%, and the third used a range from 0.0% to 1.0%. (R pp 259-60

[8] Dissenters also seek to diminish the significance of the risks that RAI identified by asking the Court to apply hindsight and consider their unsupported assertion as to what has (or has not) happened in the industry *after* the Transaction Date. (DB 113.) Setting aside that there is nothing in the record on this issue, this request directly contradicts their stance at trial. "Dissenters objected at trial to RAI's effort to introduce evidence relating to the period after the Transaction Date as irrelevant to the determination of fair value." (R p 328 ¶ 20 (footnote omitted).) The Business Court sustained Dissenters' objection, so Dissenters should be estopped from changing course and relying on matters that they successfully argued to be irrelevant.

¶ 264.) The Business Court found that these PGR ranges "were based on research into, and their [the Financial Advisors'] own experience and knowledge regarding, the tobacco industry and RAI's competitive position within the industry, including their understanding of the threats and potential upsides facing the Company and tobacco companies generally". (R p 260 ¶ 266.) The Business Court found the reliability of the Financial Advisors' PGR ranges enhanced by the fact that one of them, Lazard, used the same PGR range in valuing RAI in this transaction (where RAI was the seller) as it did when valuing RAI in the 2015 Lorillard Transaction (where RAI was the purchaser). (R p 262 ¶ 270.) The Financial Advisors also "checked their analyses using terminal exit multiples, among other things, as a 'sanity check'".[9] (R p 261 ¶ 268.) Based "on its review of the evidence, the Court [found] the PGR ranges used by the Financial Advisors to be reasonable and reliable". (R p 268 ¶ 282.)

[9] A "terminal exit multiple" is a measure of a company's growth in the "terminal period", *i.e.*, after the end of the year-by-year projections. In the ordinary case, a company's terminal exit multiple should be near but below the current multiple because most companies' growth rates in the future can be expected to be lower than the current growth rate. (R p 261 ¶ 268.)

In response, Dissenters again press arguments that are contrary to the facts found by the Business Court after trial. *First*, Dissenters argue that the Financial Advisors' PGR ranges are too low because they are below the rate of inflation (DB 114-17), but the Business Court found—citing the testimony of three fact witnesses and an expert—that "it is not unusual to see a zero or negative PGR used for companies or industries that are in structural decline, like the tobacco industry". (R p 259 ¶ 263.)

Second, Dissenters criticize Lazard for being consistent—for using the same PGR when valuing RAI in the Lorillard transaction as when valuing it in the Merger. (DB 116.) They argue this was inappropriate because the combined RAI/Lorillard entity was projected to have higher growth than standalone RAI. (*Id.*) As the Business Court found, however, "Lazard's work on the Lorillard Transaction included a valuation of the *pro forma* combined 'new and improved' RAI—the exact same company that was then sold to BAT—meaning that any 'fundamental change' had already been considered in the valuation performed for the Lorillard Transaction". (R p 262 ¶ 270.) Lazard's consistency across different transactional contexts (RAI as buyer and as seller) was a virtue, not a vice.

Third, Dissenters argue that the Financial Advisors' PGR ranges do not take account of the 7-8% growth rates in years six through ten of the ten-year projections from the June 2016 Strategy Day. (DB 114.) But as shown above, the Business Court found that the latter years of the ten-year projections were "broad brush" extrapolations of current trends that did not account for the possibility of material disruptions to RAI's business. (R p 202 ¶ 138.) Those factual findings preclude Dissenters' argument that a PGR in this case must take the ten-year projections into account.

In fact, Dissenters' insistence on using the ten-year projections is one of the key problems with their expert's DCF model. Their valuation expert, Mark Zmijewski, did not estimate a PGR of his own and had "no opinion on growth rates for this company". (R p 266 ¶ 277.) He instead "relied entirely on the PGR calculated by" a different expert, Fredrick Flyer. (*Id.*) Flyer "was *asked by Dissenters' counsel* to use a 1% or 1.25% PGR in conjunction with the growth rates extracted from the last five years of" the ten-year projections, to calculate a "blended" PGR. (R p 265 ¶ 275 (emphasis added).) "This blended rate is simply a mathematical calculation in which Flyer converted his 1.0% PGR and the growth rates for the years covered by the [ten-year projections] into a single flat rate." (*Id.*) Zmijewski then took this "blended" PGR, which amounted to 2.24%, and plugged it into his DCF model. (R p 265 ¶ 276.) The Business Court found that "the vast majority of Zmijewski's valuation is dependent on the PGR that was used"—meaning that Zmijewski's valuation depended largely on Flyer's PGR, about which Zmijewski had no opinion. (R p 266 ¶ 277.) "[S]imply changing the PGR from 2.2% to 0%, the midpoint of Goldman and Lazard's PGR ranges, in Zmijewski's DCF analysis decreased his valuation from $92.17 to $58.00 per share." (*Id.*)

Thus, Dissenters' DCF valuation is driven entirely by their PGR, and pursuant to instructions from Dissenters' counsel, their PGR incorporates the growth rates in years six to ten of the ten-year projections. But the Business Court found, based on uncontradicted trial evidence, that those growth rates were unreliable and not a sound basis for valuation. The Court found that "Flyer's PGR analysis ignores . . . the substantial evidence showing that these ten-year projections were not intended to create a probability-weighted value of future cash flows, disregarded significant assumptions and sensitivities that could dramatically impact RAI's business, and were largely extrapolations of current industry trends and dynamics without substantial change". (R p 267 ¶ 280.) Given those factual findings—which Dissenters *do not challenge* as lacking support—Dissenters' PGR is unsustainable. As a result, their DCF valuation, which is the *only* valuation evidence they offer, comes crashing down.

Fourth, Dissenters argue that it is unreasonable to assume that RAI's growth would "experience a 'cliff-like' drop" at the end of the forecast period. (DB 117.) The Business Court's factual findings address this too, explaining that a PGR "averages over the time with maybe some positive and then negative in the future and averages across scenarios[,] some of which may be very large negative events that happen", meaning that "a company with a 0% growth rate could continue to see positive growth for some time, which would then be balanced out by negative growth and/or by the possibility of a major adverse event". (R p 264 ¶ 274.) Dissenters insist on describing a 0% PGR as a "cliff" but never challenge (or even acknowledge) this contrary finding.

Fifth, in a reprise of their argument that the Financial Advisors should have used the ten-year extrapolated projections from Strategy Day, Dissenters argue that the Financial Advisors' PGR ranges are too low because they were applied after five years of explicit projections rather than after ten years. (DB 47.) This too ignores the Business Court's factual findings. In particular, based on "JPMorgan's contemporaneous documents" and the trial testimony of a JPMorgan representative, the Business Court found that "[t]he evidence suggests . . . JPMorgan used a *higher* PGR than it otherwise would have used if it had begun applying the PGR after ten years of projections". (R p 263 ¶ 272 (emphasis added).) Indeed, if it were to use ten years of projections, "JPMorgan discussed internally changing the range of PGRs to a negative range", rather than the positive 0.0%-1.0% range it actually used after five years. (*Id.*) In other words, the Business Court rejected—as a factual matter—Dissenters' contention that applying the PGR after five years rather than ten would lead to a lower valuation, because Dissenters' implicit assumption that the *same* PGR would be used in both instances was unfounded.[10]

[10] This also dispenses with Dissenters' false assertion that "[i]t is undisputed that the failure to account for the expected growth in years six through ten reduced the value of RAI by $20 per share". (DB 13-14 (emphasis omitted).)

(iii) The Business Court's Factual Findings Support the Financial Advisors' Discount Rates.

The third main input into a DCF analysis is a discount rate, which is a way to take account of the time value of money. It is "a rate of return used to discount future cash flows back to present value". (R p 268 ¶ 283.) The Business Court concluded there was "very little disagreement" among the discount rate calculations performed by the Financial Advisors and both parties' experts. (R p 268 ¶ 285.) Based on the record, the Business Court concluded that the rate calculated by RAI's expert "has greater evidentiary support" (R p 269 ¶ 286), and Dissenters do not dispute that conclusion on appeal (DB 107 n.30).

2. Market Indicators of Value

The Business Court's factual findings in support of the Financial Advisors' DCFs, and against Dissenters' DCF, are enough to sustain its fair value determination based on a valuation tool that Dissenters concede was appropriate for the Business Court to rely on.

But here, there is much more. The Financial Advisors' DCFs are corroborated by numerous other valuation methods, whereas Dissenters' DCF stands alone as vastly higher than any other indicator of RAI's value. As the Business Court explained, a DCF analysis "is only reliable when it can be verified by alternative methods to DCF or by real world valuations". (R p 304 ¶ 362 (quoting *S. Muoio & Co. LLC v. Hallmark Entm't Invs. Co.*, No. 4729-CC, 2011 WL 863007, at *18 (Del. Ch. Mar. 9, 2011), *aff'd*, 35 A.3d 419 (Del. 2011)).) *Every* piece of contemporaneous evidence of value supports the Business Court's fair value determination of no more than $59.64 and further demonstrates that Dissenters' litigation-driven $92.17 valuation is an extreme outlier with no factual basis or corroboration.

First, the "unaffected" trading price of RAI's common stock prior to BAT's initial offer supported the Business Court's fair value determination. On 20 October 2016, the day before BAT's initial offer was announced, RAI's stock closed at $47.17 per share. (R p 229 ¶ 197.) Its "52-week trading average prior to BAT's initial offer was approximately $49.00". (*Id.*) The volume weighted average trading price of RAI stock from the closing of the Lorillard Transaction in June 2015 until BAT's October 2016 offer was $46.26. (R p 230 ¶ 198.) And RAI's all-time high trading price was $54.48. (R p 229 ¶ 197.) All of these prices were consistent with the Business Court's fair value determination of no more than $59.64.

Second, an analysis of the likely unaffected trading price of RAI's common stock after the date of BAT's initial offer further supported the Business Court's fair value determination. As the Business Court recognized, the appraisal statute required it to value RAI stock as of the Transaction Date in July 2017, rather than when BAT made its offer in October 2016. But it was not feasible to consider RAI's stock price in July 2017 as a relevant proxy for fair value because it was then trading primarily by reference to the likelihood of, and price of, a transaction with BAT. (R pp 235-36 ¶ 208.) Accordingly, to take account of intervening developments such as the increased possibility of corporate tax reform after the 2016 election, RAI's expert, Paul Gompers, calculated an "Adjusted Unaffected Stock Price" as of the Transaction Date. (R p 236 ¶ 210.) He indexed RAI's stock price on 20 October 2016 to the stock price performance of its closest competitor, Altria, and to the performance of the S&P 500 generally from 20 October 2016 through 24 July 2017. (*Id.*) That analysis led to implied Transaction Date trading prices of $55.33 per share based on the performance of Altria's stock, and $53.78 per share based on the performance of the S&P 500.[11] (R pp 236-37 ¶ 210.) As the Business Court found, this Adjusted Unaffected Stock Price analysis was "persuasive evidence that suggests that the deal price is consistent with, and Dissenters' proposed valuation is inconsistent with, RAI's fair value on the Transaction Date". (R p 237 ¶ 211.)

Third, the negotiated deal price supported the Business Court's fair value determination. As the Business Court explained, there were "numerous objective indicia of a robust deal process that led to a deal price that reliably reflected RAI's fair value". (R p 289 ¶ 332.) The evidence includes the following facts found by the Business Court, none of which Dissenters challenge on appeal:

- The members of the Transaction Committee "were fully independent of BAT and able to consider the proposed transaction (and any alternatives) free of any conflicts, focused only on the best interests of the RAI shareholders other than BAT". (R p 190 ¶ 113.)

- The Transaction Committee included sophisticated executives with substantial experience in considering and negotiating complex mergers and acquisition transactions (*id.*), and was delegated the power and authority to, "among other things, evaluate, discuss and negotiate the terms and conditions of, approve, recommend, and/or reject the October 20 Offer, any other potential transaction with

[11] "At trial, no evidence was offered of a material, value-relevant event between October 20, 2016 and July 25, 2017 that affected RAI separately from the tobacco industry or the market as a whole." (R p 236 ¶ 210 n.38.)

BAT, and any potential alternative strategic transaction" (R p 191 ¶ 114).

- The Transaction Committee had as its Financial Advisors three "highly sophisticated and respected investment banks with extensive experience advising large companies in corporate transactions, including in the tobacco sector". (R p 192 ¶ 118.) There was "no credible evidence that any of the Financial Advisors took any action in connection with the Merger to cause a transaction with BAT at less than fair value". (R p 193 ¶ 119.) "To the contrary, there was credible testimony that the Financial Advisors' long-term reputations were more important to each of them than the compensation to be earned on the Merger and that attempting to depress the merger price would tarnish that reputation." (*Id.*)

- "[T]he record is clear that the Financial Advisors received all the information they believed they needed for their valuation work, and no credible evidence was offered at trial supporting any effort by RAI management to hide information to depress the resulting valuation of the Company." (R p 212 ¶ 159 (citation omitted).)

- "Multiple witnesses testified that RAI seriously considered strategic alternatives, including remaining independent from BAT" (R p 220 ¶ 177), but "there was no admissible evidence at trial from any source that any third party was interested in purchasing RAI with or without BAT's support" (R p 218 ¶ 174).[12]

- "[T]he Transaction Committee twice rejected BAT's merger offers without making a counterproposal—showing the Transaction Committee thoroughly explored the viability of RAI's remaining independent as an alternative to executing a transaction with BAT." (R p 220 ¶ 177.)

[12] The Business Court found the only evidence offered by Dissenters to suggest that Japan Tobacco would have been interested in purchasing RAI (*see* DB 38)—an "internal email within Goldman reporting what an unnamed person at Japan Tobacco allegedly said"—to be "hearsay and hardly persuasive". (R p 294 ¶ 340.)

- "As a result of the Transaction Committee's efforts, BAT increased its offer to purchase RAI's common stock four times from a per-share value of $56.50 in the October 20 offer to a per-share value of $59.64 when the transaction was announced on January 17, 2017, amounting to an additional $4.5 billion in deal value for RAI's shareholders and a 26.4% premium over the Unaffected Stock Price". (R p 221 ¶ 181.)

- Each of the Financial Advisors separately evaluated the final BAT offer and determined that it was "fair from a financial point of view to the RAI shareholders other than BAT". (R p 222 ¶ 183.)

- "At the shareholder vote on the Merger, RAI's shareholders overwhelmingly approved the deal, by both a majority (83%) of the outstanding shares and by a majority (71%) of the non-BAT-owned outstanding shares. Nearly 72% of the non-BAT-owned shares were voted in the Merger, and 99% of those shares were voted in favor of the Merger." (R p 227 ¶ 189.)

Fourth, stock market analyst commentary supported the Business Court's fair value determination. Analyst price targets for RAI as a standalone company ranged from $47 to $62 per share. (R p 247 ¶ 234.) In addition, when the acquisition by BAT became public, "not a single analyst . . . said that BAT was getting a steal". (R p 247 ¶ 234.) On the contrary, analyst commentary on the deal price was uniformly positive. No contemporaneous analyst reports indicated that the deal price dramatically undervalued RAI. Some analysts commented that the deal price was high from BAT's perspective given that it was on the upper end of equity analyst price targets and because RAI was trading at a relatively high multiple at the time. (R pp 226 ¶ 187, 189 ¶ 109.)

Fifth, the Business Court's fair value determination is consistent with the pre-litigation assessment of one of the Dissenters. In November 2016, after BAT had made its initial offer to purchase RAI, Dissenter Mason Capital sent the RAI Transaction Committee a letter intended to persuade the Transaction Committee to seek a higher price from BAT. (R p 248 ¶ 235.) The letter included a multiples-based valuation of RAI that arrived at a "Market Value of Equity" of $54.44 per share. (R p 248 ¶ 236.) Mason Capital's representative at trial testified that this $54.44 value was "how we, Mason Capital, think that [RAI's] stock should be valued on its own". (R pp 248-49 ¶ 237.) She also testified that this did "not include any sort of overhang from BAT's holdings" and did "not include any sort of minority discount". (R p 249 ¶ 238.) This was simply how Mason Capital valued RAI's stock at the time. The Business Court found that "[t]he difference between Mason Capital's contemporaneous $54.44 valuation and its litigation valuation of $92.17 cannot be explained by the discovery of nonpublic information in the litigation process" and concluded that "[t]he substantial discrepancy in Mason

Capital's contemporaneous and litigation-driven valuations of RAI's shares undermine[s] the credibility and reliability of the latter". (R pp 249-50 ¶ 239.) Dissenters' brief makes no mention of their own contemporaneous valuation of RAI.

Sixth, JPMorgan, Lazard and Gompers conducted "comparable companies" analyses that compared financial multiples implied by the deal price with multiples derived from the trading prices of other companies in the tobacco industry, which were selected because they are subject to a similar set of regulatory risk and consumer trends. (R pp 237-38 ¶ 213, 238-39 ¶ 216.) Of the peers considered, Altria was the closest fit to RAI because, like RAI, its primary business is the sale of cigarettes in the United States. (R p 239 ¶ 217.) Based on this analysis, JPMorgan came to a range of values between $36.50 and $51.75 and Lazard came to a range of $40.86 to $49.67. (R p 238 ¶ 215.) Using the median multiples of his full set of peers, Gompers came to $49.70 (using the next 12 months' projected earnings) and $51.76 (using projected earnings for the 12 months after that). (R p 240 ¶ 218.) Using Altria's multiple, he came to $46.18 and $48.52, respectively. (*Id.*)

Although the Business Court ultimately gave these analyses “no weight” in assessing fair value, it found that “[o]ne purpose for calculating the multiples of comparable companies is to check the results of other valuation techniques”. (R pp 238 ¶ 216, 243 ¶ 224.) It therefore found them to be “relevant information that, when considered in connection with other valuation concepts and techniques, supports a conclusion that [Dissenters’] $92.17 per share valuation is excessive”. (R pp 242-43 ¶ 224.) Among other things, if the $92.17 valuation were correct, it would lead to financial multiples that would suggest that RAI’s “prospects are twice as good as . . . the other peer companies in the industry”, which “would be an unrealistic conclusion not supported by the evidence presented at trial and raises significant doubt concerning the reliability of [Dissenters’] valuation”. (R p 242 ¶ 223.)

Seventh, the Financial Advisors and Gompers conducted “precedent transactions” analyses using financial multiples derived from prior transactions similar to the Merger, which resulted in implied valuation ranges for RAI from $38.12 per share to $60.00 per share. (R pp 243-44 ¶ 226.) Although the Business Court found the precedent transactions analyses to be “of limited value because of the differences in the selected transactions, the specific values generated by the various precedent transactions analyses performed contemporaneously by the Financial Advisors, as well as by Gompers in his analysis, provide support that the deal price of $59.64 was at or above RAI's fair value and that [Dissenters'] valuation was clearly excessive". (R p 247 ¶ 233.)

Eighth, Dissenters themselves repeatedly urged the Business Court to rely on a valuation analysis that (when all the facts were revealed at trial) strongly supported the Court's finding that the fair value of RAI was no more than $59.64. In connection with RAI's acquisition of Lorillard in 2015, Lazard conducted an analysis that implied a valuation range for the combined RAI/Lorillard entity of $60.15 to $93.39 per share. (R p 272 ¶ 296.) Dissenters "relied on the high-end of this valuation in pre-trial briefing and at trial as evidence supporting the reasonableness of their proposed $92.17 per share valuation". (R p 272 ¶ 297.) However, as was revealed at trial, Dissenters failed to account for the fact that, following the close of RAI's acquisition of Lorillard, RAI effected a two-for-one stock split in August 2015—doubling the number of outstanding shares of RAI common stock. (R pp 272-73 ¶ 297.) Thus, when Dissenters compared Lazard's 2015 analysis to their DCF valuation in this case, they were not comparing apples to apples—they were comparing "one apple to two apples", and were therefore wrong by a factor of two. As a result of the stock split, Lazard's valuation from the Lorillard deal in 2015 equates to a range of between $30.08 and $46.70 per share at the Transaction Date in 2017. (R p 273 ¶ 297.) The Business Court reasonably concluded that rather than supporting Dissenters' DCF valuation, "[Lazard's 2015] valuation (which Dissenters themselves touted as an appropriate benchmark) strongly undermines it and instead supports the deal price as fair value for RAI's shares". (R p 273 ¶ 297.) Neither at trial nor on appeal have Dissenters offered any reason for changing their mind on the reliability and persuasiveness of the Lazard analysis. It is obvious that they walked away from that analysis solely because additional facts were uncovered at trial showing that the Lazard analysis—like *all* other contemporaneous evidence in the record—supports the Business Court's fair value determination.

In sum, competent—indeed, overwhelming—evidence supports the Business Court's findings that Dissenters' valuation of $92.17 was "an extreme outlier" and that "the fair value of RAI as of the date of the

Merger was no more than the $59.64 per share that Dissenters have already been paid". (R pp 274-75 ¶¶ 302-04.)

II. DISSENTERS' CRITICISMS OF THE BUSINESS COURT'S ANALYSIS ARE WITHOUT MERIT.

Dissenters' various criticisms of the Business Court's opinion rest largely on mischaracterizing its analysis or ignoring its findings of fact. None of those criticisms has any merit, much less warrants disturbing the Business Court's judgment.

A. The Business Court Valued RAI as of the Closing Date.

Dissenters claim that "the Business Court committed legal error by failing to value [RAI] as of the Transaction Date". (DB 64-65 (emphasis omitted).) That is a gross misstatement of the Business Court's opinion. The Business Court clearly understood that it was required to determine the fair value of Dissenters' shares as of the Transaction Date, and that is precisely what it did.

To begin with, the Business Court accurately stated the law, noting that "[t]he North Carolina appraisal statute provides that fair value must be determined 'immediately before the effectuation of the corporate action as to which the shareholder asserts appraisal rights'". (R p 283 ¶ 320 (quoting N.C.G.S. § 55-13-01(5)).) The Court also accurately understood what the statute means, noting that it "must determine fair value *as of the Transaction Date* rather than when the Merger Agreement was signed in January 2017". (*Id.* (emphasis added).) And if there were any doubt, the Business Court went on to observe that "[i]f the value of the corporation changes between the signing of the merger agreement and the closing, then the fair value determination must be measured by the operative reality of the corporation *at the effective time of the merger*". (*Id.* (emphasis added) (quoting *In re Appraisal of Stillwater Mining Co.*, Consol. C.A. No. 2017-0385-JTL, 2019 WL 3943851 (Del. Ch. Aug. 21, 2019), *aff'd*, ___ A.3d ___, 2020 WL 6038341 (Del. Oct. 12, 2020)).)

The Business Court did not only explain the law correctly; it also did what that law requires. Consistently throughout its opinion, the Business Court made clear that its fair value determination was as of the Transaction Date. For example, it found that "the fair value of RAI *as of the date of the Merger* was no more than the $59.64 per share that Dissenters have already been paid" (R p 275 ¶ 304 (emphasis added)), that "the $59.64 per share that RAI has already paid Defendants equals or exceeds the fair value of RAI shares *as of the date of the Merger*"

(R p 143 ¶ 3 (emphasis added)), and that "the fair value of RAI *at the Merger closing on July 25, 2017* was no more than the deal price of $59.64" (R p 228 ¶ 194 (emphasis added)).

Moreover, the Business Court expressly recognized that "in the time between the October 20 Offer and the Transaction Date, events took place that may have affected RAI's standalone value", such as the outcome of the 2016 U.S. elections. (R p 236 ¶ 209.) For example, the Court noted "speculation that the Republican-led Congress would pass a tax bill that would lower the corporate tax rate and that there would be a more benign regulatory climate for the U.S. tobacco industry". (*Id.*) The Court expressly considered Gompers's Adjusted Unaffected Stock Price analysis, which was intended to "estimate the effect that these and other market industry developments would likely have had on RAI's stock price between BAT's October 20 Offer and the closing of the Merger on July 25, 2017". (R p 236 ¶ 210.) There can be no doubt that the Business Court valued RAI as of the Transaction Date.

Despite this extensive discussion and analysis by the Business Court to arrive at a Transaction Date fair value, Dissenters insist that the Business Court did not do what the Business Court said it did.

Instead, Dissenters contend that "the Business Court elected to value RAI based on the value of the deal price" as of the signing of the Merger Agreement in January 2017. (DB 65.) Specifically, Dissenters argue that because the Court found the fair value of RAI to be no more than $59.64 per share, it pegged fair value to "the amount of the merger consideration determined six months earlier [than the Transaction Date] when the deal was struck on the underlying transaction". (DB 64.) That argument is refuted by the same paragraph of the Business Court's opinion on which Dissenters rely, which states that "[t]he evidence at trial . . . establishes the fair value of RAI's shares *as of the Transaction Date* to be no more than $59.64 per share". (R p 313 ¶ 382 (emphasis added).)

Nevertheless, Dissenters insist that because the Business Court referred to $59.64 per share, which was the cash value of the merger consideration as of signing in January 2017, that means the Business Court must have done a valuation as of that date. They observe that the stock portion of the merger consideration appreciated in value between January 2017 and the Transaction Date in July, and they contend they should have received, at a minimum, the $65.87 per share that the merger consideration was worth as of the Transaction Date. (DB 70-71.)

There are three fatal flaws in this argument. *First*, as noted, in reaching its fair value determination, the Business Court expressly took into account the very events between signing and closing that Dissenters say caused the increase in the value of the merger consideration over that period. *Compare* DB 67-68 (arguing that the Court should have considered increases in equity markets and the value of other major U.S. tobacco companies) *with* R pp 236-37 ¶ 210 (considering the stock price "performance of [RAI's] closest competitor, Altria" and "the performance of the S&P 500 generally"). *Compare* DB 69 (arguing that the Court should have considered "the increased likelihood of corporate tax reform and an accommodative regulatory climate" for tobacco in the U.S.) *with* R p 209 ¶ 209 (considering the prospect of "a tax bill that would lower the corporate tax rate" and "a more benign regulatory climate for the U.S. tobacco industry").

Second, the Business Court did not determine RAI's fair value to *be* $59.64 per share—and it certainly did not peg fair value to the specific cash/stock mix comprising the merger consideration. Rather, as the Business Court repeatedly stated, based on the totality of the evidence, it found the fair value of RAI as of the Transaction Date to be "***no more***

than" $59.64. (R pp 228 ¶ 194, 275 ¶ 304, 313 ¶ 382, 314 ¶ 384.) This takes the legs out from under Dissenters' argument. Dissenters proceed as though the Business Court found fair value to be $59.64 as of January 2017 and then neglected to take account of subsequent appreciation. In reality, the Business Court found that, even accounting for events between January and July, RAI's fair value as of the Transaction Date was *still* no higher than $59.64 per share. Indeed, the Business Court made this clear on the very first page of its opinion, finding that "the $59.64 per share that RAI has already paid Defendants *equals or exceeds* the fair value of RAI shares *as of the date of the Merger*". (R p 143 ¶ 3 (emphasis added).) Dissenters may disagree with that finding, but there should be no dispute that is what the Business Court in fact found.[13]

Third, Dissenters overlook the true significance of $59.64 per share. It was not just the cash value of the merger consideration at signing. In addition, as the Business Court repeatedly noted, it was the amount that

[13] This also shows the falsity of Dissenters' repeated statements to the effect that the Business Court "simply deferred to the value of the merger consideration" (DB 3-4) or "adopt[ed] the price negotiated by RAI and BAT" (DB 9). As discussed further below, the Court considered the deal price as one of many indicators of value, as part of the overall body of evidence in the record. (*See* Part II.B.)

"RAI ha[d] already paid" to Dissenters for their shares. (R p 143 ¶ 3; *see* R p 275 ¶ 304 ("the $59.64 per share that Dissenters have already been paid").) Under the appraisal statute, upon receiving a signed appraisal form from a dissenting shareholder, a corporation is required to pay that shareholder "the amount the corporation estimates to be the fair value of their shares, plus interest". N.C.G.S. §§ 55-13-22, 55-13-25(a). Here, in September 2017, after receiving Dissenters' signed forms and before the initiation of this case, RAI estimated fair value to be $59.64 per share and paid all Dissenters that amount, plus interest from the Transaction Date. (R p 228 ¶ 192.)

Accordingly, in this case, if the Business Court found the fair value of RAI's shares to be $59.64 or less, then no further payment would be due. *See* N.C.G.S. § 55-13-30(e). Because RAI did not seek, and the statute does not provide for, any refund of amounts already paid to a dissenting stockholder, there was no need for the Business Court to assess how far below $59.64 the Transaction Date fair value may have been. To discharge its responsibility under the statute, it was enough for the Business Court to find, as it did, that the fair value of RAI as of the Transaction Date was "no more than" $59.64 per share.

While it is true that Dissenters ultimately received less for their shares than other RAI shareholders who did not seek appraisal (DB 71), that is a risk that these sophisticated investors chose to accept when they, unlike other shareholders, requested an independent judicial determination of the fair value of their shares.

B. The Business Court Did Not "Rel[y] Solely on the Value of the Merger Consideration".

Dissenters claim that the Business Court "failed to conduct an independent valuation using generally accepted valuation techniques". (DB 72-73.) In their telling, "the Business Court did not value RAI at all, and instead relied solely on the value of the merger consideration". (DB 72.) Dissenters are doubly wrong. *First*, they take an unduly narrow conception of what type of valuation techniques an appraisal court may employ. *Second*, their assertion that "the Business Court relied solely on the value of the merger consideration" (*id.*) is a misstatement of what the Court actually did.

Contrary to Dissenters' claim, the Business Court did not simply defer to the deal price and adopt it as fair value. As the Business Court stated, "the court cannot adopt at the outset an 'either-or' approach, thereby accepting uncritically the valuation of one party, as it is the

Court's duty to determine the core issue of fair value on the appraisal date". (R p 282 ¶ 319 (internal quotation marks omitted).) Accordingly, in its comprehensive opinion, the Business Court carefully considered evidence presented at trial under each of the "customary and current" valuation concepts and techniques described above. The Court then grounded its conclusion as to the fair value of RAI in far more than just the deal price. In addition to explaining why the deal price had sufficient indicia of reliability as to fair value, the Court also pointed to other evidence of value, including:

- *Market price*. "The market valued RAI stock at well under $59.64 prior to BAT's first offer and likely would have continued to do so through the Transaction Date if the Merger had not occurred." (R p 313 ¶ 383.)

- *Discounted cash flow analyses*. "Properly conducted DCF analyses, including three separate analyses conducted by RAI's highly regarded, independent, and conflict-free financial advisors, support a fair value of $59.64 or less." (R pp 313-14 ¶ 383.)

- *Precedent transactions and comparable companies as cross-checks*. "The acquisition multiples in precedent transactions, while of less value, suggest a fair value below $59.64, and when considered together with the trading multiples for comparable companies, at a minimum and with all other evidence of value introduced at trial, provide a useful market or sanity check . . . ." (R p 314 ¶ 383.)

- *Financial analyst price targets*. "The $59.64 per share deal price, measured as of January 16, 2017, was at the upper end of the unaffected analyst price targets for RAI as a standalone company." (R p 247 ¶ 234.)

- *Mason Capital's contemporaneous valuation.* "Mason Capital's letter to the Transaction Committee [valuing RAI at $54.44 per share] is persuasive evidence of Mason Capital's pre-litigation views of RAI's value." (R p 249 ¶ 238.)

In dismissing all of this evidence and asserting that "an independent judicial determination" was especially necessary in this case (DB 73), Dissenters revert to their discredited conspiracy theory and again ignore the Business Court's factual findings. They contend that the deal price and Financial Advisor analyses should be disregarded because the Transaction Committee and the Financial Advisors "were not in possession of material, value-relevant information: RAI's detailed ten-year cash projections". (*Id.*) But the Business Court expressly found that "RAI management provided each of the Financial Advisors with . . . projections of operating income and growth rates for years six through ten of the June 2016 Strategic Plan". (R p 207 ¶ 149.) "The Financial Advisors were thus aware of the forecasted compound annual growth rates of 7% to 8% for the out years of those projections". (R pp 207-08 ¶ 149.) While Dissenters claim that the Financial Advisors were in the dark without the underlying spreadsheets supporting those numbers

(DB 46-47), the Business Court found otherwise, determining that "all three Financial Advisors knew the projected trajectory and could have insisted on further detail if they believed it was necessary". (R p 208 ¶ 149; *see also* R p 212 ¶ 159 (noting that "the Financial Advisors received all the information they believed they needed for their valuation work").)

Moreover, the Business Court found "little relevance in RAI's year six through ten projections for valuation purposes" (R p 308 ¶ 371), as "[t]he fact that extrapolations provided the most fundamental inputs to years six through ten of the ten-year projections was not contradicted" at trial (R p 204 ¶ 141). Dissenters do not even challenge the Business Court's findings on this point. They instead repeatedly urge that the Court should have used these projections, in the face of extensive evidence about the extrapolated content of the projections, the broad brush manner in which they were created and the very limited purposes for which they were used—all of which properly led the Business Court to find that they were inappropriate for a DCF or any other valuation purposes.

Ultimately, the "independent judicial valuation" sought by Dissenters is nothing more than a request for this Court on appeal to throw out all of the other indicators of value in the record (and the factfinding by the Business Court) and rest everything on their made-for-litigation DCF model, which the Business Court found was an extreme and unreliable outlier based on the facts established at trial (which are, again, factual findings the Dissenters ignore on appeal).

C. The Business Court Properly Considered Deal Price as a Reliable Indicator of Fair Value.

Dissenters next argue that the Business Court's supposed decision to "defer to deal price" was an "incorrect[] appli[cation of] Delaware law to the North Carolina appraisal statute" (DB 75). That is wrong in a number of respects.

First, the premise of the argument is inaccurate. As explained above, the Business Court did not "defer to deal price". Instead, the Court considered the negotiated deal price as one of many mutually reinforcing indicators of the fair value of RAI.[14] (*See* Part II.B above.)

[14] Nor is it correct to say, as Dissenters do in this section of their brief, that the Business Court "conclud[ed] that the fair value of RAI as of the Transaction Date was the value of the merger consideration on the Deal Date". (DB 74.) That is not what the Court held. As explained above, it held that the fair value of RAI as of the Transaction Date was no more than the $59.64 per share that RAI had already paid to Dissenters, such that no additional payment was due for Dissenters' shares.

Second, to the extent Delaware law is relevant, Dissenters are wrong to argue that Delaware courts would not consider deal price as a reliable piece of evidence of fair value in the circumstances of this case. They contend that "no Delaware court has deferred to deal price without a market check". (DB 82.) In fact, however, the Delaware courts have declined to impose "minimum requirements for . . . sale processes to meet before the deal price can be considered as a persuasive indicator of fair value". *In re Appraisal of Columbia Pipeline Grp.*, C.A. No. 12736-VCL, 2019 WL 3778370, at *42 (Del. Ch. Aug. 12, 2019); *see also LongPath Cap., LLC v. Ramtron Int'l Corp.*, C.A. No. 8094-VCP, 2015 WL 4540443, at *21 (Del. Ch. June 30, 2015) ("I am not aware of any case holding that a multi-bidder auction of a company is a prerequisite to finding that the merger price is a reliable indicator of fair value."). The courts instead review the deal process "as a whole". *Columbia Pipeline*, 2019 WL 3778370, at *42.

As the Business Court explained, "the persuasiveness of the deal price depends on the reliability of the sales process that generated it". (R p 286 ¶ 326 (quoting *Stillwater*, 2019 WL 3943851, at *21.) "A deal price serves as a persuasive indicator of fair value where the sale process bears objective indicia of fairness", such as "negotiations at arm's-length; board deliberations without any conflicts of interest; buyer due diligence and receipt of confidential information about the company's value; and seller extraction of multiple price increases". *In re Appraisal of Panera Bread Co.*, C.A. No. 2017-0593-MTZ, 2020 WL 506684, at *19 (Del. Ch. Jan. 31, 2020) (internal quotation marks and brackets omitted).

Here, the Business Court found there to be "numerous objective indicia of a robust deal process" (R p 289 ¶ 332), including each and every one of the indicia identified in *Panera*. (R pp 289-92 ¶¶ 333-38 (detailing, on a paragraph-by-paragraph basis, six of the indicia on which the Court relied).) After marching through this analysis, the Court found

> "based on the evidence presented . . . that the Merger was negotiated at arm's length by independent, fully informed, and deeply knowledgeable directors with the assistance of independent and experienced advisors, all of whom had extensive experience in the tobacco industry and a deep and impeccable knowledge of RAI and its potential opportunities, challenges, and future prospects. The Committee and the Board acted with full transparency and in relentless pursuit of value, rejected two BAT offers outright, indicating their seriousness in continuing as an independent entity, and extracted four price increases from BAT resulting in an additional $4.5 billion for RAI's shareholders."

(R p 297 ¶ 347.) Dissenters do not challenge the sufficiency of the evidence to support *any* of these findings. As further objective indicia of the reliability of the deal price as a measure of fair value, the Business Court also found (again without challenge from Dissenters) that "[t]he non-BAT shareholders voted overwhelmingly (99% of shares voted) in favor of the Merger, a transaction that had received widespread favorable reaction from industry observers and analysts". (R p 297 ¶ 347.) Based on these unchallenged findings and others, the Business Court reached the permissible conclusion that "under the circumstances present here, even without more aggressive outreach and a competitive auction, the resulting deal price is reliable evidence of RAI's fair value". (R pp 297-98 ¶ 347.)

Dissenters respond by contending that the Business Court's approach was foreclosed by the Delaware Supreme Court's decision in *Global GT LP v. Golden Telecom, Inc.*, 993 A.2d 497 (Del. Ch.), *aff'd*, 11 A.3d 214 (Del. 2010), which they describe as "controlling law". (DB 80.) As they interpret it, *Golden Telecom* requires ignoring all of the objective indicia of fairness identified by the Business Court because BAT was unwilling to sell its shares in RAI to a third-party bidder. Even setting aside that *Golden Telecom* is not "controlling" in North Carolina, the case is distinguishable. The special committee of the acquired company's board in that case treated the deal like "a merger proposal by a controlling stockholder", 993 A.2d at 508, but as shown above, the Business Court found that was not the case here: the RAI Transaction Committee "negotiated at arm's length" (R p 297 ¶ 347), "rejected two BAT offers outright, indicating their seriousness in continuing as an independent entity" (*id.*), and "seriously considered strategic alternatives to a merger with BAT" (R p 290 ¶ 334). Further, in *Golden Telecom*, "the weight of the evidence suggest[ed] that the market believed that [the buyer] was getting a bargain", 993 A.2d at 509, but the Business Court found that here "the market believed the Transaction Committee succeeded in negotiating a fair price" (R p 298 ¶ 348). As a further distinction from *Golden Telecom*, the Business Court found here as a matter of fact that even if BAT had been willing to sell its RAI shares, "there were few (if any) companies in the tobacco industry or adjacent industries that could have made an offer for RAI" (R p 293 ¶ 340), such that "[n]othing in the record suggests that increased competition would have produced a better result" (R p 297 ¶ 347).[15]

Moreover, as the Business Court recognized, the relevance of the deal price is not an on-off switch. (*See* R pp 285-89 ¶¶ 324-32.) Even when a court does not use the deal price as the dispositive determination of fair value, it can still be relevant evidence and carry substantial weight. *See, e.g*, *Jarden*, 2019 WL 3244085, *4 (finding the fair value was consistent with the "less reliable, but still relevant, deal price less synergies value"); *see also Blueblade Cap. Opportunities LLC v. Norcraft Cos.*, C.A. No. 11184-VCS, 2018 WL 3602940, at *39 (Del. Ch. July 27, 2018) (even if the merger price by itself is not a reliable indicator of value, "[t]hat does not mean, however, that the Merger Price is *irrelevant* for purposes of the Court's fair value determination"). Dissenters offer no authority at all for the proposition that an appraisal court must completely ignore the deal price, particularly when there are so many

[15] In the Delaware Supreme Court's latest word on appraisal, from just last month, *Brigade Leveraged Capital Structures Fund Ltd. v. Stillwater Mining Co.*, ___ A.3d ___, 2020 WL 6038341, at *5 (Del. 2020), the Court did not even mention *Golden Telecom*, while affirming the Chancery Court's determination that certain "objective indicia" of fairness present in that case provided "a cogent foundation for relying on the deal price as a persuasive indicator of fair value". *Id.* at *6.

objective indicia of fairness supporting its reliability as an indicator of fair value.

Third, Dissenters unfairly accuse the Business Court of "fundamentally fail[ing] to understand" the difference between appraisal law and fiduciary duty cases. (DB 15.) Indeed, they go so far as to charge the Business Court with "holding that a transaction that does not constitute a breach of fiduciary duty need not be independently appraised". (DB 87.) The Business Court did no such thing, and Dissenters are once again ignoring what the Business Court actually wrote. The Business Court *expressly noted the distinction* between the fiduciary inquiry and the appraisal inquiry, stating that in an appraisal "it is not sufficient for . . . directors to achieve the best price that a fiduciary will pay if that price is not a fair price". (R p 281 ¶ 317 (internal quotation marks and bracket omitted).) Furthermore, the Business Court clearly recognized the nature of its task, observing that "[u]nder the North Carolina and Delaware appraisal statutes, '[t]he trial court's ultimate goal in an appraisal proceeding is to determine the fair or intrinsic value of each share on the closing date of the merger'". (R p 278 ¶ 313 (quoting *Stillwater*, 2019 WL 3943851, at *19).)

To make matters even worse, Dissenters' basis for accusing the Business Court of being "confus[ed]" is misleading. Dissenters point to one paragraph of the Business Court's opinion and say that "the only Delaware Supreme Court decision cited by the Business Court" for a particular proposition was a fiduciary duty case called *Barkan v. Amsted Industries, Inc.*, 567 A.2d 1279, 1287 (Del. 1989). (*See* DB 85-86 (discussing R pp 287-88 ¶ 329).) Dissenters neglect to observe that the Business Court, in that same paragraph, also cited *three* Delaware Chancery Court decisions, *all of which were appraisal cases*. (R pp 287-88 ¶ 329.) Moreover, in a recent appraisal case that the Business Court relied on in its opinion, which Dissenters do not mention, the Delaware Chancery Court cited *Barkan* for the *same proposition* for which the Business Court cited it in this case. *See Panera*, 2020 WL 506684, at *24 (citing *Barkan* and noting that "[t]he Delaware Supreme Court has held that when 'the directors possess a body of reliable evidence with which to evaluate the fairness of a transaction, they may approve that transaction without conducting an active survey of the market'"). It follows that the Business Court was not "confused".

Dissenters also suggest, here and elsewhere in their brief, that the deal price negotiated by the parties should be ignored because of this Court's decision in *Corwin v. British American Tobacco PLC*, 371 N.C. 605, 821 S.E.2d 729 (N.C. 2018). That is incorrect. In *Corwin*, this Court concluded that an RAI shareholder had failed to plead facts sufficient to show that BAT had control of RAI and owed the other RAI shareholders fiduciary duties. 371 N.C. at 625, 821 S.E.2d at 743. Dissenters characterize the decision as giving BAT "the 'green light' to use the leverage inherent in its large position and presence on the [RAI] board" to disadvantage other shareholders. (DB 88.) But *Corwin* was a *pleadings stage* decision. Here, unlike in *Corwin*, the underlying facts have now been tested through discovery and trial. The Business Court carefully reviewed the negotiation history of the Transaction and found no evidence that BAT used its influence at RAI to secure a deal price that undervalued the company. Indeed, the Business Court found that "RAI had freedom to make decisions independent of BAT" (R p 290 ¶ 334) and forcefully rejected Dissenters' various efforts to argue that RAI's management or Board took steps to aid BAT (R pp 290-97 ¶¶ 334-47.) Like much of Dissenters' brief, their reliance on *Corwin* disregards the fact that there was a trial here, after which the Business Court made detailed findings of fact that Dissenters have failed to challenge.[16]

D. The Business Court Properly Considered Gompers's Adjusted Unaffected Stock Price Analysis as an Indicator of Fair Value on the Transaction Date.

Dissenters bring two separate challenges to the Business Court's consideration of Gompers's Adjusted Unaffected Stock Price analysis. *First*, Dissenters re-argue the facts underlying this analysis, without ever acknowledging that the Business Court has conclusively resolved these factual disputes against them. (DB 89-91, 95-99.) *Second*, Dissenters bring an evidentiary challenge to the Business Court's admission of Gompers's testimony on this subject. (DB 91-95.)

Both challenges fail, for the reasons below. Before addressing the specific flaws in Dissenters' arguments, however, it bears emphasizing that the Adjusted Unaffected Stock Price analysis was just one of several indicators of value on which the Business Court relied. Even if

[16] Dissenters also overstate the breadth of the *Corwin* dissent. The dissenting opinion did not focus on whether "BAT had actual control over RAI" in the abstract. (DB 23 n.1.) Rather, as the dissent noted, "the allegations of control are with regard to a particular transaction that is being challenged—the Lorillard acquisition." 371 N.C. at 628 (internal quotation marks omitted); *see also id.* at 646 (concluding that "plaintiff has sufficiently alleged actual control by BAT over the board *in the Lorillard acquisition*" (emphasis added)). The present case involves a different transaction and a different set of facts, which were reviewed in great depth by the Business Court.

Dissenters' challenge to this analysis had merit (which it does not), that would not warrant reversing the Business Court's ultimate fair value determination, which rests on numerous other grounds. *See, e.g.*, R p 186 ¶ 102; *see also Faucette v. 6303 Carmel Rd., LLC*, 242 N.C. App. 267, 274, 775 S.E.2d 316, 323 (N.C. Ct. App. 2015) ("The appellant thus bears the burden of showing not only that an error was committed below, but also that such error was prejudicial—meaning that there was a reasonable possibility that, but for the error, the outcome would have been different." (quoting *Medford v. Davis*, 62 N.C. App. 308, 311, 302 S.E.2d 838, 840 (N.C. Ct. App. 1983))); *Burgess v. C.G. Tate Constr. Co.*, 264 N.C. 82, 83, 140 S.E.2d 766, 767 (1965) ("The burden is on appellant to show not only that there was error in the trial but also that there is a reasonable probability that 'the result was materially affected thereby to his hurt." (quoting *Garland v. Penegar*, 235 N.C. 517, 519, 70 S.E.2d 486, 488 (1952))).

1. The Business Court's Factual Findings Regarding Gompers's Adjusted Unaffected Stock Price Are Supported by the Record.

The Business Court found that "[e]xtensive evidence . . . show[ed] that RAI's fair value was in line with the value that the market ascribed to RAI", and thus that "the market's view of the value of RAI is persuasive evidence of underlying fair value". (R p 229 ¶ 196.) Included in that "extensive evidence" was a market-based metric, RAI's "Adjusted Unaffected Stock Price", that the Business Court found to be "persuasive evidence" of RAI's fair value. (R p 237 ¶ 211.) As explained above (pp 39-40, 76-77), that analysis indexed RAI's 20 October 2016 stock price to market and industry benchmarks to estimate where RAI's stock price would have traded as of the Transaction Date if BAT had not made an offer to buy the company.[17] The analysis indicated that "while RAI's stock price may have appreciated to some degree in the time between the October 20 Offer and the Transaction Date, RAI's stock would still have traded 7% to 10% below the deal price as of July 24, 2017". (R p 237 ¶ 211.)

Dissenters first challenge the starting point of this analysis, contending that the 20 October 2016 price of $47.17 per share did not reflect RAI's fair value on that date "because it failed to incorporate

[17] As explained above at pp 76-77, RAI's actual stock price at the time of closing is not an accurate proxy for fair value because it incorporated value attributable to BAT's announced offer, which cannot be included in RAI's fair value. (R pp 235-36 ¶ 208; N.C.G.S. § 55-13-01(5).)

material non-public information that BAT had and the investing public did not". (DB 90.) But the Business Court expressly found to the contrary, finding that no "nonpublic information warrants disregarding RAI's Unaffected Stock Price as evidence of value". (R pp 233-34 ¶ 203.) Likewise, each of the two pieces of supposedly material non-public information on which Dissenters rely fly in the face of findings of fact that Dissenters do not challenge. Specifically, Dissenters contend that the market did not know RAI "was projecting strong 7-8% growth in years six through ten of its ten-year projections". (DB 90.) As discussed above, however, the ten-year projections simply cannot bear the weight that Dissenters place on them. The Business Court made detailed factual findings about the manner in which those projections were created and the limited purpose for which they were intended. (*See* above pp 28-29, 63-64; R pp 202 ¶ 138, 203 ¶ 140.) It found that "[t]he projected growth rates were not based on any underlying material, value-relevant information about specific business plans or other developments". (R p 235 ¶ 206.) They were instead "based largely on extrapolations of current volume and pricing trends in the industry, which were publicly available and therefore already likely to be reflected in RAI's stock price". (R p 234 ¶ 205.)

The other supposedly material non-public information Dissenters identify is the authorization RAI's Board gave management to repurchase RAI stock "at prices up to $65 per share". (DB 90.) But Dissenters' own expert "pointedly declined to testify that the authorization ceiling was value-relevant information even when prompted by counsel". (R p 235 ¶ 207.) For good reason. As the Business Court found, the authorization ceiling "was not a valuation of RAI. Rather, . . . it was an internal corporate authorization for a purchasing program, which was intentionally set at a price that was higher than what RAI management ever expected it would need to spend". (*Id.*; *see also* R p 214 ¶ 165 (finding that it "was not management's intention to set the share repurchase authorization ceiling at the 'intrinsic value' of RAI's shares").)

Dissenters next argue that RAI's 20 October 2016 stock price was not a reliable indicator of fair value as of that date because BAT made its initial offer at an "opportunistic" time when RAI's stock had fallen. (DB 90.) This again ignores the factual findings of the Business Court, which determined that RAI's common stock price of $47.17 on 20 October 2016 "did not represent a substantial deviation from the price at which RAI's stock was previously trading". (R p 229 ¶ 197.) This finding was well-supported (*see* above pp 22-23), and Dissenters do not argue otherwise.

2. The Business Court's Admission of Gompers's Testimony Regarding the Adjusted Unaffected Stock Price Was Within Its Discretion.

The Business Court's determination of evidentiary issues concerning expert testimony is reviewed under an abuse of discretion standard. *See State v. Anderson*, 322 N.C. 22, 28, 366 S.E.2d 459, 463 (1988) ("In applying [Rule 702], the trial court is afforded wide discretion and will be reversed only for an abuse of that discretion.").

Dissenters claim the Business Court abused its discretion in admitting Gompers's testimony regarding his Adjusted Unaffected Stock Price analysis. (DB 91.) Dissenters offer two bases in support of their argument, both of which train on the adequacy of the evidence supporting the Business Court's finding that "the market for RAI stock was semi-strong form efficient". (R p 232 ¶ 202.)

First, they argue that market efficiency *must* be established through expert testimony and that factual evidence alone can never be sufficient proof. (DB 94-95.) That is wrong. As the Business Court stated, "there is no legal or evidentiary rule in North Carolina requiring a court's determination of market efficiency to reflect a consideration of expert testimony". (R p 322 ¶ 11.) In contrast, Dissenters draw their bright-line evidentiary rule from a rhetorical flourish in a single Delaware case. (DB 94 (citing *Stillwater,* 2019 WL 3943851, at *50.) But *Stillwater* had no cause to decide, or even consider, whether market efficiency can be proven without expert testimony—because the question was not presented in that case. While Dissenters claim it would be "unprecedented" to find market efficiency without expert testimony (DB 94-95), it is their hard-and-fast rule that has no precedent: they identify no case in which a court has held, as a matter of law, that factual evidence is insufficient to show that a stock trades in an efficient market. To the contrary, courts in appraisal proceedings have considered numerous factual criteria in assessing whether the market for a particular security is efficient. *See Dell*, 177 A.3d at 24-27 (identifying numerous facts in the record suggesting an efficient market and reversing lower court's decision in part because it "ignored the efficient market hypothesis long endorsed by this Court"); *see also Jarden,* 2019 WL 3244085, at *27; *In re Appraisal of Solera Holdings, Inc*., 2018 WL 3625644, at *24 (Del. Ch. July 30, 2018). As with other matters of proof, expert testimony on market efficiency may (or may not) be helpful, but there is no law or rule that makes it mandatory.[18]

Second, Dissenters argue that Gompers's Adjusted Unaffected Stock Price analysis lacked appropriate foundation because it relied on the opinion of another expert (Professor Anil Shivdasani) who did not testify at trial. (DB 91.) But as the Business Court found, "given the evidence introduced by RAI, which was not disputed by Dissenters, there [wa]s a sufficient *factual* record" for the Court to find market efficiency. (R p 232 ¶ 202 (emphasis added).) For this reason, Dissenters' reliance on *J.B. Hunt Transport, Inc. v. General Motors Corp*., 243 F.3d 441 (8th Cir. 2001), is misplaced. (*See* DB 93.) That case involved the exclusion of an expert's testimony because the *only* foundation for its relevance was

[18] Moreover, in this case, while *neither* side presented an expert that specifically opined on the efficiency of the market for RAI stock, "[e]xperts for *both* sides . . . agreed that the market for most publicly traded stocks on most days is close to semi-strong form efficient, particularly stock for large companies like RAI". (R p 232 ¶ 202 (emphasis added).)

the testimony of another expert that had been excluded. *J.B. Hunt*, 243 F.3d at 444-45. Here, Gompers's testimony was supported by substantial, uncontroverted fact evidence. (R p 231-33 ¶¶ 201-02.)[19]

Dissenters also appear to dispute whether the facts relied on by the Business Court are sufficient to allow the conclusion of an efficient market for RAI stock. Tellingly, however, while Dissenters devote five pages of their brief to criticizing the relevance of the (undisputed) facts on which the Business Court relied (DB 95-99), Dissenters do not advance a solitary shred of trial evidence pointing in the other direction. Dissenters identify literally nothing in the record that shows the market for RAI stock to have been inefficient. Thus, they ask this Court to reject the detailed findings of the Business Court as clearly erroneous without putting so much as a feather on the other side of the scale.

In any event, Dissenters' criticism of the relevance of the Business Court's factual findings is unfounded. The record included evidence showing, among other things, that (i) RAI was publicly traded on the

[19] Dissenters' remaining cases are even further afield. They involve experts who simply "parrot[ed]" the opinions of a non-testifying expert without independently verifying the non-testifying expert's conclusions. (DB 93-94 (citing cases).) Even Dissenters do not contend that Gompers tried to pass off Shivdasani's opinions as his own.

NYSE, making it highly liquid, (ii) RAI was a very large company with a market capitalization of nearly $70 billion as of 20 October 2016, (iii) information about RAI was both widely available and readily disseminated to the market, (iv) RAI's historical stock price increased and decreased in relation to the release of new company-specific information and market-wide trends and (v) RAI's stock was followed by 16 equity analysts, who frequently published research about the company. (R p 232 ¶ 202.) These same factors have been considered by other appraisal courts to support the conclusion that a stock trades on an efficient market. *See Jarden*, 2019 WL 3244085, at *27-29; *Dell*, 177 A.3d at 7; *DFC*, 172 A.3d at 352-53, 372-73. The Business Court was in very good company in relying on these factors to assess market efficiency.

Despite the fact that appraisal courts *have* considered these factors, Dissenters argue that courts *should not* do so because they "are not designed or intended to identify markets in which trading price is a reliable proxy for fundamental value". (DB 96.) This request for the Court to break new ground by rejecting the relevance of these factors is particularly inappropriate in this case. The primary reason a stock with these "informationally efficient" characteristics might not trade at its intrinsic value is if there is material nonpublic information about the company's prospects. *See Fir Tree Value Master Fund, LP v. Jarden Corp.*, 236 A.3d 313, 324 n.56 (Del. 2020) ("[T]he share price of a company's stock, even when informationally efficient, may diverge occasionally from the stock's fundamentally efficient price. This divergence occurs, however, only when and to the extent that there is material nonpublic information that is not impounded in a company's share prices." (citation omitted)). Here, as noted above, the Business Court made a factual finding that there was no material nonpublic information as of BAT's offer on 20 October 2016 (R pp 233-34 ¶ 203)—meaning there is no reason that the traditional market efficiency factors on which the Business Court relied would lead to a mistaken result.

E. The Business Court Properly Determined that Fair Value Does Not Include a "Control Premium".

Dissenters next argue that the Business Court improperly failed to add a so-called "control premium" when considering market-based evidence of RAI's value. (DB 99-100.)[20] Once again, Dissenters completely ignore—indeed do not even mention—the Business Court's factual findings on this point.[21] They instead provide a now-discredited theoretical disquisition on the meaning of a control premium, which was refuted by the trial testimony *of their own expert*.

As the Business Court properly found, the record evidence showed that "[a] control premium is the additional value that a buyer ascribes to an asset under the assumption that the buyer will be able to derive more value from the asset". (R p 273 ¶ 298.) It is "what an acquirer is willing to pay because they can better manage that asset, drive additional cash flows from that asset or get synergies". (R p 273 ¶ 298.) In other words, "[t]he value attributable to a control premium is a subjective value on behalf of the acquirer; that is, it only reflects the value the acquirer believes it can add" by *improving* the financial performance of the

[20] As with Dissenters' challenge to the Adjusted Unaffected Stock Price analysis discussed above, this challenge addresses only a subset of the various indicators of value on which the Business Court relied. For example, it does not relate to the deal price, the Financial Advisors' DCF calculations, analyst and market reaction, or precedent transactions. Thus, even if Dissenters' challenge had merit (which it does not), it would not warrant upsetting the Business Court's fair value determination. *See Faucette*, 242 N.C. App. at 274; *Burgess*, 264 N.C. at 83.

[21] Dissenters focus entirely on the Business Court's conclusion in paragraph 354 of its opinion, without acknowledging the lengthier treatment of the issue in paragraphs 298-301.

company. (R p 273 ¶ 299.) It is not what the statutory definition of fair value contemplates: "the value of that company under the existing management—assuming that no transaction occurred". (R p 310 ¶ 375.)

The Business Court grounded this finding in the trial testimony of *both sides*' experts. Gompers explained that "the control premium represents the increase in value . . . that can be generated because the new acquirer can be more efficient [and] do things better than the existing management. And that's why somebody buys the assets because they believe that they're going to be better. . . . And so that control premium represents the value only under the control of the entity that buys it." (T p 912:10-17.) Likewise, *Dissenters*' expert, Professor Bilge Yilmaz, testified that fair value should be determined for the company "as an independent firm that is expected to go on as an independent entity". (R pp 273-74 ¶ 300; T pp 1866:24-1867:4.) To emphasize the point, when asked to "explain the definition of fair value that [he] used for the purpose of [his] analyses", he testified: "Just to be sure we are all on the same page, this does not have any kind of minority discount or some kind of acquisition premium or control premium attached to it." (R pp 273-74 ¶ 300; T pp 1866:24-1867:10.)

Ignoring all of this, Dissenters wrongly contend that the Business Court relied *only* on other testimony from Gompers, in which he explained that it is improper to add a control premium to a DCF valuation. (DB 101-02.) Dissenters contend that because *this* testimony related to a DCF valuation, it is irrelevant to the Business Court's conclusion that a control premium should not be added to market-based evidence like stock price. (*Id.*) But as shown above, the Business Court relied on a wealth of *other* testimony that Dissenters omit from their brief. In any event, even in this testimony, Gompers explained that "[t]he way to think about it is that there's a set of projections under the existing management and the DCF value of that will equal the stock price". (T p 787:5-7; *see also id.* at 787:19 ("DCF value should equal the share price with no discount").) The cited testimony was therefore equally applicable to market-based evidence like stock price, precisely as the Business Court found.[22]

[22] Dissenters also focus on other testimony from Gompers, in which he described a minority discount as the "flip of a control premium". (DB 100-01.) But in this respect, Gompers is again in accord with Yilmaz in explaining that the "fair value" of an independent entity includes *neither* a minority discount *nor* a control premium. So this testimony is no help to Dissenters. In any event, determining which testimony in the record to credit is squarely the province of the Business Court; there is no doubt that there is more than sufficient evidence (which Dissenters simply ignore) to support the Court's finding here.

Thus, without any support in the record—indeed, not a single citation to any of their own experts—they ask this Court to strike out on a path that finds no support in current law or the academic literature. They assert that an appraisal court *must* add a control premium to market-based valuations of a public company to account for an "implicit minority discount" present in publicly traded shares.[23] (DB 100-01.) In support, Dissenters cite three opinions from Delaware courts, the most recent of which is from 2004. (DB 100-02.) To the extent these opinions were ever the law in Delaware, that is no longer true. As the Delaware Supreme Court held earlier this year, "[t]here is no 'long-recognized principle' that a corporation's unaffected stock price cannot equate to fair value". *See Fir Tree*, 236 A.3d at 316. In that opinion, the Court affirmed an appraisal decision in which the trial court relied on publicly traded stock price as evidence of fair value, without indicating that the price

[23] Rather than afflicting all stocks, a "minority discount" is "[a] reduction in the value of a closely-held business's shares that are owned by someone who has only a minority interest in the business". *Minority Discount*, Black's Law Dictionary (11th ed. 2019). Thus, the appraisal case law about minority discounts in Model Act states like North Carolina relates largely to closely held companies. *See, e.g.*, *Brown v. Arp & Hammond Hardware Co.*, 141 P.3d 673, 676, 684 (Wyo. 2006); *First W. Bank Wall v. Olsen*, 621 N.W.2d 611, 614, 617 (S.D. 2001); *see also* R pp 300-01. Dissenters' reliance on the portion of N.C.G.S. § 55-13-01(5) that requires fair value to be determined without "discounting for lack of marketability or minority status" is therefore unwarranted.

incorporated a minority discount and without adding a control premium. *See id.* Other recent Delaware Supreme Court appraisal decisions have likewise considered stock price as evidence of fair value without adding a control premium. *See, e.g.*, *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*, 177 A.3d 1, 6 (Del. 2017); *Aruba Networks, Inc.*, 210 A.3d at 138 ("[T]he price a stock trades at in an efficient market is an important indicator of its economic value that should be given weight . . . .").

Dissenters' attack on the Business Court's citation to an article by Professors Hamermesh and Wachter on the grounds that it applies only to issues that are supposedly unique to Delaware law's conception of "fair value" (DB 102-03) is unfounded. The passage cited by the Business Court is not tied to Delaware law; it focuses on "financial or empirical scholarship" and it could not possibly be clearer. (R p 301 ¶ 354 ("[N]ot a single piece of financial or empirical scholarship affirms the core premise of the IMD [implicit minority discount]—that public company shares systematically trade at a substantial discount to the net present value of the corporation." (citing Lawrence A. Hamermesh & Michael L. Wachter, *The Short and Puzzling Life of the "Implicit Minority Discount"* *in Delaware Appraisal Law*, 156 U. Pa. L. Rev. 1, 5-6 (2007))).) The Business Court's citation to this scholarship to corroborate the factual record was not an error, particularly when Dissenters offer nothing in response.[24]

Dissenters' invocation of this Court's decision in *Corwin v. British American Tobacco PLC*, 371 N.C. 605, 821 S.E.2d 729 (2018), is also off base. (DB 103-04.) The *Corwin* Court was not asked to, and did not, address whether RAI's shares traded at a discount to their fair value. *See id.* at 606, 624. Indeed, to the extent *Corwin* is relevant, it supports the Business Court's determination because it affirmed the dismissal of a claim that BAT was a controlling stockholder—making it *less* likely that there was any such discount in RAI's trading price. To be sure, the dissenting opinion in *Corwin* deemed the allegations of control sufficient

[24] Dissenters' misguided effort to distinguish Delaware and North Carolina law on this point is curious, given that their only support for their control premium argument is in Delaware trial court cases from the turn of the century. In any event, Dissenters' description of the Hamermesh and Wachter article is wrong. The authors do not say, as Dissenters contend, that Delaware courts have determined that fair value "should reflect whatever minority discount inheres in the market price of a corporation's stock". (DB 103.) Rather, the authors say that, in the absence of a controller, there *is no* minority discount to fair value, "let alone a wrongful discount". *See* Hamermesh & Wachter, at 52-53. Ironically, the section of the article that Dissenters cite is titled "Why the Delaware Bench and Bar Fell Into Error" and explains why outdated cases, such as those on which Dissenters rely, were incorrect. *Id.*

to warrant proceeding on to discovery, but, as noted above (pp 104-05), the Business Court here actually *had* full discovery and trial, and reached its determination on the basis of an extensive factual record that contained no evidence that a control premium should be added to market-based metrics of RAI's value.

Dissenters' partial quotation of the *Corwin* dissent's concern about BAT's being able to "get the milk without buying the cow" is especially inapt. (DB 103.) The dissent was discussing allegations in Corwin's complaint that RAI's Board had "agreed to allow BAT to access Reynolds's game-changing technology without adequate compensation", and that "this 'forestalls a takeover by making Reynolds a significantly less attractive takeover target for BAT,' or in other words, it allows BAT to 'get the milk without buying the cow'". *Corwin*, 371 N.C. at 646 (Hudson, J., dissenting). In the transaction now under review, however, BAT *did* pursue a takeover—it bought the proverbial cow. The only question is the fair value of the shares it bought, and *Corwin* does not speak to that question.[25]

III. THE BUSINESS COURT DID NOT ABUSE ITS DISCRETION BY ADMITTING GOMPERS'S TESTIMONY.

Dissenters contend that the Business Court made other incorrect evidentiary rulings pertaining to Gompers's testimony (beyond those discussed above in Part II.D.2). Specifically, Dissenters claim that they were entitled to an adverse inference regarding the efficiency of RAI's stock and the exclusion of certain of Gompers's testimony because it constituted improper "vouching" and improper summarization of facts. These evidentiary issues were committed to the sound discretion of the Business Court, *see Anderson*, 322 N.C. at 28, 366 S.E.2d at 463, and Dissenters have not shown that the Business Court abused that discretion.

[25] Dissenters' final argument—that not adding a control premium to market-based metrics would make appraisal a worthless remedy (DB 105-06)—is just a rehash of their view that appraisal should capture the value that a buyer pays because it believes it can improve the financial performance of the company. That is not correct. An appraisal dissenter is entitled to no more and no less than the fair value of the shares it holds, as if the company were continuing as an independent entity, without the benefits the buyer will bring. *See* N.C.G.S. § 55-13-01(5). The appraisal remedy is a protection against shareholders being forced to sell their shares for *less* than what they are currently worth; it is not a tool for claiming *additional* value.

A. The Business Court Appropriately Denied Dissenters' Request for an Adverse Inference.

Prior to trial, RAI notified Dissenters that it had chosen not to call Professor Shivdasani to provide an expert opinion at trial regarding market efficiency. Dissenters likewise chose not to elicit trial testimony from Shivdasani, either through a trial subpoena (he resides in Chapel Hill) or through his deposition testimony pursuant to Rule 32(a)(4) of the North Carolina Rules of Civil Procedure. Dissenters also chose not to introduce *any* evidence of their own regarding market efficiency. Instead, they requested an adverse inference against RAI on the issue of market efficiency pursuant to the "missing witness rule". The Business Court's decision not to draw an adverse inference was well within its discretion.[26] (R p 327 ¶ 18.)

"The 'missing witness rule' is not a rule; it is simply a '*permissible* inference that a factfinder *may* draw from the absence of a potential witness who might have knowledge of facts at issue in the case.'" (R p 326 ¶ 17 (quoting *Harris v. State*, 458 Md. 370, 182 A.3d 821, 832 (Md. 2018)

[26] Even if it had not been within the Business Court's discretion, error on this ground would not justify reversal, given the wide variety of other evidence supporting the Business Court's fair value determination. (*See* above n.20.)

(emphasis added)).) Dissenters have not identified a single instance in which a North Carolina court was *required* to draw an adverse inference based on a witness's absence from trial. Additionally, "North Carolina courts have never suggested that the missing witness rule should apply to expert witnesses". (R p 327 ¶ 19.) The rule has been applied only to *fact* witnesses with unique information unavailable from another source. *See, e.g.*, *Sunbelt Rentals, Inc. v. Head & Engquist Equip., L.L.C.*, No. 00-CVS-10358, 2003 WL 21017456, at *49 (N.C. Super. Ct. May 2, 2003).

Pointing to authority from other states, Dissenters contend that the missing witness rule should apply to expert witnesses (DB 121-22), but they do not address the authorities cited by the Business Court, including decisions by the Supreme Courts of New Jersey and South Carolina, that offer persuasive reasons why the missing witness rule ought not to apply to experts. (R pp 327-28 ¶ 19.) The New Jersey Supreme Court in *Washington v. Perez* held that it was reversible error for a trial court to grant a missing witness instruction regarding an expert witness. 219 N.J. 338, 359-65, 98 A.3d 1140, 1152-55 (N.J. 2014). After describing in detail the development of the missing witness rule, including that it "should not be a reflexive response whenever a party fails to call an expected witness", *id.* 361, the court in *Washington* noted that "[t]here are significant distinctions between the testimony of expert witnesses and the testimony of fact witnesses, which are pertinent to the adverse inference charge", *id.* at 361-64. Among the reasons identified were (i) the fact that modern discovery rules afford an opposing party significant information about an expert witness's testimony, such that the testimony is "unlikely to be a mystery to the parties and their counsel when a case proceeds to trial"; (ii) "an expert is unlikely to be in exclusive possession of factual evidence that would justify an adverse inference charge", and "any facts or data that support the expert's opinion must be disclosed in his or her report"; (iii) court rules "do not preclude a party from choosing among multiple experts identified before trial, or foregoing the presentation of expert testimony entirely"; and (iv) "there are many strategic and practical reasons that may prompt a party who has retained an expert witness to decide not to present the expert's testimony at trial", including cost, redundancy and availability. *Id.* at 1153-55.

The South Carolina Supreme Court analyzed the applicability of the missing witness rule in the context of a psychiatric expert. *In re Gonzalez*, 409 S.C. 621, 627-35, 763 S.E.2d 210, 213-17 (S.C. 2014). After describing the origin and rationale behind the missing witness rule, that court determined that the complexity of expert witness testimony was ill-suited to application of an adverse inference, which would allow a non-expert factfinder "to simply *speculate* as to what the expert might have said". *Id.* at 635. Accordingly, the court held that "[b]ecause of the risk of unfairness that such adverse inferences could impose, we hold today that a party's invocation of the missing witness rule should be limited to *fact* witnesses, and it should not be applied to *opinion* witnesses".[27] *Id.*

Instead of addressing these cases, Dissenters assert without explanation that their chosen set of out-of-state authority is "better-reasoned". (DB 121.) Dissenters are mistaken. Unlike the authorities cited by the Business Court, which analyzed in detail whether the missing witness rule should apply to experts, none of Dissenters' cases actually addressed that issue head on. *See Taylor v. Kohli*, 162 Ill.2d 91, 96-98, 642 N.E.2d 467, 469-70 (Ill. 1994) (addressing whether a party

[27] Dissenters' suggestion that the *only* reason a party might not call one of its experts at trial is to "hide" the expert's testimony (DB 118, 123-24) ignores these courts' cogent explanations, as well as the realities of trial practice, in which parties routinely decide not to call witnesses who were on their original witness lists. Were it otherwise, *RAI* would be entitled to the benefit of an adverse inference on fair value, because Dissenters chose not to call one of their own valuation experts, Robert Taylor. (R p 125 ¶ 19; R p 145 ¶ 6 n.1.)

effectively abandoned its expert witness before trial); *DeVito v. Feliciano*, 22 N.Y.3d 159, 165-66, 1 N.E.3d 791, 796 (N.Y. 2013) (addressing whether a party's treating physician's testimony would be cumulative); *Cler v. Providence Health System-Oregon*, 349 Or. 481, 488-90, 245 P.3d 642, 647 (Ore. 2010) (stating that the trial court improperly permitted portions of counsel's closing statement addressing matters outside the record); *Kovach v. Solomon*, 732 A.2d 1, 10-11 (Pa. Super. Ct. 1999) (addressing whether a party's failure to remove a witness from its witness list seven days before trial in violation of a local rule prevented the witness from being "equally available" to opposing counsel); *Dickey v. McCord*, 63 S.W.3d 714, 722 (Tenn. Ct. App. 2001) (affirming the lower court's *refusal* to apply missing witness rule to an expert).[28]

Moreover, Shivdasani was not a "missing" witness. Dissenters were free to seek to serve a trial subpoena or to introduce his deposition testimony through Rule of Civil Procedure 32(a)(4). N.C. R. Civ.

[28] Dissenters also cite the Connecticut Supreme Court's 1994 decision in *State v. Ross*, 230 Conn. 183, 646 A.2d 1318 (Conn. 1994) (DB 122), but fail to note that the legislature in Connecticut has expressly prohibited the use of the missing witness instruction in civil cases, *see* Conn. Gen. Stat. § 52-216c, and that Connecticut's Supreme Court has held that the missing witness instruction may not be applied in criminal cases. *State v. Malave*, 250 Conn. 722, 730, 737 A.2d 442, 447 (Conn. 1999) ("[W]e conclude that the rule should be abandoned in criminal cases.").

P. 32(a)(4) ("The deposition of a witness, whether or not a party, may be used by any party for any purpose if the court finds: . . . the witness is an expert witness whose testimony has been procured by videotape as provided for under Rule 30(b)(4)."). Dissenters contend that their ability to introduce Shivdasani's testimony is irrelevant because, as RAI's expert, he was in their view under RAI's control—and they argue that "a witness who is under the control of one party . . . is not 'equally available' to the other side". (DB 125.) But their own cases say the opposite. *See, e.g.*, *People v. Gonzalez*, 68 N.Y.2d 424, 428, 502 N.E.2d 583, 586 (N.Y. 1986) ("It is to be emphasized that the 'availability' of a witness is a separate consideration from that of 'control'. 'Availability' simply refers to the party's ability to produce such witness."). The fact is that Dissenters offer no explanation for why they elected not to call an expert whose report they claim to have been favorable for them, whose deposition testimony was on videotape and whose opinions they now deem to be so critically important.[29] As noted previously (p 113),

[29] That has not stopped Dissenters from asserting on appeal what they (incorrectly) contend Shivdasani's testimony would have shown. (DB 120, 124 n.34.) If that testimony were as helpful as they contend, they could and should have offered it at trial. Having foregone the opportunity to do so, their incorrect characterization of it should be disregarded on appeal.

Dissenters also failed to introduce any evidence of their own regarding market efficiency.[30]

Further, the Business Court was well within its discretion to find that the missing witness rule ought not to apply in this case because RAI had a reasonable basis not to offer testimony from Shivdasani—specifically, that his testimony was unnecessary because, as the Business Court ultimately found, there was sufficient evidence and testimony from other witnesses establishing the facts necessary for the Court to find that RAI's stock traded efficiently. R p 289 ¶ 333; *see, e.g.*, *Taylor*, 162 Ill. 2d at 96 ("In general, the missing-witness instruction is available when . . . there is no reasonable excuse shown for the failure to produce the witness."); *State v. Montgomery*, 163 Wash. 2d 577, 599, 183 P.3d 267, 278 (Wash. 2008) ("[T]he doctrine applies only if the witness's absence is not satisfactorily explained."); *see also* McCormick on Evidence § 264 (7th ed. 2016) ("if the testimony of the witness would be merely cumulative, the inference is unavailable").

[30] Dissenters' ability to call Shivdasani under Rule 32(a)(4) is another basis for distinguishing the out-of-state authority on which Dissenters rely. None of those jurisdictions has a comparable rule. Indeed, in the first case they cite, the appellate court held that the trial court erred in permitting an opposing party's expert's deposition testimony to be introduced when the expert was not called to testify at trial. *See Taylor*, 162 Ill. 2d at 96.

B. Gompers Did Not Improperly "Vouch" for the Work of Others.

Dissenters assert that portions of Gompers's expert testimony evaluating the reasonableness of the inputs used in RAI's financial advisors' DCF analyses amounted to improper "vouching". (DB 126-28.) Vouching occurs when an expert merely "parrots" or "rubber stamps" an opinion from another witness. *See In re Wagner*, No. 06-cv-01026, 2007 WL 966010, at *3-4 (E.D. Pa. Mar. 29, 2007); *Loeffel Steel Prods., Inc. v. Delta Brands, Inc.*, 387 F. Supp. 2d 794, 824 (N.D. Ill. 2005). The Business Court was well within its discretion to conclude that Gompers did not "rubber stamp" the DCF analyses performed by the Financial Advisors.

As Gompers explained at trial, he formed his opinion regarding the reasonableness of the Financial Advisors' DCF inputs only after conducting detailed analyses commonly performed by financial economists. (*See* T pp 745:2-20; 746:7-747:13.) Gompers testified that he performed precisely the same type of analysis to review the Financial Advisors' DCF analyses as if he were conducting his own DCF-based valuation. (T p 745:2-20.) And in addition to reviewing the Financial Advisors' DCF inputs, Gompers did his own multiples analyses to serve as market checks on the Financial Advisors' DCF inputs and overall valuations. (*See* T pp 752:1-753:18; 770:7-771:6; 779:25-780:16.) The Business Court properly found that Gompers did not rubber stamp the results of the Financial Advisors' DCF valuations—he extensively evaluated and stress-tested the Financial Advisors' DCF inputs and made his own expert determination that they were reasonable.[31] (R pp 320-21 ¶¶ 8-9.)

An examination of the authorities relied upon by Dissenters demonstrates how flawed their characterization of Gompers's testimony is. The lone North Carolina case on which Dissenters rely for their "no vouching" principle, *State v. Bullock*, No. COA10-320, 2010 WL 4290134 (N.C. Ct. App. Nov. 2, 2010), stands for a very different proposition than the one Dissenters espouse. (DB 126-27.) Based on "the application of North Carolina Rules of Evidence 608(a) and 405(a)", each of which relates to the introduction of character evidence, the court in *Bullock*

[31] Dissenters' framing of Gompers's testimony as "[o]ne of the worst abuses in civil litigation" (DB 126) is unfortunate and baseless. Contrary to Dissenters' unsupported accusations, Gompers's testimony about opinions he personally formed based on work that he did, which was fully disclosed and tested through discovery, was accurate and credible, as the Business Court found. (R pp 320-25.)

stated that "[t]he testimony of an expert to the effect that a prosecuting witness is believable, credible, or telling the truth is inadmissible evidence". *Id.* at *3 (quoting *State v. Bailey*, 89 N.C. App. 212, 219, 365 S.E.2d 651, 655 (1988)). This "no vouching" concept is inapplicable here because Gompers's testimony did not pertain to the personal credibility or veracity of any other witness.

Dissenters next assert that this case is "analytically indistinguishable" from *FrontFour Capital Grp. LLC v. Taube*, No. 2019-0100-KJSM, 2019 WL 1313408 (Del. Ch. Mar. 11, 2019), a merger case from Delaware. (DB 129.) Again, Dissenters' comparison is inapt. In *FrontFour*, the defendants' expert opined only on the "process" used by the investment banks. 2019 WL 1313408, at *26. In contrast, Gompers went well beyond "process"; he stress-tested the substance of the Financial Advisors' work and assessed the validity of their inputs and assumptions. (*See* T pp 745:2-747:13.) Rather than simply opining that RAI's Financial Advisors used a proper "process" for performing a DCF analysis, Gompers scrutinized the inputs that the Financial Advisors selected, analyzed them by performing customary valuation techniques of the kind he would have performed had he done his own valuation, and on the basis of that independent work concluded that the Financial Advisors' DCF inputs were reasonable. (*See id.*; T pp 752:1-757:23.)

Dissenters' other cases from outside North Carolina fare no better. They cite *In re Wagner* for the proposition that "[t]he Federal Rules of Evidence do not permit experts to simply 'parrot' the ideas of other experts or individuals." (DB 128 (quoting *In re Wagner*, 2007 WL 966010, at *4).) But the trial court in *Wagner* overturned the magistrate judge's decision to exclude testimony from an expert witness, and permitted that testimony because, among other things, the expert's opinion was based on "the type of materials upon which an expert in his field would rely". *In re Wagner*, 2007 WL 966010, at *3. Just so here. Gompers used his expertise as a financial economist to assess the reasonableness of the inputs to the Financial Advisors' DCF analyses and to cross-check them by using other valuation methodologies, such as comparable companies and precedent transactions analyses, which are commonly used by financial economists. (*See* T pp 745:2-747:13; 752:1-757:23.) He did not simply repeat the Financial Advisors' conclusions; he applied his training and expertise to form an independent opinion as to the soundness of their work.

Dissenters' reliance on *Loeffel* also is misplaced. There, the trial court excluded an expert witness from testifying because the expert himself admitted that the theory on which he relied was "beyond [his] ken". *Loeffel*, 387 F. Supp. 2d at 824 (internal quotation marks omitted). *Ash Grove Cement Co. v. Employers Insurance* suffers from a similar defect. 246 F.R.D. 656, 661 (D. Kan. 2007) (excluding testimony that was "within the province of an expert on coatings" by an expert who represented that he would "not serve as a coatings expert"). In contrast to the experts in *Loeffel* and *Ash Grove Cement*, Gompers is indisputably qualified as an expert in financial economics and has extensive expertise applying the valuation methodologies in this case.

Virginia Power Energy Marketing, Inc. v. EQT Energy, LLC also provides no support for Dissenters. No. 11cv630, 2012 WL 13034278, at*1 (E.D. Va. May 9, 2012). There, the trial court properly excluded one of an expert's "opinions" that read, in its entirety, "I have reviewed the Protivti [sic] report produced by Guy Davis and, in my opinion, its analysis is consistent with the standard process used in the industry to quantify the value of natural gas pipeline firm capacity release agreements." *See* Expert Report of George Briden at 5, *Va. Power Energy*

Mktg., Inc. v. EQT Energy, LLC, 2012 WL 7040505. Such an opinion is plainly unhelpful to the trial court, fails to disclose the bases for the expert's own independent conclusion and warrants exclusion.

In *HealthOne v. UnitedHealth Grp.*, No. 10-cv-01633-WYD, 2012 WL 94678 (D. Colo. Jan. 12, 2012), on which Dissenters also rely (DB 127), the court *denied* a motion to exclude expert testimony and found that if the information at issue was of a type "reasonably relied upon by experts in [their] field in forming opinions or inferences", then such evidence "may be proper". *Id.* at *6. Both *Matter of James Wilson Associates*, 965 F.2d 160 (7th Cir. 1992) and *Dura Automotive Systems of Indiana, Inc. v. CTS Corp.*, 285 F.3d 609 (7th Cir. 2002), involved an expert who sought to testify in areas beyond his "domain of expertise" by adopting the statements of a non-testifying expert in a different specialty. *James Wilson Associates*, at 172-73; *Dura Auto.*, at 613-14. Here, Gompers testified about corporate valuation—a subject squarely within his expertise.

The Business Court acted within its discretion in rejecting Dissenters' "vouching" objection to Gompers's testimony.

C. Gompers Did Not Impermissibly Summarize Fact Evidence or Hearsay.

Dissenters' attack on the Business Court's decision overruling their intertwined objections that Gompers's testimony was a "summation of the factual record" and "recitation of hearsay" contained in analyst reports (DB 126-35) fails on every level.

The testimony identified by Dissenters as improper summary in fact reflects the proper application of Gompers's expertise as a financial economist to the facts of this case. For example, Gompers explained the economic problems with performing a DCF using projections that ignore known risks to RAI's cash flows (T pp 732:24-733:7), why as a matter of DCF methodology it was appropriate for the Financial Advisors to use the October 2016 projections even though they were optimistic (T p 735:8-24), and why the PGR and discount rate ranges used in mid-2016 to derive the ceiling for management's authority to make share repurchases did not alter his opinions about the Financial Advisors' DCF inputs (T p 760:14-22). He did not merely "re-hash" the record. Rather, in each case, Gompers applied his own specialized expertise to the record evidence and offered independent opinions grounded in financial economics. The Business Court's decision is therefore amply supported. (R pp 321-25.)

Dissenters' claim that Gompers engaged in "recitation of hearsay" contained in analyst reports (DB 130) fails for a similar reason. Rule 703 permits experts to rely on hearsay and other inadmissible evidence to support their opinions. N.C. R. Evid. 703 ("If of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence."). Numerous witnesses—including the Financial Advisors, both sides' experts and a representative of one of the Dissenters—testified that analyst reports are commonly relied upon when forming opinions on corporate valuation. (R pp 323-25 ¶¶ 13-15.) That is what Gompers did when he "examined each individual analyst report and explained how the reports supported his conclusions". (R p 325 ¶ 15.)

This Court's opinion in *State v. Robinson*, 330 N.C. 1, 409 S.E.2d 288 (N.C. 1991) (cited at DB 130), does not help Dissenters. There, an expert psychologist sought to testify about the results of an experiment without actually offering an opinion based on those results. *Id.* at 25-26. The court determined that, because the expert was not using the experiment as a basis for his opinion, the testimony was offered only for the truth of the experiment's results and was thus hearsay. *Id.* Here, by contrast, the Business Court found that Gompers explained how the analyst reports informed his opinions. (R p 325 ¶ 15; *see also* T pp 729:24-731:5; 745:2-747:2; 751:3-18; 801:21-23; 802:12-803:8.) Dissenters' other authorities are inapplicable for the same reason. *See, e.g.*, *SEC v. Bankatlantic Bancorp, Inc.*, No. 12-60082, 2013 WL 12009694, at *8-9, 12 (S.D. Fla. Nov. 14, 2013) (excluding expert testimony where substance of analyst reports was conveyed without expert's offering any opinion to which the reports related).

In response, Dissenters appear to say that Gompers could not have used the hearsay analyst reports to support his opinions because, in their view, he did not offer any opinions. (DB 132 ("Gompers did not rely on analyst reports to perform his own discounted cash flow analysis. Gompers *did not perform a discounted cash flow analysis at all.*" (emphasis in original)); DB 133 ("Gompers admitted that he *did not* use analyst reports in connection with his own perpetuity growth rate analysis because *he did not perform any such analysis*." (emphasis in original)).) At its core, Dissenters' argument is that a DCF analysis is the only valuation concept or technique through which a financial economist may offer a valuation opinion (such that not doing an independent DCF valuation from the ground up is equivalent to offering no opinion at all), and that Gompers's opinions and the bases for them should have been excluded by the Business Court for that reason. Dissenters cite no authority for that proposition. As the Business Court properly found, "Gompers performed extensive independent work" applying his undisputed expertise in order to, among other things, "test the Financial Advisors' DCF-based valuations of RAI . . . and to explain why Zmijewski's valuation of RAI was an outlier when compared to all other evidence of value in this case". (R pp 321-22 ¶ 10.)

The Business Court did not abuse its discretion in admitting Gompers's testimony.

IV. DISSENTERS ARE NOT ENTITLED TO AN INTEREST AWARD BECAUSE THEY ALREADY RECEIVED FAIR VALUE (PLUS INTEREST) FOR THEIR SHARES.

Dissenters' interest calculation, proffered as an application of the "plain language" of N.C.G.S. § 55-13-30(e), is both inconsistent with the plain language and substantively absurd, and it was correctly rejected by the Business Court. (R p 312 ¶ 379 ("[Dissenters'] interpretation would result in an interest award to Dissenters in this action of over $100 million even though the Court has concluded that RAI paid them fair value for their shares. The Court concludes that this is a nonsensical result, one supported neither by the text of the statute nor the intent of the legislature.").)

A. Dissenters Ignore the Statutory Definition of "Interest".

Dissenters' argument is premised on the statutory language providing for judgment "for the amount, if any, by which the court finds the fair value of the shareholder's shares, *plus interest*, exceeds the amount paid by the corporation to the shareholder". N.C.G.S. § 55-13-30(e) (emphasis added). Dissenters interpret the italicized words "plus interest" in effect to mean "plus an amount calculated by applying the statutory interest rate to the entire fair value of the shares for the entire period between the merger closing and satisfaction of a judgment". But that is not how "interest" is defined in the statute. Under N.C.G.S. § 55-13-01(6), "interest" is calculated by applying the statutory rate "from the effective date of the corporate action *until the date of payment*" (emphasis added). Thus, under the plain language of the statute (as in common understanding), interest stops running on an amount when that amount is paid.

The following example demonstrates why this common sense interpretation is warranted (and why Dissenters' interpretation was properly rejected). Suppose the Business Court had found the fair value of RAI shares to have been $60. The statutory phrase "plus interest" would then have required calculating interest on $60 "until the date of payment". For the first $59.64, interest would run until it was paid in 2017. For the remaining $0.36, interest likewise would have run until it was paid per the Court's hypothetical judgment at the end of the appraisal proceedings. This straightforward application of the statutory text corresponds with the ordinary understanding of "interest" in finance and in the English language.[32] By contrast, under Dissenters' interpretation, interest would continue to run on the $59.64 even after RAI paid that amount, in violation of the statutory definition. It would

[32] This reading also makes sense of the phrase "if any" in N.C.G.S. § 55-13-30(e). With this phrase, the statute contemplates that in some instances the fair value of the shares "plus interest" will not exceed the amount already paid. Under Dissenters' reading, that would likely never happen unless a company wildly overestimates fair value and overpays a dissenter under N.C.G.S. § 55-13-25. In fact, under Dissenters' reading, shareholders could still receive interest awards even if the corporation paid *more* than fair value, because interest would continue to accrue during the litigation.

also allow Dissenters to earn a return on that $59.64 twice—once at the statutory rate from RAI and once at whatever rate they earned in the market since RAI paid them that money in 2017.[33]

B. Dissenters' Interpretation of the Statute Has Been Rejected Overwhelmingly.

The one case cited by Dissenters adopting their preferred interest calculation stands alone. *See Torrington Rsch. Co. v. Marvin*, No. CV064005175, 2010 WL 1667580 (Conn. Super. Ct. Apr. 6, 2010) (cited at DB 137). In contrast to the Connecticut trial court opinion in *Torrington*, the case law in Model Act states with statutory language similar or identical to North Carolina's calculates interest in a manner consistent with the Business Court.[34] Dissenters do not address this point, wrongly ignoring extensive contrary authority. Further,

[33] The perverse effect of Dissenters' interpretation would be to limit corporations' incentive to make robust payments to dissenting shareholders. After all, if interest continued to run on any amounts paid to the dissenters, then corporations would be better off paying less and keeping more of the money for themselves during the pendency of appraisal proceedings.

[34] *See, e.g.*, *Pueblo Bancorporation v. Lindoe, Inc.*, 63 P.3d 353, 357 (Colo. 2003); *Ely, Inc. v. Wiley*, No. LA-22998, Slip Op. at 9 (Iowa Dist. Ct. Aug. 31, 1994), *rev'd on other grounds*, 546 N.W.2d 218 (Iowa Ct. App. 1996); *First W. Bank Wall v. Olsen,* 621 N.W.2d 611, 615 (S.D. 2001); *Utah Res. Int'l, Inc. v. Mark Techs. Corp.*, 342 P.3d 761, 768 (Utah 2014); *HMO-W Inc. v. SSM Health Care Sys.*, 266 Wis. 2d 69, 72-75, 667 N.W.2d 733, 735-36 (Wis. Ct. App. 2003); *Brown v. Arp & Hammond Hardware Co.*, 141 P.3d 673, 677 (Wyo. 2006).

Torrington has not been cited by any other case, in Connecticut or elsewhere, in calculating interest on an appraisal award. Although the court in *Torrington* did apply Dissenters' method of calculating interest, the parties had not briefed the issue and the court's opinion did not discuss it. *See id.* at *7. Moreover, the difference in the two calculation methods was likely not a major focus in *Torrington* because the total sum of interest awarded was approximately $8,400. *Id.* Here, Dissenters' interpretation would result in a windfall award of over $100 million, even though the Business Court concluded that RAI timely paid Dissenters fair value for their shares. (R p 312 ¶ 379.) Dissenters do not even attempt to justify this absurd result.[35]

Finally, Dissenters note that Pennsylvania revised the relevant portion of its Model Act-based appraisal statute, and therefore assert that North Carolina "has not adopted a formulation that calls for interest to be paid only on the difference between fair value and amounts previously paid to dissenting stockholders by the corporation". (DB 137.)

[35] Contrary to Dissenters' argument, it is not just the "sheer amount" of the requested interest award here that makes it absurd. Awarding *any* amount of interest in an appraisal action would be absurd when the court finds that the corporation has already timely paid a dissenting stockholder fair value for its shares. If a corporation timely pays all that is due (as the Business Court found RAI had done), then there is no outstanding amount to pay interest on.

But as another Model Act state's Supreme Court explained in response to a similar argument about a Model Act revision: "[a]n equally plausible explanation for the legislature's failure to amend" the statute "is that the legislature deemed no revisions necessary" because as already written the statute does not require calculating interest in the way Dissenters propose. *See Brown v. Arp & Hammond Hardware Co.*, 141 P.3d 673, 684 (Wyo. 2006).

CONCLUSION

For these reasons, the judgment of the Business Court should be affirmed.

Respectfully submitted, this 16th of November, 2020.

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This the 16th day of November, 2020.

By: /s/ Donald H. Tucker, Jr.
Donald H. Tucker, Jr.

The weighted average cost of capital we updated with the new inputs. But it was largely the same methodology. And then of course the perpetual growth rate, we ended up using the same rate because, in our view, nothing had fundamentally changed in the industry during the intervening two years. In fact -- yeah. Nothing had really changed.

Q. So you used the same perpetual growth rate range in these two circumstances, notwithstanding the fact that in one case your client was buying and in another case it was selling?

A. That's right. We did.

Q. And you believe that was appropriate?

A. Yes. No, in fact, I think -- it's not to suggest you wouldn't -- any deviation from that would need to be based in some facts, and nothing had changed. So it would have been peculiar for us to deviate from that -- that approach in the absence of any new information.

Q. Now, you mentioned in your -- in an earlier instance something of a peer set. Is that the same or different than comparable companies?

A. Right. It's the same. The comparable companies.

Q. So once again, in the context in which your client was a buyer and in a separate context in which it was a seller, you used the same comparables and -- or peer set?

A. That's right. We did.

Q. And you used some of the same precedent transactions?

A. Yeah. Many of the same precedent transactions, including the Lorillard transaction itself was in the peer set. It was one of the higher value numbers.

Q. Okay. And so now going back to the mechanics of the BAT version of the DCF analysis, what weighted average cost of capital did you use?

A. We used 5 to 6 percent range.

Q. And that was the same as you used in Lorillard?

A. Well, actually it was lower because some of the inputs had -- had decreased, notably the risk free rate. And the beta, one of the assumptions was very low for Reynolds. But we used 5 to 6 percent, which was lower than the Lorillard range.

Q. What do you mean by beta?

A. Beta is just -- is a way of looking at the correlation of a company relative to the market. And then that covariance, that correlation is then part of the capital asset pricing model. So you use that beta to look at the market risk. And the relationship between those two is what you add to the risk view rate to come up with a cost of equity. So a cost of equity that appropriately factors in the risk profile of that particular asset.

And when we update those, we look at those assumptions at that time. So that's why it can vary over time.

Q. And so you ran your DCF analysis into the Excel spreadsheet program. Yes?

A. That's right. Ultimately. Yes.

Q. And you ran it at a variety of inputs of different range -- the range of perpetual growth rate went from negative 5 to positive 5?

A. That's right.

Q. And you ran zero as well?

A. We ran zero as well.

Q. And you ran a range of weighted average cost to capital?

A. That's right.

Q. And from that, you then produced a view as to the value of RAI's shares?

A. That's right.

Q. Okay. Did you use any additional metrics to either test your view that resulted from the DCF or to take a look at it in any way?

A. Yes. So we spent a lot of time looking at the analysis and making sure that it properly -- that it properly reflects the -- that it makes sense. That it's reasonable.

One is, on the DCF specifically, we will -- I think

I mentioned earlier that when you look at the terminal value you can calculate it in two ways: You can apply the perpetual growth rate, which is the way we did it, but the other methodology is to look -- you could do it as a multiple of earnings at the terminal value.

And what we do is we imply -- we look at the implied exit multiple of that terminal value at -- from the DCF that we do. And that's a way to sanity check the numbers.

And, in this case, that implied exit -- range of exit multiples was in line with the public trading multiples of the peer group. And that's something we do always to make sure that the DCF output is grounded in reality.

The other thing is we make sure that the terminal value -- we look at how much of that -- how much of the total value is comprised by the terminal value. And in this case, it was roughly 80 percent, which is in line with what you'd expect with a five-year forecast. So that's part -- that's one of the steps we perform is we really look at the DCF and make sure that it's -- that the values that it's yielding make sense.

And then we triangulate and look at the precedent transactions and the public comparables and -- you would expect them to be in line with each other, not perfectly in line because precedent transactions will typically be higher than the public trading multiples for -- for the reason that precedent transactions are controlled transactions. So they typically carry a premium. So you would expect them to be above trading values where there is no -- not takeover premium.

And then discounted cash flows, because typically we're doing discounted cash flows, including internal numbers that may not be in the market, you will sometimes get a wider range and a higher range on the outer set in the same way that we did, in this case, which is typical. The DCF is typically the higher value and then you have the precedent transactions and then you have the public trading multiples in -- in the -- in what we call the football field or the display page.

Q. How would you characterize the nature of the DCF if you change some of the -- let's say, if you used a wide range of perpetual growth rates, would you expect to get very wide-ranging results?

A. Yes. It's mechanical. And it's an important point because if you have too wide a range of perpetual growth rates, you're going to get a very wide range of outputs. And that just makes it harder to be informative. If you have too wide a range, it's -- you're not really forming a view. You're just putting in assumptions and inputting a big -- a big number, a big range in front of somebody, it's not very informative.

So we -- you tend to have to keep the perpetual growth range fairly lateral in order to not get too wide a range. And like I said, we always sanity check it relative to the implied exit multiples that -- that's associated with that.

Q. And did you do that here in the BAT transaction, the sanity check?

A. Yeah. We did. We did. Sure.

Q. Okay. If I could have you look at -- well, let me do it this way.

MR. RAFFERTY: Your Honor, I'm going to offer PX0115 for which there is no objection because I simply want to show one page. It's the proxy statement. It's one of the binders we handed up to you at the break. I just want to show one page from it. And in the paper it's kind of blurry so I can put it up on the screen.

THE COURT: All right.

MR. RAFFERTY: I don't believe there's any objection.

THE COURT: You're offering PX115?

MR. RAFFERTY: It's the 13E-3. Yes.

THE COURT: Objection?

MS. SADIGHI: No objection, Your Honor.

THE COURT: All right. Admitted.

(PX115 was marked and admitted into evidence.)

MR. RAFFERTY: Could you go to 582.

MS. SADIGHI: I apologize, Your Honor. Could we have one moment?

THE COURT: Mr. Rafferty, which page are you directing the witness to?

MR. RAFFERTY: Oh, I'm sorry, Your Honor. 582. But I think they may want to make some kind of objection. So why don't you hold off.

MS. SADIGHI: Your Honor, the confusion is, we understand that he's using one excerpt. We do have an objection to the entirety of the Schedule 13E-3 to the extent of how it is used.

MR. RAFFERTY: (Indicating.)

(Discussion held off the record.)

MS. SADIGHI: I apologize.

MR. RAFFERTY: Okay. It's on the stipulation, Your Honor. So. . .

THE COURT: All right. So there's --

MR. RAFFERTY: So could we go back to page --

THE COURT: So what -- why don't we state it on the record so it's clear what we've been --

MS. SADIGHI: To be clear on the record, my initial response was correct. We have agreed. There's no objection to PX115.

would think of as the intrinsic or the fundamental value is the expected cash flow. So it would be that cash flow which was somehow probability weighted among sort of good outcomes and bad outcomes and it's that central tendency. If you don't have the expected cash flows, you're not going to get to that intrinsic or fundamental value.

Q. So how do you deal with the situation in which a business faces a variety of critical risks in trying to identify the right cash flows to use?

A. So sometimes it's possible in certain circumstances to have a set of projections which are somehow the midpoint. You know, they sort of -- sort of lie in the middle of what might happen on the upside or what might happen on the downside. Other times, what you actually need to do is do explicit modeling of those scenarios.

And so if there are some upside scenario where good events happen, you'd assess the probability of those things happening. And if there are potential negative events, you have a scenario which looked at the financial implications of those negative events happened and weighted by the probability of those two.

Q. So maybe it would be useful to illustrate this. We have a demonstrative we can put up on the screen. It's Slide No. 2 in the deck.

So can you tell us, Professor, what it is we're looking at here on Slide 2?

A. So this is just a hypothetical example. And probably the easiest way to think about it is perhaps -- let's think about a pharmaceutical company. And that pharmaceutical company is developing a new drug. And if we assume for a second that there's a 40 percent likelihood that that drug gets FDA approval, and if it does get FDA approval, then those incremental cash flows from the new drug are going to follow that blue line.

And so over time, the cash flows from that company are going to grow from 200 million if the drug is approved in the first year, all the way up to a billion dollars in year five. But, again, we know that drug approval is not certain and so if we assume that there's a 60 percent chance that the drug's not approved, then the cash flows from this pharmaceutical company might increase like that red line. And so starting at 200 million and at year five end up at only 400 million because they don't have that new drug.

Q. So is the blue line kind of the good case and red line is the bad case?

A. Exactly. Optimistic, pessimistic, upside, downside. You could characterize it a lot of ways.

Q. And if you were doing a discounted cash flow of this company, which of these two lines would you use as the -- as the expected cash flows?

A. You'd use neither one. You'd use something which was in between. You'd probability weight those two cash flow series. And you'd get something which would be in between.

Q. So let's turn to the next slide. And so what are we looking at here with this green line?

A. Yes. In this hypothetical example, the green line would represent the expected cash flow. And it's just a -- it's just taking 60 percent -- 60 percent of the downside scenario and 40 percent of the upside scenario.

So the only cash flow series that would give you the intrinsic or fundamental value of this company would be that middle green line. To use the blue line or the red line would be wholly inappropriate.

Q. So if you had a student who was valuing this company, you would tell that student to use which line?

A. It would be the green line.

Q. Okay. And what if the student used the blue line to do the valuation, what would you tell her she had done wrong?

A. I would tell her that she missed one of the fundamental premises of finance which is that value when you do a DCF is wholly dependent, entirely dependent on using the expected cash flows, not the best case or upside scenarios.

Q. Did you form a view as to whether the projections that were used by the bankers in this matter complied with the principles that you just articulated?

A. I did.

Q. And what was that view?

A. So my view after, you know, reviewing industry information and analyst reports and the like is that the cash flows, those five years of projections that the financial advisors used are more like the blue line, more like an upside case, as opposed to the green line, the expected value case.

Q. So did those projections that you looked at take account of all potential outcomes that the company was facing?

A. No. It was clear in both the way that the cash flows were described by the company and disclosed in the proxy that it was assuming business as usual. And when you look through in terms of looking at what the sort of industry experts are saying about the issues in the tobacco industry, there are some things which are potential upside scenarios in terms of market share and the like, but there's a description of a tremendous number of game changing downside risks.

So, you know, I've sat through the Court for a number of days and if you look through, reading through industry reports from experts and the analysts, you know, things like nicotine reformulation by the FDA, the menthol ban, changes to the age of purchase of cigarettes, the increases in state and federal excise taxes, or cannibalization from new products, all of those things could be major game changers. And were one of them to occur in the next three years, five years or ten years, it would have major negative implications for cash flow.

Q. Now, is it your understanding that management at RAI just ignored the risks entirely when they put the projections together?

A. No. I think the description is that, because they couldn't be certain when those risks might occur and could not assess exactly the probability, they didn't factor them into the projections. The projections were business as usual, but they were very clear at saying that these risks were out there and were real probabilities occurring. And the further you went in time, the increased in probability that at least one or multiple of those risks would occur in that time frame.

Q. Now, you mentioned it and I should have asked you, but have you had the opportunity to be here for any portion of the trial?

A. I've been here since Tuesday morning. Yes.

Q. And did you hear Ms. Crew testify this morning?

A. I did.

Q. And she was asked a number of questions on cross-examination about whether as a business matter, it would have been appropriate for her and her team to model in what were characterized as speculative events. Do you remember hearing those questions?

A. Yes.

Q. And do you remember Ms. Crew answering that she did not think it was appropriate to do that as a business matter so that she could in fact continue to run the business?

A. Yes.

Q. And then she was asked a question about whether it would be appropriate to factor in those kinds of risks in a situation in which the company was being sold. Do you recall that?

A. Yes.

Q. And do you remember her testimony was that it would be appropriate in that case because you needed to value the company rather than just run it on a day-to-day business?

MR. ROLNICK: Objection, Your Honor. Leading and mischaracterizes the testimony.

THE COURT: I'll sustain the -- I'll sustain the objection. The last four questions have been more of a memory test than they have been to actually get to the point so why don't you get to the point.

BY MR. BORNSTEIN:

Q. The point I was going to get to was to ask: Do you agree with Ms. Crew's testimony on this subject?

A. I do. I mean, to ignore real probable events that could occur over some reasonable finite sort of time period that could dramatically change the cash flows of the business would violate all the principles of value. And so you need to take them into consideration in some way.

To ignore them and to use projections which do not embed them would be 100 percent wrong.

Q. And do you agree with Ms. Crew that there are different considerations in doing projections to run the business on a day-to-day basis and doing projections for valuation purposes?

MR. ROLNICK: Objection again, Your Honor. He's asking a question that asks whether he agrees with testimony that was given and characterizing it. It's inappropriate. We would ask --

THE COURT: I'll sustain it. Just ask him the question as opposed to the agreement.

MR. BORNSTEIN: Sure. Absolutely.

BY MR. BORNSTEIN:

Q. Is it the case that projections that someone does in the purpose of managing the business on a day-to-day business can be different in this respect from projections that someone does for the purpose of valuing the entity as a going concern?

A. A hundred percent. And maybe sort of an example.

I've been on the board of some start-up companies. I've advised lots of my students who have started companies. And what I tell them is that you need -- you need different sets of projections. You need projections to run the business. And those projections may not be the same thing as the expected outcome that you'd use to value the business because you need to build the business as if things continue to go.

If there's -- if it -- for example, if you're a biotech company, you can't be certain that the drug's going to be approved, but you have to continue to operate the business as if you believe it will be approved. So managing the business on that scenario of approval, even if from a valuation sense, it's only 40 percent likely that it would be approved. And so absolutely, it's not only what I teach, it's what I've advised when I've been on the board that you can have projections for business purposes, but the evaluation for valuation purposes could be substantially different.

Q. And if we have a situation where there is a company where there are differences between the management focused projections and the valuation focused projections, what would be the effect on the reliability of the discounted cash flow for using the management focused projections rather than the valuation focused projections?

A. So typically management projections for operating a business tend to be more optimistic. They tend to be sort of upside. Things are going to go well and I want to build a business to be able to execute if those things go well.

If you were to use management projections for operating the business and you don't adjust for some of these negative probabilities, you're going to overvalue the company. It's going to be an optimistic valuation.

Q. So in light of that, was it a mistake for the financial advisors to use the projections that they used to support their fairness opinion?

A. No, I don't think so.

Q. And why is that?

A. Well, what the financial advisors were tasked with doing was to assess whether or not the deal offered by BAT treated the non-BAT shareholders fairly. Were they getting sort of fair compensation, fair return for their shares? So to the extent that the projections that they were using were optimistic, were upside, not factoring in some of these downside risks, it would -- it would be -- it would be an optimistic valuation.

So if the deal price was at or above that, they could reasonably conclude that the RAI shareholders, the non-BAT RAI shareholders were getting sort of, you know, compensated above the intrinsic value.

Q. So if the output of the DCF analysis the bankers did were still lower than were in the range of the deal price, you're saying, even if they're optimistic, what flows from that?

A. Well, that the true intrinsic value based, or the fundamental value based on expected cash flows would be lower. And therefore, they could reasonably conclude that -- that -- that the non-BAT RAI shareholders were receiving fair compensation. They were receiving their value.

Q. So if the price that's being paid is higher than an optimistic value, that price is by definition fair?

A. From a financial -- I can't opine as a matter of law.

Q. Of course.

A. That's for the judge. But from a financial economics perspective, that would be true.

Q. Okay. And one question just to touch quickly on something you said, which was that management tends to have optimistic projections, is there a basis for that opinion in the field of financial economics?

A. Yes. So there are a number of academic studies which have looked at realized financial performance relative to internal projections. And generally speaking, internal projections tend to be -- management internal projections generally tend to be optimistic.

Q. Now, in doing a discounted cash flow analysis, are there any rules about the number of years of projections that you need to have to do it right?

A. No. There's no hard and fast rules. Generally, you want to project out toward some steady state. But there's, again, no hard and fast rule, whether it's five, three, ten.

Q. Well, we heard a lot of testimony -- and since you were here, you heard a lot of testimony -- about whether five-year projections were appropriate or ten-year projections were appropriate.

Can you do a reliable DCF analysis with five years of cash flow projections?

A. Absolutely. I've done them. I've seen, you know, reasonable valuations done. So absolutely.

Q. And there was a spreadsheet that was up on the screen for some time yesterday morning. Do you remember that?

A. Yes. I was here for that. Yes.

Q. And I want to ask just a few questions related to that spreadsheet and the questioning around it --

THE COURT: Why don't we -- before you do that, why don't we take the midmorning break and then come back and let you move into that subject.

MR. BORNSTEIN: Of course. Thank you.

THE COURT: All right. We'll be adjourned for 15 years or five years into the future. It's, like, theoretically or practically forever into the future. When you assume a perpetuity growth rate, you're assuming that that company will grow at that rate forever into the future.

Q. And how does a financial economist go about selecting what perpetuity growth rate to use in the DCF?

A. You analyze the industry, you analyze the company. You look at the trends that are happening. You look at potential risks and the like. And from an analysis of that information, you then sort of come up with your estimate of what you believe an appropriate perpetuity growth rate is.

Q. And are there, you know, typical boundaries that are recognized in economics that people think about in selecting a growth rate?

A. Yes. For a typical business, it's usually the case that most valuation professionals, most -- myself included -- would use a perpetuity growth rate somewhere between inflation and nominal GDP growth. And the way to think about that is, if you have a company which is going to stay -- stay its steady state and it's going to stay the same size in sort of real economic terms, that sort of says its performance, its cash flows are going to grow at the rate of inflation. And what that is sort of saying is this firm is going to stay the same size forever.

A second possibility is that the company will grow at the overall rate of the economy. So generally, the economy grows faster than inflation on average. And so if this company is sort of going to grow roughly proportional to the overall economy, then you would assume that the perpetuity growth rate would be the rate of nominal GDP growth into the future.

Q. Are there circumstances in which it is appropriate to use a growth rate that is below the rate of inflation?

A. Absolutely.

Q. In what circumstances?

A. So I've been involved in circumstances where I've done valuations where there's no terminal value. So the -- say it's a patent and you're trying to value a patent. Once it expires, there's no sort of positive free cash flow. So there's no terminal value. There are other circumstances in which there are companies or industries that are in real decline, meaning that they're disappearing for a variety of reasons.

It could be new technology obviates the need for that particular business and that business is going to generally go away over time. It could be a business like cigarettes in which for health and regulatory reasons, that that business is going away over time.

Q. Now, did you come up with your own perpetuity growth rate number here?

A. No.

Q. So what work did you do in looking at the perpetuity growth rates that were selected by the financial advisors?

A. I did the same work that I would do if I were to have chosen my own perpetuity growth rate. Looked at industry reports. Looked at industry data. Read through the volumes of analyst reports in the case. And came up with an assessment and a set of information by which I could evaluate the choices which were made by the financial advisors. But it was the same set of work that I did that I would have done had I come up with my own estimate.

Q. And is the work that you just described the work that financial economists do in the ordinary course of their field?

A. Oh, any time I've done my own valuation, I've done -- I do that exact same set of things where you look at industry reports, analyst reports and the like, to come up with an assessment of what you think an appropriate perpetuity growth rate would be.

Q. And what did the bankers here conclude was the appropriate growth rate to use, or range of rates?

A. So Goldman Sachs and Lazard used the same range. Their range was minus .5 percent to plus .5 percent.

JPMorgan used a slightly higher range which was from zero to 1 percent.

Q. And what did you conclude about the ranges that they selected?

A. My conclusion is that, you know, range centered around zero sort of makes sense. Those are reasonable terminal growth rates.

Q. What's the basis of that opinion?

A. So when you look, most of the investment analysts actually who were following RAI were projecting negative long run growth.

Second, it was clear from my analysis of the industry reports and from the analysts that there were, you know, major changes in the industry. Volumes had been declining for quite some time and it was clear from the industry experts that the ability to continue to offset those volume declines with price increases was potentially going to be limited in the future.

And then the third thing was the discussion of what were these very large game changing risks which faced the industry? I think I've mentioned a couple of them earlier. So things like FDA regulation of nicotine, the menthol ban, restrictions on age purchases of product, state and federal excise taxes, new products like vapor and its cannibalization.

All of those things could have dramatic step order function changes in a negative way to the industry and those were very real possibilities.

Q. In addition to looking at this publicly available information like analyst reports and so forth, did you also look at any of the internal documentation from RAI or testimony of the like?

A. Certainly. So I reviewed the various internal documents, the public disclosures and say the proxy, the -- and sort of the testimony, and it was clear from that that management itself understood that these very large risks were out there and were very real probabilities over a reasonable horizon, and that those things would dramatically change the business in sort of a very negative way.

Q. There have been a number of questions over the course of the trial focused on what's been characterized as a cliff. Do you remember that coming up?

A. I do.

Q. Can you tell us whether a -- the use of a zero percent perpetuity growth rate means that a company is falling off a cliff?

A. Yes. I mean, that's actually a mischaracterization of what a zero percent growth rate means.

So if you think about it -- so practically speaking first of all, what a zero percent growth rate means is that if you have nine billion of cash flow or five billion of cash flow in year five, you'd have that exact same amount in year six and year seven and year eight so your cash flow would stay the same. So it's five billion in six, five billion in seven, five billion in eight. But the thing that we need to sort of understand about this perpetuity growth rate is that it really is meant to capture two sort of factors. The first of which is as I mentioned earlier, there's a time series of growth rates.

So that perpetuity growth rate is meant to capture not just what happens in the next two, three, four, five years, but what happens over the life of the business.

So it's time averaging over, like, infinity in some sense. So if you look over the next 20 years, maybe it grows somewhat quickly over the next three to five years, but eventually it's going to decline by 5, 10, 15, 25 or 30 percent. And so that zero percent can capture some growth -- some positive growth now but then averaging with this big negative growth into the future.

The second thing it captures is just the fact that projections are just estimates and they're never perfect. And I think the way we should think about it is that zero percent captures the fact that it's possible that RAI would continue to grow at 7 or 8 percent through year ten, but as the -- you know, as the industry analysts and experts sort of acknowledge and the company itself, there are real probabilities that one or more of these big negative events are going to hit. It could hit in year four, year six, or year ten. And if they hit, these are going to have game changing effects.

So you could have 25, 30, 50 percent changes. I mean, if it was a menthol ban, that's sort of -- you know, the largest area of what's going on in RAI. Their best performing subset of cigarettes. And so the way to think about it is that that zero percent averages across some scenarios in which, yes, maybe it grows at 7 or 8 percent, but maybe in year eight, there's a regulatory event that has minus 25 percent.

And so the way -- the way you should think about that growth rate is it averages over the time with maybe some positive and then negative in the future and averages across scenarios some of which may be very large negative events that happen.

Q. Is there a concept of present value weighting in connection with perpetuity growth rate selection?

A. Yes. So the way to think about the first element is that that zero percent would be sort of a present value weighted calculation of the growth rates in year six, seven, eight, ten, 15, 20, 30.

Q. And can you tell us what you mean by present value weighted calculation?

A. Well, I think I explained to the Court a little earlier that there's the time value of money. That money today is worth more than money later and so the growth rate ten years from now is less important to the perpetuity growth rate than growth say in year six.

And so you would have to adjust for, say, a big negative growth rate in year ten or 15 by that time value of money, by the weighted average cost of capital.

Q. And does the perpetuity growth rate which is just a single number -- zero or .5 or whatever it is -- does that number capture that rise and fall over time?

A. That's one element of how you would get to a zero percent growth rate. Yes.

Q. And so if you have a company that is growing at, say, 7 percent over the course of five years and then you assign a zero percent perpetuity growth rate in year six, does that mean that you are saying that growth necessarily stops immediately in year six?

A. No, not at all.

Q. And that's for what reason?

A. For the two reasons I mentioned, one of which is that the perpetuity growth rate averages across all the years. The present value across all the years, as well as averaging across different scenarios that might happen. So there's nothing embedded in a zero percent growth rate which would say that this company would fall off a cliff after year five.

Q. So is it -- is it correct that the growth of RAI over the past several years has been higher than the rate of inflation?

A. Yes.

Q. Does that undermine in any way the reasonableness of the bankers' selection of a zero percent rate for perpetuity?

A. No, not at all.

Q. Can you explain why not?

A. Because part of their ability to grow quickly was driven by price -- their ability to increase prices. And it was clear that their ability to increase prices at least from the perspective of analysts in the industry and including internally, perhaps was going to be limited in the future. The ability to continue to increase at 6 or 7 or 8 percent per year would be hard.

The second thing is that, while we didn't get one of these regulatory events perhaps in the last, you know, three to five years, that says nothing about the real probability that one of those events may happen in the next three, five or sort of ten years. And so the fact that they've grown quickly over the last several years in no way negates a zero percent growth rate being reasonable.

Q. Are there customary ways to look and check the reasonableness of the perpetuity growth rate that you select when do you a DCF?

A. For sure.

I mean, so one of the things that we teach in first year finance and one of the things that you see -- one of the things that I've always done when I do valuation, as well as the thing you see that all three financial advisors doing is to gauge their perpetuity growth rate by looking at what's called the terminal year exit multiple.

Q. And what is that?

A. So we know -- and one of the things I did here in terms of a market check was to do a comparable company's multiple analysis. What a terminal year exit multiple analysis is, is just to say a particular perpetuity growth rate implies some multiple in that terminal year. So because we're calculating a terminal value, we can say, what multiple would be active or valid in order to create that terminal value? And so you calculate the EBITDA multiple, the ratio of enterprise value to EBITDA, in that final year of projection based on your choice of perpetuity growth rate.

Q. All right. So let me break down a couple of pieces of that answer.

First of all, you used the word multiple a lot. Let's make sure we're all in agreement on what you mean by that.

A. So one common -- one common check to a DCF is typically to do what we call a comparable companies or precedent transaction. Which a lot of people would just call a multiples analysis. And what that is, is it's taking the ratio of your value to some financial metric. And then --

Q. So for example.

A. For example. I was going there.

So one example -- and probably the most common is EBITDA, earnings before interest, taxes, depreciation and amortization.

And so a very common -- things that market participants do -- and you should certainly use as a check is to say what does -- you know, what does the choice of your perpetuity growth rate imply for the multiple that will exist, that ratio of enterprise value to EBITDA.

Q. And did you look at that in this matter?

A. I did, yes.

Q. So let's see if we can put on the screen please Demonstrative No. 7. And does this slide reflect the work that you did on this?

A. It does.

Q. All right. So can you tell us first of all what that very first green bar with the 12.4X is?

A. That represents the ratio of enterprise value to

EBITDA for RAI as of October 20th, before the offer from BAT. And so at that time, if you took the enterprise value and divided it by the 12 months EBITDA, you would get 12.4 times.

Q. And the enterprise value is something that you calculate how?

A. Well, you take the number of shares times the share price to get equity value. You add the value of the debt and subtract out the excess cash.

Q. So is that a measure of the value of the firm as -- as set by the market?

A. Correct. Yes.

Q. And so this first multiple is calculated as a market value of the firm divided by some measure of earnings?

A. That's correct.

Q. Okay. So then what are the next three green bars?

A. So the next three green bars just do that calculation for the terminal value of the financial advisors. So you take the total value of their -- their total terminal value and you divide it by the last year of EBITDA. And so that essentially is saying, what's the EBITDA multiple that is implied by this perpetuity growth rate that will exist in sort of year six?

Q. So let's just take a concrete example here of let's say the Goldman analysis that gets you to the 10.5X. What are the different inputs into the calculation that arise at a 10.5 times multiple?

A. It's -- so within their spreadsheets analysis, the -- they have a component of value which is called terminal value, which is the value which after the projection period, from year six forward, is the value that they calculate based on their perpetuity growth rate. So you take that terminal value and you divide it by EBITDA in year five.

So that's sort of what we call a trailing 12-month EBITDA multiple. But that gives you this 10.5 number. So the ratio of terminal value to year five EBITDA is 10.5.

Q. So the numerator is the portion of the Goldman Sachs valuation that starts in year six?

A. Correct.

Q. And the denominator is what?

A. Year five EBITDA.

Q. Okay. And then they used a range of perpetuity growth rates in the analysis --

A. Correct.

Q. -- from negative .5 to positive .5.

Do you recall which spot in the range was used to calculate the numbers on your chart here?

A. So it's the midpoint for all of these. So it's zero for Lazard and Goldman Sachs and .5 for JPMorgan.

Q. Okay. And now, can you tell anything or do you draw any conclusions as an economist from the fact that the bankers' multiples are somewhat lower than the pre-merger trading multiple in the first bar?

A. That's sort of what you expect. So their implied terminal exit multiples give you comfort that the choice of perpetuity growth rate is reasonable.

Q. And why does it give you comfort that those numbers are a little bit lower?

A. So the -- the multiple is really just dependent upon the risk of the cash flows and the growth rate. And generally we think of growth rates declining over time. So if the growth rates standing in year five looking off into the future is lower than the growth rates standing here today, then on average, multiples decline over time.

And so the fact that the multiples are a little bit lower in year five would be reasonable because, looking forward, you would expect the growth rate off into the future five years from now will be lower than the growth rate today.

Q. So tell us what the two bars over on the right are and how you calculated those.

A. So I did the exact same thing for the two experts for the Dissenter, Mr. Taylor and Professor Zmijewski. And if you do the exact same calculation that I did for the financial advisors, you arrive at implied terminal exit multiples of 17 and a half and 17.7.

Q. And can you draw any conclusions about the reasonableness of their valuations based on what we see here on the chart?

A. So as I said, this is really a test of the perpetuity growth rate. And if I were looking at this -- because again, this is an important check -- this would cause me to have serious concerns about the perpetuity growth rate that I chose.

Q. And why is that?

A. Because essentially you're assuming that mult- -- the multiple's going to go up over time. And it would generally imply that from the perspective of expectations, growth in this company is going to be accelerating. So growth in five years is going to be higher than growth today.

Q. And would it be reasonable to expect that growth in RAI would be higher five years from now than it is today?

A. No.

Q. And why is that?

A. Generally speaking, this is an industry in decline. It's been growing relatively rapidly and is expected over the next several years to grow, you know, more rapid than zero and therefore standing five years from now, we would expect it to be growing slower.

Q. Let's take a look at Slide No. 4, please. On the subject of terminal value, can you tell us what it is we're looking at here?

A. So what I did here is just to break apart the total per share enterprise value that Professor Zmijewski and Mr. Taylor calculate. And I divided into the component which is based on their projection period cash flows. It's five years for Professor Zmijewski and eight years for Mr. Taylor.

Q. And that's the green portion?

A. That's correct. And I look at that as a fraction of the overall value and then also what fraction of the overall value is due to their terminal value.

Q. And what, if any, conclusions or implications are there for you from what you've done here on the chart?

A. So what this says is that the vast, vast, vast majority of the value they come up with is in their terminal value.

And because that is totally dependent upon their perpetuity growth rate, what this says is that you need to take an extreme amount of care in choosing that perpetuity growth rate because it is the most critical factor in terms of determining the value of RAI.

Q. So are there some steps that you would then take upon seeing that your calculation led to these results?

A. Certainly. You'd want to do checks.

And one of the checks we just talked about which was a check of the implied exit multiple. But you also --

you know, again, this is sort of Finance 101. That you don't just do your DCF because as I mentioned to the Court a little earlier, DCF is just math. It's literally just formulas. And what matters are your inputs. And you want to check those inputs with other measures of value. And so you'd want to do reasonable checks of that value in other ways.

Q. Have you seen any documents internally at RAI that reflected some kind of DCF calculation?

A. I have, yes.

Q. And do you recall what the inputs were in -- in that document?

A. I do, yes.

Q. What were they?

A. So they were projections and then the discount rates and perpetuity growth rates.

Q. And do you recall what perpetuity growth rate was used by the company in connection with trying to come up with a ceiling for authorization to go purchase shares in the market if it chose to do so?

A. They used 3 percent in those projections.

Q. Okay. And -- and in that calculation?

A. In that calculation, yes.

Q. Now, does that cause you to question in any way your opinion about the reasonableness of the growth rates that the bankers used?

A. No.

Q. Please explain why not.

A. Well, the first reason is that they -- they tied that growth rate to what I would almost call a step factor calculation of their discount rate. So they had this set of factors which would increase or decrease their base discount rate based on things like protected market, new product, and the like. And those things generally are related to the sort of -- the sort of probability that those things are going to be successful or not.

And so there's a direct tie between the way they calculate the discount rate and the perpetuity growth rate. Those two things are inextricably sort of linked.

The second thing is that this wasn't done for what I would call a fundamental or intrinsic value purposes in terms of really being this probability weighted expected growth rate into the future. And that be sort of, you know -- I often talk about projections and calculations being done for different purposes. This wasn't done to estimate intrinsic or fair value. It was done to estimate the maximum price that they would be willing to pay for their shares in this repurchase program.

Q. So let me go back to the first of the two things you mentioned relating to the way they calculated the weighted average cost of capital.

To put the question kind of bluntly, did the company go about calculating weighted average cost of capital the right way?

A. No. I would have failed them in that sense.

They didn't do a market derived cost of capital where you look and you calculate -- I'm sure I'll have a chance to talk to the Court about betas and those sorts of things. But they didn't do a market derived cost of capital and therefore it's disassociated from the way we would do a valuation.

Q. So to just sort of put a pin on that for a second, when you did a -- did you do a weighted average cost of capital calculation in this case?

A. I did.

Q. And what weighted average cost of capital did you come up with?

A. 5.78.

Q. Do you remember what each of the Dissenters' experts came up with?

A. I believe Professor Zmijewski was 5.70 and Mr. Taylor was 5.75.

Q. And would you characterize that as a wild disagreement or general consensus on the right number?

A. It may be the kind of things that academics around the lunch table might argue about, but from a practical perspective, it's not important.

Q. Because everyone's pretty much --

A. Yeah. We're pretty much in the same -- in the same range.

Q. Okay. And is that also where the company came out in this share repurchase document?

A. No. They had a much higher cost of capital.

Q. Okay. And what does that imply to you about the work that they did in selecting the growth rate and the cost of capital?

MR. ROLNICK: Objection, Your Honor. He's asking him to speculate about what RAI management was thinking.

THE COURT: Well, he's asking for an opinion. I'll allow the question. Overruled.

A. So from the document which shows how they created the cost of capital, they were tying their -- the way they were talking about -- the way they were calculating their cost of capital to things which might influence the growth rate. The two were actually linked.

BY MR. BORNSTEIN:

Q. So you referenced just now a document that talked about the way they were calculating their cost of capital. Just to make sure we're all thinking about the same document, can we have PX47 on the screen?

MR. BORNSTEIN: This is in evidence already, Your flow on my own.

Q. If you had been asked to, is that something you could have done?

A. Yes.

Q. And what would you need to have done in order to do it?

A. So if I -- if I were asked to do an affirmative DCF, I would have likely done --

MR. ROLNICK: Your Honor, I'm sorry to interrupt, but I'm going to object.

If he's going to ask this witness to opine on what a DCF would have looked like had he done one, which he had every opportunity to do and we could have examined him on that, we could have deposed him on that, they chose not to do a DCF. This witness didn't do a DCF. And so I'm going to object to a hypothetical question that says, had you done one, what would it look like? That's not fair to us and it's improper.

MR. BORNSTEIN: I'm not seeking to elicit any kind of valuation information about where he would have come out had he done a DCF or anything of the like through this question. So I will be clear to the professor that's not my intent here.

THE COURT: I'll overrule the objection at this point.

BY MR. BORNSTEIN:

Q. Should I rephrase the question just to --

A. No, no, no. So the way that -- given the very real sort of large downside risk that this industry faced, I believe that an appropriate discounted cash flow that I would have done would have entailed a number of scenarios. I would have absolutely put in place a downside scenario in which some time over those first five years, a negative event would have occurred, which would have had an effect on the cash flows of RAI. And then I would have weighted those two to come up with the DCF.

Q. And this --

MR. ROLNICK: Your Honor, I move to strike that testimony.

THE COURT: Is this line of inquiry, has this been -- has this been displayed in any disclosures during discovery or was it foreclosed during deposition?

MR. ROLNICK: Not to my knowledge, Your Honor.

MR. BORNSTEIN: Your Honor, the point of this question is to respond to the arguments that Mr. Rolnick made before the examination began in which he challenged Professor Gompers for not having done a DCF analysis and all I'm asking Professor Gompers to do is to explain what he did and the rationale for why he did it the way he did it.

THE COURT: Well, actually, I think what you're asking him to do is if he had done a DCF, how would he have done it, what would he have considered. And I think Mr. Rolnick's concerns about that are well taken. So I'm going to sustain the objection.

MR. BORNSTEIN: All right. Thank you, Your Honor.

BY MR. BORNSTEIN:

Q. Let's switch to a different topic then which is the comparable companies analysis you mentioned.

And did you actually do your own comparable companies analysis?

A. I did.

Q. So let's start by saying, what is a comparable companies analysis?

A. We had a brief introduction a little while ago, but essentially it's identifying companies which you believe are peers who share sort of the same characteristics and you try to benchmark the value of the company you're valuing by looking at the multiples that those companies trade at. So you calculate for a set of companies that you identify as peer, you calculate that enterprise value to EBITDA.

Q. And why does someone do a comparable companies analysis when conducting a valuation?

A. It's a check. Again, this -- you know, discounted cash flows is just formula with some inputs into it.

And if there are multiple pieces of information that you can utilize to check that DCF, you always do it. I always do it in my analysis. When I look at financial professionals doing their analysis, they always do that analysis. Because to ignore it would be wrong because you just don't know if your DCF is using the right set of assumptions.

Q. So how do you go about selecting the companies that you would use in a comparables analysis?

A. Because you're trying to match companies based on their riskiness and their growth, what you do is you try to constrain it to firms which are in the industry and you can sort of have various filters where you try to make the set of companies as similar as possible.

Now, you never have a perfect twin. You never have a company which is going to be identical to RAI that you'll say, ah, this is exactly RAI's value.

But firms, say, here in the tobacco industry are going to have similar sets of regulatory risk and use issues and that will help them provide information to the value of RAI. Certainly the closer a company is in terms of the geography, operating in the U.S., its product mix in terms of mostly being cigarettes, that will provide more information. But to disregard companies that have other characteristics which are shared with RAI would be inappropriate.

Q. Okay. How did you go about picking the comparables that you used for your work in this case?

A. So I looked at four sources. I looked at the companies that RAI said in its SEC filings were sort of peer companies. The second thing is I used the set of companies that RAI listed during the Strategy Day as comparable companies. I did a tabulation of the investment analysts because when investment analysts analyze companies, they typically will sort of list sets of firms that they think are comparable to, say, RAI. And then finally, I looked at the list of comparables that the financial advisors used in their check of their discounted cash flow.

Q. All right. So let's put Slide 8 up on the screen, please. Are these the companies that you ultimately landed on as -- through the work you just described?

A. Yes, they are.

Q. Now, are all of these companies equally informative or equally valuable to you in doing a comparable companies analysis?

A. Well, no. Again, this gets to my earlier comment which is, certainly some of these are going to provide more information about value than others. So, for example, Altria is, you know, virtually all of their sales are cigarettes and their sales are sort of in the U.S. And so that's a much closer peer than a firm like Philip Morris which doesn't have sales in the U.S.

And so you give relatively more weight in terms of evaluating them as check of the value. But to ignore the others would be improper.

Q. And just so that they're in the trial transcript, could you tell us which are the companies that you ultimately identified?

A. Sure. So it was Altria Group, Imperial Brands, ITC, Japan Tobacco, Philip Morris, Scandinavian Tobacco, Swedish Match, and Vector Group.

Q. And what -- which of these companies do you consider to be the more informative comparables?

A. Yeah. So certainly Altria is the firm here. It's -- you know, it's the biggest rival of RAI in the U.S. In fact, it's the market leader larger than RAI. Its sales are primarily cigarettes. Virtually all of their sales are cigarettes. And they operate in the U.S. And so it has -- you know, it's subject to the same regulatory environment, the same consumer issues and the like. And so while it's not a perfect twin, it's probably the most important as a check of value.

Q. Okay. And what metrics did you then use to do this analysis? And if it's helpful we can put --

A. No, no, no.

So if we remember one concept which is value is forward looking. You know, we don't buy a stock because it arrived at during the DCF by the financial advisors seems very reasonable.

Q. And what does it tell you about the DCFs that were done by the Dissenters' experts in this case?

A. It sort of -- you know, they're sort of way off. The values they come up with are virtually twice the value you get from these comparable companies.

Q. Well, let's go back to the prior slide which has the multiples on it that you calculated. Did you also calculate the multiple that's implied by the valuations that the Dissenters' experts came up with?

A. I did.

Q. And what did you find?

A. So if you calculate the EBITDA multiple for Professor Zmijewski's analysis, you get something like 24. And the multiple for Professor Taylor -- Mr. Taylor's analysis is 23.2.

Q. And, again, as -- what does it tell you to compare those numbers to the multiples like the roughly 12 that we see for Altria and the others on the screen?

A. It sort of says that their prospects are twice as good as sort of the other peer companies in the industry.

Q. So let's look at Slide No. 12, please. What is it we're looking at here?

A. So what we're looking at is the sort of comparison -- it's sort of hard to see. But it's comparing the Altria market cap to sort of three things on the left-hand side. The first, this $67.25 billion is just the market cap implied by the RAI unaffected stock price. So that 47.17 from October, that implies a 67.25 billion-dollar valuation. Professor Zmijewski when he does his DCF, adds 64 billion on top of that and Mr. Taylor adds another 2.7 billion sort of on top of that. So they get valuations which are pretty comparable to Altria here in terms of overall value.

Q. When you say they get valuations that are comparable to Altria, who are you talking about?

A. Professor Zmijewski and Mr. Taylor.

Q. And can you draw any conclusions about the reasonableness of their valuation based on the similarity between what they found -- their implied market cap for RAI and Altria?

MR. ROLNICK: I object, Your Honor. Unless this witness has done a valuation of Altria or has somehow looked at its cash flows and attempted to determine what its true or intrinsic market value is, I don't think he's in a position to make a comparison about the reasonableness.

MR. BORNSTEIN: Your Honor, I think that's cross-examination.

THE COURT: Hang on one second.

I'll allow it. You may answer.

A. So I think you want to look at relative to say the size of the companies. And, again, Professor Zmijewski and Mr. Taylor saying that the value of RAI is, you know, almost exactly the same as Altria. But if you look -- for example, if you just look at, say, revenues, there's, you know, a big difference in the revenue between these two companies.

BY MR. BORNSTEIN:

Q. Well, let's look at the next slide, please. Slide 13. What are we seeing here on the two sides of the slide?

A. So the left graph is just what was up in the prior slide and the right graph just shows the revenue of these two companies. That RAI had 2016 revenues of 12 and a half billion and Altria's revenues were nearly 60 percent higher at 19.3 billion.

Q. And what does that tell you about the reasonableness of the Dissenters' valuations?

A. Again, this would cause me to really pause about the assumptions that I put into my valuation analysis. This check sort of says, you know, maybe there's some errors that I have in my assumptions.

Q. Because they're saying that even though RAI has substantially lower revenue, its value is comparable?

A. That's correct.

Q. Let's talk about precedent transactions. Did you do a precedent transactions analysis in this case?

A. I did.

Q. And is that a technique that is commonly used by valuation professionals?

A. It is.

Q. For what purpose?

A. Again, as a check. Again, as a reasonableness check to the valuation.

Q. And just very high level, how does one conduct a precedent transactions analysis?

A. You do it in a similar way to the -- to the comparable companies. You identify transactions that are similar because they're in the same industry and hopefully you have a similar size. And then you create those same multiples, those same sort of deal value to EBITDA multiples to see what they were purchased at.

Q. And how did you go about selecting the transactions that you used as comparables here? And we can put Slide 14 on the screen too.

A. So I searched the Capital IQ database which is just a database of transactions. I looked at all the mergers or acquisitions which were in the tobacco industry that closed within five years of the transaction here closing. And then I restricted it to those that had an enterprise value greater than $500 million.

Q. And so if we go to Slide 15, are these the transactions that resulted from that filtering?

A. They are.

Q. Okay. And they're acquisitions of Gryson, JT International, the U.S. cigarette brands and other assets of Lorillard Reynolds, the acquisition of Lorillard itself, and the acquisition of Souza Cruz; right?

A. Yes.

Q. Okay. Now, are all of these transactions in your mind equally informative of the value of Reynolds?

A. Absolutely not. You have to do a similar kind of assessment and give more weight to those which are more similar to the RAI transaction. And in this case, you know, Lorillard clearly stands out as the most helpful in terms of our assessment of value. And --

Q. For what reason?

A. Yeah. So first of all, its, you know, business is primarily, you know, and virtually all cigarettes. It's in the U.S. And, you know, in fact, the major element of this purchase was Newport, which ended up being a major -- and is a major component of RAI.

Q. So once you select your precedent transactions, what is the next thing that you do in a precedent transaction analysis?

A. So you take the sort of deal value --

Q. And, you know, may be helpful to explain this by having Slide 16 on the screen.

A. So you take sort of the implied enterprise value from the deal consideration and then you divide it by these different measures of value. Here I used three measures of value. I used the last 12 months of EBITDA and then those two forward looking measures of EBITDA that I used before.

Q. And on the screen here, is this the calculations you did with respect to the acquisition of Lorillard?

A. It is. Exactly. That's what the LO stands for up there. And so if you just do this analysis for Lorillard, the sort of implied enterprise value to last 12 months EBITDA is 11.5. The enterprise value to next 12-month EBITDA is 11.2. And then the second year out multiple is 10.5.

Q. And so let's look at Slide 17, please. What does this show?

A. It's the same type of chart that I showed for the comparable companies which is it's just looking at the average, the median, and then I pull out the one that I think is most comparable, Lorillard. And it's looking at the different measures of enterprise value to EBITDA.

Q. And can you remind us what multiples were implied by the valuations that the Dissenters' experts did?

A. 24 for Professor Zmijewski and 23.2 for Mr. Taylor.

Q. And what does this slide tell you about the reasonableness of those valuations?

A. Well, again, you know, these are in line with the comparable companies. You know, they're virtually identical to the multiples for comparable companies. And if you get implied multiples which are twice as high as these two, again it causes you -- it would cause me to have serious concern about the assumptions I'm making in my discounted cash flow.

Q. Well, let's go to the next slide, please. Can you tell us what we see here on Slide 18?

A. So this just uses those multiples to get sort of an implied value for RAI. So you take last 12 months EBITDA, next 12 months EBITDA, and then the second year beyond and you multiply it by these. And on average, these numbers are, again, for Lorillard anywhere from 41 to 42 and a half dollars up to 45 to 47.20 for the average.

Q. And what does this tell you about the multiple that BAT paid to acquire RAI in this transaction?

A. You know, that multiple was much, much higher. It was something like 15 or above 15. And so that's -- you know, that's a multiple that's substantially higher than these numbers indicate.

Q. In the beginning of the examination, you mentioned that you also looked at certain market evidence like the unaffected share price of RAI; correct?

A. I did.

Q. Can you tell us why as an economist that was something that you considered relevant to look at?

A. So if the market is efficient and there's no material, nonpublic information, then the market price will be the best estimate of a firm's, you know, intrinsic or fundamental value.

Q. And --

MR. ROLNICK: Your Honor, I object to that answer and I move to strike it. This is -- the premise of that answer was, if the market is efficient, and they had an expert who was going to opine on that issue, and they made the decision not to call that expert. I think it's inappropriate for Professor Gompers to offer any opinions about whether RAI's stock was efficient.

THE COURT: I'll allow him to testify, but it will be subject to your objection.

MR. ROLNICK: Thank you, Your Honor.

MR. BORNSTEIN: And to be clear, Your Honor, I have not asked him to offer the opinion as to whether it was efficient. And we'll deal with the objection in due course in the papers.

BY MR. BORNSTEIN:

Q. So let me just actually put that out there so it's very clear. Do you have an opinion, Professor, as to whether or not the market for RAI stock was efficient at the time of

BAT's first offer?

A. No.

Q. Okay. Do you have an opinion as a financial economist more generally as to whether large stocks like RAI that trade on a large exchange, are or not generally efficient at various points in time?

A. I think to be precise, that most of the time, large firms traded on national exchanges are trading efficiently.

Q. Have you seen any evidence in this case that has caused you to say that the stock of RAI is inefficient?

A. No. I see no evidence of inefficiency.

MR. SHINDEL: Objection, Your Honor.

MR. ROLNICK: Your Honor, I'm going to object again to this line of questioning. He just said he was not going to put this witness on to opine that the stock was efficient.

THE COURT: I'll allow him to testify but subject to your objection.

MR. ROLNICK: Thank you, Your Honor.

BY MR. BORNSTEIN:

Q. And, again, to be clear, have you formed a view as to whether it is -- the market was efficient for RAI stock at the time?

A. No.

Q. So when you just testified that you didn't see evidence indicating inefficiency, can you explain how that is consistent with the fact that you haven't formed an affirmative opinion as to efficiency?

A. Yeah. So there's nothing I've seen either in the review of the analyst reports or any evidence produced in this manner which would cause me to be concerned that the market was inefficient. There's no evidence which has been put forward that would demonstrate that RAI was trading inefficiently.

Q. There's been some testimony that I believe you've heard over the course of the past few days in which people have used the phrase minority discount.

A. Yes.

Q. Do you remember that?

A. Yes.

Q. So just as a matter of economics, what is a minority discount?

A. So we think of a minority discount -- and the way to think about it is, it's the flip of the control premium. So the way we think about a control premium is how much -- how much extra would you be willing to control these assets? And so this -- in this case, BAT paid a 26 percent premium to the prevailing stock price and so that's the controlled premium. The minority discount is just the opposite of that. It relates to where the stock trades under the existing management.

Q. So if you do a DCF valuation of the company, just in the abstract, not RAI specifically. If do you a DCF valuation of the company, does the output of the DCF if done properly, include a minority discount or a control premium?

A. So no. The way to think about it is that there's a set of projections under the existing management and the DCF value of that will equal the stock price. So you don't need to take a minority discount off of the stock price relative to the projections for that current management.

Now, a controlled premium, the reason BAT may be willing to pay more is because they think they can derive more value. So they think they can generate more cash flows. Perhaps they can get some synergy value and the like. And so the assets are worth more. So they pay a control premium. And the value they hope is that their DCF value under their control equals what they would be willing to pay for it.

But it is certainly the case that if you have projections for a company under the existing management, that DCF value should equal the share price with no discount.

Q. So assume a hypothetical company trading on an efficient market that is trading at $10 a share. Would that $10 share price on the efficient market represent the DCF value of the company or would there be some kind of discount reflected in that $10 trading price?

A. It would --

MR. SHINDEL: Objection, Your Honor. Improper hypothetical. There's no evidence in the record that the market is --

(The Court Reporter asked for clarification.)

MR. SHINDEL: It's an improper hypothetical because there's no evidence in the record that the market is efficient. Therefore, there's no foundation for the hypothetical.

MR. BORNSTEIN: Your Honor, it's a hypothetical to an expert. If it turns out that it's not consistent with the facts, that's in argument, they're free to make it in their briefs or on cross-examination.

THE COURT: I'll allow the testimony subject to the objection.

A. So the value would equal the DCF value. You don't take any discount from it. So the -- in an efficient market, those shares would trade at the discounted cash flow value.

BY MR. BORNSTEIN:

Q. And there's been -- there's been some questioning in the case that has I think attempted to imply that the discounted cash flow -- excuse me. To get from the stock price to a discounted cash flow value, you need to add a control premium. You remember testimony about that, question like that?

A. Yes.

Q. Do you agree --

MR. ROLNICK: Objection, Your Honor. I believe that mischaracterizes prior testimony. I think he should just ask the question.

MR. BORNSTEIN: I'll just ask the question. I'll withdraw it, Your Honor.

BY MR. BORNSTEIN:

Q. In your opinion as a matter of economics, is it the case that you need to add a control premium to the price of the stock trading on an efficient market to get to the discounted cash flow value of that company?

A. No.

Q. Please explain why that's not correct.

A. So as I said, the control premium is the value to somebody else who can derive more value from those assets. It's not the value of that company under the existing management -- assuming that no transaction occurred. So what you're really trying to figure out is what is this company worth if it were to have continued on its own and you don't add a control premium to that discounted cash flow value?

Q. Let's go to the -- some of the work you looked at with respect to the share price here.

When you talked about it, you referenced the unaffected share price of RAI. Can you tell me what you mean by calling it the unaffected share price?

THE COURT: Is it just too much?

(Courtroom laughter.)

MS. SADIGHI: Sorry.

THE COURT: Mr. Rolnick, we dare not start without you.

(Mr. Rolnick arrived.)

MR. BORNSTEIN: We decided to take that out of your time.

(Courtroom laughter.)

THE COURT: All counsel ready?

MR. ROLNICK: Yes. Thank you, Your Honor.

THE COURT: All right. Mr. Bornstein, you may resume your direct examination.

MR. BORNSTEIN: Thank you, Your Honor.

BY MR. BORNSTEIN:

Q. Before the lunch break we were talking about the reason why you had looked at the deal price as part of your evaluation of the Dissenters' experts fair value estimates. Can you explain why it was you looked at the deal price?

A. I had started to go into the answer and what I wanted to do was to compare the premium that was paid by BAT to purchase RAI of 26 percent to the implied premium if you were to apply the valuations done by Professor Zmijewski and Mr. Taylor. And so as I mentioned, the premium -- well, the deal premium was 26 percent. But if the valuations of

Dissenters' experts were true, the value -- the premium would have been 95 to a hundred percent.

Q. And what conclusion do you draw from that?

A. That that's just sort of -- that kind of a premium paid in an acquisition is enormous. It's huge.

Q. And what relevance does that have to your assessment ultimately of the reasonableness of their evaluation?

A. Again, it would cause you pause. This is a check. And if you see that the premium is that high, you want to go back to your assumptions into your discounted cash flow to understand what's driving this and are those reasonable assumptions.

Q. And as an economist, if there were a discrepancy of this magnitude between the deal price and the fair value of the company, would you expect that to be noticed by the market?

A. Over time for sure. One would expect the market would sort of find it out. In some sense, it would be like the proof is in the pudding. Eventually the truth would come out and the price would rise to that level.

Q. Well, when you say eventually the truth would come out, can you explain what you mean?

A. Well, I mean, as we saw earlier, the implied multiples are nearly twice as high based on the Dissenters' experts. So if there was truly some mountain of gold that was hidden, something inside RAI that was hidden, eventually that would have come out and I would have expected -- again, back to the analysis we talked about just before break -- that somehow BAT would have appreciated quite substantially because they got such a deal on purchasing of RAI.

Q. Are you saying that BAT stock would have gone up at some point when the value became known?

A. So essentially both Professor Zmijewski and Mr. Taylor are -- they're opining that, you know, $50 billion of value was transferred from the RAI shareholders to BAT because they've underpaid by $50 billion. So if that were the case, one would expect that over time -- again, the proof is in the pudding -- that those results would have come out and BAT would have gone up because people would have seen that they got such a great deal.

Q. And did you see any evidence that that has happened over time?

A. Well, no. Again, the stock price of BAT has fallen by about 60 percent since they purchased RAI.

Q. Was there anything in the analysts' coverage of the deal that was relevant to your assessment of the Dissenters' valuations of the company?

MR. ROLNICK: Your Honor, I'm going to object to that question. Whether or not analysts who are not before the Court offered opinions or not is rank hearsay. They're not here to be cross-examined. He hasn't conducted a valuation. This is just another way of summarizing argument and presenting it to the Court.

THE COURT: Well, experts can rely on inadmissible evidence and I'm going to -- I'll -- subject to your objection, I'm going to allow the testimony. But it's subject to your objection and that will be something that you can raise in your post-trial briefing.

MR. ROLNICK: Thank you, Your Honor.

BY MR. BORNSTEIN:

Q. And perhaps to grease the wheels on this a little bit, is the review of analyst coverage of a stock something that financial economists do in the ordinary course of assessing the value of a company?

A. Absolutely. Whenever I do a valuation, I look at industry analysts, I look at company analysts to try and assess what the view in terms of the state of the company, the state of the industry, certainly the financial advisors here did the same thing. And so while again, you have to filter it and sort of interpret it from, you know, just these are individuals' perspectives, it does provide you insight in terms of contemporaneously what they were thinking about in this case the deal price that was agreed to.

Q. And what did you find when you did that analysis here?

A. So I read every single analyst report around the deal, around the merger, for both RAI and for BAT. And, you know, typically the vast, vast, vast majority -- virtually all except for one, thought the deal price was rich. It was at a historic high. And that potentially BAT was overpaying.

So saw nothing -- not a single analyst who said that BAT was getting a steal.

Q. Let's take a look at Slide 27, please. And can you tell us, Professor, what Slide 27 shows?

A. So Slide 27 is just all of the evidence that I bring to bear on assessing sort of fair value here. And it starts with my unaffected stock price analysis on the top. I graph the range of discounted cash flow values from the financial analysts. My own comparable company and precedent transaction analysis, as well as the comparable company and precedent transaction analysis of the financial advisors. And what you can sort of see is that generally they all line up -- they all line up a lot.

The one outlier here is actually on the comparable companies, there's one outlier and that's ITC, this sort of Indian conglomerate. That's where you get this 82 and the 79. But other than that one comparable company, all the others line up basically right where the deal price is or actually lower.

And what I did as well is I just put Professor Zmijewski's and Mr. Taylor's discounted cash flow numbers on here just for the purposes of seeing where it lies. And you can sort of see that relative to all the other evidence that one should think about in terms of assessing the sort of fair value or the market intrinsic value of RAI, they all line up with the deal price and there's only two that are far to the right.

Q. So on the slide, what is the vertical line that cuts through the middle of everything?

A. Sure. I probably should have said. But you see at the top, it says deal price and then if you follow it over to the right, it says 59.64? That's sort of the deal price. And that vertical line, the dotted line just represents -- just represents where among all those analyses 59.64 is.

Q. And where in comparison to the dotted line do you see Professor Zmijewski and Mr. Taylor's analyses landing? A question I ask in part so it's in the transcript and not just here on the screen.

A. It's at the bottom and it's the 92.17 and the 94.33. And they are way off to the right on the far end of the -- on the far end of the graph.

Q. And what does that tell you as an economist about the reasonableness of their valuations?

A. They're unreasonable. All the checks and value go to say that it's just an unreasonable valuation of RAI. And doing any of these checks would have caused you to go back and be concerned about your inputs.

MR. BORNSTEIN: I have no further questions for you, Professor. Return the witness five minutes early.

THE COURT: All right. Cross-examine?

CROSS-EXAMINATION

BY MR. ROLNICK:

Q. Good afternoon, Professor Gompers.

A. Good afternoon.

Q. How many appraisal opinions, expert opinions have you given in the past?

A. In all states, four in Delaware, two in California, one in Massachusetts, and one in Illinois. So maybe nine, ten.

Q. And how many of those have been for Plaintiffs? And by Plaintiffs, I mean Dissenters.

A. Almost half. So, yeah, I would sort of say, if it's not half, it's sort of a significant fraction of them.

Q. Okay. So about half of them given for Plaintiffs which I'm calling Dissenters here, shareholders, and half for -- on behalf of the company; right?

A. Yeah. It's roughly speaking. It's certainly a significant fraction. I haven't always been for the tendering company.

Q. Okay. So the question was: Are you offering an opinion that the value of RAI as of the merger closing date is within the range of the discounted cash flow valuations that the financial advisors produced?

And your answer is: I haven't been asked to offer that opinion.

MR. BORNSTEIN: Your Honor, we need to see the remainder of the answer, which goes on for another two paragraphs if we're going to try to impeach the witness, we need to do it with a full answer rather than one sentence.

THE COURT: Well, under 106, let's see the rest.

BY MR. ROLNICK:

Q. It's certainly the case -- excuse me?

THE COURT: He just needs to remove the highlight.

BY MR. ROLNICK:

Q. So I'll just start with the preliminary question which is: You're not offering --

MR. BORNSTEIN: Your Honor, I think we should actually see the attempted impeachment here so we can --

THE COURT: He does need to see -- it's proper for the party opposing to see the context which is now on the screen.

BY MR. ROLNICK:

Q. So my question is: Is it the case that you're not offering an opinion that the fair value of RAI as of the closing date is within the range of discounted cash flow valuations that the financial advisors produced?

A. I was about to offer to your prior question an answer which is exactly the same as the answer I gave at my deposition. Which is, it's my view that the valuation done by the financial advisors were optimistic. Because they used optimistic cash flows in their projections, the valuation -- the actual fair value actually likely lies below because these projection were optimistic.

And that's exactly what I go on to say in response to the question that I was asked at the deposition.

Q. Okay. So I understand that you have reviewed their opinions; right?

A. I've reviewed the analysis they've done and I've come to the conclusion that their discount rates are reasonable, close to what I come up with. The perpetuity growth rate is reasonable, but the projections are optimistic. Those things would lead their valuations to be optimistic or an overestimate of fair value.

Q. Okay. You're not giving any opinion that the unaffected stock price on October 20th was the -- represented the fair value of Reynolds; correct?

A. That's correct. It has to be on the merger date that it's completed.

Q. And you're not giving any opinion that the deal price represented the fair value of RAI; correct?

A. That's correct.

Q. Okay. You're not giving any kind of an opinion that the deal process involving the sale of RAI to BAT was sufficient or adequate to produce a fair price; correct?

A. I haven't been asked to offer an opinion on the process.

Q. And you have no opinion about whether BAT's stated unwillingness to support a sale to another potential buyer may have impacted fair value; correct?

A. Again, I haven't been asked to look at that.

Q. And you're not offering the opinion that the analysts' opinions represented the fair value of Reynolds; right?

A. No, but I think they are indicators of value which is helpful to the Court.

Q. Okay. Now, I'd like to put up on the board one of the slides, PDX5.24.

(The Court Reporter asked for clarification.)

MR. ROLNICK: Yeah. PDX5.24. Yeah.

BY MR. ROLNICK:

Q. And as a preliminary matter, you would agree with me, wouldn't you, that discounted cash flow analysis is the best method to value a company provided you can do one?

A. So discounted cash flow is certainly the definition of value. It's derived from finance. But it's only as good as the inputs. It's -- as I mentioned in my direct, it's math. And without doing an analysis of checks, you can't be certain that your inputs are correct.

Q. But you'd agree with me that it is generally the preferred methodology for valuation?

A. Absolutely. But without checks, then it's just not following proper valuation procedures.

Q. Professor Gompers, we'll get to the checks. I'd just like you to answer the questions if you could. It's the preferred methodology for valuating companies; right?

A. It's the first method you would choose but not the only.

Q. Okay. But that wasn't my question. The question is: Isn't it the preferred method?

A. I would not use the word preferred. I think that's incorrect.

Q. Okay. It's almost uniformly used in valuing companies; right?

A. It's the first set of analysis I would do, but I would not use it without a check. That would be incorrect.

Q. Okay. In direct when you were being examined by my colleague, Mr. Bornstein, didn't you say, quote, I'm a firm believer that the DCF is the way to go, unquote? Wasn't that your testimony?

A. It is certainly the first approach to valuation that you would take.

Q. So it was your testimony?

A. I don't recall my exact testimony, but I think I was clear in my direct that it's the first approach, but you'd certainly want to check the inputs into that DCF.

Q. And it's the approach that you used when you were giving a fairness opinion that a deal price arrived at in a situation where a large majority shareholder indicated that it would not support a sale to a third party failed to arrive at a fair price; right?

A. If I'm asked to offer an affirmative opinion on value, I start with the DCF and then do other calculations. So absolutely I would have done DCF.

Q. In fact, you were the expert who gave a fairness opinion in Golden Telecom; right?

A. I did.

Q. And in Golden Telecom, Golden Telecom involved a situation where two shareholders who together held a large block of stock refused to sell their stock in a transaction and bought the company; right?

A. I remember Golden Telecom. I don't remember the particulars of the transaction.

Q. Okay. So you don't remember whether or not you offered an opinion that the fair value of the company wasn't the deal price in that situation but was substantially higher than the deal price, even 35 percent higher? You don't recall that?

A. I do -- let me be clear. I don't recall particulars of the way the transaction proceeded. I do recall giving an analysis and coming up with an analysis where the fair value of -- intrinsic value of the company was higher than the deal price.

Q. Okay. And do you recall that it not only was higher, but the fair value that you opined was the true value of the company, was over a hundred percent higher than the unaffected stock price of that company before the offer was made?

A. Again, I haven't reviewed the Golden Telecom report, but I'll take that as a representation.

Q. You don't remember?

A. I haven't reviewed the Golden Telecom report in quite some time so I just don't remember the exact numbers.

Q. Okay. Well, let's take a look at the Golden Telecom decision. Can we -- I think it's in your book. It's toward the end.

THE COURT: Can I have a tab reference?

MR. ROLNICK: I'm sorry?

THE COURT: A tab reference to where --

MR. ROLNICK: It's just -- it's at the end and it's

MR. BORNSTEIN: We had talked about 2:30 as the time I would commit to finished. So I'm happy -- I'm going to use less than 20 minutes anyway.

MR. ROLNICK: 20 minutes?

MR. BORNSTEIN: I'll be less than that.

THE COURT: All right. Proceed.

MR. BORNSTEIN: Thank you very much.

REDIRECT EXAMINATION

BY MR. BORNSTEIN:

Q. I'll just start where the questioning was kind of ending. This has come up a few times during the course of the day. There's been some questions about control premium. You recall those?

A. Yes.

Q. And, for example, there was a question about ITC and whether -- if you would -- I'll use the questions just now.

Mr. Rolnick asked the question whether -- if you add a 30 percent premium to your calculation of the adjusted stock price using Altria, which was 55 and change, you got to some $70 number; correct?

A. Correct.

Q. Is it correct as Mr. Rolnick's question implied, that you need to add a control premium in order to get to the fair value of the security?

A. So I can't opine as a matter of law, but it's my understanding that fair value from a financial economics perspective is to value the company as if the transaction didn't occur. So the control premium is there because the asset is worth more to the acquirer. It only exists after the transaction.

So if what you're trying to value is the firm, the fair value of the firm, assuming no transaction, you should not gross it up by some control premium.

Q. So let's look, for example, to try to make this concrete at DX277, which was the document Mr. Rolnick directed you to. Page 20. And this is the document Mr. Rolnick was referencing with the 30 percent control premium; correct?

A. Yes.

Q. Now, do you understand this chart to say that these acquirers purchased these targets at a premium of 30 percent over the stock price at which the target was trading?

A. Yes.

Q. And would that 30 percent premium be something that would have to be included in the fair value of these particular targets?

A. So, again, I can't opine as a matter of law --

Q. No. And I'm not asking a legal question.

A. Yeah. But as a matter of financial economics, no.

Because the value -- this is the control premium. This is the increase in value because it's suddenly owned by somebody else who believes they can do more with it. And therefore, the fair value, if it's valuing the company as if it continued without the acquisition, would not include that 29.4 percent premium.

Q. So maybe I should ask the question more simply then. As an economic matter, what is the relationship between fair value and a control premium?

A. So the control premium represents the increase in value, the increase in cash flows that can be generated because the new acquirer can be more efficient, they can hire new managers, they can, you know, do things better than the existing management. And that's why somebody buys the assets because they believe that they're going to be better. They're going to be able to, you know, fire lazy managers and the like. And so that control premium represents the value only under the control of the entity that buys it.

Q. So if we assume a company that's trading on an efficient market at say $10 a share, would you add some kind of control premium to that $10 price in order to reach the fair value?

A. From a financial economics perspective, no.

Q. So if -- so what would be the fair value in that circumstance, assuming a perfectly efficient market?

A. Well, in an efficient market, that price would equal the discounted value you would expect in future cash flows under the existing management. And therefore, in that scenario, the fair value would be $10 because that $10 would reflect the discounted value of those expected future cash flows with existing management.

Q. So if one of your students came to you with your adjusted stock -- unaffected stock price analysis and said I got to $53.33 for Altria using that analysis, and now to get the fair value, I have to tack on a control premium on top of that, what kind of grade would you give that?

A. If it was a financial economics class or corporate finance class, they'd certainly be marked down for doing that.

Q. And why is that?

A. Because it's just indirect. It's not -- it's not based on the fundamental principles of the way markets work in finance.

Q. Let me switch to a different subject which is the comparables companies analysis that we've been talking about for a bit. And Mr. Rolnick asked you whether you believe that none of the companies were really comparable and you told him no and then he moved on. And I want to give you the opportunity to explain why you said no to that question.

A. So because all of these companies sell cigarettes -- sell tobacco products and tobacco products are driven, yes, by different regulatory environments, but there's some commonality across all of them. And therefore, while some of them are certainly closer, and if I were to think about how I would weight these, I would certainly put more weight on those which are closer which is why I talked a lot about Altria here in terms of, you know, being the market leader with all the sales in the U.S. and virtually all tobacco.

But to ignore those other data points would just be wrong. They do provide information about the valuation of tobacco companies and hence, RAI.

Q. Well, let's focus specifically on Altria. Would it be a mistake as a matter of economics to ignore Altria as a comparable in valuing RAI as of the closing?

A. Absolutely. It provides information that would be important to valuing RAI.

Q. And when Mr. Rolnick read to you from paragraph 127 of your report where he asked if you stood by a variety of statements, he skipped two of them. I can just read them to you. He said, with respect to Altria, like RAI, it operates in the United States tobacco industry and in the cigarette market specifically. Do you stand by that statement?

A. I do.

Q. And you said additionally, this firm generated a remind the Court, you calculate this multiple as follows: You take the terminal value out five years and divide it by the -- what's called EBITDA, earnings before interest. So EBITDA. You divide it into EBITDA and say, well, that's the multiple that's implied by your terminal value. That's what it is. And from my terminal value, it's 17.7. Mathematical calculation.

And as we describe in the book and as we typically do, how do you -- what do you do with that? Well, you try to figure out is that a reasonable number, 17.7 for an EBITDA multiple for this company for its terminal value? That's what do you.

Professor Gompers compared it to the same calculation for each of the investment banks. For the financial advisors. For example Lazard's terminal value divided by that EBITDA was 11.5. And then Professor Gompers -- I don't recall exactly what he said, but he certainly pointed out those are different and how can Zmijewski be reasonable relative to the investment bankers? Look at the investment bankers. They're ten and a half to eleven and a half. Zmijewski's at 17.7.

So that was his testimony. And when I saw that, you know, I said well, there's a different chart that should be shown, not that chart. So I created a different chart which is on the next slide.

Q. And is that Slide 26?

A. Yes, it is.

Q. And what's this show?

A. So why would we get -- on Slide 25, why do we get those differences? Well, it's very simple. I just showed the Court what happens if you use a ten-year forecast, how different those values are. And that's also the same if you use, instead of the zero percent growth rate, Dr. Flyer's 2.2 percent growth rate. So what I did was I calculated -- re-calculated Goldman's DCF, JPMorgan's DCF, Lazard's DCF. And instead of using their midpoint growth rate, I used 2.2 percent, Dr. Flyer's. Then I would calculate the terminal value, divided by their EBITDA, these are the numbers you get.

And you see my 17.7 is right in the middle of the three financial advisors had they used the 2.2 percent growth terminal growth rate that Dr. Flyer opines on.

So what does that previous slide show us? The previous slide that Dr. -- Professor Gompers showed us is telling us nothing other than Zmijewski used a higher growth rate than the investment bankers. That's all that you can learn from that chart. And we know that's true and that's of course one of the big issues in this matter, is the 2.2 percent growth rate, the correct growth rate. And if it is, then the next slide, Slide 26, is the correct comparison and

I am right in the middle of the financial advisors.

Q. So just to make sure I'm clear, what you're saying is these charts say nothing other than you used a different growth rate than the financial advisors in your valuation. Is that right?

A. Yes. It's just another way to depict differences in growth rate. Yes.

Q. So moving on from your discounted cash flow valuation, did you consider any other customary valuation methodologies in valuing RAI?

A. I did. I was asked to -- by you, to consider -- use your valuation methodologies that you use typically to value Reynolds to the extent you can. And those are the DCF valuation method and the market multiple valuation method. Market multiple valuations, there's two types, two broad types. One is you go to publicly traded comparable companies, calculate their multiples, apply it to the company you're valuing. The other is you go to transactions that occurred, calculate the multiples from those transactions, and use those transaction multiples, sometimes called precedent transactions, to value the company value.

And I reviewed those two methods and concluded neither one of those methods would result in a reliable valuation of Reynolds.

Q. So let's start with the market multiples methodology that you described as the comparable company market multiple methodology. Is that okay?

A. Of course.

Q. And you said you determined in this case that you didn't rely on the comparable companies methodology to value Reynolds. Could you explain why not?

A. Yes. As a preface to that explanation, if you look at Slide 28. And this is just a little screenshot of my book. You'll just say in words what it says here.

First, all market multiples depend on risk and growth. The higher the risk, the lower the multiple. The higher the growth, the higher the multiple. So if you have a high growth company, it will have a higher multiple, all else equal, than a low growth company.

No one disagrees with that. Professor Gompers in his report agreed with that.

You don't stop there when you're using an EBITDA multiple. I'm focused just on EBITDA now. Because there's other determinants. Tax rates affect the EBITDA multiple. Depreciation, cost structure affects the EBITDA multiple. The required investments in working capital and capital expenditures affect the EBITDA multiple. The profitability, margins, rates of return all affect the EBITDA multiple. So when you think about are two companies comparable, which is the last sentence that I have in this cut out, we begin with comparable companies as potential comparable companies by looking at competitors.

That's not enough. You have to look at all these determinants of these multiples, risk, growth, for EBITDA multiple, working capital requirements, capital expenditure requirements, tax rates, cost structure, rates of return, margins, all of those factors drive multiples in one direction or another. You need to align -- what you would like to do is have a comparable company that aligns on every one of those factors. It doesn't exist but that's how you assess comparability. You can't just go out and say they're both selling cigarettes. That's good enough. That's not how it works.

Q. So in this case, how did you use all of those underlying criteria to inform your view of whether or not potential competitors or potential companies were, in fact, comparable for purposes of a market multiple valuation?

A. So first issue, first thing you do when you're doing an assignment like this is is what did the financial advisors do. And I noticed immediately that many of the identified potential comparable companies are not U.S. companies. They don't sell products in the U.S.

What does that mean? Well, first that raises a whole different set of issues. Independent of this industry, if you're looking at market multiples across countries, you perpetuity growth rates relative to what I think we would have used had we had ten years.

Q. Did you have discussions internally about what perpetuity growth rates you would use, if you had ten years worth of projections?

A. We did.

Q. And what were those discussions?

A. Well, we never came to a specific conclusion because ultimately we ended up using the five years. But I believe we would have -- we were at least socializing using a range of negative perpetuity growth rates, if we had years six through ten.

Q. And why would you have used lower growth rates if you had ten-year projections than growth rates you had used after the five years of projections?

A. Because our anticipation was that there would be, you know, some growth -- continued growth at the company in years six through ten and thus, to account for that, in the context of the five years of projections that we did have, we used a slightly higher range of perpetuity growth rates relative to if we had ten years worth of projections, and then had accounted for that potentially higher growth in years six through ten.

We would have married that with a view that the industry would continue to decline following that point in time at a likely negative rate.

Q. Now, earlier you mentioned that you did a terminal multiple analysis. Is that correct?

A. We did. Yeah.

Q. And could you explain for the Court what that means?

A. Sure. A terminal forward EBITDA multiple that is seen at the bottom right of page .261. And this document is essentially calculating the firm value EBITDA of the company following the forecast period, as if you had fast-forwarded to the end of five years. And we used this as a sanity check in the context of our valuation work because that multiple should be a turn or two -- typically is a turn or two lower than where the company trades today, given that you have gone through five years of out size growth.

Q. So using that terminal forward EBITDA multiple, did that tell you anything about the inputs that you had chosen to use in your discounted cash flow analysis?

A. It did. I think -- as we would have expected, it came in about a turn and a half below where the company trades today; and thus, ultimately, helped us conclude that the valuation work that we had done in the context of the discounted cash flow analysis was intuitive and rational.

Q. Now, here you did a discounted cash flow analysis, as well as an analysis of the multiples with precedent transactions and the multiples for comparable companies, why do you do -- why do you use three valuation methodologies?

A. Just -- just as a means of being complete and looking at as many accepted valuation methodologies in the context of looking at the value of a publicly-traded company. It is -- it would be atypical for us to do anything but look at all three of those valuation methodologies in the context of providing an opinion.

Q. Now, ultimately, did JPMorgan issue a fairness opinion?

A. We did.

Q. What's the process at JPMorgan for issuing a fairness opinion?

A. We have a very rigorous process, whereby we prepare a set of materials that do not look very different from this set of work materials that you've referenced here. It typically has a couple of additional pages just to provide additional background in the context of this situation.

And the steps that we go through are, first, that set of materials is sent to the Fairness Committee coordinator who does an initial review of the materials, the analytics, the assumptions underlying the analytics and potentially in certain circumstances, if they have views or thoughts on the way we've approached the analytics provides those points of feedback in advance of ultimately scheduling a Fairness Committee meeting, which is made up of a number of managing directors within our M&A group who do not work on that particular deal.

And then there is a -- either a meeting or a call, depending on scheduling, to review the materials with the Fairness Committee, who then has the ability to provide additional feedback on our materials and analytics.

Q. And with regard to this transaction, did you meet with the Fairness Committee before issuing the fairness opinion?

A. We did. Can't recall if it was a meeting or a call, but we did speak with them.

Q. Okay. And did the Fairness Committee have any concerns about okaying a fairness opinion to be issued here?

A. No concerns as it relates to the fairness of the transaction. There was some dialogue about what we had discussed in relation to the company's ability to provide us a ten-year forecast. But other than that, from a headline value perspective, there were no concerns.

Q. Were there any discussions about the perpetuity growth rates that you chose to use in your discounted cash flow analysis when you were -- you had your discussions with the Fairness Committee?

A. Not to my recollection. I don't recall that being a particular point of discussion.

Q. Now, I believe you said that a fairness opinion was ultimately issued by JPMorgan?

A. That's correct.

Q. And did you have any concerns about whether or not you should issue a fairness opinion for this transaction?

A. Not at all.

Q. How did you feel this transaction rated in terms of bringing value to the shareholders? Did you think it was a valuable transaction?

A. Yeah. I thought it was a fantastic transaction. I wish we had the ability to get transactions like this for all of our clients.

MS. SHAH: I have no further questions.

(PX115 was marked and admitted into evidence.)

THE COURT: Cross-examine?

MR. ROLNICK: Thank you, Your Honor. May we approach with the books, Your Honor?

THE COURT: Yes.

CROSS-EXAMINATION

BY MR. ROLNICK:

Q. Good morning, Mr. Clark. My name is Lawrence Rolnick, and I'm here representing a group of shareholders who are dissenters from the merger.

A. Morning.

Q. I'd like to show you in the first instance on

Wharton.

Currently, since 2013, I hold the endowed chair -- professorship; the Wharton Private Equity Professor chair. I also lead the school's efforts on alternative investments. My formal title is founding academic director of Josh Harris Program in Alternative Investments. I think that's new title.

In that capacity, I lead the school's efforts in both research and teaching. In that capacity, I have redesigned the school's curriculum on alternate investments, ranging from venture capital, private equity, hedge funds, corporate restructuring, destressed investment, infrastructure, finance, and so on so forth. And I have designed about ten courses and I've lead teaching of most of those courses in the last four years.

I've also created our executive education in that space, so I also train investment professionals in this area. I understand the previous witness didn't find it worthwhile to come to Wharton. Getting a CFA certificate was more attractive, but I would encourage her to rethink. That was meant as a joke, so.

Previous to my current job, I was on the faculty of Stanford Graduate School of Business, again teaching finance. Before I moved to Stanford, I had started my career at the Wharton School about 23 years ago.

Q. And have you taught any classes related to valuation?

A. Most of my investment classes are based on valuation, shareholder activism, private equity mergers and acquisition. They're all valuation based.

Q. Have you taught classes related to game theory?

A. Interestingly, finance and economics is a little unusual. At the Ph.D. level, things change dramatically. So we don't really train our students in game theory a lot at the undergraduate/MBA level. But at the Ph.D. level, both at Wharton and Stanford, I have taught game theory with application of the finance.

Q. What is your educational background?

A. My first degrees are in electrical engineering and physics. Then I switched to economics at the graduate level. I earned my master's and the Ph.D. in economics from Princeton University.

Q. What areas has your academic research focused on?

A. We divide financial economics in terms of research into two areas. Asset pricing and corporate finance. I work on both those areas.

Asset pricing is how asset allocation is done in an optimal way and also how prices are formed in financial markets. The corporate finance side is where most of my teaching is because those are popular courses, is how corporations are valued and how financial decisions should be made in corporations.

MR. SHINDEL: Your Honor, at this point, the Dissenters would tender Professor Yilmaz as an expert in economics, finance, and valuation and ask for judicial recognition of his ability to testify in that capacity.

MR. BORNSTEIN: No objection, Your Honor.

THE COURT: The witness may testify.

BY MR. SHINDEL:

Q. All right. Professor Yilmaz, what was your assignment in this matter?

A. I was asked to read, evaluate, analyze, and respond to the reports of Professor Gompers and Professor Shivdasani.

And within that, there were two main questions I was asked or expected to analyze. One of them is that pre-offer as of October 20th, 2016, was the trading price a good proxy for fair value of Reynolds, or RAI.

For the record, I will say Reynolds. RAI's is a little thicker for me to say, for some reason, but that's what I mean.

Second question is very similar in nature. Was the merger consideration as of closing date, was a good proxy for the fair value of Reynolds?

Q. And so everyone is on the same page, can you explain the definition of fair value that you used for the purpose of your analyses?

A. So this is very standard in financial economics. When we look at a company as an independent firm that is expected to go on as an independent entity, we value its total future cash flows and we divide it by -- we divide it by the number of outstanding shares fully diluted. That gives you the fair value.

Just to be sure we are all on the same page, this does not have any kind of minority discount or some kind of acquisition premium or control premium attached to it.

I was also told that this coincides with North Carolina law, but I'm not a legal scholar so I won't opine on that.

Q. And if we go to Slide No. 4, can you summarize your opinions with respect to whether RAI's pre-offer trading price is a good proxy for fair value?

A. Right. This is an important concept that we'll talk more about as to how much of the information is incorporated into prices. And at the time of the offer, there was a lot of private information that was not known by the public markets and there was also a new information came by the time the closing came.

You have to realize, October to July, there is several months that had a lot of information events were occurring. So given that information had no chance of being incorporated into prices, I don't believe the trading price had any chance of being close to fair value.

Second point is that the company had an unusual large blockholder. They usually associate that with some kind of a minority discount with the trading price. And that will be another reason that a specific discount that is worth looking into.

Q. And with reference to the next slide, can you summarize your opinion with respect to whether the merger price or transaction price is a good proxy for fair value?

A. So when I analyzed the case, I've noticed that the process did not really look for other potential buyers pre- or post-signing and there was no competitive environment created by the sellers either. And I will comment on that more as needed. So those are the things that would be obstacles in price discovery, so to say, during that sales process.

The other issue that is of importance here that is similar to the trading price prior to the offer is that, at that point when shareholders were deciding, there were still considerable amount of information that was not made available to the shareholders, nor to other potential bidders. So that always would be another reason.

And similarly to the previous case, the large blockholder will also be an obstacle on other potential bidders coming in and leading to an efficient price formation in the marketplace. So that's another thing.

This last point is a rather complicated and deep point. I'll try to make an attempt. Again, don't take me as -- I mean, I'm coming from a different profession so I think there is little bit of a miscommunication within legal scholars and finance scholars. That's my experience.

I happen to speak a lot on the law scholar events as well. This is something I'll try to -- I think economists should take on themselves to explain better. And I will try to explain well because I don't think economists have succeeded in legal scholar environment. So this will be a big issue for me.

Q. Okay. Well, we'll focus on that one later. For now I want to turn back to the trading price. And I don't think you were present in the courtroom live when Professor Gompers testified. Were you?

A. I was not. I actually went through his document -- is it called trial testimony?

Q. A copy of -- well, a rough copy of the transcript?

A. Transcript. That's right. So I'm familiar with it.

Q. So you had the opportunity to review the transcript of Professor Gompers' testimony?

A. That's right. It was a learning process for me.

No. 368A20 TWENTY-FIRST DISTRICT

SUPREME COURT OF NORTH CAROLINA

REYNOLDS AMERICAN INC.,

Plaintiff-Appellee,

v.

THIRD MOTION EQUITIES
MASTER FUND LTD, MAGNETAR
CAPITAL MASTER FUND, LTD.,
SPECTRUM OPPORTUNITIES
MASTER FUND LTD, MAGNETAR
FUNDAMENTAL STRATEGIES
MASTER FUNDS LTD, MAGNETAR
MSW MASTER FUND LTD, MASON
CAPITAL MASTER FUND, L.P.,
BLUE MOUNTAIN CREDIT
ALTERNATIVES FUND L.P.,
BLUEMOUNTAIN FOINAVEN
MASTERFUND L.P.,
BLUEMOUNTAIN GUADALUPE
PEAK FUND L.P.,
BLUEMOUNTAIN SUMMIT
TRADING L.P., BLUEMOUNTAIN
MONTENVERS MASTER FUND
SCA SICAV-SIF, and BARRY W.
BLANK TRUST,

Defendants-Appellants, and

From Forsyth County
No. 17 CVS 7086

ANTON S. KAWALSKY, trustee for the)
benefit of Anton S. Kawalsky Trust UA)
9/17/2015, CANYON BLUE CREDIT)
INVESTMENT FUND L.P., THE)
CANYONVALUE REALIZATION)
MASTER FUND, L.P., CANYON)
VALUE REALIZATION FUND, L.P.,)
AMUNDI ABSOLUTE RETURN)
CANYON FUND P.L.C., CANYON-SL)
VALUE FUND, L.P., PERMAL)
CANYON IO LTD., and CANYON)
VALUE REALIZATION MAC 18 LTD.,)
)
Defendants.)
)

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ADDENDUM

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UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Superior Court of North Carolina, Gaston County.
Business Court.

Lena Sue BEAM, (widow of C. Grier Beam),
Prue K. Beam (Widow of Dewey Beam), First
Union National Bank of North Carolina,
Trustee and First United Methodist Church
of Cherryville, North Carolina, Petitioners,
v.
WORLDWAY CORPORATION, formerly known
as Carolina Freight Corporation, Respondent.

No. 96-CVS-469.
|
Oct. 23, 1997.

{1} This is a dissent and appraisal proceeding governed by N.C.G.S. §§ 55-13-01 through 55-13-31. The case is before the Court on respondent Worldway Corporation's motion to strike the petitioners' demand for jury trial. At issue is the petitioners' right to have a jury determine the issue of fair value under the appraisal process. A hearing was held in Mecklenburg County on August 2, 1996. The Court concludes that the petitioners in this action are not entitled to a jury trial under N.C.G.S. § 55-13-30(d) and do not have the right to a jury trial under the North Carolina Constitution.

Attorneys and Law Firms

James P. McLouglin, Jr. of Moore & Van Allen and Craig P. Buie of Buckley, McMullen & Buie, attorneys for Petitioners.

Debbie W. Harden and Steven D. Gardner of Womble Carlyle Sandridge & Rice, attorneys for Respondent.

ORDER AND OPINION

RELEVANT STATUTES

***1** {2} N.C.G.S. § 55-13-30(d) provides:

> (d) The jurisdiction of the court in which the proceeding is commenced under subsection (b) is plenary and exclusive. The court may appoint one or more persons as appraisers to receive evidence and recommend decision on the question of fair value. The appraisers have the powers described in the order appointing them, or in any amendment to it. *The parties are entitled to the same discovery rights as parties in other civil proceedings. However, in a proceeding by a dissenter in a public corporation, there is no right to a trial by jury.*

N.C.G.S. § 55-13-30(d) (1990) (emphasis added).

{3} N.C.G.S. § 55-1-40 provides in pertinent part:

> In this Chapter unless otherwise specifically provided:
>
> ....
>
> (14) “Means” denotes an exhaustive definition.
>
> ....
>
> (18a) “Public corporation” means any corporation that has a class of shares registered under Section 12 of the Securities Exchange Act of 1934, as amended (15 U.S.C. Sec 781).

N.C.G.S. S 55-1-40 (Supp.1995).

{4} N.C.G.S. § 55-13-01 provides in pertinent part:

> In this Article:
>
> (1) “Corporation” means the issuer of the shares held by a dissenter before the corporate action, or the surviving or acquiring corporation by merger or share exchange of that issuer.
>
> (2) “Dissenter” means a shareholder who is entitled to dissent from corporate action under G.S. 55-13-02 and who exercises that right when and in the manner required by G.S. 55-13-20 through 55-13-28.
>
> (3) “Fair value,” with respect to a dissenters shares, means the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects....

N.C.G.S. § 55-13-01 (1990).

FACTUAL BACKGROUND

{5} Each of the petitioners was the record or beneficial owner of shares of the 4% preferred stock of Worldway Corporation ("Worldway"). Worldway was formerly known as Carolina Freight Carriers Corporation and Carolina Freight Corporation. It was previously headquartered in Cherryville, North Carolina. The individual petitioners are widows of the cofounders of Carolina Freight Corporation.

{6} On July 14, 1995, Arkansas Best Corporation, through a wholly owned subsidiary, ABC Acquisition Corporation, offered to purchase all of the outstanding shares of common stock of Worldway. At that time, Worldway had a class of shares registered under Section 12 of the Securities Exchange Act of 1934, had in excess of two thousand shareholders, and was a "public corporation" as defined by N.C.G.S. § 55-1-40(18a). As a part of the proposed transaction, the shareholders, including petitioners, were notified that ABC Acquisition Corporation would be merged into Worldway after the purchase of a sufficient number of shares of Worldway.

{7} On or before October 11, 1995, all of the petitioners gave notice of their intent to demand payment for their respective shares of preferred stock in the event the shareholders of Worldway voted to approve the merger of ABC Acquisition Corporation into Worldway as they were required to do by N.C.G.S. § 55-13-21. Had they not done so, they would have failed to meet the necessary requirements under the statute to *"be and remain a dissenter eligible to demand payment for his shares." See* N.C.G.S. § 55-13-21 official comment (1990).

***2** {8} On October 12, 1995, the common shareholders of Worldway voted to approve the merger of ABC Acquisition Corporation into Worldway. The merger was complete at 11:59 p.m. After the merger, Worldway had only one shareholder. It is undisputed that the merger created dissenters' rights in petitioners under N.C.G.S. § 55-13-02. That same day, Worldway sent petitioners the dissenters' notice required by N.C.G.S. § 55-13-22 to be sent to all shareholders who had complied with N.C.G.S. § 55-13-21. The official comment to this section of the statute states: "The basic purpose of Section 13.22 is to require the corporation to tell *all actual or potential dissenters* what they must do in order to take advantage of their right to dissent." N.C.G.S. § 55-13-22 official comment (1990) (emphasis added).

{9} On October 20, 1995, effective at the opening of the trading session, Worldways common stock, formerly registered under the Securities Exchange Act of 1934, was deregistered pursuant to application by the New York Stock Exchange, Inc. At this point, Worldway was no longer a public corporation and has not regained that status. It is a wholly owned subsidiary of Arkansas Best Corporation, a public corporation.

{10} On or before November 20, 1995, Worldway had received from petitioners a written demand for payment of their shares of preferred stock as required by N.C.G.S. § 55-13-23. Had petitioners failed to make written demand, they would have waived their rights under article 13. The official comment to this section of the statute refers to the demand for payment as the "*definitive statement by the dissenter." See* N.C.G.S. § 55-13-23 official comment (1990). In the demand for payment, a dissenter must certify whether the date on which the dissenter acquired ownership of the shares was before or after the date of announcement of the proposed corporate action giving rise to the dissenter's rights. Petitioners had also deposited their share certificates as required by this section of the statute. The official comment states: "The deposit of share certificates is necessary to prevent *dissenters* from giving themselves a 30-day option to take payment if the market price of the shares goes down, but sell their shares on the open market if the price goes up." *Id.* (emphasis added).

{11} On or before November 20, 1995, Worldway had also sent to petitioners a written offer to purchase their respective shares which N.C.G.S. § 55-13-25 required be sent to all dissenters who had complied with the demand for payment requirements. That statute provides in pertinent part: "As soon as *the proposed corporate action is taken,* or upon receipt of a payment demand, the corporation shall offer to pay each *dissenter who complied with G.S. 55-13-23* the amount the corporation estimates to be the fair value of his shares, plus interest accrued to the date of payment, and shall pay this amount to each *dissenter* who agrees in writing to accept it in full satisfaction of his demand." N.C.G.S. § 55-13-25(a) (1990) (emphasis added).

***3** {12} On or before December 20, 1995, petitioners sent Worldway the notice of their estimate of the fair value of their respective shares of preferred stock required by N C.G.S. §

55-13-28. Failure to comply with this requirement would have resulted in petitioners resuming the status of *nondissenting shareholders. See* N.C.G.S. § 55-13-28 N.C. commentary (1990).

{13} On February 8, 1996, petitioners filed their petition to determine fair value as provided in N.C.G.S. § 55-13-30. It is undisputed that at that time, Worldway was not a public corporation as defined in the statute.

{14} At each step in the process, petitioners have complied with the statutory requirements to be and remain dissenters.

I

{15} The first issue before this Court is whether the date used to determine if a dissenter is a shareholder in a public corporation is the date the petition to determine fair value is filed or the date the corporate action is taken from which the shareholder dissents.

{16} In this case, it is clear that Worldway was not a public corporation on February 8, 1996, the date the petition for fair value was filed, and that it was a public corporation on October 12, 1995, the date of the merger which was the corporate action from which petitioners dissent. The date to which this Court looks in determining the corporation's status is determinative of the right to jury trial under the statute. For the reasons set forth below, the Court concludes that the date of the corporate action from which the petitioners dissent is the date to which the Court should look in determining whether Worldway was a "public corporation" as defined in N.C.G.S. § 55-1-40(18a) and used in N.C.G.S. § 55-13-30(d).

{17} In interpreting N.C.G.S. § 55-13-30(d), this Court must ascertain and be guided by the intent of the legislature. *State v. Fulcher,* 294 N.C. 503, 243 S.E.2d 338 (1978). The intent and spirit of the Act are controlling in its construction. *In re N.C. Fire Ins. Rating Bur.,* 275 N.C. 15, 165 S.E.2d 207 (1969). In ascertaining that intent, the Court should look to the language of the statute, the spirit of the Act and what it sought to accomplish, as well as the changes that were made and how they should be effected. *Stevenson v. Durham,* 281 N.C. 306, 188 S.E.2d 281 (1972). N.C.G.S. § 55-13-30(d) was enacted as part of an overall revision of the North Carolina Business Corporation Act in 1989. The history of dissenters' rights prior to 1989 and the 1989 revisions are instructive in ascertaining the legislature's intent.

{18} Dissenters' rights are entirely statutory. No common law cause of action exists for dissent and appraisal. Indeed, North Carolina was one of the first states to create dissenters' rights. *See* Russell M. Robinson, *Robinson on North Carolina Corporation Law* § 27-1, at 519 (5th ed.1995) [hereinafter *N.C. Corporation Law*]. North Carolina first enacted a dissent and appraisal statute in 1925. From that time until the 1989 revisions at issue here, the right to a jury trial on the issue of fair value existed under the statutory scheme. *See* N.C.G.S. § 55-167 (1950), § 55-113 (1982). North Carolina has historically been home to many family-owned textile, furniture, and retail companies. It has a history of protecting the rights of minority shareholders, particularly in closely held companies. *See Meiselman v. Meiselman,* 309 N.C. 279, 307 S.E.2d 551 (1983).

***4** {19} It is against this background that the current revisions must be assessed. When the General Statutes Commission was charged with rewriting the Business Corporation Act, it delegated responsibility for creating the original draft to the Business Corporation Act Drafting Committee (the "Drafting Committee"). The Drafting Committee used the Revised Model Business Corporation Act (the "Model Act") as a basis for its work, comparing the then-existing chapter 55 with the Model Act, section by section. *See* Drafting Committee minutes of January 20, 1986. The section of the Model Act dealing with dissent and appraisal proceedings was section 13-30. It did not provide for a trial by jury in dissent and appraisal proceedings. The Drafting Committee followed the Model Act and eliminated the right to jury trial in appraisal cases. *See* Drafting Committee minutes of September 21, 1987, and October 28, 1987. It proposed to the General Statutes Commission a version of N.C.G.S. § 55-13-30 which read in pertinent part: *"The parties are entitled to the same discovery rights as parties in other civil proceedings but are not entitled to a trial by jury."* General Statutes Commission minutes of March 4, 1988. The language proposed and the Drafting Committee minutes of October 28, 1987, clearly indicate that the Drafting Committee intended to eliminate jury trials in all appraisal cases. The October 28 minutes provide:

> The committee also noted that the appraisal process, which has been liberalized by the committee, involves an adjustment of corporate rights and that a jury would have problems

> understanding the appraisal process. The Committee further noted that the right of appraisal is not a constitutional right but is part of the corporate contract in that it is part of what a shareholder buys into when he buys shares in a corporation.

{20} The Drafting committee's version of N.C.G.S. § 55-13-30 survived review in the General Statutes Commission unchanged and became a part of Senate Bill 280, which constituted the proposed Business Corporation Act revision submitted by the General Statutes Commission to the General Assembly. The Senate passed the bill without any change to N.C.G.S. § 55-13-30. When the bill was considered in the House Judiciary Committee, Representative Miller proposed to amend the last sentence of N.C.G.S. § 15-13-30(d) to read: "[T]*he parties are entitled to the same discovery rights as parties in other civil proceedings, but in a proceeding by a dissenting shareholder in a public corporations [sic] are not entitled to a trial by jury.*" House Judiciary Committee minutes of May 30, 1989. The next day, Representative Michaux proposed to amend the last sentence of N.C.G.S. § 55-13-30(d) to read as follows, *"The parties are entitled to the same discovery rights as parties in other civil proceedings. However, in a proceeding by a dissenter in a public corporation, there is no right to a trial by jury.*" House Judiciary Committee minutes of May 31, 1989. This version ultimately became law.

***5** {21} The use of the Model Act as a basis for the revisions to the Business Corporation Act was purposeful. It helped to bring North Carolina's corporation law in closer conformity with the majority of other states. This helped provide certainty for businesses interpreting North Carolina law since there would be a broader body of case law from similar statutes giving greater guidance in interpretation. It also helped remove any unique quirks in the North Carolina statutes which would discourage corporations, particularly large public companies with operations in many states, from domesticating in North Carolina. By conforming more closely to the Model Act, North Carolina made itself more attractive to public companies to incorporate here. The Model Act provided no right to trial by jury in appraisal cases for either public or private companies. There are several valid reasons for eliminating jury trials in appraisal cases. The appraisal process can be extremely complex, especially with diversified national or multinational companies. As the Drafting Committee noted, a jury could have difficulty understanding the appraisal process. Furthermore, publicly traded companies operate in an environment where there is a market mechanism which provides a strong, if not determinative, indicator of the value of minority shares. There are federal and state statutory protections built into transactions involving publicly held companies. Information from which shareholders can evaluate transactions is readily available from public companies because of disclosure and filing requirements of the federal securities laws. In the merger or purchase of a publicly traded company, minority and majority shareholders are generally treated the same.

{22} Closely held companies present a different situation. The appraisal issues are generally less complex with smaller, less diversified, locally owned companies. There is no strong market mechanism to provide an indication of value. There are no filing or disclosure requirements. Financial information may not be readily available. Squeeze-outs of minority shareholders in closely held companies have the potential of creating disproportionate benefits between minority and majority shareholders and of frustrating minority shareholder expectations which may exist in such situations. Thus, practical reasons exist for differentiating between public corporations and closely held companies in the appraisal context.

{23} It is apparent that the legislature was faced with a conflict between the benefits of conforming to the Model Act and the tradition of preserving the rights of minority shareholders in closely held companies. There were also practical reasons for differentiating between the two ownership situations. Not surprisingly, a compromise was reached which followed the Model Act with respect to public corporations and preserved the right to jury trial for minority shareholders in closely held corporations.

***6** {24} The changes from the language and structure of the last sentence in the Drafting Committee report to the last two sentences of the statute as enacted demonstrate that the distinction was being made between publicly held and privately owned companies. When that decision was made, the language had to be changed to differentiate (a) those civil proceedings in which a jury trial would not be afforded, and (b) those civil proceedings referred to in the first part of the original sentence. The change was made in a manner that deviated as little as possible from the Model Act and the Drafting Committee's proposal.

{25} The purpose behind the legislative action is instructive on the issue before the Court because the transaction to which petitioners dissent was a transaction involving a public corporation. The shareholders in the corporation were thus afforded the protection of a market mechanism for valuation, full disclosure, public information, and a similar treatment of all shareholders. This was not a transaction in a closely held corporation whose shareholders did not have those protections.

{26} The Worldway/ABC merger is typical of the common practice of a parent company using a wholly owned subsidiary or acquisition corporation as a vehicle to accomplish the purchase of a publicly held company. The acquiring corporation and the acquired corporation are frequently merged, and the surviving corporation becomes a wholly owned subsidiary of the parent corporation. There is nothing in the statutory history or language to suggest that the legislature, by amending the Drafting Committee's language, meant to extend the right to jury trials in those situations. It is far more likely that the legislators were concerned with providing a jury trial to shareholders in corporations which were closely held at the time of the transaction giving rise to dissenters rights.

{27} Focusing on the transaction also helps clarify the issue from the perspective of interpretation of the specific language and the statutory scheme. To dissent is to withhold assent. *Merriam Webster's Collegiate Dictionary* 336 (10th ed.1993). The action from which petitioners are withholding assent is the merger of Worldway and ABC Acquisition Corporation. Assent is being withheld from the action of a corporation in which the shareholder had an ownership interest. See the definition of "corporation" in N.C.G.S. § 55-13-01(l) set out above. Petitioners' position that a "dissenter in a public corporation" must refer only to a shareholder who has withheld assent from an action *and* filed a petition to determine fair value after the action has been taken is not supported by logic or the statutory scheme. The statutory focus is clearly on the time of the transaction from which the shareholder dissents. "Fair value" must be determined just before that time, not at the time of trial. It is only logical that the time to determine the status of the corporation for the purpose of ascertaining the right to a jury trial should be the same as the time of the corporate action triggering the right. Nor is petitioners' position supported by the statutory scheme. As the factual background set forth above (particularly the passages in italicized print) indicate, pursuit of dissenters' rights involves a series of steps. At each step, dissenters must take certain actions to become and remain dissenters. The status of dissenter may be gained and lost prior to the filing of a petition to determine fair value. Accordingly, article 13 as a whole does not support an inference that "dissenter in a public corporation" as used in N.C.G.S. § 55-13-30(d) refers only to a shareholder who has filed a petition.

***7** {28} Petitioners argue that the definition of "dissenter" in N.C.G.S. § 55-13-01(2) supports their position. That definition does just the opposite. It defines a dissenter as a shareholder who exercises his or her rights "when and in the manner required by G.S. 55-13-20 through 55-13-28." It thus specifically defines a dissenter without reference to the filing of a petition as set forth in N.C.G.S. § 55-13-30. Petitioners fit the description of a dissenter in a public corporation perfectly.

{29} Focusing the determination of dissenter status at the time of the corporate action has the practical benefit of fixing the determination at one point in time. Under petitioners' theory, the determination could change from time to time after the action depending on the public or private status of the surviving company in the merger. It is unlikely the legislature intended to create such a moving target.

{30} The legislative history, the purpose of the statute, the language, and the statutory scheme all support the conclusion that in a proceeding initiated by a shareholder withholding assent from an action of a public corporation giving rise to dissenters' rights, there is no right to trial by jury on the issue of fair value.

II

{31} The second issue before this Court is whether petitioners have been unconstitutionally deprived of their right to a trial by jury.

{32} Petitioners contend that if the North Carolina Business Corporation Act is read to deprive them of a jury trial on the issue of fair value, it is unconstitutional. The Drafting Committee considered that argument and rejected it. *N.C. Corporation Law* § 27-4, at 529 n. 8. The Drafting Committee was correct because dissenters' rights are a statutory creation and were not in existence at the time the North Carolina Constitution was adopted in 1868. There was no common law right to dissent and appraisal. The right was first created in 1925 by statute. Thus, the right to a jury trial on the issue of fair value could only be created by express language in the statute. *Kiser v. Kiser,* 325 N.C. 502, 385 S.E.2d 487 (1989). Such express language does not exist in article 13; to the contrary, the express language eliminates the right to a jury trial.

CONCLUSION

{33} Petitioners are "dissenters in a public corporation" as that term is used in N.C.G.S. § 55-13-30(d). That statute expressly denies their right to a trial by jury on the issue of fair value. The denial is not a violation of their constitutional rights. Respondents' motion to strike petitioners' jury demand should be granted.

{34} It is therefore, ORDERED that the demand for a jury trial in this action be stricken.

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UNPUBLISHED OPINION. CHECK
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Court of Chancery of Delaware.

BLUEBLADE CAPITAL OPPORTUNITIES
LLC, a Delaware Limited Liability Company,
and Blueblade Capital Opportunities CI LLC, a
Delaware Limited Liability Company, Petitioners,
v.
NORCRAFT COMPANIES, INC., a
Delaware corporation, Respondent.

C.A. No. 11184-VCS
|
Date Submitted: April 25, 2018
|
Date Decided: July 27, 2018

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MEMORANDUM OPINION

SLIGHTS, Vice Chancellor

***1** This statutory appraisal action arises out of a May 12, 2015, merger whereby Fortune Brands Home & Security, Inc. (“Fortune”) acquired Norcraft Companies, Inc. (“Norcraft” or the “Company”) (the “Merger”) for $25.50 cash per share (the “Merger Price”). Petitioners, Blueblade Capital Opportunities LLC and Blueblade Capital Opportunities CI LLC (together, “Blueblade”), were Norcraft stockholders on the Merger's effective date and seek a judicial determination of the fair value of their Norcraft shares as of that date.

In an appraisal action under the Delaware General Corporation Law, the trial court's “fair value” determination must “take into account all relevant factors.”[1] The relevance (or not) of certain factors “can vary from case to case depending on the nature of the [acquired] company,” the nature of the process leading to the company's sale and, perhaps most importantly, the evidence adduced by the parties at trial in support of their respective valuation positions.[2] “In some cases, it may be that a single valuation metric is the most reliable evidence of fair value and that giving weight to another factor will do nothing but distort that best estimate. In other cases, “it may be necessary to consider two or more factors.”[3] In all cases, however, the trial court's determination respecting the “relevant factors” must be grounded in the evidentiary record and “accepted financial principles.”[4]

I am cognizant of the Delaware Supreme Court's embrace of “deal price” as a strong indicator of fair value in *Dell* and *DFC.* Those decisions teach that deal price often will be a relevant factor in the trial court's fair value calculus —particularly where the respondent company was publicly traded and sold following a meaningful market check.[5] In both cases, however, despite having been urged to do so, the Supreme Court declined to adopt a rule that the deal price is presumptively reflective of fair value.[6] Mindful of *DFC* and *Dell*, I have considered carefully whether the Merger Price (less synergies) reflects the fair value of Norcraft as of the Merger date. For the reasons explained below, I am satisfied it does not.

***2** In this case, the evidence reveals significant flaws in the process leading to the Merger that undermine the reliability of the Merger Price as an indicator of Norcraft's fair value. There was no pre-signing market check; Norcraft and its advisors fixated on Fortune and never broadened their view to other potential merger partners. As the parties worked to negotiate the Merger agreement, Norcraft's lead negotiator was at least as focused on securing benefits for himself as he was on securing the best price available for Norcraft. And, while the Merger agreement provided for a thirty-five-day post-signing go-shop, that process was rendered ineffective as a price discovery tool by a clutch of deal-protection measures.

Dell reminded us that Delaware courts have "long endorsed" the "efficient market hypothesis" and emphasized "that the price produced by an efficient market is generally a more reliable assessment of fair value than the view of a single analyst, especially an expert witness who caters her valuation to the litigation imperatives of a well-heeled client."[7] I have heeded that guidance as well. Unfortunately, this case was tried before the Supreme Court decided *Dell*, and the record evidence regarding the efficiency of the market for Norcraft stock prior to the Merger is, in a word, thin. With that said, the evidence that can be drawn from the record reveals that, at the time of the Merger, Norcraft was fresh off an initial public offering of its stock, was relatively thinly traded given the niche market in which it operated and was also thinly covered by analysts. Under these circumstances, I can discern no evidence-based rationale that would justify looking to the unaffected trading price of Norcraft's stock either as a standalone indicator of fair value or as a data point underwriting the use of a deal-price-less-synergies metric.

Having concluded that flaws in the sales process leading to the Merger undermine the reliability of the Merger Price as an indicator of fair value, and that the evidence *sub judice* does not allow for principled reliance upon the efficient capital markets hypothesis, I have turned to a "traditional valuation methodology," a discounted cash flow ("DCF") analysis, to calculate the fair value of Norcraft as of the Merger date.[8] In my view, given the evidence in this record, a DCF-based valuation provides the most reliable means by which to discharge the Court's statutorily mandated function to appraise Norcraft.

Not surprisingly, both parties proffered expert testimony regarding Norcraft's fair value on a DCF basis. And, as we have come to expect in appraisal litigation, the experts' DCF analyses yielded valuations that are miles apart. Neither expert walked the high road from start to finish during their respective DCF journeys. That is to say, both experts, at times, made choices in their analyses that were not supported by the evidence or not supported by "accepted financial principles" in order to support a desired outcome. I have, therefore, borrowed the most credible components of each expert's analysis to conduct my own DCF valuation, in my best effort to obey our appraisal statute's "command that the Court of Chancery undertake an '*independent*' assessment of fair value" when performing its mandated appraisal function.[9] As explained below, my DCF analysis reveals a valuation of $26.16 per share.

***3** Insofar as *Dell* and *DFC* require that the trial court carefully consider deal price before disregarding it altogether, I have returned to the Merger Price as a "reality check" before locking in my DCF valuation as the last word on fair value. Having done so, I am satisfied that the $0.66 per share delta between the Merger Price and my DCF valuation of Norcraft is a product of the identified flaws in Norcraft's deal process. Accordingly, I conclude that the fair value of Norcraft as of the Merger date was $26.16 per share.

I. FACTUAL BACKGROUND

I recite the facts as I find them based on the evidence presented during a four-day trial. That evidence comprises testimony from thirteen fact witnesses (some presented live and some by deposition) and three live expert witnesses, along with over 500 exhibits. I accord the evidence the weight and credibility I find it deserves. As noted, both parties carried a burden to prove their respective valuation positions by a preponderance of the evidence. Thus, Petitioners were obliged to prove that their proffered valuation of Norcraft, a DCF-based valuation of $34.78 per share, represented Norcraft's fair value as of the Merger; Respondent's burden was to prove that its proffered valuation of $21.90 per share, the Merger Price less synergies, was Norcraft's fair value as of the Merger. With these competing burdens in mind, I find that the following facts were proven by a preponderance of the evidence.

A. Parties and Relevant Non-Parties

Respondent, Norcraft, is a Delaware corporation in the cabinetry manufacturing business.[10] Prior to the Merger, Norcraft's stock traded on the New York Stock Exchange.[11] On May 12, 2015, Fortune acquired Norcraft for $25.50 cash per share in the Merger.[12] In connection with that transaction, Norcraft merged with an indirect, wholly-owned subsidiary of Fortune, Tahiti Acquisition Corp. ("Tahiti"), with Norcraft surviving as a wholly-owned Fortune subsidiary.[13]

Petitioners were Norcraft stockholders as of the Merger date and collectively held 557,631 shares of Norcraft common stock.[14] It is undisputed that they properly perfected their statutory appraisal right.

Non-party, Fortune, is a home and security products company with four business segments: cabinets, plumbing, doors and security.[15] Fortune sells its products through several sales channels, "including kitchen and bath dealers, wholesalers oriented to builders or professional remodelers, industrial and locksmith distributors [and] 'do-it-yourself' remodeling-oriented home centers .... "[16]

Non-parties, Mark Buller, Christopher Reilly, Michael Maselli, Harvey Wagner, Ira Zecher and Edward Kennedy served on Norcraft's board of directors (the "Board") at all relevant times.[17] Buller also served as the Chief Executive Officer of Norcraft (and its predecessors) from 2003 to the Merger's consummation in May 2015.[18] Non-party, Leigh Ginter, was the Chief Financial Officer of Norcraft (and its predecessors) from 2003 through the Merger's consummation.[19] And non-party, Eric Tanquist, was Norcraft's Vice President of Finance Administration from approximately 2007 through the Merger's consummation.[20]

***4** Non-party, Christopher Klein, is Fortune's CEO and served in that capacity at all times relevant to this action.[21] Non-party, Robert Biggart, is Fortune's general counsel and served in that capacity at all relevant times.[22] And non-party, Jason Baab, served as Fortune's Vice President of Corporate Development and M & A at the time of the Merger.[23]

B. Pre-Merger Norcraft

As of the Merger date, "Norcraft was a leading manufacturer of kitchen and bathroom cabinetry in the United States and Canada."[24] The Company sold its products primarily to kitchen and bathroom cabinet dealers in the home repair, remodeling and new home construction markets through four business divisions: Mid Continent Cabinetry, StarMark Cabinetry, UltraCraft Cabinetry and Urban Effects (a.k.a. Norcraft Canada).[25] Prior to the Merger, Norcraft regarded Fortune, American Woodmark Corporation ("American Woodmark") and Masco as its principal competitors.[26] It also faced competition from "a large number of smaller manufacturers."[27]

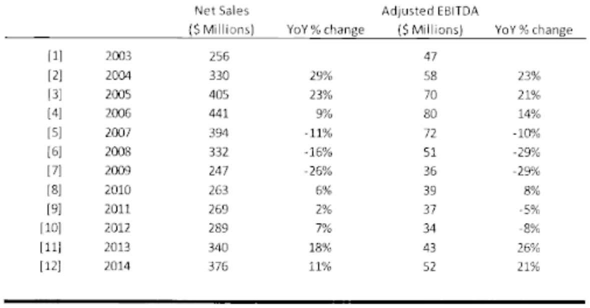
1. Buller and Two Private Equity Firms Acquire Norcraft's Operating Subsidiary in 2003

In October 2003, Buller, certain Buller family members and funds affiliated with the private equity firms Saunders, Karp & Megrue ("SKM") and Trimaran Capital Partners ("Trimaran") acquired Norcraft Companies, L.L.C. for approximately $315 million (the "2003 Acquisition").[28] At the same time, Norcraft Companies, L.L.C. converted to a Delaware limited partnership, Norcraft Companies, L.P. ("Norcraft LP"), and Buller became the CEO of that entity.[29] For the next ten years, Norcraft LP operated as a privately-held company.

2. Norcraft and the Cyclical Cabinetry Industry

***5** The undisputed evidence reveals that Norcraft operated in a cyclical industry.[30] As one naturally might expect, the cabinetry industry is directly affected by the home improvement industry, which, in turn, is affected by macro-economic conditions, including employment levels, demographic trends, availability of financing, interest rates and consumer confidence.[31] The cabinetry industry is also directly affected by housing starts, as a significant percentage of sales are connected to new home construction.[32] When housing starts decrease, as they often do for various reasons,[33] cabinet sales decrease as well.[34]

Norcraft was no exception to this cyclicality. Norcraft LP enjoyed steady growth of its earnings before interest, taxes, depreciation and amortization ("EBITDA") from 2003 through 2006—$47 million (2003) to $80 million (2006).[35] This growth was fueled, in large part, by a significant acquisition in March 2002 and a boom in the United States housing market.[36] Growth stalled, however, beginning in 2007, when Norcraft LP experienced the first of three consecutive years of declining sales and adjusted EBITDA.[37] As is typical in classically cyclical businesses, Norcraft LP saw improved sales beginning in 2010, although its adjusted EBITDA continued to decline until 2012 (with 2010 being the only exception). The attached chart illustrates the trends[38]:

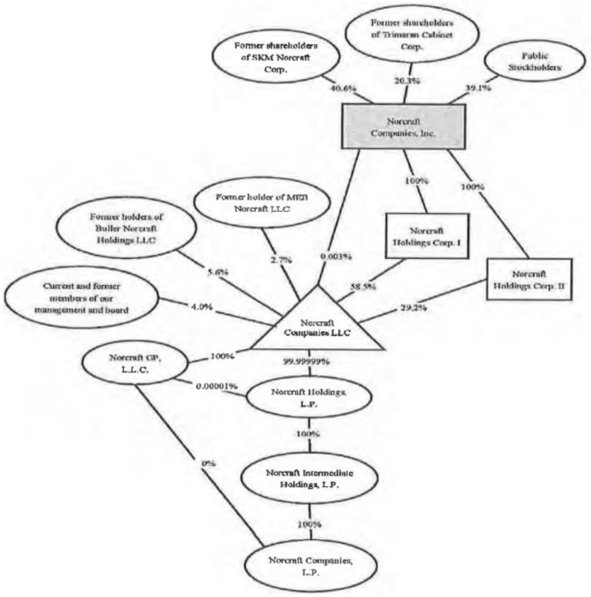


		Net Sales ($ Millions)	YoY % change	Adjusted EBITDA ($ Millions)	YoY % change
[1]	2003	256		47	
[2]	2004	330	29%	58	23%
[3]	2005	405	23%	70	21%
[4]	2006	441	9%	80	14%
[5]	2007	394	-11%	72	-10%
[6]	2008	332	-16%	51	-29%
[7]	2009	247	-26%	36	-29%
[8]	2010	263	6%	39	8%
[9]	2011	269	2%	37	-5%
[10]	2012	289	7%	34	-8%
[11]	2013	340	18%	43	26%
[12]	2014	376	11%	52	21%

As reflected in the chart, Norcraft LP's adjusted EBITDA trended up in 2013, suggesting that its six-year period of decline had come to an end, at least for the time being.[39]

3. Norcraft's IPO and Reorganization

On November 13, 2013, Norcraft completed an initial public offering ("IPO")[40] whereby the Norcraft enterprise was reorganized into the following holding company structure[41]:


Former shareholders of SKM Norcraft Corp.
Former shareholders of Trimaran Cabinet Corp.
Public Stockholders
40.6%
20.3%
39.1%
Norcraft Companies, Inc.
100%
100%
Former holder of MEZ Norcraft LLC
Former holders of Buller Norcraft Holdings LLC
Norcraft Holdings Corp. I
Norcraft Holdings Corp. II
2.7%
0.003%
5.6%
58.5%
Current and former members of our management and board
4.0%
29.2%
Norcraft Companies LLC
Norcraft GP, L.L.C.
100%
99.99999%
0.00001%
Norcraft Holdings, L.P.
100%
0%
Norcraft Intermediate Holdings, L.P.
100%
Norcraft Companies, L.P.

The newly-formed parent company, Norcraft—a publicly-traded company—was a holding company; Norcraft Companies LLC ("Norcraft LLC")[42] and its subsidiaries were the operating entities.[43] Following the reorganization, Norcraft was Norcraft LLC's sole managing member and owned (directly and indirectly) approximately 87.7% of Norcraft LLC, with Buller, his family members and certain members of Norcraft management holding the remainder.[44]

***6** As part of the IPO, Norcraft sold 7,356,634 shares of Norcraft common stock, or 39.1% of Norcraft's equity, to the public at $16.00 per share.[45] SKM and Trimaran together retained a 60.9% equity interest in Norcraft, while Buller, his family members and certain members of Norcraft management, through their convertible Norcraft LLC units, collectively held a prospective 12.3% equity interest.[46]

In conjunction with the IPO, Norcraft entered into Tax Receivable Agreements ("TRAs") with SKM, Trimaran and the Norcraft LLC unitholders (collectively, the "TRA Beneficiaries").[47] Under the TRAs, Norcraft was required to pay the TRA Beneficiaries 85% of the applicable annual tax savings, if any, that Norcraft realized as a result of certain tax benefits contributed to Norcraft by the TRA Beneficiaries, including net operating losses and asset basis step-ups.[48] The TRAs also provided that Norcraft's payment obligations to the TRA Beneficiaries would be accelerated in the event of a "Change of Control."[49] The TRAs later came to feature prominently in the Norcraft-Fortune negotiations leading up to the Merger.

C. Fortune Approaches Norcraft

On October 20, 2014, representatives of Fortune's financial advisor, RBC Capital Markets, LLC ("RBC"), contacted Buller to inform him of Fortune's interest in a potential acquisition of Norcraft.[50] Three days later, Buller met with Fortune's CEO, Christopher Klein, at Fortune's headquarters in Deerfield, Illinois to discuss a potential Norcraft-Fortune transaction.[51] During that meeting, Buller informed Klein that Norcraft was not for sale, but also indicated that he (Buller) would convey any acquisition proposal to Norcraft's Board.[52] Perhaps sensing that his Board might be inclined to pursue a deal with Fortune, Buller advised Klein that he would like to have a role in the post-Merger company in the event the parties reached an agreement.[53] Klein was noncommittal but, internally, Fortune was disinclined to bring Buller on board post-Merger.[54] At the meeting's close, Klein provided Buller with a written, non-binding proposal under which Fortune would (1) acquire "100% of [Norcraft's] equity ownership interests" for $22.00 cash per share via a tender offer (followed by a merger); and (2) satisfy Norcraft's obligations under the TRAs.[55]

***7** Buller promptly informed Norcraft's Board of Fortune's proposal, and the Board convened on November 4, 2014 to discuss it.[56] Following that meeting, Norcraft engaged legal and financial advisors to assist the Board in its consideration of Fortune's proposal.[57] The Company retained Ropes & Gray LLP ("Ropes & Gray") as its legal advisor and Citigroup Global Markets Inc. ("Citi") as its financial advisor.[58] The Board promptly tasked Citi with "review[ing] strategic alternatives of the [C]ompany, including a potential sale to Fortune."[59] Norcraft also engaged Pricewaterhouse Coopers ("PwC") to provide an assessment of the Company's contractual obligations under the TRAs.[60]

D. Norcraft's Management Prepares Long-Term Projections

Norcraft's Board met again on November 8, 2014.[61] During this meeting, "[t]he [B]oard ... discussed next steps in formulating a potential response to [Fortune], and after discussion, agreed that [Buller, Ginter and Reilly] would map out a proposed strategy and response with Citi [ ] and report their recommendations back to the [B]oard."[62] The Board also instructed Buller and Ginter to prepare five-year financial projections to facilitate the Board's evaluation of strategic alternatives (including a potential Norcraft-Fortune transaction).[63]

Buller and Ginter both had experience preparing long-term projections, having previously prepared five-year projections in connection with Norcraft's IPO and four debt financing transactions between 2003 and 2010.[64] Norcraft, however, did not prepare long-term projections in the ordinary course of its business; it only did so in connection with "extraordinary event[s]" such as financing transactions and ultimately the Merger.[65] Ordinarily, Norcraft management prepared an annual one-year budget, which forecasted Norcraft's quarterly (and monthly) performance for the upcoming year.[66] The Company's annual budgeting process began each fall and involved several steps[67]:

- First, the corporate controller for each of Norcraft's four business divisions would prepare a detailed "bottoms-up" budget for his or her division.[68] As part of that process, the division controllers "would work with [their respective] division presidents to come up with what they expected for sales growth in the [upcoming] year and... would build that into the budget[,] [along with] ... other assumptions like labor efficiencies [and] material cost."[69] In this way, the division controllers "would get a picture of what [profit and loss] would look like for [their respective divisions for] the [upcoming] year."[70]
- Next, each division controller would present his or her division-level budget to Buller and Ginter "for review and approval."[71]
- Finally, "[a]fter several rounds of... back-and-forth," Ginter would compile the division-level budgets "into a consolidated format," which was then presented to the Board for review and approval in January of the budgeted year.[72] After review, the Board typically would approve the consolidated annual budget that same month.[73]

***8** Following the Board's November 8, 2014 meeting, Buller and Ginter created two sets of five-year projections: a base-case projection (the "Base Case") and an upside-case projection (the "Upside Case"), both of which are summarized below.[74]

Base Case Projections (FY2014-2019)[75]

($ in millions)	2014E	2015E	2016E	2017E	2018E	2019E
Net Sales	$371	$409	$448	$483	$523	$568
EBITDA	$51	$59	$70	$79	$89	$100
EBIT	$36	$42	$51	$58	$68	$81
CapEx	$10	$18	$12	$15	$16	$17

Upside Case Projections (FY2014-2019)[76]

($ in millions)	2014E	2015E	2016E	2017E	2018E	2019E
Net Sales	$373	$415	$460	$507	$558	$613
EBITDA	$51	$61	$75	$89	$105	$120

EBIT	$36	$45	$56	$67	$82	$100
CapEx	$10	$18	$12	$15	$17	$18

In preparing the Base Case and Upside Case projections, Buller and Ginter took a "top-down" approach—independently projecting Norcraft's net sales, operating expenses and capital expenditures (for all business divisions) in the first instance, and then consulting with division-level management as and where needed—rather than the "bottoms-up" approach they used to prepare Norcraft's annual budgets.[77] They created the Upside Case first.[78] After preparing the Upside Case, Buller and Ginter presented it to Reilly for his review.[79] "Upon review, [Reilly opined] that the [Upside Case] ... was too aggressive ... and asked [Buller and Ginter] to go back and... do a more conservative model, which became known as the [B]ase [C]ase."[80] Buller and Ginter both believed that Norcraft could achieve the results forecasted in the Base Case and Upside Case projections, although "the [U]pside [C]ase was more of a stretch and everything would have had to go right."[81]

Buller and Ginter presented the Base Case and Upside Case projections to Norcraft's Board at a meeting on November 25, 2014.[82] After discussion, the Board approved both sets of projections for use in connection with the Board's consideration of Fortune's proposal.[83]

E. Norcraft Pushes Fortune to Increase its Offer

***9** Norcraft's Board next met on December 3, 2014.[84] During this meeting, Citi presented the Board with an analysis of Norcraft's standalone prospects and possible strategic alternatives.[85] Citi's presentation included an overview of preliminary valuation perspectives and selected strategic alternatives,[86] "including maintaining the status quo, a possible sale of the Company to [Fortune] or another buyer, as well as some other potential acquisition targets."[87] Following Citi's presentation, the Board determined that (1) "[Fortune's] proposed price of $22.00 per share was inadequate"; and (2) "[Fortune's] offer would need to be significantly and substantially higher in order for the Board to consider a potential sale of the Company at this time."[88] The Board, however, did not task Citi with pursuing alternative buyers or canvassing the market.

Two days later, Buller called Klein and conveyed to him the Board's determination.[89] Buller also explained that "if [Fortune] were interested in significantly increasing [its proposed price] ..., [Norcraft] would be prepared to share certain [non-public] information [with Fortune], under a confidentiality agreement with an appropriate standstill, in order to assist [Fortune] in understanding [Norcraft's] prospects, upside potential and intrinsic value."[90] Soon thereafter, on December 11, 2014, Norcraft and Fortune entered into a confidentiality agreement with a standstill.[91]

On January 7, 2015, Buller, Ginter and Citi representatives met with Fortune's management at Buller's home in Winnipeg, Canada to discuss the proposed Norcraft-Fortune transaction.[92] The discussion focused on the structure and timing of the proposed transaction, Norcraft's business and financial projections and the integration of Norcraft into Fortune.[93] Norcraft provided Fortune with the Base Case and Upside Case projections as well as certain preliminary information regarding the TRAs.[94] During this meeting, Buller reiterated his interest in post-closing employment with Fortune and discussed the possibility with Klein.[95] Again, Klein "ke[pt] the door open" but stopped short of making a commitment.[96]

The following week, on January 14, Norcraft's tax advisor, PwC, presented its analysis regarding the TRAs to Fortune's management and RBC.[97] PwC explained that termination of the TRAs in connection with Fortune's acquisition of Norcraft would require significant payments to the TRA Beneficiaries (including Buller).[98] PwC also identified certain tax benefits that Fortune could realize from the acquisition, including a stepped-up basis in Norcraft's assets.[99] The next day, Klein advised Buller that Fortune's tax advisor was performing its own analysis of Norcraft's obligations under the TRAs following the proposed transaction.[100] Klein also noted that Fortune would require more information about the TRAs to calculate Fortune's full payment obligations to the TRA Beneficiaries.[101]

***10** On January 27, 2015, Klein delivered to Buller a revised written indication of interest with a proposed price of $25.00

per share.[102] Buller promptly informed Norcraft's Board of Fortune's revised proposal, and the Board met on February 2 to discuss it.[103] During this meeting, Citi provided the Board with its revised valuation analysis, which incorporated Norcraft's net sales and EBITDA results for Q4 FY2014 (both of which were higher than expected) and Fortune's latest proposal of $25.00 per share.[104] Reilly then reviewed with the Board the tax benefits that Fortune would realize in connection with its proposed acquisition of Norcraft, including a stepped-up basis in Norcraft's assets.[105] After receiving Reilly's report, "the Board concluded that [Fortune] would benefit from th[at] step-up in basis going forward and should therefore value th[at] benefit in its offer price."[106]

With Citi's and Reilly's input in hand, the Board determined that Fortune's proposed purchase price of $25.00 per share was inadequate, in part because it did not value the tax benefits that Fortune would realize in connection with the proposed transaction.[107] The Board also believed, however, "that a transaction with [Fortune] could potentially create more value for [Norcraft] stockholders if at an appropriate valuation than if [Norcraft] continued independently to execute on its strategic plan. Accordingly, the Board authorized [Buller and Reilly] to continue to engage in discussions with [Fortune] to confirm if [Fortune] was willing to further increase its propos[ed] [price]."[108] Even at this stage, however, the Board did not reach out to other potentially interested parties in hopes of securing a better offer or, at least, a source of leverage in its discussions with Fortune.

The next day, Buller called Klein to convey Norcraft's position regarding Fortune's revised proposal.[109] During that call, Buller advised Klein that Fortune's proposed price remained inadequate and encouraged Fortune to increase its bid.[110] Unable to invoke the threat of an alternative transaction, Buller highlighted Norcraft's better than expected preliminary FY2014 results and FY2015 outlook as support for his pitch that Fortune pay a higher price.[111] Apparently not feeling the heat, Klein advised Buller that Fortune would consider increasing its bid but that it was unlikely that Fortune's proposed price would move significantly higher than $25.00 per share.[112]

Following Buller and Klein's February 3 call, Fortune increased its offer to $25.50 per share, indicating that this was its "best and final offer."[113] The Norcraft team was less than thrilled with Fortune's $25.50 per share proposal; indeed, Reilly and Ginter both believed that Fortune's proposal significantly undervalued Norcraft.[114] Nevertheless, the Board remained focused exclusively on Fortune. In a last-ditch effort to get Fortune to increase its "best and final offer," the Board responded with a counterproposal of $27.50 per share.[115] When Fortune rejected that counterproposal, the Board bid against itself with a second counterproposal of $26.25 per share.[116] Once again, Fortune held firm and reiterated that $25.50 per share was its best and final offer[117]—well aware that it was getting the Company for a "good price."[118] With no alternative transaction on the horizon, Norcraft's Board capitulated on February 21 at $25.50 per share, hoping to extract further value during a post-sign go-shop.[119]

F. The Parties Negotiate the Merger Agreement

***11** In late February 2015, Citi informed Fortune that Norcraft was prepared to move forward with Fortune's $25.50 per share proposal, subject to the negotiation of a merger agreement that included a forty-five-day post-signing go-shop right for Norcraft.[120] Fortune responded with a counterproposal that provided for a twenty-five-day post-signing go-shop "that would be limited to certain identified potential purchasers."[121] The counterproposal also called for a $15 million termination fee if Norcraft accepted a superior proposal received during the go-shop period and a $25 million termination fee otherwise.[122] By proposing this structure, Fortune sought to give Norcraft's Board "the minimum amount [of time it] needed to satisfy [its] fiduciary responsibility... and no more,"[123] while also "discourag[ing] potential bidders."[124]

On February 27, following negotiations, the parties eventually settled on a thirty-five day post-signing go-shop period (the "Go-Shop Period") with no restrictions on the parties Norcraft or its advisors could contact, a $10 million termination fee if Norcraft accepted a superior proposal during the Go-Shop Period and a $20 million termination fee otherwise.[125] Importantly, however, Fortune also secured information rights with respect to competing proposals and unlimited matching rights with respect to superior proposals.[126] In a final stroke of masterful bargaining, Fortune also secured the right to launch Tahiti's tender offer for all of Norcraft's outstanding common stock (at $25.50 per share) fifteen days after the start of the Go-Shop Period.[127]

In early March 2015, Fortune was given access to Norcraft's electronic data room, and on March 4, Fortune and Norcraft entered into a thirty-day exclusivity agreement.[128] Thereafter, on March 13, Buller, Ginter and Tanquist met with Fortune management to provide additional non-public information about Norcraft, and, on March 18, Fortune met with the senior management of each Norcraft business division.[129]

***12** With the Merger Price set, and negotiations between Norcraft and Fortune proceeding apace, Buller again approached Klein about post-Merger employment with Fortune. At a Fortune-initiated meeting with Norcraft management on March 6, Buller advised Klein that he wanted to head Norcraft and Fortune's combined cabinetry business post-acquisition.[130] With the price locked in, and the inevitably uncomfortable confrontation now unavoidable, Klein finally informed Buller that Fortune would have no place for him after the Merger.[131] This came as a shock to Buller, who thereafter became increasingly "disruptive."[132]

Unable to abandon the enterprise completely, Buller soon returned to Fortune with a new proposal: if he would not be a part of the combined company, then, upon Fortune's acquisition of Norcraft, Buller would acquire Urban Effects (Norcraft Canada) from Fortune.[133] After Buller announced his interest in acquiring Norcraft Canada, the Board determined, for the first time, that Buller was conflicted and, therefore, should be excluded from Board deliberations regarding the potential Norcraft-Fortune transaction.[134]

***13** Buller, for his part, was determined to acquire Urban Effects and continued to press Fortune for a commitment to sell him the business, while also continuing to lead Norcraft's negotiations with Fortune.[135] Fortune, however, was unwilling to give such a commitment while negotiations with Norcraft were ongoing—much to Buller's frustration.[136] Yet it soon became clear to Fortune that Buller's ire now risked derailing the deal.[137] To keep the peace, on March 25, Reilly emailed Buller to advise him that "[Klein] is going to offer to provide you some meaningful comfort on [C]anada...."[138] Klein's overture to Buller accomplished its intended purpose; Buller felt he had "[g]ot[ten] good comfort on UE."[139] This "comfort" included:

- Fortune's waiver of a two-year, Canada-specific non-compete covenant otherwise applicable to Buller[140]; *and*

- Fortune's agreement to modify Buller's employment agreement with Norcraft's operating subsidiary to provide that Buller would receive a severance payment if his employment was terminated without cause (including by Buller himself) within twelve months of Fortune's acquisition of Norcraft.[141]

Thereafter, it appears that Buller was content to "live with a trust me I will sell Canada to you" status quo, and ostensibly was willing to support the Norcraft-Fortune transaction again —to Fortune's great relief.[142]

With the Norcraft Canada fire contained, Fortune was soon on to the next Buller-related fire. In late March 2015, having finalized most of the merger agreement's material terms, Norcraft and Fortune found themselves unable to reach agreement on the termination payments that would be due to the TRA Beneficiaries holding Norcraft LLC units (including Buller and his family members).[143] Norcraft's and Fortune's tax advisors disagreed as to the value of certain tax attributes associated with the Norcraft LLC units, resulting in a $3 million difference in their respective calculations of the termination payments.[144]

***14** On March 26, Fortune tried to "cut a deal with Buller" on the TRA termination payments by offering to pay $2 million of the $3 million difference.[145] Buller insisted, however, that Fortune pay the entire $3 million, much to Fortune's exasperation.[146] At this point, Fortune seemingly had reached its limit with Buller and advised Citi that "if there [was] no signed [merger] agreement by [the morning of March 30, Fortune was] done."[147] Negotiations followed. Ultimately, to appease Buller and keep the deal on track, SKM and Trimaran offered to transfer $1 million of the TRA termination payments they stood to receive to the Norcraft LLC unitholders, such that the unitholders would receive the full $3 million demanded by Buller.[148] With that, the TRA fire was extinguished and Fortune had no more Buller-related fires to fight.

G. Norcraft's Board Approves the Merger and Norcraft Executes the Merger Agreement

On March 29, 2015, Norcraft's Board received Citi's fairness opinion and approved the Merger Agreement.[149] The following day, Norcraft and Fortune executed the Merger Agreement and issued a press release announcing the Merger.[150] Immediately following the execution of the Merger Agreement, Norcraft entered into TRA termination agreements with the TRA Beneficiaries—SKM, Trimaran and the Norcraft LLC unitholders—providing that the TRAs would be terminated (if the Merger was consummated) in exchange for $43.5 million in total payments to the TRA Beneficiaries.[151]

SKM, Trimaran and the Norcraft LLC unitholders also entered into Tender and Support Agreements ("TSAs") with Fortune and Tahiti,[152] whereby SKM, Trimaran and the Norcraft LLC unitholders agreed that:

- they would "promptly" tender their Norcraft shares into Tahiti's tender offer and, in any event, would do so at least two days before the offer's initial expiration date[153]; *and*

- the shares so tendered could not be withdrawn unless and until the tender offer expired or was "terminated in accordance with the terms of Merger Agreement."[154]

H. The Go-Shop

***15** The Go-Shop Period commenced with the Merger's announcement on March 30, 2015.[155] Given that Norcraft and Citi had focused exclusively on Fortune during the pre-sign "process," it was especially important that the Company run an effective go-shop to provide a meaningful market check. Yet Citi's lead banker, Eldridge, had never run a sell-side go-shop.[156] Because Norcraft's Board was unsure of the go-shop's core components, it relied completely on Citi to oversee the process.[157] Fortune, on the other hand, knew full well what was at stake. Its Vice President of M & A, Robert Baab, pushed hard for an unlimited match right and for Fortune's right to launch Tahiti's tender offer during the Go-Shop Period, understanding that both measures would make it less likely that a topping bidder would emerge.[158]

During the Go-Shop Period, Citi contacted fifty-four potential bidders: twelve potential "strategic" bidders and forty-two private equity firms.[159] Of the fifty-four parties contacted, seven entered into nondisclosure agreements—six private equity firms and American Woodmark, one of Norcraft's industry peers.[160] Only one of those seven parties, Carlyle, went on to meet with Norcraft management.[161] Carlyle ultimately did not submit a bid.[162]

Most of the parties Citi contacted indicated either that they were "not interested in competing with Fortune"[163] or that "[t]he price [was] too high."[164] At least two non-bidding parties, however, advised Citi that they could not "move fast enough [to submit a bid] in 35 days."[165]

In an effort to ensure that Fortune would reap the benefits of its hard-fought bargain, RBC and Klein devised a strategy to dissuade potentially interested parties from engaging with Norcraft. In that connection, early in the go-shop process, RBC emailed Klein advising that RBC had "a call scheduled for [April 9, 2015] with Masco"—one of the go-shop participants—"to discuss the [Merger]."[166] In this email, RBC explained that it would "emphasize [to Masco] that [Norcraft] is an asset that [Fortune has] been monitoring/targeting for a long time ... and [that Fortune] view[ed] the [Merger] as highly strategic."[167] RBC also indicated that it hoped to "get some sense from Masco as to whether or not [Masco was] likely to engage [with Norcraft]."[168] Eager to close the deal, Klein advised RBC that "[t]he trick [with Masco] ... is not to make Norcraft sound very interesting for them."[169] Klein also emphasized that he was "more interested in [RBC] shutting the door on [Masco] and [its] willingness to look at [acquiring Norcraft], versus learning a lot from [Masco] .... "[170]

***16** When Fortune's general counsel, Biggart, learned of this correspondence, he nearly had "a heart attack in [his] office."[171] He immediately "went over to see [Klein]"—before RBC's call with Masco—and "explained to him that [Fortune and its deal team] can't be doing this."[172] Biggart then warned RBC that Klein's proposed approach was "the wrong way to deal with a go-shop" and that "[RBC] can't be interfering like this."[173] Klein apparently heeded Biggart's admonition, as did RBC.[174]

As permitted by the Merger Agreement, Fortune launched Tahiti's tender offer for Norcraft's stock fifteen days into the

Go-Shop Period, on April 14, 2015, securing the support of a majority of Norcraft's outstanding common stock (per the TSAs).[175] The Go-Shop Period expired as scheduled on May 4, with Norcraft having received no competing acquisition proposals.[176] Tahiti successfully completed its tender offer on May 11, and the Merger closed the following day.[177]

I. The Parties' Experts

Both parties presented valuation experts at trial to opine on Norcraft's fair value as of the Merger date.[178] Petitioners' valuation expert was David A. Clarke; Respondent presented Yvette R. Austin Smith.[179] Petitioners also presented a deal process expert, Guhan Subramanian ("Subramanian"), to opine on the soundness (or not) of Norcraft's deal process.[180] I summarize each expert's opinion below.

1. Clarke's Opinion Regarding Norcraft's Fair Value

***17** Clarke opined that the Merger Price of $25.50 per share "does not reflect Norcraft's fair value [as of the Merger date] ... [b]ecause there was no competitive process to acquire Norcraft prior to the signing of the Merger Agreement and the post-signing go-shop process was not an effective tool for price discovery .... "[181] According to Clarke, a DCF analysis premised on the Base Case projections provides the most reliable evidence of Norcraft's fair value as of the Merger date.[182] Based on his DCF analysis, Clarke concluded that Norcraft's fair value as of the Merger was $34.78 per share.[183]

For his DCF analysis, Clarke chose to extend the Base Case projections for an additional five years (through 2024), before applying a perpetuity growth rate ("PGR") of 3.5% at the end of the projection period.[184] He also adjusted the Base Case projections to deduct for income tax expense in each projected year, which the Base Case projections presented in Norcraft's Schedule 14D-9 failed to do.[185]

After determining Norcraft's projected unlevered free cash flows through Norcraft's FY2024, Clarke then discounted each year's projected free cash flow amount to present value using a 9.6% discount rate based on an estimate of Norcraft's weighted average cost of capital ("WACC").[186] With these inputs, Clarke concluded that the present value of Norcraft's projected unlevered free cash flows through FY2024 was $297.3 million.[187]

Clarke then calculated Norcraft's terminal value by (1) dividing Norcraft's terminal year unlevered free cash flow by a capitalization rate of 6.1% and (2) discounting the quotient of that calculation to present value using Norcraft's estimated 9.6% WACC.[188] This yielded a terminal value of $509.5 million.[189] Clarke then added Norcraft's terminal value to the present value of Norcraft's projected unlevered free cash flows through FY2024 to obtain an $806.8 million operating value.[190]

***18** Clarke next made the following adjustments to Norcraft's operating value to derive Norcraft's total equity value: (1) adding Norcraft's excess cash, estimated at $44.3 million; (2) adding the value (to Norcraft) of TRA-related tax benefits, estimated at $4.4 million; (3) adding cash received by Norcraft from the (presumed) exercise of all outstanding options on Norcraft stock, estimated at $18.3 million; and (4) deducting the book value of Norcraft's long-term debt—$147.5 million, per Norcraft's Form 10-Q for Q1 FY2015.[191] After making these adjustments, Clarke concluded that Norcraft's total equity value was $726.3 million.[192] Finally, Clarke divided this aggregate value by Norcraft's "fully diluted" shares outstanding (20,880,123) to obtain an aliquot value of $34.78 per share.[193]

Clarke also performed a comparable company analysis to confirm the results of his DCF analysis.[194] For this analysis, he selected four companies for his peer group: (1) American Woodmark, (2) Masonite International Corp. ("Masonite"), (3) PGT Innovations, Inc. ("PGT") and (4) Ply Gem Holdings, Inc. ("Ply Gem").[195] The analysis yielded a $33.92 per share valuation.[196] Clarke "determined not to weight this analysis in determining a specific per share value [for Norcraft], however, due to the difficulties in finding any companies that were fully comparable to Norcraft."[197]

2. Austin Smith's Opinion Regarding Norcraft's Fair Value

Austin Smith determined that the most reliable indicator of Norcraft's fair value as of the Merger date was the Merger Price, "*less* ... contemporaneously estimated synergies [of $3.60 per share]"[198]—a metric that yields a valuation of $21.60 per share. Austin Smith also conducted an independent valuation using three different valuation methodologies: DCF, comparable company and precedent transaction analyses.[199] Based on those approaches, Austin Smith determined that Norcraft's fair value as of the Merger date "ranged from $17.48 to no more than $23.74."[200]

Austin Smith's primary DCF analysis, like Clarke's, relied on the Base Case projections (adjusted to deduct for income tax expense in each of the projected years) and applied a 3.5% PGR at the end of the projection period.[201] Unlike Clarke, however, Austin Smith did not extend the Base Case projections.[202]

***19** After determining Norcraft's projected unlevered free cash flows through Norcraft's FY2019, Austin Smith discounted each year's projected free cash flow amount to present value using a 11.2% discount rate based on her estimate of Norcraft's WACC.[203] From this, Austin Smith concluded that the present value of Norcraft's projected unlevered free cash flows through FY2019 was $151 million.[204]

Austin Smith then calculated Norcraft's terminal value by (1) dividing Norcraft's terminal year unlevered free cash flow by a capitalization rate of 7.69% and (2) discounting the quotient of that calculation to present value using Norcraft's estimated 11.2% WACC.[205] Austin Smith concluded that Norcraft's terminal value was $435 million.[206] She then added Norcraft's terminal value to the present value of Norcraft's projected unlevered free cash flows through FY2019 to obtain a $586 million operating value.[207]

Austin Smith made two adjustments to Norcraft's operating value to determine Norcraft's total equity value: (1) adding Norcraft's excess cash, estimated at $52.7 million[208]; and (2) deducting the book value of Norcraft's long-term debt—$147.5 million, per Norcraft's Form 10-Q for Q1 FY2015.[209] Having made these adjustments, Austin Smith concluded that Norcraft's total equity value was $491 million.[210] She then divided this total equity value by Norcraft's "fully diluted" shares outstanding (20,880,123) to obtain an aliquot value of $23.54 per share.[211] Finally, upon "summing th[is]... component[ ] of [Norcraft's] value" with the value of the TRA-related tax benefits that Norcraft would realize in each projected year (estimated at $0.20 per share), Austin Smith determined that "the per share value of Norcraft was $23.74" as of the Merger date.[212]

***20** As noted, Austin Smith also undertook to value Norcraft using two "market-based" valuation methodologies. Her comparable company analysis yielded a valuation of $23.46 per share and her precedent transaction analysis yielded a valuation of $17.48 per share.[213]

According to Austin Smith, "[t]he high level of consistency between [her] three separately determined estimates of fair value and the [Merger Price] (less synergies) provides strong analytical support that $21.90 accurately represents the per share fair value of Norcraft."[214] In addition, Austin Smith submits, "the fact that the [Merger Price] derived from a robust deal process" lends "additional support" to her fair value determination.[215]

3. Subramanian's Opinion Regarding Norcraft's Deal Process

Professor Subramanian served as Petitioner's deal process expert.[216] According to Subramanian, Norcraft's deal process was flawed in several respects that rendered the process "unlikely to have yielded fair value for the Norcraft shareholders."[217] The principal flaws Subramanian identifies are (1) the lack of any "competitive process to acquire Norcraft prior to the signing of the Merger Agreement"[218]; (2) information asymmetries between Fortune and potential third-party bidders[219]; and (3) the presence of certain deal protection mechanisms that curbed the efficacy of the go-shop and effectively truncated the Go-Shop Period by at least five days.[220]

a. Absence of Pre-Signing Competition

Subramanian posits that Norcraft's "decision to negotiate exclusively with Fortune" prior to signing the Merger Agreement "eliminated a standard source of bargaining leverage for Norcraft"—namely, "invok[ing] the threat of an alternative deal" to extract a higher price.[221] Consequently, Norcraft was unable to move Fortune above its proposed purchase price of $25.50.[222] Moreover, Subramanian submits, it does not appear "that Norcraft extracted something else [from Fortune] in exchange for exclusivity."[223]

As a practical matter, the absence of pre-signing competition "meant that the Norcraft Board was relying on [the] go-shop process to ensure that Norcraft shareholders received fair value."[224] According to Subramanian, this reliance was misplaced because Norcraft's go-shop process was so poorly structured that it was rendered entirely ineffective as a price discovery tool.[225]

b. Information Asymmetries

Subramanian next posits that certain information asymmetries between Fortune and prospective acquirors vitiated the effectiveness of Norcraft's go-shop process.[226] As noted, Fortune first approached Norcraft regarding a potential acquisition on October 20, 2014, and the parties signed a confidentiality agreement on December 11, 2014.[227] Exclusivity soon followed.[228] This dynamic gave Fortune a substantial head start relative to other potential suitors in evaluating the benefits and challenges of a Norcraft transaction, including the complex issues relating to the TRAs.[229] And, per Subramanian, "[t]his discrepancy ... created a severe information asymmetry problem, because it would be virtually impossible for prospective third-party bidders to [learn] as much about Norcraft as Fortune [already knew]" in the thirty-five days allotted for Norcraft's go-shop process.[230]

***21** Moreover, Subramanian submits, regardless of whether Fortune's "first mover" status provided it with an actual benefit, potential competing bidders would have perceived Fortune to enjoy an informational advantage.[231] That perceived advantage, in turn, discouraged others from bidding for Norcraft to avoid the "winner's curse"—a phenomenon that occurs in common value auction settings where the winning bidder has "buyer's remorse" because it has overpaid for the asset in question.[232] That remorse is a product, in part, of the winner's perception that it lacked an adequate understanding of the asset before it made its bid.[233] Here, Subramanian submits, because potential competing bidders for Norcraft perceived that Fortune knew more about the Company than they could hope to learn in thirty-five days, they may well have feared that they would end up overpaying to acquire Norcraft if they outbid Fortune.[234]

c. Deal Structure Minimizes Efficacy of the Go-Shop

According to Subramanian, the interaction between certain deal protection provisions in the Merger Agreement and the TSAs effectively truncated the Go-Shop Period "from 35 days to 30 days or even shorter."[235] As noted, the Merger Agreement entitled Fortune to launch Tahiti's tender offer for Norcraft's stock fifteen days into the Go-Shop Period.[236] In addition, under the TSAs, Buller, SKM and Trimaran were obligated to tender 53.6% of Norcraft's outstanding voting stock into Tahiti's tender offer "promptly following" the initiation of the offer and, in any event, no later than two days before the offer's initial expiration date.[237] And that tender could not be rescinded absent a "full-blown superior proposal."[238]

Thus, if Fortune launched Tahiti's tender offer halfway through Norcraft's go-shop process (as it did),[239] 53.6% of Norcraft's voting shares would "promptly" be tendered to Tahiti—and that tender would be irrevocable absent a superior proposal. Moreover, even if Norcraft received a superior proposal during the Go-Shop Period, Fortune would still have at least four days to match that proposal.[240]

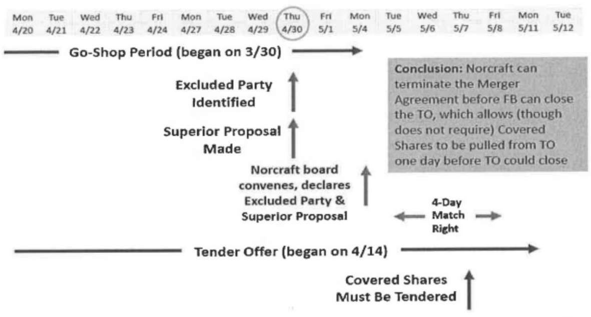
According to Subramanian, the confluence of the deal protections, the limited duration of the Go-Shop Period, Fortune's unlimited match right, the definition of "superior proposal" and Fortune's ability to launch Tahiti's tender offer during the go-shop, resulted in a systematic "tightening and shortening" of the go-shop process. The "tightening" occurred because "a third party would have to make a full-blown superior proposal, not just get to excluded party status, by the end of the 35 days."[241] The full-blown superior proposal was required for Norcraft to terminate the Merger Agreement and prevent Tahiti from accepting the shares tendered pursuant to the TSAs (a majority of the shares outstanding). Subramanian explained:

> Ordinarily, if this was a normal go-shop, you'd have excluded party status by the end of the go-shop period. But... [here] you've got to get to a superior proposal. Got to get the whole shebang done, as Chancellor Strine said it in *Lear*, by the end of the go-shop period. And in my observation and in my experience looking at these go-shops, that is a big deal. Having to get to an

> entire superior proposal by the end of the go-shop period is a very different task than getting to simply excluded party status. [242]

***22** The “shortening” occurred because any potential bidder contemplating whether to participate in the go-shop could wait no longer than April 30—what Subramanian terms the “last clear chance” date—to make its superior proposal if it wanted to ensure that (i) the Norcraft Board had the two business days it was allowed under the Merger Agreement to assess the proposal and declare it superior; (ii) Fortune's four-business-day period to match expired; and (iii) Norcraft terminated the Merger Agreement before Fortune (via Tahiti) could close on the tendered Covered Shares. The following graphic from Subramanian's report illustrates the “tightening and shortening” phenomenon:

“Last Clear Chance” For a Third-Party Was On April 30th


Mon 4/20
Tue 4/21
Wed 4/22
Thu 4/23
Fri 4/24
Mon 4/27
Tue 4/28
Wed 4/29
Thu 4/30
Fri 5/1
Mon 5/4
Tue 5/5
Wed 5/6
Thu 5/7
Fri 5/8
Mon 5/11
Tue 5/12
Go-Shop Period (began on 3/30)
Excluded Party Identified
Superior Proposal Made
Norcraft board convenes, declares Excluded Party & Superior Proposal
4-Day Match Right
Tender Offer (began on 4/14)
Covered Shares Must Be Tendered

Conclusion: Norcraft can terminate the Merger Agreement before FB can close the TO, which allows (though does not require) Covered Shares to be pulled from TO one day before TO could close

JX19 at 45-52 [18]

Subramanian also observes that, even without the “tightening and shortening” of the go-shop, Fortune's unlimited match right stands alone as a disabling feature of this go-shop. [243] According to Subramanian, from the perspective of a potential bidder, unlimited match rights are typically perceived as limiting any “pathway to success.” [244] Indeed, Subramanian submits, “[e]verybody agrees that match rights deter bids. It [is] not even a debated question.” [245]

Here again, Fortune was acutely aware of the advantage it secured, while Norcraft's Board apparently did not understand what an unlimited match right was much less how that deal protection might work to hinder the go-shop. [246] In describing the disparity in the sophistication of the two parties negotiating this Merger, Subramanian observed: “it seems like... the Fortune side was playing chess and the Norcraft side was playing checkers.” [247]

J. Procedural Posture

Petitioners filed a petition with this Court on June 22, 2015, seeking appraisal of their 557,631 shares of Norcraft common stock. [248] The Court held a four-day trial in June 2017, and the parties thereafter submitted post-trial briefing. On December 20, 2017, the Court requested supplemental submissions from the parties to address certain questions following the Delaware Supreme Court's December 14, 2017, decision in *Dell*. [249] The Court heard post-trial argument on April 25, 2018.

II. ANALYSIS

Our appraisal statute, 8 *Del. C.* § 262, provides, “[t]hrough [the appraisal] proceeding, the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors.” [250] “Easy enough,” one might say on a first read, but the judicial appraisal process, through the years, has proven to be anything but “easy.” [251]

***23** “Section 262(h) unambiguously calls upon the Court of Chancery to perform an independent evaluation of ‘fair value’ at the time of a transaction ... [and] vests the Chancellor and Vice Chancellors with significant discretion to consider ‘all relevant factors’ and determine the going concern value of the underlying company.” [252] “By instructing the court to ‘take into account all relevant factors’ in determining fair value, the statute requires the Court of Chancery to give fair consideration to ‘proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court.’ Given that ‘[e]very company is different; [and] every merger is different,’ the appraisal endeavor is ‘by design, a flexible process.’ ” [253]

Taking to heart the mandate of Section 262(h), as reiterated by our Supreme Court, I have carefully considered all relevant factors. And I have assigned those factors the weight (or not) I determined they deserve based on my evaluation of the credible evidence, and my application of “accepted financial principles” as derived from that evidence. [254]

A. The Merger Price is Not a Reliable Indicator of Norcraft's Fair Value

As our Supreme Court has recognized, "corporate finance theory reflects a belief that if an asset—such as the value of a company as reflected in the trading value of its stock—can be subject to close examination and bidding by many humans with an incentive to estimate its future cash flows['] value, the resulting collective judgment as to value is likely to be highly informative[.]" [255] So long as "all estimators hav[e] equal access to information, the likelihood of outguessing the market over time and building a portfolio of stocks beating it is slight." [256] Thus, the Supreme Court has emphasized that our courts must appreciate "the economic reality that the sale value resulting from a robust market check will often be the most reliable evidence of fair value, and that second-guessing the value arrived upon by the collective views of many sophisticated parties with a real stake in the matter is hazardous." [257]

Nevertheless, our Supreme Court has declined on several occasions to pronounce a presumption in favor of deal price in determining fair value. [258] Instead, it has reiterated the "flexible" nature of the trial court's fair value calculus, while also noting its lack of "confidence in [its] ability to craft, on a general basis, the precise pre-conditions that would be necessary to invoke a presumption" in favor of the deal price. [259]

Here, Norcraft's deal process did not include a meaningful market check and, consequently, the Merger Price was not "arrived upon by the collective views of many sophisticated parties with a real stake in the matter." [260] Prior to the execution of the Merger Agreement, the Company chose to negotiate with Fortune and Fortune alone. [261] That decision, if made as a strategic choice, does not alone render Norcraft's deal process unsound. [262] Nor does it preclude a finding that Norcraft's deal process resulted in a reliable indication of fair value (reflected by the Merger Price). Indeed, even Petitioners' expert has acknowledged that negotiating with a single potential buyer pre-signing can, in certain instances, lead to significant value. [263]

***24** But the single bidder focus here, while perhaps not amounting to a breach of fiduciary duty, [264] did not provide a meaningful market check as would yield a reliable indication of fair value. First, there is no evidence that the Board or Citi employed a single bidder approach for the sake of achieving a strategic advantage or maximizing value. Second, and more troubling, the Board's focus on only one bidder was tainted by the fact that Buller (who was conflicted) served as Norcraft's lead negotiator from start to finish.

The shambolic pre-signing process left Norcraft's post-signing go-shop as the only meaningful opportunity to check the market. [265] Unfortunately, Fortune extracted concessions from Norcraft that rendered the go-shop process equally ineffective as a price discovery tool.

1. The Board's Singular Focus on Fortune, Failure to Manage Buller's Conflicts and Misplaced Reliance on the Go-Shop

There is no dispute that neither Norcraft nor Citi contacted other bidders before Norcraft signed the Merger Agreement. This resulted in lost opportunities. Not only did Norcraft miss the opportunity to test the market before committing to Fortune, it also missed the opportunity to leverage the interest of another suitor to extract a higher price from Fortune. Given these missed opportunities, it is not surprising that, by the time the parties settled on the Merger Price, Norcraft's management still believed that the merger consideration was too low. [266] The plan, therefore, was to put all eggs in the go-shop basket as a means to achieve fair value for Norcraft stockholders. [267]

Of course, on the other side of the table, Fortune perceived the Merger Price as very favorable (to Fortune). [268] It was protective of that price and sought to avoid or limit the go-shop to preclude a topping bid. [269] And that is precisely what it did.

***25** Norcraft's Board left the negotiations principally to Buller. Yet Buller was just as (if not more) fixated on extracting commitments from Fortune regarding the TRAs and his future role with the combined company as he was on securing the best price possible for Norcraft. Fortune, for its part, was "stringing Buller along" as it negotiated with him over the Merger Price, leading him to believe he might continue his employment with Fortune post-close. [270] When Fortune finally informed Buller (after settling on the Merger Price) that he would have no place at Fortune post-close, Fortune secured Buller's continued commitment to the Merger by stringing him along again, this time by dangling the possibility that Fortune would be willing to sell Norcraft Canada to Buller after the closing. [271]

The Board either did not appreciate Buller's conflict, or chose not to manage it, until Buller announced that he would pursue the acquisition of Norcraft Canada after closing. [272] By then, Buller had been spurring with Fortune in an attempt to extract every dollar he demanded for the TRAs (diverting consideration from the stockholders) and had pushed hard for post-closing employment with Fortune. Yet all along, the Board did nothing to manage the conflict —it did not form a special committee of its members to negotiate with Fortune or take any other steps to neutralize Buller's influence. Even its half-hearted effort to recuse Buller from further Board deliberations regarding the Merger following his demonstrated interest in Norcraft Canada proved ineffective. [273]

Given that the single-bidder pre-signing process led by a conflicted negotiator yielded what at least some within Norcraft deemed unsatisfactory consideration, it was imperative that the Norcraft Board run an effective post-signing go-shop. It did not.

2. The Post-Sign Go-Shop Provides No Basis to Rely on the Deal Price

Although it is hardly clear that Norcraft's Board appreciated this fact, the ineffective pre-signing process should have made clear that the post-signing go-shop would offer the only real opportunity for a meaningful market check. [274] Unfortunately, that process fell far short on many levels, as the following evidence illustrates:

- Prior to the Go-Shop Period, it was not widely known that Norcraft was "up for sale" [275]; thus, potentially interested parties did not know that Norcraft was "in play" before the Merger was announced, putting them several steps behind Fortune in pursuing an acquisition of Norcraft [276];
- Norcraft's Board appeared to lack even a basic understanding of the terms and function of the go-shop [277];
- Any potential bidder had to value the TRAs—and provide for the satisfaction of Norcraft's payment obligations thereunder—within the Go-Shop Period, a task that Fortune had several months to complete (and struggled to navigate successfully, even with the assistance of expert tax advisors) [278];
- Fortune had an unlimited match right under the Merger Agreement, which gave Fortune four business days to match a superior proposal by a third-party bidder and two business days to match any subsequent proposal by the same bidder [279];
- ***26** In order to proceed with an alternate transaction, Norcraft had to receive a "Superior Proposal" by the end of the Go-Shop Period, "essentially require[ing] the bidder to get the whole shebang done within the [Go-Shop Period]." [280] This requirement was made more onerous by the TRAs' interaction with the Merger Agreement's go-shop provisions, allowing "Fortune [to] close its tender offer for the 54 percent [of Norcraft common stock] before Norcraft [could] terminate the merger agreement, because Norcraft [couldn't] terminate on the possibility of a superior proposal. [Rather, Norcraft could] only terminate after [it had] given Fortune four days to match. And the four days [could] go beyond the tender offer expiration." [281]
- On April 14, 2015, about two weeks into the thirty-five-day Go-Shop Period, Fortune launched Tahiti's tender offer, [282] triggering the TSAs and causing 53.6% of Norcraft's outstanding shares to be committed to supporting the Norcraft-Fortune transaction absent a superior proposal [283]; *and*
- In a fit of bad judgment, RBC attempted to contact and dissuade possible bidders from topping Fortune's bid during the go-shop. [284]

***27** Presented with this factual record, I am not persuaded that Norcraft's go-shop process provided a meaningful market check that resulted in a transaction price derived from the "collective views of many sophisticated parties with a real stake in the matter." [285] Accordingly, I do not accord any weight to the deal price in my fair value calculus. [286]

3. Insufficient Evidence to Consider the Efficient Market Hypothesis

Following our Supreme Court's renewed endorsement of the efficient capital market hypothesis in *Dell*, I requested that the parties submit supplemental post-trial briefing addressing whether Norcraft's unaffected trading price was probative of Norcraft's fair value on the Merger date.[287] Because this case was tried before the Supreme Court's decision in *Dell*, the parties presented limited evidence at trial respecting Norcraft's trading history and the market for its stock. Consequently, the parties had a rather limited record to draw upon when addressing this issue in their supplemental submissions.[288]

To the extent the trial evidence is informative at all on this issue, it does not support assigning any weight to Norcraft's unaffected trading price for purposes of determining Norcraft's fair value on the Merger date. Norcraft had a limited public trading history given that it had just completed an IPO eighteen months before the Merger.[289] What trading did occur following the IPO was relatively limited, an unsurprising phenomenon given the niche market in which Norcraft operated.[290] The analyst coverage of Norcraft's stock was relatively sparse.[291] Based on this record, I am unable to conclude that the market for Norcraft's common stock was efficient or semi-strong efficient.[292] Absent that finding, I do not assign any weight to Norcraft's unaffected trading price as an indicator of Norcraft's fair value on the Merger date.[293]

B. Norcraft's Fair Value under "Traditional Methods" of Valuation

***28** Having determined that neither the Merger Price nor Norcraft's unaffected stock price provide a reliable indicator of the Company's fair value, I must now consider the remaining valuation analyses presented by the parties' experts. In this regard, our law is clear that:

> In discharging its statutory mandate, the Court of Chancery has the discretion to select one of the parties' valuation models as its general framework or to fashion its own. The Court of Chancery's role as an independent appraiser does not necessitate a judicial determination that is completely separate and apart from the valuations performed by the parties' expert witnesses who testify at trial. It must, however, carefully consider whether the evidence supports the valuation conclusions advanced by the parties' respective experts.[294]

I have followed this guidance as I have worked through the experts' competing analyses here.

1. Comparable Companies and Precedent Transaction Analyses Are Not Reliable

As previously mentioned, both experts performed a comparable company analysis. Austin Smith also performed a precedent transaction analysis. "The utility of a comparable company [or precedent transaction] approach is dependent on the similarity between the company the court is valuing and the companies [or precedent transactions] used for comparison."[295] When there are no sufficiently comparable companies or precedent transactions, such analyses are unavailing in the search for fair value.[296]

After carefully reviewing the evidence, I see no factual basis to rely on a precedent transaction or comparable company analysis as an indicator of Norcraft's fair value as of the Merger date. The parties agree that there had not been an acquisition of any publicly-traded, "dealer channel" cabinet manufacturer—or a satisfactorily comparable business[297]— in any temporal proximity to the Merger.[298] Nor were the parties (or their experts) able to identify any truly comparable companies that could support a reliable comparable company analysis.[299] It is, therefore, unsurprising that neither expert relied on market-based approaches (comparable company or precedent transaction analyses) as the principal metric by which to value Norcraft.[300] Instead, they offered these valuations to corroborate the results they reached utilizing their preferred valuation methodologies.[301] Because I disagree that market-based valuation metrics provide any guidance here, I do not consider those metrics further.

2. The DCF Analysis

***29** "[A] DCF analysis can provide the court with a helpful data point about the price a sale process would have produced had there been a robust sale process involving willing buyers with thorough information and the time to make a bid."[302]

> The basic premise underlying the DCF methodology is that the value of a company is equal to the value of its projected future cash flows, discounted to the present value at the opportunity cost of capital. Calculating a DCF involves three steps: (1) one estimates the values of future cash flows for a discrete period, where possible, based on contemporaneous management projections; (2) the value of the entity attributable to cash flows expected after the end of the discrete period must be estimated to produce a so-called terminal value, preferably using a perpetual growth model; and (3) the value of the cash flows for the discrete period and the terminal value must be discounted back using the capital asset pricing model or "CAPM." In simpler terms, the DCF method involves three basic components: (1) cash flow projections; (2) a discount rate; and (3) a terminal value. [303]

a. The Disputed Inputs

As is typically the case, the substantial delta between the experts' DCF valuations can be traced to their disagreements regarding the DCF inputs. Their most significant disagreements are: (1) whether to extend the Base Case projections by an additional five years; and (2) how to calculate Norcraft's beta in connection with estimating Norcraft's WACC. On the latter point, the experts disagree regarding (i) the selection of appropriate guideline public companies ("GPCs") for a proxy beta calculation and whether net debt or gross debt should be used to unlever the GPC betas and relever the resulting proxy beta [304]; and (ii) whether Norcraft's observed capital structure or a target capital structure should be used to relever the concluded beta when calculating Norcraft's cost of equity. [305] The experts generally agree on the remaining DCF inputs.

i. Management Projections

"The most important input necessary for performing a proper DCF is a projection of the subject company's cash flows. Without a reliable estimate of cash flows, a DCF analysis is simply a guess." [306] While Norcraft's management (Buller and Ginter) prepared several sets of projections, the experts agree that the most reliable projections are the Base Case projections—and both experts relied on those projections in their primary DCF analyses. [307]

***30** The record reflects that Norcraft management did not prepare long-term projections in the ordinary course of Norcraft's business. [308] Nevertheless, Buller and Ginter knew how to prepare long-term projections and they approached the Base Case projections with a view to providing the Board with a reliable estimate of Norcraft's future financial performance. [309] When all was said and done, Buller and Ginter were confident they had prepared a set of realistic, reasonable projections upon which Citi and the Board could rely in assessing Norcraft's value during the course of negotiations. [310] While not perfect, I am satisfied that the Base Case projections provide a reliable foundation for a valid DCF. [311]

The experts' dispute regarding the Base Case projections does not turn on their reliability (or lack thereof), but rather on whether the projections should be extended by an additional five years. Clarke opined that the extension was necessary, while Austin Smith opined that a PGR should be applied at the end of the five-year Base Case projection period.

According to Clarke, extending the Base Case projections is necessary to capture Norcraft's future cash flows because "the Base Case [p]rojections had not reached [a] steady state at the end of the [five-year] projection period" and, therefore, "it would be inappropriate to apply a standard [PGR] at th[e] last year [of that period]." [312] To account for Norcraft's growth potential as of 2019, Clarke extended the Base Case projections by an additional five years—through 2024—"to gradually reduce growth rates over time until reaching [a 3.5%] PGR." [313]

***31** Austin Smith, on the other hand, maintains that extending the Base Case projections is inappropriate because doing so forecasts growth that Norcraft almost certainly could not achieve. In this regard, she points out that the cabinetry industry is cyclical, as demonstrated by trends in (1) the industry's historical performance (growth and decline); and (2) the historical growth (and decline) of the residential construction market.[314] Extending the Base Case projections by an additional five years implies a ten-year period of consistent growth following two years of already achieved growth. According to Austin Smith, projecting twelve years of steady growth for a business in the cabinetry industry is patently unreasonable.[315]

On this point, I find Austin Smith most credible. The evidence adduced at trial supports her view that the cabinetry industry is cyclical and follows the cycle of the residential construction market.[316] The evidentiary record also reflects that the residential construction market is projected to reach a "steady state" at or slightly before the last year of the Base Case projection period (2019).[317] Moreover, insofar as Norcraft's own management was not inclined to project Norcraft's financial results beyond FY2019, I see no basis to do so *post hoc* for the sake of reaching a litigation result.

ii. Norcraft's Estimated WACC

***32** The parties also dispute how to calculate the applicable discount rate based on Norcraft's estimated WACC. More specifically, they dispute how to calculate Norcraft's beta in connection with estimating Norcraft's cost of equity capital (a key component of WACC).

The application of a discount rate to financial projections attempts to "convert the [subject company's] expected economic income stream to present value."[318] Where the discount rate is based on the subject company's WACC, the projected future cash flows and terminal value are discounted by the WACC to bring them back to present value.[319] A company's WACC represents the cost (to the company) of financing its business operations; it comprises the weighted average of the company's cost of debt and equity[320]:

$$\text{WACC} = \left(r_{equity} \times \frac{E}{V}\right) + \left(r_{debt} \times \frac{D}{V} \times (1 - t)\right)$$

where:

r_{equity}	=	cost of equity capital
E	=	market value of the company's equity
r_{debt}	=	cost of debt capital
D	=	value of the company's debt
$V = E + D$	=	total value of the company's equity and debt
t	=	applicable tax rate

Here, both experts calculated Norcraft's cost of equity capital pursuant to CAPM.[321] Following CAPM, a company's cost of equity is calculated as follows[322]:

$$r_{equity} = r_{no\text{-}risk} + (\beta \times ERP) + SS$$

where:

$r_{no\text{-}risk}$	=	risk-free rate of return
β	=	beta coefficient of the subject company
ERP	=	equity risk premium
SS	=	size premium

The experts generally agree on many of the relevant inputs to calculate Norcraft's WACC; both experts used the same risk-free rate of return (2.75%), equity risk premium (6.21%) and size premium (2.69%).[323] The experts differed, however, in their respective estimates of Norcraft's pre-tax cost of debt. Clarke estimated Norcraft's pre-tax cost of debt as 6.95%—based on "the average of the 15-year yield-to-maturity of B and BB rated bonds" as of the Merger date.[324] Austin Smith, by contrast, estimated Norcraft's pre-tax cost of debt as 5.85%—based on the "[a]verage of (a) BofA Merrill Lynch US High Yield B Effective Yield as of 5/12/15 [the Merger date] and (b) total return on Norcraft['s] [then-outstanding] term loan (including [the] effect of issuance discount)."[325]

The experts' respective estimates of Norcraft's pre-tax cost of debt are both reasonable. As of the Merger date, Norcraft's long-term debt was rated "B2" by Moody's Global Credit Research and "B+" by Standard & Poor's, and the yield to maturity on high-yield U.S. corporate bonds with 10+ year maturity on that date was approximately 6.34%.[326] Accordingly, I use the average of the experts' respective estimates of Norcraft's pre-tax cost of debt (6.40%) for my DCF analysis.[327]

***33** As to the estimation of Norcraft's cost of equity, the experts' principal point of disagreement concerns Norcraft's beta coefficient. "Beta is a measure of the systematic risk of a stock; the tendency of a stock's price to correlate with changes in the market.... [B]etas for equity capital are used as a modifier to the equity risk premium [ ] in the context of [calculating a company's cost of equity]." [328]

A company's beta is measured by tracking relative change in the trading price of its stock over a discrete time period (the "lookback period"), with a set frequency (*e.g.*, daily, weekly, monthly). [329] When there is insufficient data on the trading history of a company's stock, the company's "beta must be an estimate based on the [observed] betas of comparable, publicly traded companies" (*i.e.*, a "proxy beta"). [330] Observed betas are *levered* betas; they reflect a company's operating risk *and* its financial risk. [331] Thus, when calculating a proxy beta, one must "unlever" each GPC's observed (levered) beta to remove the debt-related risk(s) of that particular GPC. [332] Once the GPC betas are unlevered, and the mean or median of those betas is calculated, the unlevered summary measure beta (*i.e.*, the unlevered proxy beta) must be relevered to add back financial risk. [333] The relevant financial risk, however, is the subject company's not the GPCs'. [334]

The experts generally agree that there is insufficient information regarding Norcraft's own beta to allow a reliable beta calculation based solely on that information—a function of Norcraft's limited trading history. [335] Accordingly, they agree that the use of a proxy beta is appropriate. They disagree, however, as to (1) which GPCs should be used to derive the proxy beta; (2) whether gross debt or net debt should be used to unlever the GPC betas and relever the resulting unlevered proxy beta; and (3) whether Norcraft's observed capital structure or a target capital structure should be used to relever the proxy beta.

I begin with the first point of disagreement—appropriate GPCs. Clarke used four GPCs for his proxy beta calculation —American Woodmark, Masonite, PGT and Ply Gem [336] — which he selected by applying a set of comparability-related screening criteria. [337] After selecting these four GPCs, Clarke then calculated each GPC's beta over a two-year lookback period (measured weekly) and a one-year lookback period (measured daily)—both periods relative to the Merger date—and unlevered each observed GPC beta using the gross debt of the corresponding GPC. [338] This led Clarke to derive an (unlevered) proxy beta for Norcraft of 0.80 based on the mean and median of the unlevered GPC betas. [339]

***34** Austin Smith, by contrast, identified sixteen GPCs for her proxy beta calculation; the four companies selected by Clarke and twelve additional companies, including Fortune and Masco. [340] Having selected these sixteen GPCs, Austin Smith derived a proxy beta for Norcraft based on the median of the unlevered GPC betas, measured weekly over a two-year lookback period—relative to the Merger date—and unlevered using each GPC's net debt. [341] This resulted in an unlevered proxy beta for Norcraft of 1.02. [342]

Each expert disputes the suitability of the other's selected GPCs. According to Clarke, Austin Smith's selected GPCs "were either not comparable [to Norcraft] and/or were going through significant restructuring events that impacted their historical betas." [343] Austin Smith, for her part, maintains that Clarke's methodology for selecting GPCs is "fundamental[ly]" flawed, principally because: (i) it "results in the exclusion of two of the three publicly-traded cabinet manufacturers: Fortune ... and Masco"; and (ii) it yields a relatively small set of companies, all but one of which manufacture products other than cabinets—meaning they are less comparable to Norcraft than Fortune and Masco. [344]

Both experts present valid arguments. After considering the evidentiary record, I have determined to derive a proxy beta for Norcraft based on the weekly observed betas of Fortune, Masco, American Woodmark, Masonite, PGT and Ply Gem, measured over a two-year lookback period (relative to the Merger date). I acknowledge the size difference between Norcraft, on one hand, and Fortune and Masco, on the other, but there are few publicly-traded, "dealer channel" cabinet manufacturing businesses operating in the United States from which to draw. [345] To account for this dynamic, I have selected a set of GPCs that includes publicly-traded companies directly competing with Norcraft (Fortune, Masco and American Woodmark), and also public companies operating in the same general industry that are more comparable in size to Norcraft (Masonite, PGT and Ply Gem). [346] Since neither party has provided me with a principled way to assign different weights to the betas of individual GPCs, I have determined to derive the proxy beta by taking the median of the unlevered GPC betas. [347]

***35** As to the question whether to use gross or net debt for unlevering and relevering purposes, I have determined that Clarke's approach (gross debt) is most appropriate. I consulted the finance literature cited by both experts with regard to this issue and have come to the conclusion that using gross debt is the more generally accepted approach when applying the *Hamada* unlevering and relevering formulas (as both experts did),[348] which utilize "total debt" as an input.[349] I also find that considering net debt, while it might eliminate some of the drawbacks of the *Hamada* approach if done properly,[350] complicates the analysis and adds a significant risk of error to an already abstract process.

In her deposition, Austin Smith explained that using net debt requires "a judgment call" because "public companies don't report excess cash."[351] In essence, to derive net debt, one "look[s] at how the cash balances for th[e chosen] companies changed over time, and [then] look[s] at the relationship between cash and debt, and come[s] to an assessment."[352] If insufficient data about excess cash is available, "total cash is assumed to equal excess cash."[353] Considering the many variables already at play in a DCF analysis (especially when deriving a proxy beta), I find that figures based on a "judgment call" are unreliable in the absence of a principled way to evaluate the soundness of the underlying "judgment." For all these reasons, I have utilized gross debt rather than net debt for unlevering and relevering purposes.

That takes me to the final beta-related dispute: the appropriate capital structure to relever the unlevered proxy beta. Austin Smith submits that a target capital structure based on the capital structure of comparable companies provides the most reliable input, while Clarke advocates the use of Norcraft's actual (observed) capital structure as of the Merger date. Austin Smith explains her choice by noting that Norcraft only went public in 2013 and its management had not indicated as of the Merger that it intended to maintain the Company's then-existing capital structure.[354] According to Austin Smith, it is likely that, over time, Norcraft's capital structure would come to resemble that of its peers.[355] Clarke counters that Norcraft's observed capital structure as of the Merger date was the "operative reality" of the Company at that time and, as such, is the appropriate capital structure to apply when relevering the unlevered proxy beta.[356]

Clarke has the better of this debate. While there are instances where using a target capital structure for relevering purposes would be appropriate,[357] especially where the target's capital structure is in flux, that is not the case here. It is true that, as of the Merger, Norcraft had operated for only eighteen months after its IPO. There is no evidence, however, that management intended to change Norcraft's capital structure, and any suggestion that it would do so is nothing more than sheer speculation.[358] Accordingly, I refer to Norcraft's observed capital structure as of the Merger (75% equity, 25% debt) to relever Norcraft's concluded unlevered beta.[359]

b. The Court's DCF Valuation of Norcraft

***36** Like Clarke and Austin Smith, I begin my DCF analysis with the Base Case projections, adjusted to deduct for income tax expense in each of the projected years (based on a 38% tax rate). This adjustment yields the following figures for Norcraft's net operating profit after taxes ("NOPAT")[360]:

FY2015-E (Stub)	FY2016-E	FY2017-E	FY2018-E	FY2019-E
$18.3 million	$31.8 million	$36.0 million	$41.9 million	$50.3 million

I next adjust the NOPAT figures to obtain unlevered free cash flow figures for each projected year by (1) adding back non-cash charges—depreciation, amortization and stock compensation expense; (2) deducting Norcraft's capital expenditures; and (3) deducting year-over-year change in Norcraft's net working capital ("NWC"). My adjustments with respect to each item track those made by both experts.[361]

The foregoing adjustments yield the following figures for unlevered free cash flow in each of the projected years:

FY2015-E (Stub)	FY2016-E	FY2017-E	FY2018-E	FY2019-E
$20.8 million	$36.73 million	$40.06 million	$44.36 million	$49.84 million

***37** To calculate the present value of these unlevered cash flows, like Clarke and Austin Smith, I have applied a discount rate based on Norcraft's estimated WACC. My WACC calculation also uses CAPM to estimate Norcraft's cost of equity—based on the parties' common risk-free rate of return (2.75%), equity risk premium (6.21%) and size premium (2.69%)—and uses a 6.40% pre-tax cost of debt, which yields a post-tax cost of debt for Norcraft of 3.97% (again based on a 38% tax rate).

To derive a beta for my cost of equity calculation, I have unlevered the observed weekly betas of my selected GPCs over a two-year lookback period relative to the Merger date, using the *Hamada* unlevering formula and gross debt rather than net debt. That computation yielded the following unlevered betas:

Guideline Public Company	Levered Beta	Unlevered Beta
American Woodmark	1.09	1.02
Masco	1.26	0.99
Fortune	1.15	1.07
Masonite	0.55	0.47
PGT	0.88	0.78
Ply Gem	1.60	0.98

The median of the unlevered GPC betas, 0.98, constitutes Norcraft's concluded unlevered beta. I then relevered that beta using Norcraft's observed capital structure of 75% equity and 25% debt (per Clarke's estimation), resulting in a levered beta for Norcraft of 1.187. Incorporating this levered beta into my WACC calculation, along with the other inputs already mentioned—again using Norcraft's observed capital structure —I derived a WACC for Norcraft of 10.60%. Applying Norcraft's concluded WACC to discount its projected future cash flows to present value, I have calculated the present value of those cash flows to be $149.7 million.

To calcul ate Norcraft's terminal value, I have used the Perpetuity Growth method (as did both experts),[362] which posits that terminal value equals the quotient of (1) the subject company's terminal year free cash flow (here, $51.41 million); and (2) the applicable capitalization rate (here, 7.10%)[363]—discounted to present value using the applicable discount rate (here, Norcraft's WACC of 10.60%).[364] This yields a terminal value of $477.2 million.

***38** Summing together the present value of Norcraft's projected unlevered cash flows ($149.7 million) and its terminal value ($477.2 million) results in an operating value for Norcraft of $626.9 million. To calculate Norcraft's total equity value, I then made the following adjustments to Norcraft's concluded operating value:

- adding Norcraft's excess cash as of the Merger date, calculated as $62.6 million[365];
- adding the value of the TRA-related tax benefits realized by Norcraft in each of the projected years, calculated as $4.3 million[366]; *and*
- deducting Norcraft's long-term debt as of the Merger date, calculated as $147.5 million.[367]

These adjustments to Norcraft's operating value yield a total equity value for Norcraft of $546.3 million. Dividing Norcraft's total equity value by Norcraft's fully diluted shares outstanding as of the Merger date (20,880,123),[368] I conclude that Norcraft's equity value per share on that date was $26.16.

3. The Merger Price as a "Reality Check"

***39** As explained above, I have determined that the Merger Price is not a reliable indicator of Norcraft's fair value as of the Merger date. That does not mean, however, that the Merger Price is *irrelevant* for purposes of the Court's fair value determination. To the contrary, it is appropriate to consider the Merger Price as a "reality check" on the Court's DCF valuation of Norcraft.[369] Insofar as I am obliged to articulate a principled, evidence-based explanation for the delta between the Merger Price and the Court's DCF valuation (here, $0.66 per share), I am satisfied that the process infirmities I have identified resulted in the Board leaving $0.66 per share on the bargaining table.[370] With that said, I am also satisfied that the delta between the Merger Price and the DCF value is not so great as to cause me to question whether the DCF value is grounded in reality.[371]

III. CONCLUSION

For the foregoing reasons, I have found the fair value of Norcraft shares as of the Merger date (May 12, 2015) was $26.16 per share. The statutory rate of interest, compounded quarterly, shall accrue from the date of closing to the date of payment. The parties should confer and submit an implementing final judgment within ten (10) days.

All Citations

Not Reported in Atl. Rptr., 2018 WL 3602940

Footnotes

[1] *8 Del. C.* § 262(h).

[2] *Merion Capital L.P. v. Lender Processing Servs., Inc.*, 2016 WL 7324170, at *16 (Del. Ch. Dec. 16, 2016).

[3] *DFC Global Corp. v. Muirfield Value P'rs, L.P.*, 172 A.3d 346, 388 (Del. 2017).

[4] *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd*, 177 A.3d 1, 22 (Del. 2017); *DFC*, 172 A.3d at 388 ("What is necessary in any particular [appraisal] case though is for the Court of Chancery to explain its [fair value calculus] in a manner that is grounded in the record before it.").

[5] *See**Dell*, 177 A.3d at 35; *DFC*, 172 A.3d at 349, 351, 372; *cf.**DFC*, 172 A.3d at 369 n.118 (explaining that a discounted cash flow analysis is "often used in appraisal proceedings when the respondent company was not public or was not sold in an open market check").

[6] *DFC, 111* A.3d at 348 (rejecting the petitioner's (and others') argument that the Court should adopt a presumption in favor of the deal price, stating "[w]e decline to engage in that act of creation, which in our view has no basis in the statutory text"); *Dell*, 177 A.3d at 21-22 (noting "we doubt[ ] our ability to craft the precise preconditions for invoking such a presumption").

[7] *Dell*, 177 A.3d at 24.

[8] *See**Highfield Capital, Ltd. v. AXA Fin., Inc.* 939 A.2d 34, 47 (Del. Ch. 2007) (describing DCF as a "traditional valuation methodology").

[9] *Dell*, 177 A.3d at 21 (quoting *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214, 218 (Del. 2010) (emphasis in original)); *see also**Gholl v. eMachines, Inc.*, 2004 WL 2847865, at *5 (Del. Ch. Nov. 24, 2004) (noting that both parties bear a burden of proof in a statutory appraisal trial and holding that, "[i]f neither party satisfies its burden ... the court must then use its own independent business judgment to determine fair value").

[10] JX 267 ("Norcraft FY2014 10-K") at 1, 6; JX 221 ("Merger Agreement"), pmbl. & § 1.3.

[11] JX 267 (Norcraft FY2014 10-K) at 1.

[12] Joint Pre-Trial Stipulation and Order ("PTO") ¶¶ 2y, 2ff. I commend the parties, and counsel in particular, for the substantial effort that was undertaken to prepare and submit comprehensive pre-trial factual stipulations.

[13] JX 221 (Merger Agreement), pmbl. & § 1.3; *see* PTO ¶ 2y.

[14] PTO ¶¶ 2h, 2i. Blueblade acquired all of its Norcraft stock after the Merger was announced. PTO ¶¶ 2h, 2i.

[15] PTO ¶ 2g; JX 270 ("Fortune FY2015 10-K") at 6.

[16] JX 270 (Fortune FY2015 10-K) at 5.

[17] *See* PTO ¶ 2f.

[18] PTO ¶ 2f; JX 3 (Buller Dep.) at 19:9-21. Buller was also the Chairman of Norcraft's Board at all relevant times prior to the Merger. JX 3 (Buller Dep.) at 19:9-21.

[19] PTO ¶ 2f; JX 1 (Ginter Dep.) at 18-19.

[20] PTO ¶ 2f; JX 2 (Tanquist Dep.) at 21:2—16.

[21] PTO ¶ 2g.

[22] Id.

[23] *Id.*

[24] PTO ¶ 2a.

[25] PTO ¶¶ 2b, 2c; JX 267 (Norcraft FY2014 10-K) at 6-10. For FY2014, “kitchen and bathroom cabinet dealers accounted for [86%] of Norcraft's net sales, home builders accounted for [9%], and wholesale retailers, or home centers, accounted for [5%].” PTO ¶ 2b. “[A]pproximately 58% of [Norcraft's FY2014] net sales were to the home repair and remodeling market and the remaining net sales were to the new residential construction market.” JX 267 (Norcraft FY2014 10-K) at 6. As of the Merger date, Norcraft, Fortune and Masco Corporation (“Masco”) were the only three “dealer channel” cabinet manufacturers in the United States with a market share of over 5%. *See* JX 112 (Gabelli & Co., *The Home Improvement Opportunity*, published Jan. 29, 2015 [“Gabelli Report”]) at CITI-00053582. In the cabinetry industry, the “dealer channel” comprises third parties who purchase cabinets from manufacturers (or wholesalers) and sell them to end users. *See id.*; JX 12 (Baab Dep.) at 36:8-20. In 2014, nearly half of U.S. cabinet sales (representing approximately $6 billion) were made through the dealer channel, which is generally considered the most profitable sales channel in the cabinetry industry. *See* JX 112 (Gabelli Report) at CITI-00053582, CITI-00053595; JX 1 (Ginter Dep.) at 153:17-154:1; JX 5 (Klein Dep.) at 293:25-294:3.

[26] JX 267 (Norcraft FY2014 10-K) at 11.

[27] *Id.*

[28] JX 3 (Buller Dep.) at 16:3-24. As of 2003, Norcraft Companies, L.L.C. was the operating entity in Norcraft's organizational structure. JX 400 (Norcraft Amendment No. 5 to Form S-1, filed Oct. 30, 2013 [“Norcraft Amendment 5 to Form S-1”]) at 19. For purposes of this Memorandum Opinion, I have not distinguished SKM and Trimaran from the SKM and Trimaran funds that owned Norcraft common stock prior to the Merger.

[29] JX 27 (Mar. 29, 2004 Norcraft LP Press Release) at 2. Following the 2003 Acquisition, Norcraft LP became the operating entity in Norcraft's organizational structure. JX 400 (Norcraft Amendment 5 to Form S-1) at 19. Buller and his family collectively owned approximately 11% of Norcraft LP's equity. JX 3 (Buller Dep.) at 18:6-8.

[30] TT 21:6-11, 21:20-21 (Eldridge), 96:22-97:7 (Biggart), 607:23-608:1 (Clarke).

[31] JX 267 (Norcraft FY2014 10-K).

[32] *Id.*; *see also* TT 607:23-608:1 (Clarke); JX 14 (Clarke Dep.) at 60 (“I do believe that the home building industry is cyclical and at some point the housing starts would decrease.”).

[33] JX 23 (Austin Smith Rebuttal Report) at 6.

[34] JX 267 (Norcraft FY2014 10-K).

[35] JX 20 (Austin Smith Report) at 7.

[36] JX 400 (Norcraft Amendment 5 to Form S-1) at 19.

[37] JX 20 (Austin Smith Report) at 7.

[38] *Id.*

[39] *Id.* I note that between 2006 and 2013, Norcraft LP's management struggled accurately to project the company's future performance. JX 3 (Buller Dep.) at 183-84.

[40] JX 267 (Norcraft FY2014 10-K) at 12; PTO ¶ 2j.

[41] JX 267 (Norcraft FY2014 10-K) at 12, 15, 65; PTO ¶ 2d.

[42] Norcraft LLC is not to be confused with Norcraft Companies, L.L.C. As noted, Norcraft Companies, L.L.C. was converted into Norcraft LP in connection with the 2003 Acquisition, and it continues to exist as such in the Norcraft enterprise structure. JX 400 (Norcraft Amendment 5 to Form S-1) at 19; JX 267 (Norcraft FY2014 10-K) at 12; PTO ¶ 2d.

[43] JX 267 (Norcraft FY2014 10-K) at 12.

[44] *Id.* PTO ¶ 2d. Buller et al.'s LLC units were convertible “at the option of the [unitholders]” into restricted shares of Norcraft common stock “on a one-for-one basis” or into cash (pursuant to a stated conversion formula),

with the form of consideration to be determined at Norcraft's option. JX 267 (Norcraft FY2014 10-K) at 72; *see also* JX 35 (Norcraft Form 424B4, filed Nov. 6, 2013 ["Norcraft IPO Prospectus"]) at 101-02.

[45] JX 35 (Norcraft IPO Prospectus) at 1; PTO ¶ 2d.

[46] JX 35 (Norcraft IPO Prospectus) at 102-03; JX 267 (Norcraft FY2014 10-K) at 73; PTO ¶ 2d.

[47] JX 36 (LLC Unitholder TRA), pmbl.; JX 267 (Norcraft FY2014 10-K) at 79.

[48] JX 36 (LLC Unitholder TRA) §§ 1.1, 3.1 (defining "Realized Tax Benefit" and "Cumulative Net Realized Tax Benefit").

[49] *Id.* §§ 4.1–4.3. The TRAs defined "Change of Control" to include "the acquisition, directly or indirectly, by any [unaffiliated third-party acquiror]... of beneficial ownership ... of more than 50.1% of the aggregate voting power" of Norcraft's outstanding voting stock. *Id.* § 1.1.

[50] PTO ¶ 2k.

[51] PTO ¶ 21.

[52] JX 238 (Norcraft Schedule 14D-9, filed Apr. 14, 2015 ["Norcraft Schedule 14D-9"]) at 10.

[53] Transcript of Trial ("TT") at 205:1-10 (Biggart) ("Q. You suspect that Mr. Buller first raised the desire to be employed by Fortune following any merger during a meeting on October 23, 2014. Correct? A. I believe that's when he expressed an interest to [Klein].").

[54] JX 13 (Biggart Dep.) at 86:16-87:18 ("Q. Were there any internal discussions within Fortune about hiring [Buller] post-merger? A. Yes, I talked to [Klein] directly a number of times about it. Q. What did he say? A. [Klein] said I don't know that there is a place for him ....").

[55] PTO ¶ 21; JX 69 (Fortune's Oct. 23, 2014 Proposal) at FB0049476. Fortune viewed the TRA payments as part of the Merger consideration. *See* JX 13 (Biggart Dep.) at 34:10-21, 166:10-167:8. Thus, for every dollar spent to satisfy the TRA Beneficiaries, that dollar would not be included in the consideration paid to Norcraft's public stockholders. *See* JX 249 (Funds Flow Memorandum), Ex. E.

[56] JX 238 (Norcraft Schedule 14D-9) at 10.

[57] PTO ¶ 2m; JX 238 (Norcraft Schedule 14D-9) at 10.

[58] PTO ¶ 2m; JX 238 (Norcraft Schedule 14D-9) at 10.

[59] TT 12:1-3 (Eldridge). Nathan Eldridge was Citi's lead banker in connection with the Norcraft engagement. *Id.* at 12:1-15.

[60] PTO ¶ 2m; JX 238 (Norcraft Schedule 14D-9) at 10.

[61] JX 71(Norcraft Board Minutes, Nov. 8, 2014) at NCFT0165019.

[62] *Id.* at NCFT0165020.

[63] JX 1 (Ginter Dep.) at 35-36; *see* JX 3 (Buller Dep.) at 112-16.

[64] JX 1 (Ginter Dep.) at 27-28; JX 3 (Buller Dep.) at 28:21-29:3, 102.

[65] JX 1 (Ginter Dep.) at 27:8-12.

[66] JX 1 (Ginter Dep.) at 22:4-24, 25:3-25; *see* JX 150 (Feb. 27, 2015 e-mail from Tanquist to RBC, attaching Norcraft's FY2015 budget) at NCFT0138021-24.

[67] JX 2 (Tanquist Dep.) at 25-27; JX 3 (Buller Dep.) at 24:8-26:1.

[68] JX 1 (Ginter Dep.) at 22:9-12; JX 2 (Tanquist Dep.) at 25:12-24.

[69] JX 2 (Tanquist Dep.) at 25:25-26:5.

[70] *Id.* at 26:5-7.

[71] JX 1 (Ginter Dep.) at 22:11-14; JX 3 (Buller Dep.) at 24:8-25:1.

[72] JX 1 (Ginter Dep.) at 22:15-18; JX 2 (Tanquist Dep.) at 26:8-10; JX 3 (Buller Dep.) at 24:12-18.

[73] JX 2 (Tanquist Dep.) at 26:8-10; JX 3 (Buller Dep.) at 24:15-18.

[74] JX 1 (Ginter Dep.) at 74-80; JX 99 (Jan. 9, 2015 e-mail from Reilly to other Norcraft Board members, attaching Norcraft management presentation ["Norcraft Jan. 2015 Management Presentation"]) at NCFT0146344–17. The record also contains a set of three-year projections for Norcraft, apparently created by Ginter prior to October 2014 (the "Ginter 2014 Projections"). Ginter, however, did not recall creating these projections or the purpose for which they were prepared. *See* JX 1 (Ginter Dep.) at 35:23-36:4, 53:22-54:18.

[75] JX 99 ("Norcraft Jan. 2015 Management Presentation") at NCFT0146344—47.

76 *Id.* The Base Case and Upside Case projections also included free cash flow forecasts. *Id.* at NCFT0146347. Those free cash flow forecasts, however, did not deduct for income taxes and, therefore, significantly overstated Norcraft's future free cash flows. JX 1 (Ginter Dep.) at 44-45. Accordingly, the tables depicted here do not include the free cash flow component of the Base Case and Upside Case projections.

77 JX 1 (Ginter Dep.) at 22-23, 75-76, 87-88; JX 3 (Buller Dep.) at 34-36.

78 JX 1 (Ginter Dep.) at 75-76.

79 *Id.*

80 *Id.* at 75:23-76:8.

81 *Id.* at 97:12-13; JX 3 (Buller Dep.) at 115:8-18 ("The [B]ase [C]ase is something that we felt very, very comfortable in doing, and then [in the Upside Case] we showed the upside that if everything, everything went our way, there was a possibility that we could hit the [U]pside [Case].").

82 JX 71 (Norcraft Board Minutes, Nov. 25, 2014) at NCFT0165023.

83 *Id.*; PTO ¶ 2***o***.

84 JX 71 (Norcraft Board Minutes, Dec. 3, 2014) at NCFT0165024.

85 *Id.* at NCFT0165025; JX 95 (Dec. 2, 2014 email from Reilly to other Norcraft Board members attaching Citi presentation deck).

86 JX 95 (Dec. 2, 2014 email from Reilly to other Norcraft Board members attaching Citi presentation deck).

87 JX 71 (Norcraft Board Minutes, Dec. 3, 2014) at NCFT0165025.

88 *Id.*

89 JX 238 (Norcraft Schedule 14D-9) at 11.

90 *Id.*

91 PTO ¶ 2p; JX 97 (Confidentiality Agreement).

92 PTO ¶ 2q.

93 *Id.*

94 *Id.*

95 JX 238 (Norcraft Schedule 14D-9) at 12.

96 JX 13 (Biggart Dep.) at 88:2-3.

97 PTO ¶ 2r.

98 *Id.*; JX 238 (Norcraft Schedule 14D-9) at 12. All parties agreed that Fortune's acquisition, directly or indirectly, of 100% of Norcraft's equity would constitute a "Change of Control" within the meaning of the TRAs. JX 36 (LLC Unitholder TRA) § 1.1 (defining "Change of Control"); *see* PTO ¶ 2z.

99 PTO ¶ 2r.

100 PTO ¶ 2s.

101 *Id.*

102 JX 238 (Norcraft Schedule 14D-9) at 12.

103 *See* JX 238 (Norcraft Schedule 14D-9) at 12; JX 71 (Norcraft Board Minutes, Feb. 2, 2015) at NCFT0165026-27.

104 JX 238 (Norcraft Schedule 14D-9) at 12; *see* JX 71 (Norcraft Board Minutes, Feb. 2, 2015) at NCFT0165026-27; PTO ¶ 2t. Citi's valuation employed several methodologies, including a DCF and comparable company analysis, and yielded values of $16.75 to $27 per share (based on the Base Case projections). JX 115 (Feb. 2, 2015 email from Citi, attaching Board Discussion Materials) at CITI-00063489.

105 JX 71 (Norcraft Board Minutes, Feb. 2, 2015) at NCFT0165027.

106 *Id.*

107 JX 238 (Norcraft Schedule 14D-9) at 12.

108 *Id.*

109 *Id.*

110 *Id.*

111 *Id.*; PTO ¶ 2u.

112 JX 238 (Norcraft Schedule 14D-9) at 12.

113 JX 412 (Feb. 10, 2015 email from Klein to Buller, attaching Fortune's re-revised proposal) at 2.

114 JX 1 (Ginter Dep.) at 231:21-24 (“Q: [Y]ou testified that you thought that Norcraft was undervalued in the transaction [with Fortune], right? A: Yes.”); JX 140 (Feb. 20, 2015 email from Reilly to Buller, Maselli and Citi representatives in which Reilly opines that “[Norcraft was] leaving $ on the table” by moving forward with Fortune's $25.50 per share proposal).

115 JX 412 (Feb. 10, 2015 email from Fortune to Buller attaching letter rejecting counterproposal).

116 JX 413 (email chain Klein to RBC and Fortune deal team describing counterproposal, Feb. 13, 2015) at FB0089263.

117 TT 100:4-17 (Biggart); JX 238 (Norcraft Schedule 14D-9) at 13.

118 JX 185 (Mar. 20, 2015 email from Klein to Fortune director Mackay) (“You are spot on - its [sic] a good price, and there is a risk someone comes along and tries to top the offer.”). Indeed, prior to signing the Merger Agreement, Fortune had RBC render a fairness opinion. In that regard, RBC conducted a standalone DCF analysis of Norcraft that valued Norcraft at $30.26 per share. JX 216 (Mar. 29, 2015 RBC presentation slides) at FB0047801. Fortune's management valued Norcraft even higher. Its discounted cash flow and internal rate of return (“IRR”) analysis (the “DCF/IRR Analysis”) of Norcraft as a standalone entity valued Norcraft at approximately double the Merger Price and estimated a 16% annualized IRR before accounting for synergies. JX 191 (slides from Mar. 29, 2015 Fortune board meeting regarding Norcraft acquisition) at FB0076961; JX 301 (Apr. 28, 2015 email between Fortune deal team members, attaching Fortune valuation of Norcraft dated Mar. 19, 2015).

119 JX 238 (Norcraft Schedule 14D-9) at 14; *see* TT 13-15 (Eldridge); JX 3 (Buller Dep.) at 86:13-20.

120 JX 238 (Norcraft Schedule 14D-9) at 13-14. Norcraft also sought Fortune's confirmation that (1) it would allow enhanced severance for Norcraft's outgoing senior management; and (2) the TRA payment obligations would be satisfied in full at closing. *Id.* at 14.

121 *Id.*

122 *Id.*

123 JX 5 (Klein Dep.) at 164:20-165:4.

124 JX 12 (Baab Dep.) at 99:23-100:4.

125 JX 238 (Norcraft Schedule 14D-9) at 13-14; JX 221 (Merger Agreement) §§ 5.4, 7.3(a)(ii), 8.2. The Merger Agreement defined a “superior proposal” as “a bona fide written Competing Proposal (with all percentages in the definition of Competing Proposal increased to fifty percent (50%)) that did not arise out of a breach of Section 5.4 made by a Third Party on terms that the board of directors of the Company determines in good faith, after consultation with the Company's financial and legal advisors, and considering all factors as the board of directors of the Company (in consultation with its financial and legal advisors) considers to be appropriate (including financing risk, regulatory approval risk, the conditionality, timing and likelihood of consummation of such proposal and the experience and reputation of the proposed buyer) to be more favorable to the stockholders of the Company from a financial point of view than the Offer and the other Transactions (after giving effect to all adjustments to the terms thereof which may be offered by [Fortune] in writing, including pursuant to Section 5.4(g)).” JX 221 (Merger Agreement) § 8.2 (defining “Superior Proposal”).

126 JX 221 (Merger Agreement) § 5.4(c), (g). Under the Merger Agreement, Fortune had four business days to match a superior proposal by a third-party bidder and two business days to match any subsequent proposal by the same bidder. *Id.* § 5.4(g).

127 *Id.*, pmbl. & § 1.1

128 JX 238 (Norcraft Schedule 14D-9) at 14; PTO ¶ 2w.

129 JX 238 (Norcraft Schedule 14D-9) at 15.

130 JX 163 (e-mail chain between Klein and RBC, Mar. 11, 2015) (Klein: “At one point [Buller] said in a hopeful way - ‘Do you want to hire me to run your whole cabinet business?’ I gently said no .... ”); JX 13 (Biggart Dep.) at 86:16-87:11 (explaining that Buller “was hoping that [Fortune would] hire him”).

[131] JX 163 (e-mail chain between Klein and RBC, Mar. 11, 2015); TT 205:7-14 (Biggart) (On March 6, 2015, Fortune “definitively told [Buller] he didn't have the job.”); *see also id.* 83:1-3 (Biggart).

[132] TT 205:19 (Biggart); *see* JX 163 (e-mail chain between Klein and RBC, Mar. 11, 2015) (Klein: “From that point forward [Buller] was rather short with me .... So I need some help here - in a very careful way, so as not to turn this into WWIII. [Buller] and his ego need to [be] managed.”); TT 127:11-17 (Biggart) (“Buller, at this point, is not supporting the transaction, and [Fortune was] getting the sense that he's not going to sign the merger agreement. And I'm concerned.”).

[133] JX 13 (Biggart Dep.) at 95:12-17 (“Q. Was it your understanding that Mr. Buller first raised his desire to purchase Norcraft Canada ... after he was told there's no place for you post-closing? A. I believe so, that was the first I heard about it.”); JX 168 (e-mail chain between Klein and Fortune deal team, Mar. 14, 2015) (Klein: “So, I spoke to [Buller] this morning, and he would like to buy Urban Effects.”); JX 11 (Reilly Dep.) at 156:3-9.

[134] JX 71 (Norcraft Board Minutes Mar. 19, 2015) at NCFT0165034-35. According to Buller, since he never engaged in pre-close negotiations with Fortune to acquire Norcraft Canada, he did not recuse himself from Norcraft-Fortune negotiations. JX 3 (Buller Dep.) at 235:12-240:20. In contrast, Reilly testified that Buller did recuse himself from certain Norcraft Board meetings. JX 11 (Reilly Dep.) at 158:11-24. Remarkably, the Norcraft Canada conflict was the first Buller conflict that seemed to percolate up to the Board's attention. As discussed below, the Board apparently was content to have Buller negotiate TRA payments and Merger consideration at the same time (even though the TRA payments were to be made only to select TRA Beneficiaries who were competing with Norcraft stockholders for consideration), and also content to have Buller negotiate for his own post-Merger employment with Fortune while simultaneously taking the lead for Norcraft in Merger negotiations. *See* JX 13 (Biggart Dep.) at 89:7-11; JX 5 (Klein Dep.) at 139:3-140:14.

[135] *See* JX 13 (Biggart Dep.) at 97-100; *id.* at 121:4-10 (“[Q.] As of Thursday, March 19th, was [it] your understanding that Mr. Buller was insisting on some understanding pre-signing with respect to the sale to him of the Canada business? A. That's my understanding. I believe [Buller] continued this up right until we signed the [Merger Agreement].”); TT 125:3-21 (Biggart) (explaining that Buller was upset because Fortune would not commit to sell him Norcraft Canada).

[136] *See* JX 168 (e-mail chain between Klein and Fortune deal team, Mar. 14, 2015) (Klein: “I told [Buller that his proposed acquisition of Urban Effects] would likely be a subsequent transaction - a week later or something like that, post close.”); JX 195 (e-mail chain between Klein and Fortune deal team, Mar. 25, 2015) (Klein: “[Eldridge] said I need to call [Buller] and calm him down and make him feel good”); TT 114-15 (Biggart) (explaining that Fortune did not feel comfortable negotiating a Norcraft Canada transaction with Buller pre-closing).

[137] JX 195 (e-mail chain between Klein and Fortune deal team, Mar. 25, 2015) (Klein: “[Eldridge] said I need to call [Buller] and calm him down and make him feel good.”).

[138] JX 197 (e-mail chain between Buller and Reilly, Mar. 26, 2015).

[139] JX 202 (e-mail from Buller to PwC, Mar. 27, 2015).

[140] JX 198 (e-mail chain between Norcraft and Fortune deal teams, Mar. 26, 2015) at NCFT0168392; TT 126:6-16 (Biggart) (“I got Chris Klein to agree ... that [Fortune] would waive [Buller's] noncompete in Canada, as a showing of good faith to ... Buller that we were serious when we say we're going to ... have a negotiation after the closing.... ”).

[141] JX 219 (Amendment to Buller's Employment Agreement).

[142] JX 204 (e-mail from Reilly to Maselli, Mar. 27, 2015).

[143] TT 123-26 (Biggart) (explaining the TRA-related difficulties); *id.* at 126:2-5 (Biggart) (“I called [Ropes & Gray] and said ... [w]e better do something quick or this whole deal is going to fall apart.”).

[144] TT 123-24 (Biggart).

[145] JX 13 (Biggart Dep.) at 168:2-3; JX 198 (e-mail chain between Norcraft and Fortune deal teams, Mar. 26, 2015); JX 207 (e-mail from Klein to Fortune deal team, Mar. 27, 2015); TT 126:8 (Biggart) (“[Fortune was] willing to pay 2 out of the $3 million.”).

146 JX 207 (e-mail from Klein to Fortune deal team, Mar. 27, 2015) (Klein: "We[ ] heard through [Buller's] personal lawyer that he rejects our offer of 2 of 3 million [of the] disputed TRA amount, needs all 3.... I've been very reasonable here in all of this, but really cannot go any farther. I do not wish to call [Buller] and go through all of this again with him - it could do more harm than good.") (formatting altered); TT 128:12-23 (Biggart) ("Q. What was [Buller's] response to that proposal? A. He said no. And he said, I want... everything that my accountant says I'm entitled to. He said, [my accountant] has calculated my TRA payment at 19.7 [million], I want 19.7.").

147 JX 207 (e-mail from Klein to Fortune deal team, Mar. 27, 2015).

148 JX 212 (Mar. 27, 2015 e-mail from Buller to Maselli, Reilly et al., thanking Maselli and Reilly for agreeing that Trimaran and SKM, respectively, would transfer the $1 million sum to the Norcraft LLC unitholders); TT 129:6-24 (Biggart).

149 JX 238 (Norcraft Schedule 14D-9) at 16-17.

150 PTO ¶ 2y; JX 238 (Norcraft Schedule 14D-9) at 17.

151 PTO ¶ 2z. Under the TRA termination agreements, the Norcraft LLC unitholders would receive approximately $ 19.7 million, SKM would receive approximately $15.9 million and Trimaran would receive approximately $7.9 million. *Id.*

152 PTO ¶ 2bb.

153 JX 229 (Buller Tender and Support Agreement ["Buller TSA"]) § 3; JX 230 (SKM Tender and Support Agreement ["SKM TSA"]) § 3; JX 231 (Trimaran Tender and Support Agreement ["Trimaran TSA"]) § 3. Fortune initiated Tahiti's tender offer on April 14, 2015, PTO ¶ 2ee, and the offer's initial expiration date was May 11, 2015. JX 239 (Norcraft Schedule TO, filed Apr. 14, 2015, attaching Tahiti's tender offer) at 9.

154 JX 229 (Buller TSA) § 3(b); JX 230 (SKM TSA) § 3(b); JX 231 (Trimaran TSA) § 3(b).

155 PTO ¶ 2cc.

156 TT 45:14-46:8 (Eldridge); JX 8 (Eldridge Dep.) at 49:8-12, 89:17-90:22.

157 JX 3 (Buller Dep.) at 199-200; JX 9 (Maselli Dep.) at 76:5-16; JX 11 (Reilly Dep.) at 122-29.

158 JX 12 (Baab Dep.) at 100-02; *see also* JX 149 (Feb. 27, 2015 email from Klein to Fortune deal team outlining Fortune's conditions for the go-shop, explaining their intended effect of avoiding an auction); JX 232 (e-mail chain between RBC, Klein and other members of Fortune's deal team, Apr. 7, 2015, explaining RBC should emphasize to other potential buyers that Fortune has matching rights).

159 TT 26:22-27:1 (Eldridge). Citi's contact list was developed with input from Buller and Reilly, who "suggested [certain] companies to put on the list, including companies that had reached out to [Norcraft] historically." TT 27:7-12 (Eldridge).

160 TT 27 (Eldridge); JX 243 ("Buyers Log" dated May 4, 2015, prepared by Citi ["Citi Go-Shop Log"]). The six private equity firms were The Carlyle Group ("Carlyle"), TPG Capital, Wind Point Partners, Olympus Partners, American Industrial Partners and another unidentified private equity firm. TT 27 (Eldridge); JX 243 (Citi Go-Shop Log).

161 JX 240 ("Go-Shop Process Update" dated Apr. 20, 2015, prepared by Citi); TT 157 (Biggart).

162 PTO ¶ 2cc.

163 JX 243 (Citi Go-Shop Log) at 5 ("no interest in going head-to-head with Fortune on this"), 7 ("Fortune is a logical buyer here, so hard for us to compete"), 8 ("[n]ot that interested in competing against Fortune"), 10 ("[c]an't compete with Fortune"), 11 ("[c]an't compete with Fortune").

164 *Id.* at 6, 14 ("[v]alue too high").

165 *Id.* at 15; *seeid.* at 2 ("investment is too big [ ] to consider in a short period"); TT 46:9-19 (Eldridge) ("Q. And, sir, you testified at your deposition that there were go-shop participants in this process who indicated that they would like to have more time. Correct? A. Yes. Q. And what parties were those? A. I don't recall specifically. I recall it being a general comment from a couple of people that we spoke with. They may not have been people that signed NDAs. It was just a general comment from various people that we contacted.").

166 JX 233 (e-mail chain between Klein, RBC and other members of Fortune's deal team, Apr. 7, 2015) at FB0089016.

167 *Id.*

168 *Id.*

169 *Id.*

170 *Id.*

171 TT 144:3-4 (Biggart).

172 TT 144:5-6 (Biggart).

173 TT 144:16-18 (Biggart).

174 JX 5 (Klein Dep.) at 275:6-276:14.

175 JX 221 (Merger Agreement), pmbl. & § 1.1; PTO ¶¶ 2cc, 2ee.

176 PTO ¶ 2cc.

177 JX 250 (May 12, 2015 Fortune press release); PTO ¶ 2ff.

178 TT 455-56 (Clarke); TT 698 (Austin Smith).

179 YT 455-56 (Clarke); TT 698 (Austin Smith). By any measure, both experts are well qualified. *See* JX 18 (Report of David G. Clarke, ASA [“Clarke Report”]) at 8 (describing qualifications); JX 20 (Austin Smith Report) at 3 (describing qualifications). And both did what they were engaged to do here - advocate their side's position on fair value - quite effectively. It is accepted in Delaware appraisal litigation that paid valuation experts have assumed more of an advocacy role, and less of a traditional expert witness role (as illustrated by the wide deltas we regularly see in their valuation conclusions). *SeeDell*, 177 A.3d at 24 (“the price produced by an efficient market is generally a more reliable assessment of fair value than the view of a single analyst, especially an expert witness who caters her valuation to the litigation imperatives of a well-heeled client”); *Global GT LP v. Golden Telecom*, 993 A.2d 497, 498-99 (Del. Ch. 2010) (“Both these men of valuation science *purported* to apply the same primary method of valuation—the discounted cash flow (‘DCF’) method—but the expert for the petitioners came up with a value of $139 per share and the expert for Golden came up with a value of only $88 per share—a modest $51 per share value gap.” (emphasis supplied)). Despite the repeated expressions of frustration by our courts, the practice continues. When a rushing river flows against a resisting rock, eventually the river wins out. Perhaps that is the hope among appraisal advocates and the valuation experts they engage to sponsor their positions.

180 TT 243–14 (Subramanian). Subramanian is “the H. Douglas Weaver Professor of Business Law at the Harvard Business School (HBS) and the Joseph Flom Professor of Law and Business at the Harvard Law School (HLS).” JX 19 (Expert Report of Guhan Subramanian [“Subramanian Report”]) at 2; *see id.* (describing qualifications).

181 JX 18 (Clarke Report) at 17 (quoting JX 19 (Subramanian Report) at 25) (internal quotation marks omitted). Clarke did not offer any independent analysis as to why the Merger Price is not a reliable indicator of Norcraft's fair value as of the Merger date; instead, he adopted in full Subramanian's conclusion on that point. *See* JX 18 (Clarke Report) at 6, 17.

182 *Seeid.* at 2.

183 *Id.*

184 *Id.* at 2-3. The extension of the projections, according to Clarke, was required to reduce Norcraft's growth rates gradually to a “steady state.” In this regard, Clarke notes that “if [he] had to use 2019 as the final year of [his] projections, [he] would then need to use a higher [PGR of 4.4%] to account for the tapering of [Norcraft's] growth to a steady state.” JX 21 (Rebuttal Report of David G. Clarke, ASA [“Clarke Rebuttal Report”]) at 27 n.62.

185 JX 18 (Clarke Report) at 24; JX 1 (Ginter Dep.) at 44—45.

186 JX 18 (Clarke Report) at 3, 42. To derive Norcraft's WACC, Clarke first “calculated [1] Norcraft's cost of equity based on the capital asset pricing model (‘CAPM’) and [2] Norcraft's long-term[,] [after-tax] cost of debt.” *Id.* at 3, 33. Clarke next multiplied (1) Norcraft's estimated cost of equity (11.4%) by the proportion of equity in Norcraft's capital structure (approximately 75%), as measured by Norcraft's (undiluted) market capitalization immediately before the Merger's announcement ($396 million); and (2) Norcraft's estimated after-tax cost of debt (4.31%) by the proportion of debt in Norcraft's capital structure (approximately 25%), as measured by

the book value of Norcraft's long-term debt on March 29, 2015 ($147.5 million). *Id.* at 33, 42 & sched. 5-B. Finally, Clarke summed the product of each calculation to obtain a WACC of 9.6%. *Id.* at 33.

[187] *Id.*, sched. 2-A (DCF analysis).

[188] *Id.*, sched. 2-A (DCF analysis). Terminal year free cash flow is the future value implied by (1) the subject company's projected revenue and expense items in the final year of the discrete projection period; and (2) the subject company's estimated PGR. *See id.* Clarke calculated Norcraft's capitalization rate as the positive difference of Norcraft's estimated WACC (9.6%) and estimated PGR (3.5%). *Id.* at 43.

[189] *Id.*, sched. 2-A (DCF analysis).

[190] *Id.*

[191] *Id.* Operating value, as stated here, represents the present value of Norcraft's future unlevered free cash flows. *Id.* A DCF analysis, however, attempts to derive the value of the subject company's equity. *Id.* at 45. Thus, adjustments to the operating value are generally necessary to add in equity in the form of excess cash (or cash equivalents) and to remove debt. *Id.* at 45-47. Clarke based his excess cash and "cash from option exercise" estimates on the information disclosed in the Base Case projections and Norcraft's Form 10-Q for Q1 FY2015. *Id.* at 45. He based his estimation of the TRA-related tax benefits on the "[I.R.C. §] 743(b) and [net operating loss] utilization" projections included in Citi's March 28, 2015 presentation to the Norcraft Board. *Id.* at 46.

[192] *Id.* at 48.

[193] *Id.* Clarke calculated Norcraft's "fully diluted shares outstanding" as the sum of (1) the total number of Norcraft shares and stock options outstanding as of the Merger date; and (2) the total number of convertible Norcraft LLC units (convertible into Norcraft stock) outstanding on that date. *Id.*

[194] *Id.* at 2–4.

[195] *Id.* at 51.

[196] *Id.* at 4.

[197] *Id.* at 2.

[198] JX 20 (Austin Smith Report) at 29 (emphasis in original). Austin Smith based her $3.60 per share "synergies" figure on "the presentations of Citi and the work done by RBC." TT 704:24-705:1 (Austin Smith).

[199] JX 20 (Austin Smith Report) at 1.

[200] *Id.*

[201] *Id.* at 20-21, 23 & Ex. 6 (DCF Analysis). Austin Smith performed two additional DCF analyses, one relying on the Ginter 2014 Projections, which valued Norcraft at $15.59 per share, and another relying on a Capitalization of Cash Flow methodology, which valued Norcraft at $12.65 per share. *Id.* at 23-24.

[202] *Id.* at 23 & Ex. 6 (DCF Analysis).

[203] *Id.* at 20.

[204] *Id.*, Ex. 6 (DCF Analysis). To derive Norcraft's WACC, Austin Smith first calculated (1) Norcraft's cost of equity based on CAPM and (2) Norcraft's after-tax cost of debt (using a 37.69% tax rate). *Id.*, Ex. 5 (Calculation of WACC). She next multiplied (1) Norcraft's estimated cost of equity (12.4%) by a target proportion of equity in Norcraft's capital structure (86%), based on the capital structure of selected comparable companies; and (2) Norcraft's estimated after-tax cost of debt (3.6%) by a target proportion of debt in Norcraft's capital structure (14%), again based on a "comparable capital structure" approach. *Id.*, Exs. 4 (Calculation of Beta) and 5 (Calculation of WACC). Finally, Austin Smith summed the product of each calculation to obtain a WACC of 11.2%. *Id.*, Ex. 5 (Calculation of WACC).

[205] *See id.*, Ex. 5 (Calculation of WACC). This is the same approach Clarke followed to determine terminal value (with different inputs). JX 18 (Clarke Report), sched. 2-A (DCF analysis).

[206] JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis).

[207] *Id.*

[208] JX 537 (native Excel version of Austin Smith's DCF model). Austin Smith calculated Norcraft's excess cash on the Merger date based on the "Cash from Norcraft" figure in the "Funds Flow Memorandum" prepared in connection with the Merger ($54,396,335.01), JX 249 at 2, *less* a $20 million cash balance (cash for

operations, per the Base Case projections) *plus* the product of (1) Norcraft's total options outstanding as of the Merger date (1,142,383) and (2) the weighted average exercise price of those options ($16.01). JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis) (drawing option-related information from Norcraft's Q1 FY 2015 10-Q, JX 248 at 14).

[209] JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis).

[210] *Id.*

[211] *Id.* Austin Smith calculated Norcraft's fully diluted shares outstanding as 20,869,976. JX 20 (Austin Smith Report) at 13 & n.25. It is unclear how Austin Smith derived this figure, and the figure conflicts with the information set forth in Norcraft's Form 10-a for Q1 FY2015 and the “Funds Flow Memorandum” prepared in connection with the Merger. *See* JX 248 (Norcraft's Q1 FY2015 Form 10-Q) at 4, 11 (17,311,573 shares of Norcraft common stock outstanding, 2,426,167 convertible Norcraft LLC units outstanding and 1,142,383 options on Norcraft stock outstanding as of March 31, 2015); JX 249 (Funds Flow Memorandum) at 3, 11 (18,947,886 shares of Norcraft common stock outstanding, 789,854 convertible Norcraft LLC units outstanding and 1,142,383 options on Norcraft stock outstanding as of May 11, 2015). Both documents indicate a figure of 20,880,123 fully diluted shares outstanding as of the Merger date.

[212] JX 20 (Austin Smith Report) at 23.

[213] *Id.* at 25-28.

[214] *Id.* at 29.

[215] *Id.* In her reports and trial testimony, Austin Smith provided only a cursory—and mostly conclusory—discussion of Norcraft's deal process. *Seeid.* at 19-20; TT 701-703 (Austin Smith). She also acknowledged that she had never before been called upon to offer expert testimony on the efficacy of a sales process. TT 791:20—24 (Austin Smith).

[216] JX 19 (Subramanian Report) at 24-25.

[217] *Id.* at 26.

[218] *Id.*

[219] 7d. at 25, 33-36.

[220] *Id.* at 25, 45-52.

[221] *Id.* at 30 (internal quotation and footnote omitted).

[222] *Id.* at 31; *see* TT 100:4-17 (Biggart); JX 238 (Norcraft Schedule 14D-9) at 13.

[223] JX 19 (Subramanian Report) at 31.

[224] *Id.* at 32.

[225] *Id.* at 32-33.

[226] *Id.* at 25, 33-36.

[227] PTO ¶¶ 2k, 2p.

[228] PTO ¶¶ 2w.

[229] JX 19 (Subramanian Report) at 29-30, 34 (“Fortune ... signed a confidentiality agreement on December 11th, 2014, and then had 110 days of exclusive access to confidential information and management time at Norcraft before the deal was announced on March 30th, 2015.”). During the course of those 110 days, both Norcraft and Fortune had to deal not only with valuation issues relating to the Norcraft business, but also complex tax and valuation issues (with the help of separate independent experts) relating to the TRAs. JX 5 (Klein Dep.) at 137-38.

[230] JX 19 (Subramanian Report) at 34.

[231] *Seeid.* at 35.

[232] *Id.* at 35-36 (citing Guhan Subramanian, *Deal Making: The New Strategy of Negotiauctions* 87-88 (2011)).

[233] *Id.* at 40-41.

[234] *Id.* Per Subramanian, Fortune's unlimited match right compounded the “winner's curse” problem, and so operated as a “ ‘powerful disincentive’ to prospective third-party bidders.” *Id.* at 43 (footnote and citation omitted).

[235] *Id.* at 52.

236 JX 221 (Merger Agreement), pmbl. & § 1.1.

237 JX 229 (Buller TSA) § 3; JX 230 (SKM TSA) § 3; JX 231 (Trimaran TSA) § 3.

238 TT 254:21-255:7 (Subramanian); JX 221 (Merger Agreement) § 1.1.

239 PTO ¶ 2ee.

240 JX 221 (Merger Agreement) § 5.4(g).

241 TT 255:4-7 (Subramanian).

242 TT 299:18-300:4 (Subramanian).

243 JX 19 (Subramanian Report) at 41-44; JX 221 (Merger Agreement) at § 5.4(g).

244 JX 19 (Subramanian Report) at 50.

245 TT 254:4-7 (Subramanian).

246 *Compare* JX 232 (e-mail chain between RBC, Klein and other members of Fortune's deal team, Apr. 7, 2015) *with* JX 11 (Reilly Dep.) at 125:3-22 *and* JX 3 (Buller Dep.) at 206:16-207:24.

247 TT 269:8-11 (Subramanian).

248 JX 260 (Petition for Appraisal).

249 1 77 A.3d 1; D.I. 91.

250 8 *Del. C.* § 262(h).

251 *See, e.g.,In re Orchard Enters., Inc.*, 2012 WL 2923305, at *18 (Del. Ch. July 18, 2012) ("As a law-trained judge who has to come up with a valuation deploying the learning of the field of corporate finance, I choose to deploy one accepted method as well as I am able, given the record before me and my own abilities."); *Global GT LP*, 993 A.2d at 517 n.126 (explaining that "academics and professionals throw around ... ranges of value [that] are used by a law-trained judge to come to a single point estimate of value" and that "[t]he law-trained judges who must perform such analyses are more conscious than anyone of the inherent risk of error in such an endeavor, and indeed of the reality that no one can really tell if an error was made"), *aff'd*, 11 A.3d 214; *Finkelstein*, 2005 WL 1074364, at *12 ("The judges of this court are unremittingly mindful of the fact that a judicially selected determination of fair value is just that, a law-trained judge's estimate that bears little resemblance to a scientific measurement of a physical reality."). Indeed, "the judges of this Court" have lamented the challenges posed by the appraisal statute for many years. While perhaps repetitive, these expressions serve a valuable function; they serve as a longhand way of saying to the parties and the community of interest: "I've done the best I can here."

252 *DFC*, 172 A.3d at 364 (quoting 8 *Del. C.* § 262(h)).

253 *Dell*, 177 A.3d at 21 (quoting *Weinberger v. UOP*, 457 A.2d 701, 713 (Del. 1983); *Golden Telecom*, 11 A.3d at 218; and *In re PetSmart, Inc.*, 2017 WL 2303599, at *26 (Del. Ch. May 26, 2017)) (alteration in original).

254 *Dell*, 177 A.3d at 22.

255 *DFC*, 172 A.3d at 370.

256 *Id.*

257 *Id.* at 366.

258 *See, e.g., id.;Golden Telecom*, 11 A.3d at 217-18.

259 *DFC*, 172 A.3d at 366.

260 *Id.*

261 TT 13-15 (Eldridge).

262 *SeeIn re Fort Howard Corp. S'holders Litig.*, 1988 WL 83147, at *13-14 (Del. Ch. Aug. 8, 1988) (finding board-chosen single-bidder process satisfied *Revlon* duties); *In re Pennaco Energy, Inc.*, 787 A.2d 691, 706 (Del. Ch. 2001) ("[T]he mere fact that the Pennaco board decided to focus on negotiating a favorable price with Marathon and not to seek out other bidders is not one that alone supports a breach of fiduciary duty claim."); *In re MONY Gp. Inc. S'holder Litig.*, 852 A.2d 9, 21 (Del. Ch. 2004) (same) (quoting *Pennaco*, 787 A.2d at 706).

263 JX 31 (Guhan Subramanian, *Go-Shops vs. No-Shops in Private Equity Deals: Evidence and Implications*, 63 Bus. Law. 729 (2008)) at 755 ("[A] pure go-shop can be a valuable tool for extracting the highest possible price in the sale of [a] company.").

264 *M.P.M. Enters., Inc. v. Gilbert*, 731 A.2d 790, 797 (Del. 1999) ("A fair merger price in the context of a breach of fiduciary duty claim will not always be a fair value in the context of determining going concern value."); *In re Trados Inc. S'holder Litig.*, 73 A.3d 17, 78 (Del. Ch. 2013) ("A court could conclude that a price fell within the range of fairness and would not support fiduciary liability, yet still find that the point calculation demanded by the appraisal statute yields an award in excess of the merger price."); *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 466 (Del. Ch. 2011) (same).

265 Petitioners urge the Court to conclude that "a go-shop only process" is, *per se*, inadequate to generate fair value. Pet'rs' Post Trial Opening Br. 3 (citing *IQ Hldgs. v. Am. Commercial Lines*, 2013 WL 4056207 (Del. Ch. Mar. 18, 2013) and *Huff Fund Inv. P'ship v. CKx, Inc.*, 2013 WL 5878807, at *13 (Del. Ch. Nov. 1, 2013)). Having reviewed the cited authority, I do not see where *IQ Holdings* addressed the issue at all. As for *CKx, Inc.*, while the court acknowledges that a scenario where the only market check is an unsuccessful go-shop might undermine the reliability of the deal price as an indicator of fair value, the court says nothing of adopting a rule that a go-shop alone will *never* produce fair value for the target. *Id.* at * 13. I see no basis in law or fact to adopt such a rule.

266 JX 140 (e-mail from Reilly to Buller, Maselli and Citi representatives, Feb. 20, 2015) (Reilly: "I do believe we are leaving $ on the table"); TT 29:19-22 (Eldridge) (Buller "eager to try and find a buyer at a higher valuation"); JX 138 (e-mail from Ginter to Buller, Feb. 19, 2015) ("Current offer will be 10.9x or less by the time we close in April at $25.50. so we weren't happy with the deal in [O]ct[ober] but now we are?").

267 *See* JX 3 (Buller Dep.) at 85-86.

268 JX 185 (e-mail chain between Fortune director David Mackay and Klein, Mar. 20, 2015) (Mackay: "Looks very positive[.] A good strategic fit at a reasonable price ... I fully support the deal and hope no one comes along and offers more."); *id.* (Klein: "You are spot on - its [sic] a good price, and there is a risk someone comes along and tries to top the offer."); JX 300 (Mar. 31, 2015 e-mail from Fortune director Mackay to Fortune's other directors and deal team members) ("Let's hope no one bids!").

269 TT 146:18-147:9 (Biggart) (explaining a Fortune presentation analyzing potential go-shop competitors "[b]ecause at this point in time, we're about to agree to a go-shop, and our CEO is very upset about the idea of doing this"); *see also* JX 5 (Klein Dep.) at 164:11—22 ("Q. And Norcraft insisted on some type of go-shop process, right? A. Yes. Q. And in the context of negotiating that, your goal was to minimize the chances that the go-shop process would result in a higher bidder, — A. I wanted to — Q. — correct? A. — give them what they needed - the minimum amount they needed to satisfy their fiduciary responsibility which I know they had."). Of course, it is not unusual—or inherently problematic—for a prospective acquiror to want to avoid being outbid after having expended considerable time, effort and funds. Fortune's attitude, however, suggests that it appreciated the pre-sign process did not yield fair value for Norcraft stockholders and that it wanted to protect that advantage throughout the go-shop process. Again, this is precisely what the Board reasonably should have expected from the party sitting on the other side of the table.

270 JX 166 (e-mail from Klein to Fortune deal team, Mar. 12, 2015); TT 205 (Biggart) (On March 6, 2015, Fortune "definitively told [Buller] he didn't have the job.").

271 *See* JX 189 (e-mail chain between Dave Randich, head of Fortune's cabinet division, Klein and members of Fortune's deal team, Mar. 23, 2015); JX 199 (Mar. 26, 2015 e-mail from RBC to Klein and other members of Fortune's deal team); JX 202 (Mar. 27, 2015 email from Buller to PwC); JX 194 (e-mail chain between members of Norcraft and Fortune deal teams, Mar. 25, 2015).

272 JX 11 (Reilly Dep.) at 158-160.

273 JX 13 (Biggart Dep.) at 107-109, 111:6-112:3; JX 194 (e-mail chain between members of Norcraft and Fortune deal teams, Mar. 25, 2015).

274 *In re AOL, Inc.*, 2018 WL 1037450, at *9 (Del. Ch. Feb. 23, 2018) (observing "if front-end information sharing is truncated or limited, the post-agreement period should be correspondingly robust, so to ensure that information is sufficiently disseminated that an informed sale can take place and bids can be received without disabling impediments").

275 The Merger Agreement was publicly announced on March 30, 2015. *See* JX 227 (Norcraft Mar. 30, 2015 Proxy Statement) at 3. That same day, the Go-Shop Period began. PTO ¶ 2cc.

276 JX 19 (Subramanian Report) at 34; JX 243 (Citi Buyers Log) at 2 (“investment is too big [ ] to consider in a short period”); *id.* at 12 (“can't move fast enough in 35 days”); *id.* at 2, 5, 7-9 (prospective bidders explaining they had no interest in competing against Fortune).

277 *See, e.g.*, JX 3 (Buller Dep.) at 207:5-24 (“Q. Do you know what Norcraft's rights were if another proposal came in during the go-shop period? A. Don't recall. Q. Do you have any knowledge of what Norcraft could have done if one of the go-shop parties was interested and made a bid? A. We could have pursued the offer. Q. Were there any restrictions on Norcraft's ability to pursue an offer? A. Some, but I don't recall what they were.... Q. Do you recall anything about Fortune's rights if another offer came in? A. I don't recall.”); JX 8 (Eldridge Dep.) at 85:17-19 (“Q. What kind of matching rights did Fortune have in this transaction? A. I don't recall.”); JX 9 (Maselli Dep.) at 75:5-78:5 (“Q. Under the terms of the merger agreement, what needed to occur for a go-shop participant to continue to negotiate with Norcraft regarding a possible sale after the go-shop period ended? ... A. I don't know what the threshold was, but ... if it was a sufficiently robust offer, they would have an opportunity to complete the transaction.”); JX 11 (Reilly Dep.) at 121:3-130:20 (“Q. Did you personally ever consider what effect the tender and support agreements would have on the go-shop process? A. I can't recall.... To be honest with you, I'm not an expert in going private transactions, though I've been around for a while; and, in my estimation, the retention of both Ropes and Citibank and to rely on their advice and counsel with respect to the process was, you know, doing my duty. So that's kind of what we really looked to the experts to help us.... Q. What are matching rights? A. I have no idea.... Q. Okay. Well, do you know what type of matching rights Fortune had in Norcraft's go-shop process? ... A. I don't recall.... Q. Do you recall any discussions among Norcraft's directors or officers with respect to Fortune's matching rights in this go-shop process? A. I do not. Q. Under the merger agreement that Norcraft signed with Fortune Brands, what needed to happen for a go-shop participant to continue to negotiate with Norcraft regarding a possible sale after the go-shop period ended? A. I don't recall.”); *cf.* JX 1 (Ginter [CFO] Dep.) at 140:9-14 (“A. My knowledge of a go-shop is limited in that regard. I know the banks ran it for us and prepared a list of potential investors that may be interested in looking at Norcraft. But my knowledge of a go-shop is limited to that and what I learned during the process.”).

278 JX 5 (Klein Dep.) at 137-139; JX 11 (Reilly Dep.) at 164-165; JX 130 (Feb. 9, 2015 RBC presentation regarding TRA value); JX 162 (Mar. 10, 2015 RBC email attaching questions regarding TRAs).

279 JX 221 (Merger Agreement) § 5.4(g); *see**Lender Processing*, 2016 WL 7324170, at *25 (“In this case, the most persuasive explanation is that the existence of an incumbent trade bidder holding an unlimited match right was a sufficient deterrent to prevent other parties from perceiving a realistic path to success.... Without a realistic path to success, it made no sense to get involved.”). Fortune's Vice President of M & A confirmed that “the team at Fortune understood that unlimit[ed] matching rights would discourage potential bidders in a go-shop process.” JX 12 (Baab Dep.) 99-100. And, Fortune's CEO touted Fortune's match right when instructing RBC how to dissuade potential go-shop participants from bidding. JX 232 (e-mail chain between RBC, Klein and other members of Fortune's deal team, Apr. 7, 2015).

280 *In re Lear Corp. S'holder Litig.*, 926 A.2d 94, 119-20 (Del. Ch. 2007).

281 TT 289:1-7 (Subramanian).

282 PTO ¶ 2ee. As noted, the Go-Shop Period began on March 30, 2015. PTO ¶ 2cc.

283 JX 229 (Buller TSA); JX 230 (SKM TSA); JX 231 (Trimaran TSA).

284 JX 232 (e-mail chain between RBC, Klein and other members of Fortune's deal team, Apr. 7, 2015) (RBC describing its planned efforts to dissuade potential buyers); *id.* (Klein expressing his interest in RBC “shutting the door on [potential buyers] and their willingness to look at [Norcraft]”).

285 *DFC*, 172 A.3d at 366. Respondent advanced deal price less synergies as reflecting Norcraft's fair value. Accordingly, it was Respondent's burden to prove the reliability of Norcraft's deal process. Respondent, however, failed to meet that burden—its witnesses struggled to recall basic aspects of the deal process and its valuation expert presented only a cursory, mostly conclusory, analysis of that process. Petitioners, on

the other hand, presented credible evidence demonstrating that deal price less synergies is not a reliable indicator of Norcraft's fair value.

[286] This, of course, means that I give no weight to Austin Smith's deal price less synergies valuation.

[287] D.I. 91.

[288] *See*AOL, 2018 WL 1037450, at *10, n.118 (declining to engage in an extensive analysis of the efficient market hypothesis when the parties did not present either an argument to that effect or sufficient evidence to allow the court to undertake the analysis on its own).

[289] JX 216 (e-mail from RBC to Biggart, Mar. 29, 2015, attaching RBC presentation on Norcraft) at FB0047792, FB0047795.

[290] *See* JX 68 (Sept. 18, 2014 Fortune Presentation) at FB0089499; JX 215 (Citi Board Discussion Materials) at FB0049833.

[291] *See* JX 215 (Citi Board Discussion Materials) at FB0049845.

[292] *See*Dell, 177 A.3d at 25 ("A market [for a company's stock] is more likely efficient, or semi-strong efficient, if [the company] has many stockholders; no controlling stockholder; 'highly active trading'; and if information about the company is widely available and easily disseminated to the market." (quoting *DFC*, 172 A.3d at 373-74)).

[293] *See*Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc., 2018 WL 922139, at *24 (Del. Ch. Feb. 15, 2018) ("*DFC and Dell* teach that if a company's shares trade in a market having attributes consistent with the assumptions underlying a traditional version of the semi-strong form of the efficient capital markets hypothesis, then the unaffected trading price provides evidence of the fair value of a proportionate interest in the company as a going concern." (footnote omitted)).

[294] MG. *Bancorp., Inc. v. Le Beau*, 737 A.2d 513, 525-26 (Del. 1999).

[295] *IQ Hldgs., Inc.*, 2013 WL 4056207, at *1 (quoting *Doft & Co. v. Travelocity.com Inc.*, 2004 WL 1152338, at *8 (Del. Ch. May 20, 2004)) (internal quotation omitted); *see also*Merion Capital, 2013 WL 3793896, at *5; James R. Hitchner, *Financial Valuation: Applications and Models* 291-93, 297 (4th ed. 2017) (cited in JX 21 (Clarke Rebuttal Report)).

[296] *In re Orchard Enters., Inc.*, 2012 WL 2923305, at *9 (Del. Ch. July 18, 2012) ("Reliance on a comparable companies or comparable transactions approach is improper where the purported 'comparables' involve significantly different products or services than the company whose appraisal is at issue, or vastly different multiples."); *see also* Hitchner, *supra*, at 292-93.

[297] *See* JX 13 (Biggart Dep.) at 75:1-76:23, 152:22-153:1 (explaining he could not recall any precedent transaction in the dealer channel since 2010). Many of the precedent transactions identified by Austin Smith preceded the Norcraft-Fortune Merger by three or more years during a time in which the housing market was still recovering from the Great Recession. *See* JX 20 (Austin Smith Report), Ex. 14 (Precedent Transaction Method) (showing that 11 out of the 16 transactions predated 2012). The remaining transactions involved very small, non-public companies, making them unfit for comparison. *See id.* Under these circumstances, I see no reason to dwell on a precedent transaction analysis in determining Norcraft's fair value on the Merger date. *See*Merion Capital, 2013 WL 3793896, at *5 ("The utility of a market-based method depends on actually having companies that are sufficiently comparable that their trading multiples provide a relevant insight into the subject company's own growth prospects."); *see also* Hitchner, *supra*, at 304-06.

[298] *See* JX 20 (Austin Smith Report), Ex. 14 (Precedent Transaction Method) (showing that 11 out of the 16 transactions predated 2012); JX 18 (Clarke Report) at 4 n.8; JX 21 (Clarke Rebuttal Report) at 6.

[299] *Cf.* JX 20 (Austin Smith Report) at 25-28 (explaining, "of the guideline public companies, [Norcraft] is most similar to (though smaller than) American Woodmark, the only other pure-play cabinet manufacturer," "Norcraft is significantly smaller than most of the guideline public companies based on revenue, EBITDA, or assets"); TT 510:10-13 (Clarke) ("I view Norcraft being somewhat unique in that regard. So these are not — you know, these are not perfect comps.").

[300] JX 18 (Clarke Report) at 32, 55; TT 636:17-637:6 (Clarke); JX 20 (Austin Smith Report) at 29.

[301] JX 18 (Clarke Report) at 32, 55; TT 636:17-637:6 (Clarke); JX 20 (Austin Smith Report) at 29.

302 *Dell*, 177 A.3d at 35.

303 *Merion Capital*, 2013 WL 3793896, at *10 (internal citation omitted).

304 *See* Shannon P. Pratt & Roger J. Grabowski, *Cost of Capital: Applications and Examples* 223 (5th ed. 2014) (cited in JX 18 (Clarke Report)) ("Using betas of guideline public companies for estimating a proxy beta has been found to provide reasonably accurate estimates of the subject company"); Duff & Phelps, *2015 Valuation Handbook, Guide to Cost of Capital* 5-3 (2015) (cited in JX 18 (Clarke Report)); *Andaloro v. PFPC Worldwide, Inc.*, 2005 WL 2045640, at *15 (Del. Ch. Aug. 19, 2005). "A company's debt capital can be measured by [gross] debt or net debt, where net debt is equal to total debt *less* excess cash." JX 23 (Austin Smith Rebuttal Report) at 23 (emphasis in original).

305 The capital structure used to relever the subject company's unlevered beta should also be used when calculating its WACC (for weighting purposes). TT 854:17-857:10 (Austin Smith).

306 *AOL*, 2018 WL 1037450, at *11 (quoting *Del. Open MRI Radiology Assocs., P.A. v. Kessler*, 898 A.2d 290, 332 (Del. Ch. 2006)). *See also* Shannon P. Pratt, Robert F. Reilly & Robert P. Schweihs, *Valuing a Business: The Analysis and Appraisal of Closely Held Companies* 156 (4th ed. 2000) (cited in JX 18 (Clarke Report)) (hereinafter "Valuing a Business").

307 As noted, Austin Smith performed two additional DCF analyses, one relying on the Ginter 2014 Projections and another relying on a Capitalization of Cash Flow methodology. *See* JX 20 (Austin Smith Report) at 23-24. Neither analysis, however, formed the basis for her final conclusion regarding fair value. *Seeid.* at 1.

308 JX 1 (Ginter Dep.) at 27:2-28:14, 34:5-10; JX 3 (Buller Dep.) at 101:20-24.

309 JX 3 (Buller Dep.) at 115:8-18 (explaining that the Base Case projections were "something [management] felt very, very comfortable in doing"); *id.* at 114:11-22; JX 1 (Ginter Dep.) at 93:23-25 (stating the Board approved the Base Case projections); JX 11 (Reilly Dep.) at 55:9-19.

310 JX 3 (Buller Dep.) at 115:8-18. *Cf. Petsmart*, 2017 WL 230359, at * 12 (noting that the respondent company's management characterized their projections as "bordering on being too aggressive"—even "approaching 'insan[ity]' ") (alteration in original) (internal quotation marks, footnote and record citation omitted).

311 TT 473-75 (Clarke) (explaining why the Base Case projections are reasonable). Austin Smith found several "significant limitations" to the Base Case projections: (1) they were not created in the ordinary course; (2) they were not created using the same procedure as Norcraft's annual budgets (*i.e.*, bottoms-up); (3) they projected an additional five years of growth after two years of already achieved growth in a cyclical industry; and (4) Ginter and Buller, who prepared the Base Case projections, allegedly knew they were going to lose their jobs if the transaction was completed—introducing the possibility of bias. TT 734:10-736:14 (Austin Smith). Despite all of her concerns, however, Austin Smith relied on the Base Case projections for her primary DCF analysis. TT 737:13-23 (Austin Smith). *See In re Appraisal ofAncestry.com, Inc.*, 2005 WL 399726, at *18 (Del. Ch. Jan. 30, 2015) (noting that "in a number of cases Delaware Courts have relied on projections that were prepared by management outside of the ordinary course of business and with the possibility of litigation") (collecting cases).

312 JX 18 (Clarke Report) at 2.

313 *Id.* 2-3. Clarke "gradually reduce[d] growth rates over time until reaching the PGR," *id.*, by applying a "straight line reduction in growth" from the end of the Base Case projections to the end of his additional five-year projection period. TT 606-607. According to Clarke, "if [he] had to use 2019 as the final year of [his] projections, [he] would need to use a higher [PGR of 4.4%] to account for the tapering of [Norcraft's] growth to a steady state." JX 21 (Clarke Rebuttal Report) at 27 n.62.

314 JX 23 (Rebuttal Report of Yvette R. Austin Smith ["Austin Smith Rebuttal Report"]) at 5-6.

315 *Seeid.* at 4-6.

316 *See* JX 20 (Austin Smith Report) at 21-22 & Ex. 3 (Indexed Growth of Norcraft Adjusted EBITDA versus Key Economic Indicators 2013-2015); TT 21:8-9 (Eldridge) ("[B]uilding products companies are cyclical .... "); JX 23 (Austin Smith Rebuttal Report), Fig. 1 (Comparison of Normalized Growth Patterns); *id.* at Fig. 2 (Historical and Forecasted EBITDA Margins); TT 607:23-608:1 (Clarke) ("Q: Mr. Clarke, the cabinet business is cyclical, isn't it? A. Yes."); *see also* JX 23 (Austin Smith Rebuttal Report), Fig. 1 (Comparison of Normalized

Growth Patterns); *id.* at Fig. 2 (Historical and Forecasted EBITDA Margins); JX 5 (Klein Dep.) at 312:4-10. In light of this determination, I decline to apply Petitioners' suggested 4.4% PGR since that PGR is based on an unrealistic assessment of Norcraft's future financial performance. *See* JX 21 (Clarke Rebuttal Report) at 27 n.62.

[317] *See* JX 112 (Gabelli Report) (stating, as of January 2015, "[w]e see a gradual recovery in housing that will materialize over the next several years"); JX 535 (Fortune Investor Presentation, "Maximum Long-Term Value," May 1, 2015) ("Expectation is for the housing market to return to steady state (1.5 million [new construction] starts and 5-6% [average] annual [repair and remodeling] growth) by 2017 or 2018."). According to "accepted financial principles," *Dell*, 177 A.3d at 22, "terminal value must reflect an appropriate estimate of sustainable growth." Pratt, *supra*, at 49. "[F]or cyclical businesses [ ] the discrete [projection] period commonly corresponds to the number of years or periods until the point is reached where the net cash flow represents an average base net cash flow expected over an *entire* business cycle," *i.e.*, until the midpoint of the cycle. *Id.* at 47 (emphasis supplied); *see also* Robert W. Holthavsen & Mark E. Zmijewski, *Corporate Valuation: Theory, Evidence & Practice* 216 (2014) ("[T]he steady state for a company in a cyclical industry should be at the midpoint of the cycle."). Clarke's extension of the Base Case projections posits a ten-year growth trend but does not account for cyclicality in the cabinetry industry and the impact of such cyclicality on Norcraft's free cash flows. *See* JX 14 (Clarke Dep.) at 60-61 (explaining his extension does not reflect cyclicality prior to 2025); JX 23 (Austin Smith Rebuttal Report), Fig. 1 (Comparison of Normalized Growth Patterns); JX 18 (Austin Smith Report), Fig. 1 (Norcraft Net Sales and EBITDA (Historical 2003-2014) (citing JX 99 (Norcraft Jan. 2015 Management Presentation))). *See also*AOL, 2018 WL 1037450, at *19 ("In a fast-paced industry with significant fluctuations, where management is hesitant to project beyond four years, using a three-stage DCF model or a ten year projection period seems particularly brazen.").

[318] Pratt, *supra*, at 8; *see also* Duff & Phelps, *supra*, at 10-15.

[319] Pratt, *supra*, at 546 ("WACC generally works as a substitute for the enterprise-cash-flow discount rate."). *See also* Valuing a Business, *supra*, at 184.

[320] Valuing a Business, *supra*, at 184; Duff & Phelps, *supra*, at 10-16.

[321] JX 18 (Clarke Report) at 33; JX 20 (Austin Smith Report), Ex. 5 (WACC Calculation).

[322] Duff & Phelps, *supra*, at 2-13.

[323] JX 21 (Clarke Rebuttal Report) at 27.

[324] JX 18 (Clarke Report) at 41.

[325] JX 20 (Austin Smith Report), Ex. 5 (WACC Calculation). The BofA Merrill Lynch US High Yield B Effective Yield "represents the effective yield of the ICE BofA[ ] [Merrill Lynch] US Corporate B Index, a subset of the ICE BofA[ ] [Merrill Lynch] US High Yield Master II Index tracking the performance of US dollar denominated below investment grade rated corporate debt publically issued in the US domestic market. This subset includes all securities with a given investment grade rating B." ICE BofAML US High Yield B Effective Yield, retrieved from FRED, Fed. Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/BAMLH0A2HYBEY (last visited July 24, 2018). By way of reference, Citi used a pre-tax cost of debt of 5.3% in its calculation of Norcraft's WACC and RBC used 4.5%. *See* JX 18 (Clarke Report) at 41 n.91.

[326] JX 267 (Norcraft FY2014 10-K) at 21; ICE BofAML US High Yield B Effective Yield, retrieved from FRED, Fed. Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/BAMLH0A2HYBEY (last visited July 24, 2018); S & P U.S. High Yield Corporate Bond 10+ Year Index, *available online at* https://us.spindices.com/indices/fixed-income/sp-us-high-yield-corporate-bond-10-year-index (last visted on July 24, 2018). The experts do not challenge each other's estimates of Norcraft's pre-tax cost of debt. *See* JX 21 (Clarke Rebuttal Report) at 31 ("Austin Smith's conclusion [regarding Norcraft's pre-tax cost of debt] is in the range of reasonableness given Norcraft's improving performance and generally positive industry outlook as well being consistent with the financial advisors' cost of debt estimate.").

[327] This average figure tracks the ICE BofA Merrill Lynch US High Yield B Effective Yield as of the Merger date (6.39%) and the S & P U.S. High Yield Corporate Bond 10+ Year Yield to Maturity as of that date (6.34%). ICE BofAML US High Yield B Effective Yield, retrieved from FRED, Federal Reserve Bank of St. Louis; https://

fred.stlouisfed.org/series/BAMLH0A2HYBEY (last visited July 24, 2018); S & P Dow Jones Indices LLC, S & P U.S. High Yield Corporate Bond 10+ Year Index, *available online at* https://us.spindices.com/indices/fixed-income/sp-us-high-yield-corporate-bond-10-year-index (last visited on July 24, 2018).

[328] Duff & Phelps, *supra*, at 5-1.

[329] *Id.* at 5-3.

[330] *Id.*; Pratt, *supra*, at 223. When calculating a company's beta, change in the trading price of the company's stock is measured relative to change in the returns of the overall market (or a proxy therefor) over the relevant observation period. JX 18 (Clarke Report) at 34.

[331] JX 18 (Clarke Report) at 34-35.

[332] *See* Duff & Phelps, *supra*, at 5-25 and 10-17.

[333] *See* JX 18 (Clarke Report) at 34-35.

[334] *See* Duff & Phelps, *supra*, at 10-21; Pratt, *supra*, at 244.

[335] *See JX* 18 (Clarke Report) at 37-39; JX 23 (Austin Smith Rebuttal Report) at 18-20. While Clarke found Norcraft's observed beta “statistically relevant,” he did not rely upon that beta beyond using it to define the lower end of a range of betas. He ultimately selected the higher end for his DCF. *See JX* 18 (Clarke Report) at 37-39.

[336] JX 18 (Clarke Report) at 51. Clarke notes in his report that RBC used all four of his chosen companies and Citi used three of the four in their respective analyses of Norcraft. *Id.*

[337] *Id.* at 48-49. Clarke's screening criteria were: (1) public company; (2) industry classification of “Building Products”; (3) 2014 Calendar Year Revenue between $40 million and $4 billion; (4) primary geographic location in the U.S. or Canada; and (5) no recent major divestures or pending significant acquisitions. *Id.* Clarke's application of these criteria yielded a set of sixty-five companies, which Clarke then screened “for companies with a minimum expected EBITDA margin of 7.5% for fiscal year 2016 (approximately half of Norcraft's EBITDA margins) and a maximum expected EBITDA margin of *22.5%* for fiscal year 2016 (approximately 50% above Norcraft's margins). In addition, [he] screened for companies that had forecasted 2016 revenue growth between 5% (approximately half of Norcraft's expected growth) and 15% (approximately 50% above Norcraft's expected growth). Based on those two criteria, the 65 companies were reduced to 28.” *Id.* at 50. Clarke then determined that four of those companies—his four chosen GPCs—“had a primary business in manufacturing products for the [repair and remodeling] and/or new construction residential home construction [markets].” *Id.*

[338] *Id.* at 38 & sched. 5-C; JX 517 (native Excel version of Clarke's DCF model).

[339] JX 18 (Clarke Report) at 39 (“An unlevered beta of 0.80 is slightly above the median and average of the one-year daily betas of the [GPCs] (0.75 to 0.79) while slightly below the median and average two-year weekly betas of the [GPCs] (0.81 to 0.87).”). Clarke relevered his concluded unlevered beta for Norcraft based on Norcraft's actual (observed) capital structure as of the Merger date (75% equity, 25% debt, per Clarke). *Id.*, sched. 5-B. This resulted in a relevered beta for Norcraft of 0.97. *Id.*

[340] JX 20 (Austin Smith Report) at 26 & Ex. 4 (Beta Calculation). The other ten GPCs were: Armstrong World Industries, Inc., Beacon Roofing Supply, Inc., Builders FirstSource, Inc., Caesarstone Ltd., Continental Building Products, Inc., Mohawk Industries, Inc., Patrick Industries, Inc., Quanex Building Products Corporation, Trex Company, Inc. and Universal Forest Products, Inc. *Id.*, Ex. 4 (Beta Calculation). Austin Smith divided her sixteen GPCs into two groups: Group I (comprising American Woodmark, Masco and Fortune), “which consists of companies operating specifically (though not exclusively) in the cabinet market, and Group II [comprising the rest of the GPCs], which consists of companies operating in the general residential building products sector.” *Id.* at 26.

[341] *Id.*, Exs. 4 (Beta Calculation) and 5 (WACC Calculation).

[342] *Id.*, Exs. 4 (Beta Calculation) and 5 (WACC Calculation). Austin Smith relevered her concluded unlevered beta for Norcraft based on a target capital structure comprising 86% equity and 14% debt. *Id.*, Ex. 5 (Calculation of WACC). This yielded a relevered beta for Norcraft of 1.12. *Id.*

[343] JX 21 (Clarke Rebuttal Report) at 28.

[344] JX 23 (Austin Smith Rebuttal Report) at 17.

[345] *See* JX 112 (Gabelli Report) at CITI-00053582.

[346] *See* Pratt, *supra*, at 223 (“The more guideline companies used in the sample size, the better the accuracy.”); *id.* (“The accuracy is also enhanced if the guideline public companies are reasonably close in size to the subject company. When the guideline public companies are larger than the subject company, the beta estimate for the subject company is likely biased low because of the propensity of betas of larger companies to be smaller than the betas of smaller companies.”). My selection of GPCs is further supported by RBC and Citi's choices of GPCs. RBC included all six of the selected companies, JX 216 (Mar. 29, 2015 e-mail from RBC to Biggart, attaching RBC presentation) at FB0047799, and Citi included five out of the six (it did not include Masonite). JX 505 (Citi Discussion Materials for the Fairness Opinion Committee) at CITI-00075076.

[347] *See* Pratt, *supra*, at 204 (explaining that to derive a proxy beta, one will take the median or an average of the unlevered betas). This approach also avoids additional risk for error that might flow from assigning different weights. *See* JX 530 (Bradford Cornell, *Corporate Valuation, Tools for Effective Appraisal and Decision Making* (1993)) at 68. As previously explained, Austin Smith derived a proxy beta for Norcraft based on the median of the unlevered betas of her selected GPCs. JX 20 (Austin Smith Report), Exs. 4 (Beta Calculation) and 5 (WACC Calculation). Clarke's proxy beta calculation, by contrast, took into account both the median and the mean of the unlevered betas of his selected GPCs. JX 18 (Clarke Report) at 39. My proxy beta calculation utilizes the median rather than the mean of the unlevered GPC betas. I took that approach to account for Masonite. Austin Smith and Clarke included Masonite in their respective analyses but both acknowledged that its business was less comparable to Norcraft than some of the other companies considered. Indeed, Masonite exhibited a significantly lower unlevered beta that risked distorting the Court's measurement of Norcraft's relative operating risk (if the Court were to use the mean for summary measure purposes).

[348] JX 18 (Clarke Report), sched. 5-B (Cost of Equity Calculation per CAPM); JX 20 (Austin Smith Report), Exs. 4 (Calculation of Beta) and 5 (Calculation of WACC).

[349] Pratt, *supra*, at 243. The *Hamada* unlevering formula is as follows:

$$\beta_{unlevered} = \frac{\beta_{levered}}{\left(1+\left((1-\text{tax rate})\times(\text{Total Debt/Equity})\right)\right)}$$

Id. at 247.

By corollary, the *Hamada* relevering formula is:

$$\beta_{levered} = \beta_{unlevered} \times \left[1+(1-\text{tax rate})\times\frac{\text{Total Debt}}{\text{Total Equity}}\right]$$

Id.

[350] *Seeid.* at 262-63.

[351] JX 16 (Austin Smith Dep.) at 192:5-12.

[352] *Id.* at 192:13-16.

[353] *Id.* at 192:18-21.

[354] *See* JX 23 (Austin Smith Rebuttal Report) at 22; TT 764:1-19 (Austin Smith).

[355] *See* TT 764:1-19; JX 23 (Austin Smith Rebuttal Report) at 22.

[356] TT 506:11-17 (Clarke).

[357] *See* Duff & Phelps, *supra*, at 1-15, 1-16.

[358] TT 859:4-16 (Austin Smith) (“Q. And you testified earlier that you found no evidence in the record which would guide you in selecting what that target capital structure would be for Norcraft. Correct? A. That's right. Q. And so you had to use the data from comparable companies. Correct? A. Right. Q. And just to be explicit, there's no evidence in the record that Norcraft had any expectation of changing its capital structure after the transaction. Correct? A. That's correct.”). Austin Smith herself recognizes that use of a target capital

structure is only appropriate when "the company's existing capital structure is not equal to the company's target capital structure." JX 23 (Austin Smith Report) at 21-22. According to Austin Smith, Clarke's estimation of Norcraft's actual capital structure as of the Merger date is erroneous because it fails to account for Buller et al.'s ownership of Norcraft LLC units convertible into a 12.3% equity ownership interest in Norcraft (in the form of shares of Norcraft common stock). *Id.* at 21. Austin Smith's criticism in this regard is based on her (apparent) assumption that the conversion of the Norcraft LLC units into Norcraft common stock would not affect the per share trading price of that stock. *See id.* (calculating Norcraft's fully diluted market capitalization on the Merger date without adjusting for the potential dilutive effect of a Norcraft-LLC-unit-to-Norcraft-common-stock conversion on the per share trading value of Norcraft common stock). Upon reviewing the record, it is unclear how such a conversion would affect Norcraft's market capitalization—and, by extension, the equity component of Norcraft's capital structure. In addition, Austin Smith's calculation of Norcraft's fully diluted market capitalization on the Merger date does not account for the exercise of all outstanding options on Norcraft stock on that date. *See id.* ("The total equity in Norcraft['s] capital structure was $452 million ... not the $396 [million] calculated by Mr. Clarke. The operating cash flows of Norcraft were supported not just by the equity of Norcraft Inc. but also by [Buller et al.'s] ownership interest [in Norcraft] LLC."); *but cf.id.* at 13 & n.25 ("[Norcraft's] implied fully diluted market capitalization was $532 million based on the transaction price of $25.50 [multiplied by] *20,869,976* fully diluted shares [outstanding].") (emphasis supplied). Moreover, as previously noted, Austin Smith's calculation of Norcraft's fully diluted shares outstanding as of the Merger date is inconsistent with the information set forth in Norcraft's Form 10-Q for Q1 FY2015 and the Funds Flow Memorandum prepared in connection with the Merger. The inclusion of all options on Norcraft stock outstanding as of the Merger date in the equity component of Norcraft's fully diluted capital structure (together with all Norcraft common stock and convertible Norcraft LLC units outstanding on that date) implies a capital structure of approximately 76% equity and 24% debt. I am satisfied, therefore, that Clarke's estimation of Norcraft's actual capital structure on the Merger date captures Norcraft's "operative reality" on that date. Accordingly, I have adopted that estimation.

[359] For these same reasons, I refer to that same capital structure to calculate Norcraft's WACC (for weighting purposes).

[360] The calculation of Norcraft's NOPAT (and unlevered free cash flow) for FY2015 is based on the Base Case projections for the May-December 2015 period. Hence the "Stub" notation. Austin Smith took this same approach in her DCF analysis. JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis). I have adopted Austin Smith's approach in this regard, given that the operative valuation date here is May 12, 2015 (the Merger date).

[361] *See* JX 18 (Clarke Report), sched. 2-A (DCF Analyis); JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis). In calculating the period-over-period change in Norcraft's NWC, both experts excluded Norcraft's current TRA liability in each of the projected years. JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis) ("Working capital excludes tax-related items."); *see* JX 517 (native Excel version of Clarke's DCF model). The rationale for this exclusion appears to be that Norcraft's payment obligations under the TRAs are non-ordinary-course, non-operating liabilities. *See* JX 18 (Clarke Report) at 29, 46. It is, therefore, more accurate to describe the experts' respective NWC-related computations as calculating period-over-period change in Norcraft's net operating working capital ("NOWC"). The Court's calculation of period-over-period change in Norcraft's NWC —or rather, its NOWC—likewise excludes Norcraft's current TRA liability in each of the projected years. I also note that both experts departed from the Base Case projections' forecast of Norcraft's "current portion of long-term debt" in FYs 2018 and 2019. *See* JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis); JX 517 (native Excel version of Clarke's DCF model); JX 509 (native Excel version of Base Case projections). Both experts projected a $1.5 million figure for each year, whereas the Base Case projects zero for both years. *Compare* JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis) *and* JX 517 (native Excel version of Clarke's DCF model), *with* JX 509 (native Excel version of Base Case projections). The record is unclear as to why, exactly, the experts chose to depart from the Base Case in this particular respect. Nevertheless, because both experts

made the same adjustment to the Base Case projections with regard to Norcraft's "current portion of long-term debt" in FYs 2018 and 2019, i have followed suit.

[362] JX 18 (Clarke Report) at 43 ("I calculated [Norcraft's] terminal value using the Perpetuity Growth Method[.]"); JX 20 (Austin Smith Report) at 20 ("To calculate [Norcraft's] terminal value I relied upon the Gordon Growth (or Perpetuity Growth) model.").

[363] In the Perpetuity Growth model, the capitalization rate is calculated as the positive difference between the applicable discount rate and the subject company's PGR. JX 18 (Clarke Report) at 43. I have used Norcraft's WACC (10.60%) as the applicable discount rate and a 3.5% PGR for Norcraft, which together imply a capitalization rate of 7.10%.

[364] *Id.* Mindful of Clarke's justified criticism of Austin Smith's calculation of Norcraft's terminal year free cash flow, my calculation of that value adjusts for the fact that Norcraft's projected depreciation and amortization expense in the final year of the Base Case projections (FY2019) exceeds Norcraft's projected capital expenditures in that year by approximately $100,000. The adjustment entails implying a 3:4 relationship between Norcraft's depreciation/amortization expense and capital expenditures in perpetuity and thereby avoids "underinvesting in net PP & E." JX 21 (Clarke Rebuttal Report) at 25; *see* Hitchner, *supra*, at 138 ("[I]n a growing business, long-term annual estimated capital expenditures exceed annual depreciation, primarily due to inflation."); *see also* Gilbert E. Matthews & Arthur H. Rosenbloom, *Delaware's Unwarranted Assumption that Capex Should Equal Depreciation in a DCF Model*, (May 15, 2018), https://corpgov.law.harvard.edu/2018/05/15/delawares-unwarranted-assumption-in-dcfpricing/ ("The assumption that depreciation equals capital expenditures is only appropriate if it is also assumed that there is no growth and no inflation. However,... the normalized capital expenditures of a [perpetually] growing company must materially exceed depreciation over time.").

[365] Both experts added Norcraft's estimated excess cash to its operating value in order to calculate the Company's total equity value. JX 18 (Clarke Report), sched. 2-A (DCF Analysis); JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis). The experts differed, however, in how they calculated Norcraft's excess cash and thus reached different estimates of that figure. As noted, Austin Smith calculated Norcraft's excess cash on the Merger date based on the "Cash from Norcraft" figure in the "Funds Flow Memorandum" for the Merger ($54,396,335.01), JX 249 at 2, *less* a $20 million cash balance (cash for operations, per the Base Case projections), *plus* the product of (1) Norcraft's total options outstanding as of the Merger date (1,142,383) and (2) the weighted average exercise price of those options ($16.01). JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis). Clarke, by contrast, calculated Norcraft's excess cash on the Merger date as the sum of (1) the cash balance indicated in Norcraft's Q1 FY2015 Form 10-Q ($63,135,000), JX 248 at 4, and (2) the Merger-related fees indicated in that same filing ($1.2 million), *less* $20 million cash for operations (per the Base Case projections). JX 18 (Clarke Report) at 45. I have adopted Clarke's approach, but have added to his excess cash figure Norcraft's cash receipts from the exercise of all options outstanding on the Merger date (1,142,383) at the weighted average exercise price ($16.01). JX 248 (Norcraft's Q1 FY2015 Form 10-Q) at 14. I find that this holistic approach best approximates Norcraft's "operative reality" as of the Merger date.

[366] Clarke valued the TRA-related tax benefits realized by Norcraft in each of the projected years at $4.4 million, JX 18 (Clarke Report) at 46, while Austin Smith valued them at $4.2 million. JX 20 (Austin Smith Report), Ex. 7 (Tax Characteristics Analysis). Having considered each expert's (quite complicated) approach to valuing those tax benefits, I find that both approaches—and both resulting valuations—are reasonable (they differ by approximately $200,000). Accordingly, I have adopted the average of the experts' respective value estimates.

[367] Like Clarke and Austin Smith, I have drawn this figure directly from Norcraft's Q1 FY2015 Form 10-Q. JX 248 (Norcraft's Q1 FY2015 Form 10-Q) at 4; JX 18 (Clarke Report) at 47; JX 20 (Austin Smith Report), Ex. 6 (DCF Analysis).

[368] JX 248 (Norcraft's Q1 FY2015 Form 10-Q) at 11.

[369] *SeeAOL*, 2018 WL 1037450, at *2 ("I take the parties' suggestion to ascribe full weight to a [DCF] analysis ... [and thus] relegate transaction price to a role as a check on that DCF valuation: any such valuation

significantly departing from even the problematic deal price here should cause me to closely revisit my assumptions.”).

370 I am mindful that “[t]he issue in an appraisal is not whether a negotiator has extracted the highest possible bid. Rather, the key inquiry is whether the dissenters got fair value and were not exploited.” *Dell*, 177 A.3d at 33. Here, in light of the identified flaws in Norcraft's deal process (pre- and post-sign), I find it more likely than not that the Board “left a portion of [Norcraft's] fundamental value on the table.” *Verition P'rs Master Fund*, 2018 WL 922139, at *44.

371 *See**AOL*, 2018 WL 1037450, at *2.

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Supreme Court of Delaware.

BRIGADE LEVERAGED CAPITAL STRUCTURES FUND LTD. and Brigade Distressed Value Master Fund Ltd., Petitioners Below, Appellants,
v.
STILLWATER MINING COMPANY, Respondent Below, Appellee.

No. 427, 2019
|
Submitted: July 15, 2020
|
Decided: October 12, 2020

Synopsis
Background: Stockholders brought appraisal action following acquisition of corporation through a reverse triangular merger. After a bench trial, the Court of Chancery, J. Travis Laster, Vice Chancellor, 2019 WL 3943851, deferred to the merger price of $18 per share as the most reliable indicator of corporation's fair value. Stockholders appealed.

Holdings: The Supreme Court, Tamika Montgomery-Reeves, J., held that:

the Court of Chancery did not abuse its discretion by holding that deal price was a reliable indicator of corporation's fair value, and

the Court of Chancery did not abuse its discretion in declining to grant a deal price adjustment.

Affirmed.

Procedural Posture(s): On Appeal; Judgment.

Court Below—Court of Chancery of the State of Delaware, C.A. No. 2017-0385-JTL

Upon appeal from the Court of Chancery. **AFFIRMED**.

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Before SEITZ, Chief Justice; VAUGHN, and MONTGOMERY-REEVES, Justices.

Opinion

MONTGOMERY-REEVES, Justice:

***1** On May 4, 2017, Sibanye Gold Ltd. ("Sibanye") acquired Stillwater Mining Co. ("Stillwater") through a reverse triangular merger. Under the terms of the merger agreement, each Stillwater share at closing was converted into the right to receive $18 of merger consideration. Between the signing and the closing of the merger, the commodity price for palladium, which Stillwater mined, increased by nine percent, improving Stillwater's value.

Certain former Stillwater stockholders dissented to the merger, perfected their statutory appraisal rights, and pursued this litigation. During the appraisal trial, petitioners argued that the flawed deal process made the deal price an unreliable indicator of fair value and that increased commodity prices raised Stillwater's fair value substantially between the signing and closing of the merger. On August 21, 2019, the Court of Chancery issued its memorandum opinion (the "Memorandum Opinion"), holding that the $18 per share deal price was the most persuasive indicator of Stillwater's fair value at the time of the merger. The court did not award an upward adjustment for the increased commodity prices.

The petitioners now appeal the Court of Chancery's decision, arguing that the court abused its discretion when it ignored the flawed sale process and petitioners' argument for an upward adjustment to the merger consideration.

Having reviewed the parties' briefs and the record on appeal, and after oral argument, this Court holds that the Court of Chancery did not abuse its discretion when it deferred to the deal price as a reliable indicator of fair value without an upward adjustment. Therefore, this Court affirms the Court of Chancery's August 21, 2019 Memorandum Opinion and September 27, 2019 Post-Trial Judgment order.

I. BACKGROUND [1]

Stillwater Mining Company was a publicly traded Delaware corporation primarily engaged in the business of mining and processing platinum group metals ("PGMs") from the J-M Reef in Montana. The J-M Reef is the only PGM mine in the United States, with the only other significant deposits located in South Africa and Russia. Stillwater has two producing mines at the J-M Reef, Stillwater Mine and East Boulder. [2] Stillwater also owns one of the largest PGM recycling operations in the world, which provides additional market supply of PGMs. [3] In light of its operations, Stillwater's common stock trading price is heavily influenced by the spot and forward pricing of the PGM palladium. [4]

By October 2015, Stillwater's board of directors (the "Board") and management had become concerned that both the palladium and platinum markets were facing long-term "structural decline[s]," [5] largely due to the decline in gasoline and diesel-powered automotive markets, the primary end-use of Stillwater's PGMs. [6] Accordingly, the Board began to consider strategic alternatives, including a merger of equals or the sale of some of Stillwater's business operations. [7]

***2** In 2016, the Board's fears materialized as Stillwater's stock price declined, reflecting a decrease in the spot price of palladium that continued throughout the year. Due to the downturn in the trading price, the Board authorized Michael McMullen, Stillwater's CEO and board member, to inquire into strategic opportunities and report back to the Board. [8] Also around this time, McMullen privately expressed unease at the company's situation and began considering his exit from Stillwater. [9]

A. McMullen Engages with Sibanye

On January 30, 2016, Sibanye requested a meeting to discuss the acquisition of Stillwater. [10] Without the Board's knowledge or approval, McMullen met with Neal Froneman, Sibanye's CEO, on March 1, 2016. [11] At the meeting, McMullen asked Froneman to provide "an informal proposal" that included "an idea of valuation" and "transaction structure." [12] He told Froneman that any potential acquisition would need to feature "a large cash component." [13] McMullen also stated that Stillwater would need to "be priced at a premium of 30% over Stillwater's thirty-day volume-weighted average price ('VWAP')." [14] After the meeting, Froneman had the impression that a deal "was doable if we got the valuation right." [15] McMullen took these actions without involving the Board, and he did not inform the Board about his discussions with Sibanye at the Board's next regularly scheduled meeting in May 2016. [16]

By July 2016, Stillwater's stock price and the price of palladium had largely recovered. On July 21, 2016, Sibanye provided a preliminary, non-binding indication of interest at $15.75 per share in cash. [17] Shortly thereafter, on July 27 and 28, 2016, Stillwater's Board met in "executive session" with McMullen to discuss Sibanye's offer. [18] On August 9, 2016, Stillwater executed a confidentiality agreement with Sibanye and provided Sibanye data room access. [19]

B. Stillwater Engages with Other Parties

On August 10, 2016, the Board met and directed management to begin outreach to other potentially interested parties. [20] But instead of working to generate "as much interest as possible" in a transaction with Stillwater, McMullen continued to focus on courting Sibanye. [21] Nonetheless, Stillwater's management met with Bank of America Merrill Lynch ("BAML") on August 18, 2016, to discuss potential options. [22] At that meeting, BAML got "the sense ... that a sale was a possibility" and independently contacted a list of fifteen potential acquirers about purchasing Stillwater. [23] Meetings were arranged with a number of interested parties, including Hecla, Coeur, Kinross, and Gold Fields. [24] By early October, both Hecla and Coeur conducted site visits and obtained access to the data room. [25]

On October 3, 2016, the Board met, reviewed a list of eighteen potential acquirers, and directed McMullen to solicit proposals from investment banks and create an internal cash flow model to value the company.[26] Additionally, Brent Wadman, Stillwater's General Counsel, recommended that the Board form a special committee to oversee the sale process. Since the July 2016 meeting between McMullen and Sibanye, Wadman had become concerned that McMullen was rushing the sale process to facilitate his exit from the company.[27] The Board sought the advice of external counsel, Holland & Hart LLP, as to whether any conflicts existed and whether a special committee should be formed.[28] With Holland & Hart LLP's advice, the Board determined that no conflicts of interest existed at that time.[29] The Board formally retained BAML on November 7, 2016, and BAML immediately conducted a market check.[30] On November 11, 2016, the Board retained Jones Day for its "substantial experience in advising Delaware publicly traded companies in respect of potential strategic transactions."[31]

***3** By the next Board meeting on November 23, 2016, twenty-four parties had received some type of formal or informal contact from BAML or Stillwater management. Four of those parties accessed the data room, four conducted site visits, and one, Sibanye, submitted an indication of interest.[32] McMullen informed the Board that he viewed Sibanye's initial offer of $15.75 per share as insufficient.[33] At the Board's direction, BAML reached out to additional parties, and one, Northam, signed a non-disclosure agreement and accessed the data room.[34] Two other parties—Northern Star and Independence—informed Stillwater that they were only interested in a merger of equals.[35]

On December 1, 2016, Sibanye revised its offer to $17.50-$17.75 per share in cash.[36] On December 2, 2016, Stillwater's Board rejected the revised offer.[37] That same day, BAML provided its internal discounted cash flow model valuing the company between $10.78 and $14.14 per share.[38] BAML also provided a financial analysis of the two merger of equals proposals from Northern Star and Independence.[39] After reviewing the financial analysis, the Board ultimately determined not to pursue either merger of equals transaction, finding neither tenable for a number of reasons.[40]

On December 3, 2016, Sibanye made its "best and final" offer of $18 per share to acquire Stillwater.[41] The $18 price represented a 22.6% premium over the unaffected trading price and a 24.4% premium over the 30-day volume-weighted average price.[42] At this point, although five parties had signed nondisclosure agreements and gained access to Stillwater's non-public information, Sibanye was the only party to make a bid.[43]

C. Stillwater Signs with Sibanye

On December 8, 2016, BAML provided an opinion to the Board that Sibanye's offer was fair to stockholders.[44] The Board considered BAML's fairness opinion in its deliberations, approved the merger, and signed the merger agreement.[45] The transaction was publicly announced on December 9, 2016.[46]

In March 2017, Wadman resigned as general counsel. Wadman's resignation letter cited his concerns about how the deal process unfolded and his belief that McMullen used the process to engage in self-dealing.[47] Stillwater negotiated a settlement with Wadman, and the company issued a statement that did not mention the reasons for his resignation.[48]

During the 138 days between the signing and the stockholder vote, no other bidder made a topping bid over $18 per share, but the price of palladium and Stillwater's trading price increased during that time.[49] Still, on April 26, 2017, approximately 75% of the issued outstanding shares eligible to vote approved the merger.[50] On May 4, 2017, the sale of Stillwater to Sibanye closed.[51]

D. Appraisal Litigation

On May 22, 2017, appellants, petitioners-below, initiated this appraisal litigation.[52] The Court of Chancery conducted a four-day trial and held post-trial argument on May 1, 2019.

On August 21, 2019, the court issued its Memorandum Opinion.[53] The Court of Chancery held that "Sibanye proved that the sale process was sufficiently reliable to make the deal price a persuasive indicator of fair value."[54] Further, the court stated that while "[t]he evidence demonstrated that Stillwater's trading price could provide a persuasive indicator of value, ... it was a less persuasive indicator than the deal price."[55] It also held that "[n]either side proved that its DCF valuation provided a persuasive indicator of fair value. The experts disagreed over too many inputs, and the resulting valuation swings were too great, for [the court] to rely on a model when a market-tested indicator is available."[56] Thus, the court deferred to the merger price of $18 per share as the most reliable indicator of Stillwater's fair value.[57] It also declined to make an upward adjustment to the price to account for Stillwater's increase in value after signing, holding that petitioners did not prove that they were entitled to a deal price adjustment.[58] On September 27, 2019, the Court of Chancery entered its Post-Trial Judgment order.

E. Petitioners Appeal the Court's Memorandum Opinion and Order

***4** On October 8, 2019, Petitioners filed a timely Notice of Appeal. On appeal, Petitioners argue that the Court of Chancery abused its discretion by ignoring the flawed sale process and holding that the deal price of $18 per share reflected Stillwater's fair value at closing.[59] Further, Petitioners argue that the court relied on an incorrect conclusion to justify its decision to not adjust the deal price upward to account for rising commodity prices.[60]

Sibanye responds that the Court of Chancery correctly examined Stillwater's sale process and held that the process presented sufficient indicia of reliability, making the deal price the best indicator of Stillwater's fair value.[61] Further, it argues that because Petitioners' arguments concerning the deal price adjustment were wholly conclusory, the court correctly held that Petitioners "failed to prove ... 'that the deal price should be adjusted upward to reflect a change in value between signing and closing.' "[62]

On review, this Court holds that the Court of Chancery did not abuse its discretion when it relied on the deal price as the most reliable indicator of Stillwater's fair value. Nor did the Court abuse its discretion when it declined to adjust the deal price.

II. STANDARD OF REVIEW

This Court reviews errors of law *de novo*.[63] We review statutory appraisal awards for abuse of discretion and "grant significant deference to the factual findings of the trial court."[64] "So long as the Court of Chancery has committed no legal error, its factual findings will not be set aside on appeal unless they are clearly wrong and the doing of justice requires their overturn."[65] "We defer to the trial court's fair value determination if it has a 'reasonable basis in the record and in accepted financial principles relevant to determining the value of corporations and their stock.' "[66]

III. ANALYSIS

Under 8 *Del. C.* § 262(a), a dissenting stockholder to a merger "shall be entitled to an appraisal by the Court of Chancery of the fair value of the stockholder's shares of stock." In an appraisal proceeding, the Court of Chancery must "determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, ... to be paid upon the amount determined to be the fair value."[67] "To reach this per-share valuation, the court should first envisage the entire pre-merger company as a 'going concern,' as a standalone entity, and assess its value [on the closing date of the merger] as such."[68] "Then, once this total standalone value is determined, the court awards each petitioning stockholder his pro rata portion of this total—his proportionate interest in [the] going concern plus interest."[69]

When determining a company's fair value in an appraisal, "the Court shall take into account all relevant factors."[70] Although "[t]he value of a corporation is not a point on a line, but [instead] a range of reasonable values," the court must "assign one particular value within this range as the most reasonable value in light of all the relevant evidence and based on considerations of fairness."[71] "In discharging its statutory mandate, the Court of Chancery has discretion to select one of the parties' valuation models as its general framework or to fashion its own."[72] But, "[i]n the end, the trial judge must determine fair value, and 'fair value is just that, "fair." It does not mean the highest possible price that a company might have sold for.' "[73]

A. The Court of Chancery Did Not Abuse its Discretion when it Held that the Deal Price was the Best Evidence of Stillwater's Fair Value

***5** Petitioners first argue that "[t]he court below erroneously concluded that the flawed sale[ ] process was sufficient to defer completely to merger price."[74] Petitioners allege that instead of analyzing the actual merger process in accordance with this Court's precedent, the Court of Chancery "constructed a made-up deal process—involving only a single bidder—to speculate that if this Court would defer completely to merger price in that (more extreme) scenario, it would likely uphold a merger-price determination here, despite the significant process deficiencies."[75] Thus, Petitioners contend that the Court of Chancery disregarded "the facts of this case" and "failed to analyze the sale[ ] process for Stillwater to determine whether it provided reliable evidence of third-party market valuation."[76]

Here, contrary to Petitioners' representations, the Court of Chancery examined Stillwater's sale process, explained its reasoning, and grounded its conclusions in the relevant facts and law. The court dedicated 56 pages of its 139-page decision to examining the reliability of the deal price. The court walked through each step of the sale process, found that there were objective indicia of reliability, and addressed each of Petitioners' arguments concerning alleged defects in the pre- and post-signing phases. After conducting this analysis, the court held that although Stillwater's sale was "rough and ready," "given the arm's-length nature of the Merger, the premium over market, and the substance of what took place during the sale process, it is not possible to say that an award at the deal price would result in the petitioners being exploited."[77] This Court cannot hold that the Court of Chancery abused its discretion in reaching this conclusion based on the record before us.

1. The Court of Chancery determined that the sale process provided objective indicia of reliability

This Court has recently examined instances when sale processes provided persuasive evidence of fair value. In *DFC*, *Dell*, and *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*,[78] this Court looked to objective factors that bolstered the reliability of the sale process and gave considerable weight to the deal price. In *DFC*, this Court considered a sale process where

> i) the transaction resulted from a robust market search that lasted approximately two years in which financial and strategic buyers had an open opportunity to buy without inhibition of deal protections; ii) the company was purchased by a third party in an arm's length sale; and iii) there was no hint of self-interest that compromised the market check.[79]

This Court concluded that "the best evidence of fair value was the deal price, as it resulted from an open process, informed by robust public information, and easy access to deeper, non-public information, in which many parties with an incentive to make a profit had a chance to bid."[80] In so holding, this Court noted that the

> refusal to craft a statutory presumption in favor of the deal price when certain conditions pertain does not in any way signal [this Court's] ignorance to the economic reality that the sale value resulting from a robust market check will often be the most reliable evidence of fair value, and that second-guessing the value arrived upon by the collective views of many sophisticated parties with a real stake in the matter is hazardous.[81]

Likewise, in *Dell*, this Court determined that the deal price deserved deference when "Dell's sale process bore many of the same objective indicia of reliability" present in *DFC*.[82] Specifically, this Court reasoned that

> when the evidence of market efficiency, fair play, low barriers to entry, outreach to all logical buyers, and the chance for any topping bidder to have the support of Mr. Dell's own votes is so compelling, then failure to give the resulting price heavy weight ... abuses even the wide discretion afforded the Court of Chancery in these difficult cases.[83]

***6** Thus, this Court in *Dell* held that, due to the objective indicia of reliability, "the deal price deserved heavy, if not dispositive, weight." [84]

Finally, in *Aruba* this Court noted "the long history of giving important weight to market-tested deal prices in the Court of Chancery and this Court" [85] and underscored that "a buyer in possession of material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller when agreeing to buy the company at a particular deal price." [86] The Court concluded that the buyer's "view of value should be given considerable weight by the Court of Chancery absent deficiencies in the deal process" because the buyer had access to nonpublic information and was able and incentivized to properly value the target. [87]

Using the above decisions as guidance, the Court of Chancery examined Stillwater's sale process and determined that it also presented " 'objective indicia' that 'suggest[ed] that the deal price was a fair price.' " [88] The court highlighted five key objective indicators that supported the reliability of Stillwater's sale process: (1) "the Merger was an arm's length transaction with a third party"; (2) "the Board did not labor under any conflicts of interest"; (3) the buyer "conducted due diligence and received confidential information about Stillwater's value"; (4) Stillwater "negotiated ... multiple price increases"; and (5) "no bidders emerged during the post-signing phase." [89] This Court has held that each of these indicators reflected a trustworthy process when evaluating the sale processes in *DFC*, *Dell*, and *Aruba*. [90] Although these indicators are fewer indicia of fairness than this Court identified when reviewing the sale processes in *DFC*, *Dell*, or *Aruba*, the court did not abuse its discretion by determining that "the objective indicia that were present provide a cogent foundation for relying on the deal price as a persuasive indicator of fair value." [91]

2. The Court of Chancery considered and rejected Petitioners' objections to the pre-signing process

***7** Having identified the objective signs that the deal price was a reliable indicator of fair value, the Court of Chancery also addressed and rejected each of Petitioners' several arguments for why the pre-signing process undermined that reliability. [92]

First, the court considered Petitioners' claim that McMullen's role in the pre-signing process and the Board's lack of "meaningful oversight" during that period sullied the reliability of the sale process. [93] The court acknowledged that aspects of the process, including McMullen's early unsupervised activities and the lack of Board involvement until later in the sale discussions, presented "flaws." [94] It held, however, that "[t]hose flaws are factors to consider, but they do not undermine the reliability of the sale price" because BAML's pre-signing canvas, the repeated rejections of Sibanye's offers, and an effective post-signing market check ensured a sufficient degree of reliability. [95] Therefore, the suboptimal executive and board involvement early on did "not inherently disqualify the sale process from generating reliable evidence of fair value." [96]

Second, the court held that although McMullen's pursuit of the merger "appears to have been motivated by his desire to maximize his personal wealth and retire," those personal interests did not undermine the sale process. [97] Instead, the court determined that McMullen's financial and personal interests were aligned with stockholders' desire to maximize the company's value. [98] And "[w]hen Sibanye indicated interest at $15.75 per share in July 2016, McMullen did not rush to sign up a deal[,]" evidencing his commitment to extract the highest possible price for the company. [99] Further, the court noted that "McMullen's personal interests as a whole do not appear materially different from interests that have not been sufficient in other cases to undermine the reliability of sale processes." [100] Thus, McMullen's personal interests did not lead him or the Board "to accept a deal price that left a portion of Stillwater's fundamental value on the table, particularly in light of the effective post-signing market check that Stillwater conducted." [101]

Third, the court analyzed Stillwater's initial "soft sell" approach and BAML's pre-signing market check. The court determined that although "the 'soft sell' strategy was not an effective means of generating interest in the Company," it "did not do anything to harm either BAML's abbreviated pre-signing process or the post-signing market check." [102] BAML reached out to fourteen parties once it was retained, and seven parties engaged to some degree in the process. [103]

While Petitioners "have criticized the timing, pacing, and scope of the pre-signing process, ... it resulted in BAML contacting the 'logical strategic buyers' before Stillwater signed up its deal with Sibanye."[104] Further, "[t]he number of meaningful contacts compares favorably with or is similar to the facts in the Delaware Supreme Court precedents."[105] Thus, while the "abbreviated pre-signing process was not ideal," the court concluded that it was still "a positive factor for the reliability of the sale process."[106]

***8** Fourth, and finally, the court rejected Petitioners' argument that "Sibanye pressured Stillwater to sign a merger agreement before the company's rising stock price made what Sibanye was willing to pay look inadequate."[107] Sibanye conducted due diligence before signing, received access to material non-public information, and was uniquely incentivized to value Stillwater properly. When Sibanye made its final offer of $18 per share, it "could have deployed cash on hand or drawn on its revolving line of credit" to increase that offer if its own valuation supported such an increase; it did not.[108] "That Sibanye did not bid higher does not mean that the price it agreed to pay did not reflect fair value when its bid prevailed."[109] Moreover, Stillwater twice rejected Sibanye's lower offers before accepting a deal for $18 per share. As such, the court held that "[t]he negotiations between Stillwater and Sibanye over price, together with Sibanye's refusal to pay more, provide[ ] strong evidence of fair value."[110]

Thus, the court considered each of Petitioners' arguments concerning the pre-signing process. This Court is satisfied that the Court of Chancery did not abuse its discretion when it held that the pre-signing process was sufficient to support reliance on the deal price as evidence of fair value.

3. The Court of Chancery considered and rejected Petitioners' objections to the post-signing process

The Court of Chancery also considered Petitioners' "relatively few" claims challenging the terms of the Merger Agreement and the Board's decisions during the post-signing period.[111]

Because the market price of palladium increased between signing and closing, Petitioners complained that "the Merger Agreement 'provided no practical way for Stillwater's stockholders to receive that additional value.' "[112] But the Court of Chancery dismissed those arguments as contradictory to the terms of the contract itself. According to the court, the Merger Agreement was not designed "to give the stockholders the benefit of a transaction that included the potential upside or downside that would result from changes in the price of palladium after signing. The Merger Agreement was trying to provide stockholders with the ability to opt for the comparative certainty of deal consideration equal to $18.00 per share."[113] Moreover, the court held that the challenge to the Merger Agreement failed because Stillwater's stockholders were not wholly barred from capitalizing on rising palladium prices; as a practical matter, "[i]f Stillwater's stockholders had wanted to capture the increased value of palladium, then they could have voted down the Merger and kept their shares."[114]

The court also rejected Petitioners' argument that the no solicitation provision and matching rights "deterred interested buyers from making a topping bid."[115] The court compared the deal protections here to the "similar suite of deal protections" in *Aruba* and held that, as in *Aruba* and other cases, these protections "did not preclude or impermissibly impede a post-signing market check."[116] Potential bidders had 138 days to submit a competing bid. "The absence of a higher bid indicates 'that the deal market was already robust and that a topping bid involved a serious risk of overpayment,' which in turn 'suggests the price is already at a level that is fair.' "[117]

Last, the Court of Chancery addressed Petitioners' argument that "the stockholders approved the Merger based on incomplete and misleading information."[118] The court noted that "[t]he disclosure theories about McMullen and Wadman would likely have some merit if the petitioners had done more to articulate them, support them with case law, and explain their relationship to a determination of fair value."[119] Despite the cursory nature of the allegations, the court acknowledged that "the proxy statement should have disclosed McMullen's interest in retiring, his roles with GT Gold and New Chris, and their implications for his employment agreement. Stockholders also should have been told that Wadman resigned because of disputes with senior management about the conduct of the sale process."[120] But, the court was not convinced that Petitioners' arguments were "sufficient to undermine the stockholder vote as an expression of the preference of a supermajority of Stillwater's stockholders for a sale rather than having the Company continue as a standalone entity."[121] Although the disclosures might have "affected stockholders' views about whether their negotiators had extracted the highest possible bid," there would not have been "any reason to revise their assessment of the Company's prospects as a standalone entity or to vote down the Merger in the belief that the Company was more valuable as a going concern in its operative reality as a widely held, publicly traded firm."[122] Nonetheless, the court did "not give heavy weight to the stockholder vote" because of the disclosure issues.[123]

***9** As with the pre-signing arguments, after analyzing and addressing all of Petitioners' post-signing process challenges, the court concluded that "Sibanye proved by a preponderance of the evidence that the sale process made the deal price a persuasive indicator of fair value. The sale process was not perfect, and the petitioners highlighted its flaws, but the facts of this case, when viewed as a whole, compare favorably" with this Court's precedents.[124] On review, given the record before the Court of Chancery, we hold that the court did not abuse its discretion in so holding.

4. The Court of Chancery properly based its deal price analysis on the sale process, not on its single-bidder hypothetical

Petitioners do not meaningfully challenge any of the Court of Chancery's specific holdings regarding the objective indicia of reliability. Nor do they meaningfully dispute the court's treatment of any of the specific arguments concerning the pre- and post-signing phases. Instead, Petitioners assert that "[t]he court below failed to analyze the sale[ ] process" because it "analyzed a hypothetical 'single-bidder' process."[125]

When addressing Petitioners' arguments concerning the lack of outreach to other buyers during the pre-signing phase, the Court of Chancery entertained the question of whether "the deal price [would] provide persuasive evidence of fair value if Stillwater had pursued a single-bidder strategy in which it only interacted with Sibanye before signing the Merger Agreement ...."[126] The court stated that it believed that "if the proponent of a single-bidder process could show that the merger agreement allowed for a passive post-signing market check in line with what decisions have held is sufficient to satisfy enhanced scrutiny, and if there were no other factors that undermined the sale process, then the deal price would provide persuasive evidence of fair value."[127]

But, contrary to Petitioners' allegations, the court did not ignore the facts pertinent to the actual process. As this Court described above, the Court of Chancery reviewed each step of the sale process before concluding that the deal price was reliable. The entirety of the court's single-bidder discussion encompasses a small portion of its lengthy analysis. Moreover, the court recognized that its analysis was hypothetical and emphasized that it "already found that the sale process exhibited objective indicia of reliability" without relying on the hypothetical.[128] As a result, that portion of the court's analysis was not necessary to its decision, does not alter its holding in this case, and is not being considered on appeal.

"What is necessary in any particular case ... is for the Court of Chancery to explain its [analysis] in a manner that is grounded in the record before it."[129] Here, the Court of Chancery thoroughly analyzed the facts surrounding Stillwater's sale process in accordance with this Court's precedent. Absent any sign that the court abused its statutory mandate, this Court will not second-guess the court's careful examination of Stillwater's sale process. Therefore, we hold that the Court of Chancery did not abuse its discretion when it held that the deal price was a reliable indicator of Stillwater's fair value.

B. The Court of Chancery Did Not Abuse its Discretion when it Declined to Grant a Deal Price Adjustment

***10** Next, Petitioners argue that the Court of Chancery abused its discretion when it declined to adjust the deal price upward to reflect the rising commodity prices between signing and closing. They argue that "[t]he trial court, while recognizing the undisputed increase in Stillwater's value between signing and closing, refused to award such accretion ...."[130] Moreover, according to Petitioners, the court wholly based its decision to not adjust the deal price on its erroneous conclusion that "Petitioners had not argued for such an adjustment."[131]

"In a statutory appraisal proceeding, both sides have the burden of proving their respective valuation positions ...."[132] Therefore, in an appraisal proceeding, the party seeking an adjustment to the deal price reflecting a valuation change between signing and closing bears the burden to identify that change and prove the amount to be adjusted.[133] The time for determining the value of a dissenter's shares is the date on which the merger closes.[134] Thus, if the value of the corporation changes between the signing of the merger agreement and the closing, then the fair value determination must be measured by the "operative reality" of the corporation at the time of the merger.[135]

A holistic review of the court's analysis suggests that it was unconvinced by Petitioners' conclusory arguments for an adjustment to the deal price and declined to grant the adjustment because Petitioners failed to meet their burden of proof.[136] While Petitioners seize on the court's language that "the petitioners never argued for an adjustment to the deal price,"[137] this reading ignores the court's analysis of numerous difficult considerations that Petitioners failed to adequately address. The court's statement that petitioners did not argue for an adjustment to the deal price may have been inartful, but it appears that the court also considered and rejected the notion of a deal price adjustment based on gaps in Petitioners' arguments.

IV. CONCLUSION

Based on the foregoing, the Court of Chancery's August 21, 2019 Memorandum Opinion and September 27, 2019 Post-Trial Judgment order are AFFIRMED.

All Citations

--- A.3d ----, 2020 WL 6038341

Footnotes

[1] This Court takes the essential facts from the Memorandum Opinion. *In re Stillwater Mining Co.*, 2019 WL 3943851 (Del. Ch. Aug. 21, 2019).

[2] *Id.* at *2.

[3] Appendix to the Opening Br. 425, 1283 (hereafter "A_").

[4] *Stillwater Mining*, 2019 WL 3943851, at *2.

[5] A2439.

[6] A2438-41; A1854-55.

[7] Appendix to the Answering Br. 30-31, 311 (hereafter "B_").

[8] *Stillwater Mining*, 2019 WL 3943851, at *4.

[9] *Id.* at *5.

[10] *Id.*

[11] *Id.*

[12] *Id.*

[13] *Id.*

[14] *Id.* at *5.

[15] *Id.*

[16] *Id.* at *5-6.

[17] *Id.* at *6.

[18] *Id.* at *7; B1088-94.

[19] *Stillwater Mining*, 2019 WL 3943851, at *7; A1856; A2458-59.

[20] *Stillwater Mining*, 2019 WL 3943851, at *7.

[21] *Id.*

[22] *Id.*

[23] *Id.*

[24] *Id.* at *7-8.

[25] *Id.* at *8; B40-41; B1095-96.

[26] *Stillwater Mining*, 2019 WL 3943851, at *8-9.

[27] *Id.* at *9.

[28] *Id.*

[29] *Id.*

[30] *Id.* at *10.

[31] *Id.*

[32] *Id.* at *11-12.

[33] *Id.* at *12.

[34] *Id.* at *13.

[35] *Id.* at *12.

[36] *Id.* at *13.

[37] *Id.* at *13-14.

[38] *Id.* at *14.

[39] *Id.*

[40] *Id.*

[41] *Id.* at *15.

[42] *Id.* at *16.

[43] *Id.* at *15.

[44] *Id.*

[45] *Id.* at *15-16.

[46] *Id.* at *16.

[47] *Id.* at *17.

[48] *Id.*

[49] *Id.*

[50] *Id.*

[51] *Id.*

[52] *Id.* at *17.

[53] *Id.* at *1.

[54] *Id.*

[55] *Id.*

[56] *Id.*

[57] *Id.*

[58] *Id.* at *50.

[59] Opening Br. 38-40.

[60] *Id.* at 26.

[61] Answering Br. 18-20.

[62] *Id.* at 29 (quoting *Stillwater Mining*, 2019 WL 3943851, at *50).

[63] *SmithKline Beecham Pharms. Co. v. Merck & Co.*, 766 A.2d 442, 447 (Del. 2000).

[64] *DFC Glob. Corp. v. Muirfield Value P'rs*, 172 A.3d 346, 363 (Del. 2017).

[65] *Montgomery Cellular Hldg. Co. v. Dobler*, 880 A.2d 206, 219 (Del. 2005).

[66] *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*, 177 A.3d 1, 5-6 (Del. 2017) (quoting *DFC*, 172 A.3d at 348-49).

[67] 8 *Del. C.* § 262(h).

[68] *Dell*, 177 A.3d at 20.

[69] *Id.* at 21 (citations and internal quotation marks omitted).

[70] 8 *Del. C.* § 262(h).

[71] *Cede & Co. v. Technicolor, Inc.*, 2003 WL 23700218, at *2 (Del. Ch. Dec. 31, 2003, revised July 9, 2004), *aff'd in part, rev'd in part on other grounds*, 884 A.2d 26 (Del. 2005).

[72] *M.G. Bancorp., Inc. v. Le Beau*, 737 A.2d 513, 525-26 (Del. 1999).

73 *Fir Tree Value Master Fund, LP v. Jarden Corp.*, 2020 WL 3885166, at *7 (Del. Jul. 9, 2020) (quoting *DFC*, 172 A.3d at 370) (citing *Dell*, 177 A.3d at 20).

74 Opening Br. 5.

75 *Id.* at 37.

76 *Id.*

77 *Stillwater Mining*, 2019 WL 3943851, at *44.

78 210 A.3d 128, 135 (Del. 2019).

79 172 A.3d at 349.

80 *Id.*

81 *Id.* at 366.

82 *Dell*, 177 A.3d at 28.

83 *Id.* at 35.

84 *Id.* at 23.

85 *Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc.*, 210 A.3d 128, 135 (Del. 2019); *see also id.* at 135 n.41 (collecting cases).

86 *Id.* at 137.

87 *Id.*

88 *Stillwater Mining*, 2019 WL 3943851, at *22 (quoting *Dell*, 177 A.3d at 28).

89 *Id.* at *22-23.

90 *See, e.g.*, *DFC*, 172 A.3d at 349 (noting as persuasive that "the company was purchased by a third party in an arm's length sale"); *Dell*, 177 A.3d at 28 (crediting the deal price because the special committee was "composed of independent, experienced directors and armed with the power to say 'no' " and the special committee "persuaded Silver Lake to raise its bid six times"); *id.* at 33 (finding that absence of higher bid meant "that the deal market was already robust and that a topping bid involved a serious risk of overpayment," which "suggests the price is already at a level that is fair"); *Aruba*, 210 A.3d at 137 (emphasizing that the buyer was armed with "material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller").

91 *Stillwater Mining*, 2019 WL 3943851, at *23.

92 *Id.* at *23-44.

93 *Id.* at *30-34.

94 *Id.* at *31.

95 *Id.* at *44.

96 *Id.* at *31.

97 *Id.* at *33.

98 *Id.* at *34.

99 *Id.*

100 *Id.* Specifically, the Court of Chancery compared McMullen's potential conflicts with disputed conflicts addressed by this Court's decisions in *Aruba*, 210 A.3d at 141-42, and *Dell*, 177 A.3d at 32-34. *Stillwater Mining*, 2019 WL 3943851, at *33.

101 *Stillwater Mining*, 2019 WL 3943851, at *34.

102 *Id.*

103 *Id.* at *35.

104 *Id.* (quoting *Aruba*, 210 A.3d at 136).

105 *Id.* (citing *Aruba*, 210 A.3d at 136-39, 142; *Dell*, 177 A.3d at 28; *DFC*, 172 A.3d at 350, 355, 376).

106 *Id.* at *36.

107 *Id.* at *36, *36-38.

108 *Id.* at *38.

109 *Id.*

110 *Id.*

111 *Id.* at *38.

112 *Id.*

113 *Id.* at *39.

114 *Id.*

115 *Id.*

116 *Id.* at *41.

117 *Id.* at *42 (quoting *Dell*, 177 A.3d at 33).

118 *Id.*

119 *Id.* at *43.

120 *Id.*

121 *Id.*

122 *Id.*

123 *Id.*

124 *Id.* at *44.

125 Opening Br. 37.

126 *Stillwater Mining*, 2019 WL 3943851, at *24.

127 *Id.* at *30.

128 *Id.* The court also clarified "I am not suggesting that the Delaware Supreme Court has ever endorsed a single-bidder process for purposes of appraisal, nor that any of the precedents that this decision has discussed are squarely on point. Nor am I claiming to have any privileged insight into how the Delaware Supreme Court would or should evaluate the persuasiveness of a single-bidder strategy on the facts of any particular case." *Id.*

129 *DFC*, 172 A.3d at 388.

130 Opening Br. 24.

131 *Id.*

132 *M.G. Bancorp., Inc. v. Le Beau*, 737 A.2d 513, 520 (Del. 1999).

133 *See In re Appraisal of Columbia Pipeline Gp.*, 2019 WL 3778370, at *45 (Del. Ch. Aug. 12, 2019) ("The petitioners contend that Columbia's value increased during this period. As the party arguing for an upward adjustment to the deal price, the petitioners bore the burden of proof on this issue.").

134 *Cede & Co. v. Technicolor, Inc.*, 684 A.2d 289, 298 (Del. 1996).

135 *Id.*

136 *Stillwater Mining*, 2019 WL 3943851, at *48.

137 *Id.*

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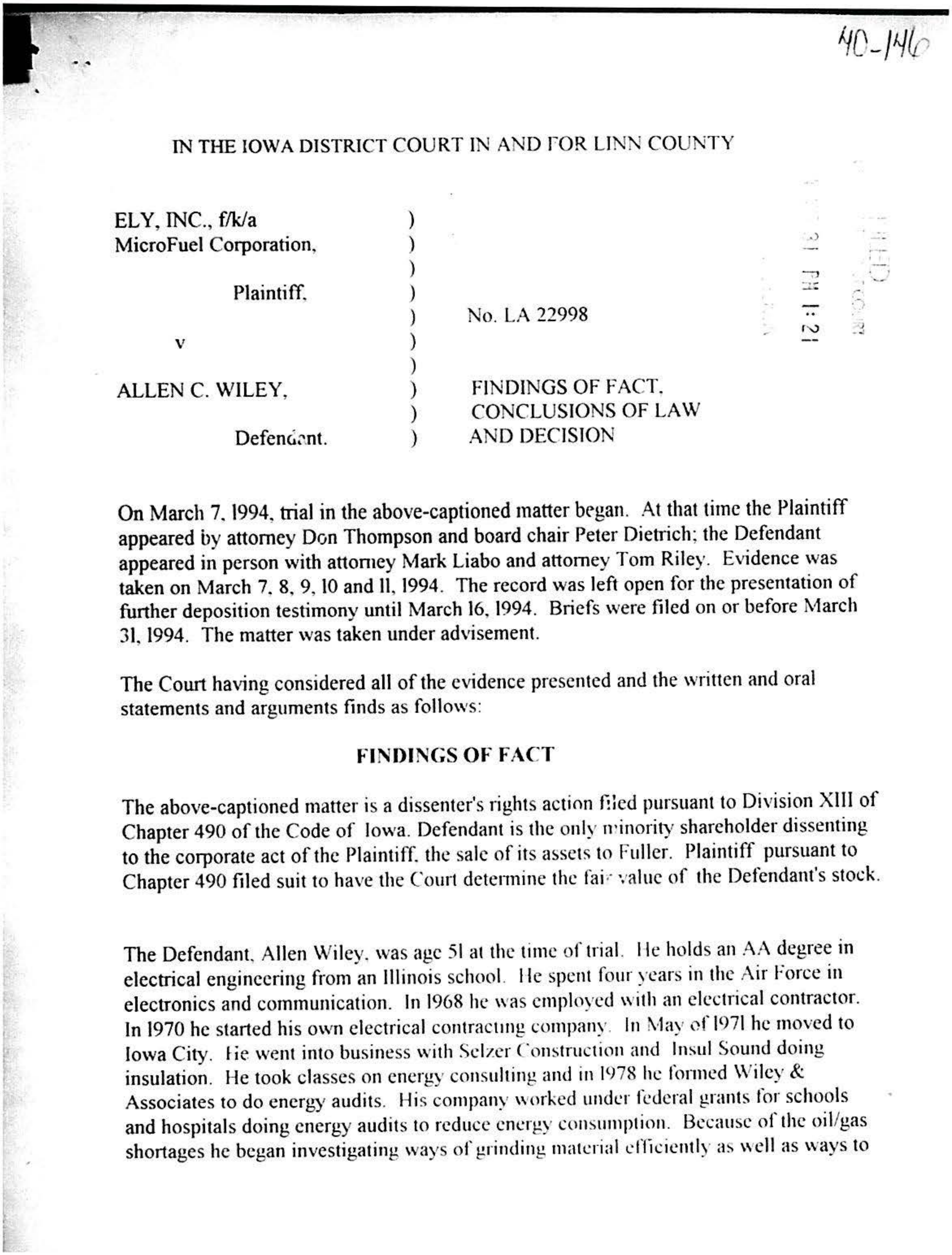

40-146

IN THE IOWA DISTRICT COURT IN AND FOR LINN COUNTY

FILED
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ELY, INC., f/k/a MicroFuel Corporation,	)	
	)	
Plaintiff.	)	
	)	No. LA 22998
v	)	
	)	
ALLEN C. WILEY,	)	FINDINGS OF FACT,
	)	CONCLUSIONS OF LAW
Defendant.	)	AND DECISION

On March 7, 1994, trial in the above-captioned matter began. At that time the Plaintiff appeared by attorney Don Thompson and board chair Peter Dietrich; the Defendant appeared in person with attorney Mark Liabo and attorney Tom Riley. Evidence was taken on March 7, 8, 9, 10 and 11, 1994. The record was left open for the presentation of further deposition testimony until March 16, 1994. Briefs were filed on or before March 31, 1994. The matter was taken under advisement.

The Court having considered all of the evidence presented and the written and oral statements and arguments finds as follows:

FINDINGS OF FACT

The above-captioned matter is a dissenter's rights action filed pursuant to Division XIII of Chapter 490 of the Code of Iowa. Defendant is the only minority shareholder dissenting to the corporate act of the Plaintiff, the sale of its assets to Fuller. Plaintiff pursuant to Chapter 490 filed suit to have the Court determine the fair value of the Defendant's stock.

The Defendant, Allen Wiley, was age 51 at the time of trial. He holds an AA degree in electrical engineering from an Illinois school. He spent four years in the Air Force in electronics and communication. In 1968 he was employed with an electrical contractor. In 1970 he started his own electrical contracting company. In May of 1971 he moved to Iowa City. He went into business with Selzer Construction and Insul Sound doing insulation. He took classes on energy consulting and in 1978 he formed Wiley & Associates to do energy audits. His company worked under federal grants for schools and hospitals doing energy audits to reduce energy consumption. Because of the oil/gas shortages he began investigating ways of grinding material efficiently as well as ways to

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convert oil and gas burners back to coal burners. His thought was to use micronized coal. The concept of micronized coal was known but fairly new. He had learned of the TAS Company, which was using the process. Micronized coal reduces the particulates (ash) as well as reduces the size of the ash. It burns almost totally with little carbon and cools off better. Micronized coal has the composition of talcum powder.

He analyzed various milling devices: the hammer mill which uses attrition, the mortar and pestle or roller mills, and the fluid energy mills which cause material to be fired at one another with steam or compressed air. Each of these had an advantage or a disadvantage. The mortar and pestle being the most common was a simple application but it was difficult to get the particles small enough to become micronized and also the fines could build up between the rollers. With the hammer mills the erosion rate was too high. The fluid energy was a good concept but it was too costly.

Mr. Wiley concluded that if one could create fluid energy by mechanical means, it might become economically viable. His thought was to create fluid energy by using specific waves of air to collide the particles. He developed a drawing of a MicroMill using the fluid energy method and in January of 1986 applied for patents. In May of 1990 he obtained four U.S. patents: one for the method and three for the apparatus including shapes of blades, the rotational impact zone and air waves. His MicroMill would vacuum the air and the material into the mill in no more than a four-inch lump size. The lumps would rotate creating a tornado. The air flow would move up toward the impeller. The chunks would be thrown into the rotational impact zone and be crushed into smaller bands of material. Centrifugal force keeps the particulars in the mill until they are small enough to be shot out.

In order to obtain the patents, he had to demonstrate that the grinding actually took place in the rotational impact or ris zone. When the particulates are small enough they are caught in an air stream and exhausted out into a classifier, a horizontal cyclone where they would be classified. If they were too large, the particulates would go back into the MicroMill for further micronization. If they were small enough, they would go into the furnace. His first idea was to use the mill for micronizing coal; however, there were other possible applications, such as grinding limestone or sorbent or grinding grain. He thought it could be used in the utility industry as well as industry, for example, at an asphalt plant micronized coal could be used as fuel in an aggregate dryer.

In 1985 he put together a group of investors. Oil prices were high and people were looking for a way to go back to using coal more efficiently with less emissions. He sold 80 percent of the stock in the company in January of 1986 to Nebraska Boilers/National Dynamics. The demonstration facility was built in Lincoln, Nebraska. A complete system was sold to an asphalt plant in Illinois. When the price of oil fell, National

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Dynamics lost interest in the technology and the Defendant purchased the company back in May of 1987. In order to complete the purchase he needed to raise funds. He was to pay 1 million dollars for the company and had six months to raise the money. He knew that large coal-fired utilities consume lots of oil because some substance is needed that will flame immediately to ignite the burners. However, the drawback to oil is that it leaves a film on the external surfaces of a furnace and it smokes. He theorized micronized coal, although you would still need a gas gun to ignite it, would provide a quicker startup and a lower turndown. In other words, he thought that MicroMills would keep furnaces in utilities on ready reserve. So in order to raise funds he contacted various utilities and venture capital firms. He eventually formed MicroFuel Corporation in June of 1987. The original investors were IES Energy, Inc., Midwest Services (Iowa Public Service), and Arete. Wiley stayed in as a minority shareholder owning approximately 12 percent of the stock. This provided funds to buy out National Dynamics.

It become obvious that a larger mill was needed for larger furnaces. There were two big technical issues to be addressed: the impeller needed to be redesigned for replaceable blades and the bearing frame needed to be redesigned. In 1989, 1990 and early 1991 little progress was made on upsizing the mill. Technically the bearing issue was still not solved, so during that period of time money was being put into the company by the investors with no money coming in. By the end of 1991 the bearing frame had been redesigned, the problem solved and the impeller problem had been solved except for the material of the blades.

In October of 1991 one unit was sold to Clyde Carruthers in Australia. In 1991 more stock was sold to IES for 25 cents per share. In July of 1989 they had paid 50 cents per share, and then 1 dollar per share. In the summer of 1991 IES loaned the company up to $600,000 on a line of credit. It was only drawn down to $350,000. Also in 1991 MicroFuel (hereinafter referred to as MFC) was having discussions with the Tennessee Valley Authority (hereinafter referred to as TVA) about the Clean Coal IV Project. As a result of the Federal Clean Air Act certain monies were available through the Department of Energy (DOE) under the Clean Coal IV Project for the development and demonstration of technologies which could utilize coal but still meet the emissions standards for NOx set out in Clean Air Act. The Clean Air Act required phase I companies to meet the emissions standards by January of 1995 and phase II companies to meet the standards by the year 2000. Thus, the utility industry and the TVA in particular were investigating various ways to convert their boilers and furnaces to meet the emissions standards. They became interested in the MicroMill technology and micronized coal and through 1991 and 1992 were involved in discussions with the company (MFC) about demonstration projects and investments.

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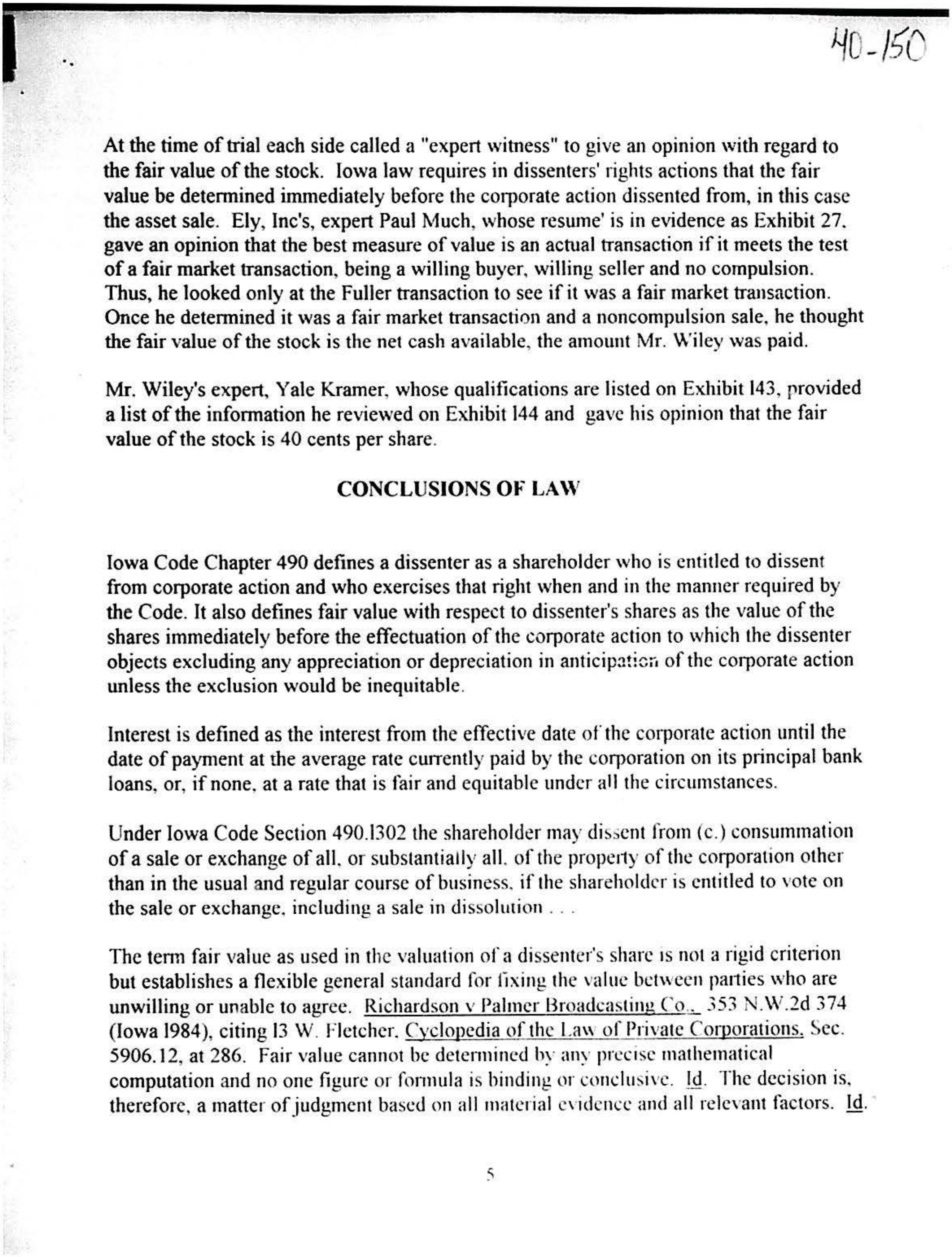
Also during the 1991-92 period MFC's board of directors, in particular IES representative Peter Dietrich, began to search for additional investors and/or strategic partners. They were attempting to find a company with similar product lines and market capabilities, as well as some strength and money, things the current investors did not have available. As of August of 1991 it was costing about $50,000 a month to keep the company operational and it really had no cash or income. The current stockholders were polled and stock was offered at 25 cents a share but no one came forward. A conventional lender was not available either. Thus, the prospect in August of 1991 for other monies from other sources appeared to be zero. IES agreed to loan the company the dollars indicated above. All of the assets of the corporation were pledged on the note and the due date of the note was April 1 of 1992. An audit as of December 31 of 1991 of MicroFuel listed a cash balance of $49,096 and shareholders' equity of $19,627. They had lost most of the equity during the preceding year.

According to Mr. Deitrich's testimony, by the end of 1991 the MFC company had lost $2,841,000. Eventually it appeared that Fuller Corporation was interested in purchasing the company. Fuller Corporation is a wholly owned United States subsidiary of Smidth Manufacturing out of Denmark. It manufactures and markets equipment to various industries, including the utility industry. They had grinding products that they were already selling to utilities and had research capabilities. Eventually a firm offer was made by Fuller to purchase all of the assets of MicroFuel. The Defendant, through his company Wiley & Associates, attempted to match that offer or make a better offer. Both offers were presented to the shareholders without a recommendation and on September 2 of 1992 at the meeting of the shareholders the Fuller deal was accepted with Mr. Wiley dissenting and one other shareholder abstaining. The essential terms of the deal are attached to Exhibit 3 as Exhibit A. Basically Fuller would make a $750,000 down payment which would first go to pay off liabilities and then be distributed between the shareholders. There was also the possibility of royalties over a period of seven years based on sales of units, with a maximum royalties of $6.5 million.

Based on the sale, by a majority, board of directors of Ely, Inc., determined the fair value of Defendant Wiley's shares in the corporation by a written unanimous consent effective December 1, 1992, to be "... the amount of cash currently available for distribution to Mr. Wiley in proportion to his shares, 12 percent of the outstanding shares of the corporation, the sum of $24,000 (estimated fair value)." They further determined the applicable percentage rate to be 3 percent from and after September 4 of 1992 and that Mr. Wiley shall be entitled to future distributions of any royalties paid by Fuller during the contract period in proportion to his shareholdings by assignment of 12 percent of the royalty payment to the corporation under the contract. The Defendant was paid $24,200 for the fair value of his stock plus interest. It is that amount he dissents from. Given those figures he was paid approximately 2.5 cents per share.



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At the time of trial each side called a "expert witness" to give an opinion with regard to the fair value of the stock. Iowa law requires in dissenters' rights actions that the fair value be determined immediately before the corporate action dissented from, in this case the asset sale. Ely, Inc's, expert Paul Much, whose resume' is in evidence as Exhibit 27. gave an opinion that the best measure of value is an actual transaction if it meets the test of a fair market transaction, being a willing buyer, willing seller and no compulsion. Thus, he looked only at the Fuller transaction to see if it was a fair market transaction. Once he determined it was a fair market transaction and a noncompulsion sale, he thought the fair value of the stock is the net cash available, the amount Mr. Wiley was paid.

Mr. Wiley's expert, Yale Kramer, whose qualifications are listed on Exhibit 143, provided a list of the information he reviewed on Exhibit 144 and gave his opinion that the fair value of the stock is 40 cents per share.

CONCLUSIONS OF LAW

Iowa Code Chapter 490 defines a dissenter as a shareholder who is entitled to dissent from corporate action and who exercises that right when and in the manner required by the Code. It also defines fair value with respect to dissenter's shares as the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects excluding any appreciation or depreciation in anticipation of the corporate action unless the exclusion would be inequitable.

Interest is defined as the interest from the effective date of the corporate action until the date of payment at the average rate currently paid by the corporation on its principal bank loans, or, if none, at a rate that is fair and equitable under all the circumstances.

Under Iowa Code Section 490.1302 the shareholder may dissent from (c.) consummation of a sale or exchange of all, or substantially all, of the property of the corporation other than in the usual and regular course of business, if the shareholder is entitled to vote on the sale or exchange, including a sale in dissolution . . .

The term fair value as used in the valuation of a dissenter's share is not a rigid criterion but establishes a flexible general standard for fixing the value between parties who are unwilling or unable to agree. Richardson v Palmer Broadcasting Co., 353 N.W.2d 374 (Iowa 1984), citing 13 W. Fletcher, Cyclopedia of the Law of Private Corporations, Sec. 5906.12, at 286. Fair value cannot be determined by any precise mathematical computation and no one figure or formula is binding or conclusive. Id. The decision is, therefore, a matter of judgment based on all material evidence and all relevant factors. Id.

Courts must take into consideration all factors and elements which reasonably might enter into the fixing of value. Thus, market value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or could be ascertained . . . and which throw any light on future prospects . . . must be considered . . . Litton Industries v Lehman Bros. Kuhn Loeb, Inc., 709 F. Supp. 438 (SDNY 1989).

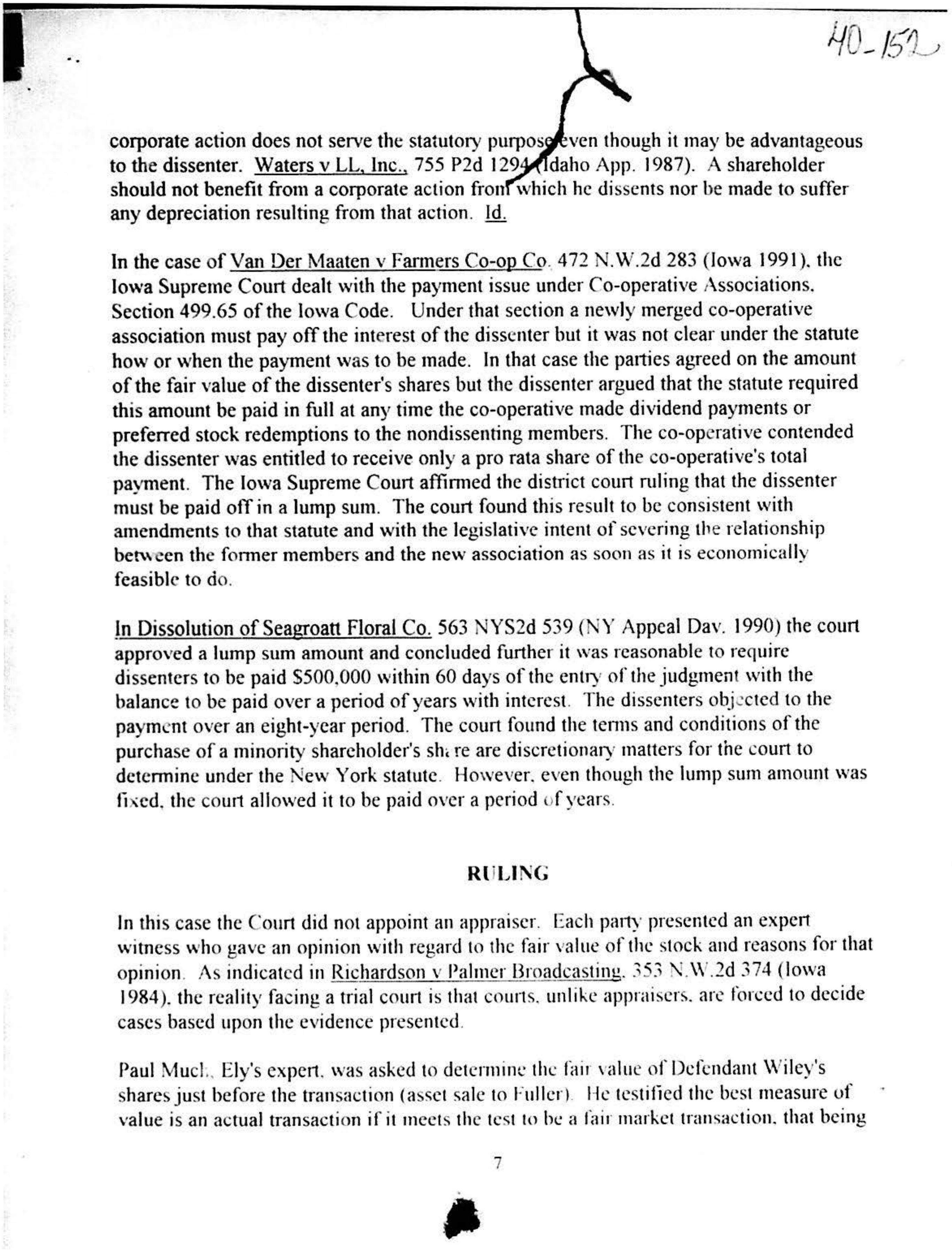
Three factors which are discussed most often in determining fair value include:
1. Market value which is the amount that stock would be sold between a willing seller and a willing buyer, 2. Net asset value which is defined as the share which the stock represents and the value of the net assets of the corporation, and 3. Investment value which is the present value of the anticipated future earnings of a business considered as a going concern. See Woodward v Quigley, 133 N.W.2d 38 (Iowa 1965) and 18A AmJur 2d Corporations, Sec. 846 (1985).

The Iowa Supreme Court has stated that all three approaches to valuation should be viewed as relevant factors to be considered rather than as essential components. Richardson, 353 N.W.2d at 378. It is unwise to attempt to state every factor that may bear on the value of stock in a particular case. The underlying theory is one of compensating the owner of stock for his property rights and no one method of valuation should be relied on exclusively.

Courts must decide cases based upon the evidence presented. Parties to a "fair value" case may be unable to find witnesses whose testimony will correspond to each recognized element of fair value. Further, testimony as to any particular element may appear to the court to be so unreliable that it has no place in influencing the final result. Trial courts may reject valuation techniques that are not supported by the evidence, but they should look to valuation techniques that are easy to understand and provide a reliable guide to value. Value is always determined as of a specific date and is based upon all pertinent facts and conditions which were either known or reasonably anticipated on that date. Sieg Co. v Kelly, 512 N.W.2d 275 (Iowa 1994).

Iowa Code Section 490.1330(5)(a) provides that each dissenter is entitled to a judgment for the amount, if any, by which the court finds the fair value of the dissenter's shares, plus interest, exceeds the amount paid by the corporation, but it does not specify provisions as to time and method of payment to the dissenter.

The dissenter's rights statute requires fair value be determined immediately before the corporate action to which the dissenter objects. A contract provision which gives the dissenter the value of his shares at some point subsequent to the effective date of the



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corporate action does not serve the statutory purpose even though it may be advantageous to the dissenter. Waters v LL, Inc., 755 P2d 1294 (Idaho App. 1987). A shareholder should not benefit from a corporate action from which he dissents nor be made to suffer any depreciation resulting from that action. Id.

In the case of Van Der Maaten v Farmers Co-op Co. 472 N.W.2d 283 (Iowa 1991), the Iowa Supreme Court dealt with the payment issue under Co-operative Associations, Section 499.65 of the Iowa Code. Under that section a newly merged co-operative association must pay off the interest of the dissenter but it was not clear under the statute how or when the payment was to be made. In that case the parties agreed on the amount of the fair value of the dissenter's shares but the dissenter argued that the statute required this amount be paid in full at any time the co-operative made dividend payments or preferred stock redemptions to the nondissenting members. The co-operative contended the dissenter was entitled to receive only a pro rata share of the co-operative's total payment. The Iowa Supreme Court affirmed the district court ruling that the dissenter must be paid off in a lump sum. The court found this result to be consistent with amendments to that statute and with the legislative intent of severing the relationship between the former members and the new association as soon as it is economically feasible to do.

In Dissolution of Seagroatt Floral Co. 563 NYS2d 539 (NY Appeal Dav. 1990) the court approved a lump sum amount and concluded further it was reasonable to require dissenters to be paid $500,000 within 60 days of the entry of the judgment with the balance to be paid over a period of years with interest. The dissenters objected to the payment over an eight-year period. The court found the terms and conditions of the purchase of a minority shareholder's share are discretionary matters for the court to determine under the New York statute. However, even though the lump sum amount was fixed, the court allowed it to be paid over a period of years.

RULING

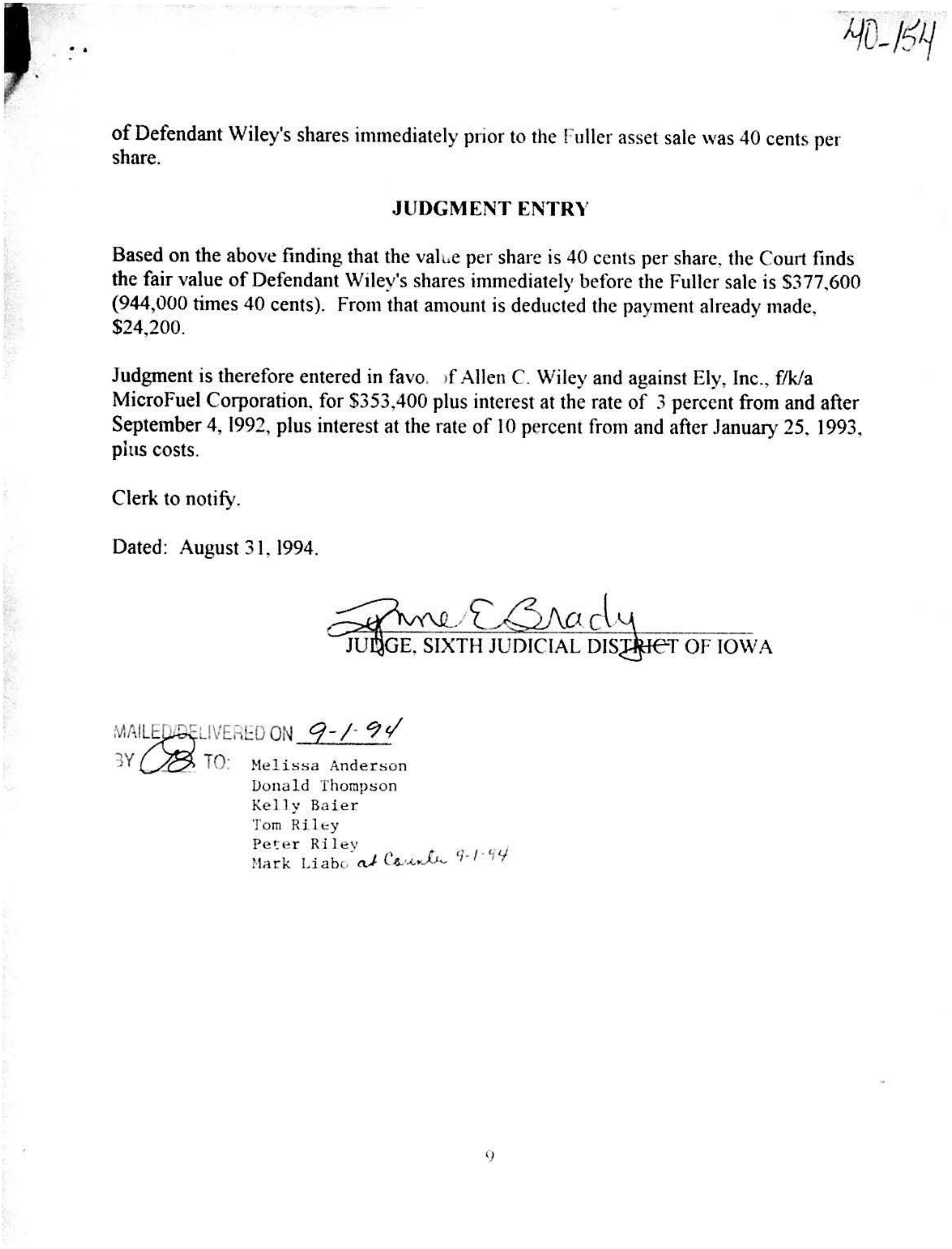
In this case the Court did not appoint an appraiser. Each party presented an expert witness who gave an opinion with regard to the fair value of the stock and reasons for that opinion. As indicated in Richardson v Palmer Broadcasting, 353 N.W.2d 374 (Iowa 1984), the reality facing a trial court is that courts, unlike appraisers, are forced to decide cases based upon the evidence presented.

Paul Much, Ely's expert, was asked to determine the fair value of Defendant Wiley's shares just before the transaction (asset sale to Fuller). He testified the best measure of value is an actual transaction if it meets the test to be a fair market transaction, that being one between a willing buyer and a willing seller and under no compulsion, a. arm's length. He looked at the sale by Ely, Inc., to Fuller to see if it was a fair market transaction. Having determined in his own mind that it was in fact a fair market transaction and a noncompulsion sale, he testified the fair value of Wiley's stock would be the net cash available.

This Court, however, finds Mr. Much's testimony to be unreliable for a couple of reasons. The first and most important is that he was to determine the fair value of the stock before the corporate transaction, yet he used the transaction itself to determine the value. To determine fair value one must basically ignore the corporate transaction since the fair value occurs immediately before said action. In addition, he felt the Fuller sale was not a compulsion sale but evidence from witnesses involved indicates Ely, Inc., was essentially out of money and the note held by IES, the major shareholder, had been called. It appears to the undersigned from the seller's standpoint this really was a compulsion sale. Ely, Inc., had very few options available at the time of the sale.

Regarding Defendant Wiley's expert, Yale Kramer, Exhibit 144 sets out a ten-page listing of evidence, depositions, documents that he reviewed prior to reaching an opinion with regard to fair value. He really did not consider the Fuller transaction itself and opined that fair value does not equal an actual sale. Among things Mr. Kramer considered were the fact the average price per share paid by all of the shareholders was 43 cents; that discussions with Kim's House of Trading from South Korea appeared to support $1.27 per share value as of December of 1990; that in April of 1991 IES valued the stock at 37 cents per share; that the Department of Energy and TVA were supportive of a demonstration of the MicroMill technology during the Clean Coal IV Project; that shares in January of 1992 were offered to Duke Power at a dollar per share; in March of 1992 Ely, Inc.'s chairman of the board Peter Dietrich (also an employee of IES) stated an opinion that MicroFuel was worth between 7 and 9 million dollars; that Mr. Dietrich in July of 1992 prepared a discounted cash flow concluding the share value ranged from 49 cents to 32 cents and, further, in August of 1992 the TVA was willing to provide substantial funds for a percentage of the technology patents and a license agreement. Having reviewed those facts and circumstances and further having considered all of the items set out in Exhibit 144, Mr. Kramer gave his opinion that the fair value of Wiley's stock immediately before the transation was 40 cents per share.

Having found Mr. Much's testimony and opinion cannot be relied on because he based his value only on the transaction itself, not before the transaction, the Court is faced with deciding whether or not Mr. Kramer's valuation is reliable. This Court now finds Mr. Kramer's valuation is reliable and appropriate. He considered all of the evidence and documentation available and he further has the background and expertise to make said valuation. This Court now accepts his valuation and adopts it and hereby finds the value



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of Defendant Wiley's shares immediately prior to the Fuller asset sale was 40 cents per share.

JUDGMENT ENTRY

Based on the above finding that the value per share is 40 cents per share, the Court finds the fair value of Defendant Wiley's shares immediately before the Fuller sale is $377,600 (944,000 times 40 cents). From that amount is deducted the payment already made, $24,200.

Judgment is therefore entered in favo.)f Allen C. Wiley and against Ely, Inc., f/k/a MicroFuel Corporation, for $353,400 plus interest at the rate of 3 percent from and after September 4, 1992, plus interest at the rate of 10 percent from and after January 25, 1993, plus costs.

Clerk to notify.

Dated: August 31, 1994.

Lynne E Brady
JUDGE, SIXTH JUDICIAL DISTRICT OF IOWA

MAILED/DELIVERED ON 9-1-94
BY CB TO: Melissa Anderson
Donald Thompson
Kelly Baier
Tom Riley
Peter Riley
Mark Liabo at Counter 9-1-94

2019 WL 1313408
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UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

FRONTFOUR CAPITAL GROUP LLC, and FrontFour Master Fund, Ltd., on Behalf of Themselves and Similarly Situated Stockholders of Medley Capital Corporation, Plaintiffs,
v.
Brook TAUBE, Seth Taube, Jeff Tonkel, Mark Lerdal, Karin Hirtler-Garvey, John E. Mack, Arthur S. Ainsberg, Medley Management, Inc., Sierra Income Corporation, Medley Capital Corporation, MCC Advisors LLC, Medley Group LLC, and Medley, LLC Defendants.

C.A. No. 2019-0100-KSJM
|
Date Submitted: March 9, 2019
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Date Decided: March 11, 2019
|
Date Revised: March 22, 2019

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MEMORANDUM OPINION

McCORMICK, V.C.

***1** Due to the press of time,[1] aspects of this decision lack polish or extended treatment.

March came in like a lion. Snow flurries and gray overcast covered downtown Wilmington for most of March's early days. The courthouse witnessed another flurry of activity during those days as the plaintiffs, FrontFour Capital Group LLC and FrontFour Master Fund, Ltd. ("FrontFour"), tried their expedited claims to enjoin transactions orchestrated by twin brothers Brook and Seth Taube.

The challenged transactions, which were announced on August 9, 2018, would combine an asset management firm founded and majority owned by the Taube brothers, Medley Management, Inc. ("Medley Management"), with two business development corporations that Medley Management advises, Medley Capital Corporation ("Medley Capital"), and Sierra Income Corporation ("Sierra"). If the transactions proceed, Sierra will acquire first Medley Capital and then Medley Management in two cross-conditioned mergers, with Sierra as the surviving combined entity (the "Proposed Transactions"). Medley Management will receive per share $ 3.44 cash, plus $ .065 in cash dividends, and the right to receive .3836 shares of Sierra stock, which represents a premium of approximately 100% to Medley Management's trading price. The Taube brothers and their management team will receive lucrative employment contracts with the combined company. Medley Capital stockholders, including FrontFour, will receive per share the right to 0.8050 shares of Sierra stock, which provides no premium against Medley Capital's net asset value ("NAV").

The Taube brothers proposed the transactions in late June 2018. They touted size/scale, asset quality, and internalized management resulting from the transactions as beneficial to all of the parties. They set an aggressive timeline to permit announcement of a deal in early August 2018 in connection with the release of second-quarter financials. In response to the proposal, each of the three affiliated entities empowered a special committee to negotiate and, if appropriate, recommend the transaction. It was July 11th before the Medley Capital special committee had retained a financial advisor and was prepared to negotiate, leaving only a few weeks to negotiate under the Taube brothers' timeline. During that time, the Medley Capital special committee negotiated a slightly better exchange ratio, secured the Taube brothers' agreement to waive payments in connection with a valuable tax receivable agreement (“TRA”), and obtained the opinion of an independent compensation expert that the Taube brothers' compensation packets were reasonable. The committee members also secured for themselves the agreement that two of the four of them—to be determined through an interview process following announcement of the Proposed Transactions—would serve on the board of the combined entity.

***2** From a distance, this process appeared arm's-length. The December 2018 proxy recommending that the stockholders approve the Proposed Transactions certainly made it seem that way.

At trial, FrontFour proved otherwise. FrontFour commenced this litigation on February 11, 2019. They claimed that the Medley Capital directors, who include the Taube brothers, breached their fiduciary duties to the common stockholders by entering into the Proposed Transactions. They accused Sierra of aiding and abetting in those breaches. They also claimed that Medley Capital's public disclosures failed to provide several categories of information material to stockholders considering the Proposed Transactions.

In reality, when the Taube brothers proposed the transactions in June 2018, Medley Management was facing enormous financial pressure. Medley Management had engaged in two sales processes in 2017, both of which failed, which left merging with affiliates as Medley Management's only solution. As part of the 2017 sales processes, Medley Management had secured standstill agreements from around thirty potential bidders, which prevented those third parties from proposing transactions with Medley Capital. During negotiations with one bidder during the 2017 sales process, the Taube brothers had already agreed to give up the TRA for substantially less consideration than they will receive under the Proposed Transactions. In 2018, Medley Management received two inbound expressions of interest for Medley Capital, which they ignored. The Medley Capital special committees did not know *any* of this information before this litigation. They were not told. They did not ask.

In the midst of this informational vacuum, Medley Capital's special committee members determined not to run any pre-signing market check or consider alternative transactions. They made this determination, although around that time at least one stockholder was agitating for Medley Capital to engage in a sales process. They capitulated to the aggressive timeline, although Medley Capital had no business reasons for rushing toward a deal. Then, they insulated the deal from a post-signing market check by agreeing to deal protections, including a no-shop.

This post-trial decision finds that the Proposed Transactions trigger the entire fairness test. FrontFour proved that half of the Medley Capital special committee was beholden to the Taube brothers, and thus the Taube brothers dominated and controlled the board with respect to the Proposed Transactions. Defendants failed to meet their burden of proving that the Proposed Transactions are entirely fair. The deal protections of the merger agreement also fail enhanced scrutiny.

As relief, FrontFour seeks a curative shopping process, devoid of Medley Management's influence, free of any deal protections, plus full disclosures. One obstacle prevents the Court from issuing this relief: FrontFour failed to prove that the acquirer, Sierra, aided and abetted in the other defendants' breaches of fiduciary duties. Under the Delaware Supreme Court's decision in *C & J Energy*,[2] an injunction may not issue if it would “strip an innocent third party of its contractual rights” under a merger agreement, unless the party seeking the injunction proves that the third party aided and abetted a breach of fiduciary duty by the target directors. Ordering a go-shop despite the no-shop and preventing enforcement of the deal protections would effectively strip Sierra of its contractual rights.

***3** And so, what came in like a lion goes out like a lamb: Under *C & J Energy*, FrontFour's requested relief must be denied.

Medley Capital's stockholders, however, are entitled to corrective disclosures. The proxy creates the misleading impression that the special committee replicated arm's-length negotiations amid the conflicts tainting the Proposed Transactions. To vote on an informed basis, the stockholders must know the reality—that the majority of the members of the special committee failed to act independently when negotiating the Proposed Transactions. Further, the stockholders are entitled to additional disclosures concerning third-party expressions of interests. On this topic, disclosures to date have been incomplete or, in one instance, outright false. Any stockholder vote on the Proposed Transactions is enjoined pending corrective disclosures consistent with the matters discussed in this decision.

I. FACTUAL BACKGROUND

Trial took place over one and three-quarter days. The record comprises over 800 trial exhibits, live testimony from six fact and two expert witnesses, deposition testimony from five fact witnesses, and ninety-seven stipulations of fact.[3] The parties submitted pre-trial and post-trial briefs. These are the facts as I find them after trial.

A. The Taube Brothers, the Medley Entities, and Medley Capital

Each of the entities named as a defendant in this action is an affiliate of Medley Management, a publicly traded asset management firm formed by Brook and Seth Taube. Brook, Seth, and their younger brother, Chris, control Medley Management through majority ownership.[4] Medley Management is the parent entity of several registered investment advisors, which manage several funds, including Medley Capital and Sierra (collectively, the "Medley Entities"). The Medley Entities' organizational structure is reflected in the attached chart.[5]

Medley Capital is a business development corporation ("BDC") formed by the Taube brothers in 2011.[6] BDCs are special investment vehicles regulated under the Investment Company Act of 1940 (the " '40 Act") and designed to facilitate capital formation for small and middle-market companies.[7] Medley Capital describes its business as "generat[ing] income and capital appreciation by lending directly to privately held middle market companies ...."[8] Medley Capital "source[s] investment opportunities through direct relationships with companies, financial intermediaries ..., as well as through financial sponsors."[9] Medley Capital launched its initial public offering in 2011.[10]

***4** Medley Capital licenses its name from the Medley Entities.[11] Medley Capital has no employees, offices, or physical assets of its own; all of this is supplied by its external advisor, MCC Advisors LLC ("Advisors"), a Medley Management subsidiary. The Medley Entities experience total insider overlap. Every member of Medley Capital's management team holds management positions, and each of Medley Capital's inside directors hold board seats in other Medley Entities, including Medley Management, Advisors, and Sierra.[12]

Advisors manages Medley Capital pursuant to an Amended and Restated Investment Management Agreement (the "Management Agreement") dated January 19, 2014.[13] Under that agreement, Medley Capital pays Advisors a base management fee of 1.75% of Medley Capital's gross assets and a two-part incentive fee calculated from net investment income ("NII") and net capital gains.[14] Advisors has broad discretion in making investment decisions and directing Medley Capital's rights under its debt instruments.[15] Such external management arrangements are common among BDCs.[16]

Under the '40 Act, a majority of Medley Capital's board of directors (the "Board") must be independent, and Medley Capital cannot enter into any transaction with its external advisor without the approval of a majority of its independent directors.[17] Medley Capital has a seven-member Board divided into three classes.[18] The directors are elected by a plurality vote and serve staggered three-year terms.[19] Medley Capital's current Board comprises three inside directors and four independent directors.[20] Medley Capital's inside directors are Brook Taube, Seth Taube, and their friend of thirty years, Jeff Tonkel.[21] Medley Capital's outside directors are John E. Mack, Karin Hirtler-Garvey, Arthur S. Ainsberg, and Mark Lerdal.[22] Mack, Hirtler-Garvey, and Ainsberg joined the Board in 2011.[23] Lerdal joined the Board in 2017.[24]

Under the '40 Act, Medley Capital's independent directors must annually review and, if appropriate, approve its Management Agreement.[25] In the approval process, the outside directors confer with counsel and review management fee levels of other BDCs.[26] Under the '40 Act, the Management Agreement must be terminable at will on

60 days' notice without a termination fee.[27] The outside directors have never considered Advisors' performance[28] or threatened (or even considered threatening) to terminate the Management Agreement as part of their annual review or otherwise.[29]

***5** In sum, Medley Capital depends on the Taube brothers for its day-to-day operations, office space, office equipment, staff, and even its name. Medley Capital has the right to terminate Advisors' Management Agreement, but has never considered using that right. Termination of that agreement would not extricate Medley Capital from the Taube brothers' influence in any event, given the other points of overlap.

Another salient fact: None of Medley Capital's fiduciaries (officers and directors) have interests aligned with the interests of Medley Capital's common stockholders.

As to the inside directors and management, their financial interests lie in Medley Management,[30] although the Taube brothers beneficially own just under 15% of Medley Capital's common stock.[31] If the Proposed Transactions close, the Taube brothers and Tonkel will each receive compensation for their Medley Management interests, as well as lucrative compensation packages more secure than the at-will Management Agreement.[32]

As to the outside directors, the value of their director fees dwarfs the value of their Medley Capital common stock.[33] Ainsberg, Hirtler-Garvey, and Mack have each been paid over $ 1 million for serving on the Board and its committees.[34] For the company's fiscal year ending September 30, 2018, Ainsberg earned $ 299,000 as a Medley Capital director, representing roughly half of his 2018 income.[35] Lerdal has been paid $ 288,702 for his two years as Medley Capital director.[36] By contrast, at the deal price, the value of all of the outside directors' combined common stock is under $ 40,000.[37] In the Proposed Transactions, two of Medley Capital's four outside directors will serve on the Board of the combined company; all four outside directors interviewed for the position after the Merger Agreement was signed.[38]

B. Pre-Signing Events

1. Medley Management's Failed Sales Processes

***6** Since its January 20, 2011 IPO, by every industry measure, Medley Capital has been in a steady financial decline.[39] This decline occurred during a period of sustained stock market and sector share price increases.[40] Medley Capital's performance is poor compared to its peers.[41] Due to Medley Capital's poor financial performance,[42] Medley Management faced financial pressures.[43]

In May 2017, Medley Management embarked on a process to consider a range of strategic transactions.[44] Medley Management retained UBS and Credit Suisse to conduct outreach.[45] Nineteen parties expressed interest and seven executed confidentiality agreements, but the process ultimately failed.[46]

***7** In October 2017, Medley Management determined to restart the process and reach out to potential bidders.[47] Medley Management retained Goldman Sachs & Co. LLC ("Goldman") and Broadhaven Capital Partners, LLC ("Broadhaven").[48] They invited thirty-eight potential strategic partners to participate in the preliminary round of a two-round sale process.[49] Twenty-four of them executed confidentiality agreements.[50] Medley Management received three "viable" first-round, non-binding indications of interest.[51] Only one bidder, "Party X," made a second-round proposal.[52] From January 12, 2018, through January 24, 2018, Medley Management and Party X engaged in negotiations and exchanged numerous proposals and counterproposals.[53]

The confidentiality agreements executed by third parties in Medley Management's two sales processes prevented the third-parties from offering to enter into any transaction with funds managed by Medley Management, including Medley Capital.[54] These restrictions applied for a "standstill period" following execution of the agreements. The standstill periods ranged from twelve to twenty-four months.[55]

On January 26, 2018, the Medley Capital Board convened a meeting to receive updates on Medley Management's sales process.[56] Brook Taube reported on the process as well as the status of negotiations with Party X.[57] His report to the Board was high-level. It omitted information that he had presented to Medley Management's board of directors that same day.[58] The Board was not informed, for example, that the arm's-length parties were only willing to pay premia of 8.4% (one third-party) – 30.0-55.4% (Party X). They were not told that Party X had dropped its price due to concerns about the performance of Medley Management. They were not made aware of the standstill provisions restricting transactions at Medley Capital. Before this litigation, none of the Board members ever asked for or were made aware of this information.

***8** If consummated, Party X's proposal would result in a change of control of Medley Management, triggering Medley Capital's approval rights under the Management Agreement.[59] To consider the impact of the Party X proposal on Medley Capital,[60] the Board determined to establish a special committee.[61] The Board appointed to the committee Ainsberg, Hirtler-Garvey, Mack, and Lerdal, with Ainsberg as chair (the "Special Committee").[62] The committee retained Kramer Levin as legal advisors.[63]

On March 15, 2018, Party X submitted a revised bid that reduced the proposed purchase price significantly and changed other important terms.[64] Medley Management determined that the revised proposal was not in the best interests of Medley Management and terminated discussions.[65] On May 2, 2018, Party X informed Medley Management that it did not intend to continue to pursue a potential transaction.[66]

In April 2018, a third-party, Origami Capital Partners, LLC ("Origami"), reached out to Medley Capital several times to propose a potential transaction.[67] On April 4, 2018, Origami submitted an indication of interest.[68] Medley Capital publicly denied ever receiving that letter.[69] But Origami addressed the April 2018 letter to both Brook Taube and Marilyn Adler, a Medley Capital Senior Managing Director.[70] And Adler *responded* to the letter: "I am excited to tell you that Medley has agreed to discuss a process for the sale. I've given your name as a possible buyer. I am having a discussion this week and will update you as I know more."[71] Brook Taube still maintains: "It's not clear to me where the mysterious correspondence came from."[72] Before this litigation, the Special Committee was not aware of Origami's 2018 overtures.

As part of Medley Management's negotiations with Party X, the Medley Entities' founders (the Taube brothers and other executives) agreed to give-up their TRA,[73] which was worth approximately $ 5.9 million for fifteen years following Medley Management's IPO.[74] Before this litigation, the Special Committee was not informed of Medley Management's negotiations with Party X concerning the TRA.

2. Medley Management's Proposed Transactions with Medley Capital and Sierra

***9** By May 2018, Brook Taube felt that Medley Management was "under enormous pressure" financially.[75] Wells Fargo noted that Medley Capital's "NAV has dropped for a remarkable fifteen quarters,"[76] and observed Medley Capital's "severe underperformance."[77] In Mack's words, by May 2018, Medley Capital's credit portfolio was "bottoming out."[78] The management team faced fee waivers at Medley Capital[79] and NAV issues "across the board," which would have a "meaningful impact on [Medley Management]."[80]

Intensifying this pressure, in 2016, the Taube brothers caused Medley LCC, a subsidiary of Medley Management, to a Master Investment Agreement with affiliates of Fortress Credit Advisors, LLC ("Fortress"). Under the agreement, Fortress provided approximately $ 40 million in capital for Medley Capital projects. Fortress received a put right that, if exercised, forces Medley to "immediately redeem" Fortress's interest.[81] This put right can be triggered in if Medley LLC fails to pay Fortress a preferred distribution or if Medley ceases to control Advisors.[82]

Brook Taube proposed implementing drastic steps, including closing Sierra Total Return Fund[83] to boost cash flow, ending the Sierra distribution to gain $ 4 million in EBITDA, and imposing other cost saving initiatives to squeeze another $ 2 million out of the business.[84] On May 9, 2018, Brook even requested that two of his senior management members agree to defer cash payments owed to them and take Medley Management stock instead.[85] His colleagues declined.[86] Before this litigation, the Special Committee was unaware of the pressures Medley Management faced during this time period.[87] In a candid moment during trial, Ainsberg admitted that he wished he had known.[88]

As one solution, the Taube brothers and their team began to contemplate a three-way combination between Medley Management, Medley Capital, and Sierra. Sierra is a non-traded BDC specializing in first lien, second lien, and subordinated debt of middle market companies with annual revenue between $ 50 million and $ 1 billion.[89] Like Medley Capital, Sierra is externally managed by a Medley Management subsidiary.[90] Sierra is much larger than Medley Capital. As of September 30, 2018, Sierra had total net assets of $ 687,862,000 and a NAV per share of $ 7.05.[91]

***10** Internally, Medley Management referred to this new proposal as "Project Integrate."[92] Brook Taube had conceived of this transaction in March 2018 as a fallback to the Party X deal.[93] By May 21, 2018, Project Integrate was at the top of the list of alternatives, and the management team was "very supportive."[94] By May 30, 2018, Brook Taube had asked Goldman and Broadhaven to consider the proposed three-way combination.[95]

At Sierra and Medley Capital board meetings on June 18 and 19, 2018, respectively, Medley Management formally introduced the idea of the three-way combination.[96] The initial proposal was that each share of Medley Capital stock would be converted into the right to receive 0.76 shares of Sierra common stock. Sierra would acquire Medley Management for $ 3.75 in cash and 0.41 shares of Sierra common stock.[97]

The minutes of the January 19, 2019 Board meeting summarize Medley Management's rationale behind the proposed transaction.[98] In sum, the major benefits of the proposed transaction touted by the transaction's proponents are: increased scale, increased liquidity, diversified asset pool, and internalization.[99]

Of course, the Proposed Transactions posed significant conflicts. In an effort to simulate arm's-length dealings, each of the three entities empowered a special committee to negotiate and, if appropriate, approve the transaction. Like Medley Capital, Sierra had formed a special committee in January 2018 to consider the impact of the Party X transaction;[100] the committee had been in a holding pattern since that time. Each of the committees hired financial advisors. Medley Management hired Barclays Capital Inc. ("Barclays");[101] Medley Capital hired Sandler O'Neill + Partners, L.P. ("Sandler"), as discussed below; and Sierra hired Broadhaven.

***11** Brook Taube facilitated the Sierra special committee's retention of Broadhaven. He thought highly of Broadhaven's Todd Owens,[102] having known him for years.[103] However, Medley Management had determined to retain Goldman only for Project Integrate—"two fees on the Integrate didn't make sense."[104] So, Brook Taube agreed to introduce Broadhaven to the Sierra special committee,[105] even though Broadhaven was still engaged by Medley Management.[106] Brook Taube suggested the idea to Tonkel on June 6, 2018. Broadhaven terminated its engagement with Medley Management on June 16, 2018, and pitched the Sierra special committee on June 18, 2018.[107] The Sierra special committee formally retained Broadhaven on June 29, 2018.[108] Although Broadhaven terminated its Medley Management engagement without receiving any payment, the Sierra special committee agreed to make an up-front payment of $ 1 million, the same amount Broadhaven would have earned as a transaction fee if the Medley Management strategic process had concluded successfully.[109]

3. Medley Capital's Special Committee Process

On June 19, 2018, the Medley Capital Board expanded the scope of the Special Committee's charter to consider the Proposed Transactions.[110] The Special Committee was empowered to evaluate and negotiate any proposed business combination, hire independent legal and financial advisors, determine whether the transaction was in the best interests of Medley Capital's stockholders, and recommend the approval or rejection of the transaction.[111]

a. What the Special Committee did.

The Special Committee retained a financial advisor. They interviewed two candidates. Ainsberg and Hirtler-Garvey participated in person; Mack and Lerdal participated by phone.[112] On June 21, 2018, at Brook Taube's recommendation, the committee members interviewed Medley Management's recent financial advisor, Credit Suisse.[113] On June 22, 2018, the committee interviewed Sandler.[114] The committee members met again on June 22 and 25, 2018, to select financial advisors, and they determined to retain Sandler.[115] Ainsberg signed Sandler's engagement letter on June 29, 2018.[116] Sandler gained access to the data room that day.[117]

***12** The Special Committee next met on July 11, 2018, to consider the Proposed Transactions.[118] Chris Donohoe of Sandler gave a presentation to give the committee "a solid grounding in understanding what Medley Capital looked like, what the other companies coming in would look like, and what a combined company would look like ...."[119] They authorized Sandler to negotiate on their behalf.[120] The committee's goals in these negotiations was to obtain "greater value for [the Medley Capital] stockholders" and "make sure that the combined company was better positioned to succeed."[121] To reach those goals, the committee (through Sandler) asked for cash consideration.[122] In the alternative, they authorized Sandler to push for less cash to leave the combined company.[123] Sandler negotiated on the founders' TRA and the management team's post-closing compensation.[124] Finally, Sandler set out to "ensure that the disinterested shareholders of [Medley Capital] had representation and say in the management of the combined business" through board representation in the combined company.[125]

Sandler began to negotiate on July 11, 2018.[126] Through negotiations, the founders agreed to waive the annual TRA payment,[127] Sierra agreed to permit two Medley Capital directors to join their Board,[128] and Sierra agreed to a higher exchange ratio than originally proposed.[129] At Sandler's request, Sierra obtained a compensation expert's opinion concerning the management compensation packages.[130] The opinion was provided on August 3, 2018,[131] with a supporting presentation.[132] Sierra did not agree to any cash consideration for Medley Capital stockholders.[133]

On July 29, 2018, Medley Management, Medley Capital, and Sierra reached final agreement on the ratios.[134] In the preceding three weeks, the Special Committee had met eight times.[135]

After settling on the economic terms, the parties focused on the legal terms of the merger agreement.[136] The Special Committee met four more times.[137] The record concerning negotiations of the deal protections is sparse. At least one document reflects that, as of August 8, 2018, the termination fee was still being negotiated.[138]

***13** On August 9, 2018, Sandler presented its opinion to the Special Committee that the Medley Capital Merger Consideration was fair to Medley Capital stockholders from a financial point of view.[139] On August 9, 2018, the Special Committee approved Medley Capital's merger agreement with Sierra.[140]

b. What the Special Committee did not do.

Out of the gate, the Special Committee failed to assert control over the timing of the process. At the June 2018 Medley Capital Board meeting, Medley Management presented an aggressive timeline, which contemplated that the parties would execute definitive transaction agreements and announce a transaction by July 31, 2018.[141] This made sense for Medley Management, which had shopped itself for more than a year prior to that point. By contrast, Medley Capital had not undertaken any strategic process before the June meeting.[142] Between its January 26, 2018 formation and the June 19, 2018 Board meeting, the Special Committee did not hold any meetings, retain a financial advisor, or engage in any substantive discussions with the Taube brothers or other members of Medley Management about a strategic transaction.[143] Unlike Medley Management, the Special Committee was starting from scratch. Unlike Medley Management, the Special Committee had no reason to rush deliberations. Yet, the committee capitulated to the timeline Medley Management proposed.

Then, throughout the negotiations, Brook Taube pressured the Special Committee to stick to the aggressive timeline. He denies this,[144] but contemporaneous documents prove otherwise.[145] In a July 11, 2018, email to the Medley Management Board, Brook Taube emphasized that "[t]ime is not in our favor given performance, inquiries, letters, etc."[146] He specifically flagged the possibility of "unwanted interloping" and emphasized that it was "real and should be taken seriously by the board."[147] He went on to underscore the fact that the transaction represented a "100% premium and a great deal" for Medley Management.[148] On July 27, 2018, Brook instructed Medley Management and Goldman to advise Medley Capital that they "have a fiduciary obligation to close."[149] That same day, he emailed Broadhaven: "Make this happen!!!!!!"[150] On July 31, 2018, Brook Taube emailed Jeff Tonkel while Tonkel was on a "Sierra call with Tony."[151] He instructed Tonkel: "Thursday board meetings are the ***time to push these guys hard*** in person."[152] On August 1, 2018, Brook reported to the Medley Management Board that "[w]e and Goldman continue to believe the risk is substantial if we announce earnings without simultaneously announcing this deal."[153] On August 5, 2018, Lerdal texted Brook Taube: "Are we on track? Anything you need from me?" Taube responded: "Let's talk soon / ***Pushing Hard*** :-)"[154]

***14** The Special Committee did not analyze the value of Medley Management, or understand what Medley Management would obtain in the Proposed Transactions, although in effect Medley Capital and Medley Management were competing for consideration. The Medley Management transaction and Medley Capital/Sierra Merger were cross-conditioned, and the new, combined company would own Medley Management post-closing.

The Special Committee did not consider alternative transactions,[155] although disgruntled stockholders were publicly advocating for a sale process as of April 2018. In a letter to the Board dated April 17, 2018, one Medley Capital stockholder wrote: "We believe the Board of Directors should immediately undertake a serious effort to sell the business (the underlying investment portfolio and the Management Agreement). We believe there is an attractive market for [Medley Capital's] investment portfolio well above where [Medley Capital's] current stock trades."[156] Although the Special Committee was broadly empowered, they laser-focused on only one option. Sandler corroborated—they viewed their role as evaluating the three-way combination only.[157]

The Special Committee did not conduct a pre-signing market check. When asked why, Hirtler-Garvey said she was happy with the transaction at hand.[158] She wanted a deal with Medley Management. Ainsberg testified to his belief that the 2017 Medley Management sales processes "effectively" checked the market for Medley Capital.[159] He believed that Party X's offer had the potential to result in a deal with Medley Capital.[160] Mack went further, testifying that he understood the Party X transaction to be geared toward a deal with Medley Capital, not with Medley Management.[161] This, of course, was wrong. Brook Taube testified, and contemporaneous evidence reflects, that the 2017 sales processes and negotiations with Party X aimed to develop strategic transactions and generate potential bidders *for Medley Management*, not Medley Capital.[162] Medley Capital was *not* "effectively" shopped.

***15** Although Medley Management's prior two sales processes informed the Special Committee's decision not to conduct a pre-signing market check, the committee members did *nothing* to inform themselves of basic aspects of those two sales processes. As discussed above, one member did not know that the process aimed to generate a deal for Medley Management, not Medley Capital.[163] No one asked about the terms of the potential Party X transaction or any other proposal received by Medley Management as part of those processes.

Critically, none of the committee members knew that approximately thirty confidentiality agreements contractually foreclosed potential third parties from proposing a transaction with Medley Capital. Of the thirty agreements, only two standstill periods expired before the Proposed Transactions were announced on August 9, 2018.[164] The other twenty-eight agreements restricted potential counterparties during the entire period that the Special Committee was negotiating the Proposed Transactions.[165]

When asked about the standstill agreements during his deposition, Mack stated his belief that "[t]his is a management issue, not a director [issue]."[166] He thought that more signed standstill agreements would be *beneficial* for Medley Capital.[167] He admitted, "I was not familiar with the specifics," and disclaimed any interest in being informed: "I may not want to know how sausage is made."[168]

The Special Committee did not probe meaningfully into the value of Medley Management. Medley Management's financial projections forecasted "hockey stick" growth in the outer years of the forecast based on revenue from new projects and clients.[169] Sandler ran a sensitivity analysis, but lacked much of the information that was concerned with whether the NII benefit from the deal was just projected growth, or whether there was underlying value and earnings to support the figures.[170]

Also, the Special Committee did not know about two expressions of interest from third parties concerning a transaction with Medley Capital. The first was from Origami, discussed above. The Special Committee did not learn of Origami's 2018 outreach until Origami publicly disclosed it in February 2019.[171] The second was from Lantern, which executed a confidentiality agreement on May 23, 2018, as part of the Medley Management sales process.[172] On July 3, 2018, Tom Schmidt of Lantern reached out to Goldman about its interest in acquiring Medley Management and potentially recapitalizing Medley Capital.[173] Schmidt followed up on July 10.[174] He followed up again on July 20, this time expressing frustration.[175] On July 30, Lantern submitted an indication of interest.[176] Among other things, Lantern explained that it was "interested in exploring alternatives for providing a significant cash infusion of ***new capital into Medley Capital*** to the extent it is prudent."[177] Lantern's recapitalization idea did not reach the Special Committee before execution of the Merger Agreement.

C. The Proposed Transactions

***16** On August 9, 2018 the Special Committee unanimously recommended that the Board approve the merger agreement with Sierra (the "Merger Agreement").[178] Medley Management, Medley Capital, and Sierra announced the Proposed Transactions on August 9, 2019.[179]

The Merger Agreement contains a series of deal protection provisions. Section 7.10 of the Merger Agreement prevents Medley Capital from soliciting or engaging with parties submitting "Competing Proposals" unless it constitutes a "Superior Proposal" or is likely to lead to one.[180] "Competing Proposal" is defined as an offer to acquire 20% or more of Medley Capital's securities or assets or a liquidation.[181] "Superior Proposal" is defined as a Competing Proposal that is on terms more favorable, from a financial point of view, than the Merger Agreement and is as likely to close.[182] Section 7.10(e) of the Merger Agreement provides that the Medley Capital Board may not make an "Adverse Recommendation Change" or enter into any agreement (other than a confidentiality agreement), subject to a fiduciary out.[183] Section 9.4 of the Medley Capital Merger Agreement provides for a $ 6 million "Termination Fee," which Medley Capital must pay if either party terminates the Medley Capital Merger Agreement after the Medley Capital Board effects an "Adverse Recommendation Change," or if Medley Capital terminates the Medley Capital Merger Agreement to enter into a definitive agreement contemplated by a Superior Proposal.

***17** Employment contracts connected to the merger provide for lucrative positions for Medley Management's senior management.[184] The cost of these employment contracts exceeds the estimated synergies arising from the Proposed Transactions.[185]

D. Post-Signing Events

1. FrontFour's Reaction

FrontFour beneficially owns 1,674,946 shares of Medley Capital common stock, which constitutes approximately 3.1% of Medley Capital's outstanding shares.[186] FrontFour first learned of the Proposed Transactions when they were publicly announced on August 9, 2018.[187]

FrontFour's corporate representative, David Lorber, testified at trial that he was "perplexed" by the announcement.[188] He believed that Medley Management had performed poorly over the prior five years, "erod[ing] significant NAV value, as well as stock price," yet "Medley Management was receiving an excessive amount of value" in the Merger Transactions.[189]

A FrontFour analyst reached out to Medley Capital to "better understand the transaction"[190] and eventually was placed in contact with Medley Capital's risk management officer, Sam Anderson.[191] They spoke on the phone in late September.[192] FrontFour was not aware during that call that Anderson was also a senior managing director of Medley Management.[193] During the call, FrontFour's representative asked why the proxy had not yet been issued.[194] Anderson responded suggesting that the parties to the Merger Transactions were having difficulty agreeing on the disclosures, which raised concerns for FrontFour.[195] After the call, FrontFour asked to be placed in contact with Medley Capital's independent directors.[196] Instead, Brook Taube responded. He promised to "revert back."[197] He did not timely do so.[198]

***18** On November 2, 2019, FrontFour nominated Lorber and Clifford Press as candidates for election as directors at Medley Capital's next annual meeting of stockholders.[199] On November 20, 2018, FrontFour obtained a telephonic meeting with Ainsberg and Hirtler-Garvey.[200] John Fredericks, Medley Capital's Chief Compliance Officer—who is also Medley Management's General Counsel and Sierra's Chief Compliance Officer—joined the call and did all of the talking.[201] On November 27, 2018, Medley Capital responded to questions raised by Lorber on the call.[202] On December 13, 2018, FrontFour issued an open letter to stockholders opposing the Proposed Transactions.[203]

2. Medley Capital's Public Disclosures

During an investors call on August 10, 2019, Medley Capital management represented that the proxy statement would be filed within weeks.[204] Medley Capital issued the proxy statement on December 21, 2019.[205] It was flawed.[206] On January 11, 2019, FrontFour commenced litigation in this Court pursuant to 8 *Del. C.* § 220 to compel Medley Capital to produce book and records for inspection.[207] After an initial scheduling conference with the Court, Medley Capital voluntarily produced to FrontFour stocklist materials and certain core documents concerning the Merger.[208] On January 30, 2019, FrontFour raised questions regarding the adequacy of the disclosures in the Proxy.[209] On February 5, 2019, Medley Capital issued the Proxy Supplement and postponed the stockholder vote until March 8, 2019.[210]

3. Multiple Third Parties Express Interest in Medley Capital

After Medley Capital issued the proxy, multiple third parties expressed interest in entering into an alternative transaction with Medley Capital.

- *ZAIS.* On January 2, 2019, ZAIS submitted a letter proposing that the Special Committee appoint ZAIS as the new investment advisor for the sole purpose of managing an orderly sale or liquidation of Medley Capital.[211] ZAIS requested the opportunity to meet the Special Committee to share its views. The Special Committee met to consider the proposal on January 9, 2019.[212] Nobody acting on behalf of the Special Committee ever contacted ZAIS. On January 24, 2019, Brook Taube instructed ZAIS that the Medley Capital Merger Agreement prohibited contact.[213]

***19** • *NexPoint.* On January 24, 2019, NexPoint Advisors, L.P. ("NexPoint") submitted a letter of intent proposing that Medley Capital terminate the Management Agreement and replace Advisors with NexPoint, which would charge a lower fee and make a cash payment to Medley Capital.[214] On January 31, 2019, NexPoint made a second proposal contemplating the combination of Medley Capital and Sierra and the retention of $ 100 million in cash otherwise earmarked for Medley Management stockholders in the Proposed Transactions.[215] NexPoint also proposed to pay $ 25 million to the combined company for the benefit of stockholders, to provide a reduced fee structure and lowered costs (resulting in at least $ 9 million in annual savings), and to purchase at least $ 50 million of combined company shares over a five-quarter period.[216]

On February 1, 2019, NexPoint made both its proposals public.[217] On February 6, 2019, Medley Capital and Sierra issued a press release indicating that their respective special committees had unanimously determined not to pursue the second NexPoint Proposal.[218] The press release purported to identify the reasoning behind the determinations by the Special Committees. But Medley Management had drafted the press release before the Special Committee had even made its determination.[219]

- *Origami.* On February 11, 2019, Origami issued an open letter to the Medley Capital Board, proposing to buy 100% of the interests of Medley Capital's wholly owned subsidiary, Medley SBIC, for $ 45 million cash.[220] Origami also disclosed that it had reached out several times during the spring of 2018 and sent a formal letter on April 4, 2018 expressing interest but had never received a response. [221] On February 14, 2019, Origami sent another letter clarifying and reiterating its interest in a potential transaction. [222] On February 19, 2019, Medley Capital rejected Origami's proposal. [223]

- *Marathon.* On March 1, 2019, Marathon Asset Management L.P. ("Marathon") submitted a letter to the Special Committee proposing that Medley Capital remain as an independent company, terminate the Management Agreement, and enter into a new management contract with Marathon. [224]

The Special Committee held meetings to consider the multiple expressions of interest. But nobody reached out to ZAIS, except to confirm that the Merger Agreement prohibited contact. [225] Nor has anyone acting on behalf of the Special Committee contacted NexPoint or Origami, despite their expressed willingness to improve their proposals. [226] The Special Committee has never asked for a waiver of the non-solicitation provisions of the Merger Agreement to enable discussions with any of these potential counterparties, nor has it attempted to secure better terms from the Taube brothers. [227]

***20** In sum, the Special Committee considered each offer, but did not engage with any competing bidder, and seems to question the need to do so. [228] Their attitude is best captured by Lerdal in a text to Brook Taube. Around the time of the Special Committee meeting at which the ZAIS offer was considered, Lerdal texted Brook Taube: "Are we going to respond to every f**ksake on the planet?" [229]

E. The Litigation

FrontFour commenced this litigation on February 11, 2019, and amended the complaint the next day to reflect the Origami offer. [230] Defendants stipulated to an expedited schedule, and the parties agreed to hold trial before the March 8, 2019 stockholder vote. [231] The parties substantially completed document production by February 24, 2019, took twelve depositions between February 26 and March 4, 2019, and submitted pretrial briefs and a form of pretrial order on March 4, 2019. [232] A pretrial conference was held on March 5, 2019. [233] Trial took place on March 6 and 7, 2019. [234]

II. ANALYSIS

The Amended Complaint asserts three counts: Count I contends that the Taube brothers, Tonkel, and the Special Committee members breached their fiduciary duties to FrontFour and the members of the Class in connection with the approval of the Proposed Transactions. [235] Count I challenges the Proposed Transactions under the entire fairness standard (the "Entire Fairness Claim"), and the deal protections of the Merger Agreement under enhanced scrutiny (the "Enhanced Scrutiny Claim"). Count II contends that the Medley Capital directors breached their fiduciary duty of disclosure (the "Disclosure Claims"). [236] Lastly, Count III contends that Medley Management, Sierra, Advisors, and two other Medley Entities—Medley Group and Medley LLC—aided and abetted in the other Defendants' breaches of fiduciary duties. [237]

A. Entire Fairness Claim

"Delaware has three tiers of review for evaluating director decision-making: the business judgment rule, enhanced scrutiny, and entire fairness." [238] Entire fairness review arises "when the board labors under actual conflicts of interest," [239] such as when a controlling stockholder stands on both sides of a challenged transaction [240] or when a controlling stockholder competes with the minority stockholders for consideration. [241]

***21** FrontFour argues that the Proposed Transactions should be reviewed under Delaware's most onerous standard, [242] entire fairness. The Taube brothers stand on both sides of the Proposed Transactions, so entire fairness applies if they are deemed controllers. FrontFour bears the burden of proving by a preponderance of the evidence facts necessary to trigger entire fairness. If entire fairness is triggered, Defendants bear the burden of proving by a preponderance of the evidence that the Proposed Transactions are entirely fair.

1. Entire Fairness Applies Because the Taube Brothers Are Controllers.

The Taube brothers beneficially own less than 15% of Medley Capital, and those shares are subject to "echo voting" requirements. Although a majority stockholder is a controlling stockholder as a matter of law, [243] a minority stockholder can also be deemed a controller.[244] In determining whether a minority stockholder is a controller, the level of stock ownership is not the predominant factor, and an inability to exert influence through voting power does not foreclose a finding of control.[245]

***22** Under Delaware law, a plaintiff can demonstrate that a minority stockholder exercised *de facto* control by showing that: (a) the stockholder "actually dominated and controlled the majority of the board generally";[246] or (b) the stockholder "actually dominated and controlled the corporation, its board or the deciding committee with respect to the challenged transaction."[247]

FrontFour has proven facts necessary to trigger entire fairness under the second theory. Specifically, FrontFour has proven that at least half of the Special Committee members were not independent from the Taube brothers when negotiating the Proposed Transactions. Under Delaware law, calling a director "independent" does not make it so. To be independent, a director "must ***act*** independently."[248] An independent director should demonstrate "the care, attention and sense of individual responsibility to the performance of one's duties ... that generally touches on independence."[249]

Mack, who did not testify at trial, demonstrated a lack of independence through his deposition testimony, where:

- Mack spoke to Brook Taube on the phone frequently, at least weekly, about business matters.[250]

- Mack knew that the Taube brothers managed Medley Capital's investments, but couldn't identify any other person involved in managing Medley Capital's portfolio.[251]

- Mack had no idea what Medley LLC was, who owned it, or the role it played in the Taube brothers' control of the Medley family of entities.[252]

- Mack had no understanding of what Medley Management's business was in 2017.[253]

- Mack could not identify the Taube brothers' or Tonkel's roles at Medley Management, the very source of their conflicts.[254]

- ***23** Mack did not know that the Taube brothers controlled Medley Management, and did not think it was important to consider their ownership of Medley Management in evaluating the Proposed Transactions.[255]

- Mack "was not familiar with the specifics" of the transaction process and "may not want to know how sausage is made."[256]

- Based on a call with Brook Taube, Mack believed Goldman Sachs was engaged to assist Medley Capital.[257]

- Mack did not believe the standstill provisions should have been reviewed by the Board, calling it a "management issue, not a director [issue]" and suggesting "the more the merrier."[258]

- Mack did not think it was important for the Medley Capital Board to be informed when Medley Management entered contracts that were binding on Medley Capital.[259]

- Mack had no idea whether Medley Capital paid performance fees to Advisors in 2017, or how the fees Advisors collected from Medley Capital affected Advisors' ability to pay its employees.[260]

- Mack believed that the Party X proposal was geared toward a deal with Medley Capital, not Medley Management.[261]

- Mack could not recall whether he considered having Sandler perform any form of a market check.[262] Instead, he relied on Brook Taube for his purported knowledge that "we were looking at strategic alternatives."[263]

- Mack did not believe that Medley Capital had ever solicited the market on its own behalf and was indifferent about the failure to do so.[264]

- Mack did not think the personal interests of the Taube brothers in closing the Proposed Transactions were relevant considerations in evaluating the transactions.[265]

- Mack did not have any understanding as to the significance of the Taube brothers' Medley Capital stockholdings or how they came to hold that position. [266]

- Mack was completely unaware as to the financing arrangement that the Taube brothers had with Fortress, which intensified the "enormous pressure" that drove the Taube brothers' decision to pursue the Proposed Transactions. [267]

- Mack did not think the fund's recent performance was an important consideration in the annual review of Advisors' contract with Medley Capital. Mack stressed the Board would consider comparisons to the fees and legal restrictions of comparable advisory arrangements, but did not think that recent performance was particularly important. [268]

- The lack of cash consideration for Medley Capital stockholders in the Proposed Transactions raised no concerns for Mack, even in the face of the large cash component that Medley Management was going to receive in the transactions. [269]

- Mack was indifferent to the compensation levels that would be paid to senior management in the combined company, even in the face of conversations concerning the fact that the compensation packages could potentially eliminate the benefits touted for Medley Capital stockholders in the Proposed Transactions. [270] Mack was satisfied that it was a concern for Sierra's board because they were negotiating and deciding the compensation, rather than the Medley Capital Board. [271]

***24** The record also reflects that half of Mack's annual income in the past three years had come from his service on the Board, making him susceptible to wanting to stay in the good graces of the Taube brothers. [272]

Lerdal was similarly susceptible to Brook Taube's outsized influence as Medley Capital's founder. [273] Lerdal desired to continue as director after formation of the combined company. He curried favor from Brook Taube during the selection process. When he was not selected, he contacted Brook Taube for other personal favors. The record reflects that Lerdal, who did not testify at trial, was loyal to Brook Taube, not the Medley Capital common stockholders:

- Lerdal shared information about the Special Committee's process with Brook. [274]

- Lerdal personally kept Brook up to date on market interest in Medley Capital, warning him by text on August 15, 2018 that the company "has some bargain hunters." [275]

- Four days before approving the merger, Lerdal asked Brook: "Are we on track? Anything you need from me?" [276] The two talked on the phone soon thereafter.

- The day the Special Committee approved the Proposed Transactions, Lerdal praised Brook as the "architect" of the deal and stated that he was "excited for the future whether the Sierra guys give me the nod or not." [277]

- When the Special Committee decided to turn down a bidder in February 2019, Lerdal texted Brook: "Hang in there brother. The deal is still the best option." [278] The two then exchanged an additional fourteen messages.

- When Brook Taube suggested that the "predictable naysayers" would be the first people removed from their positions during the Proposed Transactions, Lerdal was quick to support the idea, texting "Freak the naysayers." [279]

- Lerdal requested personal updates by text on the merger behind-the-scenes from Brook, asking "How do we look?" on October 9, 2018. Brook responded that there was "[G]ood news yesterday from [the SEC]" and that the deal was "Read[y] to go when 'advisors' stop fussing." [280]

- Lerdal's texts effortlessly wove ingratiating personal adoration with business details. On October 26, 2018, he texted Brook that he had played a game of golf in Brook's honor, and offered "an open invitation to visit and I'll host any time." [281]

- In an August 1, 2017 email, Lerdal complained that the Taube brothers gave the Board "too much information," asserted that the company could not pay him enough to make him continue being diligent and thorough, and bragged about how he would conduct himself in future litigation against the company. [282]

***25** In short, the majority of the members of the Special Committee lacked independence from the Taube brothers.

The Special Committee also sat supine in negotiations concerning the Proposed Transactions, allowing the Taube brothers to dominate the process by: setting the deal structure; controlling the flow of information; withholding information; withholding details about Medley Management's own value and the existence of offers from third parties; locking out "interlopers" through standstill agreements, deal protections, and an aggressive timeline; and rushing the committee's deliberations. In the end, the Special Committee allowed Medley Management to extract a huge premium while Medley Capital stockholders received none.

The Special Committee deferred to the Taube brothers although the committee had ample negotiating leverage—the ability to terminate the Management Agreement or simply reject the deal, either of which would have had devastating consequences for Medley Management. Terminating the Management Agreement would trigger Fortress's rights under the joint venture. Rejecting the deal would foreclose Medley Management's only viable solution to the enormous financial pressure they labored under.

It bears noting that there is nothing inherently wrong under Delaware law with the structure of the Medley Entities. Most BDCs have corporate structures similar to Medley Capital and Sierra—they rely on external advisors for management, administration, office space, staff, and other aspects of their existence. As a critical counterbalance to management's extensive control over the day-to-day operations, the '40 Act requires that the majority of the directors on BDC boards are independent from management. At no point in time is this protection more critical than in the context of a conflicted transaction. In this case, FrontFour has demonstrated that the Taube brothers are controllers *not* because of flaws inherent in the structure of BDCs, but rather, because those tasked with standing independent from the Taube brothers willfully deferred to their authority.

2. The Proposed Transactions Are Not Entirely Fair.

"The concept of fairness has two basic aspects: fair dealing and fair price."[283] Although the two aspects may be examined separately, "the test for fairness is not a bifurcated one as between fair dealing and price. All aspects of the issue must be examined as a whole since the question is one of entire fairness."[284] Defendants bear the burden of demonstrating that fair dealing and fair price.[285]

Fair dealing "embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained."[286] "The scope of this factor is not limited to the controller's formal act of making the proposal; it encompasses actions taken by the controller in the period leading up to the formal proposal."[287] "Particular consideration must be given to evidence of whether the special committee was truly independent, fully informed and had the freedom to negotiate at arm's length."[288]

***26** In this case, the timing, structure, initiation, and negotiation of the Proposed Transactions were conceived for the purpose of—and did—advance the Taubes' interest at the expense of Medley Capital's other stockholders. In the events leading up to the Proposed Transactions, the Taube brothers created an informational vacuum, which they then exploited. The Special Committee was not truly independent and did not negotiate at arm's length. In sum, Defendants have not proven that the Proposed Transactions were the product of fair dealing.

The second aspect of the entire fairness inquiry is fair price. Fair price "relates to the economic and financial considerations of the proposed merger, including all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock."[289]

The primary evidence presented at trial on the issue of fair price consists of the opinions of the parties' respective experts.[290] Defendants offered the testimony of Dr. Marc Zenner, who performed regression analyses intended to show the benefits of size/scale, asset quality, and internalized management.[291] That analysis did not support the propositions for which it was offered. One analysis explained only 11% of the variation in p/NAV multiples.[292] The other was not statistically significant and lacked explanatory power.[293] Zenner also conducted a comparable transactions analysis, but 50% of his "transactions" were offers that never resulted in an actual merger.[294] Zenner did not opine on the value of Medley Capital, a fair price to acquire Medley Capital, or the value of the combined company if the Proposed Transactions were to occur. He opined that the process used by various investment banks was reasonable, but an expert cannot simply vouch for the work of someone else.[295] Zenner opined that Medley Capital's trading price following the announcement of the proposed transaction supported a finding of fair price. Zenner, however, was unable to exclude other possible causes of Medley Capital's stock price bump in response the Proposed Transactions.[296]

By contrast, FrontFour's expert Dr. William Kennedy credibly testified that the fair value of Medley Capital is $ 5.07 per share and the price being offered is well below that.[297]

Ultimately, this is a case in which a deeply flawed process obscures the fair value of Medley Capital. The record reveals that the Taube brothers obstructed any pre-signing price competition from “interlopers.”[298] The two aspects of the entire fairness standard interact.[299] Just as “[a] strong record of fair dealing can influence the fair price inquiry, ... process can infect price.”[300] Any inability to determine the degree to which the flawed process infected the price works to Defendants' detriment, as they bear the burden of proof on this issue.[301]

B. Enhanced Scrutiny Claim

***27** The parties engaged in a robust dispute concerning whether deal protections or the Proposed Transactions in their entirety are subject to and pass enhanced scrutiny.[302] Any Delaware law enthusiast would relish the opportunity to dilate on the issues raised, but the press of time requires a more direct approach.

FrontFour challenges three deal protections in the Merger Agreement: a no-shop, an adverse-recommendation-change requirement, and a termination fee.[303] Enhanced scrutiny applies to deal protections, and the burden lies on Defendants to justify those protections.[304] Defendants cannot meet that burden here.

The suite of deal protections at issue would pass muster under most circumstances, but not in this case. The Court's analysis is fact intensive and context specific.[305] Due to extreme process flaws that led to the Proposed Transactions, the deal protections are not within the range of reasonableness.[306]

***28** Of the three challenged deal protections, the no-shop is the primary offender. No-shop provisions paired with a fiduciary out are not unique.[307] No-shop provisions are used to entice acquirers to make a strong offer by contractually eliminating the risk that the acquirer is a stalking horse used to generate a bidding war.[308] That justification has no application here. The Proposed Transactions are among affiliated entities. All of the parties were aware, when negotiating the deal protections, that there was no pre-signing auction or market check and no risk that Sierra was being used as a stalking horse. There was also no risk that Medley Capital would lose the “bird in hand” if the transaction was shopped.[309]

Incrementally, the other two deal protections are also problematic. The adverse-recommendation-change provision[310] unduly cabins the Board.[311] Although the termination fee is not unreasonable on its own, in combination with the other deal protections, it too falls outside the range of reasonableness.[312]

C. Disclosure Claims

***29** “[T]o establish a violation of the duty of disclosure, [a plaintiff] must prove that the omitted fact would have been material to the stockholder action sought.”[313] The materiality standard requires that fiduciaries disclose all facts which “under all the circumstances ... would have assumed actual significance in the deliberations of the reasonable shareholder.”[314] “A material fact is one that a reasonable stockholder would find relevant in deciding how to vote. It is not necessary that a fact would change how a stockholder would vote.”[315] “A material fact is one that a reasonable investor would view as significantly altering the ‘total mix’ of information made available.”[316] However, once fiduciaries have “traveled down the road of partial disclosure,” they must “provide the stockholders with an accurate, full, and fair characterization of [the] events.”[317]

Controlling stockholders “have large informational advantages that can only be imperfectly overcome by the special committee process, which almost invariably involves directors who are not involved in the day-to-day management of the subsidiary.”[318] Accordingly, controllers owe “a duty of complete candor when standing on both sides of a transaction and must disclose fully all the material facts and circumstances surrounding the transaction.”[319]

Applying these principles, FrontFour has proven that Defendants violated their duties of disclosure to inform stockholders of the process that led to the Proposed Transactions and the expressions of interest from third parties.

1. Process Disclosures

The Proxy describes the deployment of three different special committees to mitigate conflicts and replicate arm's-length bargaining.[320] The description creates the misleading impression that the Special Committee process at Medley Capital was effective. In reality, during the negotiation process, the Special Committee was disabled by its ignorance of: the details of the bids made for Medley Management during Project Elevate; the "enormous pressure" facing Medley Management and the Taubes;[321] and the standstill agreements that forbade potential transaction partners from presenting proposals directly to Medley Capital without Medley Management's consent. These process failures and others identified in this decision are material to stockholders considering the Proposed Transactions.

The Proxy and Medley Capital's other public filings disclose certain of these process flaws now, but they fail to mention that the Special Committee only learned of these items after the execution of the Merger Agreement (and in some cases only after this litigation began).[322] The timing of the Board's knowledge is a critical fact that would impact any stockholder's assessment of the quality of the transaction process.[323]

2. Other Indications of Interest—Lantern, NexPoint, Origami, and ZAIS

***30** Following FrontFour's January 30, 2019 letter to the Medley Capital Board,[324] Medley Management disclosed on February 5, 2019 certain terms of eleven indications of interest. It characterized each as a "non-binding indication of interest received by Medley Management."[325] Medley Capital separately issued supplemental disclosures regarding offers made by NexPoint on January 31, 2019, to replace Medley Management as manager, and Origami on February 11, 2019, to acquire Medley SBIC.

Defendants never disclosed to stockholders that Lantern had expressed interest in a recapitalization transaction with Medley Capital, or that Lantern had executed a standstill agreement with Medley Management that prohibited it from making its recapitalization proposal directly to Medley Capital.[326]

Defendants also never disclosed ZAIS's January 2, 2019 proposal to replace Medley Management as Medley Capital's investment advisor for the "explicit task of managing an orderly sale or liquidation of Medley Capital."[327] Nor have Defendants disclosed Brook Taube's January 24, 2019 rejection of ZAIS's proposal on behalf of Medley Capital, citing the non-solicitation provision in the Medley Capital Merger Agreement.[328] Text message correspondence between Brook Taube and Lerdal on the day of the Special Committee's January 9, 2019 meeting shows that Medley Management coordinated with the Special Committee regarding whether and how to respond to ZAIS. None of this was disclosed.[329]

Stockholders cannot make a fully informed decision regarding the Proposed Transactions unless they know about Lantern's expressed interest in a recapitalization, the ZAIS proposal, and Brook Taube's response citing the Medley Capital Merger Agreement.[330]

Further, on February 13, 2019, Defendants publicly denied that Medley Management received an offer from Origami to purchase Medley SBIC in April 2018.[331] Medley Capital's February 13 press release stated: "Contrary to Origami's public statements, the Company never received a proposal to buy the SBIC Subsidiary from Origami until yesterday. Origami did not propose to buy the equity of the SBIC subsidiary for 60% of its fair market value or at any price last April as suggested by Origami's press release."[332] This disclosure creates the impression that Origami fabricated the fact of the proposal.

Origami did not fabricate the fact of the proposal. In fact, Medley Capital received an April 11, 2018 letter from Origami addressed to Brook Taube and Marilyn Adler, Senior Managing Director, Medley Capital, expressing "interest in purchasing 100% of Medley Capital Corporation and its affiliates' interest in Medley SBIC."[333] Adler responded, dispelling any notion that the email failed to transmit.[334] Whether Brook Taube never saw Origami's proposal, as he contends, is irrelevant to the truth: Medley Management received it. "Whenever directors communicate publicly or directly with shareholders about the corporation's affairs, with or without a request for shareholder action, ... the *sine qua non* of directors' fiduciary duty to shareholders is honesty."[335] Medley Capital must correct its disclosures regarding Origami.[336]

D. Aiding and Abetting

***31** To establish an aiding and abetting claim against Sierra, FrontFour was required to prove that Sierra *knowingly participated* in the other Defendants' breach of fiduciary duty.[337] This is "a stringent standard that turn[s] on proof of scienter."[338] FrontFour bears the burden for the aiding and abetting claim.[339]

"The adjective 'knowing' modifies the concept of 'participation,' not breach."[340] The underlying wrong does not have to be knowing or intentional; it can be a breach of the duty of care.[341] Under Section 876(b) of the Restatement (Second) of Torts, knowing participation exists when a third party:

> (a) does a tortious act in concert with the other or pursuant to a common design with him, or
>
> (b) knows that the other's conduct constitutes a breach of duty and gives substantial assistance or encouragement to the other to so conduct himself, or
>
> (c) gives substantial assistance to the other in accomplishing a tortious result and his own conduct, separately considered, constitutes a breach of duty to the third person.[342]

For purposes of a board decision, the requirement of participation can be established if the third party "participated in the board's decisions, conspired with [the] board, or otherwise caused the board to make the decisions at issue."[343] In particular, a third party can be liable for aiding and abetting a breach of the duty of care if the third party "purposely induced the breach of the duty of care ...."[344] The method of facilitating the breach can include "creating the informational vacuum" in which the board breaches its duty of care.[345]

***32** A court's analysis of whether a secondary actor "knowingly participated" is necessarily fact intensive. Illustrative factors include the following:

> - The nature of the tortious act that the secondary actor participated in or encouraged, including its severity, the clarity of the violation, the extent of the consequences, and the secondary actor's knowledge of these aspects;
> - The amount, kind, and duration of assistance given, including how directly involved the secondary actor was in the primary actor's conduct;
> - The nature of the relationship between the secondary and primary actors; and
> - The secondary actor's state of mind.[346]

At trial, FrontFour succeeded in raising suspicions concerning the independence of the Sierra special committee's financial advisor, Broadhaven. Broadhaven's conflicts alone, however, do not prove that Sierra knowingly participated in the other Defendants' fiduciary breach. Broadhaven did act as Sierra's agent, and Sierra knew that Broadhaven had previously worked for Medley Management. But this is the extent of Sierra's *scienter* FrontFour proved at trial. Broadhaven was not "the fiduciary and primary wrongdoer."[347] Nor was Broadhaven a "representative of the [Sierra] who either controls [Sierra] or who occupies a sufficiently high position that [its] knowledge is imputed to [Sierra]."[348]

FrontFour provided no window into the deliberations on the Sierra side of the negotiations to permit the Court to conduct the fact-intensive inquiry demanded. FrontFour did not call any of the Sierra special committee members live or by deposition. FrontFour adduced no evidence that the Taube brothers controlled the Sierra portion of the process or dominated the Sierra board. FrontFour did not brief their aiding and abetting claim before or after trial.[349]

Accordingly, FrontFour has failed to prove that Sierra aided and abetted in the other Defendants' breaches of fiduciary duties.

E. Remedy

To recap, FrontFour has proven that: Conflicted insiders tainted the process that led to the Proposed Transactions. The Special Committee negotiated with willful blinders, not knowing: the value that third-parties had placed on Medley

Management; that Medley Management felt "enormous pressure" to enter into a transaction; that standstill agreements prevented third parties from coming forward; and that Medley Management—not Medley Capital—was shopped in the 2017 sale process on which they relied when determining not to conduct a pre-signing market check. Compounding these problems, the Special Committee agreed to deal protections preventing an effective post-signing market check.

***33** At this stage, the most equitable relief for the Medley Capital stockholders would be a curative shopping process, devoid of Medley Management's influence, free of any deal protections, plus full disclosures. Thereafter, if no better proposal surfaces, the Medley Capital stockholders would have the opportunity to cast a fully informed vote for or against the Proposed Transactions. This relief is precisely what FrontFour seeks.

Yet, ordering such relief would require the Court to blue-pencil Sierra's merger agreement with Medley Capital (and, by implication, its cross-conditioned agreement with Medley Management) so that Medley Capital could solicit additional competing bids in contravention of the no-shop provision. In other words, FrontFour's requested relief would keep Sierra "on the hook" to purchase Medley Capital in case the "go-shop" process fails to yield a better offer. Such a revision of the Merger Agreements would deny Sierra the benefit of its bargain and force Sierra to comply with terms to which it never agreed.

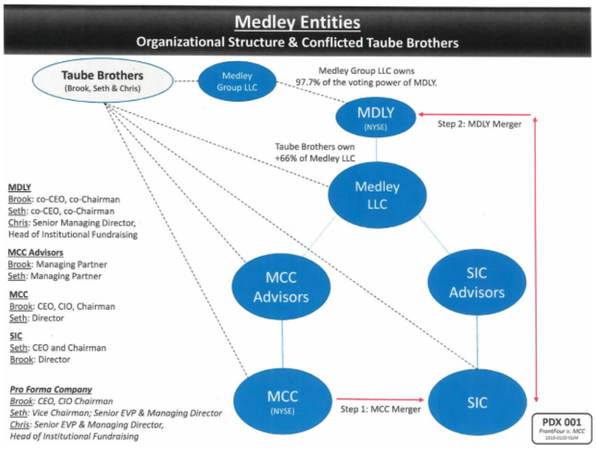
Under the Delaware Supreme Court's decision in *C & J Energy*,[350] an injunction may not issue if it would "strip an innocent third party of its contractual rights" under a merger agreement, unless the party seeking the injunction proves that the third party aided and abetted a breach of fiduciary duty by the target directors. FrontFour has failed to prove that Sierra aided and abetted in the breaches of fiduciary duties. Under these circumstances, *C & J Energy* leaves this Court no discretion—the most equitable remedy for Medley Capital stockholders cannot be granted.

To ensure that Medley Capital stockholders are fully informed on any vote on the Proposed Transactions, FrontFour is entitled to corrective disclosures consistent with this decision, and Defendants are enjoined from consummating the Mergers until such disclosures have been made.[351] FrontFour may also pursue a damages claim by amending their complaint, if FrontFour so chooses.

III. CONCLUSION

For the foregoing reasons, the Court holds that Medley Capital's directors violated their fiduciary duties in entering into the Proposed Transactions. Medley Capital is ordered to issue corrective disclosures in accordance with this decision and to permit the stockholders sufficient time in advance of any stockholder vote to assimilate the information. Judgment on Counts I and II of the Amended Complaint are entered in favor of FrontFour to the extent set forth in this decision, and judgment on Count III is entered in favor of Defendants. FrontFour's request to permanently enjoin the Proposed Transactions is denied.[352]

Attachment



Medley Entities

Organizational Structure & Conflicted Taube Brothers

Medley Group LLC owns 97.7% of the voting power of MDLY.

Taube Brothers own +66% of Medley LLC

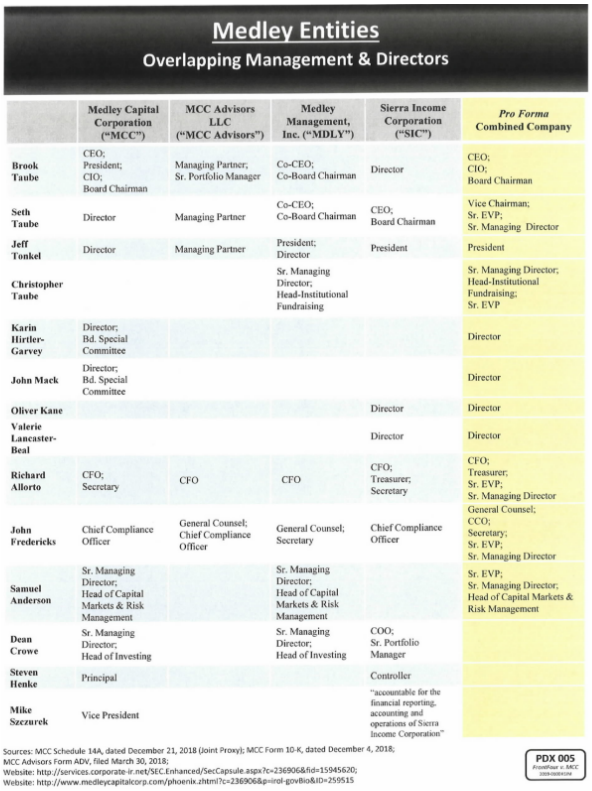
MDLY
Brook: co-CEO, co-Chairman
Seth: co-CEO, co-Chairman
Chris: Senior Managing Director, Head of Institutional Fundraising

MCC Advisors
Brook: Managing Partner
Seth: Managing Partner

MCC
Brook: CEO, CIO, Chairman
Seth: Director

SIC
Seth: CEO and Chairman
Brook: Director

Pro Forma Company
Brook: CEO, CIO Chairman
Seth: Vice Chairman; Senior EVP & Managing Director
Chris: Senior EVP & Managing Director,
Head of Institutional Fundraising



Medley Entities

Overlapping Management & Directors

	Medley Capital Corporation (“MCC”)	MCC Advisors LLC (“MCC Advisors”)	Medley Management, Inc. (“MDLY”)	Sierra Income Corporation (“SIC”)	*Pro Forma* Combined Company
Brook Taube	CEO; President; CIO; Board Chairman	Managing Partner; Sr. Portfolio Manager	Co-CEO; Co-Board Chairman	Director	CEO; CIO; Board Chairman
Seth Taube	Director	Managing Partner	Co-CEO; Co-Board Chairman	CEO; Board Chairman	Vice Chairman; Sr. EVP; Sr. Managing Director
Jeff Tonkel	Director	Managing Partner	President; Director	President	President
Christopher Taube			Sr. Managing Director; Head-Institutional Fundraising		Sr. Managing Director; Head-Institutional Fundraising; Sr. EVP
Karin Hirtler-Garvey	Director; Bd. Special Committee				Director
John Mack	Director; Bd. Special Committee				Director
Oliver Kane				Director	Director
Valerie Lancaster-Beal				Director	Director
Richard Allorto	CFO; Secretary	CFO	CFO	CFO; Treasurer; Secretary	CFO; Treasurer; Sr. EVP; Sr. Managing Director
John Fredericks	Chief Compliance Officer	General Counsel; Chief Compliance Officer	General Counsel; Secretary	Chief Compliance Officer	General Counsel; CCO; Secretary; Sr. EVP; Sr. Managing Director
Samuel Anderson	Sr. Managing Director; Head of Capital Markets & Risk Management		Sr. Managing Director; Head of Capital Markets & Risk Management		Sr. EVP; Sr. Managing Director; Head of Capital Markets & Risk Management
Dean Crowe	Sr. Managing Director; Head of Investing		Sr. Managing Director; Head of Investing	COO; Sr. Portfolio Manager	
Steven Henke	Principal			Controller	
Mike Szczurek	Vice President			“accountable for the financial reporting, accounting and operations of Sierra Income Corporation”	

Sources: MCC Schedule 14A, dated December 21, 2018 (Joint Proxy); MCC Form 10-K, dated December 4, 2018;
MCC Advisors Form ADV, filed March 30, 2018;
Website: http://services.corporate-ir.net/SEC.Enhanced/SecCapsule.aspx?c=236906&fid=15945620;
Website: http://www.medleycapitalcorp.com/phoenix.zhtml?c=236906&p=irol-govBio&ID=259515

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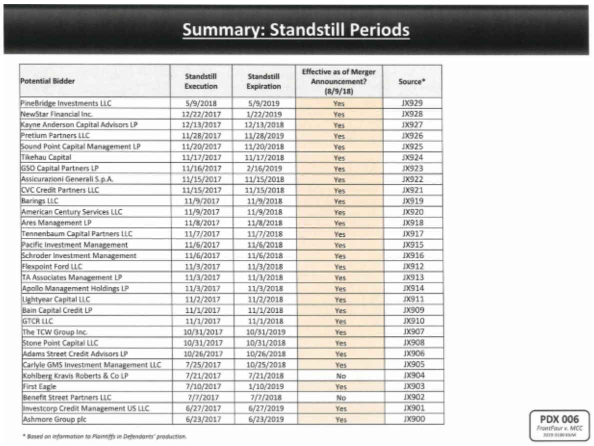

Summary: Standstill Periods

Potential Bidder	Standstill Execution	Standstill Expiration	Effective as of Merger Announcement? (8/9/18)	Source*
PineBridge Investments LLC	5/9/2018	5/9/2019	Yes	JX929
NewStar Financial Inc.	12/22/2017	1/22/2019	Yes	JX928
Kayne Anderson Capital Advisors LP	12/13/2017	12/13/2018	Yes	JX927
Pretium Partners LLC	11/28/2017	11/28/2019	Yes	JX926
Sound Point Capital Management LP	11/20/2017	11/20/2018	Yes	JX925
Tikehau Capital	11/17/2017	11/17/2018	Yes	JX924
GSO Capital Partners LP	11/16/2017	2/16/2019	Yes	JX923
Assicurazioni Generali S.p.A.	11/15/2017	11/15/2018	Yes	JX922
CVC Credit Partners LLC	11/15/2017	11/15/2018	Yes	JX921
Barings LLC	11/9/2017	11/9/2018	Yes	JX919
American Century Services LLC	11/9/2017	11/9/2018	Yes	JX920
Ares Management LP	11/8/2017	11/8/2018	Yes	JX918
Tennenbaum Capital Partners LLC	11/7/2017	11/7/2018	Yes	JX917
Pacific Investment Management	11/6/2017	11/6/2018	Yes	JX915
Schroder Investment Management	11/6/2017	11/6/2018	Yes	JX916
Flexpoint Ford LLC	11/3/2017	11/3/2018	Yes	JX912
TA Associates Management LP	11/3/2017	11/3/2018	Yes	JX913
Apollo Management Holdings LP	11/3/2017	11/3/2018	Yes	JX914
Lightyear Capital LLC	11/2/2017	11/2/2018	Yes	JX911
Bain Capital Credit LP	11/1/2017	11/1/2018	Yes	JX909
GTCR LLC	11/1/2017	11/1/2018	Yes	JX910
The TCW Group Inc.	10/31/2017	10/31/2019	Yes	JX907
Stone Point Capital LLC	10/31/2017	10/31/2018	Yes	JX908
Adams Street Credit Advisors LP	10/26/2017	10/26/2018	Yes	JX906
Carlyle GMS Investment Management LLC	7/25/2017	10/25/2018	Yes	JX905
Kohlberg Kravis Roberts & Co LP	7/21/2017	7/21/2018	No	JX904
First Eagle	7/10/2017	1/10/2019	Yes	JX903
Benefit Street Partners LLC	7/7/2017	7/7/2018	No	JX902
Investcorp Credit Management US LLC	6/27/2017	6/27/2019	Yes	JX901
Ashmore Group plc	6/23/2017	6/23/2019	Yes	JX900

* *Based on information to Plaintiffs in Defendants' production.*

PDX 006
FrontFour v. MCC
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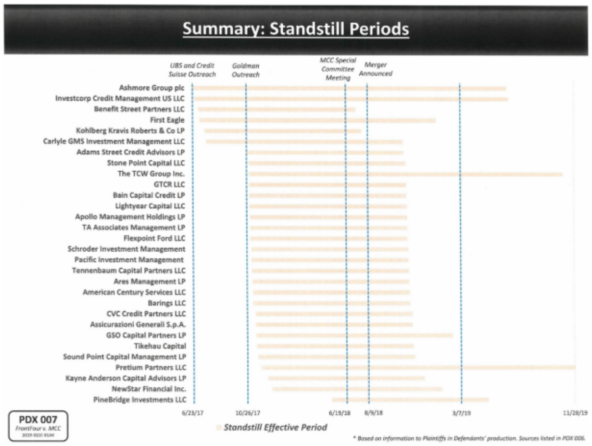

Summary: Standstill Periods

PDX 007
FrontFour v. MCC
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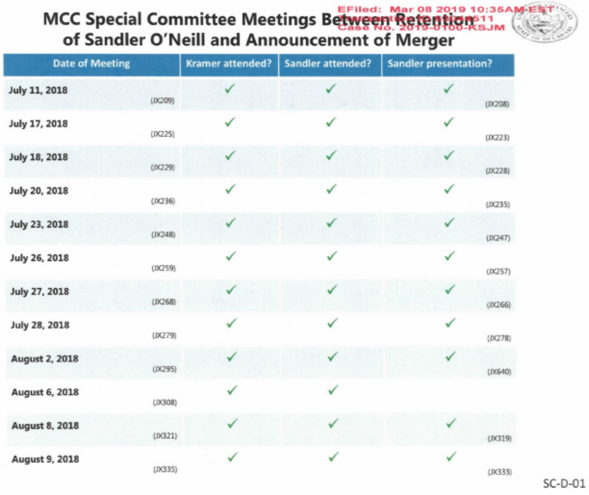
* *Based on information to Plaintiffs in Defendants' production. Sources listed in PDX 006.*



MCC Special Committee Meetings Between Retention of Sandler O'Neill and Announcement of Merger

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Date of Meeting	Kramer attended?	Sandler attended?	Sandler presentation?
July 11, 2018 (JX209)	✓	✓	✓ (JX208)
July 17, 2018 (JX225)	✓	✓	✓ (JX223)
July 18, 2018 (JX229)	✓	✓	✓ (JX228)
July 20, 2018 (JX236)	✓	✓	✓ (JX235)
July 23, 2018 (JX248)	✓	✓	✓ (JX247)
July 26, 2018 (JX259)	✓	✓	✓ (JX257)
July 27, 2018 (JX268)	✓	✓	✓ (JX266)
July 28, 2018 (JX279)	✓	✓	✓ (JX278)
August 2, 2018 (JX295)	✓	✓	✓ (JX640)
August 6, 2018 (JX308)	✓	✓	
August 8, 2018 (JX321)	✓	✓	✓ (JX319)
August 9, 2018 (JX335)	✓	✓	✓ (JX333)

SC-D-01

All Citations

Not Reported in Atl. Rptr., 2019 WL 1313408

Footnotes

[1] This litigation commenced on February 11, 2019. The parties stipulated to an expedited schedule to accommodate a March 31, 2019 drop-dead date under the challenged merger agreements. Pre-trial briefs were submitted on Monday, March 4. Over 800 trial exhibits arrived in Chambers on Tuesday, March 5. Trial took place on March 6–7. On the second day of trial, the acquirer informed the Court that its “rights under the Merger Agreements will be eviscerated if the Court does not issue a decision on Plaintiffs' request for an injunction by 9 a.m. on Monday, March 11.” Post-trial briefs were filed at 8 a.m. on Saturday, March 9. Daylight savings time began on Sunday, March 10, further depriving the Court of an hour and confirming Murphy's law.

[2] *C & J Energy Servs., Inc. v. City of Miami Gen. Empls.' and Sanitation Empls.'* Ret. Tr., 107 A.3d 1049, 1071–72 (Del. 2014).

[3] The Factual Background cites to: docket entries (by docket "Dkt." number); trial exhibits (by "JX" number); the trial transcript ("Trial Tr."); and stipulated facts set forth in the Parties' Pretrial Order (Dkt. 128) ("PTO"). The parties called by deposition John Mack, Russ Hutchinson on behalf of Goldman Sachs, John Simpson on behalf of Broadhaven, Jeffrey Young on behalf of Origami, and Thomas Surgent on behalf of NexPoint. The transcripts of their respective depositions are cited using the witnesses' last names and "Dep. Tr." (*e.g.*, "Mack Dep. Tr.").

[4] The three Taube brothers own about 82% of Medley Group LLC. Trial Tr. at 311:17–312:11 (Taube). Medley Group LLC, in turn, owns 97.7% of Medley Management. *Id.* at 321:12–14.

[5] *See* Dkt. 136, Ex. A: PDX 001. This decision refers to a number of demonstratives that summarize the record evidence and were publicly filed by the parties. Referring to charts has the added bonus of appealing to the visual learner. The Charts need a cipher, as this decision uses different defined terms to refer to each of the Medley Entities to improve readability: MDLY = Medley Management; MCC = Medley Capital; SIC = Sierra.

[6] PTO ¶¶ II.3, II.5.

[7] *See generally* U.S. Securities and Exchange Commission, *Fast Answers: Investment Company Registration and Regulation Package*, available at https://www.sec.gov/investment/fastanswers/divisionsinvestmentinvcoreg121504htm.html#P75_10439 (last visited Mar. 7, 2019); Morrison Foerster, *FAQs About BDCs*, https://media2.mofo.com/documents/faqbusiness-development-companies.pdf (last visited Mar. 11, 2019). *See also* Medley Capital Corp., Annual Report (Form 10-K) at 30 (Feb. 14, 2018) ("We are classified as a non-diversified investment company within the meaning of the '40 Act, which means that we are not limited by the '40 Act with respect to the proportion of our assets that we may invest in securities of a single issuer.").

[8] JX 013 at p.4.

[9] *Id.*

[10] PTO ¶ II.21.

[11] JX 051 at p.23.

[12] *See* Dkt. 136, Ex. A: PDX 005 ("Medley Entities: Overlapping Management & Directors").

[13] JX 004. Advisors provides Medley Capital's office facilities, equipment, and other administrative services to Medley Capital pursuant to a separate administration agreement. PTO ¶ II.23; JX 051 at p.23. For the years ended September 30, 2017, 2016, and 2015, Medley Capital paid Advisors $ 3.8 million, $ 3.9 million, and $ 4.1 million, solely for administrative expenses, respectively. *Id.*

[14] PTO ¶ II.24; JX 004 § 8.

[15] Trial Tr. at 313:17–315:23 (Taube testimony). "We [Advisors] make the loans on behalf of Medley Capital ... as the manager, we manage all aspects of the loan from inception through to repayment, and the board isn't involved in how we process the loan at any time." *Id.* at 315:7–14.

[16] *See* Trial Tr. at 417:22–418:5 (Hirtler-Garvey).

[17] *See* 15 U.S.C. § 80a-56; JX 430 at p.14.

[18] Medley Capital Corp., Registration Statement Amendment (Form N-2/A) (Nov. 23, 2010), Ex. 99.A.3 ("Medley Capital Certificate of Incorporation") § 6.3; *Id.*, Ex. 99.B.3 ("Medley Capital Bylaws") § 3.1 ("The number of directors which shall constitute the whole of the Board of Directors shall be seven.").

[19] Medley Capital Certificate of Incorporation § 6.3.

[20] Medley Capital Corp., Annual Report (Form 10-K) at 72 (Dec. 4, 2018).

[21] PTO ¶¶ II.4–6; Medley Capital Corp., Annual Report (Form 10-K) at 72 (Dec. 4, 2018); Trial Tr. at 318:12–16 (Taube testifying that he has known Tonkel since college).

[22] PTO ¶¶ II.7–10.

[23] *Id.* ¶¶ II.7–9.

[24] *Id.* ¶ II.10.

[25] 15 U.S.C. § 80a-15(a)(2).

[26] Trial Tr. at 163:10–21 (Ainsberg); Mack Dep. Tr. at 40:21–41:9.

[27] *Id.* § 80a-15(a)(3); PTO ¶ II.23; *see* Trial Tr. at 286:20–287:2 (Taube); *Id.* at 162:24–163:21 (Ainsberg).

[28] Trial Tr. at 197:11–14 (Ainsberg) ("Q.... [T]he Medley Capital board has never considered declining to renew Medley Capital Advisors' contract due to poor performance, has it? A. It has not.").

[29] Mack Dep. Tr. at 43:10–12 ("Q: Has the Board ever considered terminating the investment management agreement? A: Not that I'm aware of."); Trial Tr. at 197:11–14 (Ainsberg) ("Q: ... [T]he Medley Capital board has never considered declining to renew Medley Capital Advisors' contract due to poor performance, has it? A. It has not."); *id.* 390:1–5 (Hirtler-Garvey) ("Q: Now, did you ever discuss with your special committee members or with the other independent directors of the board, I guess, terminating that contract? A. We have not.").

[30] The Taube brothers have close to a 100% ownership interest in Management. *See* PTO ¶ II.5 ("Seth Taube, with Brook Taube, is the beneficial owner of ... 97.7% of the voting interests in [Medley Management] common stock"); PDX 001. Tonkel owns 6% of the units in Medley LLC, which are exchangeable for shares of MDLY Class A stock. PTO ¶ II.6.

[31] PTO ¶ II.5 ("Seth Taube, with Brook Taube, is the beneficial owner of 14.6% of Medley Capital common stock"); Trial Tr. at 281:19–21 (Taube) ("Management and Medley [Management] have, in combination, approximately 14.9 percent interest in Medley Capital Corporation shares.").

[32] Under the terms of the Proposed Transactions: Brook Taube will be Chairman and CEO of the combined company, receive an annual base salary of $ 600,00, and be eligible for additional performance-based compensation of $ 1,200,00 cash and $ 2,000,000 in restricted shares; Seth Taube will be Vice Chairman, Senior Executive Vice President, and Senior Managing Director of the combined company, receive an annual base salary of $ 480,000, and be eligible for additional performance-based compensation of $ 600,000 in cash and $ 1,150,000 in restricted stock; and Tonkel will be President, receive an annual base salary of $ 480,000, and be eligible for additional performance-based compensation of $ 600,000 cash and $ 1,150,000 in restricted stock. PTO ¶¶ II.69–71.

[33] Ainsberg owns only 3,000 shares of Medley Capital stock, which he purchased shortly after joining the Medley Capital Board (JX 001); Hirtler-Garvey owns only 3,000 shares of Medley Capital stock, which were purchased shortly after the IPO (JX 003); Mack owns only 1,000 shares of Medley Capital stock, which were purchased in 2012 (JX 002); and Lerdal does not own any shares of Medley Capital stock. None of them have elected to receive Medley Capital stock in lieu of cash compensation since 2011, and none of the independent directors have acquired shares in Medley Capital since 2012. JX 1–JX 3; JX 417 at p.559.

[34] Each independent director receives an annual fee of $ 90,000. Medley Capital Corp., Annual Report (Form 10-K) at 78 (Dec. 4, 2018). In addition, Chairman of the Audit Committee receives an annual fee of $ 25,000, and chairpersons of the Nominating, Corporate Governance, and Compensation Committees receive annual fees of $ 10,000. *Id.* Other members of the Audit Committee, the Nominating and Corporate Governance Committee, and the Compensation Committee receive annual fees of $ 12,500, $ 6,000, and $ 6,000, respectively. Each independent director on the special merger committee received a one-time retainer of $ 25,000, the chairman of the special committee receives a monthly fee of $ 15,000 and other members receive a monthly fee of $ 10,000. *Id.* For Medley Capital's fiscal year ending on September 30, 2018, Ainsberg received $ 299,000, Hirtler-Garvey received $ 267,500, Mack received $ 275,000, and Lerdal received $ 252,500. *Id.*

[35] JX 622 at pp.7–11.

[36] Medley Capital Corp., Proxy Statement (Form DEF 14A), Proposal I (Dec. 21, 2017) (reporting compensation of $ 36,202 for fiscal year ending Sept. 30, 2017); Medley Capital Corp., Annual Report (Form 10-K) at 78 (Dec. 4, 2018) (reporting compensation of $ 252,500 for the fiscal year ending September 30, 2018).

[37] Seven thousand shares x $ 5.68 per share. JX 700, Medley Capital Corp., Proxy Statement (Form DEFM14A) (Dec. 21, 2018) ("Medley Capital Proxy").

[38] Mack Dep. Tr. at 102:2–14; Trial Tr. at 387:15–23; JX 379 at p.1.

[39] *See* Dkt. 118, Pls.' Pretrial Br. at 17, Chart & n.3 (compiling data). Between its IPO and the announcement date of the challenged transactions, Medley Capital's stock plummeted by approximately 72% and its cumulative return was -34%. JX 507 at p.7. The deterioration in Medley Capital's net investment income ("NII"), a key metric in measuring BDC performance and a proxy for BDC earning power, and dividend are particularly dramatic. Since 2014, NII has plunged by 85% (from $ 1.58 to $ 0.23 per share), and the dividend has fallen by 65% (from $ 1.48 to $ 0.52 per share). JX 443 at p.8; Trial Tr. at 194:4–12 (Zenner). Because dividends have exceeded NII, Medley Capital has operated with an unsustainable shortfall since 2016. *Id.*

[40] JX 509 at p.7.

[41] The S & P BDC Index has had a positive 57% return since 2011. JX 443 at p.3; Trial Tr. at 469:23–470:2 (Zenner) (testifying that Medley Capital's performance had been poor relative to its peers). As of August 9, 2018, Medley Capital had the largest discount to NAV (53%) of any BDC. JX 343 at p.33. As of year-end, Medley Capital has continued to languish at a 55% discount to NAV—the single largest NAV discount among the 46 BDCs covered by Raymond James' investment banking group in their "BDC Weekly Insight" report (published January 3, 2019) and nearly 3x the BDC average discount of 19%. JX 434 at p.7.

[42] At the end of 2017, the Management Agreement appears to have accounted for 21% of Medley Management's fee-earning assets under management ("fee earning AUM" or "FEAUM"). Medley Management, Inc., Annual Report (Form 10-K) at 52–53 (Mar. 29, 2018). FrontFour quantifies the Management Agreement as producing about 30% of Medley Management's fee revenue. JX 443 at p.10. Whichever way one computes the value of the Management Agreement to Medley Management, it is clearly significant.

[43] Between 2016 and 2017, base management fees paid to Medley Capital Advisors fell from $ 19.5 million to $ 17.8 million. JX 051. The incentive fee had fallen from $ 8.0 million to $ 0.9 million in the same period, and Advisors was likely to lose all of its incentive fees from Medley Capital in 2018. JX 051 at F-51.

[44] *Id.* at 288:17–289:22; PTO ¶ II.27; Medley Capital Proxy at 57. Medley Management internally referred to this process as "Project Redwood." JX 027 (Project Redwood Management Presentation).

[45] PTO ¶ II.27.

[46] *Id.*; Medley Capital Proxy at 57–58. On July 2017, two interested parties submitted non-binding bids, but neither bid progressed beyond the initial indication of interest. PTO ¶ II.30; JX 621 (Pls.' Expert Report of Dr. Kennedy) at ¶ 26 ("one cash proposal included an acquisition of [Medley Management] and [Advisors], and the other proposed a combination in exchange for consideration of cash and stock of the combined entity"); Medley Capital Proxy at 57 ("In July 2017, two of the interested parties submitted non-binding bids to acquire [Medley Management] and [Advisors]. One of the interested parties proposed an acquisition of [Medley Management] and [Advisors] for cash, and the other proposed a combination in exchange for consideration of cash and stock of the combined entity. However, neither bid progressed beyond the initial indication of interest.").

[47] Medley Management referred to this process internally as "Project Elevate." *See* JX 029 (Project Elevate: Confidential Information Packet). The relevant record materials are: *id.*; JX 068 (Project Elevate: January 2018 Discussion Materials); JX 635 (Project Elevate: Apr. 2018 Process Summary); JX 639 (Project Elevate: July 2018 Process Summary); JX 646 (Project Elevate: Deal Point List); JX 035 (Project Elevate: Oct. 2017 Discussion Materials); JX 047 (Project Elevate: First Round Bid Summary Materials); JX 064 (Project Elevate: Discussion Materials); JX 205 (Project Elevate: July 2018 Process Updates).

[48] JX 054 (letter engaging Goldman "as financial advisor in connection with the possible sale of all or a portion of [Medley Management]"); Medley Capital Proxy at 58.

[49] JX 085.

[50] Medley Capital Proxy at 58.

[51] *Id.*

[52] JX 057; JX 635 at p.3.

[53] Medley Capital Proxy at 58.

[54] They prevented the third parties from offering to acquire or be involved in “any acquisition, transaction, merger or other business combination relating to all or part of ... any funds advised by [Medley Management] or acquisition transaction for all or part of the assets of ... any funds advised by [Medley Management].” PTO ¶ II.28; *see, e.g.*, JX 037 (Schroders Conf. Agr.) § 10.a. The agreements also restricted the third parties' ability to “encourage, initiate, induce or attempt to induce [Medley Capital] ... to terminate, amend or otherwise modify their advisory agreements with [Medley Management] during the Standstill Period.” PTO ¶ II.29. *See, e.g.*, Schroders Conf. Agr. § 10.h.

[55] *See* Dkt. 136, PDX 006 (Summary: Standstill Periods); *id.* PDX 007 (Summary: Standstill Periods, cont.).

[56] JX 065 at p.1.

[57] *Id.* at pp.1–2.

[58] *Compare* JX 067 (including half-page summary of the Goldman process and background on Party X) *with* JX 068 (including comprehensive information about the Medley Management bidding process, the terms of each bid, and financial terms proposed by Party X).

[59] JX 065 at p.2 (Jan. 26, 2018 Medley Capital Board meeting minutes, Brook reported that the contemplated transaction “would result in a change in control due to the fact that [Medley Capital's] investment advisory agreement would be assigned to [Party X].”).

[60] Trial Tr. at 293:13–24 (Taube) (“You know, when the determination was made to proceed with [Party X], we identified that, due to the assignment of the contract, that that was a decision that needed to be made. My recollection is that [the] special committee was formed so that they could make that decision and determination on their own without the interested board members.”).

[61] JX 065 at pp.2–4.

[62] *Id.*

[63] *Id.* at p.5. The Medley Capital Board approved a $ 25,000 retainer for each committee member, a stipend of $ 15,000 per month for the committee chair, and a stipend of $ 10,000 per month for all other members. *Id.*

[64] JX 087; Medley Capital Proxy at 59; JX 635 at p.5.

[65] PTO ¶ II.40; Medley Capital Proxy at 59.

[66] PTO ¶ II.41.

[67] JX 101; JX 107.

[68] JX 544.

[69] Medley Capital Corp., Current Report (Form 8-K) at 1 (Feb. 13, 2019) (“Contrary to Origami's public statements, the Company never received a proposal to buy the SBIC Subsidiary from Origami until yesterday.”).

[70] JX 100. Origami addressed the letter to Adler because it believed at the time that Adler was *instructed* to solicit expressions of interest to purchase Medley SBIC. Young Dep. Tr. at 78:6–7. Knowing that Brook and Adler worked together, Origami contacted the two of them. *Id.* at 77:13–15. Origami was “surprised and disappointed that [Brook] refused to respond.” *Id.* at 77:16–18.

[71] JX 108.

[72] Trial Tr. at 373:22–374:1.

[73] For some background on TRAs, see Lynnley Browning, *Squeezing Out Cash Long After the I.P.O.*, New York Times (Mar. 13, 2013), *available at* https://dealbook.nytimes.com/2013/03/13/private-equity-squeezes-out-cash-long-afterits-exit/ (last visited Mar. 9, 2019).

[74] Trial Tr. at 246–47 (Sterling).

[75] JX 126 (May 9, 2018 email from Brook Taube).

[76] JX 078 (Wells Fargo Equity Research Report, *Medley Capital: We Were Wrong, But Staying the Course* (Feb. 6, 2018)); *see also* JX 618 (Defs.' Expert Report of Dr. Zenner) at p.56.

[77] JX 129 (Wells Fargo Equity Research Report, *Medley Capital: When the Going Gets Tough ...* (May 10, 2018)); *see also* JX 618 (Defs.' Expert Report of Dr. Zenner) at p.58.

[78] Mack Dep. Tr. at 61:16–25.

[79] On May 4, 2018, Medley Capital Advisors voluntarily elected to waive $ 380,000 of the base management fee payable for the quarter ended March 31, 2018. JX 417 at p.16.

[80] JX 126 at p.1. Trial Tr. at 287:18–23 (Taube) ("[W]e were under pressure. And by that I mean, we were not going to make the quarter. And I think on any quarter, we're doing our best to make the earnings that we are targeting. In this quarter, as I recall, a few hundred thousand dollars was the difference.").

[81] *Id.* § 6.3.

[82] *Id.* § 6.2.

[83] "[A]nother [investment] vehicle that was intended and still does follow in the tracks of [Sierra]." Trial Tr. at 282:14–17.

[84] *See* JX 119.

[85] JX 126 (May 9, 2018 email from Brook Taube).

[86] JX 701; JX 133.

[87] Trial Tr. at 215–17 (Ainsberg), 287–88 (Taube).

[88] *Id.* at 215:18–217:2.

[89] PTO ¶ II.12; JX 656.

[90] Medley Capital Proxy at 21.

[91] *Id.* at 360.

[92] *See* JX 091; JX 092.

[93] JX 092 (Mar. 29, 2018 email from Brook: "I like project integrate / Let's see if we can defer recapture and tax ... and keep TRA / That would be good :-)").

[94] *See* JX 134.

[95] JX 140.

[96] JX 162; JX 163; JX 164.

[97] JX 164.

[98] Those minutes state: "[T]here was an industry-wide push for increased scale, ... potential benefits of increased scale include better financing options, investment opportunities, and cost savings, among other benefits. In particular, by scaling the institutional manager, [the combined company, "Newco"] would be able to commit capital for investments alongside strategic partners and other institutional investors. He also pointed out that the Potential Transaction would create a streamlined organizational structure allowing for significant reductions in fixed costs and expenses. In addition, following the Potential Transaction, Newco would experience increased scale and liquidity. Newco would have approximately $ 1.2 billion in assets and would be the second largest internally managed [BDC] and the seventh largest BDC overall. Discussion ensued among members of the Board. Mr. Taube further noted that compared to externally managed BDCs, internally managed BDCs traded at a substantial market premium to book, or net asset value, and that issuing shares while trading at a premium would in and of itself be accretive. Mr. Taube emphasized, however, that it is not possible to precisely predict how the market would react to the Potential Transaction." JX 164 at p.2.

At this point, it bears noting that none of the Board or Special Committee meeting minutes from June 2018 forward were finalized until after FrontFour commenced this litigation. Trial Tr. at 419:2–16 (Hirtler-Garvey); JX 293. For that reason, I do not view them as contemporaneous evidence or give them any presumptive weight, but rather use them to summarize Defendants' litigation position.

[99] JX 163 at p.7 (June 19, 2018 Medley Capital Board Presentation); Medley Capital Proxy at 26; JX 618 ¶ 25; Trial Tr. at 295:8–297:12 (Taube).

[100] Medley Capital Proxy at 71 ("[O]n January 26, 2018, [Medley] Management held meetings with the Medley Capital Board and the Sierra Board ... [the] Sierra Board established ... the Sierra Special Committee ... and authorized the committee[ ] to evaluate the merits of a potential sale of substantially all of [Advisors'] assets to Party X ....").

[101] PTO ¶ II.53. The decision to engage Barclays was made at the July 10, 2018 meeting of the Medley Management special committee. JX 204 at p.2.

[102] Trial Tr. at 349 (Taube).

[103] *Id.* at 348.

[104] *Id.* at 301; *see also id.* at 349 ("We had made the decision only to pay Goldman going forward.").

[105] *Id.*

[106] Trial Tr. at 300:21–301:3 (Taube) (B. Taube giving reasons for recommending Broadhaven to the [Sierra] special committee); JX 151 (June 13, 2018 email from B. Taube telling Broadhaven that they were "on deck" to pitch on June 18, 2018).

[107] JX 158; JX 151; JX 162.

[108] JX 031.

[109] *See* JX 191 at p.4; JX 031.

[110] JX 164.

[111] *Id.* at pp.6–8.

[112] Trial Tr. at 170:9–171:3 (Ainsberg); *Id.* at 299:19–300:1 (Hirtler-Garvey). *But see* Mack Dep. Tr. at 71:12–17 ("Q. And were you involved in the hiring of a financial advisor? A. I was not involved in the interview process. However, all of the members of the committee reviewed the submitted materials and voted on the hiring of the financial advisor.").

[113] Trial Tr. at 299:23–300:14 (B. Taube recommended Credit Suisse); JX 177 (June 21, 2018 Credit Suisse pitch book).

[114] JX 189 (Sandler engagement letter); JX 175 (June 22, 2018 Sandler pitch book); JX 187 (Email from B. Taube to J. Tonkel describing terms of Sandler engagement).

[115] JX 175; JX 430; Trial Tr. at 170–71 (Ainsberg). Mack explained his reasons for selecting Sandler: "[T]hey gave a very good presentation and they were a lot cheaper than the other guy." Mack Dep. Tr. at 72:2–4. In Ainsberg's view: "[Sandler] had extensive experience in the BDC space. They're a very highly regarded investment banker. I had known the firm for many years reputationally. I had never done any business with them. They had known the folks at [Medley Management] but hadn't had any important retention ... for a period of years." Trial Tr. at 171:8–17. And Ainsberg agreed that Sandler's "pricing for their assignment was significantly less than Credit Suisse, so finances were a factor." *Id.*

[116] PTO ¶ II.49; Medley Capital Proxy at 71.

[117] JX 703; Trial Tr. at 236:2–237:6 (Sterling).

[118] JX 209 at 2–4.

[119] Trial Tr. at 240:2–241:8 (Sterling); JX 208; JX 209.

[120] Trial Tr. at 242:2–14 (Sterling).

[121] *Id.* at 243:17–18.

[122] *Id.* at 243:21–244:4.

[123] *Id.*

[124] *Id.* at 173–74 (Ainsberg); *Id.* at 244:5–14 (Sterling).

[125] *Id.* at 244:15–19 (Sterling); *id.* at 395:9–16 (Hirtler-Garvey) ("That was an idea that they brought forward that we thought was a great idea.").

[126] JX 707.

[127] Trial Tr. at 246:12–247:6 (Sterling).

[128] JX 509 at p.5; JX 723 at 10; Trial Tr. at 244:15–19 (Sterling).

[129] Trial Tr. at 245:18–24, 246:5–8 (Sterling) (testifying that negotiations achieved a ratio that was equal to Medley Capital's "equity value or book value in the form of NAV").

[130] JX 288.

[131] The one-sentence letter reads: "It is our professional opinion that the employment agreements and the executive compensation packages attached to the merger agreement are reasonable." JX 641.

[132] JX 299; Trial Tr. at 247:21–248:1.

[133] *Id.* at 246:1–4. *See generally Id.* at 173–76 (Ainsberg).

[134] JX 280.

[135] *See* Dkt. 134, Defs.' Demonstrative SC-D-01 (Medley Capital Special Committee Meetings Between Retention of Sandler O'Neill and Announcement of Merger). *See also* JX 208 (July 11, 2018 Sandler presentation deck); JX 209 (July 11, 2018 board minutes); JX 223 (July 17, 2018 Sandler presentation deck); JX 225 (July 17, 2018 board minutes); JX 228 (July 18, 2018 Sandler presentation deck); JX 229 (July 18, 2018 board minutes); JX 235 (July 20, 2018 Sandler presentation deck); JX 236 (July 20, 2018 board minutes); JX 247 (July 20, 2018 Sandler presentation deck, draft); JX 248 (July 23, 2018 board minutes); JX 257 (July 26, 2018 Sandler presentation deck); JX 259 (July 26, 2018 board minutes); JX 266; JX 278 (July 27, 2018 Sandler presentation deck); JX 268 (July 27, 2018 board minutes) JX 279 (July 28, 2018 board minutes).

[136] Trial Tr. at 177–78 (Ainsberg).

[137] JX 295 (Aug. 2, 2018 board minutes); JX 308 (Aug. 6, 2018 board minutes); JX 321 (Aug. 8, 2018 board minutes); JX 319 (Aug. 9, 2018 Sandler presentation deck, draft); JX 333 (Aug. 9, 2018 Sandler presentation deck); JX 335 (Aug. 9, 2018 board minutes); JX 640 (Sandler Summary of Synergies).

[138] JX 332 at p.6.

[139] PTO ¶ II.58; JX 333 (Sandler Fairness Opinion Presentation deck).

[140] *Id.* ¶ II.59.

[141] *See* JX 163.

[142] *See* JX 702.

[143] *See* Medley Capital Proxy at 59–71. Despite the lack of any visible work, the Medley Capital Special Committee was paid a total of $ 280,000 between January and June 2018. JX 164 at p.6.

[144] Trial Tr. at 355:3–6 (Taube) ("Q. You were pushing the special committees of all of these entities to get a deal done; right? A. I was not.").

[145] *Compare* Trial Tr. at 352 ("We wanted to have a process that was timely but sensible.") *with* JX 289 ("Thursday board meetings are the time to *push* these guys hard in person.") (emphasis added); JX 269 ("I want to agree on ONE suggestion (not a menu) and tell them they are better off ... or at least no worse off ... *and have a fiduciary obligation to close"*) (emphasis added); JX 275 ("Make this happen!!!!!! If not ... I don't know what to say). *See also* Simpson Dep. Tr. at 623:23–225:2 ("Brook was pushing very hard – we advised the Special Committee that we had talked to Brook and that he was pushing very hard for his position.").

[146] JX 212 at p.3.

[147] JX 212 at p.3.

[148] *Id.* at p.4.

[149] JX 269.

[150] JX 275. Brookhaven's corporate representative, John Simpson, advised the Sierra special committee "that Brook was pushing very hard ... that [Broadhaven] had talked to Brook and that he was pushing very hard for his position." Simpson Dep. Tr. at 224–25.

[151] JX 289.

[152] *Id.* (emphasis added).

[153] JX 292.

[154] JX 717 at p.1 (emphasis added). Brook Taube did not produce text messages in discovery. Trial Tr. at 358. FrontFour was forced to press for them. Dkt. 127. Lerdal produced this text message after Brook Taube's deposition. Trial Tr. at 359:5–9.

[155] JX 569 ("Medley Capital did not contact any third parties for the purpose of exploring an Alternative Medley Capital Transaction between May 1, 2017 and execution of the Medley Capital Merger Agreement").

[156] JX 105. *See also* Trial Tr. at 20:8–13 (Lorber).

[157] Trial Tr. at 231:18–232:14 (Sterling).

[158] *Id.* at 419:17–420:4 (Hirtler-Garvey).

[159] *Id.* at 182:2–183:4 (Ainsberg) ("We didn't shop the company because, if one steps back and thinks about the history of [Medley Management], starting in 2017, even before the Goldman Sachs and Brookhaven involvement, Medley Management undertook a process with both Credit Suisse and UBS to look at the

marketplace to see if there would be an opportunity to come together with a group. And when [Medley Management] was doing that, as we discussed earlier, that involves [Medley Capital], because [Medley Capital] effectively would have to approve a transaction in some shape, manner, or form. So effectively what happened, both at the time of the Credit Suisse/UBS and at the time of the Goldman/Broadhaven reach-out to the street, many, many significant players in the street knew about it, that [Medley Management] was interested in the transaction. So this business effectively was -- was looked at. Now, did they look at our -- I don't know what they looked at, effectively, when they were looking at it, these other entities. I don't know what documents they were provided with. But you would assume that they, early on, before our current transaction, that these folks looked at various documents of the entities.").

[160] Trial Tr. at 225–28 (Ainsberg).

[161] Mack Dep. Tr. at 57:10–25. Mack also testified that he did not know or think about who Goldman Sachs was working for. *Id.* at 99:20–25. "They were – they were trying to shop to see whether there was a deal out there, but I'm not sure that I ever thought about who they were working for." *Id.* at 99:25–100:4.

[162] Trial Tr. at 289:21–293:24 (Taube); JX 022 (Benefit Street Partners non-binding proposal to Medley Management); JX 035 (Project Elevate Discussion Materials); JX 038 (Project Elevate Preliminary Proposal Instructions); JX 031 (Broadhaven engagement letter).

[163] Mack Dep. Tr. at 57:3–25.

[164] *See* Dkt. 136, PDX 006 (Summary: Standstill Periods); *id.* PDX 007 (Summary: Standstill Periods, cont.).

[165] *See* Dkt. 136, Ex. A: PDX 006 (Summary: Standstill Periods).

[166] JX628 at 52:7–10 ("You have to delegate things to the management. Directors direct. I'm sorry. Directors direct, managers manage.").

[167] Mack Dep. Tr. at 53:13–15 ("The fact is, as you -- as I think about it, the more the merrier. It's -- then it's just become a part of a process.").

[168] Mack Dep. Tr. at 53:13–22.

[169] JX 341 at p.28.

[170] Trial Tr. at 254:5–11 (Sterling).

[171] *Id.* at 213:10–23 (Ainsberg).

[172] JX 137.

[173] JX 197.

[174] JX 213.

[175] JX 234 ("I have not been able to get you guys to respond since Tuesday. Left messages at the office for you as well as email. Not trying to be difficult but would like some input on scheduling. If I need to get to NYC I will do that. Thank you.").

[176] JX 286.

[177] JX 283 at p.2 (emphasis added).

[178] PTO ¶ II.59; JX 336.

[179] JX 350.

[180] JX 317 (Merger Agr.) § 7.10(d) ("Notwithstanding anything to the contrary contained in this Agreement, at any time prior to the date that [Medley Capital] Stockholder Approval is obtained (in the case of [Medley Capital]) or [Sierra] Stockholder Approval is obtained (in the case of [Sierra]), in the event that [Medley Capital] (or its representatives on [Medley Capital's] behalf) or [Sierra] (or its representatives on [Sierra's] behalf) receives a Competing Proposal from any Third Party, (i) [Medley Capital] and its representatives or [Sierra] and its representatives, as applicable, may contact such Third Party to clarify any ambiguous terms and conditions thereof (without the [Medley Capital] Board or [Sierra] Board, as applicable, being required to make the determination in clause (ii) of this Section 7.IO(d)) and (ii) [Medley Capital] and the [Medley Capital] Board and its representatives or [Sierra] and the [Sierra] Board and its representatives, as applicable, may engage in negotiations or substantive discussions with, or furnish any information and other access to, any Third Party making such Competing Proposal and its representatives and Affiliates if the [Medley Capital] Board or [Sierra] Board, as applicable, determines in good faith (after consultation with its outside financial

advisors and legal counsel) that (A) such Competing Proposal either constitutes a Superior Proposal or could reasonably be expected to lead to a Superior Proposal and (B) failure to consider such Competing Proposal could reasonably be expected to be inconsistent with the fiduciary duties of the directors of [Medley Capital] or [Sierra], as applicable, under Applicable Law; provided, that (x) such Competing Proposal did not result from any material breach of any of the provisions set forth in this Section 7.10, (y) prior to furnishing any material non-public information concerning [Medley Capital] or [Sierra], as applicable, [Medley Capital] or [Sierra], as applicable, receives from such Third Party, to the extent such Third Party is not already subject to a confidentiality agreement with [Medley Capital] or [Sierra], as applicable, a confidentiality agreement containing confidentiality terms that are not less favorable in the aggregate to [Medley Capital] or [Sierra], as the case may be, than those contained in the Confidentiality Agreement (unless [Medley Capital] or [Sierra], as applicable, offers to amend the Confidentiality Agreement to reflect such more favorable terms) (it being understood and agreed that such confidentiality agreement need not restrict the making of Competing Proposals (and related communications) to [Medley Capital] or the [Medley Capital] Board or to [Sierra] or the [Sierra] Board, as the case may be) (an ***'Acceptable Confidentiality Agreement'***) and (z) [Medley Capital] or [Sierra], as the case may be, shall (subject to the terms of any confidentiality agreement existing prior to the date hereof) promptly provide or make available to the other party any material written non-public information concerning it that it provides to any Third Party given such access that was not previously made available to the other party or its representatives.") (emphasis original).

181 *Id.* § 1.1 (" ***'Competing Proposal'*** means any inquiry, proposal or offer made by any Third Party: (a) to purchase or otherwise acquire, directly or indirectly, in one transaction or a series of transactions (including any merger, consolidation, tender offer, exchange offer, stock acquisition, asset acquisition, binding share exchange, business combination, recapitalization, liquidation, dissolution, joint venture or similar transaction), (i) beneficial ownership (as defined under Section 13(d) of the Exchange Act) of twenty percent (20%) or more of any class of equity securities of [Medley Capital] or [Sierra], as applicable, or (ii) any one or more assets or businesses of [Medley Capital] or its Subsidiaries or [Sierra] or its Subsidiaries that constitute twenty percent (20%) or more of the revenues or assets of [Medley Capital] and its Subsidiaries, taken as a whole, or [Sierra] and its Subsidiaries, taken as a whole, as applicable; or (b) any liquidation of [Medley Capital] or [Sierra], in each case other than the Merger and the other transactions to occur at Closing in accordance with this Agreement.") (emphasis original).

182 *Id.* (" ***'Superior Proposal'*** means any bona fide written Competing Proposal made by a Third Party that the [Medley Capital] Board or the [Sierra] Board, as applicable, determines in good faith, after consultation with its outside financial advisors and legal counsel, and taking into account the terms and conditions of such proposal, the party making such proposal, all financial, legal, regulatory and other aspects of such proposal, as well as the likelihood of consummation of the Competing Proposal relative to the Merger and such other factors as the [Medley Capital] Board or [Sierra] Board, as applicable, considers to be appropriate, is more favorable to [Medley Capital's] stockholders or [Sierra's] stockholders, as applicable, from a financial point of view than the Merger and the other transactions contemplated by this Agreement (including any revisions to the terms of this Agreement committed to by [Sierra] to [Medley Capital] in writing in response to such Competing Proposal made to [Medley Capital] or by [Medley Capital] to [Sierra] in writing in response to such Competing Proposal made to [Sierra] under the provisions of Section 7.10(f); provided however, for these purposes, to the extent relevant to the Competing Proposal in question, all percentages in subsections (a)(i) and (a)(ii) of the definition of Competing Proposal shall be increased to fifty percent (50%).") (emphasis original).

183 *Id.* § 7.10(e) ("Except as otherwise provided in this Agreement, (i) the [Medley Capital] Board shall not effect [a Medley Capital] Adverse Recommendation Change and the [Sierra] Board shall not effect [a Sierra] Adverse Recommendation Change (each, an ***'Adverse Recommendation Change'***), (ii) [Medley Capital] Board shall not approve or recommend, or allow [Medley Capital] to execute or enter into, any letter of intent, memorandum of understanding or definitive merger or similar agreement with respect to any Competing Proposal (other than an Acceptable Confidentiality Agreement), and (iii) the [Sierra] Board shall

not approve or recommend, or allow [Sierra] to execute or enter into, any letter of intent, memorandum of understanding or definitive merger or similar agreement with respect to any Competing Proposal (other than an Acceptable Confidentiality Agreement); provided however, that notwithstanding anything in this Agreement to the contrary, if at any time prior to the receipt of [Medley Capital] Stockholder Approval (in the case of [Medley Capital]) or the [Sierra] Stockholder Approval (in the case of [Sierra]), [Medley Capital] or [Sierra], as the case may be, has received a Competing Proposal that its board of directors has determined in good faith (after consultation with its outside financial advisor and legal counsel) constitutes a Superior Proposal, the [Medley Capital] Board or [Sierra] Board, as applicable, may (x) make an Adverse Recommendation Change in connection with such Superior Proposal if the board of directors effecting the Adverse Recommendation Change determines in good faith (after consultation with its outside financial advisor and legal counsel) that failure to make an Adverse Recommendation Change could reasonably be expected to be inconsistent with the fiduciary duties of the [Medley Capital] Board or [Sierra] Board, as applicable, under Applicable Law, and/or (y) authorize, adopt or approve such Superior Proposal and cause or permit [Medley Capital] or [Sierra], as applicable, to enter into a definitive agreement with respect to such Superior Proposal concurrently with the termination of this Agreement in accordance with Section 9.1(g) or 9.1(i), as applicable, but in each case only after providing the Notice of Adverse Recommendation or Notice of Superior Proposal, as applicable, and entering into good faith negotiations as required by Section 7.IO(f).") (emphasis original).

[184] Trial Tr. at 405:13–20 (Hirtler-Garvey). Brook Taube will be Chairman and CEO of the combined company and will receive an employment package that includes a base $ 600,000 annual salary and a $ 3.2 million incentive bonus comprising $ 2 million in restricted stock units and $ 1.2 million in cash. PTO ¶ II.69. Seth Taube will be Vice Chairman, Senior Executive Vice President and Senior Managing Director of the combined company and will receive an employment package, with a base $ 480,000 annual salary and a $ 1.75 million incentive bonus comprising $ 1.15 million in restricted stock units and $ 600,000 in cash. PTO ¶ II.70. Tonkel will serve as President of the combined company and will receive an employment package, with a base $ 480,000 annual salary and a $ 1.75 million incentive bonus comprising $ 1.15 million in restricted stock units and $ 600,000 in cash. PTO ¶ II.71.

[185] Trial Tr. at 405:16–406:3 (Hirtler-Garvey).

[186] Dkt. 128, Pretrial Order ("PTO") ¶ II.1; JX466; JX 720. FrontFour is on the "smaller scale of hedge funds. Assets under management are ... about $ 150 million." Trial Tr. at 11, 55 (Lorber).

[187] *Id.* at 16.

[188] *Id.*

[189] *Id.* at 16:11–18:6.

[190] *Id.* at 18:19–24.

[191] *Id.* at 24:19–24.

[192] *Id.* at 24:22–23.

[193] *Id.* at 24:6–18.

[194] *Id.* at 25:10–16.

[195] As Lorber described: "[Anderson] said to Steve [FrontFour's representative], 'have you ever done a merger before?' Steve said, 'you know, yes, I have.' And Sam said, 'have you ever done a three-way merger?' Steve said, 'no, actually I haven't.' And then Sam said, 'well, it's very difficult to get three parties to agree on what actually happened.' That was quite alarming. Given that what actually [happened] should be factual. It shouldn't be difficult to get people to agree on what actually happened." *Id.* at 25:10–24.

[196] *Id.* at 26.

[197] *Id.*

[198] *Id.* at 27:16–20.

[199] JX 396. Lorber testified that this was the deadline for nomination letters. Trial Tr. at 29. Medley Capital has not noticed the 2019 annual meeting. *Id.* at 31.

[200] JX 409; Trial Tr. at 27–28. The meeting was held telephonically, as Medley Capital refused FrontFour's request for an in-person meeting. *Id.* at 28.

[201] *Id.* at 28.

[202] JX 409.

[203] JX 421.

[204] JX 365 (Transcript of Aug. 10, 2018 Medley Investor Conference Call re: Merger Overview) at p.2 (“there will be further detail in our proxy which will file in the next few weeks”); Trial Tr. at 25:10–14 (Lorber).

[205] *See* Medley Capital Proxy.

[206] It claimed that, “because each of the proposals submitted included various conditions and carve-outs, and different forms of consideration, some of which was contingent, and in light of the fact that none were binding, it would be both *impracticable* and *speculative* to assign a particular value to any such proposal.” *Id.* at 57 (emphasis added); *see also Id.* at 59. But it was possible to derive enterprise, equity and corresponding per-share values for Medley Management (as well as implied premium calculations) from each of the IOIs; Medley Management and its advisors did exactly that when communicating internally. JX 705.

[207] C.A. No. 2019-0021-KSJM.

[208] *Id.* at Dkt. 17 (Oral Argument on Pls.' Mot. to Expedite and the Court's Ruling).

[209] JX 706.

[210] JX 513.

[211] JX 432.

[212] JX 439.

[213] JX 459; Trial Tr. at 366:22–367:10 (Taube).

[214] JX 458.

[215] JX 472.

[216] *Id.*

[217] JX 488. After NexPoint made its proposals public, ISS changed its recommendation to voting against the Proposed Transactions. ISS initially recommended voting in favor of the merger based on the theory that it was the better of two bad options. JX 463 at p.2 (describing the Proposed Transactions as “the better of the two underwhelming options available to shareholders”).

[218] JX 524.

[219] JX 514.

[220] JX 544.

[221] *See id*; *see also* JX 101.

[222] JX 557.

[223] JX 564.

[224] Medley Capital Corp., Non-Management Solicitation Material (Form DFAN14A) (Mar. 6, 2019).

[225] JX 459; Trial Tr. at 366:22–367:10 (Taube).

[226] Trial Tr. at 188:21–189:1 (Ainsberg); *id.* at 424:2–425:3 (Hirtler-Garvey).

[227] Also, as discussed above, in May 2018, Lantern expressed an interest in a possible transaction that involved a recapitalization of Medley Capital. JX 138. On July 3, 2018, a Lantern representative again reached out to Goldman: “[A]ny chance we can talk today? I have been speaking with Todd Owens [of Broadhaven] about our interest in acquiring [Medley Management] and recapitalizing Medley Capital. Thanks!” JX 197. By that time, Project Integrate was underway. The Special Committee was unaware of this offer when they were negotiating the Proposed Transactions, and it has never been disclosed to Medley Capital stockholders. Despite a call that apparently took place between Lantern and “the company” in late July 2018, followed by an email to Russ Hutchinson, no one from Medley Capital pursued Lantern's proposal. JX 254; Trial Tr. at 188:21–189:1 (Ainsberg) (“Q. And what happened with respect to the proposals, at least at the – what's happened so far with respect to the proposals? That is to say, Zais, NexPoint, and Origami. A. They've all been rejected.”).

[228] Trial Tr. at 222:16–225:7 (Ainsberg); *id.* at 423:5–425:3 (Hirtler-Garvey).

[229] JX 717 at p.11.

[230] Dkt. 1; Dkt. 8 (“Am. Compl.”).

231 Dkt. 63; Dkt. 79.

232 Dkt. 271, 81, 116, 117, 118, 124.

233 Dkt. 128, PTO ¶ II.130.

234 Dkt. 133.

235 Am. Compl. ¶¶ 144–52.

236 *Id.* ¶¶ 153–60.

237 *Id.* ¶¶ 161–67.

238 *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 457 (Del. Ch. 2011).

239 *Id.*

240 *Kahn v. Tremont Corp. (Tremont II)*, 694 A.2d 422, 428 (Del. 1997); *Kahn v. Lynch Commc'n Sys., Inc.*, 638 A.2d 1110, 1115 (Del. 1994); *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983).

241 *In re John Q. Hammons Hotels Inc. S'holder Litig.*, 2009 WL 3165613, at *12 (Del. Ch. Oct. 2, 2009), *interlocutory appeal refused*, 984 A.2d 124 (Del. 2009) (TABLE); *see In re Delphi Fin. Gp. S'holder Litig.*, 2012 WL 729232, at *12 n.57 (Del. Ch. Mar. 6, 2012) (applying entire fairness where the controlling stockholder received differential merger consideration); *see also In re Primedia, Inc. S'holders Litig.*, 67 A.3d 455, 487 (Del. Ch. 2013) (applying entire fairness where "the [m]erger conferred a unique benefit on" the controlling stockholder).

242 *In re Trados Inc. S'holder Litig.*, 73 A.3d 17, 44 (Del. Ch. 2013).

243 *Lynch*, 638 A.2d at 1113 (observing that a stockholder becomes a fiduciary if it "owns a majority interest in ... the corporation" (internal quotation marks omitted)); *see In re PNB Hldg. Co. S'holders Litig.*, 2006 WL 2403999, at *9 (Del. Ch. Aug. 18, 2006) (Strine, V.C.) ("Under our law, a controlling stockholder exists when a stockholder ... owns more than 50% of the voting power of a corporation ...."); *Williamson v. Cox Commc'ns, Inc.*, 2006 WL 1586375, at *4 (Del. Ch. June 5, 2006) ("A shareholder is a 'controlling' one if she owns more than 50% of the voting power in a corporation.").

244 *See Lynch*, 638 A.2d at 1113 (observing that a stockholder becomes a fiduciary if it "*exercises control* over the business affairs of the corporation" (emphasis original)); *In re Tesla Motors, Inc. S'holder Litig.*, 2018 WL 1560293, at *19 (Del. Ch. Mar. 28, 2018) (concluding on a motion to dismiss that it was reasonably conceivable that Musk, owner of 22.1% of company's common stock, was a controller based on well-pled facts related to "Musk's voting influence, his domination of the Board during the process leading up to the [challenged acquisition] against the backdrop of his extraordinary influence with the Company generally, the Board level conflicts that diminished the Board's resistance to Musk's influence, and the Company's and Musk's own acknowledgement of his outsized influence"); *Calesa Assocs. v. Am. Capital, Ltd.*, 2016 WL 770251, at *10–12 (Del. Ch. Feb. 29, 2016) (concluding on motion to dismiss that it was reasonably conceivable that stockholder owning 26% of the company's stock exercised actual control where the plaintiff alleged instances of actual control beyond the fact that the stockholder "exercised duly obtained *contractual* rights to its benefit and to the detriment of the company"); *In re Zhongpin Inc. S'holders Litig.*, 2014 WL 6735457, at *7–8 (Del. Ch. Nov. 26, 2014) (concluding on motion to dismiss that it was reasonably conceivable that stockholder owning only 17.3% of the company's stock was a controller because the stockholder was CEO and the company's 10-K stated that the stockholder effectively controlled the company), *rev'd on other grounds sub nom. In re Cornerstone Therapeutics Inc. S'holder Litig.*, 115 A.3d 1173 (Del. 2015); *Williamson*, 2006 WL 1586375, at *4–5 (concluding on a motion to dismiss that it was reasonably conceivable that two stockholders, owning collectively 17.1% of the company's stock, jointly controlled the company based on their ability to nominate two of the five directors, their ability to influence the flow of revenue into the corporation, and their potential "veto" power over certain corporate decisions); *In re Cysive, Inc. S'holders Litig.*, 836 A.2d 531, 535, 551–52 (Del. Ch. 2003) (Strine, V.C.) (finding post-trial that a stockholder owning 35% of the company's stock controlled the company because he was a "hands-on" "Chairman and CEO of [the company]," and because he had the ability to "elect a new slate [of independent directors] more to his liking without having to attract much, if any, support from public stockholders" through his familial ties with the company's other stockholders); *O'Reilly v. Transworld Healthcare, Inc.*, 745 A.2d 902, 912–13, 915–16

(Del. Ch. 1999) (concluding on motion to dismiss that it was reasonably conceivable that a 49% stockholder exercised actual control where the plaintiff alleged that the stockholder forced the board to comply with its terms on the merger through threats).

245 *See* *Tesla*, 2018 WL 1560293, at *14 ("[T]here is no absolute percentage of voting power that is required in order for there to be a finding that a controlling stockholder exists." (quoting *PNB Hldg.*, 2006 WL 2403999, at *9)); *Calesa Assocs.*, 2016 WL 770251, at *11 (explaining that there is "no correlation between the percentage of equity owned and the determination of control status"); *see In re Crimson Expl. Inc. S'holders Litig.*, 2014 WL 5449519, at *10–12 (Del. Ch. Oct. 24, 2014) (collecting cases discussing when a stockholder may be considered a controlling stockholder).

246 *Tesla*, 2018 WL 1560293, at *13; *In re Rouse Props., Inc.*, 2018 WL 1226015, at *12 (Del. Ch. Mar. 9, 2018) (citing *Sciabacucchi v. Liberty Broadband Corp.*, 2017 WL 2325152, at *17 (Del. Ch. May 31, 2017); *Cysive*, 836 A.2d at 531, and *Lynch*, 638 A.2d at 1114–15); *see In re* *Primedia Inc. Deriv. Litig.*, 910 A.2d 248, 257 (Del. Ch. 2006) ("[T]he plaintiffs need not demonstrate that [the alleged controller] oversaw the day-to-day operations of Primedia. Allegations of control over the particular transaction at issue are enough.").

247 *Rouse*, 2018 WL 1226015, at *12 (citing *Williamson*, 2006 WL 1586375, at *4); *Tesla*, 2018 WL 1560293, at *13; *see also* *Basho Techs. Holdco B, LLC v. Georgetown Basho Inv'rs, LLC*, 2018 WL 3326693, at *27 (Del. Ch. July 6, 2018) ("Broader indicia of effective control also play a role in evaluating whether a defendant exercised actual control over a decision. Examples of broader indicia include ownership of a significant equity stake (albeit less than a majority), the right to designate directors (albeit less than a majority), decisional rules in governing documents that enhance the power of minority stockholder or board-level position, and the ability to exercise outsized influence in the board room, such as through high-status roles like CEO, Chairman, or founder." (footnotes omitted)).

248 *Telxon Corp. v. Meyerson*, 802 A.2d 257, 264 (Del. 2002) (emphasis added); *see also* *Tesla*, 2018 WL 1560293, at *17 ("Even an independent, disinterested director can be dominated in his decision-making by a controlling stockholder.").

249 *Aronson v. Lewis*, 473 A.2d 805, 816 (Del. 1984) *overruled on other grounds by* *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000); *accord* *Tremont II*, 694 A.2d at 430; *Telxon*, 802 A.2d at 264.

250 Mack Dep. Tr. at 16–17.

251 *Id.* at 23–24.

252 *Id.* at 30–31.

253 *Id.* at 44.

254 *Id.*

255 *Id.* at 31.

256 *Id.* at 53.

257 *Id.* at 46–47.

258 *Id.* at 52–53.

259 *Id.* at 52–53.

260 *Id.* at 63.

261 *Id.* at 57. Until his deposition, Mack "never really thought about the entities" involved in the proposal. *Id.* at 118; *see id.* ("I thought it was Medley Capital, but I would say that's just me not digging into who the parties are.").

262 *Id.* at 73.

263 *Id.* at 53.

264 *Id.* at 72–73.

265 *Id.* at 32.

266 *Id.* at 33–34.

267 *Id.* at 34–35.

268 *Id.* at 42–43.

269 *Id.* at 79.

270 *Id.* at 82–83.

271 *Id.* at 80–81, 83.

272 *Id.* at 10–11.

273 *See* *Basho Techs.*, 2018 WL 3326693, at *27 (explaining that a broader indicia of effective control includes “the ability to exercise outsized influence in the board room, such as through high-status roles like CEO, Chairman, or founder”).

274 JX 717 at p.11 (text message chain on January 9, 2019 at 2:56 p.m.: Lerdal: “Old ladies and their schedules ...”; Brook: “Whoa”; Lerdal: “Recommendation will be forthcoming. Proper response. Your question was the proper one.”; Brook: “Which one?”; Lerdal: “Are we going to respond to every f**ksake on the planet?”)

275 *Id.* at p.4.

276 *Id.* at p.1.

277 *Id.* at p.2.

278 *Id.* at p.4.

279 *Id.* at p.4.

280 *Id.* at p.5.

281 *Id.* at pp.6–7.

282 JX 023.

283 *Weinberger*, 457 A.2d at 711.

284 *Id.*

285 *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1163 (Del. 1995) (defendants must prove “to the *court's* satisfaction that the transaction was the product of both fair dealing and fair price” (emphasis original) (internal quotation marks omitted)).

286 *Id.* at 1162 (citing *Weinberger*, 457 A.2d at 711).

287 *In re Dole Food Co., Inc. S'holder Litig.*, 2015 WL 5052214, at *26 (Del. Ch. Aug. 27, 2015).

288 *Lynch*, 638 A.2d at 1120–21. *See also* *In re Tele–Commc'ns, Inc. S'holders Litig.*, 2005 WL 3642727, at *10 (Del. Ch. Dec. 21, 2005) (“[A]n important element of an effective special committee is that it be fully informed in making its determination.”); *Tremont II*, 694 A.2d at 431 (“In evaluating this claim the Court of Chancery correctly stated that “[a] controlling shareholder ... must disclose fully all material facts and circumstances surrounding the transaction.”) (citing *Kahn v. Tremont Corp. (Tremont I*), 1996 WL 145452, at *15 (Del. Ch. Mar. 21, 1996)).

289 *Lynch*, 638 A.2d at 1115 (*citing* *Weinberger*, 457 A.2d at 711).

290 *See* Trial Tr. at 427:3–502:21 (Zenner examination); JX 618 (Zenner Report); Trial Tr. at 94:6–152:20 (Kennedy examination); JX 621 (Kennedy Report).

291 JX 621 (Kennedy Report).

292 Trial Tr. at 475–76 (Zenner).

293 *Id.* at 474–75.

294 *Id.* at 491–92.

295 *See, e.g.*, *Va. Power Energy Mktg., Inc. v. EQT Energy, LLC*, 2012 WL 13034278, at *1 (E.D. Va. May 9, 2012) (holding that a “comment upon the opinion of another expert ... is not a proper subject for expert opinion evidence”).

296 Trial Tr. at 488:3–8 (Zenner).

297 Trial Tr. at 96–98, 103–111 (Kennedy).

298 *In re Appraisal of Dell Inc.*, 2016 WL 3186538, at *36 & n.36 (Del. Ch. May 31, 2016) (“[T]he bulk of any price competition occurs before the deal is signed.”), *aff'd in part, rev'd in part sub nom.* *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd*, 177 A.3d 1 (Del. 2017).

299 *Dole*, 2015 WL 5052214, at *34.

300 *Reis*, 28 A.3d at 467; *accord* *Ross Hldg. & Mgmt. Co. v. Advance Realty Gp., LLC*, 2014 WL 4374261, at *33 (Del. Ch. Sept. 4, 2014) (“Robust procedural protections may support a determination that price was fairly within a range of reasonable values, and a failure of process may prevent a Court from reaching such a conclusion.”); *see* *William Penn P'ship v. Saliba*, 13 A.3d 749, 758 (Del. 2011) (“Merely showing that the

sale price was in the range of fairness, however, does not necessarily satisfy the entire fairness burden when fiduciaries stand on both sides of a transaction and manipulate the sales process."); *Gentile v. Rossette*, 2010 WL 2171613, at *9 (Del. Ch. May 28, 2010) ("From a tainted process, one should not be surprised if a tainted price emerges."); *Bomarko, Inc. v. Int'l Telecharge, Inc.*, 794 A.2d 1161, 1183 (Del. Ch. 1999), *as revised* (Nov. 16, 1999), *aff'd*, 766 A.2d 437 (Del. 2000) ("[T]he unfairness of the process also infects the fairness of the price."); *HMG/Courtland Properties, Inc. v. Gray*, 749 A.2d 94, 116 (Del. Ch. 1999) (holding that the defendants did not satisfy their burden by showing that the price was "within the low end of the range of possible prices that might have been paid in negotiated arm's-length deals" where "[t]he process was ... anything but fair"); *Tremont II*, 694 A.2d at 432 ("[H]ere, the process is so intertwined with price that under *Weinberger*'s unitary standard a finding that the price negotiated by the [special committee] might have been fair does not save the result.").

301 *Auriga Capital Corp. v. Gatz Props.*, 40 A.3d 839, 857–58 (Del. Ch. 2010), *aff'd* 59 A.3d 1206 (Del. 2012). *See also* *id.* at 874–75 ("[The defendant] has argued throughout this litigation that [the property] was worth less than its debt and thus any surplus over zero was a fair price, but I cannot accept this as true based on the record before me. [The defendant] himself is responsible for this evidentiary doubt. He fended off [a potential buyer], gave incomplete information to [the appraiser hired by the LLC], and did not promote a fair Auction process. Thus, I do not view the Auction process as generating a price indicative of what [the property] would fetch in a true arm's-length negotiation. Rather, the evidence suggests that [the property] was worth more than what [the defendant] paid. [The defendant] was not motivated to bid his best price because he knew that he was the only bidder before he finalized his offer ... The fact that we do not have concrete evidence of what a fully negotiated third-party deal would have produced is [the defendant's] own fault, and such ambiguities are construed against the self-conflicted fiduciary who created them.").

302 FrontFour urges the Court to apply enhanced scrutiny to the entirety of the Proposed Transactions, not just the deal protections. They argue that, "as conceived, the entire Transaction is an improper defensive measure implemented by [Medley] Management to advance its own interests ...." Pls.' Post-Trial Br. at 65.

303 More specifically, the deal protections are: (1) a no-shop provision preventing each party from attempting to undermine the Merger Agreement by soliciting other bids, subject to a "Superior Proposal" fiduciary out; (2) an "adverse recommendation change" requirement that the Medley Capital Board recommend that the stockholders vote in favor of the merger, subject to a fiduciary out; and (3) a "termination fee" provision requirement the payment of $ 6 million to Sierra under certain conditions. Defendants' expert quantifies the termination fees as 2.79% of the deal value, and FrontFour does not dispute this computation. JX 618 at p.31.

304 *See* *Paramount Commc'ns, Inc. v. Time Inc.*, 571 A.2d 1140, 1151 (Del. 1989); *Mills Acq. Co. v. Macmillan Inc.*, 559 A.2d 1261, 1288 (Del. 1988). "Deal protections" are provisions of a merger agreement that compensate a jilted third party if the target does not consummate the deal or obstructs disruption of the deal by another transaction. Leo E. Strine, Jr., *Categorical Confusion: Deal Protection Measures in Stock-for-Stock Merger Agreements*, 56 Bus. Law. 919, 922 (2001) [hereinafter *Categorical Confusion*]. Under default rules of the Delaware General Corporation Law, a stockholder can sell control of the company in the minimum number of days permitted under federal securities law. *Id.* at 924 & n.14. Deal protection measures disturb this natural ordering by obstructing a stockholders' ability to engage in other transactions once a merger agreement is signed. Further, mergers require stockholder approval. To be effective, the stockholder vote must be "meaningful and voluntary." *See* 8 *Del. C.* § 251(c). By safeguarding the merger, deal protections encroach on the voluntary nature of the stockholder vote. *Williams v. Geier*, 671 A.2d 1368, 1387 (Del. 1996).

305 *La. Mun. Police Emps.' Ret. Sys. v. Crawford*, 918 A.2d 1172, 1181 n.10 (Del. Ch. 2007) ("The inquiry, by its very nature fact intensive, cannot be reduced to a mathematical equation."); *id.* ("Our courts do not 'presume that all business circumstances are identical or that there is any naturally occurring rate of deal protection, the deficit or excess of which will be less than economically optimal.... [A] court focuses upon the real world risks and prospects confronting [directors] when they agreed to the deal protections.") (internal quotation marks and citation omitted); *see also* *In re BioClinica, Inc. S'holder Litig.*, 2013 WL 5631233, at *8 (Del. Ch. Oct. 16, 2013) ("a no-solicitation provision, a poison pill, a reasonable termination fee, information

rights, and a top-up option ... *in the context of an otherwise reasonable sales process*, have been found non-preclusive" (emphasis added)); *In re Cogent, Inc. S'holder Litig.*, 7 A.3d 487, 501–09 (Del. Ch. 2010) (assessing the preclusive effect of deal protections individually and "in the aggregate"); *Orman v. Cullman*, 2004 WL 2348395, at *6 (Del. Ch. Oct. 20, 2004) (noting that deal protection devices may be unreasonable even if not coercive or preclusive); *Stahl v. Apple Bancorp, Inc.*, 16 Del. J. Corp. L. 1573, 1587 (Del. Ch. Aug. 9, 1990) (Allen, C.) ("Thus, where it is applicable, *Unocal* requires a judicial judgment finely focused upon the particulars of the case.").

306 *Omnicare, Inc. v. NCS Healthcare, Inc.*, 818 A.2d 914, 935 (Del. 2003).

307 *See, e.g.*, *In re Cogent*, 7 A.3d at 502 & n.40 (collecting decisions) ("Potential suitors often have a legitimate concern that they are being used merely to draw others into a bidding war. Therefore, in an effort to entice an acquirer to make a strong offer, it is reasonable for a seller to provide a buyer some level of assurance that he will be given adequate opportunity to buy the seller, even if a higher bid later emerges.").

308 *Id.* at 502.

309 Interestingly, Defendants' expert, Dr. Marc Zenner, presented a comparable transactions analysis related to deal protection devices. In that analysis two-thirds of his comparable set involved a pre-signing formal auction. Of course, this renders the set *not* comparable to the Proposed Transactions. Trial Tr. at 494–95. It also supports the notion that no-shops are outside of the range of reasonableness absent a pre-signing market canvas or efforts to assess potential price competition pre-signing. *See* *Forgo v. Health Grades, Inc.*, C.A. No. 5716-VCS, at 16:18–20 (Del. Ch. Sept. 3, 2010) (TRANSCRIPT) ("Well, you know, if you're not going to do as much on the front end, you got to make sure the back end works.").

310 Merger Agr. § 7.10(e).

311 *See generally In re Complete Genomics, Inc. S'holder Litig.*, C.A. No. 7888-VCL, at 17 (Del. Ch. Nov. 9, 2012) (TRANSCRIPT) (stating that placing restrictions on a board's "ability to change its recommendation" that mirror "the types of conditions and procedures frequently and historically used to regulate a target's contractual ability to terminate a merger agreement and accept a superior proposal" is "fraught with peril"). This Court provided a definitive summary of the relevant issues in *In re Primedia, Inc. Shareholders Litigation*:

> Delaware law requires that a board of directors give a meaningful, current recommendation to stockholders regarding the advisability of a merger including, if necessary, recommending against the merger as a result of subsequent events. This obligation flows from the bedrock principle that when directors communicate publicly or directly with shareholders about corporate matters, the *sine qua non* of directors' fiduciary duty to shareholders is honesty. The duty of loyalty, which mandates that directors act in stockholders' best interests, consequently requires ensuring an informed stockholder vote. The obligation to change as recommendation prior to a stockholder vote can be further viewed as a duty to update a prior material statement. A board may not suggest or imply that it is recommending the merger to the shareholders if in fact its members have concluded privately that the deal is not now in the best interest of the shareholders. ***In light of these principles, the target board must have an ability to make a truthful and candid recommendation consistent with its fiduciary duties—and this duty will be applicable whether or not there is a superior offer.***"

67 A.3d 455, 491–92 (Del. Ch. 2013) (internal quotations and citations omitted) (emphasis added).

312 *See* *In re Del Monte Foods Co. S'holders Litig.*, 25 A.3d 813, 840 (Del. Ch. 2011) (enjoining defensive measures not because the defensive measures themselves failed enhanced scrutiny but because they were "the product of a fiduciary breach").

313 *Unanue v. Unanue*, 2004 WL 2521292, at *10 (Del. Ch. Nov. 3, 2004).

314 *In re Novell, Inc. S'holder Litig.*, 2013 WL 322560, at *13 (Del. Ch. Jan. 3, 2013) (citation omitted).

315 *Klang v. Smith's Food & Drug Ctrs., Inc.*, 702 A.2d 150, 156 (Del. 1997) (footnotes omitted).

316 *Zaucha v. Brody*, 1997 WL 305841, at *5 (Del. Ch. June 3, 1997); *see* *Novell*, 2013 WL 322560, at *13 (explaining that material facts are those which, "under all the circumstances ... would have assumed actual significance in the deliberations of the reasonable shareholder." (citation omitted)).

317 *Arnold v. Soc'y for Sav. Bancorp., Inc.*, 650 A.2d 1270, 1280 (Del. 1994); *see also Rodgers v. Bingham*, C.A. No. 2017-0314-AGB, at 81 (Del. Ch. June 1, 2017) (TRANSCRIPT).

318 *In re Pure Res., Inc., S'holders Litig.*, 808 A.2d 421, 450 (Del. Ch. 2002).

319 *Kahn v. Lynch Commc'n Sys., Inc.*, 669 A.2d 79, 88 (Del. 1995).

320 *See* JX 430 at 72–73.

321 *See* *Morrison v. Berry*, 191 A.3d 268, 287–88 (Del. 2018), *as revised* (July 27, 2018) (reversing trial court's dismissal of disclosure claim after concluding that "stockholders were entitled to know the depth and breadth of the pressure confronting the Company" given "the Company chose to speak on the topic").

322 *See* Trial Tr. at 203–217 (Ainsberg); *Id.* 409–416 (Hirtler-Garvey); JX 628 at pp.13–15.

323 *See* *In re Rural Metro*, 88 A.3d 54, 94 (Del. Ch. 2014) (concluding after a trial that, at the time they approved the transaction, the [directors] were unaware of RBC's last minute efforts to solicit [a] buy-side financing role from Warburg ... and did not know about RBC's manipulation of its valuation metrics," and holding that, "[u]nder the circumstances, the Board's decision to approve Warburg's bid lacked a reasonable informational basis and fell outside the range of reasonableness."); *In re Del Monte Foods Co. S'holders Litig.*, 2011 WL 2535256, at *10 (Del. Ch. June 27, 2011) (fee award opinion emphasizing that lead counsel "uncovered facts not previously known to the [target] board" that "empowered the [target] directors to re-evaluate their prior decisions and reliance on [their financial advisor]").

324 JX 706.

325 JX 513 at pp.3–4.

326 JX 138 at p.4; Trial Tr. at 340–43 (Taube).

327 JX 432.

328 JX 459.

329 *See* Trial Tr. at 366 (Taube); JX 717 at p.11 ("Proper response forthcoming ... Are we going to have to respond to every f**ksake on the planet?").

330 *See* *In re Topps Co.*, 926 A.2d 58, 77 (Del. Ch. 2007) (issuing an injunction after finding that proxy statement misrepresented competing bidder's acquisition proposals and failed to disclose CEO's potentially bid-deterring statements to the market).

331 JX 553 at p.3.

332 *Id.*

333 JX 100.

334 JX 108 ("I am excited to tell you that Medley has agreed to discuss a process for the sale. I've given your name as a possible buyer. I am having a discussion this week and will update you as I know more."); Trial Tr. at 374–75 (Taube).

335 *Malone v. Brincat*, 722 A.2d 5, 10 (Del. 1998).

336 *In re Topps Co.*, 926 A.2d at 77 (issuing injunction after finding that proxy statement misrepresented competing bidder's acquisition proposals).

337 *See* *Malpiede v. Townson*, 780 A.2d 1075, 1096 (Del. 2001) (setting out the elements of an aiding and abetting claim).

338 *In re MeadWestvaco S'holders Litig.*, 168 A.3d 675, 688 (Del. Ch. 2017) (alteration in original) (internal quotation marks omitted); *see* *Allied Capital Corp. v. GC-Sun Hldgs., L.P.*, 910 A.2d 1020, 1039 (Del. Ch. 2006).

339 *Dole*, 2015 WL 5052214, at *3.

340 *Rural Metro*, 88 A.3d at 97.

341 *Singh v. Attenborough*, 137 A.3d 151, 152–53 (Del. 2016) (ORDER); *see* *RBC Capital Markets LLC v. Jarvis*, 129 A.3d 816, 862 (Del. 2015) (affirming imposition of liability on financial advisor who aided and abetted the board's breach of its duty of care). *See generally* Restatement (Second) of Torts § 876 cmt. d (1979) (explaining that secondary liability can attach where the underlying breach "is merely a negligent act" and "applies whether or not the [underlying wrongdoer] knows his act is tortious").

342 Restatement (Second) of Torts § 876(b) (1979); *see In re PLX Tech. Inc. S'holders Litig.*, 2018 WL 5018535, at *47–50 (Del. Ch. Oct. 16, 2018); *Anderson v. Airco, Inc.*, 2004 WL 2827887, at *2–3 (Del. Super. Nov. 30, 2004).

343 *Malpiede*, 780 A.2d at 1098.

344 *RBC Capital*, 129 A.3d at 842 (upholding finding of aiding and abetting where financial advisor inexplicably modified its precedent transaction analysis); *In re Wayport Litig.*, 76 A.3d 296, 322 n.3 (Del. Ch. 2013) ("[A] non-fiduciary aider and abettor could face different liability exposure than the defendant fiduciaries if, for example, the non-fiduciary misled unwitting directors to achieve a desired result."); *Del Monte*, 25 A.3d at 836 (holding that investment bank's knowing silence about its buy-side intentions, its involvement with the successful bidder, and its violation of a no-teaming provision misled the board); *Goodwin v. Live Entm't, Inc.*, 1999 WL 64265, at *28 (Del. Ch. Jan. 25, 1999) (granting summary judgment in favor of defendants charged with aiding and abetting a breach of the duty of care but suggesting that such a claim could proceed if "third-parties, for improper motives of their own, intentionally duped the Live directors into breaching their duty of care"); *see also Mills Acq.*, 559 A.2d at 1283–84, 1284 n.33 (describing management's knowing silence about a tip as "a fraud on the Board"). *Cf. Singh*, 137 A.3d at 152 ("[A]n advisor whose bad-faith actions cause its board clients to breach their situational fiduciary duties ... is liable for aiding and abetting."); *Technicolor*, 663 A.2d at 1170 n.25 ("[T]he manipulation of the disinterested majority by an interested director vitiates the majority's ability to act as a neutral decision-making body.").

345 *Rural Metro*, 88 A.3d at 97 (holding that a party is liable for aiding and abetting when it "participates in the breach by misleading the board or creating the informational vacuum"); *see Mesirov v. Enbridge Energy Co., Inc.*, 2018 WL 4182204, at *15 (Del. Ch. Aug. 29, 2018) (sustaining claim for aiding and abetting against financial advisor for preparing misleading analyses and creating an informational vacuum); *In re TIBCO Software Inc. S'holders Litig.*, 2015 WL 6155894, at *25 (Del. Ch. Oct. 20, 2015) (same); *In re Nine Sys. Corp. S'holders Litig.*, 2014 WL 4383127, at *48 (Del. Ch. Sept. 4, 2014) (holding that interested director aided and abetted breach of duty by failing to adequately explain valuation, thereby misleading the board and creating an informational vacuum), *aff'd sub nom. Fuchs v. Wren Hldgs., LLC*, 129 A.3d 882 (Del. 2015) (TABLE).

346 *Dole*, 2015 WL 5052214, at *42.

347 *PLX*, 2018 WL 5018535, at *49.

348 *Id.*

349 Because FrontFour failed to brief the claim, it was waived. *See In re IBP, Inc. S'holders Litig.*, 789 A.2d 14, 62 (Del. Ch. 2001) (explaining that a party waived its argument by not raising it in its opening post-trial brief); *Zaman v. Amadeo Hldgs., Inc.*, 2008 WL 2168397, at *15 (Del. Ch. May 23, 2008) (explaining that the party waived a defense by failing to raise it in its answer and its pre-trial brief because "[t]hey gave no fair notice").

350 107 A.3d 1049, 1054, 1071–72 (Del. 2014).

351 *See In re MONY Gp. Inc. S'holder Litig.*, 852 A.2d 9, 32–33 (Del. Ch. 2004) (enjoining a transaction until "necessary supplemental disclosure" is made and noting that because the remedy "can be accomplished quickly, there is no basis to believe that an injunction will result in any harm to ... the defendants"); *Matador Capital Mgmt. Corp. v. BRC Hldgs., Inc.*, 729 A.2d 280, 300 (Del. Ch. 1998) (enjoining a transaction until "corrective disclosures consistent with the matters discussed herein" were made and disseminated); *see also State of Wisc. Inv. Bd. v. Bartlett*, 2000 WL 193115, at *2 (Del. Ch. Feb. 9, 2000) (enjoining a transaction to provide time for the stockholders "to assimilate information necessary to assure that they may cast an informed vote").

352 The parties have not briefed the issue of class certification and this decision does not resolve it.

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2012 WL 94678
United States District Court, D. Colorado.

HEALTHONE OF DENVER, IND., a Colorado corporation; HCA–Healthone LLC, a Colorado limited liability company, Plaintiffs,
v.
UNITEDHEALTH GROUP INCORPORATED, a Minnesota corporation, Defendant.

Civil Action No. 10–cv–01633–WYD–BNB.
|
Jan. 12, 2012.

Attorneys and Law Firms

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ORDER

WILEY Y. DANIEL, Chief Judge.

I. INTRODUCTION

***1** THIS MATTER is before the Court on Defendant UnitedHealth Group Incorporated's ["United Health"] Motion to Exclude Testimony of Plaintiffs' Expert Kenneth B. Germain and for Filing Under Seal filed June 17, 2011 (ECF No. 56). A response was filed to the motion on July 11, 2011, a reply was filed on July 28, 2011, and a surreply was filed on October 24, 2011. The portion of the motion that seeks to restrict public access to the expert report of Mr. Germain is granted.[1]

As to the portion of the motion that seeks to exclude Plaintiffs' expert Kenneth Germain, UnitedHealth argues that his testimony should be excluded under Fed.R.Evid. 702 as unhelpful, unreliable and prejudicial because Mr. Germain allegedly "seeks improperly to draw an inference from UnitedHealth's assertion of the attorney-client privilege, to parrot another expert's testimony, and invade the province of the Court." (Mot. to Exclude Testimony 1). Thus, UnitedHealth asserts that his opinions are not relevant or reliable, and should be excluded as they have been in multiple other cases.

The specific opinions that Mr. Germain seeks to offer according to his March 31, 2011 report (Ex. 1 to Def.'s Motion) are that: (1) UnitedHealth should not have used the "UnitedHealthOne" mark because "competent legal advice would have informed it" that use of the mark would violate Plaintiffs' rights (Germain Report at ¶ 8(a)); (2) the survey of Basil G. Englis, another of Plaintiffs' experts, is reliable, legitimate, and admissible and "deserves much credence" (*Id.* at ¶ 8(b)); and (3) the "modern, federalized, widespread doctrine of 'reverse confusion' applies to this case" (*Id.* at ¶ 8(d)). UnitedHealth argues that: (1) Mr. Germain's opinion that UnitedHealth should not have used the "UnitedHealthOne" mark relies improperly on the fact that UnitedHealth asserted the attorney-client privilege; (2) Mr. Germain's opinion regarding the Englis survey is outside the scope of Mr. Germain's expertise and introduces improper legal conclusions; and (3) Mr. Germain's proposed testimony regarding "reverse confusion" attempts to usurp the function of the Court, whose role it is to instruct the jury on the rules of law that apply to the case. I find for the reasons discussed below that United Health's motion should be granted in part and denied in part at this juncture of the case.

II. *ANALYSIS*

A. *Legal Standard*

The court must make two inquiries in connection with whether an expert opinion is admissible. *Ralston v. Smith & Nephew Richards, Inc.,* 275 F.3d 965, 969 (10th Cir.2001). "First, the court ha[s] to determine whether ... the expert ... [i]s qualified by 'knowledge, skill, experience, training, or education' to render an opinion. *Id.* (quoting Fed.R.Evid. 702). A key issue is whether the expert testimony will aid the jury in its determination of the critical issue in the case. *Specht v. Jensen,* 853 F.2d 805, 807 (10th Cir.1988); *see also Wilson v. Muckala,* 303 F.3d 1207, 1219 (10th Cir.2002) ("The 'touchstone' of admissibility of expert testimony is its helpfulness to the trier of fact."). "Expert testimony is appropriate when it relates to issues that are beyond the ken of people of ordinary intelligence.' " *Curtis v. Okla. City Pub. Schs. Bd. of Educ,* 147 F.3d 1200, 1218 (10th Cir.1998) (quotation omitted). "The Tenth Circuit takes a liberal approach to the question of whether proffered expert testimony will assist the jury. Doubts about whether an expert's testimony will be useful should generally be resolved in favor of admissibility unless there are strong factors such as time or surprise favoring exclusions." *Cook v. Rockwell Int'l Corp.,* 580 F.Supp.2d 1071, 1083 (D.Colo.2006).

***2** Second, if the expert is so qualified, the court has to determine whether the opinions are "reliable" under the court's gatekeeping role as set forth in *Daubert v. Merrell Dow Pharmaceuticals, Inc.,* 509 U.S. 579 (1993). When "[f]aced with a proffer of expert scientific testimony ... the trial judge must determine ..., pursuant to Rule 104(a), whether the expert is testifying to (1) scientific knowledge that (2) will assist the trier of fact to understand or determine a fact in issue." *Id.* at 592. "This entails a preliminary assessment of whether the reasoning or methodology underlying the testimony is scientifically valid and of whether that reasoning or methodology properly can be applied to the facts in issue." *Id.* at 592–93. Factors to consider in making this determination include: (a) whether the theory or technique of the expert can be and has been tested, (b) "whether the theory or technique has been subjected to peer review and publication"; (c) the known or potential rate of error of the theory or technique; and (d) whether the theory or technique is "generally accepted". *Id.* at 593–94. The inquiry is a flexible one and "must be solely on the principles and methodology, not on the conclusions the expert generates." *Id.* at 594–595. If the evidence is "shaky but admissible" under the above standard, "[v]igorous cross-examination, presentation of contrary evidence, and careful instruction on the burden of proof are the traditional and appropriate means of attacking" the evidence. *Id.* at 596.

The Supreme Court expanded this analysis in *Kumho Tire Co., Ltd. v. Carmichael,* 526 U.S. 137 (1999), holding that *Daubert's* gatekeeping function also applies to the testimony of experts who are not scientists, but who have "technical" and "other specialized" knowledge. *Id.* "[W]here such testimony's factual basis, data, principles, methods, or their application are called sufficiently into question, ... the trial judge must determine whether the testimony has 'a reliable basis in the knowledge and experience of [the relevant discipline].' " *Id.* at 149 (quoting *Daubert,* 509 U.S. at 592). The factors identified in *Daubert* may or may not be pertinent in assessing the reliability of these opinions, depending on the nature of the issue, the expert's particular expertise, and the subject of his or her testimony. *Id.* at 150.

B. *Whether Mr. Germain's Opinions Should Be Excluded*

According to Mr. Germain's expert report, he is an attorney and has taught "Trademarks", Intellectual Property "and other related classes. (Ex. 1 to Def.' s Mot., ¶ 1(a).) He states that he has often served in an expert witness capacity in civil cases involving a wide variety of issues related to the selection, adoption, use, registration, maintenance and infringement of trade designations of all kinds" and has "been called upon as a potential expert witness on trademark and unfair competition matters on dozens of occasions...." *Id.,* ¶ 1(b).)

***3** While UnitedHealth has raised the applicability of *Daubert,* Mr. Germain does not appear to be relying on scientific testimony but on his experience and training in the area of trademarks and unfair competition. Thus, many of the *Daubert* factors are not relevant. Further, his opinion is not improper simply because it is not scientific. Rule 702 authorizes opinion testimony by experts with "specialized knowledge" which can be acquired through experience and training. *United States v. Garza,* 566 F.3d 1194, 1199 (10th Cir.2009).

Also and importantly, UnitedHealth does not seek to disqualify Mr. Germain based on any lack of skill, specialized knowledge, experience, or qualifications, other than with respect to his lack of expertise in connection with surveys. Indeed, Plaintiffs note that Mr. Germain's trademark opinions have been accepted in similar cases as reliable, qualified and helpful testimony, including a case within this Court which was ultimately affirmed by the Tenth Circuit. *See Vail Associates, Inc. v. Vend–Tel–Co., Ltd.,* Case No. 1:01–cv–01172 (D.Colo. Jan. 4, 2005), *affd,* 516 F.3d 853, 861–863 (10th Cir.2008). While UnitedHealth asserts that Mr. Germain's opinions have been excluded in a number of cases, which cases are attached to its motion, those cases were all decided on the basis of the particular opinions to be delivered in that case. Here also, I will address the specific opinions of Mr. Germain that UnitedHealth objects to and the admissibility of same.

Before doing so, however, I address generally the legal parameters for expert opinions. This should guide the parties in connection with their presentation of expert testimony, including that of Mr. Germain. "Rule 704(a) of the Federal Rules of Evidence 'allows an expert witness to testify in the form of an opinion or inference even if that opinion or inference embraces an ultimate issue to be determined by the trier of fact.' " *United States v. Bedford,* 536 F.3d 1148, 1158 (10th Cir.2008) (citing *A.E. ex rel Evans v. Indep. Sch. Dist. No. 25,* 936 F.2d 472, 476 (10th Cir.1991)). "However, an expert may not simply tell the jury what result it should reach without proving any explanation of the criteria on which that opinion is based or any means by which the jury can exercise independent judgment." *United States v. Dazey,* 403 F.3d 1147, 1171 (10th Cir.2005). "Expert testimony of this sort is sometimes excluded on the ground that it 'usurps the function of the jury in deciding the facts, or interferes with the function of the judge in instructing the jury on the law.' " *Id.*

Further, "[e]xpert witnesses may not testify as to ultimate issues of law governing the jury's deliberations, because instructing the jury is the function of the trial judge." *United States Aviation Underwriters, Inc. v. Pilatus Bus. Aircraft, Ltd.,* 582 F.3d 1131, 1150 (10th Cir.2009). Expert testimony is also not proper "when the purpose of testimony is to direct the jury's understanding of the legal standards upon which their verdict must be based." *Specht,* 853 F.2d at 810. Thus, "[w]hile testimony on ultimate facts is authorized under Rule 704, ... testimony on ultimate questions of law is not favored." *Id.* at 808. "The basis for this distinction is that testimony on the ultimate factual questions aids the jury in reaching a verdict; testimony which articulates and applies the relevant law, however, circumvents the jury's decision-making function by telling it how to decide the case ." *United States Aviation Underwriters,* 582 F.3d at 1150 (citing *Specht,* 853 F.2d at 808).

***4** While "[a]n 'expert may not state legal conclusions drawn by applying the law to the facts, [a]n expert may ... refer to the law in expressing his or her opinion.' " *Bedford,* 536 F.3d at 1158 (quotation omitted). Indeed, an expert witness "may properly be called upon to aid the jury in understanding the facts in evidence even though reference to those facts is couched in legal terms." *Specht,* 835 F.2d at 809. Such testimony is proper so long as "the expert does not attempt to define the legal parameters within which the jury must exercise its fact-finding function." *Id.* Thus, in *Specht,* the court noted that "the question, 'Did T have capacity to make a will?' would be excluded, while the question, 'Did T have sufficient mental capacity to know the nature and extent of his property and the natural object of his bounty to formulate a rational scheme of distribution?' would be allowed." *Id.* 807–08.

These concepts were further explored in *Smith v. Ingersoll–Rand Co.,* 214 F.3d 1235 (10th Cir.2000). In that case, the defendant claimed that a forensic expert's "explanation of hedonic damages constituted impermissible testimony on an ultimate question of law", violating the court's "admonition that 'in no instance can a witness be permitted to define the law of the case.' " *Id.* at 1246 (quoting *Specht,* 853 F.2d at 810). The Tenth Circuit stated that "[t]his rule is not ... a per se bar on any expert testimony which happens to touch on the law; an expert may be 'called upon to aid the jury in understanding the facts in evidence even though reference to those facts is couched in legal terms.' " *Id.* (quoting *id.* at 809).

I now turn to the opinions that are objected to by UnitedHealth.

1. *Opinions as to UnitedHealth's Assertion of the Attorney–Client Privilege*

UnitedHealth first asserts that Mr. Germain's opinion relies improperly on the fact that UnitedHealth asserted the attorney-client privilege or invades that privilege by producing an alleged "adverse inference". UnitedHealth points to the fact that Mr. Germain begins his report by inferring that (1) UnitedHealth's attorney probably gave UnitedHealth "bad news" and warned against using the "UnitedHealthOne" mark (Germain Report at ¶¶ 10(b), 12); (2) UnitedHealth's attorney chose not to put that "bad news" in writing (*id.* at ¶ 10); (3) UnitedHealth then ignored its attorney's advice in favor of "a 'Full speed ahead: damn the torpedoes!' attitude" (*id.* at ¶ 12); and (4) UnitedHealth's attorney or someone else "made a record of the factual and legal reason(s) seen as justifying" UnitedHealth's decision to ignore its attorney's advice. *Id.* UnitedHealth asserts that Mr. Germain predicates these inferences on the fact that UnitedHealth has claimed privilege for confidential communications with its counsel and has not asserted an advice-of-counsel defense.

In response, Plaintiffs attach a redline draft of the report that was proposed to UnitedHealth to address its objections to Mr. Germain's opinions. In that redline draft, Plaintiffs deleted almost all of what UnitedHealth found objectionable. Plaintiffs argue that UnitedHealth did not meaningfully confer with Plaintiffs as required by D.C.COLO.LCivR 7. 1, both before filing the motion and after the motion was filed when Plaintiffs tendered the redlined draft of the expert report to UnitedHealth in an attempt to ameliorate its concerns about Mr. Germain's testimony. While it does appear that UnitedHealth did not confer with Plaintiffs to the maximum extent possible, I decline to deny its motion on that basis since there was at least some effort to meet and confer.

***5** Instead, I address the redline draft of the expert report that I will assume contains what Mr. Germain will not testify to at trial based on Plaintiffs' representation in its response brief. From my review of that report, it does not appear that Mr. Germain will testify about or invoke any adverse inference about the fact that UnitedHealth has chosen not to assert reliance on counsel advice as a defense. Indeed, almost every opinion objected to by UnitedHealth about Mr. Germain improperly using the attorney-client privilege against UnitedHealth has been withdrawn from Mr. Germain's report. To the extent that Mr. Germain may, however, still seek to testify as to issues arising from the attorney-client privilege or advice of counsel, I find this testimony is improper and grant UnitedHealth's motion to exclude testimony on this issue for the reasons stated in UnitedHealth's motion.

Plaintiffs assert now that Mr. Germain will testify as an expert about the contents of the Search Report and the meaning thereof, and that his testimony will be helpful to the trier of fact. Plaintiffs further state that Mr. Germain's analysis of the Search Report requires specialized knowledge, consumes numerous hours of research and review and in no way makes any conclusions as to the ultimate issue in this case, contrary to UnitedHealth's argument. I agree with Plaintiffs that it appears Mr. Germain's expert trademark testimony about the Search Report (as outlined in the redline draft of his report) may be of assistance to the trier of fact.

Plaintiffs state that the Search Report consists of hundreds of pages of references to both registered and common-law marks, canceled registrations, failed applications, domain names, and business names. They contend that his testimony about the meaning of the Search Report would be helpful to the jury to understand the marks already in the marketplace or intended to be in the marketplace at the time UnitedHealth adopted its Marks and, therefore, what knowledge UnitedHealth had or should have had given the contents of the Search Report when it made its decision to adopt the Marks at issue. UnitedHealth has not stated any valid reason why this testimony should be excluded, and I that this testimony appears to be proper. *See* *Children's Med. Center v. Columbia Hosp* ., No. 3–04–2436–BD, 2006 WL 616000, at *5 (N.D.Tex. March 10, 2006) (denying challenge to trademark law professor's opinion on the strength of a mark based on the results of a trademark search report obtained by the plaintiffs because "[a]n expert may base an opinion on facts or data of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject" and the expert stated that search reports are "generally relied upon by trademark practitioners when advising clients as to the availability of marks for use and registration"); *see also* *Larsen v. Ortega,* 816 F.Supp. 97 (D.Conn.1992) (court found that expert testimony was proper as to his factual investigation regarding other companies that used the disputed mark, stating that "[t]here is little doubt that expert testimony on the strength of a plaintiff's trademark or on the degree of similarity within a discreet industry is proper")).[2] Thus, UnitedHealth's motion to exclude is denied as to these issues.

***6** However, I find that Mr. Germain may not opine about the results of his research as they apply to the ultimate issue of trademark infringement. *See* *Children's Med. Center,* 2006 WL 616000 at *6 n. 4; *Bay State Bank v. Baystate Fin. Servs.,* No. 03–40273–FDS, 2007 WL 6064455, at *2 (D.Mass. March 23, 2007). To the extent he was planning to testify as to this ultimate issue, UnitedHealth's motion to exclude is granted.

2. *Opinions About the Englis Survey*

UnitedHealth argues that Mr. Germain's report analyzes a consumer survey conducted by another expert, Basil Englis. It asserts that Mr. Germain does not claim to be an expert on consumer surveys and does not describe any consumer survey that he has conducted, instead referring only to his general "experience reviewing surveys." (Germain Report at TT 1(a), 13(b)). Nonetheless, Mr. Germain opines about the "substantial reliability" and "legal legitimacy" of the Englis survey as well as that the results of the survey are "admissible." (*Id.* at ¶ 8(b)).

UnitedHealth argues that although Mr. Germain concludes that the survey is "fair" and "in accord with the prevailing legal standards," (Germain Report at ¶ 13), he provides no analysis of the survey's methodology to explain those conclusions. Further, Mr. Germain has no expertise in consumer surveys. Accordingly, UnitedHealth argues that Mr. Germain's opinions regarding the Englis survey, including its "substantial reliability" and "legal legitimacy", are outside the scope of his expertise and introduce improper legal conclusions. UnitedHealth further argues that Mr. Germain's testimony regarding the survey is unhelpful to the factfinder because it is cumulative and adds nothing to Mr. Englis' opinion, and is merely an attempt to parrot and bolster the opinions of Mr. Englis.

I agree with UnitedHealth that testimony by Mr. Germain that attempts to bolster the legitimacy of the survey or merely parrot the results of a survey conducted by another person would be improper. *See Dura Auto. Sys. Of Indiana, Inc. v. CTS Corp.,* 285 F.3d 609, 613 (7th Cir.2002) ("it is common in technical fields for an expert to base an opinion in part on what a different expert believes on the basis of expert knowledge not possessed by the first expert; and it is apparent from the wording of Rule 703 that there is no *general* requirement that the other expert testify as well" but an expert may not merely parrot what the other expert said, vouch for that expert, or become that expert's "spokesman".) Plaintiffs assert, however, that they will not present such testimony.

Instead, Plaintiffs argue that citations to the survey are solely for the purpose of providing a proper foundation for Mr. Germain's opinion as required by Fed.R.Civ.P. 26(a)(2)(B). Plaintiffs further assert that Mr. Germain simply seeks to establish that the survey is a legally sufficient foundation on which he may base his opinions regarding reverse confusion, addressed below. I find that testimony from Mr. Germain about the survey may be proper if Mr. Germain can establish a proper foundation for the survey under the Federal Rules of Evidence and can show that the survey is the type of data reasonably relied upon by experts in his field in forming opinions or inferences upon the subject pursuant to Fed.R.Evid. 703. This may well depend on whether or not Mr. Germain has any familiarity with the methods or reasoning used by Mr. Englis in his survey and what his experience is with surveys. *See TK–7 Corp. v. Estate of Barbouti,* 993 F.2d 722, 732 (10th Cir.1993). I am unable to determine this from Mr. Germain's report or the briefing and find that this is an issue better left for trial. Thus, I deny the motion to exclude all testimony regarding the survey, deferring resolution of this issue until trial.

3. *Opinions About Reverse Confusion*

***7** Finally, UnitedHealth asserts that Mr. Germain's report presents opinions as to the law that he contends should apply in this case. In particular, UnitedHealth points to Mr. Germain's opinion that reverse confusion is the law in Colorado and his explanation and advocacy for this law. (Germain Report at ¶ 8(d)). Mr. Germain asserts in his opinion that "... forward and reverse confusion are *not* mutually exclusive; indeed they both can occur at the same time" and that "[a] plaintiff alleging trademark infringement can prove actionable 'likelihood of confusion' by forward *and/or* reverse confusion evidence. (*Id.* at ¶¶ 18(a) and 17(d)). Mr. Germain then concludes that there was a likelihood of confusion because UnitedHealth's advertising efforts were "very likely to produce reverse confusion between 'UnitedHealthOne' and 'HealthOne.' " (*Id.* at ¶ 19(a)). UnitedHealth argues that Mr. Germain does not provide or cite to any evidence of confusion, and that his testimony regarding "reverse confusion" attempts to usurp the function of the Court, whose role it is to instruct the jury on the rules of law.

Plaintiffs argue in response that Mr. Germain's testimony on reverse confusion will not state the law applicable to this case or opine on the ultimate issues. The ultimate issue here is whether there is a likelihood of confusion between the HealthONE marks and the United HealthOne marks. Mr. Germain is opining on *one factor* in the likelihood of confusion analysis, specifically, the actual confusion factor and how the doctrine of reverse confusion can explain the results of the Mind/Share Survey. Plaintiffs further assert that even if Mr. Germain's opinions embraced an ultimate issue, Rule 704 permits such testimony. Mr. Germain does not attempt to define the legal parameters within which the jury must exercise its fact-finding function. Instead, according to Plaintiffs, his opinion focuses on the role reverse confusion plays in the level of actual confusion shown in the control group of the Mind/Share survey. Any stating of the law concerning reverse confusion is merely foundational information for his opinions. Plaintiffs further point out that as Plaintiffs' trademark claim is not based on the doctrine of reverse confusion, there is no danger of Mr. Germain opining or instructing about any rule of law in the jury instructions. Finally, Plaintiffs assert that even if he did opine about any rule of law, the Court could eliminate any concern about that testimony by simply instructing the jury to disregard any of Mr. Germain's testimony inconsistent with its instructions.

I find that this issue should be deferred until trial where I can hear this evidence in context. I note, however, that so long as Mr. Germain does not attempt to tell the jury what the law is or define the law in the instructions, Mr. Germain's testimony on this issue may be proper. Courts routinely admit expert testimony from intellectual property attorneys in trademark cases. *See Olympia Group, Inc. v. Coopers Industries, Inc.,* No. 5:01–CV–423, 2003 WL 25767444, at *1 (E.D.N.C. April 17, 2003); *Sam's Wine & Liquors, Inc. v. Wal–Mart Stores, Inc.,* No. 92 C 5170, 1994 WL 529331, at *8 (N.D.Ill. Sep. 27, 1994). Guidance from a trademark expert regarding the individual likelihood of confusion factors or any survey results upon which to analyze those factors may be appropriate and critically helpful to the trier of fact, providing a proper foundation is laid and the expert has the experience necessary to opine as to these issues.

***8** As set forth in a leading treatise:

> Expert testimony on the factual factors that go into the ultimate finding on the confusion issue is generally quite proper and helpful to both judge and jury.... The expert testimony of expert witnesses is generally allowed on [the likelihood of confusion factors] and other factors which are used to analyze whether the designation is a valid trademark or if there is a likelihood of confusion.

4 J. Thomas McCarthy, McCARTHY ON TRADEMARKS AND UNFAIR COMPETITION § 23:2.75 ("MCCARTHY"). Furthermore, McCARTHY advises that trademark attorneys can be helpful in the jury's understanding of unfamiliar and "perhaps counter intuitive" trademark concepts. *Id.*

Indeed, McCARTHY cites a case within this Circuit where Mr. Germain's testimony was allowed to assist the jury on several of the factors relevant to likelihood of confusion in a trademark case as set forth in *Sally Beauty Co., Inc. v. Beautyco, Inc.*, 304 F.3d 964, 972 (10th Cir.2002). The case in which Mr. Germain testified, captioned *Vail Associates, Inc. v. Vend–Tel–Co., Ltd.*, Case No. 1:01–cv–01172 (D.Colo. Jan. 4, 2005), was ultimately affirmed by the Tenth Circuit, 516 F.3d 853, 861–863 (10th Cir.2008).

Vail Associates centered on the alleged trademark infringement of the plaintiff's mark VAIL by the defendant's mark 1–800–SKI–VAIL. The defendant called on Mr. Germain to testify as to four of the six *Sally Beauty* factors: strength of the mark; similarity of the marks; intent of the defendant; and the degree of care. *Vail Assocs.*, 516 F.3d at 861–63. Not only did the district court seemingly rely on Mr. Germain's opinion in its order finding for the defendant on all claims, but the Tenth Circuit extensively relied on and quoted approvingly whole portions of Mr. Germain's testimony and opinions in affirming the district court's opinion. *See id.* ("Germain's testimony that [the defendant] did not appear to intend to infringe upon [the [plaintiff]'s mark or utilize [the plaintiff]s' reputation was equally critical;" "In this case, Germain's testimony as to the similarities between the two marks at issue is entirely consistent with our analysis of the marks in *Sally Beauty* "). While the Tenth Circuit did not address any challenges to Mr. Germain's testimony, as noted by UnitedHealth, it also did not find such evidence to be improper.

Other courts have also allowed an expert to testify as to factors relevant to likelihood of confusion so long as the expert does not state the ultimate legal conclusion about likelihood of confusion or the verdict the jury should reach with respect to trademark infringement. *See* *Scurmont LLC v. Firehouse Rest. Group, Inc.*, No. 4:09–cv–00618, 2011 WL 2670575, at *8 (D.S.C. July 8, 2011); *Roederer v. J. Garcia Carrion, S.A.*, 2010 WL 489529, at *3 (D.Minn. Feb. 4, 2010); *Sam's Wine & Liquors*, 1994 WL 529331, at *8–9; *YKK Corp. v. Jungwoo Zipper Co.*, 213 F.Supp.2d 1195, 1203 (C. D.Cal.2002). Further, in *Big O Tire Dealers, Inc. v. Goodyear Tire & Rubber Co.*, 561 F.2d 1365, 1371 (10th Cir.1977), the Tenth Circuit noted that the district court was within its discretion in accepting expert testimony from a trademark attorney where the jury was instructed to ignore any testimony contrary to court's instructions.

***9** I also note that the Tenth Circuit has allowed experts to explain the law in certain circumstances. For example, in *Smith v. Ingersoll–Rand Company,* the Tenth Circuit found that the district court did not err in allowing an expert to explain his interpretation of the meaning of hedonic damages where the district court determined that such testimony was relevant. 214 F.3d at 1245–46. The expert "did not attempt to apply the facts of the case 'to the criteria he proffered to the jury; the jury remained free to exercise its fact-finding function.' " *Id.* The court found that the expert's "testimony on hedonic damages no more defined the law of the case than did his testimony regarding the computation of other types of damages" where "he described in great detail the factors the jury could consider in calculating ... lost future earnings". *Id.*

In another case, the Tenth Circuit found that " '[e]xpert testimony by an IRS agent which expresses an opinion as to the proper tax consequences of a transaction is admissible evidence,' ... so long as the expert does not 'directly embrace the ultimate question of whether [the defendants] did in fact intend to evade income taxes,' ....“ *Bedford*, 536 F.3d at 1158 (quotations omitted). *See also* *United States v. Dazey*, 403 F.3d 1147, 1172 (10th Cir.2005); *Okland Oil Co. v. Conoco, Inc.*, 144 F.3d 1308, 1328 (10th Cir.1998).

From the foregoing, I agree with Plaintiffs that consideration of the concept of reverse confusion in connection with Mr.

Germain's discussion of the actual confusion factor may be helpful if this issue is found to be relevant. However, the admissibility of this testimony will turn on many factors, including not only relevance but a balancing of the probative value over any prejudice that could result to the jury under Fed.R.Evid. 403, the extent to which Mr. Germain is qualified to render testimony on this issue in regards to the survey, and the extent to which the testimony may improperly invade the province of the Court regarding instructing on the law. This will, in turn, depend on the particular questions asked of Mr. Germain. Accordingly, a ruling on this issue at this stage of the case is premature, and UnitedHealth's motion to exclude Mr. Germain's testimony is denied as to this argument..

III. *CONCLUSION*

Based upon the foregoing, it is

ORDERED that Defendant UnitedHealth Group Incorporated's Motion to Exclude Testimony of Plaintiffs' Expert Kenneth B. Germain and for Filing Under Seal filed June 17, 2011 (ECF No. 56) is **GRANTED IN PART AND DENIED IN PART** consistent with this Order. The request to prohibit public access to Mr. Germain's report is also **GRANTED.** Mr. Germain's report will be restricted to public access at Level One. *See* D.C.COLO.LCivR 7.2.B.

All Citations

Not Reported in F.Supp.2d, 2012 WL 94678, 87 Fed. R. Evid. Serv. 502

Footnotes

[1] While the motion asks that the report be sealed, the Local Rules of this Court were revised effective December 1, 2011, as to the procedure for restriction of access to documents. Instead of requesting to seal a document, a party must request that the documents be restricted to public access based on restriction levels set forth in the Rules. D.C.COLO.LCivR 7.2.B. Since HP is asking that access to the documents be limited to the parties and the Court, I will assume that HP is seeking a Level One restriction of Mr. Germain's expert report.

[2] I reject UnitedHealth's assertion in its reply that Mr. Germain's opinions from his review of the search report are mere *ipse dixit.*

End of Document

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Only the Westlaw citation is currently available.

UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

IN RE APPRAISAL OF COLUMBIA PIPELINE GROUP, INC.

Cons. C.A. No. 12736-VCL
|
Date Submitted: May 16, 2019
|
Date Decided: August 12, 2019

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MEMORANDUM OPINION

LASTER, V.C.

***1** The petitioners brought this statutory appraisal proceeding to determine the fair value of the common stock of Columbia Pipeline Group, Inc. The valuation's effective date is July 1, 2016, when TransCanada Corporation completed its acquisition of Columbia (the "Merger"). Pursuant to an agreement and plan of merger dated March 17, 2016 (the "Merger Agreement"), each share of Columbia common stock was converted into the right to receive $25.50 in cash, subject to each stockholder's right to eschew the consideration and seek appraisal. This post-trial decision finds that the fair value of Columbia's common stock on the effective date was $25.50 per share.

I. FACTUAL BACKGROUND

The evidentiary record is vast.[1] After an initial spat during the pre-trial process, the parties agreed to 716 stipulations of fact, which were a welcome contribution. During a five-day trial, the parties submitted 1,472 exhibits, including twenty-one deposition transcripts.[2] Nine fact witnesses and five experts testified live. The following factual findings represent the court's effort to distill this record.

A. Columbia

At the time of the Merger, Columbia was a Delaware corporation whose common stock traded actively on the New York Stock Exchange under the ticker symbol "CPGX." Columbia developed, owned, and operated natural gas pipeline, storage, and other midstream assets. As a midstream company, Columbia did not own or sell the commodities that it transported or stored. Columbia's success depended on its contracts with shippers and producers.

Columbia's primary operating asset consisted of 15,000 miles of interstate gas pipelines running from New York to the Gulf of Mexico. The pipelines served the strategically important Marcellus and Utica natural gas basins in Pennsylvania, Ohio, and West Virginia. Columbia's growth-oriented business plan sought to exploit a production boom in the Marcellus and Utica basins by expanding its pipeline network and selling the additional capacity. *See* PTO ¶ 248. The plan required billions of dollars in capital expenditures, which in turn required large amounts of low-cost financing.

***2** Columbia itself was a holding company. Its principal asset was an 84.3% interest in Columbia OpCo LP ("OpCo"), which owned Columbia's operating assets. Columbia's largest business divisions operated interstate pipelines. Smaller divisions operated gas-gathering and processing systems.

Columbia also owned a 100% general partner interest and a 46.5% limited partner interest in Columbia Pipeline Partners, L.P. ("CPPL"), a master limited partnership ("MLP") whose common units traded on the New York Stock Exchange. CPPL owned the other 15.7% interest in OpCo.

Columbia's business plan depended upon using CPPL to raise equity financing for Columbia's growth projects. To raise capital using an MLP, a sponsor like Columbia sells assets to the MLP, receiving cash in return. Because the MLP is a pass-through entity, it can raise capital at a lower cost than the sponsor.[3] Columbia planned to use a variant of the typical method. Rather than having CPPL buy assets from Columbia, CPPL would buy newly issued interests in OpCo, which would use the proceeds to fund Columbia's growth plan.[4] Given the magnitude of Columbia's capital needs, analysts expected that CPPL could own over 60% of OpCo by 2020. *See, e.g.*, JX 258 at 13.

B. NiSource

When the process leading to the Merger began, Columbia was not yet a public company. It was a subsidiary of NiSource Inc., a publicly traded utility company that today serves approximately four million customers in seven states.

In 2005, Robert Skaggs, Jr. became the CEO of NiSource. He also served as chairman of its board of directors. In 2013, Skaggs told the NiSource directors that he wanted to retire in a few years. *See* Taylor Dep. 93. For planning purposes, Skaggs's financial advisor used a target retirement date of March 31, 2016, and cautioned that "the single greatest risk" to Skaggs's retirement plan was his "single company stock position in NiSource." JX 163.

Stephen Smith was NiSource's CFO. Smith, who was fifty-two years old in 2013, considered fifty-five to be the "magical age" to retire. Smith Dep. 97–98; *see* JX 199. He too targeted a retirement date in 2016.

Since 2008, Lazard Frères & Co. had been evaluating a spinoff of Columbia as part of its regular work for NiSource. *See* JX 98 at 7–9. Lazard believed that a spinoff could unlock major value for NiSource.[5] In January 2014, Lazard made a presentation to the NiSource board. Consistent with Lazard's advice, Skaggs and Smith pitched forming CPPL as part of the spinoff to provide a financing vehicle for Columbia. *See* JX 91. For much of 2014, the NiSource board weighed its options.

***3** In summer 2014, *The Deal* reported that Dominion Resources Inc. was trying to buy NiSource. The article described Skaggs as "a willing seller" but only in an all-cash deal at a 20% premium. JX 142.

C. The Spinoff

On September 28, 2014, NiSource announced that it would spin off Columbia as a separate public company. NiSource also announced the formation of CPPL as the "primary funding source" for Columbia's growth capital. JX 182 at 15. CPPL would go public in early 2015. Columbia would follow later that year.

Columbia's post-spinoff business plan contemplated "a potential capital investment opportunity of $12–15 billion over the next 10 years, positioning the company to provide enhanced earnings and dividend growth driven by its projected net investment growth." JX 174. The largest components were pipeline expansion and modernization. JX 182 at 14. If all went according to plan, then Columbia would triple in size. *See* PTO ¶ 291. The plan envisioned funding the growth by having CPPL issue equity over a sustained period.[6]

In December 2014, the NiSource board signed off on Skaggs and Smith leaving NiSource and joining Columbia. Skaggs would become CEO and chairman of the board for Columbia and CPPL; Smith would become CFO of both entities. Skaggs and Smith made the move partly because they did not "want to work forever." JX 208. By this time, two investment banks had told Smith that Columbia would "trade too rich to sell," and Smith sought a third view from Goldman Sachs & Co. *See id.* Goldman believed Skaggs and Smith were eyeing "a sale in near term." *Id.*

***4** On February 11, 2015, CPPL closed its initial public offering, generating net proceeds of approximately $1.17 billion. Under Columbia's business plan, CPPL did not plan to raise additional equity until 2016. JX 304 at 28. In the meantime, Columbia planned to draw over $500 million from a revolving credit facility. *Id.*

As part of the spinoff, Columbia borrowed $2.75 billion through a private placement of debt securities. Columbia used the proceeds to make a $1.45 billion cash distribution to NiSource and to refinance its existing debt. *See id.* Moody's Investors Service rated Columbia's debt at Baa2, one notch above non-investment grade. PTO ¶ 262. Columbia's debt level meant that it could not borrow additional capital to fund its business plan and would have to rely on CPPL. *See* JX 466; JX 1339.

Columbia anticipated that it would become an acquisition target after the spinoff. As part of its pre-transaction planning, Columbia engaged Lazard as its financial advisor.[7] As of May 2015, Lazard categorized the potential acquirers into four tiers, ranked by their ability to pay and likelihood of interest. The first tier consisted of Kinder Morgan, Inc. and Energy Transfer Equity, L.P. The second tier included TransCanada, Berkshire Hathaway Energy, Dominion, Spectra Energy Corp., NextEra Energy, Enbridge Inc., and The Williams Companies. *See* JX 300 at 35; Mir Dep. 136–48.

On May 28, 2015, Lazard contacted TransCanada and mentioned that Columbia might be for sale after the spinoff. JX 311. A contemporaneous memorandum from Skaggs's financial advisor made the point directly: "[Skaggs] noted that [Columbia] could be purchased as early as Q3/Q4 of 2015. I think they are already working on getting themselves sold before they even split. This was the intention all along. [Skaggs] sees himself only staying on through July of 2016." JX 324.

In June 2015, Lazard advised TransCanada against "opening a dialogue" until after the spinoff. JX 335. Doing so could jeopardize the spinoff's tax-free status, which required that NiSource not spin off Columbia in anticipation of a sale. *See* JX 311. Internally, TransCanada discussed that "absent a knock out offer, [Columbia] will likely go for a market check (to maximize proceeds), which we should be prepared for." JX 335.

On July 1, 2015, NiSource completed the spinoff. On its first day of trading, Columbia's stock closed at $30.34 per share.

From the spinoff until the Merger, Columbia's board of directors (the "Board") consisted of Skaggs and six outside directors. The lead independent director was Sigmund Cornelius, an oil and gas veteran who had worked in the pipeline industry and as the CFO of ConocoPhillips. The other directors were Marty Kittrell, Lee Nutter, Deborah Parker, Lester Silverman, and Teresa Taylor. Most had served as directors of NiSource before the spinoff.

D. Early Interest From Possible Buyers

On July 2, 2015, Columbia engaged Goldman to advise on any unsolicited acquisition proposals. JX 347. Over the next two weeks, Dominion and Spectra contacted Skaggs to discuss potential strategic transactions. *See* PTO ¶¶ 391–93. Skaggs viewed the Spectra outreach as trivial, but thought Dominion was worth exploring. *See* JX 359 (Skaggs classifying Spectra outreach as "casual pass" and Dominion as "notable/substantive").

***5** On July 20, 2015, Dominion expressed interest in buying Columbia for $32.50 to $35.50 per share, half stock and half cash. Lazard's contemporaneous discounted cash flow ("DCF") analysis valued Columbia at $30.75 per share, 5% higher than the trading price. *See* PTO ¶ 395. After discussing the expression of interest with the Board and receiving advice from Lazard and Goldman, Skaggs asked Dominion to raise its price to the "upper-$30s." *See id.* ¶¶ 397–98.

On August 12, 2015, Columbia and Dominion entered into a non-disclosure agreement (an "NDA"). PTO ¶ 400; *see* JX 416. The parties began due diligence, but on August 31, Dominion disengaged. Citing a decline in Columbia's stock price amid general stock market volatility, Dominion indicated that even its floor of $32.50 per share had become too high. *See* PTO ¶ 406.

By the end of August 2015, Columbia's stock price had fallen to around $25 per share. By late September, it had fallen to around $18 per share.

Meanwhile, TransCanada continued to examine Columbia as an acquisition target. *See* JX 458. TransCanada's Senior Vice President for Strategy and Corporate Development, François Poirier, was friends with Smith and asked him to dinner on October 26. *See* JX 487. It seems likely that other companies were studying Columbia as well, but it is unclear to what extent other firms were included in the scope of discovery. The petitioners issued subpoenas to Spectra, Berkshire, Dominion, and NextEra. *See* Dkts. 132, 170, 176, 217. They also obtained discovery from Goldman and Lazard.

E. The Equity Overhang

During fall 2015, the energy markets deteriorated, and the market for issuances of equity by MLPs was "effectively closed." JX 466; *see, e.g.*, Kittrell Tr. 1053–54 (citing "sea change" in MLP market that "has continued to this day"). The new market dynamics meant that Columbia could no longer use CPPL to raise equity. *See* JX 466. With $1 billion in short-term funding needs and no capacity to take on more debt, Columbia had to consider issuing equity itself, even though its cost of equity had spiked too.[8]

The confluence of problems created an "equity overhang." JX 466. If investors feared that Columbia could not obtain the capital to achieve anticipated growth rates, then they would bid down the stock. The lower price would force Columbia to issue more equity to raise the same amount of capital, and Columbia could become "mired in a vicious cycle of issuing more and more equity at lower and lower prices."[9]

***6** In a memorandum to the Board dated October 16, 2015, Skaggs summarized Columbia's situation, identifying both problems and potential solutions:

- "[T]he latest intrinsic value studies (which assume that we're able to fully manage CPG's financing, project execution, and counter-party risks) would suggest that CPG's value has dropped roughly 30%."
- "***Required Equity Financing:*** We've raised almost $4 billion of capital (CPPL equity and CPGX debt) – at a very attractive cost of capital – during the first half of '15 to launch CPG as a standalone company. ***Recall*:** because of our investment grade credit rating commitments, CPG cannot issue long-term debt until 2018. Consequently, to support CPG's committed growth program **AND** maintain our investment grade credit ratings, CPG or CPPL still must issue between ***$3 billion*** and ***$4 billion*** of equity (*i.e.*, +/- 65% of CPG's current equity market capitalization) over the next three years (*i.e.*, $1+ billion of equity per year)."
- "***Track 1 – 'Stay the Course'***. Prepare to issue ***~$1.0+* billion** (~15% of CPG) of CPGX equity at +/-$18/share by mid-January.... The current thinking is that we would need to execute the transaction prior to our YE earnings disclosure (2/15) – when we are set to announce yet another increase (~$500 million) in our annual Cap-Ex plan (*i.e.*, a near-term expansion of the equity overhang). **Downside:** if this approach doesn't alleviate the equity overhang (and rather than a positive reaction, CPGX/ CPPL languishes), we face the real threat of ongoing value erosion."
- "***Track 2 – 'Seek a Balance Sheet'***. Explore whether *Dominion* or a select group of blue chip strategic players (*e.g.*, *MidAmerican* ([Berkshire Hathaway Energy]), *Sempra*, *Enbridge*, *TransCanada*, and perhaps *Spectra*) would have a legitimate interest in CPG – at a price that's within CPG's intrinsic value range.... This approach would be an attempt to capture/optimize CPG's intrinsic value (*i.e.*, avoid selling 15% of CPGX at a deep discount); position shareholders to participate in the potential growth of the combined enterprise; fully fund our growth plan, and exert a measure of control over the fate of our employees and other key stakeholders. **Downside:** We believe there is no downside in 'soft' overtures to any or all of these potential counterparties. This approach shouldn't 'put us in play.' "

JX 466.

At a Board meeting held on October 19 and 20, 2015, Skaggs recommended a dual-track strategy in which Columbia would prepare for an equity offering while engaging in exploratory talks with potential strategic or financing partners. PTO ¶ 422. The Board agreed.

F. Renewed Talks With Possible Buyers

On October 26, 2015, Skaggs renewed talks with Dominion. Skaggs offered exclusivity in return for a prompt offer of approximately $28 per share, but he expected Dominion to respond "in the 20–25% premium zip code ($24–$25)."[10] That night Smith met with Poirier, who said that TransCanada wanted to buy Columbia. PTO ¶ 426; JX 487.

On October 29, 2015, the Board decided to wait to hear from Dominion before responding to TransCanada. JX 1399 at 2. The Board determined that Columbia would have to sell substantial public equity unless it received a merger proposal for "around $28 per share." PTO ¶ 428.

***7** On November 2, 2015, Dominion indicated that it could not offer $28 per share. Dominion proposed either (i) an all-stock merger with Dominion and its partner NextEra at an undefined "modest premium" or (ii) a Dominion equity investment in certain Columbia subsidiaries or joint ventures. *See id.* ¶ 430. That day, Columbia's stock closed at $21.12. Goldman believed that at this point, Columbia was trading "very close to 'dcf' value, against a backdrop of having traded at a discount to dcf value." JX 505.

On November 7, 2015, Skaggs followed up with Dominion about the Dominion/NextEra structure. PTO ¶ 436. On November 9, Columbia and TransCanada entered into an NDA. *Id.* ¶ 437. Over the next week, Columbia entered into additional NDAs with Dominion, NextEra, and Berkshire Hathaway Energy, and the NDA counterparties began conducting due diligence.[11]

Each NDA contained a standstill provision that prohibited the counterparty from making any offer to buy Columbia securities without the Board's prior written invitation. Most of the standstills lasted eighteen months. Each contained a feature colloquially known as a "don't-ask-don't-waive" provision (a "DADW"), which prohibited the counterparty from "making a request to amend or waive" the standstill or the NDA's confidentiality restrictions. *E.g.*, JX 526 § 3.

Although due diligence was getting off the ground, Columbia management did not think they could delay an equity offering beyond early December 2015. And waiting until the last possible minute to raise equity exposed Columbia to risk. On November 17, 2015, the Board authorized management to proceed with the equity offering as early as the week of November 30. PTO ¶ 456.

On November 24, 2015, TransCanada expressed interest in an all-cash acquisition at $25 to $26 per share. Berkshire expressed interest in an all-cash acquisition at $23.50 per share. Both expressions of interest were conditioned on further diligence. Berkshire warned that an equity offering would "kill [its] conversation" with Columbia. *Id.* ¶ 477.

On November 25, 2015, the Board decided to terminate merger talks and proceed with the equity offering. Columbia sent letters to Dominion, NextEra, Berkshire, and TransCanada instructing them to destroy the confidential information they had received under their NDAs. NextEra was disappointed to lose the opportunity, but Dominion was happy to go elsewhere. Dominion had already reached out to Questar Corporation, and in February 2016, Dominion announced that it was buying Questar for $4.4 billion, effectively ending any prospect for a Columbia-Dominion merger. *See, e.g.*, PTO ¶ 478; JX 890.

Skaggs called TransCanada and Berkshire personally to reject their offers. TransCanada's CEO, Russell Girling, asked if Columbia would forego the equity offering if TransCanada "close[d] the gap between $26 and $28 and we get it done before Christmas." JX 588; *see also* JX 575 at 4. Skaggs said no. He explained that Columbia could not risk a failed deal followed by a more expensive equity offering in 2016. *See* PTO ¶ 476; Skaggs Tr. 875–77; *see also* JX 594.

***8** The same day, Smith told Poirier that Columbia "probably" would want to pick up merger talks "in a few months." JX 588; *accord* Poirier Tr. 384. Poirier believed that Columbia could have delayed its equity raise until January, but that Columbia went ahead to improve its bargaining position. Poirier also doubted whether Columbia's directors shared management's enthusiasm for a deal. JX 594.

G. The Equity Offering

After the market closed on December 1, 2015, Columbia announced an equity offering at $17.50 per share. PTO ¶ 480. Columbia's stock had closed that day at $19.05. *Id.* ¶ 481. The below-market offering was oversubscribed and raised net proceeds of $1.4 billion. At trial, Skaggs described the offering as "an unmitigated disaster" because Columbia had "sold 25 percent of the company at 17.50." Skaggs Tr. 890. Columbia had solved its short-term funding needs, but the overhang would persist without a long-term solution. *See* JX 1060 at 6; Poirier Tr. 450; Skaggs Dep. 139.

After the equity offering, Skaggs met with Columbia's directors individually to pitch them on selling the company. He emphasized that the business plan involved a "significant amount of execution risk (both financial and operational)." JX 646.

In mid-December 2015, Poirier called Smith to reiterate TransCanada's interest in a deal. They scheduled a meeting for January. Smith Tr. 236–37. Smith involved Skaggs and Goldman, but no one told the Board that Smith was continuing talks with TransCanada.[12] Internally, TransCanada believed that the equity offering had made a deal "more challenging from a valuation standpoint," but regarded Columbia as a "very strategic" target. Poirier Tr. 445; *accord* Marchand Tr. 482.

H. The Poirier Meeting

On January 5, 2016, Smith emailed Columbia's draft 2016 management projections to Poirier. JX 680. Goldman prepared talking points for Smith to use with Poirier, and Skaggs approved them. *See* JX 679 (talking points advising that TransCanada could "avoid an auction process" with a "preemptive" price because "every dollar matters a lot to our Board"); Smith Tr. 248. The talking points were tailored to respond to positions TransCanada had taken during negotiations in November 2015, including TransCanada's stance that it was "not inclined to participate in an auction process" because it would take "resources to get[ ] fully comfortable with the growth projects." JX 575 at 4; *see* JX 589; JX 590. TransCanada had signaled that it would pay extra for exclusivity, and internally it was describing its price strategy as "preemptive." *See* JX 575 at 4.

On January 7, 2016, Smith met with Poirier. Smith literally handed him the list of talking points. Smith Tr. 247–48. Smith stressed that TransCanada was unlikely to face competition from major strategic players, telling TransCanada in substance that Columbia had " 'eliminated' the competition."[13] By doing so, Smith contravened Goldman's advice from 2015 to the effect that "[c]ompetition (real or perceived) is the best way to drive bidders to their point of indifference." JX 505.

***9** Poirier and Smith portrayed these unusual tactics as a good-faith effort to entice TransCanada to bid by assuring TransCanada that it would be worthwhile to engage in due diligence.[14] But TransCanada was going to bid anyway, as it had before. It seems intuitive that Smith's assurance about TransCanada not facing competition would have undermined Columbia's bargaining leverage. At the same time, it is not clear how much of an effect the disclosure had, because TransCanada already knew about the company-specific problems that its competitors faced. *See* Poirier Tr. 435–36 (referring to "other potential suitors being distracted" as "public knowledge").

Regardless, on January 25, 2016, Girling called Skaggs to express interest in an all-cash acquisition in the range of $25 to $28 per share, similar to what TransCanada had proposed in November 2018. PTO ¶ 516. That day, Columbia's stock closed at $17.25.

I. TransCanada Obtains Exclusivity.

In the weeks leading up to Girling's indication of interest, Skaggs had held a second round of one-on-one meetings with the Columbia directors, "priming them for a TC bid." JX 1466; *see id.* (Goldman indicating that Skaggs was "getting questions from the Board 'would you take $26 per share' – he said every day it gets harder to say no"). Lazard had advised Columbia's management that "[w]hile your valuation has swung widely, the $25–28 range is a sensible one given what we have concluded is your DCF value right now." JX 742.

On January 28 and 29, 2016, the Board met with senior management, Goldman, and Columbia's legal counsel from Sullivan & Cromwell LLP. TransCanada had indicated that it would not proceed unless granted exclusivity. The Columbia team considered whether to solicit alternative suitors like Dominion or Spectra. The Board determined that TransCanada's indicative range offered a significant premium that outweighed the costs of exclusivity. *See* PTO ¶ 519; Kittrell Tr. 1061–62 (citing Goldman and Lazard's recommendation); Taylor Tr. 1273–74 (citing high odds of closing and "great" premium).

On February 1, 2016, Columbia granted TransCanada exclusivity through March 2, 2016, which they later extended by six days (the "Exclusivity Agreement"). PTO ¶¶ 523, 551. In simplified terms, Columbia could not accept or facilitate an acquisition proposal from anyone but TransCanada, except that in response to a "bona fide written unsolicited Transaction Proposal that did not result from a breach of" the Exclusivity Agreement, Columbia could engage with another party upon notice to TransCanada. In long form, the Exclusivity Agreement provided that Columbia could not

> (a) solicit, initiate, encourage or accept any proposals or offers from any third person, other than [TransCanada], (i) relating to any acquisition or purchase of all or any material portion of the assets of [Columbia] or any of its subsidiaries, (ii) to enter into any merger, consolidation, reorganization, recapitalization, share exchange or other business combination transaction with [Columbia] or any subsidiary of [Columbia], (iii) to enter into any other extraordinary business transaction involving or otherwise relating to [Columbia] or any subsidiary of [Columbia], or (iv) relating to any acquisition or purchase of all or any material portion of the capital stock of [Columbia] or any subsidiary of [Columbia] (any proposal or offer described in any of clauses (i) through (iv) being a "Transaction Proposal"), or
>
> ***10** (b) participate in any discussions, conversations, negotiations or other communications regarding, furnish to any other person any information with respect to, or otherwise knowingly facilitate or encourage any effort or attempt by any other person to effect a Transaction Proposal;
>
> provided that in response to a bona fide written unsolicited Transaction Proposal that did not result from a breach of this letter agreement (an "Unsolicited Proposal") [Columbia] may, after providing notice to [TransCanada] as required by this letter agreement,
>
> (1) enter into or participate in any discussions, conversations, negotiations or other communications with the person making the Unsolicited Proposal regarding such Unsolicited Proposal,

> (2) furnish to the person making the Unsolicited Proposal any information in furtherance of such Unsolicited Proposal (provided that to the extent such information has not been previously provided to [TransCanada], [Columbia] shall promptly provide such information to [TransCanada]) or
>
> (3) approve, recommend, declare advisable or accept, or propose to approve, recommend, declare advisable or accept, or enter into an agreement with respect to, an Unsolicited Proposal or any subsequent Transaction Proposal made by such person as a result of the discussions, conversations and negotiations or other communications described in clause (1), if the Board of Directors of [Columbia] determines in good faith, after consultation with its outside legal counsel, that the failure to do so would reasonably be expected to be a breach of its fiduciary duties under applicable law.

JX 832 (formatting altered). The Exclusivity Agreement further provided that

> [Columbia] immediately shall cease and cause to be terminated all existing discussions, conversations, negotiations and other communications with all third persons conducted heretofore with respect to any of the foregoing. [Columbia] shall
>
> (x) notify [TransCanada] promptly (and in any event within 24 hours) if any Unsolicited Proposal, or any substantive inquiry or contact with any person with respect thereto, is made and
>
> (y) in any such notice to [TransCanada], indicate the material terms and conditions of such Unsolicited Proposal, inquiry or contact, in the case of clause (y), except to the extent the Board of Directors of [Columbia] determines in good faith, after consultation with its outside legal counsel, that providing such information would not be in the best interests of [Columbia] and its stockholders.

Id. (formatting altered).

J. TransCanada Conducts Due Diligence.

On February 4, 2016, Columbia sent TransCanada a draft of the Merger Agreement. By February 5, TransCanada had sixty-nine personnel accessing Columbia's data room. JX 784. A subset of the personnel comprised a clean team that received access to Columbia's customer contracts, enabling TransCanada to assess Columbia's counterparty risk by examining its customers' creditworthiness. *See* Poirier Tr. 401–03. The parties have referred to these important contracts as “precedent agreements.”[15]

***11** TransCanada had indicated that it would submit a bid by February 24, 2016, with the caveat that it needed backing from credit rating agencies. On February 19, the credit rating agencies warned TransCanada that acquiring Columbia could result in a downgrade. One said that TransCanada was “buying a BBB-mid asset and adding leverage.” JX 827. The other “observed that the resulting leverage from the transaction would be high in a difficult market with heightened counterparty concerns.” PTO ¶ 535. On February 24, Girling told Skaggs that TransCanada needed more time to develop a financing plan that allowed it to pay $25 to $28 per share without hurting its credit rating. *Id.* ¶ 544. Meanwhile, Columbia and TransCanada continued to exchange drafts of the Merger Agreement.

K. Columbia Demands A Price.

On March 4, 2016, the Board directed management to demand a merger proposal from TransCanada. On March 5, TransCanada offered $24 per share, below the low end of the range it had cited to secure exclusivity. Smith told Poirier that he could not recommend $24 per share to the Board, but could recommend $26.50. *See* PTO ¶ 563. TransCanada came back at $25.25, which it characterized as its best and final offer. *Id.* When Skaggs called Girling to reject the offer, Girling said: “I guess that's it.” JX 901. Skaggs told the Board that TransCanada was unlikely to reengage and that “[i]n the meantime, we have stopped all deal-work.” *Id.* Poirier told Smith that TransCanada lacked room to move on price. PTO ¶ 566.

With merger talks on hold, TransCanada's management debated how to justify paying more. *Id.* ¶ 568; JX 912; *see* JX 907. Its CFO, Don Marchand, thought a deal “at $26 would be off-the-charts in terms of premium paid and the market reaction could be quite tepid.” PTO ¶ 568. He believed the transaction was “priced close to perfection at the $25.25 offer level.” *Id.* TransCanada's COO thought Columbia was “playing ... poker to see where our barf price is.” JX 911 at 3. Poirier suggested floating a number like $25.75 or $26, then asking Columbia for another month to find capital and sort out credit rating issues. JX 905 at 3. To fund the Merger, TransCanada ultimately would sell more than $7 billion in assets and raise over $3 billion through the largest subscription receipts offering in Canadian history. JX 939; JX 1008 at 8, 13–14.

On March 6, 2016, TransCanada's management conveyed that they could support a price above $25.25 per share if Columbia's management would support a price below $26.50. *See* PTO ¶ 569. After consulting with Skaggs and Cornelius, Smith asked Poirier to offer $26 per share. *Id.* ¶¶ 570–71. Poirier replied that TransCanada's board needed until March 9 to make a decision.

L. The *Wall Street Journal* Leaks The Merger Talks.

On March 8, 2016, Columbia learned that the *Wall Street Journal* was preparing a story about TransCanada being in advanced discussions to acquire Columbia. TransCanada's exclusivity expired that night. *Id.* ¶¶ 579–81.

On March 9, 2016, TransCanada made a revised offer at $26 per share, with 90% of the consideration in cash and 10% in TransCanada stock. The offer was subject to market conditions and feedback from credit rating agencies and TransCanada's underwriters.

On March 10, 2016, the Board convened to discuss TransCanada's proposal.[16] Skaggs reminded the Board that TransCanada's exclusivity had expired. JX 1399 at 13. The Board discussed that the news story could lead to inbound offers. After the meeting, the *Wall Street Journal* broke the story.[17]

M. Spectra Reaches Out.

***12** After seeing the article, Spectra emailed Skaggs to propose merger talks.[18] On March 11, 2016, the Board decided to renew TransCanada's exclusivity through March 18, subject to further evaluation of Spectra. The Board also instructed management to waive the standstills with Berkshire, Dominion, and NextEra. *See* JX 1399 at 15; *see also* JX 950. The next day, management sent emails waiving the standstills. PTO ¶¶ 603–05.

On the morning of March 12, 2016, the Board determined that Spectra was unlikely to propose a deal superior to TransCanada's latest offer. *See* JX 1399 at 15–16. Around this time, everyone at Columbia acted as if TransCanada's exclusivity had already been renewed. The Board approved a script "to use with Spectra and other inbounds." JX 964. It stated: "We will not comment on market speculation or rumors. With respect to indications of interest in pursuing a transaction, we will not respond to anything other than serious written proposals." JX 1399 at 15–16.

Based on advice from Goldman and Sullivan & Cromwell, Skaggs proposed to send the script to TransCanada. He described this move as a way to reassure TransCanada that its deal remained on track, and to pressure TransCanada to agree to an "expedited" closing. *See* JX 964. After the Board met on March 12, Columbia's in-house counsel asked TransCanada to approve the script:

> [O]ur board has agreed to the renewal of the EA for one week subject to your agreement that this scripted response would not violate the terms of the EA (both in terms of the inbound received in the EA's gap period and going forward until signing, which unfortunately, given the leak, there is a potential that we will receive additional inquiries). Please confirm via response to this email that [TransCanada] is in agreement with this condition/interpretation and we will send over the new EA.

JX 968 at 2. Asking TransCanada whether the script violated the Exclusivity Agreement made no sense. Exclusivity had expired days before. Columbia's in-house counsel also conveyed to TransCanada that Columbia had received "an inbound from a credible, large, midstream player," without saying who it was. JX 973.

The Board had instructed Goldman to screen Spectra's calls so that Spectra could not talk directly with management. *See* JX 957; JX 1399 at 15–16. On March 12, Spectra's CFO called Goldman, and Goldman read the script. *See* JX 974 (Spectra's CFO: "[The Goldman banker] said he had to read from a script that had two messages."). The Spectra CFO told Goldman that "any indication of interest would have to be conditioned on further due diligence." *Id.* Spectra said it could "move quickly" and "be more specific subject to diligence," but the script did not allow for that option. JX 970. As one Goldman banker put it: "Does [Spectra] 'get it' that they aren't going to get diligence without a written proposal?" *Id.* The inverted approach effectively shut out Spectra. TransCanada had not bid without due diligence, and no one else was going to either. *See, e.g.*, JX 1399 at 3 (discussing TransCanada's need for "30 to 45 days of due diligence in order to firm up the potential offer").

***13** Later on March 12, Spectra's head of M&A made a follow-up call. He said to expect a written offer in the "next few days" absent a "major bust." JX 992. The banker who took the call found Spectra's assurance credible, but Skaggs and Smith were not interested.[19] The Board-approved script meant that Columbia could only entertain a "serious written proposal," which Smith defined as

> a bona fide proposal that says I will pay you X for your company. Hard and fast. No outs. No anything. No way to wiggle out of anything. This is going to happen. You're going to pay whatever you're going to pay per share and we're going to sign that agreement and we're done. I don't know of any company that would do that in that short of a timeframe.

Smith Tr. 272. Spectra never made a written offer, and TransCanada never faced competition or a meaningful threat of competition from the anonymous yet "credible, large" industry player that Columbia's management had described. *See* Poirier Tr. 417–18.

N. TransCanada Changes Its Offer.

On March 14, 2016, Columbia renewed TransCanada's exclusivity through March 18, making it retroactive to March 12. PTO ¶ 617; *see* JX 978. After the renewal, Skaggs learned that TransCanada was revising its offer. *See* JX 1005; JX 1006. Citing execution risk with the stock component, TransCanada reduced its offer from $26 per share to $25.50, all cash. PTO ¶ 618. TransCanada threatened that if Columbia did not accept its reduced offer, then TransCanada would "issue a press release within the next few days indicating its acquisition discussions had been terminated." *Id.* Exclusivity terminated automatically upon receipt of TransCanada's reduced offer. *See* JX 978.

At a telephonic meeting held the same day, the Board acknowledged that TransCanada was pushing Columbia to act before Spectra could make an offer.[20] The Board decided to proceed with TransCanada as long as the termination fee in the Merger Agreement did not exceed 3% of equity value. *See id.* On March 15, 2016, Columbia and TransCanada agreed to a termination fee of 3%.

O. The Board Approves The Merger Agreement.

On March 16 and 17, 2016, the Board convened to consider the Merger. Sullivan & Cromwell reviewed the Merger Agreement. Goldman and Lazard opined that the consideration was fair to Columbia's stockholders. Goldman presented a DCF analysis that valued Columbia's stock at $18.64–$23.50 per share. JX 1016 at 107. Lazard's DCF ranges valued the stock at $18.88–$24.38 per share on a sum-of-the-parts basis and at $20.00–$25.50 per share on a consolidated basis. *Id.* at 80; JX 1136 at 75–76. Other valuation methods generated higher and lower ranges.[21] The Board determined that there was a serious risk that TransCanada would withdraw its offer if Columbia delayed signing to buy time for Spectra. The Board also determined that Spectra was unlikely to make a competitive offer, if it made one at all.[22]

***14** At the conclusion of the meeting, the Board unanimously approved the Merger Agreement. Its terms provided for (i) a $309 million termination fee equal to 3% of the Merger's equity value, (ii) a no-shop provision, and (iii) a fiduciary out that the Board could exercise after giving TransCanada four days to match any superior proposal. JX 1025 §§ 4.02, 7.02(b).

P. Columbia's Stockholders Approve the Merger.

Columbia held a special meeting of stockholders on June 22, 2016, to consider the Merger. Holders of 73.9% of the outstanding shares voted in favor of the Merger. Holders of 95.3% of the shares present in person or by proxy at the meeting voted in favor of the Merger. PTO ¶¶ 5–6. The Merger closed on July 1, 2016.

II. LEGAL ANALYSIS

"An appraisal proceeding is a limited legislative remedy intended to provide shareholders dissenting from a merger on grounds of inadequacy of the offering price with a judicial determination of the intrinsic worth (fair value) of their shareholdings." *Cede & Co. v. Technicolor, Inc. (Technicolor*

I), 542 A.2d 1182, 1186 (Del. 1988). Section 262(h) of the Delaware General Corporation Law states that

> the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors.

8 *Del. C.* § 262(h). The statute thus places the obligation to determine the fair value of the shares squarely on the court. *Gonsalves v. Straight Arrow Publ'rs, Inc.*, 701 A.2d 357, 361 (Del. 1997).

Because of the statutory mandate, the allocation of the burden of proof in an appraisal proceeding differs from a traditional liability proceeding. "In a statutory appraisal proceeding, both sides have the burden of proving their respective valuation positions ...." *M.G. Bancorp., Inc. v. Le Beau*, 737 A.2d 513, 520 (Del. 1999). "No presumption, favorable or unfavorable, attaches to either side's valuation ...." *Pinson v. Campbell-Taggart, Inc.*, 1989 WL 17438, at *6 (Del. Ch. Feb. 28, 1989). "Each party also bears the burden of proving the constituent elements of its valuation position ..., including the propriety of a particular method, modification, discount, or premium." Jesse A. Finkelstein & John D. Hendershot, *Appraisal Rights in Mergers and Consolidations*, Corp. Prac. Series (BNA) No. 38-5th, at A-90 (2010 & 2017 Supp.) [hereinafter *Appraisal Rights*].

As in other civil cases, the standard of proof in an appraisal proceeding is a preponderance of the evidence. *M.G. Bancorp.*, 737 A.2d at 520. A party is not required to prove its valuation conclusion, the related valuation inputs, or its underlying factual contentions by clear and convincing evidence or to exacting certainty. *See Triton Constr. Co. v. E. Shore Elec. Servs., Inc.*, 2009 WL 1387115, at *6 (Del. Ch. May 18, 2009), *aff'd*, 2010 WL 376924 (Del. Jan. 14, 2010) (ORDER). "Proof by a preponderance of the evidence means proof that something is more likely than not. It means that certain evidence, when compared to the evidence opposed to it, has the more convincing force and makes you believe that something is more likely true than not." *Agilent Techs., Inc. v. Kirkland*, 2010 WL 610725, at *13 (Del. Ch. Feb. 18, 2010) (internal quotation marks omitted).

***15** "In discharging its statutory mandate, the Court of Chancery has discretion to select one of the parties' valuation models as its general framework or to fashion its own." *M.G. Bancorp.*, 737 A.2d at 525–26. "The Court may evaluate the valuation opinions submitted by the parties, select the most representative analysis, and then make appropriate adjustments to the resulting valuation." *Appraisal Rights*, *supra*, at A-31 (collecting cases). The court also may "make its own independent valuation calculation by ... adapting or blending the factual assumptions of the parties' experts." *M.G. Bancorp.*, 737 A.2d at 524. It is also "entirely proper for the Court of Chancery to adopt any one expert's model, methodology, and mathematical calculations, *in toto*, if that valuation is supported by credible evidence and withstands a critical judicial analysis on the record." *Id.* at 526. "If neither party satisfies its burden, however, the court must then use its own independent judgment to determine fair value." *Gholl v. eMachines, Inc.*, 2004 WL 2847865, at *5 (Del. Ch. Nov. 24, 2004).

In *Tri-Continental Corporation v. Battye*, 74 A.2d 71 (Del. 1950), the Delaware Supreme Court explained in detail the concept of value that the appraisal statute employs:

> The basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him, *viz.*, his proportionate interest in a going concern. By value of the stockholder's proportionate interest in the corporate enterprise is meant the true or intrinsic value of his stock which has been taken by the merger. In determining what figure represents the true or intrinsic value, ... the courts must take into consideration all factors and elements which reasonably might enter into the fixing of value. Thus, market value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or which could be ascertained as of

> the date of the merger and which throw any light on future prospects of the merged corporation are not only pertinent to an inquiry as to the value of the dissenting stockholder's interest, but must be considered .... [23]

Subsequent Delaware Supreme Court decisions have adhered consistently to this definition of value. [24] Most recently, the Delaware Supreme Court reiterated that "[f]air value is ... the value of the company to the stockholder as a going concern," *i.e.* the stockholder's "proportionate interest in a going concern." *Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc.*, 210 A.3d 128, 132–33 (Del. 2019).

***16** The trial court's "ultimate goal in an appraisal proceeding is to determine the 'fair or intrinsic value' of each share on the closing date of the merger." *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*, 177 A.3d 1, 20 (Del. 2017) (quoting *Cavalier Oil*, 564 A.2d at 1142–43). To accomplish this task, "the court should first envisage the entire pre-merger company as a 'going concern,' as a standalone entity, and assess its value as such." *Id.* (quoting *Cavalier Oil*, 564 A.2d at 1144). When doing so, the corporation "must be valued as a going concern based upon the 'operative reality' of the company as of the time of the merger," taking into account its particular market position in light of future prospects. *M.G. Bancorp.*, 737 A.2d at 525 (quoting *Cede & Co. v. Technicolor, Inc. (Technicolor IV)*, 684 A.2d 289, 298 (Del. 1996)); *accord Dell*, 177 A.3d at 20. The concept of the corporation's "operative reality" is important because "[t]he underlying assumption in an appraisal valuation is that the dissenting shareholders would be willing to maintain their investment position had the merger not occurred." *Technicolor IV*, 684 A.2d at 298. Consequently, the trial court must assess "the value of the company ... as a going concern, rather than its value to a third party as an acquisition." *M.P.M. Enters., Inc. v. Gilbert*, 731 A.2d 790, 795 (Del. 1999).

"The time for determining the value of a dissenter's shares is the point just before the merger transaction 'on the date of the merger.' " *Appraisal Rights*, *supra*, at A-33 (quoting *Technicolor I*, 542 A.2d at 1187). Put differently, the valuation date is the date on which the merger closes. *Technicolor IV*, 684 A.2d at 298; *accord M.G. Bancorp.*, 737 A.2d at 525. If the value of the corporation changes between the signing of the merger agreement and the closing, then the fair value determination must be measured by the "operative reality" of the corporation at the effective time of the merger. *See Technicolor IV*, 684 A.2d at 298.

The statutory obligation to make a single determination of a corporation's value introduces an impression of false precision into appraisal jurisprudence.

> [I]t is one of the conceits of our law that we purport to declare something as elusive as *the* fair value of an entity on a given date .... [V]aluation decisions are impossible to make with anything approaching complete confidence. Valuing an entity is a difficult intellectual exercise, especially when business and financial experts are able to organize data in support of wildly divergent valuations for the same entity. For a judge who is not an expert in corporate finance, one can do little more than try to detect gross distortions in the experts' opinions. This effort should, therefore, not be understood, as a matter of intellectual honesty, as resulting in *the* fair value of a corporation on a given date. The value of a corporation is not a point on a line, but a range of reasonable values, and the judge's task is to assign one particular value within this range as the most reasonable value in light of all the relevant evidence and based on considerations of fairness. [25]

Because the determination of fair value follows a litigated proceeding, the issues that the court considers and the outcome it reaches depend in large part on the arguments advanced and the evidence presented.

> An argument may carry the day in a particular case if counsel advance it skillfully and present persuasive evidence to support it. The same argument may not prevail in another

> case if the proponents fail to generate a similarly persuasive level of probative evidence or if the opponents respond effectively.

Merion Capital L.P. v. Lender Processing Servs., L.P., 2016 WL 7324170, at *16 (Del. Ch. Dec. 16, 2016). Likewise, the approach that an expert espouses may have met "the approval of this court on prior occasions," but may be rejected in a later case if not presented persuasively or if "the relevant professional community has mined additional data and pondered the reliability of past practice and come, by a healthy weight of reasoned opinion, to believe that a different practice should become the norm ...." *Global GT LP v. Golden Telecom, Inc. (Golden Telecom Trial)*, 993 A.2d 497, 517 (Del. Ch.), *aff'd*, 11 A.3d 214 (Del. 2010).

***17** In this case, the parties proposed three valuation indicators: (i) the deal price minus synergies, (ii) Columbia's unaffected trading price, and (iii) a DCF analysis. The petitioners relied on the DCF analysis. The respondent relied on the other two metrics. Although technically the respondent in an appraisal proceeding is the surviving company, the acquirer is typically the real party in interest on the respondent's side of the case. In this case, that party is TransCanada. Reflecting this reality, this decision refers to the respondent's arguments as TransCanada's.

A. Deal Price

TransCanada contends that the deal price of $25.50 per share is a reliable indicator of fair value if adjusted downward to eliminate elements of value arising from the Merger. The petitioners argue that the deal price should receive no weight, but that if it does receive weight, then it should be adjusted upward to reflect improvements in value that Columbia experienced between signing and closing. As the proponent of using the deal price, TransCanada bore the burden of establishing its persuasiveness. Each side bore the burden of proving its respective adjustments.

1. Guidance Regarding How To Approach The Deal Price

In three recent decisions, the Delaware Supreme Court has endorsed using the deal price in an arm's-length transaction as evidence of fair value.[26] In each decision, the Delaware Supreme Court weighed in on aspects of the sale process that made the deal price a reliable indicator of fair value, both by describing guiding principles and by applying them to the facts of the case. These important decisions illuminate what a trial court should consider when assessing the deal price as a valuation indicator.

a. *DFC*

The first decision—*DFC*—involved the acquisition of a payday lender (DFC Global) by a private equity firm (Lone Star). *In re Appraisal of DFC Glob. Corp.* (*DFC Trial*), 2016 WL 3753123, at *1 (Del. Ch. July 8, 2016) (subsequent history omitted). The respondent urged the court to rely on the deal price as the most reliable evidence of fair value. *Id.* To assess the deal price, the trial court examined the strength of the sale process, explaining that the deal price "is reliable only when the market conditions leading to the transaction are conducive to achieving a fair price." *Id.*

The pre-signing sale process for DFC Global lasted two years, but proceeded in fits and starts. In April 2012, DFC Global hired a banker to explore a sale to a private equity firm. *Id.* at *3. The banker selected six firms, and a seventh expressed interest independently. By September 2012, none had bid, and the banker spent the next year reaching out to another thirty-five private equity firms and three potential strategic buyers.

In September 2013, two private equity firms—Crestview Partners and J.C. Flowers & Co.—expressed interest in a joint acquisition. In December 2013, Lone Star expressed interest in a transaction at $12.16 per share. After Crestview withdrew from the joint bid, J.C. Flowers expressed interest in a transaction at $13.50 per share.

During due diligence, DFC Global provided both bidders with a lowered set of projections, leading Lone Star to reduce its expression of interest to $11 per share. In March 2014, DFC Global entered into exclusive negotiations with Lone Star. During the exclusivity period, DFC Global provided an even lower forecast, and Lone Star dropped its formal bid to $9.50 per share. Lone Star gave DFC Global twenty-four hours to accept, but later extended the deadline by five days. DFC Global accepted, and the parties announced the transaction publicly on April 2, 2014. It closed on June 13, 2014. *Id.* at *4.

***18** In the appraisal proceeding, the court first worked through the parties' DCF valuations and the respondent's comparable-companies analysis. Having done so, the court turned to the deal price, describing it as "an appropriate factor to consider" and observing that the company "was purchased by a third-party buyer in an arm's-length sale" after a process that "lasted approximately two years and involved [DFC Global's] advisor reaching out to dozens of financial sponsors as well as several potential strategic buyers." *Id.* at *21. The court noted that the deal "did not involve the potential conflicts of interest inherent in a management buyout or negotiations to retain existing management ...." *Id.* Instead, Lone Star took the opposite approach and replaced most of the key executives. *Id.* At the same time, the court expressed concern that DFC Global was facing a period of regulatory uncertainty in which it could not access its full range of strategic options. The evidence also indicated that Lone Star had "focused its attention on achieving a certain internal rate of return and on reaching a deal within its financing constraints, rather than on [DFC Global's] fair value." *Id.* at *22. The trial court also observed that Lone Star had secured exclusivity during a critical phase of the sale process and pressured the company into the final price with an exploding offer. *Id.* at *23. The post-signing phase, by contrast, was relatively open, with a termination fee that "was reasonable and bifurcated to allow for a reduced fee in the event of a superior proposal." *Id.*

The trial court ultimately concluded that each of the three indicators that the parties advanced—the DCF analysis, the comparable-companies analysis, and the deal price—had limitations. But all three provided meaningful insight into DFC Global's value, and all three fell within a reasonable range. The court therefore averaged them, arriving at a valuation of $10.21 per share. *Id.* That outcome reflected a premium of 7.5% over the deal price of $9.50 per share.

On appeal, the Delaware Supreme Court reversed. In its first argument for reversal, the respondent contended that the Delaware Supreme Court should presume that the deal price reflects fair value under specified conditions, effectively asking the Delaware Supreme Court to overrule its decision in *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214 (Del. 2010). There, the high court had rejected a similar request to establish a presumption, explaining that "Section 262(h) neither dictates nor even contemplates that the Court of Chancery should consider the transactional market price of the underlying company. Rather, in determining 'fair value,' the statute instructs that the court 'shall take into account all relevant factors.' " *Id.* at 217 (quoting 8 *Del. C.* § 262(h)). The *Golden Telecom* decision observed that "[r]equiring the Court of Chancery to defer—conclusively or presumptively—to the merger price, even in the face of a pristine, unchallenged transactional process, would contravene the unambiguous language of the statute and the reasoned holdings of our precedent." *Id.* at 218.

In *DFC*, the Delaware Supreme Court again declined to establish a presumption, but cautioned that its

> refusal to craft a statutory presumption in favor of the deal price when certain conditions pertain does not in any way signal our ignorance to the economic reality that the sale value resulting from a robust market check will often be the most reliable evidence of fair value, and that second-guessing the value arrived upon by the collective views of many sophisticated parties with a real stake in the matter is hazardous.

DFC, 172 A.3d at 366. The justices also cautioned that "we have little quibble with the economic argument that the price of a merger that results from a robust market check, against the back drop of a rich information base and a welcoming environment for potential buyers, is probative of the company's fair value." *Id.*

The Delaware Supreme Court then elaborated on what fair value means when evaluating a deal price:

> [F]air value is just that, "fair." It does not mean the highest possible price that a company might have sold for had Warren Buffett negotiated for it on his best day and the Lenape who sold Manhattan on their worst.... Capitalism is rough and ready, and the purpose of an appraisal is not to make sure that the petitioners get the highest conceivable value that might have been procured had every domino fallen out of the company's way; rather, it is to make sure that they receive fair compensation for their shares in the sense that it reflects what they deserve

> to receive based on what would fairly be given to them in an arm's-length transaction.

***19** *Id.* at 370–71.

Addressing the merits, the Delaware Supreme Court reversed the trial court's determination of fair value, noting that the trial court had made the following post-trial findings of fact:

i) the transaction resulted from a robust market search that lasted approximately two years in which financial and strategic buyers had an open opportunity to buy without inhibition of deal protections;

ii) the company was purchased by a third party in an arm's length sale; and

iii) there was no hint of self-interest that compromised the market check.

Id. at 349 (formatting altered). The high court further observed that

> [a]lthough there is no presumption in favor of the deal price, under the conditions found by the Court of Chancery, economic principles suggest that the best evidence of fair value was the deal price, as it resulted from an open process, informed by robust public information, and easy access to deeper, non-public information, in which many parties with an incentive to make a profit had a chance to bid.

Id.

The Delaware Supreme Court cited “the failure of other buyers to pursue the company when they had a free chance to do so” as one of several “objective factors that support the fairness of the price paid ....” *Id.* at 376. The high court also observed that Lone Star “was subjected to a competitive process of bidding[.]” *Id.* at 350. That finding was supported by the competition between Lone Star and J.C. Flowers before signing and the passive market check after signing. The Delaware Supreme Court also explained that “the fact that the ultimate buyer was alone at the end provides no basis for suspicion” given the trial court's findings that

i) there was no conflict of interest;

ii) [DFC Global's investment banker] had approached every logical buyer;

iii) no one was willing to bid more in the months leading up to the transaction before management significantly adjusted downward its projections; and

iv) management continued to miss its targets after Lone Star was the only buyer remaining.

Id. at 376 (formatting altered). The Delaware Supreme Court found that “the record does not include the sorts of flaws in the sale process that could lead one to reasonably suspect that the ultimate price paid by Lone Star was not reflective of DFC's fair value.” *Id.*

Based on this analysis, the Delaware Supreme Court determined that the Court of Chancery's “decision to give one-third weight to each metric was unexplained and in tension with the Court of Chancery's own findings about the robustness of the market check.” *Id.* at 388. The senior tribunal therefore remanded the case for the trial court to “reassess [its] conclusion as to fair value in light of our decision.” *Id.* at 388–89.

b. *Dell*

The second decision—*Dell*—involved a management buyout of Dell Inc. in which its founder and CEO (Michael Dell) teamed up with a private equity firm (Silver Lake) to acquire the company. When the merger agreement was signed, the deal price was $13.65 per share. With the stockholder vote trending against the merger, the buyout group increased its bid to $13.75 per share (the “Final Merger Consideration”).

***20** The respondent contended that the Final Merger Consideration was the best evidence of Dell's fair value on the closing date. *In re Appraisal of Dell Inc. (Dell Trial)*, 2016 WL 3186538, at *21 (Del. Ch. May 31, 2016) (subsequent history omitted). To analyze this contention, the trial court separately examined the pre- and post-signing phases of the transaction process.

The trial court found that bidding during the pre-signing phase had not produced fair value. Three factors contributed to this determination: (i) the bidders' use of leveraged-buyout models to price their bids, (ii) evidence that the stock market had undervalued Dell by focusing on its disappointing short-term prospects, and (iii) limited pre-signing competition. *See id.* at *29–37.

For present purposes, the third factor is most pertinent. The trial court determined that pre-signing competition was limited because Dell's special committee only invited one other private equity firm to compete with Silver Lake at any given time, and all of the firms priced the deal using the same leveraged-buyout financing model that Silver Lake had used. *See id.* at *9–10, *30–31, *37. The committee did not approach strategic buyers during the pre-signing phase, in part because one of the committee's financial advisors (Evercore) discouraged the committee from contacting a wider universe of buyers until the go-shop process, when the advisor would earn a premium for generating a higher bid. *Id.* at *6, *11. The committee's other financial advisor (JPMorgan) expressed concern about the absence of a competitive dynamic and its effect on the bidding. *See id.* at *6, *37.

Having found that the pre-signing phase failed to support the reliability of the deal price, the trial court examined whether the post-signing phase validated it. The merger agreement contemplated a go-shop period, and during this phase, two financial sponsors emerged with competing recapitalizations. In response, and to secure a favorable stockholder vote, the buyout group increased its price to the Final Merger Consideration. *Id.* at *14, *16–18, *37–38. The trial court found that the results of the go-shop ruled out a large gap between the Final Merger Consideration and fair value, because if Dell's value had approached what the petitioners claimed, then a strategic bidder would have intervened. But the trial court also concluded that impediments to bidding undercut the reliability of the go-shop as a price-discovery tool, citing (i) the magnitude of the transaction, (ii) Mr. Dell's participation in the buyout group, including his financial incentives as a net buyer of shares and his valuable relationships with customers, and (iii) information asymmetries between the buyout group and competing bidders. *See id.* at *40–44.

Having concluded that the respondent did not carry its burden of proving the reliability of the deal price, the trial court relied on a DCF analysis. After resolving various disputes between the parties, the trial court made a fair-value determination of $17.62 per share, a result 28% over the deal price. This outcome appeared consistent with the result from the sale process, because it exceeded what a financial sponsor would pay under a leveraged-buyout model, but was below the level where the valuation gap would be sufficiently attractive for a strategic buyer to intervene. It suggested that the company's best option was to remain independent and ride out what appeared to be a trough in the stock price. The trial court perceived that this dynamic permitted the buyout group to take the company private at a premium to market but at a discount to fair value. *See id.* at *51.

***21** On appeal, the Delaware Supreme Court reversed. Consistent with its earlier decisions in *Golden Telecom* and *DFC*, the high court stressed that that "there is no requirement that the court assign some mathematical weight to the deal price ...." *Dell,* 177 A.3d at 23. But on the facts presented, the high court held that the trial court "erred in not assigning any mathematical weight to the deal price" under circumstances suggesting that "the deal price deserved heavy, if not dispositive weight." *Id.*; *accord id.* at 30 ("Overall, the weight of evidence shows that Dell's deal price has heavy, if not overriding, probative value.").

The Delaware Supreme Court explained that Dell's sale process featured "fair play, low barriers to entry, outreach to all logical buyers, and the chance for any topping bidder to have the support of Mr. Dell's own votes ...." *Id.* at 35. In reaching this conclusion, the Delaware Supreme Court viewed the pre-signing process favorably, noting that (i) the members of the special committee who ran the sale process were "independent, experienced ... and armed with the power to say 'no,' " (ii) the committee persuaded the buyout group to raise its bid six times, from an initial range of $11.22-to-$12.16 to $13.65, and (iii) there was "[n]othing in the record [that] suggests that increased competition would have produced a better result." *Id.* at 11, 28. The Delaware Supreme Court also cited "leaks that Dell was exploring strategic alternatives," which corroborated Evercore's assumption that "interested parties would have approached the Company before the go-shop if serious about pursuing a deal." *Id.* at 28. Finally, the high court cited JPMorgan's view that "any other financial sponsor would have bid in the same ballpark as Silver Lake." *Id.*

The Delaware Supreme Court also viewed the post-signing process favorably. The high court cited the number of parties that the committee's bankers contacted and the fact that the go-shop's structure was more flexible than other go-shops. *Id.*

at 29. As with its assessment of the pre-signing phase, the Delaware Supreme Court stressed the absence of evidence that another party was interested in proceeding, explaining that "[f]air value entails at minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay." *Id.*; *see id.* at 32, 34. The absence of a higher bid meant "that the deal market was already robust and that a topping bid involved a serious risk of overpayment[,]" which in turn "suggests the price is already at a level that is fair." *Id.* at 33.

Although it reversed the trial court's finding of fair value, the Delaware Supreme Court did not require that the trial court adopt the deal price: "Despite the sound economic and policy reasons supporting the use of the deal price as the fair value award on remand, we will not give in to the temptation to dictate that result." *Id.* at 44. The high court left it to the trial judge to reach his own conclusion, while "giv[ing] the [trial judge] the discretion on remand to enter judgment at the deal price if he so chooses, with no further proceedings." *Id.*

c. *Aruba*

The third decision—*Aruba*—involved the acquisition of a technology company (Aruba Networks) by a much larger competitor (Hewlett-Packard). *See* *Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc. (Aruba Trial)*, 2018 WL 922139 (Del. Ch. Feb. 15, 2018) (subsequent history omitted). The respondent asked the court to give heavy weight to the deal price. To evaluate its reliability, the trial court examined the sale process in light of the Delaware Supreme Court's decisions in *Dell* and *DFC.*

***22** The pre-signing sale process in Aruba had two phases. In late August 2014, HP approached Aruba about a deal. *Id.* at *7–8. Aruba hired an investment banker (Qatalyst), and the banker and Aruba management anticipated obtaining a deal for around $30 per share. *Id.* at *9. The companies entered into an NDA that restricted HP from speaking with Aruba management about post-transaction employment, and HP began conducting due diligence. After receiving projections from Aruba, HP determined that with synergies, the pro forma value of acquiring Aruba was as high as $32.05 per share. *Id.* at *11. Meanwhile, Qatalyst identified thirteen potential partners and approached five of them. For reasons having "nothing to do with price," none was interested. *Id.* at *10.

Despite the restriction in the NDA, HP asked Aruba's CEO, Dominic Orr, to take on a key role with the combined entity. Orr replied that he had no objection. *Id.* at *11. The parties seemed to be making progress towards a deal, but the HP board of directors balked at making a bid without further analysis, recalling the fallout from HP's disastrous acquisition of Autonomy Corporation PLC in 2011. By the end of November 2014, Orr felt the process had dragged on long enough, and with the approval of the Aruba board, he terminated the discussions. *Id.* at *12.

For its part, HP continued to evaluate an acquisition of Aruba. In December 2014, HP tapped Barclays Capital Inc. as its financial advisor, a firm that had worked for Aruba and had been trying for months to secure the sell-side engagement. *Id.* at *13. On January 21, 2015, HP's CEO met Orr for dinner. During the meeting, when HP's CEO proposed resuming merger talks, Orr responded positively and suggested trying to announce a deal by early March. But HP's CEO also told Orr that because Qatalyst had represented Autonomy when HP acquired it, HP would not proceed if Aruba used Qatalyst. *Id.* at *14.

The Aruba board decided to move forward with the deal and informed Qatalyst about HP's ukase. Aruba was obligated to pay Qatalyst a fee in the event of a successful transaction, so it kept Qatalyst on as a behind-the-scenes advisor. From then on, Qatalyst's primary goal was to repair its relationship with HP, and Qatalyst regarded a successful sale of Aruba to HP as a key step in the right direction. Aruba also needed a new HP-facing banker. It hired Evercore, a firm that was trying to establish a presence in Silicon Valley. During the sale process, Evercore likewise sought to please HP, viewing HP as a major source of future business. *See id.* at *9, *15–16, *19, *21.

The ensuing negotiations proceeded quickly. HP had anticipated making an opening bid of $24 per share, but after Orr's enthusiastic response, HP opened at $23.25 per share. *Id.* at *16–17. Qatalyst reached out to a sixth potential strategic partner, but it was not interested. *Id.* at *17. The Aruba board decided to counter at $29 per share. Evercore conveyed the number to Barclays, but when Barclays dismissed it, Evercore emphasized Aruba's desire to announce a deal quickly. *Id.* at *17–18. On February 10, 2015, twenty days after HP resumed discussions with Orr, the Aruba board agreed to a price of $24.67 per share. *Id.* at *19. The parties negotiated a merger agreement, and on March 1, 2015, the Aruba board approved it.

The post-signing phase was uneventful. On March 2, 2015, Aruba and HP announced the merger. The merger agreement (i) contained a no-shop clause subject to a fiduciary out, (ii) conditioned the out for an unsolicited superior proposal on compliance with an unlimited match right that gave HP five days to match the first superior proposal and two days to match any subsequent increase, and (iii) required Aruba to pay HP a termination fee of $90 million, representing 3% of the Aruba's equity value. No competing bidder emerged, and on May 1, 2015, Aruba's stockholders approved the merger. *Id.* at *21–22.

***23** The trial court found that under *Dell* and *DFC*, Aruba's sale process was sufficiently reliable to make the deal price a persuasive indicator of fair value. The HP-Aruba transaction was an arm's-length merger. The ultimate decision-makers for Aruba—the board and the stockholders—did not face any conflicts of interest. During the sale process, Aruba extracted price increases from HP. There was also evidence that the deal price credited Aruba with a portion of the substantial synergies that the merger would create. And the merger agreement's deal protections were relatively customary and would not have supported a claim for breach of fiduciary duty. *Id.* at *36–38. The trial court therefore viewed the HP-Aruba merger as “a run-of-the-mill, third party-deal,” where “[n]othing about it appears exploitive.” *Id.* at *38.

The trial court next turned to the petitioners' specific challenges to the deal price. The petitioners argued that deal price resulted from a closed-off sale process in which HP had not faced a meaningful threat of competition. *Id.* at *39. The trial court rejected that contention, noting that the petitioners failed “to point to a likely bidder and make a persuasive showing that increased competition would have led to a better result.” *Id.* (citing Dell, 177 A.3d at 28–29, 32, 34). The petitioners proved that HP knew that it did not face a meaningful threat of competition, but they did not show that anyone else would have paid more. *Id.* at *41. Instead, the record showed that none of the six parties that Qatalyst contacted was willing to bid, and no one emerged between signing and closing. *Id.*

The petitioners next argued that the negotiators' incentives undermined the sale process, citing the desire of Aruba's bankers to cater to HP and the more subtly divergent interests of Aruba's CEO. The trial court found that although the petitioners proved that Aruba could have negotiated more aggressively, they did not prove that “the bankers, [the CEO], the Aruba Board, and the stockholders who approved the transaction all accepted a deal price that left a portion of Aruba's fundamental value on the table.” *Id.* at *44.

In other portions of the decision, the trial court found that Aruba's unaffected trading price was a reliable indicator of fair value and rejected the parties' DCF valuations as unreliable. These holdings left the trial court with two reliable valuation indicators: the unaffected trading price and the deal price. The trial court determined that the unaffected trading price was the better measure of the fair value of Aruba's shares. *See id.* at *53–55.

On appeal, the Delaware Supreme Court reversed. The high court found that the trial court had incorrectly relied on the unaffected trading price, but it accepted the trial court's finding that the deal price was a reliable indicator of fair value. *Aruba*, 210 A.3d at 141–42.

Addressing the petitioners' claim that the sale process lacked a competitive bidding dynamic, the Delaware Supreme Court explained that the trial court had misinterpreted *DFC* and *Dell* as downplaying the value of competition. *See id.* at 136. The Delaware Supreme Court emphasized that

> when there is an open opportunity for many buyers to buy and only a few bid (or even just one bids), that does not necessarily mean that there is a failure of competition; it may just mean that the target's value is not sufficiently enticing to buyers to engender a bidding war above the winning price.

Id. The high court then applied this principle to the facts in *Aruba*:

> Aruba approached other logical strategic buyers prior to signing the deal with HP, and none of those potential buyers were interested. Then, after signing and the announcement of the deal, still no other buyer emerged even though the merger agreement allowed for superior bids. It cannot be that an open chance for buyers to

> bid signals a market failure simply because buyers do not believe the asset on sale is sufficiently valuable for them to engage in a bidding contest against each other. If that were the jurisprudential conclusion, then the judiciary would itself infuse assets with extra value by virtue of the fact that no actual market participants saw enough value to pay a higher price. That sort of alchemy has no rational basis in economics.

***24** *Id.* On the facts presented, the level of competition in *Aruba* was sufficient to support the reliability of the deal price.

The Delaware Supreme Court also explained that

> a buyer in possession of material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller when agreeing to buy the company at a particular deal price, and that view of value should be given considerable weight by the Court of Chancery absent deficiencies in the deal process.

Id. at 137. The high court observed that HP and Aruba went "back and forth over price" and that HP had "access to nonpublic information to supplement its consideration of the public information available to stock market buyers ...." *Id.* at 139. The Delaware Supreme Court elsewhere emphasized that "HP had signed a confidentiality agreement, done exclusive due diligence, gotten access to material nonpublic information," and "had a much sharper incentive to engage in price discovery than an ordinary trader because it was seeking to acquire all shares." *Id.* at 140. On the facts presented, the extent of the negotiations in *Aruba* was sufficient to support the reliability of the deal price.

The high court ultimately concluded that Aruba's sale process was sufficiently reliable to render the deal price the best measure of fair value. The Delaware Supreme Court declined to use the trial court's estimate of the deal price minus synergies, instead adopting HP's contemporaneous synergies estimate and remanding with instructions that "final judgment be entered for the petitioners in the amount of $19.10 per share plus any interest to which the petitioners are entitled." *Id.* at 142.

2. Applying The Delaware Supreme Court's Precedents To This Case

The Delaware Supreme Court's precedents indicate that the sale process in this case was sufficiently reliable to make the deal price a persuasive indicator of fair value. These authorities call for rejecting the petitioners' challenges to the sale process.

a. Objective Indicia Of Deal-Price Fairness

When assessing whether a sale process results in fair value, it is critical to recall that "fair value is just that, 'fair.' " DFC, 172 A.3d at 370. "[T]he key inquiry is whether the dissenters got fair value and were not exploited." *Dell*, 177 A.3d at 33. "The issue in an appraisal is not whether a negotiator has extracted the highest possible bid." *Id.* Rather, "the purpose of an appraisal is ... to make that [the petitioners] receive fair compensation for their shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction." DFC, 172 A.3d at 370–71.

When applying this standard, the Delaware Supreme Court has cited "objective indicia" that "suggest[ ] that the deal price was a fair price." *Dell*, 177 A.3d at 28; *accord* DFC, 172 A.3d at 376. In each of its recent decisions, the Delaware Supreme Court found that the objective indicia outweighed the sale processes' shortcomings. In this case, a similar analysis shows that the deal price is a reliable indicator of fair value.

***25** First, the Merger was an arm's-length transaction with a third party. *See* DFC, 172 A.3d at 349 (citing fact that "the company was purchased by a third party in an arm's length sale" as factor supporting fairness of deal price). TransCanada was a pure outsider with no prior stock ownership in Columbia.

Second, the Board did not labor under any conflicts of interest. Six of the Board's seven members were experienced outside directors. *Cf.* *Dell*, 177 A.3d at 28 (citing fact that special committee was "composed of independent, experienced directors and armed with the power to say 'no' " as factor supporting fairness of deal price). Columbia's stockholders were widely dispersed, and the petitioners have not identified divergent interests among them.

Third, TransCanada conducted due diligence and received confidential insights about Columbia's value.[27] Like the acquirer in *Aruba*, TransCanada "had signed a confidentiality agreement, done exclusive due diligence, gotten access to material nonpublic information," and had a "sharp[ ] incentive to engage in price discovery ... because it was seeking to acquire all shares." *Aruba*, 210 A.3d at 140.

Fourth, during the first pre-signing phase, Columbia contacted other potential buyers, and those parties failed to pursue a merger when they had a free chance to do so. *See* *DFC*, 172 A.3d at 376 (citing "failure of other buyers to pursue the company when they had a free chance to do so" as factor supporting fairness of deal price). The degree of pre-signing interaction is similar to or compares favorably with the facts in the Delaware Supreme Court precedents.[28]

Fifth, Columbia negotiated with TransCanada and extracted multiple price increases. *See* *Aruba*, 210 A.3d at 139 (citing "back and forth over price"); *Dell*, 177 A.3d at 28 (citing fact that special committee "persuaded Silver Lake to raise its bid six times"). After TransCanada offered $24 per share, Columbia said no. When TransCanada raised its offer to $25.25, Columbia again said no. The deal price of $25.50 per share was more than any other party had ever seriously offered, including before the equity offering when Columbia sold 25% of its stock for less than its trading price.

***26** Finally, no bidders emerged during the post-signing phase, which is a factor that the Delaware Supreme Court has stressed when evaluating a sale process.[29] The suite of deal protections in the Merger Agreement fell within the norm, making the absence of a topping bid significant.

Considering these factors as a whole, the sale process that led to the Merger bore objective indicia of fairness that rendered the deal price a reliable indicator of fair value.

b. Management Conflicts

As their central theme in this case, the petitioners argue that Skaggs and Smith engineered a fire sale of Columbia to obtain personal benefits.[30] They cite evidence that both had targeted a 2016 retirement date. *E.g.*, JX 163; JX 251. Each had a change-in-control agreement that paid out triple the sum of his base salary and target annual bonus if he retired after a sale of Columbia. If the sale occurred after July 1, 2018, then the multiple would drop from triple to double. PTO ¶¶ 206, 217; Taylor Tr. 1263. When Columbia separated from NiSource, both joined Columbia knowing that it was likely to be an acquisition target. According to the petitioners, the executives then strived to engineer a near-term sale, knowing they would come out ahead even in a sale at less than fair value.

The *Aruba* decision involved a sale process where the top executive and the company's investment bankers had conflicting incentives. The CEO wanted to retire, but he cared deeply about the company and its employees. When HP proposed to acquire Aruba and keep the CEO on to integrate the companies, it offered the perfect path "to an honorable personal and professional exit." *Aruba Trial*, 2018 WL 922139, at *5; *see id.* at *43 (analyzing CEO's conflict). Aruba's investment bankers faced more direct conflicts because both wanted to curry favor with HP. Qatalyst was desperate to save its Silicon Valley franchise, and Evercore was auditioning for future business. *Id.* at *43. The trial court acknowledged the petitioners' concerns, but found that the conflicting incentives did not undermine the deal price as an indicator of fair value:

> The evidence does not convince me that the bankers, Orr, the Aruba Board, and the stockholders who approved the transaction all accepted a deal price that left a portion of Aruba's fundamental value on the table. Perhaps different negotiators could have extracted a greater share of the synergies from HP in the form of a higher deal price. Maybe if Orr had been less eager, or if Qatalyst had not been relegated to the back room, then HP would have opened at $24 per share. Perhaps with a brash Qatalyst banker leading the negotiations, unhampered by the Autonomy incident, Aruba might have negotiated more effectively and gotten

> HP above $25 per share. An outcome along these lines would have resulted in HP sharing a greater portion of the anticipated synergies with Aruba's stockholders. It would not have changed Aruba's standalone value. Hence, it would not have affected Aruba's fair value for purposes of an appraisal.

***27** *Id.* at *44. On appeal, the Delaware Supreme Court accepted the reliability of the deal price as a valuation indicator and used it when making its own fair value determination. *Aruba*, 210 A.3d at 141–42.

The *Dell* decision also involved a conflict: Mr. Dell, the company's founder and top executive, was a buy-side participant in the management buyout and would emerge from the transaction with a controlling stake. He did not lead the negotiations on the sell side (that task fell to the special committee), but the trial court regarded his involvement as a factor cutting against the reliability of the deal price. For example, the trial court found that Mr. Dell gave the buyout group a leg-up given his relationships within the company and his knowledge of its business, and the trial court accepted the testimony of a sale-process expert that if bidders competed to pay more than what Mr. Dell's group would pay, then they risked a winner's curse. *Dell Trial*, 2016 WL 3186538, at *42–43. Mr. Dell also was a net purchaser of shares in the buyout, so any increase in the deal price cost him money.

> If Mr. Dell kept the size of his investment constant as the deal value increased, then Silver Lake would have to pay more and would demand a greater ownership stake in the post-transaction entity. Subramanian showed that if Mr. Dell wanted to maintain 75% ownership of the post-transaction entity, then he would have to contribute an additional $250 million for each $1 increase in the deal price. If Mr. Dell did not contribute any additional equity and relied on Silver Lake to fund the increase, then he would lose control of the post-transaction entity at a deal price above $15.73 per share. Because Mr. Dell was a net buyer, any party considering an overbid would understand that a higher price would not be well received by the most important person at the Company.

Id. at *43 (footnote omitted). These factors did not make Mr. Dell's involvement with the buyout group preclusive, as that term is used in an enhanced scrutiny case, because Mr. Dell testified credibly that he was willing to work with any bidder, and there was evidence that two of the buyout group's competitors had questioned Mr. Dell's value. But for purposes of price discovery in an appraisal case, the trial court perceived that Mr. Dell's involvement and incentives undermined the effectiveness of the sale process and the reliability of the deal price. *Id.* at *44.

On appeal, the Delaware Supreme Court held that Mr. Dell's involvement in the buyout group had not undermined the sale process. *See* *Dell*, 177 A.3d at 32–33. The high court noted that "the [trial court] did not identify any possible bidders that were actually deterred because of Mr. Dell's status." *Id.* at 34. The Delaware Supreme Court also emphasized Mr. Dell's willingness to work with rival bidders during due diligence and the absence of evidence that Mr. Dell would have left the company if a rival bidder prevailed. *Id.* at 32–34. The high court concluded that the lack of a higher bid did not call into question the sale process, because "[i]f a deal price is at a level where the next upward move by a topping bidder has a material risk of being a self-destructive curse, that suggests the price is already at a level that is fair." *Id.* at 33.

***28** In this case, management's divergent interests fell short of the conflicts that failed to undermine the sale process in *Dell*. The alignment issue confronting Skaggs and Smith more closely resembled the negotiators' incentives in *Aruba*. Like Aruba's CEO and its bankers, Skaggs and Smith had personal reasons to secure a deal under circumstances where disinterested participants might have preferred a standalone option: Their change-in-control benefits incentivized them to favor selling Columbia before 2018. To minimize the risk of missing that window, it was safer to act sooner rather than later. *See* *In re Rural Metro Corp.*, 88 A.3d 54, 94–95 (Del. Ch. 2014) (discussing how incentives of contingently compensated representative are generally aligned with principal's but diverge over whether to do a deal at all), *aff'd sub nom.* *RBC Capital Mkts., LLC v. Jervis*, 129 A.3d 816 (Del. 2015).

But Skaggs and Smith also had countervailing incentives to pursue the best deal possible. Their change-in-control benefits included significant equity components that appreciated with a higher deal price. After the Merger, Skaggs retired and received change-in-control payments totaling $26.8 million, with over $19 million from equity awards. Skaggs received an additional $30 million when the Merger cashed out his nearly 1.2 million shares and phantom shares of Columbia stock. Smith similarly retired and received change-in-control payments totaling $10.9 million, with over $7.3 million from equity awards. PTO ¶¶ 654, 656; JX 1370 at 17–18; *see* JX 1346 ¶¶ 12, 27.

> When directors or their affiliates own "material" amounts of common stock, it aligns their interests with other stockholders by giving them a "motivation to seek the highest price" and the "personal incentive as stockholders to think about the trade off between selling now and the risks of not doing so."

Chen v. Howard-Anderson, 87 A.3d 648, 670–71 (Del. Ch. 2014) (quoting *In re Dollar Thrifty S'holder Litig.*, 14 A.3d 573, 600 (Del. Ch. 2010)); *see also* *Lender Processing*, 2016 WL 7324170, at *22 (discussing incentive to maximize deal price where target managers were net sellers and would not retain jobs post-merger). That said, the equity components in the change-in-control benefits did not fully solve the alignment problem, because their contingent nature made their recipients more averse to losing a deal, thereby limiting their incentive to push for the final nickel or quarter. *See* *Rural Metro*, 88 A.3d at 94–95 (discussing how incentives of contingently compensated representative and principal diverge during final negotiations).

In sum, there is evidence to support the petitioners' theory, and I have considered it seriously. Ultimately, however, I cannot credit it. Although Skaggs and Smith wanted to retire, they were professionals who took pride in their jobs and wanted to do the right thing. They were not going to arrange a fire sale for below Columbia's standalone value, and the Board would not have let them.

Consistent with their incentives and professional responsibilities, Skaggs and Smith rejected opportunities for a quick sale. When Dominion expressed interest at an all-time high valuation, Skaggs demanded more. Instead of taking what they could get from Berkshire or TransCanada in fall 2015, Skaggs and Smith recommended a dilutive equity raise. JX 534; JX 1399 at 2–3. When Columbia told TransCanada that it was pursuing the equity raise, Girling offered a prompt deal at a higher price. JX 588. Skaggs thought that was too risky for Columbia and declined. A Columbia director recognized that by pursuing the equity raise, Skaggs and Smith had opted for "BIG, at least near, financial hits to your net worth." JX 621.

When negotiations with TransCanada resumed, Skaggs remained focused on obtaining a fair price. While awaiting TransCanada's formal offer in February 2016, Skaggs told Cornelius that "if the cash portion of the initial salvo [is] below $25, I would be inclined to not even counter." JX 855. When TransCanada offered $24, Skaggs and Smith said it was a nonstarter. *See* PTO ¶ 563. TransCanada came back at $25.25, and Skaggs recommended that the Board reject it. JX 1399 at 10; Skaggs Tr. 908–10; *see* Cornelius Tr. 1142–43. The Board agreed, and after Skaggs told Girling, Lazard and Skaggs believed the deal had died and that Columbia would be proceeding with its standalone plan. *See* JX 901; JX 906; JX 913.

***29** The most troubling event in the deal timeline is Smith's one-on-one meeting with Poirier, when he explained that TransCanada lacked competition. But Columbia did not take TransCanada's $24 per share offer, or even its $25.25 offer. Skaggs and the Board held out for a higher price, ultimately obtaining the Merger consideration of $25.50.

There is some evidence that if the Board had said no to $25.50 per share, then TransCanada would have looked for ways to go back up to $26. *See* Poirier Tr. 420–21. That prospect is insufficient to undermine the deal price for appraisal purposes. *See* *Dell*, 177 A.3d at 33 (explaining that fair value in an appraisal is not a measure of "whether a negotiator has extracted the highest possible bid"); *accord* *DFC*, 172 A.3d at 370.

The evidence does not convince me that the Skaggs, Smith, and the Board accepted a deal price that left a portion of Columbia's fundamental value on the table. As in *Aruba*, perhaps different negotiators could have done better. If they had, then the higher price would have resulted in TransCanada sharing a portion of the anticipated synergies with Columbia's stockholders. It would not have affected whether Columbia's stockholders received fair value.

c. Claims Of Favoritism During The Pre-Signing Process

In their second attack on the sale process, the petitioners contend that the pre-signing phase "yields no reliable indication of fair value" because Columbia favored TransCanada over opportunities with other buyers. *See* Dkt. 428 at 73–74. It is true that Columbia began to favor TransCanada over time, but that was because a deal with TransCanada offered higher and more certain value than the alternatives.

The *Aruba* decision illustrates how a targeted pre-signing process can evolve to focus on a single bidder without undermining the deal price as an indicator of fair value. There, the initial phase of the sale process involved outreach to five potential strategic partners, and Aruba's banker later contacted a sixth. All declined to bid. During the second phase of the process, Aruba effectively engaged in a single-bidder negotiation with HP, and the petitioners proved that HP knew that it did not face a meaningful threat of competition. *Aruba Trial*, 2018 WL 922139, at *40–41. As the high court made clear on appeal, this fact pattern did not mean that there was insufficient competition, nor did it render the deal price unfair. *See* *Aruba*, 210 A.3d at 136 ("[W]hen there is an open opportunity for many buyers to buy and only a few bid (or even just one bids), that does not necessarily mean that there is a failure of competition; it may just mean that the target's value is not sufficiently enticing to buyers to engender a bidding war above the winning price.").

The sale process in this case followed a similar pattern. It is true that Columbia did not treat all bidders identically, but Columbia's actions did not result in an ineffective sale process or unreliable deal price. Rather than favoring TransCanada throughout, Columbia initially expected Dominion to be the logical buyer. After TransCanada's unsolicited outreach to Smith in October 2015, Columbia remained focused on Dominion, believing that it could pay more. *See* PTO ¶ 428. In early November 2015, when Dominion said it could not meet the Board's ask of $28 per share, Lazard recommended broadening the process with private outreach to TransCanada, Berkshire, and Spectra to "put pressure on [Dominion]." JX 503 at 2–3. Goldman agreed and recommended conducting a broader market test only if the private process failed to produce a bid materially greater than $24 per share. *See* JX 505.

***30** The targeted pre-signing process ultimately included Dominion, NextEra, TransCanada, and Berkshire, but not Spectra. The petitioners fault Columbia for not pursuing Spectra, but they failed to prove that more vigorous pursuit "would have produced a better result." *Dell*, 177 A.3d at 28. On November 3, 2015, Spectra's CEO emailed Skaggs to request a meeting or telephone call "in the next couple of weeks to discuss what we may be able to accomplish together." JX 500. The two talked by phone on November 9. During the call, Spectra's CEO "referenced potential strategic opportunities for Columbia and Spectra, but provided no specifics ... and did not request a follow-up meeting or conversation." PTO ¶ 438. Skaggs told Spectra to move quickly, because otherwise Columbia would end talks and proceed with an equity offering. Skaggs Tr. 960; *see id.* at 871. After the call, Spectra went "radio silent." Skaggs Tr. 879; *accord* JX 541. On November 17, Skaggs reported to the Board that Spectra's CEO "had again expressed interest in a potential strategic transaction ... but had only spoken in terms of generic transaction considerations and had not provided a specific, actionable proposal or requested a substantive follow-up." PTO ¶ 456. In a November 25 update to the Board, Skaggs confirmed that "no additional word had been received" from Spectra. *Id.* ¶ 471. Spectra had a "free chance" to pursue Columbia during the pre-signing phase. *DFC*, 172 A.3d at 376. Spectra's failure to act does not undermine the fairness of the deal price.

The petitioners next claim that Columbia gave more information to TransCanada than to others in November 2015. The simple answer is that the bidders requested different levels of information. Berkshire was the most demanding.[31] TransCanada was next, and both TransCanada and Berkshire asked for redacted precedent agreements. Dominion did not receive them because it did not ask.

The petitioners also complain that Skaggs gave TransCanada and Berkshire an informal bid deadline of November 24, 2015, without sharing the deadline with Dominion. Columbia told all of the parties it contacted to act quickly before Columbia pivoted to an equity offering, so Dominion knew there was time pressure. *See* Skaggs Tr. 960–61. By November 22, because of extensive interactions with TransCanada and Berkshire, Columbia management expected imminent indications of interest from those firms. Dominion "ha[d] been radio silent." JX 569. Sure enough, TransCanada and Berkshire made prompt bids, and Dominion did not. The petitioners cite an email from November 25, 2015 in which Dominion's partner, NextEra, expressed surprise when Columbia called off the sale process to pursue an equity offering, saying that the deadline "was news to us —we were working on it." JX 592. Dominion and NextEra knew they had to move quickly, and had they been more interested, they would have. There is no evidence that an expression of interest from Dominion and NextEra would have been sufficiently competitive and sufficiently actionable to cause Columbia to forego the equity offering and agree to a preemptive transaction at a higher value than the Merger.

The petitioners likewise claim that Columbia unduly favored TransCanada after the equity offering. As it did throughout the process, Columbia pursued the best opportunity. Columbia first focused on Dominion. Because of Dominion's reticence, Columbia next focused on Berkshire and TransCanada. After the equity offering, Berkshire withdrew for good, calling Columbia's business model "fundamentally broken." *See* JX 547. TransCanada, by contrast, called to express continued interest. That call spurred Smith's meeting with TransCanada in January 2016. *See* Smith Tr. 323; *accord id.* at 234.

As with the evidence regarding management conflicts, Smith's one-on-one meeting with Poirier is the most serious evidence of favoritism towards TransCanada. But as noted in the section on management's incentives, Columbia did not take TransCanada's $24 per share offer, or even its $25.25 offer. Skaggs and the Board forced Columbia to pay $25.50. The results of Columbia's negotiations compare favorably with the facts in *Aruba* and *DFC*. During the meat of the negotiations in *Aruba*, the company focused exclusively on HP, which knew that it was not facing competition. HP had anticipated offering $24 per share and then giving ground. When Aruba's CEO responded with enthusiasm to HP's approach, HP instead made an opening bid of $23.25. Although HP later increased its bid, after adjusting for a corrected share count, HP described the deal price of $24.67 as "the new $24.00." *See* *Aruba Trial*, 2018 WL 922139, at *39–41. Likewise, in *DFC*, Lone Star was the only bidder that negotiated price with DFC Global, and rather than increasing its bid, Lone Star lowered it twice. *See* *DFC Trial*, 2016 WL 3753123, at *3–4.

***31** The petitioners make similar arguments about Columbia's decision to grant exclusivity to TransCanada and to treat the exclusivity as effectively remaining in place even after it terminated. As with Smith's meeting with Poirier, the fact that only one bidder bids "does not necessarily mean that there is a failure of competition ...." *Aruba*, 210 A.3d at 136. The trial court in *DFC* found that DFC Global had granted Lone Star exclusivity at an inopportune point in the negotiations and that Lone Star had pressured the company with an exploding offer. *See DFC Trial*, 2016 WL 3753123, at *23. But those factors did not undermine the reliability of the deal price given the objective indicia of fairness that were also present in this case. *See* *DFC*, 172 A.3d at 349–50, 375–76.

As with their arguments about management incentives, the petitioners have mustered evidence that supports their theory of bidder favoritism, but they failed to show that Columbia favored TransCanada to a degree that left fundamental value on the table. The Board and management believed that TransCanada was the optimal buyer to pursue, which is why they gave TransCanada exclusivity and continued to deal with TransCanada. *See* PTO ¶ 519. Put simply, "[n]othing in the record suggests that increased competition would have produced a better result." *Dell*, 177 A.3d at 28.

d. The Standstills

The petitioners appear to argue that the standstills distinguish this case from those where the deal price was reliable despite weak interest from potential suitors. They assert that Columbia permitted TransCanada to breach its standstill by reengaging after the equity offering, while at the same time failing to waive the standstills that bound rival bidders. Although the Board ultimately waived the standstills with Dominion, NextEra, and Berkshire in March 2016, the petitioners say it should have done so sooner, claiming that by that point TransCanada had an insurmountable head start towards a transaction.

Each party that engaged with Columbia during fall 2015 entered into an NDA containing a standstill provision substantially in the form of the following:

> In consideration for being furnished with Evaluation Material by [Columbia], each Party (each such Party in such context, the "Standstill Party") agrees that until the date that is eighteen months after the date of this [NDA], unless [Columbia's] board of directors otherwise so specifically requests in writing in advance, the Standstill Party shall not, and shall cause its Representatives not to ... directly or indirectly,
>
> (A) acquire or offer to acquire, or seek, propose or agree to acquire ... beneficial ownership ... or constructive economic ownership ... of any securities or material assets

> of [Columbia], including rights or options to acquire such ownership,
>
> (B) seek or propose to influence, advise, change or control the management, board of directors, governing instruments or policies or affairs of [Columbia], including by means of a solicitation of proxies ..., contacting any person relating to any of the matters set forth in this [NDA] or seeking to influence, advise or direct the vote of any holder of voting securities of [Columbia] or making a request to amend or waive this provision or any other provision of this Section 3 or of Section 1 or Section 2 or
>
> (C) make any public disclosure, or take any action that could require the other Party to make any public disclosure, with respect to any of the matters that are the subject of this [NDA]....

JX 526 § 3 (formatting altered); *see* PTO ¶ 455. The standstills prohibited the counterparties from "seek[ing]" to acquire Columbia or influence its management without the Board's prior written invitation.

***32** The petitioners proved at trial that TransCanada breached its standstill several times. The first breach occurred in mid-December 2015, when Poirier called Smith to convey TransCanada's continued interest in acquiring Columbia. The second breach occurred when Poirier and Smith met in January 2016. There are other instances.[32]

The petitioners posit that but for their own standstills, Berkshire, Dominion, or NextEra would have competed with TransCanada in spring 2016, driving up the deal price. But there is no evidence that Dominion or NextEra had any interest in reengaging with Columbia after the equity offering, and Berkshire refused to do so.[33]

***33** In March 2016, Columbia waived the standstills. If Berkshire, Dominion, or NextEra wanted to bid, then they could have done so in the post-signing phase (but they did not). Their failure to do so resembles the fact pattern in *Aruba*, which cited the absence of bidding during a passive post-signing market check as supporting the fairness of the price. *See* *Aruba*, 210 A.3d at 136 ("[A]fter signing and the announcement of the deal, still no other buyer emerged even though the merger agreement allowed for superior bids."). The *DFC* decision also involved a passive post-signing market check in which no bidders emerged. *DFC*, 172 A.3d at 359.

The evidence does not show that the standstills undermined the fairness of the deal price. None of the standstill parties wanted to bid, and they in fact did not bid.

e. Claims About An Information Vacuum

In a variant of their arguments about bidder favoritism, the petitioners contend that Skaggs and Smith misled the Board or otherwise ran the sale process unsupervised. They posit that but for these actions, the Board would have engaged more vigorously with other bidders. If credited, these arguments would show that the Board could have gotten more than fair value, but they would not show that the deal price fell below that mark. *See* *DFC*, 172 A.3d at 370 (noting that "the purpose of an appraisal is not to make sure that the petitioners get the highest conceivable value that might have been procured had every domino fallen out of the company's way").

On different facts, fraud on the board could lead to a deal price below fair value. In this case, the petitioners' assertions are largely unsupported. The Board received a steady flow of information, with Skaggs regularly keeping the directors informed through written memos, presentations during meetings, and one-on-one communications.[34]

The petitioners contend that Skaggs misled the Board in November 2015 by failing to report that Spectra asked for a meeting, but Skaggs testified credibly that he regarded Spectra's passes as "casual passes" that "weren't serious." Skaggs Tr. 946. The petitioners also say that Skaggs should have told the Board that he gave TransCanada and Berkshire a bid deadline of November 24, 2015, without sharing the deadline with the other suitors. The better view of the evidence is that Skaggs told all of the interested parties that they had to move quickly before Columbia pivoted to an equity offering in December. TransCanada and Berkshire received more specific guidance because they showed the most interest. The petitioners also assert that Skaggs should have told the Board that not all suitors received the same due diligence in November 2015, but the bidders got what they requested.

As with the petitioners' other challenges to the sale process, their best argument centers on Smith's meeting with Poirier on January 7, 2016. Smith sent Poirier confidential due diligence materials and assured him that TransCanada faced no competition. The Board did not authorize the meeting or the disclosures.[35] And although Skaggs generally was forthcoming with the Board, in this instance Skaggs told the Board that TransCanada had reached out to Smith, without mentioning that Smith met with Poirier and without reporting Smith's unauthorized disclosures. *See* JX 698.

***34** The petitioners have identified a flaw in the process, but they have not shown that it led to a price below fair value. After Poirier's meeting with Smith, TransCanada proposed a price range similar to its indication from before the equity offering. Columbia declined and pushed back.

The petitioners also assert that when the Board met on January 28 and 29, 2016, Skaggs "manipulate[d] the Board into approving a TransCanada bid." Dkt. 428 at 21–22. Skaggs presented a chart discussing what the directors "would have to believe" about Columbia's future trading price to reject a merger proposal at $26 per share, and Skaggs recommended that the Columbia directors accept an offer at $26 unless they believed Columbia would trade at $30.11 in 2017. JX 753 at 9. Goldman prepared the initial version of the chart, and at trial, the petitioners pressed Skaggs on why his version omitted a column which showed that the directors should be indifferent to an offer at $26 per share if they believed Columbia would trade at $27.69 at a 8.5% cost of equity in 2016. *See* Skaggs. Tr. 982–90. In reality, Skaggs' chart was Goldman's summary of the other charts it had prepared. *Compare* JX 753 at 9, *with* JX 726 at 4. The absent column came from a chart that Skaggs did not present. Skaggs did not mislead the Board by presenting the summary chart in its entirety.

Finally, the petitioners fault Skaggs for not telling the Board that on March 12, 2016, Spectra requested due diligence and promised a written offer "in the next few days," or that Goldman thought Spectra was "serious." JX 992. The Board had previously approved a script that required a "serious written proposal" as a condition to diligence. Skaggs prepared for an offer from Spectra by having Goldman get an ability-to-pay analysis ready. *See* JX 1009. Goldman determined that at a price of $25.50, Spectra risked a credit downgrade and dilution until 2019.[36] Spectra never made a written offer.

The petitioners did not prove that the Board was misled or deprived of material information. The petitioners did prove that management at times knew more about the sale process, which is inevitable because directors do not run companies on a day-to-day basis. The record does not show that informational differences led to a deal price below fair value.

f. The Stockholder Vote

In an entire fairness case, the unitary entire fairness standard "embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained." *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983). Drawing on an entire fairness case, TransCanada posits that the informed approval of disinterested stockholders, especially by a large margin, "is compelling evidence that the price was fair." *ACP Master, Ltd. v. Sprint Corp.*, 2017 WL 3421142, at *29 (Del. Ch. July 21, 2017), *aff'd*, 2018 WL 1905256 (Del. Apr. 23, 2018) (ORDER). The petitioners take the opposite tack and argue that if they can show defects in the stockholder approval process, such as disclosure violations, then that should undermine a claim that the deal price reflects fair value.

***35** It is not self-evident that stockholder approval should have the same implications for an appraisal proceeding as an entire fairness case, given that the former is a statutory remedy that turns solely on inadequacy of price, while the latter is a liability proceeding in which the entire fairness test is used to determine whether fiduciaries have breached their duties.[37] The entire fairness test can apply to a wide range of transactions, only some of which require stockholder approval under the Delaware General Corporation Law. A complex body of law governs the extent to which stockholder approval lowers the standard of review from entire fairness to the business judgment rule, shifts who bears the burden of proving fairness, or operates as evidence of fairness under the unitary entire fairness test. *See, e.g.*, *ACP Master*, 2017 WL 3421142, at *16–19, *29. When an appraisal proceeding follows a long-form merger like the one in this case, stockholder approval is a statutory prerequisite. *See* 8 *Del. C.* § 251(c). The Merger would not have closed (and appraisal rights would not have been triggered) unless the stockholders approved the transaction. How different levels of stockholder approval should affect the valuation inquiry is something that our cases have yet to work out.

In this case, TransCanada argues that holders of approximately 95.3% of the shares that were present in person or by proxy at Columbia's meeting of stockholders favored the Merger. Under Delaware law, a merger requires the approval of holders of a majority of the outstanding shares, making that the appropriate denominator for consideration. *See* 8 *Del. C.*

§ 251(c). Under this voting standard, a non-vote counts the same as a "no" vote. In Columbia's case, holders of 73.9% of its shares voted in favor of the Merger, making the rate of approval perhaps not as high as it might appear. Neither side introduced expert testimony or other evidence that would enable the court to assess the degree to which this level of approval reflected an endorsement of the deal price, other than recognizing the obvious fact that a majority of the outstanding shares approved it.

The petitioners argue that the court should not give any weight to stockholder approval in this case because the proxy statement that Columbia distributed to its stockholders was materially misleading. *See* JX 1136 (the "Proxy"). The petitioners cite a list of issues, but three are most significant.

The first concerns an omission and a misleading partial disclosure about Columbia's NDAs. The Proxy disclosed that Columbia had entered into NDAs in November 2015 with Parties B, C, and D, but the Proxy did not disclose that the NDAs contained standstills, much less DADWs. The Proxy then disclosed misleadingly that "[u]nlike TransCanada, none of Party B, Party C or Party D sought to re-engage in discussions with [Columbia] after discussions were terminated in November 2015." *Id.* at 46. The Proxy failed to provide the additional disclosure that all four parties were subject to standstills with DADWs, that TransCanada breached its standstill, and that Columbia opted to ignore TransCanada's breach.

In an effort to blunt these issues, TransCanada points out that the Proxy disclosed that "none of Party A, Party B, Party C or Party D would be subject to standstill obligations that would prohibit them from making an unsolicited proposal to the Board following announcement of entry into the merger agreement with TransCanada." *Id.* at 60. TransCanada cites a secondary source indicating that some 80% of surveyed NDAs contained standstills and 64% contained DADWs, then argues that stockholders should have known that the NDAs contained these restrictions and that Columbia waived them. Stockholders should not have had to guess about whether the NDAs contained these powerful provisions, and while it was true that the restrictions did not apply post-signing, the Proxy created the misleading impression that Parties B, C, and D were not bound by standstills during the pre-signing period.

***36** These problems with the Proxy were material. A reasonable stockholder would have found it significant that TransCanada and Parties B, C, and D were bound by standstills in fall 2015 and that TransCanada was permitted to breach its standstill to pursue the Merger. A leading treatise on mergers and acquisitions identifies benefits to standstills, but also warns of potential dangers.

> [I]t may well be that the presence of [standstill] provisions will cause third parties to put their highest and best prices on the table in any pre-signing market check or auction since, for them, there will be no "tomorrow." However, such provisions, especially if coupled with either a provision that prohibits the target from waiving the prohibition or one which does not permit the third party from requesting [*sic*] a waiver undercuts the effectiveness of the post-signing market check.

Lou R. Kling & Eileen T. Nugent, *Negotiated Acquisitions of Companies, Subsidiaries and Divisions* § 4.04[6][b], at 4-92 (2019 ed.) (footnotes omitted). The limitations imposed by the standstills and DADWs made their presence material to Columbia's stockholders.

The petitioners next cite the Proxy's failure to disclose that Skaggs and Smith were planning to retire in 2016. TransCanada disputes the factual claim, arguing that Skaggs was open to continuing work and observing that the Board wanted Smith to stay on as CFO after the Merger. It was not inevitable that Skaggs or Smith would retire in 2016, but they wanted to and did. *See, e.g.*, JX 1034 (Smith asking advisor immediately after signing: "[D]o you think I can retire now?"). Although this decision has found that Skaggs and Smith's desire to retire did not undermine the sale process, a reasonable stockholder would have regarded their plans as material. *See, e.g.*, In re Lear Corp. S'holder Litig., 926 A.2d 94, 114 (Del. Ch. 2007) ("[A] reasonable stockholder would want to know an important economic motivation of the negotiator singularly employed by a board to obtain the best price for the stockholders, when that motivation could rationally lead that negotiator to favor a deal at a less than optimal price, because the procession of a deal was more important to him, given his overall economic interest, than only doing a deal at the right price.").

Finally, the petitioners cite the Proxy's partial disclosure regarding Smith's meeting with Poirier on January 7, 2016. *See* JX 1136 at 46. The Proxy failed to mention that Smith invited a bid and told Poirier that TransCanada did not face competition. TransCanada downplays the meeting as preliminary and immaterial given the generous deal price. Stockholders could decide how much weight to give the information, but the information itself was material.

The petitioners proved that the Proxy contained material misstatements and omissions. In light of the flawed Proxy, this decision does not give any weight to the stockholder vote for purposes of evaluating the reliability of the deal price.

g. The Deal Protections

The petitioners contend that the deal protection measures in the Merger Agreement undermined the effectiveness of the sale process. Under the Delaware Supreme Court's precedents, the deal protections did not have that effect.

The Merger Agreement contained a no-shop clause with a fiduciary out. As is customary, the Merger Agreement provided broadly that Columbia could not solicit, provide information to, or engage in discussions with any party other than TransCanada, then created an exception identifying circumstances under which Columbia could respond to an interested party. The first half of Section 4.02(a) of the Merger Agreement established the broad prohibition, stating:

> ***37** The Company agrees that, except as permitted by this Section 4.02, neither it nor any of its Subsidiaries nor any of the officers and directors of it or its Subsidiaries shall, and it shall instruct and use its reasonable best efforts to cause its and its Subsidiaries' employees, investment bankers, attorneys, accountants and other advisors or representatives (such officers, directors, employees, investment bankers, attorneys, accountants and other advisors or representatives, collectively, "Representatives") not to, directly or indirectly:
>
> (i) initiate, solicit or encourage any, or the making of any, inquiry, indication of interest, proposal or offer that constitutes, or could reasonably be expected to lead to, any Acquisition Proposal;
>
> (ii) engage in, continue or otherwise participate in any discussions or negotiations regarding, or provide any information or data to any Person relating to, any inquiry, indication of interest, proposal or offer that constitutes, or could reasonably be expected to lead to, an Acquisition Proposal; or
>
> (iii) otherwise knowingly facilitate any effort or attempt to make any inquiry, indication of interest, proposal or offer that constitutes, or could reasonably be expected to lead to, an Acquisition Proposal.

JX 1025 § 4.02(a) (the "No-Shop Clause") (formatting altered).

The second half of Section 4.02(a) of the Merger Agreement carved out the exception to the general prohibition. It stated:

> Notwithstanding anything in the foregoing to the contrary, prior to the time the Company Requisite Vote is obtained, the Company may, subject to the Company providing prior notice to Parent,
>
> (A) provide information in response to a request therefor by a Person who has made a bona fide written Acquisition Proposal that did not result from a breach of this Section 4.02 if the Company receives from the Person requesting such information an executed confidentiality agreement on terms not less restrictive to the other party than those contained in the Confidentiality Agreement (it being understood that such confidentiality agreement need not prohibit the making, or amendment, of an Acquisition Proposal but which shall not prohibit the Company from fulfilling its obligations under this Section 4.02); provided, however, that the Company shall promptly after the execution thereof provide a true and complete copy to Parent of any such confidentiality agreement and any such information to the extent not previously provided to Parent, in each case, redacted, if necessary, to remove the identity of the Person making the proposal or offer; or
>
> (B) engage or participate in any discussions or negotiations with any Person who has made such an unsolicited bona fide written Acquisition Proposal, if and only to the extent that,
>
>> (x) prior to taking any action described in clause (A) or (B) above, the board of directors of the Company determines in good faith (after consultation with its outside legal counsel) that the failure to take such action would reasonably be expected to result in a breach of the directors' fiduciary duties under applicable Law and

> (y) in each such case referred to in clause (A) or (B) above, the board of directors of the Company has determined in good faith based on the information then available and after consultation with its outside legal counsel and its financial advisor that such Acquisition Proposal either constitutes a Superior Proposal or could reasonably be expected to result in a Superior Proposal....

Id. § 4.02(a) (the "Superior-Proposal Out") (formatting altered).

***38** Importantly for present purposes, the Superior-Proposal Out permitted Columbia to provide due diligence information in response to "a request therefor by a Person who has made a bona fide written Acquisition Proposal," subject only to the bidder entering into an NDA "on terms not less restrictive to the other party than those contained in" the NDA with TransCanada. It also provided that the NDA did not have to contain a standstill, thereby eschewing the deal lawyer's trick of turning the requirement that the bidder sign an equivalent confidentiality agreement into a powerful backdoor defensive measure. The provision also authorized Columbia to redact the name of the person making written Acquisition Proposal. This aspect of the provision did not require a superior-proposal determination before furnishing due diligence, nor did it impose any delay before Columbia could comply. *Cf.* *In re Compellent Techs., Inc. S'holder Litig.*, 2011 WL 6382523, at *6–8 (Del. Ch. Dec. 9, 2011) (discussing a radically buyer-friendly version of superior-proposal out and possible alternative formulations). The definition of Acquisition Proposal made this aspect of the provision easy to satisfy by defining that term as

> any proposal or offer ... relating to any transaction or series of transactions involving
>
> (A) any direct or indirect sale, lease, transfer, exchange, acquisition or purchase of any assets or one or more businesses that constitute more than fifteen percent (15%) of the net revenues, net income, or assets of the Company and its Subsidiaries, taken as a whole, or more than fifteen percent (15%) of the total voting power of any class of equity securities of the Company,
>
> (B) any direct or indirect sale, exchange, transfer or other disposition, tender offer or exchange offer or similar transaction that, if consummated, would result in any Person or "group" ... acquiring beneficial or record ownership of more than fifteen percent (15%) of the total voting power of any class of securities of the Company, or
>
> (C) any merger, reorganization, consolidation, share exchange, business combination, recapitalization, liquidation, joint venture, partnership, dissolution or similar transaction involving the Company (or any Subsidiary or Subsidiaries ... whose business constitutes more than fifteen percent (15%) of the net revenues, net income or consolidated assets of the Company and its Subsidiaries, taken as a whole).

JX 1025 § 4.02(b)(i) (formatting altered).

The Superior-Proposal Out required that before engaging or participating in any discussions or negotiations, Columbia had to made additional determinations. First, the Board had to determine "in good faith (after consultation with its outside legal counsel) that the failure to take such action would reasonably be expected to result in a breach of the directors' fiduciary duties under applicable Law." Second, the Board had to determine that the Acquisition Proposal "either constitutes a Superior Proposal or could reasonably be expected to result in a Superior Proposal," with that term defined as

> a bona fide written Acquisition Proposal that did not result from a breach of this Section 4.02 relating to any acquisition or purchase by a Person or group of Persons of
>
> (A) assets that generate more than fifty percent (50%) of the consolidated total revenues of the Company and its Subsidiaries, taken as a whole, (B) assets that constitute more than fifty percent (50%) of the consolidated total assets of the Company and its Subsidiaries, taken as a whole, or (C) more than fifty percent (50%) of the total voting power of the equity securities of the Company,
>
> in each case, that the board of directors of the Company determines in good faith (after consultation with its financial advisor and outside legal counsel)
>
> [1] is reasonably likely to be consummated in accordance with its terms, taking into account
>
> > (x) the timing and likelihood of consummation of the proposal (including whether such Acquisition Proposal is contingent on receipt of third party financing or is terminable by the acquiring Person or group upon payment of a termination fee),

> ***39** (y) all legal, financial and regulatory aspects of the Acquisition Proposal and
>
> (z) the Person or group making the Acquisition Proposal (including in respect of the potential effects of any actions that might be required by any Government Antitrust Entity in connection with the consummation of such transaction), and
>
> [2] if consummated, would result in a transaction more favorable to the Company's stockholders from a financial point of view than the Merger.

Id. § 4.02(b)(ii) (formatting altered; Arabic numerals added). This dimension of the Superior-Proposal Out contained relatively middle-of-the-road standards for its exercise. *Cf.* Compellent, 2011 WL 6382523, at *6–8.

The Merger Agreement also contained a no-change-of-recommendation provision with its own fiduciary out. As with the structure of the No-Shop Clause and Superior-Proposal Out, the provision first broadly prohibited the Board from taking any action or agreeing to take any action to (i) change its recommendation in favor of the Merger, (ii) recommend any Acquisition Proposal, (iii) cause or permit Columbia to enter into any letter of intent, agreement in principle, acquisition agreement, or merger agreement regarding any Acquisition Proposal, other than a confidentiality agreement as contemplated by the Superior-Proposal Out, or (iv) take any action to exempt an Acquisition Proposal from any takeover statute. JX 1025 § 4.02(c). The Merger Agreement then provided that if Columbia received a Superior Proposal *and* the Board determined that its fiduciary duties required it, then the Board could change its recommendation or, if it wished, terminate the Merger Agreement for purposes of entering into an agreement with respect to Superior Proposal. Before taking either step, Columbia had to give TransCanada notice that the Board intended to take that action, and TransCanada then would have four business days to match the Superior Proposal. The matching right was unlimited, and any new or revised Superior Proposal triggered an additional matching period of four business days. The pertinent provisions stated:

> Notwithstanding anything to the contrary set forth in [the no-change-of-recommendation provision], prior to the time [that stockholder approval of the Merger] is obtained and so long as the Company is in compliance with [No-Shop Clause]:
>
> (i) the board of directors of the Company may
>
> (A) effect a Change of Recommendation in response to a Superior Proposal that is not otherwise withdrawn at the time of the Change of Recommendation or
>
> (B) cause the Company to terminate this Agreement for the purpose of entering into a definitive agreement with respect to a Superior Proposal that is not otherwise withdrawn at the time of such termination (provided that the Company shall have paid the Termination Payment prior to or concurrently with such termination), which definitive agreement the Company shall enter into concurrently with or immediately following such termination,
>
> in either case, if and only if the board of directors of the Company determines in good faith (after consultation with its financial advisor and outside legal counsel) that the failure to take any such action would be inconsistent with the directors' fiduciary duties under applicable Law; provided, however, that the board of directors of the Company may not take any such action unless
>
> ***40** (1) the Company first provides written notice to Parent (a "Superior Proposal Notice") advising Parent that the board of directors of the Company intends to either effect a Change of Recommendation or terminate this Agreement pursuant to Section 7.01(c)(i), which notice shall specify the reasons therefor and include the material terms and conditions of the applicable Superior Proposal and attach a copy of the most current draft of any written agreement relating thereto,
>
> (2) during the four (4) Business Day period following receipt by Parent of the Superior Proposal Notice (the "Superior Proposal Negotiation Period") (it being understood that the first Business Day following the day on which a Superior Proposal Notice is received shall be the first day of the Superior Proposal Negotiation Period), the Company negotiates in good faith with Parent and its Representatives, to the extent requested by Parent, with respect to any revisions to the terms of the transactions contemplated by this Agreement proposed by Parent; provided, however, that if during any Superior Proposal Negotiation Period there shall occur any subsequent amendment to any material term of the applicable Superior Proposal, the Company shall provide a new Superior Proposal

> Notice and a new Superior Proposal Negotiation Period shall commence (provided that, with respect to any Superior Proposal, each new Superior Proposal Negotiation Period that commences shall be for a period of four (4) days, except that in no event shall any new Superior Proposal Negotiation Period shorten the four (4) Business Day duration of the first Superior Proposal Negotiation Period) and
>
> (3) at or after 5:00 p.m., New York City time, on the last day of the Superior Proposal Negotiation Period, the board of directors of the Company (after consultation with its financial advisor and outside legal counsel) determines that the Superior Proposal would continue to be a Superior Proposal, taking into account any changes to the terms of this Agreement theretofore agreed to by Parent in writing ....

Id. § 4.02(d)(i) (formatting altered). A separate fiduciary out permitted the Board to change its recommendation in response to an "Intervening Event," defined as "an event, fact, occurrence, development or circumstance that was not known to" the Board "as of the date of this Agreement (or if known, the consequences of which were not known to the board of directors of the Company as of the date of this Agreement) ...." *Id.* § 4.02(d)(ii). Unlike with a Superior Proposal, the Board could not terminate the Merger Agreement in response to an Intervening Event.

If the Board terminated the Merger Agreement in response to a Superior Proposal or if Columbia's stockholders failed to approve the Merger, then Columbia was required to (i) pay TransCanada a $309 million termination fee and (ii) reimburse TransCanada for "authorization, preparation, negotiation, execution and performance" expenses not to exceed $40 million. *Id.* § 7.02(c). Those amounts represented 3.42% of the total equity value of the Merger, which was $10.2 billion. TransCanada believed that a Superior Proposal would "effectively require total consideration greater than $26.27 per share" because the termination fee was equivalent to 77 cents per share, or roughly 3% of $25.50. JX 1093 at 6. The $40 million expense reimbursement would increase the per-share figure by another 10 cents.

Although these provisions created obstacles for competing bidders, they did not undermine the sale process for appraisal purposes. Commentators have perceived that under the Delaware Supreme Court's recent appraisal decisions, a sale process will function as a reliable indicator of fair value if it would pass muster if reviewed under enhanced scrutiny in a breach of fiduciary duty case.[38] The combination of deal protection measures would not have supported a claim for breach of fiduciary duty.[39]

***41** The facts of *Aruba* involved a similar suite of deal protections. The merger agreement in that case "prohibited Aruba from soliciting competing offers and required the Aruba Board to continue to support the merger, subject to a fiduciary out and an out for an unsolicited superior proposal" and included a termination fee equal to 3% of the merger's equity value. *Aruba Trial*, 2018 WL 922139, at *21, *38. The matching rights were similar too: HP had "an unlimited match right, with five days to match the first superior proposal and two days to match any subsequent increase, and during the match period Aruba had to negotiate exclusively and in good faith with HP." *Id.* at *38 (footnote omitted). Viewing the deal protections holistically, the Delaware Supreme Court found that potential buyers had an open chance to bid, which supported the high court's use of a deal-price-less-synergies metric to establish fair value. *See* Aruba, 210 A.3d at 136.

The outcome in *Aruba* comports with guidance from a frequently cited treatise, which identifies "critical aspects" of a merger agreement that does not "preclude or impermissibly impede a post-signing market check." Kling & Nugent, *supra*, § 4.04[6][b], at 4-89 to -90.

> First, the economics of the executed agreement must be such that it does not *unduly* impede the ability of third parties to make competing bids. Types of arrangements that might raise questions in this regard include asset lock-ups, stock lock-ups, no-shops, force-the-vote provisions, and termination fees. The operative word is "unduly;" the impact will vary depending upon the actual type of device involved and its specific terms.
>
> * * *
>
> Second, the target should be permitted to disclose confidential information to any third party who has on its own (i.e., not been solicited) "shown up" in the sense that it has submitted a proposal or, at a minimum, an indication of interest which is, or which the target believes is, reasonably likely to lead to (and who is capable of consummating) a higher competing bid. In this regard, the target should also be able to negotiate with such third parties. This removes any informational advantage that the initial (anointed) purchaser may have.
>
> * * *

> Finally, the target board of directors should have the contractual right, without violating the acquisition agreement, to withdraw or modify its recommendation to shareholders with respect to the transaction provided for in the executed acquisition agreement.

Id. at 4-90 to -94.1 (footnotes omitted). Using this framework, the deal protections did not preclude or impermissibly impede a post-signing market check. Columbia waived the standstills with Dominion, NextEra, and Berkshire before signing the Merger Agreement, so those provisions did not operate as a constraint during the post-signing period. Any party could obtain due diligence simply by submitting a bona fide written Acquisition Proposal and entering into the required confidentiality agreement; the initial Acquisition Proposal did not itself have to be a Superior Proposal. If the competing bidder then made an Acquisition Proposal that either constituted or could reasonably be expected to result in a Superior Proposal, and if the Board determined that its fiduciary duties required it, then the Board could negotiate with the competing bidder. And if the competing bidder made a Superior Proposal that TransCanada was unable or unwilling to match, then the Board could withdraw or modify its recommendation in support of the Merger Agreement. Going beyond what the treatise describes, Columbia could take the additional step of terminating the Merger Agreement and entering into an agreement regarding the Superior Proposal, subject only to paying a termination fee and expense reimbursement equal to 3.42% of the Merger's equity value.

The petitioners try to bolster their argument about the deal protections by contending that the Proxy distorted the informational content of the post-signing phase by creating the false impression that Parties B, C, and D were never subject to standstills, which they say a competing bidder would take into account when deciding whether to intervene. Under this view, if those parties and TransCanada had been conducting due diligence in November 2015, and if only TransCanada renewed its interest later on, then a party considering a competing bid might reasonably believe that TransCanada was paying top dollar because only TransCanada had decided to proceed. Under those circumstances, a potential competing bidder might view Columbia as fully vetted and decline to bid because of the winner's curse.[40] But a potential topping bidder might be more likely to take the risk of competing with TransCanada if it perceived that TransCanada had been able to move forward while standstills blocked its competitors. In that case, the competing bidder might think there was value that had not yet been priced.

***42** This argument presents a variation of the winner's-curse theory that the Delaware Supreme Court rejected in *Dell*. There, the trial court found that Mr. Dell's participation gave the buyout group advantages that competing bidders would struggle to overcome and which therefore would deter bidding. *See* *Dell Trial*, 2016 WL 3186538, at *36, *42–44. The Delaware Supreme Court explained that "the likelihood of a winner's curse can be mitigated through a due diligence process where buyers have access to all necessary information." *Dell*, 177 A.3d at 32. The high court also cited the trial court's observation that strategic buyers "are less subject to the winner's curse because they typically possess industry-specific expertise and have asset-specific valuations that incorporate synergies." *Id.* (internal quotation marks omitted). Finally, the Delaware Supreme Court emphasized the absence of evidence that another party was interested, explaining that "[f]air value entails at minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay." *Id.* at 29.

Similarly in this case, any competing bidder could gain access to due diligence by submitting a bona fide written Acquisition Proposal and entering into a confidential agreement. Moreover, all of the likely bidders were strategic buyers. Most importantly, the petitioners have not shown that anyone would have made a topping bid. Columbia's sale process involved most of the parties that its bankers thought would be interested, including Berkshire, Dominion, and NextEra. *See* JX 499. Each knew that it was subject to a standstill, and each would have believed that others were similarly bound. None wanted to buy Columbia at anything near TransCanada's price. Spectra was never bound by a standstill, yet did not bid. There is no persuasive evidence that any other party wanted to bid. The evidence instead shows that no one wanted to bid. As in *Dell*, the most plausible explanation is that "a topping bid involved a serious risk of overpayment." *Dell*, 177 A.3d at 33. That in turn suggests that the deal price was "already at a level that is fair." *Id.*

The petitioners failed to show that the Proxy distorted bidder behavior during the post-signing phase. More broadly, the petitioners failed to prove that the deal protection measures undermined the validity of the deal price. The better view of the evidence is that if a bidder had been serious, then it would have come forward.

h. The Sale Process Was Reliable.

TransCanada proved by a preponderance of the evidence that the sale process made the deal price a persuasive indicator of fair value. The sale process was not perfect, and the petitioners highlighted its flaws, but the facts of this case, when viewed as a whole, compare favorably or are on par with the facts in *DFC*, *Dell*, and *Aruba*.

In reaching this conclusion, I recognize the existence of other decisions that have sought to apply the teachings of *DFC* and *Dell*, and which have declined to rely on the deal price as an indicator of fair value.[41] The petitioners have cited similarities between aspects of the sale processes in those cases and aspects of the sale process in this case, arguing that the deal price here was unreliable.

In this decision, I have attempted to adhere to the principles expressed in *DFC*, *Dell*, and *Aruba* and to take into account how those decisions applied those principles to the facts. Those factual applications have important implications for the outcome here.

I also continue to regard it as important that the Delaware Supreme Court's decisions in *Dell* and *DFC* reversed trial court decisions for failing to give adequate weight to the deal price. In each case, the Delaware Supreme Court regarded the sale process as sufficiently good that the deal price deserved "heavy, if not dispositive, weight." *Dell*, 177 A.3d at 23; *see* *DFC*, 172 A.3d at 349, 351. The decisions did not address when a sale process would be sufficiently bad that a trial court could give the deal price no weight. The decisions also did not address when a sale process that was not as good would still be good enough for a trial court to give the deal price weight. Technically, the holdings did not delineate when a sale process was sufficiently good that the trial court should give it heavy if not dispositive weight. The Delaware Supreme Court could have believed the sale processes in *DFC* and *Dell* warranted that level of consideration without excluding the possibility that a not-as-good sale process could deserve the same treatment. I thus do not believe that the Delaware Supreme Court's favorable comments regarding the sale processes in *Dell* and *DFC* establish minimum requirements for other sale processes to meet before the deal price can be considered as a persuasive indicator of fair value.

***43** The *Aruba* decision points in the same direction. There, the trial court found the sale process to be sufficiently reliable to use the deal price as a valuation indicator, but declined to give it weight. The Delaware Supreme Court accepted that the sale process was sufficiently reliable and used the deal price as the exclusive basis for its own fair value determination. As with *Dell* and *DFC*, the *Aruba* decision did not have to address when a sale process was sufficiently bad that a trial court could decline to rely on the deal price.

The sale process in this case had aspects that compare favorably with the processes in *DFC*, *Dell*, and *Aruba*. It also had aspects that differed from the processes in those cases. On balance, TransCanada proved that the deal price is a reliable indicator of fair value.

3. The Synergies Deduction

"[I]t is widely assumed that the sale price in many M&A deals includes a portion of the buyer's expected synergy gains, which is part of the premium the winning buyer must pay to prevail and obtain control." *DFC*, 172 A.3d at 371. "In an arm's-length, synergistic transaction, the deal price generally will exceed fair value because target fiduciaries bargain for a premium that includes ... a share of the anticipated synergies ...." *Olson v. ev3, Inc.*, 2011 WL 704409, at *10 (Del. Ch. Feb. 21, 2011). "[S]ection 262(h) requires that the Court of Chancery discern the going concern value of the company irrespective of the synergies involved in a merger." *M.P.M. Enters.*, 731 A.2d at 797. To derive an estimate of fair value, the court must exclude "any synergies or other value expected from the merger giving rise to the appraisal proceeding itself ...." *Golden Telecom Trial*, 993 A.2d at 507. "Of course, estimating synergies and allocating a reasonable portion to the seller certainly involves imprecision, but no more than other valuation methods, like a DCF analysis ...." *Aruba*, 210 A.3d at 141.

TransCanada announced a total of $250 million in target annual synergies, with $150 million attributable to cost and revenue synergies and $100 attributable to financing synergies. PTO ¶¶ 555, 632, 642; *see* Marchand Tr. 489–490. The financing synergies resulted predominantly from TransCanada generating funds at its lower cost of capital, then channeling them through offshore financing structures to generate tax advantages. Marchand Tr. 490.

The petitioners have questioned the financing synergies because they were not labeled "synergies." In a board presentation, TransCanada labeled the cost and revenue saving as "synergies" and the financing benefits as "offshore."[42] The label is not dispositive. *See* Marchand Tr. 518. The Merger created value if it enabled TransCanada to finance Columbia's business plan using its lower cost of capital. To the extent that value is included in the transaction price, it is value arising from the accomplishment or expectation of the Merger that must be deducted under Section 262(h).

TransCanada asked its valuation expert, Mark Zmijewski, to value the synergies. Using a standard DCF methodology, Zmijewski calculated the net present value of the synergies at $4.64 per share. JX 1351 Ex. VI-3. Zmijewski did not use a DCF analysis to value Columbia, and he disagreed with many aspects of the DCF analysis prepared by the petitioners' expert, so there is some irony in Zmijewski using it here. In *Highfields*, this court declined to use a synergies estimate that the respondent's expert prepared using a DCF analysis, in part because the respondent's expert had not used a DCF methodology when rendering his other valuation opinions. *See Highfields Capital, Ltd. v. AXA Fin., Inc.*, 939 A.2d 34, 60–61 (Del. Ch. 2007).

***44** The real question is the extent to which the deal price included synergies. TransCanada's CFO testified that the deal price included 100% of the estimated synergies. *See* Marchand Tr. 490–91. Zmijewski tried to support this testimony by analyzing the reaction of TransCanada's stock to the announcement of the Merger. He found that TransCanada's share price dropped, which was consistent with the view that the Merger was a "bad deal for ... TransCanada" and a "good deal for Columbia." Zmijewski Tr. 1447–48. Zmijewski's analysis operated at the level of the overall deal price; it did not address the more detailed level of the synergy deduction. *See* JX 1350 ¶¶ 63–65.

The contemporaneous evidence does not indicate that TransCanada allocated synergies to Columbia, much less all of the synergies. TransCanada relies on a presentation to its board that references the full value of both the cost and financing synergies and claims it shows that the synergies were fully allocated to Columbia. *See* JX 935 at 12. The page where these figures appear calculates transaction multiples by taking enterprise values for Columbia that were implied by various prices per share, then dividing those multiples by EBITDA metrics, some of which add synergy figures. *See id.* This table does not indicate that the synergies were allocated to Columbia, and the "football field" page in the presentation places the deal price comfortably within TransCanada's DCF valuation of Columbia without synergies. *See id.* at 6. TransCanada also observes that after Columbia rejected its offer of $25.25 per share, Poirier suggested attempting to identify additional synergies that could justify increasing the offer. *See* JX 911 at 1, 4. TransCanada says that if it had not already priced the synergies into its offer, then there would have been no need to search for additional synergies. But the email exchange shows a range of views among TransCanada executives about the amount that TransCanada should be willing to pay. The email does not suggest that TransCanada had topped out its bid with all of the synergies going to Columbia.

Other internal TransCanada documents focus only on cost synergy estimates of $150 million per year. *See* JX 878 at 48; JX 886 at 28. One informative package of materials for the TransCanada board of directors values Columbia at $26.51 per share using a DCF methodology, then values the cost synergies at $1.93 per Columbia share, with a sensitivity range of $1.89 to $2.61 per share. *See* JX 1008 at 54; *accord* JX 1018 at 1, 24, 26. The deal price of $25.50 per share falls comfortably within TransCanada's valuation ranges without any allocation of synergies. *See* JX 1008 at 50; JX 1018 at 22; JX 1365 ¶¶ 91–92. It also appears, as TransCanada argues, that there were many sources for merger-related value creation that justified paying a premium over Columbia's trading price, and the cost, revenue, and financing synergies were simply the easiest to quantify. *See*, *e.g.*, JX 1027 (synergy overview). But the fact that TransCanada perceived synergies does not mean that the deal price included them.[43]

***45** Given this evidence, I am not able to credit TransCanada's position that Columbia received 100% of synergies worth $4.64 per share. TransCanada bore the burden of proving a downward adjustment for synergies. TransCanada did not meet its burden of proof. TransCanada likely could have justified a smaller synergy deduction, but it claimed a larger and unpersuasive one. This decision therefore declines to make any downward adjustment to the deal price.

4. Change In Value Between Signing And Closing

Because the valuation date in an appraisal is the date on which the merger closes, fair value must be determined based on the "operative reality" at the effective time. *See Technicolor IV*, 684 A.2d at 298. The deal price provides an indication of the value of the company on the date of signing. It does not necessarily provide an indication of the value of the company on the date of closing. In this case, over three months passed between the signing of the Merger Agreement on March 17, 2016, and the closing of the Merger on July 1, 2016. The petitioners contend that Columbia's value increased during this period. As the party arguing for an upward adjustment to the deal price, the petitioners bore the burden of proof on this issue.

By treating the petitioners as having argued that Columbia's value increased between signing and closing, this decision is giving the petitioners the benefit of the doubt on an argument they did not explicitly make. The petitioners argued that if the court adopted Columbia's unaffected trading price as an indicator of fair value, then it should make an upwards adjustment because Columbia's value would have increased by the time of closing. The petitioners did not make the same argument about the deal price, but the same logic applies. Using either the unaffected trading price or the deal price results in a temporal gap between the valuation indicator and the closing date. In this case, the date for the unaffected trading price was March 9, 2016. The parties signed the Merger Agreement on March 17. The deal closed on July 1. The length of the intervening periods differs by only eight days.

The problem with giving the petitioners the benefit of the doubt on this argument is that they did not suggest a means of adjusting the deal price to reflect the increases in value that resulted from the factors they cite. Perhaps an expert could have constructed a metric, but the petitioners in this case did not provide one. For purposes of adjusting the deal price, the petitioners failed to satisfy their burden of proof.

The petitioners' arguments for an upward adjustment are also unpersuasive in their own right. They contend that Columbia's value increased because the market for CPPL's equity recovered and because commodity prices improved. The petitioners did not provide persuasive evidence on either point.

a. An Improved Market For CPPL Equity

In their first argument for an upward adjustment, the petitioners contend that Columbia's value increased between signing and closing because the market for CPPL's peers recovered. They proposed using changes in indices of peer companies to translate those developments into an increased trading price for CPPL. They also cite circumstantial evidence that CPPL's trading price was rising in late February and early March 2016, possibly suggesting an upward trend that would have continued if Columbia had not announced the Merger. *See* Dkt. 390 Ex. D.

The petitioners' theory builds on the fact that after the spinoff, CPPL's trading price declined as part of broader investor dissatisfaction with MLPs. Columbia recognized that it could not use CPPL to raise the growth capital needed for its business plan, so it explored less attractive alternatives like a parent-level equity raise. The petitioners argue that if CPPL's trading price had recovered, then Columbia could have used CPPL to fund its business plan.

***46** As their primary evidence of a price change, the petitioners cite the Alerian MLP Index and the Alerian Natural Gas MLP Index (the “Gas Index”), both of which improved by approximately 17% between signing and closing.[44] CPPL's price did not improve during the same period; it fell. The petitioners address this difficulty by pointing to two analyst reports and to internal emails from a petitioner fund, which suggest that CPPL's trading price dropped after the announcement of the Merger because market participants feared that TransCanada would not transfer assets to CPPL to the same degree as Columbia would have on a standalone basis. *See* JX 1069 at 8; JX 1056; JX 1061.

There are several problems with the petitioners' reliance on the indices. The broader Alerian MLP Index is a poor proxy for CPPL. It consists of firms that transport or store energy commodities generally, and it tends to tracks the price of crude oil. *See* Jeffers Tr. 743–44; Jeffers Dep. 75; *see also* JX 740 at 9–10. The Gas Index provides a better proxy, but the petitioners' industry expert testified that the higher prices and lower yields associated with that index resulted from the announcement of the Merger, which restored the market's faith in natural gas MLPs. *See* Goodof Tr. 151. To the extent his testimony accurately captured the reasons for the change, then any increase in value implied by the Gas Index would have resulted from the accomplishment or expectation of the Merger and would need to be excluded under Section 262(h). In actuality, TransCanada demonstrated that the lower yields resulted from changes in the composition of the Gas Index. *See* JX 1470; Goodof Tr. 152–54. TransCanada also demonstrated that the lower yields did not reach the level that Columbia needed to use CPPL to fund its business plan. *See* Adamson Tr. 1338–39. The change in the Gas Index does not persuasively support an increase in Columbia's value.

More broadly, Columbia's inability to raise growth capital through CPPL reflected investors' wider concerns about MLPs. Because of developments in the broader MLP industry, this model of raising capital was fundamentally broken. *See* JX 547; JX 1345 at 72–76. It was particularly broken at Columbia, which faced additional difficulties in raising capital because of its high debt load. *See* Adamson Tr. 1332–37. A three-month uptick in the two Alerian indices does not prove that Columbia fixed its model and does not support an increase in Columbia's value.

b. An Improved Market For Commodities

In their second argument, the petitioners cite changes in commodity prices. They point out that after the spinoff, Columbia's trading price dropped as energy stocks fell out of favor because of a decline in commodity prices. They argue that as commodity prices recovered, energy stocks recovered. They point out that between signing and closing, the prices of natural gas and natural gas futures increased by 58.79% and 55.15%, respectively. *See* PTO ¶¶ 685, 690.

One difficulty with this argument is that Columbia's stock price did not recover with commodity prices. It remained stagnant until the Merger leaked on March 9, 2016. *See* Dkt. 390 Ex. A. The bigger difficulty with this argument is something everyone agrees on: Columbia's value does not depend on commodity prices, except at the extremes when ultra-low commodity prices could affect the creditworthiness of Columbia's counterparties. *See* PTO ¶¶ 293–94. The petitioners correctly point out that the declining stock market hurt Columbia in fall 2015, and they say that the mirror-image trend should benefit Columbia on the upside. But in fall 2015, the declining market hurt Columbia because it could not use CPPL to raise equity capital. Columbia then faced the prospect of raising equity capital by issuing its own shares in a declining market, which would dilute Columbia's value and threaten a downward spiral. The problems that Columbia faced from a declining market did not reflect operational problems. They reflected constrained financing alternatives. The commodity-price story does not support an increase in Columbia's value.

5. The Conclusion Regarding The Deal Price

***47** TransCanada proved that the deal price is a reliable indicator of fair value. TransCanada failed to prove that the consideration provided in the Merger included synergies of $4.64 per share. The petitioners failed to prove that Columbia's value increased between signing and closing, and they failed to prove how any change in value could be translated into an adjustment to the deal price. The market-tested indicator for the fair value of Columbia is therefore $25.50 per share.

B. The Unaffected Trading Price

TransCanada contends that the unaffected trading price of Columbia's stock is a strong indicator of Columbia's fair value. The petitioners contend that the court should not give any weight to Columbia's trading price. As the proponent of this valuation metric, TransCanada bore the burden of demonstrating its reliability.

Both sides retained experts who rendered opinions on the persuasiveness of the unaffected trading price as an indicator of fair value. TransCanada relied on Zmijewski, who is an emeritus professor of finance at the University of Chicago and a consultant at Charles River Associates. The petitioners relied on Eric Talley, a professor of law at Columbia University and co-director of the Millstein Center for Global Markets and Corporate Ownership.

The parties debated many issues relating to the unaffected trading price, including (i) whether the trading price could provide insight into fundamental value, (ii) whether the trading price contained an implicit minority discount, (iii) whether investors lacked access to or the trading price otherwise failed to incorporate material information about Columbia's value, and (iv) whether investor sentiment about broader trends in the energy markets artificially depressed Columbia's trading price. This decision could devote many pages to parsing through the competing expert testimony, the parties' evidentiary showings, and their legal arguments.

Ultimately, however, Delaware precedent demonstrates that a reliable trading price is not a prerequisite to a reliable determination of fair value based on a deal-price-less-synergies metric. Consequently, assuming TransCanada failed to prove that the trading price was a reliable indicator of fair value, that ruling would not undermine this court's ability to rely on the deal price. Indeed, even if the petitioners proved affirmatively that the trading price was an *unreliable* indicator of fair value, that finding would not undermine this court's ability to rely on the deal price. On the facts of this case, the deal-price-less-synergies metric is the most reliable approach, making the analysis of the trading price comparatively unimportant.

The Delaware cases that have developed the deal-price-less-synergies metric demonstrate that a reliable trading price is not a prerequisite to a reliable deal-price-based determination of fair value. The *Union Illinois* decision was the first time a Delaware court deployed the deal-price-less-synergies metric,[45] and that decision used it as the exclusive basis for valuing a privately held company. *See* Union Illinois, 847 A.2d at 343 ("UFG was not a public company and therefore its shares were not listed for trading on a stock exchange."). The foundational decision for the deal-price-less-synergies metric thus deployed it in the absence of any trading price, much less a reliable trading price. *See* *id.* at 357, 364 (awarding "the value of the Merger Price net of synergies" after finding that the deal price was "the most reliable evidence of fair value" and "giving 100% weight to that factor").

***48** Three years after *Union Illinois*, the *Highfields* decision was next to deploy the deal-price-less-synergies metric, and the first to use it for a widely held, publicly traded firm. *See* *Highfields*, 939 A.2d at 61 (giving 75% weight to deal-price-less-synergies metric). The court regarded the trading price as an *unreliable* indicator of fair value, because the "stock price included an element of value reflecting merger speculation leading up to [the merger's] announcement." *Id.* at 58. Even so, the court had no difficulty finding that after deducting synergies, the deal price was a reliable indicator where it "resulted from an arm's-length bargaining process where no structural impediments existed that might prevent a topping bid." *Id.* at 59. The *Highfields* decision shows that the deal-price-less-synergies metric does not require a *reliable* trading price.

After *Highfields*, the deal-price metric lay dormant for six years before returning to prominence in a string of five decisions issued between 2013 and 2015.[46] Each of those decisions determined fair value based solely on the deal price, and in finding that the deal price was reliable, each decision focused predominantly on whether the merger resulted from a "proper transactional process."[47] The decisions did not view the reliability of the deal price as turning on the reliability of the trading price. Only one of the decisions considered the reliability of the trading price. In *AutoInfo*, the petitioners argued that the company "was thinly traded and lacked financial analyst coverage[,]" which led to "the market underpric[ing] the company because it was ignorant of its potential." *AutoInfo*, 2015 WL 2069417, at *12. The court rejected this argument as a basis for undermining the deal price as an indicator of fair value, explaining that "the Merger price does not reflect the value that a potentially uniformed market attributed to AutoInfo." *Id.* The court noted that the deal price generated a premium of 22% over the unaffected trading price and concluded that "[w]hile the market may have been uninformed about AutoInfo before the sale process, it subsequently gained ample information" by virtue of the sale process. *Id.* The reliability of the sale process rendered irrelevant the potential unreliability of the trading price.

The decisions that followed *Highfields* and preceded the Delaware Supreme Court's decision in *DFC* thus illustrate a general rule that trading-price reliability is not a prerequisite for deal-price reliability. *DFC* does not suggest a contrary rule. The *DFC* decision cited with approval both *Union Illinois*, where the trial court used the deal price for a privately held company, and multiple post-*Highfields* rulings that had relied on the deal price without regard to the trading price or despite evidence that it was unreliable. *See* *DFC*, 172 A.3d at 363 n.84.

***49** *Dell* also does not suggest a contrary rule. The Delaware Supreme Court found that both the trading price and the deal price were reliable indicators of value. *See* *Dell*, 177 A.3d at 5-7, 24-27, 35. The high court did not hold that its finding as to the latter depended on the former. Instead, the *Dell* decision regarded the trial court's treatment of the trading price and the deal price as independent sources of error.

The Delaware Supreme Court's most recent appraisal decision cuts the same way. In *Aruba*, the Delaware Supreme Court held that the trial court erred by relying on the unaffected trading price. The high court indicated that the trading price was unreliable partly because the market had not received information about Aruba's strong earnings. *See* *Aruba*, 210 A.3d at 138–39. At the same time, the decision accepted the trial court's finding that the deal price was a reliable valuation indicator. *See* *id.* at 141–42. The Delaware Supreme Court pointed to HP's "access to nonpublic information to supplement its consideration of the public information available to stock market buyers," including that it "knew about Aruba's strong quarterly earnings before the market did, and likely took that information into account when pricing the deal." *Id.* at 139. The reliability of the deal price thus operated independently of the trading price. Like *DFC*, the *Aruba* decision cited *Union Illinois* and *Highfields* with approval. *See* *id.* at 135 n.41.

Based on these authorities, this decision does not have to make a finding regarding the reliability of the trading price as a condition to relying on the deal price. It remains conceivable that there could be a case where the parties anchored deal negotiations off the trading price, but this is not that case. All of the bidders, including TransCanada, submitted expressions of interest based on their views of Columbia's value. Although the various parties at times referred to market premiums when discussing bids or potential bids, the bids were not priced at a premium over the trading price. TransCanada's chief concern about the trading price was that Columbia might demand a big premium, creating a risk of overpayment. *See, e.g.*, JX 594 (Poirier remarking that "[if] the stock trades up, [Columbia's] pricing expectations will increase accordingly, and this transaction will be challenging for us.").

As in *Aruba*, TransCanada submitted its formal bids after conducting extensive due diligence and receiving considerable non-public information, including (i) long-term management projections and (ii) the precedent agreements that secured Columbia's growth projects. TransCanada and Columbia then went back and forth over price based on the confidential information that Columbia possessed and TransCanada had obtained. These efforts "improved the parties' ability to estimate" Columbia's "going-concern value over that of the market as a whole." *Aruba*, 210 A.3d at 139.

To reiterate, if the petitioners proved that the trading price in this case was an unreliable indicator of fair value, then it would not undermine the reliability of the deal price given the manner in which Columbia proceeded. This decision therefore has not parsed the parties' many arguments about the trading price. I have considered that form of market evidence, and having done so, I regard the deal price as a more reliable indicator of value. Relying on the trading price would only inject error into the fair value determination.

C. The Discounted Cash Flow Method

***50** The petitioners contend that the court should determine Columbia's fair value using a DCF analysis prepared by their expert, William Jeffers. He valued Columbia at $32.47 per share. TransCanada did not submit its own DCF analysis. Instead, Zmijewski critiqued Jeffers's model. As the proponent of valuing Columbia based on the work of their expert, the petitioners bore the burden of proving the reliability of his valuation.

The DCF method is a technique that is generally accepted in the financial community. "While the particular assumptions underlying its application may always be challenged in any particular case, the validity of [the DCF] technique *qua* valuation methodology is no longer open to question." *Campbell-Taggart*, 1989 WL 17438, at *8 n.11. It is a "standard" method that "gives life to the finance principle that firms should be valued based on the expected value of their future cash flows, discounted to present value in a manner that accounts for risk." *Andaloro v. PFPC Worldwide, Inc.*, 2005 WL 2045640, at *9 (Del. Ch. Aug. 19, 2005).

> The DCF model entails three basic components: an estimation of net cash flows that the firm will generate and when, over some period; a terminal or residual value equal to the future value, as of the end of the projection period, of the firm's cash flows beyond the projection period; and finally a cost of capital with which to discount to a present value both the projected net cash flows and the estimated terminal or residual value.

In re Radiology Assocs., Inc. Litig., 611 A.2d 485, 490 (Del. Ch. 1991) (internal quotation marks omitted).

In *Dell* and *DFC*, the Delaware Supreme Court cautioned against using the DCF methodology when market-based indicators are available. In *Dell*, the high court explained that "[a]lthough widely considered the best tool for valuing companies when there is no credible market information and no market check, DCF valuations involve many inputs—all subject to disagreement by well-compensated and highly credentialed experts—and even slight differences in these inputs can produce large valuation gaps." *Dell*, 177 A.3d at 37–38. The high court warned that when market evidence is available, "the Court of Chancery should be chary about imposing the hazards that always come when a law-trained judge is forced to make a point estimate of fair value based on widely divergent partisan expert testimony." *Id.* at 35. Making the same point conversely in *DFC*, the Delaware Supreme Court advised that a DCF model *should* be used in appraisal proceedings "when the respondent company was not public or was not sold in an open market check ...." *DFC*, 172 A.3d at 369 n.118. The high court commented that "a singular discounted cash flow model is often most helpful when there isn't an observable market price." *Id.* at 370.

This case is not one where a DCF valuation is likely to provide a reliable indication of fair value. Columbia was publicly traded, widely held, and sold in a process that began with pre-signing outreach and finished with an open, albeit passive, post-signing market check. Jeffers's valuation of $32.47 per share stands in contrast with contemporaneous market evidence.

- Jeffers's valuation is 27% higher than the deal price of $25.50 per share.
- Jeffers's valuation is 64% higher than the unaffected trading price of $19.75 per share.[48]
- Jeffers's opinion that the value of Columbia materially exceeded the deal price conflicts with the market behavior of other potential strategic acquirers who had shown interest in Columbia, and who did not step forward to top TransCanada's price.

***51** *Dell* and *DFC* teach that a trial court should have greater confidence in market indicators and less confidence in a divergent expert determination. *See* Dell, 177 A.3d at 35–38; *DFC*, 172 A.3d at 369–70 & n.118.

Consistent with the Delaware Supreme Court's observations in *Dell* and *DFC*, Jeffers's DCF valuation had many inputs, and Zmijewski questioned a number of them. The proper choices were matters of legitimate debate, and the outcome of those debates generated large swings in the valuation output.

For Columbia, the swings were particularly large because management's business plan (the "0&12 Plan") forecasted major capital expenditures between 2016 and 2021, resulting in projected negative cash flow of nearly $4 billion during that period. *See* Zmijewski Tr. 1457–58. As a result, all of the positive value derived from the terminal period. In Jeffers's calculation, the terminal value represented 125% of his valuation of Columbia. Jeffers Tr. 783–85. Given this fact, small changes in the assumptions and inputs that generated the terminal value, such as the discount rate, growth rate, or base-year free cash flow, had a much larger effect on the valuation of Columbia than they would on a typical valuation. *See* Zmijewski Tr. 1457–58. This court has questioned the utility of a DCF in a case where the terminal value represented 97% of the result, finding that "[t]his back-loading highlights the very real risks" presented by using that methodology and "undermin[ing] the reliability of applying the DCF technique."[49]

***52** For example, Jeffers used a beta derived from a five-year regression of weekly returns. Based on his review of the forward pricing curves for natural gas and crude oil, Zmijewski argued that Jeffers should have used a shorter period. Zmijewski also pointed out that Columbia's financial advisors both used betas derived from two-year regressions of weekly observations, and TransCanada's financial advisor used a beta derived from a one-year regression of daily observations. Using a two-year regression of weekly returns would lower the output of the Jeffers DCF model to $18.10 per share. *See* Zmijewski Tr, 1463–67; JX 1368 ¶ 94.

In another example, Jeffers separately valued Columbia's three sources of cash flow: its operating income, its distributions from its limited partner interest in CPPL, and its distributions from its general partner interest in CPPL. But Zmijewski pointed out that Jeffers treated all three as if they were subject to identical risks, thereby underestimating the cost of capital for the limited partner and general partner interests. Correcting Jeffers's discount rates for these cash flows would lower his valuation to a range of $18.96 to $19.23 per share. *See* Zmijewski Tr. 1458–60; JX 1368 ¶ 108.

A final example involves the terminal value calculation. Jeffers used a perpetuity growth rate of 3%. The Proxy indicates that Lazard's DCF analysis implied perpetuity growth rates from 1.4% to 1.9%, and that Goldman's was 1% to 2%. *See* JX 1136 at 65, 75. Reducing Jeffers's terminal growth rate to 1.5% would lower his valuation to $17.28 per share. *See* JX 1368 Ex. V-2.

The wide swings in output that result from legitimate debate over reasonable inputs undermine the reliability of Jeffers's DCF model. And the experts' debates went further, with Zmijewski raising significant questions about the reliability of the Jeffers model's core input (Columbia's management projections). Although the preparation of the 0&12 Plan started with a bottoms-up process, senior management added a "growth wedge" or "initiative layer" to meet top-down targets. Zmijewski Tr. 1454–56; *see also* JX 491. These add-ons assumed significant returns on unidentified projects that lacked customers or regulatory approval. *See* Adamson Tr. 1317–18; Skaggs Tr. 881–82; Mayo Dep. 273. This too raised fundamental questions about the reliability of Jeffers's DCF analysis as a whole.

If this were a case where a reliable market-based metric was not available, then the court might have to call the balls and strikes of the valuation inputs. In this case, the DCF technique "is necessarily a second-best method to derive value." *Union Illinois*, 847 A.2d at 359. This decision therefore does not use it. *See* Solera, 2018 WL 3625644, at *32.

III. CONCLUSION

The fair value of Columbia's common stock at the effective date was $25.50 per share. The legal rate of interest, compounded quarterly, shall accrue on the appraised value from the effective date until the date of payment. The parties shall cooperate on a form of final order. If there are additional issues for the court to resolve before entering a final order, then the parties shall submit a joint letter within fourteen days that identifies them and proposes a path to conclude this case at the trial level.

All Citations

Not Reported in Atl. Rptr., 2019 WL 3778370

Footnotes

[1] Citations in the form "PTO ¶ —" refer to stipulated facts in the pre-trial order. Dkt. 397. Citations in the form "[Name] Tr." refer to witness testimony from the trial transcript. Citations in the form "[Name] Dep." refer to witness testimony from a deposition transcript. Citations in the form "JX —— at —" refer to a trial exhibit with the page designated by the last three digits of the control or JX number or, if the document lacked a control or JX number, by the internal page number. If a trial exhibit used paragraph numbers, then references are by paragraph.

[2] The parties designated the transcripts as joint exhibits rather than lodging them separately. The JX designations made it more difficult to determine during briefing when a deposition transcript was being cited and whose testimony it was. It would be more helpful to have the deposition transcripts lodged and collected in a separate binder, then cited in the form "[Name] Dep." I offer this point not to criticize the parties' approach, which was a reasonable one, but rather as a suggestion for the future.

[3] *See* Tom Miesner, *A Practical Guide to US Natural Gas Transmission Pipeline Economics*, 8 J. Pipeline Eng'g 111, 112 (2009); Matthew J. McCabe, Comment, *Master Limited Partnerships' Cost of Capital Conundrum*, 17 U. Pa. J. Bus. L. 319, 325 (2014).

[4] JX 258 at 2; *see* JX 886 at 34 ("[Columbia's] 'Drop Downs' are atypical in that the transaction is effected through [CPPL] acquiring incremental interests in OpCo .... [Columbia's] interest in OpCo is accordingly diluted down.").

[5] *See id.* at 46 (Lazard anticipating stock-price improvement of up to $12 per share; observing that NiSource traded "at a premium valuation relative to its diversified utility peers, but at a discount to the blended consolidated multiple implied by MLP valuations for [Columbia]"); *see also* JX 231 at 2 (consulting firm remarking in January 2015 that despite "40% drop in gas price since 2014" and "pressure" on "[g]as basin economics," that "original [spinoff] rationale holds: Utilities and [Columbia] are separate businesses, the market is supportive of focused players, growth stories and risk profiles are different"). *See generally* Mir Dep. 55–73. As anticipated, separating NiSource, Columbia, and CPPL increased their total market capitalization by approximately $4 billion. *See* JX 404 at 6.

[6] *See* Mir Tr. 1197 ("[T]he business plan was dependent on being able to raise a lot of equity through the MLP, CPPL. The MLPs at the time were the de facto means of raising equity for pipeline and midstream projects."); JX 300 at 20 (Lazard warning that Columbia's "[f]inancing plan [was] highly dependent on CPPL's ability to issue equity at attractive terms over time"); JX 480 at 7 (Lazard identifying upside of "[s]trong access to capital and low cost of CPPL equity" and downside of "CPPL unable to access equity market at attractive terms (potentially requiring [Columbia] to issue equity)"); JX 214 at 17 (CPPL IPO pitch materials indicating CPPL's equity would "be the primary source of new funding for Columbia OpCo expansion capital projects"); JX 277 at 4 (analyst report identifying risks like "highly leveraged balance sheet," growth plan's execution risk, and

"financing strategy which relies almost completely on [CPPL's] ability to access the equity capital markets during the next several years"); *see also* Kittrell Tr. 1052 ("As part of the spin, we had been able to launch [CPPL] in January of 2015 and raise just over a billion dollars. We also had done a series of debt financings as of the spin for about $3 billion. So that gave Columbia $4 billion of permanent capital to kind of come out of the chute with as a standalone independent company. That still left $3 to 4 billion of capital that we were going to need for '16, '17, and '18."); JX 96 at 12 (Lazard observing that the "most successful" MLPs had "low-risk assets and visible growth opportunities, driven by either organic investments or dropdowns from a supportive general partner that is motivated to grow IDR distributions [to itself]").

[7] JX 167; *see* Mir Tr. 1195–97. Pre-spinoff, the operative entity was Columbia Energy Group, but for simplicity this decision uses "Columbia."

[8] *See id. Compare* JX 753 at 4 (Skaggs explaining in January 2016 that "for CPPL to be a viable equity currency," prices would have to improve to at least $21 per unit by 2017 and at least $27 per unit by 2018), *with* Dkt. 390 Ex. D (stipulated CPPL price chart showing prices below $14 per unit in late 2015).

[9] *Id.*; *see id.* ("[I]f there is a real or perceived expectation of reduced growth rates, all the more pressure is placed on the value of CPG's currencies, thereby exacerbating the challenge."); Mir Tr. 1198–1202 (discussing equity overhang at Columbia and CPPL levels); JX 1351 ¶¶ 100–01 (respondent's expert opining that "disruption in the MLP market and [Columbia's] equity overhang could have forced [Columbia] into issuing increasingly large numbers of shares to raise equity as the market drove down the value of [Columbia] shares in expectation of repeated [Columbia] equity issuances" (citing Jonathan Berk & Peter DeMarzo, *Corporate Finance* 888 (4th ed. 2017)).

[10] *Id.* ¶ 425; *see* Skaggs Tr. 862–63; Cornelius Tr. 1133–34; *see also* JX 493.

[11] *Id.* ¶¶ 442–49, 452–54. Goldman regarded Berkshire and TransCanada as the most likely buyers, followed by Dominion. *See, e.g.*, JX 499 ("We know D[ominion] is interested, but at a price."). Poirier expected an auction. *See* JX 528. He encouraged his colleagues to act quickly because Columbia had a "massive financing overhang" and was preparing to "prefund[ ] [its] 2016/17 capex with a $1bn equity issuance." *Id.*

[12] *See* PTO ¶ 500; Smith Tr. 248; *see also* JX 646 (Goldman: "[TransCanada] indicated that they could be ~ $28.00/share."); Poirier Dep. 148 ("The goal posts of 26 and 30 would translate to 24 and 28 post equity issuance.").

[13] *See* JX 736 at 11; *id.* (noting that Dominion ("capital, HSR"), Enbridge ("complex structure"), Energy Transfer Equity ("overextended"), and Kinder Morgan ("out of the market") were unlikely to be suitors for Columbia); Poirier Dep. 149–52.

[14] *See* Smith Tr. 343 ("It was to negotiate with him, to basically say ... the market is in disarray. There are number of, you know, big players that are dealing with issues. This is your opportunity, you know, to step up to the plate and make an offer that will get the attention of the board."); Poirier Dep. 150–51 (framing Smith's approach as "encouragement to dedicate time and resources" by describing TransCanada's strong odds of success at the right price); Poirier Tr. 435 ("He was simply trying to encourage us to be aggressive, that there was an opportunity for us to acquire this company.").

[15] Broadly speaking, precedent agreements address future customer needs and can help justify pipeline expansion to regulators. *E.g.*, Mayo Dep. 277 ("[Precedent agreements are] the agreements signed before the final contract."). Columbia's precedent agreements covered infrastructure construction and defined the quantities of natural gas to transport, transportation path, and terms of service. PTO ¶ 280. A party with access to the precedent agreements could discern whether a given Columbia customer "was an ExxonMobil" or "a single B grade producer" prone to default in a downturn. *See* Marchand Tr. 526; *see also* JX 815 (TransCanada due diligence memo finding credit terms relatively disappointing yet "normal for U.S. regulated natural gas pipeline projects"); JX 829 (analyst report stating that Columbia "requires credit support for non-I grade customers equivalent to 12–24 months of demand charges").

[16] In internal emails exchanged on March 10, 2016, TransCanada's bankers discussed that "[t]he [Columbia] board is freaking out and told the management team to get a deal done with 'whatever it takes' .. Oddly, the [Columbia] team has relayed this info to [TransCanada]." JX 938. This exchange could suggest that there

was a path for Columbia to extract additional merger consideration from TransCanada, but the petitioners have not briefed this document, and I take no position on it.

[17] *See* Ben Dummett et al., *Keystone Pipeline Operator TransCanada in Takeover Talks*, Wall St. J., March 10, 2016, https://www.wsj.com/articles/keystone-pipeline-operator-transcanada-in-takeover-talks-1457627686 ("TransCanada ... is in takeover talks with Columbia Pipeline Group Inc., a U.S. natural-gas pipeline operator with a market value of about $9 billion. The companies could reach a deal in the coming weeks, according to people familiar with the matter.").

[18] JX 949. Goldman received calls too. *See* JX 951 at 3 ("One question [Skaggs] asked is shd [*sic*] we let [TransCanada] know we are getting calls."); *see also* JX 948 (Goldman banker indicating "[n]ot a lot of interest [from Columbia's management] in engaging with Spectra. Would be all-stock deal, they don't love Spectra's assets.").

[19] *See id.* (Smith email to Goldman and management: "We need to think about what the protocol is if we get a letter. Presumably, the Board would have to respond officially, we would have to notify [TransCanada] and we should think about what our response is if they make it public after being rebuked."); Skaggs Tr. 1021–22 ("Q. ... During this stage when you were getting an inbound call from the CEO of Spectra, an inbound e-mail from the CEO of Spectra, a call from the CFO of Spectra to Goldman Sachs, and a call from the chief development officer of Goldman Sachs, did you, Mr. Skaggs, or another member of management, do anything to respond to Spectra? And since I'm going to anticipate what you're going to say, other than tell Goldman to look at the script. A. That was it, sir. Q. So the answer's no. A. No.").

[20] *See* JX 1399 at 17 ("The Board ... acknowledged that proceeding with TransCanada on the expedited timetable would mean that the Company would potentially be entering into the merger agreement without having the opportunity to consider [the] formal proposal from Spectra" that Goldman expected to arrive "in the next few days.").

[21] *See, e.g.*, JX 1016 at 78–79, 107; JX 1136 at 66, 74–77.

[22] *See* PTO ¶ 625. The Board made a related determination that the renewed Exclusivity Agreement prohibited Columbia from soliciting an offer from Spectra or anyone else. *See id.* That was inaccurate. The renewed Exclusivity Agreement expired upon "written notification to [Columbia] that [TransCanada] has determined that it is no longer interested in pursuing a Potential Transaction on terms at least as favorable to the stockholders of [Columbia] as the terms discussed ... on March 10, 2016." JX 978 at 4. TransCanada's March 10 proposal offered $26 per share. TransCanada's reduced offer of $25.50 per share terminated exclusivity. But if the Columbia directors had considered this fact, it would not have changed how they proceeded. When exclusivity terminated the first time, the Board acted as if it remained in place, and the script used with Spectra was the functional equivalent of exclusivity. *See* JX 968. The Board worried about losing the TransCanada offer, and it regarded that risk as outweighing the benefit of an expedited solicitation process involving other bidders.

[23] *Id.* at 72. Although *Battye* is the seminal Delaware Supreme Court case on point, Chancellor Josiah Wolcott initially established the meaning of "value" under the appraisal statute in *Chicago Corporation v. Munds*, 172 A. 452 (Del. Ch. 1934). Citing the "material variance" between the Delaware appraisal statute, which used "value," and the comparable New Jersey statute that served as a model for the Delaware statute, which used "full market value," Chancellor Wolcott held that the plain language of the statute required "value" to be determined on a "going concern" basis. *Id.* at 453–55. *But see* *Union Ill. 1995 Inv. Ltd. P'ship v. Union Fin. Gp., Ltd.*, 847 A.2d 340, 355–56 (Del. Ch. 2004) ("This requirement that the valuation inquiry focus on valuing the entity as a going concern has sometimes been confused as a requirement of § 262's literal terms. It is not."). The going-concern standard also tracks the judicially endorsed account in which the appraisal statute arose "as a means to compensate shareholders of Delaware corporations for the loss of their common law right to prevent a merger or consolidation by refusal to consent to such transactions." *See, e.g.*, *Alabama By-Products Corp. v. Cede & Co.*, 657 A.2d 254, 258 (Del. 1995). As *Battye* explains, the appraisal statute calls for valuing the corporation as a going concern, using its operative reality as it then existed as a standalone entity, because that is the alternative that the dissenters wished to maintain. *Battye*, 74 A.2d at 72. Commentators

have questioned the accuracy of the historical trade-off, but it remains part of the foundational understanding that has informed the concept of fair value. *See* Lawrence A. Hamermesh & Michael L. Wachter, *The Fair Value of Cornfields in Delaware Appraisal Law*, 31 J. Corp. L. 119, 130 n.52 (2005) ("The historical accuracy of this trade-off story is questionable, however, given the fact that the appraisal remedy was often added well after the adoption of statutes permitting mergers without unanimous consent." (citing Robert B. Thompson, *Exit, Liquidity, and Majority Rule: Appraisal's Role in Corporate Law*, 84 Geo L.J. 1, 14 (1995))).

[24] *See, e.g.*, *Montgomery Cellular Hldg. Co. v. Dobler*, 880 A.2d 206, 222 (Del. 2005); *Paskill Corp. v. Alcoma Corp.*, 747 A.2d 549, 553 (Del. 2000); *Rapid-Am. Corp. v. Harris*, 603 A.2d 796, 802 (Del. 1992); *Cavalier Oil Corp. v. Harnett*, 564 A.2d 1137, 1144 (Del. 1989); *Bell v. Kirby Lumber Corp.*, 413 A.2d 137, 141 (Del. 1980); *Universal City Studios, Inc. v. Francis I. duPont & Co.*, 334 A.2d 216, 218 (Del. 1975).

[25] *Cede & Co. v. Technicolor, Inc.*, 2003 WL 23700218, at *2 (Del. Ch. Dec. 31, 2003), *as revised* (July 9, 2004), *aff'd in part, rev'd in part on other grounds*, 884 A.2d 26 (Del. 2005); *accord* *Finkelstein v. Liberty Dig., Inc.*, 2005 WL 1074364, at *12 (Del. Ch. Apr. 25, 2005) ("The judges of this court are unremittingly mindful of the fact that a judicially selected determination of fair value is just that, a law-trained judge's estimate that bears little resemblance to a scientific measurement of a physical reality. Cloaking such estimates in grand terms like 'intrinsic value' does not obscure this hard truth from any informed commentator.").

[26] *See* *Aruba*, 210 A.3d at 135; *Dell*, 177 A.3d at 23; *DFC Glob. Corp. v. Muirfield Value P'rs*, 172 A.3d 346, 367 (Del. 2017).

[27] *See* *Aruba*, 210 A.3d at 137 (emphasizing that buyer armed with "material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller"). *But see* *In re Dunkin' Donuts S'holders Litig.*, 1990 WL 189120, at *9 (Del. Ch. Nov. 27, 1990) ("A bidder's objective is to identify an underpriced corporation and ... acquire it at the lowest price possible."); *cf.* *DFC*, 172 A.3d at 374 n.145 (rejecting reliance on evidence indicating buyer's contemporaneous belief that it purchased target "at trough pricing"; commenting that "it is in tension with the statute itself to argue that the subjective view of post-merger value of the acquirer can be used to value the respondent company in an appraisal"; observing "[t]hat a buyer views itself as having struck a good deal is far from reliable evidence that the resulting price from a competitive bidding process is an unreliable indicator of fair value").

[28] *See* *Aruba*, 210 A.3d at 136–39, 142 (adopting deal price less synergies as fair value where company's banker contacted six potential buyers after HP's initial outreach, none were interested, sale process terminated, and sale process later resumed as single-bidder engagement with HP); *Dell*, 177 A.3d at 28 (finding competitive pre-signing process where Silver Lake competed one-at-a-time with interested parties); *DFC*, 172 A.3d at 350, 376 (finding "competitive process of bidding" where company's banker contacted "every logical buyer," three expressed interest, and two named a preliminary price with one dropping out before serious negotiations commenced).

[29] *See* *Aruba*, 210 A.3d at 136 ("It cannot be that an open chance for buyers to bid signals a market failure simply because buyers do not believe the asset on sale is sufficiently valuable for them to engage in a bidding contest against each other."); *Dell*, 177 A.3d at 29 ("Fair value entails at a minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay."); *id.* at 33 (finding that absence of higher bid meant "that the deal market was already robust and that a topping bid involved serious risk of overpayment," which "suggests the price is already at a level that is fair").

[30] At times, the petitioners also targeted a third executive—Glen Kettering—who served as President of Columbia. He was less involved in the sale process than Skaggs and Smith, and the petitioners never deposed him. Although Kettering retired after the Merger and received change-in-control benefits, the evidence does not support the contention that he pushed for an early sale.

[31] Smith Tr. 316; *see* JX 562 (Goldman describing Berkshire's requests as atypically granular for "early [ ] M&A dialogue"); JX 555 (Berkshire requesting separate operating models for each OpCo subsidiary); JX 550 (detailed Berkshire diligence questionnaire); JX 565 (same); JX 568 (same); JX 551 (responding to Berkshire request about MLP tax structure); JX 554 (same). *See generally* PTO ¶¶ 460–66 (describing Berkshire diligence).

32 *E.g.*, JX 746 (Skaggs writing to Board on January 26, 2016: "Consistent with our recent one-on-one conversations about a potential inbound overture, TransCanada's ... CEO called me on Monday afternoon (1/25) to outline a proposition to acquire CPG.").

Before Poirier and Smith met in January 2016, Poirier assured Smith that he could share due diligence materials without TransCanada breaching the standstill. *See* JX 485 at 2 ("My understanding is that our respective counsels have talked, and that we are ok to proceed with exchanging information. As we destroyed all non public [*sic*] information, in addition to the data room index, would it be possible to receive again the information you previously sent, including the board summaries?"). At trial, Poirier unpersuasively rationalized his overtures to Smith as complying with the standstill because he "wasn't submitting a formal offer for the company." Poirier Tr. 387. Poirier is an experienced investment banker. He should have understood the standstill's scope. When pushed, he cited unspecified legal advice from TransCanada's counsel. *See id.*; *id.* at 454.

On January 22, 2016, TransCanada's in-house counsel drafted an email to Columbia's in-house counsel opining that an upcoming call between Girling and Skaggs would not breach the standstill, because although "there may be some broad discussion regarding valuation of [Columbia]," Girling would not make an offer to buy. JX 735. The point of talking numbers was to facilitate a bid, thus breaching the standstill. TransCanada's in-house counsel concluded her email by seeking confirmation that TransCanada would not breach the standstill "in the event [that it made] a verbal or written offer or proposal." *Id.* That request effectively sought waiver of the DADW, also a breach.

33 The petitioners advance a similar argument about the threat of massive tax liability deterring potential acquirers from buying Columbia. NiSource spun off Columbia in a tax-free transaction, but an acquirer could become liable for the tax if it had negotiated to buy Columbia before the spinoff and then bought it afterwards. *See* I.R.C. § 355(c)(2), (e); Tres. Reg. § 1.355-7(b)(3)(iii); Rev. Rul. 2005-2 C.B. 684. The petitioners cite an April 2016 email in which TransCanada's CFO cited "rumblings, that we are unable to confirm or refute, that Enbridge may have had prior discussions with NiSource that could impact the tax-free status of the spin of Columbia." JX 1108. With the potential exception of TransCanada, there is no direct evidence of anyone negotiating with NiSource before the spinoff. *See, e.g.*, JX 311 (circumstantial evidence of TransCanada and Lazard engaging in talks before spinoff). The petitioner failed to carry their burden of proof on this issue.

34 By February 2016, Skaggs was updating the Board on an at least weekly basis. *See, e.g.*, JX 780; JX 785; JX 806; JX 808; JX 830; JX 846; JX 852; JX 855. By March, Skaggs was updating the Board on a near-daily basis. *See, e.g.*, JX 874; JX 913; JX 929; JX 939; JX 945; JX 962; JX 964; JX 995; JX 1004; JX 1007; JX 1010.

35 *See, e.g.*, Kittrell Tr. 1107–08 ("Q.... And it's fair to say that the board never authorized management to tell any potential bidder that Columbia had eliminated the competition for a competing bid. Right? A. The board would never have given that specific direction."); *accord* Kittrell Dep. 164 (describing Smith's strategy as "counterintuitive").

36 *See* JX 1022; JX 1016 at 20; *see also* Mir Tr. 1212 (describing Lazard's view that Spectra was "not a credible or capable buyer").

37 *See generally* Charles Korsmo & Minor Myers, *Reforming Modern Appraisal Litigation*, 41 Del. J. Corp. L. 279, 320–25 (2017) (comparing appraisal with fiduciary review with primary focus on deals without a controlling stockholder); Charles Korsmo & Minor Myers, *Appraisal Arbitrage and the Future of Public Company M&A*, 92 Wash. U. L. Rev. 1551, 1607–09 (2015) (same).

38 *Compare* Lawrence A. Hamermesh & Michael L. Wachter, *Finding the Right Balance in Appraisal Litigation: Deal Price, Deal Process, and Synergies*, 73 Bus. Law. 961, 962 (2018) (commending outcomes in *Dell* and *DFC* and arguing that "the Delaware courts' treatment of the use of the deal price to determine fair value does and should mirror the treatment of shareholder class action fiduciary duty litigation"), *and* *id.* at 982–83 (citing *Dell* and *DFC* and observing, "What we discern from the case law, however, is a tendency to rely on deal price to measure fair value where the transaction would survive enhanced judicial scrutiny .... Thus, in order to determine whether to use the deal price to establish fair value, the Delaware courts are engaging in the same sort of scrutiny they would have applied under *Revlon* if the case were one challenging the merger

as in breach of the directors' fiduciary duties." (footnote omitted)), *with* Charles Korsmo & Minor Myers, *The Flawed Corporate Finance of* Dell *and* DFC Global, 68 Emory L.J. 221, 269 (2018) (criticizing *Dell* and *DFC* as "conflat[ing] questions of fiduciary duty liability with the valuation questions central to appraisal disputes").

39 *See, e.g.*, *Dent v. Ramtron Int'l Corp.*, 2014 WL 2931180, at *8–10 (Del. Ch. June 30, 2014) (rejecting fiduciary challenge to "(1) a no-solicitation provision; (2) a standstill provision; (3) a change in recommendation provision; (4) information rights for [the acquirer]; and (5) a $5 million termination fee" where termination fee represented 4.5% of equity value and change-of-recommendation provision included unlimited match right); *In re Novell, Inc. S'holder Litig.*, 2013 WL 322560, at *10 (Del. Ch. Jan. 3, 2013) (describing "the no solicitation provision, the matching rights provision, and the termination fee" as "customary and well within the range permitted under Delaware law" and observing that "[t]he mere inclusion of such routine terms does not amount to a breach of fiduciary duty"); *In re Answers Corp. S'holders Litig.*, 2011 WL 1366780, at *4 & n.47 (Del. Ch. Apr. 11, 2011) (describing "a termination fee plus expense reimbursement of 4.4% of the Proposed Transaction's equity value, a no solicitation clause, a 'no-talk' provision limiting the Board's ability to discuss an alternative transaction with an unsolicited bidder, a matching rights provision, and a force-the-vote requirement" as "standard merger terms" that "do not alone constitute breaches of fiduciary duty" (quoting *In re 3Com S'holders Litig.*, 2009 WL 5173804, at *7 (Del. Ch. Dec. 18, 2009))); *In re Atheros Commc'ns, Inc. S'holder Litig.*, 2011 WL 864928, at *7 n.61 (Del. Ch. Mar. 4, 2011) (same analysis for no-solicitation provision, matching right, and termination fee); *In re 3Com*, 2009 WL 5173804, at *7 & n.37 (also same analysis for no-solicitation provision, matching right, and termination fee (collecting authorities)).

40 *Cf.* *In re Toys "R" Us, Inc. S'holder Litig.*, 877 A.2d 975, 1015 (Del. Ch. 2005) ("[I]n his scholarly work Subramanian argues that [the] combination of a termination fee and matching rights raises the fears second bidders have of suffering a 'winner's curse.' This is the anxiety that a first bidder will match the initial topping bid, only to refuse to match the next topping gambit, leaving the second bidder having paid more than was economically rational. This fear, Subramanian points out, is further exacerbated by the common circumstance that first bidders often have superior information on the target, and presumably know when to say when. Of course, the other side of this story is that the first bidder has taken the risk, suffered the search and opportunity costs, and done the due diligence required to establish the bidding floor.").

41 *See* *Blueblade Capital Opportunities LLC v. Norcraft Cos.*, 2018 WL 3602940, at *23–27 (Del. Ch. July 27, 2018); *In re Appraisal of AOL, Inc.*, 2018 WL 1037450, at *8–10 (Del. Ch. Feb. 23, 2018) (subsequent history omitted). After post-trial briefing and argument in this case, this court took a similar approach in *In re Appraisal of Jarden Corporation*, 2019 WL 3244085, at *24–25 (Del. Ch. July 19, 2019).

42 JX 935 at 12. In the presentation, TransCanada estimated $150 million in financing synergies. TransCanada lowered this estimate to $100 million for purposes of communicating to the markets, viewing the lower number as more realistic and achievable. *See* Marchand Tr. 494–96.

43 The petitioners argue that the alternative is zero, relying on an article from 1987 that Zmijewski cited in his report. *See* JX 9. The authors examined a sample of tender offers from 1963 to 1984 and observed that "[o]nly when competing bids are actually made do we observe greater returns to target shareholders and a dissipation of the initial gains to the stockholders of the bidding firms." *Id.* at 22–23. The petitioners argue that Columbia never solicited competing bids, so Columbia could not have extracted any synergies. The article does not support this claim. It finds that targets extract a share of surplus even in single-bidder contests, but also finds that only in multi-bidder contests do the returns to bidders dissipate. The article thus supports the view that TransCanada did not share all of its synergies with Columbia. It does not support the view that TransCanada did not share any of its synergies with Columbia.

44 The petitioners also rely on a Wells Fargo research report that mentions that certain MLPs had success raising capital in 2016, but it did not focus on natural gas MLPs. *See* JX 1468. The successful equity raises largely involved blue-chip sponsors, offered preferred units that Columbia could not support because of its debt load, or were completed through at-the-market raises, a technique that could not have sustained Columbia's business plan. *See* Adamson Tr. 1333–40, 1406–09.

45 As precedent for the deal-price-less-synergies metric, the *Union Illinois* decision cited three cases: *M.P.M. Enterprises*, *Cooper v. Pabst Brewing Company*, 1993 WL 208763 (Del. Ch. June 8, 1993), and *Van de Walle v. Unimation, Inc.*, 1991 WL 29303 (Del. Ch. Mar. 7, 1991). *See* *Union Illinois*, 847 A.2d at 343 (citing the three cases and stating that "our case law recognizes that when there is an open opportunity to buy a company, the resulting market price is reliable evidence of fair value").

The *Pabst* decision appears to be the first Delaware case to determine fair value by drawing on the pricing of the deal that gave rise to the appraisal proceeding, but the *Pabst* court did so in a manner that differed from *Union Illinois.* After a public auction involving competitive bidding by multiple suitors, G. Heileman Brewing Company acquired Pabst Brewing Company through a structurally coercive, two-tiered tender offer, in which Heileman paid $32 per share in the first step and squeezed out the remaining stockholders in the back-end merger for a package of subordinated debentures with a face value of $24 per share. *Pabst*, 1993 WL 208763, at *2, *8. The court rejected all of the parties' valuation methods, forcing the court to "make a determination based upon its own analysis." *Id.* at *8. The court reached a fair value conclusion of $27 per share by blending the front-end and back-end consideration to reach a value of $29.50, and then deducting a control premium, which the court estimated "did not exceed $2.50 per share." *Id.* at *8, *10. The court did not equate the control premium with a synergies-based deduction.

After *Pabst*, the concept of a deal price metric next surfaced in *M.P.M. Enterprises.* The petitioners were minority stockholders in privately held company that was sold to a third-party buyer. The trial court valued the company using a DCF analysis. The respondent appealed, asserting that the trial court erred by failing to give weight to the transaction price and relying heavily on *Van de Walle*, a breach of fiduciary duty action in which a controlled company was sold to a third party and all stockholders received consideration having the same value. As one of many reasons for entering judgment in favor of the defendants, the *Van de Walle* court cited the arm's-length negotiations between the seller and the buyer. In an eloquent turn of phrase that has figured prominently in twenty-first century appraisal decisions, the *Van de Walle* court observed that "[t]he fact that a transaction price was forged in the crucible of objective market reality (as distinguished from the unavoidably subjective thought process of a valuation expert) is viewed as strong evidence that the price is fair." 1991 WL 29303, at *17. In *M.P.M. Enterprises*, however, the Delaware Supreme Court distinguished *Van de Walle* as a breach of fiduciary duty case and observed that "[a] fair merger price in the context of a breach of fiduciary duty claim will not always be a fair value in the context of determining going concern value." 731 A.2d at 797. The high court did express agreement with "the general statement made by the Court in *Van de Walle*" to the effect that "[a] merger price resulting from arms-length negotiations where there are no claims of collusion is a very strong indication of fair value." *Id.* But the high court again cautioned that "in an appraisal action, that merger price must be accompanied by evidence tending to show that it represent the going concern value of the company rather than just the value of the company to one specific buyer." *Id.* Citing the trial court's broad discretion when assessing fair value, the high court in *M.P.M. Enterprises* affirmed the trial court.

46 *Merion Capital LP v. BMC Software, Inc.*, 2015 WL 6164771 (Del. Ch. Oct. 21, 2015); *LongPath Capital, LLC v. Ramtron Int'l Corp.*, 2015 WL 4540443 (Del. Ch. June 30, 2015); *Merlin P'rs LP v. AutoInfo, Inc.*, 2015 WL 2069417 (Del. Ch. Apr. 30, 2015); *In re Appraisal of Ancestry.com, Inc.*, 2015 WL 399726 (Del. Ch. Jan. 30, 2015); *Huff Fund Inv. P'ship v. CKx, Inc.*, 2013 WL 5878807 (Del. Ch. Nov. 1, 2013). At the trial level in *Golden Telecom*, this court stated that "an arms-length merger price resulting from an effective market check is entitled to great weight in an appraisal." *Golden Telecom Trial*, 993 A.2d at 507. The trial court in *Golden Telecom* declined to apply the deal-price-less-synergies metric on the facts of the case because two large stockholders holding a combined 44% of the equity stood on both sides of the transaction and a special committee treated the deal as if the company had a controlling stockholder. *Id.* at 508–09.

47 *Ramtron*, 2015 WL 4540443, at *20; *see* *BMC*, 2015 WL 6164771, at *14 ("robust, arm's-length sales process"); *Ancestry.com*, 2015 WL 399726, at *16 ("[T]he process here ... appears to me to represent an auction of the Company that is unlikely to have left significant stockholder value unaccounted for.").

48 For reasons previously discussed, this decision has not relied on the unaffected trading price as a valuation metric and has not made a finding as to whether or not the trading price was reliable. The significant distance

between the trading price of $19.75 and expert valuation of $32.47 per share is nevertheless worth observing, because it suggests that at least one of these metrics, and possibly both, is wrong.

[49] *Union Illinois*, 847 A.2d at 361; *see In re Appraisal of Solera Hldgs., Inc.*, 2018 WL 3625644, at *32 (Del. Ch. July 30, 2018) (discounting petitioners' DCF analysis in part because "nearly ***88%*** of the petitioners' enterprise valuation is attributable to periods *after* the five year Hybrid Case Projections"). In *Union Illinois* and *Solera*, as in this case, growth rates drove the back-loading of the valuation. In other decisions, when valuators used an exit multiple to derive the terminal value, this court has criticized valuations where a high percentage of value resulted from the terminal period because "the entire exercise amounts to little more than a special case of the comparable companies approach." *Gray v. Cytokine Pharmasciences, Inc.*, 2002 WL 853549, at *9 (Del. Ch. Apr. 25, 2002) (criticizing a valuation on this basis where the terminal value accounted for over 75% of the total value); *see Gholl*, 2004 WL 2847865, at *13 (criticizing discounted cash flow valuation where exit multiples method for calculating terminal year value resulted in the terminal value representing over 70% of its total present value); *Prescott Gp. Small Cap. v. Coleman Co., Inc.*, 2004 WL 2059515, at *24-25 (Del. Ch. Sept. 8, 2004) (same criticism of terminal value derived using exit multiple method that comprised 70% to 80% of present value).

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UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

IN RE APPRAISAL OF DELL INC.

Consol. C.A. No. 9322–VCL
|
Submitted: May 11, 2015
|
Decided: July 13, 2015
|
Date Revised: July 30, 2015

Synopsis

Background: Beneficial owners of stock filed petitions for appraisal after corporation announced a going-private merger. Corporation asserted that stockholders had lost their appraisal rights, and corporation moved for summary judgment.

The Court of Chancery, Laster, Vice Chancellor, held that continuous holder requirement, mandating that a petitioner seeking appraisal of stock in light of proposed merger continuously hold the shares for which appraisal is sought as a holder of record through the effective date of the merger, barred beneficial owner of stocks from pursuing appraisal.

Motion granted.

Procedural Posture(s): Motion for Summary Judgment.

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MEMORANDUM OPINION

LASTER, Vice Chancellor.

***1** The petitioners are five institutions[1] who owned common stock of Dell Inc. They sought appraisal after Dell announced a going-private merger. Dell contends that they did not hold their shares continuously through the effective date of the merger and therefore lost their appraisal rights.

The Funds held their shares through custodial banks. By virtue of this relationship, the Funds did not have legal title to the shares; they were beneficial owners. But the custodial banks did not have legal title either. The shares they held were registered in the name of Cede & Co., which is the nominee of the Depository Trust Company ("DTC").[2]

DTC's place in the ownership structure results from the federal response to a paperwork crisis on Wall Street during the late 1960s and early 1970s. Increased trading volume in the securities markets overwhelmed the back offices of brokerage firms and the capabilities of transfer agents. No one could cope with the burdens of documenting stock trades using paper certificates. The markets were forced to declare trading holidays so administrators could catch up. With trading volumes continuing to climb, it was obvious that reform was needed. Congress directed the SEC to evaluate alternatives that would facilitate trading.

After studying the issue, the SEC adopted a national policy of share immobilization. To carry out its policy, the SEC placed a new entity—the depository institution—at the bottom the ownership chain. DTC emerged as the only domestic depository. Over 800 custodial banks and brokers are participating members of DTC and maintain accounts with that institution. DTC holds shares on their behalf in fungible bulk, meaning that none of the shares are issued in the names of DTC's participants. Instead, all of the shares are issued in the name of Cede. Through a Fast Automated Securities Transfer account (the "FAST Account"), DTC uses an electronic book entry system to track the number of shares of stock that each participant holds.

***2** By adding DTC to the bottom of the ownership chain, the SEC eliminated the need for the overwhelming majority of legal transfers. Before share immobilization, custodial banks and brokers held shares through their own nominees, so new certificates had to be issued frequently when shares traded. With share immobilization, legal title remains with Cede. No new certificates are required.

Although the depository system solved the paperwork crisis, it complicated other aspects of the legal system. Appraisal is one of those areas. When a transaction triggers appraisal rights, Section 262 of the Delaware General Corporation Law (the "DGCL") permits "[a]ny stockholder of a corporation" who complies with its requirements to litigate a proceeding that will result in a judicial determination of the "fair value of the shares." 8 *Del. C.* §§ 262(a) & (h). The statute states that "[a]s used in this section, the word 'stockholder' means a holder of record of stock in a corporation." *Id.* § 262(a) (the "Record Holder Requirement"). One of the statutory requirements is that a stockholder who wishes to pursue appraisal must "continuously hold[ ] such shares through the effective date of the merger." *Id.* (the "Continuous Holder Requirement").

Many appraisal decisions have involved disputes over these requirements. In one recurring scenario, companies argued that a petitioner had lost its appraisal rights when DTC followed its usual procedures, surrendered the shares held in fungible bulk for the merger consideration, and distributed the merger consideration to its participants, who then deposited it in their customers' accounts.[3] In *Alabama By–Products Corp. v. Cede & Co.*, 657 A.2d 254 (Del.1995), the Delaware Supreme Court held that if a petitioner had properly perfected its appraisal rights through Cede, then the petitioner would not lose its appraisal rights if DTC surrendered the shares in exchange for the merger consideration. The court reached this conclusion because the surrender did not comply with the appraisal statute's requirements for withdrawing or settling a properly perfected appraisal claim. The practical effect of this decision was to "impose upon the corporation the responsibility of overseeing the surrender of shares after a merger." *Id.* at 263.

***3** To help issuers oversee the surrender of shares, DTC modified its procedures. Now, when a beneficial owner causes Cede to demand appraisal, DTC removes the shares covered by the demand from the fungible bulk tracked in the FAST Account. DTC does this by causing the issuer's transfer agent to issue a paper stock certificate for the number of shares held by the beneficial owner. The paper certificate is issued in Cede's name, so the same record holder continues to hold the shares for purposes of the Continuous Holder Requirement.

In this case, DTC followed its procedures and issued paper stock certificates in Cede's name for the Funds' shares. DTC then contacted the custodial banks to make arrangements for delivering the resulting valuable pieces of paper. But here another back-office procedure kicked in. For various understandable business reasons (insurance requirements, recordkeeping for internal audit, mitigating risk of theft, etc.), some banks and brokers only hold stock certificates that are issued in the names of their own nominees. The Funds' custodial banks followed this policy.

When DTC contacted the custodial banks, each instructed Dell's transfer agent to record a transfer of the shares to its nominee and issue a certificate in its nominee's name.

Dell's transfer agent complied. The Funds remained the beneficial owners. The custodians remained the custodians. But now there were new nominees on the stock ledger.

Dell has moved for summary judgment, arguing that these back-office steps resulted in new record holders and broke the chain of title for purposes of the Continuous Holder Requirement. Under Delaware cases that pre-dated the federal policy of share immobilization, the record holder for purposes of the DGCL was the person that appeared on the stock ledger. After the SEC created the depository system, the Delaware courts adhered to this rule. They did not distinguish the voluntary relationship between a client and its custodial bank or broker (the "broker level" of ownership) from the federally mandated relationship between the custodial bank or broker and DTC (the "depository level" of ownership). Delaware cases simply treated Cede as the holder of record and applied the Continuous Holder Requirement strictly. Under these decisions, the motion must be granted.

A different approach is possible and, in my view, preferable. Federal law looks through Cede and recognizes the custodial banks and brokers as record holders, just as before the federal mandate. If Delaware law took a similar approach, the Funds would retain their appraisal rights, because ownership by the relevant DTC participants never changed. Were I writing on a blank slate, I would account for the federal policy of share immobilization by interpreting the term "stockholder of record" as used in Section 262(a) to parallel its content under the federal securities laws. In other words, the term “stockholder of record” would include a DTC participant. But that is not how our cases have interpreted the statutory term, and this court is bound by those precedents. Dell's motion for summary judgment is therefore granted.

I. FACTUAL BACKGROUND

The facts are drawn from the parties' submissions in connection with Dell's motion for summary judgment. There are no disputes of material fact about the Funds' exercise of their appraisal rights or the re-titling of their shares.

A. The Funds' Ownership Of Dell Shares

On February 5, 2013, Dell agreed to a merger in which each publicly held share of Dell common stock would be converted into the right to receive $13.75 in cash, subject to the right of stockholders to seek appraisal. The Funds held at least 922,975 shares of Dell common stock. Like most investors, the Funds did not hold legal title to their shares. The Funds owned the shares indirectly through accounts at custodial banks. Two of the Funds used J.P. Morgan Chase (“JP Morgan”) as their custodian. The others used The Bank of New York Mellon (“BONY”).

***4** The custodial banks did not own record title either. JP Morgan and BONY are two of more than 800 custodial banks and brokers who are participating members of DTC.

> The vast majority of publicly traded shares in the United States are registered on the companies' books not in the name of beneficial owners—i.e., those investors who paid for, and have the right to vote and dispose of, the shares—but rather in the name of “Cede & Co.,” the name used by The Depository Trust Company (“DTC”).
>
> Shares registered in this manner are commonly referred to as being held in “street name.” ... DTC holds the shares on behalf of banks and brokers, which in turn hold on behalf of their clients (who are the underlying beneficial owners or other intermediaries).

John C. Wilcox, John J. Purcell III, & Hye–Won Choi, *“Street Name” Registration & The Proxy Solicitation Process, in A Practical Guide to SEC Proxy and Compensation Rules* 10–3, 10–3 (Amy Goodman et al. eds., 4th ed. 2007 & 2008 Supp.) [hereinafter *Street Name*] (footnote omitted).

The history of how we arrived at this ownership structure is important and informative.[4]

> Prior to 1970, negotiation was the most common method used to transfer stock in the United States. The owner would endorse the physical certificate to the name of the assignee on the back of the certificate. This endorsement instruct[ed] the corporation, upon notification, [about] the change in ownership of the shares on its corporate books. If the parties used the services of a broker, the seller would transfer the certificate to his brokerage firm. The brokerage firm representing the customer buying the security would receive the physical certificate and transfer it to the buyer as the new record owner of the security. Occasionally, the new owner might request that the physical certificate remain at the street address of the brokerage firm to facilitate the transfer of the certificate in a subsequent sale.

Wolfe, *supra,* at 180 (footnotes omitted).

> Transfer of securities in the traditional certificate-based system was a complicated, labor-intensive process. Each time securities were traded, the physical certificates had to be delivered from the seller to the buyer, and in the case of registered securities the certificates had to be surrendered to the issuer or its transfer agent for registration of transfer.

Prefatory Note at 2.

***5** By the late 1960s, increased trading rendered the certificate system obsolete. The paperwork burden reached “crisis proportions.” *Id.*

> Stock certificates and related documents were piled "halfway to the ceiling" in some offices; clerical personnel were working overtime, six and seven days a week, with some firms using a second or even a third shift to process each day's transaction. Hours of trading on the exchange and over the counter were curtailed to give back offices additional time after the closing bell. Deliveries to customers and similar activities dropped seriously behind, and the number of errors in brokers' records, as well as the time to trace and correct these errors, exacerbated the crisis.

Wolfe, *supra,* at 181 n.49 (quoting *SEC Study* at 219 n.1). "The difficulty that brokers and dealers experienced in keeping their records due to the volume of transactions and their thin capitalization caused many brokerage firms to declare bankruptcy and many investors to realize losses." *Id.* at 182.

Congress responded by passing the Securities Investor Protection Act of 1970, which directed the SEC to study the practices leading to the growing crisis in securities transfer. 15 U.S.C. § 78kkk(g). The SEC recommended discontinuing the physical movement of certificates and adopting a depository system. Wolfe, *supra,* at 182 n.58 (citing *SEC Study* at 13). Congress then passed the Securities Acts Amendments of 1975, which directed the SEC to "use its authority under this chapter to end the physical movement of securities certificates in connection with the settlement among brokers and dealers of transactions in securities consummated by means of the mails or any means or instrumentalities of interstate commerce."15 U.S.C. § 78q–1(e). In a resulting report, the SEC found that "registering securities in other than the name of the beneficial owner" was essential to establishing "a national system for the prompt and accurate clearance and settlement of securities transactions." Kahan & Rock, *supra,* at 1237 n.49.

Thus was born the federal policy of immobilizing share certificates through a depository system. "Congress called for a more efficient process for comparison, clearing, and settlement in a national market system, and for the end of the physical movement of securities certificates in connection with the settlement of transactions among brokers and dealers." Egon Guttman, *Transfer of Securities: State and Federal Interaction,* 12 Cardozo L.Rev. 437, 447 (1990); *accord*S. REP. NO. 94–75 at 5 (1975) ("A national clearance and settlement system is clearly needed."). To comply, "[b]rokerages and banks created [depositories] to allow them to deposit certificates centrally (so-called 'jumbo certificates,' often representing tens or hundreds of thousands of shares) and leave them at rest." Larry T. Garvin, *The Changed (And Changing?) Uniform Commercial Code,* 26 Fla. St. U.L.Rev. 285, 315 (1999).

In 1973, just after the paperwork crisis and with the federal writing on the wall, the members of the New York Stock Exchange created DTC to serve as a depository and clearing agency. Originally there were three regional depositories in addition to DTC: the Midwest Securities Depository Trust Company, which held through its nominee, Kray & Co.; the Pacific Securities Depository Trust Company, which held through its nominee, Pacific & Co; and the Philadelphia Depository Trust Company, which held through its nominee, Philadep & Co. "[I]n the 1990's DTC ... assumed the activities of the [other] depositories." Carnell & Hanks, *supra,* at 26. Today DTC is the world's largest securities depository and the only domestic depository. Kahan & Rock, *supra,* at 1238 n.50. "DTC is owned by its 'participants,' which are the member organizations of the various national stock exchanges (*e.g.,* State Street Bank, Merrill Lynch, Goldman Sachs & Co.)." *Street Name* at 10–6 to 10–7.

***6** DTC has been estimated to hold "about three-quarters of [the] shares in publicly traded companies." Garvin, *supra,* at 315; *accord* Kahan & Rock, *supra,* at 1236; *Street Name* at 10–4 n.2. "The shares of each company held by DTC are typically represented by only one or more 'immobilized' jumbo stock certificates held in DTC's vaults." *Street Name* at 10–7. "The immobilized jumbo certificates are the direct result of Section 17A(e) of the Exchange Act, in which Congress instructed the SEC to 'use its authority ... to end the physical movement of securities certificates....' " *Id.* at 10–7 n.10.

The depository system is what enables public trading of securities to take place. In 2014, the NYSE reported average *daily* volume of approximately 1 *billion* shares and approximately 4 *million* separate trades. *See* NYSE Factbook, http://www.nysedata.com/factbook (last visited

June 19, 2015). The failure of the certificate-based system to keep up with much lower trading volumes in the 1960s demonstrates that it cannot meet current demand. *Prefatory Note* at 2. Without immobilization and DTC, "implementing a system to settle securities within five business days (T+5), much less today's norm of T+3 or the current goals of T+1 or T+0, would simply be impossible." Kahan & Rock, *supra,* at 1238. Trading at current levels is only possible because of share immobilization and DTC. *Street Name* at 10–7; *accord* Garvin, *supra,* at 315–16; *Prefatory Note* at 2–3.

Because of the federal policy of share immobilization, it is now Cede—not the ultimate beneficial owner and not the DTC-participant banks and brokers—that appears on the stock ledger of a Delaware corporation. Cede is typically the largest holder on the stock ledger of most publicly traded Delaware corporations. *Street Name* at 10–6. To preserve the pre-immobilization status quo—at least at the federal level—the SEC provided that for purposes of federal law, the custodial banks and brokers remain the record holders. Depositories are defined as "clearing agencies." 15 U.S.C. § 78c(23)(A). The term "record holder" is defined as "any broker, dealer, voting trustee, bank, association or other entity that exercises fiduciary powers which holds securities of record in nominee name or otherwise or as a participant in a clearing agency registered pursuant to section 17A of the Act." 17 C.F.R. § 240.14c–1(i). The term "entity that exercises fiduciary powers" is similarly defined as "any entity that holds securities in nominee name or otherwise on behalf of a beneficial owner but does not include a clearing agency registered pursuant to section 17A of the Act or a broker or a dealer." *Id.* § 240.14c–1(c). Federal law thus looks through DTC when determining a corporation's record holders. For example, when determining whether an issuer has 500 or more record holders of a class of its equity securities such that it must register under 15 U.S.C. § 78***l***(g), DTC does not count as a single holder of record. Each DTC participant member counts as a holder of record. Michael K. Molitor, *Will More Sunlight Fade The Pink Sheets?,* 39 Ind. L.Rev. 309, 315–16 (2006) (citing SEC interpretive releases).

The federal regulations also ensure that a corporation can easily find out the identities of the banks and brokers who hold shares through DTC. Federal regulations require that DTC "furnish a securities position listing promptly to each issuer whose securities are held in the name of the clearing agency or its nominee." 17 C.F.R. § 240.17Ad–8(b). The participant listing is known colloquially as the "Cede breakdown," and it identifies for a particular date the custodial banks and brokers that hold shares in fungible bulk as of that date along with the number of shares held. A Delaware corporation can obtain a Cede breakdown with ease. In 1981, this court noted that a Cede breakdown could be obtained in a matter of minutes. *Hatleigh Corp. v. Lane Bryant, Inc.,* 428 A.2d 350, 354 (Del. Ch.1981). A Cede breakdown can now be obtained through DTC's website or by calling the DTC "Proxy Services Hotline." Issuers use the Cede breakdown to understand their stockholder profile, and proxy solicitors use it when advising clients. Commentary regards the information as reliable. *Handbook for the Conduct of Shareholders' Meetings* 40 (ABA Business Law Section, Corporate Governance Committee ed., 2000) (identifying the "lists of holders obtained from depositories" as one of the documents that can be relied on in "determining the shares entitled to vote and tabulating the vote").

***7** A publicly traded corporation cannot avoid going through DTC. Federal law requires that when submitting a matter for a stockholder vote, an issuer must send a broker search card at least twenty business days prior to the record date to any "broker, dealer, voting trustee, bank, association, or other entity that exercises fiduciary powers in nominee name" that the company "knows" is holding shares for beneficial owners. 17 C.F.R. § 240.14a–13(a). Rule 14a–13 provides that "[i]f the registrant's list of security holders indicates that some of its securities are registered in the name of a clearing agency registered pursuant to Section 17A of the Act (e.g., 'Cede & Co.,' nominee for Depository Trust Company), the registrant *shall make* appropriate inquiry of the clearing agency and thereafter of the participants in such clearing agency." *Id.* § 240.14a–13(a) n.1 (emphasis added). An issuer cannot look only at its own records and treat Cede as a single, monolithic owner.

B. The Funds Seek Appraisal, And DTC Certificates The Shares.

Dell was a publicly traded company and the merger involved a stockholder vote, so Dell had to go through the federally mandated process to identify the custodial banks and brokers that held its shares through DTC, then send information through them to the beneficial holders. The list of DTC-participants included JP Morgan and BONY. Through JP Morgan and BONY, information reached the Funds.

The Funds exercised appraisal rights for the 922,975 shares that are the subject of this motion. Because they owned their shares in street name through their custodial banks, the Funds caused Cede to demand appraisal on their behalf. On July 12, 2013, before the vote on the merger, Cede made appraisal demands for the Funds.

DTC held all of the Dell shares registered in street name in fungible bulk, which enabled DTC to track their ownership through electronic bookkeeping entries in the FAST Account. When the Funds caused Cede to make appraisal demands for their shares, DTC moved a corresponding number of shares out of the FAST Account by directing Dell's transfer agent to issue uniquely numbered certificates. By issuing paper certificates, DTC sought to avoid inadvertently surrendering the shares for the merger consideration along with other shares in the FAST Account. This procedure protected Dell, which effectively had "the responsibility of overseeing the surrender of shares after a merger." *Ala. By–Prods.,* 857 A.2d at 263.

Dell's transfer agent is the American Stock Transfer & Trust Company, LLC (the "Transfer Agent"). On July 24, 2013, at DTC's request, the Transfer Agent issued paper stock certificates in Cede's name for the shares owned beneficially by the Funds

C. DTC Delivers The Certificates To The Custodians, Who Re–Title Them.

As a matter of course, DTC does not act as a custodian of paper stock certificates for its participants, even if those certificates are issued in Cede's name. A participant can pay to have a vault at DTC for its certificates, but that is a separate service. Unless a participant has arranged for a vault, DTC will contact the participant and deliver the paper certificate to the participant for safekeeping.

JP Morgan and BONY do not have vaults at DTC. Therefore, after the Transfer Agent delivered the paper certificates for the Funds' shares, DTC made arrangements to deliver them to JP Morgan and BONY.

When a DTC participant receives a paper certificate from DTC, procedures differ. Some leave the certificates in Cede's name and place them in their vaults. Others require that the certificates be re-registered in the names of their own nominees. JP Morgan's and BONY's internal policies do not permit them to hold paper certificates unless the shares are titled in the names of their own nominees. The custodial banks therefore instructed Cede to authorize the shares to be re-titled in the names of their nominees.

On August 5, 2014, Cede endorsed the Funds' certificates to the custodial banks. Over the next three weeks, the custodial banks arranged for the Transfer Agent to reissue the shares in the names of their nominees. The Transfer Agent reissued the shares held for Milliken and Manulife in the name of Hare & Co. and the shares held for Curtiss–Wright in the name of Mac & Co., which are BONY's nominees. The Transfer Agent reissued the shares held for T. Rowe Price in the name of Kane & Co. and the shares held for Northwestern in the name of Cudd & Co., which are JP Morgan's nominees.

***8** There was an additional hiccough at BONY. Shortly after the Transfer Agent reissued the shares, BONY conducted a routine weekly sweep of its vault. BONY found the stock certificates for the shares beneficially owned by Manulife and Milliken and redeposited them with DTC in the FAST Account.

On September 12, 2013, a majority of Dell's shares voted in favor of the merger. A few weeks later, on October 4, BONY realized that the shares beneficially owned by Manulife and Milliken had been re-deposited in the FAST Account. BONY withdrew them from DTC and had new certificates issued in the name of Hare & Co.

Other than taking steps to cause DTC to demand appraisal for their shares through Cede, the Funds had no involvement in any of the transfers. The Funds did not explicitly approve any or the transfers or cause any of them to take place. The Funds concede that under their agreements with their custodial banks, they gave their custodians authority to make these types of back-office transfers.

D. The Merger Closes, And The Funds Seek Appraisal.

The merger closed on October 29, 2013. The Funds filed timely petitions seeking appraisal. They disclosed the issues relating to the re-titling of their shares. Dell moved for summary judgment.

II. LEGAL ANALYSIS

Under Court of Chancery Rule 56, summary judgment "shall be rendered forthwith if ... there is no genuine issue as to any material fact and ... the moving party is entitled to a judgment as a matter of law." Ct. Ch. R. 56(c). The facts underlying the motion are undisputed, and its outcome turns purely on the following question of law: Does the Continuous Holder

Requirement bar a beneficial owner from pursuing appraisal if there has been an administrative transfer at the depository level? Under current law, the answer is yes.

Read together, the Continuous Holder Requirement and the Record Holder Requirement mandate that an appraisal petitioner "continuously hold" the shares for which appraisal is sought as a "holder of record" through the effective date of the merger. 8 *Del. C.* § 262(a). There is no dispute that the Funds continuously held their shares as beneficial owners through the effective date of the merger. There is also no dispute that the Funds' custodial banks continuously held the shares on behalf of the Funds through the effective date of the merger. The outcome of the motion turns on the implications of a single event for "holder of record" status: a change in the name on the shares from DTC's nominee to the custodial banks' nominees.

The appraisal statute does not define what it means to be a "holder of record." No other provision of the DGCL defines what it means to be a "holder of record." The current interpretation is circular: "The appraisal statute confers the right to an appraisal only upon the stockholder of record in the corporation. Consequently, only the person appearing on the corporate records as the owner of stock in the corporation may qualify for an appraisal...." *Engel v. Magnavox Co.,* 1976 WL 1705, at *1 (Del. Ch. Apr. 22, 1976). But that statement begs the question: What are the records of the corporation for purposes of determining legal ownership?

In a simplified model of a Delaware corporation, the corporate secretary maintains a document called the stock ledger. From the corporation's standpoint, the stock ledger identifies all of the legally relevant transactions in the corporation's shares, including the date when any person acquires shares and the number of shares acquired, and the date when any person transfers shares and the number of shares sold. If a holder transfers shares without notifying the corporation, the corporation is not required to discover that fact, nor need the corporation voluntarily treat the new holder as the legal owner. The corporation can rely on its records until a stockholder takes proper steps to transfer title to the shares. Under this system, a paper stock certificate is not actually a share of stock. It is only evidence of ownership of a share of stock. [5]

***9** If the corporation needs to determine who its current stockholders are as of a particular date, the corporate secretary uses the stock ledger to prepare a stock list. The stock list identifies those stockholders who own stock as of a given date, together with the number and type of shares owned, based on the records. *See*8 *Del. C.* § 219(a) & (c). Evidencing the connection between this process and the concept of a record holder, the date used for preparing the stock list is called the "record date." [6]

For most contemporary public corporations, the simplified model no longer holds. Virtually all public corporations have outsourced the maintaining of the stock ledger to a transfer agent, as Dell did. The stock ledger and the stock list as of a particular record date are corporate records, but they exist and are maintained outside the corporation.

A. Existing Delaware Law Applied To This Case

If the only relevant records are those maintained by Dell or the Transfer Agent, then summary judgment must be granted in favor of Dell. Under existing precedent, Cede was the stockholder of record for purposes of the Funds' shares and therefore made the appraisal demand. "The record holder must ... continuously hold such shares [seeking appraisal] through the effective date of the merger...." *In re Appraisal of Transkaryotic Therapies, Inc.,* 2007 WL 1378345, at *3 (Del. Ch. May 2, 2007). It is the "record holder—not the beneficial owner—[that] is subject to the statutory requirements for showing entitlement to appraisal and demonstrating perfection of appraisal rights under Sections 262(a) and (d)." *In re* Ancestry.com*, Inc.,* 2015 WL 66825, at *8 (Del. Ch. Jan. 5, 2015). The re-titling of a certificated share after the demand but before the effective date violates the Continuous Holder Requirement by causing record ownership to change. *See* *Nelson v. Frank E. Best Inc.,* 768 A.2d 473, 477 (Del. Ch.2000) (Strine, V.C.) (noting that after Cede transferred record ownership of shares seeking appraisal to appraisal petitioner "Cede's demand was invalid, because Cede would not 'continuously' be the holder of record between the ... date of Cede's demand and the effective date of the Merger, as is required by 8 *Del. C.* § 262(a).").

There is no dispute that on Dell's records as maintained by the Transfer Agent, legal ownership of Funds' shares changed from Cede to the four current nominees: Mac & Co., Kane & Co., Hare & Co., and Cudd & Co. When the shares were re-titled, the Funds lost their appraisal rights.

In an effort avoid this result, the Funds cite *Alabama By–Products* and contend that "because the right to appraisal vests at the time of perfection, the redemption of the beneficial owners' shares by the custodian and record holder without the knowledge of the beneficial owners [does] not extinguish the beneficial owners' right to appraisal of the fair value of their shares." Petitioners' Br. at 13. The issue in *Alabama By–Products* was whether the surrender by DTC of the appraisal petitioners' shares and the subsequent distribution of the merger consideration deprived the appraisal petitioners of properly perfected appraisal rights. At the time of the surrender, more than sixty days had elapsed since the closing of the merger, and an appraisal petition had been filed within the statutory time period. Under the appraisal statute, a stockholder cannot unilaterally withdraw an appraisal demand more than sixty days after the merger closes, and any withdrawal after the filing of a petition requires court approval. 8 *Del. C.* § 262(h). The Delaware Supreme Court held that DTC's surrender of the shares more than sixty days after the merger closed, post petition, and without court approval did not compromise the petitioners' appraisal rights because the surrender did not satisfy the statutory requirements.

***10** To bring themselves within the scope of *Alabama By–Products,* the Funds describe their appraisal rights as "perfected," but the only step in the statutory process that had been completed at the time of the re-titling was the making of a demand. The merger had not yet closed, the time for unilateral withdrawals had not yet elapsed, and no appraisal petition had been filed. When the Funds' shares were re-titled, their appraisal rights remained fragile and easily lost through voluntary action by the holder. The custodial banks instructed DTC and the Transfer Agent to re-title the shares, and under current law, ownership changes driven by DTC's role in the depository system are regarded as voluntary transfers. At the stage when the re-titling occurred, the statutory provisions found controlling in *Alabama By–Products* did not yet apply.

The Funds also contend that the Continuous Holder Requirement should be "liberally construed for the protection of objecting stockholders, within the boundaries of orderly corporate procedures and the purpose of the requirement," which is a passage quoted from *Raab v. Villager Industries, Inc.,* 355 A.2d 888, 891 (Del.1976). But as the language of this passage shows, *Raab* addressed the procedure for making objections under the version of the appraisal statute that existed before 1976. In that statutory scheme, a stockholder who wanted to exercise appraisal rights had to send a written objection to the corporation before the merger vote, then submit a written demand for appraisal after the merger vote. *See* 2 Balotti & Finkelstein, *supra,* § 262 at IX–159. The purpose of the first step—the written objection—was "merely to give notice." *Zeeb v. Atlas Powder Co.,* 87 A.2d 123, 127 (Del.1952). The Delaware Supreme Court construed the objection requirement more liberally than the demand requirement because "[t]he purpose of the objection [was] of lesser importance than the demand for payment." *Raab,* 355 A.2d at 891.

Stockholders seeking appraisal no longer have to make a separate objection, so *Raab* 's language regarding the "liberal construction" of this requirement is no longer relevant. Delaware decisions have *not* generally construed other aspects of the appraisal statute liberally in favor of stockholders.*See generally* Jesse A. Finkelstein & John D. Hendershot, *Appraisal Rights in Mergers & Consolidations* at A–97 (5th ed. 2010) (collecting cases). The Delaware Supreme Court has endorsed a principle of strict construction, explaining that "[b]y exacting strict compliance ..., the appraisal statute ensures the expedient and certain appraisal of stock." *Ala. By–Prods.,* 657 A.2d at 263. In subsequently re-affirming its adherence to the principle, the Delaware Supreme Court cautioned that strict construction should be applied "even-handedly, not as a one-way street." *Berger v. Pubco Corp.,* 976 A.2d 132, 144 (Del.2009). In other words, both petitioners and the corporation must adhere strictly to the appraisal statute's requirements; neither gets the benefit of the doubt under more a lenient rule of "liberal construction." Given these pronouncements and existing precedent, the Funds cannot rely on a principle of liberal construction to preserve their appraisal rights.

Finally, the Funds have pointed to the fact that they did not know about or approve the nominee-level transfers. It is undisputed that their agreements with their custodial banks permitted the banks to re-title the shares. Our law currently treats ownership changes driven by the depository system as voluntary transfers, making this a risk that the Funds accepted. By choosing to hold through intermediaries, the Funds assumed the risk that the intermediaries might "act contrary to [their] interests." *Ala. By–Prods.,* 657 A.2d at 262.

B. The Possibility Of A Different Approach

***11** There is another possible interpretation of the Record Holder Requirement. When Congress and the SEC created the depository system, they added DTC at the bottom of the ownership chain and introduced Cede as the new omnibus record holder, but the identities of the custodial banks and brokers did not go away. They continue to appear on the DTC participant list. As discussed in the Factual Background, the DTC participant list is an integral part of the federally mandated ownership scheme. A publicly traded corporation cannot avoid going through DTC. *See*17 C.F.R. § 240.14a–13(a). Rule 14a–13 requires that the issuer "make appropriate inquiry" of DTC to identify the custodial banks and brokers who own shares through Cede. *Id.*§ 240.14a–13(a) n.1. An issuer cannot rely on the stock ledger maintained by its transfer agent, pretend that Cede is a single record holder, and ignore the Cede breakdown. For purposes of federal law, Cede is *not* a record holder. 15 U.S.C. § 78c(23)(A). The record holders are the banks and brokers on the DTC participant list. 17 C.F.R. § 240.14c–1(i).

Were I writing on a blank slate, I would hold that the "records" of the corporation for purposes of determining who is a "stockholder of record" include the DTC participant list. Under this interpretation, the custodial banks and brokers who appear on the DTC participant list would be stockholders of record for purposes of Delaware law, just as they are for federal law and just as they were before share immobilization. If that rule applied, then the motion for summary judgment would be denied, because there was no change of ownership at the DTC participant level.

In my view, this interpretation better reflects current reality. Viewed pragmatically, the federal policy of share immobilization compelled publicly traded Delaware corporations to outsource one part of the stock ledger—the DTC participant list—to DTC, just as Delaware corporations have chosen to outsource other parts of the stock ledger to transfer agents. Before share immobilization, banks and brokers appeared on the stock ledger as registered holders. After share immobilization, the same banks and brokers appear on the stock ledger indirectly through DTC and the Cede breakdown. Just as Delaware law treats the outsourced stock ledger as a record of the corporation, albeit one maintained by a third party, Delaware law likewise should treat the outsourced DTC participant list as a record of the corporation, albeit one maintained by DTC.

Adopting this approach would recognize that the changes in ownership driven by the role of DTC in the depository system result from the federal policy of share immobilization. This case provides a fitting example. But for the federal mandate, JP Morgan and BONY would have appeared through their nominees on the stock ledger maintained by the Transfer Agent. There would have been no need to re-title the shares. The Funds lost their appraisal rights because of a system imposed by federal law.

But in light of existing precedent, I do not believe that this court is free to interpret the "holder of record" language in this manner. I previously advocated treating DTC participants as holders of record for purposes of analyzing whether the shares they held could be voted without a DTC omnibus proxy. *See Kurz v. Holbrook,* 989 A.2d 140 (Del. Ch.), *aff'd in part, rev'd on other grounds sub nom.Crown EMAK P'rs, LLC v. Kurz,* 992 A.2d 377 (Del.2010). The *Kurz* decision posited that recognizing DTC participants as record owners would have beneficial effects for other areas of Delaware law, including appraisal. *See Kurz,* 989 A.2d at 174 ("In some circumstances, Delaware corporations should benefit from looking through DTC to the holdings of the participant banks and brokers. Reducing the number of shares available for appraisal arbitrage is one area that springs to mind.").

On appeal, the Delaware Supreme Court reversed the *Kurz* decision on other grounds, rendering it unnecessary for the high court to consider whether DTC participants should be treated as record holders. The Delaware Supreme Court nevertheless characterized the discussion of the DTC participant list as "*obiter dictum* " that was "without precedential effect."[7] The high court stated that

> ***12** a legislative cure is preferable. The DGCL is a comprehensive and carefully crafted statutory scheme that is periodically reviewed by the General Assembly. Indeed, the General Assembly made coordinated amendments to section 219 and section 220 in 2003. Any adjustment to the intricate scheme of which section 219 is but a part should be accomplished by the General Assembly through a coordinated amendment process.

EMAK P'rs, 992 A.2d at 398.

I respectfully disagree with expressed preference for a legislative cure. In my view, the question of what constitutes the records of the corporation for purposes of determining who is a "holder of record" is a quintessential issue of statutory interpretation appropriate for the judiciary to address. As the Delaware Supreme Court has explained, "[i]n our constitutional system, this court's role is to interpret the statutory language that the General Assembly actually adopts, even if unclear and explain what we ascertain to be the legislative intent without rewriting the statute to fit a particular policy position.” *Taylor v. Diamond State Port Corp.,* 14 A.3d 536, 542 (Del.2011). “[T]he Constitution invests the Judiciary, not the Legislature, with the final power to construe the law.” *Nationwide Mut. Ins. Co. v. Darden,* 503 U.S. 318, 325 (1992). The interpretation of statutory text is “one of the Judiciary's characteristic roles.” *Japan Whaling Ass'n v. Am. Cetacean Soc.,* 478 U.S. 221, 230 (1986).

***13** The Delaware courts play a particularly significant role in the corporate arena.[8] Historically the judiciary, rather than the General Assembly, has taken the lead when addressing corporate law issues.[9] Two leading commentators have noted that the Delaware Supreme Court has not traditionally deferred to the prospect of legislative action. Rather, “the Delaware Supreme Court has shown a certain degree of discomfort with, perhaps even hostility to, legislative intrusions into its domain.”[10]

The significant role played by the Delaware courts stems from the fact that, *contra EMAK,* the DGCL has not been viewed traditionally as a comprehensive code, but rather as a broadly enabling statute that leaves ample room for private ordering and interpretation.[11] In an article written while serving as a Vice Chancellor, Chief Justice Strine distinguished between the “Delaware Model,” in which the statute is “largely enabling and provides a wide realm for private ordering,” and the “Mandatory Statutory Model,” under which the corporate code would be “quite detailed and prescriptive.” Leo E. Strine, Jr., *Delaware's Corporate–Law System: Is Corporate America Buying an Exquisite Jewel or A Diamond in the Rough?A Response to Kahan & Kamar's* Price Discrimination in the Market for Corporate Law, 86 Cornell L.Rev. 1257, 1260 (2001). Because the latter type of statute “would dictate how things should happen, there would be less room for judicial interpretation, but also less space for director choice.” *Id.* Chief Justice Veasey has drawn a similar distinction in his own scholarly writings:

> ***14** A flexible or indeterminate regime, such as we have had in Delaware, is distinct from a rigid codification system that prevails in many systems outside the United States. That is part of the genius of our law. Life in the boardroom is not black and white; directors and officers make decisions in shades of gray all the time. A “clear” law, in the sense of one that is codified, is simply not realistic.... There can be no viable corporate governance regime that is founded on a “one size fits all” notion.

E. Norman Veasey & Christine T. Di Guglielmo, *What Happened in Delaware Corporate Law and Governance from 1992–2004?A Retrospective on Some Key Developments,* 153 U. Pa. L.Rev. 1399, 1412–13 (2005) (footnotes omitted). The “skeletal framework” set forth in the flexible DGCL necessarily requires judicial interpretation. *Id.* at 1411.

A review of applicable precedent teaches that for purposes of the issue discussed in this case, there is ample room for a continuing judicial role. A statutory amendment is one method of modernizing the law, but it is not the only way.

1. The Creation Of The Record Holder Requirement

The statutory appraisal remedy dates back to the adoption of the DGCL in 1899. The original statute contained a section that stated:

> If any stockholder in either corporation consolidating aforesaid, who objected thereto in writing, shall within twenty days after the agreement of consolidation has been filed and recorded, as aforesaid, demand in writing from the consolidated corporation payment of his stock, such consolidated corporation shall, within three months thereafter, pay to him the value of the stock at the date of consolidation.

21 Del. Laws c. 273 § 56 (1899). The provision referred only to the right of “any stockholder” to seek payment of the value of his stock, without specifying whether the stockholder had to be a holder of record.

***15** Nearly five decades later, despite a series of intervening amendments, the Delaware appraisal statute continued to refer to "any stockholder" having the right to seek appraisal. The question of whether a beneficial owner could seek appraisal was finally raised in a proceeding arising out of the merger between Salt Dome Oil Corporation and Gulfboard Oil Corporation. *See* *Schenck v. Salt Dome Oil Corp.,* 34 A.2d 249 (Del. Ch.1943), *rev'd,*41 A.2d 583 (Del.1945).

William Schenck and his fellow petitioners owned a total of 7,100 shares of Salt Dome common stock, which were registered on its books in the name of Guido Pantaleoni, Jr. They also owned a total of 10,000 shares of Gulfboard common stock, which were registered on its books in the name of Berberich & Co. The petitioners made timely objections to the merger and submitted timely demands for appraisal. They did so in their own names, although their objections and demands identified the record holders and the number of shares for which appraisal was sought. The respondent corporations argued that the petitioners could not seek appraisal unless their names appeared on the stock ledger, regardless of whatever other information they might provide or documentation they might introduce to substantiate their ownership.

Chancellor Harrington rejected this argument, reasoning that on the facts presented, a court of equity could recognize the petitioners as the real owners of the shares. *Schenck,* 34 A.2d at 252. He declined to construe the term stockholder "in a strictly legal sense" as limited to holders of record. *Id.* Instead, he reasoned that "Section 61 of the General Corporation Law [the appraisal statute] is clearly for the protection of objecting shareholders [and] should be liberally construed to that end." *Id.* Although the Chancellor acknowledged that a corporation can only look to its stock list to determine who its stockholders are, he concluded that "the real owner of the shares, nevertheless, has substantial rights that may be materially affected by a corporate consolidation." *Id.*

The companies appealed, and the Delaware Supreme Court took the opposite view. In reaching its conclusion, the high court discussed (i) the nature of the appraisal remedy, which it regarded as an action at law rather than a proceeding in equity, (ii) existing authorities which said that a corporation could rely exclusively on the information in its records to determine stockholder status, and (iii) a balancing of competing public policies, in which the importance of certainty and predictability prevailed, particularly given the absence of any benefit to the corporation from the then-prevailing system of beneficial ownership.

First, the Delaware Supreme Court viewed the appraisal proceeding as a legal rather than equitable proceeding. Because appraisal was a statutory remedy, the high court reasoned that "[t]he right of an unregistered transferee of stock to object to a proposed agreement of merger must be looked for in the statute." *Salt Dome,* 41 A.2d at 587. The court found "nothing in the language of the statute that makes clear the legislative intent to bestow the remedy provided upon an equitable owner of stock, but much, indeed, to the contrary." *Id.* at 588. Rather than an equitable action for breach of fiduciary duty, the appraisal proceeding resembled a debt collection action. A stockholder could collect an appraisal award "as other debts are by law collectible, that is, by suit at law, judgment at law, and by the usual legal process."*Id.*

***16** Second, the Delaware Supreme Court summarized existing authorities addressing the rights that a beneficial owner had at law:

> The term, 'stockholder', ordinarily, is taken to apply to the holder of the legal title to shares of stock. In most jurisdictions registration, or its equivalent, is essential to pass the legal title as against the corporation; and the unregistered transferee is not entitled to the rights and privileges of a stockholder in his relations with the corporation. Whatever may be the equitable rights that may arise by a delivery of the stock certificate accompanied with a power of attorney for its transfer, the legal title and legal rights and liabilities of the stockholder of record remain unchanged until the transfer is actually accomplished. The record owner may be but the nominal owner, and, technically, a trustee for the holder of the certificate, but legally he is still a stockholder, and may be treated as the owner by the corporation.

Id. at 585 (citations omitted). After reviewing Delaware authorities addressing other stockholder rights, most notably the right to vote, the court concluded that only a registered stockholder was entitled to exercise legal rights and be treated as a stockholder by the corporation. *Seeid.* at 585–89.

Third, the *Salt Dome* court turned to considerations of public policy:

> With respect to matters intracorporate affecting the internal economy of the corporation, or involving a change in the relationship which the members bear to the corporation, there must be order and certainty, and a sure source of information, so that the corporation may know who its members are and with whom it must treat, and that the members may know, in a proper case, who their associates are. Especially is this true in a merger proceeding which is essentially an intracorporate affair. The merging corporations are entitled to know who the objecting stockholders are so that the amount of money to be paid to them may be provided. The stockholders in general are entitled to know the dissentients and the extent of the dissent. The corporation ought not to be involved in possible misunderstandings or clashes of opinion between the non-registered and registered holder of shares. It may rightfully look to the corporate books as the sole evidence of membership.

Id. at 589 (citation omitted). The Supreme Court reasoned that the relationship between the customer and the broker was a voluntary one, making it appropriate to place any attendant risk on the stockholder: "If, for any reason, [a stockholder] chooses to allow his shares to be registered on the corporate books in the name of another, it is not a denial of his right of actual ownership to require him to establish his rights and pursue his remedy through the nominee of his own selection." *Salt Dome,* 41 A.2d at 589. The high court therefore held that "only the registered holder of stock is a 'stockholder' within the sense of the word as used in" the appraisal statute. *Id.*

Importantly for present purposes, *Salt Dome* only addressed the broker level of the beneficial ownership chain. The decision obviously pre-dated the federal policy of share immobilization—still three decades in the future—so the Delaware Supreme Court could not have considered whether any distinctions were warranted at the depository level of ownership, the competing policy considerations raised by the federal response to Wall Street's paperwork crisis, or the benefits that the system provided to issuers. At the time, the decision to hold in street name properly could be regarded as a matter of choice, rather than involving at least one level of beneficial ownership (the depository level) that resulted from federal law. The Delaware Supreme Court also could regard exclusive reliance on the stock ledger as promoting "order and certainty" and providing a "sure source of information." After the federal policy of share immobilization, a legal rule that looks no further than Cede has the opposite effect. It masks the implications of beneficial ownership and promotes uncertainty.

***17** Perhaps most important, the *Salt Dome* decision did not pre-judge what documents might encompass the appropriate records for determining registered status and whether, after the adoption of the depository system, those records should include the DTC participant list. What the *Salt Dome* decision does show, however, is that interpreting the appraisal statute to determine which stockholders are entitled to appraisal is an appropriate subject for the courts.

2. Post-*Salt Dome,* Pre–Codification Cases

After *Salt Dome,* the Delaware Supreme Court adhered to the Record Holder Requirement in *Olivetti Underwood Corp. v. Jacques Coe & Co.,* 217 A.2d 683 (Del.1966) and *Carl M. Loeb, Rhoades & Co. v. Hilton Hotels Corp.,* 222 A.2d 789 (Del.1966). The Court of Chancery applied it in *Application of General Realty & Utilities Corp.,* 42 A.2d 24 (Del. Ch.1945). The *Olivetti* decision is noteworthy because it re-framed the corporation's prerogative to rely on its records as a restriction on the corporation's ability to look any further than its records.

The petitioners in *Olivetti* were brokers who were registered stockholders of Olivetti Underwood Corporation. The brokers made appraisal demands in which they notified Olivetti that they were record holders and did not beneficially own the stock registered in their names. Underwood moved to dismiss the petitions, arguing that the brokers failed to submit proof of their authority to act for the beneficial owners. Citing *Salt Dome,* the Court of Chancery reasoned that the corporation "ha[d] no right to raise any issue as to the right of a registered owner to seek a statutory appraisal and such a stockholder has no duty to supply proof as to that issue." *Abraham & Co. v. Olivetti Underwood Corp.,* 204 A.2d 740, 741 (Del. Ch.1964). Underwood appealed.

The Delaware Supreme Court affirmed. After quoting *Salt Dome* at length, the high court summarized "the rule of the *Salt Dome* case" as follows: "[T]here is no recognizable stockowner under the merger-appraisal provisions of our Corporation Law except a registered stockholder." *Olivetti,* 217 A.2d at 686. By restating the holding of the earlier decision in this fashion, the Delaware Supreme Court expanded the rule. Where the *Salt Dome* decision permitted a corporation to confine itself to dealing with registered stockholders in intra-corporate affairs, the *Olivetti* opinion required it. The court went further and stated that the corporation "should avoid becoming involved in the affairs of registered stockholders vis-á-vis beneficial owners," admonishing that "the relationship between, and the rights and obligations of, a registered stockholder and his beneficial owner are not relevant issues in a proceeding of this kind." *Id.* at 686, 687.

3. The Codification Of The Record Holder Requirement

During the 1967 revisions to the DGCL, the General Assembly codified the Record Holder Requirement. The new version of the appraisal statute included the following language:

> When used in this section, the word "stockholder" means a holder of record of stock in a stock corporation and as a member of record of a non-stock corporation; the words "stock" and "share" mean and include what is ordinarily meant by those words and also membership or membership interest of a member of a non-stock corporation.

56 Del. Laws c. 50 § 262(a) (1967). In his landmark treatise, Professor Folk explained the purpose of the new text.

> Section 262(a), as revised in 1967, defines "stockholder," for purposes of the appraisal remedy, as a holder of record. Although the prior statute was not couched in terms so confined, the prior cases consistently limited the remedy to record owners on the theory that a corporation should, in estimating the number of dissenters, be able to rely exclusively upon corporate records of stock ownership and should not become involved in disputes between registered and nonregistered stockholders. Moreover, the unregistered stockholder is not harmed, since it is within the power to obtain the advantages of record ownership by a transfer into his own name.

***18** Ernest L. Folk, III, *The Delaware General Corporation Law: A Commentary and Analysis* 373 (1972) (footnotes omitted). Professor Folk also warned that the concept of record ownership did not operate only as an impediment to appraisal petitioners: "The registered stockholder requirement cuts both ways. Not only is the corporation entitled to look solely to record ownership, but in fact it may ordinarily not inquire into the authority of a registered holder to act for beneficial owners." *Id.* at 374 (footnotes omitted).

All of the qualifications and limitations of the common law version of the Record Holder Requirement apply to the statutory version. The amendment pre-dated the federal policy of share immobilization, although that initiative soon would loom on the horizon. Because the depository system had not yet been established, the General Assembly had no ability to consider the depository level of ownership or the competing policy considerations that led to its creation. Notably, the language of the statutory provision only required that the stockholder be "a holder of record of stock in a stock corporation and as a member of record of a non-stock corporation...." It did not specify what documents might encompass the appropriate records for determining registered status and whether, after the adoption of the depository system, those records should include the DTC participant list.

4. Delaware's Limited Acknowledgement Of Share Immobilization

During the mid–1970s, the SEC implemented the federal policy of share immobilization. Delaware decisions largely ignored this development. Rather than distinguishing between the broker level and the depository level, they treated both as a matter of convenience that resulted exclusively from the private contractual relationship between a broker and its clients. That perception was inaccurate.

A representative decision is *Carico v. McCrory Corp.,* 4 Del. J. Corp. L. 595 (Del. Ch. July 13, 1978). The defendant corporation received a timely written objection from the beneficial holder of the corporation's stock. The objection failed to disclose the identity of the record holder, Cede. The corporation objected to the claim on the ground that a proper written objection was not received from or on behalf of the record holder of the stock in issue. This court agreed, noting that "[i]t is well established that an objection which does not enable the resulting corporation to identify the actual record holder is insufficient." *Id.* at 598. The court reasoned similarly in *Engel v. Magnavox Co.,* 1976 WL 1705, as did the Delaware Supreme Court in *Raab*. In fairness, these decisions involved merger objections made by beneficial owners at the top of the ownership chain, so it did not matter whether the record owner was Cede or a broker or custodial bank. In either case, the wrong party made the objection.

In contrast to these decisions, when considering actions brought under a different section of the DGCL, the Court of Chancery showed greater sensitivity to the depository revolution. When stockholders sought to obtain a stock list under Section 220, Delaware decisions held that the Cede breakdown was part of the list.[12] Ever since, Delaware decisions have ordered the production of a Cede breakdown as part of the stock list.[13] The decisions did not limit stockholder status to the names appearing on the stock ledger, in which case the inquiry would have stopped with Cede and the breakdown would have been irrelevant. *See Olson v. Buffington,* 1985 WL 11575, at *3 (Del. Ch. July 17, 1985) ("This Court has recognized that a party entitled to a stocklist pursuant to § 220 is also entitled to a Cede breakdown even though technically Cede is the record holder on the company's books.").

5. An Opportunity Lost: The *Enstar* Decisions

***19** An opportunity to confront the implications of the depository system for appraisal finally arose in litigation arising out of a merger involving Enstar Corporation. *See In re Appraisal of Enstar Corp.* (*Enstar I*), 1986 WL 8062 (Del. Ch. July 17, 1986), *rev'd sub nom.Enstar Corp. v. Senouf (Enstar II*), 535 A.2d 1351 (Del.1987). The litigation began as an appraisal proceeding, but Enstar reached a global settlement of the appraisal litigation. After Enstar refused to pay two of the appraisal petitioners, the matter transformed itself into a breach of contract case, with the petitioners seeking to enforce their entitlement to the settlement consideration.

One petitioner was Lucie Senouf. Before the merger, she held 10,441 shares in an account with Drexel Burnham Lambert Incorporated, which in turn held them through DTC. The other petitioner was Margaret Earle. Before the merger, she held 20,000 shares in an account with Prudential–Bache Securities Inc., which in turn held them through DTC. Neither Senouf nor Earle caused Cede to make an appraisal demand. An individual named Mr. Champy made the demand for Senouf. Prudential–Bache made a demand for Earle. Enstar argued that neither petitioner had validly perfected appraisal rights and was not entitled to participate in the settlement.

Senouf and Earle sought to take advantage of the settlement, and the case went to trial before then-Vice Chancellor, later Justice Hartnett. The petitioners did not argue that, by virtue of the depository system and the DTC participant list, Drexel and Prudential–Bache should be considered stockholders of record. Instead, they contended that the disclosures in Enstar's proxy statement did not accurately describe the role of DTC and Cede and misleadingly stated that "[a] record holder *such as a broker* who holds Common Shares ... as nominee for beneficial owners ... must exercise appraisal rights on behalf of such beneficial owners...." *Enstar I,*1986 WL 8062, at *4 (emphasis added).

Vice Chancellor Hartnett held that on the facts presented, Senouf and Earle had satisfied the Record Holder Requirement. He described the depository system in some detail, although predominantly as a voluntary choice by brokers. To get the flavor, it is worth quoting his description at length:

> CEDE & Co. is a partnership used by The Depository Trust Company as its nominee to hold securities for its participants—all of which are brokerage firms, banks and

> other financial institutions. Neither The Depository Trust Company nor CEDE & CO. hold any shares for themselves but only hold shares as nominees for the participants in The Depository Trust Company. At the time of the merger CEDE & Co. was listed on the books of ENSTAR as holding over 7 million shares of its stock and there was no breakdown on the books of ENSTAR of the actual beneficial ownership of the CEDE holdings.
>
> The use of CEDE & Co. and similar central security depositories to hold shares for stockbrokers, which shares are in turn held by the stockbrokers for their customers, has emerged as a major, if not dominant, method for the holding of shares of publicly traded corporations. The function performed by the central security depositories is to provide a central facility for the storage of enormous numbers of stock certificates and to provide a means for the transfer of shares without the actual transfer of certificates.
>
> * * *
>
> The publicly held corporations are well aware of the system and it is obviously to their advantage to have their shares held by central security depositories because this aids capital formation and it relieves the corporation of the paperwork which would be required if every owner of a share of stock had his shares listed in his own name on the books of the corporation.

***20** *Id.* at *1–2.

Vice Chancellor Hartnett contrasted the petitioners' knowledge about Cede with what Enstar knew. In short, he found that neither Senouf nor Earle knew that her broker was a DTC participant or that her shares were registered in Cede's name. By contrast, there was

> no question that ENSTAR knew that a large number of its shares were held in the name of CEDE ... and that CEDE ... was a nominee used by [DTC] which in turn held the shares for [its] participants—stock brokerage firms, banks and other financial institutions which in turn held them for their customers, the actual beneficial owners.

Id. at *2. He also discussed the Cede breakdown, finding that

> ENSTAR received a monthly breakdown from [DTC] of all the shares held in CEDE['s] name which showed the name of the stock broker, etc., for whom the shares were being held and which purportedly listed the number of shares held for each broker. ENSTAR was also entitled to receive, on request, supplementary lists.

Id. At the time of the merger, Enstar knew from participant list that Cede "held 379,268 shares for customers of Prudential–Bache and 40,169 shares for customers of Drexel–Burnham Lambert." *Id.* Vice Chancellor Hartnett stressed that despite knowing about Cede, Enstar's proxy materials made no mention of it.

Vice Chancellor Hartnett ultimately resolved the case on equitable grounds. He concluded that

> [w]hen the totality of the circumstances present here are considered, it is clear that ENSTAR had reasonable constructive notice that Mrs. Earle's and Mrs. Senouf's shares were listed on the corporation records under the name "CEDE & CO." and that its refusal to permit Mrs. Earle and Mrs. Senouf to receive the settlement consideration [provided to appraisal claimants] is based on impermissible hypertechnicalities.

Id. at *7. He thus ordered Enstar to pay the settlement consideration to the petitioners.

Enstar appealed, and the Delaware Supreme Court reversed. The high court viewed the case as a traditional dispute involving beneficial holder status, rather than a new scenario resulting from the depository system. The high court thus relied predominantly on existing precedent, such as *Salt Dome,* and subsequent cases interpreting the statutory language of the Record Holder Requirement. *Enstar II,* 535 A.2d at 1354. The court also observed that requiring record holder status was consistent with cases interpreting of other sections of the DGCL, including 8 *Del. C.* § 219(c), and that the rule was "harmonious with the Uniform Commercial Code," which permits a corporation to "treat the *registered owner* as the person *exclusively* entitled to vote, to receive notifications and otherwise to exercise all the rights and powers of an owner." *Id.* (emphasis in original) (quoting 6 *Del. C.* § 8–207(1)). The court does not appear to have been presented with the argument that by virtue of the DTC participant list, Drexel and Prudential–Bache should have been considered registered owners.

Although the Delaware Supreme Court touched on the practice of holding through DTC, the high court did not consider the origins of the requirement or the overlay of federal law. The Supreme Court regarded DTC as simply a new form of doing business, observing that that "[t]he use of security depositories by brokerage firms now is a common practice." *Id.* Of particular note, the court commented that "[t]he decision [to use DTC] is a matter which is strictly between the broker and its clients." *Id.* As support for this proposition, the Supreme Court cited the testimony of Mr. Karasek, an employee of Prudential–Bache who signed the appraisal demand for Earle. He had testified that

> ***21** [i]f the client wants their (sic) stock in street name, then Prudential–Bache will buy the securities for the client ...; the client has determined she wants it in street name. That's how it's done.
>
> * * *
>
> The choice is up to the client.

Id. (alterations in original). Reflecting on Mr. Karasek's testimony and citing Delaware cases pre-dating share immobilization, the high court commented that "[i]n making that choice [*i.e.,* the choice to hold in street name], the burden must be upon the stockholder to obtain the advantages of record ownership. The legal and practical effects of having one's stock registered in street name cannot be visited upon the issuer. The attendant risks are those of the stockholder, and where appropriate, the broker." *Id.* (citations omitted).

Later in the decision, the Supreme Court reiterated its view that Cede's role in the case resulted from a private decision made by the petitioners and their brokers:

> Here, the problem is one between the plaintiffs and their brokers. Enstar cannot, and should not, be blamed for the failure of a nominee or broker to correctly perfect appraisal rights for a beneficial owner. Several other brokers properly instructed CEDE & Co. to demand an appraisal on behalf of their customers. The failures of Prudential–Bache or Drexel in that regard should not be shifted to, or borne by, Enstar. The dispute, if any, is between these brokers and their clients.

Enstar II, 535 A.2d at 1355. Elsewhere, the Supreme Court quoted at length from Salt Dome and held:

> Thus, in the interest of promoting certainty in the appraisal process ..., a valid demand must be executed by or on behalf of the holder of record, whether that holder is the beneficial owner, a trustee, agent or nominee. Any other result would embroil merging corporations in a morass of confusion and uncertainty, none of which was of their making.

Id. at 1356.

Finally, the Delaware Supreme Court rejected the argument that Enstar's disclosures about perfecting appraisal rights were misleading. The high court held that the disclosures gave proper instructions for perfecting appraisal rights and that "the relationship between a beneficial stockholder and a nominee are not relevant matters of concern to the merging corporations." *Id.* at 1357.

In my view, the Delaware Supreme Court's decision in *Enstar II* reflected incorrect assumptions about the depository system. First, *Enstar II* assumed that custodial banks and brokers freely chose to move to the depository system for their own convenience.[14] To the contrary, the depository system was a necessary response to the late 1960s paperwork crisis and embodied in a federal mandate. The *Enstar II* court similarly treated the holding of shares through depositaries as something that is optional for end-users, *i.e.,* actual investors. While it is true theoretically that any particular investor could opt out of the depository system and chose to hold in record name,[15] only a few could do so before the system would break down. Just as some individuals can choose not to receive vaccinations and free ride on the immunity of the group, so too can a small minority of stockholders elect to hold shares directly. But without widespread participation in the depository system, securities markets would again drown in paperwork. The system was imposed by Congress and the SEC, and almost-universal participation is a *de facto* requirement.

***22** Second, *Enstar II* assumed that the depository system imposes only costs on issuers and yielded them no benefits.[16] Yet by the time of the *Enstar II* decision, the depository system was what enabled public trading of securities to take place. Issuers could not undertake an initial public offering or otherwise access the equity markets without depository ownership. Being able to raise capital through the public markets is an obvious benefit to issuers. So is avoiding the costly paperwork burdens that previously brought the markets to a stop. *See* Part I.A., *supra.* These benefits have only grown more profound since *Enstar II.*

Third, *Enstar II* reiterated the *Salt Dome* decision's concern about the uncertainty and practical difficulties a Delaware corporation would face in identifying its stockholders if asked to look beyond the stock ledger. With the Cede breakdown, those concerns do not exist. When *Enstar II* was written, a Cede breakdown could be obtained easily, and it provided a reliable listing of the depository institutions that held through DTC. Today, it is even easier to obtain a Cede breakdown, and because trades are now tracked in real time rather than awaiting an end-of-the-day netting-out process, the list is even more accurate.

Finally, *Enstar II* asserted at several points that the nominee relationship was not a matter of concern for the merging corporation.[17] That is not accurate either. Under federal law, the corporation whose stockholders would vote on the merger —and who could be eligible for appraisal rights—must go through DTC to identify its custodian banks and brokers for purposes of mailing out proxy materials. The issuer cannot ignore DTC and pretend that Cede is a single holder of record.

Notably, *Enstar II* did not address whether DTC participants should be regarded as record holders for purposes of Delaware law, as they are for federal law. No one seems to have made the argument, and neither court considered it. Although *Enstar II* seems to have collapsed the distinction between the broker level of beneficial ownership and the depository level, it did so on the assumption that the pertinent legislative facts had not changed since *Salt Dome.*[18] In my view, that was misguided.

***23** *Enstar II* does appear to have regarded construing the Record Holder Requirement as an appropriate exercise of judicial authority. As I see it, the question of whether DTC participants should be regarded as holders of record remains open for the Delaware Supreme Court to decide, should it wish to do so.

6. The Rise Of Appraisal Arbitrage

The most recent decisions to consider the role of DTC have involved the practice of appraisal arbitrage, a strategy in which investors purchase shares in order to pursue appraisal. In *Transkaryotic,* this court held that funds who bought shares after the record date for a merger could seek an appraisal for the shares purchased after the record date, without having to show that the shares were not voted in favor of the merger. 2007 WL 1378345, at *3. Subsequent decisions have followed *Transkaryotic.*[19]

The outcome in *Transkaryotic* turned on the role of Cede as the omnibus holder of record. On the record date for the merger, Cede held 29,720,074 shares. Acting in accordance with the instructions of its participants, Cede voted 12,882,000 shares in favor of the merger, leaving 16,838,074 shares eligible for appraisal. The petitioners beneficially owned 2,901,433 shares on the record date and acquired another 8,071,217 shares after the record date. They sought appraisal for all 10,972,650 shares, which was less than the total number of appraisal-eligible shares. This court regarded that fact as dispositive because under *Olivetti,* "the actions of the beneficial holders are irrelevant," and only "the record holder's actions determine perfection of the right to seek appraisal." *Id.* at *4, *3. Elaborating, the court explained that

> [t]he issue here mirrors that in *Olivetti* .... [Transkaryotic] seeks to examine relationships between Cede (the record holder) and certain nonregistered, beneficial holders in order to determine the existence of appraisal rights. But the Supreme Court has already deemed this relationship to be an improper and impermissible subject of inquiry in the context of an appraisal. The law is unequivocal. A corporation need not and should not delve into the intricacies of the relationship between the record holder and the beneficial holder and, instead, must rely on its records as the sole determinant of membership in the context of appraisal.

Id. at *4.

In my view, the rise of appraisal arbitrage suggests the need for a more realistic assessment of the depository system that looks through Cede to the DTC participants. But first, a caveat: Looking through DTC would not eliminate the ability of appraisal petitioners to seek appraisal for shares acquired after the record date, which is an outcome that opponents of appraisal arbitrage frequently advocate. As to that possibility, it is not clear to me why the law should treat a stockholder's right to seek an appraisal differently than how it treats other legal rights. An appraisal claim is simply a chose in action. As such, the claim passes with the shares.[20] In a market economy, the ability to transfer property, including intangible property, is generally thought to be a good thing; it allows the property to flow to the highest-valuing holder, thereby increasing societal wealth. For creditors, the ability to sell a bundle of property rights that the buyer can enforce is unquestioned. When a creditor assigns a loan, even one in default, the right to enforce the loan passes to the new holder. No one objects that the assignee purchased a lawsuit. It is not apparent to me why a right held by the equity side of the capital structure should be treated differently, particularly when the right to bring an appraisal proceeding has been compared by the Delaware Supreme Court to a debt collection action.[21] Consequently, no one should view my arguments in favor of looking through DTC as a way to eliminate appraisal arbitrage entirely—itself a debatable policy goal.[22] Custodial banks and brokers still could buy shares after the record date and seek appraisal for those shares. And of course, even under a regime that denied appraisal rights to shares purchased after the record date, investors still could accumulate large appraisal-eligible stakes between the time of deal announcement and the record date. *See* *Salomon Bros. Inc. v. Interstate Bakeries Corp.,* 576 A.2d 650, 654 (Del. Ch.1989) (finding "nothing inequitable about an investor purchasing stock in a company after a merger has been announced with the thought that, if the merger is consummated on the announced terms, the investor may seek appraisal").

***24** Nevertheless, in my view, looking through Cede to the DTC participants would be an improvement. Under the appraisal statute, a record holder is only supposed to be able to seek appraisal for shares (i) owned on the date of statutorily compliant demand for appraisal, (ii) held continuously through the effective date of the merger, and (iii) not voted in favor of the merger. *Ancestry.com,* 2015 WL 66825, at *4. Taken together, Cede's dominant holdings and the current one-size-fits-all interpretation of the Record Holder Requirement prevent courts from applying these requirements effectively. Cede owns too many shares, and with share immobilization, ownership does not change.

By contrast, if the focus were to move beyond Cede, it should be possible to develop a more nuanced jurisprudence. The number of shares held by banks and brokers does change, and those changes may have legal salience. Or situations may arise that lend themselves to specific rulings, such as if a broker acquires a large block of shares after the record date in a negotiated transaction. In that case, the seller should be readily identifiable, and it should be an easy matter to determine how the shares were voted. The federal securities laws require that banks and brokers obtain voting instructions from their clients, and banks and brokers satisfy this requirement by sending out voting instruction forms. *See generally* Keir D. Gumbs et al., *Debunking the Myths Behind Voting Instruction Forms and Vote Reporting,* 21 Corp. Gov. Adv. 1 (July/Aug. 2013). It also may be possible to use voter instruction forms for other purposes, such as confirming whether or not particular shares held by an appraisal claimant on the record date were voted in favor of the merger. And as this case shows, there also may be records at the broker level which, if examined, would allow the courts to apply other statutory limitations more accurately. We already make these types of distinctions when dealing with the right to vote, which was the principal right relied on by analogy in *Salt Dome* for the creation of the Record Holder Requirement.[23] Under this more flexible approach, the corporation "generally is entitled to rely on its own stock list," but the list is not conclusive; questions of ownership and the ability to exercise associated rights can be the subject of proof. *Preston,* 650 A.2d at 649.

***25** It would have been preferable, in my view, to begin developing this case law in 2010. *See Kurz,* 989 A.2d at 174 (arguing that treating DTC participants as holders of record could help "[r]educ[e] the number of shares available for appraisal arbitrage"). Yet the need for a more flexible approach has not gone away. Looking through Cede is obviously imperfect, but until share tracing becomes possible, the perfect should not be the enemy of the good. Viewed pragmatically, looking through Cede to the custodial banks and brokers on the participant list merely returns Delaware law to the state in which it existed before the federal policy of share immobilization, restoring the conditions that prevailed when *Salt Dome* was written and later when the Record Holder Requirement was codified.

III. CONCLUSION

Under current law, Dell's motion for summary judgment must be granted. The Funds lost their appraisal rights when their shares were re-titled in the names of their custodial banks' nominees. Were it up to me, I would hold that the concept of a "stockholder of record" includes the custodial banks and brokers on the DTC participant list. But given existing precedent, I believe that only the Delaware Supreme Court can change how our case law interprets the Record Holder Requirement. This court obviously has no ability to tell the Delaware Supreme Court what to do. This decision has attempted only to present the reasons why one trial judge believes that a different approach would be superior.

All Citations

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Footnotes

[1] The five institutions are (i) the Northwestern Mutual Series Fund, Inc. Equity Income Portfolio ("Northwestern"), (ii) the Manulife U.S. Large Cap Value Equity Fund ("Manulife"), (iii) the T. Rowe Price Funds SICAV U.S. Large Cap Value Equity Fund ("T. Rowe Price"), (iv) the Milliken Retirement Plan ("Milliken"), and (v) the Curtiss–Wright Corporation Retirement Plan ("Curtiss–Wright"). Although three are "funds" and two are "plans," this decision refers to them as the Funds. The collective referent is purely for convenience.

[2] Technically, both the Funds and the custodial banks were "entitlement holders." This term defined is under Article 8 of the Delaware Uniform Commercial Code as a "person identified in the records of a securities intermediary as the person having a security entitlement against the securities intermediary." 6 *Del. C.* § 8–102(a)(7). The term "securities intermediary" means either "a clearing corporation," *i.e.* DTC, or "a person, including a bank or broker, that in the ordinary course of its business maintains securities accounts for others and is acting in that capacity," *i.e.,* the custodial banks. *Id.* § 8–102(a)(14).

[3] *See, e.g., S. Prod. Co. v. Sabah,* 87 A.2d 128 (Del.1952); *Roam–Tel P'rs v. AT & T Mobility Wireless Op. Hldgs. Inc.,*2010 WL 5276991 (Del. Ch. Dec. 17, 2010) (Strine, V.C.); *Matter of Enstar Corp.,* 513 A.2d 206 (Del. Ch.1986); *LeCompte v. Oakbrook Consol., Inc.,* 1986 WL 2827 (Del. Ch. Mar. 7, 1986); *Engel v. Magnavox Co.,* 1976 WL 1705 (Del. Ch. Feb. 5, 1976); *Abraham & Co. v. Olivetti Underwood Corp.,* 204 A.2d 740 (Del. Ch.1964), *aff'd sub nom.Olivetti Underwood Corp. v. Jacques Coe & Co.,* 217 A.2d 683 (Del.1966). *See generally* 1 R. Franklin Balotti & Jesse A. Finkelstein, The *Delaware Law of Corporations & Business Organizations* § 9.44, at 9116 (3d ed. 2014) ("Prior to the Delaware Supreme Court's ruling in *Alabama By–Products Corp. v. Cede & Co.,* appraisal rights could be forfeited through any tender at any time, even if the tender was inadvertent and an appraisal petition had been filed." (footnote omitted)). The Delaware cases traditionally treated the receipt of the transaction consideration as something inadvertent. Under Article 8 of

the UCC, a securities intermediary is required by law to "take action to obtain a payment or distribution made by the issuer of a financial asset" and is "obligated to its entitlement holder for a payment or distribution made by the issuer of a financial asset if the payment or distribution is received by the securities intermediary." 6 *Del. C.* § 8–505(a) & (b).

4 A variety of sources provide consistent accounts of the origins of the depository system. *See, e.g.,* Securities and Exchange Commission, *Study Of Unsafe And Unsound Practices Of Brokers And Dealers,* H.R. Doc. No. 92–231, 92d Cong., 2d Sess. 9–10 (1971) [hereinafter *SEC Study*]; Uniform Commercial Code, Prefatory Note to Article 8 (revised 1994) [hereinafter *Prefatory Note*]; *Street Name* at 10–6 n.5; Teresa Carnell & James J. Hanks, Jr., *Shareholder Voting and Proxy Solicitation: The Fundamentals,* Maryland Bar Journal 23, 26 (Jan./Feb. 2004); David C. Donald, *Heart of Darkness: The Problem at the Core of the U.S. Proxy System and Its Solution,* 6 Va. L. & Bus. Rev. 41, 45, 50–61 (2011); Marcel Kahan & Edward Rock, *The Hanging Chads of Corporate Voting,* 96 Geo. L.J. 1227, 1237–38 & nn.45–50, 1273–74 (2008); Emily I. Osiecki, Alabama By–Products Corp. v. Cede & Co.: *Shareholder Protection Through Strict Statutory Construction,* 22 Del. J. Corp. L. 221, 223–28 (1997); Suellen M. Wolfe, *Escheat and the Challenge of Apportionment: A Bright Line Test To Slice A Shadow,* 27 Ariz. St. L.J. 173, 178–88 (1995); Businesses & Subsidiaries–The Depository Trust Company (DTC), http://www.dtcc.com/about/businesses-and-subsidiaries/dtc.aspx (last visited June 5, 2015).

5 *See*8 *Del. C.* § 158 ("The shares of a corporation shall be *represented* by certificates, provided that the board of directors of the corporation may provide by resolution or resolutions that some or all of any or all classes or series of its stock shall be uncertificated shares.") (emphasis added); *Testa v. Jarvis,* 1994 WL 30517, at *6 (Del. Ch. Jan. 12, 1994) (Allen, C.) (noting that "possession of a certificate does not itself constitute ownership of shares"); *Haskell v. Middle States Petroleum Corp.,* 165 A. 562, 563 (Del. Ch.1933) ("[A] person may be the legal owner of stock even though he has received no certificate; therefore, the certificate is only evidence of ownership."); *Smith v. Universal Serv. Motors Co.,* 147 A. 247, 248 (Del. Ch.1929) ("The status of stockholder in a corporation is not dependent on the issuance to him of a certificate of stock. The certificate is only an evidence of ownership—a muniment of title."); *Mau v. Mont. Pac. Oil Co.,* 141 A. 828, 831 (Del. Ch.1928) ("Possession of a certificate is not essential to the ownership of stock."); *Baker v. Bankers' Mortg. Co.,* 135 A. 486, 488 (Del. Ch.1926) ("Certificates of stock are themselves only evidence of shares. They are not the shares.") (Wolcott, Jos., C.), *aff'd sub nom.Sohland v. Baker,* 141 A. 277 (Del.1927).

6 *See id.* § 213 (establishing procedures for fixing a record date for determining the stockholders of record entitled (i) to notice of any meeting of stockholders (§ 213(a)), (ii) to vote at any meeting of stockholders (§ 213(a)), (iii) to act by written consent without a meeting (§ 213(b)), or (iv) to receive a dividend or other distribution or allotment of rights (§ 213(c))).

7 *EMAK P'rs,* 992 A.2d at 398. There is perhaps some irony in using dictum to characterize a portion of a decision as dictum, although perhaps greater irony in using dictum to instruct trial judges not to use dictum. *See Gatz Props., LLC v. Auriga Capital Corp.,* 59 A.3d 1206 (Del.2012). *See generally* Mohsen Manesh, *Damning Dictum: The Default Duty Debate In Delaware,* 39 J. Corp. L. 35, 54–63 (2013) (exploring tensions in *Gatz*). My discussion of an alternative approach to the Record Holder Requirement is admittedly dictum. I considered the alternative of setting forth these views in a law review article or speech, as *Gatz* suggested, but it seemed to me that to the extent a trial judge wished to suggest to an alternative approach that the Delaware Supreme Court might consider, a judicial opinion that could be reviewed by the Delaware Supreme Court would provide an appropriate and efficient vehicle.*See, e.g., In re Cox Commc'ns, Inc. S'holder Litig.,* 879 A.2d 604, 642–48 (Del. Ch.2005) (Strine, V.C.) (recommending change in standard of review for controller squeeze-outs); *Agostino v. Hicks,* 845 A.2d 1110, 1121 (Del. Ch.2004) (recommending change in standard for distinguishing between direct and derivative actions); *In re Caremark Int'l Inc. Deriv. Litig.,* 698 A.2d 959, 967–70 (Del. Ch.1996) (Allen, C.) (recommending change in the law's approach to the duty of oversight). One obvious benefit is that in the event of an appeal, should there by one, the Delaware Supreme Court will have all of the arguments before it in one place. Unless and until the alternative approach discussed in this opinion is adopted by the Delaware Supreme Court, no one should be misled into believing that it has precedential

effect. *Cf.* *Gotham P'rs, L.P. v. Hallwood Realty P'rs, L.P.,* 817 A.2d 160, 167 (Del.2002) (expressing concern that dictum in trial court opinion "should not be ignored because it could be misinterpreted in future cases as a correct rule of law" and "could be relied upon adversely by courts, commentators and practitioners in the future").

8 Lawrence Hamermesh, *How We Make Law in Delaware, and What to Expect from Us in the Future,* 2 J. Bus. & Tech. L. 409, 409 (2007) ("The best-known of the principal policymakers in Delaware are the members of the judiciary."); Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law,* 58 Vand. L.Rev. 1573, 1591 (2005) ("The most noteworthy trait of Delaware's corporate law is the extent to which important and controversial legal rules are promulgated by the judiciary, rather than enacted by the legislature."); Jill E. Fisch, *The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters,* 68 U. Cin. L.Rev. 1061, 1075 (2000) ("Delaware corporate law relies on judicial lawmaking to a greater extent than other states.").

9 *See, e.g.,* Hamermesh, *supra,* at 414 ("[W]e view the courts as the first line of defense, the first responders in dealing with complex situations. When drafting legislation, we abstain from addressing complicated matters that are hard to figure out, allowing them to develop through the common law."); Omari Scott Simmons, *Branding the Small Wonder: Delaware's Dominance and the Market for Corporate Law,* 42 U. Rich. L.Rev. 1129, 1159 (2008) ("As a result of the legislature's preference against regulatory prescription and its deference to the judicial branch, Delaware courts are often the first responders to corporate law controversies."); *see also* Lawrence A. Hamermesh & Norman M. Monhait, *A Delaware Response to* Delaware's Choice, 39 Del. J. Corp. L. 71, 75 (2014) (agreeing that the Corporation Law Council and the General Assembly "have often subscribed to a ... 'wait-and-see approach' proposing and enacting, respectively, amendments to the DGCL only when there are persuasive reasons to do so" and endorsing a continuing policy of "reticence to initiate legislative action").

10 Kahan & Rock, *Symbiotic Federalism,supra,* at 1594. The commentators referred to "numerous examples of this tendency" and provided five examples. *Id.* at 1594–96. All involved statutory interpretation. *Id.* One involved the interpretation of the appraisal statute. *Id.* (citing the narrow interpretation given to language in 8 *Del. C.* § 262(h) in *Weinberger v. UOP, Inc.,* 457 A.2d 701, 713 (Del.1983)).

11 *See, e.g., Shintom Co. v. Audiovox Corp.,* 888 A.2d 225, 227 (Del.2005) (describing the DGCL as "an enabling statute that provides great flexibility for creating the capital structure of a Delaware corporation."); *In re Topps Co. S'holders Litig.,* 924 A.2d 951, 958 (Del. Ch.2007) (Strine, V.C.) (describing the DGCL as "a broadly enabling statute"); *Jones Apparel Gp., Inc. v. Maxwell Shoe Co.,* 883 A.2d 837, 845 (Del.Ch.2004) (Strine, V.C.) (noting that the DGCL is "is widely regarded as the most flexible in the nation because it leaves the parties to the corporate contract (managers and stockholders) with great leeway to structure their relations, subject to relatively loose statutory constraints"); *Matter of Appraisal of Ford Hldgs., Inc. Preferred Stock,* 698 A.2d 973, 976 (Del. Ch.1997) (Allen, C.) (explaining that "unlike the corporation law of the nineteenth century, modern corporation law contains few mandatory terms; it is largely enabling in character"); *accord* E. Norman Veasey & Christine T. Di Guglielmo, *History Informs American Corporate Law: The Necessity of Maintaining A Delicate Balance in the Federal "Ecosystem",* 1 Va. L. & Bus. Rev. 201, 204 (2006) ("Corporate statutes, like the Delaware General Corporation Law, continue to take an enabling approach and allow wide latitude for private ordering."); Edward P. Welch & Robert S. Saunders, *Freedom and Its Limits in the Delaware General Corporation Law,* 33 Del. J. Corp. L. 845, 847 (2008) ("The DGCL gives incorporators enormous freedom to adopt the terms they believe are most appropriate for the organization, finance, and governance of their particular enterprise.").

12 *See Hatleigh Corp. v. Lane Bryant, Inc.,* 428 A.2d 350 (Del. Ch.1981); *Giovanini v. Horizon Corp.,* 1979 WL 178568 (Del. Ch. Sept. 10, 1979).

13 *E.g., Berger v. Pubco Corp.,* 2008 WL 4173860, at *3 (Del. Ch. Sept. 8, 2008); *Wynnefield P'rs Small Cap Value, L.P. v. Niagara Corp.,* 2006 WL 2521434, at *2 (Del. Ch. Aug. 9, 2006); *Envtl. Diagnostics, Inc. v. Disease Detection Intern., Inc.,* 1988 WL 909658, at *3 (Del. Ch. July 15, 1988) (Allen, C.); *RB Assocs. of N.J., L.P. v. Gillette Co.,* 1988 WL 27731, at *2 (Del. Ch. Mar. 22, 1988) (Allen, C.); *Shamrock Assocs. v. Tex.*

Am. Energy Corp., 517 A.2d 658, 661 (Del. Ch.1986); *Weiss v. Anderson, Clayton & Co.,* 1986 WL 5970, at *4 (Del. Ch. May 22, 1986) (Allen, C.).

[14] *See* *Enstar II,* 535 A.2d at 1354 ("The decision [to use DTC] is a matter which is strictly between the broker and its clients."). Other Delaware decisions during this period reflected the same assumption. *See, e.g., RB Assocs.,* 1988 WL 27731, at *3 (describing DTC system as a "mechanism of convenience for the brokerage firms"); *Olson,* 1985 WL 11575, at *3 (describing Cede as "but a name used for the convenience of the brokerage houses"); *Hatleigh,* 428 A.2d at 353 (remarking that DTC exists "for the benefit of those firms participating in the Depository Trust Company so as to simplify their stock transfer transactions on behalf of their customers"); *Giovanini,* 1979 WL 178568, at *1 (describing Cede as a "mechanism of convenience for the brokerage firms").

[15] *See, e.g.,*6 *Del. C.* § 8–508 ("A securities intermediary shall act at the direction of an entitlement holder to change a security entitlement into another available form of holding for which the entitlement holder is eligible, or to cause the financial asset to be transferred to a securities account of the entitlement holder with another securities intermediary."); *id.* cmt. 1 ("If security certificates in registered form are issued for the security, and individuals are eligible to have the security registered in their own name, the entitlement holder can request that the intermediary deliver or cause to be delivered to the entitlement holder a certificate registered in the name of the entitlement holder or a certificate indorsed in blank or specially indorsed to the entitlement holder.... If the security can be held by individuals directly in uncertificated form, the entitlement holder can request that the security be registered in its name."); *see also*8 *Del. C.* § 158 ("Every holder of stock represented by a certificate shall be entitled to have a certificate ... representing the number of shares registered in certificate form.").

[16] *See* *Enstar II,* 535 A.2d at 1353 n.2 ("Whether a beneficial stockholder participates in a depository system is a matter between the beneficial stockholder and his broker, and is not a consideration for issuers."); *accord* *Wynnefield P'rs Small Cap Value L.P. v. Niagara Corp.,* 2006 WL 1737862, at *3 (Del. Ch. June 19, 2006) (same), *rev'd on other grounds,*907 A.2d 146 (Del.2006) (ORDER); *Am. Hardware Corp. v. Savage Arms Co.,* 136 A.2d 690, 692 (Del.1957) ("If an owner of stock chooses to register his shares in the name of a nominee, he takes the risks attendant upon such an arrangement....").

[17] *Enstar II,* 535 A.2d at 1354 ("The legal and practical effects of having one's stock registered in street name cannot be visited upon the issuer. The attendant risks are those of the stockholder, and where appropriate, the broker."); *id.* at 1355 ("Here, the problem is one between the plaintiffs and their brokers. Enstar cannot, and should not, be blamed for the failure of a nominee or broker to correctly perfect appraisal rights for a beneficial owner.... The dispute, if any, is between these brokers and their clients.")

[18] The concept of "legislative facts" refers to the empirical assumptions about the world that courts necessarily make when deciding cases. *See In re* *Oracle Corp. Deriv. Litig.,* 824 A.2d 917, 940 (Del. Ch.2003) (Strine, V.C.) (deploying concept and citing Kenneth Culp Davis, *An Approach to Problems of Evidence in the Administrative Process,* 55 Harv. L.Rev. 364, 402–403 (1942)). *See generally* Leo E. Strine, Jr., *The Inescapably Empirical Foundation of the Common Law of Corporations,* 27 Del. J. Corp. L. 499, 502–503 (2002) (describing concept at greater length).

[19] *See, e.g.,* *Merion Capital LP v. BMC Software, Inc.,* 2015 WL 67586 (Del. Ch. Jan. 5, 2015);*Ancestry.com,* 2015 WL 66825.

[20] *See generally* *In re Activision Blizzard Inc. S'holder Litig.,* ––– A.3d ––––, 2015 WL 2438067, *13–25 (Del. Ch. May 21, 2015). Choses in action are transferrable under Delaware law when they are the types of claims that would survive the death of the transferor and pass to his personal representative. *See* *Indus. Trust Co. v. Stidham,* 33 A.2d 159, 160–61 (Del.Super.1942). By statute in Delaware, "[a]ll causes of action, except actions for defamation, malicious prosecution, or upon penal statutes, shall survive...." 10 *Del. C.* § 3701.

[21] *See* *Salt Dome,* 41 A.2d at 588. Indeed, even the right to control how shares vote transfers with the shares, notwithstanding the legal expedient of the record date, because the subsequent holder can compel the seller to issue him a proxy (assuming the seller can be identified). *Commonwealth Assocs. v. Providence Health Care, Inc.,* 641 A.2d 155, 158 (Del. Ch.1993) (Allen, C.); *In re Giant Portland Cement Co.,* 21 A.2d 697, 701

(Del. Ch.1941); *In re Canal Constr. Co.,* 182 A. 545, 547–48 (Del.1936) (Wolcott, Jos., C.); *Italo Petroleum Corp. of Am. v. Producers' Oil Corp. of Am.,* 174 A. 276, 280 (Del. Ch.1934) (Wolcott, Jos., C.).

[22] Strong arguments can be made that appraisal represents a more rational and efficient alternative to traditional fiduciary duty litigation. *See* Charles R. Korsmo & Minor Myers, *Competition and the Future of M & A Litigation,* 100 Iowa L.Rev. Bull. 19, 25–28 (2015); Charles R. Korsmo & Minor Myers, *Appraisal Arbitrage and the Future of Public Company M & A,* 92 Wash U.L.Rev. (forthcoming 2015); Charles Korsmo & Minor Myers, *The Structure of Stockholder Litigation: When Do The Merits Matter,* 75 Ohio State L.J. 829, 859–67 (2014). At one point, the Delaware Supreme Court appeared to prioritize appraisal over fiduciary duty litigation by holding that "a plaintiff's monetary remedy [following a merger] ordinarily should be confined to the more liberalized appraisal proceeding herein established." *Weinberger v. UOP, Inc.,* 457 A.2d 701, 714 (Del.1983). That promise did not survive the decisions in *Rabkin v. Philip A. Hunt Chemical Corp.,* 498 A.2d 1099 (Del.1985), and *Cede & Co. v. Technicolor, Inc.,* 542 A.2d 1182 (Del.1988). *See generally Andra v. Blount,* 772 A.2d 183, 192 (Del. Ch.2000) (Strine, V.C.) (explaining that *Rabkin* and *Cede* effectively overruled the appraisal-as-basic-remedy aspect of *Weinberger*).

[23] *See, supra,* n.19 (citing cases in which court permitted post-record date acquirer of shares to determine how shares were voted, notwithstanding legal ownership on stock list); *Preston v. Allison,* 650 A.2d 646, 649 (Del.1994) (looking through name of registered holder on stock list and recognizing voting rights of beneficial owners where form of ownership was mandated by federal law); *Sutter Opportunity Fund 2 LLC v. Cede & Co.,* 838 A.2d 1123, 1129 (Del. Ch.2003) (permitting issuer to look through Cede for purposes of analyzing whether proponents of a proposal for a matter to be submitted to a vote met a 10% minimum threshold in partnership agreement); *Seidman & Assocs., L.L.C. v. G.A. Fin., Inc.,* 837 A.2d 21, 29 (Del. Ch.2003) (same); *In re Ne. Water Co.,* 38 A.2d 918, 923 (Del. Ch.1944) (treating statutory reference to stockholder status being determined by name on stock list as "a limited but practical rule of evidence for the ready ascertainment of persons entitled to notice of and to vote at a stockholders' meeting" but not dispositive in all cases); *In re Diamond State Brewery, Inc.,* 2 A.2d 254, 257 (Del. Ch.1938) (Wolcott, Jos., C.) ("The court is not bound in a review proceeding [of an election] by the showing of stockholders made on the corporation's books."); *cf.Rainbow Navigation, Inc. v. Pan Ocean Navigation, Inc.,* 535 A.2d 1357, 1359 (Del.1987) ("We now hold that when the stock ledger is blank or non-existent, the Court of Chancery has the power to consider other evidence to ascertain and establish stockholder status.").

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Court of Chancery of Delaware.

IN RE: APPRAISAL OF JARDEN CORPORATION

CONSOLIDATED C.A. No. 12456-VCS
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Date Submitted: May 1, 2019
|
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MEMORANDUM OPINION

SLIGHTS, Vice Chancellor

***1** This statutory appraisal action arises from a merger whereby Newell Rubbermaid, Inc. ("Newell") acquired Jarden Corporation ("Jarden" or the "Company") (the "Merger") for cash and stock totaling $59.21 per share (the "Merger Price"). Petitioners, Verition Partners Master Fund Ltd., Verition Multi-Strategy Master Fund Ltd., Fir Tree Value Master Fund, LP and Fir Tree Capital Opportunity Master Fund, LP (together "Petitioners"), were Jarden stockholders on the Merger's effective date and seek a judicial appraisal of the fair value of their Jarden shares as of that date.

At the close of the trial, I observed, "[w]e are in the classic case where ... very-well credentialed experts are miles apart.... There's some explaining that is required here to understand how it is that two very well-credentialed, I think, well-intended experts view this company so fundamentally differently."[1] This observation was prompted by the all-too-frequently encountered disparity in the experts' opinions regarding Jarden's fair value. Jarden's expert, Dr. Glenn Hubbard, applying a discounted cash flow ("DCF") analysis, opines that Jarden's fair value as of the Merger was $48.01 per share. Petitioners' expert, Dr. Mark Zmijewski, applying a comparable companies analysis, contends that Jarden's fair value as of the Merger was $71.35 per share. To put the disparity in context, Dr. Zmijewski's valuation implies that the market mispriced Jarden by over $5 billion.

In a statutory appraisal action, the trial court's function is to appraise the "fair value" of the dissenting stockholder's "shares of stock" by "tak[ing] into account all relevant factors."[2] The statute does not define "fair value" but our courts understand the term to mean the petitioner's "pro rata share of the appraised company's value as a going concern."[3] This definition of fair value "is a jurisprudential, rather than purely economic, construct."[4] Even so, the remarkably broad "all relevant factors" mandate necessarily leads the court deep into the weeds of economics and corporate finance. These are places law-trained judges should not go without the guidance of experts trained in these disciplines. In other words, corporate finance is not law. The appraisal exercise is, at bottom, a fact-finding exercise, and our courts must appreciate that, by functional imperative, the evidence, including expert evidence, in one appraisal case will be different from the evidence presented in any other appraisal case. Different evidence, of course, can lead to different decision paths and different outcomes. After all, the appraisal exercise prescribed by the governing statute contemplates a trial—a good, old-fashioned trial—where the parties carry burdens of proof, present their evidence in hopes of meeting that burden and subject their adversary's evidence to the "crucible of cross-examination" in keeping with the traditions of our adversarial process of civil justice.[5]

***2** Our Supreme Court has had several opportunities recently to provide direction with regard to certain frames of reference this court should consider while performing the statutory appraisal function.[6] I will not recount those holdings here as they are well known. Suffice it to say, as I approached my deliberation of the evidence in this case, my "takeaway" from the Supreme Court's recent direction reduced to this: "What is necessary in any particular [appraisal] case [ ] is for the Court of Chancery to explain its [fair value calculus] in a manner that is grounded in the record before it." [7] That is what this court endeavors to do after every trial and what I have endeavored to do here. [8]

The parties have reveled in the statutory mandate that the court consider "all relevant factors." Indeed, they have joined issue on nearly every possible indicator of fair value imaginable, including market indicators (unaffected market price, deal price less synergies, Jarden stock offerings shortly before the Merger) and traditional valuation methodologies (comparable companies and DCF analyses). [9] The result: an unfortunately long opinion, made so by a sense that I needed to traverse every road the parties waived me down right to the bitter end, even if that road did not lead to the desired fair value destination. Appraisal litigation can be unwieldy. This is one of those cases. Apologies in advance to those who read on.

I begin my fair value analysis where I believe I must —with the market evidence. [10] As explained below, I have found Jarden's unaffected market price of $48.31 per share is a reliable indicator of its fair value at the time of the Merger. This finding is supported by credible, unrebutted expert testimony from Dr. Hubbard, including an event study that analyzed the market's response to earnings and other material announcements. Dr. Hubbard's expert analysis of the Unaffected Market Price is corroborated by credible evidence, including that Jarden had no controlling stockholder, its public float was 93.9%, it was well covered by numerous professional stock analysts, its stock was heavily traded and it enjoyed a narrow bid-ask spread. As important, there was no credible evidence that material information bearing on Jarden's fair value was withheld from the market as of the Merger. This market evidence was persuasive and I have given it substantial weight in my fair value determination.

***3** As noted, the Merger consideration, or "deal price," was $59.21 per share. Respondent proffers this evidence as a reliable indicator fair value, particularly when synergies are "backed out" as required by our law. [11] Petitioners respond that the sale process leading to the Merger was highly flawed because Jarden's lead negotiator was willing to sell Jarden on the cheap and the Jarden board of directors (the "Board") failed to test the market before agreeing to sell the Company to Newell. After considering the evidence, I agree with Petitioners that the sale process left much to be desired. Jarden's lead negotiator acted with little to no oversight by the Board and, in doing so, got way out in front of the Board and Jarden's financial advisors in suggesting to Newell a price range the Board would accept to sell the Company before negotiations began in earnest. There was no pre-signing or post-signing market check. Moreover, the contemporaneous evidence regarding deal synergies was conflicting and the parties' experts acknowledged that valuing the synergies and assessing which party took that value in the Merger was especially difficult in this case. For these reasons, I have placed little weight on the deal price less synergies beyond considering that evidence as a "reality check" on my final fair value determination.

As additional market evidence of Jarden's fair value, Respondent points to Jarden's decision to finance a sizeable acquisition just prior to the Merger (in the midst of negotiations) with an equity offering valued at $49.00 per share. When the market reacted poorly to the acquisition, Jarden announced that it would buy back up to $50 million in Jarden shares at prices up to $49.00 per share as a signal of confidence to the market. This contemporaneous evidence of Jarden management's internal valuation of the Company, performed to facilitate Jarden's acquisition strategy in furtherance of its standalone operations, is relevant market evidence of fair value. While far from dispositive, Jarden's internal efforts to value itself as a going concern for business, not litigation, purposes provides a useful input.

In keeping with their theme that the market evidence is not reliable, Petitioners have focused on "traditional valuation methodologies" to carry their burden of proving Jarden's fair value as of the Merger. Their valuation expert opines that a comparable company/market multiples analysis provides the best evidence of fair value, and that methodology supports his conclusion that Jarden's fair value at the Merger was $71.35 per share. The credibility, or not, of this methodology depends in large measure on the quality of the comparables. And then the appraiser must select an appropriate multiple. After considering the evidence, I am satisfied that Petitioners' comparable companies analysis is not credible because Jarden had no reliable comparables. Consequently, I give no weight to the results derived from this valuation approach.

Not surprisingly, both parties proffered expert evidence regarding Jarden's fair value based on DCF and, not surprisingly, the experts' DCF analyses yielded results that were solar systems apart. After carefully reviewing the evidence, including the valuation treatises submitted as evidence in support of the experts' conclusions, I am satisfied that both experts utilized inputs in their DCF models that were not justified and that skewed the results.[12] Accordingly, I have utilized the most credible components of both expert's analyses to conduct my own DCF valuation, in my best effort to obey our appraisal statute's "command that the Court of Chancery undertake an '*independent*' assessment of fair value" when performing its mandated appraisal function.[13] As explained below, my DCF analysis reveals a valuation of $48.13 per share.

***4** After considering all relevant factors, I have appraised Jarden's fair value as of the Merger at $48.31 per share. This value, derived from the unaffected market price, is consistent with Jarden's DCF value and the less reliable, but still relevant, deal price less synergies value.

I. FACTUAL BACKGROUND

I recite the facts as I find them by a preponderance of the evidence after a four-day trial beginning in June 2018. That evidence consisted of testimony from twenty-eight witnesses (twenty-five fact witnesses, some presented live and some by deposition, and three live expert witnesses) along with more than 2,000 exhibits. To the extent I have relied upon evidence to which an objection was raised but not resolved at trial, I will explain the bases for my decision to admit the evidence at the time I first discuss it.

A. Parties and Relevant Non-Parties

Prior to its acquisition by Newell on April 15, 2016 (the "Merger Date"), Jarden was a consumer products company that held a diversified portfolio of over 120 quality brands.[14] This portfolio included well-known goods like Ball jars, Coleman sporting goods, Crock-Pot appliances and Yankee Candle candles.[15] Jarden was incorporated in Delaware with headquarters in Boca Raton, Florida, and corporate offices in Norwalk, Connecticut and Miami, Florida.[16] Prior to the Merger, Jarden traded on the New York Stock Exchange.[17] Following the Merger, the combined company was re-named Newell Brands, Inc. ("Newell Brands").[18]

Petitioners are Verition Partners Master Fund Ltd., Verition Multi-Strategy Master Fund Ltd., Fir Tree Value Master Fund, LP and Fir Tree Capital Opportunity Master Fund, LP.[19] Petitioners acquired their Jarden shares after the announcement of the Merger and were stockholders as of the Merger Date. They collectively hold 2,435,971 shares of Jarden common stock.

B. The Company

Jarden traces its origins to Alltrista Corporation, a company that was spun off in 1993 from Ball Corporation's canning business.[20] In 2000, Martin Franklin and Ian Ashken acquired Alltrista after having initiated a stockholder campaign to unseat Alltrista's board and senior management.[21] By 2001, Franklin and Ashken served as Alltrista's Chief Executive Officer and Chief Financial Officer, respectively, and renamed the company Jarden.[22] In August 2003, James Lillie joined the Jarden team as Chief Operating Officer.[23] Their shared goal was to create the "best consumer products company in the world."[24]

Franklin served as CEO and Chairman of the Board until 2011,[25] when Jarden reorganized its management structure. The Company created the "Office of the Chairman," comprising Franklin as Executive Chairman, Ashken as Vice Chairman and CFO,[26] and Lillie as CEO.[27] As a result of this reorganization, Franklin surrendered direct control of Jarden's day-to-day operations, but remained chiefly in charge of capital distribution and M&A activity.[28] Lillie and Ashken took over the day-to-day operation of the Company.[29] Ashken also maintained a dominant role in Jarden's financial planning and acquisitions.[30]

***5** As a holding company,[31] Jarden maintained a unique, decentralized structure. Its various businesses functioned autonomously, allowing them to pursue outside opportunities and synergies.[32] The respective business unit heads exercised full control over the development of their individual strategic plans.[33] Even so, the businesses stayed in constant communication with Jarden senior management regarding operations.[34]

C. Jarden Experiences Strong Growth from 2001–2015

Jarden pursued a two-pronged growth strategy, focusing on internal growth and growth via acquisitions.[35] In this regard, management set a goal of 3 to 5% annual internal revenue growth,[36] 10 to 15% earnings per share ("EPS") growth, 3 to

5% organic top-line growth, 7 to 10% EBITDA growth and 20 to 50 basis points of gross margin growth.[37] These targets produced laudable results. From 2010 through 2015, Jarden saw average organic yearly revenue growth of 4.8%, the top of its targeted range.[38] In fact, Jarden was regarded as "best in class by any measure in terms of shareholder returns over 15 years, 10 years, 5 years, 3 years, 1 year."[39] Jarden's margins experienced continued expansion and it met or exceeded its guidance in all but one quarter of its existence.[40] By 2015, Jarden generated over $1.2 billion in segment earnings and revenues of almost $9 billion.[41] This reflected an increase in revenue of 4.8% year over year in fiscal year 2015.[42]

Given its impressive results, it is not surprising that Jarden's stock performed well and traded efficiently. In 2012, Jarden joined the "S&P 400."[43] By the end of 2015, Jarden's market capitalization topped $10.2 billion, placing it among the top 20% of all US publicly traded firms.[44] More than twenty professional financial analysts followed Jarden, reporting regularly on the Company's business operations and forecasts.[45] In addition to its high average trading volume, Jarden's "bid-ask spread" was just 0.02% and its public float was approximately 94% of its outstanding stock.[46] Jarden's stock trading price historically responded to the announcement of value-relevant information as one would expect in a semi-strong efficient market.[47]

M&A drove Jarden's growth.[48] With Franklin at the helm, Jarden acquired over 40 companies and brands, its stock grew over 5,000% and its sales progressed from approximately $305 million in 2001 to over $8.6 billion in 2015.[49] Franklin and his team were not only well-known "deal-makers" in the public markets,[50] they were among "the best performers in the sector."[51]

***6** Under Franklin's leadership, Jarden management constructed a well-conceived convention for singling-out and completing acquisitions.[52] Jarden avoided acquisitions that would insert it in spaces where major pure-play competitors, like Proctor & Gamble, operated.[53] Jarden, instead, concentrated on acquiring top brands in niche markets.[54] This strategy developed secure trenches that presented barriers to others who might look to compete with Jarden's niche product lines.[55] It also enabled Jarden globally to expand its brands.[56]

D. Jarden Shifts Its Strategic Focus

Jarden's businesses sold their products across a vast spread of distribution channels, including business-to-business, direct-to-consumer ("DTC"), e-commerce retailers, and club, department store, drug, grocery and sporting goods retailers.[57] In 2014, Jarden committed to expanding its DTC operations by promoting then-Vice President of International Development, Leo Trautwein, to Vice President of Direct to Consumer and Revenue Development. Trautwein, along with Jarden management, developed a DTC Council that comprised of representatives from Jarden and each of its individual business units.[58] The DTC Council aimed to detect DTC best practices and put in place DTC initiatives.[59] It set meaningful benchmarks to enhance DTC sales.[60] In their July 2015 Board presentation, Jarden management expected online sales to represent 13% of Jarden's total sales by 2019, equating to 15.9% of total EBITDA.[61] The DTC initiative, on the other hand, was expected to yield a 55–60% return on investment.[62] As it turned out, from 2012 through 2016, Jarden's DTC e-commerce sales (i.e., not including brick and mortar DTC sales) experienced a more than 270% increase in five years—expanding from roughly $237 million to $643 million.[63]

E. Jarden Makes Two Major Acquisitions Just Prior to the Merger

Jarden completed two of the largest acquisitions in its history in 2015. In July 2015, Jarden acquired the Waddington Group, Inc. for approximately $1.35 billion.[64] Waddington manufactures plastic consumables for the $14 billion U.S. food sector market.[65] The acquisition was projected to yield revenue of $840 million in 2016 with an approximately 20% EBITDA margin.[66]

In November 2015, Jarden acquired the parent company of Jostens, Inc. for $1.5 billion.[67] Jostens was a market leader in manufacturing and marketing yearbooks, rings, caps and gowns, diplomas, regalia and varsity jackets, mainly selling to schools, universities and professional sports leagues.[68] Jarden predicted the Jostens acquisition would not only offer Jarden "unique access to the difficult-to-enter academic market,"[69] but also would allow Jarden to grow a number of its existing distribution channels and develop new ones, intensifying Jarden's DTC impact.[70] Jostens provided superior market positions, steady financial performance, strong margins and attractive cash flow to Jarden's portfolio.[71] Indeed, Jostens' gross margins were anticipated to better Jarden's overall margins and, in fact, the transaction was instantly accretive.[72]

***7** Overall, Jarden anticipated that these two acquisitions would push Jarden's total annual revenues over the $10 billion threshold. At the same time, however, they simultaneously would increase Jarden's debt to a point where Jarden would be unable to make another substantial acquisition for at least another year.[73]

F. Franklin Considers a Sale of Jarden

Jarden was not Franklin's only business interest. In 2013, Franklin founded Platform Specialty Products Corporation ("Platform"), a specialty chemicals production company, with financial backing from Bill Ackman.[74] In 2014, Franklin founded Nomad Foods Ltd. ("Nomad"), a frozen foods company headquartered in the U.K.[75] Franklin also ran a "family investment vehicle" called Mariposa Capital.[76] Mariposa entities often acquired orphan brands, like its acquisition of Royal Oak in 2016.[77] In 2017, after the Merger, Franklin created a special purpose acquisition vehicle, J2 Acquisition Limited ("J2"), that raised more than $1 billion in order to buy consumer-focused brands.[78] Franklin also looked forward to pursuing business ventures with his sons, as his father did with him.[79]

In early July 2015, during a meeting between Franklin and Roland Phillips of Centerview Partners relating to Nomad, Phillips mentioned that Newell's CEO, Michael Polk, wanted to meet Franklin.[80] As discussed below, Newell had previously retained Centerview to assist with Newell's search for transformative M&A opportunities.[81] Understanding that Polk would likely want to talk about a Newell/Jarden transaction, Franklin told Phillips he would take the meeting, he "would gladly take equity, [and he] ha[d] no issue with someone else running the combined business."[82]

Later that month, Franklin met with Bill Ackman, his Platform partner, and expressed his willingness to sell Jarden so he could devote more energy to Platform and Nomad.[83] Ackman emailed Warren Buffett the following day and indicated that Franklin would entertain a negotiated sale of Jarden to Berkshire Hathaway.[84]

Franklin was not authorized by the Board to entertain discussions regarding a sale of Jarden nor did he disclose to the Board his discussions with Phillips or Ackman.[85]

G. Newell and Franklin Meet

***8** Like Jarden, Newell was a major consumer products company with a vast portfolio of products sold under brands like Sharpie, Paper Mate, Elmer's, Rubbermaid, Lenox, Graco and Baby Jogger.[86] In 2011, Newell implemented a strategic roadmap known as the "Growth Game Plan" under the direction of its new CEO, Polk.[87] This plan incorporated an initiative known as "Project Renewal" to streamline the Company's business structure and decrease costs.[88]

For many years, Newell operated as a traditional holding company, much as Jarden did, owning several portfolio businesses that essentially functioned as independent companies.[89] In 2010, Newell retooled by implementing an integrated operating company model as contemplated by Project Renewal.[90] Newell "delayered the structure of the company, ... releas[ing] a whole bunch of money" that was invested back into Newell's brands.[91] As a result, Newell doubled its brand expenditures, creating fast-tracked growth and amplified margins for its business.[92] By the fall of 2014, Newell realized that the "investment firepower" Project Renewal generated "was going to wane" by late 2018.[93] It needed a new growth plan.

In late 2014, Newell initiated a strategy of pursuing "transformational M&A" opportunities that would generate larger scale and market share in its central businesses, in addition to new prospects for growth.[94] This new strategy prompted Newell to engage Centerview to produce a list of possible targets for Newell and to arrange "get-to-know-you meetings" as requested.[95] While Jarden was included on Centerview's list, it was the target "least familiar" to Newell since it "had been built [steadily] through acquisitions from 2001 onward" and was, therefore, in Newell's eyes, a "relatively new company."[96] Polk had reservations about Jarden because it was seen as a "company of diversified niche categories," when Polk was "looking for scaled brands and big, global categories." [97] Even so, Polk asked Centerview to arrange the "get-to-know-you meeting" with Franklin. [98] As noted, Franklin agreed to take the meeting. [99]

Franklin and Polk's first meeting took place at the Barclays' investor "Back-to-School" conference on September 9, 2015 (the "Back-to-School Meeting"). [100] The conversation exposed their different perspectives regarding the roles they played at their respective companies—Franklin defined his role at Jarden as creating value and "[t]hat's it," while Polk defined his role at Newell as building stronger brands and a stronger company. [101] In other words, Franklin focused on M&A, while Polk concentrated on organic growth. [102] Near the meeting's end, Franklin directed the conversation to where he believed Polk wanted it to go by confirming that his team was open to "strategically connecting" with Newell. [103] The meeting closed with both Franklin and Polk agreeing to continue the conversation about a potential deal. [104]

***9** Polk reported back to the Newell board that Franklin "cut straight to the chase about being willing to sell his company and offered a deeper discussion over the next few weeks." [105] At this point, however, Franklin still had not informed Jarden's Board that he was entertaining Newell's overture. [106] Indeed, it was not until several days after the Back-to-School meeting that Franklin made individual calls to members of the Board to let them know about his discussions with Polk. [107]

For his part, Polk warmed quickly to the idea of acquiring Jarden, believing that Jarden would provide scale and immediate cost synergies once Newell consolidated Jarden's operations per Project Renewal. [108] As Polk explained, "we believed we had the potential, based on what we could see through the public data, to apply the playbook we'd just run on Newell Rubbermaid to a broader set of categories that looked very similar to the categories that we were managing as part of [Newell]." [109]

On October 5, 2015, Franklin and Polk met again, this time on Franklin's yacht in Miami, along with Ashken, Lillie and Mark Tarchetti, Newell's then-Chief Development Officer (the "Boat Meeting"). [110] While Franklin informally provided some advance notice of the Boat Meeting to certain members of the Board, he did not obtain Board approval to meet with Newell and certainly did not have Board approval to discuss the financial parameters of a deal. [111] But that is precisely what he did.

***10** Franklin advised Newell's team that Newell's offer for Jarden would have to "start with a six" and would have to include a significant cash component if Newell's goal was to gain control of the combined company. [112] According to Franklin, he arrived at this number based, in part, on his understanding of Jarden's value as determined in connection with the Jostens acquisition which was underway as of the Boat Meeting. [113] He also wanted to state a number he believed Newell had the "ability to pay," [114] and he assumed a price of $70.00 or higher was "laughable." [115] At the time of the Boat Meeting, Jarden's stock was trading in the high $40s. [116] Therefore, by this metric, a price "starting with a six," by any measure, would be a premium for Jarden's stockholders. [117] According to Franklin, even if $60 per share undervalued Jarden, [118] Franklin believed Jarden stockholders would reap additional value by sharing in the upside of the Merger with stock in the combined company. [119]

On the other side of the table, Polk expressed Newell's hope that a merger would open substantial synergies given the Newell team's demonstrated ability to consolidate business functions and utilize the resulting cost savings to produce growth. [120] Jarden's team had a more modest outlook on possible synergies in the early stages of the discussions, but became progressively more "excited" by the opportunity to unlock significant transaction synergies as the negotiations advanced. [121]

Although he had not sought Board approval to meet with Newell, Franklin briefed the Board on the Boat Meeting within a matter of days, including his admonition to Newell that an offer would need to "start with a six." [122] The Board was supportive and encouraged Franklin and his team to continue the discussions with Newell within Franklin's outlined parameters. [123]

Jarden did not formally engage Barclays until November 2015. Even so, Franklin contacted Welsh, his personal Barclays banker, on October 16, 2015, after the Boat Meeting. [124] Franklin told Welsh he already signaled to Newell that Jarden would agree to sell at $60 per share and instructed him to start developing an analysis supporting a transaction in the range of $60–$69 per share. [125]

H. The Ebb and Flow of the Negotiations

***11** On October 9, 2015, Newell distributed a press release revealing that Tarchetti and another executive would leave Newell at the end of the year. [126] Franklin was "very upset" Polk had not informed him that "his chief lieutenant" was on his way out of Newell. [127] Franklin was so upset, in fact, that he entertained the idea of "stopping the conversations at that point" because he "didn't want to look stupid in front of [the Jarden] board ... [by] having a conversation with someone that wasn't serious." [128] Within days of the announcement, Franklin and Polk had a "tough conversation" where Polk explained that Tarchetti would stay with Newell if the parties agreed to a deal. [129] After this, Franklin "got over it" and negotiations continued. [130]

As the parties were discussing a Jarden/Newell combination, Jarden was closing the Jostens deal. On October 14, 2015, Jarden announced it would acquire Jostens and finance the acquisition through an equity offering priced at $49.00 per share and additional debt. [131] The next day, Jarden presented five-year projections to potential financing sources that reflected net sales growth of 3.1% (the "Lender Presentation"). [132]

The market reacted negatively to the Jostens acquisition. [133] Jarden's stock price dropped approximately 12% over the following two weeks and analysts' reduced their Jarden price targets accordingly. [134] The Board determined that Jarden needed to project confidence to the market. Accordingly, in early November 2015, it approved a stock buy-back up to $50 million at prices capped at $49.00 per share. [135] Jarden ultimately repurchased 276,417 shares on November 2, 2015, at an average price of $45.96 per share, and repurchased an additional 775,685 shares on November 3, 2015, at an average price of $48.05 per share. [136]

On October 15, 2015, Franklin caused Jarden to enter into a mutual confidentiality and standstill agreement with Newell, and the parties began preliminary due diligence. [137] True to form, Franklin did not seek Board authorization to begin diligence on Jarden's behalf. [138] The next day, also without the Board's authorization, Franklin and Polk spoke on the phone to continue negotiations on the cash and stock components of a deal, and Franklin introduced the concept of Jarden taking seats on the combined company's board. [139]

On October 22, 2015, Franklin, Ashken and Lillie met with Newell representatives at Jarden's offices in Norwalk, Connecticut (the "Norwalk Meeting") and shared non-public information, including a set of three-year financial projections. [140] The three-year projections, apparently created in connection with the negotiations, incorporated financials for both the Waddington and Jostens acquisitions, [141] and forecast 5% revenue growth, i.e., growth at the high end of Jarden's historic guidance range of 3% to 5%. [142]

***12** Entering into negotiations with Newell, Jarden had set the market standard for average annual revenue growth within the 3% to 5% range. [143] These growth figures were meant to reflect Jarden's "organic growth" range, but they included revenue from "tuck-in" acquisitions, where a Jarden portfolio company would acquire a target. [144] Other public companies operating as holding companies typically do not include tuck-in acquisitions when projecting "organic growth." [145] Nevertheless, even when tuck-in acquisitions are excluded, Jarden generally performed in line with its target growth range. [146]

At trial, Lillie justified giving Newell projections at the very top of the Company's 3%–5% guidance range by explaining that 5% was a "round number[ ]." [147] He went on to explain that, while the projections given to Newell were not "wildly optimistic," Jarden internally projected growth "in the fours." [148] Polk took notice of Jarden's "really aggressive" projections. [149] He and his team determined that it was best to stick with the 3.1% growth projections as stated in the Lender Presentation when evaluating the transaction. [150]

In November 2015, Jarden's financial advisor, Barclays, asked Jarden management for projections extended to 2020. [151] In response, Lillie told Barclays to "extrapolate out" the three-year forecast at a continuing growth rate of 5% (the "November Projections"). [152] Barclays used these five-year projections in its analyses of the potential transaction and in its fairness opinion. [153]

In addition to negotiating price terms during the Norwalk Meeting, Newell and Franklin began to discuss specifics regarding change-in-control payments that would be due to Franklin, Ashken and Lillie in the event of a merger.[154] And, again, Franklin did not seek Board approval before undertaking these discussions.[155]

Following the Norwalk Meeting, Franklin, Ashken, Lillie and John Welsh of Barclays on behalf of Jarden, and Polk and Tarchetti on behalf of Newell, met for dinner.[156] Franklin believed whether the transaction would be consummated depended on whether Tarchetti stayed at Newell.[157] Accordingly, he asked Tarchetti to share his thoughts on the potential transaction.[158] Tarchetti declined to respond, explaining he believed Newell still lacked adequate information to evaluate the transaction.[159] Franklin was not happy.

***13** After this "difficult dinner" among the negotiators, Franklin told Ashken and Lillie, "I'm done. I don't want to deal with this."[160] Likewise, Polk said he thought about "pull[ing] the plug" on the negotiations.[161] After a "conciliatory" call between Lillie and Tarchetti, however, the parties decided not to "let a bad dinner get in the way of looking at whether this makes sense[,]" and negotiations continued.[162]

The Board held its first formal meeting to discuss a potential Newell transaction on October 28, 2015.[163] There was no discussion of a pre-signing market check.[164] Instead, the Board focused its attention on Newell and directed that negotiations continue.[165]

In the meantime, Newell retained both Goldman Sachs ("Goldman") and Bain & Company ("Bain") as additional financial advisors to assist in evaluating a possible acquisition of Jarden.[166] Tasked with performing a thorough evaluation of Jarden's product categories, Bain's initial assessment was that Jarden's portfolio demonstrated strong performance across many promising product segments,[167] but its historic organic growth rate, once "tuck-in" acquisitions were separated, was at most 3.5%.[168] Early in the process, Centerview had projected that potential synergies of $500 million to $900 million would result from a combination with Jarden.[169] By the end of October 2015, Bain was estimating that the combination had the "potential to create $700M–$800M in cost synergies."[170] Bain's assessment encompassed "annualized savings" that would recur annually.[171]

Through due diligence, Newell discovered "almost every deal Jarden had done, which were profound in number, had been left standalone with almost no cost synergies or revenue synergies realized."[172] As a result of this holding company structure, Newell and its advisors believed that Jarden presented a substantial opportunity to replicate Newell's Project Renewal success by combining Jarden's businesses into Newell's operating company structure.[173]

I. Newell Makes an Offer and Jarden Negotiates

***14** On November 10–11, 2015, the Newell board met to discuss, among other things, whether to make an offer to acquire Jarden.[174] On the first day, Tarchetti presented the results of the diligence efforts so far, in addition to management's perspective on the benefits of a merger with Jarden.[175] On the second day, Bain and Goldman presented their analysis of potential synergies.[176] Bain opined that the potential Newell/Jarden "combination would enable ~ $600M in cost savings opportunities, with potential upside to ~$700M."[177] Goldman appraised cost synergies based on comparable transactions ranging from 2.1% to 14.0% of revenue, with a median of 10.0%, translating to roughly $850 million of annual cost synergies resulting from the acquisition.[178]

Despite Bain and Goldman's synergies estimates, Newell and its advisors structured their deal model on an estimate of $500 million in annual cost synergies.[179] With this estimate, Newell's model priced Jarden at $57.00 to $61.00 per share.[180] Within these parameters, the Newell board understood that if its management team did not realize the $500 million synergies estimate, then Newell shareholders would not receive any increase in EPS.[181] After the advisors' presentations, the Newell board authorized management to negotiate an acquisition of Jarden at a price between $57.00 and $60.00 per share, with cash consideration up to $21.00 per share.[182]

On November 12, 2015, Polk sent Franklin an offer whereby Newell would acquire Jarden in a cash-and-stock transaction consisting of $20.00 cash plus a fixed exchange ratio of 0.823 Newell shares for each share of Jarden common stock, representing total per share consideration of $57.00. [183] The offer reflected an 18% premium over Jarden's then-current share price ($48.19) and a 19% premium to Jarden's 30-day volume-weighted average share price ($47.89). Newell arrived at the cash and stock mix to preserve Newell's investment grade credit rating and dividend policy. [184] Polk's offer letter made clear that Newell "expect[ed] that Mr. Franklin would join the Newell Brands Board of Directors given the role he has played in Jarden's performance and strategy to date," and allowed that Newell was "open to adjusting the size of our board and taking on a limited number of [additional] members from Jarden's board." [185]

The Board met that day to discuss Newell's offer. [186] Barclays made a presentation regarding the adequacy of Newell's $57.00 offer in which it provided a preliminary valuation of Jarden based on Jarden's historic market price as well as comparable companies, precedent transactions and DCF analyses. [187]

While the $57.00 per share offer was higher than Jarden's stock had ever traded, the Board unanimously decided "it was not inclined to engage in discussions and possible negotiation with [Newell] on the economic terms set forth in the [offer] [l]etter," and authorized management to "seek to obtain a revised proposal with more favorable proposed terms." [188] The Board "emphasized that the Company was not for sale and that it would consider a potential business combination with [Newell] only on terms that appropriately valued the relative contribution (including revenue and EBITDA) of each standalone company to the pro forma combined company." [189]

***15** The Board authorized Franklin to continue negotiations with Newell, but did not authorize him to make a counteroffer because, as director Robert Wood testified, doing so would "tie their hands." [190] Franklin, however, recalled, "the board basically authorized [him] to go back and have further discussions and ... push the envelope to try to come back to them with an enhanced offer from Newell." [191]

During the November 12 Board meeting, Franklin suggested that the Board formally engage Barclays as the lead banker for the Company and UBS Group AG as "co-investment banker." [192] Jarden thought a transaction of this magnitude justified having two banks on board to guide the Company through the process. [193] Barclays, in particular, had a longstanding, fruitful relationship with Franklin and it knew Jarden well. [194] Accordingly, Franklin believed Barclays was positioned to provide Jarden with "genuine good advice" on the potential merger. [195] And he believed UBS would serve as a well-informed source for "second opinions." [196] The retention of UBS, however, did cause Jarden director Ros L'Esperance to recuse herself from all deliberations and votes of the Board, as she led UBS's Client Corporate Solutions Group. [197]

***16** On November 16, 2015, Jarden and Newell, along with their financial advisors, met to continue negotiations over the potential transaction. [198] In advance of the meeting with Newell, the Jarden management team scheduled an evening Board dinner anticipating there would be new developments in the negotiations that would require the Board's prompt attention. [199] In yet another demonstration of Franklin getting ahead of his Board, Franklin announced to the Newell team at the outset of the meeting that their $57.00 offer was too low and then made a counteroffer of $63.00 per share—$21.00 in cash with the balance in stock of the combined company. [200] The Newell team balked. Not only did they decline the counteroffer on the spot, they also refused to raise their $57.00 offer. [201] Discussions turned "acrimonious" and the meeting abruptly adjourned. [202]

After the meeting, Ashken emailed the Board to advise that the parties were at impasse and there was no need for the scheduled Board dinner. [203] According to Ashken, "[a]s far as we were concerned the deal was dead." [204]

J. Newell Increases Its Offer

On November 21, 2015, Newell submitted a revised offer to acquire Jarden for $21.00 in cash plus a floating exchange ratio between 0.85 to 0.92 Newell shares for each Jarden share to be determined based on Newell's trailing 10-day unaffected volume weighted average price ("VWAP") at the time of signing, with a target price of $60.00 per share. [205] This revised proposal was a 30% premium over Jarden's then-current stock price ($46.33) and a 27% premium over Jarden's 30-day VWAP ($47.43). Newell reiterated that it expected the potential merger to produce annual cost synergies of approximately $500 million. [206] It also renewed its offer for

Franklin, Ashken, Lillie and a new independent director to join the board of the combined company. [207]

The Board convened the following day to discuss the $60.00 per share offer. After discussions with its financial advisers, the Board determined that the offer would be accepted and that Newell would be granted exclusivity during a period of confirmatory due diligence. [208] Outside director Robert Wood testified that the Board viewed the revised offer "much more favorably," [209] and explained that while the Board thought Jarden's forecast of 5% growth over the next three years was achievable, "the [B]oard's level of concern [regarding future growth] was higher" following recent acquisitions. [210] Specifically, the Board had come to appreciate that Jarden could not sustain historic growth without pursuing "bigger and bigger acquisitions," a strategy the Company had found was increasingly difficult to execute. [211] As a result, Wood and the other directors believed the $60.00 offer provided more value for shareholders than Jarden could deliver as a standalone company. [212]

***17** Franklin believed the $60.00 offer represented a 13.5x EBITDA multiple, "a high multiple, by any standard, for our business ... [and] the highest multiple, by far, our company would have ever traded or been valued." [213] By way of comparison, just a few weeks before Newell delivered its revised offer, Jarden had acquired Jostens for $1.5 billion, representing a 7.5x EBITDA multiple. [214] The Board also concluded that Jarden stockholders stood to benefit from any synergies on top of the $500 million estimate baked into the purchase price, by remaining invested in the combined company following the Merger. [215]

As noted, the Board agreed to mutual exclusivity. [216] This, of course, disabled any market check prior to consummation of the Merger. [217] The Board thought "Newell was the best and most likely acquirer of our business" and there were no other "companies that had the same fit in terms of synergies and ability to pay as Newell." [218] From the Board's perspective, Jarden was a "very diverse business" operating in siloed industries that were not of interest to other large consumer product companies. [219] Accordingly, the Board and management understood that Jarden would likely continue standalone unless a unique opportunity for a business combination came along. [220] Newell provided that opportunity.

K. Jarden and Newell Finalize Deal Documents

Over November 29 and 30, 2015, Jarden and Newell convened at Jarden's Norwalk, Connecticut offices, where the Newell team continued its diligence and presented its strategic plan for the combined company. [221] Both Newell and Jarden knew from the outset that a deal could only be done if a substantial portion of the consideration was Newell stock. [222] Because Newell understood this and appreciated the magnitude and significance of Jarden's assets to the combined company, Newell committed that certain Jarden directors would be offered a seat on the Newell board post-closing. [223] Newell specifically wanted Franklin to sit on the combined board to provide a positive signal to the market of his confidence in the future of the combined company. [224]

***18** The parties understood that Newell's management team would lead the combined company since capturing synergies through the implementation of Project Renewal was the "logic for the deal." [225] Franklin, Ashken and Lillie each were subject to two-year non-competition covenants in event they were terminated following a change of control. [226] Newell wanted to draw out these non-competition covenants to four years. [227] It also wanted to have access to Franklin, Ashken and Lillie as consultants post-closing if needed. [228] Accordingly, Newell, Franklin, Ashken and Lillie negotiated an "Advisory Services Agreement" that extended their non-competes but also provided for Mariposa (on behalf of the three executives) to be paid an annual consulting fee of $4 million for three years ($12 million in total). [229] The Advisory Services Agreement provided that Mariposa "shall, upon the request of [Newell], devote up to an average of 120 hours per fiscal quarter" to Newell, and that Franklin and Ashken waived "any and all fees and compensation" they would have ordinarily received as directors of Newell during the term of the agreement. [230]

L. The Leak

On December 7, 2015, *The Wall Street Journal* reported that Newell and Jarden were discussing a potential business combination, though the article did not reveal the specifics of who would be buying whom or the transaction consideration. [231] In reaction to this news, Newell's shares traded up 7.4%, closing at $48.16 and Jarden's shares traded up 3.7%, closing at $50.09.[232]

Following the leak, and resulting impact on the companies' stock prices, the parties agreed that it no longer made sense to calculate the final exchange ratio based upon the 10-day trailing VWAP as of the day of signing.[233] Ashken contacted Tarchetti to re-negotiate and the parties ultimately settled on a fixed ratio of 0.862,[234] resulting in total merger consideration at that time of $60.03 based upon Newell's closing stock price on December 11, 2015.[235]

The 10-day trailing VWAP through the last unaffected day prior to the leak, was $44.60.[236] If Jarden held firm to the original agreement, on top of the $21.00 in cash, Jarden stockholders would have received 0.874 shares of Newell stock for every share of Jarden stock they owned.[237] In other words, Jarden stockholders would have received $120 million more in consideration if not for the renegotiation.

M. Jarden and Newell Stockholders Approve the Merger

***19** On December 10, 2015, the Board met to discuss the status of negotiations and to assess whether the transaction continued to make sense. Lillie opened the meeting by presenting the 2015 estimated financial results that demonstrated 4.4% growth in organic net sales over 2014.[238] Barclays also presented a summary of the transaction's proposed terms and an analysis of Jarden's standalone value.[239] The meeting minutes emphasize that “the Company has not been and is not currently for sale and that remaining independent (as a standalone entity) is the sole alternative to the proposed business combination with Newell, which offers unique revenue and cost synergies and long-term value accretion opportunities for the Company's stockholders.”[240]

Jarden's negotiating team had been discussing change of control payments with Newell for several weeks but raised the subject with the Board for the first time at the December 10 meeting.[241] Ashken recommended to the Board that he, Franklin and Lillie receive their 2017 and 2018 Restricted Stock Awards (“RSAs”) should the transaction with Newell be approved.[242] The RSAs would not have been due under the existing employment agreements but Franklin's team instructed Barclays to include the RSAs in the shares outstanding calculation used for its valuation analyses of the transaction and they had already presented that share calculation to Newell.[243] John Capps, Jarden's General Counsel, advised the Board that Jarden was legally obligated to grant the RSAs even though the agreements themselves were, at best, ambiguous on the point.[244] Ultimately, the Board's Compensation Committee recommended that the Board award the 2017 and 2018 RSAs.[245]

The Board met next on December 13, 2015. Barclays presented the revised proposed deal terms and its revised valuation of Jarden as a standalone company.[246] Barclays also orally presented its opinion that the proposed merger was fair from a financial point of view to Jarden and its stockholders.[247] After hearing from Barclays and reviewing the final deal terms, the Board approved the Merger.[248] The Board also approved the separation agreements and amendments to the employment agreements with Franklin, Ashken and Lillie.[249] The final Merger Agreement provided that Jarden stockholders would receive 0.862 shares of Newell stock plus $21.00 in cash for each Jarden share, representing a value as of signing of $60.03.[250]

***20** The Newell board also met on December 13 to consider the final transaction terms and to receive Goldman and Centerview's final presentations.[251] In their analyses, both Goldman and Centerview used five-year projections for Jarden, assuming 3.1% revenue growth during FY18–20, consistent with the Lender Presentation and below the 5% revenue growth forecast in the November Projections.[252] Goldman maintained its estimate of $500 million in annual cost synergies.[253] Centerview estimated $500–$700 million in synergies.[254] After the presentations by its advisors, the Newell board approved the terms of the final Merger Agreement and the parties announced the Merger.[255]

N. The Market Reacts

The Merger announcement, released on December 14, 2015, stated “[Newell] anticipates incremental annualized cost synergies of approximately $500 million over four years.”[256] In response to the announcement, Jarden's stock price closed at $54.09, roughly 12% above the unaffected trading price of $48.31 from December 4, 2015.[257] The delta between Jarden's stock price and the implied Merger Price (i.e., the merger arbitrage spread) slowly narrowed following the announcement and ultimately converged in the days leading up to the closing.[258]

Newell's stock price rose 7.4% on December 7, 2015, when financial media outlets first reported the parties were negotiating.[259] When the final terms of the transaction were made public on December 14, 2015, however, Newell's stock price declined by 6.9% to $42.15.[260] After accounting for market fluctuations, Newell's stock price after the announcement of the Merger terms reflected, at best, a neutral market response.[261]

On February 26, 2016, Jarden reported its 2015 year-end results, including a considerable loss in operating income and net income as compared to the prior two years.[262] A few days later, on February 29, 2016, Lillie shared weak results for the first quarter of 2016 with the Board.[263] Lillie also shared the final 2016 budget, which was adjusted downward to reflect year-end revenue of $9.79 billion (as compared to the $10.15 billion in the November Projections).[264]

***21** During March and April 2016, before the Merger closed, Jarden management prepared updated multi-year projections for the period 2016 to 2020 (the "April Projections").[265] The original version of the April Projections reflected a "bottoms up build" from the business units and forecast a 4.4% compound annual revenue growth rate.[266] This was well below the 5.0% forecast in the November Projections.[267]

Jarden and Newell stockholders voted to approve the Merger on April 15, 2016.[268] As of the closing, the mix of cash and Newell shares valued Jarden at $59.21 per share.[269]

O. Post-Closing

By January 2016, Bain shortened the time Newell would realize $500 million in recurring annual cost synergies from four years to three.[270] By May 2016, Bain raised its projection of potential cost savings to a range of $900 million to $1 billion.[271] In February 2017, Newell announced it would meet the initial estimate of $500 million in annual cost synergies by Q3 2018, and doubled the size of its total cost synergy target from $500 million to $1 billion, to be reached by 2021.[272] Newell also announced its intention to divest several businesses—both historical Jarden and Newell—and to exit certain product lines.[273] In early 2018, Newell announced it would sell businesses accounting for almost 50% of its customer base and approximately one-third of its revenue.[274]

The Jarden/Newell integration did not go smoothly.[275] Newell Brands (the combined company) faced an uphill battle with the divestitures of highly-profitable and valuable businesses.[276] In early 2018, Franklin resigned from the Newell Brands board in spectacular fashion, publicly proclaiming that Polk was "ruining the company" and calling for Polk's ouster.[277] Ashken, L'Esperance and long-time Newell director, Dominico De Sole, left the Newell Brands board soon after.[278]

***22** After leaving, Franklin, Ashken and Lillie united with Starboard Value LP, an activist hedge fund, to advance a slate of directors to challenge the Newell Brands board.[279] Carl Icahn entered the mix and ultimately was successful in placing his slate of five directors on the Newell Brands board, thereby effectively ending the Franklin/Starboard-led challenge.[280] In the fallout of the proxy contest, Tarchetti, President of Newell Brands, resigned.[281]

P. Procedural Posture

Between June 14, 2016 and August 12, 2016, four petitions for appraisal were filed in connection with the Merger.[282] By order of the Court dated October 3, 2016, the four appraisal actions were consolidated.[283] On July 5, 2017, Merion Capital LP, Merion Capital II LP and Merion Capital ERISA LP were dismissed from the consolidated action after reaching settlement agreements with Jarden.[284] On July 7, 2017, Dunham Monthly Distribution Fund, WCM Alternatives: Event-Driven Fund, Westchester Merger Arbitrage Strategy sleeve of the JNL Multi-Manager Alternative Fund, JNL/Westchester Capital Even Driven Fund, WCM Master Trust, The Merger Fund, The Merger Fund VL and SCA JP Morgan Westchester were also dismissed, again after reaching settlement agreements with Jarden.[285]

The Court held a four-day trial in June 2018. Three experts testified. For Petitioners, Dr. Mark Zmijewski evaluated the standalone value of Jarden on the Merger Date by conducting a market multiples analysis and a DCF analysis, ultimately relying on his multiples (comparable company) analysis for his fair value conclusion. He opined that Jarden's fair value on the Merger Date was $71.35 per share. Dr. Zmijewski holds the Charles T. Horngren Professorship at the University of Chicago Booth School of Business.

For Respondent, Dr. Glenn Hubbard evaluated the standalone value of Jarden on the Merger Date by analyzing market evidence, including Jarden's unaffected market price and the Merger Price less synergies, and traditional valuation methodologies, including comparable companies and DCF. Based on his DCF analysis, which he correlated to the market evidence, Dr. Hubbard opined that Jarden's fair value on the Merger Date was $48.01 per share. Dr. Hubbard holds the Russell L. Carson Professorship in Finance and Economics in the Graduate School of Business of Columbia University, where he is also the Dean.[286]

Respondent also presented the testimony of Dr. Marc Zenner, a retired investment banker. Dr. Zenner testified that the projected synergies estimates reported in the joint proxy statement issued by Jarden and Newell in connection with the Merger were conservative and that the synergies were taken by Jarden stockholders. He also opined that the Board's decision not to hold an auction for Jarden was reasonable because Jarden's size and diverse product portfolio made it unlikely that a merger partner more suitable than Newell would have emerged.

***23** Following post-trial briefing and argument, the Court wrote to the parties, as previewed at the conclusion of post-trial oral argument, to advise that it would postpone the issuance of its post-trial opinion in this case until our Supreme Court issued its decision in *Aruba*.[287] The parties submitted brief (and unsolicited) letters regarding *Aruba* on April 30 and May 1, 2019, at which time the matter was submitted for decision.

II. ANALYSIS

Delaware's appraisal statute, 8 *Del. C.* § 262(h) provides, in part:

> Through [the appraisal] proceeding, the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors.[288]

"Section 262(h) unambiguously calls upon the Court of Chancery to perform an independent evaluation of 'fair value' at the time of a transaction ... [and] vests the Chancellor and Vice Chancellors with significant discretion to consider 'all relevant factors' and determine the going concern value of the underlying company."[289] "By instructing the court to 'take into account all relevant factors' in determining fair value, the statute requires the Court of Chancery to give fair consideration to 'proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court.' "[290] Since " '[e]very company is different; [and] every merger is different,' the appraisal endeavor is 'by design, a flexible process.' "[291]

I have carefully considered all relevant factors. I have weighed those factors according to the credible evidence in the record and applied "accepted financial principles" as derived from that evidence.[292] To follow is my independent evaluation of Jarden's fair value as informed by my findings of fact.

A. Merger Price Less Synergies

Respondent has proffered the Merger Price less synergies as a reliable indicator of fair value, and for good reason. Our Supreme Court has stated, "a buyer in possession of material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller when agreeing to buy the company at a particular deal price, and that view of value should be given considerable weight by the Court of Chancery absent deficiencies in the deal process."[293] This court has heeded the Supreme Court's guidance and regularly rests its appraisal analysis on the premise that when a transaction price represents an unhindered, informed and competitive market valuation, that price "is at least first among equals of valuation methodologies in deciding fair value."[294]

In *PetSmart*, I observed, "[a]fter years of striving for it, Vince Lombardi finally arrived at the understanding that perfection in human endeavors is not attainable."[295] "Even in the best case, a process to facilitate the sale of a company, constructed as it must be by the humans who manage the company and their human advisors, will not be perfect."[296] With that said, I am mindful of our Supreme Court's guidance in *Dell*, where the Court observed that certain factors, including "fair play, low barriers to entry, [and] outreach to all logical buyers," are reflective of the kind of "robust sale process" that will discover a company's fair value.[297]

***24** The "sale process" for Jarden, if one can call it that, raises concerns. To be sure, there was no need for a full-blown auction of Jarden. In this regard, Dr. Zenner's testimony, corroborated by other evidence, was credible.[298] Moreover, there were signs of arms-length, provocative negotiating between Jarden and Newell.[299] This is not surprising given that Jarden's negotiators owned millions of Jarden's shares and had every incentive to negotiate a good deal.[300] But the evidence revealed a troubling theme. Franklin immediately took charge and, consistent with a stereotypical "cut to the chase" CEO mentality,[301] he laid Jarden's cards on the table before the negotiations began in earnest and before the Board and its financial advisors had a chance to formulate a plan. Petitioners are right to complain that Franklin's approach may well have set an artificial ceiling on what Newell was willing to pay.

Franklin did not inform the Board he was meeting with Polk at the Back-to-School Meeting or the Boat Meeting, and he certainly did not receive authority from the Board to suggest a price ("beginning with a 6") at which the Board might agree to sell the Company.[302] Franklin made counteroffers unauthorized by the Board.[303] He negotiated his change-in-control compensation with no authorization from (or knowledge of) the Board.[304] And he recommended Barclays as the lead financial advisor for the deal without fully disclosing his prior substantial relationship with the bank, just as he nudged the Board to hire UBS as a second banker as a "kiss" in gratitude for its prior uncompensated work for the Company.[305]

***25** As factfinder, these flaws in the sale process, coupled with the fact that there was no effort to test the Merger Price through any post-signing market check, raise legitimate questions regarding the usefulness of the Merger Price as an indicator of fair value.[306] As explained below, the difficulty in assessing the extent to which Newell ceded synergies to Jarden in the Merger makes the Merger Price less synergies an even less reliable indicator of fair value.

In *Merion Capital LP v. BMC Software Inc.*, the court set forth a useful framework to approach the appraisal statute's mandate that the court appraise "the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation."[307] *BMC* recommends a "two-step analysis[:]" "first, were synergies realized from the deal; and if so, were they captured by the sellers in the deal price?"[308]

There is no dispute here that synergies were realized in the Merger, as one would expect when two strategic partners combine.[309] Indeed, the synergies created the "logic for the deal" from Newell's perspective.[310] The first announcement of the Merger stated, "[Newell] anticipates incremental annualized cost synergies of approximately $500 million over four years."[311] This remained the case through the release of the joint proxy statement.[312] Internally, Newell believed the $500 million estimate was conservative.[313] Nevertheless, the experts have focused on the expected synergies as disclosed in the joint proxy statement ($500 million), and they have assumed that estimate is accurate.[314] In the absence of any real expert analysis of the issue, I have no basis in the evidence to depart from that assumption.

As for whether Jarden captured the synergies in the Merger, the evidence is less clear. There is evidence in the trial record that would suggest Newell believed it was not paying any of the synergies at the $59.21 per share Merger Price.[315] During negotiations, Polk told his board that if Newell could "get the deal done between $60 and $65 [per share], we are basically getting the synergies with no value ascribed to them."[316] After the Merger, Polk further suggested that the premium over market price that Newell paid in the Merger was not for synergies but instead was for control of the combined company.[317] Polk explained, "Jarden shareholders get a premium versus their current stock price for [Jarden]. The Newell shareholders get ownership of [Jarden], and after the synergies are delivered, the future value creation that comes through the new combination."[318] Even Franklin questioned whether the premium to market price that Newell paid was for control of the combined entity.[319]

***26** On the other hand, Jarden points out that there is evidence Newell was keenly aware of synergies and that it was incorporating synergies into its value thesis for the Merger.[320] Dr. Hubbard supported Jarden's view of the evidence that Jarden stockholders realized the value of the synergies by conducting two separate analyses. First, he performed a "discounted value of cash flows" analysis, in which the expected future cash flows from the synergies (net of the costs to achieve them) were discounted to their value as of the Merger Date, to conclude that the synergies had a value of $4.2 billion, or $17.43 per Jarden share. This happens to line up nicely with the delta between the unaffected market price ($48.31) and the Merger Price ($59.21), indicating that the delta, or premium, represented expected synergies.[321] He then prepared a market-based analysis of the expected synergy value in which he observed that the rise in stock price of both companies after the leak of merger negotiations revealed that the market appreciated the presence of significant synergies. The fact that Newell's stock price fell when Jarden's rose after announcement of the Merger indicates the market appreciated that the anticipated synergies would accrue to the Jarden stockholders.[322]

Jarden bears the burden of demonstrating "what, if any, portion of [the synergies] value was included in the price-per-share ...."[323] The evidence on this point stands in equipoise. It is difficult to square Polk's contemporaneous assessment of where the synergies would land with Newell's internal valuation exercises and Dr. Hubbard's straightforward analysis of the issue. Given the state of the evidence, I give little weight to the Merger Price less synergies evidence when assessing fair value.[324] Not because I believe the Merger created no synergies. And not because I believe that Jarden stockholders probably did not receive the value of the synergies that were created by the deal. I place less weight on this market-based valuation approach in this case because the sales process was not well-conceived or well-executed and the expert analysis of the transaction synergies raised more questions than it answered.

B. Unaffected Market Price

Jarden has proffered its unaffected stock trading price, $48.31 per share (the "Unaffected Market Price"), as strong evidence of the Company's fair value.[325] According to Jarden, "[t]his value impounded the collective judgments of thousands of stockholders, as well as the more than twenty professional analysts that followed Jarden."[326] Jarden supports its position that the Unaffected Market Price is indicative of fair value with detailed analysis from Dr. Hubbard.[327] Petitioners elected not to counter that evidence with expert evidence of their own.[328] Instead, they attacked Dr. Hubbard's opinion as lacking in doctrinal and factual foundation. For reasons explained below, I find Dr. Hubbard's analysis of the reliability of Jarden's Unaffected Market Price as an indicator of fair value both credible and persuasive.

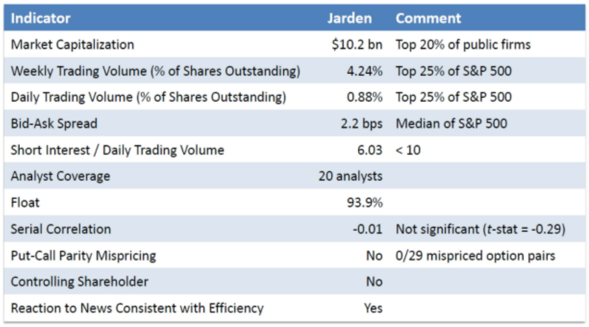
1. The Market for Jarden's Stock Was Efficient

***27** In an efficient stock market, "a company's market price quickly reflects publicly available information."[329] In this environment, the company's trading price "balances investors' willingness to buy and sell the shares in light of [available] information, and thus represents their consensus view as to the value of the equity in the company."[330] Efficient markets aggregate all available information and quickly digest new information, which is then reflected by proportionate changes in market price.[331] When the market is efficient, the trading price of a company's stock can be a proxy for fair value.[332]

As Dr. Hubbard explained, several factors support the conclusion that Jarden's stock traded in a semi-strong efficient market.[333] The stock was traded on the New York Stock Exchange ("NYSE") and Jarden became a member of the S&P 400 index in 2012.[334] In 2015, Jarden's shares traded with a daily and weekly average trading volume in the top 25% of the S&P 500.[335] High trading volume contributes to the efficiency of the market.[336] Jarden's market capitalization of approximately $10.2 billion placed it in the top 20% of all publicly traded firms.[337] High market capitalization leads to greater "interest in the security being analyzed," which, in turn, "increases the likelihood that new information will be quickly incorporated into the stock price."[338]

Jarden had no controlling shareholder.[339] In fact, Jarden had a 94% public float.[340] A high public float is another factor indicating an efficient market for Jarden's stock because the more holders of a security that are not insiders with access to non-public information, the more likely the market will demand that information be released for public consumption.[341] Jarden stock exhibited a "bid-ask spread" of only 0.02%.[342] A narrow bid-ask spread indicates minimal information asymmetry between insiders and the public markets and, as a result, higher market efficiency.[343] Approximately twenty professional market analysts covered and disseminated reports on Jarden in the year prior to the Merger Date.[344] Jarden exhibited no serial correlation, meaning there were no patterns detached from events or news from the Company that would enable the market to divine future price movements based purely on past performance.[345] Additionally, Jarden's Unaffected Market Price aligned with options market pricing, suggesting there were no arbitrage opportunities for Jarden stock.[346]

***28** Dr. Hubbard summarized the factors allowing him to conclude that Jarden's stock traded in a semi-strong efficient market in a helpful chart:



Indicator	Jarden	Comment
Market Capitalization	$10.2 bn	Top 20% of public firms
Weekly Trading Volume (% of Shares Outstanding)	4.24%	Top 25% of S&P 500
Daily Trading Volume (% of Shares Outstanding)	0.88%	Top 25% of S&P 500
Bid-Ask Spread	2.2 bps	Median of S&P 500
Short Interest / Daily Trading Volume	6.03	< 10
Analyst Coverage	20 analysts	
Float	93.9%	
Serial Correlation	-0.01	Not significant (*t*-stat = -0.29)
Put-Call Parity Mispricing	No	0/29 mispriced option pairs
Controlling Shareholder	No	
Reaction to News Consistent with Efficiency	Yes	

For context, and to illustrate that Jarden's stock price historically reacted appropriately to material information, Dr. Hubbard performed an event study to trace how, in the two years prior to the Merger, Jarden's stock price responded quickly and appropriately to earnings announcements and other performance guidance, even when the news was unanticipated.[347] In each instance, Dr. Hubbard traced the public disclosure of material information, the reaction of analysts to the information and the commensurate adjustment, up or down depending upon whether the news was positive or negative, in the trading price of the stock.[348]

The evidence shows that Jarden's stock reached a pre-Merger peak of $56.25 on July 20, 2015, and then declined gradually over the next few months in response to poor earnings reports.[349] The decline was marked by low quarterly growth and it prompted Jarden to lower its guidance for the second and third quarters of 2015.[350] Jarden's stock price recovered somewhat in the fourth quarter and closed at $48.31 on December 4, 2015 (i.e., the Unaffected Market Price).[351] After *The Wall Street Journal* article reported on the merger negotiations the following Monday, Jarden's stock price rose and continued to rise to $54.09 on December 14, 2015, the day Jarden and Newell officially announced the Merger.[352] The steady climb continued following the announcement and then plateaued before the calendar year ended.[353] Jarden's stock price oscillated between $59.00 and $50.00 until early March 2016.[354] In March, as the negotiations finalized and the Merger Date neared, Jarden's share price approached but never exceeded the Merger Price of $59.21.[355] As Dr. Hubbard explained:

> The fact that Jarden's stock price never closed above the Merger Price is a strong indicator that fair value is no greater than the Merger Price. If investors believed that the Company was worth materially more, then one would expect to see the market price exceeding the Merger Price in anticipation of a topping bid. In more than five percent of M&A deals since 2001, the merger arbitrage spread the day after the merger announcement was negative, implying that the market expected a topping bid.[356]

Newell's stock also traded in an efficient market and the market's reaction to the announcement of the Merger with respect to Newell's trading price provides further evidence that the Unaffected Market Price is reflective of Jarden's fair value.[357] Newell's stock price jumped after the leak of negotiations when the terms of the deal were unknown.[358] The market reacted differently, however, when the terms of the Merger were announced. Newell's stock price dropped significantly (6.9%). Dr. Hubbard explained the significance: "The initial positive reaction to the deal rumors suggests that the market was hopeful that some value would accrue to Newell, but after learning the terms of the deal and additional information about synergies, the market reassessed and shifted the value from Newell to Jarden." [359]

***29** After carefully reviewing the evidence, I am satisfied that Jarden's Unaffected Market Price is a powerful indicator of Jarden's fair value on the Merger Date. Petitioners' attempts to undermine this evidence, as explained below, were not persuasive.

2. Petitioners Did Not Persuasively Rebut Jarden's Market Evidence

Petitioners mount three challenges to the reliability of Jarden's Unaffected Market Price: (a) as of the date fixed for the Unaffected Market Price (December 4, 2015), the market lacked material information concerning Jarden (i.e., information asymmetry) that skewed the trading price; (b) the Unaffected Market Price must be adjusted to account for a so-called "conglomerate discount" and a "minority discount;" and (c) the Unaffected Market Price was stale by the time the Merger closed on April 15, 2016. [360] I address each in turn.

a. Information Asymmetry

According to Dr. Zmijewski, Jarden's market-based evidence should be disregarded because the market lacked material information as of the date fixed for Jarden's Unaffected Market Price. [361] Dr. Zmijewski cited the decline in the federal risk-free rate, the rise in Jarden's share price and the divergence between Jarden management and market analysts' projections for Jarden's future performance as reasons the Unaffected Market Price was not a reliable indicator of fair value. [362] Importantly, Dr. Zmijewski also observed that Jarden stockholders had no access to the November Projections as of the date fixed for the Unaffected Market Price. The evidence supports the factual predicates for these observations, but it does not support a conclusion that the absent facts resulted in the kind of information asymmetry that would render the Unaffected Market Price unreliable.

As for the decline in the federal risk-free rate, Dr. Zmijewski states that, "[a]ll else equal, the decline in the risk-free rate results in an increase in Jarden's Fair Value," and goes on to argue that because the federal risk-free rate declined from December 2015 to April 2016, Jarden's fair value must be higher than the Unaffected Market Price. [363] Interest rates on U.S. Treasury 20-year constant maturity bills declined 19%, from 2.65% to 2.14%, between December 4, 2015 and April 15, 2016. [364] Dr. Hubbard conceded that, if "all else" were, in fact, "equal," as Dr. Zmijewski posited, then Jarden's fair value would increase as the risk-free rate decreased. [365] But then Dr. Hubbard exposed the flaw in Dr. Zmijewski's elephant-sized assumption that "all else" remained "equal." Specifically, Dr. Hubbard referred directly to market data showing that, as the interest rate on 20-Year Treasury Bonds declined between December 2015 and April 2016, stock prices in general, represented by the S&P 500 Market Index, did not increase in response. [366] Contrary to Dr. Zmijewski's "all else equal" assumption, the evidence shows that the stock market declined just as the risk-free rate declined. [367] In other words, the correlation that supports the supposed information asymmetry is no correlation at all.

***30** Regarding the lack of consensus between Jarden management and third-party analysts' projections, Dr. Hubbard emphasized the qualitative difference between unvarnished raw *information* tracking Jarden's performance and well-reasoned *opinions* about Jarden's prospects. [368] Jarden's revenue projections for 2016, 2017, and 2018 were 1.0%, 1.7% and 2.6% higher, respectively, than financial analysts' consensus forecast. [369] Jarden's EBITDA projections for 2016, 2017 and 2018 were 1.3%, 6.6% and 9.0% higher, respectively, than financial analysts' consensus forecasts. Jarden's November Projections incorporated this data but were not released to the public until March 2016, and thus would not have been incorporated into the Unaffected Market Price. [370] But is this evidence of information asymmetry? Dr. Hubbard hypothesized the answer is no. [371]

To test his hypothesis, Dr. Hubbard turned to his event study. The November Projections were disclosed in the joint proxy in March 2016. If the November Projections revealed information not previously incorporated in Jarden's stock price, Hubbard reasoned, then both Jarden and Newell's stock price should have proportionately reflected that information. In other words, if the November Projections justified more value (according to Dr. Zmijewski substantially more value), then Newell's stock price should have increased substantially to reflect that Newell was acquiring Jarden at less than fair value. [372] But, of course, that is not what happened; Jarden's stock price climbed while Newell's stock price dropped. [373] Moreover, Jarden's April Projections lowered the Company's financial guidance to forecasts more in line with the analysts' earlier projections.[374] Dr. Hubbard persuasively opined that the April Projection's convergence with the analysts' forecasts was a strong indication that the difference between the November Projections (as disclosed in the joint proxy) and the analysts' projections was not attributable to unreasonable market pessimism, but instead showed that market analysts had more accurately estimated Jarden's 2016 outlook than Jarden's management (who may have been motivated by factors other than actual anticipated results when making their forecasts).[375]

The credible evidence reflects no information asymmetry. The market was well informed and the Unaffected Market Price reflects all material information.

b. The Conglomerate and Minority Discounts

Dr. Zmijewski also criticizes Dr. Hubbard's Unaffected Market Price analysis because it does not account for Jarden's massively diversified portfolio of operating companies (the conglomerate discount) and does not adjust for embedded agency costs (the minority discount).[376] Here again, Dr. Zmijewski flags the issues but makes no attempt to quantify their impact, if any.[377]

***31** As for the conglomerate discount, the evidence does not support that this is even "a thing," meaning it is not clear that this notion is accepted within the academy or among valuation professionals.[378] With that said, there is evidence that Jarden's unique structure and diversified portfolio did pose valuation challenges. Newell's Tarchetti described Jarden as a "fast-changing company" that was difficult to appraise, in part, due to its complexity and tendency to grow and evolve at any point in time.[379] Even so, the Company's high trading volume and the intense scrutiny paid it by market analysts has convinced me that the market understood Jarden's holding company structure as an operative reality, considered the high overhead costs associated with decentralized management and imputed those factors into Jarden's Unaffected Market Price.[380]

The minority discount, likewise, does not fit here. For a company without a controlling stockholder, the premise is that the appraiser must consider the conflict of interest between Company management and a diffuse stockholder base and account for minority trading multiples.[381] Setting aside that Petitioners have offered no credible evidentiary basis to quantify any minority discount here, I see no basis to even try given that the foundation for applying the discount has not been laid. Jarden's management was well known to stockholders and well known to the market. But for the Merger, they were not going anywhere as the Company was not for sale.[382] As Dr. Hubbard explained, under these circumstances, Jarden's agency costs were embedded in its operative reality and reflected in its Unaffected Market Price.[383]

c. Staleness of the Unaffected Market Price

Petitioners also argue that the Unaffected Market Price was stale as of the Merger Date.[384] I disagree. There is no evidence to suggest that Jarden gained value from the date set for the Unaffected Market Price and the closing of the Merger, or that the market was deprived of information that might have been perceived as enhancing value. Indeed, following a period where Jarden had been especially acquisitive, the Company was experiencing declines in operating income and net income and management was giving the Board revised, more conservative projections for 2016.[385] The April Projections forecasted reduced revenue growth and increased working capital investment for FY17–20.[386] This is not a case where the credible evidence reveals that the Unaffected Market Price was demonstrably below Jarden's fair value as of the Merger.

* * * * * * * * * * *

After carefully considering the evidence, I find that the Unaffected Market Price is a reliable indicator of Jarden's value as a going concern on the Merger Date. I have given it substantial weight in my assessment of fair value.

C. The Other Market Evidence

As Jarden was negotiating with Newell, it was also pursuing an acquisition of Jostens. To raise capital for that deal, Jarden initiated a share offering priced at $49.00 per share.[387] At the time, the stock was trading in the mid-$40s.[388] When the market reacted poorly to the Jostens acquisition, and the stock price fell, the Board believed it needed to send a signal that the Company and its management were optimistic about Jostens.

So it authorized a $50 million stock buyback,[389] and it set the price cap again at $49.00 because, after internal assessments, it believed that price reflected Jarden's value.[390] Ultimately, Jarden repurchased 276,417 shares on November 2, 2015, at an average price of $45.96 per share, and another 775,685 shares on November 3, 2015, at an average price of $48.05 per share.[391] This evidence is by no means dispositive. But it is persuasive evidence that, in the weeks leading up to the leak of the merger negotiations, uncluttered by transactional or forensic incentives, both the Company and the market saw Jarden's value well below what Petitioners seek here.

D. Comparable Companies

***32** Both parties' experts performed comparable companies analyses to estimate Jarden's value relative to sets of proposed peer firms. Applying his comparable companies analysis, Dr. Zmijewski concluded that Jarden's fair value on the Merger Date, based on Jarden's 2016 forecasted EBITDA using the 90th, 75th and 50th percentiles of his peer set, was $81.44, $70.49 and $66.30, respectively.[392] Based on Jarden's 2017 forecasted EBITDA, the market multiples based-valuation using the 90th, 75th and 50th percentiles of his peer set, revealed a per share value of $77.39, $72.20 and $65.56, respectively.[393] For his part, Dr. Hubbard disclaimed the efficacy of a comparable companies valuation for Jarden, but then performed his own comparable analysis for the sake of completeness, resulting in a value range of $40.12 to $55.21 per share.[394] Before addressing the experts' divergent analyses and conclusions, it is useful to review basic concepts, separated from forensics.

1. The Comparable Companies Methodology

As a threshold matter, before a comparable companies multiples analysis can be undertaken with any measure of reliability, it is necessary to establish a suitable peer group through appropriate empirical analysis.[395] In fact, nearly every text in the record states that the accuracy of a multiples-based valuation depends entirely on the existence of comparable peers:

- Holthausen & Zmijewski (JX 242): "While selecting comparable companies might not appear to be too difficult, we often quickly conclude that not many, if any, companies are truly comparable to the company we are valuing for purposes of a market multiple valuation once we understand all the different dimensions of comparability and begin to analyze the potential comparable companies ... simply selecting close competitors is not sufficient to ensure the companies are comparable, as we observe a substantial amount of variation in multiples within an industry."[396]

- Koller (JX 2516): "Selecting the right peer group is critical to coming up with a reasonable valuation using multiples."[397]

- Damodaran (JX 2515): "... finding similar and comparable firms is often a challenge, and frequently we have to accept firms that are different from the firm being valued on one dimension or the other. When this is the case, we have to either explicitly or implicitly control for differences across firms on growth, risk, and cash flow measures."[398]

- Berk & DeMarzo (JX 2032): "Of course, firms are not identical. Thus, the usefulness of a valuation multiple will depend on the nature of the differences between firms and the sensitivity of the multiples to these differences."[399]

McKinsey recommends beginning the peer group identification process with the Standard Industrial Classification ("SIC") or Global Industry Classification Standard ("GICS") codes.[400] While these codes are a good starting point for selecting a peer group, the industry-specific company lists they produce require significant refinement to identify truly comparable firms.[401]

To isolate a relevant peer group from a larger industry data set, the appraiser must identify firms with similar risk profiles, costs of capital, return on invested capital and growth.[402] It is better to have a smaller number of peers that truly compete in the same markets with similar products than including aspirational or nearly comparable companies.[403] In order effectively to narrow down a list of potential comparables according to growth and risk, the analysis must consider whether the companies have similar "value drivers" as the target.[404] As Dr. Zmijewski described in his text:

> ***33** [A] company's product lines, customer types, market segments,

> types of operation, and so forth are all important aspects to consider when we identify comparable companies. Even after all these are taken into consideration, two companies can be in the same industry yet not be comparable on all of the characteristics that are important for a market multiple valuation. [405]

In addition, the finance literature advises against relying on peers provided by the target company's management. This reasoning reflects common sense; optimistic executives often provide "aspirational peers" rather than companies that actually compete head-to-head with their firm. [406]

The importance of selecting a proper peer set in the performance of a proper comparable companies analysis cannot be overstated. Because this threshold task is so important, and yet so difficult, the valuation treatises generally view the comparable companies methodology as inferior to other methodologies: "a *key shortcoming* of the comparables approach is that it does not take into account the important differences among firms," therefore "[u]sing a valuation multiple based on comparables is *best viewed as a 'shortcut'* to the discounted cash flow methods of valuation." [407]

If, and only if, a proper peer set can be selected, the next step in the comparable companies analysis is to select an appropriate multiple and then determine where on the distribution of peers the target company falls. [408] The Enterprise Value to EBITDA multiples valuation ("EV/EBITDA") is widely accepted as the most reliable data set for a comparable companies analysis. [409] In this regard, it appears that the preference is to use forward-looking projections instead of a firm's historical earnings data. [410] Forward-looking multiples are deemed more consistent with the principles of valuation, especially in the context of estimating the present value of a company as a going concern. [411] Projections generally exhibit less variation across peer companies compared to historical data, and although long-term earnings projections are favored, one- and two-year forecasts are reliable when they uniformly represent the firm's long-term prospects. [412]

***34** With these generally accepted features of a proper comparable companies valuation in mind, I turn to the experts' comparable companies valuation of Jarden.

2. The Experts Attempt But Fail to Select a Valid Peer Set

Both experts developed their peer set by drawing from the peer set developed by Barclays in its valuation work for the Company with regard to the Merger. They then made adjustments based on their own sense of comparability. For his part, Dr. Zmijewski conceded that he "did not do any qualitative assessment of any inherent differences between the Jarden business and the business of its peers companies." [413] Giving such deference to the peer set selected by management, without any meaningful, independent assessment of comparability, is not useful and, frankly, not credible. [414] Dr. Zmijewski made no mention of GICS or SIC codes in his report and there is no indication that he employed them, or any other objective criteria, in his selection of a peer set. [415]

Failing to ground his peer set in any objective methodology is all the more problematic given Dr. Zmijewski's apparent willingness to adjust the management/Barclays' peer set when it suited him to yield a higher valuation for Jarden. As stated in his report, Dr. Zmijewski excluded Kimberly-Clark Corporation and Colgate-Palmolive Company, which were both included in the Barclays list, because both companies maintain a significantly larger market capitalization than Jarden and the other comparables. [416] The notion that a company with a very large market capitalization is not a true peer of a company with a relatively smaller market capitalization has a certain lay appeal. But Dr. Zmijewski's own text makes clear that "there is no theoretical model we are aware of that includes size as a determinant of market multiples." [417] It may well be that Kimberly-Clark and Colgate-Palmolive are not "comparables" for Jarden, but the absence of any meaningful analysis or explanation in Dr. Zmijewski's report leaves the Court with no way to determine if the exclusion was arbitrary or principled. [418]

***35** Before addressing Dr. Hubbard's peer set, it must be emphasized that Dr. Hubbard does not sponsor the comparable companies methodology as the appropriate means by which to assess Jarden's fair value. [419] His preferred methodology is DCF.[420] Nevertheless, Dr. Hubbard engaged with Dr. Zmijewski on comparable companies and, not surprisingly, reached a very different conclusion after doing so.

Dr. Hubbard assessed Jarden's peers by using GICS codes.[421] He then cited to over a dozen industry analyst reports that corroborated his peer set, which included companies that were larger and smaller than Jarden and companies that were not on the Barclays list.[422] Once he completed his peer set, however, Dr. Hubbard emphasized his view that Jarden's unique and highly diversified portfolio of businesses, its aggressively acquisitive growth strategy and its holding company structure made the selection of a valid peer set for a comparable companies analysis a fundamentally flawed exercise since Jarden "lack[ed] truly comparable peers."[423]

After carefully reviewing the evidence, I am convinced that Dr. Hubbard is correct—Jarden had no comparable peers, at least not as developed in the credible evidence presented at trial. Under these circumstances, the fact that Dr. Zmijewski engaged in no real analysis when developing his peer set is not surprising.[424]

Having found that the first, and most important, element of a proper comparable companies analysis is lacking in this record, I give the experts' comparable companies conclusions no weight in my fair value determination.[425] Accordingly, I move next to the parties' competing DCF valuations.

E. Discounted Cash Flow

***36** As I approach the parties' fantastically divergent conclusions following their DCF analyses, I am mindful of our Supreme Court's admonition that, tempting as it is to select the entirety of one expert's analysis over the other's, my review of the experts' opinions must not be presumptively binary:

> The role of the Court of Chancery has evolved over time to the present requirement that the court independently determine the value of the shares that are the subject of the appraisal action. Even though today a Chancellor may be faced with wildly divergent values presented by the parties' experts, the acceptance of one expert's value, *in toto*, creates the risk that the favored expert will be accorded a status greater than that of the now eliminated [expert appraiser]. This is not to say that the selection of one expert to the total exclusion of another is, in itself, an arbitrary act. The testimony of a thoroughly discredited witness, expert or lay, is subject to rejection under the usual standards which govern receipt of such evidence. The nub of the present appeal is not merely that the Chancellor made an uncritical acceptance of the evidence of SAP's appraiser but that he announced in advance that he intended to choose between absolutes.[426]

As I discuss below, in many important respects, the experts have utilized very different inputs in their DCF models leading to a substantial delta between their ultimate DCF valuations—Dr. Zmijewski's DCF valuation produced a range of $70.36 and $70.40 per share;[427] Dr. Hubbard's DCF valuation is $48.01 per share.[428] The number and degree of their differences has necessitated the lengthy discussion that follows. For reasons I explain, I have adopted some of both expert's inputs to construct my own DCF model. Based on that model, my DCF valuation is $48.13 per share.

I begin by noting where the experts agree. First, they agree that DCF is a widely used and industry-accepted means of calculating the value of a corporation as a going concern. Dr. Hubbard likes DCF best to value Jarden, while Dr. Zmijewski uses his DCF valuation to corroborate his comparable companies analysis.[429] Both experts used the Weighted Average Cost of Capital ("WACC") method to determine the appropriate discount rate. Both agreed that the November Projections were the appropriate cash flow forecasts upon which their DCF models should be based. Both largely agreed on the required net investment to drive growth through the year 2020, which is the last year included in the November Projections. And both agreed that the Capital Asset Pricing Model ("CAPM") was appropriate to calculate

Jarden's Cost of Equity. Because I see no basis in the evidence to depart from these stipulations, I adopt them without further analysis.

***37** The bulk of the experts' disagreements relate to how Jarden will perform in the terminal period beyond the November Projections' explicit forecasts.[430] I address and do my best to resolve each of the disagreements below.

1. Jarden's Future Cash Flows

As noted, both experts used the November Projections for their DCF analyses.[431] Even so, both made different adjustments to the projections to calculate Jarden's unlevered free cash flows.[432] After reviewing the adjustments, I find that their adjustments for EBITDA, depreciation and amortization, and Dr. Zmijewski's adjustment for projected taxes, are appropriate.[433] These adjustments yield the following for Jarden's Net Operating Profits after taxes (“NOPAT”):[434]

FY2016-E	FY2017-E	FY2018-E	FY2019-E	FY2020-E
$869 million	$967 million	$1,062 million	$1,146 million	$1,235 million

Using Jarden's NOPAT, I have calculated Jarden's unlevered free cash flows for each projection year by: (1) adding back depreciation; (2) deducting Jarden's year-over-year change in working capital; and (3) deducting Jarden's capital expenditures. These adjustments track those made by Dr. Hubbard (albeit at a 35% marginal rate),[435] and yield the following as Jarden's unlevered free cash flow in each of the projected years:

FY2016-E	FY2017-E	FY2018-E	FY2019-E	FY2020-E
$572 million	$701 million	$783 million	$853 million	$927 million

2. Jarden's Terminal Value

Jarden's terminal value is the value of the Company beyond the discrete projection period as defined in a discounted future earnings model (“Terminal Value”).[436] In the context of the experts' DCF analyses for Jarden, Terminal Value refers to Jarden's estimated value taking into account all future cash flows at the end of the November Projection's explicit forecast period assuming a stable growth rate in perpetuity.[437]

Dr. Zmijewski's Terminal Value calculation and accompanying analysis mostly relies on his comparable companies analysis,[438] which I have found not reliable for reasons already stated. Dr. Hubbard used a formula developed by McKinsey & Co. to calculate Jarden's Terminal Value. The McKinsey formula involves dividing the value of cash flow in the Terminal Period by the difference between the Discount Rate (the rate at which future cash flows are discounted to present) and Jarden's Terminal Growth Rate.[439] According to Dr. Hubbard, this formula generally provides that “all else remaining equal,” a company's terminal value is larger when cash flow is high, and the discount rate is low or the growth rate is high.[440] The “all else remaining equal” caveat, Hubbard explains, assumes that increased growth will be supported by increased investment which, in turn, reduces cash flow.[441] In other words, increasing investment in the Terminal Period will proportionately reduce Jarden's cash flow and thereby lower Jarden's measurable value in the Terminal Period. To calculate Jarden's Terminal Value, it is necessary to estimate its Terminal Growth Rate, Terminal Investment Rate and Discount Rate.

a. Terminal Growth Rate

***38** “Of all the inputs into a discounted cash flow valuation model, none creates as much angst as estimating the [terminal] growth rate. Part of the reason for it is that small changes in the [terminal] growth rate can change the terminal value significantly[.]”[442] The terminal growth rate (“TGR”) describes Jarden's long-term growth in revenue, earnings and cash flow in the Terminal Period, which includes the years starting in 2021 and onward. Since acquisitions are typically not considered in organic growth rate calculations,[443] a key question is whether Jarden's several tuck-in acquisitions should be included in the TGR.[444]

Both experts measure Jarden's TGR based on estimates of U.S. nominal GDP growth and long-term economic inflation. This method makes sense and is generally accepted.[445] The experts disagreed, however, as to what forecast sources provide the most useful data.[446]

Dr. Zmijewski derived a 2.1% projected long-term inflation rate from four estimates of U.S. economic outlooks and an expected nominal GDP growth rate of 4.3% from three projections of U.S. GDP growth.[447] Based on these projections, Dr. Zmijewski applied the midpoint of 3.2%, which he asserts is a reasonable long-term growth rate for Jarden.[448] Dr. Zmijewski's TGR analysis included an assessment of the Company's acquisition-driven and organic growth, and the results showed Jarden's historic organic growth rate to be roughly 3.1%.[449] As corroboration, Dr. Zmijewski emphasized that key players in the Merger projected that Jarden would grow between 2.0% to 4.0% annually in perpetuity.[450]

For his Composite DCF calculation, Dr. Zmijewski used the 2.1% projected U.S. inflationary growth rate as Jarden's TGR.[451] Dr. Zmijewski explained he used U.S. inflation as Jarden's TGR as a "conservative" measure because the Composite DCF relies on calculations supplemented by comparable companies data, and Jarden's long-term growth was estimated to be much higher than any of the companies in Dr. Zmijewski's peer set.[452] For his Jarden-Specific DCF analysis, Dr. Zmijewski set Jarden's TGR at 3.2%, which he suggested conforms to the other Jarden-only measurements and calculations in that valuation.[453]

Dr. Hubbard's report set Jarden's TGR at 2.5% based on several inflation and nominal GDP growth forecasts for the U.S. economy and the European Union's Eurozone.[454] He noted that his TGR comports with the TGR utilized by Goldman Sachs and Centerview in advising Newell, both of which used a TGR of 2.0% in their valuations of Jarden.[455] He also pointed to analyst reports by Deutsche Bank and RBC Capital that estimated Jarden's TGR at 1.5% and 2.5%, respectively.[456] Finally, he noted that his TGR is consistent with Jarden's historic organic growth, which he determined to be 2.2% annually.[457] With all these factors considered, Dr. Hubbard concluded that his 2.5% TGR falls squarely between his estimated range of inflation and nominal GDP and aligns well with Jarden's historic organic growth when fairly adjusted for "tuck-in" acquisitions.[458]

***39** Dr. Zmijewski took issue with Dr. Hubbard's adjustments for "tuck-ins" because the adjustments result in double counting certain companies that did not fit Jarden's definition of a "tuck-in."[459] Dr. Hubbard conceded this error, revised his analysis and found Jarden's organic, non-acquisitive growth rate to be 3.2% annually.[460] Despite his upward revision to Jarden's historic organic growth, Dr. Hubbard did not change his 2.5% TGR estimate.[461]

Jarden's "tuck-in" acquisitions, although relatively small in scale, are acquisition-driven growth, not organic growth.[462] Accordingly, Dr. Hubbard's attempt to account for "tuck-in" acquisitions when estimating Jarden's TGR is well taken. Dr. Hubbard's reluctance, however, to acknowledge the impact of his organic growth rate miscalculation on his estimate of Jarden's TGR is not.[463] Moreover, considering Dr. Hubbard's revised 3.2% historic organic growth rate in light of his economic research supporting long-run inflation in the range of 2.0% annually, and nominal GDP growth in the range of 4.07% annually, with a midpoint of roughly 3.04%,[464] Dr. Hubbard's 2.5% TGR is not supported.

Dr. Zmijewski calculated Jarden's historic organic growth rate to be 3.1%.[465] His economic research supported U.S. long-run inflation at 2.1% annually and nominal GDP growth at 4.3% annually.[466] And his estimates are within one- or two-tenths of a percentage point of Dr. Hubbard's. The midpoint of each experts' inflation and GDP estimates is approximately 3.1%, which aligns with Dr. Hubbard's 3.2% revised historic organic growth rate and Dr. Zmijewski's 3.2% midpoint TGR in his Jarden-Specific DCF.[467] The literature recommends a conservative approach to estimating long-term growth rates for a DCF valuation, in recognition that many companies experience cyclical growth in relation to the overall economy.[468] Jarden was considered a GDP growth business.[469]

Based on these factors, and the credible evidence in the trial record, I apply a 3.1% TGR. In my view, this reflects the most credible aspects of the experts' analyses and comports with the most persuasive view of Jarden's historic growth.

b. Terminal Investment Rate

The experts' disagreement over the terminal investment rate ("TIR") accounts for 87% of the disparity in their DCF valuations.[470] In other words, of the $22.39 difference between Dr. Hubbard's DCF per share value of $48.01 and Dr. Zmijewski's DCF per share value of $70.40, $19.56 is attributable to the disagreement over Jarden's TIR. After carefully considering the experts' analyses of TIR, and exposing what I believe to be flaws in both, I have determined that an appropriate TIR for Jarden is 27.75%.

***40** The disagreement between the experts boils down to whether Dr. Hubbard improperly relied upon accounting theory when calculating TIR.[471] Dr. Zmijewski's approach to Jarden's TIR aligns, in concept, with the Bradley-Jarrell Plowback Formula, which provides, in broad terms, that the rate of reinvestment must be measured by what is realistically required to drive real growth.[472] Real growth, under the plowback paradigm, is measured by the delta between the company's growth rate and inflationary growth, which is driven by the greater economy and not cash reinvestment.[473] In other words, as Jarden's growth slowed over time and became steadier, the Company required less capital expenditure to drive real growth because a greater percentage of its overall growth was driven by inflation and broader economic factors. According to Dr. Zmijewski, because Jarden was a steady-growth company that expected lower growth in the Terminal Period, it required a much lower TIR, which he calculated at only 4.9%.[474]

Dr. Hubbard calculated TIR by applying a formula from McKinsey & Co.[475] The McKinsey formula posits that a company's return on invested capital ("ROIC") should converge towards its WACC over time.[476] The formula rests on the premise that a company operating in a competitive industry will not "have both high and rising forever returns on invested capital."[477] Applying the McKinsey formula,[478] Dr. Hubbard used 2.5% as his TGR and 7.38% as his WACC/ROIC, yielding a TIR of 33.9%.[479]

Dr. Zmijewski expressed four principal criticisms of Dr. Hubbard's application of the McKinsey formula.[480] First, according to Dr. Zmijewski, Dr. Hubbard incorrectly assumes that any new investment Jarden made starting in 2021 would not create any value.[481] Second, Dr. Zmijewski believes Dr. Hubbard improperly defined investments to include only working capital and capital expenditures, which, according to Dr. Zmijewski, is the accounting definition of investments (meaning "what you put on a balance sheet") that does not account for real world economics.[482] In other words, Dr. Hubbard's definition of investment excludes research and development, advertising and human capital expenditures that would create value for Jarden in years beyond 2021.[483] Third, Dr. Hubbard's definition of net investment as investment above depreciation is, again, an accounting definition that does not fit when calculating TIR.[484] Fourth, Dr. Hubbard improperly calculated WACC by "using accounting rates of return" instead of "economic rates of return," which do "not measure the same thing."[485]

***41** Dr. Hubbard's testimony that, in competitive industries, the return on new invested capital should equal the company's WACC was credible, and it is supported by the valuation treatises.[486] Although I found credible Dr. Hubbard's well-reasoned premise that companies like Jarden cannot maintain growth without sufficient investment to drive growth above inflation over time, his relatively high TIR raises at least yellow flags. At first glance, the empirical analysis Dr. Hubbard undertook to support his 33.9% TIR appears reasonable, particularly given Jarden's historic investment rates, which averaged roughly 26.9% of comparable growth over six years.[487] But why study six years here when Dr. Hubbard's TGR estimation was premised on five years of Jarden's historic growth?[488] By including the sixth year, 2010, in his calculation, Dr. Hubbard was able to reach a significantly higher number for Jarden's historical average growth. After excluding the 2010 investment rate of 64.3%, Jarden's five-year average investment rate is 21.6%.

In view of Jarden's five-year 21.6% average historic investment rate, Dr. Zmijewski's 4.6% TIR is too low; it unreasonably assumes rising ROIC for more than 40 years into the Terminal Period, unreasonably assumes all new investment in the Terminal Period will be comprised entirely of working capital, and is based on a methodology that conflicts with the valuation goal of striking a balance between investment and growth.[489] The November Projection's forecast of net investment in 2021 at 9.8%, likewise, stands out as low relative to Jarden's five-year average investment rate. The midpoint of Dr. Hubbard's 33.9% TIR and Jarden management's projected 9.8% TIR is roughly 21.8%. With a calculated TGR of 3.1%, which coincides with Jarden's historic organic growth rate, the appropriate TIR should reflect Jarden's historic investment rate but account for a slight increase to accommodate sustained growth in the Terminal Period. The credible evidence, in my view, supports a TIR for Jarden of 27.75%.[490]

c. Jarden's Weighted Average Cost of Capital/Discount Rate

As previously stated, both experts' DCF models used Jarden's WACC as the input for the Discount Rate in the DCF formula.[491] The Discount Rate converts Jarden's future cash flows from the November Projections to present value as of the Merger Date.[492] WACC reflects Jarden's cost of equity and debt financing and the relative weight of each in Jarden's capital structure.[493] Given that a DCF valuation is meant to calculate Jarden's value as a going concern, the components relied upon to calculate WACC should represent Jarden's prospective outlook.[494] The experts agreed on one of the relevant inputs to calculate Jarden's WACC, the risk-free rate of return. They differed, however, in their respective estimates of Jarden's capital structure, beta, equity risk premium, and whether a size premium was appropriate.[495] I address each issue below.

***42** The application of a discount rate to financial projections converts the target company's future income stream at its expected opportunity cost of capital to its present value.[496] A company's WACC represents the cost (to the company) of financing its business operations; it comprises the weighted average of the company's cost of debt and equity:[497]

$$\text{WACC} = \left(r_{equity} \times \frac{E}{V}\right) + \left(r_{debt} \times \frac{D}{V} \times (1 - t)\right)$$

where:

r_{equity}	=	cost of equity capital
E	=	market value of the company's equity
r_{debt}	=	cost of debt capital
D	=	value of the company's debt
$V = E + D$	=	total value of the company's equity and debt
t	=	marginal tax rate

i. Jarden's Capital Structure

A company's capital structure indicates what percentage of its activities is financed by debt and what percentage is financed by equity.[498] Determining the correct capital structure is essential to WACC because without a clear picture of a company's debt-to-equity ratio, the cost of financing future operations will be improperly weighted.[499]

Both experts recognized the impact of the substantial amount of convertible debt in Jarden's capital structure.[500] Jarden's convertible debt conceptually existed as both debt and equity components in its capital structure, and both experts valued the debt and equity components of Jarden's convertible notes separately.[501]

Dr. Zmijewski calculated Jarden's capital structure based on Jarden's median capital structure ratios in the last four quarters before December 4, 2015.[502] According to the previous year's ratios, Dr. Zmijewski selected a Jarden capitalization ratio of 69% combined equity and 31% debt.[503]

For his part, Dr. Hubbard examined Jarden's capital structure ratio for the five years prior to the Merger.[504] He noted that Jarden maintained a debt level of roughly 50% from the last quarter of 2010 through 2011, but beginning in 2012, Jarden's debt to equity ratio began shifting due to Jarden's increased acquisition activity.[505] As Jarden stepped up acquisitions between 2012 and 2015, its total debt nearly doubled but its equity value expanded in even greater proportions.[506] By the third quarter of 2015, Jarden's market capitalization nearly tripled and its capital structure had shifted from nearly a 50:50 ratio to 37.5% debt and 62.5% equity.[507] Following the Yankee Candle acquisition in 2013, Jarden's goal was to de-lever itself to three times its bank leverage-to-EBITDA ratio.[508]

Dr. Hubbard observed that, in order to capture Jarden's value as a going concern, the capital structure ratio used in the WACC analysis should reflect Jarden's long-run target capital structure.[509] He concluded that, because Jarden was on a trajectory of lower debt leading up to the Merger, and its long-term goal was to achieve an even lower debt-to-equity ratio, Jarden's average debt in the one-year period before the Merger was the best estimate of Jarden's target capital structure for WACC.[510] Based on that judgment, Dr. Hubbard calculated a capital structure equal to Jarden's one-year average ratios of 36.1% debt and 63.9% equity.[511]

***43** The valuation literature suggests that because of the increased use of convertible securities, assessing the debt-to-EBITDA ratio alongside capital structure helps build a more comprehensive picture of a company's leverage risk. [512] Both experts were cognizant of the effect of Jarden's convertible securities on its capital structure, and Dr. Hubbard went on to consider changes in Jarden's debt-to-EBITDA ratio and the corresponding effect on Jarden's future leverage risk. [513]

The two experts relied on one year of debt-to-equity information to calculate their capital structure estimates. Dr. Zmijewski calculated Jarden's capital structure according to its median debt-to-equity ratios prior to the unaffected trading date of December 4, 2015. [514] That is where Dr. Zmijewski's analysis ended. Dr. Hubbard made a similar assessment of Jarden's capital structure as it stood just prior to the unaffected trading date, but did not end his analysis there. Instead, Dr. Hubbard assessed Jarden's target debt-to-EBITDA ratios, which reflected the capital structure Jarden set as a forward-looking goal well before merger negotiations began. [515]

This further analysis makes sense. The cost of capital analysis should be based on target debt-to-equity ratios instead of current ratios. [516] Target capital structure represents the ratios expected to prevail over the life of the business and the literature stresses that relying solely on current capital structure can distort the cost of capital analysis. [517] Overly optimistic capital structure targets must be accounted for if they are expected to take many years to be realized. [518] Jarden's target capital structure and debt-to-EBITDA ratio was not overly optimistic under the circumstances. As of 2015's third quarter, Jarden's leverage had shifted downward to 37.5% as its market capitalization grew, [519] and Jarden planned to continue its deleveraging strategy until it reached a debt-to-EBITDA ratio of 3.0x. [520] Adjusting Jarden's 37.5% debt as of September 30, 2015, to conform to its target leverage ratio would lower Jarden's debt ratio to 33.3%. [521] Based on the dramatic swings in Jarden's capital structure in the five years prior to the Merger, a 4.2% deleveraging was well within Jarden's ability to achieve in the short term.

Because Dr. Hubbard's analysis conservatively includes Jarden's forward-looking target capital structure in his capitalization analysis, I adopt Dr. Hubbard's capital structure of 63.9% equity and 36.1% debt. [522] Accordingly, I adopt Hubbard's estimated equity and debt values for Jarden at $10,596,000,000 and $5,043,000,000, respectively. [523]

ii. Jarden's Cost of Debt

A company's cost of debt reflects “the current cost to the firm of borrowing funds to finance projects.” [524] Generally, it is derived from three variables: (1) the riskless rate, (2) the default risk (and associated default spread) of the company and (3) the tax advantage associated with debt. [525]

***44** Dr. Zmijewski estimated Jarden's after-tax Cost of Debt at 2.8%. [526] He arrived at this figure by calculating a Debt Beta of 0.36 based on Moody's Long-Term Corporate Family Rating of Ba3 for Jarden as of December 4, 2015, and the Duff & Phelps debt beta estimate for Ba debt as of March 2016. [527]

Dr. Hubbard estimated Jarden's Cost of Debt based on a tax adjusted yield to maturity rate of 5.30%. [528] This yielded a Cost of Debt of 3.2%. [529]

I agree with Dr. Zmijewski that calculating the cost of below-investment-grade debt by using yield to maturity sets the cost of debt too high. [530] I adopt his Cost of Debt of 2.8%

iii. Jarden's Tax Rate

Jarden's tax rate is 35%, which is the top marginal corporate tax rate for U.S. companies at the time of the Merger. [531]

iv. Jarden's Cost of Equity

Establishing an accurate Cost of Equity is an essential subcomponent of Jarden's WACC. Both experts used the Capital Asset Pricing Model (“CAPM”) to calculate Jarden's cost of equity capital. [532] This approach calculates Jarden's risk separately from systematic risk to produce a reliable estimate of Jarden's Cost of Equity. [533] CAPM has four components: the risk-free rate, equity beta, equity risk premium, and if necessary, a size premium. [534] Following CAPM, a company's cost of equity is calculated as follows: [535]

$$r_{equity} = r_{no\text{-}risk} + (\beta \times ERP) + SS$$

where:

$r_{no\text{-}risk}$	=	risk-free rate of return
β	=	beta coefficient of the subject company
ERP	=	equity risk premium
SS	=	size premium

• The Risk-Free Rate

The only point of agreement between the experts in the WACC analysis is the risk-free rate of return. Both experts set their analyses' risk-free rate at the 20-year constant maturity U.S. Treasury Bonds return as of the Merger. [536] That rate was 2.14%. [537] Relying on 20-year U.S. Treasury Bonds for the risk-free rate is universally accepted practice in corporate valuation. [538]

• Beta

Beta, in short, is a measurement of the systemic risk that a particular security adds to a market portfolio. [539] The consensus from the corporate finance literature in the record is that the conventional approach for estimating equity beta for a publicly traded company, like Jarden, is through a regression analysis of the historical returns of its stock against the returns of a market index. [540] In other words, equity beta is derived by assessing a stock's sensitivity to and correlation with changes in the aggregate market. A beta regression analysis requires three parameter-setting choices. First, the time period for measuring returns must be established. [541] Second, the return interval at which measurements will be taken over the duration of the designated time period must be specified. [542] Third, an appropriate market index must be identified that will represent the cumulative market over time as a control to measure the target company's market price. [543]

***45** The experts disagreed on the relevant time periods and return intervals to use in their regression analyses. From the evidence, it appears the most appropriate (and commonly used) parameters are two- or five-year time periods and weekly or monthly return intervals. [544]

The control market index should be one developed from the exchange where the target company's stock trades. [545] For companies traded on the NYSE, like Jarden, it is reasonable to use either the NYSE Composite or the S&P 500 Index. [546] The experts agreed that the S&P 500 is an appropriate market index and both used the S&P 500 as their control to measure Jarden. [547]

In addition, both experts relied on Jarden's historical market returns data and estimated Jarden-specific betas. Yet, they disputed whether it was necessary to balance Jarden's beta with betas estimated from historical returns of comparable companies.

In his report, Dr. Zmijewski calculated two equity betas to use in his Jarden-Specific DCF and Composite DCF analyses. To estimate Jarden's beta as of the Merger Date, Dr. Zmijewski measured the equity beta for Jarden and for each of a list of comparable companies based on five years of weekly returns ending on the Merger Date. [548] He then performed a regression analysis for each company against the S&P 500 for the same period that showed Jarden's unlevered beta was 1.04 and that the unlevered beta for his comparable companies (plus Jarden) was 0.86. [549] Finally, he made adjustments to account for Jarden's cash and other financial assets and relevered each beta to produce a Jarden-specific equity beta of 1.24 (the "Jarden-Specific Beta") and a combined equity beta for his comparable companies (plus Jarden) of 1.01 (the "Composite Beta"). [550]

Dr. Hubbard's regression analysis yielded an equity beta of 1.18 (the "Hubbard Beta") that was based on Jarden's daily returns for one year ending on December 4, 2015. [551] Unlike Dr. Zmijewski, Dr. Hubbard did not balance his Jarden-specific beta regression analysis with beta estimates of comparable companies. Instead, he regressed Jarden's single year daily returns against the S&P 500 during the one-year period and calculated an unlevered beta of 0.771. [552] Like Dr. Zmijewski, he then adjusted for cash and financial assets and re-levered the beta to produce a Jarden equity beta of 1.18. [553] Dr. Hubbard also calculated Jarden-specific betas from two years of weekly returns and five years of monthly returns, but ultimately decided to use the single year daily returns beta to mitigate the potential confounding effects of several large acquisitions Jarden completed in the five years prior to the Merger. [554] Dr. Hubbard explained that he chose the year ending on December 4, 2015, in order to avoid contaminating his regression analysis with news of the possible merger. [555]

***46** The literature in the record supports the use of comparable companies in a beta regression because companies in the same industry face similar “operating risks” and therefore should have similar operating betas.[556] This, of course, assumes that “truly” comparable peers exist that can meaningfully be compared to the target company.[557] Here again, Dr. Zmijewski failed convincingly to demonstrate that his comparable companies shared similar risk profiles with Jarden.[558] As Dr. Hubbard persuasively testified, Dr. Zmijewski provided no analysis or discussion to support this assumption.[559] Without a thorough explanation and corroborating evidence of how Dr. Zmijewski's comparable companies had risk profiles comparable to Jarden's “complex”[560] and “unique”[561] structure and business model, I am disinclined to consider on Dr. Zmijewski's Composite Beta.

Jarden's stock consistently traded in the upper quartile of market volume on the NYSE from 2011 to 2015.[562] And its share price had a positive correlation with the market, as defined by the S&P 500, throughout the same time period.[563] With this in mind, I am persuaded that Dr. Hubbard's decision to use daily interval measurements is reasonable, and his opinion that Jarden's market returns data provide a reliable measurement of Jarden's beta is supported by the literature in the record.[564]

Dr. Hubbard corroborated his calculated beta with a second regression using two-year weekly returns that yielded a Jarden-specific beta of 1.22.[565] Dr. Zmijewski's beta estimates were derived from a five-year period of weekly returns, and his Jarden-specific analysis produced a beta of 1.24 for Jarden alone.[566] The spread between Dr. Hubbard's beta and Dr. Zmijewski's Jarden-specific beta is 0.06, which, according to the literature, suggests that the Jarden-specific beta estimates have a low error rate across different time and interval measurements.[567] A narrow error rate between firm-specific beta estimates of different intervals and time periods indicates the estimates are converging on the company's true beta.[568]

Moreover, it is important to note that, when estimating beta, the goal is to evaluate Jarden's *future* beta, and by extension, the sensitivity of Jarden's share price to *future* market risk as predicted by its historical performance.[569] Because betas generally converge on the general market beta (1.0) over time,[570] and Jarden, by all indicators, was a mature, highly traded company, I am satisfied that Dr. Hubbard's beta (1.18) is a reasonable estimate of Jarden's share price sensitivity to future market risk.

• Equity Risk Premium

***47** Equity Risk Premium (“ERP”) “captures the compensation per unit of risk that investors demand in order to hold risky investments rather than riskless investments.”[571] The experts' disagreement over the proper methodology for estimating Jarden's ERP reflects the lack of consensus regarding this issue within the valuation community at large.[572] One aspect of the broader debate that has played out here is whether to approach ERP as Long-Term Historical ERP, Supply-Side ERP, or an adjusted hybrid ERP derived from the available data. As explained by Dr. Hubbard, when appraisers estimate ERP from Long-Term Historical ERP, they consult historical data regarding stock premiums, in his case from 1926 through 2015.[573] As explained by Dr. Zmijewski, Supply-Side ERP incorporates adjustments to the Long-Term Historical ERP to account for a long-term decline in risk premiums that upwardly bias the Long-Term Historical rate in order more effectively to represent recent market conditions.[574]

Dr. Zmijewski set Jarden's ERP at the Supply-Side ERP estimate of 6.03%.[575] Dr. Hubbard determined the proper ERP to be 6.47%, which is the mid-point between the Long-Term Historical ERP and Supply-Side ERP.[576] After considering the evidence, I am satisfied that Dr. Zmijewski's estimate of ERP reflects a more principled approach. First, there is strong support for the use of the forward-looking Supply-Side ERP in the valuation literature.[577] Second, as Dr. Zmijewski persuasively observes, Dr. Hubbard's “mid-point” ERP estimate is unexplained and appears to lack any methodological foundation.[578]

• Size Premium

Dr. Zmijewski opined that a size premium must be incorporated in the calculation of Jarden's equity cost of capital given that, according to the Duff & Phelps classification, Jarden is within the second decile of public companies, which justifies a size premium of 0.57%.[579] Dr. Hubbard implied that a Size Premium was not necessary but provided no credible explanation for that position.[580] The valuation texts in the record make the point that beta captures some, but not all of a company's size premium and that a size premium is an empirically observed correction to the CAPM.[581] I agree with Dr. Zmijewski and the literature that the CAPM should include a size premium when appropriate, as here, and adopt his size premium of 0.57% for Jarden.

* * * * * * * * * *

Dr. Zmijewski calculated a Composite Cost of Equity, but for reasons previously stated, I have disregarded estimates based on Jarden's so-called comparable companies. Dr. Zmijewski calculated a Jarden-specific Cost of Equity at 10.21%.[582] Dr. Hubbard calculated Jarden's Cost of Equity at 9.74%.[583] In my view, for reasons stated, neither view lines up entirely with the credible evidence. Accordingly, I have calculated Jarden's Cost of Equity with the following CAPM inputs that reflect what I deem proven by a preponderance of the evidence: Dr. Hubbard's Beta of 1.18, Dr. Zmijewski's Equity-Risk Premium of 6.03%, Dr. Zmijewski's Size Premium of 0.57% and both experts' risk-free rate of 2.14%. With these inputs, I have calculated Jarden's Cost of Equity to be 9.83%.

Jarden's Calculated WACC: Dr. Zmijewski calculated a Jarden-Specific WACC of 7.88%.[584] Dr. Hubbard calculated a WACC of 7.38%.[585] Once again, for reasons stated, I have found that neither experts' calculated WACC is supported entirely by the credible evidence. Instead, I calculate WACC with the following inputs: a 9.83% Cost of Equity, a 2.8% Cost of Debt, a 35% marginal tax rate and a capital structure of 63.9% equity and 36.1% debt. These inputs yield a WACC of 6.94% for Jarden.[586] Thus, I adopt a Discount Rate of 6.94%.[587]

3. The Final Calculation of Terminal Value

Based on the credible evidence, I calculate Jarden's terminal value to be $17.7 billion, using the following equation:[588]

$$TV_t = \frac{NOPLATPA_{T+1}(1 - \frac{g_\infty}{ROIC})}{WACC - g_\infty}$$

where:

TV_t = terminal value (at time T)
$NOPLATPA_{T+1}$ = unlevered free cash flow (at time T + 1).
$ROIC$ = incremental return on new invested capital
g_∞ = terminal growth rate
$WACC$ = Weighted Average Cost of Capital

In order to arrive at the unlevered free cash flow for year 2021, I subtracted the predicted revenue for 2021 from the predicted capital expenditures for 2021.[589] The predicted revenue for 2021 is $12.9 billion, 4.964% higher than the 2020 revenue.[590] The predicted capital expenditure for 2021 is $334 million, 2.6% higher than the 2020 capital expenditure.[591]

4. The DCF Calculation of Fair Value

Using 6.94% as the Discount Rate, I calculate Jarden's enterprise value using the following formula:[592]

$$EV = \sum_{t=1}^{t=\infty} \frac{FCF_t}{(1 + WACC)^t}$$

where:

FCF_t = unlevered cash flow in period t, terminal value in the final period
$WACC$ = Weighted Average Cost of Capital

The final adjusted enterprise value is $16.6 billion.[593]

5. Jarden-Specific Adjustments to the DCF Valuation

***49** In order to determine the final share price under a DCF approach, the appraiser must account for Jarden's excess cash and debt in its enterprise value.[594] Dr. Hubbard additionally adjusts for tax effects related to future profits not captured by tax rates, liability from net unrecognized tax benefits and pensions.[595] I do not find any of Dr. Hubbard's arguments for these additional adjustments persuasive and, in any event, his proposed further adjustments have a marginal impact on the final share value.[596]

a. Excess Cash

Companies commonly keep liquid cash in order to conduct their operations.[597] If the company holds more cash than necessary, the surplus is a source of value to the equity holders and must be added to the DCF valuation.[598] Jarden held $799 million of cash and cash equivalents at the end of the first quarter of 2016.[599] As of the Merger, Jarden required $50 million in cash for working capital purposes.[600] The excess cash balance, or the difference between the total cash and the required cash, is $749 million, which I add to the enterprise value.

b. Nonconvertible Debt

As of March 31, 2016, Jarden's non-convertible debt totaled $5.04 billion.[601] Debt is a claim on the assets of the firm and must, therefore, be subtracted from the DCF enterprise value.[602]

c. Convertible Debt

To measure the value of Jarden's unconverted convertible notes at the Merger Date, Dr. Hubbard uses a standard options pricing methodology to estimate the embedded warrants value since they are economically analogous to an option on Jarden's common stock.[603] This formula relies on various inputs for each series of notes, including the time remaining until maturity, the conversion price, the current value of Jarden's stock, the risk-free rate and the expected volatility of Jarden's stock returns.[604] Using these inputs, Dr. Hubbard estimated the equity components of the convertible notes to be $0.71 billion in total at the Merger Date.[605] He further valued the debt component of the convertible notes by discounting the remaining coupons and principal value of each note at Jarden's 5.3% cost of debt. In total, the value of the debt component of the convertible notes is $1.00 billion. The total value of Jarden's convertible securities is the sum of the debt and equity components. At the Merger Date, the value of Jarden's convertible debt totaled $1.71 billion.[606] Dr. Hubbard's approach was conservative, made sense and I adopt it here.

6. Number of Shares

I calculate the shares outstanding, following Dr. Zmijewski's calculation,[607] by subtracting the Jarden stock awards issuable to executives in connection with the merger transactions and the Jarden common stock expected to be issued upon assumed conversion of outstanding Jarden convertible notes from the total estimated shares of Jarden's common stock entitled to the Merger consideration. With these inputs, the total amount of outstanding shares and restricted stock units as of the Merger was 219.9 million common shares.[608]

7. Equity Value per Share from DCF Analysis

***50** After adding non-operating assets to the enterprise value, and subtracting non-operating liabilities, Jarden's equity value as of the Merger Date was $10.59 billion. On a per share basis, the DCF valuation is $48.13.

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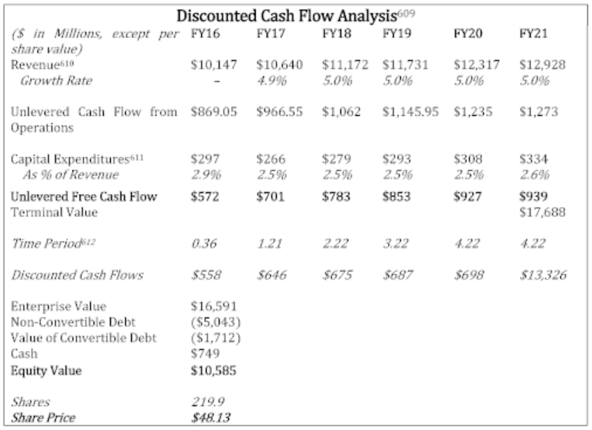

Discounted Cash Flow Analysis[609]

($ in Millions, except per share value)	FY16	FY17	FY18	FY19	FY20	FY21
Revenue[610]	$10,147	$10,640	$11,172	$11,731	$12,317	$12,928
Growth Rate	-	*4.9%*	*5.0%*	*5.0%*	*5.0%*	*5.0%*
Unlevered Cash Flow from Operations	$869.05	$966.55	$1,062	$1,145.95	$1,235	$1,273
Capital Expenditures[611]	$297	$266	$279	$293	$308	$334
As % of Revenue	*2.9%*	*2.5%*	*2.5%*	*2.5%*	*2.5%*	*2.6%*
Unlevered Free Cash Flow	**$572**	**$701**	**$783**	**$853**	**$927**	**$939**
Terminal Value						$17,688
Time Period[612]	*0.36*	*1.21*	*2.22*	*3.22*	*4.22*	*4.22*
Discounted Cash Flows	*$558*	*$646*	*$675*	*$687*	*$698*	*$13,326*
Enterprise Value	$16,591					
Non-Convertible Debt	($5,043)					
Value of Convertible Debt	($1,712)					
Cash	$749					
Equity Value	**$10,585**					
Shares	*219.9*					
Share Price	***$48.13***					

[Editor's Note: The preceding image contains the reference for footnote[609], [610], [611], [612]]

8. The DCF Valuation Comports With the Market Evidence

As indicated above, I have determined that the Unaffected Market Price, $48.31, is a reliable indicator of Jarden's fair value as of the Merger Date. While I have questioned the reliability of the Merger price less synergies approach, I recognize that the most reliable estimate of fair value under that approach is approximately $46.21. My DCF valuation yields a fair value of $48.13. What stands out here, of course, is that Petitioners' proffered estimate of fair value for Jarden of $71.35 is, to put it mildly, an outlier.

Based on the preponderance of evidence, I am satisfied that the Unaffected Market Price is the best evidence of Jarden's fair value on the Merger Date. Insofar as I am obliged to articulate a principled, evidence-based explanation for the delta between the Unaffected Market Price and the DCF valuation (here, $0.18 per share), I am satisfied the difference reflects the subjective imperfections of the DCF methodology. The DCF valuation corroborates the most persuasive market evidence and provides comfort that I have appraised Jarden as best as the credible evidence allows.

III. CONCLUSION

For the foregoing reasons, I have found the fair value of Jarden shares as of the Merger was $48.31 per share. The legal rate of interest, compounded quarterly, shall accrue from the date of closing to the date of payment. The parties shall confer and submit an implementing order and final judgment within ten days.

All Citations

Not Reported in Atl. Rptr., 2019 WL 3244085

Footnotes

[1] Trial Tr. 1315:21–1316:5.

[2] 8 *Del. C.* § 262(h).

[3] *DFC Global Corp. v. Muirfield Value P'rs, L.P.*, 172 A.3d 346, 367 (Del. 2017). *DFC* explained that the statutory definition of fair value has been distilled further to require the court "to value the company on its stand-alone value." *Id.* at 368.

[4] *Id.* at 367 (citing *Cavalier Oil Corp. v. Hartnett*, 564 A.2d 1137 (Del. 1989)). As the Court further explained, "the definition of fair value used in appraisal cases is a jurisprudential concept that has certain nuances that neither an economist nor market participant would usually consider when either valuing a minority block of shares or a public company as a whole." *Id.*

[5] *Gilbert v. M.P.M. Enters., Inc.*, 1998 WL 229439, at *3 (Del. Ch. Apr. 24, 1998) (noting that while certain approaches to a DCF valuation might be endorsed in other cases, the experts endorsing those approaches had not been "subject to the crucible of cross-examination" in the appraisal trial conducted by the court and the court would not consider their testimony from other cases). *See also Merion Capital L.P. v. Lender Processing Servs., Inc.*, 2016 WL 7324170, at *16 (Del. Ch. Dec. 16, 2016) (noting that the "relevant factors" informing the fair value determination will "vary from case to case depending on the nature of the [acquired] company"); *DFC*, 172 A.3d at 388 (observing: "[i]n some cases, it may be that a single valuation metric is the most reliable evidence of fair value and that giving weight to another factor will do nothing but distort that best estimate. In other cases, it may be necessary to consider two or more factors."); D.R.E. 702 (recognizing that lay fact-finders may rely upon expert testimony when the expert's "scientific, technical or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue"). In this regard, it is worth noting that submitting the fair value determination to a "court-appointed 'appraiser' " was "essentially required practice under the appraisal statute before 1976." Lawrence A. Hammermesh & Michael L. Wachter, *Finding the Right Balance in Appraisal Litigation: Deal Price, Deal Process, and Synergies*, 73 Bus. Law 961, 976 (2018). Now that expert "appraisers" have been "eliminated as a statutory requirement," it is for the court to decide fair value based on its assessment of the factual evidence presented at trial, including expert evidence, using traditional fact-finding methods. *Id.*

[6] *See DFC*, 172 A.3d 346; *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*, 177 A.3d 1 (Del. 2017); *Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc.*, 2019 WL 1614026 (Del. Apr. 16, 2019).

[7] *DFC*, 172 A.3d at 388.

[8] In this regard, I reiterate with renewed appreciation then-Chancellor Chandler's astute observation in the *Technicolor, Inc.* appraisal saga:

> [V]aluation decisions are impossible to make with anything approaching complete confidence. Valuing an entity is a difficult intellectual exercise, especially when business and financial experts are able to organize data in support of wildly divergent valuations for the same entity. For a judge who is not expert in corporate finance, one can do little more than try to detect gross distortions in the experts' opinions. This effort should, therefore, not be understood, as a matter of intellectual honesty, as resulting in the fair value of a corporation on a given date. The value of a corporation is not a point on a line, but a range of reasonable values, and the judge's task is to assign one particular value within this range as the most reasonable value in light of all the relevant evidence and based on the considerations of fairness.

Cede & Co. v. Technicolor, Inc., 2003 WL 23700218, at *2 (Del. Ch. Dec. 31, 2003), *aff'd in part, rev'd in part on other grounds*, 875 A.2d 602 (Del. 2005), *withdrawn from bound volume, opinion amended and superseded*, 884 A.2d 26 (Del. 2005).

[9] Respondent's expert undertook a precedent transactions analysis as well but the parties did not engage on this valuation approach at trial, so I will not address it here. *See* JX 1816 at ¶11.

[10] *DFC*, 172 A.3d at 369–70 (observing that “[m]arket prices are typically viewed [as] superior to other valuation techniques because, unlike, e.g., a single person's [DCF] model, the market price should distill the collective judgment of the many based on all the publicly available information about a given company and the value of its shares.”).

[11] *See* *ACP Master, Ltd. v. Sprint Corp.*, 2017 WL 3421142, at *31 (Del. Ch. July 21, 2017) (collecting cases and noting that if the court were to rely upon “deal price, it would have to determine the value of synergies and back them out.”).

[12] To the extent the parties sought to rely upon valuation texts or articles addressing valuation methodologies, they were directed to submit these sources as evidence in the case. Unlike a law review article cited by a party in support of a legal proposition, a text or scholarly article addressing economic or valuation principles contains factual matter, the admissibility of which must be tested under Delaware's Uniform Rules of Evidence. In my view, it is not proper for parties to an appraisal case, or any other case for that matter, to refer to, or expect the court *sua sponte* to refer to, a scholarly work addressing a matter that has been the subject of expert testimony without first having the work received as evidence in the case or at least tested under evidentiary standards. Nor is it proper, in my view, for parties to an appraisal case to cite to decisions of this court, or our Supreme Court, for the proposition that a particular valuation methodology should be applied to value the target company. While legal authority may support the contention that a valuation methodology has been accepted by Delaware courts as generally reliable, I see no value in referring to the factual conclusions of another court in another case while appraising the fair value of another company when attempting to fulfill the statutory mandate that I determine the fair value of this Company.

[13] *Dell*, 177 A.3d at 21 (quoting *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214, 218 (Del. 2010) (emphasis in original)); *see also* *Gholl v. eMachines, Inc.*, 2004 WL 2847865, at *5 (Del. Ch. Nov. 24, 2004) (noting that both parties bear a burden of proof in a statutory appraisal trial and holding that, “[i]f neither party satisfies its burden ... the court must then use its own independent business judgment to determine fair value.”).

[14] Stip. Joint Pre-Trial Order (“PTO”) ¶¶1, 6, 36.

[15] PTO ¶41. Trial Tr. 49:20–50:10 (Lillie). Because consumable household staples primarily comprised Jarden's product offerings, Jarden's growth correlated to Gross Domestic Product (“GDP”) growth. JX 860 at 1 (“As we suspected [Jarden] is a GDP growth business”).

[16] PTO ¶36.

[17] *Id.* ¶39.

[18] *Id.* ¶1.

[19] *Id.* ¶¶14–35.

[20] JX 1780 (Franklin Dep.) at 5:14–18.

[21] JX 1778 (Ashken Dep.) at 77:11–17.

[22] JX 1778 (Ashken Dep.) at 9:3–5; JX 1780 (Franklin Dep.) at 5:20–25.

[23] PTO ¶62.

[24] JX 1777 (Lillie Dep.) at 195:17–23.

[25] PTO ¶54.

[26] JX 1778 (Ashken Dep.) at 8:24–11:5.

[27] Trial Tr. 368:3–19 (Franklin).

[28] Trial Tr. 367:15–22, 467:20–22 (Franklin).

[29] JX 1778 (Ashken Dep.) at 11:9–10, 15:20–22.

[30] *Id.* at 10:20–11:10.

[31] PTO ¶38.

[32] JX 1777 (Lillie Dep.) at 11:5–12:24, 49:6–50:13.

[33] JX 502 at 5; JX 1804 (Polk Dep.) at 17:15–21.

[34] *Id.*

[35] JX 502 at 6.

[36] *Id.* at 21.

[37] JX 1192 at 11; JX 1777 (Lillie Dep.) at 11:5–14; JX 1775 (Sansone Dep.) at 101:5–20, 146:21–147:3.

[38] JX 786 at 17.

[39] Trial Tr. 423:1–9 (Franklin).

[40] Trial Tr. 451:14–18, 451:19–21(Franklin); Trial Tr. 81:10–11 (Lillie) ("Q. That was one quarter miss in 13 years? A. Yes."); JX 1779 (Tarchetti Dep.) at 265:16–266:7.

[41] Trial Tr. 53:12–24 (Lillie); JX 1459 ("Consistent with its guidance, the Company expects that net sales for 2015 will be approximately $8.6 billion").

[42] JX 1519 at 47.

[43] *See* JX 1816 at ¶47. The S&P 400 refers to the Standard & Poor's MidCap 400 index.

[44] *Id.*

[45] *Id.* at ¶¶46–48 and Figure 11; JX 1439.

[46] JX 1816 at ¶¶45–48.

[47] *Id.* at ¶¶48–50; *see also* Trial Tr. 1019:24–1020:23 (Hubbard).

[48] Trial Tr. 370:17–18 (Franklin) ("We were building a business, both organically and by acquisition."); JX 578 at 33.

[49] JX 1519 at 40, 44; JX 30 at 36; JX 502 at 19; JX 1459.

[50] JX 1519 at 40.

[51] Trial Tr. 125:12–22 (Gross); JX 502 at 25; JX 1773 (Talwar Dep.) at 21:19–22:3, 27:6–10.

[52] The strategy included targeting: (i) category-leading positions in niche consumer markets; (ii) with recurring revenue and margin growth channels; (iii) robust cash flow characteristics, including substantial EBITDA multiples; (iv) a successful management team; and (v) strong transaction valuations, with value-generating presynergies. JX 502 at 25.

[53] JX 1778 (Ashken Dep.) at 24:25–25:21; JX 1773 (Talwar Dep.) at 28:4–13.

[54] *Id.*

[55] JX 1777 (Lillie Dep.) at 133:2–21; JX 1773 (Talwar Dep.) at 27:11–24.

[56] JX 502 at 11.

> [We] ... looked at everything. Again, it goes back to being professional opportunists, in terms of building a business. You've got to—you know, we were a fairly unusual group. We started from a $200 million business 15 years prior, to becoming a 10-plus billion dollar business 15 years later. It wasn't done from sitting behind a desk. We were building a business, both organically and by acquisition.

Trial Tr. 370:11–18 (Franklin).

[57] PTO ¶40.

[58] JX 763 at 25.

[59] JX 514 at 10.

60 JX 1393.

61 JX 763 at 22.

62 *Id.* at 17.

63 JX 1795 at 21.

64 PTO ¶110.

65 JX 527 at 23, 26.

66 *Id.* at 23; JX 606 at 3–4.

67 PTO ¶113.

68 JX 726 at 15.

69 *Id.*

70 Trial Tr. 455:3–9 (Franklin) ("Q. And in 2015, you were spending real money on direct-to-consumer and expanding your distribution channels. Correct? A. Well, we bought a business that expanded our distribution capabilities. We bought Jostens for the same kind of reason. It gave us a different access into schools.").

71 JX 726 at 11; JX 823 at 3–4.

72 JX 726 at 12.

73 JX 1816 at ¶¶46–48, Figure 11; JX 1439.

74 PTO ¶234. As of the Merger Date, Ashken was a director of Platform. *Id.* ¶61; JX 576 at 2.

75 PTO ¶235. As of the Merger Date, Lillie was a director of Nomad. *Id.* ¶63.

76 JX 1780 (Franklin Dep.) at 359:15–16; PTO ¶97. Lillie and Ashken were also investors in Mariposa. Trial Tr. 527:11–13 (Franklin).

77 PTO ¶282. But for the Merger, Franklin would have pursued the Royal Oak transaction for Jarden. Trial Tr. 559:4–560:5 (Franklin). Jarden's lead independent director, Michael Gross, also participated in the Royal Oak acquisition. *Id.*; JX 1807 (Gross Dep.) at 14:22–15:10. Gross and Franklin have been close personal friends for 30 years. JX 1807 (Gross Dep.) at 15:14–18.

78 PTO ¶249; JX 1807 (Gross Dep.) at 93:7–8. Ashken and Lillie were also investors in J2. JX 1770.

79 JX 765; JX 1804 (Polk Dep.) at 71:20–72:12; JX 1779 (Tarchetti Dep.) at 164:14–165:3.

80 JX 533; JX 490; PTO ¶125; Trial Tr. 584:12–585:24 (Polk). Phillips previously worked opposite Franklin in a transaction with Nomad. Trial Tr. 585:14–18 (Polk); Trial Tr. 373:6–18 (Franklin).

81 Trial Tr. 576:5–13 (Polk); JX 490; JX 524; PTO ¶123.

82 JX 533; PTO ¶125.

83 JX 576 at 2.

84 *Id.*

85 JX 1807 (Gross Dep.) at 28:9–19; JX 1788 (L'Esperance Dep.) at 121:10–122:3; JX 1786 (Wood Dep.) at 157:25–158:14.

86 PTO ¶79. Newell was a member of the NYSE and the S&P 500. PTO ¶84. It was followed by at least 16 financial analysts and, like Jarden, its stock exhibited the attributes of a narrow "bid-ask spread," a high average trading volume and a large public float. JX 1816 at ¶57, Figure 15.

87 Trial Tr. 566:21–567:8 (Polk).

88 Trial Tr. 567:9–569:3 (Polk); *see also* Trial Tr. 721:22–722:5 (Torres).

89 PTO ¶80. Trial Tr. 566:11–20 (Polk).

90 Trial Tr. 566:11–20 (Polk).

91 Trial Tr. 567:20–569:3 (Polk).

92 Trial Tr. 571:2–7 (Polk).

93 Trial Tr. 571:20–572:2 (Polk).

94 Trial Tr. 572:6–574:19 (Polk).

95 Trial Tr. 576:12–582:1 (Polk). *See* JX 655; JX 860.

96 Trial Tr. 581:10–17 (Polk).

97 Trial Tr. 581:18–582:1 (Polk).

98 Trial Tr. 584:12–24 (Polk); Tr. 373:19–24 (Franklin).

[99] Trial Tr. 375:5–14 (Franklin). As Franklin explained, "[i]f a CEO wants to meet with me, I'll always want to meet with him." Trial Tr. 376:17–20 (Franklin).

[100] JX 902; PTO ¶¶127, 129.

[101] Trial Tr. 588:3–13 (Polk).

[102] Trial Tr. 586:14–21 (Polk).

[103] Trial Tr. 376:13–20 (Franklin); Tr. 588:22–589:7 (Polk).

[104] JX 902 at 2.

[105] *Id.*

[106] JX 1788 (L'Esperance Dep.) at 54:13–22; JX 1786 (Wood Dep.) at 25:2–7, 26:10–19. The Board met on September 28, 2015, but the minutes do not reflect any discussion of a potential transaction with Newell or Franklin's September 9th meeting with Polk. *See* JX 691; PTO ¶131.

[107] Trial Tr. 378:24–380:18, 480:16–17 (Franklin); JX 1788 (L'Esperance Dep.) at 57:2–23, 58:22–59:3 (Franklin called board members to advise them on meeting); JX 1807 (Gross Dep.) at 26:24–27:12 (same); JX 1786 (Wood Dep.) at 28:20–29:8, 33:20–34:4 (same).

[108] Trial Tr. 566:9–20 (Polk).

[109] Trial Tr. 598:10–16 (Polk); JX 1779 (Tarchetti Dep.) at 29:18–30:9, 32:10–33:9 (explaining Jarden "was by far the most likely [acquisition] candidate to reapply the Newell Rubbermaid business model" of consolidation, which "could release a large amount of value").

[110] JX 685 at 2; JX 902 at 2; PTO ¶132. Trial Tr. 383:23–384:8 (Franklin). Following the Merger, Tarchetti became the President of the combined entity. JX 1779 (Tarchetti Dep.) at 14:17–21.

[111] JX 1788 (L'Esperance Dep.) at 58:9–21; JX 1786 (Wood Dep.) at 31:12–25; PTO ¶133. I note that Franklin's testimony that he did not intend to negotiate definitive deal parameters during the Boat Meeting was credible. Trial Tr. 486:11–16 (Franklin). It appears, instead, that Franklin intended to lay out certain expectations and then "tell[ ] [the] Newell [team that] if they had different expectations, they shouldn't bother spending time, effort, and money." Trial Tr. 489:14–17 (Franklin). As Franklin explained, "I didn't want to go down the path of having any real substantive conversations unless they understood that we were looking for a real premium." Trial Tr. 469:2–22 (Franklin); *see also* Trial Tr. 384:21–385:2 (Franklin); JX 1778 (Ashken Dep.) at 64:4–9 (explaining "we sort of made it very clear that Jarden wasn't for sale; but if we got an extraordinary offer our job was to create value for our shareholders, so we would always listen to whatever Mike had to say").

[112] JX 1794 (Christian Dep.) at 159:9–160:14; JX 1780 (Franklin Dep.) at 72:2–3; JX 1804 (Polk Dep.) at 85:24–86:7; JX 1779 (Tarchetti Dep.) at 305:24–306:10; PTO ¶134.

[113] JX 2502; JX 1778 (Ashken Dep.) at 64:17–65:4, 97:14–98:2; JX 1785 (LeConey Dep.) at 27:10–21; Trial Tr. 369:22–370:2, 471:11–472:16 (Franklin). While Jarden had asked Barclays to prepare some preliminary combination models and to do some "rough math" prior to the Boat Meeting (Trial Tr. 472:7–8 (Franklin); JX 688), Jarden had no formal analysis of its standalone value, nor had it retained a financial advisor when Franklin set the range for a transaction at $60–$69 per share. JX 1789 (Welsh Dep.) at 135:14–136:3; Trial Tr. 470:18–471:8 (Franklin).

[114] JX 1780 (Franklin Dep.) at 95:15–19. *See also* Trial Tr. 473:24–475:1 (Franklin) (explaining his sense of Newell's financial limits).

[115] Trial Tr. 391:24–392:10 (Franklin).

[116] Trial Tr. 385:10–14 (Franklin).

[117] Trial Tr. 385:24–386:4 (Franklin); Trial Tr. 666:6–7 (Polk) ("And I interpreted that to be between 60 and 69, which is a very wide range."); *see also* JX 1778 (Ashken Dep.) at 65:21–23 (referring to a price in the $60s as "a very, very, very, very full price").

[118] Trial Tr. 474:14–475:1 (Franklin); JX 1780 (Franklin Dep.) at 103:3–13.

[119] Trial Tr. 475:18–476:22 (Franklin).

[120] Trial Tr. 598:3–16 (Polk) (explaining that "the logic for the deal" was the expectation of synergies by recreating the success of Project Renewal); *see also* JX 674 at 2 (Polk noting that "there are tons of synergies because they have not done what we have done with Renewal (they are a holding company)") (emphasis in original).

[121] Trial Tr. 387:13–388:23 (Franklin); *see also* Trial Tr. 664:3–665:8 (Polk).

[122] Trial Tr. 391:24–392:10 (Franklin).

[123] JX 1788 (L'Esperance Dep.) at 60:5–13 (discussing Franklin's view that any offer "needed to start with a 6 handle" and explaining that "[g]iven where the stock was trading, that made a lot of sense"); *see also* JX 1786 (Wood Dep.) at 49:3–11.

[124] Trial Tr. 548:22–549:4 (Franklin); JX 1789 (Welsh Dep.) at 135:14–136:3.

[125] JX 769; JX 785; JX 915; JX 977; JX 1073; JX 1203; JX 1862; Trial Tr. 550:16–20 (Franklin); JX 1789 (Welsh Dep.) at 137:22–138:18.

[126] Trial Tr. 392:8–15 (Franklin); *see also* JX 1778 (Ashken Dep.) at 62:23–63:2.

[127] Trial Tr. 392:16–393:6 (Franklin).

[128] *Id.*

[129] Trial Tr. 393:7–394:2 (Franklin).

[130] *Id.*

[131] JX 2502 at 2, 10.

[132] JX 775.

[133] JX 871 at 1; JX 1779 (Tarchetti Dep.) at 259:14–261:13.

[134] On October 13, 2015, the day prior to the Jostens announcement, Jarden's stock price was $50.69. Jarden's stock price fell to $44.80 by the end of October 2015. PTO Ex. A; *see also* JX 1816 at ¶¶66–68.

[135] Trial Tr. 404:1–9 (Franklin). Franklin testified, "we were buyers up to [$]49, which we considered full value at the time." Trial Tr. 404:16–18 (Franklin).

[136] JX 900 at 2.

[137] JX 1565 at 85; PTO ¶135. Trial Tr. 394:23–395:4 (Franklin).

[138] JX 1780 (Franklin Dep.) at 136:12–15; JX 1565 at 85. *See* Trial Tr. 492:5–10 (Franklin) (explaining Jarden's Board learned of the confidentiality agreement).

[139] PTO ¶136.

[140] JX 786 at 110; PTO ¶138; Trial Tr. 396:17–397:2 (Franklin); Trial Tr. 602:24–603:15 (Polk).

[141] JX 786 at 110; JX 1777 (Lillie Dep.) at 131:7–12, 148:6–149:5.

[142] JX 786 at 111; *see also* Trial Tr. 827:19–828:11 (Waldron).

[143] JX 1777 (Lillie Dep.) at 24:16–25:8.

[144] Tuck-in acquisitions usually amounted to less than 1% of Jarden's yearly revenue. *See, e.g.*, JX 380 at 11; JX 1778 (Ashken Dep.) at 20:6–16; JX 432 at 5; JX 380 at 3, 11.

[145] Trial Tr. 929:9–930:9 (Zenner).

[146] JX 1816 at ¶30; JX 1831, Ex. 5A. Jarden achieved "organic growth" of 4% (including tuck-in acquisitions) and adjusted organic growth of 3.2% (excluding all acquisitions), from 2011 to 2015. *Id.*

[147] Trial Tr. 106:13–107:3 (Lillie).

[148] Trial Tr. 106:1–9 (Lillie); JX 1777 (Lillie Dep.) at 252:15–253:6.

[149] Trial Tr. 604:3–12 (Polk) (explaining Newell did not use Jarden's projections because "I didn't believe 6 percent and 5 percent compounded. Those were really aggressive growth rates in the environment."); *see also id.* 604:22–605:21 (Polk) (explaining that Newell utilized more realistic projections when analyzing Jarden's value).

[150] JX 1252 at 12; JX 1247 at 29.

[151] JX 927 at 1.

[152] *Id.*

[153] JX 1045 at 31; JX 1205 at 44. With only minor adjustments for 2015 year-end actuals, the November Projections were also included in the Company's proxy statement regarding the Merger.

[154] JX 791 (Tarchetti told a colleague that "Martin change of control" was on a list of discussion points Franklin brought to the meeting on October 22); JX 1807 (Gross Dep.) at 33:20–35:4.

[155] JX 1807 (Gross Dep.) at 38:12–16, 67:13–25; JX 1788 (L'Esperance Dep.) at 89:6–8; JX 1786 (Wood Dep.) at 67:12–15, 68:11–13.

156 Trial Tr. 397:8–10, 399:6–10 (Franklin); *see also* JX 1789 (Welsh Dep.) at 154:4–10.

157 Trial Tr. 397:15–398:4 (Franklin) ("I thought it was a little odd that, you know, a potential $20 billion transaction would all hinge on the whims of the guy who is not the CEO, who is not even on the board ....").

158 *Id.*

159 Trial Tr. 398:5–20 (Franklin); JX 1779 (Tarchetti Dep.) at 201:6–202:7.

160 Trial Tr. 398:16–20 (Franklin).

161 Trial Tr. 615:5–14 (Polk); *see also* JX 799 at 2.

162 JX 1779 (Tarchetti Dep.) at 221:24–222:9; Trial Tr. 398:21–399:5 (Franklin).

163 JX 815; PTO ¶140; JX 1807 (Gross Dep.) at 35:9–36:17; JX 1786 (Wood Dep.) at 58:9–14.

164 JX 1786 (Wood Dep.) at 94:22–95:6; JX 1807 (Gross Dep.) at 46:17–20; JX 1785 (LeConey Dep.) at 87:2–13; JX 1789 (Welsh Dep.) at 162:20–163:9.

165 JX 815.

166 JX 1779 (Tarchetti Dep.) at 246:17–247:7; Trial Tr. 725:7–14 (Torres).

167 Trial Tr. 734:12–14 (Torres). Bain continued to analyze Jarden's category growth rates through closing. It eventually determined that Jarden's categories "were relatively weak and were actually losing market share," like the Coleman brand that lost distribution to dominant outlets such as WalMart. This prompted Bain to downgrade its category growth rate for Jarden to 2.5% as of closing. Trial Tr. 737:16–738:8 (Torres). When additional information became available post-closing, Bain further decreased Jarden's category growth rate to 2.2%. Trial Tr. 739:2–8 (Torres).

168 Trial Tr. 753:1–7 (Torres).

169 Trial Tr. 600:16–601:7 (Polk); *see also* JX 1309 at 80.

170 JX 706 at 3; Trial Tr. 746:22–23 (Torres).

171 Trial Tr. 741:4–742:2 (Torres).

172 JX 1779 (Tarchetti Dep.) at 251:9–14; Trial Tr. 722:8–16 (Torres).

173 Trial Tr. 598:10–16, 686:17–687:13 (Polk) (the "logic for the deal" was to apply the Newell integration playbook to Jarden's businesses); *see also id.* 699:6–9 (Polk) ("the costs associated with [Jarden's] decentralized model, that's where the synergies were").

174 JX 957 at 1.

175 *Id.* at 1–2.

176 *Id.* at 3 (Bain "highlighted three key benefits of the deal: transformational scale; high cost synergies; and likely above average revenue synergies due to channel overlap and the ability to apply the Growth Game Plan to selected categories at [Jarden]").

177 JX 973 at 42; Trial Tr. 767:2–24 (Torres).

178 JX 943 at 11.

179 Trial Tr. 614:4–18, 678:12–16 (Polk).

180 *Id.*

181 Trial Tr. 678:12–16 (Polk) ("The deal architecture assumed $500 million of gross synergies. If we didn't deliver $500 million of gross synergies, we would not have delivered the operating margin outcomes, and we would not have delivered accretive EPS.").

182 Trial Tr. 616:12–23 (Polk); JX 957 at 9.

183 JX 986; PTO ¶142.

184 JX 986 at 2.

185 *Id.*

186 JX 976 at 1–2; PTO ¶143.

187 JX 977.

188 JX 976 at 2–3; Trial Tr. 405:12–16 (Franklin).

189 JX 976 at 2; PTO ¶145.

190 JX 1786 (Wood Dep.) at 91:22–25; *see also* JX 1807 (Gross Dep.) at 48:3–8 ("Q. Did Jarden to your knowledge ever make a counteroffer to Newell? A. Not that I'm aware of. Q. Did the Board ever discuss parameters of the counteroffer? A. Not that I'm aware of.").

191 Trial Tr. 406:2–5 (Franklin).

192 JX 976 at 3.

193 Trial Tr. 562:4–5 (Franklin) ("The board wanted a second advisor."); *see also* JX 1778 (Ashken Dep.) at 100:12–101:6.

194 Trial Tr. 407:2–15 (Franklin). Barclays earned about $180 million from all of Franklin's businesses, including nearly $70 million from Platform alone in the four years between Platform's founding and the Merger Date. JX 1805; Trial Tr. 546:11–17 (Franklin). Barclays' history with Franklin and his businesses earned Franklin "Platinum client" status. JX 438; JX 1789 (Welsh Dep.) at 50:25–54:4. The Board made no inquiry regarding the thickness of Franklin's relationship with Barclays and there is no indication that either Franklin or Barclays made any effort to disclose their past relationships to the Board. *See* JX 976; JX 1070.

195 Trial Tr. 407:16–408:3 (Franklin).

196 Trial Tr. 560:22–24 (Franklin). Franklin explained to the Board that UBS had done work for the Company in the past for free, and described the UBS engagement in connection with the Newell transaction as giving UBS a "kiss." Trial Tr. 561:19–562:12 (Franklin) ("I described it at one point as giving them a kiss. It was a way of saying thanks for all the work that you've done that you didn't get compensated for. We—you know, you're on par with a couple of other firms to do this advisory work for us for the board, and we're happy to have you do that work."). Petitioners argue that this means UBS was paid for doing no work and that the payment diverted value from stockholders. This is not a fair characterization of UBS's role. The record reflects that UBS prepared Board decks, led discussions at Board meetings and was generally available to the Board as a sounding board. Trial Tr. 560:22–24 (Franklin); JX 1785 (LeConey Dep.) at 35:23–36:10. Whether UBS's compensation was fully earned is beyond the scope of this appraisal proceeding.

197 Trial Tr. 408:4–15 (Franklin); JX 1807 (Gross Dep.) at 44:10–14; JX 976 at 3; PTO ¶146. *See* JX 1565 at 89 ("With respect to UBS, it was noted that Ms. Ros L'Esperance is the Head of Client Corporate Solutions of UBS, and as such she would be recused from all deliberations and votes of the Jarden board, if any, in respect of the possible business combination with Newell Rubbermaid.").

198 Trial Tr. 408:24–409:8 (Franklin); JX 1001 at 1.

199 Trial Tr. 411:4–10 (Franklin).

200 Trial Tr. 409:1–8 (Franklin); Trial Tr. 618:24–619:3 (Polk); JX 1789 (Welsh Dep.) at 214:2–9; JX 1779 (Tarchetti Dep.) at 297:3–12, 300:8–16; JX 1807 (Gross Dep.) at 48:3–8; JX 1016 at 3; JX 1786 (Wood Dep.) at 91:15–92:2; PTO ¶148.

201 Trial Tr. 410:2–7 (Franklin).

202 JX 1778 (Ashken Dep.) at 116:22–119:20 ("[A]s we explained to them, we were not sellers. If you want to buy it, buy it. But don't waste our time. And it was a pretty acrimonious meeting. And it didn't make any difference to us whether we bought or sold."); *see also* Trial Tr. 410:8–24 (Franklin).

203 JX 1778 (Ashken Dep.) at 116:13–21.

204 JX 1778 (Ashken Dep.) at 119:6–9. Franklin similarly explained: "I went back to the board and said, This deal is dead. We tried to get a better offer out of them, and they refused." Trial Tr. 504:23–505:1 (Franklin).

205 JX 1069; JX 1066 at 2; JX 1149; PTO ¶153; JX 1064 at 2; *see also* Trial Tr. 619:18–620:5 (Polk) ($21.00 was "the limit to what we could afford" in cash consideration). According to Franklin, Newell "blinked" and agreed to increase its offer. Trial Tr. 412:19–413:2 (Franklin).

206 JX 1064 at 3; *see also* JX 1779 (Tarchetti Dep.) at 307:4–8 ("So by this stage, we'd obviously recommended to the board that we should try to consummate the transaction because we believed the synergies would create a lot of value for both parties.").

207 JX 1064 at 3.

208 JX 1070 at 2; PTO ¶¶155, 157. Franklin went over the terms of the revised offer, discussing the increased proposed cash consideration from $20.00 to $21.00 per share and the formula for determining the exchange

ratio. JX 1070 at 1. Barclays also presented its analysis of the updated offer, including a revised valuation analysis of Jarden as a standalone company. JX 1079 at 27–28.

[209] JX 1786 (Wood Dep.) at 112:5–6.

[210] *Id.* at 55:7–15.

[211] *Id.* at 55:10–56:9.

[212] *Id.* at 49:3–11. *See also* JX 1778 (Ashken Dep.) at 68:19–23, 69:23–70:4 ("When we looked at it and we thought, you know, if we can realize something that begins with a 6 for our shareholders is that more than we could expect if we continue to run the operations and did all the stuff? And we felt the answer was yes.").

[213] Trial Tr. 415:2–11 (Franklin).

[214] Trial Tr. 415:19–23 (Franklin).

[215] Trial Tr. 684:13–685:22 (Polk) (explaining that $500 million in synergies was assumed in the deal model, but "if there's future value to be created, more synergies, more growth, then any equity owner benefits from that"); *see also* Trial Tr. 415:2–15 (Franklin). Franklin described the $60.00 offer as "a full and fair price by any measure." Trial Tr. 444:5–10 (Franklin).

[216] JX 1070 at 2–3; PTO ¶¶155, 157. During the exclusivity period, Franklin and Ashken continued to negotiate the terms of the Merger Agreement, but also negotiated for Franklin, Ashken, and Lillie to continue with the combined company as paid consultants through Mariposa. *See* JX 906; JX 1061; JX 1074.

[217] JX 1786 (Wood Dep.) at 102:6–8 (explaining the Board's view that "it would not be value enhancing and perhaps very distracting to management to run an auction"). Respondent acknowledges that the Board never considered authorizing its bankers to reach out to other potential strategic buyers or financial sponsors. *Id.* at 94:22–95:6.

[218] *Id.* at 100:13–23.

[219] Trial Tr. 419:21–420:5 (Franklin); *see also* Trial Tr. 918:10–921:11 (Zenner) (explaining that other large consumer product companies had targeted businesses and were probably not interested in a diversified company like Jarden). Until Newell surfaced, no potential acquirer had expressed interest in Jarden during its entire 15-year history. Trial Tr. 425:10–13 (Franklin).

[220] JX 1786 (Wood Dep.) at 129:2–130:14; JX 1778 (Ashken Dep.) at 65:5–10.

[221] JX 1565 at 90; JX 1116 at 194–242.

[222] Trial Tr. 475:2–7 (Franklin); Trial Tr. 617:5–18 (Polk).

[223] Trial Tr. 621:9–13 (Polk).

[224] Trial Tr. 620:17–20 (Polk); Trial Tr. 406:24–407:1 (Franklin) ("[I]t would almost look odd if I didn't agree to serve as a director in the go-forward company."); JX 1779 (Tarchetti Dep.) at 120:3–16, 124:6–18 (discussing Franklin's role as the "face of Jarden" and the importance of having Franklin on the board of the combined entity, which would serve as an endorsement of the Merger); JX 1803 (Cowhig Dep.) at 153:24–154:3.

[225] Trial Tr. 686:17–687:13 (Polk) ("We wanted as part of—the deal terms, to get control of the company. Because there was no way that, without our leadership of the change agenda, those synergies were going to be realized."); JX 1778 (Ashken Dep.) at 153:15–19.

[226] JX 1778 (Ashken Dep.) at 163:13–14.

[227] *Id.* at 163:14–19 (explaining Newell was "very keen to have [the noncompete period] be four years" because Newell "had had a bad experience" before with competition from a past executive); *see also* JX 1807 (Gross Dep.) at 58:16–59:9 (noting Newell was "requiring that the management team extend their non-compete agreements from two to four years," which was a "big ask" since management was in the prime of their careers).

[228] Trial Tr. 526:18–20 (Franklin); JX 1779 (Tarchetti Dep.) at 347:15–349:7.

[229] JX 1233 at 2–3.

[230] *Id.*

[231] JX 1150 at 1–2; JX 1148; PTO ¶164. According to one witness, Newell's counsel leaked news of the Merger to a reporter. JX 1779 (Tarchetti Dep.) at 322:23–323:9.

[232] PTO, Exs. A, B.

[233] Trial Tr. 424:1–5 (Franklin); Trial Tr. 658:16–659:2 (Polk) (explaining that after the leak, Newell “had to” negotiate a fixed exchange rate because “we would have had exposure, potentially, if the stock had run one way or the other”); JX 1779 (Tarchetti Dep.) at 325:17–23 (fixing the exchange ratio was “in the interest of both parties because the stock prices were very volatile, and it was against the spirit of the agreement to not reflect the fact that there had been a leak”); JX 1778 (Ashken Dep.) at 136:12–17 (same).

[234] JX 1195 at 1.

[235] JX 1241 at 5; Trial Tr. 507:1–19 (Franklin).

[236] JX 1218 at 2. Had Jarden negotiated for a 0.90 exchange ratio, Jarden stockholders would have received $380 million in additional equity. *Id.*

[237] *Id.*

[238] JX 1207 at 3.

[239] JX 1205.

[240] JX 1202 at 1.

[241] *Id.*

[242] *Id.*

[243] JX 906 at rows 15–17; JX 1057; JX 1072 at 1–2.

[244] JX 1786 (Wood Dep.) at 158:15–159:5. In addition to his work as Jarden's General Counsel, Capps has served as General Counsel for Platform since 2016. S&P Global Market Intelligence, *Platform Specialty Products* (ESI:NYSE) (2019). Capps was also to be a beneficiary of any grant of 2017 and 2018 RSAs. JX 1565 at 146–147.

[245] JX 1231 at 18. There is no evidence the Compensation Committee ever looked at the employment agreements. JX 1231 at 16; JX 1807 (Gross Dep.) at 66:12–22, 81:15–82:2 (“I don't even know if I've seen it before.”).

[246] JX 1232; JX 1231 at 2.

[247] JX 1231 at 2; *see* JX 1255. Barclays delivered its written fairness opinion the following day. JX 1255.

[248] JX 1231 at 4. The Jarden board reiterated “its belief that the combined company's long-term value, prospects and benefits from the merger would exceed the value that could be realized by Jarden's stockholders were Jarden to continue operating on a stand-alone (independent) basis.” *Id.* at 3.

[249] *Id.* at 4, 9. The amended employment agreements for Franklin, Ashken and Lillie extended the term of their non-competes upon termination from two years to four years. JX 1326 at 15. They also confirmed the acceleration of certain RSAs in connection with the transaction. JX 1326 at 15; *see also* Trial Tr. 638:11–16 (Polk) (explaining that the negotiations concerning the RSAs were between the Jarden executives and the Jarden board). Franklin, Ashken and Lillie had three-year “evergreen” employment agreements. Under those agreements, they each were guaranteed their 2017 and 2018 RSAs, which the Board agreed to grant prior to the Merger. JX 1778 (Ashken Dep.) at 142:23–143:4, 146:4–7; Trial Tr. 517:9–19 (Franklin). Using Newell's stock price as of the Merger Date to determine the exchange ratio cash equivalent, Franklin received a total of $71.04 per share in Merger-related consideration, Ashken received a total of $76.11 per share and Lillie received an equivalent of $81.69 per share. JX 1818 at ¶40.

[250] JX 1231 at 2. The final Merger consideration represented a premium of 24.3% over the unaffected market price of $48.31 on December 4, 2015 (the last day of trading before the leak) and a premium of 24% over the VWAP of $48.35 for the 30-day period prior to December 11, 2015. *Id.*

[251] JX 1251 at 1–2.

[252] JX 1252 at 12; JX 1247 at 29; *see also* JX 775 at 5. Newell also used numbers in line with the Lender Presentation projections in its internal modeling and in the presentation made to rating agencies on December 7, 2015. JX 1154 at 41.

[253] JX 1230 at 10.

[254] JX 1228 at 7. Bain's report in advance of the meeting estimated total annual synergies ranging from $585 million to $1 billion, comprised of $500–$700 million in cost synergies and $85–$320 million in revenue

synergies. JX 1139 at 50. Bain was “very comfortable” Newell would meet at least the low end of its estimate range. Trial Tr. 773:14–22, 774:17–775:6 (Torres).

255 PTO ¶¶179, 181.

256 JX 1269 at 3.

257 PTO, Ex. A.

258 JX 1816 at ¶53. Jarden's stock price never closed above the implied Merger price prior to closing. *Id.* at ¶54.

259 *Id.* at ¶58.

260 *Id.* at ¶59.

261 *Id.* at ¶¶59–60.

262 JX 1519 at 68. Net income fell by nearly 40% as compared to 2014 year-end. *Id.* Jarden also adjusted its guidance downward twice during 2015. JX 454 at 4, 17, 41. And, in November 2015, Lillie advised investors that Q4 2015 organic growth would be in the 2–4% range, not the 3–5% range as earlier reported. JX 1034 at 1.

263 JX 1514 at 1–2; *see also* Trial Tr. 622:15–17 (Polk) (noting that Jarden fell below its goals for Q1 2016).

264 *Id.*; Trial Tr. 440:22–441:1 (Franklin); *see also* JX 1510; Trial Tr. 823:13–19, 856:1–6 (Waldron). The 2016 budget assumed Jarden would remain a standalone company. Trial Tr. 830:16–21 (Waldron).

265 JX 1562 (revised multi-year plan projecting $9.816 billion in total revenue); *see also* Trial Tr. 833:5–834:11 (Waldron). Newell asked for a copy of Jarden's updated multi-year plan in mid-March 2016, which Jarden provided. Trial Tr. 833:5–834:11 (Waldron). Newell later asked Jarden to reevaluate the operating cash flow assumptions in the plan. After doing this, Jarden circulated a revised version on April 1, 2016. Trial Tr. 832:24–838:3 (Waldron). *See also* JX 1563; JX 1597; JX 1598. While this revision included minor adjustments, the annual revenue and EBITDA projections remained the same as those estimated in the unrevised plan. *Id.*

266 Trial Tr. 834:12–835:11 (Waldron).

267 JX 1598; JX 1565; *see also* JX 1826 at ¶88, Figure 16. Newell incorporated the revised multi-year plan into its own multi-year forecast. Newell's forecast, however, assumed growth at 3.5%. JX 1691 at 95; Trial Tr. 626:4–627:15 (Polk).

268 PTO ¶183. Over 97% of voting Jarden stockholders approved the Merger (representing 83% of the outstanding shares). JX 1663 at 7.

269 JX 1816 at ¶10. The per share decrease in consideration from $60.03 to $59.21 reflects the change in Newell's stock price from signing to closing.

270 Trial Tr. 780:14–781:2 (Torres); *see also* JX 1373 at 11.

271 Trial Tr. 781:18–782:20 (Torres); JX 1691 at 7.

272 Trial Tr. 783:4–784:7 (Torres).

273 JX 1666; JX 2015; Trial Tr. 447:16–18 (Franklin); Trial Tr. 796:22–797:11, 798:20–799:11, 800:20–801:24, 802:18–804:3 (Torres).

274 JX 1801; JX 1802; Trial Tr. 802:18–803:4 (Torres). Franklin strongly objected to this strategy. JX 1808; JX 1809; JX 1825; JX 1807 (Gross Dep.) at 16:9–14.

275 JX 1803 (Cowhig Dep.) at 191:13–20.

276 Newell Brands announced an agreement to sell Waddington in April 2018 for $2.3 billion, almost $1 billion more than the price Jarden paid less than three years prior. Trial Tr. 450:18–451:2 (Franklin) (“Q. Okay. Waddington, you bought for 1.35 million [sic] in July of 2015. Correct? A. Correct. Q. And Newell sold that business this year for 2.3 billion. Right? A. Correct. Q. They made almost a billion on that. Right? A. Yes.”).

277 Trial Tr. 447:2–11 (Franklin); JX 1808; JX 1809; JX 1823; JX 1834.

278 JX 1803 (Cowhig Dep.) at 184:17–188:12; JX 1809.

279 Trial Tr. 447:12–15 (Franklin); JX 1809.

280 JX 1822.

281 Newell Brands, Inc., Form 8-K at 3 (dated May 17, 2018).

282 PTO ¶11.

283 D.I. 13.

[284] D.I. 35.

[285] D.I. 37.

[286] The expert reports were submitted under seal. At the close of this case, the Court will unseal the reports. Perhaps the legal and business academies will find interesting, and worthy of study and classroom discussion, how two such well-credentialed experts in their fields reached such wildly divergent conclusions regarding the fair value of the same company as of the same date.

[287] D.I. 154.

[288] 8 *Del. C.* § 262(h).

[289] *DFC*, 172 A.3d at 364 (quoting 8 *Del. C.* § 262(h)).

[290] *Dell*, 177 A.3d at 21 (quoting *Weinberger v. UOP*, 457 A.2d 701, 713 (Del. 1983)).

[291] *Id.*

[292] *Id.* at 22.

[293] *Aruba*, 2019 WL 1614026, at *6.

[294] *In re Appraisal of AOL Inc.*, 2018 WL 1037450, at *1 (Del. Ch. Feb. 23, 2018). *See also In re Appraisal of PetSmart, Inc.*, 2017 WL 2303599, at *27 (Del. Ch. May 26, 2017) (collecting cases).

[295] *In re Appraisal of PetSmart, Inc.*, 2017 WL 2303599, at *27 (citing Chuck Carlson, *Game of My Life: 25 Stories of Packer Football* (Sports Pub. 2004) (quoting Coach Lombardi as opening his first Packers team meeting in 1959, after twenty years of coaching, by saying: “Gentleman, we are going to relentlessly chase perfection, knowing full well we will not catch it, because nothing is perfect.”)).

[296] *Id.* (citing *Merlin P'rs LP v. AutoInfo, Inc.*, 2015 WL 2069417, at *14 (Del. Ch. Apr. 30, 2015) (observing that no “real-world sales process” will live up to “a perfect, theoretical model”)).

[297] *Dell, Inc.*, 177 A.3d at 35.

[298] Dr. Zenner testified that auctions are less effective as companies increase in scale and complexity. Trial Tr. 915:3–14, 916:17–917:17 (Zenner). For sale transactions over $5.4 billion, as here, only one in five are the product of an auction. *Id.*; JX 1817, App'x C-5. *See also* JX 1827 at ¶¶53–54 (explaining that the most logical strategic partners were too small to buy the Company); JX 1786 (Wood Dep.) at 101:18–102:11 (Jarden routinely “looked at likely people we could have business combinations with or that we could acquire ... [and] didn't think there was anybody out there who would come in and make a preemptive offer to buy the company”); Trial Tr. 921:12–923:16 (Zenner); JX 1817 at ¶95 (explaining that financial sponsors were not interested in Jarden because its leverage was too high); Trial Tr. 419:6–8 (Franklin) (“In 15 years of building the company, I haven't had one company come and sort of make an offer to buy Jarden.”); JX 1789 (Welsh Dep.) at 143:5–10 (“The combination with Newell was viewed to be a highly strategic combination that couldn't necessarily be replicated with other counterparties....”); JX 1785 (LeConey Dep.) at 88:3–4 (“UBS was not aware of any other buyers that were interested in acquiring all of Jarden.”).

[299] Trial Tr. 504:23–505:1 (Franklin) (“I went back to the board and said, This deal is dead. We tried to get a better offer out of them, and they refused.”); JX 1778 (Ashken Dep.) at 119:6–9; *see also* JX 1807 (Gross Dep.) at 41:3–15.

[300] JX 1816 at ¶169, Figure 23.

[301] I appreciate Franklin was no longer CEO when he negotiated with Newell. With regard to M&A, however, his role as Executive Chairman was tantamount to that of a typical CEO. Trial Tr. 367:15–22, 467:20–22 (Franklin).

[302] JX 1788 (L'Esperance Dep.) at 54:13–22, 58:9–21, 121:10–122:3; JX 1786 (Wood Dep.) at 25:2–7, 26:10–19, 31:12–25, 32:2–17, 157:25–158:14. Franklin's revelation at the Boat Meeting that he would like to exit from Jarden in order to have more time to pursue business ventures with his sons also made an impression on Polk and, when coupled with his direction regarding an acceptable offer price, likely communicated to Newell that he was eager, maybe overly eager, to do a deal. *See* JX 765 (Tarchetti reporting that Franklin revealed “his desire for an exit, which as the company figurehead is difficult. He says he would like to inve[st] in business with his sons having taken some money off the table (assuming he has about 0.5bn if this happened”)); Trial Tr. 71:20–72:12 (Polk); Trial Tr. 164:14–165:3 (Tarchetti). There is other evidence in the record that Franklin

was perceived as an anxious seller. *See* JX 576 (Bill Ackman's July 2015 email to Warren Buffett, copying Franklin, attempting to interest Buffett in acquiring Jarden); JX 533; JX 1786 (Wood Dep.) at 157:25–158:14; JX 860 (Centerview set up the first meeting between Franklin and Polk, marketing Jarden to Newell as a “willing seller.”); JX 902 at 2 (Polk stating that Franklin “cut straight to the chase” about his willingness to sell Jarden).

303 JX 1807 (Gross Dep.) at 38:12–16, 48:3–8, 67:13–25; JX 1786 (Wood Dep.) at 72:9–18, 91:15–92:2; JX 1788 (L'Esperance Dep.) at 89:6–8.

304 JX 1049. The Board justified the compensation awards after the fact. JX 1212 at 15; JX 1565 at 146. Moreover, as Franklin and Ashken were telling Newell they were entitled to the 2017 and 2018 RSAs, Jarden's Compensation Committee had not discussed the possibility of awarding those grants. JX 1145; JX 1202. The Board was told by in-house counsel Capps—who was also receiving 2017 and 2018 RSAs—that Jarden was contractually obligated to make these awards even though the agreements at issue were not clear on the point. JX 1629 at 5; JX 1786 (Wood Dep.) at 158:15–159:5. There are other troubling facts relating to the change-in-control payments, including that Franklin arranged for his long-time legal counsel to advise the Board with respect to the payments and the payments ultimately resulted in the lead negotiators for Jarden receiving substantially more in Merger consideration than Jarden's other stockholders. *See* JX 1145; JX 1234; JX 1235; JX 1236; Trial Tr. 534:18–536:11–18 (Franklin); JX 1780 (Franklin Dep.) at 362:20–22. Respondent argues the RSAs that made up most of the Merger consideration differential Franklin and the other Jarden managers received were owed to them “in the regular course absent a sale.” Resp't Jarden Corp.'s Opening Post-Trial Br. (“ROB”) at 57. The Merger agreement, however, terminated the employment contracts under which the RSAs were granted. *See* JX 1235. Franklin and the other Jarden managers claimed they were contractually owed the 2017 and 2018 RSAs under their employment agreements before the separation agreements even existed. JX 906 at rows 15–17; JX 1057; JX 1072; JX 1786 (Wood Dep.) at 158:15–159:5. The Board then justified the disconnect by explaining the 2017 and 2018 RSAs served as consideration for the commitment to add two more years to the non-compete covenants. JX 1565 at 146. Of course, when the dust settled, the separation agreements extended the term of the non-compete covenants by only one year. JX 1234; JX 1235; JX 1236.

305 JX 1805; Trial Tr. 546:11–17 (Franklin); JX 438; JX 1789 (Welsh Dep.) at 50:25–54:4; JX 1780 (Franklin Dep.) at 269:6–19.

306 By so finding, I do not intend to suggest that Franklin or any Jarden fiduciary breached any fiduciary duty. That inquiry is beyond the scope of this appraisal proceeding. *See* *In re Unocal Expl. Corp. S'holders Litig.*, 793 A.2d 329, 340 (Del. Ch. 2000) (noting that a breach of fiduciary finding is beyond the scope of statutory appraisal).

307 *Merion Capital LP v. BMC Software Inc.*, 2015 WL 6164771 (Del. Ch. Oct. 21, 2015).

308 *Id.* at *17.

309 JX 1817 at ¶¶32–33, 41–43.

310 Trial Tr. 686:17–687:13 (Polk) (“We wanted as part of—the deal terms, to get control of the company. Because there was no way that, without our leadership of the change agenda, those synergies were going to be realized.”); JX 1778 (Ashken Dep.) at 153:15–19.

311 JX 1269 at 3.

312 JX 1565 at 85.

313 JX 1228 at 7. Bain had estimated synergies ranging from $585 million to $1 billion, comprised of $500–$700 million in cost synergies and $85–$320 million in revenue synergies. JX 1139 at 50.

314 JX 1817 at ¶40; JX 1816 at ¶183;

315 JX 1100 at 18; JX 1804 (Polk Dep.) at 100:2–5, 101:15–16.

316 JX 1100 at 18.

317 Trial Tr. 649:5–8 (Polk); JX 2022 (“The premium is designed to get Newell management control.”); JX 1804 (Polk Dep.) at 100:2–5, 101:15–16 (When asked “how did you come to the conclusion that a modest premium to their current market valuation would give Newell control,” Polk responded “I knew that it was a quid pro

quo" and "[i]f we were going to pay a premium for the asset, we need management control."). Of course, Polk clarified that control was necessary to achieve the synergies since Newell was not satisfied that Jarden management would take the steps needed to create synergies. *See* Trial Tr. 686:17–22 (Polk).

318 JX 1804 (Polk Dep.) at 115:4–9.

319 Trial Tr. 476:3–5 (Franklin).

320 Trial Tr. 598:10–21, 599:14–600:6, 614:4–18, 678:12–6 (Polk); JX 1803 (Cowhig Dep.) at 62:20–63:2; JX 1779 (Tarchetti Dep.) at 29:6–30:9; JX 674 at 2 (September 2015 Polk email, emphasizing the "tons of synergies" to be realized by employing the Project Renewal strategy) (emphasis in original); Trial Tr. 725:7–14, 742:3–743:19 (Torres); JX 973 at 36; JX 1139 at 50, 56; JX 1565 at 67.

321 JX 1816 at ¶¶181–83; JX 1831 at ¶4, Figure 25; Trial Tr. 1087:23–1091:9 (Hubbard).

322 JX 1816 at ¶188 ("These results indicate that the market expected nearly all of the synergy value to accrue to Jarden shareholders, consistent with academic research finding that most of the benefits of mergers accrue to target-firm shareholders."); Trial Tr. 1090:18–20 (Hubbard).

323 *BMC Software*, 2015 WL 6164771, at *17.

324 To be clear, and as explained below, I am satisfied from the evidence that the Merger Price exceeded fair value. It is less clear, however, what exactly justified the premium Newell was willing to pay for Jarden. This is partially a product of the complications in valuing synergies where the merger consideration includes stock, versus a strictly cash-for-stock merger.

> In such a transaction, shareholders of both constituent corporations remain shareholders in the continuing combined enterprise. Thus, both groups—acquirer shareholders and target shareholders—are able to participate pro rata in gains arising out of the merger. Therefore, a premium to the target's shareholders cannot be justified, as in a cash acquisition, on the premise that it is the only way to permit those shareholders to share in the gains arising from the merger.

Lawrence A. Hamermesh, *Premiums in Stock-for-Stock Mergers and Some Consequences in the Law of Director Fiduciary Duties*, 152 U. Pa. L. Rev. 881, 884 (2003).

325 As noted, news of the potential merger between Jarden and Newell leaked to the public on Monday, December 7, 2015. *See* JX 1150 at 1–2; JX 1148; PTO ¶164; JX 1164; Liz Hoffman, Dana Mattioli & Dana Cimilluca, *Newell Rubbermaid, Jarden in Merger Talks, The Wall Street Journal* (2015), https://www.wsj.com/articles/newell-rubbermaid-jarden-in-merger-talks-1449521419 (last visited July 19, 2019). The last day Jarden stock was traded without being affected by news of the merger negotiations was Friday, December 4, 2015. JX 1231 at 2. On that day, Jarden stock closed at $48.31 per share. JX 1816 at ¶47.

326 ROB at 2.

327 Trial Tr. 1267:17–1268:5 (Hubbard) ("I've seen nothing in the record that would suggest to me the unaffected stock price is not the right anchor [for fair value].").

328 Trial Tr. 323:15–326:14 (Zmijewski). *See also* Trial Tr. 1021:2–9 (Hubbard) ("Does Dr. Zmijewski in his reports dispute that either Newell or Jarden traded in an efficient market? A. Not in his reports, no. Q. And did you hear that in his testimony? A. I did not. I was present, and I didn't hear that.").

329 JX 1816 at ¶45. *See also* JX 2032, Jonathan Berk & Peter DeMarzo, *Corporate Finance* 301 (Pearson Education Limited, 4th ed. 2017) ("Berk & DeMarzo, *Corporate Finance*"); JX 2515, Aswath Damodaran, *Investment Valuation: Tools and Techniques for Determining the Value of Any Asset* 4 (Wiley, 3d ed. 2012) (Damodaran, *Investment Valuation*); JX 2516, Tim Koller et al., McKinsey & Co., *Valuation: Measuring and Managing the Value of Companies* 37–38 (Wiley, 6th ed. 2015) ("Koller, *Valuation*").

330 JX 1816 at ¶45.

331 JX 2032, Berk & DeMarzo, *Corporate Finance* at 302.

332 JX 1816 at ¶45; Trial Tr. 323:15–324:4 (Zmijewski) (acknowledging that one "can look to stock price to corroborate a fair value conclusion"); Trial Tr. 1017:11–14 (Hubbard) ("For the unaffected stock price to be relevant, Your Honor, to your consideration, you need to believe that it's an unbiased indicator of the value of the firm. That's an efficient market.").

333 Dr. Hubbard stated,

> [t]here are tests for whether a market is efficient, tests that economists suggest, but tests that have been widely used in courts. So I used a number of factors that capture the scope of the firm, whether analysts follow it, transactions cost, liquidity, and so on. I do those tests for both Jarden and Newell and conclude that both trade in an efficient market, semi-strong form.

Trial Tr. 1017:11–14 (Hubbard).

[334] Resp't Jarden Corp.'s Pre-Trial Br. at 6.

[335] JX 1816 at ¶44, Figure 10.

[336] JX 242, Robert W. Holthausen & Mark E. Zmijewski, *Corporate Valuation: Theory, Evidence & Practice* 301–03 (Cambridge Business Publishers, 1st ed. 2014) ("Holthausen & Zmijewski, *Corporate Valuation*").

[337] JX 1345, Duff & Phelps LLC, *2016 Valuation Handbook: Guide to Cost of Capital* (Chapter 3) 9 (John Wiley, 2016) ("Duff & Phelps, *Valuation Handbook*").

[338] JX 1816 at ¶46.

[339] *Id.* at ¶48.

[340] *Id.*

[341] JX 2032, Berk & DeMarzo, *Corporate Finance* at 73.

[342] JX 1816 at ¶¶47–48.

[343] *Id.* at ¶47.

[344] *Id.* at ¶48.

[345] *Id.*

[346] *Id.*; JX 2032, Berk & DeMarzo, *Corporate Finance* at 73 ("The term *efficient* market is also sometimes used to describe a market that, along with other properties, is without arbitrage opportunities.") (emphasis in original).

[347] JX 1816 at ¶49; JX 2514 at 8–11; Trial Tr. 1019:2–16 (Hubbard).

[348] *Id.*

[349] JX 1816 at ¶51.

[350] *Id.*

[351] *Id.*

[352] *Id.* at ¶52.

[353] *Id.* at ¶¶52–53.

[354] *Id.*

[355] *Id.* at ¶54.

[356] *Id.*

[357] The Merger marks the rare instance where two public companies of comparable size, comparable capital structure and comparable stock trading patterns combine. As Dr. Hubbard explained, for most of the reasons one can conclude that Jarden traded in an efficient market, the same can be said for Newell. *Id.*, Figure 15.

[358] *Id.* at ¶58.

[359] *Id.* at ¶60. *See also id.* at ¶62 ("According to the analysts covering Newell at the time, consumer recession fears, merger integration risks, and the high initial leverage resulting from the Merger were key factors affecting Newell's stock price.").

[360] Jarden is justified in pointing out that while he raised the criticisms, Dr. Zmijewski did "not explicitly opine on whether or not any of these factors actually depressed Jarden's [unaffected] market price relative to fair value." JX 1826 at ¶98. *See also* JX 1828 at ¶90 (Dr. Zmijewski making observations regarding the Unaffected Market Price but not correlating them).

[361] JX 1828 at ¶90; JX 1826 at ¶98.

[362] *Id.*

[363] JX 1818 at ¶30.

[364] *Id.* at ¶¶29–31.

[365] JX 1826 at ¶¶99–100.

[366] *Id.*, Figure 17.

[367] *Id.*

[368] *Id.* at ¶¶101–04.

[369] JX 1818 at ¶31.

[370] *Id.*

[371] Trial Tr. 1022:21–1023:14 (Hubbard).

[372] JX 1826 at ¶¶101–04.

[373] *Id.* at ¶¶103–04. I acknowledge, and understand, Petitioners' "tethering" argument, but I reject it as not supported by the credible evidence. The argument is that the market was not efficient as of the Merger because, after the announcement of the Merger, "Jarden's stock price was tethered to Newell and to the perception of the stockholders of both companies that there was a large risk that Jarden could not be successfully integrated." Pet'rs' Post-Trial Opening Br. at 60. Newell's stockholders may have reacted to that risk, as reflected in the stock's performance after the announcement, but there is no evidence that Jarden's stockholders, or the market, associated that risk with Jarden. *See* Trial Tr. 1020:12–23 (Hubbard); JX 2514 at 9; JX 1816 at ¶¶184–90.

[374] JX 1826, Figures 18, 19.

[375] *Id.* That the November Projections did not really move the needle is not surprising. They were optimistic, to be sure, but their projected growth was consistent with prior forecasts, albeit at the top of the range. JX 927 at 1; Trial Tr. 106:1–107:3 (Lillie). They were also not out of line with the views of several of the many analysts that followed the Company. *See, e.g.*, JX 1401; JX 1407; JX 1439.

[376] JX 1818 at ¶¶37–39.

[377] JX 1826 at ¶¶108–12; JX 2505 (Zmijewski Dep.) 318:23–319:4, 320:8–11. Dr. Zmijewski's opinion that the market had not assessed Jarden's acquisitions of Jostens and Waddington, as best I can tell, is nothing more than speculation. The fact that the market reacted poorly to the Jostens acquisition does not mean it did not understand it. Nor is there credible evidence that the market did not know, or understand, that Jarden had leveraged up to do the Jostens and Waddington deals.

[378] Trial Tr. 1029:3–9 (Hubbard) ("academics differ in opinions on whether there is or isn't [a conglomerate discount]"); JX 1826 at ¶111 & n.176 (citing academic commentary rejecting the notion of a conglomerate discount).

[379] JX 1779 (Tarchetti Dep.) at 32–33.

[380] JX 1826 at ¶¶108–10; Trial Tr. 1029:10-21 (Hubbard); Trial Tr. 335:9–21 (Zmijewski) ("Q. So the holding company structure of Jarden, whatever its affects may be, were the operative reality of Jarden. Correct? As of the merger date? A. That's true.").

[381] JX 2505 (Zmijewski Dep.) at 319:22–320:16; JX 1818 at ¶¶37–39.

[382] JX 1778 (Ashken Dep.) 117:10–17; Trial Tr. 378:14–17 (Franklin).

[383] JX 1826 at ¶¶106–07. *See also* JX 59, Lawrence A. Hamermesh & Michael L. Wachter, *The Short and Puzzling Life of the "Implicit Minority Discount" in Delaware Appraisal Law*, 156 U. Pa. L. Rev. 1, 2 (2007).

[384] JX 1818 at ¶30.

[385] JX 1519 at 68; JX 1514 at 2.

[386] JX 1562; Trial Tr. 821:6–828:1, 830:7–835:11 (Waldron).

[387] JX 2502.

[388] JX 1780 (Franklin Dep.) 201:19–24.

[389] Trial Tr. 404:1–9 (Franklin); JX 900.

[390] JX 1780 (Franklin Dep.) 241:11–14.

[391] JX 900 at 2.

[392] *Id.* at 65.

[393] *Id.* It is not entirely clear to me that Dr. Zmijewski feels as strongly about his comparable companies valuation of Jarden as Petitioners do. *See* JX 1828 at ¶8 ("I do not consider revenue multiples to be reliable to value Jarden ....").

[394] JX 1816 at ¶200.

[395] JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 510, 527–30; Trial Tr. 1068:13–15 (Hubbard) ("If you use [a] comparables [analysis], you have to be sure they are really comparable or you are introducing error yourself.").

[396] JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 527–29.

[397] JX 2516, Koller, *Valuation* at 345.

[398] JX 2515, Damodaran, *Investment Valuation* at 20.

[399] JX 2032, Berk & DeMarzo, *Corporate Finance* at 296.

[400] JX 2516, Koller, *Valuation* at 345–46.

[401] *Id.* at 346; JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 528–29.

[402] JX 2516, Koller, *Valuation* at 346. *See also* JX 2032, Berk & DeMarzo, *Corporate Finance* at 710; Damodaran, *Investment Valuation* at 462 ("A comparable firm is one with cash flows, growth potential, and growth risk similar to the firm being valued .... The implicit assumption being made here is that firms in the same sector have similar risk, growth, and cash flow profiles and therefore can be compared with much more legitimacy").

[403] *Id.* Trial Tr. 1068:13–15 (Hubbard) ("I mean, it's really just a restatement of garbage in, garbage out. If you don't have genuine comparables, you're not going to get much out of the approach.")

[404] JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 529–30.

[405] *Id.* at 529.

[406] JX 2516, Koller, *Valuation* at 346.

[407] JX 2032, Berk & DeMarzo, *Corporate Finance* at 296–97 (emphasis supplied). *See* Trial Tr. 1068:13–15 (Hubbard) ("Given the difficulty of finding comparables for this company in particular, this is a methodology that I used for completeness and for the record for the Court, but it would not be a principal method I would advocate that the Court center on."). *See also* JX 1826 at ¶17.

[408] JX 1816 at ¶194; JX 2516, Koller, *Valuation* at 335 ("Empirical evidence shows that forward-looking multiples are indeed more accurate predictors of value than historical multiples are.").

[409] The EBITDA multiples valuation is generally considered more reliable than a revenue multiples approach because the EBITDA approach accounts for firms' operating efficiency and is not affected by leverage differences between firms. JX 2032, Berk & DeMarzo, *Corporate Finance* at 710.

[410] *Id.* at 710, 714; JX 2516, Koller, *Valuation* at 334–36; JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 532.

[411] JX 2516, Koller, *Valuation* at 334; Trial Tr. 159:7–14 (Zmijewski) ("Well, value is derived from what's going to happen or what you expect to happen in the future, so looking forward is always better than looks backward.... If historical information doesn't predict the future, it's not useful at all. It's only the forward-looking information that's useful.").

[412] *Id.* at 335–36.

[413] Trial Tr. 294:16–20 (Zmijewski); JX 1818 at ¶55 ("I base my set of comparable companies on those companies identified by Jarden's CEO, Mr. Lillie and the comparable companies used by Jarden's financial advisor, Barclays."); JX 1828 at ¶¶68–70. I note it is not clear that Dr. Zmijewski drew his peer set from the right Barclays list. The list endorsed by management was prepared by Barclays' equity analyst team while Dr. Zmijewski drew his list from the one prepared by Barclays' investment banking team. Trial Tr. 264:23–268:14 (Zmijewski). Moreover, I find Dr. Zmijewski's narrow focus on the Barclays list as the sole basis for his comparable companies peculiar given the extent to which he is critical of the Barclays Fairness Opinion. *See* JX 1818 at ¶¶1–42; JX 1826 at ¶¶46–47.

[414] JX 1826 at ¶17; JX 2516, Koller, *Valuation* at 346; JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 511 ("The key issues in valuing companies using market multiples are choosing appropriate comparable companies that would be priced similar to the company being valued and the making adjustments to the financial numbers used so that distortions to the valuation do not arise from accounting differences or certain events that can affect the financial statements in ways that render the numbers less useful for a market multiple valuation."). Dr. Zmijewski's decision apparently to ignore Barclays' qualification that its peer set

would have to be adjusted to account for qualitative differences between Jarden and the peer set was never adequately explained. Trial Tr. 294:24–296:24 (Zmijewski); JX 1565 at 127–28; JX 1205 at 11, 17.

[415] JX 1816 at ¶¶194–96.

[416] JX 1818 at ¶57.

[417] JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 525. Given his willingness to defer to peer sets prepared by others, it is surprising that Dr. Zmijewski failed to reconcile his exclusion of Kimberly-Clark and Colgate-Palmolive from his peer set with the fact that those companies were included in the peer sets developed by several of the analysts who followed Jarden. JX 1826 at ¶¶43–45.

[418] Dr. Hubbard flagged Dr. Zmijewski's size discrepancy in his rebuttal report. As Dr. Hubbard noted, although the market capitalization of Kimberly-Clark and Colgate-Palmolive were, respectively, 4.6 and 6.0 times *larger* relative to Jarden, three of Dr. Zmijewski's selected peers were correspondingly *smaller* than Jarden. JX 1826 at ¶¶40–43. WD-40 Company, Energizer Holdings and Helen of Troy were 7.3, 3.9 and 3.7 times *smaller* than Jarden, respectively, yet each of these firms remained in Dr. Zmijewski's peer set. *Id.* Dr. Zmijewski provided no credible justification for the disparate, asymmetrical treatment of large and small companies in his peer set. *Id. See also* Trial Tr. 935:6–936:17 (Zenner); JX 1827 at ¶¶45–47 (credibly addressing the fallacy created by Dr. Zmijewski's inconsistent approach to exclusion and inclusion of comparables based on size).

[419] JX 1826 at ¶¶15–17.

[420] Trial Tr. 1103:21–24 (Hubbard).

[421] JX 1816 at ¶195.

[422] JX 1826 at ¶¶38–35. Dr. Hubbard's peer set included firms with core business lines comparable to Jarden's core business, namely housewares, household appliances, consumer durables, apparel and personal products industry actors. JX 1816 at ¶195.

[423] JX 1826 at ¶17.

[424] JX 1818 at ¶¶55–57. As noted, Dr. Zmijewski offered no empirical analysis of Jarden's growth, risk, or value drivers as compared to any of the firms in his peer group. *Id. But see* JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 529–30 ("... simply selecting close competitors is not sufficient to ensure the companies are comparable .... Once we identify competitors, we analyze both the company being valued and the competitors with respect to characteristics that determine the variation in market multiples—such as future growth prospects, risk future profitability, and future expected investment requirements.").

[425] The party sponsoring a comparable companies valuation has the burden of proving that the target has validly assessed peers. *See In re Appraisal of SWS Gp., Inc.*, 2017 WL 2334852, at *10 (Del. Ch. May 30, 2017). Petitioners have not met that burden. In reaching this conclusion, I am mindful that Jarden, itself, employed a comparable companies analysis, among other approaches, when it performed internal valuations. But Petitioners have not proffered those valuations as evidence of Jarden's fair value. Instead, they have presented Dr. Zmijewski's version of a comparable companies analysis, which differed substantially from the Company's valuations. Accordingly, they had the burden of proving that the *Zmijewski* comparable companies valuation was a reliable indicator of fair value. For reasons I have explained, I have determined they have not carried that burden. In other words, the fact the Company employed comparable companies analyses in the past to value Jarden might be evidence that the methodology can work for Jarden, but the appraiser still has to apply the methodology in a principled way. That principled application of the methodology is what is lacking here. As a final note, for what it's worth, I did find Dr. Zmijewski's approach to selecting a proper multiple for Jarden to be more credible than Dr. Hubbard's approach, particularly given that he focused his multiples analysis on Jarden's 2016 and 2017 projected earnings, as prescribed in the valuation texts, while Dr. Hubbard based his multiples analysis on Jarden's historical EBITDA and revenue data. *Compare* JX 1818 at ¶¶74–76 (Zmijewski) *with* JX 1816 at ¶¶194–200. *See* JX 2032, Berk & DeMarzo, *Corporate Finance* at 710, 714; JX 2516, Koller, *Valuation* at 334–36; JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 532 (expressing preference for using forward-looking projections over a firm's historical earnings data when determining a proper multiple). Of course, this observation is worth little given the lack of credible evidence that Dr. Zmijewski created a proper peer set.

426 *Gonsalves v. Straight Arrow Publ'rs, Inc.*, 701 A.2d 357, 361 (Del. 1997). *See also* *M.G. Bancorp., Inc. v. Le Beau*, 737 A.2d 513, 525–26 (Del. 1999) (reiterating the Chancellor's role “as an independent appraiser” and observing that “[i]n discharging its statutory mandate, the Court of Chancery has the discretion to select one of the parties' valuation models as its general framework or to fashion its own”).

427 Dr. Zmijewski made two DCF calculations: an industry-specific DCF, which incorporated his comparable companies analyses (“Composite DCF”), and a Jarden-specific DCF (“Jarden-Specific DCF”). JX 1818 at ¶¶70–72.

428 JX 1816 at ¶149; JX 1831 at ¶3.

429 Pet'rs' Pre-Trial Br. at 33.

430 JX 2514 at 14. Indeed, as Jarden points out, “over 83% of value in each of [Dr.] Zmijewski's DCFs is from the terminal period.” Resp't Jarden Corp.'s Answering Post-Trial Br. at 60.

431 JX 1565 at 143.

432 JX 1816 at ¶¶75–78, Ex. 9; JX 1818 at ¶51, Ex. VI-7A.

433 I adopt Dr. Zmijewski's 35.0% marginal tax rate for Jarden because Dr. Hubbard made no effort to support his effective tax rate of 36.3%. JX 1816 at ¶¶96–97; JX 1828 at ¶¶9–11. A 35% marginal tax rate comports with the tax rates applied by Barclays, Centerview, Goldman Sachs and Jarden management—all of which set Jarden's marginal tax rate between 33% and 35%. JX 1828 at ¶¶9–10, 24.

434 JX 1816 at ¶¶75–78, Ex. 9; JX 1818 at ¶51, Ex. VI-7A.

435 JX 1816 at ¶¶75–78, Ex. 9. I track Dr. Zmijewski's free cash flows analysis with respect to the tax rate because I agree with him that Dr. Hubbard's approach to estimating Jarden's tax rate in the projected years is not adequately supported. JX 1828 at ¶¶9–11.

436 JX 2032, Berk & DeMarzo, *Corporate Finance* at 256.

437 *Id.* (“[W]e estimate the value of the remaining free cash flow beyond the forecast horizon by including a[ ] ... one-time cash flow at the end of the forecast horizon .... [The terminal value] represents the market value (as of the last forecast period) of the free cash flow ... at all future dates.”).

438 Trial Tr. 300:17–24 (Zmijewski) (“I paired the comparable companies risk assessment with a lower growth rate because the comparable companies ... were expected to perform at a lower growth rate. And for the Jarden-specific risk assessment, I used the midpoint of the expected inflation and expected GDP growth.”)

439 JX 1816 at ¶¶84–85.

440 *Id.*

441 *Id.*

442 JX 2515, Damodaran, *Investment Valuation* at 308.

443 Trial Tr. 930:2–9 (Zenner) (“So it's a little bit like saying I baked gluten-free bread for you, but I added some wheat because the consistency is going to be better. So it's kind of saying I'm providing organic growth, but I'm adding some tuck-in transactions.”).

444 For Jarden, “tuck-ins” were defined as an acquisition where the target company's last twelve months (“LTM”) of revenue was less than 1.0% of Jarden's LTM revenue. JX 1828 at ¶¶46–47.

445 JX 2515, Damodaran, *Investment Valuation* at 306–07 (“no firm can grow forever at a rate higher than the growth rate of the economy in which it operates”); JX 2516, Koller, *Valuation* at 122.

446 JX 1816 at ¶¶87–92; JX 1818 at ¶¶52–53.

447 JX 1818 at ¶¶52–53.

448 *Id.* at ¶¶53–54.

449 JX 1828 at ¶¶46–47.

450 JX 1818 at ¶¶52–54, Ex. VI-2. Polk estimated Jarden would grow at 3.0% (mirroring U.S. GDP growth), while Bain forecasted Jarden's growth to be between 2.0% and 4.0%. *Id.*

451 *Id.* at ¶¶67–69.

452 *Id.*

453 *Id.* at ¶¶70–72.

454 JX 1816 at ¶¶86–92.

[455] *Id.* at ¶¶89–90, Figure 20.

[456] *Id.* at ¶¶89–92, Ex. 5A.

[457] JX 1826 at ¶¶32–34, Figure 6. Dr. Hubbard maintains that the Company's 3.0% to 5.0% growth projections in the years following 2015 do not agree with its 2.2% historic organic growth because management incorrectly failed to account for "tuck-in" acquisitions. *Id.*; JX 1816 at ¶¶90–92.

[458] JX 1816 at ¶¶90–92, Ex. 5A; JX 1826 at ¶¶32–34, Figure 6.

[459] JX 1828 at ¶¶46–48.

[460] Trial Tr. at 1116–18 (Hubbard); JX 1831 at ¶8.

[461] JX 1831 at ¶8.

[462] JX 1826 at ¶32 ("[I]n recent history, tuck-ins contributed approximately 1.8 percentage points to the "organic" growth reported by management, indicating that Jarden would need to continue tuck-in acquisitions in order to achieve the five percent growth in the Proxy Projections.").

[463] Trial Tr. at 1116–18 (Hubbard); JX 1831 at ¶8.

[464] JX 1816 at ¶¶86–90.

[465] JX 1828 at ¶¶46–48.

[466] JX 1818 at ¶¶52–53.

[467] I note that the literature cautions against relying on comparable companies when estimating terminal value because inconsistencies in projected growth rates between the target company and those of the peer group can either overvalue or undervalue the target business. JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 212.

[468] Trial Tr. 215:20–216:17 (Zmijewski); JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 216–17.

[469] JX 1818 at ¶¶52–53.

[470] JX 1816 at ¶¶149–150; JX 1818 at ¶¶70–72; JX 1831 at ¶3.

[471] Trial Tr. 195:18–20 (Zmijewski) ("He's using accounting data as if it were economic concepts. That doesn't work. And so that's my major disagreement with him."); Trial Tr. 197:14–17 (Zmijewski) ("These are all economic concepts. They're not—you can't sort of say here's an accounting number and it matches this. These are economic concepts, not accounting concepts").

[472] JX 63; JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 235–37.

[473] *Id.*; JX 1828 at ¶¶37–38.

[474] JX 1828 at ¶¶34–35, 45. Dr. Zmijewski never expressly sets his TIR at 4.9%, but implicitly determines that net investment in 2021 and onward will equal $60 million, or approximately 4.9% of operating profits. JX 1826 at ¶¶54–55, 62, 66–67, Figure 14. Dr. Zmijewski also assumed that depreciation will equal capital expenditures in the Terminal Period, and that Jarden's cash investment required to drive terminal growth will grow coequally with Jarden's other financial metrics. JX 1818, Ex. VI-6A (Dr. Zmijewski made some adjustments to the historical financial data such that normalized depreciation is equal to normalized capital expenditures of $308 million).

[475] Trial Tr. 1045:21–1046:2 (Hubbard).

[476] JX 1816 at ¶94.

[477] Trial Tr. 1055:16–18 (Hubbard).

[478] *IR* = *g/RONIC*, where *g* is the terminal growth rate and *RONIC* is the return on new invested capital. JX 1816 at ¶94; JX 2516, Koller, *Valuation* at 31; JX 2515, Damodaran, *Investment Valuation* at 312–14.

[479] JX 1816 at ¶94. As discussed in more detail below, Dr. Hubbard calculates WACC as follows: Jarden's capital structure weights 36.1% debt and 63.9% equity, coupled with a cost of debt (after tax) of 3.20% and a cost of equity of 9.74%, results in a WACC of 7.38%. JX 1816 at ¶128, Ex. 15.

[480] Trial Tr. 196:9 (Zmijewski) ("Well, I have four issues.").

[481] Trial Tr. 196:11–16 (Zmijewski).

[482] Trial Tr. 197:19–198:17 (Zmijewski).

[483] Trial Tr. 198:7–15 (Zmijewski).

[484] Trial Tr. 198:18–199:6 (Zmijewski).

485 Trial Tr. 199:7–11 (Zmijewski).

486 Trial Tr. 1046:11–1049:23 (Hubbard); JX 2516, Koller, *Valuation* at 102, 250–56; JX 2515, Damodaran, *Investment Valuation* at 291, 299–300.

487 JX 1816 at ¶¶93–95, Ex. 10A; JX 1826 at ¶¶54–61.

488 JX 1816, Exs. 5A–5D (*compare* Ex. 10A starting at FY10 *with* Exs. 5A, C, D starting at FY11).

489 Trial Tr. 1055:14–18 (Hubbard) ("I just don't know of firms and industries that have both high and rising forever returns on invested capital."); Trial Tr. 1051:12–16 (Hubbard) ("you can't simply change your growth, particularly your real growth, which is what is being done in this experiment, and not have any additional investment"); JX 2514 at 21 (a graph depicting the dramatically outsized ROIC implicated by Dr. Zmijewski's TIR); JX 2516, Koller, *Valuation* at 19; JX 2515, Damodaran, *Investment Valuation* at 302; JX 2032, Berk & DeMarzo, *Corporate Finance* at 711.

490 This sets the TIR at the midpoint between Dr. Hubbard's TIR of 33.9% and Jarden's historic average investment rate of 21.6%. It also assumes a ROIC for Jarden of 11.2%, which is reasonable given Jarden's innovative and highly acquisitive growth strategy and a WACC of 6.94% (as discussed below). JX 1828 at ¶39.

491 Trial Tr. 1066:21–23 (Hubbard) ("Q. And if we could, did you estimate the weighted average cost of capital for purposes of your DCF analysis? A. I did. Both Professor Zmijewski and I tendered estimates of the weighted average cost of capital."); JX 1816 at ¶¶98–129; JX 1818 at ¶¶65–66.

492 JX 1816 at ¶¶98–99.

493 *Id.*; JX 1818 at ¶¶46–49; Trial Tr. 190:1–3 (Zmijewski) ("[WACC] is a standard calculation. You calculate the equity costs of capital, the after-tax debt cost of capital. You weight those two.").

494 *Id.*; JX 2516, Koller, *Valuation* at 295–97.

495 Trial Tr. 244:2–6 (Zmijewski) ("[W]e have the same risk-free rate. We have a different equity risk premium, a slightly different beta. He doesn't use a size premium. I do. So we have some differences in our calculations here.").

496 JX 1818 at ¶68; JX 1816 at ¶98; JX 2516, Koller, *Valuation* at 269.

497 JX 1818 at ¶49; JX 2516, Koller, *Valuation* at 269–72.

498 JX 1816 at ¶99; JX 2516, Koller, *Valuation* at 215–19.

499 *See* Trial Tr. 1070:2–6 (Hubbard).

500 JX 1816 at ¶¶100–03; JX 1818 at ¶63.

501 *Id.*

502 JX 1818 at ¶64.

503 *Id.*

504 JX 1816 at ¶98.

505 *Id.* at ¶¶100–04, Figure 21.

506 *Id.*

507 *Id.*

508 *Id.* at ¶¶100–07, Figure 21; JX 1777 (Lillie Dep.) at 86–87.

509 JX 1816 at ¶¶98–99.

510 *Id.* at ¶¶104–05.

511 *Id.*

512 JX 2516, Koller, *Valuation* at 217.

513 JX 1816 at ¶¶100–07, Figure 21; JX 1818 at ¶63. *See also* Trial Tr. 161 (Zmijewski) (explaining how he accounted for convertible securities).

514 JX 1818 at ¶64.

515 JX 1816 at ¶¶103–07, Figure 21.

516 JX 1816 at ¶105; JX 2516, Koller, *Valuation* at 295–97.

517 JX 2516, Koller, *Valuation* at 295–97.

518 *Id.* at 295; JX 1816.

519 JX 1816.

520 *Id.* at ¶¶100–07, Figure 21; JX 1777 (Lillie Dep.) at 86–87.

521 JX 1816 at ¶¶103–07, Figure 21.

522 *Id.* at ¶105.

523 *Id.*, Ex. 11A.

524 JX 2515, Damodaran, *Investment Valuation* at 211. *See also* JX 1816 at ¶106; JX 1818 at ¶63.

525 *Id.*

526 JX 1818, Ex. VI-5.

527 *Id.* at ¶64.

528 JX 1816 at ¶¶108–09. Trial Tr. 1218:11–13 (Hubbard) (Q. "You measured Jarden's cost of debt by using yield to maturity. Correct? A. I did.").

529 *Id.*

530 JX 1828 at ¶20; JX 2032, Berk & DeMarzo, *Corporate Finance* at 412 ("When the firm's debt is risky, however, the debt yield will overestimate the debt cost of capital, with the magnitude of the error increasing with the riskiness of the debt.").

531 Trial Tr. 1213:16–18 (Hubbard).

532 JX 1818 at ¶64; JX 1816 at ¶110.

533 *Id.*

534 JX 1816 at ¶110; JX 2516, Koller, *Valuation* at 278–87; JX 2032, Berk & DeMarzo, *Corporate Finance* at 385–92.

535 JX 1818 at ¶64; JX 2516, Koller, *Valuation* at 279; JX 2515, Damodaran, *Investment Valuation* at 208; JX 2032, Berk & DeMarzo, *Corporate Finance* at 387.

536 JX 1816 at ¶111; JX 1818 at ¶64.

537 *Id.*

538 JX 2515, Damodaran, *Investment Valuation* at 155; JX 2516, Koller, *Valuation* at 275–76; JX 2032, Berk & DeMarzo, *Corporate Finance* at 411–12.

539 JX 1818 at ¶58; JX 1816 at ¶112; JX 2516, Koller, *Valuation* at 279; JX 1345, Duff & Phelps, *Valuation Handbook* at 2–14; JX 2515, Damodaran, *Investment Valuation* at 183; JX 2032, Berk & DeMarzo, *Corporate Finance* at 413. *See* Trial Tr. 187:10–13 (Zmijewski) ("beta is a measure of risk of a company or an asset that you—that you can measure statistically using a statistical model.").

540 JX 2515, Damodaran, *Investment Valuation* at 183. *See also* JX 1816 at ¶¶113–20.

541 *Id.*

542 *Id.*

543 *Id.*

544 JX 2516, Koller, *Valuation* at 283–84. *See* JX 1816 at ¶114.

545 JX 2515, Damodaran, *Investment Valuation* at 188.

546 *Id.*; JX 2032, Berk & DeMarzo, *Corporate Finance* at 413. *See* JX 1816 at ¶115.

547 JX 1816 at ¶¶111–20; JX 1818 at ¶¶58–61.

548 JX 1818 at ¶¶58–61.

549 *Id.* at ¶¶60–61, Ex. VI-4.

550 *Id.* at ¶¶59–61, Ex. VI-5; JX 1828 at ¶16. Dr. Zmijewski explained that the Jarden-Specific Beta was higher due to a "lack of precision relative to the precision [of] using a set of comparable companies" and because of Jarden's higher long-term growth relative to that of his comparable companies. JX 1818 at ¶¶60–61.

551 JX 1816 at ¶¶114–16.

552 *Id.* at ¶¶117–20.

553 *Id.*

554 *Id.* at ¶¶114–16. Dr. Hubbard noted that the single year daily beta of 1.18 was "not substantially different" from his two-year weekly beta of 1.22. *Id.* at ¶¶117–20.

555 *Id.* at ¶¶114–16.

556 JX 2516, Koller, *Valuation* at 286.

[557] *Id.* at 283–85; JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 306 ("... if we have a set of *truly* comparable companies, we feel we can gain precision in our estimate of the cost of capital by using multiple companies.") (emphasis supplied).

[558] JX 1828 at ¶¶12–16.

[559] Trial Tr. 1068:13–1069:15 (Hubbard); JX 1826 at ¶¶72–75.

[560] JX 1818 at ¶29 ("More specifically, I discuss ... complexity of Jarden's information and holding company (or platform) business model strategy").

[561] Trial Tr. 104:7–105:18 (Lillie), 262:19–263:23 (Zmijewski) ("None of those companies is an apple-to-apple comparison to Jarden or each other. Comparable Companies—there just isn't any such thing as a twin company. It doesn't exist.").

[562] JX 1816 at ¶¶45–50. In addition, both experts' beta estimates are positive, which indicates a parallel correlation with changes in the overall market.

[563] JX 1816 at ¶¶112–20.

[564] *Id.*; JX 2516, Koller, *Valuation* at 284; JX 2515, Damodaran, *Investment Valuation* 183, 187–95.

[565] *Id.*

[566] JX 1818 at ¶¶58–61.

[567] JX 2515, Damodaran, *Investment Valuation* at 192–95; JX 1816, Ex. 22F; JX 1818 at ¶¶60–61.

[568] JX 2516, Koller, *Valuation* at 286; JX 2515, Damodaran, *Investment Valuation* at 192–93.

[569] JX 2516, Koller, *Valuation* at 281; JX 2032, Berk & DeMarzo, *Corporate Finance* at 413; JX 241, Holthausen & Zmijewski, *Corporate Valuation* at 295.

[570] JX 2515, Damodaran, *Investment Valuation* at 187.

[571] JX 1816 at ¶121.

[572] *See* Trial Tr. 1072:2–4 (Hubbard) ("So the question is, what is the equity risk premium. And this is one where economists have a range of views.").

[573] JX 1816 at ¶¶122–24. *See* Trial Tr. 1072:5–8 (Hubbard) ("My own view in my own work and in the work I'm tendering here is that the so-called historical risk premium is the best measure of the equity risk premium."). *See also* JX 2515, Damodaran, *Investment Valuation* at 161 ("In practice, we usually estimate the risk premium by looking at the historical premium earned by stocks over default-free securities over long time periods.").

[574] JX 1828 at ¶18. *See* Trial Tr. 1072:8–15 (Hubbard) ("There is an alternative view ... a so-called supply-side risk premium. I'm not quite sure why that word, because it's not about supply and demand, it's really about whether you include price earnings multiples expansion. That number is lower.") *See also* JX 1345, Duff & Phelps, *Valuation Handbook* at 11.

[575] JX 1828 at ¶17.

[576] JX 1816 at ¶126. Dr. Hubbard took the mid-point of the Long-Term Historical ERP at 6.9% and Supply-Side ERP at 6.03% to produce his 6.47% ERP estimate for Jarden. Trial Tr. 1072:16–19 (Hubbard) ("I prefer the historical risk premium. I'm cognizant of the fact Delaware courts have also paid attention to the supply-side risk premium. So I picked the midpoint of the two.").

[577] JX 1345, Duff & Phelps, *Valuation Handbook* at 5.

[578] JX 1828 at ¶18. The lower Supply-Side ERP is supported by Duff & Phelps' later recommended estimates of adjusted Long-Term ERP of 5.0% as of March 31, 2018. *See* Trial Tr. 1073:1–4 (Hubbard) ("But if one's view is your interest in supply side is governed by Duff & Phelps' recommendation, Duff & Phelps has, indeed, changed its recommended approach.").

[579] JX 1818 at ¶64.

[580] JX 1826 at ¶78; Trial Tr. at 1078:4–9 (Hubbard) ("I don't have a size premium. He does. My quibble is more the way he's estimated it, given the data source he has. But, again, for the Court's consideration in the interest of the Court's time, I don't think these are super important.").

[581] JX 242, Holthausen & Zmijewski, *Corporate Valuation* at 320–21 (discussing the "empirical evidence that the CAPM overstates the returns to large firms and understates the returns to small firms").

[582] JX 1818, Ex. VI-5.

[583] JX 1816 at ¶127.

[584] JX 1818 at ¶66.

[585] JX 1816 at ¶11.

[586] I note that this WACC is within the range calculated by Centerview but below the WACC calculated by Goldman Sachs, Deutsche Bank, RBC and Barclays.

[587] JX 2516, Koller, *Valuation* at 295–97.

[588] JX 1816 at ¶95; JX 2515, Damodaran, *Investment Valuation* at 313.

[589] *See* JX 1818 at ¶51.

[590] I took the average of the revenue growth rates for the provided fiscal years of 2017–20 to determine the percentage increase.

[591] I took the average of the capital expenditure growth rates for the provided fiscal years of 2017–20 to determine the percentage increase.

[592] JX 2515, Damodaran, *Investment Valuation* at 585. *See* JX 1818 at ¶60.

[593] In other words, I added the discounted cash flows from each time period in the FY16–FY21 range—$558 million, $646 million, $675 million, $687 million, $698 million, $13.3 billion respectively—to arrive at the total enterprise value.

[594] JX 1818 at ¶¶69–72; JX 1816 at ¶¶130–47.

[595] JX 1816 at ¶¶143–47.

[596] *See* Trial Tr. 1079:17–21 (Hubbard) ("Maybe I should start with the bottom line. If you were to look at all of these [enterprise value adjustments], they're a little over a dollar a share, and I think $1.06 altogether, because they go in different directions.").

[597] JX 1816 at ¶139.

[598] Trial Tr. 1081:17–20 (Hubbard) ("[E]ssentially you want to add back excess cash that the company has. And we both agree on that, and we both agree on what the total cash was. It was $799 million.").

[599] JX 1816 at ¶140.

[600] *Id.*

[601] *Id.* at ¶141.

[602] *Id.*; JX 2516, Koller, *Valuation* at 309; JX 2515, Damodaran, *Investment Valuation* at 440.

[603] JX 1816 at ¶142.

[604] *Id.*, Ex. 18C.

[605] *Id.*, Ex. 18A.

[606] *Id.*

[607] JX 1818 at ¶70. Dr. Hubbard adjusted his final share count number to align with Dr. Zmijewski's number after double counting Jarden's restricted stock. JX 1831.

[608] JX 1565 at 242.

[609] As explained above, the DCF Analysis makes the following assumptions: WACC equals 6.9%; Terminal Growth equals 3.1%; ROIC equals 11.2%; FY21 Revenue Growth equals 5%; FY21 Capital Expenditure as a percent of Revenue equals 2.6%; Fully Diluted Share Count equals 219.9 million.

[610] Drs. Hubbard and Zmijewski both agree on Jarden's Revenue numbers for FY16–FY20 reported in Standard and Poor's Capital IQ. *See* JX 1816, Ex. 9; JX 1818, Ex. VI-7A.

[611] Drs. Hubbard and Zmijewski both agree on Jarden's Capital Expenditure numbers for FY16–FY20 as derived from Standard and Poor's Capital IQ and Jarden's FY10-15 10K. *See* JX 1816, Ex. 9; JX 1818, Ex. VI-1.

[612] Time Period is calculated based on the mid-year convention used by Dr. Hubbard. JX 1816, Ex. 16. I note, for 2016, the mid-point uses the period from April 15, 2016 to December 31, 2016. *Id.*

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MEMORANDUM OPINION

Zurn, Vice Chancellor.

In this appraisal action, I must determine the fair value of each share of the subject company on the closing date of its acquisition. I find that the process by which the company was sold bore several objective indicia of reliability, which were not undermined by flaws in that process. I therefore find that the deal price is persuasive evidence of fair value, and give no weight to other valuation metrics. I deduct some synergies, but find others were not adequately proven. I undergo that synergies analysis solely to fulfill my statutory mandate, rather than to effectuate any transfer of funds between the parties, because the company prepaid the entire deal price and has no recourse for a refund under the appraisal statute.

I. BACKGROUND[1]

This appraisal action generated an extensive record. During six days of trial, the parties introduced 1,336 exhibits and lodged seventeen depositions in evidence.[2] Five experts and six fact witnesses testified live. These are the Court's findings based on a preponderance of the evidence.

Respondent Panera Bread Company ("Panera" or the "Company") is a national bakery-cafe concept in the United States and Canada.[3] Panera is a corporation organized and existing under the laws of Delaware, with headquarters in St. Louis, Missouri.[4] Until July 18, 2017, Panera's stock was listed on the NASDAQ stock exchange under the symbol "PNRA."[5]

On that date, JAB Holdings B.V. purchased Panera for $315.00 per share.[6] That entity is a private limited liability company incorporated under the laws of the Netherlands that indirectly has a controlling interest in JAB Holding Company, LLC.[7] JAB Holding Company, LLC is a private limited liability company incorporated under the laws of Delaware and headquartered in Washington D.C. that indirectly has held a controlling interest in Panera since the acquisition.[8] JAB Holding Company S.à.r.l. has an ultimate controlling interest in JAB Holdings B.V., JAB Holding Company, LLC and Panera.[9] I refer to all of these entities collectively as "JAB."

In the wake of JAB's acquisition, certain dissenting Panera stockholders ("Petitioners" or "Dissenting Stockholders") are entitled to an appraisal of the fair value of their Company shares in accordance with their demands.[10] Petitioners hold 785,108 shares of Panera's common stock.[11] Petitioners include Short Hills Capital Partners, holding 35,800 shares of Panera common stock;[12] Weiss Asset Management, including 2017 Arlington, LLC, holding 154,669 shares of Panera common stock;[13] Canyon International LLC, holding 31,794 shares of Panera common stock;[14] and Yellowstone Global LLC, holding 47,692 shares of Panera common stock.[15] Each of the Petitioners demanded appraisal before the vote on the merger, held the appraisal shares through the merger date, and maintained their appraisal demand.

***2** Relevant non-parties include Panera board members Domenic Colasacco, Fred K. Foulkes, Larry J. Franklin, Diane Hessan, Thomas E. Lynch, William W. Moreton, Ronald M. Shaich, Mark Stoever, and James D. White.[16]

Shaich founded Panera in 1981.[17] He served on the board from 1981 to December 2018 in various capacities, including Chairman, Co-Chairman, Executive Chairman, and Non-Executive Chairman.[18] Shaich served as Chief Executive Officer from 1984 to May 2010, when he stepped back from the Company to co-found an organization called "No Labels," which he hoped would reduce partisanship in American politics.[19] During this time, Shaich remained Panera's largest stockholder and Executive Chairman, and Moreton served as CEO.[20] In 2012, Moreton had a family issue and asked Shaich to return to a greater leadership position.[21] Shaich agreed and served as Co-Chief Executive Officer, along with Moreton, from March 2012 to August 2013.[22] At that time, Moreton stepped down as Co-Chief Executive Officer, and Shaich resumed his role as sole Chief Executive Officer until January 1, 2018.[23] The market and the restaurant industry both recognize Shaich as a visionary.[24]

Moreton joined Panera's board in May 2010, after serving as Executive Vice President and Chief Financial Officer from October 1998 to March 2003 and Executive Vice President and Co-Chief Operating Officer from November 2008 to May 2010.[25] Moreton also served as President and Co-Chief Executive Officer from March 2012 to August 2013, Chief Financial Officer (Interim) from August 6, 2014 to April 15, 2015, and Executive Vice Chairman from August 2013 to July 18, 2017.[26]

Colasacco, the lead independent director, served as an outside director along with directors Hessan, Foulkes, Franklin, Lynch, Stoever, and White.[27]

Panera's relevant management includes Blaine Hurst, who began serving as Panera's Chief Executive Officer after Shaich left that post in January 2018.[28] Prior to that time, Hurst served as Executive Vice President and Chief Transformation and Growth Officer from December 2010 to December 2016.[29] Then, Hurst served as Panera's President from December 2016 to January 2018.[30]

Michael Bufano has served as Panera's Chief Financial Officer, since April 2015.[31] Bufano also served as the Vice President of Planning from July 2010 to August 2014.[32]

Andrew Madsen was Panera's President from May 2015 to December 9, 2016, when he left the Company.[33]

A. Shaich Founds Panera And Leads It Through Unmatched Growth.

In 1980, Shaich founded a single 400-square-foot cookie store.[34] That store would eventually become Panera. In 1982, Shaich merged the cookie store with a small regional bakery called Au Bon Pain.[35] That entity purchased the Saint Louis Bread Company in 1987.[36] Shaich took this company public in 1991,[37] rebranded the Saint Louis Bread Company as Panera in 1997, and divested the Au Bon Pain division in 1999.[38] After the divestiture, Shaich changed the company's name to Panera Bread Company.[39] After divesting Au Bon Pain, Panera stock traded at $6.00 per share.[40]

***3** Panera pioneered a new restaurant segment called "fast casual," which found a niche between "quick service restaurants like McDonald's and Wendy's and restaurants like that and casual dining, full sit-down service."[41] From 2000 to 2010, Panera expanded rapidly into a national restaurant chain.[42] Panera operated in three segments: company bakery-cafe operations, franchise operations, and fresh dough and other product operations.[43] By 2004, Panera's stock was trading around $30.00 per share, and by 2010, it was trading around $70.00 per share.[44]

Despite the Company's growth, by 2010 or 2011, Shaich felt "great distress" because Panera's same store sales were weakening and market share gains slowed.[45] Increasingly, Panera faced competitive pressures and needed to differentiate for future growth.[46] In response to these pressures, Shaich spent his time as Executive Chairman focusing almost exclusively "on a range of strategic and innovation efforts for Panera."[47] During this time, Shaich wrote "the Amazon memo" on how he would compete with Panera if he were not part of the Company.[48] His vision focused on changing the guest experience, creating a new ordering system, and providing a delivery service.[49] After discussing these initiatives with Moreton, Shaich led the effort to prototype these ideas during the 2010–2012 period before re-assuming a management post as co-CEO in 2012.[50]

In 2013, Panera signaled to the market that it was "deploying significant transaction-driving initiatives."[51] By early 2014, *Fortune* magazine featured Panera's "big bet on tech," detailing how Shaich's early prototypes had developed into new company initiatives.[52] After launching that technology in fourteen cafes, the Company formally announced the Panera 2.0 initiative in April 2014.[53] Panera 2.0 offered "a series of integrated technologies to enhance the guest experience"[54] through "new mechanisms for ordering, payment, food production, and, ultimately, consumption."[55] Panera 2.0 enhanced ordering through Rapid Pick-Up, fast lane kiosks, and online/mobile ordering.[56] Panera also committed to "operational excellence" with new production equipment and systems to increase capacity and accuracy.[57] Along with these changes, Panera focused on "activat[ing] innovation in store design."[58] To adopt these initiatives, Hurst "create[d] a 'digital flywheel' whereby all systems and consumer touchpoints—point of sale (PoS), back of house, integrated customer data, big customer data, one-to-one marketing—are interconnected for operational gain."[59]

These initiatives rolled out in stages. In 2014, the Company kicked off Panera 2.0 with Rapid Pick-Up, an advanced ordering system.[60] Over the next two years, the Company rolled out the remaining Panera 2.0 initiatives to all company-owned bakery-cafes.[61]

***4** Panera developed other initiatives during this period of innovation. In 2013, the Company rolled out two initiatives including Panera at Home, providing consumer packaged goods, as well as Panera catering hubs, which were attached to bakery-cafes.[62] In 2015, Panera launched its "Food As It Should Be" campaign, developing "clean food" without "artificial colors, flavors, preservatives, and sweeteners."[63] In 2016, Panera rolled out its national delivery program.[64]

While leading Panera through these initiatives, in early February 2015, Shaich informed the board that he wanted to step away from Panera and pursue other endeavors.[65] Shaich had returned to Panera when Moreton needed him. And although Shaich extended his time with the Company through 2015, he did not want to remain at Panera forever.[66] Shaich explained to the board that after working on innovations as Executive Chairman during the 2010 to 2012 period, he "had come back to transform" Panera and felt he had "done [his] work in getting [Panera 2.0] going."[67] The board outlined a succession plan during a board meeting held on February 26, 2015.[68] The identified succession candidate, Madsen, became Panera's president in May 2015 with the intention of replacing Shaich as CEO in 2016.[69] But the board did not view Madsen as a suitable replacement,[70] so Shaich stayed on as CEO. Shaich annually reminded the board of his desire to leave.[71] At the time of the merger, Shaich owned approximately six percent of Panera's outstanding stock.[72]

B. Panera Tracks Its Initiatives Through A Five-Year Strategic Plan And Five-Year Financial Model.

In May 2015, management assembled all of Panera's new initiatives into a strategic plan (the "Five-Year Strategic Plan").[73] To track the financial effects of these initiatives, management also created a five-year financial model (the "Five-Year Financial Model") that tracked "between 15 and 30 key initiatives and many projects underneath each of them that we had various assumptions on, how they would perform, how they would roll out" and forecasted five years of future results.[74] Management based the Five-Year Financial Model on the Five-Year Strategic Plan and would evaluate them side-by-side "to really understand what the vision involved and the costs involved in what we saw."[75] This Five-Year Financial Model operated as a "roadmap" that management updated every six months and that the board discussed, at least in part, at every meeting.[76]

***5** At its core, the 2015 Five-Year Financial Model set a goal to double earnings per share over the next five years and "re-engage" double-digit earnings growth, including projected earnings before interest, tax, depreciation and amortization ("EBITDA") of nearly $750 million by 2019.[77] Shaich recognized that "[f]ew companies have taken on as audacious a path to renewal."[78]

Some board members were skeptical. Moreton described the Five-Year Financial Model as "what's classically called a hockey stick projection" that faced "healthy skepticism in the board."[79] Lynch wrote to Shaich in October 2016, "I worry, *though not with a lot of basis*, that we are overestimating our future earnings power. We are now in a negative 3 transaction comp environment and I am concerned that we *could* be overestimating our ability to fight this headwind."[80] Moreton recognized management risk-adjusted the Five-Year Financial Model "in part," but "major" risk remained around execution.[81] Colasacco considered Panera's Five-Year Strategic Plan as "not impossible, not a lie, not a bad faith effort in any way," but "one possible range of scenarios that could play out[.]"[82] Some analysts agreed: "[W]e remain on the sidelines as PNRA's stock appears to incorporate the benefits of its strategic initiatives and the outlook is not without risks."[83]

C. Investors React, And Panera Weighs Its Options.

In reaction to the Five-Year Strategic Plan, an investment fund called Luxor Capital threatened a proxy contest because it opposed the "very significant capital spending" necessary to support the plan.[84] The board engaged Goldman Sachs & Co. LLC ("Goldman") in March 2015 to advise it in a strategic review of potential opportunities to maximize stockholder value.[85] On June 25, 2015, Goldman presented potential strategic alternatives alongside valuation scenarios under the Five-Year Strategic Plan.[86]

***6** Consistent with the Five-Year Financial Model, Goldman "assume[d] 100% implementation success with no probability weighting adjustment."[87] For this reason, Goldman called the Five-Year Strategic Plan "aggressive" because "everything would have to go exactly as was foreseen," which "[t]hey didn't think [ ] was very likely."[88] Goldman advised that Panera's "growth initiatives were too early on in the game for the market ... to give [Panera] full credit for [the Five-Year Strategic Plan]."[89] Goldman evaluated a potential sale and advised that a financial sponsor would not have interest in Panera,[90] but identified a "limited number of potential strategic buyers," with Starbucks as the most likely.[91] At the end of the meeting, the board determined

> that while the Company would, as it had done in the past, continue to observe the markets and consider activities in the best interest of shareholders on an ongoing basis, given current conditions it was not in the best interest of the Company and its stockholders to engage in a process to initiate and pursue a strategic transaction or solicit interest from potential purchasers at this time.[92]

After consulting with Goldman, Panera agreed to some of Luxor's demands.[93] Luxor dropped their remaining demands after Panera "convince[d] them that [its] G&A actually was average to low for the industry as a whole, and the technology investments were necessary for initiatives."[94]

D. Panera Counteracts Failures And Plants Seeds For Future Rewards.

In 2016, following the adoption of the Five-Year Strategic Plan, Panera reduced its estimate for 2019 EBITDA by almost $128 million as "revenues hadn't increased in line with" expectations and the Plan was not "going quite as smoothly as [Panera] had hoped."[95] Panera offset the initiatives' high costs by orchestrating share buybacks, refranchising, and implementing nonstrategic cost reduction.[96]

In the wake of this setback, Shaich led efforts to publicize the Five-Year Strategic Plan to generate market recognition. Through "hundreds"[97] of presentations, Shaich shared Panera's plan of "sustained double-digit EPS earnings growth."[98] The market responded and gave Panera "a great deal of credit for the initiatives already done."[99] Panera's stock rose to $214.54 by July 2016.[100]

E. Panera and Shaich Weigh Their Options.

In the midst of Shaich's PR campaign, Shaich received an unusual call from Starbucks CEO Howard Schultz, proposing a visit.[101] Shaich discussed the visit with Colasacco and other board members, explaining, "Howard doesn't come up on a Saturday afternoon for just anything. Maybe he [i]s interested in a transaction."[102] To prepare, Shaich asked Goldman for an updated comparison of selected restaurant companies that Goldman had presented the year before in 2015.[103] This comparison included updated financial metrics for Starbucks and other restaurants in the fast growth, quick service, and casual dining segments.[104]

***7** When Schultz and Shaich met on July 31, 2016, Schultz proposed a collaboration between Starbucks and Panera "whereby Panera would provide food to Starbucks for lunch and breakfast and [Starbucks] would upgrade [Panera's] coffee program."[105] After the meeting, Shaich updated Moreton, Colasacco, and Lynch.[106] Lynch viewed this as "[t]he first step of the dance," so that Starbucks could pursue "a potential acquisition attempt by Starbucks of Panera."[107] Colasacco commented that the proposed collaboration was "[c]ertainly worth exploring further, though raises many questions."[108] And Moreton thought it was "interesting ... even if not tying every thing up in a nice bow."[109]

At the August 2 board meeting, the board reviewed elements of the Five-Year Strategic Plan and Five-Year Financial Model, per usual.[110] During the executive session of that meeting, Shaich informed the board about Starbucks' proposed collaboration.[111] Moreton characterized the board's response by explaining, "if [Starbucks] wanted to take advantage of our food and things, the best way to do that would be to acquire the company."[112] With that directive, Shaich had a new focus for future conversations with Schultz.[113]

Schultz had invited Shaich to Seattle to visit Starbucks' roastery that fall;[114] the teams met October 4 through 5.[115] Starbucks came to discuss a joint venture, with Starbucks selling Panera's food and Panera selling Starbucks coffee.[116] Shaich used this opportunity to attempt to solicit an offer.[117] Both Shaich and Schultz discussed their companies' "very intimate strategic plans."[118] During the visit, Shaich pitched Schultz the Five-Year Strategic Plan.[119] On October 26, Shaich rejected Schultz's joint-venture idea, but floated the idea that Starbucks could purchase Panera.[120] Schultz responded: "we're really interested in this. Let's get a group of people to work on it."[121]

Moreton worked with Shaich to interface with Starbucks and help conduct financial analyses.[122] In November, the companies discussed their shared goal "to determine whether [the] companies can unlock significant value by combining."[123] Panera proposed EBITDA and synergies figures for the combined companies, which Starbucks generally found reasonable.[124] Starbucks took this analysis and ran the numbers internally.[125] At the end of November,[126] Schultz called Shaich to explain that after giving it "some serious thought,"[127] Starbucks was "not going forward" with the transaction.[128] Although Starbucks viewed the combination as a "pretty good idea," Starbucks could not "get to [Panera's] public market price, let alone pay a premium"[129] and "there were other things going on within Starbucks."[130] The parties did not discuss any further.[131]

***8** In tandem with Panera's conversations with Starbucks, in August 2016, Shaich acted on his own initiative and asked Goldman to facilitate an introductory meeting with JAB.[132] Goldman inquired after JAB's CEO Olivier Goudet,[133] but JAB postponed meeting with Panera until "early the next year"[134] because JAB was busy pursuing an acquisition that fall.[135]

F. Panera Reaches An "Inflection Point," And Shaich Engages With JAB.

Although Panera continued to face competitive pressures, it experienced impressive growth and success with its initiatives. Panera's stock price rose from $170.00 per share in 2014 to $210.00 per share in early December 2016.[136] As of October 2016, Panera was the ninth most valuable restaurant company in America with a market capitalization of $4.5 billion.[137] Panera completed its Panera 2.0 rollout for company-owned bakery-cafes by the end of 2016.[138] And by the end of 2016, Panera served approximately 9 million customers per week, making it one of the largest food service companies in the United States.[139]

By January 13, 2017, Panera removed all of its "No No List" ingredients in pursuit of its "clean food" goal.[140] Panera hit another benchmark on February 8, 2017, when MyPanera accounted for 51% of the Company's transactions, becoming the largest customer loyalty program in the restaurant industry.[141] Other Panera 2.0 initiatives experienced success, with digital orders representing 26% of sales[142] and the Rapid Pick-Up Program representing about 9% of sales.[143]

On February 7, 2017, Shaich announced 2017 to be Panera's "inflection point"[144]: "[w]ith peak investments and significant scale behind us, we are now focused on completing the rollout of our initiatives and reaping the benefits."[145] In particular, "[t]he company has guided to double digit EPS growth for 2017."[146] The market reacted positively to this announcement and Panera's stock rose $20.00 that day.[147]

In this positive environment, Shaich prepared to meet JAB's Chief Executive Officer, Olivier Goudet, and Head of M&A, David Bell.[148] Shaich prepared for the meeting with Goldman, who arranged his introduction to JAB.[149] Shaich informed some of Panera's directors before the meeting, and Colasacco helped Shaich gather JAB's public information.[150] JAB hosted Shaich at its Washington, D.C. office on February 9.[151] During the meeting, Shaich presented Panera's standard external investor presentation.[152] Bell interpreted the presentation as a way to try to entice JAB to come and make an offer for Panera.[153] During his pitch, Shaich discussed his thirty-year career at Panera, but was "very uncertain" about his personal plans.[154] Shaich saw that Goudet's eyes lit up as Shaich discussed Panera.[155]

***9** On Friday, February 24, Shaich, Goudet, and Bell had a follow-up phone discussion during which JAB expressed its interest in acquiring Panera.[156] The next day, Shaich and Colasacco met to discuss JAB's expression of interest.[157] At this time, Shaich did not engage a financial advisor or engage in negotiations.[158] Shaich planned to inform the rest of the board at the upcoming Wednesday, March 1 board meeting.[159]

At that board meeting, Shaich informed the full board of JAB's interest.[160] Shaich did not mention that he had initiated the conversation with JAB.[161] The board discussed Shaich's introductory meeting and conversations with JAB, as well as JAB's potential interest in an acquisition of the Company.[162] "[T]he Board authorized Mr. Shaich to continue conversations with JAB and to report back to the Board with an update as to the discussions and the status of any offer."[163] At that time, the board did not retain a financial advisor, as it had not received a formal offer.[164]

At this same meeting, the board reviewed 2016 financial results and tracked them against the Five-Year Strategic Plan and the projections in the Five-Year Financial Model.[165] Panera management typically updated the Five-Year Financial Model every spring and fall since May 2015.[166] In March, management updated the Five-Year Financial Model in preparation for merger discussions with JAB.[167]

G. JAB Makes An Offer, And Both Parties Secure Advisors.

On March 10, 2017, Shaich met with Bell and Goudet in Washington D.C.[168] JAB offered to acquire Panera at a price of $286.00 per share in cash.[169] At this time, Panera's stock was trading at $234.91; the offer represented a 21.7% premium.[170]

JAB was a serial acquirer that maintained a "playbook" for their acquisitions.[171] Following that playbook, JAB conditioned their offer to Panera on (i) a confidentiality provision; (ii) a public support measure for Shaich and certain affiliates; (iii) a no-shop provision with a fiduciary out; (iv) matching rights; and (v) a 4.0% termination fee.[172] JAB's terms did not include a financing or regulatory condition.[173] JAB expressed the desire and ability to sign on April 7, 2017, with an announcement on April 10, 2017.[174] At trial, Bell explained the "playbook."[175] Regarding the deal's speed, JAB was "not interested in a protracted negotiation that results in significant management distraction, so they always go very quickly."[176] Because of this short timeline, JAB also never discusses post-merger leadership roles during negotiations.[177] Bell also explained that a bilateral deal is part of the JAB playbook in part because it typically leads to the lowest price.[178]

***10** JAB hired Ernst & Young in March 2017 to conduct their due diligence review of Panera.[179] JAB conducted their diligence in five days because Panera's public information and "transparency is off the charts."[180] During the process, Bell expressed satisfaction with the smooth diligence and was "really impressed by the speed and quality of the data."[181] He also noted that Panera was one of the "cleanest companies they have ever seen."[182]

As for financing, Goudet told Shaich that JAB would "use [Goldman] for our financing, so it is logical we take them on the buyside."[183] Shaich and Moreton were not concerned about using another advisor, despite Panera's prior relationship with Goldman.[184] JAB recommended that Panera use Adam Taetle from Barclays or David Ciagne from Morgan Stanley because it was "important [for Panera] to pick someone who understands [JAB's] playbook, otherwise could be dangerous."[185] Ciagne was JAB's coverage banker at Morgan Stanley.[186]

Upon receipt of an offer, on March 14, the board engaged advisors. The board retained Sullivan & Cromwell LLP ("Sullivan & Cromwell") as the board's outside legal counsel for the potential transaction with JAB.[187] Frank Aquila served as Sullivan & Cromwell's lead partner on the matter.[188] Shaich proposed engaging Barclays Capital or Morgan Stanley as Panera's financial advisor,[189] but did not tell the board that JAB had suggested those firms, or specifically Ciagne.[190] After deliberation and discussion, the board directed the Company to explore a potential engagement and selected Morgan Stanley as its financial advisor.[191] Specifically, on Aquila's recommendation, Panera selected Michael Boublik of Morgan Stanley.[192] Boublik had not worked for JAB, and neither Bell, nor anyone else at JAB, knew him.[193]

***11** On March 15, Morgan Stanley cleared an initial conflicts check.[194] Two days later, Morgan Stanley gave Panera a key request list that included the Five-Year Strategic Plan, and started putting together initial valuation metrics.[195] Then, on March 20, Sullivan & Cromwell informed the board that Morgan Stanley "had cleared an initial conflicts check on March 15 and the parties were now negotiating an engagement letter for the transaction."[196]

On March 29, Panera management and Morgan Stanley met to review the Five-Year Strategic Plan and Five-Year Financial Model as updated after the March 1 board meeting.[197] Paul Kwak, a Vice President of M&A at Morgan Stanley,[198] prepared questions about Panera's Five-Year Financial Model.[199] In conducting its analysis, Morgan Stanley "immediately noticed that [management projections] were clearly more bullish and had higher growth, higher margins than what the street consensus was,"[200] but used the Five-Year Financial Model to develop its management case DCF analysis.[201]

On March 30, the bank sent its engagement letter.[202] Panera agreed to pay Morgan Stanley $42 million: $8 million became payable upon execution of the merger agreement, and the remainder was contingent upon closing.[203] The disclosure letter identified the scope of conflict and formally disclosed all of Morgan Stanley's prior dealings with JAB.[204] Morgan Stanley disclosed they "have provided, currently are providing, and/or in the future may provide, certain investment banking and other financial services to the Company, The Potential Buyer, and the Buyer Related entities."[205] Morgan Stanley also included in the letter that other than Patrick Gallagher, no senior deal team member "is a member of the coverage team for the Potential Buyer or the Buyer Related Entities."[206]

Even though Panera's deal team did not include any JAB coverage bankers, a JAB coverage banker twice passed messages between the JAB and Panera deal teams. First, on March 27 (before execution of the engagement letter), Ciagne emailed Boublik to communicate JAB's fears that Morgan Stanley was not doing enough to assure Panera that JAB could finance the deal.[207] Second, on April 1, Boublik caused Ciagne to deliver the board's message to JAB that "Panera is serious, and there has to be a higher price."[208] The board did not know that Ciagne had previously communicated with Boublik about financing.[209] Indeed, Shaich and Moreton learned about that communication for the first time at trial.[210]

H. Panera Rejects JAB's Offer, And JAB Compresses The Timeline.

On March 14, the board met to discuss JAB's $286.00 offer.[211] The board agreed that JAB would need to raise its offer and authorized Shaich to pursue further discussions in pursuit of a higher price.[212] The board instructed Shaich to inform JAB "that the Board would not agree to any proposed offer for the Company that was not significantly higher than the $286.00 per share currently proposed by JAB."[213]

***12** The next day, Morgan Stanley conducted initial valuation work with Panera's trading history, trading multiples, and precedent transaction multiples.[214] From this and JAB's bidding precedents, Morgan Stanley was comfortable that it could negotiate a price that was above $300.00.[215]

On March 17, Morgan Stanley advised Shaich and Moreton on JAB's historical bidding approach and helped them formulate a strategy to raise JAB's offer price.[216] Shaich stayed up until 3 a.m. digesting JAB's historical bidding approach.[217] While reviewing, Shaich wrote to Moreton that he wanted to push JAB on price; Moreton cautioned him not to push it too hard by being too greedy, because "pigs get fat, hogs get slaughtered."[218]

The next day, on March 18, Shaich informed JAB that although the board approved continued discussions and targeted due diligence, it expected that JAB would have to increase their $286.00 offer north of $300.00 per share.[219] JAB agreed to discuss the possibility of offering a higher price internally and to get back to Shaich on March 20.[220]

On March 20, JAB made a second offer of $296.50 per share, with the warning that JAB would "not go one penny over 299. We're not going to hit 300."[221] Panera's stock had closed at $255.24 the day before, so the offer represented a 16.2% premium to that trading price.[222] The board met that same day to review the second offer.[223] The board "supported continued discussions with JAB and JAB initiating due diligence on the Company but expressed its expectation that any final offering price be significantly higher."[224] Boublik agreed and commented, "I would hope that we get another collective move of at least the same magnitude."[225]

On March 22, Shaich and Moreton communicated to Bell and Goudet the board's expectation to Bell and Goudet that JAB find additional value in the Company.[226] Shaich explained, "You've made a meaningful move once, and I and my board appreciate that, but it's going to take another meaningful move once again ... I'm confident that once we sit down and go through our business plan and you've done your diligence you'll be able to get there."[227]

A few days later, on March 26, JAB and Panera signed a confidentiality agreement and discussed the due diligence process.[228] Bell testified that when JAB makes an offer without a financing contingency, they conduct due diligence at "the appropriate level" "to have this minimum amount of information in order to ensure that [they] could get the debt commitments" from their lenders.[229] In these discussions, JAB asked Panera to move up the transaction with an anticipated announcement during the week of April 3.[230] Shaich recognized that JAB wanted to move quickly,[231] but responded that it was "material" to Panera that JAB "robustly (and genuinely) understand the drivers in the business [s]o they can fully appreciate the value that we understand is here and seek from them."[232]

***13** Shaich and Moreton also spoke with their legal and financial advisors about the feasibility, benefits, and risks of JAB's proposed accelerated timeline.[233] The transaction was the fastest in Kwak's career.[234] Nevertheless, Panera's advisors said that they had adequate time.[235] The board liked the shortened timeline, valuing less distraction.[236] It was feasible for the board because of its extensive review of the Five-Year Strategic Plan, Panera's financial results, and the Five-Year Financial Model.[237] Shaich understood that the Company's future value lay in its initiatives, so he conditioned the compressed timeline on meeting with JAB to review the Five-Year Strategic Plan and Five-Year Financial Model.[238] JAB agreed and the parties agreed to work toward entering into a definitive agreement during the week of April 3.[239]

On March 27, JAB's counsel provided Sullivan & Cromwell a draft merger agreement and a draft voting agreement.[240] The board did not counteroffer on deal price or deal terms at that time.

Also on March 27, the Company learned that a Bloomberg reporter had called Bell inquiring about a possible sale of Panera.[241] Shaich wrote in an email that he learned this through "a desperate call from [D]avid [B]ell [after] Bloomberg called him inquiring about Panera." [242] At trial, Shaich commented that during the call, Bell had "anxiety in his voice" and "was very nervous and concerned about it." [243] Despite the JAB playbook's tenet of confidentiality, [244] JAB did not walk after the leak. Instead, JAB began their diligence in Panera's data room on March 28. [245]

While JAB was conducting their due diligence, Morgan Stanley presented its initial valuation analysis to the board. [246] At the March 30 board meeting, Morgan Stanley presented seven different valuation metrics to guide the negotiations and frame JAB's outstanding offer of $296.50. [247] Morgan Stanley also identified and ranked "Potential Interlopers" by their strategic rationale and ability to pay. [248] In order, these included Starbucks, Chipotle, Restaurant Brands International ("RBI"), Dunkin', Domino's, McDonald's, Yum!, and Darden. [249] Morgan Stanley ruled out financial sponsors, [250] focused on strategic buyers like Starbucks, and explained why others were unlikely to compete. [251] In its analysis, Morgan Stanley recognized that Starbucks had "[p]reviously engaged with [Panera] in acquisition discussions," and "[h]ad mentioned concerns that acquisition multiple would be above where Starbucks traded." [252]

***14** This analysis fit with Shaich's and the board's deep knowledge of the industry. [253] According to Shaich, the "big three" were not viable options: Starbucks had just passed on Panera months earlier; Chipotle was in an *E. coli* crisis; and RBI had just acquired Popeyes. [254] As for the remainder, Shaich knew Dunkin' very well, had discussions with them, and knew they were 100% franchised, operated at smaller volume, and would not be interested in Panera. [255] Shaich knew Domino's CEO as a dear friend and understood their business was 100% franchised and 100% pizza and that they were not acquiring. [256] Shaich previously had discussions with McDonald's and knew that, based on mistakes in their acquisition history, they had pulled back and were not acquiring, so Panera "wouldn't be for them." [257] Shaich also had discussions with Yum! years earlier and knew that, at the time of the merger, Yum! faced activist pressure to leave China and also would not run company stores. [258] Finally, Shaich knew that Darden was acquiring Cheddars and faced activist pressure. [259] Shaich explained: "[I]t was just patently clear to me that, knowing what I know, and knowing these people and where this had played out, that there really wasn't a viable interested party." [260] The board agreed. Moreton explained that "there was nobody else out there talking to [the board] about potentially acquiring [the Company], nor did [the board] think there would be." [261]

I. JAB Reviews Panera's Five-Year Strategic Plan And Five-Year Financial Model And Makes Their Final Offer.

Shaich met with four JAB leaders on March 31, as well as two of their advisors. [262] The group met for three to four hours, and Shaich presented a deck titled "Five-Year Strategy & Financial Model." [263] The Company presented nonpublic information, including the status of the Five-Year Strategic Plan and the financial projections contained in the Five-Year Financial Model. [264] Days later, on April 2, JAB confirmed its pre-diligence estimates for cost savings [265] and internally revised their target price upwards from $290.00 to $305.00 per share. [266]

The next day, on the morning of April 3, Bloomberg reported that Panera was exploring strategic options, including a possible sale of the Company to potential suitors such as JAB, Starbucks, and Domino's. [267] In response to the leak, Panera's stock price jumped to $261.87, an 8% increase from the pre-public speculation price, and closed at $282.63. [268]

Later that day, on April 3, Shaich, Hurst, and Bufano met with JAB's senior partners including Goudet, Bell, Peter Harf (JAB senior partner), Bart Becht (JAB partner and chairman), and two of their advisors. [269] The Company presented a deck also titled "Five-Year Strategy & Financial Model," [270] which was substantially similar to the deck delivered to the other JAB leaders on March 31. [271] Both decks contained an in-depth look into the Five-Year Strategic Plan and the Five-Year Financial Model. [272] Both decks discussed Panera's opportunities in international franchising, [273] "Panera At Home" (including coffee), [274] and technology. [275]

The April 3 deck contemplated "other opportunities" that would stem from combining JAB and Panera. [276] These opportunities included joint efforts in consumer packaged goods ("CPG"), coffee, international expansion, technology, marketing, real estate modeling, sourcing, and franchising.[277] The parties did not quantify the amount of savings generated by these efforts.[278] After this discussion, Bell explained that JAB

> ***15** did some back-of-the-envelope math and got excited about it. But since we had no discussion with anyone about it, and it was a short period of time, we didn't, quote/unquote, put it in the model, financially. But I will tell you—you even heard it earlier—coffee was core to our strategy of doing this. It's just something that was difficult for us to quantify at the time we were doing diligence.[279]

JAB did not quantify any growth opportunity synergies either before or after diligence.[280]

Also on April 3, Panera countered JAB's draft merger agreement and proposed lowering the termination fee from 4.0% to 2.5% of the equity value of the transaction.[281] In response to that counter, also on April 3, JAB communicated to Shaich a "best and final" offer of $315.00 per share and a 3.0% termination fee.[282] The $315.00 offer represented a 34.1% premium from the March 10 trading price of $234.91 and a 20.3% premium from the March 31 pre-public speculation trading price of $261.87.[283] JAB informed Panera that this offer would expire when the United States market opened on April 5.[284]

J. Morgan Stanley Offers Its Fairness Opinion, And Panera Approves The Deal.

At 9:00 p.m. on April 3, Morgan Stanley's fairness committee met to discuss the proposed transaction between Panera and JAB, and found that the $315.00 per share offer exceeded the historical trading range, analyst price targets, public trading benchmarks, and the street discounted equity value analysis.[285] The analysis also showed that the $315.00 per share offer fell within the range of precedent transactions, management discounted equity value analysis, and both the street and management discounted cash flow analyses.[286] The committee prepared to present these findings to the board the next day.

On April 4 at 9:30 a.m., the board held a meeting to discuss JAB's "last and final" offer.[287] Shaich, Bufano, and Hurst presented highlights from the "Five-Year Strategic Plan & Financial Model" previously shared with JAB leaders.[288] During this meeting, management also reviewed the Company's full Five-Year Financial Model with the board.[289]

Morgan Stanley presented its fairness committee's findings.[290] The analysis included the evolution of merger discussions; a summary of JAB proposals with implied transaction multiples; a JAB company and precedent transaction overview; Panera's historical stock performance, next-twelve-month multiple measurements, and valuation comparables; and analyst perspectives on Panera.[291]

Morgan Stanley also presented its preliminary standalone valuation summary from both a street case and an internal management case based on the Five-Year Model.[292] The discounted cash flow analysis for the street case ranged from $231.00 to $318.00 per share, while the management case ranged from $300.00 to $410.00 per share.[293] The board discussed these valuations at length and asked Morgan Stanley questions about the underlying assumptions.[294] Morgan Stanley explained that the management case reflected assumptions for Panera's various initiatives and that "all those initiatives had to go right in order to achieve this management case and then ... there was execution risks in executing or in getting all those initiatives to the point that management was assuming within their management case."[295] While Morgan Stanley highlighted the effect of these assumptions, it accepted management's data in creating the management case and did not test it for reasonableness.[296] Morgan Stanley concluded that the merger consideration of $315.00 per share "was fair to and in the best interests of, from a financial point of view, the Company's shareholders and that it would be prepared to issue an opinion to the Company and its Board to that effect."[297]

***16** After the board discussed their perspectives on the proposed transaction and the valuation of the Company, "[t]he directors expressed their strong support for the proposed transaction, noting particularly that the price was fair for the Company's shareholders and that the deal protection mechanisms in the merger agreement were not preclusive to an alternative proposal for the Company's shares."[298] The board then recessed and reconvened at 4:00 p.m. for the final review of the proposed transaction.[299]

At that time, Sullivan & Cromwell updated the board about the merger agreement, the voting agreement, and the non-competition agreement.[300] Boublik orally delivered Morgan Stanley's fairness opinion (confirmed the next day in writing)[301] that the merger was fair from a financial point of view to Panera and its stockholders.[302] The board unanimously approved the proposed resolutions to adopt, execute, and deliver the merger agreement.[303]

On April 5, Panera and JAB issued a joint press release announcing the merger.[304]

K. Panera Solicits And Obtains Stockholder Approval.

On May 12, Panera filed a preliminary proxy statement on Schedule 14A recommending that Panera's stockholders vote in favor of the merger.[305] On June 1, Panera issued a definitive Schedule 14A proxy statement, by which Panera notified all stockholders of their appraisal rights for their shares of Panera common stock pursuant to 8 *Del. C.* § 262, and attached a copy of 8 *Del. C.* § 262 as Annex C to the proxy.[306] On June 16, Panera issued supplemental disclosures.[307] On July 11, Panera stockholders approved the merger at a special meeting, at which over 97% of votes cast favored the merger, representing 80.26% of the outstanding shares.[308]

The merger closed on July 18.[309] No potential bidders emerged at any time, including after Bloomberg's March 27 request for comment or after the parties announced the deal on April 5.[310] As of the merger date, Panera operated 910 company-owned bakery-cafes and 1,132 franchisee bakery-cafes across 46 states, the District of Columbia, and Ontario, Canada.[311]

On November 8, Panera announced that effective January 1, 2018, Shaich would step down as Chief Executive Officer of Panera and remain with the Company as Executive Chairman, and Hurst would succeed Shaich as Chief Executive Officer.[312]

L. Dissenting Stockholders Seek Appraisal.

In early July 2017, thirty Dissenting Stockholders notified Panera of their desire to exercise their appraisal rights pursuant to 8 *Del. C.* § 262 over a collective 1,863,578 shares of Panera common stock.[313] The Dissenting Stockholders did not withdraw their demands within sixty days of the effective date of the merger.[314]

Between August 16, 2017 and September 13, 2017, Dissenting Stockholders filed five separate petitions seeking appraisal relating to the merger. The Court consolidated those petitions into this action.[315]

Between December 19, 2017 and May 10, 2018, Panera prepaid twenty-nine of the Dissenting Stockholders the full amount of the merger consideration, $315.00, and statutory interest accrued through the payment date, for each share of Panera common stock beneficially owned.[316]

***17** Certain Dissenting Stockholders withdrew their demands, and Panera and these Dissenting Stockholders jointly stipulated to dismiss their petitioners from this action.[317]

The Court held a six-day trial between April 1 and April 8, 2019. Post-trial briefing was completed on August 1.[318] The Court ordered supplemental briefing on August 22,[319] which the parties completed on September 27.[320] The Court held post-trial argument on October 7.[321]

II. ANALYSIS

Petitioners contend that the fair value of their shares is $361.00.[322] Petitioners support this valuation with a three-pronged approach. They give no weight to deal price.[323] Instead, they give 60% weight to a discounted cash flow model prepared by their expert, Israel Shaked, professor of finance and economics at Boston University's Questrom School of Business.[324] Petitioners attribute 30% of their valuation to Shaked's comparable companies analysis, and 10% to his precedent transaction analysis.

Throughout this proceeding, including at trial, Respondent pursued a valuation of $304.44.[325] Respondent argued that deal price minus synergies deserves dispositive weight. Respondent's expert was Glenn Hubbard, the Dean and Russell L. Carson Professor in finance and economics at the Graduate School of Business of Columbia University, as well as professor of economics at Columbia University.[326] Seizing on Bell's trial testimony regarding revenue synergies, Respondent lowered its valuation to $293.44 in post-trial briefing. Respondent seeks a refund of any difference between its prepayment at $315.00 per share and fair value.

A. Legal Standard

"An appraisal proceeding is a limited legislative remedy intended to provide shareholders dissenting from a merger on grounds of inadequacy of the offering price with a judicial determination of the intrinsic worth (fair value) of their shareholdings."[327] "Section 262(h) unambiguously calls upon the Court of Chancery to perform an independent evaluation of 'fair value' at the time of a transaction ... [and] vests the Chancellor and Vice Chancellors with significant discretion to consider 'all relevant factors' and determine the going concern value of the underlying company."[328] The determination of fair value is intended to ensure the stockholder is "paid for that which has been taken from him, *viz.*, his proportionate interest in a going concern."[329] Valuation of the corporation as a going concern must be "based upon the operative reality of the company as of the time of the merger, taking into account its particular market position in light of future prospects."[330] "Given that '[e]very company is different; every merger is different,' the appraisal endeavor is 'by design, a flexible process.' "[331]

***18** "In a statutory appraisal proceeding, both sides have the burden of proving their respective valuation positions by a preponderance of [the] evidence."[332] In evaluating the parties' positions, "[n]o presumption, favorable or unfavorable, attaches to either side's valuation,"[333] and "[e]ach party also bears the burden of proving the constituent elements of its valuation position ..., including the propriety of a particular method, modification, discount, or premium."[334] Because the Court determines fair value based on an adversarial presentation blending facts, opinions, and argument, the Court's conclusions in one appraisal proceeding may not squarely inform its conclusions in another.[335]

The appraisal exercise occurs in the context of the efficient market hypothesis, "long endorsed" by the Delaware Supreme Court.[336] "It teaches that the price produced by an efficient market is generally a more reliable assessment of fair value than the view of a single analyst, especially an expert witness who caters her valuation to the litigation imperatives of a well-heeled client."[337] In view of this principle, the Delaware Supreme Court has acknowledged "the economic reality that the sale value resulting from a robust market check will often be the most reliable evidence of fair value, and ... second-guessing the value arrived upon by the collective views of many sophisticated parties with a real stake in the matter is hazardous."[338] At the same time, the Delaware Supreme Court does not view "the market [a]s always the best indicator of value, or that it should always be granted some weight."[339] "There is no presumption that the deal price reflects fair value."[340] "[T]he persuasiveness of the deal price depends on the reliability of the sale process that generated it."[341] If the sale process is not open or sufficiently reliable, "the deal price should not be regarded as persuasive evidence of fair value."[342]

***19** There is no checklist or set of minimum characteristics for giving weight to the deal price.[343] Indeed, Delaware Supreme Court precedent announced in "*Aruba*, *Dell*, and *DFC* do[es] not establish legal requirements for a sale process."[344] A deal price serves as a persuasive indicator of fair value where the sale process bears "objective indicia of fairness that rendered the deal price a reliable indicator of fair value."[345] Vice Chancellor Glasscock described a "*Dell* compliant" process as one "where (i) information was sufficiently disseminated to potential bidders, so that (ii) an informed sale could take place, (iii) without undue impediments imposed by the deal structure itself."[346] In *Stillwater*, Vice Chancellor Laster recited several objective indicia of reliability approved by the Delaware Supreme Court: negotiations "[at] arm's-length";[347] board deliberations without "any conflicts of interest";[348] buyer "due diligence and recei[pt of] confidential information about [the company's] value";[349] and seller "extract[ion of] multiple price increases."[350] The Delaware Supreme Court has particularly stressed the absence of post-signing bidders as an objective indicator that the sale process was reliable and probative of fair value. [351]

The presence of objective indicia of reliability does not establish a presumption in favor of the deal price. [352] Where these indicia are present, I must determine whether they outweigh weaknesses in the sale process, or whether those weaknesses undermine the persuasiveness of the deal price. [353]

B. Panera's Sale Process Was Sufficiently Reliable To Make Deal Price Persuasive Evidence Of Fair Value.

I find several objective indicia of reliability in this case. As a prefatory matter, Panera's stock traded in an efficient market, such that indicia of reliability in Panera's sale process support giving weight to deal price. [354] First, as Petitioners' process expert James Redpath recognized, the parties negotiated in an arm's-length transaction. [355] Redpath similarly conceded that the board was independent, and labored without conflicts of interest. [356]

***20** Second, JAB assessed Panera's value using both Panera's extensive public information and focused due diligence into Panera's confidential information. [357] In *DFC*, deal price was the best evidence of fair value in part because it was "informed by robust public information[ ] and easy access to deeper, non-public information." [358] Bell found Panera's "transparency [was] off the charts[,]"and JAB's legal advisors shared the view that "much of [JAB's diligence] is check the box and that they have reviewed everything that is public." [359] Shaich explained that he presented the Five-Year Strategic Plan "hundreds of times" to "internal groups, external groups" and "every investment conference" he attended ("twenty a year") "to get everybody to understand [ ] what's the vision and where we were." [360]

In addition, JAB received and reviewed the specific nonpublic information that Shaich believed would lead JAB to see greater value in Panera. [361] After reviewing that information, JAB internally raised their offer from $296.50 to $305.00, as the information confirmed a "[s]ignificant [c]ash [o]pportunity" through working capital and other cost savings. [362] Ultimately, JAB offered Panera $315.00. [363] Although JAB limited their access to non-public information, they did so as a natural result of Panera's widespread public dissemination of meaningful information.

Third, Panera used Boublik's guidance [364] and Shaich's doggedness to extract two price increases. [365] Even operating under their own preferred terms of engagement, JAB raised their price twice. The board rejected JAB's initial $286.00 offer, communicating its expectation that JAB would find more value for the Company during the diligence process. [366] Boublik agreed and encouraged Shaich, the lead negotiator, and Moreton, a board negotiation advisor, to seek additional value. [367] When JAB revised their offer to $296.50, JAB also explained that they would not raise the offer a penny over $299.00. [368] This was still too low for the board. [369] Shaich and Moreton listened to Morgan Stanley's guidance and believed the Company could break JAB's stated ceiling price without giving a counteroffer. [370] Morgan Stanley was right. After conducting diligence, confirming its anticipated cost savings, and reviewing the Five-Year Strategic Plan and Five-Year Model, JAB raised its price to $315.00. [371]

***21** Fourth, no other potential bidders emerged, despite a leak during negotiations and nonpreclusive deal protections. [372] A leak gives potential bidders notice of the transaction and an opportunity to bid. [373] According to Kwak, leaks typically happen at the tail end of a process, [374] and a potentially interested buyer with the capacity to acquire a $7 billion company would "have the experience and the know-how and the team members to know that you do need to move swiftly because at any point they could sign a transaction with the rumored buyer." [375] Kwak explained that when a rumored transaction surfaces, coverage bankers immediately identify and contact potential buyers "to explore whether th[ose] compan[ies] ha[ve] interest in pursuing an acquisition." [376]

The first evidence of a leak emerged on March 27, when Bloomberg called JAB for a comment. The leak concerned Bell greatly, evidencing that JAB feared another bidder might surface. The transaction became public on April 3, when Bloomberg published its article. [377] No bidders surfaced.

Further, no third-party bidders expressed interest or submitted a bid during the three-month post-signing period after the parties announced the deal. [378] Panera's deal protections included a no-shop provision with a fiduciary out, matching rights, a 3% termination fee, and 104 days between signing and closing.[379] Morgan Stanley considered each post-signing protection to be customary or insufficiently preclusive to post-signing bidders.[380] Kwak viewed a 3 to 4% break-up fee as "typical" and 3% as "customary,"[381] and recognized that even "customary" matching rights "may discourage in a way and make it more challenging" for other bidders to come forward, but such rights would not prevent them.[382] Kwak testified at trial that an interested bidder "could contact and put forth an offer to the company."[383] Kwak concluded there was sufficient time between signing and closing, noting, "[I]f there was someone, we would have expected to at least get some form of an inbound."[384]

Petitioners have not meaningfully challenged the terms Panera's post-signing passive market check, or offered any evidence that an interested bidder did not have a reasonable chance to bid.[385] To the contrary, Redpath conceded, "[t]here was sufficient time for a topping bidder to emerge post-signing."[386] After the leak and the public deal announcement, other market participants "failed to pursue a merger when they had a free chance to do so."[387] "The failure of any other party to come forward provides significant evidence of fairness, because '[f]air value entails at minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay.' "[388]

***22** In particular, none of the "big three"[389] potential bidders that Morgan Stanley identified—Starbucks, Chipotle, and RBI—showed any interest in bidding for Panera, both before and after the parties announced the deal. Chipotle knew about the leak before the deal signed, but did not express interest before or after signing.[390] Both RBI and Chipotle sent post-announcement congratulatory messages to Morgan Stanley after the parties announced the deal.[391]

Finally, Panera solicited all logical buyers consistent with its knowledge of the Company's value and the market. The Delaware Supreme Court has identified "outreach to all logical buyers" as a key indicator of reliability.[392] Petitioners contend that Panera engaged in a closed, single-bidder strategy during the pre-signing process. Respondent asserts that Panera engaged "all logical buyers."[393]

In *Dell*, the board similarly limited its pre-signing canvass to two bidders, based on its financial advisor's recommendation that those two firms were "among the best qualified potential acquirers" and that "there was a low probability of strategic buyer interest in acquiring the company."[394] The *Dell* board also conducted a go-shop, soliciting interest from sixty-seven potential bidders.[395] As a result, the Supreme Court determined the deal price "deserved heavy, if not dispositive, weight."[396]

Panera led outreach to all logical buyers: Starbucks and JAB. The negotiations with the two companies followed the same pattern. Shaich asserted Panera's value based on the Five-Year Strategic Plan to "sell[ ]" the company, or solicit interest,[397] listened to gauge interest, and then consulted with the board.[398] The failed negation with Starbucks prepared Shaich and the board to negotiate with JAB.

As a recap, in June 2015, Goldman identified several potential strategic bidders, and identified Starbucks as Panera's most likely buyer.[399] Starbucks was the most likely bidder because Panera was "such a valued company" "trading at very high multiples."[400] Goldman concluded a financial buyer was unlikely, and the board understood that financial sponsors were limited and none could afford the Company.[401] With that analysis, the board decided that it should remain an independent company, but that "the Company would, as it had done in the past, continue to observe the markets and consider activities in the best interest of shareholders on an ongoing basis."[402]

***23** About a year later, in July 2016, Starbucks initiated a possible collaboration[403] and the board instructed Shaich to solicit Starbucks' interest in an acquisition.[404] In August 2016, Shaich started the conversation with JAB, another potential buyer that was conducting acquisitions at "huge multiples."[405] Shaich explained:

> I saw an article in Nation's Restaurant News, I think [JAB] had just done an acquisition. They were buying companies every six months at huge multiples. And I thought they were at least worth getting to know in some way, so I picked up the phone and called Goldman, said do you know

> these guys and can you introduce me.
>
> That was August.[406]

After August, Panera continued its negotiations with Starbucks, which concluded by December 2016.[407] JAB expressed interest in meeting with Shaich, but with another ongoing acquisition, JAB did not engage with Shaich until February 2017.[408] After JAB expressed interest in acquiring Panera on March 24, Shaich probed Goldman for more information about the acquisition landscape, especially after RBI announced its acquisition of Popeyes on February 21.[409] Goldman replied, "Best buyer today is a JAB, with a long term perspective that counters near term valuation trends. Or Starbucks. Or a merger with someone like Chipotle."[410] Shaich shared Goldman's analysis with Colasacco.[411]

As conversations with JAB proceeded, Morgan Stanley identified the same four strategic primary strategic buyers as Goldman: JAB, Starbucks, Chipotle, and RBI.[412] Morgan Stanley also excluded other potential acquirers. Morgan Stanley recognized that Dunkin and Dominos were highly leveraged like RBI and all three would have difficulty paying all cash.[413] Beyond this, Morgan Stanley recommended that Dunkin and Dominos also had "slightly different business models" and lacked a clear strategic fit.[414] With this guidance from both Goldman and Morgan Stanley, the board viewed JAB as the only remaining logical bidder. Like Goldman, Morgan Stanley viewed Starbucks as the only other potential buyer that could afford Panera,[415] but the board had already exhausted that option.[416] The board knew that Chipotle was recovering from a food safety crisis and otherwise focused on share buybacks.[417] And the board knew that RBI had agreed to acquire Popeyes.[418] The board concluded that no other bidders were out there.[419] Morgan Stanley confirmed the board's conclusion: "JAB represents the buyer with the most interest, wherewithal, and ability to pay and would be a good fit."[420] Moreton summarized, "we had just gone through the key strategic buyer. Starbucks had told us no. And Morgan Stanley and Goldman had told us there were no financial bidders out there. So we really thought this was an opportunity to see if we could get a price that was reasonable for shareholders."[421] The leak added certainty to the board's conclusion.[422]

***24** Petitioners argue that a logical buyer universe of only two buyers is "absurd" because "Panera could not have known buyers were 'out' without ever conducting a market check."[423] The Delaware Supreme Court has held that when "the directors possess a body of reliable evidence with which to evaluate the fairness of a transaction, they may approve that transaction without conducting an active survey of the market."[424] And "if a board fails to employ any traditional value maximization tool, such as an auction, a broad market check, or a go-shop provision, that board must possess an impeccable knowledge of the company's business for the Court to determine that it acted reasonably."[425]

I find that the board possessed a robust body of evidence that it used to determine the universe of logical buyers. The board's impeccable knowledge of the market in the pre-signing phase, and the lack of interested bidders in the post-signing phase, leads me to find that the board led outreach to all logical buyers. Because Panera engaged with Starbucks first, JAB's confidentiality requirement did not preclude the board's outreach to all logical buyers. The absence of a wider canvass or go-shop does not change the reliability of Panera's outreach.[426] This decision was confirmed when no other bidders came forward either after the leak or during the post-signing passive market check. The preponderance of the evidence shows that the board used its knowledge of the market and its advisors' advice to engage all logical buyers in a value-maximizing process.

Panera's deal process bears many indicia of reliability, including an arm's length negotiation, a disinterested and independent board, numerous price increases, no emerging bidders post-leak or post-announcement, and outreach to all logical buyers. The process also terminated with an open passive post-signing market check. I therefore turn to the weaknesses in the process to determine whether they undermine its reliability.

C. Weaknesses In Panera's Process Do Not Undermine The Deal Price's Reliability.

Petitioners point to weaknesses in the pre-signing process that they believe undermine the deal price's reliability. They focus on actions taken by the board, Shaich, and Morgan Stanley. In all, I find that the transaction's flaws do not undermine its numerous indicia of reliability.

1. The board did not undermine the deal process.

Petitioners characterize the pre-signing phase as exhibiting the board's "apathy," ignorance, and "flat-footed[ness]."[427] According to Petitioners, these traits manifested in the board's failures to 1) authorize Shaich's initial outreach to JAB, 2) oversee the negotiations, 3) negotiate with a proper valuation, 4) reject JAB's confidentiality and speed provisions, and 5) negotiate deal protections.

First, while the board had authorized Shaich to solicit Starbucks' interest in acquiring Panera,[428] Shaich did not obtain specific board authorization for his August 2016 outreach to JAB. Shaich's independent outreach did not generate a response until early 2017. At that time, when JAB offered to meet with Shaich, Shaich informed Colasacco and other board members.[429] When JAB expressed an interest in acquiring Panera on February 24, 2017, Shaich informed Colasacco the next day,[430] and informed the board three business days later on March 1.[431] Thus, although Shaich initiated Panera's outreach to JAB, he timely and fully updated the board when JAB expressed interest in a transaction.[432] Shaich did not negotiate for a role post-merger or negotiate for change-in-control compensation.[433] Petitioners provided no evidence that the outreach alone—Shaich's only act that was not specifically authorized—led to any diminution in value or in the board's power to negotiate or decline a transaction with JAB.

***25** Second, while Shaich initiated and led the negotiations, the board exercised active oversight. The board of directors "has the sole power to negotiate the terms on which the merger will take place and to arrive at a definitive merger agreement embodying its decisions as to those matters."[434] The preponderance of the evidence shows the board negotiated the terms of the merger and unanimously approved the final merger agreement.

A CEO's rogue negotiations can undermine a deal process. In *Jarden*, the CEO "immediately took charge and, consistent with a stereotypical 'cut to the chase' CEO mentality, he laid Jarden's cards on the table before the negotiations began in earnest and before the board and its financial advisors had a chance to formulate a plan."[435] Beyond this, the *Jarden* CEO failed to inform the board of the negotiations.[436] He also did not receive authorization from the board to suggest a price, make counteroffers, or negotiate his "change-in-control compensation," but did so anyway.[437] These facts contributed to the Court's finding that the merger price was not a reliable indicator of fair value.[438]

I do not find similar troubling facts in this case. Unlike in *Jarden*, the board directed Shaich's negotiations, and Shaich observed the bounds of the board's authorization. Shaich informed the board of JAB's interest before JAB made an offer.[439] At that time, the board authorized Shaich to "continue the conversations with JAB and report back to the Board with an update as to the discussions and the status of any offer."[440] When JAB offered to acquire Panera on March 10, 2017, for $286.00 per share, Shaich formally informed the board on March 14.[441] The board instructed Shaich to move forward with the discussions,[442] but directed him to communicate to JAB that the board "would not agree to any proposed offer for the Company that was not significantly higher than the $286.00."[443]

The board also used Sullivan & Cromwell as its outside legal counsel for the potential transaction with JAB.[444] Sullivan & Cromwell advised the board during its March 14 meeting and helped the board select financial advisors.[445] On March 15, the board initiated the process to retain Morgan Stanley as its financial advisor.[446] From then on, Shaich and Moreton worked with the board and Morgan Stanley to adopt a proven strategy to raise JAB's price through diligence.[447]

When JAB raised their offer to $296.50 per share on March 20,[448] Shaich informed the board that same day.[449] At the meeting, the board considered the offer, and "various directors asked questions and provided their thoughts and comments."[450] Shaich testified that "the board supported [him] in pushing" JAB to a higher price[451] and "expressed its expectation that any final offering price be significantly higher."[452]

***26** Shaich conveyed that message to JAB and focused on generating additional value through the diligence process.[453] When JAB asked to move up the announcement by a week, Shaich discussed this proposal with Moreton, Bufano, and the Company's legal and financial advisors, and explained he did not find the compressed timeline material; he cared about JAB understanding Panera's value.[454] Accordingly, Shaich told

JAB that "[w]e think we need to spend some more time with you so we can show you the prospects in our plan, in order to get you comfortable at a value that my board and I can support."[455] While Shaich led diligence meetings between Panera and JAB, the board counteroffered against JAB's 4.0% termination fee, proposing 2.5%.[456]

At the culmination of JAB's diligence, Shaich informed the board of JAB's final offer.[457] The board then reviewed the Five-Year Strategic Plan and Five-Year Model,[458] vetted the deal with Morgan Stanley,[459] and ultimately "expressed their strong support for the proposed transaction."[460] Later that same day, the board reconvened to discuss the proposed merger with Sullivan & Cromwell.[461] After discussing the proposed merger, the board unanimously approved the proposed resolutions to adopt, execute and deliver the merger agreement.[462] The preponderance of the evidence shows that the board directed Shaich's negotiations and "arrive[d] at a definitive merger agreement embodying its decisions as to th[ose] matters."[463] Petitioners have likewise failed to prove that Shaich acted outside the bounds of the board's authorization.

Third, Petitioners assert the board negotiated in the dark, without a formal valuation by its advisors. The board entered negotiations with an existing deep knowledge of internal metrics of Panera's value. During the negotiations, the board analyzed seven valuation metrics with Morgan Stanley. When considering JAB's final offer, the board evaluated Morgan Stanley's standalone valuation for Panera.

Initially, the board did not have a full valuation, but it had steeped itself in management's numbers. At several prior board meetings, the board reviewed parts of the Five-Year Strategic Plan and Five-Year Financial Model. Without a valuation, the board was not prepared to make a counteroffer when JAB's initial offer came in,[464] so it limited its negotiating position to general pricing guidance. This dovetailed with Morgan Stanley's advice, based on JAB's bidding precedents, to focus on raising JAB's ceiling.[465]

On March 14, the board instructed Shaich to convey to JAB that it would not agree to any proposed offer for the company that was not significantly higher than $286.00.[466] Again, when JAB raised its offer to $296.50 and stated a max price of $299,[467] the board did not think JAB's $296.50 was high enough and directed Shaich to communicate to JAB that they expected additional value.[468]

***27** Morgan Stanley met with management to review Panera's updated Five-Year Financial Model, an essential input for Morgan Stanley's valuation.[469] Morgan Stanley incorporated these numbers into its implied transaction multiples and illustrative valuation matrices.[470] On March 30, Morgan Stanley presented its preliminary valuation analysis to the board.[471] This presentation contained two illustrative valuation matrices, Panera's historical stock performance, next-twelve-month multiples, operating comparables, valuation comparables, precedent transactions, and JAB's precedent transaction overview.[472] This presentation did not include Panera's standalone valuation.

Morgan Stanley's full valuation, including Panera's standalone valuation, came on April 4, the day after the board received JAB's final $315.00 per share offer.[473] Also on April 4, the board discussed the updated Five-Year Financial Model.[474] The standalone valuation included two DCFs: the management case generated from Panera's Five-Year Financial Model, and the street case generated from consensus of broker projections.[475] The board assessed these metrics using its knowledge of the Five-Year Financial Model. When reviewing the management case DCF, Morgan Stanley cautioned the board that risks could prevent Panera from reaching the valuation predicted using the Five-Year Financial Model. Morgan Stanley explained that "[y]ou've got to believe that 80+% of your value is in the terminus" and highlighted risks in competition and execution.[476] The board asked questions about "assumptions used in the presentation and differences among the various valuation techniques."[477] The board ultimately decided that the management case "wasn't the proper way to look at the valuation."[478] Morgan Stanley presented its oral fairness opinion for the transaction, which it would provide in writing the following day.[479] After Morgan Stanley left, the board met in executive session and discussed the transaction and the Company's valuation.[480] The board found JAB's $315.00 offer consistent with its understanding of Panera's value and unanimously approved the transaction.[481]

It is problematic that the board, through Shaich, gave early guidance toward a price that was not "deeply in the

$300s,"[482] but this pricing guidance was not a potentially binding counteroffer, and did not set a ceiling on the price. The board rejected JAB's initial offer because it knew Panera's value from its continual review of the Five-Year Financial Model. Panera's strategy of pressuring JAB to raise its ceiling ushered in an offer that Morgan Stanley opined was fair and the board found consistent with its understanding of Panera's value. The board checked its understanding of Panera's value against Morgan Stanley's seven valuation metrics on March 31. And the board reviewed and discussed the Company's standalone value in depth on April 4 by reviewing the Five-Year Financial Model and Morgan Stanley's DCF valuations. Although the board did not have each of these valuation metrics at the outset of the negotiations, it reviewed each of them before it accepted JAB's final offer.

***28** Fourth, while JAB conditioned its offer on confidentiality and speed, Panera's board valued those traits as a way to minimize disruption. The board had enacted confidentiality protections in its discussions with Starbucks, too. In both negotiations, Shaich and other board members used their Gmail accounts.[483] Shaich did this because he worried "intensely" about disruption.[484] At trial, Shaich explained:

> I am very sensitive to any discussion about anything that could be perceived as a potential acquisition and upsetting the company. ... It would upset our relationships with our franchisees, our vendors, and, quite frankly, would shut down the work on this transformation plan for three to six months, whatever time period that would be the basic discussion in the company.[485]

Thus, JAB's desire for speed benefitted the Company.[486] Moreton explained it was "to our advantage to go quickly from the standpoint we don't want to disrupt our people either, if things got out in the press. So everyone said they had adequate time, so we said, Okay. Let's shoot for it."[487] Colasacco agreed: "I would like this period to be as short as possible, because I believe that eventually management becomes aware, general management becomes aware. In the due diligence process—other processes, it's hard—it's very hard to keep a secret."[488]

This internal practice aligned with Morgan Stanley's guidance to limit outreach outside of Panera. Morgan Stanley advised that JAB would "walk away if [Panera] or its advisors talk[ed] to other parties."[489] Morgan Stanley encouraged compliance:

> Based on our familiarity with [JAB's] behavior, we did believe that their threat to walk was real. And we do see potential buyers throughout our projects really do walk away if, for example, a deal leaks or they get roped into an auction process, because there are certain buyers that just have no interest being in part of an auction process.[490]

Redpath confirmed that "if you were serious about JAB, you would need to pursue those discussions on an exclusive basis."[491]

When JAB sought to accelerate the process by one week, Shaich conditioned the tight timeframe on "a full vetting of the five-year and our strategic presentation because for [Panera] this is a discussion of value" to ensure that JAB would "robustly (and genuinely) understand the drivers in the business [s]o they [could] fully appreciate the value that we understand is here and seek from them."[492] The board also ensured Panera's advisors had adequate time.[493] After conducting diligence and attending these meetings, JAB internally revised their target price upwards to $305.00 per share[494] and eventually offered $315.00.[495]

***29** Finally, contrary to Petitioners' complaint, the board negotiated for less restrictive deal protections. Panera's deal protections included a no-shop provision with a fiduciary out, matching rights, and a 3% termination fee.[496] During negotiations, the board achieved a reduction in the termination fee from 4.0% to 3.0% by counteroffering 2.5%.[497] Kwak testified, "a 3 percent break-up fee is customary. And our rule of thumb is, generally for a transaction of this size, 3 to 4 percent is typical."[498] Kwak testified that the deal's no-shop with the fiduciary out and matching rights were also customary.[499] Redpath agreed.[500]

The board successfully negotiated a lower termination fee. Otherwise, it assented to the no-shop with a fiduciary out because the board understood that JAB was the only remaining logical buyer. The board otherwise assented to the deal terms, including matching rights, which its advisors viewed as "customary."[501] Petitioners have not shown that the board failed to challenge JAB's suggested deal protections. Instead, the board "bargain[ed] for value in negotiating the deal protections and only acceded to the termination fee when it reached terms regarding price and deal certainty that it viewed as attractive."[502]

The preponderance of the evidence does not support a finding that the Panera board was apathetic, ignorant, or flat-footed. Rather, I find that the board started the negotiations well versed in Panera's financials and projections; empowered Shaich to press JAB to raise its price and fully consider Panera's internal evidence of value, and supervised the negotiations; obtained a full valuation in time to meaningfully consider JAB's final offer within JAB's compressed timeline; and successfully negotiated less restrictive deal protections. The board's performance does not render Panera's pre-signing process unreliable.

2. Shaich's personal interests did not undermine the sale process.

Petitioners contend that Shaich led negotiations despite personal conflicts, specifically his desire to retire. Shaich's prior attempts to step down had been unsuccessful, and Shaich disliked aspects of running a public company.[503] According to Petitioners, Shaich acquiesced to JAB's demand for exclusivity and left value on the table so that he could separate from the Company.[504]

In *Aruba*, the Delaware Supreme Court used the deal price as the most reliable indicator of value when making its fair value determination.[505] That was true even though the company's top executive had conflicting incentives over retirement. At trial, this Court found that these conflicts did not undermine the deal price as an indicator of fair value because the conflict "would not have changed [the company's] standalone value."[506] The *Stillwater* Court recently synthesized the role of conflicts in evaluating fair value: the "critical question" in considering a CEO's motivation is whether "personal interests undermined the sale process."[507]

***30** A CEO's significant stock holdings may align her personal interests with the company's. "When directors or their affiliates own 'material' amounts of common stock, it aligns their interests with other stockholders by giving them a 'motivation to seek the highest price' and the 'personal incentive as stockholders to think about the trade off between selling now and the risks of not doing so.' "[508] Alternatively, a CEO's personal interests can derail negotiations and cast doubt on the reliability of deal price as a fair value. In *Norcraft*, the Court found the CEO was as focused on securing a role with the future company as he was on securing the best deal price.[509] During the process, the CEO negotiated to divert funds from the merger into tax receivable agreements that would benefit him personally.[510]

Petitioners have not proven that Shaich was conflicted or otherwise uncommitted to obtaining the best price possible because he wanted to retire. The record shows that when the Company needed him, Shaich came back to his role as Co-CEO with Moreton. And when Moreton had to step down, Shaich stayed on. Then, when Shaich's successor failed to materialize, he promised he would not leave the Company in a lurch.[511] Shaich repeatedly prioritized the Company's success over his preferred professional trajectory. Unlike the executive in *Norcraft*, Shaich did not negotiate future employment with JAB,[512] even with analyst speculation at closing that Shaich could now "run the company privately[,] [n]ot a bad deal!"[513]

The record shows that Shaich was intent on driving the price upwards. During the negotiations, the board cautioned Shaich, holding him back: on March 17, Moreton cautioned not to push it too hard by being too greedy, because "pigs get fat, hogs get slaughtered."[514] The next day, Shaich informed JAB that they would have to increase their initial offer beyond $300.00 per share.[515] During the negotiations, Morgan Stanley described Shaich as "supremely focused on finding a good home for the company and preserving the legacy of the business he's built for 35 years."[516] No evidence disturbs this conclusion.

My perceptions of Shaich from trial do not fit with Petitioners' theory. Shaich testified that he would not have sold Panera without getting the best price.[517] I believe him. Shaich's commitment to realizing value for Panera appeared to run deep. In my view, his commitment stemmed from his pride in Panera, a desire to reward those who had built Panera with him, and an attachment to Panera itself.[518] Correspondence between Moreton and Shaich on the date of the sale shows Shaich's perspective. Moreton wrote:

> Ron - I imagine that you have thought about Louie and your Dad more than a few times these past few days. This morning I woke up thinking of George Kane and him asking you: Ronnie - how much cash do we have. The answer today would be quite a lot. I am sure George (and your Dad and Louie) are resting peaceful and are incredibly proud of you. You have touched so many lives ... especially mine.[519]

Shaich replied, “Wonderful and very sad ... Indeed I was thinking about my dad yesterday. He always told me to take the money ... I always ignored him ... Though that has never been my way [t]his is probably the right time ...”[520] Shaich's trial testimony on this email was credibly emotional.

***31** After weighing all the evidence, I am convinced that Shaich would not, and did not, agree to a deal after a 35-year career before he found the right place and value for Panera. Shaich wanted to exit Panera and he led the negotiations. Those parallel facts do not convince me that either he or the impartial board accepted a low offer—or any offer—because of Shaich's personal goals. Shaich's desire to retire did not undermine the deal process or diminish Panera's standalone value. “As a matter of professional pride, he wanted to sell [Panera] for the best price he could.”[521]

3. Morgan Stanley's actions and advice did not undermine the pre-signing process.

Petitioners view Morgan Stanley as a conflicted advisor because of the firm's late conflict disclosures, financial incentives, and backchannel discussions about financing via a JAB coverage banker. Petitioners also try to cast doubt on the adequacy of Morgan Stanley's representation. Respondent counters that Morgan Stanley informed the board of its prior work with JAB, and the board determined Morgan Stanley was not conflicted; Panera and Morgan Stanley used JAB's coverage banker to drive up value; and Morgan Stanley's financial incentives aligned with Panera's stockholders. I take each in turn.

a. Morgan Stanley disclosed its prior JAB work to the board.[522]

On March 15, the board initiated the process to retain Morgan Stanley as its financial advisor.[523] Moreton testified that he participated in those discussions, and that Morgan Stanley had disclosed its prior work for JAB.[524] Nothing in the record casts doubt on this testimony.[525] Then, on March 20, Sullivan & Cromwell informed the board that Morgan Stanley “had cleared an initial conflicts check on March 15 and the parties were now negotiating an engagement letter for the transaction.”[526] Morgan Stanley provided its formal disclosure of past work with JAB on March 30, but the board already knew that Morgan Stanley had previous engagements with JAB.[527] There is no indication that these disclosures changed the board's view of Morgan Stanley's ability to serve as its financial advisor. Moreton reflected on the disclosures and testified:

> [Y]ou wonder if it might be an advantage because they might understand JAB. And certainly, I had faith in the fact that the people that were going to work on the transaction on our behalf were of the utmost integrity, and so it didn't bother me individually or the board as a collective whole.[528]

***32** The facts here diverge from those in *Jarden*, in which the board “made no inquiry” about advisor conflicts and “there [wa]s no indication that either [the CEO] or [the advisor] made any effort to disclose their past relationships to the board."[529] In this case, Morgan Stanley shared its past JAB work twice, including a formal representation letter. The board reviewed the formal disclosure in advance, even if only by a few days, before approving the deal. Petitioners have provided no basis to conclude that the timing of Morgan Stanley's disclosures undermined Panera's sale process.

b. Morgan Stanley's financial incentives were commonplace and unremarkable.

Contingency clauses are standard in financial advisor agreements and seldom create a conflict of interest. "Contingent fees for financial advisors in a merger context are somewhat 'routine' and previously have been upheld by Delaware courts."[530] This Court has recognized that "[c]ontingent fees are undoubtedly routine; they reduce the target's expense if a deal is not completed; perhaps, they properly incentivize the financial advisor to focus on the appropriate outcome."[531]

Petitioners contend that Morgan Stanley's compensation relied on the signing and closing of the deal *with JAB*. Morgan Stanley's $40 million fee was contingent in part on signing for $8 million and in part on closing for $32 million.[532] The fee contingency does not specify that the signing and closing must have involved JAB for Morgan Stanley to be compensated under the terms of the agreement. Contrary to Petitioners' contention, the fact remains that, had another bidder emerged, Morgan Stanley's compensation would result from a "proposed sale of the Company" to "any buyer."[533]

A conflict in advising a company in favor of a sale rather than in remaining a standalone company is possible. No such conflict exists here. Morgan Stanley presented the board with a full valuation analysis that included a standalone valuation based on a number of metrics, including the comparatively high management case based on the Five-Year Strategic Plan. And although Petitioners contend that Panera should not have agreed to JAB's price because its standalone value was far higher, the $315.00 offer still fell within the management case's valuation range.[534] Rather than accepting the management case, the board recognized that there was execution risk to the Five-Year Strategic Plan, including that Shaich would not be there to guide Panera 3.0 and beyond. Both the board and Morgan Stanley found that the price was fair for the Company's stockholders. In any event, Morgan Stanley's fairness opinion would not have precluded a board determination that it was better for Panera to remain a standalone company.

c. Both parties used Morgan Stanley coverage contacts outside the deal team to press their respective advantages.

In its disclosure letter, Morgan Stanley advised that with the exception of Gallagher, no senior deal team member "is a member of the coverage team for the Potential Buyer or the Buyer Related Entities."[535] Morgan Stanley did not create a wall between its JAB coverage team, including Ciagne, and its Panera senior deal team.[536] Kwak testified that Morgan Stanley "didn't set up a wall because there was no conflict[.]"[537]

***33** Ciagne, as a member of JAB's coverage team, relayed two communications between the deal teams. In the first, on March 27, JAB told Ciagne to tell Boublik that JAB feared Morgan Stanley was not doing enough to assure Panera that JAB could finance the deal.[538] In the second, on April 1, Boublik told Ciagne to tell JAB "Panera is serious, and there has to be a higher price."[539] Although the board did not know that Ciagne passed JAB's message to Boublik,[540] the board used Ciagne to pass its own message to JAB.[541]

Petitioners point to Ciagne's involvement as a fatal flaw in Panera's process. If this channel affected the deal price, it would have increased it. JAB limited their message to JAB financing, while the Company used it to ratchet up pressure and leverage the price. In my view, this flaw did not undermine a fair process.

d. Petitioners have not shown that Morgan Stanley's advice was inadequate.

JAB's negotiation playbook contains four key principles: bilateral, confidential, friendly, and fast.[542] The playbook earned respect in the marketplace because JAB had intimated they would walk if their counterpart did not follow it.[543] But on one occasion when a JAB target, Krispy Kreme, pushed JAB to deviate to the target's advantage, JAB still closed the deal.[544] Morgan Stanley knew about Krispy Kreme's success, and Petitioners fault Morgan Stanley for not counseling Panera to similarly pursue a go-shop or reduced termination fee.

Petitioners fail to acknowledge that Morgan Stanley informed the board of Krispy Kreme's negotiation process and advised Panera to adopt a similar negotiation strategy.[545] Morgan Stanley educated Shaich and Moreton "very quickly" on JAB's negotiation playbook and assisted them in developing their own strategy.[546] On March 17, Boublik sent Shaich and Moreton a proposed script and slide decks summarizing "JAB Historical Bidding Precedents" and "JAB Merger Backgrounds."[547] Morgan Stanley presented these detailed precedent analyses when the board was "thinking about strategies in terms of how to go back to JAB in terms of negotiation ... to show that JAB has bid up from their initial bid in the past and ... to show how much they had bid up after their initial bid."[548] Shaich reviewed this deck and used it to inform his negotiation strategy.[549]

Moreton viewed these decks as "very important" because "they were able to show us, in the bidding precedents, how JAB's transactions had gone from the initial discussions and initial bids, through due diligence, to the end, and how they had a history of raising their offer price as they went through."[550] Shaich stayed up digesting this deck until 3 a.m.,[551] and later thanked Boublik "for [his] very valued input," noting "it really made a difference in how [Shaich] approached it ... particularly relative to the history of their other deals."[552]

***34** The JAB Merger Backgrounds deck detailed the Krispy Kreme offer, strategy, and negotiation timeline. After JAB made Krispy Kreme an initial offer, Krispy Kreme asked for more time because it did not have a complete long-term financial plan and felt it could not yet "appropriately assess JAB Holdings' indication of interest."[553] While Krispy Kreme was securing this information and advisors, JAB postponed the Krispy Kreme negotiations until after it closed an acquisition with Keurig Green Mountain, Inc.[554] While JAB was working on the Keurig deal, a financial buyer expressed interest in Krispy Kreme, but did not engage in negotiations.[555] Four and a half months after the initial offer, JAB and Krispy Kreme resumed their negotiations.[556] Krispy Kreme's board insisted on additional value based on their internal diligence, and threatened a go-shop unless JAB increased the price and reduced the termination fee.[557] JAB accepted Krispy Kreme's counteroffer, resulting in a 12% bid premium and a reduced termination fee.[558] Petitioners assert that Krispy Kreme negotiated for six months, when in reality, JAB postponed negotiations while pursuing another deal. Once they resumed negotiations, they lasted forty-five days.

In comparison, Shaich initially reached out to JAB in August 2016, but JAB was pursuing another transaction at the time. At the conclusion of that deal, Panera and JAB negotiated for forty days. Unlike Krispy Kreme, Panera's board did not need additional time to educate itself on Panera's long-term financial plan: the Five-Year Financial Model was the board's catechism. Like Krispy Kreme, the board insisted that JAB find additional value through diligence.

Petitioners assert that Morgan Stanley should have advised the board to seek a go-shop like Krispy Kreme. Krispy Kreme had another interested bidder. Panera's board and Morgan Stanley understood that there were no other bidders out there with the interest and capacity to purchase Panera.[559] Accordingly, instead of pursuing a go shop, the board obtained a lower 3.0% termination fee and conditioned JAB's timeline on a review of the Five-Year Strategic Plan and Five-Year Financial Model, which generated an additional $18.50 in value.[560] In the end, no other party expressed an interest in acquiring Panera, which confirms the board's understanding that a go-shop would not result in a higher price for Panera stockholders. Morgan Stanley did not fail to advise the board about prior negotiating strategies. Rather, I find Morgan Stanley helped the board implement a proven negotiation strategy, with the lessons learned from the Krispy Kreme transaction, to generate additional value.

Next, Petitioners contend that Morgan Stanley provided inadequate substantive advice by failing to perform a leveraged buyout ("LBO") analysis, thereby failing to assess a financial sponsor's ability to purchase Panera. Morgan Stanley understood that "for an LBO of [$]6 to $7 billion, putting in equity that represents more than 60 percent of the total purchase price is just not what financial sponsors do for their LBO."[561] Petitioners' process expert agreed that it was unlikely that a financial sponsor would be interested in Panera,[562] and Petitioner's valuation expert failed to perform an LBO analysis.[563] Petitioners have not shown any flaw with Morgan Stanley's focus on strategic bidders. This is especially true when Morgan Stanley found that financial sponsors could not afford Panera, and identified only one bidder besides JAB that could afford Panera: Starbucks.[564]

*35 To Petitioners, Morgan Stanley's most significant shortcoming is its failure to evaluate Panera's standalone value until the final day of the transaction. Petitioners have not shown that the board did not know Panera's standalone value before it approved the merger. The board had a deep knowledge of Panera's performance and projections derived from the Five-Year Strategic Plan that it reviewed at every meeting,[565] including the March 1 board meeting.[566] The board received and reviewed Morgan Stanley's full valuation before voting for the merger.[567] That valuation included a standalone valuation derived from the Five-Year Strategic Plan.[568] Petitioners have not shown that reviewing the valuation earlier would have convinced the board to reject JAB's offer, or that the valuation even encouraged remaining a standalone entity. The deal price fell within the range of the management case DCF.[569] While the board had very little time with the valuation, this flaw did not undermine value, particularly given the board's facility with Panera's financials.

In all, I find that some of the Company's pre-signing deal decisions were sub-optimal. Morgan Stanley's JAB coverage banker was involved in the deal communications, Shaich pushed for an offer "not deep in the 300s" before the board received a full valuation, and the accelerated timeline meant the board had very little time with Morgan Stanley's valuation. I find that these issues did not undermine the sale process "so as to prevent the deal price from serving as a persuasive indicator of fair value."[570]

Panera's board had a deep knowledge of the market and of Panera's value. The board led discussions with the two logical bidders, which were identified by the board through their extensive personal knowledge, and by Goldman in 2015, Goldman in 2017, and Morgan Stanley in 2017. The board negotiated with JAB according to their advisors' strategy, which was tailored to JAB and executable based on the board's working knowledge of Panera's value. The board authorized Shaich to lead these negotiations, which he did in reliance on board members and Morgan Stanley; in full transparency to the board; and in relentless pursuit of value. That strategy successfully extracted two price increases totaling $18.50 per share and a lower termination fee, and generated a final offer that the board concluded was fair in view of Morgan Stanley's comprehensive valuation. Panera's outreach to the only two logical buyers resulted in a deal that both the board and its advisors identified as fair to its stockholders. Accordingly, I find Panera's deal process to be persuasive evidence of fair value.

D. Respondent Has Proven $11.56 In Synergies.

Section 262 mandates that I determine fair value "exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation."[571] I must "exclude from any appraisal award the amount of any value that the selling company's shareholders would receive because a buyer intends to operate the subject company, not as a stand-alone going concern, but as a part of a larger enterprise, from which synergistic gains can be extracted."[572] This excludes not only "the gains that the particular merger will produce, but also the gains that might be obtained from any other merger."[573] And because deal price is a persuasive metric of fair value in this case, I must also "excise[ ] a reasonable estimate of whatever share of synergy or other value the buyer expects from changes it plans to make to the company's 'going concern' business plan that has been included in the purchase price as an inducement to the sale."[574] Respondent bears the burden of proving any downward adjustment to deal price.

*36 Respondent contends that the Court should excise $21.56 per share from the deal price because it proved that JAB anticipated, and paid for, synergies from deploying their characteristic management framework. Respondent identifies three categories of such synergies: incremental cost savings, incremental leverage tax benefits, and revenue synergies. Petitioners generally assert that JAB is a financial sponsor, not a strategic buyer, and specifically challenge Respondent's evidence of synergies.

Panera's board and financial advisors viewed JAB as a strategic buyer,[575] and JAB identified Panera as a strategic acquisition.[576] JAB had previously acquired Einstein Bros., Caribou Coffee, and Krispy Kreme.[577] JAB identified Panera as a "Fresh Baked / Coffee Adjacency" that would fill gaps in their portfolio by expanding JAB's holdings in the coffee and fresh baked lunch category.[578] Even if JAB were not a strategic buyer, labeling them as a financial acquirer would not do the work Petitioners hope it would. "[I]n theory, if the acquisition of a company by a financial acquirer is at a market price that includes speculative elements of value which arise only from the merger, that acquisition value may exceed the going-concern value."[579] That is the case here.

JAB has a three-pronged "playbook" that they implement after a deal closes. That playbook addresses people, cost and cash, and growth.[580] Under the people prong, JAB develops a "short list of CEO candidates," installs a "CFO and establish[es] Product Management Office," assesses the "management team," and deploys the "JAB ownership model."[581] Under their cost and cash prong, JAB identifies "[q]uick wins in cash, working capital (particularly AP), [and] cost structure" to implement a "cash and cost discipline culture."[582] As for growth, JAB conducts target-specific analyses and identifies strategic opportunities from combining companies under its umbrella.[583] JAB approached Panera with the intention of extracting synergies through these plays. JAB's pre-diligence model, setting a target price of $290.00, was based in part on value gains from implementing their playbook at Panera.[584]

First, JAB measured the investment opportunity for its cash and cost prong, recognizing Panera's lack of "discipline culture" in working capital and supply chain.[585] JAB's initial investment model outlined $300 million in working capital savings.[586] JAB had successfully implemented working capital changes at Krispy Kreme, Caribou Coffee, and Peet's Coffee.[587] JAB planned similar changes for Panera by increasing the Company's days payable outstanding from about four to about fifty to ninety days.[588]

***37** As for cost savings opportunities, JAB identified potential savings in SG&A, store level efficiency, and supply chain amounting to $70 to over $100 million.[589] To accomplish this, JAB hoped to cut public company expenses, optimize franchise costs, introduce procurement savings, and reduce waste.[590]

After performing due diligence, JAB concluded their diligence confirmed "significant" opportunities for cash and for cost savings.[591] JAB confirmed $300 to $500 million by maximizing working capital, more than $30 million in procurement savings, $18 million in SG&A optimization, $15 million in supply chain optimization, and $2.5 to $5 million in public company costs.[592] JAB expanded working capital estimates as "[Panera] currently has the lowest [days payable outstanding] across nearly all public peers and much lower than other JAB Beech assets."[593] At this point, JAB recognized that they would have to pay more than their early target price[594] and raised their internal target offer from $290.00 to $305.00.[595]

In addition to the management playbook, JAB applied their bedrock negotiation playbook principle of not conditioning their deal on receiving financing approval, and securing financing during the diligence phase.[596] Respondent noted that because JAB financed $3 billion for the deal, Panera would carry greater debt than it did as a standalone value.[597] JAB quantified their anticipated debt and associated tax effects when they formulated their target deal price.[598]

Hubbard found that "[i]nternal documents show that JAB anticipated significant synergies from the acquisition of Panera, and factored these synergies into their valuation of Panera."[599] Hubbard found that with increased debt, Panera would have higher interest tax deductions, generating a merger-specific tax synergy of $9.18 per share.[600] Hubbard agreed with the cost and cash synergies as well, finding synergies totaling $37.29 per share.

Petitioners argue that these cost savings and tax synergies are not merger-specific synergies because Panera management could have also made these changes.[601] In support, Petitioners cite *Huff Fund Investment Partnership v. CKx, Inc.*, in which this Court found that the record contained insufficient evidence to support a finding that the respondent formed its bid on, or believed that there were, merger-specific cost savings.[602]

That is not true of this case. Panera's management culture and priorities did not support the changes JAB intended to make. Panera was in the "habit" of paying its vendors within four to six days[603] and invested in extensive initiatives.[604] JAB's "Cash Opportunities" arose from Panera's failure to "focus on working capital at all" while spending "top dollar to get the best without ever re-engineering costs out of the business."[605] Panera forecasted cost savings, but limited its changes to sourcing and process improvements.[606] Any overlap between Panera's forecast and JAB's playbook demonstrates differences in scale. As an example, Panera evaluated "FDF" and G&A savings in its forecast, predicting new cost savings between $300,000 and $600,000 each year from 2018–2021;[607] JAB projected $18 million in its first year alone.[608] JAB believed that it could achieve much greater savings because of its expertise in executing those savings across their portfolio companies.[609] When Hurst saw JAB's plan, he thought JAB had "lost their freakin' minds based on SG&A savings."[610] JAB contemplated "Day 1 [p]laybook implementation."[611]

***38** As for the tax synergies, Petitioners argue that Panera could "re-leverage its balance sheet as it saw fit" so the tax deductions associated with JAB's $3 billion financing were not an element of value arising from the merger.[612] Petitioners concede that Panera's debt increased "dramatically" after the transaction, from $480 million to $2.7 billion.[613] Here, unlike in *Huff*, the evidence shows JAB had similarly financed other deals in the past and saw value in doing it again with Panera, while Panera intentionally maintained low debt.[614]

The preponderance of the evidence demonstrates that JAB formed its bid in anticipation of applying its management playbook to Panera to generate merger-specific savings. Before JAB made an offer, it recognized that it could realize working capital and cost savings when it ran its plays on Panera. JAB formed its initial offer in view of that predicted value. JAB confirmed it could realize that value during due diligence, and that conclusion informed their offer price. JAB predicted additional value in tax savings from increasing the Company's debt through JAB's characteristic financing technique. Hubbard calculated the combined value of these synergies at $37.29 per share.[615] I find that by running its plays on Panera, JAB predicted $37.29 in value arising out of the merger.

Hubbard estimated that JAB built in 31% of these synergies, or $11.56, into the merger price.[616] In support, Hubbard cites a 2013 Boston Consulting Group study of 365 deals that analyzes the "median portion of synergies shared with the seller."[617] Petitioners object to the BCG study's breadth and its lack of specificity across industry or comparable companies. Respondent cites *Solera* for the proposition that this study is an appropriate estimation of synergies belonging to the buyer.[618] But the adoption of a methodology, expert opinion, or metric in one appraisal action does not mandate its adoption in a different appraisal action.[619] This Court's previous acceptance of Hubbard's proffered study is not conclusive in this case. Instead, I find that Petitioners have not cast doubt on the reliability of this study, or put forward a more appropriate percentage. Respondent has proven deduction of cost and tax synergies of $11.56 per share by a preponderance of the evidence.[620]

***39** I turn now to JAB's third playbook prong of growth, in which Respondent sees revenue synergies. Unlike the cost and cash playbook prongs, JAB did not quantify these growth opportunities in its models. JAB recognized that while it is "relatively simplistic to quantify potential cost savings[,] [i]t's much more difficult to quantify for-sure growth areas, even though they may be extremely important."[621] Leading up to and throughout trial, Respondent and its expert presented a fair value that did not quantify any revenue synergies attributable to JAB's growth opportunities. This is consistent with the record evidence and both parties' experts' opinions.

In their pre-diligence model, JAB identified growth opportunities for coffee, technology, international expansion, and CPG.[622] At a March 31 meeting, Panera also identified opportunities in international franchising, CPG (including coffee), and technology.[623] After this meeting, on April 2, JAB created its post-diligence model, expressly clarifying that CPG, coffee, and international expansion were "Growth Areas Not in [the] Investment Model[.]"[624] In this same model, as explained, JAB increased its internal target price to $305.00 based on quantified anticipated cost savings.[625]

At an April 3 meeting, the parties again discussed opportunities for CPG, coffee, international expansion, technology, as well as marketing, real estate, food sourcing, and franchising.[626] Bell testified that these strategic growth opportunities played a role in JAB's decision to increase their offer from $305.00 to $315.00[627] because JAB

> did some back-of-the-envelope math and got excited about it. But since we had no discussion with anyone about it, and it was a short period of time, we didn't, quote/unquote, put it in the model, financially. But I will tell you —you even heard it earlier—coffee was core to our strategy of doing this. It's just something that was difficult

> for us to quantify at the time we were doing diligence.[628]

Bell testified that JAB took a "leap of faith" on these "strategic opportunities," and justified the $10.00 increase with their "back-of-the-envelope" calculations.[629] Later, Bell testified that coffee procurement was not a "back-of-the-envelope" calculation because JAB "hadn't done the analysis."[630]

After trial, Respondent latched onto a new synergy theory that deducted $10.00 per share for these growth or revenue synergies. Respondent's post-trial position finds no support from its expert. Hubbard did not include any revenue synergies in his analysis.[631] When pressed, Hubbard affirmatively declined to adopt Bell's testimony, as he saw no support for it in the trial exhibits or in his work for Respondent.[632] "Thus, in its zeal to reach a desired litigation outcome, Respondent finds itself in the awkward position of advancing a position at odds with its own expert ...."[633] At post-trial argument, Respondent's counsel explained that they "never asked [Hubbard] to adjust his opinion" because the trial strategy required Hubbard to stick with his synergy analysis, leaving counsel to argue the additional $10.00 in synergies in post-trial briefing.[634]

***40** This series of events casts doubt over Respondent's post-trial position on revenue synergies. At bottom, Respondent puts forward conclusory fact testimony contradicted by JAB's contemporaneous financial modeling and rejected by its expert. There is no evidence that JAB quantified revenue synergies. JAB's financial modeling assumes the opposite: "no uplift ... from any strategic synergy opportunities."[635] JAB's contemplation of potential growth opportunities is insufficient to prove ten dollars' worth of revenue synergies in JAB's best and final offer price. Further, JAB provided no evidence to support the conclusion that all ten dollars inured to JAB's benefit and should be excised from the amount paid to stockholders. Hubbard did not find any revenue synergies, and therefore did not apportion any. Respondent has failed to prove revenue synergies that would support an excise of $10.00 from the deal price. In all, Respondent has proven $11.56 from its cost savings and tax synergies. The deal price minus synergies valuation method yields a price per share of $303.44.

E. The Supplied Alternative Valuation Methodologies Are Unreliable.

While Respondent asserts that deal price minus synergies deserves dispositive weight, Petitioners press three alternative valuation methodologies: discounted cash flow ("DCF"), comparable companies, and precedent transactions.[636] In the context of a persuasive deal price, I disregard those methodologies for the reasons that follow.

1. Petitioners have not proven their DCF model's reliability.

"While the particular assumptions underlying its application may always be challenged in any particular case, the validity of [the DCF] technique *qua* valuation methodology is no longer open to question."[637] Nevertheless, the Supreme Court "cautioned against using the DCF methodology when market-based indicators are available."[638] Compared to a persuasive, market-based deal price metric, "the DCF technique 'is necessarily a second-best method to derive value.' "[639]

Petitioners and Respondent each introduced a DCF valuation prepared by their expert. Hubbard introduced a DCF that generated a value of $291.71 per share.[640] He gave his DCF no independent weight, but viewed it solely as corroborative of his deal-price-minus-synergies value of $303.44.[641]

In a "very subjective" weighting exercise, Shaked gave sixty percent weight to his DCF model, which generated a value of $354.00 per share, exceeding the deal price by $39.00.[642] By this model, Shaked asserted over a billion dollars was left on the table.[643] The experts are approximately $63.00 per share apart. Because Petitioners are urging the Court to give significant weight to Shaked's DCF model, they bear the burden of convincing the Court that the model is sufficiently reliable to merit weight in the face of Panera's reliable deal process.

Petitioners have fallen short: Shaked's model as presented at trial is of questionable reliability. The primary flaw is Shaked's concession regarding the investment rate for the terminal period. In his report, he put forward an investment rate of 3.1% that he "conservative[ly]" cushioned with a

$116 million buffer, as "kind of an extra slack for the maintenance."[644]

***41** Hubbard put forward a 35.6% investment rate.[645] This rate was based on the principle that "growth isn't free,"[646] particularly in the extraordinarily competitive restaurant industry.[647] He anchored his investment rate in Panera's historical investment rate,[648] and utilized the formula IR=g/RONIC, where the investment rate equals the terminal growth rate over the return on new invested capital.[649] Hubbard set RONIC equal to the weighted average cost of capital ("WACC") on the premise that "[i]n a competitive industry, abnormal profits tend to vanish over time."[650] In Respondent's view, Shaked's original investment rate assumed "startlingly high returns on ROIC [([return on invested capital)] forever."[651]

When Shaked took the stand at trial, he addressed this criticism by presenting for the first time a "corrected" ROIC chart with an investment rate that diverged from, and was significantly higher than, the investment rate in his report.[652] Shaked did not base his "corrected" chart on the analysis found in his report or mentioned in his deposition. Notwithstanding this correction, Shaked did not adjust his DCF with the "corrected" investment rate.

When Hubbard applied Shaked's corrected investment rate to his other DCF inputs, he found "the valuation attached to this [investment rate] is $100 off the one he is tendering."[653] Hubbard testified that if Shaked were to plug his corrected 33% investment rate into his DCF, this would erase much of the difference between the experts' DCF calculations.[654]

After Hubbard's testimony, Shaked took the stand as a rebuttal witness, but did not address his failure to adjust his DCF in light of his corrected investment rate.[655] Shaked's trial concession on his investment rate weakens his credibility: he abandoned the rate in his report after learning of Hubbard's criticisms, but stood by his DCF reliant on that rate, even after Hubbard pointed out the inconsistency.

Shaked's original, unadjusted investment rate is a significant driver of his DCF model. Hubbard pointed to this aspect of Shaked's model to explain the wild swings in value when substituting different perpetuity growth rate ("PGR") inputs. Under Shaked's initial model, inputting the different growth rates from banker-supplied DCFs creates outputs that are $1.3 billion apart.[656] This sensitivity to PGR arises because Shaked initially assumed such a low investment rate while predicting outsized growth.[657] Because "the perpetuity growth rate and the investment rate are linked," changing the PGR in Shaked's original model would cause "a very large swing in his DCF value."[658] Shaked described his model's sensitivity to PGR based on his low investment rate as a "built-in problem."[659] Given the significant impact of Shaked's initial investment rate on his DCF, his concession on that input and failure to adjust the model introduces fatal unreliability.

Above, I determined that the market guides my analysis of this transaction. The Supreme Court has "cautioned against using the DCF methodology when market-based indicators are available."[660] Shaked's shift in his investment rate, the fact that he did not adjust his DCF to accommodate that shift, and the significance of his original investment rate to the output of his DCF render his model unreliable. Petitioners have failed to carry their burden to establish that Shaked's DCF model is a sufficiently reliable indicator, particularly in the shadow of a reliable market-based deal price. I do not attribute any weight to this metric.[661]

2. There is not a suitable peer group for a reliable comparative companies analysis.

***42** "[B]efore a comparable companies multiples analysis can be undertaken with any measure of reliability, it is necessary to establish a suitable peer group through appropriate empirical analysis."[662] "If, and only if, a proper peer set can be selected, the next step in the comparable companies analysis is to select an appropriate multiple and then determine where on the distribution of peers the target company falls."[663] Where the experts' identified companies are "too divergent from [the company] in terms of size, public status, and products, to form meaningful analogs for valuation purposes,"[664] this Court will disregard this valuation metric.[665]

The parties dispute the relevant peer group and argue that neither expert tested the reasonableness of the comparable companies selected. Hubbard selected comparable companies by reviewing equity analysts' reports in the year before the merger date and selecting the firms mentioned by three or more analysts at least once.[666] As a result, Hubbard included companies that operate outside the fast casual segment, including full-service restaurants like Brinker International, Darden Restaurants, Texas Roadhouse, and The Cheesecake Factory.[667] Hubbard found this analysis produced fair values ranging from $218.58 to $310.99[668]; he did not afford any weight to his comparable companies analysis, but viewed it as corroborative of deal price.[669] Petitioners question Hubbard's peer group as it includes much smaller companies, including sectors other than fast casual, and does not widely overlap with the comparable companies the bankers identified.

Meanwhile, Respondent highlights that weakness in Shaked's metric. Shaked used a peer group identified by at least 75% of bankers involved.[670] These results exclude all of the fast casual companies the bankers contemporaneously identified, except for Chipotle.[671] It also included and excluded similarly situated companies. For example, Shaked included McDonald's and Burger King, but excluded Wendy's; he included Domino's, but excluded Papa John's.[672] Shaked found this approach resulted in fair values falling between $377.00 and $382.00 per share; he weighed this valuation at 30%.[673]

Where an expert defers to a peer set without conducting a "meaningful, independent assessment of comparability" between the seller's business and the business of its peer companies it "is not useful and, frankly, not credible."[674] Neither expert presents a reliable empirical analysis to show a suitable peer group; both sets have material weaknesses. For that reason, I do not find comparable companies as a fair measure of value. Instead, I view both parties' comparable companies analyses as an attempt to corroborate their preferred valuation. I decline to afford them any weight.

3. There are insufficient comparable precedent transactions to generate a reliable valuation metric.

***43** Both parties' experts performed a precedent transaction analysis.[675] Hubbard selected precedent transactions by reviewing eleven transactions that Morgan Stanley included in its April 4, 2017 presentation to the board.[676] He "calculated valuations that are corroborative using multiples of EV/EBITDA based on ... precedent transactions" that led to a price per share range of $143.58 to $236.22.[677] Hubbard used this data point as corroborative and gave it no weight[678] because a precedent transaction analysis is "model-based" while "the market evidence is the real world."[679]

Shaked conducted a precedent transaction analysis by using data from the FactSet database filtered by acquisitions of restaurant companies in the United States or Canada with an enterprise value over $1 billion.[680] He then compared Panera's forecasted revenue growth to the upper quartile EBITDA multiples of three comparative transactions and conducted an analysis that led to a price per share range of $338.00 to $361.00 with a midpoint of $350.00 per share.[681] Even though Shaked explained at trial that he "was not really very thrilled with getting only three transactions[,]"[682] he still afforded it 10% weight.

The accuracy of these analyses depends, as with a comparable companies analysis, on the closeness of the comparable transaction. As Morgan Stanley recognized, there was not a "particular transaction that should serve as a direct comparable."[683] I find that neither sample size is reliable enough to afford it weight.

F. Respondent Is Not Entitled To A Refund Of Its Prepayment.

I turn now to the relief sought. The Company prepaid Dissenting Stockholders the full deal price, or $315.00 per share. Petitioners have obtained more than fair value, which I have found to be $303.44. The Company seeks a refund in the amount of the deducted synergies, or the difference between fair value and prepayment, plus interest on that amount. Petitioners and Respondent did not agree to a clawback provision in the event Respondent overpaid. Respondent cites no support for its request. Like others who have thought about this issue, including counsel's firm, I find the request for a refund has no present basis in Delaware's appraisal statute.[684]

Under Section 262(h), a surviving corporation seeking to lessen the significant amount of interest that can otherwise accrue in an appraisal action can prepay petitioning stockholders "an amount in cash."[685] As the General Assembly explained, "[t]here is no requirement or inference that the amount so paid by the surviving corporation is equal to, greater than, or less than the fair value of the shares to be appraised."[686] Upon prepayment, interest accrues only upon the sum of the difference between the amount prepaid and the judicially determined fair value, and any interest accrued to date unless paid at that time.[687] Section 262 does not explicitly contemplate any refund. Accordingly, appraisal litigants sometimes stipulate to a clawback provision in their prepayment agreement.[688]

***44** "Under Delaware law, the appraisal remedy is entirely a creature of statute."[689] "The goal of statutory construction is to determine and give effect to legislative intent."[690] "The courts may not engraft upon a statute language which has been clearly excluded therefrom by the Legislature."[691] "[S]uch action would place the court in a position of making law."[692] Nor may this Court "assume that the omission was the result of an oversight on the part of the General Assembly."[693] Where, as with Section 262, "a statute is silent on a particular matter, the otherwise detailed nature of the statute in other respects can be significant."[694] "[I]n drafting Section 262(h), the General Assembly made a determination as to the proper balance of the competing interests of appraisal petitioners, who have been cashed out of their preferred investment and denied the ability to invest the merger consideration in the market pending outcome of the case, and respondents, against whom too large an interest award may operate as a penalty."[695]

Here, the only permissible conclusion is fortunately a logical one: the General Assembly intended to omit a refund mechanism. In 2016, the General Assembly enacted an optional and scalable prepayment scheme without mention of a refund. It did so in the shadow of the Model Business Corporation Act (the "Model Act"), adopted by the majority of other states, which is a mandatory and fixed prepayment scheme: it mandates prepayment of what the corporation believes is fair value to stockholders who purchased their stock before the merger was announced, and permits it for stock acquired after the merger announcement.[696] Other amendments to Section 262 have tracked the Model Act, evidencing a legislative awareness of its content.[697] The Model Act is silent on the effects of overpayment, like Section 262, and has been interpreted to allow petitioning stockholders to keep any overpayment.[698]

Commentators have also interpreted Section 262's silence as an indication that overpayment is not recoverable.[699] This Court has not yet resolved the issue.[700] I conclude Section 262 does not explicitly provide for a refund, and that therefore I cannot order one. I am not the first to conclude that the Court must stay within the bounds of Section 262's plain language. In 1948, the Delaware Supreme Court concluded that because the operative version of Section 262 did not provide for interest, the judiciary could not award it.[701] More recently, before the prepayment provision was enacted, Vice Chancellor Glasscock found he was unable to order prepayment.[702] After those exercises in judicial restraint, amendments in the statute soon followed.[703] I will not encroach on the General Assembly's prerogative.[704]

III. CONCLUSION

***45** For the reasons discussed above, I find the fair value of the Company's common stock at time of the merger was $303.44, calculated as deal price minus synergies. Respondent chose to prepay the $315.00 deal price to the Dissenting Stockholders. Because Respondent is not entitled to a refund of the difference between $315.00 and $303.44, Petitioners have received more than fair value. The parties shall submit a stipulated implementing order.

All Citations

Not Reported in Atl. Rptr., 2020 WL 506684

Footnotes

[1] Citations in the form "PTO ¶ —" refer to stipulated facts in the pre-trial order. *See* Docket Item ("D.I.") 108. Citations in the form "[Name] Tr." refer to witness testimony from the trial transcript. Citations in the form "[Name] Dep." refer to witness testimony from a deposition transcript. Citations in the form "JX — at —" refer to a trial exhibit.

[2] *See* D.I. 103, Ex. 1. The subset of exhibits the parties relied on is set forth on the schedule of evidence. *See* D.I. 148, Ex. A; D.I. 151.

[3] PTO ¶¶ 48, 89.

[4] *Id.* ¶ 48.

[5] *Id.* ¶ 49.

[6] *Id.* ¶ 1.

[7] *Id.* ¶¶ 66–67.

[8] *Id.* ¶ 65.

[9] *Id.* ¶ 68.

[10] *Id.* ¶ 20.

[11] *Id.* ¶ 22.

[12] *Id.* ¶ 26.

[13] *Id.* ¶ 32.

[14] *Id.* ¶ 37.

[15] *Id.* ¶ 42.

[16] *Id.* ¶ 50. These directors served from January 2016 until the merger closed.

[17] *Id.* ¶ 51.

[18] *Id.*

[19] *Id.*; Shaich Tr. 936:2–937:10.

[20] Shaich Tr. 937:11–938:1.

[21] *Id.* 940:12–21; *accord* PTO ¶ 51.

[22] PTO ¶ 51.

[23] *Id.*; *see also* JX0005.

[24] PTO ¶ 98.

[25] *Id.* ¶ 52.

[26] *Id.*

[27] *See id.* ¶¶ 53–59.

[28] *Id.* ¶ 60.

[29] *Id.*

[30] *Id.*

[31] *Id.* ¶ 61.

[32] *Id.*

[33] *Id.* ¶ 62.

[34] *Id.* ¶ 86; Shaich Tr. 924:4–17.

[35] PTO ¶ 86.

[36] *Id.*

[37] *Id.*; Shaich Tr. 926:20–927:3.

[38] PTO ¶ 86.

[39] *Id.*

[40] JX0400 at 17.

[41] Moreton Tr. 710:23–711:12.

[42] Moreton Tr. 714:5–20, 732:11–24. From 2007–2009, Panera also expanded by acquiring Paradise Bakery & Café, a Phoenix, Arizona-based concept with over 70 locations in 10 states. PTO ¶¶ 87–88.

[43] PTO ¶ 92.

[44] *See* JX0400 at 18.

[45] Shaich Tr. 938:2–16.

[46] *Id.* 938:2–939:22.

[47] PTO ¶ 102.

[48] Shaich Tr. 938:7–939:8.

49 *Id.* 938:7–939:10.

50 *Id.* 938:7–939:16; *see also* PTO ¶ 51; Moreton Tr. 742:23–743:8.

51 JX0006 at 1.

52 *See* JX0007 (examining Panera 2.0 and the associated costs of the investments); *see also* JX0008 (CheatSheet article detailing the purchase of a “to-go bread bowl via smart phone”).

53 JX0009 at 1–2.

54 *Id.* at 1.

55 *Id.* at 2.

56 *Id.* at 1–2.

57 *Id.* at 2.

58 Shaich Tr. 946:3–8.

59 JX2009 at 2; *accord* JX0564 at 79.

60 PTO ¶¶ 113–14.

61 *Id.* ¶¶ 115, 121, 126.

62 *Id.* ¶¶ 106–109.

63 Shaich 945:19–23.

64 PTO ¶ 122.

65 Moreton Tr. 718:21–719:11.

66 Shaich Tr. 1017:23–1018:10.

67 *Id.* 1017:23–1018:10.

68 JX0010 at 3; *accord* Moreton Tr. 718:14–719:11.

69 PTO ¶ 62.

70 Moreton Tr. 800:3–17.

71 Shaich Tr. 1017:23–1018:10.

72 *Id.* 1026:11–24.

73 PTO ¶ 117; JX0315; Moreton Tr. 724:4–725:6.

74 Moreton Tr. 724:18–22, 768:19–769:8; *accord* PTO ¶ 118.

75 Moreton Tr. 724:4–725:6.

76 PTO ¶ 118; *see also* Moreton Tr. 734:19–735:4, 764:17–765:8; Shaich Tr. 1015: 19–21; Colasacco Dep. 197:19–198:19. Petitioners object to Respondent's use of Colasacco's deposition testimony at trial. *See* D.I. 108 ¶ 216; D.I. 131; D.I. 148 Ex. A at 9. Under Court of Chancery Rule 32, “[t]he deposition of a witness, whether or not a party, may be used by any party for any purpose if the Court finds ... that the witness is out of the State of Delaware, unless it appears that the absence of the witness was procured by the party offering the deposition.” Ct. Ch. R. 32(a)(3)(B). Colasacco is a Massachusetts resident and Petitioners do not contend that Panera procured Colasacco's absence from Delaware. D.I. 119 at 24:2–14, 25:9–11. Petitioners argue that even if the testimony could come in under Rule 32, Delaware Rule of Evidence 802 precludes this testimony. *See* Trial Tr. at 642:11–16. Rule 32 testimony is not an out of court statement, but treated “as though the witness were then present and testifying.” Ct. Ch. R. 32(a). Colasacco's testimony is thereby admissible under Rule 32.

77 JX0315 at 3–4; *accord* Shaich Tr. 941:10–943:18 (“So I had a goal of sustained double-digit earnings but reengaging this company and moving it forward—it was mature—and taking it to the next place.”).

78 JX0315 at 131; JX0134 at 118.

79 Moreton Tr. 729:2–20; *accord* Colasacco Dep. 217:3–219:15 (understanding that “if it worked I would have considered it a home run,” but recognizing “there aren't many companies that can do” “25 percent per annum compounded for five years,” so the model “had some risk attached to achieving it”).

80 JX0228 at 2 (emphasis in original).

81 Moreton Dep. 218:23–219:20 (“So the risk then switches to: Is it possible? Yes. Is it a guarantee? No. And what's the major ... risk ... is around execution. So ... that's really the time period that we're in and how Panera saw it during my time.”). Petitioners identify the Company's 90% confidence in its ability to achieve several

initiatives in the model. *See* JX0616 at 29. In using this to cast the Five-Year Financial Model as risk adjusted, however, Petitioners improperly conflate the model's "comp buffer"—designed to learn how different initiatives overlap—with risks associated with competition or execution. *See* Moreton Tr. 740:4–741:15, 860:15–861:7.

[82] Colasacco Dep. 217:3–219:15.

[83] JX0104 at 1; *see also* JX0343 at 19 (analysts acknowledging that Panera's strategic initiatives were "a very ambitious target").

[84] Moreton Tr. 720:18–721:20; Colasacco Dep. 65:19–66:20.

[85] PTO ¶ 75.

[86] *See* JX0019 at 18–25; PTO ¶ 120.

[87] *See, e.g.*, JX0019 at 19–20, 24, 33, 34, 41, 42, 44, 50, 52, 56.

[88] Moreton Tr. 773:9–774:5.

[89] *Id.* 770:24–771:15.

[90] JX0019 at 18; Shaich Tr. 956:4–22; Moreton Tr. 770:24–771:19.

[91] *See* Shaich Tr. 955:24–957:7, 958:1–19; *accord* Moreton Tr. 770:24–771:19.

[92] JX0019 at 2.

[93] *See* Moreton Tr. 722:11–19 ("[W]e agreed to increase our share buyback, again a program we'd had going on for a long time, but we agreed to buy back $500 million worth of shares over a 12-month period. We agreed to evaluate selling company stores to franchisees without a specific number.").

[94] *Id.* 722:11–23.

[95] *Id.* 776:5–778:16, 778:17–779:2.

[96] *Id.* 785:17–786:8; JX0238 at 33.

[97] Shaich Tr. 948:6–13, 960:8–961:3; *see, e.g.* JX0194 at 1; JX0192 at 5, 11; JX2028 at 3, 17; JX0032 at 51; JX0041 at 5, 22; JX0064 at 2; JX0260 at 4–5, 15; JX0331 at 3–4; JX0345 at 4–5, 14; JX0029; JX1039; JX0063 at 3; JX0304.

[98] JX0063 at 3.

[99] Moreton Tr. 792:4–13.

[100] JX0104 at 1.

[101] Shaich Tr. 965:11–966:5; *accord* Moreton Tr. 793:14–22.

[102] Shaich Tr. 967:13–19.

[103] JX0111.

[104] *See id.* at 4–5.

[105] *See* JX0110; JX0118; JX0772 at 56; Moreton Tr. 793:14–22.

[106] JX0116; JX0118; JX1012; *accord* Shaich Tr. 968:22–969:5.

[107] JX0118; Shaich Tr. 969:17-970:1.

[108] JX1012.

[109] JX0116.

[110] *See* JX0122 at 2; JX0128.

[111] JX0116; JX0122 at 1; JX0125 at 4; *accord* Moreton Tr. 794:8–796:8.

[112] Moreton Tr. 796:3–8.

[113] *See id.* 796:9–17.

[114] *See* JX0239 at 2–3.

[115] *See* JX0156; JX0153; *accord* Shaich Tr. 970:14–21.

[116] *See* JX0156 at 4.

[117] Shaich Tr. 970:6–972:8.

[118] *Id.* 971:20–972:8.

[119] *Id.* 970:14–21.

[120] JX0197; *accord* Shaich Tr. 972:12–973:3.

[121] Shaich Tr. 973:4–16.

[122] JX0243; JX0250; Moreton Tr. 797:2–798:22; Shaich Tr. 974:2–10.

[123] JX0243.

[124] *See* JX0250; Moreton Tr. 798:6–17.

[125] Moreton Tr. 796:21–797:1.

[126] JX0266; JX0263.

[127] Shaich Tr. 973:4–11.

[128] *Id.* 975:15–24.

[129] *Id.* 974:11–22, 975:15–976:10; *accord* JX0625 at 4 ("There were conversations with Starbucks last year, they ultimately declined to proceed citing that Panera was trading too richly (and it has since only traded up)."); JX0772 at 56; Moreton Tr. 798:23–799:10.

[130] Shaich Tr. 976:1–4.

[131] Moreton Tr. 799:24–800:2.

[132] Shaich Tr. 976:11–23; *accord* Bell Tr. 1143:12–15.

[133] Bell Tr. 1143:4–22.

[134] *Id.* 1143:16–22.

[135] *Id.* 1143:12–22; *accord* Shaich Tr. 976:24–977:6.

[136] Moreton Tr. 792:4–13; *accord* Shaich Tr. 976:5–10; JX0631 at 10.

[137] JX1041 at 4.

[138] PTO ¶ 126.

[139] *Id.* ¶ 91.

[140] *Id.* ¶ 127; JX0306.

[141] PTO ¶ 129. Panera completed rollout of its MyPanera customer loyalty program in November 2010. *See* JX0003.

[142] JX0741 at 1.

[143] JX0359 at 4.

[144] JX0331 at 3–4.

[145] JX0342 at 7.

[146] JX0129 at 1.

[147] *See* Moreton Tr. 801:20–21; JX0364 at 1; JX0342 at 7.

[148] JX0334.

[149] Shaich Tr. 976:11–977:6; *accord* JX0318; JX0334.

[150] *See* Shaich Tr. 977:17–978:7; JX0338.

[151] PTO ¶ 130.

[152] *See* JX0374; PTO ¶ 130.

[153] Bell Tr. 1147:11–1148:8.

[154] *Id.* 1148:9–22.

[155] Shaich Tr. 1043:15–1043:24.

[156] PTO ¶ 131.

[157] *See* JX0287 at 9; *accord* Shaich Tr. 980:11–981:4; 1045:15–22.

[158] Shaich Tr. 1044:5–1044:24.

[159] PTO ¶ 131; JX0407 at 1; JX0408 at 3–4.

[160] JX0408 at 3–4.

[161] Shaich Tr. 1048:2–1048:17.

[162] PTO ¶ 131; JX0408 at 3–4.

[163] PTO ¶ 131; JX0408 at 4.

[164] Shaich Tr. 984:14–23 ("I don't think anybody on the board, myself or anybody on the board would have thought to bring an investment banker in. We had been through this kind of process before, and bankers are very expensive, and we had no offer. So I think we needed to understand, what was JAB going to say."); *accord* Moreton Tr. 804:18–805:1; Colasacco Dep. 138:18–139:15.

[165] *See* JX0407 at 47–102; JX0408 at 1 ("The agenda for the Board of Directors meeting included the following matters: administrative matters, Special Focus topics, including a review of the 2016 Key Initiatives, 2017 Key Initiatives and financial plan and related business strategy updates, review of financial results ....").

[166] PTO ¶ 118; Moreton Tr. 780:24–781:9, 859:4–16.

[167] Moreton Tr. 828:22–830:18.

[168] PTO ¶ 132.

[169] *Id.*

[170] JX0631 at 6.

[171] Bell Tr. 1107:24–1108:22; Shaich Tr. 1039:22–24.

[172] PTO ¶ 132.

[173] *Id.*

[174] *Id.* ¶ 133.

[175] Bell Tr. 1104:2–1106:9, 1107:24–111:8.

[176] JX0581.

[177] Bell Tr. 1109:17–1111:8.

[178] Bell Dep. 49:9–14.

[179] PTO ¶¶ 79–80.

[180] JX0581.

[181] *Id.*

[182] *Id.*

[183] JX0418 at 2. Goldman participated in a $3 billion credit facility in connection with the merger. Goldman agreed to provide 33.3% of the credit facility, along with J.P. Morgan Chase & Co. and the Bank of America Corporation. PTO ¶ 76.

Petitioners moved to restrict Respondent's use of any JAB evidence to support its case. *See* D.I. 139 at 12 n.53. I considered and denied this argument in my March 20, 2019 bench ruling on Petitioners' motion in limine. *See* D.I. 111. I maintain that Petitioners' attempt and failure to obtain additional discovery in the Netherlands precludes their later attempt to restrict use of any documents in this Court. *See id.* at 5:9–6:9. Petitioners deposed Bell and received documents from Bell as a custodian. Petitioners used Bell's testimony and JAB documents in its post-trial arguments. Petitioners have not shown that Respondent relied on any JAB documents that were not produced in discovery. For these reasons, along with those explained in my March 20 bench ruling, Petitioners' request is denied.

[184] Moreton Tr. 775:17–22; Shaich Tr. 988:19–999:4 ("I knew Goldman, but I knew many bankers. I had worked with others. And I think that I felt we could be well represented in many ways.").

[185] JX0418 at 2.

[186] Kwak Tr. 1194:7–13.

[187] PTO ¶ 77.

[188] *Id.* ¶ 78.

[189] *Id.* ¶ 135.

[190] *See* JX0421 at 2.

[191] PTO ¶ 135; JX0421 at 2. On March 15, the board initiated the engagement process with Morgan Stanley. PTO ¶ 137. On April 2, the Company entered into an engagement letter with Morgan Stanley. JX0596.

[192] JX0466 at 2. Boublik was the lead senior banker from Morgan Stanley advising Panera management and the board in connection with the potential transaction with JAB during the Panera engagement. At Morgan Stanley, he served as Chairman of M&A for the Americas and Managing Director. PTO ¶ 71.

[193] Bell Tr. 1113:21–1114:4.

[194] PTO ¶ 141.

[195] JX0689; Kwak Tr. 1256:8–1258:8.

[196] JX0448 at 1.

[197] PTO ¶ 151.

[198] *Id.* ¶ 72.

[199] *See* JX0606.

[200] Kwak Tr. 1219:23–1220:16.

[201] *See* JX0625 at 3.

[202] JX0562.

[203] JX0789 at 52–53.

[204] PTO ¶ 155; JX0562.

[205] JX0562 at 2.

[206] *Id.* at 3.

[207] *See* JX2021.

[208] Moreton Tr. 837:9–838:9.

[209] Shaich Tr. 1068:21–1070:1.

[210] *Id.* 1068:21–1070:1; Moreton Tr. 905:7–908:11.

[211] PTO ¶¶ 134, 136.

[212] *Id.* ¶¶ 134, 136.

[213] *Id.* ¶ 134.

[214] *See* Kwak Tr. 1208:6–1209:9.

[215] *See id.*

[216] JX0455.

[217] *See* Shaich Tr. 996:10–997:5.

[218] JX0435; *accord* Moreton Tr. 822:9–823:1.

[219] PTO ¶ 139.

[220] *Id.*

[221] *Id.* ¶ 140; *accord* Shaich Tr. 1002:9–23; JX0483.

[222] JX0552 at 3.

[223] PTO ¶ 141.

[224] JX0448 at 1; *see also* JX0432 at 2.

[225] JX0456 at 2.

[226] PTO ¶ 142.

[227] JX0494 at 1.

[228] PTO ¶¶ 144–45.

[229] Bell Tr. 1105:3–1106:9.

[230] *See* PTO ¶ 146.

[231] *See* JX0494 at 1.

[232] JX0491.

[233] PTO ¶ 143.

[234] Kwak Tr. 1254:24–1255:3.

[235] Moreton Tr. 827:10–24; *accord* Kwak Tr. 1233:10–20.

[236] Colasacco Dep. 142:11–143:15.

[237] *See, e.g.*, Moreton Tr. 748:4–13, 768:13–769:8, 780:22–781:9, 805:2–16, 839:17–840:3; Shaich Tr. 951:18–952:2, 1015:15–21.

[238] JX0491; *accord* JX0490.

[239] PTO ¶ 146.

[240] *Id.* ¶ 149; JX1011.

[241] PTO ¶148; JX0513.

[242] JX0513.

[243] Shaich Tr. 1007:7–17.

[244] *See* JX0418 at 2 (“We are making a friendly, confidential offer. If there is a leak, we will walk away.”); Bell Tr. 1104:5–16 (referencing JX0418 and stating “the way we give offers at JAB, among other things, is to

require confidentiality. We think it's in the mutual interests of both parties. It's just the way we work. And so we said that fundamental to our offer was the fact that it had to remain confidential."); Kwak Tr. 1196:22–1198:1 (testifying that Morgan Stanley was familiar with the JAB playbook and understood that JAB's threat to walk was real).

245 PTO ¶ 150.

246 *Id.* ¶ 154; JX0545 at 1–2; JX0552.

247 PTO ¶ 154; *accord* JX0552 at 3–12 (valuing the Company through a multiples-based valuation matrix from the street and management cases, historical trading and multiples analyses, comparable companies analyses and a precedent transactions analysis).

248 JX0552 at 14–15.

249 *Id.*

250 Kwak Tr. 1199:9–1200:3, 1228:18–1229:5.

251 *See* JX0552 at 14–15.

252 *Id.* at 14.

253 Shaich Tr. 1019:18–1021:16; Moreton Tr. 811:19–812:17, 824:3–12, 912:12–16.

254 Shaich Tr. 1019:18–1020:13.

255 *Id.* 1020:14–19.

256 *Id.* 1020:20–23.

257 *Id.* 1020:24–1021:4.

258 *Id.* 1021:5–9.

259 *Id.* 1021:10–12.

260 *Id.* 1021:13–16.

261 Moreton Tr. 811:19–812:17; *accord id.* 912:7–11 ("[T]here was nobody else to reach out to ... [w]e went through the process.").

262 JX0546 at 1. These leaders included Bell, Axel Bhat (JAB partner and CFO), Trevor Ashley (JAB principal), and Tim Hennessy (JAB Beech CFO). *Id.*

263 Shaich Tr. 1010:9–22; JX0564.

264 *See generally* JX0564; *accord* Moreton Tr. 840:14–23.

265 JX0593 at 49–50 (confirming JAB's pre-diligence estimates and predicting $365 to $570 million in cost savings).

266 *Compare* JX0400 at 44, *with* JX0593 at 65.

267 PTO ¶ 159; JX0609.

268 *See, e.g.*, JX0631 at 5; JX0982 at 61.

269 JX0546 at 1.

270 JX0607.

271 *Compare* JX0564, *with* JX0607.

272 *See* JX0564; JX0607; *accord* Moreton Tr. 840:14–23.

273 *See* JX0564 at 131; JX0607 at 145.

274 *See* JX0564 at 141–152; JX0607 at 155–169.

275 JX0564 at 154–158; JX0607 at 171–175.

276 JX0607 at 229.

277 *Id.*

278 *See id.*

279 *See* Bell Tr. 1129:2–24.

280 *See* JX0400 at 43; JX0593 at 64.

281 PTO ¶ 160.

282 *Id.* ¶ 161.

283 JX0631 at 6.

284 PTO ¶ 161.

[285] *See* JX0627 at 20.

[286] *See id.*

[287] PTO ¶ 163.

[288] *Id.*; JX0608; JX0628 at 1; JX0629.

[289] PTO ¶ 164; JX0629; JX0616; *accord* Moreton Tr. 840:4–20.

[290] *See* PTO ¶ 165; JX0631.

[291] JX0631 at 1–14.

[292] *Id.* at 15–20.

[293] *Id.* at 19.

[294] JX0628 at 2; Moreton Tr. 843:14–845:3.

[295] Kwak Tr. 1236:18–1237:10. Kwak explained:

> A few considerations:
>
> You've got to believe that 80+% of your value is in the terminus
>
> Everything has got to go right; there is always risk of execution which may not be captured by our calculated WACC
>
> All initiatives are proven strategies, but not all are proven on a large scale
>
> Restaurant space is competitive – our guys are ahead of the pack now in terms of technology, for instance, but it's a r[i]sk that others are striving to catch up[.]

JX0625 at 3–4.

[296] Kwak Tr. 1221:2–11, 1235:17–1236:8, 1240:11–13.

[297] JX0628 at 2.

[298] *Id.* at 3.

[299] *Id.*

[300] PTO ¶ 167; JX0630 at 1.

[301] JX0647.

[302] PTO ¶ 167; JX0628 at 2.

[303] PTO ¶ 167; JX0630 at 2.

[304] PTO ¶ 170; *accord* JX0655.

[305] PTO ¶ 2.

[306] *Id.* ¶ 3.

[307] *Id.* ¶ 4.

[308] *Id.* ¶¶ 5-6; JX0842 at 3.

[309] PTO ¶ 7.

[310] Kwak Tr. 1215:24–1218:2; Moreton Tr. 842:22–843:2.

[311] PTO ¶ 89.

[312] *Id.* ¶ 180.

[313] *Id.* ¶ 9.

[314] *Id.* ¶ 10.

[315] *Id.* ¶ 11.

[316] *Id.* ¶ 13.

[317] *See id.* ¶¶ 14–19.

[318] *See* D.I. 134.

[319] D.I. 142.

[320] *See* D.I. 144.

[321] *See* D.I. 154.

[322] JX0983 at 10.

[323] *Id.*; *accord* Shaked Tr. 394:10–12.

[324] JX0983 at 6.

[325] *See* JX0982 at 55–56; *accord* Hubbard Tr. 1479:23–1480:6.

[326] JX0982 at 5.

[327] *Cede & Co. v. Technicolor, Inc.*, 542 A.2d 1182, 1186 (Del. 1988).

[328] *DFC Glob. Corp. v. Muirfield Value P'rs, L.P.*, 172 A.3d 346, 364 (Del. 2017) (quoting *Golden Telecom, Inc. v. Glob. GT LP*, 11 A.3d 214, 217–18 (Del. 2010)); *accord* 8 *Del. C.* § 262(h).

[329] *Tri-Continental Corp. v. Battye*, 74 A.2d 71, 72 (Del. 1950); *accord Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc.*, 210 A.3d 128, 132–133 (Del. 2019).

[330] *In re Appraisal of Stillwater Min. Co.*, 2019 WL 3943851, at *19 (Del. Ch. Aug. 21, 2019) (internal quotation marks omitted) (quoting *M.G. Bancorp., Inc. v. Le Beau*, 737 A.2d 513, 525 (Del. 1999)), *judgment entered* 2019 WL 4750400 (Del. Ch. Sept. 27, 2019).

[331] *Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*, 177 A.3d 1, 21 (Del. 2017) (footnote omitted) (quoting *In re Appraisal of PetSmart*, 2017 WL 2303599, at *26 (Del. Ch. May, 26, 2017), and then quoting *Golden Telecom*, 11 A.3d at 218).

[332] *M.G. Bancorp.*, 737 A.2d at 520.

[333] *Pinson v. Campbell-Taggart, Inc.*, 1989 WL 17438, at *6 (Del. Ch. Feb. 28, 1989).

[334] *Stillwater*, 2019 WL 3943851, at *18 (quoting Jesse A. Finkelstein & John D. Hendershot, *Appraisal Rights in Mergers and Consolidations*, Corp. Prac. Series (BNA) No. 38-5th, at A-90 (2010 & 2017 Supp.)).

[335] *See In re Appraisal of Jarden Corp.*, 2019 WL 3244085, at *1 (Del. Ch. July 19, 2019), *reargument granted in part, denied in part*, 2019 WL 4464636 (Del. Ch. Sept. 16, 2019). *Merion Capital L.P. v. Lender Processing Servs., L.P.*, 2016 WL 7324170, at *16 (Del. Ch. Dec. 16, 2016); *Glob. GT LP v. Golden Telecom, Inc.*, (*Golden Telecom Trial*), 993 A.2d 497, 517 (Del. Ch.), *aff'd*, 11 A.3d 214 (Del. 2010);

[336] *Dell*, 177 A.3d at 24.

[337] *Id.*

[338] *DFC*, 172 A.3d at 366.

[339] *Dell*, 117 A.3d at 35.

[340] *Stillwater*, 2019 WL 3943851, at *21 (citing *Dell*, 177 A.3d at 21; *DFC*, 172 A.3d at 366–67).

[341] *Id.*

[342] *Id.* at *22; *accord Aruba*, 210 A.3d at 137 ("[A] buyer in possession of material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller when agreeing to buy the company at a particular deal price, and that view of value should be given considerable weight by the Court of Chancery absent deficiencies in the deal process."); *Jarden*, 2019 WL 3244085, at *23 ("This court has heeded the Supreme Court's guidance and regularly rests its appraisal analysis on the premise that when a transaction price represents an unhindered, informed and competitive market valuation, that price 'is at least first among equals of valuation methodologies in deciding fair value.' " (quoting *In re Appraisal of AOL Inc.*, 2018 WL 1037450, at *1 (Del. Ch. Feb. 23, 2018))).

[343] *See Stillwater*, 2019 WL 3943851, at *21.

[344] *Id.* at *22.

[345] *Id.* at *44.

[346] *AOL*, 2018 WL 1037450, at *8.

[347] *Stillwater*, 2019 WL 3943851, at *22 (citing *DFC*, 172 A.3d at 349).

[348] *Id.*; *see also DFC*, 172 A.3d at 375–76.

[349] *Stillwater*, 2019 WL 3943851, at *23 (citing *Aruba*, 210 A.3d at 137–38); *see also Dell*, 177 A.3d at 30 (review of "the Company's confidential information"); *DFC*, 172 A.3d at 355–56 (same).

[350] *Stillwater*, 2019 WL 3943851, at *23 (citing *Aruba*, 210 A.3d at 139; *Dell*, 177 A.3d at 28).

[351] *Id.* (citing *Aruba*, 210 A.3d at 136 ("It cannot be that an open chance for buyers to bid signals a market failure simply because buyers do not believe the asset on sale is sufficiently valuable for them to engage in a bidding contest against each other."); *Dell*, 177 A.3d at 29 ("Fair value entails at minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay."); *id.* at 33 (finding that absence of higher bid meant "that the deal market was already robust and that a topping bid involved a serious risk of overpayment," which "suggests the price is already at a level that is fair")).

352 *Id.* at *22.

353 *Cf. id.* (synthesizing the three recent Supreme Court appraisal decisions in *Aruba*, *Dell*, and *DFC*).

354 This point does not appear to be in serious dispute. Petitioners' opening post-trial brief did not assert that Panera's stock did not trade in an efficient market. The parties discussed the efficiency of the market for Panera's stock only while talking past each other about whether weight should be given to Panera's stock price. *Compare* D.I. 138 at 60–65, *and* D.I. 141 at 23, *with* D.I. 140 at 40–46. Out of an abundance of caution, I make the unsurprising finding that Panera "ha[d] many stockholders; no controlling stockholder; 'highly active trading'; and ... information about the company [was] widely available and easily disseminated to the market." *See* Dell, 177 A.3d at 25 (citation omitted). Panera also had a large market capitalization, substantial public float and trading volume, a low bid-ask spread, a high number of equity analysts, and a rapid response to transaction rumors. *See* id. at 7, 25. Hubbard's report on these factors was persuasive and supported by evidence presented at trial. JX0982 at 58–61; Hubbard Tr. 1504:11–1505:14, 1506:11–24. In my view, these straightforward factors are plainly present and provide conclusive evidence of an efficient market for Panera's stock. This conclusion is undisturbed by Shaked's analyses of market reactions to Panera news, which I find to be plagued by subjectivity in what is "new and material" information, and a failure to account for trading volume. *See* JX0988 at 83–84, 90–92.

355 Redpath Tr. 635:6–9. Redpath is a senior investment banking partner at Cypress Associates, a "nationally recognized investment banking firm." *See id.* 499:9–14, 505:18–21.

356 *Id.* 635:24–638:9, 643:12–644:8. Petitioners claim a special committee was necessary here, but Petitioners cannot point to a conflict that a special committee could remedy where Panera had seven independent board members on its nine-member board.

357 JX0476 at 2; JX0583 at 1.

358 172 A.3d at 349.

359 JX0461 at 1; JX0581; *accord* JX0476 at 2 ("Remember, this is a very clean public company, so have to tone down the voluminous generic requests ....").

360 Shaich Tr. 921:7–9, 948:2–18, 960:8–961:3, 962:17–23; *see, e.g.*, JX0194 at 1; JX0192 at 5, 11; JX2028 at 3, 17; JX0032 at 51; JX0041 at 5, 22; JX0064 at 2; JX0260 at 4–5, 15; JX0331 at 3–4; JX0345 at 4–5, 14; JX0029; JX1039; JX0063 at 3; JX0304.

361 JX0490; *accord* Moreton Tr. 840:7–23.

362 JX0593 at 49–50. These findings are discussed further in Section II(D), *infra*.

363 PTO ¶ 161.

364 Kwak Tr. 1206:15–1207:6; *accord* Moreton Tr. 821:7–14 ("Q. Did Panera at any time in the negotiations give a, quote, unquote, counteroffer in the sense of a specific price point at which it would agree to a deal? A. No. We never did. This was part of the strategy that Morgan Stanley helped craft, that there was no reason to do that. At this point, it was just a push for more.").

365 Shaich Tr. 999:9–1002:4.

366 PTO ¶¶ 139, 141; JX0448 at 1; *accord* Moreton Tr. 822:1–8 ("JAB's transactions had gone from the initial discussions and initial bids, through due diligence, to the end, and how they had a history of raising their offer price as they went through.").

367 Moreton Tr. 820:4–13; *accord* JX0519 at 1.

368 PTO ¶ 140; *accord* Shaich Tr. 1002:9–23; JX0483.

369 PTO ¶ 141 ("The Board supported moving forward with further discussions and due diligence but again expressed its expectation that any final offering price be significantly higher.").

370 *See* Moreton Tr. 821:7–822:8.

371 PTO ¶ 161.

372 *Id.* ¶¶ 148, 159; Kwak Tr. 1215:24–1218:2.

373 *In re Appraisal of Solera Hldgs., Inc.*, 2018 WL 3625644, at *14 (Del. Ch. July 30, 2018) (analyzing *Dell* and commenting that "[g]iven leaks in the press that Dell was exploring a sale ... the world was put on notice of the possibility of a transaction so that any interested parties would have approached the Company before

the go-shop if serious about pursuing a deal." (internal quotation marks omitted)); *cf.* DFC, 172 A.3d at 376 (identifying "the failure of other buyers to pursue the company when they had a free chance to do so" as an objective indicator of fairness supporting deal price).

374 Kwak Tr. 1216:11–1217:16.

375 *Id.* 1216:11–23.

376 *Id.* 1216:24–1217:16.

377 JX0609.

378 Kwak Tr. 1242:11–1243:3. In Kwak's view, the leak gave interested bidders sufficient time to come forward before signing. *Id.* 1242:11–23. Redpath agreed. JX0985 at 76 ("There was sufficient time for a topping bidder to emerge post-signing.").

379 PTO ¶¶ 132, 161; JX0789 at 71–75, 79–81; *see also* JX0772 at 97–100, 106–107.

380 *See, e.g.*, Kwak Tr. 1240:14–21, 1241:10–24.

381 *Id.* 1241:10–15.

382 *Id.* 1241:16–24.

383 *Id.* 1241:5–9.

384 *Id.* 1242:11–23.

385 This Court has recently posited that deal price is persuasive evidence of fair value, even with a limited pre-signing outreach, if the merger agreement's deal protections are sufficiently open to permit a post-signing passive market check in line with what decisions have held is sufficient to satisfy enhanced scrutiny. *Stillwater*, 2019 WL 3943851, at *24–30. As *Stillwater*'s holdings have been appealed to the Delaware Supreme Court, I limit my holding today to the unremarkable conclusion that no bidders emerged in the face of nonpreclusive deal protections. But with the aid of the parties' briefing on the issue, it seems to me that Panera's post-signing market check would survive enhanced scrutiny and therefore under *Stillwater*, would support deal price as fair value. For example, in *C & J Energy*, the parties bargained for a suite of deal protections, including a no-shop clause subject to a fiduciary out, a 2.27% termination fee, and a post-signing passive market check lasting 153 days. *See C & J Energy Servs., Inc. v. City of Miami Gen. Emps.*, 107 A.3d 1049, 1063 (Del. 2014). The Delaware Supreme Court explained that under this suite, "a potential competing bidder faced only modest deal protection barriers," *id.* at 1052, and "there were no material barriers that would have prevented a rival bidder from making a superior offer," *id.* at 1070. In support, the Delaware Supreme Court approvingly cited *In re Dollar Thrifty Shareholder Litigation*, 14 A.3d 573, 612–13, 615 (Del. Ch. 2010). In *Dollar Thrifty*, this Court found the board used reasonable judgment to deal exclusively with the buyer without conducting a pre-signing market check where deal protections included a no-shop provision with a fiduciary out, matching rights, a 3.9% termination fee, and a passive post-signing market check lasting 126 days. *Id.* at 592–93, 614–16. And in *In re PLX Technology Inc. Stockholders Litigation*, the Delaware Supreme Court affirmed this Court's damages ruling where the trial court determined damages based on a quasi-appraisal theory that the company should have remained a standalone company. 211 A.3d 137 (Del. 2019) (TABLE), *aff'g In re PLX Tech. Inc. S'holders Litig.*, 2018 WL 5018535 (Del. Ch. Oct. 16, 2018). At trial, this Court found that the sale process as a whole was sufficiently reliable to reject a DCF methodology where the process included a fifty-day passive, post-signing market check with a suite of deal protections, including a no-shop with a fiduciary out, unlimited matching rights, and a 3.5% termination fee. *PLX*, 2018 WL 5018535 at *2, *26–27, *44, *55. Panera's deal protections differ little from those in *C & J Energy*, *Dollar Thrifty*, and *PLX*. Panera's 3.0% termination fee falls on the low end of the range presented by these deals. As for the time between announcement and closing or injunction, Panera's falls in the middle. Each deal contained a no-shop provision with a fiduciary out, and *Dollar Thrifty* and *PLX* included matching rights. Panera's deal protections fall within what Delaware courts have held to satisfy enhanced scrutiny.

386 JX0985 at 76.

387 *DFC*, 172 A.3d at 376; *accord Stillwater*, 2019 WL 3943851, at *35.

388 *Stillwater*, 2019 WL 3943851, at *42 (quoting *Dell*, 177 A.3d at 29); *see also Dell*, 177 A.3d at 32–34; *Aruba*, 210 A.3d at 136.

389 Shaich Tr. 1019:18–1020:13.

390 *See* JX0700 at 2.

391 *See id.*; JX0654 at 1–2. The other referenced potential bidder in the Bloomberg article, Domino's, expressed that it was not interested and was not "having any conversations regarding the purchase of Panera" because it has "a lot more opportunity for growth in pizza." JX0609 at 2, 4.

392 *Dell*, 117 A.3d at 35.

393 *Id.*

394 *Id.* at 9 (quoting *In re Appraisal of Dell*, 2016 WL 3186538, at *6 (Del. Ch. May 31, 2016), *aff'd in part, rev'd in part sub nom. Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd.*, 177 A.3d 1 (Del. 2017)).

395 *Id.* at 12.

396 *Id.* at 23.

397 *Compare* Shaich Tr. 970:14–21; 971:20–973:3, *with id.* 978:8–979:18; *accord* Bell. Tr. 1147:11–1148:8.

398 *Compare* Shaich Tr. 968:9–969:5, *with id.* 980:8–981:4, 983:7–984:13.

399 JX0019 at 18; Shaich Tr. 955:7–956:3, 958:1–19; *accord* Moreton Tr. 770:22–771:19.

400 Shaich Tr. 955:18–23; *accord* Moreton Tr. 770:22–771:19.

401 Shaich Tr. 956:14–957:7.

402 JX0019 at 2; *accord* JX0022 at 3–4 (Goldman's November 4, 2015 board presentation confirming the board's decision to remain a standalone company due to the broader market trends).

403 *See* JX0110; JX0118; JX0772 at 56.

404 JX0125 at 4; Moreton Tr. 795:10–796:17.

405 Shaich Tr. 976:11–23.

406 *Id.*

407 *Id.* 975:15–24; Moreton Tr. 798:23–799:10.

408 Shaich Tr. 976:24–977:6; *accord* JX0318; JX0334.

409 JX0399 at 1–2.

410 *Id.*

411 *Id.* at 1.

412 JX0625 at 4; JX0631 at 23. The companies that Petitioners cite as potential buyers were identified by Morgan Stanley and passed over because of fit or limitations. *See* JX0631 at 23–24; JX0625 at 4.

413 *See* JX0625 at 4.

414 *Id.*

415 JX0631 at 23; *accord* Kwak Tr. 1226:21–1227:12.

416 Shaich Tr. 974:11–22, 975:23–976:10, 1019:18–1020:5; *accord* JX0625 at 4 ("There were conversations with Starbucks last year, they ultimately declined to proceed citing that Panera was trading too richly (and it has since only traded up)."); JX0772 at 56; Moreton Tr. 798:23–799:10.

417 Shaich Tr. 1020:6–9; JX0631 at 23.

418 *See* JX0631 at 23.

419 Moreton Tr. 811:19–812:17 ("[T]here was nobody else out there talking to [the board] about potentially acquiring [the Company], nor did [the board] think there would be."); *see also id.* 912:7–11 ("[T]here was nobody else to reach out to ... [w]e went through the process."). Market analysts confirmed this conclusion after the Bloomberg leak: "[W]e believe Starbucks is the only one with any real (even slight) probability. We also note that JAB might be interested, given its acquisitions of Krispy Kreme, Einstein/Noah, Keurig, Caribou, and Peet's Coffee. ... All-in, we suspect JAB would be the more likely suitor than Starbucks, as we believe a newly minted CEO and a relatively sizable acquisition would increase Starbucks' risk profile." JX0609 at 12–13.

420 JX0625 at 4.

421 Moreton Tr. 824:3–12.

422 JX0625 at 4 ("Since the leak yesterday, no one has come forward to express an interest.").

423 D.I. 140 at 17.

424 *Barkan v. Amsted Indus., Inc.*, 567 A.2d 1279, 1287 (Del. 1989).

425 *In re OPENLANE, Inc. S'holders Litig.*, 2011 WL 4599662, at *5 (Del. Ch. Sept. 30, 2011).

426 Petitioners point to Morgan Stanley's label of "Potential Interlopers" in claiming that Panera should have contacted additional potential bidders. As explained herein, the preponderance of the evidence shows that Panera contacted all logical buyers. Morgan Stanley's label, which they later changed to "Potentially Interested Parties," does not disturb this result. *Compare* JX0552 at 14–15*, with* JX0631 at 23–24; *accord* Kwak Tr. 1237:11–20. And even if the use of the term "interlopers" signaled a fear of intruders, as explained herein, Morgan Stanley advised the board to negotiate for less restrictive deal terms, enabling another interested party to bid.

427 D.I. 139 at 20, 48.

428 *See* JX0116; JX0122 at 1; JX0125 at 4; *accord* Moreton Tr. 794:8–795:13, 796:3–8.

429 *See* JX0338; Shaich Tr. 977:17–978:7; *accord* Moreton Tr. 803:7–11 ("Did any of the directors know about Mr. Shaich's discussions with JAB before the March 1st board meeting? A. Certainly, I did. I believe Domenic did, and perhaps Tom [Lynch] did.").

430 *See* JX0287 at 9; *accord* Shaich Tr. 980:11–981:4.

431 JX0408 at 3–4; *accord* Moreton Tr. 802:17–803:11. Moreton described Shaich's "typical way of communicating [as] concentric circles, first with [him], and then Domenic [Colasacco], our lead director, and Tom Lynch, and then the board as a whole." Moreton Tr. 794:2–7. Shaich testified about this procedure, and explained that on an unspecified date he informed the board that he used Goldman to reach out to JAB. *See* Shaich Tr. 1048:2–23. Shaich had followed this same pattern in the Starbucks negotiations. When Schultz proposed a collaboration with Panera on July 31, 2016, Shaich informed Moreton, Lynch, and Colasacco that evening, and informed the board two days later on August 2. *See* JX0118; JX0116; JX0122 at 1; JX0125 at 4; *accord* Moreton Tr. 793:14–795:13.

432 JX0408; Shaich Tr. 983:7–984:13.

433 JX0421 at 1; Bell Tr. 1109:17–1111:8.

434 Stephen M. Bainbridge, *Mergers and Acquisitions* 56 (2d ed. 2009) (citing 8 *Del. C.* § 251(b)); *accord* 8 *Del. C.* § 141 ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors ....").

435 *Jarden*, 2019 WL 3244085, at *24 (footnote omitted).

436 *Id.* at *9, *24.

437 *Id.* at *24.

438 *Id.* at *25.

439 JX0408 at 3–4 (Shaich reported, "while no offer had been made during those discussions, Olivier Goudet, Chief Executive Officer of JAB, and David Bell, Head of M&A of JAB, indicated that JAB had internally discussed the potential for a transaction with the Company and JAB was considering making an offer to buy the Company"); *accord* Shaich Tr. 977:23–978:7.

440 JX0408 at 4.

441 PTO ¶ 134.

442 JX0421 at 1–2.

443 PTO ¶ 134.

444 *Id.* ¶ 77.

445 *Id.* ¶¶ 134–135; JX0466 at 2.

446 PTO ¶ 137.

447 JX0455, JX2019; Kwak Tr. 1206:15–1207:6, 1208:6–1209:9; Moreton Tr. 821:7–14, 821:15–822:8; Shaich Tr. 996:15–1000:11.

448 PTO ¶ 140;

449 *Id.* ¶¶ 140–41; *see* JX0448 at 1.

450 *See* JX0448 at 1.

451 Shaich Tr. 1004:14–18.

[452] PTO ¶ 141; JX0448 at 1.

[453] *See* JX0494 at 1; JX0491; JX0490; JX0519.

[454] *See* JX0491.

[455] JX0494 at 1; *accord* JX0490.

[456] PTO ¶ 160.

[457] *Id.* ¶ 163.

[458] *Id.* ¶ 164; JX0608; JX0629.

[459] PTO ¶ 165; JX0631.

[460] JX0628 at 3.

[461] PTO ¶ 167.

[462] *Id.*; JX0630 at 2.

[463] Bainbridge, *supra* note 434, at 56.

[464] *See* Kwak Tr. 1214:18–1215:14 ("I don't remember that we suggested that [the board] not offer a number. But ... as an advisor, we certainly were not in a position to make any recommendations of a number at that time because we had not completed our valuation analysis.").

[465] *See supra* Section II(C)(3)(d).

[466] PTO ¶ 136. Moreton explained that "significantly higher" would "convey that [the board] had to get the best price that we could, and that we thought that they had to go over their ceiling. And we thought that when they had a chance to go through and do the diligence on the company, that they would be able to do that." Moreton Tr. 823:14–824:2. In rejecting JAB's initial offer, Shaich explained, "[i]n order for our Board to get fully comfortable with and supportive of a transaction, your value will need to reflect a price 'that begins with a 3' ... [a]lthough I am not suggesting you need to be deeply in the $300s, I am also not talking about $300.00 either." JX2019 at 2.

[467] PTO ¶140; *accord* Shaich Tr. 1002:9–23; JX0483.

[468] PTO ¶ 141; JX0448 at 1.

[469] PTO ¶ 151.

[470] *See* JX0552 at 3, 6.

[471] PTO ¶ 153; JX0545; JX0552.

[472] *See* JX0552.

[473] PTO ¶¶ 161, 165.

[474] *Id.* ¶ 164; JX0608; JX0629; Moreton Tr. 831:22–832:5.

[475] *See* JX0628 at 2.

[476] JX0625 at 3–4.

[477] JX0628 at 2; *accord* Moreton Tr. 843:14–845:3.

[478] Moreton Tr. 843:14–845:3.

[479] PTO ¶¶ 167, 171; JX0630 at 1; JX0647.

[480] JX0628 at 3.

[481] PTO ¶ 167; JX0628 at 3 (stating that after conferring as a board, "[t]he directors expressed their strong support for the proposed transaction, noting particularly that the price was fair for the Company's shareholders and that the deal protection mechanisms in the Merger Agreement were not preclusive to an alternative proposal for the Company's shares"); JX0630 at 2.

[482] JX2019 at 2.

[483] *Compare* JX0118, *and* Shaich Tr. 969:6–10, *with* JX0318 at 1, *and* JX0435, *and* JX0491, *and* Shaich Tr. 1000:12–23; 1004:19–1005:7.

[484] Shaich Tr. 1000:15–23, 1004:19–1005:13.

[485] *Id.* 969:6–16; *accord id.* 957:8–24.

[486] JX0581 (stating JAB is "not interested in a protracted negotiation that results in significant management distraction, so they always go very quickly").

[487] Moreton Tr. 827:17–24.

488 Colasacco Dep. 142:11–25; *see also id.* 143:6–9 ("[A] short period, a yea or nay period on whether [JAB] would ... have an actual interest in signing an agreement was a positive.").

489 JX0418 at 2.

490 Kwak Tr. 1197:16–1198:7.

491 Redpath Tr. 658:1–11.

492 JX0491.

493 Moreton Tr. 827:17–24; *accord* Kwak Tr. 1233:14–20.

494 JX0593 at 65.

495 PTO ¶ 161.

496 *Id.* ¶¶ 132, 161; JX0789 at 71–75, 79–81; *see also* JX0772 at 97–101, 106–107.

497 PTO ¶¶ 160–61.

498 Kwak Tr. 1241:10–15.

499 *Id.* 1240:14–21, 1241:16–24.

500 JX0990 at 39.

501 Kwak Tr. 1241:16–22 ("Q. And there were also matching rights in the merger agreement here. In Morgan Stanley's view, did matching rights prevent other bidders from coming forward? A. It doesn't prevent. It may discourage in a way and make it more challenging, but it doesn't prevent other bidders from coming forward.").

502 *Dollar Thrifty*, 14 A.3d at 614.

503 *See* Shaich Tr. 1077:11–1079:14.

504 Petitioners present a secondary contention that Shaich was apathetic on price because he focused on closing a deal so that he could liquidate and diversify his assets. There is no evidence in the record that he wished to liquidate. Redpath Tr. 645:12–646:11 (identifying no evidence of Shaich's intent to liquidate his Panera assets); Shaich Tr. 1022:20–1023:1 ("I hadn't diversified in 36 years. Why was I going to start now?"). For this reason, I focus my analysis on the potential conflict from Shaich's desire to step away from Panera.

505 *Aruba*, 210 A.3d at 141–42.

506 *See* *Stillwater*, 2019 WL 3943851, at *32–34 (citing *Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc.*, 2018 WL 922139, at *7–8 (Del. Ch. Feb. 15, 2018), *reargument denied*, 2018 WL 2315943 (Del. Ch. May 21, 2018), *judgment entered* (Del. Ch. 2018), *rev'd and remanded*, 210 A.3d 128 (Del. 2019)).

507 *Id.* at *32.

508 *Chen v. Howard-Anderson*, 87 A.3d 648, 670–71 (Del. Ch. 2014) (quoting *Dollar Thrifty*, 14 A.3d at 600); *see also* *Merion Capital*, 2016 WL 7324170, at *22 (noting the CEO in "particular had an incentive to maximize the value of his shares, because he planned to retire.").

509 *Blueblade Capital Opportunities LLC v. Norcraft Cos., Inc.*, 2018 WL 3602940, at *25 (Del. Ch. July 27, 2018), *judgment entered*, (Del. Ch. Aug. 8, 2018).

510 *Id.*

511 Shaich Tr. 1017:23–1018:10.

512 Bell Tr. 1109:17–1111:8; Shaich Tr. 1023:10–13; Hurst Tr. 1349:14–1350:10.

513 JX0777 at 2.

514 JX0435; *accord* Moreton Tr. 822:9–823:1.

515 JX2019 at 2.

516 JX0582 at 1.

517 Shaich Tr. 1024:7–1025:14.

518 *See, e.g.*, Moreton Tr. 856:11–857:15 ("Mr. Shaich went to bed thinking about Panera and how to make it better and woke up thinking about Panera and how to make it better. He had the shareholders' interests in mind at all times."); Shaich Tr. 1021:10–1022:19 ("This was my life, and I very much wanted to maximize the value for that, and I very much wanted to do something that served all the constituencies of our company. In particular, our shareholders, who had hung with me through some tough times, and I wanted to deliver for them.").

519 JX0657.

520 *Id.*

521 *Stillwater*, 2019 WL 3943851, at *34.

522 As I determined above, although Shaich passed along JAB's suggestion that the board should choose either Barclays or Morgan Stanley, the board's legal advisor recommended Michael Boublik of Morgan Stanley, and the board followed that recommendation. *See* JX0466 at 2. Boublik did not have preexisting relationships with JAB. JAB did not select Panera's financial advisors.

523 PTO ¶ 137.

524 Moreton Tr. 816:11–21.

525 Even Petitioners' process expert conceded that Morgan Stanley cleared conflicts. Redpath Tr. 673:16–674:1.

526 JX0448 at 1.

527 JX0562; Kwak Tr. 1222:7–16; *accord* Moreton Tr. 833:21–834:1 ("[Q.] Was this the first time that the board was learning that Morgan Stanley had previous engagements with JAB? A. No. The board knew about it immediately, as we did, so this was just more formal.").

528 Moreton Tr. 816:22–817:7; *see also* Kwak Tr. 1197:6–1197:10 (testifying that "because [Morgan Stanley] had team members that [were] familiar with [JAB's] strategy, we were able to, very quickly, have discussions with Ron Shaich and Bill Moreton and to educate them on JAB's practices in the past").

529 *Jarden*, 2019 WL 3244085, at *15 n.194.

530 *Smurfit-Stone*, 2011 WL 2028076, at *23 (citing *In re Atheros Commc'ns, Inc.*, 2011 WL 864928, at *8 (Del. Ch. Mar. 4, 2011); *In re Toys 'R' Us, Inc., S'holder Litig.*, 877 A.2d 975, 1005 (Del. Ch. 2005)).

531 *Atheros*, 2011 WL 864928, at *8.

532 JX0789 at 52–53.

533 JX0594 at 1; Kwak Tr. 1190:15–17.

534 JX0631 at 19, 38; Kwak Tr. 1280:22–1281:5.

535 JX0562 at 3.

536 Kwak Tr. 1195:1–16, 1293:3–12, 1294:24–1295:2.

537 *Id.* 1293:3–12.

538 *See* JX2021.

539 Moreton Tr. 837:9–838:9; *accord* JX0582 at 1 ("[O]ur goal is to have [Ciagne] deliver a message that (i) suggests our very strong confidence in [the] business and (ii) points to our valuation expectations, directionally.").

540 Shaich Tr. 1068:21–1070:1; Moreton Tr. 905:7–908:11.

541 Moreton Tr. 837:23–838:9 ("The purpose was not for this individual, who I never met, to negotiate. It was simply for one more message to Olivier that the price has to be over $300 and they have to do the best that they can. So we were pulling every lever we could think of to try to get the price increase.").

542 Bell Tr. 1107:24–1108:17.

543 Kwak Tr. 1197:16–1198:7.

544 JX0455 at 13–23.

545 *Id.* at 5, 13–23.

546 Kwak Tr. 1196:22–1197:10 (attributing Morgan Stanley's insights into the JAB playbook to Gallagher, who was a JAB coverage team member), 1206:15–1207:6; *accord* JX0431 at 1; JX0432.

547 PTO ¶ 138; JX0455.

548 Kwak Tr. 1202:5–1203:9.

549 Shaich Tr. 997:6–998:3.

550 Moreton Tr. 821:15–822:8.

551 *See* Shaich Tr. 996:10–997:5.

552 JX0456 at 2. At trial, Shaich explained how Boublik "pushed [him] at some critical times when there was a question to push for more price, and to push against JAB for more price." Shaich Tr. 995:18–996:6; *see also id.* 1003:11–21 ("He pushed me intensely. I mean, you know, there's this question, you don't want to blow this up. On the other hand, you want to push for as much as you can get, X plus 1. And Michael and I went

through, and we went through their precedent history, and I think the sense was it was a wise, all considered, smart bet to push this deal further, even though this was already a very attractive offer for the company.").

553 JX0455 at 15.

554 *Id.* at 17.

555 *Id.*

556 *Id.* at 18.

557 *Id.* at 21.

558 *Id.* at 5.

559 Kwak Tr. 1200:4–17 (sharing Morgan Stanley's perspective with the board that "it wasn't likely that the potentially interested parties that we had, considering at that time their strategic rationale and a potential combination with Panera, and ... their ability to pay an all-cash offer ... [were] going to be likely to compete with a transaction that JAB had put forth"); Shaich Tr. 1021:13–16 ("[I]t was just patently clear to me that, knowing what I know, and knowing these people and where this had played out, that there really wasn't a viable interested party.").

560 JX0491; *accord* JX0490.

561 Kwak Tr. 1199:9–24; *see also id.* 1228:18–1229:5.

562 *See* Redpath Tr. 663:10–664:22.

563 *See generally* JX0983.

564 Kwak Tr. 1226:21–1227:12; Shaich Tr. 1019:18–1020:5.

565 Shaich Tr. 951:21–952:2.

566 *See* JX0407 at 1, 46–205; JX0408 at 2–3.

567 *See* JX0631.

568 *Id.* at 15–20.

569 *Id.* at 19.

570 *Stillwater*, 2019 WL 3943851, at *30.

571 8 *Del. C.* § 262(h) ("[T]he Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation ....").

572 *Aruba*, 210 A.3d at 133 (quoting *Union Ill. 1995 Inv. Ltd. P'ship v. Union Fin. Grp., Ltd.*, 847 A.2d 340, 356 (Del. Ch. 2004)).

573 *Id.* (citing *Solera*, 2018 WL 3625644, at *1; *Highfields Capital, Ltd. v. AXA Fin., Inc.*, 939 A.2d 34, 60–64 (Del. Ch. 2007); *Union Ill.*, 847 A.2d at 355–56).

574 *Id.* (citing *Solera*, 2018 WL 3625644, at *1; *Highfields Capital*, 939 A.2d at 59–61; *Union Ill.*, 847 A.2d at 343); *see also* *DFC*, 172 A.3d at 368 (recognizing that a "going concern" valuation requires the court to excise "any value that might be attributable to expected synergies by a buyer, including that share of synergy gains left with the seller as a part of compensating it for yielding control of the company").

575 Shaich Tr. 956:4–957:7; Moreton Tr. 824:3–12; Kwak Tr. 1200:18–1201:14.

576 *See* JX0400 at 3–4.

577 *Id.* at 4.

578 *Id.* at 3–4.

579 *Huff Fund Inv. P'ship v. CKx, Inc.*, 2014 WL 2042797, at *2 (Del. Ch. May 19, 2014), *judgment entered,* (Del. Ch. June 17, 2014), *aff'd,* 2015 WL 631586 (Del. Feb. 12, 2015) (TABLE); *see also* *Petsmart*, 2017 WL 2303599, at *31 n.364 (recognizing "synergies financial buyers may have with target firms arising from other companies in their portfolio").

580 JX0400 at 32.

581 *Id.*

582 *Id.*

583 *Id.*

584 *See id.* at 43–44.

585 *Id.* at 32, 34, 37.

586 *Id.* at 43.

587 JX0554 at 15 ("Cost rationalization and synergies. JAB's plans to achieve cost synergies and working capital improvements could fail to materialize .... Mitigating factors: JAB has a long-track record of successful acquisitions and integration, and have delivered expected cost savings on recent deals including Keurig Green Mountain and Krispy Kreme."); JX0589 at 19 ("Working Capital—Panera currently has ~ 4 days payable compared to Keurig at ~50, Caribou at >90, and Peet's at ~ 85."); *accord* Bell Tr. 1121:13–1122:10, 1123:3–23; Hubbard Tr. 1495:8–19.

588 JX0982 at 51; *accord* Hubbard Tr. 1666:5–13.

589 JX0400 at 37.

590 *Id.*; JX0589 at 23.

591 *See* JX0593 at 49–50.

592 JX0593 at 49–50, 52–54, 78; JX0982 at 49–50; Bell Tr. 1131:12–22. Shaked agreed with the public company cost savings. *See* Shaked Tr. 368:4–16.

593 JX0593 at 49.

594 Bell Tr. 1133:9–18.

595 *See* JX0593 at 65.

596 Bell Tr. 1106:21–1107:23.

597 Hubbard Tr. 1493:24–1494:7.

598 *See* JX0593 at 69.

599 JX0982 at 41.

600 *Id.* at 54; Hubbard Tr. 1493:24–1494:7.

601 Petitioners' expert testified "the company elected not to" increase its days payable outstanding. Shaked Tr. 451:2–8.

602 2014 WL 2042797, at *3. The Court explained it was not "reaching the theoretical question of under what circumstances cost-savings may constitute synergies excludable from going-concern value under Section 262(h)." *Id.*

603 Hurst Dep. 219:4–23 ("[T]he general philosophy had been pay quickly, use that as leverage in some of the vendor relationships to actually get a lower price. But it ultimately became just the habit of Panera."); *accord* Shaked Tr. 451:21–452:13.

604 JX0984 at 42 ("Panera invested over $120 million in IT from mid-2014 through mid-2017.").

605 JX0400 at 37.

606 *See* JX0607 at 181–85.

607 *See id.* at 185.

608 *See* JX0593 at 78.

609 Bell Tr. 1122:4–1123:23; *cf.* JX0904 at 1.

610 Hurst Dep. at 203:8–24 (internal quotation marks omitted).

611 *See* JX0593 at 48.

612 PTO ¶ 76.

613 D.I. 139 at 58.

614 JX0593 at 77 ("The company had $332.0 million of net debt in December 2016."); JX0238 at 16.

615 JX0982 at 55.

616 *Id.* at 55–56.

617 *Solera*, 2018 WL 3625644, at *28 & n.364.

618 *Id.* at *28 & n.364.

619 *Jarden*, 2019 WL 3244085, at *1 ("The appraisal exercise is, at bottom, a fact-finding exercise, and our courts must appreciate that, by functional imperative, the evidence, including expert evidence, in one appraisal case will be different from the evidence presented in any other appraisal case."); *accord* *Stillwater*, 2019 WL 3943851, at *20 ("[T]he approach that an expert espouses may have met 'the approval of this court on prior occasions,' but may be rejected in a later case if not presented persuasively or if 'the relevant professional

community has mined additional data and pondered the reliability of past practice and come, by a healthy weight of reasoned opinion, to believe that a different practice should become the norm ....' " (quoting *Golden Telecom Trial*, 993 A.2d at 517)).

[620] Petitioners argue that the Court should not agree with Hubbard's analysis because he "ignores the negative synergies, or costs, that resulted from the acquisition." D.I. 140 at 81. Petitioners have not shown that JAB failed to consider these costs when JAB evaluated their implementation of their playbook, calculated Panera's resulting value, or formed their offer price. I do not find that this undermines Hubbard's synergy analysis.

[621] Bell Tr. 1127:13–21.

[622] *See* JX0400 at 38–41. Possible plans included leveraging Panera's technology platform across JAB's portfolio, enhancing Panera's in-store coffee program, focusing on CPG, increasing K-cup sales, and expanding internationally. *Id.* at 32.

[623] *See* JX0564 at 131, 141–152, 154–158.

[624] *See* JX0593 at 57–62. Although JAB had developed a "coffee procurement savings program," they did not include these synergies in the post-diligence model. *Id.* at 60–61; *accord* Bell Tr. 1123:3–1126:19, 1129:2–24.

[625] *See* JX0593 at 65.

[626] *See* JX0607 at 145, 155–169, 171–175, 229.

[627] *See* Bell Tr. 1135:1–10 ("Q. And when you went higher, to 315, did those strategic opportunities or synergies play a role in the decision to raise your offer from 305 to 315? A. I would say they did, because, you know, again, as a long-term holder, we ended up for this one going to a price that was below ... a return. That we priced into a return that was below what we initially thought we would have to do. But we took a big leap of faith on these strategic opportunities, which we didn't quantify in the model.").

[628] *Id.* 1129:5–24.

[629] *Id.* 1132:5–21; 1134:19–1135:10.

[630] *Id.* 1168:8–21 ("Q. Coffee procurement, was that one of the ones that was on the back of the envelope? A. I don't even think it was that, because we hadn't done the analysis.").

[631] *See* JX0982 at 55–56; *accord* Hubbard Tr. 1593:17–1594:3, 1694:22–1695:8.

[632] Hubbard Tr. 1482:18–24, 1663:6–14, 1664:20–24, 1665:24–1666:4.

[633] *Manichaean Capital, LLC v. SourceHOV*, C.A. No. 2017-0673-JRS, at 54 (Del. Ch. Jan. 30, 2020).

[634] D.I. 154 at 117:21–120:13 ("We never asked him to adjust his opinion. ... And, you know, frankly, Your Honor, that's a trial strategy decision that I made, right? These are the sort of things that we do. And I still think that we have a strong record evidence for this $10.").

[635] JX0593 at 64.

[636] Neither party argues in favor of the unaffected stock price.

[637] *Pinson*, 1989 WL 17438, at *8 n.11. "The DCF model entails three basic components: an estimation of net cash flows that the firm will generate and when, over some period; a terminal or residual value equal to the future value, as of the end of the projection period, of the firm's cash flows beyond the projection period; and finally a cost of capital with which to discount to a present value both the projected net cash flows and the estimated terminal or residual value." *Cede & Co. v. Technicolor, Inc.*, 1990 WL 161084, at *7 (Del. Ch. Oct. 19, 1990).

[638] *Stillwater*, 2019 WL 3943851, at *60 (citing *Dell*, 177 A.3d at 37–38, and *DFC*, 172 A.3d at 369–370, 369 n.118).

[639] *Id.* at *61 (quoting *Union Ill.*, 847 A.2d at 359).

[640] JX0982 at 84.

[641] As explained, Hubbard did not accept Respondent's post-trial market value of $293.44.

[642] Shaked Tr. 179:12–181:12, 239:24–241:17.

[643] Hubbard Tr. 1483:15–1584:11.

[644] Shaked Tr. 203:9–19 (explaining the reason for the buffer as a hypothetical: "let's assume that in my terminal year, the maintenance will be 259, not 143. This is 81 percent increase compared to what it used to be.

Last year is 143, and I assume that it will be 259. So I build in $116 million, kind of an extra slack for the maintenance").

645 JX0982 at 95–96.

646 D.I. 141 at 67 (citing Hubbard Tr. 1536:22–1537:7).

647 *Id.* (citing JX0982 at 14–20; Goldin Tr. 1409:22–1411:24).

648 *See id.* at 68 (citing Hubbard Tr. 1546:17–1547:6; 1687:7–19).

649 JX0982 at 96.

650 *Id.*

651 *See* D.I. 141 at 63.

652 Shaked Direct Demonstrative Deck at 148 ("Assumed Panera will be using 2/3 of its net income to pay out dividends and/or repurchase shares, and will have 1/3 of it flow to retained earnings (grow book value of equity)."); *see* Hubbard Tr. 1571:21–1572:18.

653 Hubbard Tr. 1571:21–1572:18.

654 *See id.* 1570:9–1571:15.

655 *See* Shaked Tr. 1699:14–1742:7.

656 *See id.* 486:5–18.

657 *See* Hubbard Tr. 1536:3–21.

658 *Id.* 1572:19–1574:6.

659 Shaked Tr. 311:11–312:8.

660 *See* *Dell*, 177 A.3d at 37–38; *DFC*, 172 A.3d at 369–370, 369 n.118.

661 *See* *Solera*, 2018 WL 3625644, at *29 (citing *Union Ill.*, 847 A.2d at 359); *id.* at *32.

662 *Jarden*, 2019 WL 3244085, at *32.

663 *Id.* at *33.

664 *Hoyd v. Trussway Hldgs., LLC*, 2019 WL 994048, at *5 (Del. Ch. Feb. 28, 2019).

665 *See* *Merion Capital, L.P. v. 3M Cogent, Inc.*, 2013 WL 3793896, at *5 (Del. Ch. July 8, 2013) ("[W]hen the 'comparables' involve companies that offer different products or services, are at a different stage in their growth cycle, or have vastly different multiples, a comparable companies or comparable transactions analysis is inappropriate.").

666 JX0982 at 115.

667 Hubbard Dep. 360:5–361:23.

668 JX0982 at 12–13, 120–21.

669 *Id.* at 123.

670 Shaked Tr. 439:23–440:18.

671 *Compare* JX0983 at 150–51, *with* JX0554 at 44, *and* JX0589 at 39, *and* JX0826 at 37.

672 *See* Shaked Tr. 441:9–14, 439:16–22.

673 JX0983 at 59–61.

674 *Jarden*, 2019 WL 3244085, at *34.

675 *See* JX0982 at 121–22; JX1023; JX0983 at 59–60.

676 JX0982 at 121.

677 *See id.* at 123.

678 *See id.*

679 Hubbard Tr. 1481:13–23.

680 JX0983 at 59.

681 *Id.* at 59–60.

682 Shaked Tr. 255:4–17; *see also id.* 180:24–181:12.

683 Kwak Tr. 1210:8–1211:6.

684 *See generally* Charles K. Korsmo & Minor Myers, *Interest in Appraisal*, 42 J. Corp. L. 109 (2016); R. Garrett Rice, *Give Me Back My Money: A Proposed Amendment to Delaware's Prepayment System in Statutory Appraisal Cases*, 73 Bus. Law 1051 (2018); Abigail Pickering Bomba et al., *Proposed Appraisal Statute*

Amendments Would Permit Companies To Reduce Their Interest Cost—Likely To Discourage "Weaker" Appraisal Claims And Make Settlement Of "Stronger Claims" Harder, Fried Frank M&A Briefing (Mar. 23, 2015), https://www.friedfrank.com/siteFiles/Publications/FINAL% 20-% 203-23-2015% 20-% 20Proposed% 20Appraisal% 20Statute% 20Amendments.pdf; Arthur R. Bookout et al., *Delaware Appraisal Actions: When Does It Make Sense to Prepay?*, Skadden, Arps, Slate, Meagher & Flom LLP (May 29, 2018), https://www.skadden.com/insights/publications/2018/05/insights-the-delaware-edition/delaware-appraisal-actions.

[685] 8 *Del. C.* § 262(h).

[686] Del. H.B. 371, 148th Gen. Assem., 80 Del. Laws, ch. 265, §§ 8–11 (2016).

[687] 8 *Del. C.* § 262(h).

[688] *E.g.*, *Artic Invs. LLC v. Medivation, Inc.*, C.A. No. 2017-0009-JRS, D.I. 20 at 5 (Del. Ch. Mar. 6, 2016) (stipulating for clawback rights if the prepayment amount were to exceed the Court's fair value determination of the appraisal shares along with any accrued interest); *see* Rice, *supra* note 684, at 1082 (recognizing that petitioners sometimes stipulate to clawbacks).

[689] *Ala. By-Prods. Corp. v. Cede & Co. ex rel. Shearson Lehman Bros.*, 657 A.2d 254, 258 (Del. 1995) (citation and internal quotations omitted).

[690] *One-Pie Invs., LLC v. Jackson*, 43 A.3d 911, 914 (Del. 2012) (quoting *LeVan v. Indep. Mall, Inc.*, 940 A.2d 929, 932 (Del. 2007)).

[691] *Giuricich v. Emtrol Corp.*, 449 A.2d 232, 238 (Del. 1982).

[692] *Goldstein v. Mun. Court for City of Wilm.*, 1991 WL 53830, at *5 (Del. Super. Jan. 7, 1991) (citing *State v. Rose*, 132 A. 864, 867 (Del. Super. 1926)).

[693] *Giuricich*, 449 A.2d at 238.

[694] *Terex Corp. v. S. Track & Pump, Inc.*, 117 A.3d 537, 544 (Del. 2015), *as revised* (June 16, 2015).

[695] *Huff Fund Inv. P'ship v. CKx, Inc.*, 2014 WL 545958, at *3 (Del. Ch. Feb. 12, 2014).

[696] Model Bus. Corp. Act § 13.24(a) (2016).

[697] *Compare* Del. H.B. 160, 144th Gen. Assem., 76 Del. Laws, ch. 145 §§ 13, 16 (2007), *and* 8 *Del. C.* § 262(h), *with* Model Bus. Corp. Act § 13.01 (adopting the legal rate as the applicable interest rate for dissenting stockholders).

[698] *See* Model Bus. Corp. Act § 13.30(e); *see also* Rice, *supra* note 684, at 184–86; Mary Siegel, *An Appraisal of the Model Business Corporation Act's Appraisal Rights Provisions*, 74 Law & Contemp. Probs. 231, 236 (2011) ("[I]f the corporation's estimate of fair value is greater than the amount ultimately determined by the court, the corporation will have paid this greater amount to the shareholder without any statutory right to require the shareholder to return the difference between the court's determination of fair value and the corporation's estimate of fair value." (footnote omitted)).

[699] *See* Korsmo & Meyers, *supra* note 864, at 125; Bookout et al., *supra* note 864.

[700] In *Artic Investments LLC v. Medication, Inc.*, the company argued under an unjust enrichment theory that the Court should find the corporation entitled to a refund for overpayment after trial. *See* C.A. No. 2017-0009-JRS, D.I. 15 at 24 (Del. Ch. Mar. 28, 2017). The Court did not resolve this issue, or grant the party's proposed stipulation for a clawback provision, before the parties stipulated to dismissal. *See id.* D.I. 23 (Del. Ch. Mar. 6, 2018).

[701] *Meade v. Pac. Gamble Robinson Co.*, 58 A.2d 415, 417–18 (Del. 1948).

[702] *See* *Huff*, 2014 WL 545958 at *3.

[703] *See* 47 Del. Laws ch. 136, § 7 (1949) (affording the Court the power to award interest); Del. H.B. 371, 148th Gen. Assem., 80 Del. Laws, ch. 265, §§ 8–11 (2016) (creating the possibility of prepayment).

[704] "[T]he expression of dictum is ordinarily to be avoided." *State ex rel. Smith v. Carey*, 112 A.2d 26, 28 (Del. 1955). Accordingly, I note only that refraining from awarding a refund here does not offend my sensibilities. A refund is not available under the Model Act, which tethers the mandatory prepayment amount to the corporation's position on fair value, and therefore gives the prepayment amount significance in the litigation context. Under the DGCL, prepayment is optional, and a corporation can pay any amount it chooses without making a commitment to fair value. Prepayment under the DGCL is a business decision, made with

knowledge of the company's sale process that is superior to the stockholder's, and with counsel's prediction of how long the litigation may take and how much interest may accrue. In my view, expressed in dictum, the case for a refund under the DGCL is less compelling than under the Model Act, which does not provide for one.

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UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

IN RE APPRAISAL OF SOLERA HOLDINGS, INC.

CONSOLIDATED C.A. No. 12080-CB
|
Date Submitted: April 6, 2018
|
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MEMORANDUM OPINION

BOUCHARD, C.

***1** In this appraisal action, the court must determine the fair value of petitioners' shares of Solera Holdings, Inc. as of March 3, 2016, when Vista Equity Partners acquired Solera for $55.85 per share, or approximately $3.85 billion in total equity value, in a merger transaction. Unsurprisingly, the parties have widely divergent views on this question.

Relying solely on a discounted cash flow analysis, petitioners contend that the fair value of their shares is $84.65 per share —approximately 51.6% over the deal price. Until recently, respondent consistently argued that the "best evidence" of the fair value of Solera shares is the deal price less estimated synergies, equating to $53.95 per share. After an appraisal decision in another case recently used the "unaffected market price" of a company's stock to determine fair value, however, respondent changed its position to argue for the same measure of value here, which respondent contends is $36.39 per share —about 35% below the deal price.

Over the past year, our Supreme Court twice has heavily endorsed the application of market efficiency principles in appraisal actions. With that guidance in mind, and after carefully considering all relevant factors, my independent determination is that the fair value of petitioners' shares is the deal price less estimated synergies—*i.e.*, $53.95 per share.

As discussed below, the record reflects that Solera was sold in an open process that, although not perfect, was characterized by many objective indicia of reliability. The merger was the product of a two-month outreach to large private equity firms followed by a six-week auction conducted by an independent and fully authorized special committee of the board, which contacted eleven financial and seven strategic firms. Public disclosures made clear to the market that the company was for sale. The special committee had competent legal and financial advisors and the power to say no to an underpriced bid, which it did twice, without the safety net of another bid. The merger price of $55.85 proved to be a market-clearing price through a 28-day go-shop that the special committee secured as a condition of the deal with Vista, one which afforded favorable terms to allow a key strategic competitor of Solera to continue to bid for the company.

The record further suggests that the sales process was conducted against the backdrop of an efficient and well-functioning market for Solera's stock. Before the merger, for example, Solera had a deep base of public stockholders, its shares were actively traded on the New York Stock Exchange and were covered by numerous analysts, and its debt was closely monitored by ratings agencies.

In short, the sales process delivered for Solera stockholders the value obtainable in a *bona fide* arm's-length transaction and provides the most reliable evidence of fair value. Accordingly, I give the deal price, after adjusting for synergies in accordance with longstanding precedent, sole and dispositive weight in determining the fair value of petitioners' shares as of the date of the merger.

I. BACKGROUND

***2** The facts recited in this opinion are my findings based on the testimony and documentary evidence submitted during a five-day trial. The record includes over 400 stipulations of fact in the Stipulated Joint Pre-Trial Order ("PTO"),[1] over 1,000 trial exhibits, including fourteen deposition transcripts, and the live testimony of four fact witnesses and three expert witnesses. I accord the evidence the weight and credibility I find it deserves.

A. The Parties

Respondent Solera Holdings, Inc. ("Solera" or the "Company") is a Delaware corporation with headquarters in Westlake, Texas.[2] Solera was founded in 2005 and was publicly traded on the New York Stock Exchange from May 2007 until March 3, 2016, when it was acquired by an affiliate of Vista Equity Partners ("Vista") in a merger transaction (the "Merger").[3]

From Solera's inception through the Merger, Tony Aquila served as Chairman of the Board of Directors (the "Board"), Chief Executive Officer, and President of Solera.[4] Over this time period, Aquila made all top-level decisions about product innovation, corporate marketing, and investor relation efforts.[5] After the Merger, Aquila remained the CEO of Solera.[6]

Petitioners consist of seven funds that were stockholders of Solera at the time of the Merger: Muirfield Value Partners LP, Fir Tree Value Master Fund, L.P., Fir Tree Capital Opportunity Master Fund, L.P., BlueMountain Credit Alternatives Master Fund L.P., BlueMountain Summit Trading L.P., BlueMountain Foinaven Master Fund L.P., and BlueMountain Logan Opportunities Master Fund L.P. Petitioners collectively hold 3,987,021 shares of Solera common stock that are eligible for appraisal.[7]

B. Solera's Business

In early 2005, Aquila founded Solera with aspirations to bring about a digital evolution of the insurance industry, starting with the processing of automotive insurance claims.[8] Aquila viewed Solera as a potential disruptor, akin to Amazon.com, Inc., in its specific industry.[9]

Solera, in its current form, is a global leader in data and software for automotive, home ownership, and digital identity management.[10] At the time of the Merger, Solera's business consisted of three main platforms: (i) Risk Management Solutions; (ii) Service, Maintenance, and Repair; and (iii) Customer Retention Management.[11] The Risk Management Solutions platform helps insurers digitize and streamline the claims process with respect to automotive and property content claims.[12] The Service, Maintenance, and Repair platform digitally assists car technicians and auto service centers to diagnose and repair vehicles efficiently, accurately, and profitably, and to identify and source original equipment manufacturer and aftermarket automotive parts.[13] The Customer Retention Management platform provides consumer-centric and data-driven digital marketing solutions for businesses that serve the auto ownership lifecycle, including property and casualty insurers, vehicle manufacturers, car dealerships, and financing providers.[14] Solera was operating in 78 countries at the time of the Merger.[15]

C. Solera Expands Aggressively Through Acquisitions

***3** Solera's business was not always so diverse. During the Company's early years, the vast majority of Solera's revenues was derived from claims processing.[16] But the claims business was facing pressure[17] as a result of maturation,[18] advances in automotive technology like collision avoidance and self-driving cars,[19] and competition.[20]

In August 2012, Aquila implemented a plan called "Mission 2020" to increase Solera's revenue and EBITDA through acquisitions and diversification.[21] Solera aspired to become a "cognitive data and software and services company" that would address the entire lifecycle of a car.[22]

The Mission 2020 goals included growing revenue from $790 million in fiscal year 2012 to $2 billion by fiscal year 2020, and increasing adjusted EBITDA from $345 million to $800 million over that same period.[23] To meet these benchmarks, Solera implemented its "Leverage. Diversify. Disrupt." ("LDD") business strategy.[24]

LDD was a three-pronged strategy. First, Solera sought to "leverage" its claims processing revenue in a given geographic area to gain a foothold in that area. Second, Solera sought to "diversify" its service offerings in the given geographic area. Third, Solera's longer-term objective was to "disrupt" the market by integrating its service offerings such that vehicle owners and homeowners could use Solera's software to manage their purchases, maintenance, and insurance claims all in one place.[25]

D. The Market's Reaction to LDD

Between the formulation of Mission 2020 and the Merger, Solera invested approximately $2.1 billion in acquisitions.[26] These acquisitions often were "scarcity value transactions" that involved Solera paying a premium for unique assets.[27] The multiples Solera paid in these acquisitions not only were relatively high but were increasing over time, generating lower returns on invested capital.[28] As a result, Solera's leverage increased while its EPS essentially remained flat and its EBITDA margins shrank.[29]

Some analysts were skeptical of Solera's evolution-through-acquisitions strategy, taking a "show me" approach to the Company.[30] These analysts struggled to understand Solera's diversification plan[31] and complained that management's lack of transparency about the Company's strategy impeded their ability to value Solera appropriately.[32] Aquila, the Board, and other analysts believed that the market misunderstood Solera's value proposition and that its stock traded at a substantial discount to fair value.[33]

Compounding the challenges Solera was facing in the equity markets, Solera was encountering difficulties in the debt markets. Solera needed to have access to debt financing to execute its acquisition strategy, but by the time of the Merger, Solera was unable to find lenders willing to finance its deals due to its highly-levered balance sheet. For example, upon the announcement that Solera planned to issue tack-on notes in November 2014, "the proceeds of which, along with balance sheet cash, [were] expected to effect a strategic acquisition," Moody's Investors Service downgraded Solera's credit rating from Ba2 to Ba3.[34] Moody's noted that "the company has been actively pursuing acquisitions, often at very high purchase multiples," and warned that "[r]atings could be downgraded [further] if the company undertakes acquisitions that, after integration, fail to realize targeted margins."[35]

***4** In late May 2015, management began discussing an $850 million notes offering with Goldman Sachs, the proceeds of which the Company planned to use to fund acquisitions and refinance outstanding debt.[36] The offering fell approximately $11.5 million short, and Goldman was forced to absorb the notes that it could not sell into the market.[37] In July 2015, Moody's downgraded Solera again,[38] commenting "[t]he ongoing, cumulative impacts of debt assumed for acquisitions and for the buyout of its joint venture partner's 50% share ... plus ramped up share buybacks and dividends, have pushed Moody's expectations for [Solera's] intermediate-term leverage to approximately 7.0 times, a level high even for a B1-rated credit."[39] As Aquila testified, Solera was "out of runway" shortly before the Merger to execute the rest of its acquisition strategy because creditors were unwilling to loan funds to Solera at tolerable interest rates.[40]

E. Aquila Expresses Displeasure with his Compensation at Solera

Solera's stock price affected Aquila personally. His compensation was tied to "total shareholder return," and the majority of his stock options were underwater.[41] Aquila did not receive a performance bonus in 2011, 2012, or 2013.[42] In February 2015, he emailed Thomas Dattilo, Chair of the Compensation Committee, saying "I've poured a great deal of time, inventions and sacrifice during this time in the company's transition and I really need to get something meaningful for it."[43] At one point, Aquila threatened to leave Solera if his compensation was not reconfigured.[44]

The Board recognized Aquila's value to the Company and took his request and threat to leave seriously. Dattilo commented "the way [S]olera is structured, we would probably need three people to replace him, and even that would not really fulfill the Solera requirements because of the pervasive founder[']s culture found there. ... Solera possibly couldn't exist without Tony."[45] Although the Compensation Committee was looking for a solution to address Aquila's underwater stock options, they ultimately "didn't get it done."[46]

F. Aquila Privately Explores a Sale of Solera

Around the time that Aquila complained to the Board about his compensation, he began to engage in informal discussions with private equity firms regarding a potential transaction to take the Company private. In December 2014, Aquila was introduced to David Baron, an investment banker at Rothschild Inc. ("Rothschild").[47] Aquila and Baron met again in January 2015, when they "talked through a bunch of buy-side ideas" and Aquila expressed his frustration at the disconnect between Solera's stock price performance relative to its peers and his own views on the Company's growth opportunities.[48]

In March 2015, Aquila was introduced to Orlando Bravo, a founder of the private equity firm Thoma Bravo LLC ("Thoma Bravo"), and Robert Smith, the founder of Vista.[49] Before these two meetings, Aquila was aware that both Thoma Bravo and Vista recently had launched new multi-billion dollar funds.[50]

On April 29, 2015, Baron contacted Brett Watson, the head of Koch Equity, to tell him, without identifying Solera as the target, about an opportunity to invest in preferred equity.[51] Baron wrote in an email to Watson: "I'd like you to speak for as much of pref[erred stock] as possible – Ceo objective is to try to get control back[.] I'm going to clear it w[ith] chairman/ceo next week."[52]

***5** On May 4, 2015, Baron travelled to Aquila's ranch in Jackson Hole, Wyoming, bringing with him a presentation book that included leverage buyout ("LBO") analyses that the two had previously discussed.[53] Two days later, during an earnings call on May 6, Aquila raised the possibility of taking Solera private as a means of returning money to its stockholders while still pursuing its growth strategy:

> Q (Analyst): And just if I can bring that around to [the Solera CFO's] comment about being opportunistic in share repurchases when you think the stock is detached from intrinsic value, you haven't bought a lot of stock. So how do we square that circle in terms of what you think the Company is worth today?
>
> A (Aquila): Look, you're bringing up a great point. So, look, it is a chicken-or-egg story. We're going to make some of you happy, which we're trying to go down—we're trying to keep the ball down the middle of the fairway. We definitely like to hit the long ball as much as we can. But in reality, we have to do what we're doing, and we have to thread the needle the way we are. Our only other alternative is either to take up leverage, buy stock right now. That's going to cause a ratings issue. That's going to cause some dislocation. We want to buy content because we want double-digit businesses in the emerging content world as apps take a different role on your phone to manage your risks and your asset. So when you think of that, we've done a decent job. We bought, I don't know, $300 million worth of stock back since we did the stock buying program, and our average price is, like, $52, $53.
>
> So we're kind of dealing with all the factors—we got the short game playing out there. And we've got to thread the needle. ***And the only other option to that is to go private and take all the shares out***.[54]

Aquila testified that this comment was "not preplanned," and he was not "trying to suggest that [going private] was a decision that had been made."[55]

A few days later, on May 11, 2015, Aquila met with Smith from Vista and his partner Christian Sowul in Austin, Texas.[56] After the meeting, Sowul followed up with Baron, saying "we are very interested. [T]ony sounded like now is the time. [N]ext 4-6 weeks."[57]

Also on May 11, the Board commenced a series of meetings and dinners in Dallas, Texas.[58] Before these meetings, Aquila discussed with every Board member the possibility of pursuing strategic alternatives, given that Solera was "out of runway" to execute its growth-by-acquisition strategy.[59] Company director Stuart Yarbrough encouraged Aquila to have these conversations with the other directors, and explained that the Board felt Solera was "being criticized in the market" and knew that the Company was paying higher multiples for larger acquisitions.[60]

On May 12, 2015, Company director Michael Lehman emailed Yarbrough and Larry Sonsini of the law firm Wilson Sonsini Goodrich & Rosati about the possibility of retaining his firm to assist in reviewing strategic alternatives. Lehman stated in the email: "Tony and the board have just begun conversations about 'evaluating strategic alternatives,' " of which "[o]ne of the more attractive conceptual alternatives is a 'going private,' which would likely mean that the CEO would have significant stake in that entity [ ] (think Dell computer type transaction)."[61]

***6** In an executive session on May 13, the Board unanimously agreed that Aquila should "test the waters" with financial sponsors.[62] In doing so, the Board recognized that Aquila would probably have a significant equity stake in a private Solera, posing an "inherent" conflict in his outreach to private equity firms.[63] The Board authorized Aquila to "put together a target list" of large private equity firms and to "go have discussions and see what the interest was."[64] The Board decided to start with private equity firms and add strategic firms later in the process because it believed that strategic firms presented a greater risk of leaks[65] and an interested strategic bidder could get up to speed quickly.[66] The Board also wanted to focus on larger private equity firms to avoid the complexity of firms having to partner with each other.[67] At this stage, the Board prohibited "any use of nonpublic information."[68]

G. A Special Committee is Formed after Aquila "Tests the Waters"

Between May 13 and June 1, 2015, Aquila, with assistance from Rothschild, contacted nine private equity firms: Pamplona, Silver Lake, Apax, Access Industries, Hellman & Friedman, Vista, Blackstone, CVC Capital Partners, and Thoma Bravo.[69] Aquila and Rothschild had follow-up contact with at least Silver Lake,[70] Blackstone,[71] and Thoma Bravo[72] between June 1 and July 14, 2015. After his meeting with Aquila, Orlando Bravo emailed Baron, saying "Unreal meeting. I love Tony man. We want to do this deal."[73] On July 18, 2015, Aquila reported back to the Board that Thoma Bravo was going to make an offer for Solera.[74]

On July 19, 2015, Thoma Bravo submitted an indication of interest to purchase Solera at a price between $56-$58 per share. In the letter submitting their bid, Thoma Bravo stated that they "are contemplating this deal solely in the context of being able to partner with Tony Aquila and his management team."[75]

On July 20, 2015, the Board discussed the indication of interest received from Thoma Bravo and formed a special committee of independent directors to review the Company's strategic alternatives (the "Special Committee").[76] The Special Committee consisted of Yarbrough (Chairman), Dattilo, and Patrick Campbell, each of whom had served on multiple boards and had extensive M & A experience.[77] The Special Committee was granted the "full power and authority of the Board" to review, evaluate, negotiate, recommend, or reject any proposed transaction or strategic alternatives.[78] The Board resolution establishing the Special Committee further provided that "the Board shall not recommend a Possible Transaction or alternative thereto for approval by the Company's stockholders or otherwise approve a Possible Transaction or alternative thereto without a prior favorable recommendation of such Possible Transaction or alternative thereto by the Special Committee."[79]

H. The Special Committee Begins its Work

On July 30, 2015, the Special Committee met with its legal advisors, Sullivan & Cromwell LLP and Richards, Layton & Finger P.A., and financial advisor Centerview Partners LLC ("Centerview").[80] Rothschild remained active in the sales process and was formally engaged to represent the Company,[81] but, in reality, it also continued to represent Aquila personally.[82]

***7** At its July 30 meeting, the Special Committee approved a list of potential buyers to approach, including six strategic companies that were selected based on their business initiatives and stated future plans, and six financial sponsors (including Vista) that were selected based on their experience and interest in the technology and information services industry and their capability to execute and finance a transaction of this size.[83] The Special Committee also distributed to management a short document that Sullivan & Cromwell prepared concerning senior management contacts with prospective bidders, which, aptly for a company focused on the automotive industry, was referred to as the "Rules of the Road."[84] The document stated, among other things, that "senior management must treat potential Bidders equally" and refrain from "any discussions with any Bidder representatives relating to any future compensation, retention or investment arrangements, without approval by the independent directors."[85]

Between July 30 and August 4, 2015, Centerview contacted 11 private equity firms and 6 potential strategic bidders, including Google and Yahoo!, the two that Special Committee Chair Yarbrough believed were most likely to bid.[86] Aquila already had "tested the waters" with some of the private equity firms that the Special Committee contacted. All six strategic firms contacted declined to explore a transaction involving Solera.[87] At this time, the Special Committee did not contact IHS Inc. ("IHS"), another possible strategic acquirer, because IHS was one of Solera's key competitors and the Special Committee had "a low level of confidence" in IHS's ability to finance a transaction.[88]

From time to time, Aquila, through Rothschild and his legal counsel, Kirkland & Ellis LLP,[89] apprised the Special Committee on his thoughts about the sales process. On July 30, 2015, Baron told the Special Committee's legal and financial advisors in an email that Aquila did not want IHS included in the sales process, stating "fishing expedition, too competitive, need 50% stock ..."[90]

On August 3, 2015, Aquila's counsel sent the Special Committee a proposed "Management Retention Program."[91] This proposal stated that "an incremental $75 million cash retention pool" should be created to align management and shareholder incentives, and to "enhance impartiality of management among all potential buyers."[92] The proposal warned that under the current compensation plan, "the program inadequately aligns management's interests with those of stockholders and exposes the Company to risks of losing key managers through closing" of a transaction.[93] Solera did not implement this proposed "Management Retention Program," but the Compensation Committee did award Aquila a $15 million bonus in August 2015.[94]

I. The Special Committee Solicits First-Round Bids and News of the Sales Process Leaks

By August 11, 2015, Yarbrough viewed "the state of the world to be one where if there's going to be a deal, it's going to be with a private equity firm."[95] On August 10, 2015, at the direction of the Special Committee, Centerview sent a letter to the five remaining parties inviting them to submit first-round bids by August 17, 2015.[96] These parties had signed confidentiality agreements and were provided Board-approved five-year projections for the Company, which were based on projections created in the normal course of business but then modified in connection with the sales process (the "Hybrid Case Projections").[97] Before the August 17 bid deadline, Baron spoke to certain potential bidders directly without involving Centerview.[98]

***8** By August 17, 2015, two potential bidders had dropped out of the sales process, believing "that they would not be able to submit competitive bids."[99] The remaining three financial sponsors provided indications of interest: Vista offered $63 per share, Thoma Bravo offered $60 per share, and Pamplona offered $60-$62 per share.[100] Each made clear that they wanted Aquila's participation in the deal.[101]

On August 19, 2015, news of the sales process leaked when Bloomberg reported that Solera was "exploring a sale that has attracted interest from private equity firms."[102] The next day, the Company issued a press release announcing that it had formed the Special Committee and that it was contemplating a sale.[103] Also on August 20, the Financial Times reported that Vista was "considering a bid of $63 per share" and that Thoma Bravo and Pamplona were "considering separate bids for $62 per share."[104]

In a further development on August 20, Advent International Corporation, a private equity firm, reached out to Centerview and Rothschild separately to express interest in the Company.[105] Centerview confirmed to Baron that it planned to ignore the inquiry,[106] about which the members of the Special Committee were never informed.[107] The Special Committee also was not made aware of interest that Providence Equity Partners, L.L.C.,[108] another private equity firm, expressed to Centerview on August 26.[109] When Centerview made Baron aware of this inquiry, he responded: "Too late obv[iously] but Tony not a fan ..."[110] Neither Advent nor Providence gave any indication as to the price they would be willing to pay for Solera or the amount of time they would need to get up to speed.[111]

During the August 22-23, 2015 weekend, Smith traveled to Aquila's ranch en route to his own ranch in Colorado.[112] Before the meeting, Smith's team at Vista researched the size of the option pools that Vista had offered management in its "recent take privates" so that Smith would "know the comps before his meeting with [T]ony."[113] Aquila did not have authorization from the Special Committee to discuss his post-transaction compensation at this time.[114] Shortly after the meeting, Vista began to model a 9% option pool with a 1% long-term incentive plan (LTIP), up from the 5% option pool with a 1% LTIP that Vista had modeled before Aquila's meeting with Smith.[115]

J. IHS Expresses Interest in a Potential Transaction

On August 21, 2015, IHS contacted Centerview to express its interest in a potential acquisition of Solera at an unspecified valuation and financing structure.[116] By August 23, IHS suggested that it would be able to submit a bid in excess of $63 per share, and it indicated that it could complete due diligence and execute definitive transaction documents within ten calendar days despite not yet having received nonpublic information.[117] The parties entered into a confidentiality agreement on August 24.[118]

***9** On August 26, 2015, senior representatives of IHS, including its CFO, attended a meeting with the Company's management, before which Aquila had a one-on-one conversation with IHS's CFO for 90 minutes.[119] Centerview requested numerous times that IHS's CEO Jerre Stead attend the management meeting, but he declined even though the acquisition would have been the largest in IHS's history.[120] By August 27, Solera had provided IHS with non-public Company information, including the Hybrid Case Projections.[121]

On September 1, IHS submitted a bid of $55-$58 per share, comprised of 75% cash and 25% stock, and included "highly confident" letters from financing sources.[122] On September 2, Aquila travelled separately to meet with Stead personally, who commented that IHS was "looking at another big deal as well."[123] The next day, IHS submitted a revised bid of $60 per share, but did not specify the mix of consideration and did not include any indication of financing commitments.[124] IHS said it could complete diligence "within a matter of days."[125]

K. The Special Committee Negotiates with Potential Buyers

On September 4, 2015, Vista and Thoma Bravo submitted revised bids.[126] Pamplona had dropped out of the sales process by this point,[127] and the Special Committee felt like it was "moving backwards" in its negotiations with IHS.[128]

Both of the active bidders lowered their offers. Thoma Bravo lowered its bid to $56 per share, attributing the drop to "challenges in availability and terms of financing (both debt and equity) due in part to turbulence in global financial markets."[129] Vista lowered its bid to $55 per share, but subsequently indicated that it could increase its price to $56 per share.[130] Vista explained that it dropped its bid because of changes to Solera's balance sheet, increased financing costs, and a decline in Vista's forecasted EBITDA for Solera.[131] Unbeknownst to Solera, one of the reasons Vista lowered its bid is that it had made a spreadsheet error in its financial model before submitting its first-round bid, resulting in the model overstating Solera's future equity value by approximately $1.9 billion.[132] If this error had been noticed and corrected, Vista's first-round bid would have been closer to $55 per share, rather than $63 per share.[133]

On September 5, 2015, Aquila signaled that he was willing to roll over $15 million of his Solera shares in a transaction with any bidder.[134] That day, the Special Committee met[135] and decided to press for more from the bidders, proposing to Vista that it either raise its price to $58 per share, or agree to a go-shop and reduced termination fee to enable Solera to continue discussions with IHS.[136] Vista agreed to the go-shop and the termination fee reduction on September 7, but also told Centerview that day that one of its anticipated sources of equity financing had withdrawn its commitment and that it would need additional time to obtain replacement financing to support its bid.[137]

***10** On September 8, Vista lowered its bid to $53 per share.[138] Vista told Solera that its bid would expire at midnight, and that "[a]fter midnight, we will not be spending any more time on" Solera.[139] The Special Committee rejected Vista's bid as inadequate that same day,[140] and decided "to let the process play out."[141] The Special Committee set September 11, 2015 as a deadline for Vista and Thoma Bravo to make final bids.[142] On September 9, Bloomberg reported that Solera had received bids from Vista and Thoma Bravo, and that the Company was "nearing a deal to sell itself for about $53 a share."[143]

When September 11 arrived, Thoma Bravo offered $54 per share, expiring at midnight and contingent on Solera "shutting off dividends" and reducing advisory fees.[144] The Special Committee said "no."[145] The press again reported in real time, with Reuters writing that Vista and Thoma Bravo had "made offers that failed to meet Solera's valuation expectations," and that Solera was "trying to sell itself to another company"—IHS—"rather than an investment firm."[146]

The next morning, on September 12, Vista submitted an all-cash, fully financed revised bid of $55.85 per share that also included the go-shop and termination fee provisions the Special Committee had requested.[147] The Special Committee tried to push Vista up to $56 per share, but

Vista refused, saying $55.85 was its best and final offer.[148] Centerview opined that $55.85 per share was fair, from a financial point of view, to Solera stockholders.[149] Later in the day on September 12, the Special Committee accepted Vista's offer after receiving Centerview's fairness opinion, and the Board approved the transaction.[150] On September 13, the Company and Vista entered into a definitive merger agreement (the "Merger Agreement").[151]

L. The Go-Shop Period Expires and the Merger Closes

On September 13, 2015, Solera announced the proposed Merger.[152] The press release stated that the purchase price valued Solera at approximately $6.5 billion, including net debt, "represent[ing] an unaffected premium of 53% over Solera's closing share price of $36.39 on August 3, 2015."[153]

In advance of the press release, Baron sent a celebratory email to his colleagues, in which he noted "we were the architects with the CEO from the beginning as to how to engineer the process from start to finish."[154] The next morning, an internal email of the Fir Tree petitioners praised the transaction as yielding a "Good price!"[155]

The Merger Agreement provided for a 28-day go-shop period during which the termination fee would be 1% of the equity value for any offer made by IHS, a reduction from the 3% termination fee applicable to any other potential buyer.[156] The Special Committee reached out to IHS the day after signing the Merger Agreement and gave IHS nearly full access to the approximately 12,000-document data room that the private equity firms had been given access to during the pre-signing sales process.[157]

***11** On September 29, 2015, with two weeks left in the go-shop, IHS informed Solera that it would not pursue an acquisition of the Company. IHS noted that it "was appreciative of the go-shop provisions negotiated in the merger agreement ... and the fact that [Solera] had provided equal access to information in order for IHS to consider a bid."[158] On October 5, 2015, Solera issued its preliminary proxy statement, which disclosed a summary of the Hybrid Case Projections.[159] The go-shop expired on October 11, without Solera receiving any alternative proposals.[160]

On October 15, 2015, Vista sent Aquila a proposed compensation package, offering Aquila the opportunity to obtain up to 6% of Solera's fully-diluted equity.[161] This amount was later revised up, with Vista offering Aquila up to 10% of the fully-diluted equity. Under the revised plan, Aquila would invest $45 million in the deal—$15 million worth of his shares of Solera and $30 million borrowed from Vista.[162] Vista's proposal positioned Aquila to earn up to $969.6 million over a seven-year period if Vista achieved a four-times cash-on-cash return.[163]

On October 30, 2015, Solera issued its definitive proxy statement concerning the proposed Merger, which also included a summary of the Hybrid Case Projections.[164] On December 8, Solera's stockholders voted to approve the Merger. Of the Company's outstanding shares, approximately 65.4% voted in favor, approximately 10.9% voted against, and approximately 3.4% abstained.[165] The Merger closed on March 3, 2016.[166] The next day, Aquila signed a new employment agreement with Solera.[167]

II. PROCEDURAL POSTURE

On March 7 and March 10, 2016, petitioners filed their petitions for appraisal. The court consolidated the petitions on March 30, 2016. A five-day trial was held in June 2017, and post-trial argument was held on December 4, 2017.

At the conclusion of the post-trial argument, the court asked the parties to confer to see if they could agree on an expert the court might appoint to opine on a significant issue of disagreement concerning the methods the parties' experts used to determine the terminal period investment rate in their discounted cash flow analyses. On December 19, 2017, the parties advised the court that they were unable to reach agreement on a suggested expert and each submitted two candidates for the court's consideration.

On February 22, 2018, Solera filed a motion requesting the opportunity to submit supplemental briefs to address the implications of certain appraisal decisions issued after the post-trial argument. The court granted this motion on February 26, 2018, noting in its order that it had "made no decision about whether to proceed with an independent expert" and would "revisit the issue after reviewing the supplemental submissions."[168] Supplemental briefing was completed on April 6, 2018.[169]

III. ANALYSIS

A. Legal Standard

Petitioners request appraisal of their shares of Solera under 8 *Del. C.* § 262. "An action seeking appraisal is intended to provide shareholders who dissent from a merger, on the basis of the inadequacy of the offering price, with a judicial determination of the fair value of their shares."[170] Respondent has not disputed petitioners' eligibility for an appraisal of their shares.

***12** In an appraisal action, the court has a statutory mandate to:

> [D]etermine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors.[171]

Appraisal excludes any value resulting from the merger, including synergies that may arise,[172] because "[t]he basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him, viz., his proportionate interest in a going concern."[173] In valuing a company as a "going concern" at the time of a merger, the court must take into consideration the "operative reality"[174] of the company, viewing the company as "occupying a particular market position in the light of future prospects."[175] A dissenting stockholder is then entitled to his proportionate interest in the going concern.[176]

In using "all relevant factors" to determine fair value, the court has significant discretion to use the valuation methods it deems appropriate, including the parties' proposed valuation frameworks, or one of the court's own fashioning.[177] This court has relied on a number of different approaches to determine fair value, including comparable company and precedent transaction analyses, a discounted cash flow model, and the merger price.[178] "This Court may not adopt at the outset an 'either-or' approach, thereby accepting uncritically the valuation of one party, as it is the Court's duty to determine the core issue of fair value on the appraisal date."[179] "In an appraisal proceeding, the burden to establish fair value by a preponderance of the evidence rests on both the petitioner and the respondent."[180]

B. *DFC*, *Dell*, and Recent Court of Chancery Appraisal Decisions

***13** Over the past year, the Delaware Supreme Court has issued two decisions providing important guidance for the Court of Chancery in appraisal proceedings: *DFC Global Corporation v. Muirfield Value Partners, L.P.*[181] and *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*[182] Given their importance, a brief discussion of each case is appropriate at the outset.

In *DFC*, petitioners sought appraisal of shares they held in a publicly traded payday lending firm, DFC, that was purchased by a private equity firm.[183] This court attempted to determine the fair value of DFC's shares by equally weighting three measures of value: a discounted cash flow model, a comparable company analysis, and the transaction price.[184] The court gave equal weight to these three measures of value because it found that each similarly suffered from limitations arising from the tumultuous regulatory environment that was swirling around DFC during the period leading up to its sale.[185] The court's analysis resulted in a fair value of DFC at approximately 8% above the transaction price.[186]

The Delaware Supreme Court reversed and remanded to the trial court.[187] Based on its own review of the trial record, the Supreme Court held that the Court of Chancery's decision to afford only one-third weight to the transaction price was "not rationally supported by the record,"[188] explaining:

> Although there is no presumption in favor of the deal price ... economic principles suggest that the best evidence of fair value was the deal price, as it resulted from an

> open process, informed by robust public information, and easy access to deeper, non-public information, in which many parties with an incentive to make a profit had a chance to bid.[189]

The Supreme Court further explained that the purpose of appraisal "is not to make sure that the petitioners get the highest conceivable value," but rather "to make sure that they receive fair compensation for their shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction."[190]

***14** According to the Supreme Court, "[m]arket prices are typically viewed superior to other valuation techniques because, unlike, e.g., a single person's discounted cash flow model, the market price should distill the collective judgment of the many based on all the publicly available information about a given company and the value of its shares."[191] The "collective judgment of the many" may include that of "equity analysts, equity buyers, debt analysts, [and] debt providers."[192] The Supreme Court cautioned that "[t]his, of course, is not to say that the market price is always right, but that one should have little confidence she can be the special one able to outwit the larger universe of equally avid capitalists with an incentive to reap rewards by buying the asset if it is too cheaply priced."[193]

Several months after deciding *DFC*, the Supreme Court reiterated the same appraisal thesis in *Dell,* where the trial court had reached a determination of fair value at approximately 28% above the transaction price.[194] In *Dell*, the Supreme Court found that the Court of Chancery erred by relying completely on a discounted cash flow analysis and affording zero weight to market data, *i.e.*, the stock price and the deal price, because "the evidence suggests that the market for Dell's shares was actually efficient and, therefore, likely a possible proxy for fair value."[195] With respect to the company's stock price, the Supreme Court explained:

> Dell's stock traded on the NASDAQ under the ticker symbol DELL. The Company's market capitalization of more than $20 billion ranked it in the top third of the S & P 500. Dell had a deep public float and was actively traded as more than 5% of Dell's shares were traded each week. The stock had a bid-ask spread of approximately 0.08%. It was also widely covered by equity analysts, and its share price quickly reflected the market's view on breaking developments.[196]

The Supreme Court thus held that "the record does not adequately support the Court of Chancery's conclusion that the market for Dell's stock was inefficient and that a valuation gap in the Company's market trading price existed in advance of the lengthy market check, an error that contributed to the trial court's decision to disregard the deal price."[197]

With respect to the deal price, the Supreme Court said that "it is clear that Dell's sale process bore many of the same objective indicia of reliability" as the one in *DFC*, which "included that 'every logical buyer' was canvassed, and all but the buyer refused to pursue the company when given the opportunity; concerns about the company's long-term viability (and its long-term debt's placement on negative credit watch) prevented lenders from extending debt; and the company repeatedly underperformed its projections."[198] Given leaks in the press that Dell was exploring a sale, moreover, the world was put on notice of the possibility of a transaction so that "any interested parties would have approached the Company before the go-shop if serious about pursuing a deal."[199]

Dell's bankers canvassed the interest of 67 parties, including 20 possible strategic acquirers during the go-shop, and the go-shop's overall design was relatively open and flexible.[200] The special committee had the power to say "no," and it convinced the eventual buyer to raise its bid six times.[201] The Supreme Court thus found that "[n]othing in the record suggests that increased competition would have produced a better result. [The financial advisor] also reasoned that any other financial sponsor would have bid in the same ballpark as [the buyer]."[202] Significantly, the Court did not view a dearth of strategic buyer interest as negatively impacting the reliability of the deal price, explaining:

> ***15** Fair value entails at minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay. The Court of Chancery ignored an important reality: if a company is one that no strategic buyer is interested in buying, it does not suggest a higher value, but a lower one.[203]

In sum, the Supreme Court held that "[o]verall, the weight of evidence shows that Dell's deal price has heavy, if not overriding, probative value."[204] It summarized its decision as follows:

> In so holding, we are not saying that the market is always the best indicator of value, or that it should always be granted some weight. We only note that, when the evidence of market efficiency, fair play, low barriers to entry, outreach to all logical buyers, and the chance for any topping bidder to have the support of Mr. Dell's own votes is so compelling, then failure to give the resulting price heavy weight because the trial judge believes there was mispricing missed by all the Dell stockholders, analysts, and potential buyers abuses even the wide discretion afforded the Court of Chancery in these difficult cases.[205]

Shortly after *Dell* was decided, the Court of Chancery rendered appraisal decisions in *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*[206] and *In re Appraisal of AOL Inc.*[207]

In *Aruba*, the court observed that the Supreme Court's decisions in *DFC* and *Dell* "endorse using the deal price in a third-party, arm's-length transaction as evidence of fair value" and "caution against relying on discounted cash flow analyses prepared by adversarial experts when reliable market indicators are available."[208] The court further observed that *DFC* and *Dell* "recognize that a deal price may include synergies, and they endorse deriving an indication of fair value by deducting synergies from the deal price."[209] Rather than hold that the deal price less synergies represented fair value, however, the *Aruba* court determined that fair value was "the unaffected market price" of petitioners' shares, which was more than 30% below the transaction price.[210] The court identified "two major shortcomings" of its "deal-price-less-synergies figure" that supported this conclusion and explained its rationale for using the "unaffected market price" as follows:

> First, my deal-price-less-synergies figure is likely tainted by human error. Estimating synergies requires exercises of human judgment analogous to those involved in crafting a discounted cash flow valuation. The Delaware Supreme Court's preference for market indications over discounted cash flow valuations counsels in favor of preferring market indications over the similarly judgment-laden exercise of backing out synergies.
>
> Second, my deal-price-less-synergies figure continues to incorporate an element of value derived from the merger itself: the value that the acquirer creates by reducing agency costs. A buyer's willingness to pay a premium over the market price of a widely held firm reflects not only the value of anticipated synergies but also the value created by reducing agency costs. The petitioners are not entitled to share in either element of value, because both arise from the accomplishment or expectation of the merger. The synergy deduction compensates for the one element of value arising from the merger, but a further downward adjustment would be necessary to address the other.
>
> ***16** Fortunately for a trial judge, once Delaware law has embraced a traditional formulation of the efficient capital markets hypothesis, the unaffected market price provides a direct route to the same endpoint, at least for a company that is widely traded and lacks a controlling stockholder. Adjusting down from the deal price reaches, indirectly, the result that the market price already provides.[211]

In *AOL*, the court similarly construed *DFC* and *Dell* to mean that where "transaction price represents an unhindered, informed, and competitive market valuation, the trial judge must give particular and serious consideration to transaction price as evidence of fair value" and that where "a transaction price is used to determine fair value, synergies transferred to the sellers must be deducted."[212] In doing so, the court coined the phrase "Dell Compliant" to mean a transaction "where (i) information was sufficiently disseminated to potential bidders, so that (ii) an informed sale could take place, (iii) without undue impediments imposed by the deal structure itself."[213] The court found that the sales process did not satisfy this standard and ultimately determined the fair value of petitioners' shares based on its own discounted cash flow analysis ($48.70 per share), which was about 2.6% less than the deal price ($50 per share).[214]

C. The Parties' Contentions

Petitioners contend that the fair value of their shares is $84.65 per share—approximately 51.6% over the deal price. Their sole support for this valuation is a discounted cash flow model prepared by their expert, Bradford Cornell, Visiting Professor of Financial Economics at the California Institute of Technology.[215] Cornell also performed a multiples-based comparable company analysis "as a reasonableness check" but gave it no weight in his valuation.[216]

Respondent's expert was Glenn Hubbard, the Dean and Russell L. Carson Professor in Finance and Economics at the Graduate School of Business of Columbia University, as well as Professor of Economics at Columbia University. He concluded that the "best evidence of Solera's value is the market-generated Merger price [$55.85], adjusted for synergies [$1.90] to $53.95."[217] Hubbard also conducted a valuation based on a discounted cash flow model, which resulted in a valuation of $53.15 per share, but found the methodology to be less reliable in this instance.[218] Hubbard further considered, as a "check," Solera's historical valuation multiples, analysts' stock price targets, and valuation multiples from comparable companies and precedent transactions.[219]

This sharp divide of $31.50 per share between the experts' DCF models is the result of a number of disagreements regarding the proper inputs and methods to use in the analysis. The most significant disagreements are explained later.

***17** Throughout trial and post-trial briefing, respondent consistently maintained that the best evidence of Solera's value at the time of the Merger was the deal price minus synergies. Seizing on the *Aruba* decision, respondent changed course during supplemental briefing, arguing that "[i]n light of recent cases, the best evidence of Solera's fair value is its unaffected stock price of $36.39 per share."[220]

D. Determination of Solera's Fair Value

I now turn to my own independent determination of the fair value of Solera's shares with the guidance from *DFC* and *Dell* in mind. Those decisions teach that deal price is "the best evidence of fair value"[221] when there was an "open process,"[222] meaning that the process is characterized by "objective indicia of reliability."[223] Such "indicia" include but, consistent with the mandate of the appraisal statute to consider "all relevant factors,"[224] are not limited to:

- "[R]obust public information,"[225] comprised of the stock price of a company with "a deep base of public shareholders, and highly active trading,"[226] and the views of "equity analysts, equity buyers, debt analysts, debt providers and others."[227]

- "[E]asy access to deeper, non-public information,"[228] where there is no discrimination between potential buyers and cooperation from management helps address any information asymmetries between potential buyers.[229]

- "[M]any parties with an incentive to make a profit had a chance to bid,"[230] meaning that there was a "robust market check"[231] with "outreach to all logical buyers"[232] and a go-shop characterized by "low barriers to entry"[233] such that there is a realistic possibility of a topping bid.

- A special committee, "composed of independent, experienced directors and armed with that power to say 'no,' "[234] which is advised by competent legal and financial advisors.

- "[N]o conflicts related to the transaction,"[235] with the company purchased by a third party in an arm's length sale[236] and "no hint of self-interest."[237]

If the process was open, then "the deal price deserve[s] heavy, if not dispositive, weight."[238] This is not to say that the market is always correct: "In some cases, it may be that a single valuation metric is the most reliable evidence of fair value and that giving weight to another factor will do nothing but distort that best estimate. In other cases, it may be necessary to consider two or more factors."[239] Whichever route it takes, however, the Court of Chancery is required to "justify its methodology (or methodologies) according to the facts of the case and relevant, accepted financial principles."[240]

1. The Deal Price Less Synergies Deserves Dispositive Weight

***18** For the reasons explained below, I find that the Merger was the product of an open process that, although not perfect, has the requisite objective indicia of reliability emphasized in *DFC* and *Dell*. Thus, I conclude that the deal price, minus synergies, is the best evidence of fair value and deserves dispositive weight in this case. My consideration of the evidence supporting this conclusion follows in three parts focusing on (i) the opportunity many potential buyers had to bid, (ii) the Special Committee's role in actively negotiating an arm's-length transaction, and (iii) the evidence that the market for Solera's stock was efficient and well-functioning.

a. Many Heterogeneous Potential Buyers Had a Meaningful Opportunity to Bid

Appraisal decisions have placed weight on the deal price when the process "involved a reasonable number of participants and created credible competition" among bidders.[241] Here, Solera reached out to nine large private equity funds in May and June 2015 during the "test the waters" period.[242] Then, after Thoma Bravo submitted an indication of interest on July 19, 2015,[243] the Special Committee engaged with 18 potential bidders, 11 financial and 7 strategic firms.[244] As Hubbard testified, a "broad range of sophisticated buyers," both financial and strategic, had the chance to bid for Solera.[245] Petitioners' own expert offered no opinion "that more bidders should have been contacted."[246]

Not only were the 18 potential bidders directly contacted and aware that Solera could be acquired at the right price, but "the whole universe of potential bidders was put on notice,"[247] with increasing specificity over time, that the Company was considering strategic alternatives.[248] Aquila publicly presaged the sales process during the Company's earnings call on the May 6, 2015,[249] and the Company confirmed it had formed a Special Committee and was contemplating a sale on August 20, 2015,[250] the day after Bloomberg reported that Solera was "exploring a sale that has attracted interest from private equity firms."[251]

The press revealed not only the identities of potential buyers, but also the approximate amounts of their bids. On August 20, 2015, for example, the Financial Times reported that Vista was "considering a bid of $63 per share," with Thoma Bravo and Pamplona "considering separate bids for $62 per share."[252] On September 9, 2015, Bloomberg reported that Solera had received bids from Vista and Thoma Bravo, and that the Company was "nearing a deal to sell itself for about $53 a share."[253] Two days later, Reuters wrote that Vista and Thoma Bravo "had made offers that failed to meet Solera's valuation expectations," and that the Company was "trying to sell itself to another company"—IHS—"rather than an investment firm."[254] The visible threat of other buyers made the sales process more competitive.[255] Given these public disclosures, any potential bidder knew in essentially real time that Solera was exploring a sale and the approximate price levels of the offers.[256] Yet no one else ever seriously showed up to make a topping bid.

***19** Petitioners point out that Advent and Providence were excluded from the sales process, but whether either would have bid competitively is unknown. Notably, when Advent and Providence expressed interest to Solera's bankers, neither provided any indication as to their ability to pay or their sources of financing; rather, their introductory emails were perfunctory, suggesting to me that they were just "kicking the tires."[257] There also is no evidence that either of them followed up to express any further interest in Solera, either before or during the go-shop period.[258]

The fact that only one potential strategic bidder—IHS—made a bid does not undermine the reliability of the sales process as a price discovery tool. That six potential strategic acquirers declined to explore a transaction involving Solera shows that six sophisticated, profit-motivated actors were offered the opportunity to participate in a sales process to acquire the Company, yet none was interested enough to even sign a non-disclosure agreement.[259] As noted above, our Supreme Court forcefully made this point in *Dell*:

> The Court of Chancery stressed its view that the lack of competition from a strategic buyer lowered the relevance of the deal price. But its assessment that more bidders—both strategic and financial—should have been involved assumes there was some party interested in proceeding. Nothing in the record indicates that was the case. Fair value entails at a minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay. The Court of Chancery ignored an important reality: if a company is one that no strategic buyer is interested in buying, it does not suggest a higher value, but a lower one.[260]

The record shows, furthermore, that the mere presence in the sales process of IHS, as a strategic bidder that was one of Solera's key competitors, incentivized the financial sponsors to put forth more competitive bids.[261]

The record also reflects that the Company provided all seriously interested bidders access to deeper, non-public information after they signed non-disclosure agreements. Although the Special Committee initially excluded IHS from the process due to competitive concerns and doubts about its ability to finance a deal,[262] once news of the sales process leaked out, the Special Committee worked promptly to accommodate IHS. After IHS contacted Centerview on August 21, 2015 to express interest,[263] representatives of Solera and IHS held a management meeting by August 26,[264] and Solera provided IHS with the Hybrid Case Projections by August 27.[265] And, after IHS's CEO failed to attend the management meeting on August 26, Aquila traveled separately to meet him.[266] IHS ultimately declined to make a topping bid during the go-shop period, but it was not for lack of access to information. Solera gave IHS nearly full access to the approximately 12,000-document data room,[267] and IHS specifically commented that it "was appreciative of ... the fact that [Solera] had provided equal access to information in order for IHS to consider a bid."[268]

***20** Finally, I am not persuaded by petitioners' argument that "[t]he sale of Solera took place against the backdrop of extraordinary market volatility," such that it "was not the product of a well-functioning market."[269] According to petitioners, the court should not rely on the Merger price as evidence of fair value because there was macroeconomic volatility, "evidenced by the VIX spiking to an [sic] historic high [on August 24, 2015] and sharp declines in global equity markets,"[270] which constrained potential bidders' ability to finance and willingness to enter a deal.[271] In support of this theory, petitioners called Dr. Elaine Buckberg as an expert on market volatility.[272]

Buckberg testified that "investors are less willing to proceed with investments in the face of substantial uncertainty and volatility," and that when investors "do decide to proceed with an investment in the face of such uncertainty, they would expect to be compensated for the additional risk with a lower price."[273] In that vein, Yarbrough, the Chairman of the Special Committee, candidly acknowledged that market volatility impacted "the financing side, [it] was making it more difficult on the debt financing side, and I think it also trickled over into the equity piece, too."[274]

As an initial factual matter, it is questionable whether the level of market volatility during the sales process was as extraordinary as petitioners suggest. On August 24, 2015, the VIX closed at 40.74.[275] Although petitioners describe this as the VIX's "highest point since January 2009" and "a level exceeded only six times in the VIX's twenty-seven year history,"[276] that assertion appears to be an exaggeration. As Hubbard testified, the August 24 closing VIX has been exceeded on 157 days in the VIX's history.[277] The August 24 spike also was relatively short-lived. By August 28, just four days after closing at 40.74, the VIX had fallen back to "about 26," and had fallen further by September 11, the last trading day before the Special Committee accepted Vista's $55.85 bid.[278] Including the spike on August 24, the "average VIX was 19.4 in August 2015 and 24.4 in September, as compared to an average of 19.7 since 1990."[279]

Even accepting that market volatility impacted the sales process by increasing financing costs and decreasing the price that financial sponsors were willing to pay, petitioners' argument is unavailing in my opinion for two reasons. First, Buckberg made no attempt to quantify the impact of volatility on the Merger price.[280] Second, and more importantly, petitioners' position ignores that they are only entitled to the fair value of Solera's stock at the time of the Merger, not to the best price theoretically attainable had market conditions been the most seller-friendly.[281] As the Supreme Court pointedly explained in *DFC*:

> Capitalism is rough and ready, and the purpose of an appraisal is not to make sure that the petitioners get the highest conceivable value that might have been procured had every domino fallen out of the company's way; rather, it is to make sure that they receive fair compensation for their shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction.[282]

***21** The record demonstrates that the Merger price "resulted from an open process, informed by robust public information, and easy access to deeper, non-public information, in which many parties with an incentive to make a profit had a chance to bid."[283] Thus, consistent with our high court's recent teachings, economic principles suggest that the Merger price is what petitioners "deserve to receive" for their shares.

b. A Fully-Empowered Special Committee Actively Negotiated the Merger

Reliance on the deal price as evidence of fair value is strengthened when independent representatives of a target company actively negotiate with potential buyers and demonstrate a real willingness to reject inadequate bids.[284] Here, the record indicates that Solera's Special Committee was both competent and effective.

On July 20, 2015, the day after receiving an indication of interest from Thoma Bravo, the Board delegated to the Special Committee the "full power and authority of the Board" to review, evaluate, negotiate, recommend, or reject any proposed transaction or strategic alternative.[285] The authorizing resolution further provided that Solera could not do a deal without the Special Committee's approval.[286] All three directors on the Special Committee were independent and experienced.[287] Yarbrough, the Chairman of the Special Committee, testified knowledgeably and forthrightly at trial about the process undertaken by the Special Committee, which was aided by reputable legal and financial advisors.[288] Petitioners tellingly make no effort to impugn the motives of any of the members of the Special Committee.

The record also demonstrates that the Special Committee actively engaged with the bidders, did not favor any one in particular, and expressed a willingness to walk away from bids that it did not find satisfactory. The Special Committee *twice* rejected bids that it considered inadequate —Vista's bid at $53 per share[289] and Thoma Bravo's bid at $54 per share[290]—each time without the safety net of another offer.[291] The Special Committee's initial decision to defer inviting IHS into the sales process was reasonable, given its concerns about protecting Solera's competitively sensitive information and about IHS's ability to finance a transaction.[292] In any event, that decision became academic after news of the sales process leaked in the press, at which point the Company promptly engaged with IHS for over two weeks before signing a deal with Vista. Critically, as a condition of that deal, the Special Committee extracted the right to conduct a go-shop and for a reduced 1% termination fee for IHS (as opposed to 3% for other bidders) to facilitate continued discussions with IHS.[293] And, for reasons explained below, the negotiations with all bidders were not skewed by an artificially low stock price, since the market for Solera's stock before the Merger appears to have been efficient.[294]

***22** Finally, the evidence shows that the Special Committee made a thoughtful, reasoned decision to accept Vista's "last and final" offer at $55.85 after countering with $56 and being rejected.[295] Before the Special Committee did so, Centerview counseled the Special Committee that "[i]t is uncertain whether extending the process will result in higher and fully financed offers, or will lead to further deterioration in Vista's bid" and that the "Vista bid can act as a pricing floor while IHS is given a further opportunity to bid at a reduced termination fee pursuant to the go-shop negotiated by the Committee."[296] As Yarbrough testified, with that advice in mind, the Special Committee unanimously decided to accept Vista's offer after comparing it to the Company's stand-alone prospects:

> We then asked for Centerview to go through a presentation analysis of [Vista's bid], with the preliminary steps to their fairness opinion. And then we ultimately had a vote on it, discussed stand-alone, decided that we preferred the 55.85 and moving forward with an all-cash, riskless deal. And so we had a unanimous vote on the special committee, and then we had a board meeting shortly thereafter where Centerview again presented to the board. We made our recommendation to the board and then the board unanimously accepted the recommendation.[297]

In response to this evidence, petitioners advance essentially two arguments challenging the integrity and quality of the sales process. I address each in turn.

Petitioners' primary challenge is that Aquila's conflicts of interest tainted the sales process through meetings he (with Baron's assistance) held with private equity firms before, and on one notable occasion after, the Special Committee was formed. Although Solera's Board could have done a better job of monitoring Aquila and his interactions with potential buyers, particularly after the Special Committee was in place, those interactions did not compromise the integrity or effectiveness of the sales process in my opinion.

The reality is that Aquila's participation in a transaction was a prerequisite for a financial sponsor to do a deal. As petitioners put it, "Aquila ***is*** Solera."[298] Consistent with that reality, all of the private equity firms that later submitted bids made clear that those bids depended on Aquila continuing to lead the Company.[299] In other words, a go-private transaction never would have been a possibility without buyers becoming personally acquainted and comfortable with Aquila. Thus, Aquila engaging in one-on-one conversations with private equity firms before the Special Committee was formed had the utility of gauging interest in the Company to see if undertaking a formal sales process made sense. Critically, there is no indication in the record that any of those contacts predetermined or undermined the process when the Special Committee took charge.

That said, once the Company had received an indication of interest and put the Special Committee in place, the Special Committee should have monitored Aquila's contacts with potential bidders more carefully. Petitioners justifiably criticize Aquila's private two-hour meeting with Vista in August, shortly after which Vista began to model a larger option pool for post-Merger Solera executives.[300] Although Aquila and Sowul (a principal at Vista) both testified that compensation was not discussed during that meeting or at any time before the deal with Vista was signed[301]—and there is no direct evidence that it was—the timing is certainly suspicious and casts doubt on whether Aquila abided by the "Rules of the Road" advice the Special Committee's counsel provided, *i.e.*, to refrain from discussing post-Merger employment and compensation during the sales process.[302] If best practices had been followed, a representative of the Special Committee would have accompanied Aquila to the August meeting with Vista as a precaution.[303]

***23** Even if it is assumed that compensation discussions did occur during this meeting, nothing in the record indicates that any of Aquila's (or Baron's) actions before or during the sales process compromised or undermined the Special Committee's ability to negotiate a deal.[304] The record is devoid of any evidence, for example, that Aquila participated in price discussions with any of the bidders or influenced the outcome of a competitive sales process. Indeed, petitioners do not contend that Aquila ever discussed price with the Special Committee or any bidder, nor do they contend that he played any role in the deliberations or decision-making process of the Special Committee more generally.

Further, the record does not show that structural issues inhibited the effectiveness of the go-shop.[305] To the contrary, IHS indicated that it appreciated that the Company was transparent and facilitated its diligence. There also was a lower termination fee if IHS submitted a topping bid. In short, IHS had a realistic pathway to success,[306] but it ultimately decided not to submit a topping bid.

As a secondary matter, petitioners advance a one-paragraph argument that the Merger was a *de facto* MBO (management buyout) because the Special Committee "knew" that if Solera was to be sold, it was going to be sold to a private equity firm, and all the private equity firms made clear that they "only wanted Solera if Aquila was part of the deal."[307] Petitioners thus contend that the Merger warrants "heightened scrutiny."[308] This argument fails for essentially two reasons.

First, contrary to petitioners' characterization of the transaction, the Merger did not have the requisite characteristics of an MBO. Petitioners' own expert (Cornell) agreed that the common definition of an MBO is a transaction "where, when it was negotiated, senior management was a participant in the transaction as an acquirer," but then conceded that the Merger was not an MBO because "it was not a joint purchase between management and another party."[309] During the sales process, Aquila did not have an agreement with Vista or any other bidder to participate as a buyer in a particular transaction.[310] To the contrary, he expressed a willingness to invest $15 million in a transaction with *any* of the potential buyers, not just Vista.[311] Further, Aquila was a not an "acquirer" in the Merger[312] because, before the transaction, Aquila's holdings at the $55.85 per share were worth approximately $55 million,[313] and after the Merger, Aquila invested $45 million into the post-Merger company.[314] In short, as Cornell admitted, the Merger was not even "similar to an MBO."[315]

***24** Second, petitioners contend that MBOs should be subject to "heightened scrutiny" but fail to explain why. As the Supreme Court stated in *Dell*, even though there may be "theoretical characteristics" of an MBO that could "detract[ ] from the reliability of the deal price,"[316] the deal price that results from an MBO is not inherently suspect or unreliable *per se*.[317] Here, to repeat, the Special Committee had the full authority to control the sales process, and exercised that authority by deciding which bidders to contact, how to respond to bids, and ultimately whether to approve the Merger.

c. The Equity and Debt Markets Corroborate that the Best Evidence of Solera's Fair Value was the Merger Price

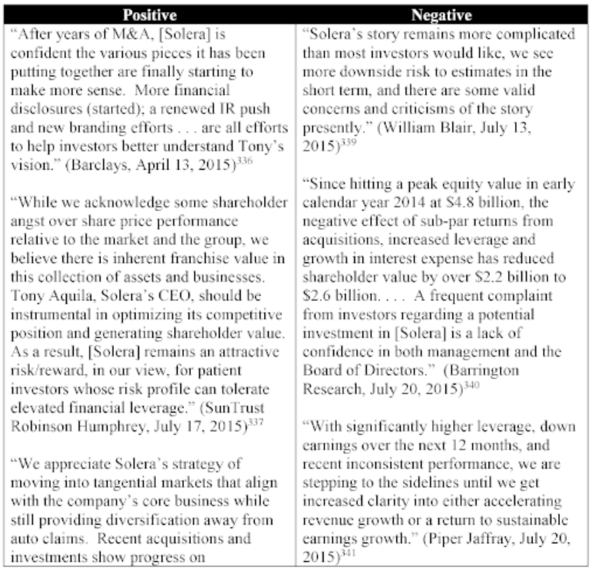
In *DFC,* the Supreme Court endorsed the economic proposition that the "price at which [a company's] shares trade is informative of fair value" in an appraisal action when "the company had no conflicts related to the transaction, a deep base of public shareholders, and highly active trading," because "that value reflects the judgments of many stockholders about the company's future prospects, based on public filings, industry information, and research conducted by equity analysts."[318] The Court in *Dell* reiterated the same point, explaining that in an efficient market "a mass of investors quickly digests all publicly available information about a company, and in trading the company's stock, recalibrates its price to reflect the market's adjusted, consensus valuation of the company."[319] My inference from *DFC* and *Dell* is that the Supreme Court has emphasized this point because the price of a widely dispersed stock traded in an efficient market may provide an informative lower bound in negotiations between parties in a potential sale of control.[320]

Here, the record supports the conclusion that the market for Solera's stock was efficient and well-functioning, since: (i) Solera's market capitalization of about $3.5 billion placed it in the middle of firms in the S & P MidCap 400 index;[321] (ii) the stock was actively traded on the New York Stock Exchange, as indicated by weekly trading volume of 4% of shares outstanding;[322] (iii) the stock had a relative bid-ask spread of approximately 0.06%, in line with a number of S & P MidCap 400 and S & P 500 companies;[323] (iv) the Company's short interest ratio indicated that, on average, investors who had sold the stock short would be able to cover their positions in about two days, which was faster than about three-quarters of S & P 400 MidCap companies and about half of S & P 500 companies;[324] (v) at least eleven equity analysts covered Solera during the year before the Merger;[325] and (vi) Solera's stock price moved sharply as rumor of the sales process leaked into the market.[326]

***25** The proxy statement for the Merger identified August 3, 2015 as the unaffected date for purposes of calculating a premium.[327] As of that date, a well-informed, liquid trading market determined, before news of a potential transaction leaked into the market, that the Company's stock was worth $36.39.[328] Significantly, research analysts' price targets had been declining in the months before news of a potential transaction, and these targets remained *below* the deal price through announcement of the Merger.[329] As Hubbard put it, the takeaway from these two objective indications of value is that "market participants playing with real money, looking at the information that they have, don't think that the stock is worth $55.85 during that period."[330]

Despite these market realities, petitioners contend that Solera was worth $84.65 per share—more than double its unaffected stock price of $36.39 per share as of August 3.[331] Although one would expect a control block to trade at a higher price than a minority block,[332] petitioners are unable to explain such a gaping disconnect between Solera's unaffected market price and the Merger price.

Petitioners argue that the pre-Merger stock price was artificially low because the market for Solera was not efficient due to asymmetric information. More specifically, petitioners contend that Solera was "poised to 'harvest returns' "[333] from acquisitions it made between 2012 and 2015, but management struggled to disclose sufficient information, due to competitive concerns, to allow the market to value the Company properly.[334] This argument ignores evidence that many equity investors and analysts actually *did* understand Solera's long-term plans, with some approving of management's strategy but others not buying the story.[335] Consider the following varied perspectives that analysts (and one of the petitioners) expressed within just a few months before news of the sales process leaked to the press:



Positive	Negative
"After years of M&A, [Solera] is confident the various pieces it has been putting together are finally starting to make more sense. More financial disclosures (started); a renewed IR push and new branding efforts . . . are all efforts to help investors better understand Tony's vision." (Barclays, April 13, 2015)[336]	"Solera's story remains more complicated than most investors would like, we see more downside risk to estimates in the short term, and there are some valid concerns and criticisms of the story presently." (William Blair, July 13, 2015)[339]
"While we acknowledge some shareholder angst over share price performance relative to the market and the group, we believe there is inherent franchise value in this collection of assets and businesses. Tony Aquila, Solera's CEO, should be instrumental in optimizing its competitive position and generating shareholder value. As a result, [Solera] remains an attractive risk/reward, in our view, for patient investors whose risk profile can tolerate elevated financial leverage." (SunTrust Robinson Humphrey, July 17, 2015)[337]	"Since hitting a peak equity value in early calendar year 2014 at $4.8 billion, the negative effect of sub-par returns from acquisitions, increased leverage and growth in interest expense has reduced shareholder value by over $2.2 billion to $2.6 billion. . . . A frequent complaint from investors regarding a potential investment in [Solera] is a lack of confidence in both management and the Board of Directors." (Barrington Research, July 20, 2015)[340]
"We appreciate Solera's strategy of moving into tangential markets that align with the company's core business while still providing diversification away from auto claims. Recent acquisitions and investments show progress on	"With significantly higher leverage, down earnings over the next 12 months, and recent inconsistent performance, we are stepping to the sidelines until we get increased clarity into either accelerating revenue growth or a return to sustainable earnings growth." (Piper Jaffray, July 20, 2015)[341]

[**Editor's Note:** The preceding image contains the reference for footnotes [336] , [337] , [338] , [339] , [340] , [341] , [342]]

***26** These reviews suggest that there was disagreement in the financial community over Solera's strategy, not that the market as a whole did not understand it. Given the many factors indicating that the market for the Company's stock was efficient, the market presumably would have digested all of these sentiments and incorporated them into Solera's stock price. Yet Solera's pre-Merger unaffected stock price as of August 3 was still only $36.39.

The debt market further corroborates that, given its operative reality, Solera was not as valuable as petitioners contend. Petitioners do not dispute that the debt market had run dry for Solera as a public company as of the Merger. With its leverage already rising, the Company made an acquisition in November 2014, financing the deal with a $400 million notes offering.[343] Moody's promptly downgraded the Company's credit rating from Ba2 to Ba3.[344] In July 2015, after Solera issued $850 million of senior unsecured notes to finance another acquisition and retire outstanding debt, Moody's downgraded Solera again, from Ba3 to B1.[345] Further exemplifying Solera's challenges in taking on additional debt to finance acquisitions, the July 2015 debt offering fell short, and Goldman Sachs had to absorb $11.5 million of notes that it was unable to syndicate into the market.[346]

By July 2015, "despite the lucrative fees that investment bankers make from refinancing a large tranche of public company debt and syndicating a new issue,"[347] Solera had run "out of runway" in the debt market.[348] "In other words, participants in the public bond markets weren't convinced they would get their money back if they gave it to [Solera], and [Solera] was not offering enough interest to compensate investors for the risk they saw in the company."[349] Petitioners' own expert admitted that the acquisition debt market for Solera was tight at equity values greater than the Merger price.[350] In short, the debt market, like many equity market participants, viewed Solera skeptically and perceived its growth-by-acquisition strategy as laden with risk.[351]

***27** * * * * *

To summarize, the Merger was the product of a two-month outreach to large private equity firms in May and June, a six-week auction by an independent Special Committee that solicited eleven private equity and seven strategic firms, and public announcements that put a "For Sale" sign on the Company. The Special Committee had competent advisors and the power to say no to an underpriced bid, which it did twice. The Merger price of $55.85 proved to be a market-clearing price through a 28-day go-shop and a three-month window-shop. No one was willing to pay more. Thus, as this court once put it, the "logical explanation ... is self-evident": Solera "was not worth more" than $55.85 per share.[352]

2. Merger Fees Should not be Added to the Deal Price

Petitioners argue that, "if deal price is an indicator of fair value," the court should add nearly $450 million—or $6.51 per share—to the Merger price. According to petitioners, this is the amount of transaction costs Vista incurred in connection with the Merger for buyer fees and expenses, seller fees, debt fees, and an "early participation premium" to retire debt in connection with the transaction.[353] Petitioners offer no precedent or other legal support for this request. They simply contend that these costs should be added because the court's "focus should be on what Vista was actually willing to spend to buy the Company."[354] This argument fails for two independent reasons.

First, petitioners' argument cannot be squared with the definition of "fair value" in the appraisal context that our Supreme Court recently articulated in *DFC* when explaining the purpose of appraisal:

> [F]air value is just that, "fair." It does not mean the highest possible price that a company might have sold for had Warren Buffet negotiated for it on his best day and the Lenape who sold Manhattan on their worst. ... ***[T]he purpose of appraisal*** is not to make sure that the petitioners get the highest conceivable value that might have been procured had every domino fallen out of the company's way; rather, it ***is to make sure that they receive fair compensation for their shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction.***[355]

The Merger price was the result of arm's-length bargaining between the Special Committee and Vista. Perhaps Vista would have been willing to pay more than $55.85 for the Company, but that is irrelevant to the court's independent determination of *fair* value as that term was explained in *DFC*.[356]

***28** Second, policy concerns counsel against adding transaction fees to the deal price in determining Solera's fair value. If stockholders received payment for transaction fees in appraisal proceedings, then it would compel rational stockholders in even the most pristine deal processes to seek appraisal to capture their share of the transaction costs (plus interest) that otherwise would be unavailable to them in any non-litigated arm's-length merger. This incentive would undermine the underlying purpose of appraisal proceedings as explained in *DFC*.

3. Deduction for Merger Synergies

The appraisal statute provides that "the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger."[357] Thus, the "appraisal award excludes synergies in accordance with the mandate of Delaware jurisprudence that the subject company in an appraisal proceeding be valued as a going concern."[358]

Synergies do not only arise in the strategic-buyer context. It is recognized that synergies may exist when a financial sponsor is an acquirer.[359] As of trial, Vista owned 40 software businesses, three of which (EagleView, Omnitracs, and DealerSocket) Vista believed had significant "touch points" with Solera from which synergies could be realized.[360]

Vista modeled out four different categories of synergies in its financial analysis of the Company during the bidding process.[361] Respondent's expert presented evidence at trial concerning three of those categories: portfolio company revenue synergies, private company cost savings, and the tax benefits of incremental leverage.[362] In total, he calculated total expected synergies of $6.12 per share.[363] From there, respondent's expert made a "conservative" estimate that 31% of the value of the synergies—equating to $1.90 per share—remained with the seller by using the lowest percentage identified in one of three empirical studies.[364]

I find this evidence, which petitioners made no effort to rebut, convincing.[365] Deducting $1.90 from the Merger price of $55.85 leads to a value of $53.95 per share. For all the reasons discussed above, and based on my lack of confidence in the DCF models advanced by the parties (as discussed next), I conclude that this amount ($53.95 per share) is the best evidence of the fair value of petitioners' shares of Solera at the time of the Merger.

4. The Dueling Discounted Cash Flow Models

***29** Consistent with the court's duty to consider "all relevant factors" in determining Solera's fair value,[366] I consider next the DCF models the parties' experts prepared. Compared with a market-generated transaction price, "the use of alternative valuation techniques like a DCF analysis is necessarily a second-best method to derive value."[367]

In this action, both parties' experts created "three-stage" DCF models consisting of (i) the five-year Hybrid Case Projections (fiscal years 2016 through 2020), (ii) a five-year transition period (fiscal years 2021 through 2025), and (iii) a terminal period beginning in fiscal year 2026.[368] The outcome of these models nonetheless resulted in widely divergent DCF valuations—$84.65 per share for petitioners, and $53.15 per share for respondent.

As a preliminary matter, I find comfort that respondent's DCF analysis is in the same ballpark as the deal price less estimated synergies.[369] On the other side of the ledger, given my conclusions about the quality of the sales process for Solera, petitioners' DCF analysis strikes me as facially unbelievable as it suggests that, in a transaction with an equity value of approximately $3.85 billion at the deal price,[370] potential buyers left almost $2 billion on the table by not outbidding Vista. Our Supreme Court has acknowledged that a DCF that results in a valuation so substantially below the transaction price may indeed lack "credibility on its face."[371]

***30** "Delaware courts must remain mindful that 'the DCF method is [ ] subject to manipulation and guesswork [and that] the valuation results that it generates in the setting of a litigation [can be] volatile."[372] "[E]ven slight differences in [a DCF's] inputs can produce large valuation gaps."[373] A number of factors explain the gaping difference between petitioners' and respondent's DCF analyses, and, notably, many of these disagreements relate to how to value Solera into perpetuity. Such assumptions about Solera's business in the terminal period, *i.e.*, *ten-plus years into the future*, are unavoidably tinged with a heavy dose of speculation.

I highlight below some of the major areas of disagreement between the parties. This discussion is meant to be illustrative and not exhaustive. All of these disagreements predictably result in a higher asserted valuation by petitioners and a lower asserted valuation by respondent.

The most significant point of contention in the DCF models concerns the estimated amount of cash that Solera would need to reinvest over the terminal period.[374] This "plowback" rate is the percentage of after-tax operating profits that the Company would need to invest to grow at a specified rate into perpetuity.[375] Using the method identified in "many leading valuation texts including Damodaran (2012) and Koller, Goedhart and Wessels (2015)," which petitioners' expert has called the "traditional model,"[376] respondent argues that the required reinvestment rate is 37.1%.[377] Petitioners, on the other hand, argue that the inflation plowback formula published in articles written by Bradley and Jarrell should be used, resulting in a required reinvestment rate of only

16.4%.[378] According to petitioners, holding all else constant in respondent's DCF analysis, the difference between using these two reinvestment rates yields a huge $23.90 per share difference in Solera's valuation.[379]

Another notable area of disagreement in the DCF models is Solera's return on invested capital ("ROIC") in the terminal period. Respondent assumed, consistent with "a theory this court has repeatedly cited with approval,"[380] that in the long run the present value of Solera's growth opportunities would disappear due to increased competition, so the Company's ROIC would gradually converge with its weighted average costs of capital ("WACC").[381] Petitioners disagree with applying the convergence model to Solera. They contend that the Company possesses "moats" around its business, such as barriers to entry, competitive advantages, and market dominance, that will give it *perpetual* advantages over potential competitors.[382] Petitioners thus argue that Solera will earn a return of 4.5% *above* its WACC in perpetuity during the terminal period.[383] When the court asked petitioner's expert how he landed on 4.5%, his response was candid: "It's a little bit of a finger in the wind."[384]

***31** The parties also disagree about how to account for stock-based compensation ("SBC") in their DCF models, both for the discrete period and the terminal period. Respondent applied the "cash basis" method to stock-based compensation expense, using the cash amount that the Company would have to spend to account for SBC as a normalized percentage of revenue.[385] Petitioners did not independently calculate SBC and instead used the Company's projections.[386] These projections were calculated on a book basis, benchmarked to Solera's actual stock price, and assumed to grow at 5% annually.[387]

The parties also handled the contingent tax liability attached to Solera's foreign earnings very differently. As of the Merger, the Company had earned approximately $1.2 billion in foreign profits, for which it had only paid taxes where those profits were earned.[388] Solera historically designated these profits as permanently reinvested earnings ("PRE"). Before these earnings can be repatriated to the United States or paid to stockholders, the Company must pay the residual tax, *i.e.*, the marginal amount between the U.S. tax rate and the amount already paid internationally.[389] Respondent assumed that $350 million of foreign earnings that had been de-designated as PRE would be repatriated as of the Merger had there not been a deal, and that the rest of Solera's foreign profits, both past and future, would be repatriated on a rolling basis following a five-year deferral period.[390] This repatriation would cause Solera to pay more in taxes, decreasing the Company's value. Petitioners, by contrast, assumed that such taxes would *never* be paid because they contend the timing of repatriation is unknown and thus these tax liabilities are speculative.[391]

Finally, the parties disagreed about the amount of cash to be added back to Solera's enterprise value in order to convert it to equity value. This court has repeatedly held that only "excess cash" is to be added back.[392] Solera had approximately $480 million of cash at closing.[393] During the sales process, the Company's CFO did a country-by-country analysis and determined that Solera needed $160 million to $165 million to fund its operations.[394] Respondent used that analysis to deduct $165 million from the Company's $480 million of cash at closing and added back the difference, *i.e.*, $315 million.[395] Petitioners, on the other hand, added back *all* of the $480 million, reasoning that "with modern computer technology, a good CFO doesn't need any wasting cash," and that "it would require an incompetent corporate treasurer for a big chunk of the cash balance to be wasting cash."[396]

* * * * *

There are other points of disagreement in the parties' DCF models, but it is not necessary to detail them here. As explained above, the Merger price was the product of "an open process, informed by robust public information, and easy access to deeper, non-public information, in which many parties with an incentive to make a profit had a chance to bid."[397] Given the huge gap between petitioners' DCF valuation and the Merger price, which I have found to be a reliable indicator of value in accordance with the teachings of *DFC* and *Dell*, I find petitioners' DCF valuation not to be credible on its face and accord it no weight.[398]

32** My decision to do so is corroborated by the fact that nearly ***88% of petitioners' enterprise valuation is attributable to periods *after* the five-year Hybrid Case Projections.[399] In other words, petitioners' DCF valuation is largely a prediction about the Company's operations many years into the future. Such predictions, even when informed, are unavoidably speculative, where small variances in a DCF's inputs can lead to wide valuation swings.[400]

I also give no weight to respondent's DCF valuation, but for a different reason. Although that valuation is close to my Merger price less synergies calculation, respondent's own expert opined that his DCF valuation is "less reliable" than the Merger price minus synergies valuation "given the uncertainties ... surrounding several inputs to the DCF valuation."[401] I agree, and will accord the value of the Merger price minus synergies dispositive weight in this case.[402]

5. Respondent's Unaffected Stock Price Argument is Unavailing

In the wake of our Supreme Court's decisions in *DFC* and *Dell*, the Court of Chancery determined in *Aruba* that the fair value of petitioners' shares in an appraisal proceeding was the thirty-day average unaffected market price of the company's shares, *i.e.*, $17.13 per share.[403] In reaching this conclusion, Vice Chancellor Laster declined to adopt his deal price ($24.67 per share) less synergies figure of $18.20 per share because of his concerns that this figure (i) "likely was tainted by human error," and (ii) "continues to incorporate an element of value derived from the merger itself: the value that the acquirer creates by reducing agency costs."[404]

In its supplemental brief, respondent argues that, "in light of recent cases, the best evidence of Solera's fair value is its unaffected stock price of $36.39 per share."[405] This argument, which advocates for a fair value determination about 35% below the deal price, reflects a dramatic change of position that I find as facially incredible as petitioners' DCF model. Before, during, and after trial (until *Aruba* was decided), respondent and its highly credentialed expert—a former chairman of the President's Council of Economic Advisors[406]—consistently asserted that the "market-generated Merger price, adjusted for synergies" of $53.95 per share is the "***best evidence*** of Solera's value" as of the date the Merger.[407] For the reasons explained above, the court independently has come to the same conclusion.

Notably, nothing prevented respondent from advancing at trial the "unaffected market price" argument the *Aruba* court embraced. The scholarship underpinning the notion that *both* synergies and agency costs are elements of value derived from a merger that should be excluded under Section 262(h) has been in the public domain for many years and was readily available when this case was tried.[408] Yet respondent made no effort to advance this theory at trial and, thus, petitioners were afforded no opportunity to respond to it. In this respect, I agree with the sentiment Vice Chancellor Glasscock expressed in a similar situation that "the use of trading price to determine fair value requires a number of assumptions that ... are best made or rejected after being subject to a forensic and adversarial presentation by interested parties."[409]

***33** As an example, even if one were to accept the legal theory that agency costs represent an element of value derived from the merger itself, little exists in the record to give the court any comfort about Solera's true unaffected market price. The $36.39 per share figure on which the Company relies represents the closing price on a *single* day, August 3, 2015.[410] Although the Company used that date in its proxy statement as the unaffected date for purposes of calculating a premium,[411] and I have referenced it in this opinion a number of times for context, the parties never litigated the issue of Solera's unaffected market price and the court is in no position based on the trial record to reliably make such a determination.

With respect to the merits of the theory that agency costs represent an element of value derived from the merger itself, the *Aruba* court explained that the "concept of reduced agency costs is the flipside of the benefits of control," with the "key point" being that "control creates value distinct from synergy value."[412] This is because, as Professors Hamermesh and Wachter explain, "the aggregation of the shares is value-creating because a controller can then exercise the control rights involving directing the strategy and managing the firm."[413] They go on to argue that the "normative justification for awarding the value of control to the controller parallels the rationale for awarding the value of synergies to the bidder. Efficiency requires that those who create an efficient transaction—either through creating synergies or eliminating agency costs—should receive the value that they create."[414]

Significantly, however, a number of this court's appraisal decisions, one of which was affirmed in relevant part on appeal, suggest that the value of control is properly part of the going concern and not an element of value that must be excised under Section 262(h).[415] In *Le Beau v. M.G. Bancorporation., Inc.*, for example, respondent used a "capital market" approach that "involved deriving various pricing multiples from selected publicly-traded companies, and then applying those multiples to MGB," the target corporation.[416] Then-Vice Chancellor Jacobs rejected the methodology because it "results in a minority valuation."[417] The Supreme Court affirmed this determination, explaining that the trial court's conclusion that the "capital market approach contained an inherent minority discount that made its use legally impermissible in a statutory appraisal proceeding [was] fully supported by the record evidence that was before the Court of Chancery and the prior holdings of this Court construing Section 262."[418]

Similarly, in *Borruso v. Communications Telesystems International*, Vice Chancellor Lamb held that "a control premium should be added to adjust the market value of the equity derived from the comparable company method."[419] The court explained it reasoning as follows:

> ***34** [T]he comparable company method of analysis produces an equity valuation that inherently reflects a minority discount, as the data used for purposes of comparison is all derived from minority trading values of the comparable companies. Because that value is not fully reflective of the intrinsic worth of the corporation on a going concern basis, this court has applied an explicit control premium in calculating the fair value of the equity in an appraisal proceeding.[420]

More recently, then-Vice Chancellor Strine took the same approach in *Andaloro v. PFPC Worldwide, Inc.*[421] There, the court approved adjusting a comparable companies analysis by adding a control premium where "[w]hat is being corrected for is the difference between the trading price of a minority share and the trading price if all the shares were sold."[422]

Our Supreme Court held long ago that the going concern value of a company must be determined in an appraisal case "irrespective of the synergies involved in a merger."[423] *DFC* and *Dell* both make the same point.[424] Although *DFC* and *Dell* are transformative decisions in my view in their full-throated endorsement of applying market efficiency principles in appraisal actions,[425] I do not read those decisions—both of which unmistakably emphasize the probative value of deal price[426]—to suggest that agency costs represent an element of value attributable to a merger separate from synergies that must be excluded under Section 262(h). Had that been the Supreme Court's intention, I believe it would have said so explicitly.

Accordingly, I reject respondent's newly-minted argument that Solera's closing price on August 3, 2015 of $36.39 is the best evidence of Solera's fair value as of the date of the Merger.

IV. CONCLUSION

For the reasons explained above, petitioners are entitled to $53.95 per share as the fair value of their shares of Solera, plus interest accruing from the date the Merger closed, March 3, 2016, at the rate of 5% percent over the Federal Reserve discount rate from time to time, compounded quarterly.[427]

The parties should confer and submit a form of implementing order for the entry of final judgment consistent with this opinion within ten business days. It is the court's intention to unseal the expert reports in this case in their entirety upon entry of a final judgment. If, however, a party believes good cause exists to maintain any portion of any of the expert reports under seal, that party must file a motion within ten business days identifying the specific part that warrants further confidential treatment and explaining the basis for continuing such treatment.

***35 IT IS SO ORDERED.**

All Citations

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Footnotes

[1] The court appreciates the parties' efforts in reaching agreement on a thorough set of factual stipulations.

[2] PTO ¶ 75.

[3] *Id.* ¶¶ 1, 77 & Ex. A.

[4] *Id.* ¶ 81.

[5] *Id.* ¶ 82.

[6] *Id.* ¶ 83.

[7] *Id.* ¶¶ 12, 22-24, 30-32, 39.

[8] *Id.* ¶¶ 76, 80.

[9] Tr. 369-70, 375 (Aquila).

[10] PTO ¶ 117.

[11] *Id.* ¶ 118.

[12] *Id.* ¶ 120.

[13] *Id.* ¶ 125.

[14] *Id.* ¶ 128.

[15] Tr. 659-60 (Giger).

[16] PTO ¶¶ 134-138.

[17] *Id.* ¶ 163.

[18] Tr. 23-24 (Cornell); JX0121.0007.

[19] Tr. 32 (Cornell); JX0092.0012-13.

[20] Tr. 207-08 (Cornell); 758-60 (Yarbrough); JX0092.0014-15.

[21] PTO ¶¶ 159-61, 163.

[22] Tr. 372-73, 381 (Aquila).

[23] PTO ¶ 160.

[24] *Id.* ¶ 132.

[25] *Id.* ¶ 133.

[26] *Id.* ¶ 165.

[27] Tr. 386-88 (Aquila).

[28] *Id.* at 387 (Aquila), 1063 (Hubbard); JX0899.0050-51.

[29] JX1101.0056, 151-52, 175-76.

[30] JX1101.0030.

[31] PTO ¶ 241; Tr. 478-79 (Aquila).

[32] PTO ¶¶ 244-46.

[33] Tr. 464-67 (Aquila), 861 (Yarbrough); JX0175.0108 (William Blair & Company); JX0301.0001 (Goldman Sachs); JX0325.0001 (Goldman Sachs).

[34] JX0140.0003. “Ba” obligations are those “judged to be speculative and are subject to substantial credit risk.” *Rating Symbols and Definitions*, MOODY'S INV'R SERV. 6 (June 2018), https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

[35] JX0140.0003.

[36] Tr. 409-11 (Aquila); JX0258.004.

[37] Tr. 412-14 (Aquila); JX0318.001.

[38] Tr. 416-17 (Aquila); JX0310.0004.

[39] JX0310.0004. “B” obligations are those “considered speculative and are subject to high credit risk.” *Rating Symbols and Definitions*, MOODY'S INV'R SERV. 6 (June 2018), https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

[40] Tr. 414 (Aquila).

[41] *Id.* at 460, 485 (Aquila); JX0088.0002.

[42] Tr. 461 (Aquila).

[43] PTO ¶ 222.

[44] *Id.* ¶ 224; JX0174.0002-03.

[45] JX0174.0002.

[46] Tr. 464 (Aquila).

[47] PTO ¶ 251.

[48] *Id.* ¶ 252.

[49] Tr. 480 (Aquila); PTO ¶¶ 258-60.

[50] Tr. 481-84 (Aquila).

[51] PTO ¶ 262.

[52] JX0208.0002.

[53] Tr. 500-01 (Aquila); JX1120.0004, 17.

[54] JX0214.0014-15 (emphasis added).

[55] Tr. 424-25 (Aquila).

[56] JX0251.0001.

[57] JX0234.0001.

[58] Tr. 762-63 (Yarbrough).

[59] *Id.* at 425-27 (Aquila), 760-62 (Yarbrough).

[60] *Id.* at 862-64 (Yarbrough).

[61] JX0250.0003.

[62] Tr. 428-29 (Aquila), 762-63, 816 (Yarbrough).

[63] Tr. 829-31 (Yarbrough); JX0250.0003.

[64] Tr. 865 (Yarbrough).

[65] *Id.* at 764 (Yarbrough).

[66] *Id.* at 764-65 (Yarbrough).

[67] *Id.* at 865 (Yarbrough).

[68] *Id.* at 764 (Yarbrough).

[69] PTO ¶¶ 268, 271-78.

[70] *Id.* ¶ 279.

[71] *Id.* ¶¶ 277, 280, 282.

[72] *Id.* ¶¶ 278, 283-84.

[73] JX0315.0001.

[74] Tr. 526-27 (Aquila).

[75] PTO ¶ 285.

[76] *Id.* ¶¶ 286-87. The written consent establishing the Special Committee is dated July 23, 2015 (*see* JX0359), but it is stipulated that it was formed on July 20, 2015. PTO ¶ 287.

[77] PTO ¶ 287; Tr. 754-56, 771-772 (Yarbrough).

[78] JX0359.0002.

[79] *Id.*

[80] Tr. 776-78 (Yarbrough); PTO ¶ 289.

[81] JX0625; JX0673.0020; JX1161.0001. Both Centerview and Rothschild each were paid approximately $25 million in advisory fees. JX0673.0020.

[82] Tr. 568 (Aquila); JX1170.

[83] PTO ¶ 289.

[84] Tr. 782-83 (Yarbrough); JX0380.0003-05.

[85] JX0380.0005.

[86] PTO ¶ 295; Tr. 870-71 (Yarbrough).

[87] PTO ¶ 298.

[88] Tr. 780-82 (Yarbrough).

[89] JX1170.

[90] JX0378.0001.

[91] Tr. 546 (Aquila); JX0402.

[92] JX0402.0003, 07.

[93] JX0402.0003.

[94] Tr. 558, 589 (Aquila).

[95] *Id.* at 854 (Yarbrough).

[96] PTO ¶ 299; JX0756.0044.

[97] PTO ¶ 388; JX0445.0005.

[98] *See* JX0467.0001 (Silver Lake); JX0456.0001 (Pamplona).

[99] JX0465.0001.

[100] PTO ¶ 302.

[101] JX0340.0003; JX0464.0005, 08.

[102] PTO ¶ 305.

[103] *Id.* ¶ 306.

[104] JX0499.0002.

[105] JX0497.0001-02 (August 20, 2015 email from Advent to Centerview); JX0517.0001 (August 21, 2015 email referencing Advent call to UK head of Rothschild).

[106] JX0497.0001.

[107] Tr. 844-45 (Yarbrough).

[108] *Id.* at 845-46 (Yarbrough).

[109] JX0556.0001.

[110] *Id.*

[111] JX0497; JX0556.

[112] Tr. 597-98 (Aquila); JX0523; JX0525.

[113] JX0525.0002.

[114] Tr. 833 (Yarbrough).

[115] JX0525.0001; JX0541.0001.

[116] PTO ¶ 307.

[117] *Id.* ¶ 308.

[118] *Id.* ¶ 309.

[119] *Id.* ¶ 312.

[120] *Id.* ¶ 312; Tr. 441 (Aquila), 793 (Yarbrough).

[121] PTO ¶ 313.

[122] *Id.* ¶ 317.

[123] Tr. 442-44 (Aquila).

[124] PTO ¶ 321.

[125] JX0611.0002.

[126] PTO ¶¶ 322, 324.

[127] *Id.* ¶ 311.

[128] Tr. 796-97 (Yarbrough).

[129] PTO ¶¶ 322-23.

[130] *Id.* ¶ 324.

[131] JX0620.0001-02; JX0626.0001.

[132] Tr. 934-35, 964-67 (Sowul). Petitioners question the veracity of this explanation, but I found Sowul's testimony on the point to be credible and one of petitioners' own experts confirmed the spreadsheet error. *Id.* at 301-04 (Buckberg).

[133] *Id.* at 934-35 (Sowul).

[134] PTO ¶¶ 382-84; Tr. 589 (Aquila); JX0623.

[135] JX0628.

136 PTO ¶ 325.

137 *Id.* ¶¶ 329-31.

138 *Id.* ¶ 332.

139 JX0638.0001.

140 PTO ¶ 334.

141 Tr. 969-70 (Sowul).

142 *Id.* at 806 (Yarbrough).

143 JX0644.0001.

144 PTO ¶ 338; Tr. 806 (Yarbrough).

145 Tr. 807 (Yarbrough).

146 JX0651.0001.

147 PTO ¶ 339; JX0756.0052; Tr. 807-08 (Yarbrough).

148 PTO ¶ 339.

149 *Id.* ¶ 341; Tr. 807-08 (Yarbrough); JX0661.0001-04.

150 *Id.* ¶¶ 346-47.

151 *Id.* ¶ 348.

152 JX0681.

153 JX0681.0001.

154 JX0670.0002.

155 JX0683.0001.

156 PTO ¶ 350.

157 *Id.* ¶ 351; Tr. 811 (Yarbrough). Solera withheld six documents. Four of the six documents concerned Digital Garage, a strategically sensitive new smartphone application, and the other two concerned personnel matters. Tr. 811 (Yarbrough); PTO ¶ 139-44.

158 PTO ¶ 354.

159 *Id.* ¶ 355.

160 *Id.* ¶ 356.

161 JX0744.0001, 03; Tr. 611-614 (Aquila).

162 PTO ¶¶ 382-387; JX0760.0004.

163 JX0760.0004, 09-10.

164 PTO ¶ 5; JX0756.0069.

165 PTO ¶¶ 6-7.

166 *Id.* ¶ 1.

167 JX0855.0001.

168 Dkt. 122.

169 Dkt. 125.

170 *Cavalier Oil Corp. v. Harnett*, 564 A.2d 1137, 1142 (Del. 1989) (citation omitted).

171 8 *Del. C.* § 262(h).

172 *See M.P.M. Enters., Inc. v. Gilbert*, 731 A.2d 790, 797 (Del. 1999).

173 *Tri-Cont'l Corp. v. Battye*, 74 A.2d 71, 72 (Del. 1950).

174 *M.G. Bancorporation, Inc. v. Le Beau*, 737 A.2d 513, 525 (Del. 1999).

175 *Matter of Shell Oil Co.*, 607 A.2d 1213, 1218 (Del. 1992).

176 *Cavalier Oil*, 564 A.2d at 1144.

177 *In re Appraisal of Ancestry.com, Inc.*, 2015 WL 399726, at *15 (Del. Ch. Jan. 30, 2015) (citing *Glob. GT LP v. Golden Telecom, Inc.* 11 A.3d 214, 218 (Del. 2010)).

178 *See Laidler v. Hesco Bastion Envtl., Inc.*, 2014 WL 1877536, at *6 (Del. Ch. May 12, 2014) (compiling authorities); *see also In re Lane v. Cancer Treatment Ctrs. of Am., Inc.*, 1994 WL 263558, at *2 (Del. Ch. May 25, 1994) ("[R]elevant factors to be considered include 'assets, market value, earnings, future prospects, and

any other elements that affect the intrinsic or inherent value of a company's stock.' ") (quoting *Weinberger*, at 711).

179 *In re Appraisal of Metromedia Int'l Gp., Inc.*, 971 A.2d 893, 899-900 (Del. Ch. 2009) (citation omitted).

180 *Laidler*, 2014 WL 1877536, at *6 (citing *M.G. Bancorporation., Inc., v. Le Beau*, 737 A.2d at 520).

181 172 A.3d 346 (Del. 2017).

182 177 A.3d 1 (Del. 2017).

183 *DFC*, 172 A.3d at 348.

184 *In re Appraisal of DFC Glob. Corp.*, 2016 WL 3753123, at *1 (Del. Ch. July 8, 2016), *rev'd*, *DFC*, 172 A.3d 346.

185 *See id.* at *21 ("Each of these valuation methods suffers from different limitations that arise out of the same source: the tumultuous environment in the time period leading up to DFC's sale. As described above, at the time of its sale, DFC was navigating turbulent regulatory waters that imposed considerable uncertainty on the company's future profitability, even its viability. Some of its competitors faced similar challenges. The potential outcome could have been dire, leaving DFC unable to operate its fundamental businesses, or could have been very positive, leaving DFC's competitors crippled and allowing DFC to gain market dominance. Importantly, DFC was unable to chart its own course; its fate rested largely in the hands of the multiple regulatory bodies that governed it. Even by the time the transaction closed in June 2014, DFC's regulatory circumstances were still fluid.").

186 *DFC*, 172 A.3d at 360-61.

187 *Id.* at 351.

188 *Id.* at 349.

189 *Id.*

190 *Id.* at 370-71.

191 *Id.* at 369-70.

192 *Id.* at 373.

193 *Id.* at 367.

194 *In re Appraisal of Dell Inc.*, 2016 WL 3186538, at *1, 18 (Del. Ch. May 31, 2016), *rev'd*, *Dell*, 177 A.3d 1.

195 *Dell*, 117 A.3d at 6.

196 *Id.* at 7.

197 *Id.* at 27.

198 *Id.* at 28 (citing *DFC*, 172 A.3d at 374-77); *see also id.* ("[The financial advisor] did not initially solicit the interest of strategic bidders because its analysis suggested none was likely to make an offer.").

199 *Id.*

200 *Id.* at 29.

201 *Id.* at 28.

202 *Id.*

203 *Id.* at 29 (citation omitted).

204 *Id.* at 30. *See also id.* at 23 ("In fact, the record as distilled by the trial court suggests that the deal price deserved heavy, if not dispositive, weight.").

205 *Id.* at 35.

206 2018 WL 922139 (Del. Ch. Feb. 15, 2018), *reargument denied*, 2018 WL 2315943 (Del. Ch. May 21, 2018).

207 2018 WL 1037450 (Del. Ch. Feb. 23, 2018).

208 2018 WL 922139 at *1-2 (citations omitted).

209 *Id.* at *2 (citation omitted).

210 *Id.* at *1, 4.

211 *Id.* at *2-4 (internal citations, quotations, and alterations omitted).

212 2018 WL 1037450, at *1.

213 *Id.* at *8.

214 *Id.* at *21. Just last week, the Court of Chancery similarly found in another case that flaws in a sales process leading to a merger undermined the reliability of the merger price as an indicator of fair value. *Blueblade Capital Opportunities LLC v. Norcraft Cos., Inc.*, 2018 WL 3602940, at *1-2 (Del. Ch. July 27, 2018).

215 JX0898.0094-95, 200.

216 JX0898.0098.

217 Resp't's Post-Trial Opening Br. 1 (Dkt. 106); *see also* JX0894.0125-26.

218 JX0894.0126.

219 *Id.*

220 Resp't's Suppl. Post-Trial Br. 5 (Dkt. 123).

221 *DFC*, 172 A.3d at 349.

222 *Id.*

223 *Dell*, 177 A.3d at 28.

224 8 *Del. C.* § 262(h) ("In determining such fair value, the Court shall take into account all relevant factors."); *see also* *DFC*, 172 A.3d at 364 (affirming *Golden Telecom* and restating that "§ 262(h) gives broad discretion to the Court of Chancery to determine the fair value of the company's shares, considering 'all relevant factors' ").

225 *DFC*, 172 A.3d at 349.

226 *Id.* at 373.

227 *Id.*

228 *Id.* at 349.

229 *Dell*, 177 A.3d at 32-34.

230 *DFC*, 172 A.3d at 349.

231 *Id.* at 366.

232 *Dell*, 177 A.3d at 35.

233 *Id.*

234 *Id.* at 28.

235 *DFC*, 172 A.3d at 373.

236 *Id.* at 349.

237 *Id.*

238 *Dell*, 177 A.3d at 23.

239 *DFC*, 172 A.3d at 388.

240 *Dell*, 177 A.3d at 22 (citation omitted).

241 *Merion Capital L.P. v. Lender Processing*, 2016 WL 7324170, at *18 (Del. Ch. Dec. 16, 2016).

242 PTO ¶¶ 268, 271-78.

243 *Id.* ¶ 285.

244 *Id.* ¶¶ 295, 307-09.

245 Tr. 1029-31, 1036-37 (Hubbard).

246 *Id.* at 132 (Cornell).

247 *In re Appraisal of PetSmart, Inc.*, 2017 WL 2303599, at *28 (Del. Ch. May 26, 2017); *see also* Tr. 1036 (Hubbard) ("Once a sales process became public in the Bloomberg story, anyone who wished to bid on this asset could certainly have jumped in."); *Dell*, 177 A.3d at 28 ("[G]iven leaks that Dell was exploring strategic alternatives, record testimony suggests that [Dell's banker] presumed that any interested parties would have approached the Company before the go-shop if serious about pursuing a deal.").

248 Tr. 789 (Yarbrough) ("And then an upside of that is that everybody in the world knew that we were looking at strategic alternatives at that point.").

249 JX0214.0014-15.

250 PTO ¶ 306.

251 *Id.* ¶ 305.

252 JX0499.0002.

253 JX0644.0001.

254 JX0651.0001.

255 *Lender Processing*, 2016 WL 7324170, at *18 ("Importantly, however, if bidders perceive a sale process to be relatively open, then a credible threat of competition can be as effective as actual competition.").

256 Leaks of the amounts of the bids theoretically could have functioned to anchor the bidding process, but Solera never publicly confirmed the validity of these reports and petitioners have never argued that these leaks had any impact on the competitive dynamic among bidders.

257 *See* JX0497; JX0556.

258 As petitioners acknowledge, it also is doubtful whether including more financial sponsors in the sales process (beyond the eleven that the Special Committee contacted) would have meaningfully increased competition between the bidders. Pet'rs' Post-Trial Opening Br. 27-28 (Dkt. 105). *See also* *Lender Processing*, 2016 WL 7324170, at *17 (citation omitted) ("Financial sponsors ... predominately use the same pricing models, the same inputs, and the same value-creating techniques.").

259 *See* *DFC*, 172 A.3d at 349 ("Any rational purchaser of a business should have a targeted rate of return that justifies the substantial risks and costs of buying a business. That is true for both strategic and financial buyers.").

260 177 A.3d at 29 (citing *DFC*, 172 A.3d at 375 n.154 ("[T]he absence of synergistic buyers for a company is itself relevant to its value.")).

261 *See* Tr. 973-74 (Sowul) ("And so that party, that IHS, that strategic, could, in theory, pay a lot more than we could. And we knew they were interested.... So we would have to pay as little as we can to maximize our returns but pay as much as we can so that we can be competitive against a strategic."); *see also* *PetSmart*, 2017 WL 2303599, at *29 (citation omitted) ("Importantly, the evidence reveals that the private equity bidders did not know who they were bidding against and whether or not they were competing with strategic bidders. They had every incentive to put their best offer on the table.").

262 Tr. 780-82 (Yarbrough).

263 PTO ¶ 307.

264 *Id.* ¶ 312.

265 *Id.* ¶ 313.

266 *Id.* ¶ 312; Tr. 442-43 (Aquila).

267 PTO ¶ 351; Tr. 811 (Yarbrough).

268 PTO ¶ 354.

269 Pet'rs' Post-Trial Opening Br. 28.

270 *Id.* at 28-29. VIX stands for the CBOE Volatility Index, which Buckberg described as "a measure of market expectations of near-term volatility conveyed by S & P 500 stock index option prices." JX0895.0012 (Buckberg expert report).

271 Pet'rs' Post-Trial Opening Br. 28-33.

272 Tr. 250 (Buckberg).

273 *Id.* at 253 (Buckberg).

274 *Id.* at 852 (Yarbrough).

275 JX0895.0026.

276 Pet'rs' Post-Trial Opening Br. 15.

277 Tr. 1042-43 (Hubbard).

278 *Id.* at 337-38 (Buckberg).

279 JX0899.0027.

280 *See* Tr. 295-96 (Buckberg); *see also* *DFC*, 172 A.3d at 350 ("[T]he fact that a financial buyer may demand a certain rate of return on its investment in exchange for undertaking the risk of an acquisition does not mean that the price it is willing to pay is not a meaningful indication of fair value.").

281 *DFC*, 172 A.3d at 370.

282 *Id.* at 370-71.

283 *Id.* at 349.

284 *See Dell*, 177 A.3d at 28 ("The Committee, composed of independent, experienced directors and armed with the power to say 'no,' persuaded [the bidder] to raise its bid six times. Nothing in the record suggests that increased competition would have produced a better result."); *PetSmart*, 2017 WL 2303599, at *30 ("Had the auction not generated an offer that the Board deemed too good to pass up, I am satisfied that the Board was ready to pursue other initiatives as a standalone company."); *Lender Processing*, 2016 WL 7324170, at *19 ("Reinforcing the threat of competition from other parties was the realistic possibility that the Company would reject the [ ] bid and pursue a different alternative.").

285 JX0359.0002.

286 *Id.*

287 Tr. 754-56, 771-72 (Yarbrough).

288 *Id.* at 776-78 (Yarbrough).

289 PTO ¶ 334.

290 *Id.* ¶ 338.

291 Tr. 806-07 (Yarbrough).

292 *See PetSmart*, 2017 WL 2303599, at *28 (emphasis in original) ("I note that the Board considered inviting the most likely strategic partner ... into the process, but made the reasoned decision that, without a firm indication of interest from [the competitor], the risks of providing [the company's] most direct competitor with unfettered access to [the company's] well-stocked data room outweighed any potential reward. Nevertheless, the evidence revealed that the Board held the door open for [the competitor] to join the auction *if* it expressed serious interest in making a bid.").

293 PTO ¶¶ 325, 339, 350.

294 *See infra* Section III.D.1.c.

295 Tr. 807-08 (Yarbrough).

296 JX0633.0013.

297 Tr. 807-08 (Yarbrough).

298 Pet'rs' Post-Trial Opening Br. 4 (emphasis in original).

299 JX0340.0003 ("We are contemplating this deal solely in the context of being able to partner with Tony Aquila and his management team.") (Thoma Bravo); JX0464.0005 ("We have been impressed by the high caliber of the management team we have met, and look forward to forming a successful and productive partnership with them and the other members of the Solera management team.") (Vista); JX0464.0008 ("Our team is ecstatic about the opportunity to partner with Tony and other members of senior management.") (Pamplona).

300 JX0525; JX0541.

301 Tr. 452 (Aquila), 971-73 (Sowul).

302 Tr. 782-83 (Yarbrough); JX0380.0003-05.

303 *See In re Lear Corp. S'holder Litig.*, 926 A.2d 94, 117 (Del. Ch. 2007) (Strine, V.C.) ("I believe it would have been preferable for the Special Committee to have had its chairman or, at the very least, its banker participate with [the CEO] in negotiations with [the buyer]. By that means, there would be more assurance that [the CEO] would take a tough line and avoid inappropriate discussions that would taint the process.").

304 I view Baron's statement in an email to his colleagues at Rothschild that "we were the architects with the CEO from the beginning as to how to engineer the process from start to finish" to be puffery. The email completely ignores Centerview's role in the sales process, and Baron's statement that he is "excited to ... market the heck out of this for future business" betrays his motivation for exaggerating his involvement in the transaction. Notably, three recipients of Baron's email were his superiors at Rothschild. JX0670.0002.

305 *Dell*, 177 A.3d at 31-32.

306 *Id.*

307 Pet'rs' Post-Trial Opening Br. 26.

308 *Id.* at 27.

309 JX0902.0005; *see also* Tr. 148-49 (Cornell).

310 JX0899.0011.

311 Tr. 589 (Aquila).

312 Tr. 1034 (Hubbard) ("Q. Was Mr. Aquila a net buyer in this transaction? A. Not the way economists would use that term, no. Q. And how do you understand that term? A. Actually, the economic definition is pretty much as the plain English. It would mean contributing new cash as a net buyer. That did not happen.").

313 JX0899.0009.

314 PTO ¶¶ 382-387.

315 Tr. 148-49 (Cornell).

316 *Dell*, 177 A.3d at 31.

317 *See id.* at 6 (noting that the features of an MBO transaction that may render the deal price unreliable "were largely absent" in the Dell MBO).

318 *DFC*, 172 A.3d at 373.

319 *Dell*, 177 A.3d at 25 (citation omitted); *see also* JX0894.0034 (Hubbard expert report) ("In a well-functioning stock market, a company's market price quickly reflects publicly available information. A market price balances investors' willingness to buy and sell the shares in light of this information, and thus represents their consensus view as to the value of the equity of the company. As a result, finance academics view market prices as an important indicator of intrinsic value absent evidence of frictions that impede market efficiency.").

320 *See* *Dell*, 177 A.3d at 27 n.131 ("This is evident as the court observed that the stock price anchors negotiations and, if the stock price is low, the deal price necessarily might be low.").

321 JX0894.0035. The S & P MidCap 400 contains 400 firms that are generally smaller than those in the S & P 500 but "capture a period in the typical enterprise life cycle in which firms have successfully navigated the challenges inherent to small companies, such as raising initial capital and managing early growth." *Mid Cap: A Sweet Spot for Performance*, S & P DOW JONES INDICES 1 (September 2015), https://us.spindices.com/documents/education/practice-essentials-mid-cap-a-sweet-spot-for-performance.pdf.

322 JX0894.0035, 137.

323 *Id.*

324 *Id.*

325 JX0894.0035.

326 *See* JX0842-43 (observing that Solera's stock rose more than ten percent on multiple times its normal daily trading volume on August 4 and 5, 2015, and concluding that "this trading activity is consistent with trading on rumors of a transaction").

327 PTO ¶ 363.

328 *Id.* ¶ 364 & Ex. A.

329 Tr. 1052-53 (Hubbard); JX0894.0047-48.

330 Tr. 1053 (Hubbard). *See also* *DFC*, 172 A.3d at 369 (quoting *Applebaum v. Avaya, Inc.*, 812 A.2d 880, 889-90 (Del. 2002)) ("[A] well-informed, liquid trading market will provide a measure of fair value superior to any estimate the court could impose.").

331 Pet'rs' Post-Trial Opening Br. 4.

332 *See, e.g.*, *DFC*, 172 A.3d at 369 n.117 ("One of the reasons, of course, why a control block trades at a different price than a minority block is because a controller can determine key issues like dividend policy."); *IRA Tr. v. Crane*, 2017 WL 7053964, at *7 n.54 (Del. Ch. Dec. 11, 2017) ("That control of a corporation has value is well-accepted.").

333 Pet'rs' Post-Trial Opening Br. 6.

334 *See, e.g.*, PTO ¶¶ 243-44.

335 *Dell*, 177 A.3d at 26-27; *see also* *id.* at 24 ("[A]nalysts scrutinized [the company's] long-range outlook when evaluating the Company and setting price targets, and the market was capable of accounting for [the company's] recent mergers and acquisitions and their prospects in its valuation of the Company.").

336 JX0202.0001.

337 JX0328.0001.

338 JX0350.0002.

339 JX0312.0002.

340 JX0348.0002.

341 JX0344.0002.

342 JX0319.0001.

343 Tr. 393-96 (Aquila).

344 JX0140.0003.

345 JX0310.0004.

346 Tr. 413-14 (Aquila); JX0318.0001.

347 *DFC*, 172 A.3d at 355.

348 Tr. 399-401 (Aquila).

349 *DFC*, 172 A.3d at 374.

350 *See* Tr. 114 (Cornell) ("[I]n this market condition, for whatever reason, there wasn't a lot of cheap debt available, and that limited what a private equity firm's going to be able to pay and satisfy itself and its shareholders."); *see also* *DFC*, 172 A.3d at 375 ("As is the case with refinancings, so too do banks like to lend and syndicate the acquisition debt for an M & A transaction if they can get it done. That is how they make big profits. That lenders would not finance a buyout of DFC at a higher valuation logically signals weakness in its future prospects, not that debt providers and equity buyers were all mistaken. So did the fact that DFC's already non-investment grade debt suffered a downgrade in 2013 and then was put on a negative credit watch in 2014.").

351 *See* *DFC*, 172 A.3d at 349 ("Like any factor relevant to a company's future performance, the market's collective judgment of the effect of ... risk may turn out to be wrong, but established corporate finance theories suggest that the collective judgment of the many is more likely to be accurate than any individual's guess. When the collective judgment involved, as it did here, not just the views of the company stockholders, but also those of potential buyers of the entire company and those of the company's debtholders with a self-interest in evaluating the regulatory risks facing the company, there is more, not less, reason to give weight to the market's view of an important factor.").

352 *Highfields Capital. Ltd. v. AXA Fin., Inc.*, 939 A.2d 34, 60 (Del. Ch. 2007).

353 Pet'rs' Post-Trial Opening Br. 34-35.

354 *Id.* at 35.

355 *DFC*, 172 A.3d at 370-71 (emphasis added).

356 The Supreme Court also made clear that a deal price arrived at by using an LBO model can be the most reliable evidence of fair value of a target company. *See* *DFC*, 172 A.3d at 350 ("[T]he fact that a financial buyer may demand a certain rate of return on its investment in exchange for undertaking the risk of an acquisition does not mean that the price it is willing to pay is not a meaningful indication of fair value.").

357 8 *Del. C.* § 262(h).

358 *Union Ill. 1995 Inv. Ltd. P'ship v. Union Fin. Gp., Ltd.*, 847 A.2d, 340, 343 (Del. Ch. 2004) (Strine, V.C).

359 *See, e.g.*, *PetSmart*, 2017 WL 2303599, at *31 n.364 (citation omitted) (noting "synergies financial buyers may have with target firms arising from other companies in their portfolio"); *Lender Processing*, 2016 WL 7324170, at *17 n.14 (noting that "a source of private value" to a financial buyer is "a synergistic portfolio company").

360 Tr. 908-16 (Sowul); JX0613.0033.

361 *Id.* at 908-09 (Sowul).

362 *Id.* at 1045-48 (Hubbard); JX0894.0066-71.

363 *Id.* at 1045-46 (Hubbard); JX0894.0070-71.

364 Tr. 1047-48 (Hubbard); JX0894.0070-71. This 31% figure is the "median portion of synergies shared with the seller" as determined by a 2013 Boston Consulting Group study of 365 deals. JX0894.0070-71. Although the appraisal statute mandates excision of synergies specific to the merger at issue, this court has used general estimates of the percentage of synergies shared, as provided by experts, to derive appraisal value from deal

price. *See* *Union Ill.*, 847 A.2d at 353 & n.26 (relying on a "reasonable synergy discount" propounded by a party's expert).

365 *See* *DFC*, 172 A.3d at 371 ("Part of why the synergy excision issue can be important is that it is widely assumed that the sales price in many M & A deals includes a portion of the buyer's expected synergy gains, which is part of the premium the winning buyer must pay to prevail and obtain control.").

366 *See* 8 *Del. C.* § 262(h) ("In determining such fair value, the Court shall take into account all relevant factors."); *DFC*, 172 A.3d at 388 ("But, in keeping with our refusal to establish a 'presumption' in favor of the deal price because of the statute's broad mandate, we also conclude that the Court of Chancery must exercise its considerable discretion while also explaining, with reference to the economic facts before it and corporate finance principles, why it is according a certain weight to a certain indicator of value.").

367 *Union Ill.*, 847 A.2d at 359.

368 JX0894.0075 (Hubbard); JX0898.0098, 0124 (Cornell).

369 *See* *S. Muio & Co. LLC v. Hallmark Entm't Invs. Co.*, 2011 WL 863007, at *20 (Del. Ch. Mar. 9, 2011) (quoting *Hanover Direct, Inc. S'holders Litig.*, 2010 WL 3959399, at *2-3 (Del. Ch. Sept. 24, 2010)) (noting that the court "gives more credit and weight to experts who apply 'multiple valuation techniques that support one another's conclusions' and that 'serve to cross-check one another's results.' "), *aff'd*, 35 A.3d 419 (Del. 2011).

370 JX0835.

371 *See* *Dell*, 177 A.3d at 36 (citations omitted) ("As is common in appraisal proceedings, each party—petitioners and the Company—enlisted highly paid, well-credentialed experts to produce DCF valuations. But their valuation landed galaxies apart—diverging by approximately $28 billion, or 126%.... The Court of Chancery recognized that '[t]his is a recurring problem,' and even believed the 'market data is sufficient to exclude the possibility, advocated by the petitioners' expert, that the Merger undervalued the Company by $23 billion.' Thus, the trial court found petitioners' valuation lacks credibility on its face. We agree."); *PetSmart, Inc.*, 2017 WL 2303599, at *2 ("Moreover, the evidence does not reveal any confounding factors that would have caused the massive market failure, to the tune of $4.5 billion (a 45% discrepancy)."); *Highfields*, 939 A.2d at 52 (citation omitted) (disregarding analysis that was "markedly disparate from market price data for [the company's] stock and other independent indicia of value").

372 *PetSmart*, 2017 WL 2303599, at *40 n.439 (quoting William T. Allen, *Securities Markets as Social Products: The Pretty Efficient Capital Market Hypothesis*, 28 J. CORP. L. 551, 560 (2003)).

373 *Dell*, 177 A.3d at 38.

374 JX0899.0004.

375 JX0899.0045.

376 JX1419.0002, 0007.

377 JX0894.0082; Tr. 1067-68, 1189 (Hubbard).

378 JX0900.0027; Tr. 64-66, 77-81 (Cornell). Respondent not only argues that it is incorrect to apply Bradley/Jarrell, but that petitioners also misapplied the formula. Specifically, respondent argues that petitioners erred by applying their Bradley/Jarrell-derived investment rate to net operating profit after tax (NOPAT) instead of net cash flow (NCF). According to respondent, this mistake resulted in improperly assuming away Solera's required maintenance investment into perpetuity. Resp't's Post-Trial Opening Br. 47, 51-52.

379 Tr. 103; JX0900.0007-08.

380 *PetSmart*, 2017 WL 2303599, at *39; *see also* *In re John Q. Hammons Hotels Inc. S'holder Litig.*, 2011 WL 227634, at *4 n.16 (Del. Ch. Jan. 14, 2011) (stating that the convergence model is "a reflection of the widely-accepted assumption that for companies in highly competitive industries with no competitive advantages, value-creating investment opportunities will be exhausted over a discrete forecast period, and beyond that point, any additional growth will be value-neutral," leading to "return on new investment in perpetuity [that] converge[s] to the company's cost of capital"); *Cede & Co. v. Technicolor, Inc.*, 1990 WL 161084, at *26 (Del. Ch. Oct. 19, 1990) (discussing that "profits above the cost of capital in an industry will attract competitors, who will over some time period drive returns down to the point at which returns equal the cost of capital"), *aff'd in part and rev'd in part on other grounds*, 634 A.2d 345 (Del. 1993).

381 Tr. 1085-87 (Hubbard).

382 JX0900.0028, 32.

383 JX0900.0031.

384 Tr. 242-43 (Cornell).

385 *Id.* at 1059-60 (Hubbard); JX0899.0043-44.

386 *Id.* at 57 (Cornell).

387 *Id.* at 1060 (Hubbard).

388 *Id.* at 692-93 (Giger).

389 *Id.* at 1094-97 (Hubbard).

390 *Id.* at 1094-98 (Hubbard).

391 *Id.* at 70-75 (Cornell); JX0900.0040-42.

392 *See, e.g.*, *In re Appraisal of SWS Grp., Inc.*, 2017 WL 2334852, at *15 (Del. Ch. May 30, 2017) (citation omitted) ("It is true as a matter of valuation methodology that non-operating assets—including cash in excess of that needed to fund the operations of the entity—are to be added to a DCF analysis.").

393 Tr. 229 (Cornell).

394 *Id.* at 695 (Giger).

395 JX0894.0103; Tr. 1092-94 (Hubbard).

396 Tr. 67-68 (Cornell).

397 *DFC*, 172 A.3d at 349.

398 *See* *Dell*, 177 A.3d at 35 ("When ... an appraisal is brought in cases like this where a robust sale process [involving willing buyers with thorough information and the time to make a bid] in fact occurred, the Court of Chancery should be chary about imposing the hazards that always come when a law-trained judge is forced to make a point estimate of fair value based on widely divergent partisan expert testimony."); *DFC*, 172 A.3d at 379 ("Simply given the Court of Chancery's own findings about the extensive market check, the value gap already reflected in the court's original discounted cash flow estimate of $13.07 should have given the Court doubts about the reliability of its discounted cash flow analysis.").

399 JX0898.0124.

400 *See* *Dell*, 177 A.3d at 37-38 ("Although widely considered the best tool for valuing companies when there is no credible market information and no market check, DFC valuations involve many inputs—all subject to disagreement by well-compensated and highly credentialed experts—and even slight differences in these inputs can produce large valuation gaps.").

401 JX0894.0126.

402 Given my conclusion to accord no weight to either side's DCF model, there is no need to retain a court-appointed expert to resolve the parties' disagreement concerning the appropriate method to determine the investment rate for the terminal period.

403 *Aruba*, 2018 WL 922139, at *1, 4.

404 *Id.* at *2-3.

405 Resp't's Suppl. Post-Trial Br. 5.

406 Tr. 1023 (Hubbard).

407 Resp't's Post-Trial Opening Br. 1 (emphasis added).

408 *Aruba*, 2018 WL 922139, at *3 n.16 (citing William J. Carney & Mark Heimendinger, *Appraising the Nonexistent: The Delaware Court's Struggle with Control Premiums*, 152 U. PA. L. REV. 845, 847–48, 857–58, 861–66 (2003); Lawrence A. Hamermesh & Michael L. Wachter, *Rationalizing Appraisal Standards in Compulsory Buyouts*, 50 B.C. L. REV. 1021, 1023–24, 1034–35, 1044, 1046–54, 1067 (2009); Lawrence A. Hamermesh & Michael L. Wachter, *The Short and Puzzling Life of the "Implicit Minority Discount" in Delaware Appraisal Law*, 156 U. PA. L. REV. 1, 30–36, 49, 52, 60 (2007); Lawrence A. Hamermesh & Michael L. Wachter, *The Fair Value of Cornfields in Delaware Appraisal Law*, 31 J. CORP. L. 119, 128, 132–33, 139–42 (2005)).

409 *AOL*, 2018 WL 1037450, at *10 n.118.

410 PTO ¶ 79 & Ex. A.

411 *Id.* ¶ 363.

412 *Aruba*, 2018 WL 922139, at *3 n.17 (citations omitted).

413 Lawrence A. Hamermesh & Michael L. Wachter, *Rationalizing Appraisal Standards in Compulsory Buyouts*, 50 B.C. L. REV. 1021, 1052 (2009).

414 *Id.*

415 *See id.* ("Finally, do minority shareholders receive the value of control that is created by the aggregation of the shares and the creation of a new controller? ... Embracing the concept of an 'implicit minority discount,' the courts would award the dissenters [the value of control], on the theory that fair value should not be reduced for lack of control.").

416 1998 WL 44993, at *7 (Del. Ch. Jan. 29, 1998), *aff'd in part and remanded in part*, 737 A.2d 513.

417 *Id.* at *8.

418 *M.G. Bancorporation., Inc., v. Le Beau*, 737 A.2d at 523 (citation omitted).

419 753 A.2d 451, 452 (Del. Ch. 1999).

420 *Id.* at 458.

421 2005 WL 2045640 (Del. Ch. Aug. 19, 2005).

422 *Id.* at *18 (citing *Borruso*, 753 A.2d 451).

423 *See Gilbert*, 731 A.2d at 797 ("[S]ection 262(h) requires that the Court of Chancery discern the going concern value of the company irrespective of the synergies involved in a merger.").

424 *Dell*, 177 A.3d at 21; *DFC*, 172 A.3d at 371.

425 *See Aruba.*, 2018 WL 2315943, at *8 & n.61 (reargument decision) (comparing *DFC* and *Dell* to how past "Supreme Court decisions had treated the unaffected trading price as a valuation indicator").

426 *Dell*, 177 A.3d at 30 ("Overall, the weight of evidence shows that Dell's deal price has heavy, if not overriding, probative value."); *DFC*, 172 A.3d at 349 ("[E]conomic principles suggest that the best evidence of fair value was the deal price.").

427 8 *Del. C.* § 262(h).

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UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

IN RE Appraisal of STILLWATER MINING COMPANY

Consol. C.A. No. 2017-0385-JTL
|
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|
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MEMORANDUM OPINION

LASTER, V.C.

***1** This post-trial decision determines the fair value of the common stock of Stillwater Mining Company ("Stillwater" or the "Company") as of May 4, 2017, which is when Sibanye Gold Limited completed its acquisition of Stillwater through a reverse-triangular merger (the "Merger"). Pursuant to an agreement and plan of merger dated December 9, 2016 (the "Merger Agreement"), each share of Stillwater common stock was converted at closing into the right to receive $18.00, subject to the right of each holder to eschew the merger consideration and seek appraisal.

The petitioners perfected their appraisal rights and litigated this appraisal proceeding. They contended that Stillwater's fair value was $25.91 per share. To justify this outcome, they relied on an expert who valued Stillwater using a discounted cash flow ("DCF") model.

The respondent in an appraisal proceeding is technically the surviving corporation, but the real party in interest is the acquirer. The petitioners' true opponent in this proceeding was Sibanye.

Sibanye contended that Stillwater's fair value was $17.63 per share. To justify this outcome, Sibanye relied on a combination of metrics, including the deal price, Stillwater's unaffected trading price with an adjustment for a valuation increase between the unaffected date and closing, and an expert valuation based on a DCF model.

Sibanye proved that the sale process was sufficiently reliable to make the deal price a persuasive indicator of fair value. Although Sibanye argued for a deduction from the deal price to account for value arising from the Merger, Sibanye failed to prove that an adjustment was warranted.

The parties engaged in lengthy debate over whether Stillwater's adjusted trading price could provide a persuasive indicator of fair value. The reliability of the adjusted trading price depended on the reliability of the unaffected trading price, and both sides engaged experts who conducted analyses and offered opinions about the attributes of the market for Stillwater's common stock. The evidence demonstrated that Stillwater's trading price could provide a persuasive indicator of value, but that it was a less persuasive indicator than the deal price. This decision therefore does not use a trading price metric.

Neither side proved that its DCF valuation provided a persuasive indicator of fair value. The experts disagreed over too many inputs, and the resulting valuation swings were too great, for this decision to rely on a model when a market-tested indicator is available.

This decision concludes that the deal price is the most persuasive indicator of fair value. Relying on any of the other valuation metrics would introduce error. The fair value of the Stillwater on the valuation date was therefore $18.00 per share.

I. FACTUAL BACKGROUND

The parties generated an extensive evidentiary record. They commendably reached agreement on 283 stipulations of fact. During four days of trial, they introduced 909 exhibits and lodged twenty-one depositions in evidence. Three fact witnesses and seven expert witnesses testified live. What follows are the court's findings based on a preponderance of the evidence.[1]

A. The Company

***2** At the time of the Merger, Stillwater was a Delaware corporation engaged in the business of extracting, processing, smelting, and refining minerals from an orebody known as the J-M Reef. Located in in the western United States, the J-M Reef contains deposits of palladium, platinum, and rhodium, which are known in the mining industry as "platinum group metals" or "PGMs." These metals are rare, and the J-M Reef is the only PGM asset in the United States. The other principal sources of PGMs are located in South Africa, Russia, and Zimbabwe**,** which present significantly greater political risk.

Stillwater was headquartered in Littleton, Colorado, and its common stock traded on the New York Stock Exchange under the symbol "SWC." Stillwater's trading price was heavily influenced by commodity prices for palladium and, to a lesser degree, platinum.

At the time of the Merger, Stillwater's operations consisted of two producing mines in south central Montana: the Stillwater Mine and the East Boulder Mine. Stillwater's other assets were development projects or exploratory properties that were not yet generating revenue.

At the time of the Merger, Stillwater's two development projects were Blitz and Lower East Boulder. Blitz expanded the Stillwater Mine eastward. Lower East Boulder was a contemplated expansion of the East Boulder mine. Stillwater's two exploratory properties in the J-M Reef were Iron Creek and the Boulder Extension. Outside of the J-M Reef, Stillwater owned two other exploratory properties: (i) Altar, a copper-gold-porphyry deposit in the San Juan province of Argentina, and (ii) Marathon, a copper-PGM deposit in Ontario, Canada.

At the time of the Merger, Michael "Mick" McMullen served as Stillwater's President and CEO and as a member of its board of directors (the "Board"). The other six members of the Board were independent, outside directors:

- George Bee was a mining engineer who had held senior management positions or served on the boards of other mining companies.

- Patrice Merrin had served as an executive or director for numerous companies and was a director of Glencore plc, a multi-national mining firm. Merrin chaired the Board's Corporate Governance and Nominating Committee.

- Peter O'Hagan had worked at Goldman Sachs for nearly twenty-three years, including as co-head of its global commodities business.

- Michael Parrett was a Chartered Professional Accountant who had served in senior management positions and as a director for other mining companies.

- Brian Schweitzer had served as Governor of Montana. He was Chairman of the Board.

- Gary Sugar had spent thirty-two years at RBC Capital Markets, where he specialized in the mining sector. He served on the boards of other mining companies.

B. McMullen Convinces The Board To Build A Mid-Cap Mining Company.

McMullen was hired in December 2013 as a "turnaround CEO." McMullen Tr. 814–16; *see* Schweitzer Tr. 170. By early 2015, McMullen had refocused Stillwater's operations, cut costs, and generally turned the Company around. At this point, McMullen believed that market conditions favored the creation of a mid-cap mining company. He thought Stillwater could achieve this outcome either by growing through acquisitions or by combining with another industry player through a merger of equals.

During a meeting of the Board in June 2015, McMullen gave a lengthy presentation on Company strategy that devoted twenty-six slides to various alternatives. *See* JX 44 at '848 to '874. McMullen's presentation discussed means of increasing earnings, increasing the trading multiple, and optimizing the capital structure, and then turned to the pros and cons of selling some or all of the business. The presentation was particularly negative about the prospect of a sale. *See id.* at '866 to '868. In another presentation, McMullen devoted over forty slides to discussing candidates for acquisitions or mergers of equals. *See id.* at '929 to '970.

***3** In addition to his own presentation, McMullen provided the Board with presentations from three investment banks. McMullen had a close relationship Dan Vujcic, then an investment banker with Jefferies Financial Group, Inc., and the Jefferies presentation was the most detailed. It analyzed an acquisition of another base metals company, focusing on Sandfire Resources NL, Western Areas Ltd., and Panoramic Resources Ltd. It also analyzed the possible acquisition of a downstream company, a possible spinoff of Stillwater's processing and trading business, and the option of maintaining the status quo. *See id.* at '014 to '080. A presentation from BMO Capital Markets was more of a high-level pitch book, but it identified selected acquisition opportunities. *See id.* at '081 to '183. A presentation from Nomura Holdings, Inc. discussed alternatives for refinancing Stillwater's convertible bonds. *See* JX 44 at '164 to '182.

Sibanye has argued that this meeting marked the start of the Board's careful and thoughtful consideration of a sale of the Company, but the purpose of the meeting was not to prepare the Board for a sale. McMullen hoped to convince the Board to back him in creating a mid-cap mining company.[2] The Board, however, resisted, recalling unsuccessful acquisitions that had necessitated hiring a turnaround CEO in the first place. During the June 2015 meeting, the Board did not provide McMullen with a mandate to pursue any strategic options. *See* JX 43.

After the June 2015 meeting, McMullen kept looking for opportunities to build a mid-cap mining company. During the second half of 2015, McMullen worked with Jefferies, BMO, and Citigroup to identify acquisition targets and merger-of-equals candidates.[3] McMullen was focused on an acquisition, particularly "something not in the PGM space to diversify risk." JX 59.

During a meeting of the Board in October 2015, McMullen gave another presentation on the Company's strategy. *See* JX 61 at '102 to '127. He highlighted the risks Stillwater faced because of its dependence on palladium, which was used principally in catalytic converters. His presentation discussed the disruptive threat posed by electric cars, which could displace gasoline-powered cars and render catalytic converters obsolete. *See id.* at '105 ("Know Your Enemy —Electric Cars"). He recommended making a diversifying acquisition from which Stillwater would "emerge as a multi mine, multi commodity and multi jurisdiction mid cap miner with a bullet proof balance sheet." *Id.* at '127. He then reviewed six possible candidates: Sandfire, Western Areas, Panoramic, Northern Star Resources Ltd., Imperial Metals, and Hecla Mining Co. *See id.* at '128 to '179. He also circulated a presentation from Jefferies that discussed an acquisition of Sandfire. *See id.* at '249 to '292. During the weeks after the meeting, Jefferies provided McMullen with more detailed analyses of a deal with Northern Star, a large gold producer in Australia. *See* JX 67; JX 68.

***4** In December 2015, McMullen and a team from Stillwater visited the mining operations of Northern Star, where McMullen had a close relationship with senior management. During the visit, McMullen met with the CEO and CFO of Northern Star and discussed a potential merger of equals. *See* PTO ¶ 145; JX 73 at '867; *see also* JX 61 at '282 to '286; JX 67. At this point in time, a merger of equals with Northern Star was McMullen's top choice among Stillwater's strategic options.

During meeting of the Board in January 2016, McMullen gave another presentation on the Company's strategy. *See* JX 86 at '002 to '040. As with the meetings in June and October 2015, his goal was to convince the Board to authorize him to build Stillwater into a mid-cap metals company. *See* JX 78 (McMullen discussing his desire to "come away from [the January] board meeting with a clear mandate"). McMullen recommended a merger of equals with Northern Star as the best option, telling the Board that the transaction "would make a very strong mid cap precious metals miner." JX 86 at '038. If Northern Star would not engage, then he recommended acquiring Sandfire or Western Areas. *See id.* at '039. He also identified some smaller acquisitions that "should be pursued independently" and "[r]egardless of whether Stillwater completes one of the larger deals." *Id.* at '040. Later in the meeting, he provided additional information about the proposed M&A strategy and further detail about Northern Star, Sandfire, Western Areas, Panoramic, Hecla, and Imperial. *See id.* at "320 to '367. McMullen also distributed a presentation from Jefferies that analyzed mergers with Northern Star and Western Areas. *See id.* at '275 to '319

At the conclusion of the January 2016 meeting, the Board gave management a mandate, but it was broad and vague. According to the minutes, "[t]he Board provided management with a sense of the Board for management to continue to pursue the options as discussed, but to return to the Board for any final decision." JX 90. During this litigation, Sibanye has argued that this mandate authorized management to pursue a sale of the Company, but that is not accurate.[4] McMullen put it best when he told a banker at Blackstone that he had "finally convinced the Stillwater board to go off and buy some things." JX 93 at '628; *see* Schweitzer Tr. 187.

C. The Company's Stock Price

While McMullen was trying to convince the Board to let him "buy some things," Stillwater's stock price was falling. The decline began in June 2016 and continued steadily through December. Over the course of this six month period, Stillwater's stock price fell by over 40%, dropping from $14.46 per share on June 1 to $8.57 per share on December 31. The market drop did not reflect any problems with Stillwater's operations. Instead, it reflected a decline in the spot price of palladium, which fell by 27% from $773.70 per ounce on June 1 to $562.98 per ounce on December 31. PTO Exs. A, B.

During the Board meeting in January 2016, McMullen had told the Board that "[d]espite our stock being down 40%, we still have options open to us today." JX 86 at '012. But during the weeks following the January 2016 meeting, the stock price fell further. On January 19, it closed at $5.29 per share, down 38% from its closing price of $8.57 per share on December 31. The drop corresponded with further declines in the spot price of palladium, which closed on January 19 at $494.83 per ounce, down another 12% from its close of $562.98 per ounce on December 31.

***5** The Company's dismal stock performance caused McMullen to conclude that Stillwater did not have a currency that it could use for either an acquisition or a merger of equals. JX 93 at '628 ("[U]nfortunately the stock price has collapsed in the last 2 weeks and I don't think Stillwater has the currency to do anything anymore. Ce [sic] la vie."); *see* McMullen Tr. 826; JX 97 at '308 to '310, '313. He felt Stillwater had missed its opportunity to expand and was now just an "an option play on the P[alladium] price." JX 93 at '628; *see* JX 97 at '313

At this point, McMullen told a banker at Blackstone that "[s]itting around for one or two years waiting for the price to recover" was "not my idea of a job." McMullen Tr. 828; JX 93 at '628. McMullen did not view himself as an "operational CEO." McMullen Tr. 814–16. He thought he "would become bored." McMullen Tr. 828. With his contract set to expire at the end of the year, McMullen began thinking about what he would do next, including the possibility of building a mining portfolio company for Blackstone. *See* McMullen Tr. 828; JX 93 at '627 to '628.

D. Sibanye Contacts McMullen.

On January 30, 2016, Sibanye reached out through BMO to arrange a meeting between McMullen and Sibanye's CEO, Neal Froneman. Without telling the Board, McMullen accepted.

The meeting took place at an industry conference on March 1, 2016. PTO ¶ 161. When Froneman broached the subject of buying Stillwater, McMullen was receptive. He asked Froneman to provide "an informal proposal" in writing that included "an idea of valuation" and "transaction structure." JX 109 at '976; *see* PTO ¶ 164. Froneman had the impression that a deal "was doable if we got the valuation right." JX 109 at '976.

After the meeting, Froneman asked McMullen for "specific guidance" about what would be acceptable. JX 110. McMullen indicated that Sibanye's offer should include "a large cash component." JX 113 at '175. He also told Froneman during these early discussions that an acceptable transaction should be priced at a premium of 30% over Stillwater's thirty-day volume-weighted average price ("VWAP"). Stewart Dep. 39; *see also* JX 162 at '283. Froneman agreed in principle to this pricing metric, and he began organizing a team to visit Stillwater's mines. *See* JX 113 at '174 to '175. Froneman asked to enter into a confidentiality agreement to facilitate diligence, but McMullen rejected the request, commenting that he wanted "to see some form of indicative, non-binding and highly confidential terms of a transaction before we go too far down the path." *Id.* at '174.

McMullen took all of these actions without involving the Board. Indeed, he did not even inform the Board about Sibanye's approach. *See* Schweitzer Tr. 189–92; Wadman Tr. 657. Instead, on March 25, 2016, he agreed to extend his employment for an additional two years. JX 114 § 4.1. His original employment agreement had been scheduled to terminate on December 31, 2016, and the Board had expected that because McMullen was a short-term, turnaround CEO, he would not stay beyond that date. Wadman Tr. 670–71; *see* Wadman Dep. at 341; Schweitzer Tr. 170, 193. But with acquisition talks in the offing, McMullen agreed to a new deal. *See* JX 114.

The new employment agreement permitted McMullen to serve concurrently as a director of Nevada Iron Limited and New Chris Minerals Limited, which later became GT Gold Corp. *See* JX 114 § 3.1, Ex. A. During 2016, McMullen did more than serve on the boards of these companies. He became Executive Chairman and CEO of Nevada Iron, and he served as Non-Executive Chairman and President of New Chris. *See* McMullen Tr. 863–64; McMullen Dep. 45, 553; JX 93 at '628. Both companies were Australian resource firms whose equity comprised a significant portion of McMullen's net worth. JX 157 at '315; *see* McMullen Tr. 709, 863–64. Over the next year, while McMullen was busy selling the Company, he also caused Nevada Iron and New Chris to engage in transformative transactions.[5]

***6** In May 2016, the Board held its next regular meeting. In connection with that meeting, McMullen did not inform the Board about Sibanye's approach or his discussions with Sibanye.[6]

E. Sibanye Submits An Indication Of Interest.

During the first week of June 2016, executives from both Sibanye and Northern Star toured the Company's mines. PTO ¶¶ 171–72. Sibanye toured as part of their exploration of a potential acquisition of the Company. Northern Star toured separately, ostensibly as part of a mutual benchmarking exercise but really in connection with a potential merger of equals. McMullen and the Company's CFO, Christopher Bateman, led Sibanye and Northern Star on separate tours and ensured that neither saw one another. McMullen claimed that despite keeping the two teams separate, each knew that the other was on site because McMullen and Bateman would alternate between the tours and McMullen had them both sign the visitors log. McMullen said he did this as a clever way to create competition between the firms. *See* McMullen Tr. 726–27.

After the visits, McMullen believed that a deal with Sibanye was more likely than with Northern Star. *See* JX 140 at '048; JX 142. Toward the end of June 2016, Northern Star reported that they were primarily interested in a joint venture involving Blitz. JX 145 at '845. That possibility did not interest McMullen. *Id.* Meanwhile, McMullen pushed Sibanye to provide an indication of interest in advance of the Board's next meeting, which was scheduled for July 28, 2016.[7]

Sibanye began working with Citigroup to develop its bid. Two of the Citigroup bankers had previously advised McMullen and Bateman about the Company's alternatives. As part of its advice, Citigroup had recommended against a sale of the Company because of the limited universe of potential buyers. *See* JX 32 at '829; *cf.* JX 42 at '422.

On July 21, 2016, Sibanye provided McMullen with a non-binding indication of interest to acquire Stillwater at $15.75 per share in cash, which valued the Company at $1.9 billion. PTO ¶ 177; JX 165. The letter described that price as reflecting "a 30% premium to Stillwater's volume-weighted average share price [(VWAP)] of US$12.12 over the last 20 trading days prior to 20 July 2016." JX 165 at '880; *see* PTO ¶ 178.

As suggested by Sibanye's offer, Stillwater's stock price had mostly recovered, reflecting a recovery in the price of palladium. At the beginning of July 2016, the stock closed at $12.25 per share, up 132% from its low of $5.29 in January. During that same period, the palladium spot price had increased 22% to $605.63 per ounce. PTO Exs. A, B. Despite the stock's performance, McMullen did not revisit potential acquisitions or a merger of equals. He was now focused on selling the Company. *See* JX 156 (email from Vujcic to McMullen stating, "[W]e'll make sure the company gets sold. Don't worry about that.").

F. McMullen Presents The Indication Of Interest To The Board.

***7** On July 27 and 28, 2016, the Board held a regularly scheduled meeting. At the end of the two-day meeting, the directors held a forty-five minute "executive session" with McMullen, who distributed and walked through a presentation titled "Business Development Update." JX 151 at '551; *see* Schweitzer Tr. 193; JX 526 at '377; Wadman Tr. 657–64. The presentation compared the Company's recent performance to various potential transaction partners, then described the pros and cons of transactions with Northern Star and Sibanye. After summarizing the terms of Sibanye's expression of interest, the presentation described the premium as "within the right range for shareholder value" and "broadly within the range of mining transactions." JX 151 at '568. McMullen gave his "strong recommendation ... to engage with Sibanye and attempt to conclude [due diligence] as quickly as possible (likely to take 2 months) and achieve a higher price." *Id.* McMullen added that he would "look to engage with other potential bidders on a low key and informal basis to determine if there are alternative bidders." *Id.* He warned: "The list of other potential bidders is short given the commodity, size of transaction and whether [Stillwater's] shareholders would want their paper. The process of determining if there are alternatives will not be a long process." *Id.* He also told the directors that "[t]he market appears to be open for people to carry out M+A, and asset values have risen to a level where you want to be a seller rather than a buyer." *Id.*

Brent Wadman, the Company's General Counsel, became concerned about what took place during the July meeting. He had not been asked to stay for the executive session and was not given access to McMullen's presentation. *See* JX 526 at '377; Wadman Tr. 657–64. He suspected that McMullen was running a sale process on his own, without Board oversight, and potentially using it as a means of exiting from the Company. Wadman believed that as General Counsel, he should have been involved. After the July meeting, Wadman asked McMullen to include him in the planning process. McMullen rebuffed him, saying that Wadman would be "brought in at a later date" and "offer[ing] no other information." JX 526 at '377; Wadman Tr. 658.

After the July meeting, McMullen told Sibanye to submit its list of due diligence questions so the Company could start pulling the information together. He told Sibanye to direct all inquiries to himself or Bateman. *See* PTO ¶ 181; JX 183.

G. McMullen Remains Committed To Sibanye.

On August 9, 2016, Stillwater and Sibanye entered into a confidentiality agreement, and Sibanye gained access to the data room. PTO ¶ 183; JX 525 at 26; *see also* JX 194. On August 10, the Board met again. *See* JX 193. McMullen testified that at this meeting, the Board instructed him "to go out and ... to sign the NDAs with the likes of Sibanye, and then, also, ... to get as much interest as possible." McMullen Tr. 835.

Rather than working closely with an investment bank to develop a process designed to generate "as much interest as possible," McMullen pressed forward with Sibanye. He interacted with some investment banks, but in a haphazard and unstructured way. For example, back in July 2016, a Macquarie banker had asked McMullen to meet for a market update. *See* JX 167. On August 10, the same day that the Board met, Macquarie proposed a formal engagement. Five days later, McMullen told Macquarie that it was "a bit early for us I think to be signing anyone up." JX 196.

One week after the Board meeting, on August 18, 2016, McMullen and Bateman met with Bank of America Merrill Lynch ("BAML"), who had arranged the meeting to pitch Stillwater on possible mergers of equals. *See* JX 199; *see also* JX 163; JX 190. The BAML presentation materials did not discuss a sale of the Company or mention Sibanye, and McMullen and Bateman did not use the meeting to identify other possible acquirers. Instead, the BAML bankers got "the sense ... that a sale was a possibility," and so they decided on their own to "pivot[ ] to focus more, as time went on, on that." Hunt Dep. 35.

Acting on their own, the BAML bankers developed a list of fifteen possible acquirers whom they approached independently, pitching a potential acquisition of Stillwater as "a banker idea." JX 206 at '360. The record does not reveal exactly how many companies BAML contacted, what the BAML bankers said, or how seriously the companies took the pitch. Because BAML did not know that Stillwater was in discussions with Sibanye, they reached out to Sibanye as part of these efforts, ironically describing that a deal for Stillwater would be "[a] little pricey." JX 207 at '093. In the end, five companies expressed interest: Sibanye; Hecla; Coeur Mining, Inc.; CITIC Resources Holdings Limited, and Anemka Resources Ltd. *See* JX 211; JX 213; JX 214; JX 217 at '588 to '591.

***8** Having made these calls on their own, the BAML bankers held a follow-up meeting with McMullen and Bateman on September 7, 2016. The pitch book identified the parties contacted and expressing interest. It then described three types of sale processes Stillwater could pursue: a "proprietary process" with a single bidder, a targeted auction involving a limited number of likely buyers, or a broad auction involving outreach to many potentially interested parties. JX 217 at '603. BAML recommended against the proprietary process because the absence of competition would minimize Stillwater's negotiating leverage. BAML also recommended against a broad auction, given the existence of a "narrow list of most likely buyers." *Id.* This left a targeted auction as the recommended route.

The pitch book described an illustrative timeline for a sale process. BAML recommended allocating the rest of September 2016 to contact potential buyers. During October and early November, the Company would enter into confidentiality agreements, respond to diligence requests, and then receive and evaluate initial indications of interest. From mid-November through early January 2017, the Company would host site visits, provide additional diligence, and then solicit and receive final bids. JX 217 at '605.

Nothing formal came out of the September 7 meeting. McMullen and Bateman did not instruct BAML to proceed, nor did they take BAML's recommendation to the Board.

Instead, McMullen and Bateman asked BAML and Vujcic, the investment banker who had been with Jefferies and was now working on his own, to arrange meetings with potential suitors at an industry conference during the week of September 20, 2016. BAML arranged a meeting with Coeur, and McMullen arranged a meeting with Hecla. *See* JX 220 at '609; JX 222; JX 224; PTO ¶ 190–91. Vujcic set up meetings with Kinross Gold Corporation and Gold Fields Limited, neither of whom had expressed interest. During each meeting, McMullen conducted what he called a "soft sound" regarding potential interest in buying the Company. PTO ¶ 192; *see id.* ¶¶ 193–97.

On the last night of the conference, McMullen had dinner with Froneman. McMullen told him that he "remain[ed] committed" to a deal with Sibanye and that "no one else is in the data room," but cautioned that he was "being flooded by investment banks" pitching ideas for deals with gold-mining companies. JX 231 at '711.

After the conference, BAML sent McMullen "a fairly detailed timeline" for a more compressed sale process. JX 225 at '629. The new timeline contemplated the process starting during the last week of September and ending during the first week of December. *See id.* at '632. BAML anticipated site visits taking place during November as part of the due diligence phase, but McMullen told BAML that the site visits needed to take place earlier in the process before parties sent their initial indications of interest: "Unless people get to site, they can't appreciate the scale of it and will not be putting their best foot forward in the indicative, non binding offers." JX 229 at '603. BAML revised the timeline, noting that they were "putting [it] together in a vacuum of info on what's taken place." *Id.* At this point, BAML had not been retained and did not yet know about Sibanye's bid. They only knew about their own, independent efforts to solicit interest.

H. The Board Decides Not To Form A Special Committee.

In anticipation of a board meeting on October 3, 2016, Wadman circulated a "list of potential buyers" to the directors. JX 234. The list identified eighteen companies and the status of Stillwater's discussions with each. According to the list, Sibanye had completed its first phase of diligence and was working with Citigroup to secure financing. Hecla and Coeur had expressed interest, entered into non-disclosure agreements ("NDAs"), and scheduled site visits. Northern Star was listed as "interested but very foucssed [sic] on a gold deal." *Id.* at '630. Six other companies were described as "[p]otentially interested" or as having "some interest," including Anglo American Platinum Limited ("Amplats"). *Id.* Six candidates were described as "[u]nlikely" and two as "not interested." *Id.* The list omitted CITIC and Anemka, even though both had expressed interest when BAML called with its "banker's idea."

***9** The list identified a representative who was responsible for interacting with each company. Evidencing the uncoordinated, unstructured nature of the Company's process, the list identified a hodgepodge of names. Vujcic was the contact for eight companies. BAML was the contact for four companies. Jefferies was the contact for another three. Macquarie was the contact for one company. An executive at New Chris, the company where McMullen served as Non-Executive Chairman and President, was listed as the contact for another company. No one had been formally engaged. Two companies had no contact listed.

During the meeting, McMullen reported on the Company's outreach to the various parties. After his presentation, the directors instructed McMullen to obtain formal proposals from investment banks for a sell-side engagement. The Board also instructed McMullen to create a cash flow model that could be used to value the Company. *See* JX 246 at '308 to '309.

Ever since the July 2016 meeting, Wadman had been concerned that McMullen was running a sale process to facilitate his exit from the Company. After McMullen rebuffed him, Wadman had shared his concerns privately with Schweitzer and Merrin. *See* Wadman Tr. 664–65; Schweitzer Tr. 157–58, 194. Neither took action.

During the October meeting, Wadman presented his concerns to the full Board and recommended the formation of a special committee to oversee the sale process. Lucy Stark of Holland & Hart LLP, the Company's longstanding outside counsel, disagreed and advised the Board that she did not believe any conflict existed that warranted the creation of a special committee. JX 246 at '309; *see* Schweitzer Tr. 159.

The directors other than McMullen then met in executive session. Schweitzer reported to Wadman that the Board had decided to form a special committee, and Wadman drafted a set of minutes memorializing the decision. *See* JX 238 at '245; Wadman Dep. 134–35; *see also* Schweitzer Tr. 205–06. But in the meantime, McMullen learned of the decision from two other directors. McMullen Tr. 745–47. The final minutes described the outcome of the executive session as follows:

> - No decision was made to pursue or not pursue a potential strategic transaction at this time. The Board further discussed the potential for a committee and agreed that, should the need arise, the committee would consist of the entire Board with the exception of the CEO. It also discussed timing and the potential engagement of an investment banking firm to assist in the assessment process.

JX 246 at '310.

I. McMullen Continues To Focus on Sibyane.

On October 15, 2016, almost two weeks after the Board directed McMullen to solicit terms from investment bankers, McMullen finally drafted and sent out an email asking bankers to respond "by no later than COB Wednesday Oct 19 2016." JX 279 at '867. Other than Macquarie, the record does not reflect what bankers received the email or whom McMullen solicited, but Macquarie, BMO, BAML, and Jefferies submitted proposals.

On October 17, 2016, Froneman told McMullen that Sibanye's offer of a "30% premium to VWAP remained unchanged" and that Sibanye's board of directors unanimously supported the transaction. JX 281 at '425. McMullen responded that he remained fully supportive of the deal. He also shared that Stillwater did not yet have a banker, telling Froneman that he had started reaching out to investment banks on a no-names basis. Demonstrating his commitment to the deal, McMullen told Froneman that he would be happy to have Stillwater's legal advisors start putting together an initial sales agreement. *Id.*

The Board met again on October 26 and 27, 2016. After reviewing the proposals from the investment banks, the Board narrowed the list to BMO and BAML. JX 295 at '790. Vujcic, whom McMullen regarded as his "in house banker," summarized the state of the Company's outreach. JX 293 at '521. *Compare* JX 262 at '485, *with* JX 234 at '630. He reported that third parties exhibited a general "[l]ack of knowledge around the significant improvement in operations and general performance," and he reported that a number of parties were either focused on other deals, not considering M&A because of prior bad acquisitions, or not considering PGM companies because of negative associations with risky jurisdictions like South Africa and Russia. JX 293 at '522. For the first time, the Board authorized management "to engage in discussions with strategic buyers, financial buyers or any other party interested in consummating a potential strategic transaction with the [Company]." JX 296 at '791.

***10** After the meeting, McMullen scheduled a second site visit for Sibanye and discussed the "timelines to and post announcement" with Froneman. JX 315 at '291 to '292; *see* PTO ¶ 214. Sibanye convinced McMullen that they needed to announce the deal by mid-December 2016. *See* JX 281 at '425; JX 282 at '776; *see also* PTO ¶ 241.

J. BAML Begins An Abbreviated Pre-Signing Market Check.

On November 7, 2016, the Board formally retained BAML. PTO ¶¶ 216–17; *see* JX 323 at '371. The Board also decided to hire "additional legal counsel with substantial experience in advising Delaware publicly traded companies in respect of potential strategic transactions." JX 323 at '372. Four days later, the Board retained Jones Day. PTO ¶ 232.

On November 8, 2016, Bateman sent BAML a package of information that included Sibanye's indication of interest from July, the non-disclosure agreements with Hecla and Coeur, a cash flow model, and instructions for accessing the data room. *See* JX 325; JX 326; JX 327; JX 328; JX 329. The next day, BAML sent management a slide deck titled "M&A Process Considerations." JX 331 at '277.

BAML understood from management that Sibanye wanted to sign up a deal in December 2016, so BAML proposed to complete its outreach to a list of parties in just two days. That timeframe was drastically shorter than the four weeks that BAML had recommended in September 2016. Anyone who expressed interest would have three weeks to conduct diligence and submit an indication of interest, just half of the six weeks that BAML had recommended in September. At that point, the Board would decide whether to proceed with Sibanye or engage with the other bidders. PTO ¶ 226; *see* JX 331 at '280. Even though McMullen had previously told BAML that it was critical for potential bidders to visit the Company's mines before making an initial indication of interest, BAML's compressed timeline did not contemplate that step.

BAML's presentation identified twenty-eight third parties divided into four categories:

- "Interested Parties"—Sibanye, Coeur, and Hecla.
- "Possibly Interested Parties"—Gold Fields, Independence Group NL, Kinross, MMG Limited, Rio Tinto, and South32 Limited.
- "Additional Parties To Contact"—Alamos Gold Inc., Anemka, CITIC, Fresnillo plc, Goldcorp Inc., IAMGOLD Corporation, Impala Platinum Holdings Limited, New Gold Inc., Northam Platinum Limited, Pan American Silver Corporation, X2 Resources, and Yamana Gold Inc.
- "Not Interested"—Northern Star, Amplats, Eldorado Gold Corporation, Evolution Mining Limited, Newcrest Mining Limited, Newmont Mining Corporation, and OZ Minerals.

JX 331 at '279. Anemka and CITIC were listed as "Additional Parties to Contact," even though they had expressed interest during BAML's earlier independent outreach. OceanaGold Corporation and Boliden AB, whom Vujcic had included in his review of the Company's outreach, were omitted from BAML's list.

BAML's presentation included scripts for its bankers to use when making their calls. For "Possibly Interested Parties," the script stated:

- Announce participants and remind parties of confidentiality;
- BofA Merrill Lynch has been retained by Stillwater Mining Company to explore strategic alternatives;
- We understand you have had some discussions previously with our client;
- We would like to further clarify your potential interest in Stillwater as the process moves forward;

***11** • Do you have any interest to learn more?

- If so, we would suggest you sign an NDA for access to diligence on the company.

PTO ¶ 225 (formatting added); JX 331 at '281. For the "Additional Parties To Contact," the script omitted Stillwater's name and asked generally about interest in the PGM sector.

- Announce participants and remind parties of confidentiality;
- We are calling to gauge your potential interest in a situation in the PGM sector;
- Our client is a leading player and low cost producer of PGMs and substantial organic production growth;
- Do you have any interest to learn more?
- If yes, disclose that our client is Stillwater and suggest they sign an NDA for access to diligence.

PTO ¶ 224 (formatting added); JX 331 at '281. For Hecla and Coeur, BAML planned to skip the call and send instructions for submitting an indication of interest by November 23. PTO ¶ 231; JX 336; JX 337.

Because of the expedited timeline, BAML decided not to contact companies in the "Not Interested" category, even though many of those companies had said they were not interested when BAML previously called them with "a banker idea." The response could have been different with a formal mandate. BAML's script for "Additional Parties to Contact" was not likely to generate interest because it did not say anything more than "a situation in the PGM sector." Because almost every other PGM company was located in a politically unstable jurisdiction, additional parties were less likely to have interest without a signal that the company involved was Stillwater. And because Stillwater had been advertising its interest in acquisitions, there was no reason for the additional parties to think that the situation involved Stillwater. *See* JX 124 at '074.

Using its scripts, BAML contacted five of the six possibly interested parties, missing Gold Fields. *See* JX 351. BAML contacted eight of the twelve additional parties, missing Alamos, Goldcorp, New Gold, and Yamana Gold. *See* PTO ¶ 230; JX 338; JX 339; JX 340; JX 341; JX 342. BAML contacted Northern Star, even though they were listed as not interested. *See* JX 351 at '953.

Three of the companies expressed interest: Anemka, Northern Star, and X2. BAML sent a confidentiality agreement and an invitation to submit a bid by November 29 to Anemka and Northern Star. BAML sent only a confidentiality agreement to X2, which quickly retracted its interest. *See* JX 395 at '412; *see also* JX 359 at '413.

Sibanye learned about BAML's market check from Bateman. JX 332 at '969. Sibanye perceived that a compressed timeline was its "only real advantage" in the process. *Id.*

K. The Abbreviated Pre-Signing Market Check Continues.

On November 17, 2016, the Board met again, with Jones Day attending for the first time. BAML and McMullen updated the Board on the outreach and "the Board directed management to continue the strategic assessment process."[8] Sibanye had already sent a draft merger agreement to Jones Day.

***12** On November 18, 2016, BAML suggested contacting Norilsk Nickel, a Russian mining company that had owned a majority stake in the Company between 2003 and 2010. JX 367. McMullen decided against it. *See* McMullen Dep. 476.

On November 20, 2016, the CFO of Northern Star informed McMullen that they were not interested in buying Stillwater but remained interested in a merger of equals. Northern Star asked McMullen to send a proposal. PTO ¶ 242.

On November 22, 2016, the CEO of Independence informed McMullen that they were not interested in buying Stillwater but were interested in a merger of equals. PTO ¶ 246. Independence asked to sign a confidentiality agreement and perform diligence, explaining that they had trouble reaching BAML. Independence did not receive a confidentiality agreement until November 25. *See* JX 403; JX 405.

The Board met again on the afternoon of November 23, 2016. McMullen reported that he had told Sibanye that its July proposal of $15.75 per share was not sufficient. He also reported that Sibanye needed the transaction to be "announced by the second week in December"; otherwise, Sibanye would need to delay the deal until the following year so that it could obtain stockholder approval to raise the capital needed to fund the Merger. JX 395 at '411. McMullen viewed a December signing as "ambitious given that ... the Company's assessment process with other potential parties was ongoing and would need to be concluded prior to proceeding with a transaction with Sibanye." *Id.*

By the time of the board meeting, twenty-four parties had received some type of formal or informal contact from BAML or Stillwater management. Four parties—Sibanye, Hela, Coeur, and Anemka—had signed NDAs and accessed the data room. Four parties—Sibanye, Hela, Coeur, and Northern Star—had conducted site visits. Two parties—Coeur and Anemka—had notified BAML that they would not proceed further. PTO ¶ 235; JX 393 at '868. Two other parties—Northern Star and Independence—had informed Stillwater that they were only interested in a merger of equals. Hecla had reported that it needed to find a partner and had asked Stillwater to extend its bid deadline from November 23 to November 30. PTO ¶ 247; JX 383. The Board extended Hecla's deadline to November 28. JX 395 at '413. By comparison, the Board had given Sibanye until November 30 to update its expression of interest from July. *See* JX 359 at '414.

After receiving these updates, the Board met in executive session, and the minutes reflected for the first time that McMullen did not participate. *See* JX 395 at '413. The Board instructed BAML to evaluate a merger of equals as a potential alternative. *Id.* When McMullen learned of the decision, he was skeptical, believing that a merger of equals could not compete with "a circa $18/share [ ]all cash offer from S[ibanye]." JX 406 at '376. He shared his negative opinion with one of the directors, who replied that a merger of equals was actionable and needed to be explored as an alternative to Sibanye. *See* JX 401.

McMullen and BAML worked together to update the presentation that McMullen had given the Board in January 2016 on a potential merger of equals. *See* JX 384; JX 396. McMullen ranked the Company's options as follows: 1) Sibanye's acquisition; 2) a merger of equals with Northern Star; and 3) do nothing or a merger of equals with Independence. JX 396 at '707.

***13** After the board meeting on November 23, 2016, BAML followed up with Hecla to solicit a specific indication of interest. *See* JX 394 at '214. Hecla did not respond, and the Company treated Hecla as having dropped out of the process.

On November 29, 2016, Northam asked to be included in the process. JX 414. BAML sent Northam a confidentiality agreement and invited them to submit a bid by December 7. PTO ¶ 258; *see* JX 423; JX 424. That same day, Independence asked for an extension to the bid deadline since they were still negotiating the confidentiality agreement. JX 411. McMullen decided that meant that Independence was not interested.

L. Sibanye Revises Its Price.

As of November 20, 2016, Sibanye anticipated borrowing $2.5 billion to complete the Merger. Of this amount, $1.98 billion would be used to pay for the Company's stock, with the consideration priced at a 30% premium over the Company's thirty-day VWAP, just as McMullen and Froneman had agreed in March. *See* JX 378 at '979, '009, '016, '017. The additional $500 million would be used to pay off the Company's debt, fund change-of-control payments for management, and pay transaction fees.

But on November 30, 2016, Sibanye ran into problems. First, Sibanye realized that the Company's stock price had increased to a point where the pricing metric would cause the total purchase price to exceed Sibanye's financing. Using the 30% premium over the thirty-day VWAP, Sibanye would have to pay approximately $18.25 per share, an amount that would require Sibanye to supplement the transaction financing with cash on hand or from its revolving credit line. *See* JX 420 at '876.

Second, Sibanye realized that it had calculated the purchase price in its indication of interest using a *twenty-day* VWAP rather than a thirty-day VWAP. *Id.* at '874. The Sibanye team recognized that they had agreed in principle to a thirty-day VWAP, but when they sent their initial indication of interest, they used a twenty-day VWAP because the Company's stock had been in a declining trend, so the shorter period resulted in a lower price. *Id.* at '873.

Citigroup recommended pretending that Sibanye had never agreed to a pricing mechanism and had instead offered a fixed price. *Id.* The Sibanye team went along and disavowed all of the communications in which they had agreed in principle to a 30% premium over the thirty-day VWAP. *See* Stewart Dep. 147–48; PTO ¶¶ 243, 245; JX 397 at '448; JX 378 at '009, '016. Going forward, Sibanye would discuss price based on an indication of interest of $15.75 per share.

M. Stillwater Negotiates With Sibanye.

On December 1, 2016, the deal teams from the Company and Sibanye met in New York City. Sibanye proposed to acquire the Company for between $17.50 and $17.75 per share in cash. PTO ¶ 261.

On December 2, 2016, the Board met in New York City. *See* JX 432; JX 430. McMullen shared Sibanye's revised offer. The minutes do not reflect any discussion of Sibanye's departure from the prior agreement in principle on a 30% premium over the thirty-day VWAP or the fact that the agreed-upon pricing metric would have supported a price around $18.25 per share. Even though BAML had worried about Sibanye using precisely this tactic, and even though McMullen had assured BAML that Sibanye would stick to the agreed-upon pricing metric, *see* JX 343 at '740 to '741, no one appears to have mentioned the change to the Board. *See* JX 432 at '414.

***14** During the meeting, BAML presented its preliminary financial analysis of the Company. Using a discounted cash flow analysis, BAML valued the Company at between $10.78 and $14.14 per share. *Id.* at '416. That same day, the Company's stock closed at $15.17 per share. PTO Ex. A.

BAML also reviewed potential merger of equals transactions with Northern Star and Independence. JX 432 at '417. According to the minutes, the Board decided not to pursue either transaction because: (i) the lack of synergies; (ii) "the significant disparity in trading multiples"; (iii) "no merger-of-equals or similar transaction appeared to be available to the Company at this time"; (iv) "neither Northern Star nor Independence Mining had signed a confidentiality agreement"; and (v) "a substantial delay in the process to pursue such a possible transaction could result in the loss of a potential transaction with Sibanye." JX 432 at '417; *see* McMullen Tr. 769. At the time, Northern Star and Independence had both proposed a merger-of-equals transaction and both had signed confidentiality agreements. There was also a meaningful probability that the Sibanye transaction would slip into the following year.

During the meeting, the Board instructed management to seek a higher price from Sibanye. That evening, McMullen and Bateman had dinner with Richard Stewart, Sibanye's Executive Vice President of Business Development. PTO ¶ 265. After the dinner, Stewart emailed Froneman that "Mick's number is 18$+ and that he thinks he can get his board across the line on that." JX 434 at '426. Froneman, Stewart, and Citigroup discussed the limits of Sibanye's financing, which would support a bid up to $18.20 per share. A 30% premium on the twenty-day VWAP for the Company's common stock was $19.20 per share. *Id.* The group decided to bid $18.00 per share, observing that "if this is truly not good enough – they will come back but we need to be firm." JX 434 at '425.

On December 3, 2016, Stewart called McMullen and offered $18 per share. PTO ¶ 267. BAML had been expecting $19 per share. *See* JX 438.

On the evening of December 3, 2016, Bateman had "a very open discussion" with one of Sibanye's bankers from Citigroup, sharing information about the Board's internal dynamics, the Company's lack of other prospects, and his preferences for employment. *See* JX 444. The Citigroup banker reported on the conversation as follows:

> - 1. Value. Didn't push back, as knows we're at our limits. Said Mick will recommend our proposal to the Board, [that two directors] are "very commercial". [Schweitzer] is the one most focused on 30% premium to 20D VWAP. I reiterated that we've truly been talking about 30D VWAP internally and with [Stillwater], which he seems to understand.
>
> - ...
>
> - 3. MOE. He seemed quite dismissive of the MOE candidate, but said certain Board members are keen to not shut it down completely (I suspect more from a litigation perspective).
>
> - 4. Chris' Plans. Said he honestly hasn't given a lot of thought to what's next, and he's generally open minded about it. ... He could be open to staying with [Sibanye], but depends on the vision and the role. He would have no desire to be a divisional CFO, but potentially interested in an Americas Head position. ...

Id. Bateman participated in this discussion one day after Jones Day had advised the Board and senior management about the risk of conflicts during the negotiations. In response, Bateman and other members of management had represented to the Board that they had not had any discussions with Sibanye about their roles. *See* JX 432 at '418.

***15** On December 4, 2016, Stewart called McMullen and told him that $18.00 was Sibanye's best and final offer. PTO ¶ 270. After Bateman's dinner with the Citigroup banker, Sibanye knew it did not have to bid higher.

Later that afternoon, McMullen shared the offer with the Board. Fearing that the timeline might slip into 2017, the directors instructed management "to progress discussions with Sibanye" and to find out whether Northam remained interested. JX 440 at '742.

On December 5, 2016, BAML reported that it had not heard anything from Northam. JX 445. That same day, Froneman called McMullen to reiterate that $18.00 per share was the best Sibanye could do given their financing constraints. PTO ¶ 272.

N. McMullen Demands His Stock Awards.

On December 7, 2016, McMullen asked Sibanye to "put something into the merger agreement" about his 2017 stock awards. JX 451. According to McMullen, Sibanye had previously agreed to the following terms:

> - On Closing of the deal, the value of the awards would be converted to cash based on the metrics of the deal (share price etc) and the amount paid out as per the normal vesting schedule in cash, namely 1/3 of the RSU value at each of the end of 2017, 2018 and 2019, and all the PSU value is paid out at the end of 2019. If any employee leaves for Good Cause (fired or diminution of job role) then the RSU's accelerate in accordance with our plan docs, but the PSU amount is still paid out at the end of 2019.

Id. McMullen told Sibanye that the Compensation Committee had "decided that the 2015 and 2016 PSU's would vest at 150% for each series in the event of an $18 bid." *Id.*

O. The Board Approves The Merger.

On December 8, 2016, the Board met to consider the Merger Agreement and decide whether to proceed with the Merger. McMullen reported that Northam had withdrawn from the process. JX 454 at '744; *see* JX 459. By this point, BAML had interacted with fourteen parties since being formally retained. Five had signed NDAs and conducted diligence. Only Sibanye had made a bid.

BAML rendered its opinion that Sibanye's offer of $18 per share was fair. The consideration of $18 per share represented a 21% premium to the Company's then-current stock price, a 21% premium to the 20-day VWAP, and a 25% premium to the 30-day VWAP. JX 453 at '260. In its presentation, BAML valued the Company between $10.58 per share and $13.98 per share using a discounted cash flow analysis. *Id.* at '279 to '281.

The Merger Agreement contained a no-shop clause with a fiduciary out that permitted the Company to provide information to and negotiate with a third-party bidder if the bidder made an "Acquisition Proposal" that constituted or was reasonably likely to lead to a "Superior Proposal" *and* the Board concluded that its fiduciary duties required it. *See* JX 525 Annex A § 6.2.4. The Board had the right to change its recommendation in favor of the Merger if a competing bidder made a superior proposal *and* the Board concluded that its fiduciary duties required it. The Board did *not* have the right to terminate the Merger Agreement to pursue the superior proposal. The Company had to proceed through the stockholder meeting and only gained the right to terminate if the stockholders voted down the deal.

***16** If the Company exercised its right to terminate after a negative stockholder vote, then the Company was obligated to pay Sibanye a termination fee of $16.5 million plus reimbursement of Sibanye's expenses up to $10 million, for a total payment of $26.5 million. The total payment represented approximately 1.2% of equity value, with the termination-fee portion reflecting 0.76% of equity value. The Company had approximately $110 million more cash than debt, resulting in a slightly smaller enterprise value than equity value. The total payment represented approximately 1.3% of enterprise value.

The Board adopted the Merger Agreement and resolved to recommend that the Company's stockholders approve it. JX 454 at '746. On December 9, 2016, Sibanye and the Company announced the Merger. Sibanye's stock price dropped 18% from $8.20 per share to $6.96 per share.

The last day of unaffected trading in Stillwater's common stock was December 8, 2016. On that date, the Company's shares closed at $14.68, equating to a market capitalization of approximately $1.8 billion. The deal price represented a 22.6% premium over the unaffected trading price and a 24.4% premium over the 30-day VWAP. During the previous two years, Stillwater's stock price had never traded above $15.58, a level it reached on August 1, 2016.

P. Vujcic Gets Paid.

After the Merger was signed, McMullen sent Vujcic a retroactive consulting agreement to compensate him for assisting with the Merger. Vujcic had two comments. First, he wanted confirmation that he would "not be named in the proxy." JX 474 at '101. Second, he was disappointed with his compensation, stating:

> - I'm a little perplexed as to why you are being so aggressive on the comp, especially when you are exposed to a potentially large claim from Jefferies and when I feel I have been pretty fair all along in (a) not locking you in earlier (trusted your guidance on compensation in July) and (b) in making every effort leading up to the board meetings in late October to give you the comfort to reiterate that Sibanye were the only show in town.

Id. at '100.

The petitioners argue that Vujcic's statement that he made "every effort ... to give you comfort to reiterate that Sibanye were the only show in town" shows that McMullen and Vujcic had been trying to eliminate the competition for Sibanye. That is a conspiratorial reading, rather than a credible reading. Vujcic was attempting to justify receiving greater compensation by pointing to his efforts to solicit other potential bidders. He showed that Sibanye was "the only show in town" by engaging in outreach and demonstrating that no one else wanted to bid. The record does not support an inference that McMullen and Vujcic deceived the Board. *See also* McMullen Dep. 442–46.

McMullen and Vujcic agreed on a fixed fee of $20,000 per month beginning on October 24, 2016, plus a discretionary bonus of $100,000. JX 477. Vujcic's name and compensation arrangement did not appear in the proxy statement. *See* JX 525.

Q. Wadman's Noisy Withdrawal

In February 2017, McMullen and Bateman negotiated the terms of their post-closing employment with Sibanye. As part of those discussions, Sibanye agreed to treat the Merger as triggering McMullen and Bateman's change-of-control payments, without the need for a second trigger such as termination or a resignation for "Good Reason." None of the Company's other employees received this special treatment. For the other employees, the Merger was only the first trigger, and no change-in-control benefits would be paid absent a second trigger.

When McMullen reported on this agreement to the Board during a meeting on February 23, 2017, Wadman objected. He had been concerned since July 2016 that McMullen and Bateman had pursued a sale of the Company in their own interest and had used the deal to advantage themselves. He regarded their special deal on change-in-control benefits as "clearly self-dealing." JX 526 at '376. The Board did not address Wadman's concerns during the meeting.

***17** One month later, Wadman resigned. In his resignation letter, Wadman restated his concerns about how the deal process unfolded. He noted that after the board meeting on February 23, 2017, McMullen and Bateman "removed [me] from all legal conversations and decision-making" and "prohibited me from doing my job." *Id.* at '377 to '378. Quoting his employment agreement, Wadman resigned for "Good Reason" based on a "material diminution" to his "nature of responsibilities, or authority." *Id.*

Over the next several days, the Company's counsel negotiated a settlement with Wadman. On March 30, 2017, the Company released a Form 8-K, which stated:

> On March 29, 2017, Brent R. Wadman, our Vice President, Legal Affairs & Corporate Secretary, terminated employment. In connection therewith, we entered into an agreement with Mr. Wadman with respect to his separation pursuant to which we will pay him up to approximately $1.49 million. This amount includes the settlement of Mr. Wadman's outstanding equity awards, which will continue to vest in accordance with their terms, including in connection with the previously announced merger with Sibanye Gold Limited.

JX 527. The Form 8-K did not mention Wadman's letter or the reasons for his resignation.

R. Stockholder Approval And Closing

During Stillwater's annual meeting on April 26, 2017, the stockholders approved the Merger Agreement. Under Delaware law, a merger requires the approval of holders of a majority of the outstanding shares, making a non-vote the equivalent of a "no" vote. Because stockholders can vote no by not voting, the percentage of the outstanding shares is the appropriate metric for evaluating the level of stockholder support for a merger. The Company had 121,389,213 shares outstanding. Holders of 91,012,990 shares voted in favor of the Merger, representing 75% of the issued and outstanding equity. Holders of 103,088,167 shares were present at the meeting in person or by proxy, so the same number of affirmative votes results in a misleadingly higher approval percentage of 88%. *See* JX 549 at 1.

The Merger closed on May 4, 2017. Between signing and closing, the spot price of palladium increased by 9.2%. The spot price of a weighted basket of Stillwater's products increased by 5.9%.

S. Post-Closing Developments

On July 1, 2017, Sibanye entered into employment agreements with Bateman and McMullen. Bateman agreed to serve as Executive Vice President—US Region, reporting directly to Froneman. Bateman waived his change-of-control benefits in return for a higher base salary and additional incentive compensation. *See* JX 585.

McMullen agreed to serve as a Technical Advisor to Sibanye. His employment agreement permitted him "to perform the functions of that role while residing in the Turks and Caicos." JX 586 at '041. Like Bateman, McMullen waived his change-of-control benefits in return for an annual salary of $712,000 plus incentive compensation. *See id.*

In November 2017, Sibanye issued a Competent Person's Report that valued the Company's operating mines at $2.7 billion as of July 31, 2017. This valuation was 23% greater than the total consideration that Sibanye paid for the Company at closing, just three months before the valuation date for the report. PTO ¶ 102; JX 615 at 205.

T. This Appraisal Proceeding

Holders of 5,804,523 shares of the Company eschewed the consideration offered in the Merger and pursued appraisal. In August 2018, the holders of 384,000 shares settled their claims. The remaining petitioners litigated their claims through trial.

II. LEGAL ANALYSIS

***18** "An appraisal proceeding is a limited legislative remedy intended to provide shareholders dissenting from a merger on grounds of inadequacy of the offering price with a judicial determination of the intrinsic worth (fair value) of their shareholdings." *Cede & Co. v. Technicolor, Inc. (Technicolor I)*, 542 A.2d 1182, 1186 (Del. 1988). Section 262(h) of the Delaware General Corporation Law states that

> the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors.

8 Del. C. § 262(h). The statute thus places the obligation to determine the fair value of the shares squarely on the court. *Gonsalves v. Straight Arrow Publ'rs, Inc.*, 701 A.2d 357, 361 (Del. 1997).

Because of the statutory mandate, the allocation of the burden of proof in an appraisal proceeding differs from a traditional liability proceeding. "In a statutory appraisal proceeding, both sides have the burden of proving their respective valuation positions ...." *M.G. Bancorp., Inc. v. Le Beau*, 737 A.2d 513, 520 (Del. 1999). "No presumption, favorable or unfavorable, attaches to either side's valuation ...." *Pinson v. Campbell-Taggart, Inc.*, 1989 WL 17438, at *6 (Del. Ch. Feb. 28, 1989). "Each party also bears the burden of proving the constituent elements of its valuation position ..., including the propriety of a particular method, modification, discount, or premium." Jesse A. Finkelstein & John D. Hendershot, *Appraisal Rights in Mergers and Consolidations*, Corp. Prac. Series (BNA) No. 38-5th, at A-90 (2010 & 2017 Supp.) [hereinafter *Appraisal Rights*].

As in other civil cases, the standard of proof in an appraisal proceeding is a preponderance of the evidence. *M.G. Bancorp.*, 737 A.2d at 520. A party is not required to prove its valuation conclusion, the related valuation inputs, or its underlying factual contentions by clear and convincing evidence or to exacting certainty. *See Triton Constr. Co. v. E. Shore Elec. Servs., Inc.*, 2009 WL 1387115, at *6 (Del. Ch. May 18, 2009), *aff'd*, 2010 WL 376924 (Del. Jan. 14, 2010) (ORDER). "Proof by a preponderance of the evidence means proof that something is more likely than not. It means that certain evidence, when compared to the evidence opposed to it, has the more convincing force and makes you believe that something is more likely true than not." *Agilent Techs., Inc. v. Kirkland*, 2010 WL 610725, at *13 (Del. Ch. Feb. 18, 2010) (internal quotation marks omitted).

"In discharging its statutory mandate, the Court of Chancery has discretion to select one of the parties' valuation models as its general framework or to fashion its own." *M.G. Bancorp.*, 737 A.2d at 525–26. "[I]t is entirely proper for the Court of Chancery to adopt any one expert's model, methodology, and mathematical calculations, *in toto*, if that valuation is supported by credible evidence and withstands a critical judicial analysis on the record." *Id.* at 526. Or the court "may evaluate the valuation opinions submitted by the parties, select the most representative analysis, and then make appropriate adjustments to the resulting valuation." *Appraisal Rights*, *supra*, at A-31 (collecting cases). The court may also "make its own independent valuation calculation by ... adapting or blending the factual assumptions of the parties' experts." *M.G. Bancorp.*, 737 A.2d at 524. "If neither party satisfies its burden, however, the court must then use its own independent judgment to determine fair value." *Gholl v. eMachines, Inc.*, 2004 WL 2847865, at *5 (Del. Ch. Nov. 24, 2004). But the court must also be cautious when adopting an approach that deviates from the parties' positions. Doing so "late in the proceedings" may "inject[ ] due process and fairness problems" that are "antithetical to the traditional hallmarks of a Court of Chancery appraisal proceeding," because the court's approach will not have been "subjected to the crucible of pretrial discovery, expert depositions, cross-expert rebuttal, expert testimony at trial, and cross examination at trial." *Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc.*, 210 A.3d 128, 140-41 (Del. 2019).

***19** In *Tri-Continental Corporation v. Battye*, 74 A.2d 71 (Del. 1950), the Delaware Supreme Court explained in detail the concept of value that the appraisal statute employs:

> The basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him, *viz.*, his proportionate interest in a going concern. By value of the stockholder's proportionate interest in the corporate enterprise is meant the true or intrinsic value of his stock which has been taken by the merger. In determining what figure represents the true or intrinsic value, ... the courts must take into consideration all factors and elements which reasonably might enter into the fixing of value. Thus, market value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or which could be ascertained as of the date of the merger and which throw any light on future prospects of the merged corporation are not only pertinent to an inquiry as to the value of the dissenting stockholder's interest, but must be considered .... [9]

Subsequent Delaware Supreme Court decisions have adhered consistently to this definition of value. [10] Most recently, the Delaware Supreme Court reiterated that "[f]air value is ... the value of the company to the stockholder as a going concern," *i.e.*, the stockholder's "proportionate interest in a going concern." *Aruba*, 210 A.3d at 132–33.

The trial court's "ultimate goal in an appraisal proceeding is to determine the 'fair or intrinsic value' of each share on the closing date of the merger." *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*, 177 A.3d 1, 20 (Del. 2017) (quoting *Cavalier Oil*, 564 A.2d at 1142–43). To accomplish this task, "the court should first envisage the entire pre-merger company as a 'going concern,' as a standalone entity, and assess its value as such." *Id.* (quoting *Cavalier Oil*, 564 A.2d at 1144). When doing so, the corporation "must be valued as a going concern based upon the 'operative reality' of the company as of the time of the merger," taking into account its particular market position in light of future prospects. *M.G. Bancorp.*, 737 A.2d at 525 (quoting *Cede & Co. v. Technicolor, Inc. (Technicolor IV)*, 684 A.2d 289, 298 (Del. 1996)); *accord Dell*, 177 A.3d at 20. The concept of the corporation's "operative reality" is important because "[t]he underlying assumption in an appraisal valuation is that the dissenting shareholders would be willing to maintain their investment position had the merger not occurred." *Technicolor IV*, 684 A.2d at 298. Consequently, the trial court must assess "the value of the company ... as a going concern, rather than its value to a third party as an acquisition." *M.P.M. Enters., Inc. v. Gilbert*, 731 A.2d 790, 795 (Del. 1999).

***20** "The time for determining the value of a dissenter's shares is the point just before the merger transaction 'on the date of the merger.' " *Appraisal Rights*, *supra*, at A-33 (quoting *Technicolor I*, 542 A.2d at 1187). Put differently, the valuation date is the date on which the merger closes. *Technicolor IV*, 684 A.2d at 298; *accord M.G. Bancorp.*, 737 A.2d at 525. If the value of the corporation changes between the signing of the merger agreement and the closing, then the fair value determination must be measured by the "operative reality" of the corporation at the effective time of the merger. *See Technicolor IV*, 684 A.2d at 298.

The statutory obligation to make a single determination of a corporation's value introduces an impression of false precision into appraisal jurisprudence.

> [I]t is one of the conceits of our law that we purport to declare something as elusive as *the* fair value of an entity on a given date .... [V]aluation decisions are impossible to make with anything approaching complete confidence. Valuing an entity is a difficult intellectual exercise, especially when business and financial experts are able to organize data in support of wildly divergent valuations for the same entity. For a judge who is not an expert in corporate finance, one can do little more than try to detect gross distortions in the experts' opinions. This effort should, therefore, not be understood, as a matter of intellectual honesty, as resulting in *the* fair value of a corporation on a given

> date. The value of a corporation is not a point on a line, but a range of reasonable values, and the judge's task is to assign one particular value within this range as the most reasonable value in light of all the relevant evidence and based on considerations of fairness.[11]

As the Delaware Supreme Court recently explained, "fair value is just that, 'fair.' It does not mean the highest possible price that a company might have sold for had Warren Buffet negotiated for it on his best day and the Lenape who sold Manhattan on their worst." *DFC Glob. Corp. v. Muirfield Value P'rs*, 172 A.3d 346, 370 (Del. 2017).

Because the determination of fair value follows a litigated proceeding, the issues that the court considers and the outcome it reaches depend in large part on the arguments advanced and the evidence presented.

> An argument may carry the day in a particular case if counsel advance it skillfully and present persuasive evidence to support it. The same argument may not prevail in another case if the proponents fail to generate a similarly persuasive level of probative evidence or if the opponents respond effectively.

Merion Capital L.P. v. Lender Processing Servs., L.P., 2016 WL 7324170, at *16 (Del. Ch. Dec. 16, 2016). Likewise, the approach that an expert espouses may have met "the approval of this court on prior occasions," but may be rejected in a later case if not presented persuasively or if "the relevant professional community has mined additional data and pondered the reliability of past practice and come, by a healthy weight of reasoned opinion, to believe that a different practice should become the norm ...." *Glob. GT LP v. Golden Telecom, Inc. (Golden Telecom Trial)*, 993 A.2d 497, 517 (Del. Ch.), *aff'd*, 11 A.3d 214 (Del. 2010).

A. The Deal Price

***21** Sibanye contends that the deal price of $18.00 per share is a persuasive indicator of fair value if adjusted downward to eliminate elements of value arising from the Merger. The petitioners argue that the deal price should receive no weight. As the proponent of using the deal price, Sibanye bore the burden of establishing its persuasiveness. Sibanye also bore the burden of proving its downward adjustment.

1. The Standard For Evaluating A Sale Process

There is no presumption that the deal price reflects fair value. *Dell*, 177 A.3d at 21; *DFC*, 172 A.3d at 366–67. Relying on the statutory requirement that the Court of Chancery must consider "all relevant factors" when determining fair value, the Delaware Supreme Court has rejected "requests for the adoption of a presumption that the deal price reflects fair value if certain preconditions are met, such as when the merger is the product of arm's-length negotiation and a robust, non-conflicted market check, and where bidders had full information and few, if any, barriers to bid for the deal." *Dell*, 177 A.3d at 21. Yet the Delaware Supreme Court has also cautioned that its

> refusal to craft a statutory presumption in favor of the deal price when certain conditions pertain does not in any way signal our ignorance to the economic reality that the sale value resulting from a robust market check will often be the most reliable evidence of fair value, and that second-guessing the value arrived upon by the collective views of many sophisticated parties with a real stake in the matter is hazardous.

DFC, 172 A.3d at 366. The Delaware Supreme Court has likewise cautioned that "we have little quibble with the economic argument that the price of a merger that results from a robust market check, against the back drop of a rich information base and a welcoming environment for potential buyers, is probative of the company's fair value." *Id.* Based on the facts presented in *DFC* and *Dell*, the Delaware Supreme Court endorsed using the deal price as a persuasive indicator of fair value in those cases. Based on the facts presented in *Aruba*, the Delaware Supreme Court used a deal-price-less-synergies metric to make its own fair value determination.

As a general matter, the persuasiveness of the deal price depends on the reliability of the sale process that generated it. When assessing whether a sale process results in fair value, the issue "is not whether a negotiator has extracted the highest possible bid." *Dell*, 177 A.3d at 33. "[T]he purpose of an appraisal is ... to make sure that [the petitioners] receive fair compensation for their shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction." *DFC*, 172 A.3d at 370–71. "[T]he key inquiry is whether the dissenters got fair value and were not exploited." *Dell*, 177 A.3d at 33.

Relying on the Delaware Supreme Court's decision in *DFC*, the petitioners assert that the deal price "deserves weight ***only*** if the merger is the product of a 'robust market search' and an arm's-length third party transaction with 'no hint of self-interest that compromised the market check.' " Dkt. 210 at 36 [hereinafter PTOB] (quoting *DFC*, 172 A.3d at 349). That is not what *DFC* held.

The petitioners have accurately quoted phrases from the decision in *DFC*, but when the Delaware Supreme Court made those observations, it was describing the trial court's findings regarding the sale process that took place in that case. The Delaware Supreme Court then determined that given those attributes, "the best evidence of fair value was the deal price." *DFC*, 172 A.3d at 349. The high court's comments in *DFC* explained why the particular sale process in that case was so good as to make the deal price "the best evidence of fair value." The decision did not identify minimum characteristics that a sale process must have before a trial court can give it weight. The decision also did not address what makes a sale process sufficiently bad that a trial court cannot give it weight. Technically, the decision did not even delineate when a sale process would be sufficiently good that a trial court should regard it as "the best evidence of fair value." The Delaware Supreme Court could have believed the sale process in *DFC* warranted that level of consideration without excluding the possibility that a not-as-good sale process could warrant the same treatment.

***22** The same is true for the Delaware Supreme Court's comments about the sale process in *Dell*. There, the Delaware Supreme Court described the sale process as having featured "fair play, low barriers to entry, outreach to all logical buyers, and the chance for any topping bidder to have the support of Mr. Dell's own votes ...." *Dell*, 177 A.3d at 35. Based on its view of the sale process, the Delaware Supreme Court suggested that "the deal price deserved heavy, if not dispositive weight." *Dell*, 177 A.3d at 23. After describing the sale process in greater detail, the Delaware Supreme Court observed, "Overall, the weight of evidence shows that Dell's deal price has heavy, if not overriding, probative value." *Id.* at 30. As in *DFC*, the Delaware Supreme Court was explaining why it regarded a particular sale process as so good that it deserved "heavy, if not dispositive weight." The Delaware Supreme Court was not identifying the minimum requirements for a sale process to generate reliable information about fair value, nor was it enumerating qualities which, if absent, would render the outcome of a sale process so unreliable as to provide no insight into fair value.

The Delaware Supreme Court's decision in *Aruba* likewise did not address the minimum requirements for a sale process to generate reliable information about fair value. There, the trial court found the sale process to be sufficiently reliable to use the deal price as a valuation indicator, but declined to give it weight. The Delaware Supreme Court accepted that the sale process was sufficiently reliable and used the deal price as the exclusive basis for its own fair value determination. As with *Dell* and *DFC*, the *Aruba* decision did not have to address when a sale process was sufficiently bad that a trial court should decline to rely on the deal price.

The decisions in *DFC*, *Dell*, and *Aruba* are highly informative because they analyze fact patterns in which the Delaware Supreme Court viewed the sale processes as sufficiently reliable to use the deal price as either (i) the exclusive basis for its own fair value determination (*Aruba*), (ii) as a valuation indicator that "deserved heavy, if not dispositive weight" (*Dell*), or (iii) as a valuation indicator that provided "the best evidence of fair value" (*DFC*). But *Aruba*, *Dell*, and *DFC* do not establish legal requirements for a sale process. Whether a sale process is sufficiently good that the deal price should be regarded as persuasive evidence of fair value, or whether a sale process is sufficiently bad that the deal price should not be regarded as persuasive evidence of fair value are invariably fact-specific questions, and the answers depend on the arguments made and the evidence presented in a given case.

2. Objective Indicia Of Reliability

In the recent appraisal decisions that have examined the reliability of a sale process, the Delaware Supreme Court has cited certain "objective indicia" that "suggest[ ] that the deal price was a fair price." *Dell*, 177 A.3d at 28; *accord* *DFC*, 172

A.3d at 376. The presence of objective indicia do not establish a presumption in favor of the deal price. The indicia are a starting point for analysis, not the end point, and in each of its recent appraisal decisions, the Delaware Supreme Court has determined that a combination of the objective indicia and other evidence outweighed the shortcomings in the sale processes that the petitioners had identified (*Aruba*) or which the trial court had regarded as undermining the persuasiveness of the deal price (*Dell* and *DFC*).

First, the Merger was an arm's-length transaction with a third party. *See* DFC, 172 A.3d at 349 (citing fact that "the company was purchased by a third party in an arm's length sale" as factor supporting fairness of deal price). It was not a transaction involving a controlling stockholder. *See* Dell, 177 A.3d at 30 (citing fact that "this was not a buyout led by a controlling stockholder" as a factor supporting fairness of deal price). Sibanye was an unaffiliated acquirer with no prior ownership interest in Stillwater.

Second, the Board did not labor under any conflicts of interest. Six of the Board's seven members were disinterested, outside directors, and they had the statutory authority under the Delaware General Corporation Law to say "no" to any merger. *See* 8 *Del. C.* § 251(b) (requiring board adoption and recommendation of a merger agreement); Dell, 177 A.3d at 28 (citing fact that special committee was "composed of independent, experienced directors and armed with the power to say 'no' " as factor supporting fairness of deal price). Stillwater's stockholders were widely dispersed, and the petitioners have not identified divergent interests among them. *Cf. id.* at 11 (citing the fact that "any outside bidder who persuaded stockholders that its bid was better would have access to Mr. Dell's votes" as a factor supporting fairness of deal price).

***23** Third, Sibanye conducted due diligence and received confidential information about Stillwater's value. *See* Aruba, 210 A.3d at 137 (emphasizing that buyer armed with "material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller"). Like the acquirer in *Aruba*, Sibanye "had signed a confidentiality agreement, done exclusive due diligence, gotten access to material nonpublic information," and had a "sharp[ ] incentive to engage in price discovery ... because it was seeking to acquire all shares." *Id.* at 140.

Fourth, Stillwater negotiated with Sibanye and extracted multiple price increases. *See id.* at 139 (citing "back and forth over price"); Dell, 177 A.3d at 28 (citing fact that special committee "persuaded Silver Lake to raise its bid six times"). In July 2016, when Sibanye indicated interest in a transaction at $15.75 per share, Stillwater did not rush into a deal. In December 2016, when Sibanye raised its indication of interest to a range of $17.50 to $17.75 per share, Stillwater again did not proceed. With the Board's backing, McMullen demanded a higher price. When Sibanye offered $18.00 per share, the Board did not immediately accept. Only after Sibanye twice stated that $18.00 per share was its best and final offer did the Board accept that price.

Most importantly, no bidders emerged during the post-signing phase, which is a factor that the Delaware Supreme Court has stressed when evaluating a sale process.[12] The Merger Agreement did not contain any exceptional deal protection features, and the total amounts due via the termination fee and expense reimbursement provision were comparatively low, representing approximately 1.2% of equity value. Excluding the expense reimbursement, the termination fee reflected only 0.76% of equity value. The absence of a topping bid was thus highly significant.

As noted, these are fewer objective indicia of fairness than the Delaware Supreme Court identified when reviewing the sale processes in *DFC*, *Dell*, or *Aruba*, and the presence of these factors does not establish a presumption in favor of the deal price. Nevertheless, the objective indicia that were present provide a cogent foundation for relying on the deal price as a persuasive indicator of fair value, subject to further review of the evidence.

3. The Challenges To The Pre-Signing Phase

The petitioners have advanced a multitude of reasons why they believe the deal price for Stillwater does not provide a persuasive indicator of fair value. The bulk of their objections concern the pre-signing phase.

As a threshold matter, the petitioners argue generally that a reliable sale process requires some degree of pre-signing outreach, citing a comment from the *Union Illinois* decision in which this court used a deal-price-less-synergies metric to value a privately held company after concluding that the company was "marketed in an effective manner." Union Ill., 847 A.2d at 350. The petitioners also cite a statement from the *AOL* decision to the effect that a sale process will provide persuasive evidence of statutory fair value when "(i) information was sufficiently disseminated to potential bidders, so that (ii) an informed sale could take place, (iii) without undue impediments imposed by the deal structure itself." *In re Appraisal of AOL Inc.*, 2018 WL 1037450, *8 (Del. Ch. Feb. 23, 2018). Neither decision established a rule that pre-signing outreach is invariably required before the deal price can serve as persuasive evidence of fair value. At least for a widely held, publicly traded company, a sale process could justify both sets of observations through the public announcement of a transaction and a sufficiently open post-signing market check.

***24** The petitioners' myriad arguments about the pre-signing process in this case raise a fundamental question: Would the deal price provide persuasive evidence of fair value if Stillwater had pursued a single-bidder strategy in which it only interacted with Sibanye before signing the Merger Agreement, recognizing that the Merger Agreement was sufficiently open to permit a meaningful post-signing market check? If the deal price would have provided persuasive evidence of fair value under those circumstances, then the additional efforts that Stillwater made before signing, even if disorganized and flawed, should not change the outcome. It is conceivable that a pre-signing process could involve features that undermined the effectiveness of a post-signing market check, such as never-waived standstill agreements containing don't-ask-don't-waive provisions, but that was not the case here. At least on the facts presented, Stillwater's efforts were additive, not subtractive. They might not have added much, but they did not detract from what Stillwater could have achieved through a single-bidder process focused on Sibanye followed by a post-signing market check.

a. The Possibility Of A Single-Bidder Strategy

Although the Delaware Supreme Court has not had the opportunity to consider a single-bidder strategy for purposes of determining the persuasiveness of a deal-price metric in an appraisal proceeding, extant precedent suggests that if Stillwater had pursued a single-bidder strategy in which it only interacted with Sibanye before signing the Merger Agreement, then the deal price would provide persuasive evidence of fair value because the Merger Agreement was sufficiently open to permit a meaningful post-signing market check. The reasoning that leads to this endpoint starts not with the recent triumvirate of appraisal cases, but rather with an important Delaware Supreme Court decision that restated the high court's enhanced scrutiny jurisprudence for purposes of applying that standard of review in a breach of fiduciary duty case. *C & J Energy Servs., Inc. v. City of Miami Gen. Empls.' & Sanitation Empls.' Ret. Tr.*, 107 A.3d 1049 (Del. 2014). The Delaware Supreme Court's enhanced scrutiny jurisprudence becomes pertinent to appraisal proceedings because, as commentators have perceived, the deal price will provide persuasive evidence of fair value in an appraisal proceeding involving a publicly traded firm if the sale process would satisfy enhanced scrutiny in a breach of fiduciary duty case.[13]

In *C & J Energy*, the Delaware Supreme Court held that plaintiffs who challenged a transaction involving only a passive, post-signing market check had not shown a reasonable likelihood that the director defendants had breached their fiduciary duties under the enhanced scrutiny standard of review. The transaction in *C & J Energy* was a stock-for-stock merger between C & J Energy Services, Inc. and a subsidiary of Nabors Industries Ltd. Although C & J Energy was nominally the acquirer, it would emerge from the transaction with a controlling stockholder, and the Delaware Supreme Court therefore examined whether the directors had fulfilled their situationally specific duty to seek the best transaction reasonably available. *See C & J Energy*, 107 A.3d at 1067.

***25** The merger in *C & J Energy* resulted from a CEO-driven process. Joshua Comstock, the founder, chairman, and CEO of C & J Energy, spearheaded the discussions. Talks between Comstock and the CEO of Nabors started in January 2014, and although Comstock discussed the deal with some of C & J Energy's directors, he did not receive formal board approval to negotiate until April. Later in the process, he made a revised offer to Nabors without board approval. The plaintiffs argued that Comstock acted without authority and misled the board about key issues. The Delaware Supreme Court found "at least some support for the plaintiffs' contention that Comstock at times proceeded on an 'ask for forgiveness rather than permission' basis." *Id.* at 1059.

There was evidence in *C & J Energy* that Comstock had personal reasons to favor a deal with Nabors. The Nabors CEO "assured Comstock throughout the process that he would be aggressive in protecting Comstock's financial interests if a deal was consummated." *Id.* at 1064. After the key terms of the transaction had been negotiated, but before it was formally approved, Comstock asked for a side letter "affirming that C & J's management would run the surviving entity and endorsing a generous compensation package." *Id.*

When the Nabors CEO balked, Comstock threatened to not sign or announce the deal. The Nabors CEO gave in, and the deal was announced as planned. *Id.* at 1064–65. In addition, there was evidence that C & J Energy's primary financial advisor was less than optimally effective and seemed to be advocating for the deal rather than advocating for C & J Energy. *See id.* at 1056. The banker also had divergent interests because of its role as a financing source for the deal. *Id.* at 1057. There were thus reasons to think that the two principal negotiators for C & J—its CEO and its banker—had personal reasons to favor a transaction with Nabors and to push for that outcome.

The merger agreement in *C & J Energy* included a no-shop clause subject to a fiduciary out and a termination fee equal to 2.27% of the deal value. *Id.* at 1063. The period between the announcement of the deal on June 25, 2014, and the trial court's issuance of the injunction on November 25, 2014, lasted 153 days. No competing bidder emerged during that period.

On these facts, the Delaware Supreme Court found no grounds for a potential breach of duty, explaining that "[w]hen a board exercises its judgment in good faith, tests the transaction through a viable passive market check, and gives its stockholders a fully informed, uncoerced opportunity to vote to accept the deal, we cannot conclude that the board likely violated its *Revlon* duties." *Id.* at 1053. Elaborating, the senior tribunal explained that a board may pursue a single transaction partner, "so long as the transaction is subject to an effective market check under circumstances in which any bidder interested in paying more has a reasonable opportunity to do so." *Id.* at 1067. The high court emphasized that "[s]uch a market check does not have to involve an active solicitation, so long as interested bidders have a fair opportunity to present a higher-value alternative, and the board has the flexibility to eschew the original transaction and accept the higher-value deal." *Id.* at 1067–68. The transaction in *C & J Energy* satisfied this test. Describing the suite of deal protections, the Delaware Supreme Court observed that "a potential competing bidder faced only modest deal protection barriers." *Id.* at 1052. Later, the court reiterated that "there were no material barriers that would have prevented a rival bidder from making a superior offer." *Id.* at 1070; *accord id.* ("But in this case, there was no barrier to the emergence of another bidder and more than adequate time for such a bidder to emerge."). The Delaware Supreme Court also cited with approval precedents in which a sell-side board had engaged exclusively with a single buyer, had not conducted a pre-signing market check, then agreed to a merger agreement containing a no-shop clause, a matching right, and a termination fee, and the resulting combination was found sufficient to permit an effective post-signing market check that satisfied the directors' duties under enhanced scrutiny.[14]

***26** Procedurally, the Delaware Supreme Court's decision in *C & J Energy* vacated an injunction that the trial court had entered in advance of the stockholder vote. In holding that the trial court had issued the injunction improvidently, the high court noted that "[t]he ability of the stockholders themselves to freely accept or reject the board's preferred course of action is also of great importance in this context." *Id.* at 1068. The role of the vote, however, should not detract from the high court's observations about the adequacy of the single-bidder process. Underscoring that point, the Delaware Supreme Court cited the trial court's apparent belief "that *Revlon* required C & J's board to conduct a pre-signing active solicitation process in order to satisfy its contextual fiduciary duties," then explicitly rejected that understanding of the enhanced scrutiny standard. *Id.* at 1068. As a result, the Delaware Supreme Court's decision in *C & J Energy* has implications that go beyond the injunction context.

One area where its implications subsequently became manifest was in a post-closing liability action where plaintiffs sought to recover from an alleged aider-and-abettor under a quasi-appraisal theory of damages. *See In re* PLX Tech. Inc. S'holders Litig., ––– A.3d ––––, 2019 WL 2144476 (Del. May 16, 2019) (TABLE). The *PLX* litigation challenged a merger agreement in which the acquirer (Avago) purchased the target (PLX) for cash. As in *C & J Energy*, the sale process was not pristine. The trial court found that a key director and the company's investment banker had divergent interests that caused them to favor a sale over having PLX remain independent, that Avago tipped the director and the banker about the timing and pricing of a deal, that the director and the banker failed to disclose the tip to the board while using the information to help them position PLX to be sold, and that the proxy statement failed to disclose these issues. *See In re PLX Tech. Inc. S'holders Litig. (PLX Trial)*, 2018 WL 5018535, at *32–35, *44–47 (Del. Ch. Oct. 16, 2018) (subsequent history omitted). Based on these findings, the trial court found a predicate breach of fiduciary duty under the enhanced scrutiny standard. The trial court also found that the sole remaining defendant—an activist stockholder affiliated with the key director—had participated knowingly in the breach. *See id.* at *48–50.

The plaintiffs' claim foundered, however, at the damages stage. The plaintiffs sought to recover compensatory damages on behalf of a class of stockholders based on the theory that PLX should have remained independent rather than being sold. Under this theory, the plaintiffs sought "out-of-pocket (*i.e.*, compensatory) money damages equal to the 'fair' or 'intrinsic' value of their stock at the time of the merger, less the price per share that they actually received," with "[t]he 'fair' or 'intrinsic' value of the shares ... determined using the same methodologies employed in an appraisal." *Id.* at *50 (internal quotation marks omitted) (collecting cases). The plaintiffs' expert used a DCF methodology to value PLX at $9.86 per share, well above the deal price of $6.50 per share. *See id.* at *51.

Although PLX's pre-signing process was marred by breaches of fiduciary duty resulting from Avago's tip to the key director and the company's banker, the trial court found that the sale process as a whole was sufficiently reliable to warrant rejecting the plaintiffs' valuation. The trial court explained that "[m]ore important than the pre-signing process was the post-signing market check." *Id.* at *55. After discussing the outcome in *C & J Energy*, the trial court reasoned that "the structure of the Merger Agreement satisfied the Delaware Supreme Court's standard for a passive, post-signing market check." *Id.* The merger agreement (i) contained a no-shop with a fiduciary subject an unlimited match right that gave Avago four days to match the first superior proposal and two days to match any subsequent increase, and (ii) required PLX to pay Avago a termination fee of $10.85 million, representing 3.5% of equity value ($309 million) and 3.7% of enterprise value ($293 million). *See id.* at *26, *44. Avago launched its first step-tender offer on July 8, 2014. No competing bidder intervened, and the merger closed thirty-five days later on August 12. *Id.* at *27. This time period compared favorably with other passive, post-signing market checks that Delaware decisions had approved.[15]

***27** On appeal, the Delaware Supreme Court affirmed the judgment based solely on the trial court's damages ruling and without reaching or expressing a view on any of the other issues raised by the case. *See* *PLX*, 2019 WL 2144476, at *1. For present purposes, the damages issue is the important one, because the trial court had determined that the suite of defensive measures in the merger agreement, together with the absence of a topping bid, provided a more reliable indication of value than the plaintiffs' discounted cash flow model. *See* *PLX Trial*, 2018 WL 5018535, at *44, *54–56. Notably for present purposes, although the burden of proof rested solely with the plaintiffs, the trial court in *PLX* made its determination using the same valuation standard that would apply in an appraisal proceeding. *Id.* at *50.

To reiterate, in its appraisal jurisprudence, the Delaware Supreme Court has not yet been asked to rule on the reliability of a sale process involving a single-bidder strategy, no pre-signing outreach, and a passive post-signing market check. The closest precedent is *Aruba*, where the dynamics of the sale during the pre-closing phase resembled a single-bidder strategy, although the company's banker did engage in some minimal outreach.

The pre-signing phase of the sale process in *Aruba* had two stages. *See* *Verition P'rs Master Fund Ltd. v. Aruba Networks, Inc. (Aruba Trial)*, 2018 WL 922139, at *7–8 (Del. Ch. Feb. 15, 2018) (subsequent history omitted). The first stage began in late August 2014, when HP approached Aruba about a deal. Aruba hired an investment banker (Qatalyst), who identified thirteen potential partners and approached five of them. For reasons having "nothing to do with price," no one was interested. *Id.* at *10. Aruba and HP entered into an NDA that restricted HP from speaking with Aruba management about post-transaction employment, and HP began conducting due diligence. *Id.* at *11. Despite the restriction in the NDA, HP asked Aruba's CEO, Dominic Orr, if he would take on a key role with the combined entity. Orr replied that he had no objection. *Id.*

The parties seemed to be making progress towards a deal, but the HP board of directors balked at making a bid without further analysis, recalling the fallout from a disastrous acquisition in 2011. In November 2014, Aruba terminated discussions, bringing the first stage of the pre-signing process to a close. *Id.* at *12.

For its part, HP continued to evaluate an acquisition of Aruba. In December 2014, HP tapped Barclays Capital Inc. as its financial advisor. That firm had worked for Aruba and had been trying to secure the sell-side mandate. *Id.* at *13. On January 21, 2015, HP's CEO met with Orr for dinner. During the meeting, when HP's CEO proposed resuming merger talks, Orr responded with enthusiasm and suggested trying to announce a deal by early March. But HP's CEO also told Orr that because Qatalyst had represented the seller in HP's disastrous acquisition from 2011, HP would not proceed if Aruba used Qatalyst. *Id.* at *14.

The Aruba board decided to move forward with the deal and informed Qatalyst about HP's ukase. Aruba was obligated to pay Qatalyst a fee in the event of a successful transaction, so it kept Qatalyst on as a behind-the-scenes advisor. From then on, Qatalyst's primary goal was to repair its relationship with HP, and Qatalyst regarded a successful sale of Aruba to HP as a key step in the right direction. Aruba also needed a new HP-facing banker. It hired Evercore, a firm that was trying to establish a presence in Silicon Valley. During the sale process, Evercore likewise sought to please HP, viewing HP as a major source of future business. *See id.* at *9, *15–16, *19, *21.

The ensuing negotiations proceeded quickly. HP had anticipated making an opening bid of $24 per share, but after Orr's enthusiastic response, HP opened at $23.25 per share. *Id.* at *16–17. Qatalyst reached out to a sixth potential strategic partner, but it was not interested. *Id.* at *17. The Aruba board decided to counter at $29 per share. Evercore conveyed the number to Barclays, but when Barclays dismissed it, Evercore emphasized Aruba's desire to announce a deal quickly. *Id.* at *17–18. On February 10, 2015, twenty days after HP resumed discussions with Orr, the Aruba board agreed to a price of $24.67 per share. *Id.* at *19. The parties negotiated a merger agreement, and on March 1, 2015, the Aruba board approved it.

***28** The post-signing phase was uneventful. On March 2, 2015, Aruba and HP announced the merger. The merger agreement (i) contained a no-shop clause subject to a fiduciary out, (ii) conditioned the out for an unsolicited superior proposal on compliance with an unlimited match right that gave HP five days to match the first superior proposal and two days to match any subsequent increase, and (iii) required Aruba to pay HP a termination fee of $90 million, representing 3% of Aruba's equity value. No competing bidder emerged, and on May 1, 2015, Aruba's stockholders approved the merger. *Id.* at *21–22.

Although the sale process in *Aruba* had flaws, the trial court found that it was sufficiently reliable to make the deal price a persuasive indicator of fair value. Overall, the trial court viewed the HP-Aruba merger as "a run-of-the-mill, third party-deal," where "[n]othing about it appear[ed] exploitive." *Id.* at *38. The petitioners argued that the deal price resulted from a closed-off sale process in which HP had not faced a meaningful threat of competition. *Id.* at *39. The trial court rejected that contention, noting that the petitioners failed "to point to a likely bidder and make a persuasive showing that increased competition would have led to a better result." *Id.* (citing Dell, 177 A.3d at 28–29, 32, 34).

The petitioners also argued that the negotiators' incentives undermined the pre-signing phase, citing the desire of Aruba's bankers to cater to HP and the more subtly divergent interests of Aruba's CEO. The trial court found that although the petitioners proved that Aruba could have negotiated more aggressively, they did not prove that "the bankers, [the CEO], the Aruba Board, and the stockholders who approved the transaction all accepted a deal price that left a portion of Aruba's fundamental value on the table." *Id.* at *44.

In other portions of the decision, the trial court found that Aruba's unaffected trading price was a reliable indicator of fair value and rejected the parties' DCF valuations as unreliable. These holdings left the trial court with two reliable valuation indicators: the unaffected trading price and the deal price. The trial court determined that the unaffected trading price was the better measure of the fair value of Aruba's shares. *See id.* at *53–55.

On appeal, the Delaware Supreme Court reversed. The high court found that the trial court had incorrectly relied on the unaffected trading price, but it accepted the trial court's finding that the deal price was a reliable indicator of fair value. Aruba, 210 A.3d at 141–42.

Addressing the petitioners' claim that the pre-signing phase of the sale process was insufficient to establish a competitive bidding dynamic, the Delaware Supreme Court emphasized that

> when there is an open opportunity for many buyers to buy and only a few bid (or even just one bids), that does not necessarily mean that there is a failure of competition; it may just mean that the target's value is not sufficiently enticing to buyers to engender a bidding war above the winning price.

Id. at 136. Applying this principle to the facts in *Aruba*, the high court explained:

> Aruba approached other logical strategic buyers prior to signing the deal with HP, and none of those potential buyers were interested. Then, after signing and the announcement of the deal, still no other buyer emerged even though the merger agreement allowed for superior bids. It cannot be that an open chance for buyers to bid signals a market failure simply because buyers do not believe the asset on sale is sufficiently valuable for them to engage in a bidding contest against each other. If that were the jurisprudential conclusion, then the judiciary would itself infuse assets with extra value by virtue of the fact that no actual market participants saw enough value to pay a higher price. That sort of alchemy has no rational basis in economics.

***29** *Id.* On the facts presented, the level of competition in *Aruba* was sufficient to support the reliability of the deal price.

The Delaware Supreme Court also explained that the negotiations between Aruba and HP over price had important implications for the reliability of the deal price:

> [A] buyer in possession of material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller when agreeing to buy the company at a particular deal price, and that view of value should be given considerable weight by the Court of Chancery absent deficiencies in the deal process.

Id. at 137. The high court noted that HP and Aruba went "back and forth over price" and that HP had "access to nonpublic information to supplement its consideration of the public information available to stock market buyers ...." *Id.* at 139. The Delaware Supreme Court elsewhere emphasized that "HP had signed a confidentiality agreement, done exclusive due diligence, gotten access to material nonpublic information," and "had a much sharper incentive to engage in price discovery than an ordinary trader because it was seeking to acquire all shares." *Id.* at 140. On the facts presented, the extent of the negotiations in *Aruba* was sufficient to support the reliability of the deal price.

The high court ultimately concluded that Aruba's sale process was sufficiently reliable to render the deal price the best measure of fair value. The Delaware Supreme Court declined to use the trial court's estimate of the deal price minus synergies, instead adopting HP's contemporaneous synergies estimate and remanding with instructions that "final judgment be entered for the petitioners in the amount of $19.10 per share plus any interest to which the petitioners are entitled." *Id.* at 142.

The *Aruba* decision technically did not involve a single-bidder process, but the dynamics closely resembled one. Although Qatalyst reached out to five bidders at the beginning of the first phase of the pre-signing process, none of those parties had any interest in Aruba. After this development, both Qatalyst and Aruba's CEO concluded that Aruba's "only (but strong) weapon is to say we go alone." *Aruba Trial*, 2018 WL 922139, at *10. Later, Aruba's CEO had a "pretty open dialogue" with HP during which he informed HP that Aruba was "not running a sales process" and did not attempt to posture about pitting HP against anyone else. *Id.* at *40 (internal quotation marks omitted). During the second phase of the pre-signing process, after HP re-engaged, HP understood that Aruba was not pursuing other options. *Id.* at *41. The negotiations unfolded in a manner consistent with a single-bidder dynamic. *See id.*

In concluding that the deal price was a reliable indicator of fair value, the trial court considered a number of factors, including that "HP and Aruba agreed to terms for the merger agreement that the petitioners have not meaningfully challenged." *Id.* at *38. After describing the suite of defensive measures in the merger agreement, the trial court noted that "[t]his combination of defensive provisions would not have supported a claim for breach of fiduciary duty." *Id.* The petitioners had argued about a lack of competition during the pre-signing phase, and the trial court had discussed that factor at length, ultimately rejecting the objection. *See id.* at *39–41. On appeal, the Delaware Supreme Court emphasized that a failure of competition does not result simply because a limited number of parties bid, “or even just one bids.” *Aruba*, 210 A.3d at 136. The Delaware Supreme Court also emphasized the reliability of the price that resulted from the “back and forth” between Aruba and HP. *Id.* at 139.

***30** Given these precedents, I cannot agree that a reliable sale process must invariably involve some level of active outreach during the pre-signing phase. By making this observation, I am not suggesting that the Delaware Supreme Court has ever endorsed a single-bidder process for purposes of appraisal, nor that any of the precedents that this decision has discussed are squarely on point. Nor am I claiming to have any privileged insight into how the Delaware Supreme Court would or should evaluate the persuasiveness of a single-bidder strategy on the facts of any particular case. It nevertheless seems to me that if the proponent of a single-bidder process could show that the merger agreement allowed for a passive post-signing market check in line with what decisions have held is sufficient to satisfy enhanced scrutiny, and if there were no other factors that undermined the sale process, then the deal price would provide persuasive evidence of fair value.

This decision has already found that the sale process exhibited objective indicia of reliability. As noted and as discussed in greater detail below, the petitioners have not raised a meaningful challenge to the post-signing market check. The operative question for purposes of examining the pre-signing phase is not whether Stillwater's process fell short of what would have been optimal, but rather whether the pre-signing process sufficiently impaired the sale process as a whole, including the post-signing phase, so as to prevent the deal price from serving as a persuasive indicator of fair value.

b. The Relative Involvement Of McMullen And The Board In The Pre-Signing Phase

In their initial challenge to the pre-signing phase, the petitioners attack McMullen's role in the pre-signing process. They contend that McMullen acted improperly by pursuing Sibanye's indication of interest without authorization from the Board and contrary to its direction to pursue acquisitions or a merger of equals. *See* PTOB at 37. They also criticize McMullen for starting to engage with Sibanye in January 2016, but failing to inform the Board until after receiving an expression of interest from Sibanye in July. During this period, McMullen met with Sibanye's senior executives at least twice to discuss a sale of Stillwater, reached an understanding with Sibanye's CEO on pricing the deal at a 30% premium over Stillwater's thirty-day VWAP, and arranged a multi-day site visit for Sibanye personnel.

The petitioners also contend that after the Board learned of Sibanye's expression of interest in July 2016, the Board did not exercise meaningful oversight over the sale process. They accurately observe that the record lacks any evidence of meaningful engagement by the Board until October 3, 2016, two months before signing, when the Board received a report on the Company's outreach to various parties, instructed McMullen to obtain formal proposals for retaining an investment bank, instructed McMullen to create a cash flow model that could be used to value the Company, and decided not to form a special committee. *See* JX 246.

The petitioners correctly contend that these facts could have contributed to findings that McMullen and the directors breached their duty of care under the enhanced scrutiny standard of review.[16] But the enhanced scrutiny analysis would not have ended there. The *C & J Energy* decision likewise involved a CEO that began deal discussions without formal board authorization, engaged for months without formally reporting to the board, made a revised offer without board approval, and generally proceeded by asking for forgiveness rather than by getting permission. *See* *C & J Energy*, 107 A.3d at 1059. After considering the totality of the sale process, the Delaware Supreme Court concluded that the facts would not support a fiduciary breach, placing heavy reliance on the directors' decision to “test[ ] the transaction through a viable passive market check ....” *Id.* at 1053.

***31** The outcome in *PLX* likewise shows that the existence of problems during the pre-signing process does not necessarily undermine the reliability of the deal price. The trial court in *PLX* found that the directors had breached their fiduciary duties under the enhanced scrutiny standard because of an undisclosed tip from the eventual buyer to a key director and the company's banker. *PLX Trial*, 2018 WL 5018535, at *15–16, *32–35, *44–47. Despite this defect, the sale process provided reliable evidence of the company's value based primarily on the adequacy of the company's post-signing market check. *See id.* at *55 (“More important than the pre-signing process was the post-signing market check.”). Applying the same damages standard that would govern in an appraisal proceeding, the trial court found that the sale process was sufficiently reliable to render the plaintiffs' damages calculation unpersuasive, resulting in a failure of proof. *Id.* at

*50–55. The Delaware Supreme Court affirmed the judgment based solely on the trial court's damages ruling. *See* PLX, 2019 WL 2144476, at *1.

McMullen's unsupervised activities and the Board's failure to engage in meaningful oversight until October 2016 represent flaws in the pre-signing process. They are factors that must be taken into account, but they do not inherently disqualify the sale process from generating reliable evidence of fair value.

In this case, McMullen's unsupervised activities did not comprise the entirety of the Company's sale process. Ultimately, after the Board engaged, Stillwater formally retained BAML, conducted an expedited pre-signing canvass, and entered into the Merger Agreement. The terms of the Merger Agreement facilitated a meaningful post-signing market check, and no other buyer emerged even though the merger agreement allowed for superior bids. As in *Dell*, the petitioners did not point to any evidence that another party was interested in proceeding and would have bid if McMullen and the Board had acted differently. *See* Dell, 177 A.3d at 29.

c. McMullen's Personal Interest In A Transaction

In their next challenge to the pre-signing process, the petitioners contend that McMullen undermined the sale process because he planned to leave Stillwater, and "he wanted the benefit of a strategic transaction (i) to boost the Company's stock price prior to his departure and (ii) to maximize his payout upon stepping down as CEO." PTOB at 39. The petitioners correctly observe that by leaving after a transaction, McMullen would be entitled to unvested equity awards and accelerated retention payments that he could not obtain if he left without a transaction.

The petitioners also point out that McMullen devoted considerable time to developing and selling his personal investments outside of Stillwater. They cite McMullen's contemporaneous service in 2016 as CEO of Nevada Iron and as President of New Chris, even though McMullen's employment agreement with Stillwater limited McMullen's outside activities to board service and otherwise required him to devote his full efforts to Stillwater. *See* JX 114. During 2016, McMullen raised money for the successor company to New Chris and sold Nevada Iron. *See* McMullen Tr. 709, 863–64. The petitioners cite McMullen's activities (i) to show that McMullen was trying to maximize his personal wealth before retiring to Turks & Caicos, (ii) to suggest that McMullen might have done a better job with the sale process if he had not been pursuing his other investments, and (iii) as further evidence that the Board failed to provide active oversight.

Sibanye takes the extreme position that "there is no evidence to suggest that Mr. McMullen was motivated by anything other than maximizing stockholder value." Dkt. 211 at 59. Sibanye points to McMullen's decision in March 2016 to extend his employment by two years, claiming simplistically that if "McMullen's intention was truly to do a quick sale and leave the company, there would have been no need for him to renew his employment agreement since his prior contract did not expire until December 31, 2016 and contained essentially the same termination benefits as the new contract." *Id.* at 60. To the contrary, McMullen understood that completing a sale to Sibanye or another buyer might extend past December 31. Extending his employment agreement was the smart play for McMullen personally. Although Sibanye has not argued this point, it was also likely good for Stillwater, because it avoided the prospect of a near-term issue with CEO succession.

***32** Sibanye has no meaningful response to McMullen's pursuit of his other activities. Sibanye says they were permitted, but the petitioners have correctly described McMullen's employment agreement as only authorizing board service, not his more active roles. Sibanye also contends that his outside interests were disclosed in public filings, but that is not the point. The issue is whether the interests undermined the sale process, not whether they were disclosed. On this final point, Sibanye asserts that the petitioners "have pointed to no evidence that these outside interests presented an actual conflict, that these interests competed with or were adverse to Stillwater's interests, or that they otherwise interfered with Mr. McMullen's ability to carry out his duties as CEO of Stillwater." *Id.*

Sibanye has focused on the critical question: whether McMullen's personal interests undermined the sale process. Senior executives almost invariably have divergent incentives during a sale process, often because of change-in-control agreements, and equally often because the transaction will have implications for their personal employment situations.

Two Delaware appraisal precedents provide insight into factual scenarios involving divergent incentives of this type. The *Aruba* decision involved a sale process where the top executive and the company's investment bankers had conflicting incentives. The CEO wanted to retire, but he cared deeply about the company and its employees. When

HP proposed to acquire Aruba and keep the CEO on to integrate the companies, it offered the perfect path "to an honorable personal and professional exit." *Aruba Trial*, 2018 WL 922139, at *5; *see id.* at *43 (analyzing CEO's conflict). Aruba's investment bankers both wanted to curry favor with HP. Qatalyst was desperate to save its Silicon Valley franchise, and Evercore was auditioning for future business. *Id.* at *43. The trial court acknowledged the petitioners' concerns, but found that the conflicting incentives did not undermine the deal price as an indicator of fair value:

> The evidence does not convince me that the bankers, Orr, the Aruba Board, and the stockholders who approved the transaction all accepted a deal price that left a portion of Aruba's fundamental value on the table. Perhaps different negotiators could have extracted a greater share of the synergies from HP in the form of a higher deal price. Maybe if Orr had been less eager, or if Qatalyst had not been relegated to the back room, then HP would have opened at $24 per share. Perhaps with a brash Qatalyst banker leading the negotiations, unhampered by the Autonomy incident, Aruba might have negotiated more effectively and gotten HP above $25 per share. An outcome along these lines would have resulted in HP sharing a greater portion of the anticipated synergies with Aruba's stockholders. It would not have changed Aruba's standalone value. Hence, it would not have affected Aruba's fair value for purposes of an appraisal.

Id. at *44. On appeal, the Delaware Supreme Court accepted the reliability of the deal price as a valuation indicator and used it when making its own fair value determination. *Aruba,* 210 A.3d at 141–42.

The *Dell* decision also involved a conflict: Mr. Dell, the company's founder and top executive, was a buy-side participant in the management buyout and would emerge from the transaction with a controlling stake. A special committee negotiated the terms of the transaction with the financial sponsor backing the deal, but the trial court regarded Mr. Dell's involvement on the buy side as a factor cutting against the reliability of the deal price. For example, the trial court found that Mr. Dell gave the buyout group a leg-up given his relationships within the company and his knowledge of its business, and the trial court accepted the testimony of a sale-process expert that if bidders competed to pay more than what Mr. Dell's group would pay, then they risked overpaying and suffering the winner's curse. *In re Appraisal of Dell Inc.* (*Dell Trial*), 2016 WL 3186538, at *42–43 (Del. Ch. May 31, 2016) (subsequent history omitted). Equally important, Mr. Dell was a net purchaser of shares in the buyout, so any increase in the deal price cost him money.

> ***33** If Mr. Dell kept the size of his investment constant as the deal value increased, then Silver Lake would have to pay more and would demand a greater ownership stake in the post-transaction entity. [The petitioners' sale-process expert] showed that if Mr. Dell wanted to maintain 75% ownership of the post-transaction entity, then he would have to contribute an additional $250 million for each $1 increase in the deal price. If Mr. Dell did not contribute any additional equity and relied on Silver Lake to fund the increase, then he would lose control of the post-transaction entity at a deal price above $15.73 per share. Because Mr. Dell was a net buyer, any party considering an overbid would understand that a higher price would not be well received by the most important person at the Company.

Id. at *43 (footnote omitted). The trial court found that for purposes of price discovery in an appraisal case, Mr. Dell's involvement and incentives undermined the reliability of the sale process and the persuasiveness of the deal price. *Id.* at *44.

On appeal, the Delaware Supreme Court held that Mr. Dell's involvement in the buyout group had not undermined the sale process. *See* Dell, 177 A.3d at 32–33. The high court noted that "the [trial court] did not identify any possible bidders that were actually deterred because of Mr. Dell's status." *Id.* at 34. The Delaware Supreme Court also emphasized Mr. Dell's willingness to work with rival bidders during due diligence and the absence of evidence that Mr. Dell would have left the company if a rival bidder prevailed. *Id.* at 32–34. The high court concluded that the lack of a higher bid did not call into question the sale process, because "[i]f a deal price is at a level where the next upward move by a topping bidder has a material risk of being a self-destructive curse, that suggests the price is already at a level that is fair." *Id.* at 33.

The facts of *C & J Energy* are also relevant. The merger in *C & J Energy* resulted from a CEO-driven process, and there was evidence that the sell-side CEO had personal reasons to favor the deal because he would be in charge of the combined company and receive significantly greater compensation. *See* *C & J Energy*, 107 A.3d at 1064. After the key terms of the transaction had been negotiated, but before it was formally approved, the CEO went so far as to demand a side letter "affirming that C & J's management would run the surviving entity and endorsing a generous compensation package." *Id.* When the acquirer balked, the CEO threatened to terminate the discussions. He got his way, and the deal was announced as planned. *Id.* at 1065. There was also evidence that C & J Energy's primary financial advisor acted as a banker for the deal rather than for C & J Energy, and the banker had divergent interests as a source of financing for the deal. *See* *id.* at 1056–57. The Delaware Supreme Court held that the facts could not support a reasonable probability that the defendants had failed to obtain the best transaction reasonably available, relying heavily on the post-signing market check. *See* *id.* at 1053, 1067–68.

In this case, McMullen's personal interests are not as serious as the buy-side conflict that failed to undermine the sale process in *Dell*. They more closely resembled the divergent sell-side interests that affected the negotiators in *Aruba* and *C & J Energy*. Like the CEOs and bankers in those cases, McMullen's change-of-control benefits gave him a personal reason to secure a deal under circumstances where a disinterested participant might prefer a standalone option. McMullen appears to have been motivated by his desire to maximize his personal wealth and retire to a greater degree than the negotiators in *Aruba*. Stillwater's general counsel (Wadman) recognized McMullen's conflict, voiced his concerns to the Board, and ultimately resigned when McMullen secured more favorable treatment in the Merger for his own change-in-control benefits and for his CFO. *See* JX 526. As a result, McMullen's motivations most closely resembled the incentives of the CEO in *C & J Energy*, who held up the entire transaction until the acquirer agreed to a side letter "affirming that C & J's management would run the surviving entity and endorsing a generous compensation package." *C & J Energy*, 107 A.3d at 1064. The Delaware Supreme Court held that the facts in *C & J Energy* did not provide reasonable grounds for a breach of fiduciary duty under the enhanced scrutiny standard of review.

***34** At the same time, McMullen had ample reason to pursue the best deal possible for Stillwater. From his testimony and demeanor, McMullen seems like someone who took considerable satisfaction in his ability to achieve outcomes. As a matter of professional pride, he wanted to sell Stillwater for the best price he could. He also had economic reasons to extract a higher price. As disclosed in the proxy statement for the Merger, McMullen held 131,248 common shares, 155,891 restricted stock unit awards, and 222,556 performance based restricted stock unit awards, for a total of 509,695 common shares or share equivalents. *See* JX 525 at 78. At the deal price, these common shares and share equivalents had a value of $9,174,510. To state the obvious, every $1 increment in the deal price generated another half-a-million dollars for McMullen.

> When directors or their affiliates own "material" amounts of common stock, it aligns their interests with other stockholders by giving them a "motivation to seek the highest price" and the "personal incentive as stockholders to think about the trade off between selling now and the risks of not doing so."

Chen v. Howard-Anderson, 87 A.3d 648, 670–71 (Del. Ch. 2014) (quoting *Dollar Thrifty*, 14 A.3d at 600); *see also* *Lender Processing*, 2016 WL 7324170, at *22 (discussing incentive to maximize deal price where target managers were net sellers and would not retain jobs post-merger).

Consistent with his personal desire to obtain a good price for Stillwater, McMullen negotiated with Sibanye to increase the consideration. When Sibanye indicated interest at $15.75 per share in July 2016, McMullen did not rush to sign up a deal. When Sibanye raised indication of interest to $17.50 to $17.75 per share in December 2016, McMullen and the Board demanded a higher price. Even after Sibanye offered $18.00 per share, McMullen wanted more. Only after Sibanye twice said that $18.00 per share was its best and final offer did McMullen and the Board finally agree to transact.

As with McMullen's initiation of the sale process and the Board's failure to engage in meaningful oversight of his activities until October 2016, McMullen's personal motivation to exit from Stillwater and maximize his personal wealth represents a flaw in the sale process. Although Wadman's noisy withdrawal highlighted these issues, McMullen's personal interests as a whole do not appear materially different from interests that have not been sufficient in other cases to undermine the reliability of sale processes. On balance, the evidence does not convince me that McMullen's divergent interests led either McMullen or the Board to accept a deal price that left a portion of Stillwater's fundamental value on the table, particularly in light of the effective post-signing market check that Stillwater conducted.

d. The "Soft-Sell"

Turning to the details of the pre-signing phase, the petitioners contend that Stillwater's pre-signing market check fell short because until BAML was formally retained, McMullen relied on a "soft sell" approach that provided potential buyers with insufficient information to conclude that Stillwater was for sale and used unauthorized agents who could not formally engage on Stillwater's behalf. *See* PTOB at 44–45.

The evidence demonstrates that on the facts of this case, the "soft sell" strategy was not an effective means of generating interest in the Company. At the same time, the "soft sell" effort did not do anything to harm either BAML's abbreviated pre-signing process or the post-signing market check. The soft sell strategy was not a positive feature of the sale process, and it does not help support the persuasiveness of the deal price, but it does not detract from it either.

e. BAML's Compressed Pre-Signing Market Check

In a further criticism of the pre-signing phase, the petitioners contend that after BAML was formally retained, BAML did not have time to run an organized and meaningful process. The petitioners complain that BAML hastily called a list of potentially interested parties, who then were given only days after signing an NDA to prepare an expression of interest. Contrary to McMullen's strong recommendation in September 2016 that any bidder visit the Company's mines before providing an expression of interest, the November timeline did not accommodate site visits until after a party made an expression of interest. *See* JX 229 at '603. At trial, the petitioners introduced testimony from a sale process expert who questioned the effectiveness of BAML's abbreviated pre-signing process. *See* Gray Tr. 567–68. Even Sibanye's sale process expert questioned the effectiveness of the type of condensed outreach that BAML attempted to conduct. *See* Stowell Tr. 947–48.

***35** The petitioners have made a persuasive case that the BAML's pre-signing process was suboptimal, but they have not shown that it was worthless, nor that it was harmful. To the contrary, when evaluated against Delaware precedents, the pre-signing efforts, while rushed, were a positive factor for the sale process.

BAML received its formal mandate on November 7, 2016. The next day, BAML received a package of information from the Company, including Sibanye's indication of interest from July, the non-disclosure agreements with Hecla and Coeur, a cash flow model, and instructions for accessing the data room. BAML understood that Sibanye was pushing to close a deal by December and swung into action to do what it could. By November 9, BAML had generated a plan for an expedited market check that contemplated reaching out to twenty parties over the next two days, working with parties who expressed interest for the rest of the month, and then receiving expressions of interest at the end of the month. At that point, the Board would decide how to proceed.

In accordance with its expedited plan, BAML engaged directly with Sibanye, Coeur, and Hecla. BAML contacted five of the six parties that BAML regarded as "Possibly Interested," missing one. BAML contacted eight of the twelve additional parties that BAML had identified, missing four. BAML also contacted Northern Star, even though they originally had been listed as not interested.

Ten of the fourteen parties had no interest, but four engaged. One quickly withdrew, two ultimately expressed interest in a merger of equals, and the fourth dropped out by late November. Coeur also dropped out, and Hecla indicated that it needed to find a partner to pursue a transaction. Although the Board extended Hecla's deadline for submitting an indication of interest, and BAML followed up with Hecla, Hecla did not respond. At the end of November, an additional party—Northam—asked to be included in the Company's process.

During a meeting on December 2, 2016, the Board considered the status of the Company's process. At that point, the Board's only definitive expression of interest was a proposal that Sibanye had submitted on December 1 to acquire the Company for between $17.50 and $17.75 per share in cash. The Board decided to focus on Sibanye, which later raised its offer to $18 per share. Northam decided to withdraw, and on December 8, the Board approved the Merger Agreement.

Although compressed and expedited, BAML's outreach resulted in fourteen other parties hearing about Stillwater. In addition to Sibanye, a total of seven parties engaged to some degree. Ultimately, no one other than Sibanye submitted an indication of interest. The plaintiffs have criticized the timing, pacing, and scope of the pre-signing process, but it resulted in BAML contacting the "logical strategic buyers" before Stillwater signed up its deal with Sibanye. *Cf.* Aruba, 210 A.3d at 136 (observing that "Aruba approached other logical strategic buyers prior to signing the deal with HP, and none of those potential buyers were interested."). The number of meaningful contacts compares favorably with or is similar to the facts in the Delaware Supreme Court precedents.[17] When considering whether a deal price provides persuasive evidence of fair value, it is pertinent that the parties contacted failed to pursue a merger when they had a free chance to do so. *See* *DFC*, 172 A.3d at 376 (citing "failure of other buyers to pursue the company when they had a free chance to do so" as factor supporting fairness of deal price).

***36** On balance, BAML's pre-signing efforts were helpful. At a minimum, the abbreviated process generated incremental interest in Stillwater and gave those parties who engaged a leg up for the post-signing market check. Even the parties who were contacted but did not engage had the benefit of knowing that a transaction potentially was afoot. As with the "soft sell" strategy, there is no evidence that BAML's abbreviated process did anything to harm the sale process. The bidders who participated in the abbreviated pre-signing phase were free to bid during the post-signing phase. There is no evidence that any were alienated or put off by the Company's pre-signing efforts.

BAML's abbreviated pre-signing process was not ideal. Nevertheless, contrary to the petitioners' contentions, it was a positive factor for the reliability of the sale process.

f. The Negotiations With Sibanye

In their penultimate objection to Stillwater's pre-signing process, the petitioners contend that Sibanye pressured Stillwater to sign a merger agreement before the Company's rising stock price made what Sibanye was willing to pay look inadequate. The evidence demonstrates that early in his discussions with Sibanye, McMullen and Froneman recognized that any transaction would require a premium over Stillwater's trading price and agreed in principle on a 30% premium over the thirty-day VWAP. On October 17, 2016, Froneman told McMullen that Sibanye's offer of a "30% premium to VWAP remained unchanged" and that Sibanye's board of directors unanimously supported the transaction. JX 281 at '425. Another Sibanye executive repeated this message on November 22. PTO ¶ 243.

Sibanye, however, needed to borrow the funds to acquire Stillwater, and by November 30, 2016, Stillwater's share price had recovered to a point where a 30% premium over the thirty-day VWAP equaled $18.25 per share. Sibanye could not pay more than $18 per share without supplementing the consideration with cash on hand or a draw from its revolving credit line, which Sibanye did not want to do. Rather than sticking with the concept of a 30% premium over a thirty-day VWAP, Sibanye disavowed that concept, instead treating its prior indication of interest from July 2016 as a fixed price of $15.75 per share. On December 1, 2016, Sibanye proposed a transaction in a range of $17.50 to $17.75 per share, below what the 30% premium to the thirty-day VWAP would have contemplated.

The petitioners object that rather than breaking off discussions or continuing the sale process, the Board negotiated a price of $18.00 per share, representing the maximum that Sibanye could pay under its financing arrangements. They argue that the highest price a bidder is willing to pay is not the same as fair value. *See, e.g.*, *M.P.M. Enters.*, 731 A.2d at 797 (cautioning that the merger price must be supported "by evidence tending to show that it represents the going concern value of the company rather than just the value of the company to one specific buyer"); *In re Appraisal of Orchard Enters., Inc.*, 2012 WL 2923305, at *5 (Del. Ch. July 18, 2012) ("[A]lthough I have little reason to doubt Orchard's assertion that no buyer was willing to pay Dimensional $25 million for the preferred stock and an attractive price for Orchard's common stock in 2009, an appraisal must be focused on Orchard's going concern value.").

The petitioners' objection resembles similar arguments that the Delaware Supreme Court rejected in *Dell* and *DFC*. In *Dell*, the trial court found that the price negotiations during the pre-signing phase were limited by what the financial sponsors could pay based on their leverage-buyout pricing models. The respondent had conceded that the LBO model was not “oriented toward solving for enterprise value,” and the special committee's financial advisors had briefed the committee about the LBO model and how financial sponsors would use it. *Dell Trial*, 2016 WL 3186538, at *29 (internal quotation marks omitted). The committee's financial advisors used a similar model to calculate the maximum prices that a financial sponsor could pay. *See id.* at *30. The evidence indicated that the financial sponsors bid consistently with the results of an LBO model, and their negotiations with the committee proceeded within that framework. *See id.* at *30–32. In addition to the record evidence, the trial court relied on treatises which explained how the price generated by an LBO model can diverge from fair value.[18] Based on this evidence, the trial court found that the original merger consideration “was dictated by what a financial sponsor could pay and still generate outsized returns,” rather than Dell's value as a going concern. *Id.* at *32.

***37** Three months later, the trial court in *DFC* reached a similar conclusion when evaluating the deal price paid by a financial sponsor (Lone Star) to acquire the company (DFC) that was the subject of the appraisal proceeding. Although the trial court regarded the deal price as sufficiently reliable to use as a valuation input, the court expressed concern that “Lone Star's status as a financial sponsor ... focused its attention on achieving a certain internal rate of return and on reaching a deal within its financing constraints, rather than on DFC's fair value.” *In re Appraisal of DFC Glob. Corp. (DFC Trial)*, 2016 WL 3753123, at *22 (Del. Ch. July 8, 2016) (subsequent history omitted).

The appeal from the trial-level ruling in *DFC* reached the Delaware Supreme Court before the appeal in *Dell*. The Delaware Supreme Court rejected the trial court's finding that the buyer's financial constraints limited the price it could pay and caused the deal price to diverge from fair value, stating:

> To be candid, we do not understand the logic of this finding. Any rational purchaser of a business should have a targeted rate of return that justifies the substantial risks and costs of buying a business. That is true for both strategic and financial buyers. It is, of course, natural for all buyers to consider how likely a company's cash flows are to deliver sufficient value to pay back the company's creditors and provide a return on equity that justifies the high costs and risks of an acquisition. But, the fact that a financial buyer may demand a certain rate of return on its investment in exchange for undertaking the risk of an acquisition does not mean that the price it is willing to pay is not a meaningful indication of fair value. That is especially true here, where the financial buyer was subjected to a competitive process of bidding, the company tried but was unable to refinance its public debt in the period leading up to the transaction, and the company had its existing debt placed on negative credit watch within one week of the transaction being announced. The “private equity carve out” that the Court of Chancery seemed to recognize, in which the deal price resulting in a transaction won by a private equity buyer is not a reliable indication of fair value, is not one grounded in economic literature or this record.

DFC, 172 A.3d at 349–50. When the Delaware Supreme Court subsequently ruled on the discussion of the LBO model in the appeal from the trial-level ruling in *Dell*, the high court relied on its decision in *DFC*, explaining:

> [W]e rejected this view [in *DFC*] and do so again here given we see “no rational connection” between a buyer's status as a financial sponsor and the question of whether the deal price is a fair price. After all, “all disciplined buyers, both strategic and financial, have internal rates of return that they expect in exchange for taking on the large risk of a merger, or for that matter, any sizeable investment of its capital.”

Dell, 177 A.3d at 28 (quoting *DFC*, 172 A.3d at 374–76).

The reasoning that led the Delaware Supreme Court to reject the implications of the LBO model for deal pricing indicates that comparable constraints on a prevailing bidder's ability or willingness to pay—whether resulting from IRR hurdles, a comparatively higher cost of capital, or limits on the availability of financing—should not undermine the deal price as an indicator of fair value if the sale process was otherwise sufficiently open. Both *Dell* and *DFC* suggest that a post-signing market test can be the predominant source of price competition. In *Dell*, the only participants during the pre-signing phase were the two financial sponsors, whom the committee permitted to participate at any one time and each of whom priced their deals using an LBO model. *See* *Dell Trial*, 2016 WL 3186538, at *9–10, *30–31, *37. In *DFC*, although the company initially engaged in a broad solicitation, the only bidders who engaged and submitted indications of interest during the pre-signing phase were two financial sponsors, one of whom soon dropped out. *See* *DFC Trial*, 2016 WL 3753123, at *4.

***38** On the facts of this case, Sibanye had the ability to pay more. Although it had not secured transactional financing that would have supported a price greater than $18.00 per share, Sibanye could have deployed cash on hand or drawn on its revolving line of credit. As a rational bidder for Stillwater, Sibanye understandably had a targeted rate of return that it needed to satisfy to justify the substantial risks and high costs of the acquisition. That Sibanye did not bid higher does not mean that the price it agreed to pay did not reflect fair value when its bid prevailed. *See* *Aruba*, 210 A.3d at 136; *Dell*, 177 A.3d at 28; *DFC*, 172 A.3d at 349–50, 374–76.

The negotiations between Stillwater and Sibanye over price, together with Sibanye's refusal to pay more, provides strong evidence of fair value. In *Aruba*, the Delaware Supreme Court explained that

> a buyer in possession of material nonpublic information about the seller is in a strong position (and is uniquely incentivized) to properly value the seller when agreeing to buy the company at a particular deal price, and that view of value should be given considerable weight by the Court of Chancery absent deficiencies in the deal process.

Id. at 137. The high court observed that HP and Aruba went "back and forth over price" and that HP had "access to nonpublic information to supplement its consideration of the public information available to stock market buyers ...." *Id.* at 139. The Delaware Supreme Court elsewhere emphasized that "HP had signed a confidentiality agreement, done exclusive due diligence, gotten access to material nonpublic information" and "had a much sharper incentive to engage in price discovery than an ordinary trader because it was seeking to acquire all shares." *Id.* at 140. Given these facts, the extent of the negotiations in *Aruba* supported the reliability of the deal price. The same observations apply to Sibanye on the facts of this case. Sibanye entered into an NDA with Stillwater, conducted extensive due diligence, obtained access to material nonpublic information, and was "in a strong position (and is uniquely incentivized) to properly value the seller when agreeing to buy the company at a particular deal price."

The fact that Stillwater and Sibanye reached agreement at $18.00 per share is entitled to considerable weight. Although the petitioners perceive it to be a weakness of the pre-sale process, the Delaware Supreme Court's precedents indicate that it was a strength.

4. The Challenges To The Post-Signing Phase

In contrast to their many objections to the pre-signing phase, the petitioners have relatively few disagreements with the post-signing phase. They advance perfunctory challenges to the terms of the Merger Agreement, claiming that it prevented the stockholders from capturing the value of an increasing palladium price and foreclosed other bids. They also contend that the proxy statement contained disclosure violations.

a. The Merger Agreement And The Price Of Palladium

The petitioners observe that the price of palladium increased between signing and closing. They then object that the Merger Agreement "provided no practical way for Stillwater's stockholders to receive that additional value." PTOB at 51. In cursory fashion, they criticize the Board for not asserting the existence of a Company Material Adverse Effect or invoking the fiduciary-out clause. *Id.* at 52. This objection is not really a criticism of the sale process, but so be it.

The petitioners never engage with the terms of the Merger Agreement and how it uses the concept of a Company Material Adverse Effect. The definition of a Company Material Adverse Effect turns on any "facts, circumstance, condition, event, change, development, occurrence, result, or effect" that is materially *adverse* to the Company. JX 575, Annex A, at A-3. The arising of a Company Material Adverse Effect does not mean that something good has happened to Stillwater, like an increase in value due to rising commodity prices. It means something very bad has happened to Stillwater. In the Merger Agreement, Stillwater represented that it had not suffered a Company Material Adverse Effect, and the Merger Agreement made the accuracy of this representation a condition to Sibanye's obligation to close. *See id.* §§ 4.10.2, 7.2.1. The Merger Agreement also made the absence of a Company Material Adverse Effect a separate condition to Sibanye's obligation to close. *See id.* § 7.2.3. Stillwater did not obtain the right to declare something akin to a Company Material Beneficial Effect and terminate the Merger Agreement on that basis. The petitioners' criticism that the Board did not declare a Company Material Adverse Effect is a turn down a blind alley.

***39** The petitioners likewise never engage with the terms of the Merger Agreement and the scope of the fiduciary out. The Board had the right to change its recommendation in favor of the Merger based on (i) its receipt of a "Superior Proposal" or (ii) the occurrence of an "Intervening Event." *See* JX 525, Annex A, § 6.2.4. As permitted by Delaware law, *see* 8 *Del. C.* § 146, the Merger Agreement contained a force-the-vote provision that obligated Stillwater to take the Merger to a stockholder vote even if the Board changed its recommendation, but the stockholders would have the benefit of the Board's negative recommendation when voting. *See id.* § 6.17.2 ("Without limiting the generality of the foregoing, the Company shall submit this Agreement for the adoption by its stockholders ... whether or not a Company Adverse Recommendation Change shall have occurred or an Acquisition Proposal shall have been publicly announced or otherwise made ...."). If the Company's stockholders voted down the Merger, or under other defined circumstances, then the Company had the ability to terminate the Merger Agreement. *See id.* § 8.1.2(ii). The Board's ability to change its recommendation for an Intervening Event, however, did not include changes in commodity prices. The Merger Agreement defined the concept of an "Intervening Event" as

> any material change, event, effect, occurrence, consequence or development with respect to the Company or Parent, as applicable, that (i) is unknown and not reasonably foreseeable as of the date hereof, (ii) does not relate to any Acquisition Proposals, and (iii) does not arise out of or result from changes after the date of this Agreement in respect of prices or demand for products.

Id. at A-6; *cf.* R. Franklin Balotti & A. Gilchrist Sparks, III, *Deal Protection Measures and the Merger Recommendation*, 96 Nw. U. L. Rev. 467, 468 (2002) (explaining the importance of an intervening event provision for the target who "discover[s] the world's largest deposit of gold under its headquarters, causing the value of the target to increase dramatically"). Post-signing changes "in respect of prices or demand" for palladium thus would not qualify as an Intervening Event and would not support a change of recommendation. The petitioners' criticism that the Board did not exercise its fiduciary out based on changes in commodity prices is another wrong turn.

The record reflects that Stillwater did not want the merger consideration to float with the price of palladium. McMullen testified that "we wanted to know with certainty what was the number that we were taking to shareholders as the value proposition." McMullen Tr. 770. That was a legitimate goal.

The petitioners may well take these explanations and run with them, claiming that the situation was even worse than they thought because the Board lacked the power to do things that the petitioners previously believed the Board had merely failed to consider. Regardless, the petitioners' bottom-line criticism of the Merger Agreement misses the point of what the contract was trying to accomplish. The Merger Agreement was not attempting to give the stockholders the benefit of a transaction that included the potential upside or downside that would result from changes in the price of palladium after signing. The Merger Agreement was trying to provide stockholders with the ability to opt for the comparative certainty of deal consideration equal to $18.00 per share.

More broadly, the petitioners are mistaken when they claim that there was no practical way for Stillwater's stockholders to receive the additional value that the increased commodity price could generate. If Stillwater's stockholders had wanted to capture the increased value of palladium, then they could have voted down the Merger and kept their shares. The spot price of palladium was readily available public information that Stillwater's stockholders could take into account when deciding how to vote.

b. The Merger Agreement And Competing Bids

In conclusory fashion, the petitioners object that the Merger Agreement "contained a no solicitation provision and 5-day matching rights," which the petitioners characterize as "more buyer friendly than the protections provided in *AOL* that this Court described as creating 'structural disadvantages dissuading any prospective bidder.' " PTOB at 51–52 (quoting AOL, 2018 WL 1037450, at *9, and noting that the decision "describe[ed] a no-shop provision with a 3.5% termination fee and unlimited 3-day matching rights"). The petitioners argue that Sibanye's matching rights deterred interested buyers from making a topping bid because Sibanye could simply match any competing proposal.

***40** The *AOL* decision was a fact-specific ruling that turned on the court's view of the sale process in that case, after hearing the witnesses at trial and considering the evidentiary record. The *Dell* and *DFC* decisions issued while the matter was pending, and the trial court requested supplemental briefing on the effect of those decisions. Both sides continued to argue for determining fair value based on financial metrics rather than by relying on the deal price. AOL, 2018 WL 1037450, at *1. The court nevertheless examined the sale process and regarded the persuasiveness of the deal price as "a close question." *Id.* On balance, the court decided not to rely on the deal price, except as cross check to a DCF valuation. In reaching this outcome, the court placed heavy weight on a comment made by AOL's CEO, shortly after the signing of the deal, in which he said he was "committed to doing the deal with Verizon" and emphasized that he "gave the team at Verizon my word that ... this deal is going to happen." Id. at *9. The court found that the comment "could reasonably cause potential bidders to pause when combined with the deal protections here." *Id.* A trial court's job is to make that type of decision and determine when the evidence warrants a case-specific departure from a general rule.

The broader Delaware corpus supports the general principle that the package of defensive measures found in the Merger Agreement in this case is sufficient to permit an effective post-signing market check, even when matching rights are present. As noted, commentators have perceived that under the Delaware Supreme Court's recent appraisal decisions, a sale process involving a publicly traded firm will function as a reliable indicator of fair value as long as it would pass muster if reviewed under enhanced scrutiny in a breach of fiduciary duty case. *See* Hamermesh & Wachter, *supra*, at 962, 982–83; Korsmo & Myers, *supra*, at 269. Based on numerous trial court precedents, the suite of deal protection measures in the Merger Agreement would not have supported a claim for breach of fiduciary duty.[19] The suite of deal protections in the Merger Agreement compared favorably with the deal protections in *C & J Energy* and *PLX*, which this decision has discussed at length.

***41** The *Aruba* decision involved a similar suite of deal protections. The merger agreement in that case "prohibited Aruba from soliciting competing offers and required the Aruba Board to continue to support the merger, subject to a fiduciary out and an out for an unsolicited superior proposal" and included a termination fee equal to 3% of the merger's equity value. *Aruba Trial*, 2018 WL 922139, at *21, *38. The matching rights were similar too: HP had "an unlimited match right, with five days to match the first superior proposal and two days to match any subsequent increase, and during the match period Aruba had to negotiate exclusively and in good faith with HP." Id. at *38 (footnote omitted). Viewing the deal protections holistically, the Delaware Supreme Court found that potential buyers had an open chance to bid, which supported the high court's use of a deal-price-less-synergies metric to establish fair value. *See* Aruba, 210 A.3d at 136.

The Delaware Supreme Court has explained that a post-signing market check is effective as long as "interested bidders have a fair opportunity to present a higher-value alternative, and the board has the flexibility to eschew the original transaction and accept the higher-value deal." *C & J Energy*, 107 A.3d at 1068. This description comports with guidance from a frequently cited treatise, which identifies "critical aspects" of a merger agreement that does not "preclude or impermissibly impede a post-signing market check." 1 Lou R. Kling & Eileen T. Nugent, *Negotiated Acquisitions of Companies, Subsidiaries and Divisions* § 4.04[6][b], at 4-89 to -90 (1992 & Supp. 2019).

> First, the economics of the executed agreement must be such that it does not *unduly* impede the ability of third parties to make competing bids. Types of arrangements that might raise questions in this regard include asset lock-ups, stock lock-ups, no-shops, force-the-vote provisions, and termination fees. The operative word is "unduly;" the impact will vary depending upon the actual type of device involved and its specific terms.
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> Second, the target should be permitted to disclose confidential information to any third party who has on its own (i.e., not been solicited) "shown up" in the sense that it has submitted a proposal or, at a minimum, an indication of interest which is, or which the target believes is, reasonably likely to lead to (and who is capable of consummating) a higher competing bid. In this regard, the target should also be able to negotiate with such third parties. This removes any informational advantage that the initial (anointed) purchaser may have.
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> * * *
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> Finally, the target board of directors should have the contractual right, without violating the acquisition agreement, to withdraw or modify its recommendation to shareholders with respect to the transaction provided for in the executed acquisition agreement.

Id. at 4-90 to -94.1 (footnotes omitted).

Using this framework, the deal protections did not preclude or impermissibly impede a post-signing market check. For starters, any party could submit a bona fide written Acquisition Proposal. If the Board determined that the Acquisition Proposal "constitutes, or could reasonably be expected to result in, a Superior Proposal" and entered into an "Acceptable Confidentiality Agreement" with the party making the proposal, then the Board could "engage in negotiations or discussions with, or furnish any information to," the party making the Acquisition Proposal. JX 545, Annex A, § 6.2.2. Additional requirements included that the Company notify Sibanye within twenty-four hours of its determination, furnish Sibanye "substantially concurrently" with any information provided to the third party, and not share any of Sibanye's confidential information unless required by law. *Id.* The Company also had to notify Sibanye of the terms of the Acquisition Proposal and the identity of the third party making it, then keep Sibanye informed of any developments on a reasonably prompt basis. *Id.* § 6.2.3.

***42** After that point, if the Board determined that the Acquisition Proposal constituted a Superior Proposal and that its fiduciary duties required it, then the Board could change its recommendation in favor of the Merger, provided that before doing so, the Board gave Sibanye five days in which to match the Superior Proposal or otherwise offer changes to the Merger Agreement to avoid the change of recommendation. The Board could also withdraw or modify its recommendation for an Intervening Event, again conditioned on giving Sibanye five days in which to propose changes to the Merger Agreement to avoid the change of recommendation. If the stockholders voted down the deal, then Stillwater could terminate the Merger Agreement, subject only to paying a termination fee and expense reimbursement equal to 1.2% of the Merger's equity value.

The post-signing market check began on December 9, 2016, when Sibanye and the Company announced the Merger. It ended on April 26, 2017, when the Company's stockholders approved the Merger Agreement. The resulting passive market check lasted 138 days, close to the 153 days in *C & J Energy* and far longer than many of the passive, post-signing market checks that the Delaware courts have approved. *See* App.

During the post-singing market check, no one bid. The failure of any other party to come forward provides significant evidence of fairness, because "[f]air value entails at minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay." *Dell*, 177 A.3d at 29; *see id.* at 32, 34. The absence of a higher bid indicates "that the deal market was already robust and that a topping bid involved a serious risk of overpayment," which in turn "suggests the price is already at a level that is fair." *Id.* at 33. As in *Aruba*, "[i]t cannot be that an open chance for buyers to bid signals a market failure simply because buyers do not believe the asset on sale is sufficiently valuable for them to engage in a bidding contest against each other." *Aruba*, 210 A.3d at 136. Instead it suggests that "the target's value is not sufficiently enticing to buyers to engender a bidding war above the winning price." *Id.*

c. The Stockholder Vote

In their last challenge to the post-signing phase, the petitioners assert that the stockholders approved the Merger based on incomplete and misleading information. They devote only two pages in their opening brief to this argument, the bulk of which describes the legal principles that apply in fiduciary duty cases. *See* PTOB at 53–54 (citing *Morrison v. Berry*, 191 A.3d 268, 282–83 (Del. 2018); and *Corwin v. KKR Fin. Hldgs., LLC*, 125 A.3d 304, 312 (Del. 2015)). The factual description of their disclosure theory appears in just three sentences:

> Stillwater's stockholders were told McMullen led the sale process, but they were never informed that he was preparing to leave the Company or the scope of his outside business ventures. In addition, Stillwater stockholders were told that Wadman left the Company prior to closing, but they were never informed of the context of his departure or his "noisy exit." Stillwater's stockholders were also provided no information regarding the Company's exploration zones.

PTOB at 53–54. They devote the same amount of space to this theory in their reply brief, although the text extends over three pages. Dkt. 228 at 26–28. In their reply brief, they argue that stockholders should have been told that Wadman raised concerns about McMullen's conflicts of interest and "his manner of soliciting interest from third parties," and that Wadman was "retaliated against for doing so." *Id.* at 27. They also argue that stockholders should have been told that McMullen "was in violation of his 2016 employment agreement" while running the sale process because of his roles with Nevada Iron and New Chris. *Id.*

***43** The petitioners' argument about Stillwater's exploration zones does not appear to hold up under their own understanding of the law. The petitioners elsewhere argued persuasively that under Industry Guide 7, promulgated by the Securities and Exchange Commission, Stillwater was not permitted to disclose information about the value of the Company's exploration zones. *See*, *infra*, Pt. II.B.3.a.

The disclosure theories about McMullen and Wadman would likely have some merit if the petitioners had done more to articulate them, support them with case law, and explain their relationship to a determination of fair value. Presumably the petitioners' believe that if stockholders had been told that McMullen was pursuing a sale in part because of his personal interest in exiting the Company and that Wadman resigned because of disputes over how McMullen handled the sale process, then some stockholders might have questioned whether the deal price reflected fair value.

These contentions would have to overcome the doctrine against self-flagellation. *See, e.g.*, *Loudon v. Archer-Daniels-Midland Co.*, 700 A.2d 135, 143 (Del. 1997). That said, the proxy statement should have disclosed McMullen's interest in retiring, his roles with GT Gold and New Chris, and their implications for his employment agreement. Stockholders also should have been told that Wadman resigned because of disputes with senior management about the conduct of the sale process.

Although I have tried to give the petitioners the benefit of the doubt by crediting their conclusory assertions in this fashion, I am not convinced that their arguments are sufficient to undermine the stockholder vote as an expression of the preference of a supermajority of Stillwater's stockholders for a sale rather than having the Company continue as a standalone entity. The Delaware Supreme Court has explained that "[t]he issue in an appraisal is not whether a negotiator has extracted the highest possible bid. Rather, the key inquiry is whether the dissenters got fair value and were not exploited." *Dell*, 177 A.3d at 33. The disclosures that the petitioners say the Company should have made could have affected stockholders' views about whether their negotiators had extracted the highest possible bid. If stockholders had been provided with information about McMullen's interests and Wadman's withdrawal, then perhaps some stockholders would have inferred that a different negotiator might have pushed for more from Sibanye or worked harder during the pre-signing phase to find a bidder who could have paid a higher price (an inference undercut by the absence of any topping bid during the post-signing phase). They would not have had any reason to revise their assessment of the Company's prospects as a standalone entity or to vote down the Merger in the belief that the Company was more valuable as a going concern in its operative reality as a widely held, publicly traded firm.

Because of the disclosure issues, this decision does not give heavy weight to the stockholder vote. Nevertheless, the vote remains a positive factor when evaluating whether the deal price reflected fair value. If stockholders believed that the Company was worth more, they could have voted down the Merger and retained their proportionate share of the Company as a going concern. By approving the Merger at $18.00 per share, they evidenced their belief that the deal price provided fair value and was not exploitive.

5. The Sale Process Was Reliable.

***44** Sibanye proved by a preponderance of the evidence that the sale process made the deal price a persuasive indicator of fair value. The sale process was not perfect, and the petitioners highlighted its flaws, but the facts of this case, when viewed as a whole, compare favorably or are on par with the facts in *C & J Energy*, *PLX*, *DFC*, *Dell*, and *Aruba*.

The sale process that led to the Merger bore objective indicia of fairness that rendered the deal price a reliable indicator of fair value. To reiterate, it was an arm's-length transaction. It was approved by an unconflicted Board and by Stillwater's stockholders. And it resulted from adversarial price negotiations between Stillwater and Sibanye. Most significantly, no bidders emerged during the post-signing phase, despite a Merger Agreement that contained a suite of deal protections that would pass muster under enhanced scrutiny.

The petitioners pointed to problems during the early phases of the sale process before the Board began exercising serious oversight and before BAML was retained. Those flaws are factors to consider, but they do not undermine the reliability of the sale price given what happened later. BAML's pre-signing canvass was a positive factor. The negotiations with Sibanye were also a positive factor. And the process culminated in an effective, albeit passive, post-signing market check. If Stillwater had pursued a single-bidder strategy and only engaged with Sibanye, then the terms of the Merger Agreement would have facilitated a sufficiently reliable post-signing market check to validate the deal price. Stillwater did more than what would have been sufficient under a single-bidder scenario.

It is theoretically possible that a more thorough pre-signing process or more vigorous negotiations might have generated a higher transaction price for Stillwater's stockholders, but the issue in an appraisal "is not whether a negotiator has extracted the highest possible bid." Dell, 177 A.3d at 33.

> Capitalism is rough and ready, and the purpose of an appraisal is not to make sure that the petitioners get the highest conceivable value that might have been procedure had every domino fallen out of the company's way; rather, it is to make sure that they receive fair compensation for their shares in the sense that it reflects what they deserve to receive based on what would fairly be given to them in an arm's-length transaction.

DFC, 172 A.3d at 370–71. "[T]he key inquiry is whether the dissenters got fair value and were not exploited." *Dell*, 177 A.3d at 33.

The Merger in this case was rough and ready. McMullen and the Board did not adhere to the best practices and transactional niceties that an advisor steeped in Delaware decisions would recommend. Nevertheless, given the arm's-length nature of the Merger, the premium over market, and the substance of what took place during the sale process, it is not possible to say that an award at the deal price would result in the petitioners being exploited.

6. The Adjustment For Value Arising From The Merger

Section 262 provides that "the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation ...." 8 *Del. C.* § 262(h). "[I]t is widely assumed that the sale price in many M&A deals includes a portion of the buyer's expected synergy gains, which is part of the premium the winning buyer must pay to prevail and obtain control." *DFC*, 172 A.3d at 371. "In an arm's-length, synergistic transaction, the deal price generally will exceed fair value because target fiduciaries bargain for a premium that includes ... a share of the anticipated synergies ...." *Olson v. ev3, Inc.*, 2011 WL 704409, at *10 (Del. Ch. Feb. 21, 2011). "[S]ection 262(h) requires that the Court of Chancery discern the going concern value of the company irrespective of the synergies involved in a merger." *M.P.M. Enters.*, 731 A.2d at 797. To derive an estimate of fair value, the court must exclude "any synergies or other value expected from the merger giving rise to the appraisal proceeding itself ....” *Golden Telecom Trial*, 993 A.2d at 507. This means the trial court “must exclude ... the amount of any value that the selling company's shareholders would receive because a buyer intends to operate the subject company, not as a stand-alone going concern, but as part of a larger enterprise, from which synergistic gains can be extracted.” *Aruba*, 210 A.3d at 133 (internal quotation marks omitted).

***45** Sibanye's valuation expert was Mark Zmijewski, an emeritus professor of finance at the University of Chicago and a consultant at Charles River Associates. Zmijewski opined that the evidence he reviewed did “not indicate that the Transaction resulted in quantifiable synergies.” JX 652 ¶ 66 [hereinafter Zmijewski Rep.]; *see* Zmijewski Tr. 1146. Sibanye told its stockholders that the price did not reflect any synergies. JX 421 at '224. McMullen testified at trial that he did not believe there were any synergies arising from the Merger. McMullen Tr. 801. There is accordingly no reason to exclude any value from the deal price based on synergies.

In this proceeding, Sibanye argued that despite the absence of quantifiable cost synergies or revenue synergies, it willingly paid more than fair value for Stillwater, resulting in a portion of the consideration reflecting value “arising from the accomplishment or expectation of the merger or consolidation ....” 8 *Del. C.* § 262(h). In its opening brief, Sibanye argued that it paid a premium for two strategic reasons: (i) to facilitate entry into the United States and (ii) to expand its share of the PGM market. Sibanye also argued that it could pay a premium in the Merger because after the Merger, it could obtain a better rating on its debt. *See also* Zmijewski Tr. 1120–22; JX 397 at '452; JX 498 at 20; JX 486 at 1; Rosen Tr. 407–08. Each of these reasons identifies a valuable aspect of Stillwater based on its operative reality as a going concern. Stillwater was the only PGM producer located in the United States, and it generated significant cash flow. None of these features represented a source of value “arising from the accomplishment or expectation of the merger or consolidation.”

Sibanye failed to meet its burden of proof to establish a quantifiable amount that the court should deduct from the deal price. This decision does not make any downward adjustment to the deal price to compensate for combinatorial value.

7. The Adjustment For Changes In Value Between Signing And Closing

Under Section 262, the time for determining the value of a dissenter's shares is the point just before the merger closes. *See Appraisal Rights, supra*, at A-33. The deal price provides a data point for the value of the company as of the date of signing, but the valuation date for an appraisal is the date of closing. Consequently, if the value of the corporation changes between the signing of the merger and the closing, the fair value determination must be measured by the “operative reality” of the corporation at the effective time of the merger. *Technicolor II*, 684 A.2d at 298.

In a merger involving a widely held, publicly traded company, some gap between signing and closing will usually exist. The customary need to prepare and disseminate disclosure documents, then complete a first-step tender offer or obtain a stockholder vote will typically result in several months elapsing between signing and closing. *See* Robert T. Miller, *The Economics of Deal Risk: Allocating Risk Through MAC Clauses in Business Combination Agreements*, 50 Wm. & Mary L. Rev. 2007, 2018–19 (2009) (discussing timelines for various transaction structures). If regulatory approvals are required, the temporal gap can expand. *Id.* at 2020–23. During this period, the value of the company could rise or fall.

Despite the customary existence of a temporal gap between signing and closing, Delaware appraisal decisions have typically not made adjustments to the deal price to reflect a valuation change during the post-signing period. In *Union Illinois*, this court relied for the first time on a deal-price-less-synergies metric when determining the fair value of a privately held bank (UFG). *See Union Ill.*, 847 A.2d at 343. Six months elapsed between signing and closing, and the petitioners objected to using the deal price because of the temporal gap. The trial court described this argument as a “quibble” and as “not a forceful objection,” because “[t]he negotiation of merger terms always and necessarily precedes consummation.” *Id.* at 358. Turning to the facts of the case, the court found that the petitioners were not able “to cite any rational explanatory factor that indicates why an investor would perceive UFG's future more optimistically on New Year's Eve 2001 than they did on the preceding Fourth of July.” *Id.* UFG had experienced “a modest upward adjustment in its [net income margin] in the second half of 2001,” but the court saw no evidence that the increase was sustainable or would alleviate UFG's problems complying with capital adequacy standards. *Id.* Although UFG had refinanced its debt, the loan came from the acquirer, and UFG was not in a position to either service that debt or refinance it completing the merger. *Id.* The court concluded that "[c]onsidered fairly, the record does not support the idea that UFG was more valuable at the end of 2001 than it was when the Merger Agreement was signed." *Id.*

***46** In *PetSmart*, this court awarded fair value based on the deal price in a case involving a publicly traded firm. *See* *In re PetSmart, Inc.*, 2017 WL 2303599, at *2 (Del. Ch. May 26, 2017). The court regarded the petitioners' argument that the merger price "was stale by the time of closing" as "at best speculative." *Id.* at *31. Citing *Union Illinois*, the court explained that "[m]ergers are consummated after the consideration is set. That temporal separation, however, does not in and of itself suggest that the merger consideration does not accurately reflect the company's going concern value as of the closing date." *Id.* The court then turned to the petitioners' case-specific arguments:

> Petitioners would have me conclude that the Merger Price was stale because, in the gap between signing and closing, PetSmart's fortunes took a miraculous turn for the better. While the record indicates that the Company did enjoy some favorable results in Q4 2014, such as an uptick in comparable store sales growth, I am not convinced that these short-term improvements were indicative of a long-term trend. In fact, all testimony at trial was to the contrary—the Board, as well as Teffner, believed that the Q4 results were temporary and provided no basis to alter their view of the Company's long-term prospects. These perceptions were born out in Q1 2015 (when the Merger closed) during which PetSmart's comparable store sales dropped to 1.7%. At year end, PetSmart reported comparable store sales growth of 0.9%, a 40% miss from the Management Projections in just the first projection year.

Id. (footnotes omitted). The petitioners in *PetSmart* thus failed to carry their burden of proving that the value of the company had changed.

Most recently, in *Columbia*, this court awarded fair value based on the deal price in another case involving a publicly traded firm. *See* *In re Appraisal of Columbia Pipeline Gp., Inc.*, 2019 WL 3778370, at *1 (Del. Ch. Aug. 12, 2019). The company developed, owned, and operated natural gas pipelines, storage facilities, and other midstream assets, and it had a business plan that called for raising large amounts of equity financing through a master limited partnership ("MLP"). Before agreeing to be acquired, the company had been unable to use the MLP structure to raise capital because of adverse trends in the MLP financing market. The merger agreement was signed on March 17, 2016, and the transaction closed on July 1, 2016. The petitioners argued that in the interim, the market for MLP equity had improved and prices for energy commodities had increased. *See id.* at *45. The court found that the petitioners had not carried their burden of proving how to quantify the alleged improvements in the form of a higher deal price. *Id.* The court also found that the improvement in two MLP indices did not persuasively support the claim that the company would have been able to raise capital efficiently through its MLP. The court similarly rejected any valuation increase based on the prices of energy related commodities, because everyone agreed that the company's value did not depend on commodities. As a midstream company, it did not own, buy, or sell the commodities that it transported or stored. *Id.*

The one arguable exception is *Lender Processing*, where this court awarded fair value based on the value of the deal price at closing, rather than at signing, where the deal consideration consisted of 50% cash and 50% stock. *See* *Lender Processing*, 2016 WL 7324170, at *1, *8. Because of the stock component, the value of the merger consideration increased from $33.25 per share at signing to $37.14 per share at closing. *Id.* The petitioners pointed to the existence of the temporal gap as a reason not to rely on the deal price or other market-based metrics associated with the signing of the deal. The respondent pointed to the absence of a topping bid as validating the deal price. After reviewing the evidence, the court concluded that the final merger consideration "was a reliable indicator of fair value as of the closing" and that "because of synergies and a post-signing decline in the Company's performance, the fair value of the Company as of the closing date did not exceed" that amount. *Id.* at *23. The acquirer's expert had not tried to quantify the synergies or the amount of the post-signing valuation decline, and the court concluded that the respondent had failed to carry its burden of proof on those issues. *Id.* at *33. By using the deal price as measured at closing rather than at signing, the *Lender Processing* decision accounted for changes in value between signing and closing, but without making an explicit adjustment.

***47** All four precedents considered whether the deal-price metric needed to be adjusted to reflect changes in value between signing and closing. The decisions thus indicate that an adjustment to the deal price can be warranted. But the decisions also show that the proponent of the adjustment must carry its burden by identifying a persuasive reason for the change and proving the amount.

At a minimum, it would seem to make sense to adjust the deal price for inflation. When the parties agreed to the deal price on December 8, 2016, they reached agreement on a price measured in dollars valued as of that date. Between that date and the closing on May 4, 2017, the purchasing power of those dollars declined. If Stillwater had precisely the same value in the abstract on May 4, 2017, as it did on December 8, 2016, it would still be necessary to adjust the number of dollars used to express that value to reflect the intervening decline in what the value of a dollar represented. Adjusting the deal price for inflation would achieve this result.[20]

As their valuation expert, the petitioners relied on Howard Rosen, a senior managing director at FTI Consulting. When adjusting the unaffected trading price, Rosen used an inflation rate of 2% per annum to account for the decrease in the value of dollars between signing and closing, then made further adjustments. *See* JX 728 ¶¶ 5.19, 5.25 to 5.28. A similar inflation-based adjustment could be made to the deal price, generating a value on the closing date of $18.14 per share, but no one argued for it.

The nature of Stillwater's business makes this case a plausible one for an upward adjustment that goes beyond inflation. Stillwater was a mining concern that primarily produced palladium and platinum. Stillwater's cash flows depended on the prices of those metals, so when the prices of those metals increased or decreased materially, the value of the Company increased or decreased materially as well. The Company's annual report for 2016 explained the relationship as follows:

> ***48** The Company's earnings and cash flows are sensitive to changes in PGM prices – based on 2016 revenue and costs, a 1% (or approximately $7 per ounce) change in the Company's average combined realized price for palladium and platinum would result in approximately a $7.1 million change to before-tax net income and a change to cash flows from operations of approximately $3.9 million.

JX 728 ¶ 5.21 (quoting Stillwater Mining Company, Annual Report (Form 10-K) (Feb. 16, 2017)). The Merger was signed on December 9, 2016. The Merger closed on May 4, 2017. Between signing and closing, the prices of palladium and platinum increased materially, with a direct effect on Stillwater's value. *Id.* ¶ 5.20.

Rosen determined that the sales-weighted price of Stillwater's commodities increased by 5.9% between signing and closing. Using the formula in Stillwater's annual report, Rosen calculated the valuation impact of the additional cash flow as ranging from $248 million (using a 11.2% WACC) to $285 million (using a 10% WACC), which equated to an increase of between $2.00 to $2.30 per share. *Id.* He regarded his estimate as conservative because he kept production constant and did not account for new sources, such as Blitz, coming on line. *Id.* ¶¶ 5.23 to 5.25. Rosen used this figure to make adjustments to the unaffected trading price. In theory, he could have made similar adjustments to the merger price.

As this discussion indicates, the petitioners never argued for an adjustment *to the deal price* based on an increase in value between signing and closing. As discussed in the next section, *Sibanye* argued that the court could make an adjustment *to the unaffected trading price* and use the adjusted trading price as an indicator of fair value. The petitioners countered that argument by proposing an adjustment of their own that resulted in the adjusted trading price exceeding the deal price. Those arguments addressed the trading price, not the deal price. There could be considerable conceptual overlap between the approaches, but there could also be significant differences.

A petitioner seeking to make valuation-based adjustments to a reliable deal price also would need to confront the implications of the post-signing market check. As in *Lender Processing*, a respondent in an appraisal case could easily argue that if a company's value increased between signing and closing, then a competing bidder would have perceived that value and offered more than the deal price. The respondent would argue that if no one bid, then that fact would call for rejecting the petitioners' evidence of a valuation increase. There are several possible responses to this argument.

One response is a relatively small point from a valuation perspective: the termination fee. Using this case as an example, if a topping bidder made a Superior Proposal, and if the Board changed its recommendation, and if the stockholders voted down the Merger, then Stillwater would have to pay Sibanye a termination fee of $16.5 million plus reimbursement of Sibanye's expenses up to $10 million, for a total payment of $26.5 million or 21.6 cents per share. Those amounts would reduce Stillwater's value to the acquirer, making the acquirer neutral as to any increase in Stillwater's value that did not clear that level. The point of indifference is actually higher, because a competing bidder would incur expenses of its own to make the competing bid. Ignoring those incremental expenses and focusing only on the sell-side fees, Stillwater's value could increase by up to $26.5 million without a rational acquirer having any reason to bid. The absence of a topping bid could not rule out a valuation change of this magnitude, but an award above the deal price that fell within the range permitted by the termination fee would likely be cold comfort to the typical appraisal petitioner.

***49** A more significant counterargument would focus on the timing of the valuation change. A premise that underlies the effectiveness of the post-signing market check is that other bidders learn that the target is for sale when the deal is announced, can examine the target for themselves, and if they value the target more highly (taking into account synergies and other sources of bidder-specific value), then they can intervene. Under this theoretical framework, competing bidders can begin work shortly after the announcement, giving them the full timeline between the signing and the vote in which to intervene. When the potential overbid would be induced by a change in the value of the target company, the time for the competing bidder to act does not begin with the announcement of the deal, but rather when the bidder learns of the valuation change. The delayed signal shortens the amount of time for the bidder to intervene. As the date of the stockholder vote approaches, it becomes less likely (all else equal) that a bidder will intervene, if only because less time is available in which to do so. Because of this effect, a failure to bid during the post-signing phase provides a much noisier signal about changes in the target's value than it does about the absence of higher-valuing bidders. In this case, the increase in value that resulted from changes in the spot price did not really begin until February 2017, two months after signing. It dropped in March, then picked up again in April, when the stockholder vote took place.

A third counterargument would examine the possibility of changes in value after the stockholder vote but before closing. As this case illustrates, a competing bidder's only meaningful opportunity to intervene is before the stockholders approve the transaction. In a case where closing is delayed significantly after the stockholder vote because of issues such as the need for regulatory approvals, the post-vote temporal gap would matter more.

Perhaps the most significant problem with relying on a post-signing market check to rule out an increase in the target's standalone value is that the resulting valuation improvement would be available to any bidder. The competition for the incremental value would likely operate as a common value auction, defined as an auction in which "every bidder has the same value for the auctioned object." Peter Cramton & Alan Schwartz, *Using Auction Theory to Inform Takeover Regulation*, 75 L. Econ. & Org. 27, 28–29 (1991). In a competition for that incremental value, the incumbent bidder's matching right would loom large. To make it worthwhile to bid, a potential deal jumper would not only have to perceive that the value of the target had increased above the level set by the deal price plus the termination fee and fee reimbursement plus the deal jumper's likely transaction costs, but also perceive a pathway to success that was sufficiently realistic to warrant becoming involved, taking into account the potential reputational damage that could result from being unsuccessful. Unless the competitor had a unique reason to value the increased cash flows more highly than the incumbent, the competitor should expect the incumbent to match any incremental bid.[21] In a case like this one, where the valuation increment would result from improved commodity prices that would be available to all bidders, a strong argument can be made that a competitor would not think that it had the ability to outbid the incumbent and would not try.

***50** The respondent in an appraisal proceeding could make similar arguments about the stockholder vote. If the reasons for the valuation increase were public, and stockholders still voted for the deal, then their behavior would provide contrary market evidence undermining the claim of increased value. In this case, the increase in commodity prices was publicly available information, and Stillwater's stockholders had the ability to vote down the deal if they thought the increased value from improving commodity prices changed matters. One obvious response to this argument is that to vote down the deal, stockholders would have had to prefer returning to Stillwater in its operative reality as a widely traded firm, where their only the options for liquidity were either to sell into the market or hold out for a higher-priced takeover down the road. Given these choices, stockholders might well have preferred the surer option of the deal price, even if they believed that the Company's value had increased between signing and closing such that the deal price no longer reflected fair value.

As this discussion shows, whether to adjust the deal price for an increase in value between signing and closing presents numerous difficult questions. In this case, the petitioners did not argue for an adjustment to the deal price, and so the parties did not have the opportunity to address these interesting issues. The court will not take them up at this late stage in the proceeding. The petitioners accordingly failed to prove that the deal price should be adjusted upward to reflect a change in value between signing and closing. *See Columbia*, 2019 WL 3778370, at *45. This decision finds that the deal price of $18.00 per share provides reliable evidence of fair value.

B. The Adjusted Trading Price

Sibanye contended that Stillwater's adjusted trading price is a reliable indicator of the fair value of the Company. Sibanye generates the adjusted trading price by making adjustments to the unaffected trading price, so the reliability of the adjusted trading price depends on the reliability of the unaffected trading price. As the proponent of using this valuation indicator, Sibanye bore the burden of establishing its reliability and persuasiveness.

Assessing the reliability of the trading price for Stillwater's common stock means getting "deep into the weeds of economics and corporate finance." *In re Appraisal of Jarden Corp.*, 2019 WL 3244085, at *1 (Del. Ch. July 19, 2019). The thicket of market efficiency is one such place where "law-trained judges should not go without the guidance of experts trained in these disciplines." *Id.* In this case, both sides retained financial experts who tried to lead the court through the undergrowth. Zmijewski addressed these issues for Sibanye. Israel Shaked, a professor of economics and finance at Boston University, addressed these issues for petitioners.

1. Informational Efficiency and Fundamental-Value Efficiency

The experts agreed on the difference between informational efficiency and fundamental-value efficiency. *See* Zmijewski Tr. 1087; JX 651 ¶¶ 13–27, 33–41 [hereinafter Shaked Rep.]. "[I]nformational Efficiency ... is concerned with how rapidly security prices reflect or impound new information that arrives to the market." Shaked Rep. ¶ 33 (quoting Alex Frino *et al.*, *Introduction to Corporate Finance* 305 (5th ed. 2013)). There are three recognized types of informational efficiency:

- **Weak:** a company's stock price reflects all historical price information.
- **Semi-Strong:** a company's stock price reflects all publicly available information.
- **Strong:** a company's stock price reflects both publicly available information and inside information.

No one claimed that the market for Stillwater's common stock could be informationally efficient in the strong sense. Everyone focused on whether the market for Stillwater's common stock was informationally efficient in the semi-strong sense. All of the references in this decision to informational efficiency as it relates to Stillwater's common stock therefore contemplate informational efficiency in the semi-strong sense.

***51** "While informational efficiency is a function of speed and how quickly new material information is incorporated into a stock's price, fundamental value efficiency is an incremental function of how accurately a market in which a stock trades discretely incorporates new material information." Shaked Rep. ¶ 42. The price of a security in a market that is fundamental-value efficient should reflect its intrinsic value, defined as "the present value of all cash payments to the investor in the stock, including dividends as well as the proceeds from the ultimate sale of the stock, discounted at the appropriate risk adjusted rate." Shaked Rep. ¶ 40. (internal quotation marks omitted). In other words, a stock trading in a market that is fundamental-value efficient is one in which the trading price "fully reflects all estimates, guidance and other public, material information that portray the risks and returns of a stock accurately, including all key drivers." *Id.* ¶ 41.

The experts agreed that it is impossible to observe whether a stock trades in a market that is fundamental-value efficient. *See* Zmijewski Tr. 1088, 1153–54; Shaked Report ¶ 41. According to the petitioners, this concession means that Sibanye cannot meet its burden of proof.

While theoretically valid, the petitioners' argument goes too far. Whether called fundamental value, true value, intrinsic value, or fair value, the really-real value of something is always an unobservable concept. No valuation methodology provides direct access to it. Fundamental value is like a Platonic form, and the various valuation methodologies only cutouts casting shadows on the wall of the cave. The real issue is not whether a particular method generates a shadow (they all do), but rather whether the shadow is more or less distinct than what other methods produce.

Reliance on the trading price of a widely held stock is generally accepted in the financial community, and the trading price or metrics derived from it are regularly used to estimate the value of a publicly held firm based on its operative reality in that configuration. For purposes of determining fair value in an appraisal proceeding, therefore, the trading price has a lot going for it.[22] Like democracy, the trading price may be imperfect, but it often will serve better than the other metrics that have been tried. *Cf.* Winston Churchill, *Churchill by Himself* 574 (Richard Langworth ed., 2008). The petitioners' admittedly valid objection that it is impossible to prove that a trading price reflects fundamental value is thus not one that automatically disqualifies the use of the trading price as a valuation indicator in an appraisal.

***52** In this regard, it is important to recognize that informational efficiency and fundamental-value efficiency are not all-or-nothing concepts. *See* Bradford Cornell & John Haut, *How Efficient Is Sufficient: Applying the Concept of Market Efficiency in Litigation*, 74 Bus. Law. 417, 418 (2019). A stock trading in a national market like the New York Stock Exchange will have more attributes of informational efficiency than a stock trading over the counter, but a party might be able to show that the particular over-the-counter market had sufficient attributes to regard the trading price as informationally efficient. The attributes of the over-the-counter market are likely to be consistent with a greater degree of informational efficiency than thinner and chunkier markets, such as markets for houses or entire companies.

Fundamental-value efficiency is likewise a matter of degree. A market could be precisely fundamental-value efficient in that it accurately prices the asset at exactly its true value. Or it might be nearly fundamental-value efficient in that it accurately prices the asset within some percentage, say plus or minus 3%, of its true value. Or it might be approximately fundamental-value efficient in that it accurately prices the asset within some wider range of its true value, such as a factor of two. *See id.* at 422 ("We might define an efficient market as one in which price is within a factor of 2 of value, i.e., the price is more than half of value and less than twice value." (quoting Fischer Black, *Noise*, 41 J. Fin. 553 (1986))).

Although it is impossible to test for fundamental value, there are indicators of fundamental-value efficiency. One indicator is directional consistency, in which the market for a security reacts positively to new material information that is positive, and negatively to new material information that is negative. *See* Shaked Rep. ¶¶ 43–44. Another indicator is proportionality, which examines not only whether the direction of the reaction to new material information is consistent with its content, but also whether the extent of the reaction corresponds with the informational content. *See id.* ¶ 45. In simplified terms, if a company announces a positive earnings surprise and its stock price increases, then that outcome is directionally consistent. If the stock price increases by an amount generally proportionate to the present value of the earnings surprise, then that outcome is proportionally consistent. A market that evidences directionality and proportionality is more likely to be fundamental-value efficient. A market that lacks evidence of directionality and proportionality is less likely to be fundamental-value efficient. *See id.* ¶ 46.

The question in this case is thus not whether the market for Stillwater's common stock was or was not informationally efficient. Nor is it whether the market for Stillwater's common stock was or was not fundamental-value efficient. The question is whether the market for Stillwater's common stock was informationally efficient enough, and fundamental-value efficient enough, to warrant considering the trading price as a valuation indicator when determining fair value. Put differently, the operative question in this case is whether Sibanye proved that Stillwater's common stock traded in a market having attributes that made the trading price a sufficiently reliable valuation indicator to be taken into account when determining fair value, either in conjunction with other metrics, or even as the sole metric, with the answer turning on both the attributes of the market for

Stillwater's common stock, and also on the relative reliability of the trading price compared to other metrics like the deal price and the outputs of DCF models. *See, e.g.*, Jarden, 2019 WL 3244085, at *4, *27–31 (determining fair value based on the unaffected trading price after concluding that it was comparatively the most reliable valuation indicator); Cornell & Haut, *supra*, at 425 ("What is important in legal applications is not some abstract notion of market efficiency. Rather, what is important is whether the market is sufficiently efficient in any particular situation.").

2. Evidence Of Market Efficiency

***53** The experts disagreed about the extent to which the market for Stillwater's shares was efficient. The experts discussed factors that courts have considered as indicative of informational efficiency. The experts also conducted event studies and opined on their implications for informational efficiency, directionality, and proportionality.

a. The *Cammer* And *Krogman* Factors

Zmijewski examined whether the market for Stillwater's shares exhibited attributes that courts have associated with informational efficiency. He relied on an instruction from Sibanye's counsel that "Delaware Courts cite as attributes of market efficiency characteristics such as market capitalization, public float, weekly trading volume, bid-ask spread, analyst following, and market reaction to breaking news and information." Zmijewski Rep. ¶ 49. He also analyzed the existence of market makers, eligibility to file SEC Form S-3, institutional ownership, and autocorrelation of stock returns, noting that these additional factors were considered in Cammer v. Bloom, 711 F. Supp. 1264 (D.N.J. 1989), and in Krogman v. Sterritt, 202 F.R.D. 467 (N.D. Tex. 2001). Zmijewski Rep. ¶ 51. For simplicity, and following the parties' lead, this decision refers to these attributes as the "*Cammer* and *Krogman* factors," even though not all of them were considered in those two cases.

Based on his review of the record, Zmijewski reached the following conclusions about these attributes:

- **Market Capitalization:** Zmijewski opined that "firms with a larger market capitalization tend to have larger institutional ownership," "tend to be listed on the New York Stock Exchange," and are therefore more likely to have shares that trade in markets that are informationally efficient. Zmijewski Rep. App. C ¶ 35 (citing Randall S. Thomas & James F. Cotter, *Measuring Securities Market Efficiency in the Regulatory Setting*, 63 L. & Contemp. Probs. 105, 115 (2000) (JX 896)). The Company's market capitalization averaged approximately $1.3 billion, exceeding roughly 60% of the combined equities of companies listed on the New York Stock Exchange and NASDAQ. *Id.*

- **Public Float:** Zmijewski opined that having a large percentage of shares in the public float is indicative of a trading market that is informationally efficient. *Id.* ¶¶ 42–43 (noting that the Delaware Supreme Court in *Dell* cited a public float of 1.5 billion shares representing 84.29% of the outstanding stock, and in *DFC* cited a public float of 37.5 million shares representing 95% of the outstanding stock). The Company's public float consisted of 106 million shares representing 87.4% of the outstanding stock. *Id.* ¶ 44.

- **Weekly Trading Volume:** Zmijewski opined that an average weekly trading volume of at least 2% warrants a "strong presumption" of informational efficiency. *Id.* ¶ 2 (quoting Cammer, 711 F. Supp. at 1286). The average weekly turnover for Stillwater was 6.8%. *Id.* ¶ 3.

- **Bid-Ask Spread:** Zmijewski opined that a bid-ask spread of less than 2.5% is indicative of a trading market that is informationally efficient. *Id.* ¶¶ 37–38 (citing *DFC*, 172 A.3d at 352; *Dell*, 177 A.3d at 1, 5–6, 24–27, 41; *In re* Sci.-Atlanta, Inc. Sec. Litig., 571 F. Supp. 2d 1315, 1340 (N.D. Ga. 2007); Cheney v. Cyberguard Corp., 213 F.R.D. 484, 501 (S.D. Fla. 2003); and Krogman, 202 F.R.D. at 478). The Company's average daily bid-ask spread was 0.10%. *Id.* ¶ 39.

***54** • **Analyst Coverage:** Zmijewski opined that the presence of at least five analysts following a company is indicative of a trading market that is informationally efficient. *Id.* ¶¶ 4–6 (relying on Thomas & Cotter, *supra*, at 115). Seven analysts followed the Company. *Id.* ¶ 7.

- **Market Makers:** Zmijewski opined that the presence of at least nineteen market makers is indicative of a trading market that is informationally efficient and that the same inference can be drawn when a company's shares trade on a centralized auction market like the New York Stock Exchange. *Id.* ¶¶ 8–9 (citing Cammer, 711 F. Supp. at 1293; Cheney, 213 F.R.D. at 499–500; *In re Dynex Capital, Inc. Sec. Litig.*, 2011 WL 781215, at *5 (S.D.N.Y. Mar. 7, 2011); and Zvi Bodie *et al.*, *Investments* 62–70 (12th ed. 2018)). The Company's stock traded on the New York Stock Exchange and had eighty-two market makers. *Id.* ¶ 10.

- **SEC Form S-3 Eligibility:** Zmijewski opined that a company's eligibility to register shares using SEC Form S-3 eligibility is indicative of a trading market that is informationally efficient. *Id.* ¶ 11 (citing Cammer, 711 F. Supp. at 1284). A company is eligible for Form S-3 if it, among other things, has been subject to the Securities Exchange Act of 1934 reporting requirements for more than one year, filed documents in a timely manner, and shown that it has not failed to pay certain obligations. *Id.* The Company filed Forms S-3 in 1996, 1998, 2001, 2009, and 2010. *Id.* ¶ 12.

- **Institutional Ownership:** Zmijewski opined that having a significant percentage of stock owned by institutional investors is indicative of a trading market that is informationally efficient. *Id.* ¶ 46 (citing Thomas & Cotter, *supra*, at 106, 119). As of September 30, 2016, institutions held approximately 90% of the Company's outstanding stock. *Id.* ¶ 47.

- **Autocorrelation:** Zmijewski opined that a lack of autocorrelation in a company's stock return is indicative of a trading market that is informationally efficient. *Id.* ¶ 48. Autocorrelation measures the extent to which the next day's stock price movement can be predicted based on the current day's stock price. Zmijewski found no evidence of statistically significant autocorrelation during the 254 trading days preceding the announcement of the Merger. *Id.*

- **Cause And Effect:** Zmijewski opined that market reactions to significant events are indicative of informational efficiency. *Id.* ¶ 13 (citing Cammer, 711 F. Supp. at 1287). Zmijewski found that after the Merger announcement, there was a quick and significant increase in trading volume. *Id.* ¶ 17. The first news of the Merger was released at 1:04 a.m on December 9, 2016. Pre-market trading opened at 4:00 a.m. The first trade occurred at 4:01 a.m. at $17.50. The Company's stock closed that day at $17.32 per share, with 38 million shares having traded. The day before, the Company's stock closed at $14.68 per share, and only 3.2 million shares were traded. *Id.* ¶¶ 15–16; *see* Zmijewski Tr. 1096.

Having considering the *Cammer* and *Krogman* factors, Zmijewski opined that "[t]he evidence indicates that Stillwater's common stock traded in a semi-strong efficient market." Zmijewski Rep. ¶ 49.

In response, Shaked disputed whether the *Cammer* and *Krogman* factors established informational efficiency to a sufficiently reliable degree. He opined that "the *Cammer* and *Krogman* factors have not been academically tested and are not truly conclusive in judging a market as semi-strong form efficient, but merely an indicator that a market is likely semi-strong form efficient." Shaked Rep. ¶ 23. The petitioners did not cite any academic studies or provide other forms of evidence that would undermine the use of the *Cammer* and *Krogman* factors, at least as a starting point for assessing informational efficiency. Zmijewski did not engage on this issue. He analyzed the factors because he understood that courts considered them.

b. The Event Studies

***55** The experts also conducted event studies. Zmijewski's event study tested for a cause-and-effect relationship between new information and a trading price reaction, which would provide evidence of informational efficiency. He examined five events—the four quarterly earnings releases leading up to the announcement of the Merger plus the announcement itself. Zmijewski characterized the events as positive or negative, and examined the market evidence to determine if the observations resulted in statistically significant abnormal returns. Three of the five did, but one of those was the reaction to the announcement of the Merger. Shaked persuasively observed that finding a statistically significant relationship between the trading price and the announcement of the Merger was trivial. *See* Shaked Tr. 468–69.

For the remaining four observations, Zmijewski found that only two resulted in statistically significant abnormal returns, and he admitted that he would have expected the rate of statistically significant results in an informationally efficient market to be higher. Zmijewski Tr. 1101. The events themselves do not suggest any reason why the market would have reacted in one instance and not the other. For example, for both the fourth quarter of 2015 and the third quarter of 2016, Stillwater announced higher earnings per share, yet only the former resulted in a statistically significant abnormal return.

Shaked conducted three event studies, and he analyzed the results not only for evidence of a cause-and-effect relationship consistent with informational efficiency, but also for evidence of directionality and proportionality that would provide indications of fundamental value efficiency. In his first study, Shaked looked at eleven quarterly earnings releases during the three-year period leading up to the announcement of the Merger and characterized their informational content as positive or negative. He then examined whether the announcement resulted in abnormal returns consistent with the direction of the news. Shaked observed that only six of the eleven releases resulted in a directionally consistent reaction; five of the eleven did not.

In his second study, Shaked examined articles, analyst reports and SEC filings during the same three-year period, yielding a total of 181 events that he believed contained material new information. News of the 181 events was published on a total of fifty-six days, resulting in fifty-six observations. Although there are reasons to question some of Shaked's events, on the whole, his identification appears credible. Of these fifty-six observations, only twelve resulted in statistically significant abnormal returns that were consistent with the directional content of the information. Moreover, there were thirty-eight days in the study period when there was a statistically significant abnormal return but no material news announcement.

In his third study, Shaked tested for proportionality by examining the reaction of the Company's stock to the announcement of a significant increase in the expansion of its mining operations in its earnings announcement for the third quarter of 2016. In the prior quarterly earnings releases, the Company forecast that the expansion would produce between 150,000 and 200,000 PGM ounces per year. JX 134 at 13; JX 187 at 17. In the earnings announcement for the third quarter of 2016, the Company increased the projection to between 270,000 and 330,000 PGM ounces per year. JX 309 at 16; *see* JX 306. Shaked estimated the pre-tax net income that would result from the increased output, taking into account the additional costs. He then prepared a discounted-cash-flow model that assumed production would ramp up by 25,000 ounces per year until 2022, continue at 125,000 ounces per year until 2031, then stop with no terminal value. Based on this model, Shaked calculated a net present value of $111.6 million for the increased production, which should have equated to a 7.08% abnormal return. Although the stock reacted positively, the observed abnormal return was only 0.39%. Shaked concluded that the Company's stock did not react in a proportionate manner, further undermining the claim of informational efficiency.

c. The Assessment Of Market Efficiency

***56** Absent any countervailing evidence, Zmijewski's analysis of the *Cammer* and *Krogman* factors would support a finding that the trading market for Stillwater's common stock had sufficient attributes to be regarded as informationally efficient. Shaked pointed out that the *Cammer* and *Krogman* factors have not been shown to provide a reliable indication of informational efficiency, but given the weight of authority on this issue, an absence of evidence on this point is no longer enough.[23]

The event studies, however, cut in the opposite direction. Courts applying the *Cammer* and *Krogman* factors have generally given greater weight to event studies compared to the other factors.[24] Based on his studies, Shaked opined that Stillwater's stock did not trade in a manner consistent with informational efficiency, and Zmijewski's event study generated relatively unconvincing results. Given this evidence, it is difficult to conclude that Stillwater's stock was informationally efficient to a degree sufficient to use the trading price as an indicator of fair value when a superior market-based metric, like the deal price, is available. That does not mean that Stillwater's stock was not informationally efficient, only that the deal price is a superior market-based metric for purposes of determining fair value.

***57** Shaked's event studies also raised questions about the degree of directionality and proportionality exhibited by the market for Stillwater's common stock. This evidence does not mean that Stillwater's stock price was unreliable, but it does make it difficult to conclude that Stillwater's stock was fundamental-value efficient to a degree sufficient to use the trading price as an indicator of fair value when a superior market-based metric like the deal price is available.

3. Evidence Of Information Gaps

The petitioners advance two other challenges to the reliability of Stillwater's trading price. Because everyone agrees that the market for Stillwater's common stock could only be informationally efficient in the semi-strong sense, the trading price could only account for publicly available information. The petitioners argue that material information about Stillwater's inferred reserves was not publicly available, meaning that the trading price could not be a reliable indicator of fundamental value. They also cite evidence indicating that the parties themselves did not trust the market's estimation of the Company's value. The former point is another strike against the trading price; the latter is not.

a. Industry Guide 7

The petitioners argue that Stillwater's trading price is not a reliable indicator of value because the market did not have access to material information related to the Company's value. On this issue, the petitioners relied on another expert: Thomas Matthews, a Principal Resource Geologist at Gustavson Associates. Matthews discussed the constraints imposed by Industry Guide 7, which specifies what the United States Securities and Exchange Commission permits a mining company to disclose. *See* JX 843 [hereinafter Industry Guide 7]; 17 C.F.R. 229.801(g).

To oversimplify a significantly more complex area, Industry Guide 7 only permits a mining company to disclose information about proven reserves or probable reserves. A proven reserve is a mineral deposit where (i) "quantity is computed from dimensions revealed in outcrops, trenches, workings or drill holes," (ii) "grade or quality are computed from the results of detailed sampling," and (iii) "the sites for inspection, sampling and measurement are spaced so closely and the geologic character is so well defined that size, shape, depth and mineral content of reserves are well-established." Industry Guide 7 ¶ (a)(2). A probable reserve is a mineral deposit where "the sites for inspection, sampling, and measurement are farther apart or are otherwise less adequately spaced," resulting in a "degree of assurance" that is "lower than that for proven reserves" but still "high enough to assume continuity between points of observation." *Id.* ¶ (a)(3). Industry Guide 7 does not permit a mining company to disclose information about inferred resources, which are mineral deposits where the quantity, grade, and quality "can be estimated" based on "geological evidence," "limited sampling," and "reasonably assumed, but not verified, geological and grade continuity." JX 7 at 4; *see* Industry Guide 7 ¶ (b)(5), Instruction 3.

Since at least 2012, the Society for Mining, Metallurgy and Exploration, Inc. has criticized this aspect of Industry Guide 7, complaining that the restrictions on reporting "limits the completeness and relevance of SEC reports for investors." JX 15 at 1. The Society contrasted Industry Guide 7 with the standards applied in other countries, which permit this disclosure. *Id.* at 2. In 2016, the SEC acknowledged the issue and proposed revisions to Industry Guide 7, but the new rules did not go into effect until 2018, long after the Merger closed. *See* Modernization of Property Disclosures for Mining Registrants, Exchange Act Release No. 34-84509, 2018 WL 5668900 (Oct. 31, 2018).

***58** Under Industry Guide 7 as it existed during the period leading up to the Merger, Stillwater could disclose information about the Stillwater Mine and East Bolder Mine, but could not disclose information about the inferred resources at Blitz, Lower East Boulder, Iron Creek, Altar, and Marathon. *See* JX 727 ¶ 13 (Matthews Reb. Rep.). For Blitz, the Company possessed but could not disclose "a resource estimation, a conceptual mine plan, material movement schedules, a capital and operating cost review, and a preliminary economic analysis for the Blitz expansion." *Id.* ¶ 12. The Company could only disclose certain drill data and briefly describe production target ranges, estimated capital spend, and timeframes. *See id.* ¶ 14.

The parties disagreed about whether disclosure of this information would cause investors to place a higher or lower valuation on the Company, but they agreed that it created an information gap for purposes of trading in the Company's stock. *See id.* ¶ 16; Zmijewski Tr. 1151. Zmijewski argued that because the effect of the information was unknowable, the court should assume that the absence of the information did not bias the trading price up or down. Sibanye also pointed out that some of the information was available in a filing that Stillwater made in March 2011 under the laws of Canada. *See* JX 9 at '055; *cf.* JX 501 at '345.

Stillwater's inability to disclose information about inferred resources under Industry Guide 7, combined with its partial disclosure of some of this information in a Canadian filing from 2011, are negative factors for purposes of using the Company's trading price as a valuation indicator. They are not dispositive in their own right, but they undermine the relative persuasiveness of the trading price.

b. Contemporaneous Evidence Of A Valuation Gap

The petitioners also cite contemporaneous evidence in the record in which knowledgeable insiders affiliated with Stillwater, its advisors, or Sibanye regarded the trading price as an unreliable indicator of value. For example:

- In May 2015, Stillwater management told the Board that "[m]uch of the value from Blitz, Lower East Boulder and recycle ramp up yet to be recognized by the market and potential buyers." JX 41 at '715.

- In January 2016, the Board thought that "the stock had been forced down significantly and ... didn't feel it really was reflective of what was going on in the business." McMullen Dep. 145.

- In June 2016, Froneman described the markets as "a bit all over the place lately." JX 152 at '532.

- In their second and third quarter 2016 reports, BMO analysts thought the Company's stock price did not reflect the value of Blitz. *See* JX 766 (stating in October 2016 that "[e]ven with arguably conservative assumptions, we maintain our opinion that the magnitude of the growth potential at Blitz is not factored into SWC shares"); Shaked Rep. ¶ 124 (quoting a June 2016 BMO report stating that "Blitz remains an underappreciated growth opportunity").

- In October 2016, Vujcic told the Board that the market perceived PGMs as "exposed to irrational producer behaviour in both South Africa and Russia." JX 293 at '522.

- During October, November, and December 2016, Stewart repeatedly stated that "[a]t an offer price of ~US$2bn (30% premium to 30 day VWAP) we are effectively paying a full price for the existing operations, 50% of Blitz and getting the remaining upside optionality for free." JX 282 at '775; *see* JX 410; JX 378 at '009; JX 447 at '981. He did not believe the market was "really considering Blitz." JX 397 at '451; *see* JX 280 at '279 (describing the Company's underperformance as "unlikely to remain as market recognises improvements are sustainable and Blitz comes on line").

***59** • In late November 2016, two weeks before signing, Stewart stated that the market was "currently at or near the bottom of the PGM cycle," suggesting a depressed stock price. JX 410 at '099; *see* PTO ¶ 257; *see also* JX 280 at '279; JX 399 at '407.

- In early December 2016, days before signing, McMullen commented on how the price of palladium had been artificially depressed. *See* JX 437 at '471 (noting that palladium was "finally starting to reflect the fundamentals")

- After announcing the Merger, Sibanye received two "deal of the year" awards and commented in both instances that the Merger was signed "at an opportune time in the commodity price cycle." JX 511; JX 641 at 1.

- At trial, Schweitzer testified that "[t]he company's stock price was all over the place from 2013 to 2016" and that he and "McMullen both believed there was a disconnect between the price of metals and the share price for Stillwater stock." Schweitzer Tr. 173.

This evidence as a whole is less extensive and persuasive than what the record demonstrated about the contemporaneous views of knowledgeable insiders regarding the existence of a valuation gap in *Dell*, and the Delaware Supreme Court in that case found that the trial court erred by giving weight to that evidence. *See Dell*, 177 A.3d 25–26; *cf.* Dell Trial, 2016 WL 3186538, at *33–36. This decision therefore does not give any weight to the petitioners' weaker showing in this case.

4. The Comparative Reliability Of The Trading Price

Through Zmijewski's analysis of the *Cammer* and *Krogman* factors, Sibanye made an initial showing that would be sufficient to support the reliability of the trading price as a valuation indicator absent contrary evidence. The results of the experts' event studies and the limitations imposed by Industry Guide 7 provided contrary evidence. Based on the parties' showings, the trading price is a less persuasive and less reliable valuation indicator in this case than the deal price. The lack of a reliable trading price does not undermine a court's ability to rely on the deal price, where the persuasiveness of the deal price has been established by analyzing the sufficiency of the sale process. *See* Columbia, 2019 WL 3778370, at *49.

This decision does not find that the trading price was so unreliable that it could not be used as a valuation indicator. If a market-tested indicator like the deal price was unavailable, then this decision might well have given weight to the trading price. Had this decision been forced to take that route, it would not have relied on the unaffected trading price, because Sibanye did not argue for its use, but instead would have taken into account the adjusted trading price.

Based on the record that the parties generated, Sibanye did not carry its burden to establish that the adjusted trading price was a sufficiently reliable valuation indicator for the court to use in determining fair value. The reliability of the adjusted trading price depended on the reliability of the unaffected trading price, and the record provides sufficient reason for concern about incorporating a trading price metric. This decision therefore does not give any weight to the adjusted trading price.

C. The Discounted Cash Flow Models

The petitioners and Sibanye each introduced a DCF valuation prepared by an expert. The petitioners relied on Rosen, whose DCF model generated a value of $25.91 per share. Sibanye relied on Zmijewski, whose DCF model generated a value of $17.03 per share. The difference amounts to approximately $1 billion in value.

***60** The DCF method is a technique that is generally accepted in the financial community. "While the particular assumptions underlying its application may always be challenged in any particular case, the validity of [the DCF] technique *qua* valuation methodology is no longer open to question." *Pinson*, 1989 WL 17438, at *8 n.11. It is a "standard" method that "gives life to the finance principle that firms should be valued based on the expected value of their future cash flows, discounted to present value in a manner that accounts for risk." *Andaloro v. PFPC Worldwide, Inc.*, 2005 WL 2045640, at *9 (Del. Ch. Aug. 19, 2005).

> The DCF model entails three basic components: an estimation of net cash flows that the firm will generate and when, over some period; a terminal or residual value equal to the future value, as of the end of the projection period, of the firm's cash flows beyond the projection period; and finally a cost of capital with which to discount to a present value both the projected net cash flows and the estimated terminal or residual value.

In re Radiology Assocs., Inc. Litig., 611 A.2d 485, 490 (Del. Ch. 1991) (internal quotation marks omitted).

In *Dell* and *DFC*, the Delaware Supreme Court cautioned against using the DCF methodology when market-based indicators are available. In *Dell*, the high court explained that "[a]lthough widely considered the best tool for valuing companies when there is no credible market information and no market check, DCF valuations involve many inputs—all subject to disagreement by well-compensated and highly credentialed experts—and even slight differences in these inputs can produce large valuation gaps." *Dell*, 177 A.3d at 37–38. The high court warned that when market evidence is available, "the Court of Chancery should be chary about imposing the hazards that always come when a law-trained judge is forced to make a point estimate of fair value based on widely divergent partisan expert testimony." *Id.* at 35. Making the same point conversely in *DFC*, the Delaware Supreme Court advised that a DCF model *should* be used in appraisal proceedings "when the respondent company was not public or was not sold in an open market check ...." *DFC*, 172 A.3d at 369 n.118. The high court commented that "a singular discounted cash flow model is often most helpful when there isn't an observable market price." *Id.* at 370.

This case illustrates the problems that the Delaware Supreme Court identified. The experts disagreed over many inputs, with small changes producing large swings in value. The briefing focused on eight inputs, with four generating the bulk of the difference.

First, the experts debated whether to apply a small-company risk premium, otherwise known as a size premium. Zmijewski applied a size premium of 1.66%, relying on Duff & Phelps, *2017 Valuation Handbook – U.S. Guide to Cost of Capital* (2017). Rosen did not apply one, arguing that it was not warranted. To the extent the court disagreed, he argued for using a premium of 1.5% drawn from Ibbotson Associates, *SBBI 2013 Valuation Yearbook* (2013). The scholarly literature on whether and how to apply a size premium is less than enlightening. The same respected scholars have found different results depending on the data set,[25] and others have engaged in vigorous debate about how to interpret the data and what inferences to draw.[26] This one dispute results in a valuation swing of $2.13 per share, accounting for approximately 24% of the difference between the two models.

***61** Second, the experts debated the size of the equity risk premium. Zmijewski used a historic supply-side risk premium of 5.97% published by Duff & Phelps. *See* JX 837; JX 893. Duff & Phelps advised practitioners to deduct 1.08% from this measurement to account for "the WWII Interest Rate Bias." JX 893 at 34. Zmijewski did not make the adjustment, explaining that it would not make sense to exclude the effect of interest rate controls during World War II, while failing to account for other periods of government control, such as the extreme phases of interest rate repression and quantitative easing that followed the 2008 financial crisis. Zmijewski Tr. 1042–43. Rosen used a forward-looking premium of 5.34%, derived from a model created by Aswath Damodaran. *See* JX 678. Zmijewski criticized the model, explaining that a user could generate approximately seventy different equity risk premiums by manipulating the inputs and objecting to some of Rosen's selections. *See* JX 893 at 47; JX 894; Zmijewski Tr. 1053–54. This one dispute results in a valuation swing of $1.33 per share, accounting for approximately 15% of the difference between the two models.

Third, the experts disputed which set of commodity price forecasts to use to generate cash flows. Zmijewski relied on price forecasts prepared by another expert for Sibanye. JX 710 (Burrows Rep.). Rosen relied on price forecasts from Bloomberg. JX 654 ¶ 8.21 (Rosen Rep.). This one dispute results in a valuation swing of $0.82 per share, accounting for approximately 9% of the difference between the two models.

Fourth, the experts diverged in their treatment of Stillwater's exploration areas. Sibanye argued that any valuation of these properties would be speculative and instructed Zmijewski not to try. Zmijewski Tr. 1074–75. Rosen estimated an "in-ground metal dollar value" for the properties, then relied on a report that examined PGM transactions in South Africa to estimate that exploration properties could be worth "between .5 percent and 2.5 percent of the estimated *in situ* dollar value of metal." Rosen Tr. 277–78; *see* JX 765. The respondent's mining expert identified many problems with Rosen's method. *See* JX 768. The dispute over the exploration areas results in a valuation swing of more than $2.00, accounting for approximately 23% of the difference between the two models.

Four other disputes account for the remaining valuation swing of $3.00 per share. Those disagreements concern how to account for the resources in mine-adjacent areas, the amount of excess cash, the value of inventory, and the value of Altar. As with the four major disputes, both sides have good reasons for their positions.

The legitimate debates over these inputs and the large swings in value they create undercut the reliability of the DCF model as a valuation indicator. If this were a case where a reliable market-based metric was not available, then the court might have to parse through the valuation inputs and hazard semi-informed guesses about which expert's view was closer to the truth. In this case, there is a persuasive market-based metric: the deal price that resulted from a reliable sale process. *Dell* and *DFC* teach that a trial court should have greater confidence in market indicators and less confidence in divergent expert determinations. *See* *Dell*, 177 A.3d at 35–38; *DFC*, 172 A.3d at 368–70 & n.118. Compared to the deal-price metric, the DCF technique "is necessarily a second-best method to derive value." *Union Illinois*, 847 A.2d at 359. This decision therefore does not use it. *See* *In re Appraisal of Solera Hldgs., Inc.*, 2018 WL 3625644, at *32 (Del. Ch. July 30, 2018).

III. CONCLUSION

The fair value of the Company's common stock at the effective time of the Merger was $18.00 per share. The legal rate of interest, compounded quarterly, shall accrue on the appraised value from the effective date until the date of payment. The parties shall cooperate to prepare a form of final order. If there are additional issues that need to be resolved, then the parties shall submit a joint letter within fourteen days that identifies them and proposes a path to bring this matter to a conclusion at the trial level.

APPENDIX

Case	Time Between Announcement of Deal and Commencement of Tender Offer	Time from Commencement of Tender Offer to Closing	Total Time for Purposes of Court Decision	Termination Fee	Other Deal Protection Measures
Yanow v. Sci. Leasing, Inc., 1988 WL 8772	4 business days, 4 calendar days	19 business days, 28 calendar days	23 business days, 32 calendar days	Expense reimbursement	Window-shop, 16.6% stock option lock-up

(Del. Ch. Feb. 5, 1988)					
In re Fort Howard Corp. S'holders Litig., 1988 WL 83147 (Del. Ch. Aug. 8, 1988)	4 business days, 4 calendar days	25 business days, 38 calendar days	29 business days, 42 calendar days	$67.8 million; 1.9% of equity value	No-shop permitting target to provide information and negotiate (i.e., a window-shop).
In re KDI Corp. S'holders Litig., 1988 WL 116448 (Del. Ch. Nov. 1, 1988)	4 business days, 6 calendar days	24 business days, 35 calendar days	28 business days, 41 calendar days	$8 million; 4.3% of equity value	Window-shop
In re Formica Corp. S'holders Litig., 1989 WL 25812 (Del. Ch. Mar. 22, 1989)	3 business days, 3 calendar days	30 business days, 43 calendar days	33 business days, 46 calendar days	Graduated fee capped at 1.9% of equity value	Strict no-shop
Braunschweiger v. Am. Home Shield Corp., 1989 WL 128571 (Del. Ch. Oct. 26, 1989)	Single-step merger. No tender offer. 143 business days, 205 calendar days, between announcement of merger and stockholder vote approving deal.			4.5% of equity value	None
Roberts v. Gen. Instr. Corp., 1990 WL 118356 (Del. Ch. Aug. 13, 1990)	5 business days, 7 calendar days	25 business days, 35 calendar days	30 business days, 42 calendar days	$33 million; 2% of equity value	Window-shop
McMillan v. Intercargo Corp., 768 A.2d 492 (Del. Ch. 2000)	Single-step merger. No tender offer. 102 business days, 148 calendar days between announcement of merger and stockholder vote approving deal.			$3.1 million; 3.5% of equity value	Window-shop
In re Pennaco Energy, Inc. S'holders Litig., 787 A.2d 691 (Del. Ch. 2001)	9 business days, 17 calendar days	20 business days, 28 calendar days	29 business days, 45 calendar days	$15 million; 3% of equity value	Window-shop
In re Cysive, Inc. S'holders Litig., 836 A.2d 531 (Del. Ch. 2003)	Single-step merger. No tender offer. 45 business days, 63 calendar days between announcement of merger and stockholder vote approving deal.			Expenses up to $1.65 million; up to 1.7% of deal value	Window-shop with matching rights
In re MONY Gp. Inc. S'holder Litig., 852 A.2d 9 (Del. Ch. 2004)	Single-step merger. No tender offer. 82 business days, 121 calendar days between announcement of merger and stockholder vote approving deal.			$50 million; 3.3% of equity value; 2.4% of deal value	Window-shop
In re Dollar Thrifty S'holder Litig., 14	Single-step merger. No tender offer. 100 business days, 144 calendar days between announcement of merger and stockholder vote approving deal.			$44.6 million with up to additional $5 million in	Window-shop with matching rights

A.3d 573 (Del. Ch. 2010)		expenses; 4.3% of deal value after accounting for options, RSUs and performance units.	
In re Smurfit–Stone Container Corp. S'holder Litig., 2011 WL 2028076 (Del. Ch. May 20, 2011)	Single-step merger. No tender offer. 89 business days, 123 calendar days between announcement of merger and stockholder vote approving deal.	$120 million; 3.4% of equity value	Window-shop with matching rights
In re El Paso Corp. S'holder Litig., 41 A.3d 432 (Del. Ch. 2012)	Single-step merger. No tender offer. 51 business days, 75 calendar days between announcement of merger and stockholder vote approving deal.	$650 million; 3.1% of equity value	Window-shop with matching rights
In re Plains Expl. & Prod. Co. S'holder Litig., 2013 WL 1909124 (Del. Ch. May 9, 2013)	Single-step merger. No tender offer. 79 business days, 117 calendar days between announcement of merger and stockholder vote approving deal.	$207 million; 3% of deal value	Window-shop with matching rights
C & J Energy Servs., Inc. v. City of Miami Gen. Empls.' and Sanitation Empls.' Ret. Tr., 107 A.3d 1049 (Del. 2014)	Single-step merger. No tender offer. 130 business days, 189 calendar days between announcement of merger and stockholder vote approving deal.	$65 million; 2.27% of deal value	Window-shop

All Citations

Not Reported in Atl. Rptr., 2019 WL 3943851

Footnotes

[1] Citations in the form "PTO ¶ —" refer to stipulated facts in the pre-trial order. Dkt. 209. Citations in the form "[Name] Tr." refer to witness testimony from the trial transcript. Citations in the form "[Name] Dep." refer to witness testimony from a deposition transcript. Citations in the form "JX — at —" refer to a trial exhibit with the page designated by the last three digits of the control or JX number. If a trial exhibit used paragraph or section numbers, then references are by paragraph or section.

[2] The two slides in the management presentations that addressed a sale contained comments like "[f]inding a willing buyer with higher priced currency is difficult," "[m]uch of the value from Blitz, Lower East Boulder and recycle ramp up yet to be recognized by the market and potential buyers," and the "[r]ecent downward trend in PGM prices not the right environment in which to be a seller." *Id.* at '866 to '867. Out of the nearly 190 slides in the banker presentations, only one discussed a possible sale. There, BMO opined that selling was "unlikely to be a value maximizing strategy until value has been extracted from all the other alternatives" available to the Company. *Id.* at '108.

[3] *See, e.g.*, JX 50 at '586 to '594; JX 52; JX 53; JX 55; JX 57; JX 58; JX 67; JX 68; PTO ¶¶ 138–39. Although principally focused on acquisitions, McMullen asked BMO in an October 2015 email for its views about "who would potentially be a buyer of Stillwater in an M+A deal?" JX 57 at '920. BMO sent back a list of twenty-one candidates, but warned that "[g]enerally as a whole we would say that we do not believe there is a high level of current interest and capability for an acquisition of Stillwater." *Id.* at '919.

[4] Only one slide in McMullen's presentation referenced a sale of the Company, and it advised that there was a "[v]ery limited number of potential buyers" and that because "commodity prices and sentiment are low," the Company "would not realize full value potentially." JX 86 at '025. By contrast, he presented multiple slides discussing positively how the Company could deploy its "capital and currency" (its stock) to make an acquisition. *See id.* at '026 to '035.

[5] *See* JX 138; JX 139 at '831; JX 154 at '087; JX 155; JX 157 at '315; McMullen Tr. 709–10; *see also* JX 349.

[6] *See* Schweitzer Tr. 189–90. McMullen testified that he told Schweitzer and Merrin about Sibanye's approach after his initial meeting with Froneman. He also claimed that he kept the Board informed as discussions progressed. McMullen's self-interested testimony conflicted with Schweitzer's more credible testimony and other record evidence.

[7] *See* JX 152 at '532 '533. At trial, McMullen testified that after Sibanye conducted its site visit, the Board told him that they wanted "some sort of written expression of interest" before starting "a data room process." McMullen Tr. 728–29. That testimony was not credible. The evidence indicates that McMullen did not brief the Board about a potential transaction with Sibanye until the July 2015 board meeting. *See* Schweitzer Tr. 189–90.

[8] JX 364 at '374. At trial, Schweitzer testified that this was the meeting at which the Board finally decided it did not need a special committee. *See* Schweitzer Tr. 157–58, 194. The minutes omit any discussion of the matter.

[9] *Id.* at 72. Although *Battye* is the seminal Delaware Supreme Court case on point, Chancellor Josiah Wolcott initially established the meaning of "value" under the appraisal statute in *Chicago Corporation v. Munds*, 172 A. 452 (Del. Ch. 1934). Citing the "material variance" between the Delaware appraisal statute, which used "value," and the comparable New Jersey statute that served as a model for the Delaware statute, which used "full market value," Chancellor Wolcott held that the plain language of the statute required "value" to be determined on a "going concern" basis. *Id.* at 453–55. *But see Union Ill. 1995 Inv. Ltd. P'ship v. Union Fin. Gp., Ltd.*, 847 A.2d 340, 355–56 (Del. Ch. 2004) ("This requirement that the valuation inquiry focus on valuing the entity as a going concern has sometimes been confused as a requirement of § 262's literal terms. It is not.").

[10] *See, e.g.*, *Montgomery Cellular Hldg. Co. v. Dobler*, 880 A.2d 206, 222 (Del. 2005); *Paskill Corp. v. Alcoma Corp.*, 747 A.2d 549, 553 (Del. 2000); *Rapid-Am. Corp. v. Harris*, 603 A.2d 796, 802 (Del. 1992); *Cavalier Oil Corp. v. Harnett*, 564 A.2d 1137, 1144 (Del. 1989); *Bell v. Kirby Lumber Corp.*, 413 A.2d 137, 141 (Del. 1980); *Universal City Studios, Inc. v. Francis I. duPont & Co.*, 334 A.2d 216, 218 (Del. 1975).

[11] *Cede & Co. v. Technicolor, Inc.*, 2003 WL 23700218, at *2 (Del. Ch. Dec. 31, 2003, revised July 9, 2004), *aff'd in part, rev'd in part on other grounds*, 884 A.2d 26 (Del. 2005); *accord Finkelstein v. Liberty Dig., Inc.*, 2005 WL 1074364, at *12 (Del. Ch. Apr. 25, 2005) ("The judges of this court are unremittingly mindful of the fact that a judicially selected determination of fair value is just that, a law-trained judge's estimate that bears little resemblance to a scientific measurement of a physical reality. Cloaking such estimates in grand terms like 'intrinsic value' does not obscure this hard truth from any informed commentator.").

[12] *See Aruba*, 210 A.3d at 136 ("It cannot be that an open chance for buyers to bid signals a market failure simply because buyers do not believe the asset on sale is sufficiently valuable for them to engage in a bidding contest against each other."); *Dell*, 177 A.3d at 29 ("Fair value entails at a minimum a price some buyer is willing to pay—not a price at which no class of buyers in the market would pay."); *id.* at 33 (finding that absence of higher bid meant "that the deal market was already robust and that a topping bid involved a serious risk of overpayment," which "suggests the price is already at a level that is fair").

[13] *See* Lawrence A. Hamermesh & Michael L. Wachter, *Finding the Right Balance in Appraisal Litigation: Deal Price, Deal Process, and Synergies*, 73 Bus. Law. 961, 962 (2018) (commending outcomes in *Dell* and *DFC*

and arguing that "the Delaware courts' treatment of the use of the deal price to determine fair value does and should mirror the treatment of shareholder class action fiduciary duty litigation"); *id.* at 982–83 (citing *Dell* and *DFC* in observing, "What we discern from the case law, however, is a tendency to rely on deal price to measure fair value where the transaction would survive enhanced judicial scrutiny .... Thus, in order to determine whether to use the deal price to establish fair value, the Delaware courts are engaging in the same sort of scrutiny they would have applied under *Revlon* if the case were one challenging the merger as in breach of the directors' fiduciary duties." (footnote omitted)); Charles Korsmo & Minor Myers, *The Flawed Corporate Finance of* Dell *and* DFC Global, 68 Emory L.J. 221, 269 (2018) (explaining that *Dell* and *DFC* "conflate questions of fiduciary duty liability with the valuation questions central to appraisal disputes").

[14] *See id.* at 1068 n.87 (citing cases including *In re Dollar Thrifty S'holders Litig.*, 14 A.3d 573, 612–13, 615 (Del. Ch. 2010) (finding that the target board's use of no-shop, matching rights, and termination fee provisions were reasonable even though the company had agreed to deal exclusively with the buyer without conducting a pre-signing market check); and *In re MONY Gp. Inc. S'holders Litig.*, 852 A.2d 9 (Del. Ch. 2004) (finding that the board acted reasonably even though it did not actively shop the company because the board was financially sophisticated, had knowledge of the relevant industry, and there was a "substantial opportunity for an effective market check" after the agreement was announced)); *id.* at 1069 (citing *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 243 (Del. 2009)).

[15] *See id.* at *44. The *PLX Trial* decision included an appendix that collected decisions approving a passive market check. The table somehow swapped the details of the passive market check in *Braunschweiger v. American Home Shield Corporation*, 1989 WL 128571 (Del. Ch. Oct. 26, 1989), with the details from *In re Formica Corporation Shareholders Litigation*, 1989 WL 25812 (Del. Ch. Mar. 22, 1989). A corrected version is attached to this decision as an appendix.

[16] *See Citron v. Fairchild Camera & Instr. Corp.*, 569 A.2d 53, 66 (Del. 1989) ("[I]n change of control situations, sole reliance on hired experts and management can taint[ ] the design and execution of the transaction. Thus, we look particularly for evidence of a board's active and direct role in the sale process." (internal quotation marks omitted)); *Mills Acq. Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1281 (Del. 1989) ("[A] board of directors ... may not avoid its active and direct duty of oversight in a matter as significant as the sale of corporate control."); *Cede & Co. v. Technicolor, Inc. (Technicolor II)*, 634 A.2d 345, 368 (Del. 1993) (explaining that directors must maintain "an active and direct role in the context of a sale of a company from beginning to end"); *In re Rural Metro Corp. S'holders Litig.*, 88 A.3d 54, 91 (Del. Ch. 2014) ("As a threshold matter, the decision to initiate a sale process falls short under enhanced scrutiny because it was not made by an authorized corporate decisionmaker. The Board did not make the decision to launch a sale process, nor did it authorize the Special Committee to start one."), *aff'd sub nom. RBC Capital Mkts., LLC v. Jervis*, 129 A.3d 816 (Del. 2015); *id.* ("One of the Delaware Supreme Court's clearest teachings is that 'directors cannot be passive instrumentalities during merger proceedings.' " (quoting *Technicolor II*, 634 A.2d at 368)).

[17] *See Aruba*, 210 A.3d at 136–39, 142 (adopting deal price less synergies as fair value where company's banker contacted five potential buyers after HP's initial outreach, none were interested, sale process terminated, and sale process later resumed as single-bidder engagement with HP, with only one quick contact to a sixth party); *Dell*, 177 A.3d at 28 (finding competitive pre-signing process where Silver Lake competed one-at-a-time with interested parties); *DFC*, 172 A.3d at 350, 355, 376 (finding "competitive process of bidding" where company's banker contacted "every logical buyer," three expressed interest, and two named a preliminary price with one dropping out before serious negotiations commenced).

[18] *See Dell Trial*, 2016 WL 3186538, at *29 & n.24 (citing Joshua Rosenbaum & Joshua Pearl, *Investment Banking: Valuation, Leveraged Buyouts, and Mergers & Acquisitions* 195–96 (2009) ("[An LBO model] is used ... to determine an implied valuation range for a given target in a potential LBO sale based on achieving acceptable returns...."); and Donald M. DePamphilis, *Mergers, Acquisitions, and Other Restructuring Activities* 506 (7th ed. 2014) ("[T]he DCF analysis solves for the present value of the firm, while the LBO model solves for the internal rate of return.")); *id.* at *29 nn. 25, 26 (citing Rosenbaum & Pearl, *supra*, at 195–96 ("In an M&A sell-side advisory context, the banker conducts LBO analysis to assess valuation *from*

the perspective of a financial sponsor. This provides the ability to set sale price expectations for the seller and guide negotiations with buyers accordingly ....” (emphasis added)); *id.* at 235–36 (“Traditionally, the valuation implied by LBO analysis is toward the lower end of a comprehensive analysis when compared to other methodologies, particularly precedent transactions and DCF analysis. This is largely due to the constraints imposed by an LBO, including leverage capacity, credit market conditions, and the sponsor's own IRR hurdles.”)).

[19] *See, e.g.*, *Dent v. Ramtron Int'l Corp.*, 2014 WL 2931180, at *8–10 (Del. Ch. June 30, 2014) (rejecting fiduciary challenge to “(1) a no-solicitation provision; (2) a standstill provision; (3) a change in recommendation provision; (4) information rights for [the acquirer]; and (5) a $5 million termination fee” where termination fee represented 4.5% of equity value and change-of-recommendation provision included unlimited matching right); *In re BJ's Wholesale Club, Inc. S'holders Litig.*, 2013 WL 396202, at *13 (Del. Ch. Jan. 31, 2013) (rejecting fiduciary challenge to a merger agreement with a no-shop provision, matching and information rights, a termination fee representing 3.1% of deal value, and a force-the-vote provision; observing that “under Delaware law, these deal protection measures, individually or cumulatively, have routinely been upheld as reasonable”); *In re Novell, Inc. S'holder Litig.*, 2013 WL 322560, at *10 (Del. Ch. Jan. 3, 2013) (describing “the no solicitation provision, the matching rights provision, and the termination fee” as “customary and well within the range permitted under Delaware law” and observing that “[t]he mere inclusion of such routine terms does not amount to a breach of fiduciary duty”); *In re Synthes, Inc. S'holder Litig.*, 50 A.3d 1022, 1049 (Del. Ch. 2012) (finding that a termination fee of 3.05% of equity value, a no-solicitation provision with a fiduciary out and matching rights, a force-the-vote provision, and a voting agreement that locked up at least 33% of the company shares in favor of the merger were not unreasonable deal protection devices); *In re Answers Corp. S'holders Litig.*, 2011 WL 1366780, at *4 & n.47 (Del. Ch. Apr. 11, 2011) (describing “a termination fee plus expense reimbursement of 4.4% of the Proposed Transaction's equity value, a no solicitation clause, a ‘no-talk’ provision limiting the Board's ability to discuss an alternative transaction with an unsolicited bidder, a matching rights provision, and a force-the-vote requirement” as “standard merger terms” that “do not alone constitute breaches of fiduciary duty” (quoting *In re 3Com S'holders Litig.*, 2009 WL 5173804, at *7 (Del. Ch. Dec. 18, 2009))); *In re Atheros Commc'ns, Inc. S'holder Litig.*, 2011 WL 864928, at *7 n.61 (Del. Ch. Mar. 4, 2011) (same analysis for no-solicitation provision, matching right, and termination fee); *In re 3Com*, 2009 WL 5173804, at *7 & n.37 (rejecting challenge to merger agreement with a no-solicitation provision, matching rights, and a termination fee in excess of 4% of equity value; describing provisions as having been “repeatedly” upheld by this court and collecting authorities).

[20] The pop-culture illustration of this principle is J. Wellington Wimpy's offer to “gladly pay you Tuesday for a hamburger today.” *See J. Wellington Wimpy*, Wikipedia, https://en.wikipedia.org/wiki/J._Wellington_Wimpy (last visited Aug. 20, 2019). Setting aside credit risk, dollars paid next Tuesday are worth less than dollars paid today, so the same price paid next Tuesday is a pleasant deal for Wimpy. The same is true for Sibanye in an appraisal. Valuing Stillwater at $18.00 per share based on an agreement reached on December 8, 2016, then using that figure to determine value as of May 4, 2017, lets Sibanye use December's dollars for a valuation in May. The statutory interest award is measured from closing, so that aspect of the appraisal remedy does not pick up the decline in the purchasing power of dollars used to measure the deal-price metric. In this respect, the petitioners are differently situated than stockholders who did not pursue their appraisal rights. They accepted the $18.00 per share and received it, without interest, shortly after May 4, 2017, once the merger consideration payouts were processed through the clearing system. The appraisal petitioners did not accept that outcome. They opted for appraisal and sought a determination of Stillwater's fair value as of May 4, 2017. Sibanye can argue legitimately that the deal price of $18.00 per share provides the best evidence of fair value, but that is a price calculated in December 2016 dollars, not May 2017 dollars.

[21] *See* Fernán Restrepo & Guhan Subramanian, *The New Look of Deal Protection*, 69 Stan. L. Rev. 1013, 1058–63 (2017) (analyzing implications of matching rights); Brian JM Quinn, *Bulletproof: Mandatory Rules for Deal Protection*, 32 J. Corp. L. 865, 870 (2007) (analyzing matching rights as the functional equivalent of a right of first refusal and explaining that “[t]he presence of rights of first refusal can be a strong deterrent

against subsequent bids" because "[s]uccess under these circumstances may involve paying too much and suffering the 'winner's curse' "); *see also* Marcel Kahan & Rangarajan K. Sundaram, *First-Purchase Rights: Rights of First Refusal and Rights of First Offer*, 12 Am. L. & Econ. Rev. 331, 331 (2012) (finding "that a right of first refusal transfers value from other buyers to the right-holder, but may also force the seller to make suboptimal offers"); Frank Aquila & Melissa Sawyer, *Diary of a Wary Market: 2010 in Review and What to Expect in 2011*, 12 M & A Law. Nov.-Dec. 2010, at 1 ("Match rights can result in the first bidder 'nickel bidding' to match an interloper's offer, with repetitive rounds of incremental increases in the offer price.... [M]atch rights are just one more factor that may dissuade a potential competing bidder from stepping in the middle of an already-announced transaction."); David I. Walker, *Rethinking Rights of First Refusal*, 5 Stan. J.L. Bus. & Fin. 1, 20–21 (1999) (discussing how a right of first refusal affects bidders).

[22] *See, e.g.*, Richard A. Booth, *Minority Discounts and Control Premiums in Appraisal Proceedings*, 57 Bus. Law. 127, 151 n.130 (2001) ("[M]arket price should ordinarily equal going concern value if the market is efficient."); William J. Carney & Mark Heimendinger, *Appraising the Nonexistent: The Delaware Court's Struggle with Control Premiums*, 152 U. Pa. L. Rev. 845, 847–48, 857–58 (2003) ("The basic conclusion of the Efficient Capital Markets Hypothesis (ECMH) is that market values of companies' shares traded in competitive and open markets are unbiased estimates of the value of the equity of such firms."); *id.* at 879 (noting that the appraisal statute requires consideration of all relevant factors and stating that "in an efficient market, absent information about some market failure, market price is the only relevant factor"); Lawrence A. Hamermesh & Michael L. Wachter, *The Short and Puzzling Life of the "Implicit Minority Discount" in Delaware Appraisal Law*, 156 U. Pa. L. Rev. 1, 52 (2007) ("Take the case of a publicly traded company that has no controller. Efficient market theory states that the shares of this company trade at the pro rata value of the corporation as a going concern."); *id.* at 60 ("As a matter of generally accepted financial theory ..., share prices in liquid and informed markets do generally represent th[e] going concern value ...."); *see also* Lawrence A. Hamermesh & Michael L. Wachter, *Rationalizing Appraisal Standards in Compulsory Buyouts*, 50 B.C. L. Rev. 1021, 1033–34 (2009) (positing trading prices should not be used to determine fair value if there is either no public market price at all, if the shares are illiquid or thinly traded, or if there is a controlling stockholder, implying that outside of these scenarios, "because financial markets are efficient, one can simply use the market value of the shares").

[23] The experts' exploration of the *Cammer* and *Krogman* factors has left me with significantly less confidence in them than I had before this litigation. There appears to be substantial overlap among the factors, such that a single attribute, like a New York Stock Exchange listing, would correlate with and lead to the satisfaction of multiple factors. For an issuer to satisfy multiple *Cammer* and *Krogman* factors is thus likely less significant than it might seem. It is also striking how many of the *Cammer* and *Krogman*, at least based on Zmijewski's report, stem from judicial opinions or law review articles, rather than from financial or economic papers. I am left with the concern that the *Cammer* and *Krogman* factors may be a convenient heuristic that law-trained judges deploy as a matter of routine, rather than because they have support in reliable research. That said, the absence of evidence is not necessarily evidence of absence, and the record in this case does not provide grounds to call the *Cammer* and *Krogman* factors into doubt.

[24] *See, e.g.*, *In re DVI, Inc. Sec. Litig.*, 639 F.3d 623, 634 (3d Cir. 2011) ("[B]ecause an efficient market is one in which information important to reasonable investors ... is immediately incorporated into stock prices, the cause-and-effect relationship between a company's material disclosures and the security price is normally the most important factor in an efficiency analysis." (internal quotation marks omitted)), *abrogated on other grounds by* *Amgen Inc. v. Conn. Ret. Plans & Tr. Funds*, 568 U.S. 455 (2013); *In re Xcelera.com Sec. Litig.*, 430 F.3d 503, 512 (1st Cir. 2005) (describing the cause and effect prong of *Cammer* as "in many ways the most important" and explaining that "[i]n the absence of such a relationship, there is little assurance that information is being absorbed into the market and reflected in its price"); *Cammer*, 711 F. Supp. at 1287 ("[S]howing a cause and effect relationship between unexpected corporate events or financial releases and an immediate response in the stock price" is "the essence of an efficient market and the foundation for the fraud on the market theory."); *see also* *Teamsters Local 445 Freight Div. Pension, Fund v. Bombardier Inc.*, 546 F.3d 196, 207 (2d Cir. 2008) (quoting *Xcelera.com* for the import of the cause and effect prong

of *Cammer*). That said, the cause-and-effect factor is not dispositive. *Beaver Cty. Empls.' Ret. Fund v. Tile Shop Hldgs., Inc*., 2016 WL 4098741, at *10–11 (D. Minn. July 28, 2016) (collecting cases and explaining that "[t]he weight of authority on this issue favors" a finding of market efficiency without a favorable resolution of the cause and effect factor).

[25] *Compare* Eugene F. Fama & Kenneth R. French, *A Five-Factor Asset Pricing Model*, 116 J. Fin. Econ. 1 (2015) (JX 681) (finding evidence of size premium in asset pricing models), *and* Eugene F. Fama & Kenneth R. French, *Common Risk Factors in the Returns on Stocks and Bonds*, 33 J. Fin. Econ. 3 (1993) (JX 680) (finding evidence that stocks with smaller market capitalizations tended to have higher average returns), *with* Eugene F. Fama & Kenneth R. French, *Size, Value, and Momentum in International Stock Returns*, 105 J. Fin. Econ. 457 (2012) (JX 679) (finding no evidence of a size premium in any region based on analyses of international stock returns from November 1989 to March 2011).

[26] *Compare, e.g.*, Cliff Asness *et al.*, *Size Matters, If You Control Your Junk*, 129 J. Fin. Econ. 479, 479 (2018) (finding "[a] significant size premium ..., which is stable through time, robust to the specification, more consistent across seasons and markets, not concentrated in microcaps, robust to non-price based measures of size, and not captured by an illiquidity premium" and arguing that challenges to the existence of the size premium "are dismantled when controlling for the quality, or the inverse 'junk', of a firm"), and Roger Grabowski, *The Size Effect Continues To Be Relevant when Estimating the Cost of Capital*, 37 Bus. Valuation Rev. 93 (2018) (responding to criticisms of Ang, *infra*), *with* Aswath Damodaran, *The Small Cap Premium: Where is the Beef?*, Musings on Markets (Apr. 11, 2015) (JX 682 at 1) (commenting that "the historical data, which has been used as the basis of the argument [for size premia], is yielding more ambiguous results and leading us to question the original judgment that there is a small cap premium" and that "forward-looking risk premiums, where we look at the market pricing of stocks to get a measure of what investors are demanding as expected returns, are yielding no premium for small cap stocks"), http://aswathdamodaran.blogspot.com/2015/04/the-small-cap-premium-fact-fiction-and.html, *and* Clifford Ang, *The Absence of a Size Effect Relevant to the Cost of Equity*, 37 Bus. Valuation Rev. 87 (2018) (JX 732 at 3–4) (concluding from survey of empirical literature that either "(1) investors ... do not believe a size effect exists and, therefore, do not demand compensation for it, or (2) investors ... believe a size effect exists, but believe the adjustment for the size effect is not made in the cost of equity"). Zmijewski has acknowledged that "there is much weaker evidence of a size effect since the original [article finding the effect] was published." JX 836 at 322.

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UNPUBLISHED OPINION. CHECK
COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

IN RE EXAMWORKS GROUP, INC.
STOCKHOLDER APPRAISAL LITIGATION

Consolidated C.A. No. 12688–VCL
|
Date Submitted: February 13, 2018
|
Date Decided: February 21, 2018

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MEMORANDUM OPINION

LASTER, Vice Chancellor.

***1** The petitioners in this appraisal proceeding seek a judicial determination of the fair value of their proportionate interest in ExamWorks Group, Inc. ("ExamWorks" or the "Company"). The Company has filed two motions for discovery sanctions.

The first motion seeks sanctions against five funds who retained the law firm of Entwistle & Cappucci, LLC as their principal counsel.[1] The Entwistle Petitioners failed to produce any documents during the period allotted for fact discovery and said nothing about any delays in production. Six weeks after the discovery cutoff, and four days after the exchange of expert reports, the Entwistle Petitioners produced 68,052 pages of documents.

The second motion seeks sanctions against all petitioners.[2] In their discovery responses, the petitioners agreed to provide the Company with copies of documents obtained from third parties. In March 2017, the petitioners obtained documents from Barclays Bank PLC. The petitioners did not produce copies of the documents. Ten weeks after the discovery cutoff, the petitioners produced over 60,000 pages of documents from Barclays.

Both motions seek sanctions for the belated production of privilege logs. None of the petitioners produced privilege logs during the discovery period. Almost two months after the discovery cutoff, the Entwistle Petitioners produced sloppy and inadequate logs. Five other petitioners had retained the law firm of Grant & Eisenhofer P.A. as their principal counsel.[3] Ten weeks after the discovery cutoff, the G & E Petitioners produced their logs. Although the G & E Petitioners did a better job than the Entwistle Petitioners, the logs arrived too late to be of any use for discovery.

This decision grants the motions and imposes sanctions for the petitioners' failures to comply with their discovery obligations.

I. FACTUAL BACKGROUND

The facts are drawn from the submissions made in connection with the motions. The parties devoted much more attention to argument and invective than to the underlying facts, making it more difficult than necessary to derive the applicable timeline. The following discussion does not comprise findings of fact in the post-trial sense, but rather represents how the record appears at this preliminary stage.

A. The ExamWorks Merger

***2** ExamWorks is a Delaware corporation with its principal place of business in Atlanta, Georgia. ExamWorks completed an initial public offering in 2010, and its stock traded on NASDAQ under the symbol "EXAM."

On April 27, 2016, ExamWorks announced that it had entered into a merger agreement with affiliates of Leonard Green & Partners, L.P. The merger closed on July 27, 2016. Pursuant to the merger agreement, ExamWorks' publicly traded common stock was converted into the right to receive $35.05 per share, subject to the holder's statutory right to eschew the merger consideration and seek appraisal.

B. This Appraisal Proceeding

After the announcement of the merger, the following investment funds perfected their appraisal rights and filed appraisal petitions in this court:

- Hudson Bay Master Fund Ltd. and Hudson Bay Merger Arbitrage Opportunities Master Fund Ltd. (together, "Hudson Bay").

- Lord Abbett Series Fund Inc.—Value Opportunities Portfolio; Lord Abbett Securities Trust—Lord Abbett Value Opportunities Fund; and Lord Abbett Research Fund, Inc.—Small Cap Value Series (collectively, the "Lord Abbett Funds").

- Water Island Global Master LP, The Arbitrage Fund, The Arbitrage Event–Driven Fund, Columbia Active Portfolio Multi–Manager Alternative Strategies Fund, and Litman Gregory Masters Alternative Strategies Fund (collectively, the "Entwistle Petitioners").

- Brookdale International Partners, L.P. and Brookdale Global Opportunity Fund (together, the "Brookdale Funds").

- Sunrise Partners Limited Partnership ("Sunrise").

- Pivot Point Capital Master LP ("Pivot Point").

- Magnetar Capital Master Fund, Ltd. and Third Motion Equities Master Fund Ltd. (together, the "Magnetar Petitioners").

Certain petitioners moved to consolidate the appraisal proceedings and for the appointment of lead counsel. By order dated September 1, 2016, the court consolidated the actions and appointed as Co–Lead Counsel the law firms of Grant & Eisenhofer, P.A. and Entwistle & Cappucci, LLC.[4] The order placed Co–Lead Counsel in charge of the consolidated action, stating:

> 10. Petitioners' Co–Lead Counsel shall set policies for the prosecution of the Consolidated Action, shall delegate and monitor the work performed by petitioners' attorneys to avoid duplication of effort or unnecessary expense, *shall coordinate on behalf of petitioners the initiation and conduct of discovery proceedings*, shall have responsibility for all Court filings and appearances (except with respect to any Entitlement Hearing), and shall have the authority to negotiate a settlement of the Consolidated Action subject to approval of petitioners and the Court.
>
> 11. Co–Lead Counsel shall be available and responsible for communications to and from this Court, including distributing orders and other directions from the Court to counsel.
>
> 12. No motion, request for discovery or other pre-trial or trial proceedings shall be initiated or filed by any petitioner except through Co–Lead Counsel. Respondent's counsel ay rely upon all agreements made with Co–Lead Counsel, or other duly authorized representative of Co–Lead Counsel, and such agreements shall be binding on all petitioners.[5]

The Consolidation Order provided that "[a]ny disputes among Co–Lead Counsel which cannot be resolved after consultation shall be decided based on a vote of the Petitioners in the Constituent Actions."[6]

C. The Scheduling Orders

***3** The parties agreed on a schedule for the action, which the court approved by order dated September 26, 2016.[7] Paragraphs 1(a)-(d) of the Initial Scheduling Order stated:

> (a) The parties shall produce documents on a rolling basis and shall substantially complete document production on or before December 2, 2016, in response to any document requests that are served on or before October 3, 2016;
>
> (b) The parties shall produce documents on a rolling basis in response to any document requests served after October 3, 2016, and shall substantially complete document production in response to such requests by the later of February 24, 2017, or eight weeks after service;
>
> (c) The parties shall produce an initial privilege log on or before January 31, 2017, and shall promptly provide supplemental privilege logs if productions made subsequent to this date withhold privileged materials;
>
> (d) All fact discovery shall be completed by July 26, 2017, including any party and third-party depositions but excluding any fact discovery subject to a motion to

> compel or motion for protective order pending on July 26, 2017.[8]

The petitioners had already served their first set of requests for production of documents on August 25, 2016. On January 24, 2017, they served subpoenas on Barclays; Leonard Green & Partners, L.P.; Bank of America Corporation; Deutsche Bank Securities, Inc.; Evercore Partners LLC; Goldman Sachs Group, Inc.; and Merrill Lynch, Pierce, Fenner & Smith, Inc.[9] Barclays was one of the banks that provided debt financing for the merger. The petitioners served a second set of requests for production of documents on February 24, 2017.

D. The Amended Scheduling Order

On April 25, 2017, the parties submitted an amended schedule for the action, which the court entered the same day.[10] Paragraphs 1(a)-(c) of the Amended Scheduling Order stated:

> (a) The parties shall produce documents on a rolling basis and shall substantially complete document production on or before May 31, 2017;
>
> (b) The parties shall produce an initial privilege log on or before June 30, 2017, and shall promptly provide supplemental privilege logs if productions made subsequent to this date withhold privileged materials;
>
> (c) All fact discovery shall be completed by October 2, 2017, including any party and third-party depositions but excluding any fact discovery subject to a motion to compel or motion for protective order pending on October 2, 2017.[11]

The Company did not serve any requests for production of documents until May 31, 2017, which was the date for substantial completion of production under the Amended Scheduling Order.

Request Number 25 in the Company's requests for production of documents asked the petitioners to produce "all Documents received [by petitioners] from third parties in connection with this Action, including all Documents received in response to a subpoena or other request."[12] On June 30, 2017, the petitioners served their responses and objections. They agreed to "produce documents pursuant to document productions received from third parties subpoenaed in connection with the Action."[13]

E. The Petitioners' Motion For A Protective Order

***4** On July 31, 2017, the Company moved for a commission to serve a subpoena on Berkshire Partners LLC.[14] On August 10, 2017, the Company gave notice that it had served a subpoena on Berkshire seeking documents and testimony.[15] Berkshire had been a potential co-investor in the merger and participated in the negotiations before dropping out.

On September 26, 2017, during a meet-and-confer session, the petitioners asked about the status of documents produced by Berkshire. The Company produced the Berkshire documents on September 27, five days before the fact discovery cutoff of October 2.[16]

During the meet-and-confer session, the Company mentioned that it was considering a deposition of a Berkshire representative. The Company subsequently notified the petitioners that it intended to depose a Berkshire witness on November 9, 2017, after the discovery cutoff of October 2, 2017.[17]

The petitioners moved for a protective order, describing the post-cutoff deposition as "an abuse of the discovery process" that "completely disregards this Court's Amended Scheduling Order."[18] After briefing and argument, I granted the motion.[19] I explained that I was not granting the motion based on any finding of "conscious sandbagging or some type of intentional discovery misconduct."[20] Rather, I described the situation as one where "not enough was done to coordinate with the petitioners to provide documents on time, to be transparent about what was going on, and then ultimately it simply happened that the deposition did not get done within the discovery time frame."[21] I ruled that in light of the timeline, "there needs to be a consequence," and "[a] fitting consequence is not to permit an exception to the discovery cutoff."[22]

F. The Entwistle Petitioners' Post–Discovery–Cutoff Production

On November 14, 2017, the Entwistle Petitioners produced 6,058 documents.[23] The documents arrived six weeks after the fact discovery cutoff of October 2 and four days after the parties exchanged initial expert reports. The Entwistle

Petitioners had not produced any documents before the discovery cutoff.

The Company determined that 4,020 of the 6,058 documents contained redactions.[24] On November 24, 2017, the Company emailed Co–Lead Counsel to ask for an explanation.[25] On November 28, the Entwistle Petitioners produced a log indicating that, for 4,073 of the 4,546 documents containing redactions, the reason for the redaction was "Confidential/Not Relevant." The log shows that many of the redacted documents were copies of press releases, news articles, or other publicly available information.[26]

The Entwistle Petitioner's production included a discounted cash flow analysis that appears to value ExamWorks in the range of $39.84 to $41.72 per share. By contrast, the petitioners' expert valued ExamWorks at $50.14 per share.[27]

G. The Petitioners' Post–Discovery Production Of The Barclays Documents

On December 6, 2017, the petitioners produced their valuation expert's rebuttal report. The report cited two documents that the petitioners had obtained from Barclays.[28] The petitioners had never provided the Company with any documents from Barclays. On December 13, the Company asked about the documents and demanded immediate production of all documents produced by Barclays or by any other party in response to a subpoena.[29]

***5** On December 14, 2017, the petitioners produced over 60,000 pages of documents that they had obtained from Barclays (the "Barclays Documents"). Since then, the parties have analyzed the documents and determined that approximately 90% were documents that the Company placed in a data room for Barclays and its other lenders. Forty-six documents were not in the data room and not otherwise found in the production.[30]

H. The G & E Petitioners' Privilege Logs

Meanwhile, on December 12, 2017, the G & E Petitioners produced their privilege logs.[31] They arrived ten weeks after the discovery cutoff.

On December 15, 2017, the G & E Petitioners produced an additional 231 documents, consisting of over 1,300 pages of information.[32] The G & E Petitioners previously had asserted privilege for the documents, but after further consideration they removed them from their logs.

If the G & E Petitioners had taken this step earlier, it would have been a good thing. Instead, the documents arrived *after* the Company had completed the depositions of the petitioners' representatives. The late documents included a Hudson Bay email containing valuation parameters and a Lord Abbett email referring to communications with other stockholders about the merger. By themselves, the two documents do not appear momentous, but they should have been produced earlier so that the Company could have questioned the petitioners' witnesses about them. One can never predict what memories a document can unlock or refresh, nor the types of testimony that resulting lines of inquiry can elicit.

I. The Meet-and-Confer Sessions

The parties held meet-and-confer sessions on December 8, 11, and 12, 2017.[33] Under the consolidation order, Co–Lead Counsel were supposed to handle the case together and take joint responsibility for the litigation. But once the Company raised the Entwistle Petitioners' late production, Grant & Eisenhofer tried to go its own way, leaving Entwistle and its Delaware counsel, Rosenthal Monhait & Goddess, to clean up their clients' mess. They offered to re-produce the documents without redactions for relevance. They also offered to produce a witness for deposition, provide a privilege log, and allow the Company to propound additional discovery on the Entwistle Petitioners. They even offered to re-open expert discovery so that the Company's expert could take into account information learned from the production and deposition. On December 11, the Entwistle Petitions re-produced the belatedly produced documents without relevancy redactions.[34]

Grant & Eisenhofer sought to deal with the Barclays Documents. They proposed to strike the references to the two Barclays Documents from their expert's rebuttal report and to not rely on any of the other Barclays Documents at trial.

No one offered to do anything about the belated privilege logs.

II. LEGAL ANALYSIS

"[T]he purpose[s] of discovery [are] to advance issue formulation, to assist in fact revelation, and to reduce the element of surprise at trial."[35] These instrumental purposes in turn serve the overarching and "well established policy" underlying pretrial disclosure, which is that "a trial decision should result from a disinterested search for truth from all the available evidence rather than tactical maneuvers based on the calculated manipulation of evidence and its production."[36] "Candor and fair-dealing are, or should be, the hallmark of litigation and required attributes of those who resort to the judicial process. The rules of discovery demand no less."[37]

***6** "Scheduling orders and discovery cutoffs further these important purposes and policies by ensuring that parties provide discovery in a timely fashion, thereby avoiding trial by surprise and the prejudice that results from belated disclosure."[38] "Parties must be mindful that scheduling orders are not merely guidelines but have the same full force and effect as any other court order."[39] "Generally speaking, Delaware courts strictly adhere to discovery cut-off dates."[40]

A party that disregards the provisions in a scheduling order that govern discovery is engaging in discovery abuse. If a party cannot meet a deadline, the onus is on that party to be forthcoming and transparent about the situation and the reasons for it. Humans are not psychic. The other side does not know that the production may be late, much less how late or why. When parties are transparent, they can cooperate to address problems without judicial involvement. Acting as officers of the court, attorneys can find solutions to keep a case on track and prepare the matter for decision. Attorneys shirk their obligations to the court and make matters worse when they fail to communicate with the other side, allow problems to escalate, and miss critical deadlines. Then they impair their credibility when they try to make excuses that do not hold up.

"Discovery abuse has no place in [Delaware] courts, and the protection of litigants, the public, and the bar demands nothing less than that [Delaware] trial courts be diligent in promptly and effectively taking corrective action to 'secure the just, speedy and inexpensive determination of *every* proceeding' before them."[41] "Trial courts should be diligent in the imposition of sanctions upon a party who refuses to comply with discovery orders, not just to penalize those whose conduct warrants such sanctions, but to deter those who may be tempted to abuse the legal system by their irresponsible conduct."[42]

"In the event this Court determines that sanctions for discovery abuses are appropriate, the sanction must be tailored to the culpability of the wrongdoer and the harm suffered by the complaining party."[43] Sanctions may serve one or more of three proper purposes: "punishment, deterrence[,] or coercion."[44] Court of Chancery Rule 37(b)(2) identifies possible sanctions that a trial court can impose for violating a discovery order, including but not limited to:

> (A) An order that the matters regarding which the order was made or any other designated facts shall be taken to be established for the purposes of the action in accordance with the claim of the party obtaining the order;
>
> (B) An order refusing to allow the disobedient party to support or oppose designated claims or defenses, or prohibiting that party from introducing designated matters in evidence; [or]
>
> (C) An order striking out pleadings or parts thereof, or staying further proceedings until the order is obeyed, or dismissing the action or proceeding or any part thereof, or rendering a judgment by default against the disobedient party[.][45]

***7** A trial court also "has the power to issue sanctions for discovery abuses under its inherent equitable powers, as well as the Court's inherent power to manage its own affairs."[46]

Delaware Supreme Court decisions teach that the entry of a default judgment under Rule 37(b)(2)(C) is "*the ultimate sanction* for discovery violations and *should be used sparingly*."[47] "Judgment by default is, of course, the extreme remedy and generally speaking the Rule has been interpreted to require some element of willfulness or conscious disregard of the order before such a sanction is imposed."[48]

"A less final but still serious discovery sanction is the entry of an order under Rule 37(b)(2)(A) that deems designated facts to be established or which draws an inference as to a particular issue that is adverse to the party that failed to comply with its discovery obligations."[49] "A more moderate but still significant discovery sanction is to alter the burden of proof on a particular issue, either by shifting it to the party that failed to comply with its discovery obligations or by increasing or decreasing the relevant standard."[50]

More typical remedies for late production are to allow additional discovery or to preclude the use of the belatedly produced material. Rule 37(b)(2) further provides that if a defendant has violated a discovery order, the court "*shall* require the party failing to obey the order or the attorney advising that party or both to pay the reasonable expenses, including attorney's fees, caused by the failure."[51] Under this rule, expenses should be awarded "unless the Court finds that the failure was substantially justified or that other circumstances made an award of expenses unjust."[52] The Delaware Supreme Court has explained that under Rule 37, "when a party fails to comply with discovery orders of the Court or otherwise engages in discovery abuses, the award of attorneys' fees and expenses to the opposing party is mandatory, absent a showing by the wrongdoer that his actions were substantially justified or that other circumstances make the award unjust."[53] The current framing of the rule with its presumptive award of fees represented a change from prior practice.[54] It was adopted "in order to encourage such sanction under such circumstances, and to that end the Rule places a burden on the disobedient party to show that his failure was justified or that the other circumstances exist making an award unjust."[55]

A. The Entwistle Petitioners' Late Production

***8** The Entwistle Petitioners violated a court order by failing to comply with the discovery cutoff in the Amended Scheduling Order. They did not produce any documents before the discovery cutoff. They did not communicate with the Company about any delay in production. They did not move to modify the discovery cutoff or seek leave to produce documents late. Six weeks after the discovery cutoff, they produced 6,058 documents consisting of 68,052 pages.

The Entwistle Petitioners have argued that they should not be held accountable for violating the Amended Scheduling Order because it took time for Co–Lead Counsel to negotiate search terms, then it took additional time for the Entwistle firm to gather and review documents from the Entwistle Petitioners. According to the Entwistle Petitioners, this is the ordinary method of collecting and producing documents, so it should not have been a problem for them to produce documents after the cutoff.

The fault lies not in the tasks that the Entwistle firm was performing but in the rate at which the firm performed them. Parties must deploy the resources necessary to meet deadlines. If meeting a deadline appears difficult or impossible, then the party facing the deadline needs to confer with the other side or seek a modification of the schedule.

The Entwistle Petitioners had sufficient resources to meet the discovery cutoff. They are sophisticated investment funds who collectively owned one million shares. At the deal price, their stake was valued at $35,050,000. At the value claimed by their expert, their stake would be worth $50,140,000. They had access to Co–Lead Counsel and Rosenthal Monhait. If they had wanted to get the collection done, they could have.

The other petitioners produced documents before the discovery cutoff. The following chart identifies the date of production, the petitioner producing documents, and the volume of documents produced:

Date	Fund	# of documents
September 5, 2017	Lord Abbett Funds	530
	Pivot Point	601
September 12, 2017	Sunrise	1,858
	Pivot Point	190
September 16, 2017	Lord Abbett Funds	2,633
October 2, 2017	Hudson Bay	1,434
	Lord Abbett Funds	297
	Sunrise	1
	Brookdale Funds	163

Magnetar Petitioners	506
TOTAL:	**8,213**

There were some other petitioners who produced documents after the fact discovery cutoff, but only dribs and drabs. The Magnetar Funds produced nine additional documents on October 3, 2017, the Lord Abbett Funds produced one additional document on October 12, and Pivot Point produced three additional documents on November 8.[56] These documents should have been produced earlier, but humans are not perfect, and sometimes documents come in late. No one else made the type of massive, post-discovery production of their own documents that the Entwistle Petitioners made.

The Entwistle Petitioners have argued that the Company's failure to request documents until May 31, 2017, somehow excused their failure to comply with the Amended Scheduling Order. The Entwistle Petitioners also have argued that because the Company was not pressing them for documents in September and October, the Company must not have wanted the documents. Both responses seek to blame the injured party and deflect attention from the Entwistle Petitioners' misconduct.

When the Company served its discovery requests, there were still four months in the schedule. That was plenty of time for the Entwistle Petitioners to gather and produce documents. If they needed more time, it was their obligation to seek it, either from the Company or the court. Whether or not the Company nagged the Entwistle Petitioners about producing documents has no effect on the locus of the obligation. The Entwistle Petitioners had a duty to produce documents in a timely fashion. They cannot shift that obligation to the Company.

***9** The bottom line is that even though the Entwistle Petitioners chose to file and litigate an appraisal claim, they shirked one of a litigant's basic obligations: gathering and producing responsive material in a timely fashion. They were happy to let the Company bear the expense of litigation while giving themselves a pass. Even when they did produce documents, the production was sloppy and haphazard.

This type of misconduct has consequences at two levels. One level involves actual prejudice in the specific case. Here, the belated production contained documents that the Company could have used in discovery, including a discounted cash flow analysis, a leveraged buy-out analysis, and communications about the Entwistle Petitioners' decision to buy or sell ExamWorks' stock and seek appraisal. The Company could have questioned representatives of the Entwistle Petitioners about these documents and used them with other witnesses as well.

A second level of prejudice involves the degradation of the litigation process. For the litigation system to function, parties must follow the rules. If participants suspect that others are not following the rules, then the process deteriorates. People who follow the rules feel like chumps when others seem to be cutting corners or breaking rules and getting ahead. People who otherwise might not think of pushing limits become more aggressive if they think everyone else is doing it. It is this broader, systemic interest that the Delaware Supreme Court seems to have had in mind when stressing that courts must address discovery abuse not only to protect litigants, but also to protect the public and the bar.[57]

As a remedy for the Entwistle Petitioners' discovery abuse, the Company seeks a terminating sanction that would dismiss the Entwistle Petitioners from the case and leave them with the deal price, without interest. They observe that, unlike in a traditional liability case, this sanction would not leave the Entwistle Petitioners empty handed. They would get $35.05 per share. They also would receive the per-share amount that was recovered in a settlement in a companion case for breach of fiduciary duty. Ironically, this sanction would let them avoid the downside risk of an appraisal award below the deal price. Depending on how the case turns out, the sanction might be a blessing.

The Delaware Supreme Court has cautioned that "a default judgment should be granted if no other sanction would be more appropriate under the circumstances."[58] Trial in this case originally was scheduled to begin on February 13, 2018, which would have limited my ability to craft an alternative sanction. After reviewing the parties' submissions, I postponed the trial so that I would have "greater flexibility in crafting a remedy, should the court conclude that a remedy is warranted."[59] Trial has not yet been rescheduled.

With the time afforded by the continuance, a lesser sanction than a default judgment becomes feasible and sufficient to remedy the Entwistle Petitioners' misconduct. The Entwistle Petitioners have already re-produced the documents without relevancy redactions. They also shall produce additional documents called for by this court's ruling on their post-discovery-cutoff privilege logs.[60] Once the Entwistle Petitioners have completed this production, they shall produce witnesses for deposition as requested by the Company. The Company is not limited to one witness, but the Company should be responsible and only request additional witnesses if the contents of the documents and the results of an initial deposition truly warrant questioning more than one witness.

***10** The Company's expert may take into account information learned from the Entwistle Petitioners' production and any depositions. The Company's expert may file a sur-rebuttal report addressing these matters. The petitioners contend that this remedy is disproportionate because it will prejudice all of the petitioners, not just the Entwistle Petitioners. That claim is overblown. As a threshold matter, Co–Lead Counsel had responsibility for conducting discovery on behalf of all petitioners, and depriving the Company of the Entwistle Petitioners' documents during discovery benefitted all petitioners. Consequently, imposing a remedy that affects all petitioners is not disproportionate. More importantly, the remedy is not excessive. The Company can file a sur-rebuttal report limited to the new material. The Company is not getting a complete do-over.

The Entwistle Petitioners shall bear all expenses associated with their late production of documents and the remedy imposed by this decision. The Company is awarded the expenses it has incurred and will incur, including attorneys' fees, for

- reviewing the Entwistle Petitioners' original production;
- following up with the Entwistle Petitioners;
- reviewing the unredacted production;
- briefing and arguing the Entwistle Motion;
- reviewing the additional documents produced in response to this decision;
- conducting the depositions contemplated by this decision; and
- working with the Company's expert to prepare the sur-rebuttal report.

Once the remedial discovery process is complete, the Company shall prepare and provide the Entwistle Petitioners with a Rule 88 affidavit documenting its fees and expenses. If the Entwistle Petitioners dispute the amount due and the parties cannot reach agreement, then the Company may file a motion to quantify the award, supported by the Rule 88 affidavit it provided to the Entwistle Petitioners.

B. The Barclays Documents

The petitioners violated a court order by failing to comply with the discovery cutoff in the Amended Scheduling Order. They agreed to produce documents from third parties, but they did not produce the Barclays Documents before the discovery cutoff. Ten weeks after the discovery cutoff, they produced the Barclays Documents.

A key difference between the Entwistle Petitioners' production and Co–Lead Counsel's production of the Barclays Documents is that the latter appears to have been inadvertent. Co–Lead Counsel explained that for all other third-party witnesses, the Company obtained copies of documents directly from the third party, rather than from the petitioners. It was no secret that the petitioners had subpoenaed documents from Barclays. The petitioners filed their notice of service for the Barclays subpoena on the same day that they gave notice of subpoenas served on six other third parties. Co–Lead Counsel reasonably believed that the Company's attorneys would handle Barclays the same way they handled the other six third parties. The failure to produce the Barclays Documents constituted excusable neglect.

The Company again seeks a terminating sanction because of the late production of the Barclays Documents, this time for all petitioners. In my view, a terminating sanction is too severe. Other, less drastic remedies are available and sufficient to address the discovery issues in this case.

One option for leveling the playing field is to hold that no one can use the Barclays Documents. Co–Lead Counsel has proposed that option, which includes striking the references to the documents from the petitioners' expert report and not using the documents at trial.

Another option for leveling the playing field is to let everyone use the Barclays Documents. Under this option, the parties would have leave to depose a Barclays witness. Both sides could prepare supplemental expert reports addressing any information in the Barclays Documents or obtained from the

Barclays witness. Both sides would be able to use the resulting discovery at trial.

***11** Because the Company was harmed by the late production of the Barclays Documents, the Company can choose which remedy it prefers. The Company has ten days to notify Co–Lead Counsel of its election.

Having found that the failure to produce the Barclays Documents was inadvertent, I will not require petitioners to reimburse the Company for the expenses incurred in reviewing the Barclays Documents or pursuing any further Barclays-related discovery, if they choose that option. I could require the petitioners to reimburse the Company for the expenses incurred briefing and arguing the Barclays Motion, but I did not require the Company to reimburse the petitioners for the expenses incurred briefing and arguing the motion for a protective order involving Berkshire. This is a similar situation and should be treated similarly.

C. The Privilege Logs

The Entwistle Petitioners and the G & E Petitioners violated a court order by failing to produce their privilege logs until after the discovery cutoff. Privilege logs are part of discovery. Producing a timely log is part of a party's obligation when asserting privilege.

In their responses to the Company's discovery requests, the Entwistle Petitioners and the G & E Petitioners represented that they would produce documents subject to claims of privilege. The burden of establishing privilege rests on the party asserting it.[61]

> [A] bare allegation that information and documents are protected from discovery by the attorney-client privilege is insufficient without making more information available .... It is incumbent on one asserting the privilege to make a proper showing that each of the criteria [underlying the attorney-client privilege] exist[s] .... A proper claim of privilege requires a specific designation and description of the documents within its scope as well as precise and certain reasons for preserving their confidentiality.[62]

An insufficiently supported claim of privilege can result in waiver.[63]

***12** The privilege log enables the party that requested documents to evaluate the producing party's claim of privilege. "The log is supposed to provide sufficient information to enable the adversary to assess the privilege claim and decide whether to mount a challenge .... Just as you can't hit what you can't see, you can't challenge what the other side hasn't described."[64] Producing a privilege log after the discovery cutoff prevents the opposing party from evaluating the log, making timely challenges, and using the resulting documents in discovery. Producing a post-cutoff log has the same effect as not producing a log, which is the same thing as not providing any support for a claim of privilege. "An improperly asserted claim of privilege is no claim of privilege at all."[65]

The Entwistle Petitioners and the G & E Petitioners failed to produce their logs until months after the discovery cutoff. On the facts of this case, waiver is an appropriate consequence. The Entwistle Petitioners and G & E Petitioners need not produce entries where (i) counsel was the author or a principal recipient (not simply a copy recipient) *and* (ii) the item post-dates the filing of the appraisal proceeding on August 25, 2016.

The Company has leave to conduct supplemental depositions of the petitioners' representatives to explore any materials produced after their depositions or as a result of this decision. Each of the petitioners shall bear the cost of the supplemental depositions of its own representatives. As with any supplemental depositions resulting from the Entwistle Petitioners' late production, the Company should not abuse this opportunity. It should only take the depositions that are necessary.

III. CONCLUSION

The motions for sanctions are granted. The parties shall proceed as directed in this decision.

All Citations

Not Reported in Atl. Rptr., 2018 WL 1008439

Footnotes

[1] *See* Dkt. 72 (the "Entwistle Motion"). This decision refers to the five funds as the "Entwistle Petitioners." The parties called them the "WI Petitioners," a cryptic moniker that seemed to refer to "Water Island," which is the name of one of the funds.

[2] *See* Dkt. 81 (the "Barclays Motion").

[3] This decision calls them the "G & E Petitioners," which is a term the parties used. Unfortunately, it is not entirely clear which petitioners are included in that term. The Barclays Motion identified the five petitioners who produced logs on December 12, 2017, as "Pivot Point Capital, Hudson Bay, Lord Abbett, Paloma, and Weiss Asset." The opposition introduced the term "G & E Petitioners" and cited this passage in the Barclays Motion. The opposition did not otherwise identify who comprises the G & E Petitioners, and I cannot find any reference on the docket to "Paloma" or "Weiss Asset" being petitioners. Because the rationale for this decision turns on the production of documents and privilege logs months after the discovery cutoff, I can leave this detail to the parties.

[4] Dkt. 5 (the "Consolidation Order").

[5] *Id.* ¶¶ 10–12 (emphasis added).

[6] *Id.* ¶ 7.

[7] Dkt. 9 (the "Initial Scheduling Order").

[8] *Id.* ¶ 1(a)-(d).

[9] *See* Dkt 24.

[10] Dkt. 31 (the "Amended Scheduling Order").

[11] *Id.* ¶ 1(a)-(c).

[12] Dkt. 73 Ex. 2, at 14.

[13] *Id.* Ex. 3, at 23.

[14] Dkt. 48.

[15] Dkt. 50.

[16] Dkt. 81 ¶ 9.

[17] *Id.* Ex. 6, at 18.

[18] Dkt. 60 ¶ 5.

[19] Dkt. 70 (the "Berkshire Ruling").

[20] Dkt. 79 at 26–27.

[21] *Id.* at 27.

[22] *Id.*

[23] Dkt. 72 ¶ 19 & Ex. 15.

[24] *Id.* ¶ 20.

[25] Dkt. 74 Ex. 17.

[26] *Id.* Ex. 19.

[27] *Id.* Ex 24.

[28] Dkt. 81 Ex. 10, App'x C.

[29] *Id.* Ex. 13, at 1.

[30] *Id.* ¶ 15–16.

[31] *Id.* ¶ 11.

[32] *Id.* ¶ 12.

[33] Dkt. 72 ¶ 26.

[34] Dkt. 74 Ex. 18.

[35] *Levy v. Stern*, 687 A.2d 573 (Del. 1996) (TABLE).

[36] *Hoey v. Hawkins*, 332 A.2d 403, 405 (Del. 1975) (internal quotation marks and citation omitted).

[37] *E.I. DuPont de Nemours & Co. v. Fla. Evergreen Foliage*, 744 A.2d 457, 461 (Del. 1999).

[38] *IQ Hldgs. Inc. v. Am. Commercial Lines, Inc.*, 2012 WL 3877790, at *2 (Del. Ch. Aug. 30, 2012).

[39] *Ams. Mining Corp. v. Theriault*, 51 A.3d 1213, 1238 (Del. 2012) (alterations omitted) (internal quotation marks and citation omitted); *accord Sammons v. Doctors for Emergency Servs., P.A.*, 913 A.2d 519, 528 (Del. 2006).

[40] *Orloff v. Shulman*, C.A. No. 852–VCL (Del. Ch. April 10, 2007) (citation omitted).

[41] *Holt v. Holt*, 472 A.2d 820, 824 (Del. 1984) (emphasis in original; quoting Delaware Superior Court Civil Rule 1).

[42] *Hoag v. Amex Assurance Co.*, 953 A.2d 713, 717 (Del. 2008) (internal quotation marks and footnote omitted).

[43] *Cartanza v. Cartanza*, 2013 WL 1615767, at *2 (Del. Ch. Apr. 16, 2013), *reargument denied*, 2013 WL 3376964 (Del. Ch. July 8, 2013).

[44] *In re Rinehardt*, 575 A.2d 1079, 1082 (Del. 1990).

[45] Ct. Ch. R. 37(b)(2)(A)–(C).

[46] *Beard Research, Inc. v. Kates*, 981 A.2d 1175, 1189 (Del. Ch. 2009) (internal quotation marks and citation omitted); *see Hoag*, 953 A.2d at 716–17 (noting court's authority to impose sanctions for discovery abuse under Rule 37 or pursuant to its "inherent authority").

[47] *Lehman Capital v. Lofland ex rel Estate of Monroe*, 906 A.2d 122, 131 (Del. 2006) (emphasis in original; internal quotation marks and citation omitted).

[48] *Sundor Elec., Inc. v. E.J.T. Constr. Co., Inc.*, 337 A.2d 651, 652 (Del. 1975) (internal quotation marks and citation omitted).

[49] *James v. Nat'l Fin. LLC*, 2014 WL 6845560, at *9 (Del. Ch. Dec. 5, 2014).

[50] *Id.*

[51] Ct. Ch. R. 37(b)(2) (emphasis added).

[52] *Id.*

[53] *Bader v. Fisher*, 504 A.2d 1091, 1096 (Del. 1986); *accord Holt*, 472 A.2d at 823.

[54] *Bader*, 504 A.2d at 1096.

[55] *Wileman v. Signal Fin. Corp.*, 385 A.2d 689, 690–91 (Del. 1978) (internal citation omitted). *See generally* 8B Charles Alan Wright, Arthur R. Miller & Richard L. Marcus, *Federal Practice and Procedure* § 2288 (3d ed. 2010).

[56] Dkt. 72 ¶ 17–18.

[57] *See Holt*, 472 A.2d at 824 ("Discovery abuse has no place in [Delaware] courts, and the protection of litigants, the public, and the bar demands nothing less than that [Delaware] trial courts be diligent in promptly and effectively taking corrective action ....").

[58] *Hoag*, 953 A.2d at 717.

[59] Dkt. 107.

[60] *See* Part II.C, *infra*.

[61] *Moyer v. Moyer*, 602 A.2d 68, 72 (Del. 1992); *accord Sokol Hldgs., Inc. v. Dorsey & Whitney, LLP*, 2009 WL 2501542, at *6 n.28 (Del. Ch. Aug. 5, 2009) (Strine, V.C.); *SICPA Hldgs., S.A. v. Optical Coating Lab., Inc.*, 1996 WL 636161, at *7 (Del. Ch. Oct. 10, 1996); *Emerald P'rs v. Berlin*, 1994 WL 125047, at * 1 (Del. Ch. Mar. 30, 1994); *Hoechst Celanese Corp. v. Nat'l Union Fire Ins. Co.*, 623 A.2d 1118, 1122 (Del. Super. 1992); *In re Fuqua Indus., Inc. S'holders Litig.*, 1992 WL 296448, at *3 (Del. Ch. Oct. 8, 1992); *Deutsch v. Cogan*, 580 A.2d 100, 107 (Del. Ch. 1990).

[62] *Int'l Paper Co. v. Fibreboard Corp.*, 63 F.R.D. 88, 93–94 (D. Del. 1974); *see also Sokol Hldgs.*, 2009 WL 2501542, at *8; *Deutsch*, 580 A.2d at 107; *Reese v. Klair*, 1985 WL 21127, at *5 (Del. Ch. Feb. 20, 1985).

[63] *See, e.g., Willemijn Houdstermaatschaapij BV v. Apollo Comput., Inc.*, 707 F. Supp. 1429, 1443 (D. Del. 1989) (ordering production of inadequately described documents); *Mechel Bluestone, Inc. v. James C. Justice Cos.,*

Inc., 2014 WL 701194, at *5 (Del. Ch. Dec. 12, 2014) (collecting authorities and ordering partial waiver on facts of case); *Klig v. Deloitte LLP*, 2010 WL 3489735, at *8 (Del. Ch. Sept. 7, 2010) (collecting authorities and finding waiver on facts of case); *Sokol Hldgs.*, 2009 WL 2501542, at *8 ("Sokol has waived the right to [assert privilege] by failing to update its privilege log to contain detailed enough descriptions ...."). *See generally* 1 Donald J. Wolfe, Jr. & Michael A. Pittenger, *Corporate and Commercial Practice in the Delaware Court of Chancery* § 7.04 (2012).

[64] *Klig*, 2010 WL 3489735, at *6.

[65] *Int'l Paper*, 63 F.R.D. at 94; *accord TCV VI, L.P. v. TradingScreen Inc.*, 2015 WL 5674874, at *8 (Del. Ch. Sept. 25, 2015); *Mechel Bluestone*, 2014 WL 701194, at *5; *M & G Polymers USA, LLC v. Carestream Health, Inc.*, 2010 WL 1611042, at *51 n.262 (Del. Super. Apr. 21, 2010); *Williams Nat. Gas Co. v. Amoco Prod. Co.*, 1991 WL 236919, at *2 (Del. Super. Nov. 8, 1991); *Council of Unit Owners of Sea Colony E. v. Carl M. Freeman Assocs., Inc.*, 1990 WL 161169, at *2 (Del. Super. Sept. 26, 1990); *Playtex, Inc. v. Columbia Cas. Co.*, 1989 WL 5197, at *2 (Del. Super. Jan. 5, 1989); *Reese*, 1985 WL 21127, at *5.

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In re Michael Anthony WAGNER, et al.

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MEMORANDUM OPINION AND ORDER

GOLDEN, J.

***1** Appellants Paul and Dawn Trostle appeal the February 3, 2006 Speaking Order of the Bankruptcy Court granting Appellee's motion *in limine* and entering judgment in favor of appellee and against appellants. After carefully considering the parties' submissions on appeal, and oral argument, the Court affirms in part and reverses in part the Speaking Order of the Bankruptcy Court.

Appellants' 14-year-old son Jeremiah was killed when Appellee Michael Wagner struck him with a car while traveling on a busy Whitehall Township road in 1997. As a suit over the accident was pending in the Court of Common Pleas of Lehigh County, Appellee filed for bankruptcy. Appellants filed an adversary action claiming that Appellee's debts were non-dischargeable under 11 U.S.C. § 523(a)(6), which forbids discharge of debts incurred through willful and malicious injury to another, and 11 U.S.C. § 523(a)(9), which forbids discharge of debts incurred through “death or personal injury caused by the debtor's operation of a motor vehicle ... if such operation was unlawful because the debtor was intoxicated from using alcohol ...” Following a trial, the Bankruptcy Court granted Appellee's motion *in limine* to strike the report and testimony of Appellant's expert Samuel Land, M.D., and held that the debts were dischargeable.

The Court reverses in part and affirms in part the Bankruptcy Court's Speaking Order. The Court reverses the portion of the Speaking Order granting Appellee's motion *in limine* which precluded the report and testimony of Dr. Land. The Court also reverses the portion of the Speaking Order entering judgment in favor of Appellee and against Appellants and finding that the debt is dischargeable under 11 U.S.C. § 523(a)(9). The remainder of the Speaking Order is affirmed, as are all of the factual findings of the Bankruptcy Court. The Court remands the case to the Bankruptcy Court for consideration of Dr. Land's report and testimony in conjunction with the record and factual findings of the Bankruptcy Court.

Facts and Issues on Appeal

Appellee admitted to drinking alcohol before the fatal accident, but was not charged with driving under the influence. His blood alcohol content (BAC) was measured as .04% when tested more than two hours after the accident. Appellants intended to offer the report and testimony of Dr. Samuel Land, a pathologist, who opined that Appellee's blood alcohol content could be extrapolated to have been over .08% at the moment of the accident. Under Pennsylvania law at the time of the accident, a driver whose BAC measured less than .05% was presumed to be unimpaired. 75 Pa.C.S.A. § 1547(d)(1). No presumption attached to a BAC between .05% and .10%, but such a BAC reading could be introduced, along with other competent evidence, to prove intoxication. *Id.* at § 1547(d)(2) (repealed). Thus, if believed, Land's testimony would have cast doubt on Appellee's claim that he was not impaired.

The Bankruptcy Court did not consider Land's report, but did listen to evidence from witnesses to the accident and its aftermath. The Bankruptcy Court concluded that the witnesses had credibly rebutted the suggestion that Appellee was operating his vehicle while impaired. The parties raise a number of issues on appeal, including:

***2** 1. Whether Appellants' appeal should be dismissed because their brief did not comply with Federal Rule of Bankruptcy Procedure 8010?

2. Whether Appellants must establish a causal connection between driving while intoxicated and the accident for the section 523(a) (9) exception to apply?

3. Whether the Bankruptcy Court abused its discretion in granting Appellee's motion *in limine* to strike the testimony of Appellants' expert Samuel Land?

4. Whether the Bankruptcy Court erred in stating that Appellants' other evidence of intoxication, besides Land's report, was irrelevant?

5. Whether the Bankruptcy Court erred in determining that Appellants had failed to satisfy their burden of proving that Appellee's operation of his vehicle at the time of the accident was unlawful because he was intoxicated, without Land's report and testimony? Appellants argue that this conclusion is against the weight of the evidence.

6. Whether the Bankruptcy Court erred in determining that the Appellants failed to meet their burden of proving Appellee's debts were incurred as a result of a willful and malicious injury under section 523(a)(6)?

The Court concludes that the Bankruptcy Court abused its discretion in granting the motion *in limine* to strike the report and testimony of Samuel Land. The Court holds that the law does not require Appellants to establish a causal link between driving while intoxicated and the accident for the section 523(a)(9) exception to apply. As to all other issues raised on appeal, the Court affirms the holding of the Bankruptcy Court. The case is remanded to the Bankruptcy Court for review consistent with this opinion.

Jurisdiction and Standard of Review

The Court has jurisdiction over this appeal pursuant to 28 U.S.C. § 158(a). A district court may not set aside the factual findings of the Bankruptcy Court unless they are clearly erroneous. *In re: TWA,* 145 F.3d 124, 131 (3d Cir.1998). The review of a Bankruptcy Court's factual findings is highly deferential. *Kool, Mann, Coffee and Co. v. Coffey,* 300 F.3d 340, 353 (3d Cir.2002) (“It is the responsibility of an appellate court to accept the ultimate factual determination of the fact-finder unless that determination either is completely devoid of minimum evidentiary support displaying some hue of credibility or bears no rational relationship to the supportive evidentiary data.”) The Bankruptcy Court's conclusions of law are subject to *de novo* review. *In re: TWA,* 145 F.3d at 131. The Court reviews the decision to exclude an expert report for abuse of discretion, which occurs when a ruling was founded on an error of law, a clearly erroneous view of the facts, or a misapplication of law to the facts. *Marco v. Accent Pub. Co.,* 969 F.2d 1547, 1548 (3d Cir.1992); *Reinert v. Larkin,* 211 F.Supp.2d 589, 607 (E.D.Pa.2002). Moreover, the Court may consider legal issues presented by the record, even if those issues were not decided by the Bankruptcy Court, when they are inextricably intertwined with other issues on appeal. *In re: Watts,* 876 F.2d 1090, 1095 n. 8 (3d Cir.1989).

Bankruptcy Rule of Procedure 8010

***3** The Federal Rules of Bankruptcy Procedure require that briefs not exceed fifty pages and contain a statement of the case, a statement of the basis of appellate jurisdiction, a table of contents and authorities, an argument, and a short conclusion. Fed. R. Bankr.P. 8010. Appellants' original brief exceeded the page limit of Rule 8010 and contained other flaws. For these reasons, Appellee urges the Court to dismiss the appeal. *In re: Gulf Woods Corp.,* 189 B.R. 320, 323 (E.D.Pa.1995). Nonetheless, because Appellants quickly submitted an amended brief that complies with the Rule, the Court will not dismiss the appeal.

The Exclusion of the Testimony of Samuel Land, M.D.

Appellants' expert Samuel Land, a forensic pathologist, based his opinion on the report of George Jackson, Ph.D., a forensic toxicologist who had been retained by the District Attorney's office to opine in the criminal investigation of the accident and resulting case. Jackson prepared his report by reviewing documents and records related to the accident, including lab and toxicology results, as well as police incident reports. (Jackson Report p. 427A-428A).

Jackson did not claim in his report that he was present at the accident, and his report was explicitly based on certain assumptions. For example, he notes that, in preparing his report, he assumed that Appellee had no food in his stomach. (*Id.* at p. 429A ¶ i). Jackson prepared calculations and an extrapolation of Appellee's BAC at the time of the accident based on the written information provided, including Appellee's height and weight, and his stated assumptions. (*Id.* at p. 428A ¶ a). Jackson concluded that Appellee's extrapolated BAC at the time of the accident was .08%. (*Id.* at p. 429A ¶ f).

In preparing his report, Land reviewed Jackson's opinion and the attached background materials. (Land Dep. p. 13). He also reviewed a blood alcohol and toxicological report on Appellee, police reports, and witness depositions. (*Id.* at p. 12, 13, 21). He testified at deposition that such materials are the type of materials upon which an expert in his field would rely in reaching a conclusion regarding the toxicological consequences of alcohol consumption. (*Id.* at p. 13). Considering the metabolic rate of the average male, the expired time between the drawing of Appellee's blood and the accident, and Appellee's reported BAC, Land calculated that Appellee's BAC was likely between .08% and .086% at the time of the accident. (*Id.* at p. 23-27). Land was deposed by Appellee's counsel.

The Bankruptcy Court excluded Land's testimony because "Dr. Land ... offers no independent factual basis to support his conclusion, but instead relies upon and repeats the opinions of Dr. Jackson." Op. at 2 n. 1. The Bankruptcy Court noted that Jackson was unavailable to be cross-examined at trial. *Id.* The Bankruptcy Court also found it significant that Land was unable to testify about facts relating to the accident, including when Appellee had his first and last alcoholic drink, what kind of drink he had, whether he had consumed the entire drink, and whether he had eaten before the accident. *Id.*

***4** The Federal Rules of Evidence do not permit experts to simply "parrot" the ideas of other experts or individuals. *See, e.g., Loeffel Steel Prod.s v. Delta Brands,* 387 F.Supp.2d 794, 824 (N.D.Il.2005) (expert testimony that simply repeated the assertions of non-expert company employees was inadmissable). Having reviewed both reports, the Court concludes that Land has done more than parrot Jackson. As Appellants point out, Land discussed his methodology at some length, recalculated the extrapolation put forward by Jackson, and actually disagreed with Jackson in some results. (Land Dep. p. 22-28). In addition to using Jackson's report, Land examined police reports and witness statements to determine whether Appellee was intoxicated. (*Id.* at 11). In his deposition, Land states specifically that these materials are the kind that are reasonably relied upon by experts in his field. (*Id.* at p. 13).

Moreover, experts are permitted to rely on materials used by other experts in developing their own opinions. *See United States v. Posey,* 647 F.2d 1048, 1051 (10th Cir.1981) (in a drug prosecution, it was permissible for one chemist to rely on tests run by another in testifying that a substance was cocaine: "It is quite reasonable for a chemist to review another chemist's analysis when forming an opinion as to the veracity of the latter's test results.") The Advisory Committee notes to Federal Rule of Evidence 703 specifically approve of medical experts' practice of gathering data and anecdotes from other doctors and nurses in developing their opinions. In a manner similar to a doctor making a diagnosis, Land used a mix of objective data and subjective analysis from another expert to opine about Appellee's physical status at the time of the accident, and to create an admissible report.

The list of specific facts about the accident with which Land is allegedly unfamiliar-such as the time of Appellee's last drink, or the contents of his last meal before his accident-would go to the weight accorded to Land's report and testimony, rather than its admissibility. It is unclear that Jackson, the initial expert, was aware of those facts, either; for example, Jackson based his report on the assumption that Appellee had no food in his stomach. (Jackson Report at 429A ¶ i). Thus, the Bankruptcy Court's doubts about the quality of Land's testimony do not relate to the evidentiary rule about experts who "parrot." As a result, the Bankruptcy Court abused its discretion in excluding Dr. Land's report.

Causation under § 523(a)(9)

Appellee argues that Appellants' claim fails not only because they did not prove intoxication, but also because they did not establish a causal link between the alleged intoxication and the accident, which Appellee maintains is required under section 523(a) (9). The statute provides that debt is non-dischargeable if it was "caused by the debtor's operation of a motor vehicle ... if such operation was unlawful because the debtor was intoxicated from using alcohol, a drug, or another substance." Because the question of whether creditors must prove causation is inextricably intertwined with the question of whether the Appellants have met their burden of proof, and because both parties address the issue of causation in their briefs, the Court has considered the issue although the Bankruptcy Court did not render a decision on it. Op. at 4 n. 3. The Court finds that the law does not require the Appellants to prove that Appellee's intoxication was the cause of the accident.

***5** Appellee points to case law in which courts have found a debt discharged, even when the debtor was driving while impaired, because the creditor failed to prove that the intoxication caused the accident. Those cases, however, are easily distinguished from this one. In *In re: Mutschler,* 1994 Bankr.LEXIS 1294, at *13 (Bankr.W.D.Pa. Aug, 26, 1994), the plaintiff failed to include in the record any evidence to suggest that the intoxication of the debtor caused the fatal accident. There was simply no discussion of vehicle speed, road conditions, or the impact of the crash on the victim and vehicles, beyond the simple assertion that a collision had occurred and a driver was impaired. *Id.* In *In re: Christiansen,* 80 B.R. 481, 483 (W.D.Mo.1987), the court noted that both the debtor and the creditor were intoxicated at the time of the accident, creating an issue regarding whose intoxication caused the collision. In this case, in contrast, the record contains significant detail about driving conditions and the impact of the accident. Moreover, there is no question that Appellant's decedent was sober at the time of the accident.

In addition, this Court is persuaded by the reasoning of the court in *General Casualty Company of Wisconsin v. Keating,* 80 B.R. 115, 118 (Bankr.E.D.Wis.1987). The *General Casualty* court noted that Congress enacted section 523(a)(9) to create an objective standard for non-dischargeability cases-if a driver is impaired, the debt is non-dischargeable. *Id.* Moreover, the court held that the debtor's preferred reading of the statute was grammatically incorrect. At the time, the non-dischargeability provision applied "wherein liability was incurred by such debtor as a result of the debtor's operation of a motor vehicle while legally intoxicated." As the court stated,

> " '[Debtor] argues that it should be construed to provide that the liability must arise as a result of intoxication; however, the statute states that the cause of the defendant's liability is "as a result of the debtor's operation of a motor vehicle." The phrase "while legally intoxicated" modifies the word "operation," denoting only a condition in existence at the time of operation. If the condition exists at that moment, inquiry need go no further." *Id.*

This logic and application of grammatical rules still applies today. Accepting this reading of the statute and unpersuaded by the authority provided by the Appellee, the Court holds that Appellants need not prove that Appellee's intoxication was the cause of the accident for section 523(a)(9) to apply.

Other Evidence of Intoxication and the Appellants' Burden of Proof

Appellants argue that the Bankruptcy Court erred in deeming their other proffered evidence of Appellee's intoxication "irrelevant." The Bankruptcy Court found Appellants' evidence was unconvincing for two reasons: first, because it was irrelevant in light of the lack of a criminal charge against Appellee; and second, because Appellee had offered "credible rebuttal evidence to establish that he was not intoxicated at the time of the accident." Op. at p. 4-5 n. 3. The Bankruptcy Court clearly evaluated Appellants' other evidence of intoxication, but did not credit it more than the rebuttal evidence of sobriety. Because the Bankruptcy Court weighed Appellants' other evidence of intoxication, this Court need not reach the question of whether the evidence was also "irrelevant."

***6** Appellants also argue that they met their burden of proving by a preponderance of the evidence that Appellee was intoxicated, even absent the report and testimony of Dr. Land. Their evidence suggested, for example, that following the accident Appellee failed some roadside sobriety tests, walked and acted strangely, drank copious amounts of fluids, and spoke in a "mush-mouthed" manner. (Appellants' Br. at 32-33). The Bankruptcy Court considered this evidence. The Bankruptcy Court was persuaded, however, by other evidence from police officers at the scene who reported that the Appellee performed some sobriety tests correctly, that his speech was not slurred, and that he walked normally. Op. at p. 5 n. 3. Moreover, the Bankruptcy Court concluded that the shock of the accident, as well as the profusion of shattered glass in the Appellee's hair, mouth, eyes, and on his feet, accounted for irregularities in Appellee's behavior. *Id.* Because there is evidentiary support for the Bankruptcy Court's conclusion that the Appellants did not meet their burden of proof without Land's report and testimony, this Court affirms the Bankruptcy Court's holding.

The § 523(a)(6) exception to non-dischargeability

The Court affirms the Bankruptcy Court's conclusion that Appellants did not meet their burden of proving Appellee's actions willful and malicious under section 523(a)(6). The Supreme Court has stated clearly that reckless or negligent acts will not produce liability under section 523(a)(6). *Kawaauhua v. Geiger,* 523 U.S. 57, 63, 118 S.Ct. 974, 140 L.Ed.2d 90 (1998). The Bankruptcy Court determined that Appellee acted in a manner "at most, negligent or reckless," op. at 5 n. 4, and this Court will not disrupt this factual finding because it is not clearly erroneous.

Appellants argue that in determining whether Appellee acted in a willful and malicious manner, the Bankruptcy Court should have focused on whether Appellee intended to commit the act which caused the injury, rather than whether he intended to cause the injury itself. The Supreme Court has rejected this approach. *Id.* at 61 ("The word 'willful' in (a)(6) modifies the word "injury," indicating that nondischargeability takes a deliberate or intentional *injury,* not merely a deliberate or intentional *act* that leads to injury.") Moreover, as Appellee rightly points out, Appellants' reading of the statute would render section 523(a)(9) superfluous-if driving under the influence could be considered willful and malicious under average circumstances, Congress would have had no need to add a specific provision to the Bankruptcy Code to address dischargeability and drunken driving. *Id.* at

62. Thus, this Court affirms the Bankruptcy Court's ruling that the debt is dischargeable under section 523(a)(6).

In sum, the Court affirms all of the Bankruptcy Court's factual findings. The Court also affirms all of the Bankruptcy Court's conclusions of law, with the exception of the decision to exclude the expert report of Samuel Land, and to enter judgment for Appellee and against Appellants and finding that the debt is dischargeable under 11 U.S.C. § 523(a)(9). The Court will remand this matter to the Bankruptcy Court solely for the consideration of the report and testimony of Samuel Land in conjunction with the record and the previous factual findings of the Bankruptcy Court.

ORDER

***7** AND NOW, this 27th day of March, 2007, after review of all the briefs in this bankruptcy appeal, and oral argument, it is hereby ORDERED that the Speaking Order of the Bankruptcy Court dated February 3, 2006 is REVERSED in part and AFFIRMED in part as follows:

1. The portion of the Speaking Order granting the Appellee's *Motion in Limine* which precluded the report and testimony of Dr. Samuel Land is REVERSED.

2. The portion of the Speaking Order entering judgment in favor of Appellee and against Appellants and finding that the debt is dischargeable under 11 U.S.C. § 523(a)(9) is REVERSED.

3. The remainder of the Speaking Order is AFFIRMED as are all of the factual findings of the Bankruptcy Court.

The Court REMANDS the case to the Bankruptcy Court for the sole purpose of considering Dr. Land's report and testimony in conjunction with the record and factual findings of the Bankruptcy Court.

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UNPUBLISHED OPINION. CHECK
COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

LONGPATH CAPITAL, LLC, a Delaware
limited liability company, Petitioner,
v.
RAMTRON INTERNATIONAL CORPORATION,
a Delaware corporation, Respondent.

C.A. No. 8094–VCP
|
Submitted: March 3, 2015
|
Decided: June 30, 2015

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MEMORANDUM OPINION

PARSONS, Vice Chancellor.

***1** In this appraisal action, the petitioner asks the Court to determine the fair value of its shares in the respondent. On November 10, 2012, a third party acquired the respondent in a hostile cash merger for $3.10 per share. The deal had an equity value of approximately $110 million and paid a 71% premium over the respondent's unaffected stock price of $1.81.

The petitioner acquired its shares after the announcement of the merger and demanded appraisal pursuant to *8 Del. C.* § 262. The respondent contends the merger price less synergies offers the most reliable measure of the fair value of its shares. That methodology, as applied by the respondent's expert, yields a value of $2.76 per share. The petitioner's expert, relying on a combination of a discounted cash flow ("DCF") analysis and a comparable transactions analysis, contends that the fair value is $4.96 per share.

For the reasons that follow, I conclude that a DCF analysis is not an appropriate method of determining fair value in this instance. The utility of a DCF ceases when its inputs are unreliable; and, in this instance, I conclude that the management projections that provide the key inputs to the petitioner's DCF analysis are not reliable. The parties agree that there are no comparable companies. The petitioner relies, in part, upon a comparable transactions approach, but I conclude that his two-observation data set does not provide a reasonable basis to determine fair value. Although the petitioner thoroughly disputes this point, I conclude that the sales process in this instance was thorough and that the transaction price less synergies provides the most reliable method of determining the fair value of the petitioner's shares. The respondent, however, has not shown that the synergies in fact amounted to $0.34 per share, as it claims. Instead, I adopt the petitioner's estimate of $0.03 per share in synergies, resulting in a fair value of $3.07 per share.

I. BACKGROUND

I begin by providing a brief overview of the parties, the respondent and its business, and the process leading up to the merger.[1] I delve more deeply into several of these and related topics in subsequent Sections.

A. The Parties

Petitioner, LongPath Capital, LLC ("LongPath"), is an investment vehicle that began acquiring shares of the respondent in mid-October 2012, about a month after the announcement of the merger.[2] Overall, LongPath timely demanded and perfected its appraisal rights as to 484,700 shares of common stock in the respondent.[3]

Respondent, Ramtron International Corporation ("Ramtron" or the "Company"), is a fabless semiconductor company that produces F–RAM. A "fabless" semiconductor company is one that does not manufacture the silicon wafers used in its products, but instead, outsources that task to a separate company known as a "fab" or a "foundry."[4] RAM stands for random access memory, a ubiquitous component of computers. F–RAM is ferroelectric RAM.[5] The benefits of

F–RAM are that it has fast read and write speeds, can be written to a high number of times, and consumes low power.[6] Importantly, F-RAM will retain memory when power is lost.[7]

***2** Nonparty Cypress Semiconductor Corporation ("Cypress") issued a bear hug letter to Ramtron on June 12, 2012, offering to buy all of its shares for $2.48 per share.[8] After Ramtron's board rejected the offer as inadequate, Cypress initiated a hostile tender offer on June 21, 2012, at $2.68 per share.[9] Ramtron and Cypress eventually reached an agreement on a transaction price of $3.10 per share and signed a merger agreement on September 18, 2012.[10] Following a subsequent tender offer—apparently in an unsuccessful effort to acquire 90% or more of the outstanding stock or at least solidify Cypress' stock holdings—and a stockholder vote, the long-form merger closed on November 20, 2012 (the "Merger").[11]

B. Ramtron's Operative Reality

Throughout this litigation, Respondent has portrayed Ramtron as a struggling company unlikely to be able to continue as a business had the transaction with Cypress not concluded successfully. Petitioner, by contrast, describes Ramtron as a company with strong patent and intellectual property protection of its core products, a successful new management team, and excellent business prospects. Indeed, in relying on the management projections, Petitioner characterizes Ramtron as a company on the verge of taking off like a rocket. Perhaps unsurprisingly, I find that Ramtron's operative reality at the time of the Merger was somewhere in between these practically polar opposite characterizations.

1. Ramtron's foundry situation

As a fabless semiconductor company, Ramtron's relationships with its foundries were vitally important. Indeed, Ramtron depended on its foundry to manufacture its products. At the time of the Merger, Ramtron's primary foundry was Texas Instruments ("TI").[12] Ramtron's contract with TI provided that, if TI decided to terminate the contract, it would have to provide three additional years of products to Ramtron. By contrast, in the event of a change-in-control transaction at Ramtron, TI could stop providing foundry services after only ninety days.[13]

Semiconductor foundries were the subject of a substantial amount of testimony at trial. As will be seen, the subject of foundries relates to both the reliability of the management predictions and the disputed cause of Ramtron's poor performance in 2012. Gery Richards, Ramtron's CFO at the time of the Merger,[14] testified that Fujitsu previously served as the Company's primary foundry. In 2009, Fujitsu gave Ramtron a "last-time buy" notice under the relevant contract, indicating that Fujitsu intended to terminate its foundry relationship with Ramtron in two years.[15]

The testimony at trial made clear that transitioning foundries is not a simple process. Semiconductors are complex products. In fact, even the silicon wafers from which the semiconductors are created are not commodities but instead vary by company.[16] Additionally, each foundry's technology differs and F–RAM, being a relatively unique product, complicates the process further. Thus, transitioning to a new foundry requires understanding the foundry's manufacturing technology and how it interacts with the semiconductors as designed, then modifying the product design to eliminate any resulting errors, then completing several rounds of product testing followed by further design modifications to eliminate any previously undiscovered errors, and then allowing the customers to evaluate the product before finally moving to full-scale production.[17] Unlike, for example, consumer RAM that one could purchase at an electronics store for a PC and then, depending on the model, simply "plug and play," Ramtron's F–RAM often was designed into the product being created by another manufacturer, thus inhibiting Ramtron's ability to unilaterally change its products in any significant way. According to T.J. Rodgers, the CEO of Cypress, even for a noncontroversial shift of "going to a different foundry, to change one of your products, you're looking at two years plus."[18]

***3** In fact, Ramtron's own track record of foundry transitions suggests that two years probably is a significant underestimate. When Fujitsu gave Ramtron a last-time buy notice in 2009, Ramtron already had been attempting to develop a second foundry relationship with TI. The effort of transitioning to TI had begun in 2004 and took seven years to complete.[19] That transition was not smooth, resulting in product shortages that caused Ramtron to place its customers on allocation.[20] Despite the difficulty of transitioning from Fujitsu to TI, Ramtron succeeded, eventually, in obtaining a reliable new foundry.

To increase its flexibility and reduce its dependence on TI, Ramtron sought to develop a second foundry relationship with IBM. That effort, however, never succeeded. Thomas Davenport, Ramtron's Vice President of Technology at the time of the Merger,[21] described the Company's attempt to work with IBM. Davenport headed up a team of six people that worked from 2009 until spring 2012, attempting to get IBM up and running as a second Ramtron foundry. They incurred $17 million in direct costs in addition to $16 million in capital equipment purchased by Ramtron and provided to IBM to enable it to produce F–RAM.[22] But, in what Davenport considered a “huge personal disappointment,”[23] the integration project failed and Ramtron never achieved a single milestone. To put the IBM investment in context, in 2011 Ramtron had approximately $66 million in revenue.[24]

The witnesses at trial uniformly attested to the difficulty of transitioning foundries.[25] Ramtron's own experience with transitioning to TI and its failed attempt to develop IBM as a foundry confirm this fact. Nevertheless, on July 20, 2012, about a month after Cypress launched its hostile bid for Ramtron, Ramtron entered into a manufacturing agreement with ROHM Co., Ltd. (“ROHM”), a Japanese company, to act as Ramtron's second fab.[26] Ramtron's management's five-year forecasts incorporate the purported cost savings that would derive from having ROHM operate as a second, or even the primary, foundry for Ramtron.

2. Ramtron's business and finances

Ramtron's board of directors installed Eric Balzer as the Company's new CEO in January 2011.[27] He hired Pete Zimmer to lead the Company's sales department. At Zimmer's recommendation, Scott Emley was hired to lead Ramtron's marketing department. Both Zimmer and Emley had worked at TI and joined Ramtron sometime in 2011.[28] Richards officially became CFO in late 2011 or 2012.[29] Thus, as of the time of the Merger, most of Ramtron's executives had been in their positions for less than two years and, in the case of Emley and Zimmer, about a year.

The difficult transition from Fujitsu to TI caused problems for Ramtron's day-today business throughout 2011 and into 2012. A brief overview of Ramtron's sales process is required in order to understand that effect. Ramtron sold some of its product directly to customers, but the majority was sold to distributors who in turn sold the products to the end users.[30] Ramtron also recognized revenue on a point-of-purchase basis instead of a point-of-sale basis. Under the point-of-purchase system, revenue is recognized when the product is shipped to a distributor. By contrast, under the point-of-sale method, revenue is only recognized when the product is sold to the end user, whether directly by the Company or indirectly by the distributor.[31]

***4** Theoretically, the two systems *should* arrive at the same results. Unless the distributors are buying exactly the same amount of inventory as they are selling during each financial reporting period, however, the systems will result in revenue being recognized at different times. To take a simplistic example, suppose a company sells 100% of its products through distributors and that the company develops a new product in the first quarter. The following chart provides an example of how the company would recognize revenue under the two different regimes assuming the company sold 100 units of the product to the distributors at $1 each over the course of a year:

Revenue Recognition Comparison

	Revenue Recognized			
Quarter	**Distributors**		***Point–of–Purchase Method***	***Point–of–Sale Method***
	Buy	**Sell**		
Q1	20	0	$20	$0
Q2	30	10	$30	$10

Q3	40	20	$40	$20
Q4	10	30	$10	$30

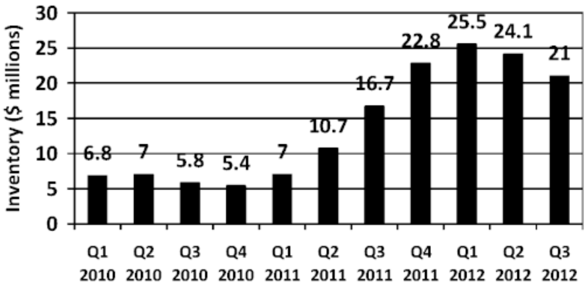
This comparison deliberately highlights an important dispute between the parties in this case: the point-of-purchase method makes it difficult to forecast actual demand because the distributors provide a buffer. Indeed, in this example, under the point-of-purchase method, demand appears to be falling, while under the point-of-sale method, it appears to be rising. Several of the witnesses testified that they believed Ramtron's point-of-purchase revenue system made it more difficult accurately to forecast future sales.[32] The revenue recognition system matters for two reasons. First, as already mentioned, distributor activity can mask actual demand. The difficult transition from Fujitsu to TI forced Ramtron to place its customers on allocation in or around 2011. Because Ramtron's F–RAM already was designed into many of their customers' products, those customers needed to ensure that they would have a sufficient supply of F–RAM. After they were placed on allocation, many customers apparently increased their orders accordingly.[33] For example, a customer that was allocated 80% of its ordered amount potentially would order five units for every four that it actually needed. This increase in orders led Ramtron to increase the number of wafers it was ordering from TI. The upshot of this chain of events was a massive inventory bubble, over-recognition of revenue, and a resulting cash crunch for Ramtron because it then had to pay for the extra inventory it ordered.[34] Because of its point-of-purchase revenue recognition, Ramtron recognized these additional distributor orders as revenue, even though the over-ordering was not reflective of “real” underlying demand, but instead, at least in part, was an effort of the customers to game the allocation system.

The second reason that Ramtron's point-of-purchase revenue recognition system is relevant is because it allows management to alter the Company's revenue by forcing more inventory into the distribution channels. This practice is known as “channel stuffing.” As discussed in more detail in Section III.A *infra,* I find that Ramtron's management did stuff the channel in the first quarter of 2012, thereby distorting the company's revenue.

The combination of over-orders from customers that were placed on allocation and Ramtron's stuffing of the channel led to a massive build-up of inventory. The chart below[35] shows the amount of inventory Ramtron had accumulated as of the time of the Merger. Because of its point-of-purchase accounting system, Ramtron already had recognized this inventory as revenue. As this chart shows, in the first quarter of 2012, Ramtron had 3.6 times as much inventory as a year earlier.

Ramtron Inventory

***5**



This inventory needed to be financed, which took a serious toll on Ramtron's cash position. Ramtron's primary lender was Silicon Valley Bank (“SVB”). Throughout 2011 and 2012, the years affected by the inventory bubble, Ramtron either missed or needed to renegotiate its loan covenants repeatedly. For example, the Company missed its April 2011 liquidity covenant and received a forbearance for May of that year.[36] A July 7, 2011 Form 8–K filing states that on June 30, 2011, Ramtron entered into a Default Waiver and Fifth Amendment to its loan agreement with SVB, an amendment that cost the Company $20,000.[37]

Around this time, Cypress began expressing an interest in Ramtron. On March 8, 2011, Cypress made a non-public written offer to Ramtron for $3.01 a share.[38] Ramtron rejected the offer as inadequate later that month. The offer represented a 37% premium over the March 8 closing price of Ramtron's stock.[39] Rodgers described the offer as including “a high market premium to say we were serious and not to try to squeeze on them.”[40]

After rebuffing Cypress and renegotiating its bank covenants, Ramtron still needed capital. SVB apparently had shifted to lending to Ramtron on an asset-backed basis, meaning that its loans were collateralized by the Company's receivables instead of being unsecured. Ramtron considered borrowing from other lenders, but concluded that the cost was too high.[41] So, in July 2011, Ramtron launched a secondary public offering of 4,750,000 shares, which was roughly 20% of its outstanding shares.[42] The secondary offering occurred at $2 per share, with a net to Ramtron of $1.79 after underwriting commissions and other charges.[43] The Company used the proceeds of this equity raise largely for working capital to pay off its excess inventory.[44]

As the above chart shows, Ramtron's inventory continued to increase throughout 2011. Despite the recent equity raise, Ramtron soon fell short on cash again. At least one internal Company email from January 2012 suggests that the first quarter covenants would be tight.[45] And, by spring 2012, the Company was in a cash crunch of sorts. Richards emailed Davenport on March 3, 2012, that "we are basically running on fumes in regards to cash management and related bank covenants, which we just announced new ones yesterday."[46] These cash management problems continued after Cypress announced its hostile bid for Ramtron on June 12, 2012. Shortly after the merger agreement was signed, Richards provided Brad Buss, Cypress' then-CFO, with cash forecasts that showed the Company would go cash negative on October 26, 2012.[47] In response, Cypress promptly began funding Ramtron.[48]

***6** Overall, the evidence shows that Ramtron continually had difficulty meeting its bank covenants, but that SVB seemed willing to renegotiate those covenants. There is no evidence that SVB ever sought to call its loans or that the Company actually faced a serious risk of foreclosure. Richards concisely summed up Ramtron's relationship with SVB as "rocky in regards to the covenants" but that he "had a good relationship with the bankers."[49] From the evidence of record, therefore, I conclude that the Company was cash-strapped and struggling from a liquidity standpoint at the time of the Merger, but that Ramtron was not, as Cypress suggests, a bankruptcy waiting to happen.

C. The Merger

On June 12, 2012, Ramtron issued a public letter declaring its intent to acquire Ramtron for $2.48 a share.[50] Interestingly, the $2.48 offer reflected the same 37% premium to market as Cypress' March 2011 offer; the decrease in price corresponded to the fall in Ramtron's stock price.[51] Ramtron rejected that offer as inadequate in a June 18 press release and announced that it had begun exploring strategic alternatives.[52]

Only two days after Cypress announced its public bid, Balzer, Ramtron's CEO, ordered the creation of new long-term management projections (the "Management Projections"). While, as discussed *infra,* the parties vigorously dispute the accuracy of Ramtron's prior forecasts, there seems to be no dispute that the Company's management had not previously created multi-year forecasts and instead generally only created five-quarter forecasts.[53] Balzer oversaw the team in charge of creating the new management projections, which consisted of Richards, Brian Yates, who worked for Richards, Zimmer, and Emley.[54]

A June 14, 2010 email chain among those five individuals shows a team undertaking a new and unfamiliar project. As if emphasizing that the projections were not being prepared in the ordinary course of Ramtron's business, Balzer wrote that he wanted a "product by product build up, with assumptions, for it to hold water in the event of a subsequent dispute."[55] Indeed, Richards testified that he understood the purpose of the projections to be twofold: marketing the company to a white knight and creating inputs for a DCF analysis.[56] The Ramtron management team had never done long-term projections before.[57] Zimmer, the head of sales, wrote that not even the automotive industry, which he apparently considered more predictable than the semiconductor industry, "can do a line item 4 year forecast."[58] He also suggested that for "[o]ut years I would simply plug in 30% CAGR,"[59] a comment that reinforces the inference that these projections were not produced in the ordinary course of business based on reliable data. Additionally, Balzer wanted the projections done using a point-of-sale approach, as opposed to Ramtron's standard point-of-purchase methodology. Ramtron's management team had never done point-of-sale projections.[60] I describe the resulting projections in significantly more detail in Section III.A *infra.*

***7** Meanwhile, Cypress' hostile offer continued. On June 21, 2012, Cypress commenced a hostile tender offer for Ramtron at $2.68 per share.[61] Ramtron's Board rejected the $2.68 price as inadequate and not in the best interests of the Company's stockholders. Accordingly, the Board recommended that the stockholders not tender their shares.[62] Shortly thereafter, Ramtron issued its second quarter 2012 earnings, which were significantly below expectations. In the first quarter of 2012, Ramtron had reported $15 million in revenue and reaffirmed its public guidance for entire-year 2012 revenue of "approximately $70 million."[63] On July 24, 2012, Ramtron reported $14.2 million in revenue for the second quarter and projected revenue of $14 to $14.5 million for the third quarter.[64] These results and projections placed the Company on track to undershoot its full-year 2012 estimate by at least $10 million. On July 26, 2012, shortly after Ramtron's announcement, Merriman Capital, the only analyst covering Ramtron, downgraded the Company from "buy" to "neutral."[65] Merriman also suspended its target price and observed that "were Cypress to pull its offer for Ramtron, these shares might very well return to the $2.00 range or perhaps lower."[66]

The witnesses at trial agreed that Ramtron's second quarter performance was disappointing.[67] The parties, however, vigorously dispute the reasons for that. Petitioner assigns basically all of the blame for the poor second quarter to Cypress and denies that it resulted from any inherent weakness in Ramtron. According to Petitioner, the distributors pulled back their orders dramatically in light of Cypress' hostile bid, because they feared being terminated after the merger. For this proposition, LongPath relies mostly on Balzer's deposition testimony.[68] Respondent argues that Ramtron's second quarter results reflected Ramtron's own operational failures.

It is conceivable that Cypress' offer may have had some negative effect on second quarter sales, but the weight of the evidence shows that operational shortcomings of Ramtron were the primary cause of the decline in sales. Ramtron appears to run on a calendar fiscal year. As such, less than three weeks remained in June (and the second quarter) when Cypress issued its bear hug letter on June 12 and at most ten days remained after Cypress initiated its hostile tender offer. The most probable explanation for the poor second quarter is that Ramtron's management had stuffed the Company's distribution channel with inventory in the first quarter of 2012, and that caused the Company's distributors to order less product in quarter two. I discuss channel stuffing in Section III. A *infra.* Here, it suffices to note that, as of the first quarter of 2012, Ramtron had $25.5 million in inventory, a 264% increase over the previous year. Even assuming Ramtron's optimistic 2012 projection of $70 million in revenue, Ramtron had roughly nineteen weeks worth of inventory, for which it already had recognized revenue, at the beginning of the second quarter of 2012.[69] A fiscal quarter contains only thirteen weeks.

Other factors support the conclusion that Cypress' hostile bid did not drive Ramtron's poor second quarter performance. First, Davenport disagreed with the allegation that the distributors were pulling back because of Cypress. Davenport viewed Zimmer's comments to that effect as excuses for not hitting his sales targets.[70] Considering that Balzer admittedly based his assertion that the distributors were withholding orders on out-of-court statements made by Zimmer, who did not testify at trial, I accord it little weight. Second, it appears from the record that a significant number of Ramtron's products are "designed into" the final products, meaning that the end users would need the semiconductors to complete their own products and thus would have relatively stable, long-term demand. This makes it unlikely that demand dipped sharply at the end of Q2 because of Cypress' bid.[71] For all of these reasons, I find that, although Cypress' bid may have contributed slightly to Ramtron's poor performance in the second quarter of 2012, the main cause of that performance was Ramtron's own business reality.

***8** Notwithstanding the poor second quarter, Cypress increased its offer price to $2.88 per share on August 27, 2012, and extended the term of the tender offer.[72] On September 10, 2012, Ramtron's Board again concluded that the offer was inadequate and recommended that the stockholders not tender their shares.[73] During the time Cypress was pursuing its hostile tender offer, Ramtron actively canvassed the market looking for other buyers. In fact, Ramtron contacted over twenty potential suitors, a process I discuss in more detail in Section III.C *infra.* None of those other companies, however, ever made a firm offer, even though the most serious of them had access to Ramtron's internal management projections.

Beginning on September 12, 2012, representatives of Cypress and Ramtron engaged in active negotiations. Cypress increased its offer to $3.01 per share on September 16 and then again to $3.08 on September 17. Later that same day, Ramtron and Cypress agreed on the final transaction price of $3.10 per share.[74] The parties signed the merger agreement on September 18,[75] and the Merger was approved by a stockholder vote on November 20, 2012.[76]

D. Procedural History

LongPath filed this appraisal action on December 11, 2012. After the parties engaged in discovery, the Court presided over a three-day trial from October 7 to 9, 2014. Eight witnesses testified, including the parties' experts. After extensive post-trial briefing, I heard final argument on March 3, 2015.

I also note, for completeness, that a stockholder class action challenging the Merger was filed on October 15, 2012. Those plaintiffs moved to preliminarily enjoin the Merger, but that motion was denied. Thereafter, the defendants in the class action moved to dismiss. On June 30, 2014, I issued a memorandum opinion granting those motions and dismissing the stockholder class action with prejudice.[77]

E. Parties' Contentions

Both parties base their positions on expert testimony. Petitioner called David Clarke as its expert; Respondent relied upon Gregg Jarrell. Not surprisingly, the experts arrived at widely disparate conclusions. Clarke contends that the fair value of Ramtron's stock as of the Merger was $4.96 a share. Jarrell opines that the stock was worth only $2.76. Petitioner's fair value of $4.96 a share is more than 274% of Ramtron's unaffected stock price of $1.81.

Clarke bases his conclusion of $4.96 per share on a combination of a DCF analysis and a comparable transactions analysis, which he weighted at 80% and 20%, respectively. Clarke relied on Ramtron's management projections and a three-stage DCF analysis to arrive at a value of $5.20 per share. He based his comparable transactions analysis on a dataset consisting of only two transactions and obtained a fair value of $3.99 per share. Because Clarke found no comparable companies, he did not rely on that valuation method.

Jarrell rather unusually began his analysis with two premises: (1) that the Merger price was the result of a fair and competitive auction; and (2) that the management projections were overly optimistic. Based on these predicates, Jarrell opted to examine the transaction price and back out any synergies in order to determine fair value. This approach resulted in a fair value of $2.76 per share. In addition, Jarrell conducted a DCF analysis, in which he relied upon the management projections he earlier concluded were overly optimistic. Based on that analysis, Jarrell opined, apparently in the alternative, that the fair value of the Company's shares was $3.08 each, a number coincidentally only two pennies from the Merger price. As a result of his analysis, Jarrell also concluded that there were no comparable companies or comparable transactions.

***9** Much has been said of litigation-driven valuations, none of it favorable.[78] Here, the parties have proffered widely disparate valuation numbers which differ, at the extremes, by $2.44 as compared to an unaffected stock price of $1.81 and a deal price of $3.10. LongPath asks this Court to adopt its $4.96 figure and conclude that the market left an amount on the table exceeding Ramtron's unaffected market capitalization. This would be a significant market failure, especially in the context of a well-publicized hostile bid and a target actively seeking a white knight. But, LongPath itself is a market participant. It bought its shares *after* the announcement of the Merger, thereby effectively purchasing an appraisal lawsuit. Although such arbitrage can be profitable on the merits when flawed deals undervalue companies, LongPath invested an amount so small that, even if I accepted its position and concluded that Ramtron's true value at the time of the Merger was somewhere in the range of $4.96 per share, this lawsuit is likely a less-than-break-even proposition for LongPath after considering its litigation expenses. Respondent, on the other hand, has submitted an eyebrow-raising DCF that, based on projections its expert *presumed* were overly optimistic, still returns a “fair” value two cents *below* the Merger price.

II. STANDARD OF REVIEW

In a statutory appraisal action brought pursuant to 8 *Del. C.* § 262, the Court is tasked with “determin[ing] the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value.”[79] The Delaware Supreme Court has held that “fair value” is “the value to a stockholder of the firm as a going concern, as opposed to the firm's value in the context of an acquisition or other transaction."[80] "Accordingly, the corporation must be valued as a going concern based upon the 'operative reality' of the company as of the time of the merger."[81] Section 262 directs that, in making this determination, "the Court shall take into account all relevant factors."[82] Our case law has made clear that "[a]ny 'techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court' may be used."[83]

As is well-known, the Delaware appraisal statute places the burden of proof on both parties.[84] "If neither party satisfies its burden, however, the court must then use its own independent business judgment to determine fair value."[85]

III. ANALYSIS

A survey of the case law reveals that there are four main, or at least recurring, valuation techniques generally presented in an appraisal action: a discounted cash flow or DCF analysis, a comparable companies approach, a comparable transactions approach, and an examination of the merger price itself, less synergies. Like all tools, each has its own strengths and weaknesses. The parties agree that there are no comparable companies. Jarrell and Clarke disagree about whether there are comparable transactions, but the universe of potential comparables, even according to Clarke, is limited to two. Both sides conducted a DCF analysis, but disagree about certain issues in addition to the reliability of the Management Projections, such as the proper size premium, the appropriate method of modeling future capital expenditures, and whether a two-step or three-step DCF is more appropriate, as well as several more minor issues. The parties strongly disagree about the appropriate weight, if any, to give the Merger price, which Respondent weighs at 100%. Petitioner places the most weight on its DCF analysis. Accordingly, I begin there and then address the utility of a comparable transactions approach before turning to the transaction price.

A. A Discounted Cash Flow Analysis Is Inappropriate Because the Management Projections Are Unreliable

***10** A discounted cash flow analysis "involves projecting operating cash flows for a determined period, setting a terminal value at the end of the projected period, and then discounting those values at a set rate to determine the net present value of a company's shares."[86] "Typically, Delaware courts tend to favor a DCF model over other available methodologies in an appraisal proceeding. However, that metric has much less utility in cases where the transaction giving rise to appraisal was an arm's-length merger, [or] where the data inputs used in the model are not reliable...."[87] The foundational inputs of a DCF are the company's cash flows.[88] In determining those inputs, this Court has placed substantial weight on the projections of the incumbent management. Indeed, "this Court prefers valuations based on management projections available as of the date of the merger and holds a healthy skepticism for post-merger adjustments to management projections or the creation of new projections entirely."[89]

The reason that "Delaware law clearly prefers valuations based on contemporaneously prepared management projections" is "because management ordinarily has the best first-hand knowledge of a company's operations."[90] These projections are useful in appraisals, because they "by definition, are not tainted by post-merger hindsight and are usually created by an impartial body.... When management projections are made in the ordinary course of business, they are generally deemed reliable."[91] By corollary, projections prepared outside of the ordinary course do not enjoy the same deference. In fact, management projections can be, and have been, rejected entirely when they lack sufficient indicia of reliability, such as when they were prepared: (1) outside of the ordinary course of business; (2) by a management team that never before had created long-term projections; (3) by a management team with a motive to alter the projections, such as to protect their jobs; and (4) when the possibility of litigation, including an appraisal action, was likely and probably affected the neutrality of the projections.[92] These factors go to the reliability of the projections. In this case, the Ramtron management projections suffer from all of these problems.

1. A new Ramtron management team prepared projections not in the ordinary course using a methodology they never had employed before

***11** The team in charge of creating the new Management Projections consisted of Richards and one of his employees, Zimmer, and Emley, with oversight by Balzer.[93] According to Richards, the projections started with the numbers provided by the sales department, because most of the Company's costs either were fixed or a percentage of revenue, so the revenue numbers were the most important inputs.[94] Zimmer and Emley were the lead individuals responsible for developing the sales (and, hence, revenue) numbers. Both had been with the Company at most a year when they began creating the new projections.[95]

Aside from having relatively new employees tasked with creating the inputs, the team that developed the Management Projections utilized: (1) a new product-by-product build-up method; (2) a point-of-sale instead of the usual point-of-purchase methodology; and (3) a multi-year projection period.[96] The Ramtron management team previously had not created projections using any of these methods, much less all three.

Additionally, the projections were not prepared in the ordinary course of business. There is no evidence Ramtron ever had prepared forecasts for more than five quarters, with the exception of Richards's deferred tax asset projections.[97] Balzer ordered the projections created immediately *after* Cypress issued its bear hug letter. Thus, these projections were prepared in anticipation of potential litigation, or, at least, a hostile takeover bid. Balzer explicitly wrote that he wanted a "product by product build up, with assumptions, for it to hold water in the event of a subsequent dispute."[98] Furthermore, at least Richards understood one of the purposes of the projections was to serve as a marketing tool in Needham's hunt for a white knight.[99] This knowledge gave the management team an incentive to err on the optimistic side.

In sum, Ramtron's new management team employed a new methodology to create long-term projections, which they were not accustomed to doing, out of the ordinary course of business, with knowledge that the projections could or would be used: (1) in a subsequent dispute; (2) in marketing the Company; (3) as the inputs for Needham's DCF analysis;[100] or (4) any combination of those three possibilities. These projections, therefore, facially lack the indicia of reliability that generally have led Delaware courts to defer to management projections. I now turn to more specific problems with the Management Projections that reinforce the conclusion that the Projections are unreliable.

2. Management's forecasting capabilities

The parties vigorously dispute Ramtron management's forecasting accuracy. One dispute, for example, involves Respondent's contention that Ramtron often missed its publicly issued guidance for annual revenue going back to 2007, four years before Zimmer and Emley even joined the Company. This line of attack is something of a red herring. The proper focus should be on the forecasting accuracy of the management team *that actually made the projections.* Whether other, prior executives had or lacked the gift of seeing into the Company's future and predicting the success of its business is less relevant and barely probative of the forecasting capabilities of the pre-Merger management team. Accordingly, I would assign little weight to Ramtron's alleged historic forecasting prowess, even assuming it was proven.

The record is surprisingly unclear on exactly what projections were made by the then-current Ramtron management team, aside from the occasional public guidance.[101] The parties' main disagreement over management's forecasting abilities concerns a waterfall chart. The chart shows forecasts by quarter. Respondent contends that the chart represents management's ongoing internal forecasts. Petitioner argues that it depicts nothing but "stretch goals." The answer is somewhat important. If the waterfall chart in fact represents actual forecasts, then Ramtron's ability to forecast its own business more than two quarters out was quite poor. On the other hand, if the chart merely reflects stretch goals, then it loses much of its impact. The weight of the evidence convinces me that the waterfall chart represented actual forecasts, but I still accord that chart only moderate weight in my evaluation of the Management Projections. Before explaining why, I have included below a portion of the waterfall chart.[102]

***12** Date	Qtr	Q1 2011	Q2 2011	Q3 2011	Q4 201
Apr. 2010	Q2 2010	$21,000			
July 2010	Q3 2010	$21,000	$23,000		

Oct. 2010	Q4 2010	$21,000	$23,000	$24,000	
Dec. 2010	Q1 2011	$21,000	$22,000	$24,000	$25,0
Jan. 2011	Q1 2011	$10,000 **$10,440**	$15,000	$20,000	$22,0
Apr. 2011	Q2 2011		$15,000 **$16,537**	$20,000	$22,0
July 2011	Q3 2011			$21,500 **$21,736**	$22,5
Oct. 2011	Q4 2011				$22,300 **$1**
Feb. 2012	Q1 2012				

Respondent's argument is straightforward: the waterfall chart appears in a presentation to the Board,[103] and there is no indication that the numbers are anything other than ordinary-course forecasts. LongPath relies on a pair of "Sales Update" presentations that refer to the numbers in the waterfall chart as "stretch goals."[104] Respondent advances the theory (and urges the Court to infer) that Zimmer, as the Vice President of Sales, referred to the forecasts as stretch goals because, as the head of sales, he primarily was responsible for failing to meet revenue targets. At trial, Ramtron's Vice President of Technology, Davenport, similarly suggested that Zimmer blamed Ramtron's poor second quarter on Cypress as an excuse to cover up his own poor performance.[105]

More practical reasons lead me to the conclusion that the waterfall chart likely represented management's actual forecasts. First, contemporaneous emails suggest that the management team saw these numbers as goals they *should* hit. In a late January 2012 email chain, Balzer writes to Zimmer, Richards, and Yates that the Company "really need[s] to find a way to hit $14.5. That is what we said we would do."[106] The first quarter 2012 forecast for that quarter was $14 million, as the chart above shows. Second, the very idea of "stretch" or "reach" goals requires targets that are, as the names imply, actually within reach.[107] Many of these forecasts were wildly incorrect. In December 2010, for example, the Company forecasted $21 million for the first quarter of 2011 (the very next quarter), a quarter in which actual revenue was $10.4 million, less than half of the forecast. Relatedly, as the actual quarter drew closer, management generally reduced its forecasts to better approximate the actual revenue. As the quote from Balzer suggests, the management team treated these numbers as real targets, not lofty stretch goals.[108] Third, if these are not actual forecasts, then the record lacks evidence of regularly created and updated management forecasts, *i.e.,* if the waterfall chart only contains stretch goals, then management's publicly issued guidance would be the only basis for assessing its forecasting.

***13** I find it most likely that management began with high aspirations for future quarters and reduced those expectations toward the actual expected results as the quarter drew nearer. This suggests that management's near-term forecasting abilities were mediocre at best. Even so, the waterfall forecasts and the public guidance forecasts were done with a different methodology than the Management Projections. Accordingly, I conclude that management, even under its traditional forecasting system, was of middling quality when it came to forecasting Ramtron's future business. Several witnesses at trial testified that, in general, the semiconductor business is difficult to forecast.[109] Indeed, after Ramtron issued its weak second quarter 2012 earnings, Merriman Capital issued a report that suspended its target price for the Company and stated: "We simply can't figure out how to model this company consistently at the current time."[110] Ramtron's management also recognized its own limited success in forecasting.[111] In sum, management's lack of success in accurately projecting future revenue in the past provides another reason to doubt the reliability of the Management Projections.

3. The projections incorporate unrealistic assumptions regarding ROHM

I also note that the Management Projections assume cost reductions, over time, associated with the transition to ROHM's foundry. The projections reflect an assumption that production of F–RAM at ROHM would to begin in January 2013 at 150,000 units a month and increase by 50,000 units per month thereafter.[112] These assumptions are too speculative to merit any deference.[113]

Ramtron entered into a manufacturing agreement with ROHM in late July 2012 pursuant to which ROHM would serve as a second foundry for Ramtron.[114] According to a July 23, 2012 press release, "Initial low-density F–RAM products have already been qualified for commercial production and Ramtron expects to receive and begin selling the first devices produced on ROHM's manufacturing line within approximately 60 days."[115] As already described, it took Ramtron *seven years* to transition entirely from Fujitsu to TI. That process went so poorly that it forced Ramtron to place its customers on allocation in 2011. Ramtron's earlier efforts to develop IBM as a second foundry took place over *three years* and caused it to incur more than $30 million in direct costs and equipment expenses. That endeavor failed entirely. Additionally, the evidence shows that, in July 2012, Ramtron was not flush with cash. The IBM venture suggests that establishing a new foundry requires a substantial monetary investment, and Ramtron's liquidity situation in the summer of 2012 makes it doubtful that Ramtron would have been able to finance the continued development of ROHM as a foundry.[116] In light of this evidence, as well as the uniform testimony on the difficulty of transitioning foundries, I do not find credible the proposition that Ramtron reasonably could expect to begin commercial production at ROHM in sixty days and start enjoying cost savings within six months.[117]

***14** Additionally, evidence presented at trial buttresses this conclusion. Consistent with the other testimony on the lead time for getting a product from concept to full-fledged commercial sale,[118] Davenport testified the term "initial low-density F–RAM products" referred to sample quantities that Ramtron was "going to take over ROHM's design and try to commercialize them as samples. They weren't cost-effective but they would seed the market."[119] In fact, Ramtron never got further than this initial sample stage. Davenport further testified that Ramtron "never got so far as transfer[ing] our designs to the ROHM foundry" before the Merger closed.[120] It also appears that ROHM technologically lagged behind both TI and IBM as a foundry.[121] I do not question the strategic judgment of Ramtron's management in seeking to implement the Company's manufacturing agreement with ROHM, but the record as a whole leads me to find that the ROHM assumptions built into the Management Projections were speculative and further undermine the reliability of those projections.

4. The Management Projections rely on 2011 and 2012 revenue figures that were distorted because of customer allocation issues and channel stuffing

As discussed in the next Subsection, the Management Projections for revenue assume a constant growth rate of 24% for 2014, 2015, and 2016.[122] This is an arbitrary method of predicting revenue growth if not supported by reasonable assumptions. Such simple modeling makes the reliability of the base year numbers crucially important—*i.e.,* if a set of projections assumes constant growth from a starting number, the inaccuracy of that foundational input affects the reliability of the entire enterprise. Substantial evidence in the record supports the conclusion that Ramtron's revenue in 2011, the last full year before Cypress' offer, is an unreliable figure.

In Section I.B.2 *supra,* I discussed the massive inventory build-up that Ramtron experienced beginning in 2011. During no quarter in 2010 did Ramtron have more than $7 million in inventory. Over the course of 2011, however, Ramtron shipped a huge amount of inventory into its distribution channels until, in the first quarter of 2012, Ramtron had $25.5 million in inventory. Even under favorable assumptions for Ramtron, that amounts to about nineteen weeks of inventory in the channel and it consists of product for which Ramtron already had recognized revenue.[123] In describing Ramtron's background, I found that this inventory build-up resulted at least in part from the supply shortages the Company faced as a result of its foundry transition. Those shortages forced the Company to place customers on allocation; the customers responded by over ordering. Because Ramtron recognized revenue when it shipped to distributors, it is reasonable to infer that an unknown, but not insignificant amount of Ramtron's revenue in 2011 actually reflected this over-ordering by customers, as opposed to a genuine surge in demand. In addition, because of the backlog of inventory that existed in the first quarter of 2012, it is logical that less revenue would be recognized later in 2012 as the inventory bubble was burned off, unless there was a significant uptick in demand.

***15** Ramtron's management, however, expected to hit their reduced forecasts for the first quarter of 2012. Although I already have discussed the difficulties with the point-of-purchase revenue recognition system, there is another pitfall not yet discussed: channel stuffing. Channel stuffing is the practice of stuffing inventory into the channel in order to recognize the attendant revenue sooner, notwithstanding the fact that the revenue does not correspond to underlying increases in demand. Hence, it is a form of revenue manipulation.

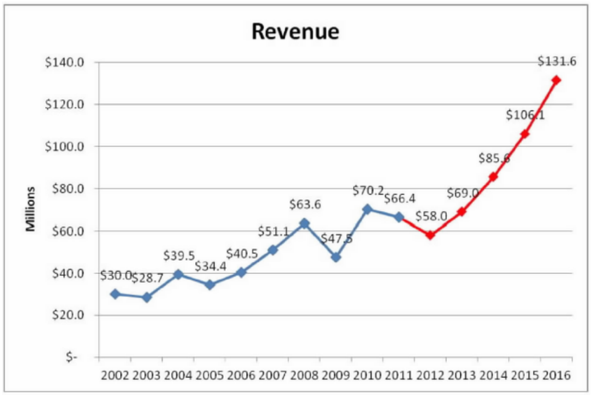
I find that Ramtron's management pushed excess inventory into the Company's distribution channels in the first quarter of 2012. In an already referenced email chain from late January 2012, Balzer remarked that the Company “really need[ed] to find a way to hit $14.5” million.[124] Zimmer responded: “I'll die trying. We'll for sure stuff channel. Next Qtr will suffer.”[125] There is no persuasive evidence that Balzer disagreed. Although Petitioner fights the channel-stuffing conclusion,[126] the combination of Zimmer's contemporaneous comments and the massive inventory buildup strongly support the conclusion that Ramtron stuffed the channel in order to make its first quarter revenue forecast.

All of this matters for two reasons. First, forcing excess inventory into the channel in early 2012 meant that there would be a corresponding fall off in revenue at some point in the future absent a demand spike.[127] As Zimmer predicted, the next quarter, Q2 2012, did suffer. Petitioner's efforts to attribute those disappointing results to Cypress' hostile offer, rather than weaknesses in Ramtron's own business practices, are unavailing.[128] Second, Ramtron's revenue figures for 2011 and the first half of 2012 do not accurately map to actual demand for the Company's products. LongPath argues that the quantification of the point-of-purchase versus point-of-sale issue reveals that, at most, Ramtron over-recognized 3.7% of its total revenue from 2010 through 2012.[129] Assuming Petitioner's math is correct, that is an over-recognition, in three years, of $6.6 million for a company that only once in its history had had more than $70 million in revenue in a single year.

The problem, however, goes beyond just the amount of improperly recognized revenue. The timing of the revenue also is affected significantly. If 2011 and 2012 are used as base years in forecasting, but those years include inflated revenue because of either over-ordering by customers placed on allocation or channel stuffing, then the reliability of the projections is affected. Thus, customer allocation issues in 2011 and channel stuffing in the first quarter of 2012 throw significant doubt on the accuracy of the underlying revenue figures for those periods. In that regard, I do not consider it productive (even assuming it is feasible) to attempt to quantify how much in extra revenue Ramtron recognized in 2011 or 2012 based on these factors.[130]

5. The projections defy historical trends

***16** Historical performance does not control a company's future performance. It is, however, a red flag when projections suggest a dramatic turnaround in a company despite no underlying changes that would justify such an improvement of business. This is the classic “hockey stick” problem. The Management Projections, prepared days after Cypress made its bid and with knowledge that Needham would use the Projections to market the Company, fall into this category. Both revenue growth and gross margins are shown as undergoing dramatic improvements. The following chart shows Ramtron's historical revenue (for the ten years before the projection period) versus its projected revenue.[131] As the graphs make clear, the projection period suggests a period of previously unknown prosperity for Ramtron. Not only is the Company's historically volatile growth rate transformed into a consistently high growth rate, but the downward trend in revenue is replaced by a sharp, unprecedented increase in absolute revenue.[132] This sharp uptick in revenue is in contrast to the fact that, at least dating back to 1994, the Company never has experienced four consecutive years of growth.



Presented in another perspective, the following chart shows the Company's compound annual growth rate (“CAGR”) over various periods.[133] Only under the arbitrary 2005–2008 timeframe, which appears to be the Company's best-ever growth period, does historic growth approach projected growth. When comparing the five or ten years preceding the projections period, it is clear that the Management Projections forecast incredible growth. Indeed, the five-year projection period implies a CAGR of 22.73%, which is roughly 3.36 times higher than the CAGR for the five years immediately preceding the projection period (2007–2011) and approximately 2.46 times greater than the ten-year period (2002–2011) before the management forecasts.

Time Period	Years	CAGR
2002-2006	5	7.79%
2005-2008	4	22.73%
2007-2011	5	6.77%
2009-2011	3	18.23%
2002-2011	10	9.23%
2012-2016	5	22.73%

Petitioner attempts to justify the Management Projections as reasonable by comparing the projections to a set of internal Cypress projections. In what was called the President's Strategic Plan (the “PSP”), Cypress forecasted the potential F–RAM market in terms of total available market, service available market (which was Cypress' term for a product's core market) and predicted share of the market.[134] Petitioner argues that, if Ramtron simply maintained the market share of the core F–RAM market that it had at the time of the Merger, then the Management Projections would be accurate. There are numerous problems with this argument: (1) Ramtron's management did not have the PSP when they were creating the Management Projections, so this thesis is an entirely post hoc justification for the Projections; (2) for the Management Projections to be accurate, Ramtron would have had to increase its market share significantly, not just maintain it; (3) to the extent that Cypress' predictions are relevant, the Management Projections would require Ramtron to capture a substantially larger portion of the market than Cypress predicted it would; and (4) perhaps most damaging to Petitioner's theory, Cypress predicted that Ramtron, operating as an improved division of Cypress, would lose market share.

***17** The chart below compares Cypress' predictions for Ramtron, as a division of Cypress, against the Ramtron Management Projections. Dollar values are in millions.

	2013	***2014***	***2015***	***2016***
Core Market	$187	$218	$254	$288
Ramtron Share of Market, as Cypress Division	$41	$55	$61	$67
Cypress F-RAM Market Share (forecast by Cypress)	22%	25%	24%	23%
Ramtron Management Projections	$69	$85.6	$106.1	$131.6
Ramtron F-RAM Market Share (Petitioner's argument)	37%	39%	42%	46%
Market Share Gap	**15%**	**14%**	**18%**	**23%**

(Management Projections— Cypress Predictions)

Petitioner's argument is unpersuasive. The PSP forecasts Ramtron as a division of Cypress—*i.e.,* after a possible merger. That alone makes the comparison of market share unavailing. More importantly, Cypress predicted a moderate, but falling market share for Ramtron or, at best, that Ramtron would maintain its market share.[135] The Management Projections predict an entirely different trend under which Ramtron's market share would increase by nearly 25%, *i.e.,* Ramtron would capture another nine percent of the core F–RAM market. By the year 2016, for the Management Projections to be accurate, Ramtron would need to hold *twice* as much of the core market as Cypress predicted it would. Considering all the evidence of record regarding projections, I find it unlikely that Cypress substantially would underestimate the potential of the very company it was about to purchase. Thus, Petitioner's attempts to show the "reasonableness" of the Management Projections by comparing them to the Cypress PSP are unconvincing. Rather, the Projections defy historical trends.

6. Management utilized other projections for ordinary business purposes

The fact which I find to be the final nail in the coffin for the Management Projections is that Ramtron did not rely on them in the ordinary course of its business. Although Balzer suggested that the Management Projections were used for other purposes, such as cash management,[136] the significance of those alleged uses is dubious. Richards, the CFO, credibly testified that he used other sets of projections for managing the Company's finances, such as providing estimated revenue and cash flow numbers to SVB, the Company's bank.

The final version of the Management Projections utilized by Needham in preparing its fairness opinion is from September 18, 2012.[137] The Needham presentation listed $58.2 million for estimated 2012 revenue, a slight discrepancy from the native excel spreadsheet of the Projections, dated August 28, 2012, which listed $58 million for 2012.[138] On July 17, 2012, however, Richards sent an email to SVB projecting $56.5 million for 2012 (the "July SVB Projections").[139] On September 10, 2012, Richards sent another update to SVB that reduced that projection to slightly less than $54 million (the "September SVB Projections").[140] Both the July and September SVB Projections pre-date the Needham presentation. The September SVB Projections are nearly 6.9% lower than the Management Projections. If the revenue growth assumptions from the Management Projections were applied to the September SVB Projections, the Management Projections would overstate five-year revenue by $31 million, even ignoring all of the other problems with the Management Projections I have discussed. Richards testified that he believed that the September SVB Projections "were more accurate" and that he provided those projections to SVB because it was the Company's "sole source of borrowing" and he wanted to keep the bank "apprised of the situation."[141]

7. There are insufficient reliable inputs to produce a reliable DCF analysis

***18** In summary, the Management Projections suffer from numerous flaws. Specifically, they: (1) were prepared by a new management team, (2) in anticipation of future disputes and of shopping the Company to potential white knights, (3) using a new methodology, and (4) were for a significantly longer period of time than previous forecasts. In addition, I note the following problems: (5) management's track record at forecasting was questionable even under their standard method of forecasting; (6) the final projections incorporate speculative elements relating to ROHM, (7) rely on distorted base year figures that resulted from customer allocation issues and channel stuffing, and (8) predict growth out of line with historical trends; and, finally, (9) management itself was providing other, "more accurate" projections to the Company's bank. None of the indicia that often justify deferring to management projections are present in this case. Thus, Petitioner has not proven that the Management Projections are reliable, and I conclude that they are too questionable to form the basis of a reliable DCF valuation.[142]

"[W]ithout reliable five-year projections, any values generated by a DCF analysis are meaningless."[143] Having found that the Management Projections are unreliable and there are no other viable projections in the record,[144] I therefore conclude that it would be inappropriate to determine fair value based on a DCF analysis in this instance.

B. The Comparable Transactions Method Does Not Produce a Reliable Value

The parties' experts agree that there are no comparable companies to Ramtron.[145] Using another approach, Clarke, petitioner's expert, opined that there were two comparable transactions from which Ramtron's value could be derived.[146] This analysis resulted in an implied value for Ramtron of $3.99 per share, and Clarke accorded it a 20% weight in his ultimate fair value determination.[147] Jarrell concluded that there were no comparable transactions.[148] For the following reasons, I conclude that Petitioner has not proven that the comparable transactions method is an appropriate valuation technique in this case.

A comparable transactions approach requires "identifying similar transactions, quantifying those transactions through financial metrics, and then applying the metrics to the company at issue to ascertain a value. The utility of a comparable transactions methodology is directly linked to the 'similarity between the company the court is valuing and the companies used for comparison.' "[149] "Reliance on a comparable companies or comparable transactions approach is improper where the purported 'comparables' involve significantly different products or services than the company whose appraisal is at issue, or vastly different multiples."[150]

***19** The purportedly comparable transactions are the acquisitions of Actel Corporation ("Actel") and Virage Logic Corporation ("Virage"), both of which Clarke concluded were companies that produced memory products but, like Ramtron, operated without their own foundry.[151] Clarke computed multiples for the two firms based on the transactions involving them for the following financial metrics: (1) equity value ("EV")/last twelve months' revenue ("LTM"); (2) EV/next twelve months' forecasted revenue ("NTM"); and (3) EV/NTM + 1.[152] Clarke then averaged the Virage and Actel multiples and derived an implied value for Ramtron from them.

Jarrell contests Clarke's choice of comparable transactions. He notes that the proxy statement in the Virage transaction included a list of comparable companies from two industries similar to Virage's and that Ramtron was not listed in either group.[153] It is unclear whether Jarrell believes that Actel is not comparable in and of itself, but he did observe that the multiples for that company support the Merger price as evidence of fair value. More importantly, Jarrell opines that the dispersion of the multiples for Actel and Virage is too great to be reliable and violates the "law of one price."[154] I agree with this criticism.

In the past, "[t]his Court has found comparable transactions analyses that used as few as five transactions and two transactions to be unreliable."[155] This "dearth of data points ... undermines the reliability" of the methodology.[156] Here, there are only two data points and the multiples (shown below) differ significantly.[157]

Target Company		*EV/LTM*	*EV/NTM*	*EV/NTM + 1*
		Revenue	*Revenue*	*Revenue*
Virage		4.43x	2.80x	2.25x
Actel		2.05x	1.72x	1.65x
	Average	**3.24x**	**2.26x**	**1.95x**
Ramtron	Financials	$58.2M	$69.0M	$85.6M
	Implied[158] **Equity Value (Unadjusted for Synergies)**	**$181.1M**	**$148.4M**	**$159.7M**

Clarke then went on to: (1) subtract a 13% synergy discount from each of the implied equity values; and (2) average the three figures to arrive at a comparable-transactions-based equity value for Ramtron of $141.9 million.

Even assuming these two transactions qualitatively are comparable transactions, in that the acquired companies operated similar businesses to Ramtron, the meager number of data points and the range of multiples indicate that this valuation approach is of questionable reliability in this instance. The EV/LTM multiple, for example, yields synergy-adjusted per share values of $2.74 to $6.13, a range of $3.39, which exceeds the Merger price of $3.10.[159] The EV/NTM multiple suggests equity values of $2.72 to $4.55, a spread of $1.83.[160] By contrast, the EV/NTM+1 multiple produces a tighter range of $3.27 to $4.53.

***20** I see little justification for Clarke's simple averaging method, particularly with only two data points. His comparable transactions approach implies per share values ranging anywhere from $2.72 to $6.13. Two of the multiples have high-low ranges exceeding Ramtron's unaffected stock price. I am not convinced it is productive to utilize a method that implies Ramtron's fair value is somewhere between 88% and 198% of the deal price.[161] Also, the EV/NTM and EV/NTM+1 multiples rely on the Management Projections, which I already have concluded are unreliable. Finally, Clarke himself attributed minimal weight to this approach—only one-fifth of his conclusion. For all of these reasons, I conclude that Petitioner has not satisfied its burden of proving that the comparable transactions approach provides a reliable indication of Ramtron's fair value.

C. The Transaction Price Provides the Best Evidence of Fair Value

A DCF analysis attempts to value a company by looking within the company, extrapolating its financials into the future, and then discounting these cash flows to present value. A comparables approach instead looks outside the company and attempts to value it by market analogy. The former method is only useful to the extent its inputs are reliable; the latter is helpful only to the extent actual comparables exist. Neither approach yields a reliable measure of fair value in this case. Instead, I conclude that the Merger price offers the best indication of fair value.

A merger price does not necessarily represent the fair value of a company, as the term "fair value" is interpreted under 8 *Del. C.* § 262. For example, in a short-form merger under Section 253, the merger price is set unilaterally by the controlling stockholder; the minority stockholders are forced out of the company and left with appraisal as their sole remedy. To presume that the merger price represented fair value in such a situation would leave the minority stockholders effectively without the remedy offered by Section 262 of an independent analysis of a company's fair value. In 2010, the Delaware Supreme Court in *Golden Telecom, Inc. v. Global GT LP*[162] explicitly rejected the argument that this Court should "defer" to the merger price. Indeed, the Supreme Court concluded that such deference would be contrary to the statutory language of Section 262, which requires consideration of "all relevant factors" in determining a company's fair value.[163]

Nevertheless, in the situation of a proper transactional process likely to have resulted in an accurate valuation of an acquired corporation, this Court has looked to the merger price as evidence of fair value and, on occasion, given that metric one-hundred percent weight.[164] In an oft-quoted passage, then-Vice Chancellor Jacobs wrote: "The fact that a transaction price was forged in the crucible of objective market reality (as distinguished from the unavoidably subjective thought process of a valuation expert) is viewed as strong evidence that the price is fair."[165] Similarly, Chief Justice Strine, then writing as a Vice Chancellor, noted: "[O]ur case law recognizes that when there is an open opportunity to buy a company, the resulting market price is reliable evidence of fair value."[166] The inquiry here is whether the Merger process resulted in a price indicative of Ramtron's fair value or, as the parties have framed it, whether there was a "competitive and fair auction"[167] for Ramtron.

***21** At the outset, I note that I am not aware of any case holding that a multi-bidder auction of a company is a prerequisite to finding that the merger price is a reliable indicator of fair value. Here, unlike in *Union Illinois* or *Huff Fund,* only one company, Cypress, made a bid. This case also differs in that the Merger was a hostile deal. As detailed below, however, I conclude that "the process by which [the Company] was marketed to potential buyers was thorough, effective, and free from any spectre of self-interest or disloyalty,"[168] and that the resulting price accordingly provides a reliable indication of Ramtron's fair value.

Ramtron could, and repeatedly did, reject Cypress' overtures. Simultaneously, Ramtron actively solicited every buyer it believed could be interested in a transaction. The Company provided several of those potential buyers with the muchvaunted Management Projections. No one bid. LongPath contends that the lack of other bidders indicates a flawed process. I disagree. Any impediments to a higher bid resulted from Ramtron's operative reality, not shortcomings of the Merger process.

1. TI and Ramtron's operative reality

Much already has been said about Ramtron's operative reality as of the Merger. Petitioner focuses on one particular factor that it contends irredeemably corrupted the sales process: Ramtron's foundry relationship with TI. Under Ramtron's manufacturing agreement with TI, Ramtron was guaranteed three additional years of production if TI terminated the agreement.[169] But, in the event Ramtron experienced a change in control, TI had the right to terminate the agreement upon ninety days notice.[170] LongPath argues that this change-in-control provision deterred prospective bidders. I reject this contention as contrary to the evidence.

The parties do not dispute that Cypress began preparing for its hostile bid well in advance. Part of that diligence involved predicting potential interlopers. Another aspect of Cypress' preparation involved essentially seeking TI's blessing for its potential bid. Because of the change-in-control provisions, Cypress sought to get some form of assurance from TI in advance of issuing its bear hug letter that TI would not exercise that right in relation to an acquisition by Cypress. Rodgers testified that he called TI's president to discuss a potential acquisition of Ramtron. In that regard, Cypress offered to avoid competing with one of TI's F–RAM products if TI agreed not to terminate the foundry relationship with Ramtron. Cypress never received a contract or other written agreement from TI—in fact, it appears that TI never explicitly agreed to support Cypress' bid. Cypress did receive, however, enough of an informal assurance that it deemed the risk of proceeding with the acquisition acceptable.[171]

As Petitioner emphasizes, Rodgers began discussing this issue with TI in March 2011, over a year before Cypress' bid for Ramtron.[172] Even so, the record is clear that Cypress never obtained a contractual commitment from TI. In an undated internal Cypress presentation analyzing the potential bid for Ramtron, the possibility of TI dishonoring its commitment is listed as a low risk, but Cypress (twice) listed the lack of TI support as a major risk to any potential deal.[173]

***22** LongPath argues that Cypress had an unfair tactical advantage and that other bidders were unlikely to get TI's support. This appears to be nothing but speculation. Ramtron's relationship with TI was part of its operative reality. A Cypress planning document, titled "Potential Interlopers," listed five such plausible interlopers. For three of them, Cypress predicted that TI would not extend foundry support because those companies directly competed with TI.[174] A different document predicted the same as to a sixth possible interloper.[175]

I find these predictions and Petitioner's reliance upon them somewhat puzzling. Even though Cypress offered not to encroach on one specific TI product line, "low power microcontrollers,"[176] in order to get an informal assurance that the manufacturing agreement would continue, the uncontradicted evidence shows that TI and Cypress directly competed in several markets and that the two companies had significant bad blood between them as a result of two previous intellectual property lawsuits.[177] Thus, applying the reasoning underlying Cypress' advisor's predictions, TI likely would not have extended foundry services to Cypress either. But, TI did make at least a nonbinding commitment to continue foundry services for Cypress.

Petitioner has not shown that any other company that wanted to acquire Ramtron was in a worse position than Cypress in terms of getting TI's assent. Indeed, some may have been better positioned than Cypress. Construed most favorably to LongPath, all bidders were in the same boat as Cypress vis-à-vis TI. Ramtron's manufacturing agreement with TI simply was part of the Company's operative reality at the time of the Merger.

Furthermore, there is no evidence that the change-in-control provisions in the TI manufacturing agreement actually deterred any of the potential bidders.[178] Ramtron apparently proceeded the furthest in discussing alternative transactions with three companies: Atmel Corp., SMART Modular, and ROHM. Nothing suggests that the TI agreement caused any of those companies to back out. Davenport testified that SMART Modular was "very hesitant due to our supply-side cost structure and the tenuousness of our supply" and also did not like the Company's "sole sourcing."[179] Atmel similarly declined because of Ramtron's "cost structure [and] in particular our wafer supply, [which] they were very, very concerned about."[180] ROHM seems to have been contemplating a minority investment, discussed in the next

Subsection, which would not have implicated the TI concerns. In short, Petitioner has not demonstrated that the change-in-control provisions in the manufacturing agreement with TI materially impaired Ramtron's sales process. Instead, Ramtron's sole or primary reliance on TI as its foundry was part of the Company's operative reality.

2. Ramtron tries to sell itself to anyone but Cypress

***23** Ramtron authorized Needham, its financial advisor, to market the Company to other potential acquirers and explore strategic alternatives. According to an August 30, 2012 Needham presentation, Needham had: (1) contacted twenty-four third parties, including Cypress; (2) sent non-disclosure agreements ("NDAs") to twelve of those entities, again including Cypress; (3) received executed NDAs from six interested parties, which did not include Cypress; and (4) remained in discussions with two companies other than Cypress.[181] This market canvass reveals that six companies were intrigued enough to enter into NDAs. It appears that those companies received or at least had access to Ramtron's Management Projections.[182] In addition, by August, Ramtron had announced its new manufacturing agreement with ROHM. Yet, despite this sales effort, not one company besides Cypress ever made a firm bid for Ramtron.

SMART Modular and Atmel were two of the companies with which talks proceeded the furthest. As noted, both companies declined to pursue a transaction because of what they viewed as problems with Ramtron's cost structure. The evidence does not reveal why each and every other company declined to bid for Ramtron. At least one that executed an NDA saw no synergies in the transaction.[183] A second did not see the acquisition fitting with the potential bidder's strategic priorities.[184] Another that apparently did have familiarity with Ramtron's technology was advised by its engineers not to move forward.[185] That company was sent, but did not sign, an NDA.

Not one of the specific explanations in the record relates to TI. Instead, what evidence there is suggests that these other companies did not see value in Ramtron exceeding Cypress' bid. The importance of this point is amplified by the fact that Needham's call log indicates that the NDAs all were executed in late June,[186] when Cypress' bid was only $2.68 a share. According to Petitioner's position in this litigation, at that point in time, the Company was being undervalued by $2.28. Ramtron's hostile bid caused a significant spike in trading volume, as revealed by Needham's stock price analyses.[187] Aside from the prospective purchasers that Needham contacted, therefore, the fact that Ramtron was in play was known in the market. Purely financial purchasers theoretically could have stepped in and made unsolicited bids and, according to LongPath's position in this litigation, snatched up Ramtron at a fire sale price. None did. Indeed, *no one even bid,* including those with inside information, even when Cypress' offer was $0.42 below the final Merger price.

Petitioner focuses at length on Ramtron's discussions with ROHM. On July 17, 2012, Ramtron's management proposed two alternative transactions to ROHM: (1) a purchase of seven million shares of Ramtron common stock at $3.50 per share together with a board seat; or (2) seven million shares of Ramtron convertible preferred stock at $4.00 per share and a board seat.[188] Three days later, on July 20, Ramtron and ROHM announced their new manufacturing agreement.[189] ROHM apparently also was interested in the potential purchase of Ramtron's common stock and, on August 11, 2012, communicated to the Company that any such purchase would be at $3.00 per share.[190]

According to Petitioner, ROHM's interest in a minority investment at a price slightly below the deal price indicates that the Merger price undervalued Ramtron. If ROHM in fact had made such an investment, I might be inclined to agree.[191] But, even in its email countering at $3.00, ROHM explicitly stated the following:

> ***24** Actually, one of our concerns at this time is the legal and financial risk for purchasing stocks of a public company with a price above the market price. Since we have to justify the purchasing price to achieve the accountability to our shareholders, we have to seek profit that can make up for the paid premium. And we have to be careful to decide the purchase price in order to avoid impairment loss of assets.[192]

ROHM itself, it seems, was concerned with justifying the above-market premium. Perhaps, because of the manufacturing agreement between it and Ramtron, ROHM might have been able to exploit synergies between the two companies or otherwise unlock value in Ramtron not available to other bidders. Ultimately, however, ROHM backed away from pursuing a deal for Ramtron at the end of August. Citing "growing apprehension in ROHM's own business environment," ROHM determined that it was "not in a position to make an investment under present business outlook."[193]

3. Ramtron extracts a substantial premium from Cypress

Finally, LongPath criticizes Cypress' hostile approach, arguing that Cypress pounded Ramtron into submission at a below-market rate. I already have found that, to the extent Cypress' hostile bid negatively altered Ramtron's performance, such effects were dwarfed by Ramtron's own business problems, which included channel stuffing earlier in the year. Those flaws are part of Ramtron's operative reality. On the other hand, there is support in the case law for disregarding *temporary* distortions in determining a company's fair value.[194] In theory, then, it could be acceptable to back out any negative effects caused by Cypress' hostile offer. The parties, however, have offered no practical way to quantify those effects, particularly as against the larger effects from Ramtron's own business problems.

In that regard, there is no evidence that Cypress' hostile approach hampered the ability of other companies to bid for Ramtron or otherwise affected the Merger process. Only one company contacted by Needham stated that it did not wish to bid against Cypress.[195] By contrast, six other companies went so far as to execute NDAs. Even if Cypress was attempting to wear Ramtron down,[196] Cypress had every right to do so and there is no evidence that it acted improperly in this regard. Furthermore, the history of the Merger runs contrary to LongPath's argument. Ramtron's Board had the ability to say no to Cypress and repeatedly did so. The Board advised Ramtron's stockholders on several occasions not to tender into Cypress' bid and, over the same time period, *Cypress raised its bid five separate times.* The price Cypress ultimately paid—which was negotiated by the Ramtron Board and Cypress—was 25% higher than Cypress' starting offer.

4. Conclusion

The Merger resulted from Cypress' hostile bid. Cypress spent three months attempting to acquire Ramtron, during which time the Company actively shopped itself to other conceivable buyers, several of which indicated serious interest. None of those potential alternative buyers made a firm offer. Cypress, however, repeatedly raised its price until it and Ramtron's Board agreed on final Merger price of $3.10 per share. This lengthy, publicized process was thorough and gives me confidence that, if Ramtron could have commanded a higher value, it would have. "For me (as a law-trained judge) to second-guess the price that resulted from that process involves an exercise in hubris and, at best, reasoned guess work."[197] As such, I conclude that the Merger price is a reliable indication of Ramtron's fair value.

D. Transaction Price Less Synergies

***25** Thus far, I have concluded that the Management Projections are unreliable, making the use of a DCF inappropriate. Additionally, the parties agree that there are no comparable companies and I concur with Respondent that the comparable transactions approach does not provide a reliable indication of fair value here. By contrast, the Merger process was thorough and supports my reliance on the Merger price as an indication of Ramtron's fair value. In the absence of alternative methodologies, I weigh the Merger price at 100% in determining the fair value of Petitioner's shares.

In an appraisal action, however, it is inappropriate to include merger-specific value. Accordingly, I must exclude from the $3.10 Merger price any portion of that amount attributable to Cypress-specific synergies, as opposed to Ramtron's value as a going concern.[198] Respondent argues that the synergies amount to $0.34 per share. Petitioner contends that the net synergies are only $0.03.

Preliminarily, I reject LongPath's contention that synergies should be subtracted not from the Merger price, but instead from the value that Cypress attributed to Ramtron, which, according to Petitioner, is between $3.90 and $5.44. Those valuations estimated Ramtron's worth as a division of Cypress. Petitioner's requested approach is contrary to the language of Section 262, which commands that I "determine the fair value of the shares *exclusive of* any element of value arising from the accomplishment or expectation of the merger or consolidation."[199] There is no basis to deduct synergies from the idiosyncratic value attributed to a company by its purchaser, because it is not clear that value would provide insight into the fair value of the target company as a going concern. Instead, the proper way of applying a merger-price-less-synergies approach is to determine the value paid for a company and then subtract that portion of the purchase price representing synergies.[200]

As to the synergies in this transaction, I find Respondent's argument that over 10% of the transaction price represented synergies to be without merit. Jarrell first provided a market-wide analysis of the premia paid by financial versus strategic buyers and from this approach concluded that average synergies could be removed from the purchase price by applying the ratio of the average financial buyers' premium to the average strategic buyers' premium, *i.e.,* effectively multiplying the Merger price by 0.73, which results in a fair value of $2.75.[201]

This general data, however, does not tell me anything about *this specific* transaction, which must be the focus in a Section 262 action. With respect to Cypress-specific synergies, Jarrell compared the Management Projections to a set of Cypress projections[202] and quantified the cost savings, which Jarrell determined to be $0.69 per share. He then assumed that Ramtron's stockholders captured between 25% and 75% of these synergies and took the midpoint of those calculations, resulting in a fair value of $2.76.[203] In addition to its back-of-the-envelope feel, this approach focuses solely on cost savings, which are positive synergies, and neglects the possibility of negative synergies, which Clarke asserts would exist here.[204]

***26** Although Clarke rejected the transaction-price-less-synergies approach, he opined that negative revenue synergies and transaction costs would have to be added back to any value based on Jarrell's estimate of synergies. I find this approach to be reasonable and supported by the record. The testimony at trial indicates that Cypress expected significant negative synergies from the Ramtron acquisition.[205] While Petitioner's approach may understate the net synergies, I find that it better conforms to the evidence adduced at trial than Ramtron's position. Accordingly, I adopt LongPath's approach to synergies and exclude $0.03 from the Merger price. This results in a fair value determination of $3.07 per share.

E. Reality Checks

As a final step, I consider it appropriate to touch briefly on some of the "real world" evidence that Petitioner contends undermines the Merger price as a reliable indicator of fair value. Some of these items are entitled to zero weight. Balzer, for example, testified at his deposition that he told Cypress at the time of its nonpublic offer in 2011 that he believed Ramtron's stock would be worth $6 to $8 "several years out."[206] This speculation, of course, is not informative as to what Ramtron was worth at the time of the Merger. Similarly, Ramtron's Chairman of the Board testified that he "personally would have paid more than $3.10."[207] The usefulness of a transaction price, however, is that "buyers with a profit motive [are] able to assess [company-specific] factors for themselves and to use those assessments to make bids with actual money behind them."[208] By contrast, hypothetical statements about how much money someone allegedly would have paid, if they actually had the money to do so, which they apparently did not, are significantly less probative.

Similarly, I give no weight to the $4 target trading price Merriman Capital announced in January 2012,[209] and reiterated in April 2012.[210] By late July, Merriman Capital had pulled its target price and admitted it could not model Ramtron accurately.[211] And, as already discussed, I do not find informative the fact that Cypress' internal documents suggest a value for Ramtron above the deal price; those documents model Ramtron as a division of Cypress and are not indicative of the fair value of Ramtron as a stand-alone company.

The one factor that does cause me some pause, however, is the ROHM potential investment. The fact that ROHM apparently was seriously considering a minority equity investment at $3.00 per share casts some doubt on the Merger price of $3.10. Ultimately, however, ROHM did not make this investment and, in fact, expressed serious concern about paying an above-market price for Ramtron stock. Because ROHM had extensive information about Ramtron and ultimately decided not to pursue the minority investment, I discount its importance. ROHM made exactly as many actual bids as the rest of the market: zero. In that regard, the ROHM equity "investment" is simply another non-event.

Indeed, I suspect that, rather than the Merger price being low, it was more likely that the ROHM proposal was inexplicably high. Recall, for example, that, in 2011, long before Cypress made its public offer, Ramtron executed a secondary public offering in which it diluted its equity holders and sold about 20% of its shares for $2.00 each, with a net to itself of $1.79. By July 2012, based on the findings in this Memorandum Opinion, Ramtron's financial condition was no better than it was when it made the secondary public offering. For these reasons, I conclude that the ROHM investment, which never actually occurred, does not cast doubt on the Merger price as a reliable indicator of fair value.

IV. CONCLUSION

***27** For the foregoing reasons, I determine the fair value of Ramtron as of the Merger date to be $3.07 per share. Counsel for Petitioner shall submit, on notice, an appropriate final order to that effect, including provisions for pre- and post-judgment interest.

All Citations

Not Reported in Atl. Rptr., 2015 WL 4540443

Footnotes

[1] The factual record is drawn, in part, from the testimony presented at trial. Citations to such testimony are in the form “Tr. # (X)” with “X” representing the surname of the speaker, if not clear from the text. Exhibits will be cited as “JX # ” and facts drawn from the parties' pre-trial Joint Stipulation are cited as “JS ¶ # .”

[2] Tr. 10 (Davidian).

[3] JS ¶ 1.

[4] *Id.* ¶ 4.

[5] Tr. 184 (Davenport).

[6] JS ¶ 2.

[7] Tr. 281 (Rodgers).

[8] JS ¶ 11.

[9] *Id.* ¶ 13.

[10] *Id.* ¶ 18.

[11] *Id.* ¶ 23.

[12] *Id.* ¶ 5.

[13] JX 322, JX 324.

[14] Before assuming the CFO position, Richards previously had served as the Company's controller. He appears to have started working at Ramtron in 2004. Tr. 49. After the Merger, he worked for Cypress for five months until March 2013. *Id* at 22–23.

[15] *Id.* at 48–49. Apparently Fujitsu did not definitively terminate the foundry relationship, but instead, was moving its plant to a new location and Ramtron determined that the expense of transitioning to the new location outweighed the benefits.

[16] *Id.* at 291 (Rodgers).

[17] *Id.* at 291–92 (describing the process of transitioning foundries). The Company's products primarily, if not entirely, were for commercial customers. The F–RAM often was “designed into” the customer's end product.

[18] *Id.* at 292. Rodgers also suggested that Ramtron's products had design flaws that increased the difficulty of transitioning.

[19] Tr. 49 (Richards).

[20] *Id.* at 50-52 (Richards); *id.* at 187-88 (Davenport).

[21] Davenport began working for Ramtron in 1986. He started as an equipment engineer and worked his way up to the Vice President position. He currently is employed by Cypress as the Vice President of Technical Staff. Tr. 183.

[22] *Id.* at 198-99; JX 128.

[23] Tr. 198.

[24] JX 215 [hereinafter “Jarrell Rpt.”] Ex. 8.

[25] Tr. 49-50 (Richards); *id.* at 198 (Davenport) (noting that the difficulty and risk of transitioning foundries is “substantially higher” in the case of transferring a specialty process like F-RAM if the new foundry has no experience with F-RAM); *id.* at 291 (Rodgers) (stating that “in general, switching foundries is a big deal” and that the process requires a company to “in effect, change the product”).

[26] JS ¶ 5.

[27] *Id.* ¶ 6.

[28] Tr. 63-64 (Richards).

[29] *Id*. at 22.

[30] *Id.* at 158 (Richards).

[31] *Id.* at 30-31 (Richards).

[32] *Id.* at 30 (Richards); *id.* at 192 (Davenport); *id.* at 299-302 (Rodgers); *id.* at 396-97 (Buss).

[33] *Id.* at 50-51 (Richards); *id.* at 187-88 (Davenport).

[34] *Id.* at 52 (Richards) (describing the resulting difficulty when TI would not extend credit for the over-order of wafers).

[35] The data in this chart is drawn from Exhibit 5 to the Jarrell Report.

[36] JX 22; Tr. 25 (Richards).

[37] JX 24.

[38] JS ¶ 8.

[39] JX 14.

[40] Tr. 285.

[41] *Id.* at 54-55 (Richards).

[42] *Id.* at 54 (Richards).

[43] JS ¶ 9.

[44] Tr. 55 (Richards).

[45] JX 35.

[46] JX 43; Tr. 28 (Richards: explaining that this reference to the new bank covenants related to the fact that Ramtron recently had renegotiated its covenants yet again).

[47] JX 151.

[48] Tr. 410 (Buss).

[49] *Id.* at 30.

[50] JS ¶ 11.

[51] Tr. 294 (Rodgers).

[52] JS ¶ 12.

[53] The sole exception appears to be a set of projections created by Richards in February 2012 and sent to the Company's auditors in an effort to corroborate the extent of Ramtron's net operating loss tax assets. JX 40. Interestingly, the 2013 forecasts included a confidence factor of 80% and the 2014 forecasts had a confidence factor of only 50%. Richards did not even bother providing a confidence factor for the 2015 forecasts. *Id.* (native file).

[54] Tr. 59 (Richards).

[55] JX 60.

[56] Tr. 59 (“Needham was going to market our company.... [O]ne of their tactics was to put us out to bid so hopefully maybe a white knight would come in. And, two, I think they used [the projections] for a discounted cash flow to come up with a basis to value the company, if you will.”).

[57] *Id.* at 63.

[58] JX 60.

[59] *Id.* By recommending use of a 30% CAGR, which generally stands for compound annual growth rate, Richards understood Zimmer to be advocating multiplying a base value by 1.3 for each year of the projection period.

[60] Tr. 63 (Richards).

[61] JS ¶ 13.

[62] *Id.* ¶ 14.

[63] JX 47.

[64] JX 96.

[65] JX 97.

[66] *Id.*

[67] Tr. 73 (Richards); *id.* at 302 (Rodgers); *id.* at 397 (Buss).

[68] JX 245 [hereinafter "Balzer Dep."] at 106 ("Part of the reason that sales fell off as soon as Cypress announced the acquisition is distributors that we had.... If these distributors were not distributors of Cypress product, it was their belief—and I heard this from Pete [Zimmer]—their belief then that Cypress would probably not protect them if they consummated the deal and they could be stuck with a whole bunch of product and, hence, they just stopped buying."). There is a potential hearsay problem with this testimony, but Respondent did not press any such objection in its briefing.

[69] A $70 million year would equate to weekly sales of, on average, $1.347 million.

[70] Tr. 209.

[71] *Id.* at 402-04 (Buss).

[72] JS ¶ 15.

[73] *Id.* ¶ 16.

[74] *Id.* ¶ 17.

[75] *Id.* ¶ 18.

[76] *Id.* ¶ 23.

[77] *Dent v. Ramtron Int'l Corp.*, 2014 WL 2931180 (Del. Ch. June 30, 2014).

[78] *E.g.*, *In re Dole Food Co.*, 2014 WL 6906134, at *11 (Del. Ch. Dec. 9, 2014) ("In appraisal proceedings, the battling experts tend to generate widely divergent valuations as they strive to bracket the outer limits of plausibility."); *Finkelstein v. Liberty Digital, Inc.*, 2005 WL 1074364, at *13 (Del. Ch. Apr. 25, 2005) ("Men and women who purport to be applying sound, academically-validated valuation techniques come to this court and, through the neutral application of their expertise to the facts, come to widely disparate results, even when applying the same methodology.").

[79] 8 Del. C. § 262(h).

[80] *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214, 218 (Del. 2010).

[81] *M.G. Bancorporation, Inc. v. Le Beau*, 737 A.2d 513, 525 (Del. 1999) (quoting *Cede & Co. v. Technicolor, Inc.*, 684 A.2d 289, 298 (Del. 1996)).

[82] 8 *Del. C.* § 262(h).

[83] *Gholl v. eMachines, Inc.*, 2004 WL 2847865, at *5 (Del. Ch. Nov. 24, 2004) (quoting *Weinberger v. UOP, Inc.*, 457 A.2d 701, 713 (Del. 1983)).

[84] *M.G. Bancorporation, Inc.*, 737 A.2d at 520 ("In a statutory appraisal proceeding, both sides have the burden of proving their respective valuation positions by a preponderance of the evidence.").

[85] *Gholl*, 2004 WL 2847865, at *5.

[86] *Doft & Co. v. Travelocity.com Inc.*, 2004 WL 1152338, at *5 (Del. Ch. May 21, 2004).

[87] *Highfields Capital, Ltd. v. AXA Fin., Inc.*, 939 A.2d 34, 52-53 (Del. Ch. 2007).

[88] *Cf.* *Laidler v. Hesco Bastion Envt'l, Inc.*, 2014 WL 1877536, at * 8 (Del. Ch. May 12, 2014) ("Though DCF is more prominently employed in Delaware appraisal litigation, both parties' experts opine that employing a DCF is not feasible here because [the company's] management never made cash flow projections in the ordinary course of its business.").

[89] *Cede & Co. v. JRC Acq. Corp.*, 2004 WL 286963, at *2 (Del. Ch. Feb. 10, 2004).

[90] *Doft & Co.*, 2004 WL 1152338, at *5.

[91] *Cede & Co. v. Technicolor, Inc.*, 2003 WL 23700218, at *7 (Del. Ch. Dec. 31, 2003), *revised* (July 9, 2004), *aff'd in part, rev'd in part,* 884 A.2d 26 (Del. 2005).

[92] *Gearreald v. Just Care, Inc.*, 2012 WL 1569818, at *4 (Del. Ch. Apr. 30, 2012) (listing these four factors as reasons not to afford deference to the projections); *see also* *Huff Fund Inv. P'ship v. CKx, Inc.*, 2013 WL 5878807, at *9-11 (Del. Ch. Nov. 1, 2013) (rejecting management projections prepared out of the ordinary course that included substantial speculative elements), *holding left unmodified*, 2014 WL 2042797 (Del. Ch. May 19, 2014), *both aff'd,* 2015 WL 631586 (Del. Feb. 12, 2015) (TABLE); *Doft & Co.*, 2004 WL 1152338, at *5-6 (finding management projections unreliable because: (1) management themselves did not regard them as reliable; and (2) the company, and seemingly the industry, was deemed nearly impossible to forecast in the short term, much less the long-term).

Recent cases continue to evaluate the reliability of management projections on similar grounds. See, e.g., *Merlin P'rs LP v. AutoInfo, Inc.*, 2015 WL 2069417, at *8 (Del. Ch. Apr. 30, 2015) (refusing to rely on management projections where: (1) management never before had prepared similar projections; (2) the projections were so “indisputably optimistic” that the petitioner's own expert testified that a discount would have been appropriate; and (3) management “itself had no confidence in its ability to forecast”); *Owen v. Cannon*, 2015 WL 3189204, at *19-21 (Del. Ch. June 17, 2015) (rejecting an attack on the management projections when those projections did not include speculative business items, were not inconsistent with historical performance, were not “created by novices,” and instead generally resulted from a “deliberate, iterative process over a period of three years to create, update and revise multi-year projections for the Company”).

[93] Tr. 59 (Richards).

[94] *Id.* at 60.

[95] *Id.* at 64.

[96] *Id.* at 63 (Richards); *see also* JX 60.

[97] *See supra* note 53.

[98] JX 60.

[99] Tr. 59.

[100] *Id.*

[101] *E.g.*, JX 47 (forecasting, on April 19, 2012, $70 million in total 2012 revenue). On February 22, 2011, Ramtron forecasted between $65 and $70 million in total 2011 revenue. JX 294. Actual revenues for 2011 were $66.4 million. JX 215 Ex. 3. The 2011 forecast likely was not made by exactly the same management team and neither the 2011 nor the 2012 forecasts utilized a point-of-sale or a bottoms-up line-item methodology. Thus, the relevance of the 2011 and 2012 forecasts, as predictors of the accuracy of the Management Projections, is marginal, at best.

[102] JX 39. This chart was included in a presentation to the Ramtron Board and is dated February 9, 2012. The first two columns indicate the month and the quarter when each particular forecast was made. The remaining columns are the quarters being forecasted. For unknown reasons, there are two sets of forecasts in the first quarter of 2011. The bolded number represents the actual results in thousands of dollars for each quarter. For example, the cell Q2 2010 by Q1 2011 represents management's forecast, as of the second quarter of 2010, for revenue in the first quarter of 2011. I have added the actual results for Q1 and Q2 2012, which were not yet known as of February 9, 2012.

[103] Indeed, an earlier version of the same chart appeared in an October 18, 2011 board presentation entitled “Financial Outlook.” JX 31. That chart similarly was entitled “Sales Forecast Waterfall Chart,” as in JX 39, and it contained no indication that the figures presented were “stretch” goals.

[104] JX 313 (Oct. 18, 2011); JX 314 (Feb. 13-14, 2012).

[105] Tr. 209, 232.

[106] JX 36.

[107] *See Gholl*, 2004 WL 2847865, at *9 (rejecting contention that management projections were unrealistic reach goals and noting: "If the 2002 budget represented management's wildest dreams come true, it would be illogical and callous to key the Bonus Plan to even higher targets that were not achievable").

[108] The February 2012 projections cumulatively estimate $67 million in revenue for 2012. This is the same number used by Richards in a set of projections prepared to justify the Company's deferred tax assets to its auditors. JX 40. Richards's use of the waterfall chart forecast numbers for projections provided to the Company's auditors further supports my finding that these were not "stretch" goals.

[109] Tr. 31-32 (Richards); *id.* at 320-21 (Rodgers: explaining that rigorous competition, technological change, and macroeconomic factors make the industry difficult to forecast); *id.* at 378-80 (Buss).

[110] JX 97.

[111] Balzer candidly conceded the Company was mediocre at forecasting:

> Q: What was the quality of those forward-looking projections when you took over as CEO?
>
> A: Probably mediocre.
>
> Q: Did you attempt to make improvements in the quality of the projections?
>
> A: Yes.
>
> Q: Did you succeed?
>
> A: I'd say no.
>
> Q: Why not?
>
> A: ... [Y]ou need to understand the market.... And while we were working very hard on that, we weren't there.

Balzer Dep. 50. These comments temper the reliability of Balzer's position that the Management Projections "were the most likely of what would happen if Cypress walked away." *Id.* at 83.

[112] JX 170 native file.

[113] *See Gearreald*, 2012 WL 1569818, at *5-6 (concluding that the requirement that a company be valued as a going concern based on its operative reality at the time of the merger required the exclusion of "speculative costs or revenues"); *see also Huff Fund Inv. P'ship*, 2013 WL 5878807, at *11 (finding the inclusion or exclusion of significant contract revenues so speculative as to render the management projections unreliable).

[114] JX 95.

[115] *Id.*

[116] *E.g.*, Tr. 410 (Buss: commenting that, upon acquiring Ramtron, Cypress discovered that the Company still had unpaid legal bills from the beginning of 2012). Indeed, Ramtron was on pace to go cash negative before the end of October 2012. JX 151.

[117] JX 170 native file (assumption of per part cost reductions).

[118] *See supra* notes 16-18 and accompanying text.

[119] Tr. 225.

[120] *Id.* at 205.

[121] *Id.* at 207-08 (Davenport: discussing ROHM's wafer yield of 20% to 60%, as against a "good" yield of 97%, which TI could achieve, all of which bears on supply costs); *id.* at 348-51 (Rodgers: testifying that ROHM lagged behind TI technologically, was not competitive in the marketplace against TI's products, and had a very different technology than TI that would make the foundry transition difficult, all of which raised questions about the economic viability of manufacturing microchips there); *id.* at 395 (Buss: stating that TI and IBM "are probably two of the best, well-run, capable fabs in the world," and that successfully introducing ROHM as a second foundry "was definitely a long shot"). The testimony of Cypress' officers and employees is obviously self-serving, but their remarks on the technological status of ROHM versus TI or IBM is not contradicted by any other evidence and comports with Ramtron's own difficult history in transferring foundries.

[122] JX 170 native file (year-over-year growth rates of -12%, 19%, 24%, 24%, and 24%, for 2012 through 2016, respectively).

[123] *E.g.* Tr. 415 (Buss: describing Ramtron's inventory problem).

[124] JX 36.

125 *Id.*

126 LongPath cites to statements by Balzer regarding other time periods that the Company should avoid stuffing the channel. JX 10; JX 242.

127 The evidence suggests that many or most of Ramtron's products were “designed into” its customers' products. This long-term supply nature of Ramtron's business reduces the likelihood of dramatic short-term demand fluctuations.

128 *See supra* notes 70-72 and accompanying text.

129 Pet'r's Post-Trial Br. 34. My rather simplistic comparison of point-of-purchase versus point-of-sale revenue recognition supra suggested that the use of one system over the other affects only the timing of the revenue, not the amount. There are various reasons why using the point-of-purchase approach also may lead to over-recognition of revenue. The distributors may return inventory because, for example, they ordered too much or the products are obsolete. Distributors also may sell to the end-user for less than the list price, leading to a reduction in the actual revenue received. *See* Tr. 299-302 (Rodgers: comparing the two revenue recognition systems).

130 Moreover, because Ramtron's management moved to a new revenue-recognition approach for the Management Projections, it is not clear what steps the Company took to avoid double counting revenue. As of the end of January 2012, Ramtron had about $21 million in inventory in its distribution channels. JX 34 (Zimmer email). That is more than a quarter's worth of revenue. But, the Company apparently did track to some extent the differences between point-of-sale and point-of-purchase revenues. JX 174.

131 The historical figures are drawn from Exhibit 8 of Jarrell's Report. These figures are for the years 2002 through 2011 and are in blue. The projected revenues are drawn from the native excel spreadsheet of JX 170, which is the final iteration of the Management Projections. The projection period is 2012 through 2016 and those numbers are displayed in red.

132 By 2012, the Company had experienced two consecutive years of revenue decreases. In fact, 2012 revenue was forecasted as less than 2008 revenue. 2016 forecasted revenue, by contrast, nearly would exceed Ramtron's 2010 and 2011 actual revenues combined.

133 The inputs are the same as the previous graph. CAGR provides the rate at which an initial value would need to grow each year in order to achieve a final amount. It is a measurement that smoothes out swings in growth over time. For CAGR, I use the formula: CAGR = ((End Value / Start Value)^(1 / Number of Years)) – 1. Note that, while, for example, 2002-2011 is a period of ten years, the input for the CAGR formula would be nine, because there are only nine periods of growth between year-end 2002 and year-end 2011. CAGR can be a misleading measurement tool, as the selection of years can dramatically affect the implied annual return. This is why multiple historical CAGR measurements are provided.

134 JX 199; Tr. 426-32 (Buss: explaining the various portions of JX 199, which is the PSP).

135 In 2017, for example, Cypress predicted a 22% market share.

136 Balzer Dep. 80–81.

137 JX 170.

138 *Id.* & native file.

139 JX 93 & native file.

140 JX 136 & native file.

141 Tr. 81.

142 My conclusion that the Management Projections are unreliable prevents me from using those inputs. It is equally dubious to use either set of the SVB Projections, because they extend only for the 2012 calendar year and one of the main problems with the Management Projections is that they forecast an unrealistic *rate* of growth. Thus, even if the SVB Projections provided a reliable 2012 input, it still would not be clear what rate of growth to apply for future years. The parties, perhaps, could have advised on this issue. Instead of arguing that the Management Projections should be discounted a certain percentage, however, the parties took the opposite tactic of wholesale adoption or rejection of the Management Projections. This has forced

the Court to choose one of those routes. Adopting instead some sort of middle ground would require me to engage in impermissible and unreliable speculation.

[143] *Huff Fund Inv. P'ship,* 2013 WL 5878807, at *9.

[144] Cypress prepared its own projections for Ramtron. JX 174. Those projections, however, predict Ramtron's performance as a division of Cypress. Tr. 321–23 (Rodgers). Accordingly, they are not useful as a predictor of Ramtron's stand-alone operating potential. Furthermore, Cypress predicted substantially more conservative figures than Ramtron's management, even after accounting for improvements that Cypress anticipated making to Ramtron.

[145] JX 214 [hereinafter "Clarke Rpt."] at 47; Jarrell Rpt. 84.

[146] Clarke Rpt. 51.

[147] *Id.* at 58.

[148] Jarrell Rpt. 87, 91.

[149] *Highfields Capital, Ltd. v. AXA Fin., Inc.*, 939 A.2d 34, 54 (Del. Ch. 2007) (quoting *In re U.S. Cellular Operating Co.,* 2005 WL 43994, at *17 (Del. Ch. Jan. 6, 2005)).

[150] *In re Orchard Enters., Inc.*, 2012 WL 2923305, at *9 (Del. Ch. July 18, 2012).

[151] Clarke Rpt. 50-51.

[152] This is "forecasted revenue for the one-year period after the next 12 months." *Id.* at 53.

[153] JX 216 [hereinafter "Jarrell Rebuttal Rpt."] at 38.

[154] *Id.*

[155] *Merion Capital, L.P. v. 3M Cogent, Inc.*, 2013 WL 3793896, at *8 (Del. Ch. July 8, 2013) (citing *In re John Q. Hammons Hotels Inc. S'holder Litig.*, 2011 WL 227634, at *5 (Del. Ch. Jan. 14, 2011) and *In re U.S. Cellular Operating Co.*, 2005 WL 43994, at *18).

[156] *Id.*

[157] Clarke Rpt. 54.

[158] The implied equity value is not an exact multiple, because Ramtron's debt of $8.8 million is subtracted out and the Company's cash of $1.3 million is added into the calculation. This results in netting out $7.5 million to obtain the implied equity value that is shown.

[159] This calculation is derived by applying the comparable transaction multiples to Ramtron's financials, subtracting $7.5 million, discounting by 13%, and then dividing by the number of shares, which I assume to be Clarke's figure of 35,528,425. Jarrell contends that the latter figure understates the number of shares by about four million units because of restricted stock and stock options.

[160] These numbers are inconsequentially different from Jarrell's calculations. The deviation seemingly results from his rounding of Clarke's determination of shares outstanding to 35,500,000.

[161] Jarrell presents a colorable argument that Virage is not, in fact, a comparable transaction. If correct, that provides yet another reason that the comparable transaction methodology is not reliable here, but I need not decide that issue. If Virage is not comparable, the Court would be left attempting to value Ramtron on the highly questionable basis of a single allegedly comparable transaction.

[162] 11 A.3d 214 (Del. 2010).

[163] *Id.* at 217-18.

[164] *In re Appraisal of Ancestry.com, Inc.*, 2015 WL 399726 (holding that the merger price was the most reliable indication of fair value and performing confirmatory DCF analysis); *Huff Fund Inv. P'ship*, 2013 WL 5878807 (finding the merger price to be the best indication of fair value in light of the lack of other reliable methods); The *Union Illinois 1995 Inv. Ltd. P'ship v. Union Fin. Gp., Ltd.*, 847 A.2d 340 (Del. Ch. Jan. 5, 2004) (concluding that the merger price offered the best indication of fair value and also performing a confirmatory DCF analysis).

[165] *Van de Walle v. Unimation, Inc.*, 1991 WL 29303, at *17 (Del. Ch. Mar. 7, 1991).

[166] *Union Illinois,* 847 A.2d at 357.

[167] *Id.* at 358.

[168] *Huff Fund Inv. P'ship*, 2013 WL 5878807, at *13.

[169] JX 322 (TI Mfg. Agreement); JX 324 (TI Mfg. Agreement Amendment No. 2) § 13.1.

170 JX 322 § 14.8(b).

171 Tr. 287–90; *id.* at 289 (Rodgers: "They explicitly refused to say 'we will support you' to the point that I didn't even try to get them to sign a document, but my inference was that they wouldn't harm us if we didn't attack them.").

172 JX 320.

173 JX 236 at 7. Because the presentation includes actual numbers for 2011, I infer that it must be from sometime in 2012.

174 JX 67.

175 JX 65.

176 Tr. 287 (Rodgers).

177 *Id.* at 286 (Rodgers: "They're a company with many divisions, like us, and they compete broadly in the market."); *id.* at 287 ("TI and Cypress have a history of conflict, and they sued us twice about 15 years ago. We won both trials, but there's not good blood."); *id.* at 237 (Kaszubinski: testifying that TI and Cypress competed); *id.* at 389-90 (Buss: "So the challenge for us is that TI does not like Cypress. TI and T.J. [Rodgers] do not get along.... I believe he had been in two prior lawsuits with them prior to my tenure, and I think he beat them both times. So there is a lot of animosity between the two companies, and it was the number one issue we wrestled with.").

178 *Id.* at 65 (Richards); *id.* at 202 (Davenport).

179 *Id.* at 201.

180 *Id.*

181 JX 125 at 8.

182 The Management Projections were in the Company's data room. E.g., JX 84. Needham's call log shows that five companies who had signed NDAs accessed the data room, though one company that executed an NDA is missing from that log. JX 88.

183 JX 114.

184 JX 70.

185 JX 76.

186 JX 88.

187 JX 125.

188 JX 90.

189 JS ¶ 5.

190 JX 109.

191 Clarke's report, for example, suggested that the average acquisition premium in the semiconductor industry is about 30%, with roughly half of that amount attributable to a control premium and the remainder attributable to synergies. Clarke Rpt. 56. An additional 15% on top of $3.00 would imply a minimum acquisition price of $3.45, exclusive of synergies.

192 JX 109.

193 JX 126.

194 *See Glassman v. Unocal Exploration Corp.*, 777 A.2d 242, 248 (Del. 2001).

195 JX 88.

196 *See* JX 89 ("Wear them down and wait is working.").

197 *Union Illinois*, 847 A.2d at 359.

198 *Huff Fund,* 2014 WL 2042797, at *2.

199 8 Del. C. § 262(h) (emphasis added).

200 *Cf. Huff Fund*, 2014 WL 2042797, at *5 (providing the example of the urban cornfield auction and the eccentric farmer, and noting that, "In an auction setting, it makes little sense to determine whether a bid incorporates information about the value of certain opportunities by considering only the idiosyncratic weight attached to that information by any particular bidder, even the winning bidder").

201 Jarrell Rpt. 43-44.

[202] JX 174.

[203] Jarrell Rpt. 46.

[204] JX 217 (Clarke Rebuttal Rpt.) at 26-27.

[205] JX 217 (Clarke Rebuttal Rpt.) at 26-27.

[206] Balzer Dep. 19.

[207] JX 246 at 76.

[208] *Union Illinois,* 847 A.2d at 359.

[209] JX 38.

[210] JX 48.

[211] JX 97.

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UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

MERION CAPITAL, L.P., Magnetar Capital Master Fund Ltd., Magnetar Global Event Driven Master Fund Ltd., Magnetar SC Fund Ltd., Hipparchus Master Fund Ltd., Compass Offshore HTV PCC Limited, Compass HTV LLC, and Blackwell Partners LLC, Petitioners,
v.
3M COGENT, INC., Respondent.

Civil Action No. 6247–VCP
|
Submitted: March 19, 2013
|
Decided: July 8, 2013

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MEMORANDUM OPINION

PARSONS, Vice Chancellor.

***1** This is the post-trial decision in an appraisal brought pursuant to 8 *Del. C.* § 262 and arising out of a merger in which a global technology conglomerate and its acquisition subsidiary acquired a biometrics technology company at a price of $10.50 per share. Relying upon a discounted cash flow ("DCF") analysis, the petitioners claim that each share of the biometrics company's common shares was worth $16.26 as of the merger date. By contrast, the respondent contends that the biometrics company's common shares were worth only $10.12 apiece as of the merger date. For the reasons set forth below, the Court concludes that, as of the merger date, the fair value of the biometrics company was approximately $963.4 million or $10.87 per share.

I. BACKGROUND

A. The Parties

Respondent, 3M Cogent, Inc. ("3M Cogent"), formerly known as Cogent, Inc. ("Cogent" or the "Company"), is a Delaware corporation that provides biometric [1] technology. Specifically, Cogent offers automated fingerprint identification systems ("AFIS") technology and other fingerprint biometrics solutions to government, immigration, and law enforcement agencies.

Petitioners are Merion Capital, L.P., Magnetar Capital Master Fund Ltd., Magnetar Global Event Driven Master Fund Ltd., Magnetar SC Fund Ltd., Hipparchus Master Fund Ltd., Compass Offshore HTV PCC Limited, Compass HTV LLC, and Blackwell Partners LLC (collectively, the "Petitioners"). At the time of the merger, Petitioners beneficially owned 5,835,109 shares of Cogent common stock (the "Shares"). [2] Petitioners dissented from the merger and perfected their appraisal rights.

Nonparty 3M Company ("3M") is a diversified technology conglomerate with a global presence in the following businesses: industrial and transportation; health care; consumer and office; safety, security, and protection services; display and graphics; and electro and communications. [3] 3M acquired Cogent (or the "Company") through its acquisition subsidiary, nonparty Ventura Acquisition Corporation ("Ventura").

B. Facts

1. The business

Cogent was founded by Ming Hsieh in 1990. From 1990 until 2004, Cogent operated as a private company and was profitable during that entire period. [4] Ultimately, Cogent went public on September 23, 2004, and thereafter was publicly traded on the NASDAQ Global Select Market under the symbol "COGT."[5] At all relevant times, Hsieh was the President, Chairman, and Chief Executive Officer ("CEO") of Cogent, and Paul Kim was the Chief Financial Officer. Before the merger, Cogent's Board of Directors (the "Board") consisted of four members: Hsieh, John Bolger, John Stenbit, and Kenneth Thornton.

2. The transaction

***2** In or around 2008, Cogent retained Credit Suisse to assist in the investigation and evaluation of potential strategic alternatives, including a sale of the Company. As part of that engagement, Credit Suisse contacted over twenty-five potential strategic and financial partners about the prospect of acquiring Cogent.[6] Cogent also retained Goldman Sachs to pursue potential strategic alternatives with NEC, a competitor of Cogent. As a result of efforts by Cogent and its advisers, in 2010, 3M, Danaher Corporation ("Danaher"), Roper Industries ("Roper"), and NEC Corporation ("NEC") expressed interest in acquiring the Company.[7]

Around that time, Cogent had direct meetings with executives of 3M in which Cogent and its advisors informed 3M that other potential suitors were in discussions with Cogent.[8] In May 2010, 3M expressed interest in pursuing a strategic transaction with Cogent at a price range of $9.25 to $10.25 per share.[9]

Shortly after 3M's verbal offer, Kim prepared financial projections for 2010–2015 (the "Five–Year Projections").[10] Up until that time, Cogent had not prepared projections beyond one year.[11] Credit Suisse compiled the projections, but relied on information supplied by Kim, Hsieh, and Mary Jane Abalos, Cogent's vice president of finance.[12] According to Kim, the Five–Year Projections were "bottom-up" projections that did not rely on industry analysts or reports.[13]

On July 2, 2010, after further discussions and due diligence with potential acquirers, Cogent received two nonbinding indications of interest: one from 3M to acquire Cogent for $10.50 per share and the other from Danaher to acquire Cogent at a range of $10.00 to $10.50.[14] Although Roper and Danaher eventually dropped out of the process, NEC and 3M remained interested in pursuing a strategic transaction with Cogent.[15]

In August 2010, 3M submitted a nonbinding written proposal to acquire Cogent for $10.50 per share.[16] The Board met on August 15, 2010, and instructed their advisor, Credit Suisse, to inform 3M that its proposal was not acceptable and to negotiate with 3M on price and terms.[17] Cogent also leveraged the offer from 3M to pressure NEC to speed up its bid.[18] Ultimately, NEC submitted a nonbinding indication of interest to acquire Cogent within the range of $11.00 to $12.00 per share.[19] In a letter dated August 19, 2010, 3M advised Cogent that its bid would expire on August 20.[20] That day, the Board met to determine how to proceed. After considering updates on the ongoing discussions with NEC, the Board approved the negotiation of a definitive merger with 3M, rejected the condition of exclusivity requested in 3M's letter, and instructed Credit Suisse to continue discussions with NEC.[21]

Finally, on August 29, 2010, the Board held another special meeting at which it considered further updates on the discussions with NEC.[22] Based on NEC's need to complete its due diligence, the existence of antitrust and regulatory issues with NEC, and Credit Suisse's opinion that the proposed merger with 3M was fair, the Board unanimously determined that it was in the best interest of Cogent to enter into the proposed merger agreement with 3M, and resolved to recommend that the shareholders approve the merger.[23]

***3** The next day, Cogent and 3M publicly announced the merger. On September 10, 2010, 3M commenced a tender offer to acquire all of the issued and outstanding common stock of Cogent for $10.50 per share. The initial tender offer closed on October 7, 2010, after which 3M controlled a majority of Cogent's outstanding shares. Because Cogent did not have enough shares to complete a short-form merger, on October 8, 2010, 3M commenced a subsequent tender offering at the same price, $10.50 per share. On October 26, 2010, the subsequent offering closed, and 3M controlled 73% of Cogent's outstanding common shares or approximately 64.9 million common shares. On December 1, 2010 (the "Merger Date"), the stockholders of Cogent approved the merger pursuant to 8 *Del. C.* § 251 (the "Merger"). As a result, Cogent became a wholly owned subsidiary of 3M and thereafter was renamed 3M Cogent, Inc.

C. Procedural History

Following the Merger, Petitioners filed their Verified Petition for Appraisal on March 4, 2011. From November 28 through November 30, 2012, I presided over a three-day trial in this action. After extensive post-trial briefing, counsel presented their final arguments on March 19, 2013. This Memorandum Opinion constitutes my post-trial findings of fact and conclusions of law.

D. Parties' Contentions

Petitioners contend that the fair value of Cogent was $16.26 per share. In support of this valuation, Petitioners rely on their expert, Dr. Bernard C. Bailey, a Ph.D. in management and Chairman and CEO of Authentix Inc., a Carlyle Group portfolio company and global leader in authentication technology.[24] In valuing the Company, Bailey performed a DCF analysis, a comparable companies analysis, and a comparable transactions analysis. Bailey relied, however, only on his DCF analysis in reaching his valuation opinion because (1) Bailey believed there were no truly comparable companies or transactions to compare to Cogent and (2), to the extent there were any potentially comparable companies and transactions, he lacked sufficient data from which to draw comparisons.

3M Cogent claims that Cogent's fair value was $10.12 per share. In support of its valuation contentions, Respondent relies on the expert testimony and reports of Henry F. Owsley and Stephen M. Schiller (collectively, the "Gordian Experts"), a partner and managing director of Gordian Group, LLC ("Gordian Group"), respectively.[25] The Gordian Experts valued the Company using a DCF analysis, a comparable companies analysis, and a comparable transactions analysis, giving each analysis equal, *i.e.,* one-third, weight.

II. ANALYSIS

A. Standard

Under Section 262 of the Delaware General Corporation Law, stockholders who meet certain requirements are entitled to an appraisal by the Court of Chancery of the fair value of their shares of stock.[26] During such an appraisal proceeding, the Court of Chancery

> shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors.[27]

The Court's task is to perform an independent evaluation of "fair value."[28] "It is within the Court of Chancery's discretion to select one of the parties' valuation models as its general framework, or fashion its own, to determine fair value in the appraisal proceeding."[29] Fair value in the context of an appraisal proceeding is the "value to a stockholder of the firm as a going concern, as opposed to the firm's value in the context of an acquisition or other transaction."[30] "Only the speculative elements of value that may arise from the 'accomplishment or expectation' of the merger," that is, any synergistic value, should be excluded from a fair value calculation on the date of the merger.[31] "One of the most important factors to consider is the very 'nature of the enterprise' subject to the appraisal proceeding."[32]

***4** In an appraisal proceeding, both sides have the burden of proving their respective valuations by a preponderance of the evidence.[33] If neither party satisfies its burden, however, the Court must use its own independent judgment to determine the fair value of the shares.[34] The Court may consider "proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court."[35] Among the techniques that Delaware courts have relied on to determine the fair value of shares are the DCF approach, the comparable transactions approach, and comparable companies analyses.[36]

B. Merger Price as Indication of "Fair Value"

Respondent seeks to have this Court rely on the merger price as evidence of the fair value of Petitioners' shares. But, the cases that Respondent cites in support of that proposition[37] pre-date the Supreme Court's statements on this issue in *Golden Telecom, Inc. v. Global GT LP.*[38]

In *Golden Telecom,* the Supreme Court stated:

> Section 262(h) unambiguously calls upon the Court of Chancery to perform an independent evaluation of "fair value" at the time of a transaction. It vests the Chancellor and Vice Chancellors with significant discretion to consider "all relevant factors" and determine the going concern value of the underlying company. Requiring the Court of Chancery to defer—conclusively or presumptively—to the merger price, even in the face of a pristine, unchallenged transactional process, would contravene the unambiguous language of the statute and the reasoned holdings of our precedent. It would inappropriately shift the responsibility to determine "fair value" from the court to the private parties. Also, while it is difficult for the Chancellor and Vice Chancellors to assess wildly divergent expert opinions regarding value, inflexible rules governing appraisal provide little additional benefit in determining "fair value" because of the already high costs of appraisal actions. Appraisal is, by design, a flexible process. Therefore, we reject [respondent's] contention that the Vice Chancellor erred by insufficiently deferring to the merger price, and we reject its call to establish a rule requiring the Court of Chancery to defer to the merger price in any appraisal proceeding.[39]

***5** More recently, Chancellor Strine refused to give any weight to merger price, stating:

> [Respondent] makes some rhetorical hay out of its search for other buyers. But this is an appraisal action, not a fiduciary duty case, and although I have little reason to doubt [respondent's] assertion that no buyer was willing to pay Dimensional $25 million for the preferred stock and an attractive price for [respondent's] common stock in 2009, an appraisal must be focused on [respondent's] going concern value. Given the relevant legal standard, the trial record did not focus extensively on the quality of marketing [respondent] by Dimensional or the utility of the "go shop" provision contained in the merger agreement....
>
> Instead, the testimony at trial focused mostly on the question that is relevant under *Cavalier Oil* and its progeny, which is the going concern value of [respondent] as of the date of the [m]erger. In this opinion, I concentrate on answering the key questions raised by the parties relevant to determining that value, which are: (i) whether the preferred stock should be valued at the $25 million liquidation preference value or on an as-converted basis in determining the value to subtract from [respondent's] equity value to derive a value for its common stock; and (ii) the enterprise value of [respondent] as a going concern on the Merger date.[40]

Here, both sides have presented expert testimony as to the going concern value of Cogent on the Merger Date. Indeed, Respondent did not seek to use the merger price of $10.50 per share, but instead relies on the Gordian Experts' analyses to arrive at a lower price of $10.12.[41] Respondent and its experts also did not attempt to adjust the merger price to remove the "speculative elements of value that may arise from the 'accomplishment or expectation' of the merger."[42] In other words, Respondent asks this Court to rely on a merger price that it has not relied on itself and that is not adjusted to produce the going concern value of Cogent. Those deficiencies render the merger price largely irrelevant to this case. Accordingly, I focus primarily on the evidence presented by the experts as to the going concern value of Cogent on the Merger Date, *i.e.,* the experts' technical analyses presented in their expert reports and in their testimony at trial.

C. Which Valuation Method?

As previously indicated, Petitioners relied solely on a DCF analysis to support their argument that the fair value of a Cogent common share on the date of the Merger was $16.26. By contrast, 3M Cogent's experts gave nearly equal weight to their DCF analysis, comparable companies analysis, and comparable transactions analysis in coming to a per common share value for Cogent of $10.12.

Generally speaking, "it is preferable to take a more robust approach involving multiple techniques—such as a DCF analysis, a comparable transactions analysis (looking at precedent transaction comparables), and a comparable companies analysis (looking at trading comparables/multiples)—to triangulate a value range, as all three methodologies individually have their own limitations."[43] A comparable or market-based approach endeavors to draw inferences about a company's future expected cash flows from the market's expectations about comparable companies.[44] "[T]he utility of a market-based method depends on actually having companies that are sufficiently comparable that their trading multiples provide a relevant insight into the subject company's own growth prospects."[45] When there are a number of corporations competing in a similar industry, these methods are most reliable. On the other hand, when the "comparables" involve companies that offer different products or services, are at a different stage in their growth cycle, or have vastly different multiples, a comparable companies or comparable transactions analysis is inappropriate.[46] Therefore, I must examine the experts' respective selections of comparable companies and transactions to evaluate their reliability.

1. Comparable companies analysis

***6** The comparable companies method of valuing a company's equity involves several steps including: (1) finding comparable, publicly traded companies that have reviewable financial information; (2) calculating the ratio between the trading price of the stocks of each of those companies and some recognized measure reflecting their income such as revenue, EBIT, or EBITDA; (3) correcting these derived ratios to account for differences, such as in capital structure, between the public companies and the target company being valued; and, finally, (4) applying the average multiple of the comparable companies to the relevant income measurement of the target company, here Cogent.[47]

The Gordian Experts conducted a comparable companies analysis that began with the selection of ten companies.[48] The Gordian Experts then determined multiples by dividing the enterprise value for each company by: (i) last twelve months ("LTM") revenue and EBITDA; and (ii) estimated forward revenue and EBITDA, as determined by public filings and other publicly available information. Next, the Gordian Experts applied a range of multiples to Cogent's LTM and estimated forward revenue and EBITDA to determine an estimated enterprise value for Cogent. Ultimately, the Gordian Experts' analysis yielded an estimated enterprise value of Cogent of $296.3 million.

Here, Petitioners attack Respondent's first expert, Owsley, and his comparable companies analysis, claiming the analysis is "unreliable, unsupported and flawed."[49] Specifically, Petitioners note that the Gordian Experts' comparable companies analysis suffers from: (1) a paucity of data; (2) a selection of companies with either no profits, a different risk profile, no government-focused customer base, or no business in the biometrics industry; and (3) a generalized lack of consistent methodology.

"The burden of proof on the question [of] whether the comparables are truly comparable lies with the party making that assertion," here the Respondent.[50] I find that Respondent and its Gordian Experts have not satisfied that burden.

As an initial matter, six of the ten comparable companies the Gordian Experts identified were significantly smaller than Cogent. Those companies each had enterprise values of less than $50 million,[51] while Cogent's enterprise value was $398.5 million.[52] This Court has rejected the use of companies as comparables where those companies were significantly different in size than the appraised company.[53] That is because, as further discussed in Section II.D.2.d *infra* concerning the equity size premium, greater risk is typically associated with equity in a small company.[54] In that regard, it would be inappropriate to compare a company with an enterprise value of $14.7 million, as was the case with BIO–Key International, Inc., to a company, such as Cogent, with an enterprise value more than 25 times higher.

***7** Moreover, not one of those same six "comparable" companies had generated a profit.[55] At trial, Schiller, who replaced Owsley as Respondent's expert, acknowledged that the type of companies that have revenue multiples but not EBITDA multiples tend to be "companies in the early stage of their growth and maturity" and "companies that are growing rapidly."[56] In contrast, Cogent had been profitable from 1990 until 2005.[57] In that regard, Schiller acknowledged that companies that had never turned a profit "are not close comparables" to Cogent.[58]

The Gordian Experts also failed to select comparable companies from the same business or industry as Cogent. For example, five of the companies selected by Owsley had no biometrics business at all.[59] Bailey, Petitioners' expert, also notes that of the ten comparable companies selected by the Gordian Experts, only one—BIO-Key International—listed Cogent as a competitor in its annual report.[60]

Finally, the Gordian Experts' failure to identify L–1 as a comparable company to Cogent before trial causes me some concern. L–1 competed directly against Cogent in a number of markets, including the LiveScan market.[61] Indeed, Schiller admitted that L–1 "was one of the closer comparables to Cogent."[62] Nonetheless, the Gordian Experts excluded L–1 based on their mistaken belief that a roughly contemporaneous L–1 transaction had closed before the Merger.[63] Importantly, L–1 had very positive financials that probably would have increased the values generated by the Gordian Experts' comparable companies analysis.[64] In that sense, therefore, the Gordian Experts' analysis likely underestimates the value of Cogent.

Based on the problems identified in this subsection, I find the Gordian Experts' comparable companies analysis to be unreliable. Furthermore, because Respondent has not met its burden of proof to show that the selected companies are truly comparable, I accord no weight to that analysis.

2. Comparable transactions analysis

A comparable transactions analysis "involves identifying similar transactions, quantifying those transactions through financial metrics, and then applying the metrics to the company at issue to ascertain a value."[65] As with the comparable companies analysis, "[t]he utility of the comparable transactions methodology is directly linked to the 'similarity between the company the court is valuing and the companies used for comparison.' "[66]

Here, the Gordian Experts began their analysis with the selection of eighteen transactions.[67] They then calculated multiples by dividing the enterprise value (as determined by the terms of the relevant transactions) for each company involved by: (i) LTM revenue and EBITDA; and (ii) estimated forward revenue and EBITDA.[68] Next, the Gordian Experts arrived at multiple ranges by eliminating the top and bottom quartile.[69] Finally, they applied a 20% discount to the multiples they obtained to take into account the need to eliminate any control or synergy premiums.[70]

***8** Petitioners' expert Bailey criticized the Gordian Experts for using revenue multiples on the ground that they are less reliable than EBITDA multiples. At trial, Bailey explained that "it's inappropriate to use a revenue multiple as a multiple for trying to value [Cogent], because it was a very profitable cash-flow-positive company operating in a robust industry."[71]

In an expert report he submitted in another case, Owsley similarly criticized the use of revenue multiples, stating that "[w]hile it is true that many analysts regularly examine revenue multiples[,] I believe that such multiples are inherently more suspect due to their relatively higher level of variance (once low and negative earners are eliminated) than EBITDA multiples."[72] Owsley's inconsistent and contradictory positions undermine the Gordian Experts' credibility on this point, which they admitted was a "judgment call."[73] Based on these facts and Bailey's reasoning, I find that Respondent has not met its burden of showing that the Gordian Experts' use of a revenue multiples approach is reliable. Therefore, I accord no weight to that part of Respondent's analysis.

Petitioners contend that the remainder of the Gordian Experts' comparable transactions analysis, *i.e.,* the LTM and forward EBITDA multiples, is flawed because there are insufficient data points to support any meaningful conclusions. For the thirty-six potential EBITDA multiples identified, the Gordian Experts were able to provide only eight meaningful multiples. That number is even smaller after one eliminates the first and fourth quartiles. This Court has found comparable transactions analyses that used as few as five transactions and two transactions to be unreliable.[74] Indeed, “[i]f it turns out that very few data points are available for a particular valuation multiple, that problem may lead to abandon[ing] that multiple or [ ] put[ting] relatively little weight on it.”[75] The dearth of data points here undermines the reliability of the EBITDA multiples.

This conclusion is buttressed by the high dispersion of the data points the Gordian Experts did obtain. “The extent to which the valuation multiples are tightly clustered or widely dispersed tends to indicate the extent to which the market focuses on that particular valuation multiple in pricing companies in the particular industry.”[76] Here, the dispersion was “extremely large.”[77] For example, while the mean of the forward EBITDA multiple was 25.4x, the standard deviation was 25.1x.[78] Thus, because there are so few data points and the results are so widely dispersed, Respondent has failed to show that its EBITDA multiples analysis is reliable.

***9** For all of these reasons, I accord no weight to Respondent's comparable transactions analysis.

3. Delaware Rules of Evidence 702 and 705

Petitioners also raised an evidentiary challenge to Schiller's testimony and rebuttal report. According to Petitioners, Schiller's testimony lacks a factual basis and should be excluded under D.R.E. 702(1) and 705(b).[79] Petitioners also seek to exclude Schiller's testimony because an expert cannot act as

> a mere conduit or transmitter of the content of an extrajudicial source. An ‘expert’ should not be permitted simply to repeat another's opinion or data without bringing to bear on it his own expertise and judgment. Obviously in such a situation, the non-testifying expert is not on the witness stand and truly is unavailable for cross-examination.[80]

Finally, Petitioners note that an expert cannot materially change his opinions after the expert discovery cutoff.[81]

To put Petitioners' objections in context, I review briefly the background of Schiller's participation in this case. In late July 2012, Owsley unexpectedly became ill and went on medical leave.[82] In October 2012, Respondent asked Schiller to assume Owsley's role in this case by taking over the partially prepared rebuttal report and preparing himself to testify.[83] As part of that preparation, Schiller read Owsley's expert report, spoke with members of the Gordian team, and ultimately adopted Owsley's conclusions.[84] Schiller testified that he “independently assessed the validity of the judgments and conclusions of Mr. Owsley's report.”[85]

On October 22, 2012, Schiller submitted a rebuttal report that reflected his conclusions and judgments.[86] Two weeks later, on November 5, Schiller sat for a deposition. At that deposition, Schiller admitted that he did not “know all the things that the team looked at as they evaluated these comparables.”[87] Schiller was unable to say, among other things, whether in selecting comparable companies the Gordian team had considered whether those companies were government contractors.[88] Nor was Schiller able to identify the portion of each comparable company's business that was involved in the biometrics business.[89]

***10** At trial, Schiller admitted that he had no role in preparing Owsley's initial report, never spoke to Owsley regarding his opening report, and had not reviewed all of the materials in Appendix C of Owsley's report.[90] Schiller also changed some of his deposition answers to reflect work he had done after the deposition.[91]

Generally speaking, an expert can replace another expert who must drop out as a result of illness. Here, Schiller was a logical choice based on his understanding of the techniques that the Gordian Group regularly applies in its valuations. Moreover, Schiller apparently examined and relied on the judgments Owsley and his team made. Given these circumstances, I do not find Schiller's testimony inadmissible.

On the other hand, Schiller's deposition testimony demonstrated that, as to some topics, Schiller barely performed sufficient research to express an informed opinion, and instead relied heavily on the opinions and data of Owsley.

Because Schiller's statements regarding the comparability of certain companies changed between his deposition and trial and Respondent provided no prior notice of that change to Petitioners, I have given no weight to Schiller's later testimony.

These problems with the evidence adduced from Schiller also undermine his reliability and credibility as a witness and create an independent basis for according Schiller's comparables analyses only minimal weight.

D. DCF Analysis of Cogent

The basic premise underlying the DCF methodology is that the value of a company is equal to the value of its projected future cash flows, discounted to the present value at the opportunity cost of capital.[92] Calculating a DCF involves three steps: (1) one estimates the values of future cash flows for a discrete period, where possible, based on contemporaneous management projections; (2) the value of the entity attributable to cash flows expected after the end of the discrete period must be estimated to produce a so-called terminal value, preferably using a perpetual growth model; and (3) the value of the cash flows for the discrete period and the terminal value must be discounted back using the capital asset pricing model or "CAPM."[93] In simpler terms, the DCF method involves three basic components: (1) cash flow projections; (2) a discount rate; and (3) a terminal value.[94] The experts in this case relied on conflicting inputs and assumptions as to all three elements of their respective DCF analyses. I now turn to those disputed inputs and assumptions.

1. Cash flow projections

***11** A primary dispute between the parties is whether the Court should rely on the Five–Year Projections prepared by Kim and Credit Suisse. Petitioners would reject management's projections and adopt two key scenarios: (1) Bailey's "Industry Growth Scenario" that assumes an industry growth rate through 2015 of 17%; and (2) Bailey's "Cash Deployment Scenario" that assumes Cogent would spend $396 million of its cash on acquisitions.[95] In contrast, Respondent urges this Court to rely on management's projections with only a few minor adjustments.

Generally, this Court "prefers valuations based on contemporaneously prepared management projections because management ordinarily has the best first-hand knowledge of a company's operations."[96] In *Gearreald v. Just Care, Inc.*,[97] however, I held that projections prepared by management "are not entitled to the same deference usually afforded to contemporaneously prepared management projections" where "management had never prepared projections beyond the current fiscal year," "the possibility of litigation, such as an appraisal proceeding, was likely," and the projections "were made outside of the ordinary course of business."[98] I also considered it relevant in *Gearreald* that the projections at issue there were prepared by directors and officers of the target company who "risked losing their positions if the ... bid succeeded and were involved in trying to convince the Board to pursue a different strategic alternative in which [they] were involved."[99]

A number of the circumstances in *Gearreald* also are present here: (1) Cogent had never prepared projections beyond the current fiscal year;[100] (2) the management projections were prepared after 3M communicated a verbal offer to Cogent, and Hsieh communicated to 3M the price at which he was willing to recommend selling;[101] and (3) the projections were prepared with significant input from Credit Suisse.[102] On the other hand, Kim had no reason to believe his job was in jeopardy, nor was he involved in any alternate bid. This last factor is significant because neither this Court nor the Delaware Supreme Court ever has adopted a bright-line test under which management projections that were created during the merger process are deemed inherently unreliable. To the contrary, in a number of cases Delaware Courts have relied on projections that were prepared by management outside of the ordinary course of business and with the possibility of litigation.[103] On the other hand, this Court has expressed skepticism with respect to projections prepared with the benefit of hindsight by testifying experts.[104]

***12** Moreover, Bailey's "Cash Deployment Scenario," which assumes that Cogent would have spent $396 million on potential targets and realized positive returns as a result of those acquisitions, is too speculative. The record shows that even though Cogent was open to acquiring companies and had examined more than twenty companies, "none of them fit into [Cogent's] acquisition target."[105] Furthermore, even if I were to assume that Cogent would have made an acquisition, which I am not inclined to do, I would not be willing to speculate as to the rate of return on that hypothetical acquisition, because it would amount to nothing more than mere conjecture and supposition.

Similarly, the record does not support adopting Bailey's "Industry Growth Scenario," as opposed to management's projections.[106] In his scenario, Bailey used industry growth rates to assume a compound annual growth rate ("CAGR") through 2015 of 17%, while the CAGR implicit in management's projections over the same period was only 12.1%. Notably, from 2006 to 2009, Cogent fell far short of industry growth rates in the biometrics industry.[107] Similarly, in 2010, management projected Cogent's revenues to grow by 8% (from $129.6 million in 2009 to $140 million in 2010).[108] In the first three quarters of 2010, however, Cogent had earned only $78.2 million in revenues.[109] If Cogent had maintained that pace for the final quarter of 2010, Cogent's 2010 revenues would have been just $104.3 million,[110] resulting in negative year-on-year revenue growth between 2009 and 2010.

Based on the evidence adduced at trial, Delaware's long-standing preference for management projections, and the absence of any persuasive evidence that Kim was at risk of losing his job, involved in another bid, or entangled in other extraordinary circumstances, I accept management's projections here as a reliable starting point for the DCF analysis in this case.

a. Free cash flow adjustments

In their respective DCF analyses, both Bailey and Owsley made adjustments to the free cash flows. First, Owsley deducted share based compensation ("SBC") from Cogent's projected cash flows, whereas Bailey did not. And second, Owsley increased working capital based on an assumption that Cogent would have working capital equal to 32.2% of revenues. Bailey, on the other hand, assumed that Cogent would need to retain only 22.9% of its incremental revenues as working capital. I examine each of those proposed adjustments next.

i. Treatment of SBC

Questions about the treatment of SBC often arise in this Court when fairness opinions fail to disclose whether the individual or entity rendering the opinion treated SBC as a non-cash expense in its DCF analysis. In those cases, the Court's standard practice has been to treat SBC as a non-cash expense.[111] Valuation literature also supports the view that a non-qualified stock option plan[112] is cash neutral or cash flow positive.[113]

***13** Respondent's authority to the contrary is inapposite. 3M Cogent relies on a blog post by Damodaran that states, "It is absurd to add back stock-based compensation (it is an operating expense ...)."[114] That blog post, however, deals with the reporting of operating income, not the appropriate treatment of SBC for cash flow purposes.[115] I agree with Damodaran that it makes sense to adjust earnings to take into account the dilutive effect of SBC. Respondent has made no showing in this case, however, that SBC will have any effect on the actual cash flows of the Company. Therefore, I conclude that SBC should not be treated as a cash expense here.[116]

ii. Working capital adjustment

"Working capital is derived by subtracting current liabilities from current assets and represents the capital the business has at its disposal to fund operations."[117] Both Petitioners and Respondent included in their revenue categories —*i.e.,* current assets—"billed accounts receivable," "unbilled accounts receivable," and "inventory and contracted related costs." They both also included in their liabilities category —*i.e.,* current liabilities—"accounts payable." The parties disagreed, however, as to the proper treatment of the following asset and liability categories for purposes of their working capital adjustment: "prepaid expenses," "long-term inventory and contracted related costs," "accrued expenses," and "other liabilities."

The Gordian Experts criticized Bailey for including those accounts in his computation of working capital, describing them as "long-term" accounts and "subject to random movement."[118] At least one treatise, however, supports Bailey's view that working capital should include the disputed categories. That treatise states:

> Operating working capital equals operating current assets minus operating current liabilities. Operating current assets comprise all current assets necessary for the operation

> of the business, including working cash balances, trade accounts receivable, inventory, and prepaid expenses. Specifically excluded are excess cash and marketable securities—that is cash greater than the operating needs of the business. Excess cash represents temporary imbalances in the company's cash position....
>
> Operating current liabilities include those liabilities that are related to ongoing operations of the firm. The most common operating liabilities are those related to suppliers (accounts payable), employees (accrued salaries), customers (deferred revenue), and the government (income taxes payable).[119]

Rather than relying on any professional or academic valuation literature, the Gordian Experts characterize their position as a "judgment" based on their "experience in looking at many companies and many projections."[120]

***14** Bailey's approach appears to be well supported and generally accepted by the financial community.[121] The explanation proffered by the Gordian Experts for their approach, on the other hand, was essentially conclusory. Based on the strong support for his view, I adopt Bailey's approach and assume that Cogent will need working capital equal to 22.9% of incremental revenues.

b. Unlevered free cash flows

The following table reflects the projections of unlevered free cash flows that the Court intends to use in conducting a DCF analysis here. These projections incorporate the SBC and working capital adjustments discussed above.

Tabular or Graphical Material not displayable at this time

The preceding image contains the reference for footnote[122].

2. Cogent's cost of capital

To discount the cash flow projections for the Company to present value, the experts for both sides computed their respective weighted average costs of capital ("WACC"). The formula used to derive WACC is:

$$WACC = [K_D \times W_D \times (1 - t)] + (K_E \times W_E)$$ [123]

Where K_D = Cost of debt capital

W_D = Average weight of debt in capital structure

t = Effective tax rate for the company

K_E = Cost of equity capital

W_E = Average weight of equity capital in capital structure

Where the capital structure is 100% equity and 0% debt, as is the case here, WACC is equal to the cost of equity.[124] To calculate the cost of equity capital, the experts for both Petitioners and Respondent used the Capital Asset Pricing Model, or CAPM, which can be expressed as:

$$K_E = R_F + (\beta \times R_{ERP}) + R_{ESP}$$ [125]

Where K_E = Cost of equity

R_F = Risk-free rate

β = Beta

R_{ERP} = Equity risk premium

R_{ESP} = Equity size premium

In simpler terms, the cost of equity equals the risk-free rate plus an equity size premium plus the company's beta times the market risk premium.

***15** The following table summarizes the parties' respective inputs for WACC or cost of equity:

Tabular or Graphical Material not displayable at this time

In the sections that follow, I discuss, in turn, the disputes between the parties as to each of the listed variables.

a. Risk-free rate

Petitioners determined Cogent's risk-free rate using the 20–year Treasury bond yield, which was 3.80% on November 30, 2010, whereas 3M Cogent used the 10–year Treasury bond yield, which was approximately 2.96% on December 1, 2010.[126] Both sides acknowledged that either the 10–year or

20–year Treasury bond yields would be appropriate metrics for the risk-free rate.[127]

In the appraisal context, this Court has used the 20–year Treasury bond yield on numerous occasions in its calculation of the risk-free rate.[128] It does not appear from these cases, however, that the issue of a 10–year versus a 20–year bond was disputed or that the Court based its use of a twenty-year rate on professional or academic valuation literature. To the contrary, the literature suggests that the 10–year Treasury bond yield is the appropriate metric for the risk-free rate in this case. For example, Damodaran states, "we believe that using the 10–year bond as the risk-free rate on all cash flows is a good practice in valuation, at least in mature markets."[129] Another well-known treatise on valuation also suggests a 10–year time horizon.[130] And, yet another source states: "[m]any analysts use the yield on a 10–year [Treasury bond] as a proxy for the risk-free rate, although the yields on a 20–year or 30–year [Treasury bond] are also reasonable proxies."[131] Based on the referenced literature and the fact that Cogent is a mature firm—as evidenced by its history of positive cash flows—I conclude that the 10–year Treasury bond yield, *i.e.,* 2.96%, espoused by Respondent is the appropriate metric for the risk-free rate in this case.

b. Beta

***16** As a matter of valuation theory, "companies that are more unstable and leveraged, less established and financially and competitively secure, and in colloquial terms 'riskier,' should have higher betas."[132] Betas also can take into account considerations like political risk to the extent such risks are priced by the market.[133] The experts' calculations of beta diverge in significant respects and are the largest driver of the price difference in their respective DCF calculations. Petitioners advocate for a beta of 0.87, while Respondent espouses a much higher beta of 1.52.[134] In this regard, the parties clash over three main topics: (1) whether to use a 1–year Bloomberg weekly raw beta or a 2–year Bloomberg weekly adjusted beta; (2) the order of operations; and (3) whether to adjust for all cash or only excess cash.

The first issue is whether the Court should start with Bailey's 1–year Bloomberg weekly raw beta of 0.708 or the Gordian Experts' 2–year Bloomberg weekly adjusted beta of 0.67.[135] At this point, the experts agree that the Court should use an observation period of one week. They differ, however, as to the sample period and whether the beta should be adjusted or raw.[136] Bailey explained that he chose a 1–year sample period to avoid the "significant noise associated with movements in the market due to the impact of the Global Financial Crisis through the period late 2007 through early 2009."[137] Owsley, on the other hand, provided no explanation of the reasons for his selection of a 2–year sample period. Accordingly, I adopt Bailey's selection of a 1–year sample period for this case.

Turning to what I have referred to as the "order of operations" issue, both Petitioners and Respondent agree that it is necessary to adjust the beta of Cogent to reflect Cogent's large cash position. To do that, Bailey cash adjusted the Bloomberg raw beta. In contrast, the Gordian Experts cash adjusted the Bloomberg adjusted beta, which is equal to (*Raw Beta x* 0.67) + [1.00 × (0.33)]. In this context, it strikes me as inappropriate to cash adjust a market-adjusted beta because it effectively cash adjusts the market. Accordingly, I conclude that the appropriate number to begin the development of beta with is the 1–year Bloomberg weekly raw beta, *i.e.,* 0.708.

The process for adjusting asset beta estimates for excess cash and investments is outlined by Pratt and Grabowski:

> The assets of the guideline public companies used in estimating beta often include excess cash and marketable securities. If you do not take into account the excess cash and marketable securities, you can arrive at an incorrect estimate of the asset beta for the operating business. This will lead to an incorrect estimate of the beta for the subject company. After unlevering the beta for the guideline public companies, you adjust the unlevered beta estimates for any excess cash or marketable securities held by each guideline public company. This adjustment is based on the principle that the beta of the overall company is the market-value weighted average of the

> businesses or assets (including excess cash) comprising the overall firm.[138]

The formula for that adjustment is as follows:

***17** β_U *or overall company unlevered or asset beta*

$$= [\textit{Asset beta for operations} \times (\textit{Operating Assets}/\textit{Total Assets})]$$

$$+ [\textit{Asset beta for surplus assets} \times (\textit{Surplus Assets}/\textit{Total Assets})]$$

If we assume that cash has a beta of zero,[139] the equation is simply:

$$\beta_U = \textit{Asset beta for operations} \times (\textit{Operating Assets}/\textit{Total Assets})$$

That equation can be restated as:

$$\textit{Asset beta for operations} = \beta_U \times (\textit{Total Assets}/\textit{Operating Assets})$$

Here, Cogent's total assets were approximately $868.7 million.[140] Operating assets are calculated using the following formula:

$$\textit{Operating assets} = \textit{total assets} - \textit{surplus assets}$$

Predictably, the parties disagree as to what proportion of Cogent's large cash reserves should be considered “surplus.” Bailey treats approximately $100 million as surplus, whereas the Gordian Experts consider all of Cogent's cash, *i.e.,* $533.2 million, to be excess. At the very least, the parties agree that the $100 million the Cogent board announced it would use to execute a share buyback is excess cash. As for the remaining $433.2 million in cash, Bailey asserts that it should be treated as an operational asset because Cogent's executives signaled “to the market that Cogent intended to utilize their cash balance to support the operations of the business in order to take advantage of the significant growth opportunities in the marketplace.”[141] Yet, that view of surplus cash contradicts the Pratt and Grabowski treatise upon which Bailey explicitly relied. Pratt and Grabowski define surplus assets as “[a]ssets that could be sold or distributed without impairing company operations.”[142] Using that broader view and a simplifying assumption that Cogent would need $50 million in maintenance cash for operations,[143] its excess cash would be $483.2 million.[144] The operational assets of Cogent then would be just $385.5 million.[145] Thus, the ratio of total assets to operating assets would be 2.253.[146] Applying previously mentioned formula, the asset beta for operations equals the overall company unlevered or asset beta (0.708) times the ratio of total assets to operating assets (2.253) or 1.595.

***18** Empirical studies have shown that measures of risk, including beta, “tend to revert towards the mean over time.”[147] Where a good set of comparables for industry betas do not exist, one can “smooth” beta by adjusting historical beta by a market beta of 1, using a 1/3 weighting factor for the market and a 2/3 weighting for the subject company's beta, in this case Cogent.[148] Here, that would result in a forward estimated beta of approximately 1.397.[149]

The Respondent also calculated beta using a peer group method, *i.e.,* a comparable companies analysis. For the reasons stated in subsection C above, I do not find the Gordian Experts' comparable companies analysis reliable. Accordingly, I rely solely on my calculation of a Cogent forward beta of 1.397 for purposes of determining the appropriate WACC here.

c. Equity risk premium

There is very little difference between the parties as to the appropriate equity risk premium. Bailey supports the use of a supply-side equity risk premium of 5.0% as published in the 2010 Ibbotson yearbook.[150] The Gordian Experts relied on a 5.2% equity risk premium, which they derived from multiple sources, including Damodaran and Ibbotson.[151]

Bailey cited a number of treatises and articles in support of his view that the Court should apply a supply-side equity risk premium.[152] Owsley's report, on the other hand, did not explain how he calculated equity risk premium (beyond identifying sources).[153] In addition, Schiller testified that he was unfamiliar with the distinction between a supply-side equity risk premium and a historic equity risk premium.[154]

Because Bailey demonstrated a stronger understanding of this subject and explained his methodology more convincingly, I conclude that the 5.20% equity risk premium used by Bailey is the appropriate value to use in this case.[155]

d. Equity size premium

***19** "In addition to the equity risk premium, an equity size premium generally is added to the company's cost of equity in the valuation of smaller companies to account for the higher rate of return demanded by investors to compensate for the greater risk associated with small company equity."[156] "A size premium is an accepted part of CAPM because there is evidence in empirical returns that investors demand a premium for the extra risk of smaller companies."[157] The opposing experts came to similar values in their determination of an equity size premium: 1.73% for Petitioners and 2.0% for Respondent.[158]

Bailey selected his equity size premium of 1.73% based on decile 7 of Ibbotson Associates' ("Ibbotson") 2010 yearbook, which encompasses companies with a market capitalization between $685,129,000 and $1,063,308,000.[159] The Gordian Experts, on the other hand, used Ibbotson's 2009 yearbook and adjusted Cogent's market capitalization to exclude its large cash reserves.

The Ibbotson table headings clearly state "market capitalization."[160] In addition, the relevant treatises focus on the market value of common equity and do not suggest making an adjustment to exclude cash reserves.[161] Consistent with Ibbotson's headings and the treatises, the Court of Chancery consistently has used market capitalization as the benchmark for selecting the equity size premium.[162]

Despite those authorities and Schiller's awareness that "the definition [for equity size premium] says market capitalization," the Gordian Experts chose a size premium by "look[ing] at the size of the market value less cash of Cogent."[163] That adjustment was based on Schiller's view that

> ***20** we're valuing ... Cogent absent its cash. We're not valuing Cogent in the DCF. Because the way the DCF works is, we value the cash streams the company throws off and then we add the cash on top of it. So we split the baby in two parts and look at the values of each.[164]

I am not persuaded, however, that Schiller's approach is consistent with the proper use of the Ibbotson tables. The Ibbotson tables were based on important research in 1981 by Rolf Banz, who found an empirical relationship between the *market value* of stocks and higher rates of return.[165] Put differently, the Ibbotson tables look at the statistical relationship between market capitalization and equity size premium. The Gordian Experts failed to present a convincing explanation as to why their use of a different metric—enterprise value—more accurately reflects the correlation that the equity size premium attempts to reflect.

While some studies—notably the Duff & Phelps *Risk Premium Report*[166]—use a metric other than the market value of equity, Respondent's expert chose to use Ibbotson's Valuation Yearbook. In doing so, they effectively embraced the view that there is a relationship between market capitalization and rate of return.

Finally, the Gordian Experts' exclusion of cash is counterintuitive. The Ibbotson tables are based on the insight that smaller companies are more risky than larger companies. The Gordian Experts' exclusion of cash decreases the "size" of the company involved, thereby increasing its equity size premium. Here, that would mean that Cogent would be more risky as a result of its cash reserves. Intuitively, however, one would expect that, all other things being equal, having cash reserves, as opposed to debt, would decrease the riskiness of a company.

For all of these reasons, I adopt Bailey's selection of an equity size premium of 1.73%.

e. Calculating Cogent's WACC

As previously discussed, the equation for CAPM is:

$$K_E = R_F + (\beta \times R_{ERP}) + R_{ESP}$$

Inputting my conclusions as to the risk-free rate, beta, equity risk premium, and equity size premium into that equation yields:

$$K_E = 2.96 + (1.397 \times 5.2) + 1.73 = 11.954\%$$

Based on Cogent's capital structure of 100% equity, Cogent's WACC would equal its cost of equity, or 11.954%.

f. The present value of Cogent's unlevered free cash flows

Using the WACC of 11.954%, the following table represents the present value ("PV"), as of the Merger date, of Cogent's five-year projected unlevered free cash flows:

***21** Tabular or Graphical Material not displayable at this time

The sum of the present value of the cash flows for 2010–2015 is $42 million.

3. Terminal value

"In a DCF analysis, future cash flows are projected for each year during a set period, typically five years. After that time, a terminal value is calculated to predict the company's cash flow into perpetuity."[167] "The two established methods for computing terminal value are the exit multiples model (a market approach) and the growth in perpetuity model [*i.e.,* the Gordon Growth Model]."[168] "Both approaches have been accepted by this court in the past."[169]

Both Bailey and the Gordian Experts estimated the terminal value of Cogent based on the perpetuity growth model or the Gordon Growth Model. The Gordian Experts also used an exit multiples approach that estimated a terminal value based on the multiples of enterprise value to estimated forward 2011 EBITDA for the set of comparable companies.[170]

a. The Gordon Growth Model

The Gordon Growth Model can be expressed as follows[171]:

$TV = {}^{\text{FCFt+1}}/_{\text{WACC - g}}$

TV = Terminal value

FCF_{t+1} = Free cash flow in the first year after the explicit forecast period

$WACC$ = Weighted average cost of capital

g = Expected growth rate of free cash flow into perpetuity

To calculate terminal value using the Gordon Growth Model, the Court must select a long-term growth rate, *i.e.,* the expected growth rate of free cash flows into perpetuity. "A viable company should grow at least at the rate of inflation and ... the rate of inflation is the floor for a terminal value estimate for a solidly profitable company that does not have an identifiable risk of insolvency."[172] But, a terminal growth rate should not be greater than the nominal growth rate for the United States economy, because "[i]f a company is assumed to grow at a higher rate indefinitely, its cash flow would eventually exceed America's [gross national product]."[173]

Relying on historical GDP and inflation data, economic analysts projections, and the growth prospects of the biometrics industry, Bailey selected a perpetuity growth rate of 4.5%.[174] The Gordian Experts, on the other hand, used a range of growth rates between 2% and 5%, and implicitly selected the midpoint of 3.5%.[175] The Gordian Experts, however, provided no analysis or explanation in support of the number they chose for the terminal growth rate.[176] Because Bailey was the only expert who sought to justify his conclusion, and his conclusion is within the range of rates identified by Respondent's expert and appears to be reasonable based on the evidence, I adopt Bailey's estimate of a 4.5% perpetuity growth rate.

***22** The parties also disagree as to whether the Court should use a two-stage or a three-stage DCF model. The Gordian Experts used a two-stage model whereby, at the end of the management projections in 2015, they estimated a single percentage figure that they would use as a proxy for Cogent's perpetual rate of growth beyond that period. Bailey, on the other hand, "gradually step[ped] down Cogent's growth rate using a linear progression over the period from 2016 through the terminal year, 2021," before applying his terminal growth percentage.[177]

"As a general matter, neither approach is inherently preferable."[178] Damodaran notes, however, that the two-stage model "is best suited for firms that are in high growth and expect to maintain that growth rate for a specific time period, after which the sources of the high growth are expected to disappear."[179] Damodaran provides two examples where this might apply:

> One scenario ... is when a company has patent rights to a very profitable product for the next few years and is expected to enjoy supernormal growth during this period. Once the patent expires, it is expected to settle back into stable growth. Another scenario where it may be reasonable to make this assumption about growth is when a firm is in an industry that is enjoying super-normal growth, because there are significant barriers to entry (either legal or as a consequence of infrastructure requirements), which can be expected to keep new entrants out for several years.[180]

The three-stage model, on the other hand, "is the most general of the models because it does not impose any restrictions on the payout ratio. This model assumes an initial period of stable high growth, a second period of declining growth, and a third period of stable low growth that lasts forever."[181] Damodaran notes that the three-stage model is best suited "for a firm whose earnings are growing at very high rates, are expected to continue growing at those rates for an initial period, but are expected to start declining gradually toward a stable rate as the firm become[s] large and loses its competitive advantages."[182]

Based on my assumptions, Cogent's earnings are expected to grow at a high rate of 11.45% for the initial period before moving to a stable growth rate of 4.5%.[183] I expect that decline will occur gradually as Cogent loses its competitive advantages in the field. Cogent is not in an industry where there are significant barriers that will disappear after 2015. Nor does Respondent identify any other reason to assume a precipitous drop-off. Accordingly, I believe that Bailey's three-stage model best reflects Cogent's expected growth over time and adopt that approach.

The following table represents my calculation of Cogent's unlevered free cash flow for the years 2016 through 2021, using a linear progression to step Cogent's growth rate down to 4.5% in 2021:

Tabular or Graphical Material not displayable at this time

Discounting those values back to the Merger Date using the WACC of 11.954% yields the following values:

Tabular or Graphical Material not displayable at this time

Thus, the sum of the present values of the cash flows for 2016–2020 is $111.5 million.

***23** Finally, using in the Gordon Growth Model equation for the third and final period, a WACC of 11.954%, a perpetuity growth rate of 4.5%, and free cash flows in 2021 of $64.4 million, I calculated Cogent's terminal value to be approximately $864 million.[184] Discounting that value using a WACC of 11.954% leads to a present value of the terminal value of $276.7 million.

b. EBITDA multiples

"Multiples approaches assume that a company will be worth some multiple of future earnings or book value in the continuing period."[185] "[A] good industry comparison is crucial if a multiplier methodology is employed."[186] Here, the Gordian Experts selected a terminal EBITDA multiple range of 6.5x to 8.5x using the companies in their comparable companies analysis. Petitioners seek to exclude Respondent's terminal multiples approach for many of the same reasons they asserted in opposition to Respondent's other market approaches. I agree with Petitioners' objections.

As discussed in Part II.C.1 *supra,* the comparable companies selected by the Gordian Experts are not sufficiently comparable to Cogent to support a reliable analysis and do not provide a good industry comparison. There are also serious evidentiary problems with Schiller's trial testimony on this subject.[187] As with the EBITDA multiples analysis of the comparable companies, here only four of the purportedly comparable companies have data from which to calculate an equity value to estimated forward EBITDA ratio.[188]

Furthermore, Owsley's report on this issue is internally inconsistent. At one point, the report states that its range of 6.5x to 8.5x is "based on ... 1st and 3rd quartile 2011 EBITDA multiples."[189] Elsewhere, the report indicates that the 1st and 3rd quartile 2011 EBITDA multiples were actually 7.5x to 9.8x.[190] At trial, Schiller defended the selection of multiples reflected in Owsley's report and described them as a "judgment call" or an "educated estimate based on what historical multiples have been adjusted for the sense that growth will have slowed to something much closer to GDP growth by that time."[191] Beyond that, however, the Gordian Experts did not provide any authorities or analysis to justify their use of an EBITDA multiples approach to determine terminal value.

For these reasons, I reject Respondent's use of terminal EBITDA multiples and instead rely solely on the Gordon Growth Model for my determination of terminal value.

4. DCF Valuation

The following table represents the Court's calculation of the valuation of Cogent using essentially Bailey's model, the aforementioned assumptions, and Cogent's cash balance of $533.2 million as of September 30, 2010[192]:

	($ millions)
PV of 2010–2015 Cash Flows	42.0
PV of 2016–2020 Cash Flows	111.5
PV of Terminal Value	276.7
Enterprise Value	430.2
Less: Net Debt	(533.2)
Equity Value	**963.4**

In sum, the equity value of Cogent as of the Merger Date was approximately $963.4 million. Assuming shares outstanding of approximately 88.6 million,[193] the price per share would be $10.87.[194]

E. Are Petitioners Entitled to Statutory Interest at the Legal Rate?

***24** Section 262(h) of the Delaware appraisal statute provides:

> Unless the Court in its discretion determines otherwise for good cause shown, interest from the effective date of the merger through the date of payment of the judgment shall be compounded quarterly and shall accrue at 5% over the Federal Reserve discount rate (including any surcharge) as established from time to time during the period between the effective date

> of the merger and the date of payment of the judgment.[195]

Nevertheless, "[a]dopting a different rate may be justified where it is necessary to avoid an inequitable result, such as where there has been improper delay or a bad faith assertion of valuation claims."[196]

Here, Respondent argues that this Court should not apply the statutory rate of interest because: (1) awarding prejudgment interest to shareholders who acquired shares after the announcement of the acquisition would be an inequitable result; and (2) Petitioners improperly delayed the resolution of this action.

1. Petitioners' post-merger acquisition of shares

3M Cogent emphasizes that Petitioners acquired shares after the Merger was announced. In such circumstances, Respondent contends, it would be inequitable to award interest at the legal rate because Delaware law disfavors the purchase of a lawsuit and statutory interest is not intended to benefit purchasers of after-acquired shares.

In *Salomon Brothers Inc. v. Interstate Bakeries Corp.,*[197] this Court addressed whether one who purchases stock after notice of a transaction is entitled to seek appraisal pursuant to 8 *Del. C.* § 262. The Court stated:

> I find nothing in the purpose or language of § 262 that would defeat [petitioner's] entitlement to an appraisal and I find nothing inequitable about an investor purchasing stock in a company after a merger has been announced with the thought that, if the merger is consummated on the announced terms, the investor may seek appraisal.[198]

In other words, Delaware law does not disfavor the purchase of shares after the announcement of a merger. Indeed, after the trial in *Salomon Brothers,* the Court awarded an 11% rate of interest to the petitioner.[199] As 3M Cogent correctly notes, however, the Court in *Salomon Brothers* did not address whether any reduction or elimination of prejudgment interest might be appropriate.

In support of denying Petitioners an award of statutory interest, Respondent avers that statutory interest was not intended to compensate shareholders who acquired their shares after the merger was announced. In *Cede & Co. v. Technicolor, Inc.,*[200] for example, the Delaware Supreme Court stated that "[t]he underlying assumption in an appraisal valuation is that the dissenting shareholders would be willing to maintain their investment position had the merger not occurred."[201] In the same vein, Respondent relies on cases that have recognized that the appraisal right was intended to protect "stockholders—who by reason of the statute lost their common law right to prevent a merger—by providing for the appraisement of their stock and the payment to them of the full value thereof in money."[202]

***25** I am mindful, however, that statutory interest also serves to avoid an undeserved windfall to the respondent in an appraisal action, who "would otherwise have had free use of money rightfully belonging to" the petitioners.[203] Even though a respondent may have been cash-rich, "the [respondent] derived a benefit from having the use of the [petitioners'] funds at no cost."[204]

In sum, the plain language of the appraisal statute calls for the payment of statutory interest unless the Court determines otherwise for good cause shown. Respondent, 3M Cogent, has not shown that it would be inequitable for Petitioners to receive the legal rate of interest for shares acquired after the merger.[205]

2. Petitioners' purported "delay"

Respondent next argues that the Court should refuse to award any interest for the period from April 28, 2011 to February 2, 2012 because Petitioners unreasonably delayed in prosecuting their case. Specifically, Respondent complains that Petitioners failed to respond in a timely manner to certain discovery requests, as well as to an inquiry by Respondent as to whether Petitioners intended to proceed with this case.

Petitioners counter that Respondent cannot complain about Petitioners' purported delay because Respondent itself failed to move with alacrity. On November 11, 2011, Petitioners proposed a schedule that called for a trial in April 2012. Notably, Respondent counter-offered, seeking a much later, October 2012 trial date. In January 2012, after extensive back-and-forth, I entered a stipulated scheduling order setting the trial for September 5 through 7, 2012. As a result of Owsley's unforeseen unavailability for medical reasons, I later postponed the trial until late November 2012.

For a case of this size and complexity, the trial was completed within a reasonable time period.[206] Even with some excusable delay, the trial was conducted within 20 months of the initial petition. Accordingly, I find that Respondent has not shown any unreasonable or improper delay and, therefore, deny Respondent's request to limit the award of interest on that basis.

III. CONCLUSION

***26** For the reasons discussed in this Memorandum Opinion, I find that the fair value of Cogent as of December 1, 2010 was $963.4 million or $10.87 per share.

The parties should confer to verify that the Court accurately has calculated Cogent's value based on the rulings herein and, assuming that it has, present a final judgment using an amount of $10.87 per share of Cogent, plus interest from December 1, 2010 to the date of the judgment at the statutory rate, compounded quarterly. Petitioners shall submit, on notice, a proposed form of final judgment within ten (10) business days.

All Citations

Not Reported in Atl. Rptr., 2013 WL 3793896

Footnotes

[1] “Biometrics” is defined as “the measurement and analysis of unique physical characteristics (as fingerprint or voice patterns) especially as a means of verifying personal identity.” Merriam–Webster's Collegiate Dictionary 124 (11th ed. 2004).

[2] Unless otherwise noted, the facts are drawn from the stipulated facts section of the parties' Joint Pre–Trial Order (Feb. 4, 2013).

[3] 3M Co., 2012 Annual Report (10–K) at 3 (Feb. 14, 2013), *available athttp://media.corporate-ir.net/media_files/irol/80/80574/Annual_Report2012.pdf.*

[4] Tr. 427 (Hsieh). References in this form are to the trial transcript. Where the identity of the testifying witness is not clear from the text, it is indicated parenthetically after the cited page of the transcript.

[5] *Id.*

[6] JX 122 at 3.

[7] Bolger Dep. 53–66; JX 157 at 17. In Cogent's proxy statement, NEC was “Company D,” Danaher was “Company G,” and Roper was “Company E.”

[8] JX 157 at 17.

[9] *Id.* at 18.

[10] JX 165. The Five–Year Projections include the latter part of 2010.

[11] Tr. 404–05(Kim).

[12] *Id.* at 389–90, 408–09.

[13] *Id.* at 395.

[14] JX 157 at 18–19.

[15] *Id.* at 19–20.

[16] *Id.* at 20.

[17] *Id.* at 20–21.

[18] JX 157 at 20–21.

[19] *Id.* at 20.

[20] *Id.* at 20–21.

[21] *Id.*

[22] *Id.* at 23.

[23] *Id.* The trading price at closing on the last trading day before the announcement of the merger was $8.92 per share.

[24] *See* JX 2 Ex. 1. Bailey holds a Ph.D. in management from Case Western Reserve University, an M.B.A. from George Washington University, an M.S. in engineering from University of California, Berkeley, and an M.S. in systems management from the University of Southern California. Bailey also is a U.S. Naval Academy graduate. *Id.*

[25] JX 1 app. A; JX 3 app. A. Gordian Group is a financial advisory firm specializing in complex capital raising and mergers and acquisitions activities, as well as the restructuring of financially distressed businesses. JX 1 app. A; JX 3 app. A.

[26] 8 *Del. C.* § 262. There is no dispute that Petitioners are entitled to an appraisal under Section 262.

[27] *Id.* § 262(h); *see also* *Tri–Cont'l Corp. v. Battye,* 74 A.2d 71, 72 (Del.1950) ("[M]arket value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or which could be ascertained as of the date of merger and which throw any light on future prospects of the merged corporation are not only pertinent to an inquiry as to the value of the dissenting stockholders' interest, but must be considered by the agency fixing the value.").

[28] *Golden Telecom, Inc. v. Global GT LP,* 11 A.3d 214, 217 (Del.2010).

[29] *Cede & Co. v. Technicolor, Inc.,* 684 A.2d 289, 299 (Del. 1996).

[30] *Golden Telecom, Inc.,* 11 A.3d at 217.

[31] *Weinberger v. UOP, Inc.,* 457 A.2d 701, 713 (Del.1983); *see also**Technicolor,* 684 A.2d at 299.

[32] *Rapid–American Corp. v. Harris,* 603 A.2d 796, 805 (Del. 1992).

[33] *M.G Bancorp., Inc. v. LeBeau,* 737 A.2d 513, 520 (Del. 1999).

[34] *Gonsalves v. Straight Arrow Publ'rs, Inc.,* 701 A.2d 357, 362 (Del.1997); *Taylor v. Am. Specialty Retailing Gp.,* 2003 WL 21753752, at *2 (Del. Ch. July 25, 2003).

[35] *Weinberger,* 457 A.2d at 713.

[36] *See**Dobler v. Montgomery Cellular Hldg. Co.,* 2004 WL 2271592, at *8 (Oct. 4, 2004); *see also Cede & Co. v. JRC Acq. Corp.,*2004 WL 286963, at *2 (Del. Ch. Feb. 10, 2004) (utilizing the DCF approach); *Gentile v. Singlepoint Fin., Inc.,* 2003 WL 1240504, at *6 (Del. Ch. Mar. 5, 2003) (utilizing the comparable transactions approach); *Borruso v. Commc'ns Telesystems Int'l,* 753 A.2d 451, 455 (Del. Ch.1999) (utilizing the comparable company approach).

[37] *Highfields Capital, Ltd. v. AXA Fin., Inc.,* 939 A.2d 34, 42 (Del. Ch.2007) ("If ... the transaction giving rise to the appraisal resulted from an arm's-length process between two independent parties, and if no structural impediments existed that might materially distort 'the crucible of objective market reality,' a reviewing court should give substantial evidentiary weight to the merger price as an indicator of fair value."); *Union Illinois 1995 Inv. Ltd. P'ship v. Union Fin. Gp., Ltd.,* 847 A.2d 340, 357 (Del. Ch.2004) ("[O]ur case law recognizes that when there is an open opportunity to buy a company, the resulting market price is reliable evidence of fair value."); *Van de Walle v. Unimation, Inc.,* 1991 WL 29303, at *17–18 (Del. Ch. Mar. 7, 1991) ("The most persuasive evidence of the fairness of the ... merger price is that it was the result of arm's-length negotiations between two independent parties, where the seller ... was motivated to seek the highest available price, and a diligent and extensive canvass of the market had confirmed that no better price was available.").

[38] 11 A.3d 214 (Del. 2010).

[39] *Id.* at 217–18.

[40] *In re Orchard Enters., Inc.,* 2012 WL 2923305, at *5 (Del. Ch. July 18, 2012) (citing *Cavalier Oil Corp. v. Harnett,* 564 A.2d 1137 (Del. 1989)), *aff'd,*2013 WL 1282001 (Del. 2013) (ORDER).

[41] *See* JX 1 at 33, Ex. 13.

[42] *Weinberger v. UOP, Inc.,* 457 A.2d 701, 713 (Del. 1983).

43 *Muoio & Co. v. Hallmark Entm't Invs. Co.,* 2011 WL 863007, at *20 (Del. Ch. Mar. 9, 2011), *aff'd,*35 A.3d 419, 2011 WL 6396487 (Del. 2011) (ORDER).

44 *In re Orchard Enters., Inc.,* 2012 WL 2923305, at *9 (Del. Ch. July 18, 2012).

45 *Id.*

46 *Id.*

47 *Andaloro v. PFPC Worldwide, Inc.,* 2005 WL 2045640, at *16 (Del. Ch. Aug. 19, 2005) (citing *Agranoff v. Miller,* 791 A.2d 880, 892 (Del. Ch. 2001)).

48 JX 1 at 17–18, 66–78.

49 Pet'rs' Opening Br. 40.

50 *ONTI, Inc. v. Integra Bank,* 751 A.2d 904, 916 (Del. Ch. 1999).

51 Those companies are (1) Authentec, Inc., (2) Aware, Inc., (3) BgenuineTec, (4) BIO–Key International, Inc., (5) Intellicheck Mobilisa, Inc., and (6) Precise Biometrics.

52 *See* JX 1 app. G at 69.

53 *See, e.g., In re PNB Hldg Co. S'holders Litig.,*2006 WL 2403999, at *25 n.125 (Del. Ch. Aug. 18, 2006) (rejecting comparable companies analysis where the "comparable publicly-traded companies all were significantly larger than [the subject company], with one having total assets of $587 million as compared to [the subject company's] assets of $216 million"); *Gilbert v. MPM Enters., Inc.,* 709 A.2d 663, 672 (Del. Ch. 1997) (stating that comparable companies whose "median asset value ... was nearly three times that of [the appraised company]" had "unreasonably skewed the results of this analysis"), *aff'd,*731 A.2d 790 (Del. 1999); *Rosenblatt v. Getty Oil Co,* 1983 WL 8936, at *26 (Del. Ch. Sept. 19, 1983) (rejecting analysis that used "smaller oil and gas producing companies as opposed to a major integrated company such as [the appraised company]"), *aff'd,*493 A.2d 929 (Del. 1985).

54 *See* Tr. 227–28 (Bailey).

55 *See* JX 1 at 70.

56 Tr. 598.

57 Tr. 427 (Hsieh).

58 Tr. 599 (Schiller). This comment applies to six of Respondent's ten comparable companies.

59 Tr. 615 (Schiller) ("Q. So half of your entire comparable companies analysis is based on companies which do no biometrics business at all; is that right? A. Yes. And as we have discussed, we judged that they were businesses that people would look at in a similar way to biometrics businesses.").

60 JX 4 at 8.

61 Tr. 102–03 (Bailey).

62 Tr. 604 (Schiller).

63 *Id.*

64 *Id.* at 607–08; JX 152.

65 *Highfields Capital, Ltd. v. AXA Fin., Inc.,* 939 A.2d 34, 54 (Del. Ch. 2007) (citing *In re U.S. Cellular Operating Co.,* 2005 WL 43994, at *17 (Del. Ch. Jan. 6, 2005)).

66 *Id.* (quoting *In re U.S. Cellular Operating Co.,* 2005 WL 43994, at *17).

67 JX 1 app. H.

68 JX 1 at 22.

69 *Id.*

70 Bailey did not challenge Respondent's 20% discount. Based on that implied acceptance, and this Court's previous observation that because "merger and acquisition data undoubtedly contains post-merger value, such as synergies with the acquiror, that must be excluded from appraisal value," it appears that some discount would be appropriate. *SeeKleinwort Benson Ltd. v. Silgan Corp.,* 1995 WL 376911, at *4 (Del. Ch. June 15, 1995).

71 Tr. 242 (Bailey).

72 Expert Report of Henry Owsley, *In re Sponsion Inc.,* No. 09–10690, 2009 WL 8179260, at ¶ 46 (D. Del. Bank. 2009).

[73] Tr. 534 (Schiller).

[74] *See**In re John Q. Hammons Hotels Inc. S'holder Litig.,* 2011 WL 227634, at *5 (Del. Ch. Jan. 14, 2011) ("[C]omparable transactions analysis was based on a set of only five transactions, which is too small a sample set in the circumstances of this case to draw meaningful conclusions."); *In re U.S. Cellular Operating Co.,* 2005 WL 43994, at *18 (Del. Ch. Jan. 6, 2005) ("Indeed, with that in mind, the Court found only two of the twenty transactions Harris identified actually to be comparable. Therefore, Petitioners and Harris have failed to persuade me that their approach, based on the price per subscriber acquired, is sufficiently reliable that it should be used instead of Sanders' more established approach."). *But see id.* at *18–19 (relying on an analysis of only five comparable transactions).

[75] Shannon Pratt, *Valuing a Business: The Analysis and Appraisal of Closely Held Companies* 321 (5th ed. 2008).

[76] *Id.* at 322.

[77] Tr. 250–52 (Bailey).

[78] *Id.*; JX 4 at 15.

[79] D.R.E. 702 provides in pertinent part: "... a witness qualified as an expert by knowledge, skill, experience, training or education may testify thereto in the form of an opinion or otherwise, if (1) the testimony is based upon sufficient facts or data...." D.R.E. 705(b) states that "An adverse party may object to the testimony of an expert on the ground that the expert does not have a sufficient basis for expressing an opinion."

[80] *Pennsylvania Brandt v. Rokeby Realty Co.,* 2005 WL 1654362, at *5 (Del. Super. May 9, 2005) (quoting *Primavera v. Celotex Corp.,* 608 A.2d 515, 521 (Pa.Super.Ct.1992)).

[81] *IQ Hldgs., Inc. v. Am. Comm. Lines Inc.,* 2012 WL 3877790, at *1 (Del. Ch. Aug. 30, 2012) ("For an expert to create a new analysis or materially change his opinions after the expert discovery cutoff risks trial by surprise and deprives the opposing party of an orderly process in which to confront and respond to the expert's views. Equally important, a new or materially changed analysis imposes burdens on the Court, which must attempt to evaluate the expert's opinions without the full benefits of adversarial testing.").

[82] Tr. 488 (Schiller).

[83] *Id.* at 488–89, 494.

[84] *Id.* at 489–92.

[85] *Id.*

[86] *Id.* at 493; JX 3.

[87] JX 179 at 42.

[88] *Id.* at 44 ("Q. Is that one of the factors that was applied to identify companies, the fact that companies are government contractors? A. I believe it was, but I was not part of the team that selected these. Certainly exposure to government contracting would have struck [ ] me as an interesting metric."); *id.* at 45 ("Q. ... [I]s it the case your team identified those as comparables because their customers include the government? A. As I said, I wasn't part of the team that selected these, so I can't speculate.").

[89] *See, e.g.,id.* at 45 ("Q. ... Do you know what portion of Intellicheck's business is in the biometrics industry? A. I do not."); *id.* at 46 ("Q. ... Do you have an understanding of what portion of VASCO's business was in the biometrics industry? A. I do not").

[90] Tr. 494.

[91] *See* JX 179 at 50 (from the deposition: "Q: Credit Suisse identified Verint Systems as a comparable company. Are you of the view that Verint Systems is not an appropriate comparable for Cogent? A: I don't have a view. I don't know Verint."); Tr. 526 (from trial: "Q: .... Why did you think Verint was not a good comparable? A. Verint would have made the cut but for the fact that they had trouble filing financial statements upon which one could rely. They had had, as I recall, a stock compensation challenge a number of years before, and they were still trying to get their house in order from an accounting perspective. We made the judgment that we should not put it in if it doesn't have numbers upon which we can rely."); *see also* Pet'rs' Opening Br. apps. A, B.

[92] *See**In re Orchard Enters., Inc.,* 2012 WL 2923305, at *12 (Del. Ch. July 18, 2012) (citing Richard Brealey, Stewart Myers & Franklin Allen, *Principles of Corporate Finance* 102 (9th ed. 2008); Bradford Cornell,

Corporate Valuation: Tools for Effective Appraisal and Decision Making 102 (1993); R. Franklin Balotti & Jesse Finkelstein, 1 *The Delaware Law of Corporations & Business Organizations* § 9.45[B][1], at 9–134 (3d ed. 2009)); *see also**Andaloro v. PFPC Worldwide, Inc.,* 2005 WL 2045640, at *9 (Del. Ch. Aug. 19, 2005).

[93] *Andaloro,* 2005 WL 2045640, at *9.

[94] *In re Orchard Enters., Inc.,* 2012 WL 2923305, at *12.

[95] *See* JX 2.

[96] *See**Doft & Co. v.* Travelocity.com *Inc.,* 2004 WL 1152338, at *5 (Del. Ch. May 20, 2004); *see also**Cede & Co. v. Technicolor, Inc.,* 2003 WL 23700218, at *7 (Del. Ch. Dec. 31, 2003) ("When management projections are made in the ordinary course of business, they are generally deemed reliable."), *aff'd in part, rev'd in part,*884 A.2d 26 (Del.2005).

[97] 2012 WL 1569818 (Del. Ch. Apr. 30, 2012).

[98] *Id.* at *5; *see also* *Technicolor,*2003 WL 23700218, at *7 ("[P]ost hoc, litigation-driven forecasts have an 'untenably high' probability of containing 'hindsight bias and other cognitive distortions.' ").

[99] *Gearreald,* 2012 WL 1569818, at *5.

[100] Tr. 405–06(Kim) ("Q. Prior to June 2010, Cogent never developed a multiyear financial model like the management projections through 2015 that Cogent disclosed in its proxy statement; right? A. I don't believe so.").

[101] JX 140 at 0002722 ("Ventura [*i.e.,* Cogent] says they turned down other offer[s] @ $11; however, if 3M hits the bid—they will sell."); Tr. 63–64 (Copman) ("Q. All right. Isn't it a fact that Cogent prepared its five year projections as part of the sales process specifically in part because 3M asked them to do so? A. We asked them to do that and they did prepare it."); *id.* at 67 ("Q. ... When Mr. Hsieh communicated to you at some point that he was looking for $11 a share, that's a data point and you would have no reason to make an offer above $11 a share; right? A. Most likely not.").

[102] Tr. 409 (Kim) ("Q. There was a back and forth, though, between you and Credit Suisse where Credit Suisse would ask questions and you would ask questions. It was a process where you worked together; right? A. Yes.").

[103] *See, e.g.,**Gilbert v. MPM Enters., Inc.,* 709 A.2d 663, 669–70 (Del. Ch. 1997), *aff'd,*731 A.2d 790 (Del. 1999) ("Petitioner asserts that the April forecast was prepared in anticipation of the merger and implies that the upcoming merger provided some reason for management deliberately to cut anticipated revenue growth and to increase [research and development] expenses.... I conclude that management was in the best position to forecast MPM's future before the merger, and finding no evidence that the April forecast included benefits to be obtained via the merger or that the April forecast represented a deliberate attempt to falsify MPM's projected revenues and expenses, I accept management's projections with minor changes to reflect MPM's actual financial results and other financial information obtained after the preparation of the projections, but before the merger."); *Union Ill. 1995 Inv. Ltd. P'ship v. Union Fin. Gp., Ltd.,* 847 A.2d 340, 350–51 (Del. Ch. 2004) (accepting management projections prepared "[d]uring the course of the sales process"); *In re Orchard Enters., Inc.,* 2012 WL 2923305, at *13 (Del. Ch. July 18, 2012) ("I adopt the fairness opinion projections because they were prepared closest to the Going Private Merger and they are therefore the best indicator of Orchard management's then-current estimates and judgments."); *Gray v. Cytokine Pharmasciences, Inc.,* 2002 WL 853549, at *4–5, *8 (Del. Ch. Apr. 25, 2002) (disregarding "litigation-driven projections" prepared by petitioner's expert in favor of projections prepared by management while an offer was pending and the company was exploring merger opportunities).

[104] *See Cede & Co. v. JRC Acq. Corp.,*2004 WL 286963, at *2 (Del. Ch. Feb. 10, 2004) ("[T]his Court prefers valuations based on management projections available as of the date of the merger and holds a healthy skepticism for post-merger adjustments to management projections or the creation of new projections entirely. Expert valuations that disregard contemporaneous management projections are sometimes completely discounted.").

[105] Tr. 437–39 (Hsieh).

[106] *See*Harris v. Rapid–American Corp., 1990 WL 146488, at *7 (Del. Ch. Oct. 2, 1990) (rejecting analysis based on "general trends" such as "industry-wide growth rates"), *aff'd in part, rev'd in part,*603 A.2d 796 (Del. 1992); *Cede & Co. v. Technicolor, Inc.,* 2003 WL 23700218, at *3 (Del. Ch. Dec. 31, 2003) (finding it unreasonable to reject management's forecast and create "hindsight forecasts based upon the industry as a whole").

[107] JX 3 ¶ 15 ("For instance, the CAGR in the biometric industry from 2006 to 2009 was 29%. By contrast, Cogent's CAGR in revenue for the same period was 8.4%.").

[108] JX 165 at 6.

[109] JX 153 at 2. Revenues for the first three quarters of 2009 had been $91.7 million. *Id.*

[110] $78.2 × $^4/_3$ = $104.3

[111] *See, e.g.,In re Celera Corp. S'holder Litig.,* 2012 WL 1020471, at *19 (Del. Ch. Mar. 23, 2012) (describing the assumption that the company's "stock-based compensation should be treated as a cash expense for purposes of its [DCF] analysis" as unusual (alteration in original)), *aff'd in part, rev'd in part,*59 A.3d 418 (Del.2012); *In re 3Com S'holders Litig.,* 2009 WL 5173804, at *3 (Del. Ch. Dec. 18, 2009) ("[I]t is plainly disclosed that Goldman treated stock-based compensation as a cash expense in its DCF Analysis. Thus, shareholders can plainly determine from reading the proxy that Goldman made a departure from the norm in conducting its discounted cash flow analysis." (citation omitted)); *Laborers Local 235 Benefit Funds v. Starent Networks, Corp.,* 2009 WL 4725866, at * 1 (Del. Ch. Nov. 18, 2009) (describing the treatment of SBC as a cash expense as a "change in norms" and the treatment of SBC as a non-cash expense as the traditional methodology).

[112] Schiller did not know whether Cogent's plan was non-qualified. Tr. 616–17. The evidence shows, however, that at least one of Cogent's stock option plans was a non-qualified plan. *See* JX 10 at 55.

[113] *See* Conrad Ciccotello, C. Terry Grant & Gerry Grant, *Impact of Employee Stock Options on Cash Flow,* 60 Fin. Analysts J. 2, 39 (Mar.–Apr. 2004) ("Exercise of [non-qualified stock options] actually *increases* operating cash flows.").

[114] JX 1 at 14 n.40 (quoting Aswath Damodaran, *From revenues to earnings: Operating, financing and capital expenses....,* Musings on Markets (June 15, 2011), *available at http://aswathdamodaran.blogspot.com/2011/06/from-revenues-to-earnings-operating.html*).

[115] JX 4 at 24–25.

[116] *See* Tr. 175–76 (Bailey).

[117] *Gholl v. Emachines, Inc.,* 2004 WL 2847865, at *14 n.97 (Del. Ch. Nov. 24, 2004) (citing Shannon Pratt, *The Lawyer's Business Valuation Handbook* 422 (2000)), *aff'd,*875 A.2d 632, 2005 WL 1413205 (Del.2005) (ORDER).

[118] Resp't's Answering Br. 26.

[119] Tim Koller, Marc Goedhart & David Wessels, *Valuation: Measuring and Managing the Value of Companies* 137–40 (5th ed. 2010) (emphasis omitted) [hereinafter Koller et al., *Valuation*].

[120] Tr. 614—15 (Schiller). In fact, Schiller admitted that he did not consult any treatises in determining what accounts needed to be adjusted. *Id.*

[121] This Court has relied on the fifth edition of *Valuation* in at least two other cases. *SeeIn re Orchard Enters., Inc.,* 2012 WL 2923305, at *9 n.60, *17 n.111, & *19 n.122 (Del. Ch. July 18, 2013); *Global GT LP v. Golden Telecom, Inc.,* 993 A.2d 497, 513 nn.91 & 94 (Del. Ch. 2010), *aff'd,*11 A.3d 214 (Del.2010). The Court also has relied on other editions of *Valuation.SeeRegal Entm't Gp. v. Amaranth LLC,* 894 A.2d 1104, 1110 (Del. Ch. 2006). Respondent criticizes Petitioners for not offering that treatise into evidence or submitting it with their papers. In an effort to reach the correct result, however, this Court regularly relies on authoritative treatises that were not entered into evidence. *SeeDuPont DCV Hldgs., Inc. v. ConAgra, Inc.,* 889 A.2d 954, 962 n.14 (Del. 2005) ("The Sellers argue that Mr. Freund's book cannot be relied on as persuasive authority, because case law precludes Delaware courts from relying on books or treatises that are not introduced into evidence. However, the cases the Sellers cite stand for the proposition that courts cannot rely on *medical* books not placed into evidence. As the Buyer correctly notes, Mr. Freund's book has been relied on by this Court and the Court of Chancery as secondary persuasive authority on several occasions." (citation omitted)).

122 In calculating Cogent's fourth quarter cash flows, Bailey "subtract[ed] Cogent's year-to-date financial metrics from its 2010 projections to arrive at its 2010 cash flows for the valuation model." JX 2 at 63.

123 *See**Gholl v. Emachines, Inc.,* 2004 WL 2847865, at *12 n.79; *Lane v. Cancer Treatment Ctrs. of Am., Inc.,* 2004 WL 1752847, at *30 (Del. Ch. July 30, 2004).

124 I have not adjusted Cogent's forward capital structure because it has such a strong cash position and a proven ability to generate significant positive cash flows.

125 *See**Cede & Co. v. JRC Acq. Corp.,* 2004 WL 286963, at *8 (Del. Ch. Feb. 10, 2004) ("Under CAPM the cost of equity is equal to the risk-free rate (the yield on 20 year Treasury bonds) plus a large company equity risk premium multiplied by the specific company adjusted beta.... Added to this figure is an equity size premium.").

126 *See* JX 1 app. I n.4; JX 2 at 47–48; United States Department of the Treasury, Daily Treasury Yield Curve Rates, http://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yieldYear&year=2010 (last visited May 16, 2013).

127 *See* JX 2 at 48 (Bailey's Rep.: "[T]he 10–year or 20–year Treasury bond yield is used as the risk-free rate of return."); Tr. 564–55 (Schiller) ("Q. Risk-free rate of return. You used the yield on the U.S. treasury ten-year bond, as of December 1, 2010, came up with 2.95 percent. Mr. Bailey used the 20–year bond and reached actually a higher rate, 3.8 percent. Is that a judgment call or is there something to disagree with there? A. It's a judgment call.").

128 *See, e.g.,**Gearreald v. Just Care, Inc.,* 2012 WL 1569818, at *9 n.61 (Del. Ch. Apr. 30, 2012) (applying 20–year risk-free rate); *Cede & Co., Inc. v. MedPointe Healthcare, Inc.,* 2004 WL 2093967, at *18 (Del. Ch. Sept. 10, 2004) ("[U]sing the 20–year Treasury rate is more reasonable under the circumstances and in keeping with the accepted practice."); *JRC Acq. Corp.,*2004 WL 286963, at *8 ("Under CAPM the cost of equity is equal to the risk-free rate (the yield on 20 year Treasury bonds)....").

129 *See* Aswath Damodaran, *The Dark Side of Valuation* 149 (2d ed. 2010); Aswath Damodaran, *What Is the Riskfree Rate? A Search for the Basic Building Blocks,* at 10 (Dec. 2008) (unpublished manuscript), *available at* http://people.stern.nyu.edu/adamodar/pdfiles/papers/riskfreerate.pdf ("[T]his would lead to use [of] the 10–year treasury bond rate as the riskfree rate on all cash flows for most mature firms."). *But cf. id.* at 9–10 ("The duration of equity will rise for higher growth firms and could be as high as 20–25 years for young firms with negative cash flows in the initial years. In valuing these firms, an argument can be made that we should be using a 30–year treasury bond rate as the riskfree rate.").

130 Koller et al., *Valuation, supra* note 119, at 236–38 ("For U.S.-based corporate valuation, the most common proxy is 10–year government STRIPS."). *But see* Shannon Pratt & Alina Niculita, *The Lawyer's Business Valuation Handbook* 24–25 (2d ed. 2010) ("As noted earlier, the risk-free rate usually is a yield-to-maturity rate available on U.S. Treasury securities as of the effective valuation date. Analysts usually use one of three maturities: 30–day, five-year, or 20–year. These maturities are used because they are the maturities for which [Ibbotson] has developed matching general equity risk premium series.... Analysts generally prefer the 20–year maturity. They recognize that it has an element of risk called *horizon risk,* or *interest rate risk,* meaning that the value of the principal will fluctuate with changing levels of interest rates, but investors generally accept this risk. The longer rates are preferable partly because they are more stable over time and less subject to short-term influences. Also, the longer maturity more closely matches the assumed long life of most businesses.").

131 Eugene Brigham & Michael Ehrhardt, *Financial Management* 347 (12th ed. 2008).

132 *Global GT LP v. Golden Telecom, Inc.,* 993 A.2d 497, 521 (Del. Ch. 2010).

133 *Id.*

134 JX 1 app. I; JX 2 at 54.

135 JX 1 app. I; JX 2 at 51. At his deposition and at trial, Schiller corrected an erroneous statement in Owsley's report that beta was calculated on a monthly basis for five years. In particular, Owsley's report conflicted with the appendix, which stated that beta was calculated on a weekly basis for two-years. JX 179 at 22–24.

136 Because the selection of adjusted versus raw beta is intertwined with the cash adjustment issue, I defer discussion of that aspect of the beta dispute until later in this section.

[137] JX 2 at 51.

[138] Shannon Pratt & Roger Grabowski, *Cost of Capital: Applications and Examples* 203 (4th ed. 2010).

[139] *See* Pet'rs' Opening Br. 29 ("[T]he beta for cash should be zero."); Resp't's Answering Br. 32 (stating that Cogent's cash should have a beta of zero).

[140] *See* JX 2 at 52–54 (multiplying average ending day price by average outstanding shares during the period).

[141] *Id.* at 53.

[142] Pratt & Grabowski, *supra* note 138, at 203.

[143] This $50 million number is based on management's projections, which assumed a "minimum cash balance" of $50 million for the years 2010–2015. *See* JX 1 at 60. Credit Suisse adopted that assumption in the preparation of its financial analysis regarding the Merger. *See* JX 122 at 32 n.4. Finally, an examination of Cogent's historical cash balance shows that of the $533.2 million in cash and cash equivalents only $32.99 million was actual cash, with the other approximately $500.2 million being in either short term or long term investments in marketable securities. *See* JX 3 at 43; JX 153 at 3, 9.

[144] $533.2 million - $50 million = $483.2 million.

[145] $868.7 million - 483.2 million = $385.5 million.

[146] ($868.7 million / $385.5 million) = 2.253.

[147] Marshall E. Blume, *On the Assessment of Risk,* 26 J. Fin. 1, 10 (1971); *see also* Pratt & Grabowski, *supra* note 138, at 167.

[148] *See* Pratt & Grabowski, *supra* note 138, at 203 ("An alternative adjustment that is used by Bloomberg and *Value Line* adjusts the historical beta to a "forward" estimated beta by averaging the historical beta estimate by two-thirds and the market beta of 1.0 by one-third."); Koller et al., *Valuation,* supra note 119, at 253 ("For well-defined industries, an industry beta will suffice. But if few direct comparables exist, an alternative is beta smoothing.").

[149] $\#_{COGT}$ = (# x 1) + ($^{2}/_{3}$ x 1.595) = 1.397.

[150] JX 2 at 55–56.

[151] JX 1 app. I.

[152] JX 2 at 55–56.

[153] JX 1 app. I.

[154] Tr. 630 (Schiller) ("Q. Your equity risk premium used a rate of 5 percent; right? A. Yes. Q. Your report doesn't explain how ... that [equity risk premium] was calculated, does it? A. No, it does not. Q. It doesn't explain whether it's a historic equity risk premium or a supply-side equity risk premium, does it? A. No. Q. Do you know which one it is? A. I'm not familiar with those analyses. The stuff I've seen does not draw a distinction between those two.").

[155] Selection of a supply-side equity risk premium is consistent with prior decisions by this Court. *See, e.g., In re Orchard Enters., Inc.,* 2012 WL 2923305, at *19 (Del. Ch. July 18, 2012) ("I therefore find that the Ibbotson Yearbook's supply-side equity risk premium of 5.2% is an appropriate metric to be applied in valuing Orchard under the CAPM."); *Gearreald v. Just Care, Inc.,* 2012 WL 1569818, at *10 (Del. Ch. Apr. 30, 2012) ("[A]lthough experts and this Court traditionally have applied the historical equity risk premium, the academic community in recent years has gravitated toward greater support for utilizing the supply side equity risk premium."); *Global GT LP v. Golden Telecom, Inc.,* 993 A.2d 497, 517 (Del. Ch. 2010) (referring to the Court's adoption of a supply-side equity risk premium, the Court stated "when the relevant professional community has mined additional data and pondered the reliability of past practice and come, by a healthy weight of reasoned opinion, to believe that a different practice should become the norm, this court's duty is to recognize that practice if, in the court's lay estimate, the practice is the most reliable available for use in an appraisal").

[156] *Gearreald v. Just Care, Inc.,* 2012 WL 1569818, at *10 (Del. Ch. Apr. 30, 2012).

[157] *In re Orchard Enters., Inc.,* 2012 WL 2923305, at *21.

[158] JX 1 at 29; JX 2 at 57, 84 n.6.

[159] JX 2 at 57; Ibbotson SBBI, *2010 Valuation Yearbook, Market Results for Stocks, Bonds, Bills, and Inflation 1926–2009.* Cogent's market capitalization at the time of the Merger was approximately $931 million.

[160] Ibbotson SBBI, *2010 Valuation Yearbook, Market Results for Stocks, Bonds, Bills, and Inflation 1926–2009.*

[161] *See, e.g.,* Pratt & Grabowski, *supra* note 138, at 233 ("Morningstar, Inc. [the parent of Ibbotson], segregates New York Stock Exchange (NYSE) stock returns into deciles by size, as measured by *the aggregate market value of common equity."* (emphasis added)); *id.* at 240 ("Traditionally, researchers have used *market value of equity* as a measure of size in conducting historical rates of return research. For instance, this is the basis of the small-company return series published in the *SBBI Yearbooks.*" (emphasis added)); James R. Hitchner, *Financial Valuation: Applications and Models* 247 (3d ed. 2011) (noting that in the *Valuation Yearbook* "Ibbotson presents index-based returns weighted on the market capitalization of each stock").

[162] *See, e.g.,In re Orchard Enters., Inc.,* 2012 WL 2923305, at *21 ("The Ibbotson Yearbook divides the stock returns of public companies into deciles by size, *measured by the aggregate market value of the companies' common equity."* (emphasis added)); *Cede & Co. v. JRC Acq. Corp.,*2004 WL 286963, at *8 (Del. Ch. Feb. 10, 2004) (selecting "market capitalization" as the benchmark over "fair value implied market capitalization"); *In re Sunbelt Beverage Corp. S'holder Litig.,* 2010 WL 26539, at *11 (Del. Ch. Jan. 5, 2010) ("The Ibbotson table assumes one already knows or has an estimate of a company's market capitalization. Based on that knowledge or estimate, one can determine which decile the company falls into and then select the corresponding premium from the Ibbotson table.").

[163] Tr. 565 (Schiller). Schiller also admitted that he was "not aware of any authority" that says that when looking at a company's market capitalization, it's appropriate to adjust it based on its cash. *Id.* at 631.

[164] *Id.* at 566.

[165] *See* Tr. 201 (Bailey) ("Those tables were developed all from seminal work that was done by Professor Rolf Banz back in 1981, in which Professor Banz did a seminal paper on adjusting the risk value of a company based upon the market value of the company."); Rolf Banz, *The Relationship Between Returns and Market Value of Common Stock,* 9 J. Fin. Econ. 3 (1981) ("The results show that, in the 1936–1975 period, the common stock of small firms had, on average, higher risk-adjusted returns than the common stock of large firms.").

[166] *See* Duff & Phelps, *Risk Premium Report 2013* (18th ed. 2013).

[167] *Global GT LP v. Golden Telecom, Inc.,* 993 A.2d 497, 511 (Del. Ch. 2010).

[168] *Gholl v. Emachines, Inc.,* 2004 WL 2847865, at *13 (Del. Ch. Nov. 24, 2004).

[169] *Id.*

[170] JX 1 at 32.

[171] Pratt & Grabowski, *supra* note 138, at 30–34.

[172] *SeeGolden Telecom, Inc.,* 993 A.2d at 511; *see alsoLane v. Cancer Treatment Ctrs. of Am., Inc.,* 2004 WL 1752847, at *31 (Del. Ch. July 30, 2004) ("I find [the] assumption that no growth would occur beyond the projected five-year period unreasonable; it must be assumed that [the company] would continue to grow at least at the rate of inflation.").

[173] Bradford Cornell, *Corporate Valuation: Tools for Effective Appraisal and Decision Making* 146–47 (1993).

[174] JX 2 at 58–60 (citing Ian Wyatt & Kathryn Byun, *The U.S. Economy to 2018: From Recession to Recovery,* Monthly Labor Review (Nov. 2009), *available at* http://www.bls.gov/opub/mlr/2009/11/art2full.pdf; Federal Reserve Bank of Philadelphia, *The Livingston Survey* (2010), *available at* http://www.philadelphiafed.org/research-and-data/real-time-center/livingston-survey/2010/livdec10.pdf).

[175] JX 1 at 31–33, 50, 86.

[176] Tr. 635–36 (Schiller) ("Q. And you don't have any specific explanation as to why the growth rate drops from 9.2 percent to 2 to 5 percent, do you? A. No.... Q. ... [Y]ou don't provide any analysis in connection with the opinion that you're offering to the Court as to what GDP would be in the future, do you? A. No, we don't. Q. And you didn't consult any authorities as to what terminal growth rate should be in 2015 or beyond, do you? A. No. We see these numbers often, but we didn't consult any authorities, no.").

[177] JX 2 at 20.

[178] *Andaloro v. PFPC Worldwide, Inc.,* 2005 WL 2045640, at *12 (Del. Ch. Aug. 19, 2005).

[179] Aswath Damodaran, *Investment Valuation: Tools and Techniques for Determining the Value of Any Asset* 329 (3d ed. 2012).

[180] *Id.* at 331.

[181] *Id.* at 340.

[182] *Id.* at 342.

[183] Using management's projections, Bailey calculated a CAGR of 11.45% for the period 2009 through 2015. JX 2 at 21.

[184] $^{\$64.4}/_{11.954\% - 4.5\ \%} = \sim\$864$

[185] Koller et al., *Valuation, supra* note 119, at 227.

[186] *Crescent/Mach I P'ship, L.P. v. Turner,* 2007 WL 2801387, at *14 (Del. Ch. May 2, 2007).

[187] *See supra* Part II.C.3.

[188] JX 1 at 44, 74.

[189] *Id.* at 86 n.1.

[190] *Id.* at 44.

[191] Tr. 580, 636–37.

[192] *See* JX 3 at 43; JX 153 at 3, 9.

[193] There were 88.616 million shares issued and outstanding as of November 2, 2012. *See* JX 157 at 2.

[194] $^{\$963.4}/_{88.6} = \$10.87$

[195] 8 *Del. C.* § 262(h); *see alsoid.* § 262(i) ("The Court shall direct the payment of the fair value of the shares, together with interest, if any.").

[196] *In re Appraisal of Metromedia Int'l Gp., Inc.,* 971 A.2d 893, 907 (Del. Ch. 2009).

[197] 576 A.2d 650 (Del. Ch. 1989), *appeal refused,*571 A.2d 787, 1990 WL 18152 (Del. 1990) (ORDER).

[198] *Id.* at 654.

[199] *Solomon Bros. Inc. v. Interstate Bakeries Corp.,* 1992 WL 94367, at *8 (Del. Ch. May 4, 1992).

[200] 684 A.2d 289 (Del. 1996).

[201] *Id.* at 298 (citing *Cavalier Oil Corp. v. Harnett,* 564 A.2d 1137, 1145 (Del. 1989)).

[202] *Schenley Indus., Inc. v. Curtis,* 152 A.2d 300, 301 (Del.1959) (citing *Chicago Corp. v. Munds,* 172 A. 452, 455 (Del. Ch.1934)).

[203] *Lane v. Cancer Treatment Ctrs. of Am., Inc.,* 2004 WL 1752847, at *36 (Del. Ch. July 30, 2004); *see also**Gholl v. Emachines, Inc.,* 2004 WL 2847865, at *18 (Del. Ch. Nov. 24, 2004) ("An award of interest serves two purposes. It compensates the petitioner for the loss of use of its capital during the pendency of the appraisal process and *causes the disgorgement of the benefit respondent has enjoyed during the same period.*" (emphasis added)).

[204] *Ryan v. Tad's Enters., Inc.,* 709 A.2d 682, 705 (Del. Ch. 1996), *aff'd,*693 A.2d 1082, 1997 WL 188351 (Del. 1997) (ORDER).

[205] In a footnote, Respondent argues that in the current interest rate environment—where the statutory rate of interest is more than seven times the federal discount rate—Petitioners have distorted incentives to seek appraisal. There are risks to both sides in an appraisal proceeding, however, and the applicable interest rate is only one of them. Moreover, "[i]t is beyond the province of courts to question the policy or wisdom of an otherwise valid law. Rather, [I] must take and apply the law as [I] find it, leaving any desirable changes to the General Assembly." *Sheehan v. Oblates of St. Francis de Sales,* 15 A.3d 1247, 1259 (Del. 2011).

[206] *See**In re Appraisal of Metromedia Int'l Gp., Inc.,* 971 A.2d 893, 907 (Del. Ch. 2009) ("For example, petitioners cannot point to unreasonable or improper delay, as this matter was tried before the Court roughly one year after the first appraisal petition was filed, a remarkably short period of time by appraisal litigation standards."). Although the Court is working to reduce the average time to trial in the future, recent appraisal actions have taken longer than this case. *See, e.g.,**Towerview LLC v. Cox Radio, Inc.,* 2013 WL 3316186 (Del. Ch. June 28, 2013) (39 months to trial); *Highfields Capital, Ltd. v. AXA Fin., Inc.,* 939 A.2d 34 (Del. Ch. 2007) (30 months to trial).

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UNPUBLISHED OPINION. CHECK
COURT RULES BEFORE CITING.

Court of Chancery of Delaware.

S. MUOIO & CO. LLC, on behalf of itself
and the class and derivatively on behalf
of Crown Media Holdings, Inc., Plaintiff,
v.
HALLMARK ENTERTAINMENT INVESTMENTS
CO., a Delaware corporation, Hallmark
Entertainment Holdings, Inc., a Delaware
corporation, H C Crown Corp., a Delaware
corporation, H.A., Inc., a Delaware corporation,
Hallmark Cards, Inc., a Missouri corporation,
William J. Abbott, Dwight C. Arn, William
Cella, Glenn Curtis, Steve Doyal, Brian E.
Gardner, Herbert A. Granath, David E. Hall,
Donald J. Hall, Jr., Irvine O. Hockaday,
Jr., A. Drue Jennings, Peter A. Lund, Brad
R. Moore, Deanne R. Stedem, Defendants,
and
Crown Media Holdings, Inc., a Delaware
corporation, Nominal Defendant.

Civil Action No. 4729–CC.
|
Submitted: Dec. 31, 2010.
|
Decided: March 9, 2011.

Attorneys and Law Firms

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MEMORANDUM OPINION

CHANDLER, Chancellor.

***1** This action challenges the fairness of the June 29, 2010 recapitalization (the "Recapitalization") of Crown Media Holdings, Inc. ("Crown" or the "Company") orchestrated by Crown's controlling stockholder and primary debt holder, Hallmark Cards, Inc. and its affiliates (collectively "Hallmark").[1] For years, Crown was unable to make its debt payments, and was forced to obtain extensions on the debt from Hallmark. In the Recapitalization, Hallmark exchanged its Crown debt for an increased percentage of Crown's Class A common stock, new preferred stock and a new and far smaller amount of debt with longer maturities, thereby permitting Crown to avoid a debt default and bankruptcy.

Hallmark initially proposed a recapitalization on May 28, 2009. Crown's board immediately created a Special Committee to consider the proposed recapitalization. Before the Special Committee could even consider the proposed recapitalization, S. Muoio & Co. LLC (a Crown stockholder) filed this action on July 13, 2009, seeking to enjoin the proposed transaction. The parties agreed to a stay of the litigation while the Special Committee considered Hallmark's proposal. They also agreed that Crown would not consummate any transaction without providing seven week's advance written notice to Muoio's counsel of the terms of the transaction. The parties further stipulated that in the event Muoio decided to pursue a preliminary injunction against the transaction, the parties would establish a schedule for its resolution during the seven week period.

Almost seven months later, on February 9, 2010, Crown announced that Hallmark and Crown had approved and executed a non-binding term sheet in connection with the

Recapitalization. On March 1, 2010, Crown announced it had entered into a Master Recapitalization Agreement memorializing the terms of the Recapitalization. After receiving that notice, however, Muoio eschewed any preliminary injunction proceedings, and instead filed an amended and supplemental complaint on March 11, 2010, dropping its request for injunctive relief and seeking rescission of the transaction. The Recapitalization closed on June 29, 2010.

Plaintiff contends that the Recapitalization was consummated at an unfair price and drastically undervalued Crown. In so doing, plaintiff asserts that Crown should be valued based on a discounted cash flow ("DCF") analysis, and that a properly conducted DCF analysis establishes that Crown's stock is worth far more than the Recapitalization, which is valued at $2.59 per share. Plaintiff also contends that Hallmark imposed the Recapitalization on the Company through an unfair process, that the Hallmark-dictated terms of the new debt and preferred stock are unfair, and that the Recapitalization unfairly transferred significant value and voting power from the Crown minority stockholders to Hallmark. In sum, plaintiff insists that the Recapitalization substantially undervalued the Company, resulting in an enormous, unjustified transfer of wealth and voting power from the Crown minority stockholders to Hallmark, all through an unfair process that included an ineffective Special Committee and Hallmark's domination of the negotiation process.

***2** This case was tried over a four-day period, from September 21 through September 24, 2010. The parties concede that the appropriate standard of review is entire fairness. I have considered the parties' post-trial briefs, and during trial I assessed the strength and credibility of the testimony offered by the various witnesses. Ultimately, my decision turns on the following factual findings: the Crown board's process was not flawed; the Special Committee was independent and negotiated at arm's length; and the record clearly demonstrates that Crown was underwater at the time of the Recapitalization—that is, it could not pay its debts as they became due and absent the Recapitalization, default or bankruptcy seemed inevitable. In addition (as is now quite common in cases of this nature), the valuation question, in part, resulted in a battle of the experts—and in this case, plaintiff's expert lost. His proffered opinion was far less credible and persuasive than defendants' experts. For the reasons more fully explained below, I find in favor of defendants and conclude that the Recapitalization was entirely fair.[2]

I. BACKGROUND

A. The Parties

Plaintiff Muoio is a New York securities advisory firm and a holder of Crown's Class A common stock. Salvatore Muoio is plaintiff's principal owner and manager.

Defendant Hallmark, a Missouri corporation headquartered in Kansas City, Missouri, is engaged in the manufacture and distribution of personal expression products. Immediately before the Recapitalization proposal, Hallmark controlled approximately 80.1% of Crown's outstanding shares; following the proposal it now controls approximately 90.3 %.[3]

Nominal Defendant Crown is a Delaware corporation with its principal place of business in Studio City, California. Crown's revenues are largely tied to advertising revenue, which in turn is driven by the ratings and demographics of its cable television channels. Crown competes for both ratings and key demographics with large media companies that are able to spread their costs across multiple cable channels. Crown's board includes the Special Committee defendants and defendants William J. Abbott, Dwight C. Arn, William Cella, Glenn Curtis, Steve Doyal, Brian E. Gardner, David E. Hall, Donald J. Hall, Jr., Irvine O. Hockaday, Jr., Brad R. Moore, and Deanne R. Stedem.

The Special Committee consists of defendants Herbert A. Granath, A. Drue Jennings, and Peter A. Lund. Granath has been a Crown director since December 2004 and has extensive experience in the broadcast and cable television industries. He served as the chairman of Disney/ABC International Television, and he also developed and was the chairman of several cable networks for ABC, including ESPN, A & E, the History Channel, and Lifetime.[4] He was also the chairman of the National Academy of Television Arts and Sciences and has won several awards for his work in the industry.[5] Lund has been a Crown director since 2000, and has extensive experience in the media sector. Lund had a long career with CBS, serving as president and CEO of CBS Television and Cable Networks and later, as president and CEO of CBS Inc.[6] He is also currently a director of DirecTV.[7] Jennings served for twelve years as the CEO of Kansas City Power & Light Company, a publicly traded company on the New York Stock Exchange. As a prominent leader in the Kansas City community, Jennings has been actively involved with several civic associations, including the Midwest Research Institute and the Bloch Endowment Fund at the Greater Kansas City Community Foundation.[8] He also served on numerous advisory boards, including the University of Kansas Medical Center and University of Kansas Endowment Association. He has been "of counsel" with the law firm Polsinelli Shughart P.C. since October 2004.[9] Jennings joined the Crown board in 2006 and he is the chair of Crown's Audit Committee.

B. Crown's Formation and its Debt Crisis

***3** In 1991, Hallmark created the family entertainment platform that became Crown following a review of its business units, which also include Crayola and other family oriented subsidiaries.[10] In the early 1990s, Hallmark acquired an extensive production library of programming that was designed to appeal to all ages. In 1998, Hallmark partnered with the National Interfaith Cable Coalition ("NICC") to relaunch the Odyssey Network as a family-friendly cable network.[11] The network was later renamed as "Hallmark Channel." Crown Media Holdings was created in 2000 to effectuate an initial public offering of Crown, providing the Company with additional capital to fund its development.

In January 2001, Crown acquired a library of over 700 original television movies, representing over 3,000 hours of programming, from a Hallmark subsidiary (the "Library Transaction").[12] This programming was used, among other things, to populate the Hallmark Channel and the Hallmark Movie Channel. With the Library Transaction, Crown assumed $220 million of debt and ultimately issued 33.3 million shares of stock to Hallmark.[13] Over the years, Hallmark supplied Crown with needed capital injections, and agreed to extend maturities on the debts owed to it by Crown. By spring 2009, however, Crown owed Hallmark over $1.1 billion in debt.[14] Crown also held a credit revolver with J.P. Morgan (the "JPM Revolver") guaranteed by Hallmark, and it owed $25 million to NICC.[15]

C. Crown's Attempts to Find a Buyer

In August 2005, the Crown board formed a special committee composed of Granath and Lund (the "2005 Special Committee") to seek a buyer for the Company and also consider other alternatives. The 2005 Special Committee retained independent legal and financial advisors, Wachtell, Lipton, Rosen & Katz and Citigroup, to engage in an extensive sales process involving key players in the cable industry as well as private equity firms. The object was to help identify a buyer for Crown. Not a single offer resulted from the 2005 Special Committee process. Thereafter, Hallmark itself engaged in discussions with several potential acquirers or other sources of financing for Crown, but was similarly unsuccessful.[16]

In August 2006, Tim Griffith became Hallmark's interim CFO and assumed responsibility for the management of Hallmark's investment in Crown. At this point, Hallmark held $1 billion of Crown's outstanding debt.[17] Crown's financial situation was precarious because Crown had never made a profit and (as stated above) efforts to sell the Company had failed up to this point. To allow Crown to continue operating as a going concern, Hallmark had previously granted Crown a waiver and standstill on its debt payments.[18] The waiver and standstill agreement was revisited every quarter, with extensions being effective for one year from the date Hallmark extended. Without the waivers and extensions, Crown's auditors would have issued a going concern qualification on Crown's financial statements for one simple reason: Crown could not pay interest on its debt (much less pay the principal of the notes due upon expiration of the standstill).

***4** In 2006, Crown hired a new CEO, Henry Schleiff, who was specifically recruited to find a buyer for Crown.[19] Schleiff had successfully sold another cable channel before joining Crown. Schleiff contacted numerous parties but ultimately failed to locate a buyer for Crown during his three year tenure as CEO. In 2007, Schleiff's efforts produced three prospective buyers: Liberty Media, Time Warner, and Hearst.[20] Each potential buyer did due diligence and spoke with management. Liberty Media expressed interest in Hallmark's stake in Crown, valuing Crown at around $800 million.[21] Liberty Media continued to show its interest, raising its enterprise value to $1 billion by 2008.[22] In other words, Liberty Media viewed Crown's enterprise value to be below the value of Crown's debt. Similarly, Time Warner did not make an offer, but put an enterprise value on Crown of $1 billion (again, below the value of its debt). Hearst never formally made an offer. In 2008 and 2009, Schleiff also turned up other potential buyers, including CBS, Hasbro, and Fox.

None made an offer above Crown's debt to Hallmark. Fox did make a proposal, in which it put the total enterprise value of Crown at $500 million and which would have required Hallmark to write off 85% of the Hallmark debt and give Fox control of the Company.[23] Hallmark was unwilling to accept those terms. Concurrently, Hallmark extended Crown's waiver and standstill to May 2010.[24]

In sum, despite continuous efforts to shop Crown since 2005, no potential buyer had placed a value on Crown that exceeded the Hallmark debt, and the most recent offer for Crown was $500 million—less than half of its debt to Hallmark. At least in Hallmark's view, given that refinancing Hallmark's debt with a third party was impossible, a recapitalization was the best path forward either to a future refinancing or a future sale. Although plaintiff disputes this, it appears that Hallmark's view was that if there was no recapitalization, bankruptcy or foreclosure were the likely alternatives.[25]

D. The Recapitalization Proposal

On May 28, 2009, Hallmark sent the Crown board a proposal for recapitalizing the Hallmark debt (the "Hallmark Proposal").[26] Under the Hallmark Proposal, Hallmark's equity ownership would increase from 67% to at least 90.1 % (possibly even up to 95%), while its voting power would increase from 80.1% to 90.3%.[27] The Hallmark Proposal included restructuring $500 million of principal amount of the Hallmark debt into a $300 million cash-pay term loan bearing an annual interest rate of 12% and a $200 million pay-in-kind term loan with an annual interest rate of 15%, both maturing on September 30, 2011.[28] The remaining Hallmark debt, which is about $600 million, would be exchanged for convertible preferred stock with a liquidation preference of approximately $640 million and a conversion price of $1.00 per share.[29] Along with this proposal, Hallmark also advised Crown that it would not continue to extend the waiver and standstill. Hallmark was neither willing, nor legally obligated, to invest further in Crown.

E. Creation of the Special Committee

***5** After receiving the Hallmark Proposal, the Crown board on June 2, 2009, formed the Special Committee, composed of independent directors Granath, Lund, and Jennings. Jennings was chosen as chairman of the Special Committee. As stated above, the Special Committee had two members with industry experience (Lund and Granath), and its chairman (Jennings) was a lawyer and former CEO of a publicly traded utility company. According to the resolutions creating the Special Committee, the Special Committee was empowered to "consider such matters as it deems advisable with respect to the Recapitalization Proposal," and authorized to "take such further action, at the Company's expense, as the Special Committee deems appropriate in order to carry out the intent and purposes" of the authorizing resolutions.[30] The resolutions prohibited the Crown board from approving or authorizing an agreement with respect to the Hallmark Proposal "without a prior favorable recommendation of the Recapitalization Proposal or the relevant part thereof by the Special Committee."[31]

F. Process of the Special Committee

The Special Committee's first task was to select its independent legal and financial advisor. The Special Committee retained Richards, Layton & Finger, P.A. ("RLF") as its independent legal counsel. After receiving presentations from various firms, the Special Committee retained Morgan Stanley as its financial advisor.[32] Once Morgan Stanley was engaged, the Special Committee promptly authorized a press release announcing the engagement, stating expressly that the Committee was "considering Hallmark Cards' proposal as well as the Company's other alternatives ."[33]

After being retained by the Special Committee, Morgan Stanley engaged in extensive due diligence of Crown, including meetings with Crown's senior management to discuss the Company's business plans and financial viability. Morgan Stanley reviewed Crown's current financial condition and provided the Special Committee with information regarding comparable companies. Based on its analysis, on September 11, 2009, Morgan Stanley advised the Special Committee that it had determined a preliminary value of Crown of between $500 million and approximately $1 billion, with a mid-point at approximately $700 to $750 million—less than the amount Crown owed to Hallmark.[34]

Crown management also made presentations to the Special Committee, updating the Committee on the cable industry and on Crown's performance in 2008 and 2009. The Special Committee was informed that the Company's performance in its key demographic (women age 25 to 54) fell below expectations and below 2008 results, and Crown's 2009 advertising sales were below 2008 sales by approximately 13% to 15%.[35] In November 2009, Crown's management revised the Company's five-year business plan by reducing the forward-looking projections in light of current market conditions and Crown's performance. Management discussed the revised plan with the Special Committee.[36] Before the Hallmark Proposal, Crown had not been able to meet its debt service on the Hallmark debt; interest on the debt alone was more than $100 million per year.[37] As a result, Crown had been operating under a series of waivers and extensions since 2006 that deferred nearly all of Crown's payment obligations—without which waivers Crown would have defaulted on the Hallmark debt. In short, Crown faced significant hurdles going forward. To make matters worse, the cable industry's gradual decline itself added more negative pressure to Crown's bleak future.[38]

***6** The Special Committee knew it had few options. Those options included: (1) refinancing the Hallmark debt; (2) pursuing a third-party sale; (3) accepting Hallmark's Proposal; or (4) negotiating the Hallmark Proposal. The Special Committee, with advice from Morgan Stanley, acknowledged that none of those options were optimal, but the status quo (*i.e.,* doing nothing) was not feasible because Crown simply could not service its debt burden and would be unable to satisfy its debts on the maturity dates.[39] Morgan Stanley took the position (and so advised the Special Committee) that Crown could not refinance the Hallmark debt with a third party in light of Crown's capital structure and debt market conditions in 2009. Moreover, given past failed sales efforts, the Special Committee determined that a third-party sale was unlikely.[40] The Special Committee reached this decision based on its own members' extensive industry experience as well as Morgan Stanley's advice.

Ultimately, the Special Committee determined that, absent a recapitalization of its debt, Crown faced a potential bankruptcy. Morgan Stanley advised that Crown's non-Hallmark stockholders likely would not receive any value in a bankruptcy proceeding. On the other hand, there were potential downsides to Hallmark in a bankruptcy, and Morgan Stanley considered it unlikely that Hallmark wanted to place Crown into bankruptcy.[41] As stated above, Hallmark, with its original proposal, had no intention of continuing to extend the waiver and standstill, and it simply did not want to invest further in Crown. Likewise, the Special Committee and Morgan Stanley believed that further extending the debt waivers and putting off Crown's significant capital structure issues were not in the best interests of Crown or its minority stockholders, because the debt owed to Hallmark would continue to grow. Therefore, the Special Committee decided not to pursue or to ask for further debt extensions. Given the potential risks and costs of a bankruptcy, Morgan Stanley believed Hallmark would be inclined to renegotiate a solution to the debt issues for Crown; Morgan Stanley also considered the Hallmark Proposal to have numerous deficiencies.[42] It was against this background that Morgan Stanley advised the Special Committee that a go-private transaction was the best alternative for the non-Hallmark stockholders. In the event Hallmark would not consider taking Crown private at a fair price, Morgan Stanley believed the Special Committee should try to negotiate for better terms in a recapitalization.

G. The Negotiations

Armed with Morgan Stanley's advice favoring a go-private transaction, the Special Committee approached Hallmark on this issue. On September 21, 2009, Jennings sent a letter on the Special Committee's behalf to Don Hall, Jr., CEO of Hallmark, proposing a go-private transaction.[43] On September 23, 2009, on behalf of Hallmark, Griffith responded that Hallmark was not interested in taking Crown private.[44] After Hallmark rejected the go-private idea, the Special Committee decided to negotiate the recapitalization. To this end, it directed Morgan Stanley to meet with Hallmark's financial advisor, Evercore Partners, to discuss a counterproposal. The Special Committee's counterproposal had several goals, including a significant reduction in Crown's outstanding debt, an extension of Crown's debt maturities, and an increase in the amount of equity retained by the unaffiliated stockholders.[45] Morgan Stanley's proposed strategy, which the Special Committee adopted, was to posit a low number for Crown's value, give Hallmark new debt equal to that number, and allow the minority stockholders to share in any upside from that number.

***7** Morgan Stanley conveyed this counterproposal to Hallmark through Evercore Partners on October 1, 2009. At a meeting on October 15, 2009, Evercore Partners conveyed to Morgan Stanley Hallmark's three concerns about the Special Committee's counterproposal: (1) Hallmark would not write off any portion of its $1.1 billion in loans to the Company; (2) a "majority of the minority" vote condition could not be a condition to closing; and (3) Crown had to pay off the NICC debt at par in due course.

Hallmark's October 15 response had a slight change from its original proposal. As a result, the Special Committee decided not to bid against itself and refused to engage. As a result of this strategy, Hallmark made “a major economic concession” and gave Morgan Stanley the perception of what could be the “framework of a negotiated transaction.”[46] Hallmark eventually submitted a revised proposal that, among other things, allowed the equity to participate in Crown's value above $500 million.[47] With that revision in hand, the Special Committee had achieved one of its important goals. That is, to the extent the value of Crown was more than $500 million, the minority stockholders' equity would have value. Hallmark's revised proposal also extended the maturity of the new debt and guaranteed a revolver in a sufficient amount.[48] Hallmark delivered a further revised term sheet to the Special Committee on November 27, 2009.[49]

Four days later, the Special Committee and Hallmark, along with their advisors, held a meeting to discuss the open issues leading up to Hallmark's most recent revised recapitalization proposal. At that meeting, Hallmark made numerous concessions, including agreeing to lower the interest rates on the new Hallmark debt for the first two years; agreeing to annual cash flow sweeps,[50] as opposed to quarterly sweeps; and agreeing to use its best efforts to support Crown in obtaining a $30 million revolver.[51] Hallmark refused to agree to additional concessions, specifically refusing to agree to: (1) a transaction after which it would own less than 90% of Crown; and (2) a transaction subject to a majority-of-the-minority vote.[52] Hallmark did offer terms for a standstill agreement in which Hallmark would guarantee a floor, in a purchase or third-party sale of Crown, of $1.00 per share to the minority stockholders.[53] The Special Committee rejected this offer by Hallmark. Despite the fact that the Special Committee and its advisors walked out of the meeting at that point, significant progress had been made, and the parties' advisors continued their discussions, including the terms of a binding standstill agreement.

H. The Special Committee Retains a Second Financial Advisor

After the December 1 meeting, based on the advice provided by Morgan Stanley, the Special Committee directed its legal advisor, RLF, to submit a revised term sheet to Evercore Partners setting forth the terms that the Special Committee would be willing to recommend to the Crown board. The Special Committee also discussed the possibility of retaining a second financial advisor to provide additional guidance on the remaining terms under consideration and, if appropriate, to render a fairness opinion. The Special Committee eventually retained Houlihan Lokey as its second financial advisor to evaluate the Recapitalization and, if possible, to provide an opinion that the Recapitalization was fair to Crown from a financial point of view. Houlihan explained that its analysis would “help bridge the gap between the Committee's potential finding that the Recapitalization is fair to the Company's stockholders (other than [Hallmark]) and the opinion that the Recapitalization is fair to the Company from a financial point of view.”[54]

I. The Special Committee and Hallmark Negotiate a Standstill Agreement

***8** On December 7, 2009, the Special Committee determined that it would send a term sheet to Hallmark's attorneys reflecting the terms the Special Committee was willing to recommend to the Crown board. Included in the terms was a stringent standstill agreement which limited Hallmark's ability to buy or sell Crown's shares.[55] Throughout December 2009 and January 2010, negotiations continued based on revisions to the Special Committee's proposed term sheet. The Special Committee and Hallmark ultimately reached an agreement on the final terms of a standstill agreement—terms that prohibited Hallmark from acquiring additional shares of Crown common stock from the closing date of the recapitalization until December 31, 2013, unless expressly approved by a special committee of the Crown board composed solely of independent and disinterested directors.[56] As of January 1, 2012, however, Hallmark will be able to acquire additional Crown shares *if* it pays a $0.50 per share premium to the minority in conjunction with a third-party sale or if it makes a tender offer for all of Crown's shares with a majority-of-the-minority tender condition.[57] The standstill agreement also limits Hallmark's ability to sell its Crown shares to a third party.[58]

J. The Special Committee Approves a Non–Binding Term Sheet

On February 9, 2010, after consulting with and receiving advice and recommendations from its advisors, the Special Committee approved a nonbinding term sheet (the “Final Term Sheet”),[59] setting forth the basic details of an agreement on the terms of the Recapitalization.[60] The Final Term Sheet was publicly filed with the SEC.[61] Morgan Stanley believed that the Final Term Sheet represented a better outcome for, and provided more value to, the minority stockholders than any of the alternatives, including the status quo.[62] Houlihan also addressed the Special Committee during the February 9, 2010 meeting. Houlihan analyzed how the minority stockholders would fare pre-recapitalization and post-recapitalization concluding that the minority stockholders received significant benefits under the Recapitalization (in the Final Term Sheet), as opposed to the status quo, in which the minority stockholders would receive no value for their shares.[63]

There were a number of improvements in the Final Term Sheet as compared to the initial Hallmark Proposal, including: (1) the minority stockholders will begin to share in Crown's upside once the value of Crown exceeds $525 million, compared to $1.168 billion in the initial Hallmark Proposal; (2) $315 million of post-Recapitalization debt (as compared to $500 million in the initial Hallmark Proposal), with a maturity date in December, 2013 (as compared to September, 2011 in the initial Hallmark Proposal); (3) reduced interest rates on the debt and a higher conversion price on the preferred stock; (4) inclusion of a $30 million revolver, guaranteed by Hallmark for the term of the new debt as compared to no revolver in the initial Hallmark Proposal; (5) the Standstill Agreement; and (6) annual, rather than quarterly, cash flow sweeps.[64] As mentioned above, the Final Term Sheet was publicly disclosed, and the Company never received any other offers to purchase the Company, even though it was disclosed as a non-binding term sheet.

K. The Special Committee Approves the Recapitalization

***9** During a February 25–26, 2010 meeting, Morgan Stanley reconfirmed its earlier advice to the Special Committee that “it would be impossible to refinance with the Company's current indebtedness,” and that it “did not think there would be any return for the equity if the Company was sold today.”[65] Morgan Stanley did not believe that other strategic options would even be available to the Company. Therefore, Morgan Stanley believed that the Recapitalization was clearly the best option for Crown and recommended that the Special Committee approve the Recapitalization. Furthermore, the Special Committee received a fairness opinion from Houlihan, and Houlihan's analysis indicated that Crown's equity would have value after the Recapitalization, as opposed to before the Recapitalization, in which it would not.[66] Based on its own business judgment and the advice from its independent legal and financial advisors, including the recommendation from Morgan Stanley and the fairness opinion by Houlihan, the Special Committee concluded that the Recapitalization was in the best interests of Crown and its minority stockholders, and recommended that the transaction be approved by the full Crown board. Relying on the Special Committee's recommendation, the full board approved the Recapitalization, which closed on June 29, 2010.

II. ANALYSIS

A. Standard of Review and Burden of Proof

A transaction between a majority stockholder and the company in which it owns a majority stake is generally reviewed under the entire fairness standard and the controlling stockholder (or the party standing on both sides of the transaction) bears the burden of proof.[67] Given Hallmark's role in the Recapitalization, the applicable standard of review for this case under Delaware law is therefore entire fairness. As its name implies, entire fairness has two components: fair dealing and fair price. These prongs are not independent and the Court does not focus on each of them individually.[68] Rather, the Court “determines entire fairness based on all aspects of the entire transaction.”[69] Fair dealing involves “questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained.”[70] Fair price involves questions of “the economic and financial considerations of the proposed merger, including all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock.”[71]

“[T]he initial burden of establishing entire fairness rests upon the party who stands on both sides of the transaction.”[72] If defendant can show that the challenged transaction was negotiated and approved by “an independent committee of directors” or an informed majority of the minority, however, the burden of proof shifts to “the challenging shareholder-plaintiff.”[73] To determine whether the burden shifts in this case, I must consider “whether the special committee was truly independent, fully informed, and had the freedom to negotiate at arm's length.”[74] To establish that a director lacks independence, plaintiff must “create a reasonable doubt that a director is not so ‘beholden’ to an interested director ... that his or her ‘discretion would be sterilized.’ “[75] In order “[t]o create a reasonable doubt about an outside director's independence, a plaintiff must plead facts that would support the inference that because of the nature of a relationship or additional circumstances ..., the non-interested director would be more willing to risk his or her reputation than risk the relationship with the interested director."[76]

***10** At trial, the evidence easily met this exacting standard, demonstrating that the Special Committee was independent, fully informed, and that it had negotiated with Hallmark at arm's length. First, plaintiff made no arguments regarding the independence of Lund and Granath, two of the three members of the Special Committee. Second, plaintiff failed to convince me that the other member, Jennings, lacked independence.

Plaintiff makes several arguments as to why Jennings lacks independence, but none of them were enough to create a reasonable doubt as to his independence. First, plaintiff contends that because of his nomination by Hallmark to the board of Crown, Jennings lacks independence. The mere nomination of a director by a majority stockholder, however, is insufficient to demonstrate lack of independence.[77] It was established at trial that aside from his service on the board of Crown, Jennings has no business or personal relationship with any of the other Crown directors.[78] Next, plaintiff points to Jennings's service for various charitable and civic organizations, and his involvement with the University of Kansas (which receives financial support from Hallmark) to challenge his independence. Although Jennings has served on the boards of numerous nonprofit organizations in the Kansas City area, none of the positions raise reasonable doubts about his independence. Moreover, plaintiff asserts that several members of the Hall family attended the University of Kansas and that the Hall family made significant donations to the University of Kansas. Plaintiff also contends that Jennings's fundraising efforts for the University of Kansas are themselves sufficient to undermine his independence. Jennings, however, has never solicited from Hallmark or the Hall family on behalf of the University of Kansas. Furthermore, Jennings does not receive any compensation for his service on University of Kansas-affiliated boards. Although he did receive a salary for his three month job as the University of Kansas's interim athletic director, he returned his salary to the University when his term was up.[79]

All these facts illustrate that cases like *In re Oracle Corp. Derivative Litigation*[80] (which involved a special litigation committee) do not apply here. For example, in *Oracle* and other similar cases, the special committee members were paid a salary by the university that received the donations, and they personally solicited donations from (or had other substantial dealings with) the donors. In short, plaintiff failed to persuade me that Jennings was beholden to or under the domination of Hallmark or the Hall family, or that Jennings was "disabled from exercising independent judgment."[81]

Accordingly, I find that all three members of the Special Committee were independent, and approved the transaction after an arm's length negotiation. Thus, plaintiff bears the burden of showing that the Recapitalization was unfair given the undisputed evidence that the transaction was approved by an independent and disinterested special committee of directors. I now begin my analysis by examining the issue of fair dealing and then turn to the related issue of fair price.

B. Fair Dealing

***11** Along with the board's composition and independence, "fair dealing addresses the timing and structure of negotiations as well as the method of approval of the transaction."[82] Considering theses factors, for the reasons set forth below, I find that the process followed here was entirely fair.

1. *Hallmark's Timing of the Recapitalization*

Plaintiff argues that Hallmark opportunistically timed its original Recapitalization proposal to burden Crown with debt as the initial step in a devised plan in which it could exercise leverage over Crown to maneuver a "perfect storm" and force recapitalization at a critical moment in Crown's life cycle.[83] Given the fact that Hallmark had all along sought a meaningful solution to Crown's crumbling capital structure, I do not accept plaintiff's contention that Hallmark had devised an elaborate scheme to unfairly time the Recapitalization. To begin with, Hallmark did not have any legal obligation to continue to waive Crown's debt obligations. Like the majority stockholder and creditor in *Odyssey Partners, L.P v. Fleming Companies, Inc.,*[84] Hallmark did not have an obligation to defer payments or to make other financial concessions for the sake of Crown, or its minority stockholders.[85] As former Chancellor Allen observed in *Thorpe v. CERBCO, Inc.,* "controlling shareholders, while not allowed to use their control over corporate property or processes to exploit the minority, are not required to act altruistically towards them."[86] Moreover, the evidence at trial indisputably showed that there was no tangible way that Crown would be able to meet its debt obligations when they were due, and that Crown had no real options other than a recapitalization or bankruptcy. Given the fact that Crown's debt crisis had developed over the years with unprofitable and not-promising operations, it is evident that Crown did not have a solution that would provide a better opportunity for future value than a recapitalization. Thus, I find that plaintiff's evidence falls far short of demonstrating Hallmark's having unfairly timed the Recapitalization.

Unfortunately that is not all of the bad news for the plaintiff. There are other reasons why plaintiff's unfair timing theory fails as well. Plaintiff's unfair timing theory is premised almost entirely on the approximately $3 billion valuation of Crown by plaintiff's expert witness, Daniel R. Schechter. I am not able to accept this theory, however, when Schechter's valuation cannot explain why no potential buyer or valuation expert (other than Schechter himself) ever perceived Crown's value to exceed its debt. First, if plaintiff's theory were correct, Hallmark would have accepted the Special Committee's offer to take Crown private (because Hallmark would have benefited from Schechter's additional $2 billion of value had it in fact existed). Second, during the nine months between the Hallmark Proposal (May 2009) and the Special Committee's approval of the Recapitalization (February 2010) in which plaintiff argues that Crown was in the "sweet spot" on the "proverbial hockey stick," none of the potential buyers tried to capture this purported upside by offering terms better than Hallmark's proposal. Third, when Hallmark saw the upside in Crown's "life cycle," surely at least one of the other sophisticated industry players and private equity buyers (players that Schechter noted regularly advise on potential cable acquisitions) would have attempted to take advantage of the purported "sweet spot" as well by offering to pay more than the value implied by the conversion price in the Recapitalization. No one did. Lastly, plaintiff argues that Hallmark proposed the Recapitalization at a critical time in Crown's life cycle, during a brief period after Crown had turned the EBITDA positive but before it shot up the curve to profitability. On this specific point, I agree with and fully credit Hallmark's expert witness (Professor Jerry A. Hausman) that absent a material change in expected cash flows, a short interval in time between two DCF valuations will not produce the type of dramatic change in value that plaintiff's theory posits. Hausman explained that only "new (unexpected) information" (the type of information that could materially affect Crown's cash flows)—not changes in the timing of a valuation—would be required to explain the dramatic change in values.[87] Unless something changes that would materially affect the expected future cash flows (and no such change occurred here), the timing of the valuation should not produce the type of change in value that plaintiff assumes. Thus, it is clear to me that plaintiff's unfair timing theory is flawed.

2. *The Special Committee's Formation and Selection of Counsel*

***12** The members of the Special Committee have extensive business and industry experience, including Lund's and Granath's experience in the television and cable industries. Plaintiff alleges that Hallmark improperly controlled the Special Committee's formation and operation, and in particular that Jennings was not independent.[88] Plaintiff attempts to show this by pointing to preliminary discussions that Jennings had with Brian Gardner, General Counsel of Hallmark and Secretary of Crown. Plaintiff insists these discussions somehow were improper, but does not allege that any of these preliminary discussions involved the substance of the Hallmark Proposal or the Recapitalization. Furthermore, no evidence exists of any discussions between Gardner and members of the Special Committee once the Special Committee was formed, other than in connection with meetings of the full Crown board.[89]

Finally, I do not recognize any legitimate issue that can be raised concerning the Special Committee's independence or the integrity of its process in its selection of one of the attorneys, Mark Gentile of RLF, identified by Gardner. Lund independently suggested Gentile, because he had previously worked with Gentile on a special committee assignment with another board.[90] At this time, Jennings also asked Gardner to see if Hallmark's Delaware counsel could suggest other Delaware counsel with experience in representing special committees (and with no Hallmark conflict).[91] Among the counsel identified by Gardner's Delaware counsel was Gentile of RLF. Then, Lund recommended Gentile to the Special Committee.[92] Based on Lund's recommendation, and the firm's reputation, the Special Committee retained RLF as its counsel. Thus, the record is clear that it was Lund's recommendation of Gentile that led the Special Committee to retain RLF. Finally, no evidence exists that Gentile had any ties to Hallmark or had any reason to favor Hallmark's interests over those of the Special Committee and Crown's minority stockholders. Based on this record, I find that the Special Committee (including its members, formation, and selection of counsel) is independent of Hallmark.

3. *The Special Committee's Mandate*

As respected practitioners have noted, "in the context of a conflict transaction, the importance of the committee's charter cannot be overstated."[93] In addition to being independent, a well-constituted special committee must have a "clear mandate setting out its powers and responsibilities in negotiating the interested transaction."[94] This Court has stated that "this mandate should include the power to fully evaluate the transaction at issue, and, ideally, include what this court has called the 'critical power' to say 'no' to the transaction."[95] Here, the members of the Special Committee interpreted their clear mandate broadly to include the power to consider the Hallmark Proposal, negotiate its terms, consider alternatives to the transaction, and ultimately recommend or reject the Hallmark Proposal.[96] Each member of the Special Committee understood that his role was to represent the interests of the minority stockholders of Crown.[97] Moreover, the Crown board could not approve the Hallmark Proposal without a favorable recommendation from the Special Committee.[98]

***13** Plaintiff contends that the Special Committee was "hamstrung by its narrow mandate"[99] (which according to plaintiff was limited to negotiating the Hallmark Proposal) and was thus unable to consider alternatives to the Hallmark Proposal. This argument is meritless as it is contrary to the evidence described above and set forth at trial. First, plaintiff selectively omits quotations from the Resolutions themselves, which broadly empowered the Special Committee to "consider such matters as it deems advisable with respect to the Recapitalization Proposal" and "take such further action, at the Company's expense, as the Special Committee deems appropriate in order to carry out the intent and purpose" of the resolutions.[100] Second, as noted above, each member of the Special Committee viewed the committee's mandate broadly as allowing it to consider the Hallmark Proposal, negotiate its terms, recommend (or not recommend) the Hallmark Proposal, and also to consider any and all alternatives to the Hallmark Proposal.[101] For example, the Special Committee had initially proposed a go-private transaction to Hallmark, which was rejected. Third, Morgan Stanley repeatedly advised the Special Committee on alternatives to the Hallmark Proposal. Fourth, the Special Committee encouraged and incentivized Morgan Stanley to pursue alternatives, such as a sale, in its engagement letter.[102] Lastly, the Special Committee commissioned a press release announcing to the world that the Special Committee was "considering Hallmark Cards' proposal *as well as the Company's other alternatives.*"[103] Finally, plaintiff alleges that Hallmark drafted the Special Committee's Resolutions. Plaintiff, however, overlooks the fact that the Special Committee's counsel completely revised the Resolutions.[104] Therefore, I find that the Special Committee was well aware of its mandate, interpreted that mandate broadly, understood that it had the power to reject the Hallmark Proposal and understood that its role was to represent the interests of Crown's minority stockholders.

4. *The Special Committee's Financial Advisors*

The Special Committee retained Morgan Stanley as one of its two independent financial advisors. As a second financial advisor, the Special Committee retained Houlihan based on the firm's reputation and on the strength of previous work that Houlihan had done for Crown. Morgan Stanley was independent from both Hallmark and Crown, and Houlihan was independent of Hallmark. Morgan Stanley and Houlihan did not work together, and neither saw the other's work.[105] Houlihan provided the Special Committee with an analysis of the *pro forma* impact of the Recapitalization on the minority stockholders, as well as a fairness opinion as to Crown.[106] Morgan Stanley did not provide a fairness opinion, but did advise the Special Committee to approve and recommend the Recapitalization.[107] The recommendation was an essential part of Morgan Stanley's retention at the outset.[108]

***14** Pursuant to 8 *Del. C.* § 141(e), the Special Committee was entitled to rely on the "information, opinions, reports or statements"[109] presented by Morgan Stanley and Houlihan. Morgan Stanley's recommendation was supported by months of work and an understanding of the cable industry and Crown's business.[110] Morgan Stanley and Houlihan were selected with reasonable care, the Special Committee reasonably believed that the task was within their professional or expert competence, and their analyses were "not so deficient that the [special] committee would have reason to question [them]."[111] In addition, under Delaware law, there is no requirement that the Special Committee obtain a formal fairness opinion as to the minority stockholders, particularly in light of the strength of the advice it received.[112] Thus, I find that the recommendation from Morgan Stanley, the fairness opinion from Houlihan, and the analysis of the *pro forma* impact on the minority stockholders from Houlihan were sufficient to satisfy the Special Committee's duty of care.

5. *The Special Committee's Process and Arm's–Length Negotiations*

Another critical issue in the fair dealing inquiry is "whether the Special Committee functioned as an effective proxy for arms-length bargaining, such that a fair outcome equivalent to a market-tested deal resulted."[113] That is, a special committee "must function in a manner which indicates that the controlling shareholder did not dictate the terms of the transaction and that the committee exercised real bargaining power 'at an arms-length.' "[114] After reviewing all the evidence that was produced at trial and the parties' written submissions, I find that the Special Committee functioned independently of Hallmark and reached the best deal possible through intense negotiations that were appropriately adversarial.

The Special Committee met formally twenty-nine times over a period of nine months. The Special Committee's legal advisors were present at each one of them. After Morgan Stanley was retained, representatives of Morgan Stanley (usually including Robert Kindler, the Global Head of Mergers and Acquisitions at Morgan Stanley) attended every one of the Special Committee's meetings. The members of the Special Committee relied on the professional advice provided by their legal and financial advisors. Notably, each member of the Special Committee assumed an active role in the process (outside its internal meetings) including speaking with a third party regarding potential interest in Crown (Lund), meeting with Muoio to discuss his concerns (Granath), actively facilitating negotiations (Jennings), and negotiating face-to-face with Hallmark (Lund).[115]

As stated earlier, the Special Committee evaluated and actively searched for alternatives to the Hallmark Proposal, including a third-party sale, a third-party refinancing, a potential bankruptcy, and continuing the status quo. After reviewing the alternatives, Morgan Stanley advised the Special Committee that neither a sale nor a refinancing was a viable option.[116] Indeed, at trial, Kindler was resolute about Morgan Stanley's views on the alternatives.[117] It also is undisputed that the Special Committee initially refused to negotiate the Hallmark Proposal and instead made its own proposal that Hallmark take Crown private, even though Hallmark had previously indicated that it was not interested in such a transaction.[118] In light of Morgan Stanley's involvement in the process of evaluating the Hallmark Proposal and considering the alternatives, as well as Morgan Stanley's deep familiarity with the market, I reject plaintiff's assertion that Morgan Stanley somehow failed to comprehend the opportunities in the market and that the Special Committee erred in relying on Morgan Stanley.

***15** After Hallmark refused to consider a go-private transaction, the Special Committee started to contemplate and address the terms and conditions for recapitalizing the Company. The Special Committee, with advice from Morgan Stanley, pushed back against the Hallmark Proposal and pursued a negotiating strategy designed to provide as much benefit as possible to the minority stockholders.[119] Morgan Stanley's proposed negotiating strategy was to choose a value for Crown at the low end of Morgan Stanley's range ($500 million), give Hallmark new debt equal to that number, and allow the minority stockholders to share in the upside above that number.[120] The Special Committee adopted this strategy, which eventually worked. In the Recapitalization, Hallmark received credit for $500 million of its debt, and Crown's minority stockholders were given the opportunity to share in Crown's value above $500 million.[121] Given this result, in which Crown's minority stockholders would have some opportunity to realize value as opposed to none, it is clear that the Special Committee's arm's-length negotiating strategy ultimately resulted in a benefit to the minority.

The Special Committee initially suggested the go-private transaction to counter Hallmark's recapitalization proposal, and when it determined that Hallmark had not made adequate concessions in response to its first counterproposal, the Special Committee refused to negotiate altogether, thereby forcing Hallmark to bid against itself and to make additional concessions. This adversarial conduct bespeaks independence, and confirms the arm's-length nature of the bargaining process.

Although the Special Committee eventually acceded to Hallmark's proposal that Hallmark own more than 90% of Crown's common shares after the Recapitalization, the Special Committee secured a binding standstill agreement that requires, among other things, independent director approval for a future short-form merger or third-party sale until December 31, 2011, and a potential $0.50 per share premium to the non-Hallmark stockholders in the event of a third-party sale until December 31, 2013. Furthermore, the Special Committee insisted on a majority-of-the-minority condition.[122] Kindler thought it unlikely that Hallmark would ever agree to such a condition,[123] but he nonetheless advised the Special Committee to maintain its position "if, for nothing else, for negotiating leverage."[124] The Special Committee eventually dropped the majority-of-the-minority condition near the end of the negotiations, in exchange for other favorable concessions from Hallmark.[125]

In the end, the Special Committee got a great result for Crown's minority stockholders. Its advisors believed and advised the Special Committee that the Recapitalization was a more attractive and viable option for Crown's minority stockholders than any other alternatives available to the Company. Accordingly, I find that the negotiated Recapitalization terms were the product of a thorough, effective, and independent Special Committee.

C. Fair Price

***16** Fair price "relates to the economic and financial considerations of the proposed [transaction], including all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock."[126] "When conducting a fair price inquiry as part of the entire fairness standard of review, the court asks whether the transaction was one 'that a reasonable seller, under all of the circumstances, would regard as within a range of fair value; one that such a seller could reasonably accept.' "[127] Here, the answer is yes, it was.

For purposes of determining whether the Recapitalization fairly valued Crown, I will first discuss the terms of the Recapitalization and then briefly review the various methodologies employed by the parties' experts in their determination of Crown's value at the time of the transaction. On the basis of that review, I then assess which methodologies are most appropriate under Delaware law and in light of the particular circumstances of this case.

1. *Terms of the Recapitalization*

The "range of fairness" aspect of the fair price inquiry "has most salience when the controller has established a process that simulates arm's-length bargaining, supported by appropriate procedural protections."[128] That is, "[a] strong record of fair dealing can influence the fair price inquiry, reinforcing the unitary nature of the entire fairness test."[129]

Here, the Special Committee's process, its demonstrated independence and arm's-length negotiations, the advice it received from its financial advisors, and the result it achieved all lend support to the conclusion that the Recapitalization was entirely fair. Crown was saddled with debt; it was essentially insolvent, seeking another extension of the Hallmark debt waiver, and faced a real threat of bankruptcy. Those are the brute facts concerning this company. The Special Committee, based on advice from its advisors, determined that the Recapitalization was the best alternative for Crown's minority stockholders.[130] As one of the Morgan Stanley representatives stated at trial: "Going into this, if you were a non-Hallmark stockholder, what you owned was equity in a company with about $1.2 billion worth of debt. And the only way you could ever achieve any value is if the company was worth more than $1.2 billion, which it wasn't. Here, by lowering the threshold to [$]500 million, we felt you were giving the equity, which started out with no value, something that had real value."[131] In addition, plaintiff's own expert, Schechter, conceded that absent the Recapitalization, Crown would not have survived long enough to realize any future value, much less value above the level of Hallmark's debt.[132] Thus, without a recapitalization, Crown was facing insolvency and its equity was worthless.

Two decisions by this Court are instructive—*In re Vision Hardware Group, Inc.,*[133] and *In re Hanover Direct, Inc. S'holders Litigation.*[134] In *Vision Hardware,* Better Vision "was an insolvent company that was in default on substantial obligations, with even greater obligations falling due in its immediate future," and with no other realistic alternative to bankruptcy.[135] TCW, a creditor of Better Vision, agreed to purchase all of Better Vision's outstanding senior and subordinated debt and sought to cash out the minority of Better Vision. Although *Vision Hardware* was a statutory appraisal action (which this is not), the Court (as here) was faced with how to value a company's debt where the company itself was on the brink of bankruptcy and had no ability to refinance its debt. Former Chancellor Allen noted that a corporation's long-term, "going concern" value becomes irrelevant and instead its value in bankruptcy becomes the relevant metric for determining fair value.[136] Thus, the *Vision Hardware* Court recognized that when a company's going concern value comes close to its liquidation value (with the increasing risk of bankruptcy) its equity value may approach zero.[137]

***17** Now consider *Hanover,* which involved a go-private merger without a special committee. Hanover's debt commitments exceeded the value of its common stock and, thus, the company was heading towards insolvency. The controlling stockholder increased its holdings of Hanover debt and preferred stock. Then it proposed a recapitalization that eliminated Hanover's minority stockholders. The *Hanover* Court found that the value of Hanover's equity was "already below sea level," and concluded that "a merger price above $0.00 (in [that] case, $0.25 per share) was entirely fair."[138]

Crown would have faced bankruptcy without a recapitalization or further forbearance by Hallmark. Plaintiff here asks me to disregard the economic reality which Crown faced. But treating Crown as if it had no liquidity crisis would require me to ignore the credible evidence adduced at trial.[139] This I cannot do. Thus, I conclude that the Recapitalization was entirely fair on its face. Nonetheless, in the interest of completeness, I will review the expert opinions.

2. *The Experts*

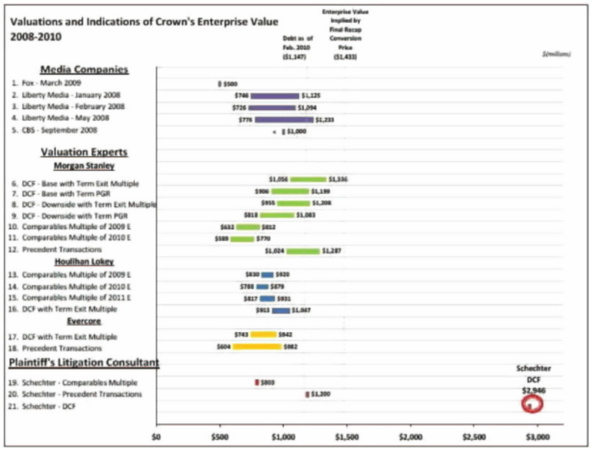
As has become common in entire fairness proceedings of this sort, the parties presented the testimony of competing valuation experts in an effort to convince me that their valuation was the most accurate.[140] At trial, plaintiff presented the expert testimony of Daniel R. Schechter from L.E.K. Consulting, LLC, and Professor Robert Hamada from the University of Chicago Booth School of Business. Schechter, abjuring all other valuation methods, only relied on a DCF analysis. Hamada, who was presented as a rebuttal expert in response to Hallmark's valuation expert, primarily identified alleged mistakes in Morgan Stanley's valuation of Crown.

As for defendants, the Special Committee presented the testimony of Christopher Lee, the Executive Director of Morgan Stanley and Richard De Rose, the Managing Director of Houlihan, to rebut Schechter's expert testimony. Hallmark presented the expert testimony of Jerry A. Hausman, the MacDonald Professor of Economics at the Massachusetts Institute of Technology. In contrast to plaintiff's valuation experts (Schechter and Hamada), Hausman is an expert on the cable television industry and the economic trends in that industry. And unlike Schechter, Hausman believes that a DCF analysis is more reliable when it can be verified by alternative valuation methods. Importantly, plaintiff did not cross-examine Hausman at trial.

This case (as earlier noted) is similar to *In re Hanover Direct, Inc. S'holders Litigation,* where the Court found that a merger price of $0.25 per share was entirely fair because the subject company's equity actually had zero value.[141] In *Hanover,* plaintiffs' expert rejected management's projections and relied solely on a single valuation methodology, while defendant's expert used a more robust approach involving multiple methodologies to support his valuation conclusions.[142] For that and other reasons, the *Hanover* Court assigned full weight to the trial testimony of defendant's expert and no weight to the testimony of the plaintiffs' expert.[143] In this case, Schechter's single methodology valuation of Crown is roughly three times higher than any of the other valuations. The more robust approaches taken by defendants' experts and advisors, however, used multiple valuation methodologies and independently reached results that fell within the same range.[144] Although there certainly may be circumstances where using only one valuation methodology is appropriate and reliable, this is not such a circumstance. Schechter's failure to incorporate other valuation methods into his analysis makes his valuation far less credible.

3. *Schechter's Analysis*

***18** Schechter valued Crown nearly three times higher than all the other valuations at $2.946 billion.[145] This result, which Schechter derived from his own DCF analysis, was an obvious outlier from the other valuations presented at trial. Schechter conducted two other valuations, comparable companies analysis ($803 million) and comparable transactions analysis ($1.3 billion), and rejected those conclusions because those valuation conclusions were "absurdly low" in comparison to his DCF analysis, which valued Crown at almost $3 billion.[146] Such an outlier valuation has caused credibility concerns in other cases before this Court.[147] The chart reproduced below visually demonstrates just how far off Schechter's single methodology valuation was as compared to the multiple valuations of Crown that had been performed by the various financial advisors engaged by the Special Committee and Hallmark, as well as other industry players who had previously looked into acquiring Crown.[148]



As the chart plainly reveals, Schechter's sole valuation of Crown using his own DCF methodology was wildly divergent from all other valuations. Hausman,[149] on the other hand, recognized the economic reality that real-world valuations done by potential buyers are "often the best source of economic information" about the value of a company.[150] Even if the generally-preferred DCF valuation approach is used, it is only reliable when it can be verified by alternative methods to DCF or by real world valuations, including especially, valuations performed by potential third-party buyers.[151]

As described earlier, Crown had been "on the market" since 2005 and management had vigorously pursued a sale. Crown's CEO, Schleiff, had a significant financial incentive to find a buyer. In the end, however, Crown was not successful in locating a buyer willing to pay even the value of Crown's debt, let alone above its debt. Hausman opined that the offers and expressions of interest in Crown by potential buyers are relevant indicators of Crown's value, especially the most recent offer by Fox in 2009 that valued Crown at approximately $370–500 million and an earlier analysis by Liberty Media in 2007 that valued Crown at approximately $466–997 million.[152] Thus, in assessing the reliability of Schechter's valuation, Hausman noted that "no observed market valuation, in either the pre-recession period or more recently (where Schechter is doing his valuation) came anywhere close to Mr. Schechter's claimed amount of $2.95 billion."[153] I agree with Hausman. If Crown was really worth $2.95 billion (as Schechter claims), the most knowledgeable and sophisticated buyers in the industry would not have readily passed on an opportunity to obtain substantial returns on an investment in Crown.[154] Because Crown's own financial statements and projections indicated that Crown had insufficient cash flow to support its debt service, Hausman reasonably determined that Crown's value was less than its debt.[155] Hausman's conclusion that the equity value was *"zero"* was in line with Morgan Stanley's analyses and was consistent with Evercore Partner's $1.025 billion valuation of Crown.[156] And again, it was consistent with earlier offers and valuations by sophisticated players in the industry, all of whom independently concluded that Crown's value is less than its debt.

***19** I am convinced that the way in which Schechter arrived at a value nearly three times that of any other valuation is flawed. Below are a few of the specific reasons that cause me to reject Schechter's opinion:

- Schechter's DCF analysis ignored management's contemporaneous projections and used his own hypothetical and overly optimistic set of projections. This Court has consistently recognized the importance of management's contemporaneous projections because "the outcome of a DCF analysis depends heavily on the projections used in the model."[157] Valuations that have ignored or altered management's contemporaneous projections are "sometimes completely discounted."[158] Here, Schechter had no legitimate reason for abandoning management's projections in favor of his more optimistic estimates developed in only a short period of time and without access to Crown's management or its data. And it was unreasonable to substitute his personal judgment for "the non-litigation business judgment of [the Company's] management."[159] Schechter disapproved management's projections for simply being too low.[160] In addition, Brian Stewart, former CFO of Crown, explained in detail that management's five year projections are created with significant input and involvement from management.[161] After an extensive review process, the five year projections are approved by the CEO and finance committee, and are presented to the full board of directors for approval.[162] Thus, I am convinced that management's projections are carefully crafted and reasonable. This kind of reliable information (i.e. reasonable management projections) should have been used by Schechter in his valuation instead of his own Panglossian views.

- Schechter unreasonably extended his optimistic projections to 2024. Crown's management, well aware of Crown's economic reality and its day-to-day operations, considers it problematic to project out more than five years.[163] Hausman explained in his rebuttal that uncertainty increases with the length of projections.[164] The Special Committee's advisors used the 2013 projections provided by Crown's management.[165] Schechter provides no explanation why he is in a better position than Crown's management (which has consistently used three to five year forecast periods) to make projections extending out fourteen years. Tellingly, plaintiff's other expert, Hamada, did not opine that Crown's management projections were of inappropriate or insufficient length for a proper DCF analysis.[166]

- Schechter's valuation disregards all the contemporaneous evidence of Crown's value, as well as the economic reality facing Crown. Indeed, Hausman believed that Schechter's "valuation fails an economic reality test."[167] Not one of the many (at least eighteen) valuations of Crown done between 2008 and the time of the Recapitalization was even close to Schechter's DCF valuation. As Vice Chancellor Laster recently noted, "what you actually like to see when you're doing a valuation is some type of overlap" between the various methodologies.[168] Well, as the chart on page 51 comparing the various valuations of Crown shows, Schechter's DCF analysis does not "overlap" with anything. But as Kindler and the Special Committee members testified at trial, every media company knew that Crown had been for sale since 2005. Three sophisticated industry players had considered Crown around the time of the Hallmark Proposal, and none of their views on value were remotely close to Schechter's DCF-they all pegged Crown's enterprise value at less than Crown's debt to Hallmark. This Court in *Gray v. Cytokine Pharmasciences, Inc.* looked to offers made by potential buyers in the three years before a transaction and found that those valuations supported the conclusion that the plaintiff's "off the charts" expert was not credible.[169] There, then-Vice Chancellor Lamb concluded that the expert's valuation was an "extreme variation from the pack" as compared to all other valuations and was thus an unreliable outlier.[170] Schechter, here, is similarly "off the charts" and I find his valuation to be unreliable. Even more oddly, Schechter ignores the Hallmark debt. He valued the Company disregarding this financial reality and did not consider Crown as a "financially distressed" company. Although Schechter baldly states that the possibility of bankruptcy was "wildly implausible and somewhat ridiculous," I find it quite plausible that bankruptcy would have been Crown's future if it had maintained the status quo.[171]

- *20 Schechter rejected both of his own market-based analyses because he was not satisfied with the results.[172] He thus relied on only one valuation methodology to support his conclusions-his "off the charts" DCF analysis. This Court has recognized that "the DCF valuation has featured prominently in this Court because it 'is the approach that merits the greatest confidence within the financial community.' "[173] Notwithstanding that general statement, the Court also gives more credit and weight to experts who apply "multiple valuation techniques that support one another's conclusions" and that "serve to cross-check one another's results."[174] Although it is true that a DCF valuation is certainly a dependable and commonly used valuation methodology, practitioners, academics, and the experts in this case acknowledge that it has its own limits and weaknesses.[175] Thus, it is preferable to take a more robust approach involving multiple techniques —such as a DCF analysis, a comparable transactions analysis (looking at precedent transaction comparables), and a comparable companies analysis (looking at trading comparables/multiples)—to triangulate a value range, as all three methodologies individually have their own limitations.[176] Here, under Schechter's comparable companies analysis, Crown had a value of $803 million, and under his comparable transactions analysis, Crown had a value of $1.2 billion.[177] Both of those numbers fall within the ranges found by Morgan Stanley and Houlihan. Schechter, however, rejected each of those valuations as "absurdly low" and "unreasonably low," respectively, and he gave them "no weight."[178] Like petitioners' expert in *Hanover,* because Schechter failed to clearly and persuasively provide any acceptable reasons for his outlier result, his methodology leaves me with little confidence in his valuation.[179]

4. *Hamada's Analysis*

Hamada's expert opinions, proffered as rebuttal to Hausman's expert report, were less a "rebuttal" to Hausman's opinions than Hamada's (and plaintiff's) effort to attack Morgan Stanley's valuation.[180] Hamada's opinions, however, are without any basis and ignore all the significant and relevant economic realities of Crown.

First, Hamada did not criticize Hausman's opinions that the offers and expressions of interest for Crown by key market players are important economic indicators to be considered in determining Crown's value.[181] Thus, it is not surprising that Hamada did not examine the offers by Liberty Media or Fox.[182] After all, he is not an expert in the cable television business, and was not in a position to adequately evaluate the contents of those offers.[183]

Second, Hamada did no analysis regarding Crown's sustainable capital structure growth, with or without the Recapitalization.[184] Hamada did not know that Hallmark, in connection with its Hallmark Proposal, would not extend its waiver and standstill beyond May 1, 2010.[185] He also was not aware that "Crown's auditors had issued a going-concern opinion for the year ended 2009," and that its revolving credit line was set to expire in 2010.[186] Indeed, Hamada did no analysis of Crown's liquidity situation in 2010 or any other year.[187]

***21** Third, Hamada's argument that Morgan Stanley mixed "apples and oranges" in its DCF valuation was misguided as well as based on Hamada's misapprehension of the facts. Specifically, Hamada argued that Morgan Stanley mixed firm-specific costs of equity and debt with an industry-average capital structure, and that this error led to an exaggerated WACC and deflated valuation of Crown.[188] Apparently, there was confusion over what each expert (Hamada and Lee) said and heard, but the evidence is clear that Morgan Stanley used a post-recapitalization cost of equity and a post-recapitalization cost of debt, along with a post-recapitalization target capital structure.[189] As a result, Hamada ultimately conceded that Morgan Stanley's approach (using a post-recapitalization cost of equity and debt, and target capital structure) would be an "apples-to-apples comparison," and at trial he confirmed this concession.[190]

Fourth, Hamada's criticism of Morgan Stanley's terminal value calculation is without merit. Morgan Stanley conducted two different terminal value calculations: a perpetuity growth rate and an exit multiple. Hamada argued that Morgan Stanley unjustifiably used low perpetuity growth rates (1–3%) and terminal multiples (or exit multiples) (6.5–8.5) to calculate Crown's terminal value.[191] He theorized that both methods adopted by Morgan Stanley contributed to an unreasonable decline in future growth rates, all of which resulted from Crown management's truncated projections.[192] At trial, however, Lee (for Morgan Stanley) testified that the purported decline between the explicit forecast period and the terminal period is typical.[193] In addition, the undisputed testimony showed that Morgan Stanley's exit multiple calculation had no precipitous decline in growth rates.[194] Ultimately, therefore, Hamada failed to convince me that Morgan Stanley's perpetuity growth rate was unreasonable or that its exit multiple calculation created a "cliff-like drop."

Finally, Hamada is not a restructuring expert and has never been paid to advise on a corporate restructuring.[195] As Hamada admitted, he has not offered an opinion as to whether the Recapitalization is fair to Crown or to its non-Hallmark stockholders—either in his rebuttal report or his trial testimony. In short, Hamada's opinions do not establish that the Recapitalization was unfair.

In sum, because Crown's outstanding debt exceeded the value of its equity before the Recapitalization, and because defendants' proffered expert testimony persuasively and thoroughly supported their valuation conclusions (and plaintiff's experts failed to convince me otherwise), I conclude that the Recapitalization was entirely fair.

III. CONCLUSION

For all the foregoing reasons, I find in favor of defendants and conclude that the process and the price of the Recapitalization were entirely fair. An Order consistent with this Memorandum Opinion has been entered.

All Citations

Not Reported in A.3d, 2011 WL 863007

Footnotes

[1] The relevant affiliates are defendants Hallmark Entertainment Investment Co., Hallmark Entertainment Holdings, Inc., H C Crown Corp., and H.A., Inc.

[2] I have considered the parties' briefing regarding numerous outstanding objections to the admissibility of testimony, reports, exhibits, documents, demonstrative exhibits, rebuttal exhibits and testimony, and handwritten notes. I overrule all of the objections and admit all of the items which are the subject of these continuing objections. I will accord each item the weight and credibility that it appropriately deserves.

[3] *See* JX 145 (Crown Schedule 13D/A); JX 85 (Crown Form 8–K (June 29, 2010)).

[4] Trial Transcript ("Tr.") 583–87 (Granath).

[5] Tr. 588–89 (Granath).

[6] Tr. 428–30 (Lund).

[7] Tr. 431 (Lund).

[8] *See, e.g.,* Tr. 663–64, 673, 734–37 (Jennings).

[9] Pre–Trial Stipulation and Order ("PTO") ¶ 26.

[10] Joint Ex. ("JX") 99 (Crown Corporate History).

[11] Tr. 597 (Granath).

[12] JX 99 (Crown Corporate History).

[13] *See* JX 305.

[14] PTO ¶ 28.

[15] JX 84 (Crown Form 14C (May 21, 2010)).

[16] Tr. 434–35 (Lund).

[17] Tr. 745 (Griffith).

[18] Tr. 747–48 (Griffith).

[19] Schleiff's employment contract provided a substantial incentive, a bonus of at least $6 million ($6–9 million), if he was successful in selling the Company. He used his extensive industry contacts and connections to constantly pitch Crown to all players in the industry. *See* Tr. 433 (Lund); 594 (Granath); 748 (Griffith); JX 312 (Crown Form 8–K (Oct. 6, 2006)).

[20] Tr. 749 (Griffith).

[21] Tr. 749–50 (Griffith).

[22] Tr. 756–58 (Griffith).

[23] Tr. 760–61 (Griffith).

[24] In the midst of these attempts and processes, in 2007, Crown was negotiating its agreements with the major cable service providers that provided Crown's programming to cable television subscribers. Crown's contracts with Comcast, Time Warner, DirecTV and Echostar (which together control about 70% of Crown's cable distribution) were set to expire during 2007. Accordingly, Hallmark extended the waiver and standstill on Crown's debt because Hallmark recognized that failing to extend could negatively impact the negotiations and any sale prospects. Thus, in late 2007 and early 2008, Schleiff successfully negotiated Crown's multi-year contracts with major cable service providers: Comcast, extended to 2022, DirecTV to 2017, and Time Warner and Echostar to 2012. *See* Tr. 746–47 (Griffith).

[25] Tr. 763–64 (Griffith); 818 (Hall).

[26] PTO ¶ 29; JX 23 (Crown Form 8–K (May 28, 2009)).

[27] JX 48 (Sept. 28, 2009 Minutes) at 3.

[28] PTO ¶ 29; JX 24 (May 28, 2009 Proposal Letter).

[29] *Id.*

[30] JX 423 (Resolutions for the Appointment of a Special Committee ("Resolutions")).

[31] *Id.*

[32] In its engagement letter, the Special Committee sought to give Morgan Stanley an incentive to find a sale transaction as an alternative to the Hallmark Proposal. *See* JX 431 (Morgan Stanley Engagement Letter) at SC00000707 ("[A]t its sole discretion, the Committee will consider paying Morgan Stanley an additional 'Discretionary Fee' in connection with any Recapitalization or Sale Transaction, as the case may be, which will

be based upon the performance of Morgan Stanley during the course of the engagement."); Tr. 837 (Kindler) ("My expectation was if there was a sale transaction, that we would get a higher fee than for recapitalization.").

33 JX 612 (Press Release (July 14, 2009)); Tr. 672–73 (Jennings).

34 Tr. 259, 262–63(Lee); 604 (Granath); 683–84 (Jennings); JX 43 (Sept. 11, 2009 Minutes); JX 448 (Morgan Stanley Sept. 11, 2009 Presentation).

35 JX (Sept. 11, 2009 Minutes); Tr. 446–47 (Lund).

36 JX 56 (Nov. 23, 2009 Minutes).

37 Tr. 768 (Jennings); 745, 796 (Griffith).

38 Tr. 424–25(Lee); 888–89 (Kindler).

39 Morgan Stanley also did not view the status quo as a viable alternative because, even if Hallmark agreed, contrary to its public statements, to continue to waive the defaults on its debt, there would be increasing uncertainty in the markets and "no assurance that the shareholders would ever get any value." *See* JX 43 (Sept. 11, 2009 Minutes).

40 Even though Crown had been shopped continuously and was seen as still for sale, Crown had not received any offers or even an expression of interest valuing the Company above its debt. *See* Tr. 450 (Lund); *see also* Tr. 602 (Granath) ("We just finished four years of constant activity trying to sell the thing. If Peter [Lund] and I were not successful with our contacts, certainly Henry [Schleiff], who was in the trade press, as I say every second day, made known to the world that the Hallmark Channel was up for sale. So, you know, unless somebody came out of the woodwork, [a sale] was not a real possibility.").

41 In fact, the Special Committee's legal counsel, RLF, advised the Special Committee that there was a "high risk" of equitable subordination to Hallmark in the event of a bankruptcy. Tr. 639 (Granath). The Committee members agreed it would be "anathema" to Hallmark to force a bankruptcy. Tr. 499–501 (Lund).

42 For example, Hallmark's proposal would extend the maturity of the Crown debt by only five quarters and failed to address the maturity of the JPM Revolver in March 2010 or the mandatory redemption of NICC's debt in December 2010. Under the Hallmark proposal, Crown would be facing another liquidity crisis in less than a year. *See* Tr. 262; JX 43 (Sept. 11, 2009 Minutes).

43 PTO ¶ 33; JX 449 (Special Committee Letter to Hallmark); Tr. 682–83 (Jennings).

44 PTO ¶ 34; JX 47 (HCC Letter to the Special Committee (Sept. 23, 2009)); Tr. 682–83 (Jennings).

45 JX 49 (Morgan Stanley Oct. 1, 2009 Presentation).

46 Tr. 280–81(Lee).

47 Tr. 853 (Kindler) ("They basically accepted our position, and it was the best outcome we could have imagined.").

48 JX 55 (Morgan Stanley Nov. 18, 2009 Presentation).

49 JX 84 (Crown Form 14C (May 21, 2010)).

50 As I understand it, a cash flow sweep is a debt covenant that requires a certain amount of available cash flow to be used for debt service in the event of excess cash flow.

51 JX 58 (Dec. 1, 2009 Minutes); JX 473 (Morgan Stanley Dec. 7, 2009 Presentation).

52 Tr. 283(Lee); 466–67 (Lund); JX 58 (Dec. 1, 2009 Minutes).

53 JX 58 (Dec. 1, 2009 Minutes).

54 JX 73 (Feb. 9, 2010 Minutes).

55 JX 475 (Email from J. Zeberkiewicz (Dec. 10, 2009)).

56 JX 84 (Crown Form 14C (May 21, 2010)) at Ex. D.

57 *Id.*

58 Special Committee Defs.' Post–Trial Answering Br. 26 ("Until December 31, 2011, Hallmark cannot sell its Crown common stock to a third party without prior approval of a special committee of the board composed of solely independent, disinterested directors. From January 1, 2012, to December 31, 2013, however, Hallmark can effect a third-party sale in a 'Premium Transaction,' in which the minority receives an additional $.50 per share premium, or in certain limited public offerings. Beginning January 1, 2014, through December 31, 2020, Hallmark is also restricted in its ability to sell a majority of the Crown stock to a third party."). The

standstill agreement defines a Premium Transaction as a transaction in which all stockholders unaffiliated with Hallmark are entitled to participate and are entitled to receive both: (1) consideration equivalent in value to the highest per-share consideration received by Hallmark in connection with the transaction, and (2) a premium, in cash, equal to $0.50 per share of common stock. JX 84 (Crown Form 14C (May 21, 2010)) at Ex. D.

[59] Before the Special Committee approved the term sheet, in January 2010, the Special Committee learned of a possible deal between Crown and Martha Stewart Living Omnimedia, Inc. (the "MSLO Transaction"). *See* JX 497 (MSLO Transaction Agreement). The Special Committee discussed the business and financial impact of the MSLO Transaction with Crown management. Given the anticipated modest impact on the Company's projected financial performance, and the Committee's evaluation of the inherent risks in the transaction, the Special Committee determined that the MSLO Transaction did not provide the Special Committee with a credible basis on which to extract improved terms from Hallmark. *See* Tr. 468–69 (Lund).

[60] PTO ¶ 35; JX 73 (Feb. 9, 2010 Minutes).

[61] JX 510 (Crown Form 8–K (Feb. 10, 2010)).

[62] *See* Tr. 314(Lee) ("We thought in our view this really was and really is the best alternative that was available to all stakeholders. We went from having a company that had a billion-two of senior secured debt on its balance sheet and having equity, not having any value until liability was satisfied, to having equity controlling—only non-affiliated equity owning 10 percent of the company roughly after only $500 million of value."); *see also* Tr. 869–70 (Kindler) ("I felt, I was actually quite certain, that we had pushed this as far as we could possibly push it. And you know, our job was to do the best job we could do for the non-Hallmark stockholders. And sitting there, looking at all the alternatives, it was very, very clear to us that there was absolutely no way of getting this company refinanced. Or the status quo, where, basically, we just kept on going on with waiver after waiver after waiver. That would have been an awful result for the non-Hallmark shareholders.").

[63] *See* Tr. 185–86 (De Rose).

[64] *See* JX 73 (Feb. 9, 2010 Minutes).

[65] JX 76 (Feb. 25–26, 2010 Minutes).

[66] *See* JX 77 (Houlihan Lokey Fairness Opinion).

[67] *Kahn v. Tremont Corp.,* 694 A.2d 422, 428 (Del.1997) ("Ordinarily, in a challenged transaction involving self-dealing by a controlling shareholder, the substantive legal standard is that of entire fairness."); *Kahn v. Lynch Commc'n Sys., Inc.,* 638 A.2d 1110, 1115 (Del.1994).

[68] *Valeant Pharms. Int'l v. Jerney,* 921 A.2d 732, 746 (Del.Ch.2007) ("[T]he fair dealing prong informs the court as to the fairness of the price obtained through that process.").

[69] *Id.; William Penn P'ship v. Saliba,* 2011 WL 440615 (Del. Feb.9, 2011).

[70] *Emerald Partners v. Berlin,* 787 A.2d 85, 97 (Del.2001) (quoting *Weinberger v. UOP, Inc.,* 457 A.2d 701, 711 (Del.1983)).

[71] *Id.* (quoting *Weinberger,* 457 A.2d at 711).

[72] *Kahn v. Lynch,* 638 A.2d at 1117 (Del.1994) (citing *Weinberger,* 457 A.2d at 710–11).

[73] *Id.* "If the controlling stockholder permits the use of both protective devices [an independent special committee *and* an informed majority of the minority], then the transaction could avoid entire fairness review. *Reis v. Hazelett Strip–Casting Corp.,* 2011 WL 303207, at *10 (Del.Ch. Jan.21, 2011) (citing *In re CNX Gas Corp. S'holders Litig.,* 4 A.3d 397, 400 (Del.Ch.2010); *In re John Q. Hammons Hotels Inc. S'holder Litig.,* 2009 WL 3165613, at *12 (Del.Ch. Oct.2, 2009); *In re Cox Commc'ns, Inc. S'holders Litig.,* 879 A.2d 604, 606 (Del.Ch.2005)). Here, as there was no majority of the minority vote, avoiding entire fairness review completely is not a possibility.

[74] *Kahn v. Lynch,* 638 A.2d at 1120, 1121.

[75] *Beam v. Stewart,* 845 A.2d 1040, 1050 (Del.2004).

[76] *Id.* at 1052.

[77] *See, e.g., Aronson v. Lewis,* 473 A.2d 805, 816 (Del.1984) ("[I]t is not enough to charge that a director was nominated by or elected at the behest of those controlling the outcome of a corporate election. That is the usual way a person becomes a corporate director.").

[78] Tr. 665, 675–76, 735–36 (Jennings).

[79] Tr. 676–77 (Jennings).

[80] 824 A.2d 917 (Del.Ch.2003).

[81] *In re J.P. Morgan Chase & Co. S'holder Litig.,* 906 A.2d 808, 821 (Del.Ch.2005). In addition to being independent and disinterested, the individual committee members impressed me as directors willing to assume the task of the committee "in a rigorous and independent manner." G. Varallo, S. Raju & M. Allen, *Special Committees: Law and Practice* 32–33 (2011).

[82] *Kahn v. Lynch Commc'ns Sys., Inc.,* 669 A.2d 79, 84 (Del.1995).

[83] Pl's Opp'n Post–Trial Br. 42 ("The Recap Proposal was opportunistically timed by Hallmark to coincide with a perceived 'perfect storm' of events that would allow it to increase its controlling stake above 90% at a bargain price, to wit, the confluence of (a) the impending expiration of the Standstill and Waiver, (b) near-frozen capital markets that would allow Hallmark to claim to be [the] 'only game in town,' and (c) a company that had finally turned EBITDA positive, but had not yet shot up the curve of the proverbial 'hockey stick.' ").

[84] 735 A.2d 386 (Del. Ch.1999).

[85] *Id.* at 411 ("Fleming was under no obligation to agree to any of these things, either as a stockholder, a supplier or a creditor."); *see Jedwab v. MGM Grand Hotels, Inc.,* 509 A.2d 584, 598 (Del.1986) ("[T]he law does not require more than fairness. Specifically, it does not, absent a showing of culpability, require that directors or controlling shareholders sacrifice their own financial interest in the enterprise for the sake of the corporation or its minority shareholders.").

[86] 1993 WL 443406, at *7 (Del.Ch. Oct.29, 1993).

[87] JX 87 (Hausman Report) ¶ 18 ("[M]arket prices only change when there is new (unexpected) information.").

[88] Plaintiff focuses on Jennings because it is crystal clear that Lund and Granath are independent of Hallmark. Lund has no relationship with anyone in the Hall family, and he has no personal or business affiliation with any Hallmark entity (other than as a director of Crown). Granath is also disinterested in the Recapitalization and independent of Hallmark and the Hall family. He was asked by Lund to join the Crown board, and he did not know any of the other members of the Crown board or any members of the Hallmark board of directors. Like Lund, Granath has no personal or business relationships with any members of the Hall family, other than as a director of Crown. Again, plaintiff made no arguments regarding the independence of Lund and Granath at trial or in its written submissions. Furthermore, as I have stated above, plaintiff offered no evidence of any financial dealings between Jennings and any member of the Hall family. In *Oracle* and other analogous cases, the committee members were paid salaries by the universities that received the donations. That is not the case here.

[89] Tr. 670–71 (Jennings).

[90] Tr. 441 (Lund).

[91] *See* JX 414 (Email chain regarding Crown Media (May 28, 2009)); Tr. 667 (Jennings).

[92] *See* Tr. 441–42 (Lund); 613 (Granath); 668 (Jennings).

[93] G. Varallo, S. Raju & M. Allen, *Special Committees: Law and Practice* 41(2011).

[94] *Gesoff v. IIC Indus., Inc.,* 902 A.2d 1130, 1146 (Del.Ch.2006).

[95] *Id.*

[96] *See, e.g.,* Jennings Dep. 92–94 ("[I]t has always been our understanding as a committee that we had the broadest of authorities to review alternatives available to the company."); Lund Dep. 92–93 ("Q. Mr. Lund, did you view the scope of the Special Committee's mandate to include exploration of alternatives other than the proposed recapitalization? A.... Yes."); Granath Dep. 59.

[97] *See* Tr. 439 (Lund) ("The special committee's responsibilities were to protect the rights of the minority stockholders."); 671 (Jennings).

[98] *See* JX 423 (Resolutions).

[99] Pl.'s Opp'n Post–Trial Br. 43.

[100] JX 423 (Resolutions).

[101] *See, e.g.,* Tr. 473–74 (Lund); 601–02 (Granath); 671–73 (Jennings).

[102] *See* JX 431 (Morgan Stanley Engagement Letter); Tr. 837 (Kindler) ("My expectation was if there was a sale transaction, that we would get a higher fee than for recapitalization.").

[103] JX 612 (Press Release (July 14, 2009)) (emphasis added); Tr. 672–73 (Jennings); 841–42 (Kindler) ("This kind of reference, looking at all alternatives, is very well understood on Wall Street; that the company is for sale, and that, basically, we'll look at everything, not just a recapitalization, but also any other alternative, including a sale.").

[104] *Compare* JX 115 (original draft of the Resolutions), *with* JX 423 (Resolutions as approved by the Crown board).

[105] *See, e.g.,* Tr. 181–82 (De Rose) ("We did not work with them together."); 890 (Kindler) ("I don't know anything about the Houlihan presentation.").

[106] *See* JX 77 (Houlihan Lokey Fairness Opinion); JX 78 (Houlihan Lokey Feb. 26, 2010 Presentation); Tr. 202 (De Rose).

[107] *See, e.g.,* Tr. 871 (Kindler) ("That is basically Morgan Stanley as an institution telling the special committee that they affirmatively recommend that they do the recap. That is just far stronger than a fairness opinion.").

[108] JX 431 (Morgan Stanley Engagement Letter).

[109] 8 *Del. C.* § 141(e) ("A member of the board of directors, or a member of any committee designated by the board of directors, shall, in the performance of such member's duties, be fully protected in relying in good faith upon the records of the corporation and upon such information, opinions, reports or statements presented to the corporation by any of the corporation's officers or employees, or committees of the board of directors, or by any other person as to matters the member reasonably believes are within such other person's professional or expert competence and who has been selected with reasonable care by or on behalf of the corporation.").

[110] The recommendation by Morgan Stanley was also approved by its internal fairness committee. *See* Tr. 872 (Kindler) ("Q. Morgan Stanley has a committee that approves the issuance of fairness opinions, doesn't it? A. Yes. Q. And did that same committee approve Morgan Stanley's recommendation in this matter? A. Yes, it did.").

[111] *In re Walt Disney Co. Deriv. Litig.,* 907 A.2d 693, 770 (Del.Ch.2005) (holding that the compensation committee was protected by 8 *Del. C.* § 141(e) in relying upon the advice of its compensation expert).

[112] *See, e.g., Smith v. Van Gorkom,* 488 A.2d 858, 876 (Del.1985) ("We do not imply that an outside valuation study is essential to support an informed business judgment; nor do we state that fairness opinions by independent investment bankers are required as a matter of law."); *Crescent/Mach I P'rs, L.P. v. Turner,* 846 A.2d 963, 984 (Del.Ch.2000) ("[F]airness opinions prepared by independent investment bankers are generally not essential, as a matter of law, to support an informed business judgment.").

[113] *In re Loral Space & Commc'ns Inc. Consol. Litig.,* 2008 WL 4293781, at *22 (Del.Ch. Sept.19, 2008).

[114] *Kahn v. Tremont,* 694 A.2d at 429.

[115] *See, e.g.,* Tr. 433–35 (Lund); 628–29 (Granath); 682–83 (Jennings); 463–64 (Lund).

[116] Tr. 260–61(Lee) ("We also evaluated the capital markets alternative as well as sale alternative, and in our view, in conjunction with discussions with our ratings advisory group and our capital markets group, ... they did not believe that the company could raise enough to take out the $1.2 billion of senior secured Hallmark debt. Likewise, on the sale side, we did not believe that in the current market, or based on the company's forecasted projections, that the company was likely to achieve a sale value of greater than $1.2 billion.").

[117] Tr. 839 (Kindler) ("[Reaching out to third parties about refinancing] would have been a pointless exercise. We have one of the premier leverage finance businesses on Wall Street. We're in the market every day. And the concept that anyone would lend this company, it just was not going to happen, so it would have been a pointless exercise to do that."); 842–43 (Kindler) ("[Considering a third party sale was] much like the refinancing. From [Morgan Stanley's] perspective as investment bankers ... the asset was for sale but the key was at what price could it possibly be sold. We're in this business. We knew what every other cable channel

was sold for. [W]e knew that it could not be sold for anywhere near what the debt was. This was just one of those circumstances where it was absolutely clear to us as investment bankers that there would be no buyer for this channel at anything near what the debt was.").

118 Tr. 261(Lee) ("We thought a go-private transaction in which Hallmark would tender for the shares of the unaffiliated shareholders was a ... good alternative, arguably the best alternative that was available, but we didn't think it was actually going to be available.").

119 Kindler explained at trial that the Hallmark Proposal provided no return to the minority stockholders. *See* Tr. 847–48 (Kindler) ("[T]he original proposal that was made by Hallmark was basically that the equity wouldn't share in anything until the company was worth over [$] 1.15, $1.2 billion."). Because both Hallmark and Morgan Stanley agreed that Crown was worth less than $1 .15 billion, the equity would have received no value under the Hallmark Proposal.

120 Tr. 270–71(Lee); 847–49 (Kindler).

121 With $500 million of debt, only $315 million of Crown's debt was converted into new debt, and $185 million of Crown's debt was converted into Crown preferred stock. PTO ¶ 37. Eventually, non-Hallmark equity ownership turned out to be the amount that exceeded Crown's aggregate value of $525 million, because of the issue with the preferred stock. Non–Hallmark stockholders were to retain 8.2% of the common stock assuming the preferred stock converted. JX 74 (Morgan Stanley Feb. 25, 2010 Presentation) at 19–20. At trial, Kindler testified "[w]e were going to be sharing at over 500 million, essentially sharing at over 525 million, because this is preferred stock at issue that we had." Tr. 855 (Kindler).

122 JX 50 (Oct. 27, 2009 Minutes).

123 Tr. 865–66 (Kindler) ("If I was in Hallmark's position, I would never agree to a majority-of-the-minority condition. It makes absolutely no sense from Hallmark's perspective, because then they're in the impossible position of having negotiated with the special committee only to find that, now, they've got to go to public stockholders to get the majority of the minority to approve. They don't even know who the public stockholders are because it changes every day.").

124 *Id.*

125 Tr. 866 (Kindler) ("[W]e kept it to negotiate. We were strong on it, right from the beginning of the transaction; and toward the end of the transaction, we were able to extract a lot of things ... all in the context of agreeing not to have the majority-of-the-minority condition.").

126 *Weinberger,* 457 A.2d at 711.

127 *Reis v. Hazelett Strip–Casting Corp.,* 2011 WL 303207, at *15 (Del.Ch. Jan.21, 2011) (citing *Cinerama, Inc. v. Technicolor, Inc.,* 663 A.2d 1134, 1143 (Del.Ch.1994), *aff'd, Technicolor Plenary,* 663 A.2d 1156; *accord Kahn v. Tremont Corp.,* 1996 WL 145452, at *1 (Del.Ch. Mar.21, 1996) ("A fair price is a price that is within a range that reasonable men and women with access to relevant information might accept."), *rev'd on other grounds,* 694 A.2d 422 (Del.1997)).

128 *Reis v. Hazelett Strip–Casting Corp.,* 2011 WL 303207, at *17 (Del.Ch. Jan.21, 2011).

129 *Id.*

130 *See, e.g.,* JX 76 (Feb. 25–26, 2010 Minutes) ("Mr. Kindler stated that he does not view the decision to approve the Recapitalization as being a close call and that he believes approval of the Recapitalization is clearly the right thing for the Committee to do. The Committee members unanimously approved and accepted the report of Morgan Stanley.").

131 Tr. 853 (Kindler).

132 *See* Tr. 53–55 (Schechter).

133 669 A.2d 671 (Del.Ch.1995), *aff'd sub nom. Young v. Vision Hardware Group, Inc.,* 676 A.2d 909 (Del.1996).

134 2010 WL 3959399 (Del.Ch. Sept.24, 2010).

135 *Id.* at 677.

136 *Id.* at 677 ("[T]he evidence shows conclusively that but for the TCW proposal and its effectuation, Better Vision was a going concern heading immediately into bankruptcy and, unless new credit was made available, liquidation. This fact has very basic importance in determining the fair value of Better Vision stock.").

[137] *Id.* ("As a company to be appraised moves closer to the lip of liquidation, the line between going concern basis and liquidation basis becomes ever finer. That is, financial differences between the results of these different types of analysis will grow smaller as the company moves close to forced liquidation.").

[138] 2010 WL 3959399, at *3.

[139] *See Finkelstein v. Liberty Digital, Inc.,* 2005 WL 1074364, at *12 (Del.Ch. Apr.25, 2005) (finding that plaintiffs' "Fantasy Island approach" to DCF valuation ignored the company's "hard economic realities.").

[140] *See In re John Q. Hammons Hotels Inc. S'holder Litig.,* 2011 WL 227634, at *3 (Del.Ch. Jan.14, 2011).

[141] 2010 WL 3959399, at *3 (Del.Ch. Sept.24, 2010) ("[T]he company was in fact 'under water' at the time of the merger. Accordingly, a merger price above $0.00 (in *[Hanover],* $0.25 per share) was entirely fair.").

[142] *Id.* at *2.

[143] *Id.* ("If a discounted cash flow analysis reveals a valuation similar to a comparable companies or comparable transactions analysis, I have more confidence that both analyses are accurately valuing a company. If an expert witness clearly and persuasively explains why he or she has included or omitted an outlier from his or her data set, I have more confidence that the expert witness's data set is less likely to lead to a biased or skewed valuation.").

[144] Morgan Stanley and Houlihan used multiple valuation methodologies, and they both arrived at values for Crown less than the amount of Crown's debt. Also, third-party indications from other players in the industry valued Crown at between $500 million and $1 billion. *See* JX 31 (June 24, 2009 Minutes). Furthermore, Hallmark's financial advisors ran thirteen different valuation exercises, and only one reflected a value above the Hallmark debt. *See* JX 401 (Email from A. Shakir) at HLMK00008502 (deriving Crown's enterprise value at $1.391 billion); *see also* Tr. 186–87 (De Rose) ("It's our view, and I believe the view of practitioners in the valuation area, that valuations are best when they are supported by multiple legs, when there are different analyses from which you can triangulate a value, and that each of the analyses are confirmatory of the other.... So it really is the sense that more methodologies are better than just relying on a single one."); 298(Lee) ("In our view, each valuation methodology has its limitations, so in order to have the best result in a valuation, we believe it makes sense, and most practitioners, I believe, and most academics, recommend that you use multiple valuation methodologies to triangulate a valuation.").

[145] JX 86 (Schechter Report) at 58.

[146] Tr. 9–11 (Schechter).

[147] *See, e.g., Gray v. Cytokine Pharmasciences, Inc.,* 2002 WL 853549, at *8 (Del.Ch. Apr.25, 2002) ("In sum, when compared to other indications of value, Davis's valuation is such an outlier that it casts doubt on its reliability, quite apart from its exact assumptions and methodologies.").

[148] Hallmark Defs.' Post–Trial Answering Br. 35. As the chart demonstrates, Schechter's own two rejected valuations are located at the very bottom of the chart and his $2.946 billion DCF value is on the far right in the circle. The chart shows the valuation numbers from the potential buyers in the past, and the valuation ranges by methodologies from defendants' financial advisors (Morgan Stanley, Houlihan and Evercore Partners).

[149] In contrast to Schechter and Hamada, Hausman is an expert on the cable industry and the economic trends in that industry. He has extensive experience as a consultant to cable and satellite TV providers, and cable TV channels. JX 87 (Hausman Report) ¶ 3; Hausman Dep. 10–16. In addition, in contrast to Schechter, Hausman has testified as an expert in the cable industry in court proceedings and has written academic papers about that industry. *Id.* at 30–31. Hausman submitted an expert rebuttal report explaining the flaws in Schechter's valuation, and as previously noted, plaintiff did not cross-examine Hausman at trial.

[150] JX 91 (Hausman Rebuttal) ¶ 2 (finding Schechter's valuation fails an economic reality test, Hausman states, "[s]ince economists typically find market outcomes to be among the best sources of economic information, I analyze whether his valuation is consistent with observed market outcomes. Market outcomes are often the best source of economic information since individuals and firms spend real money and attempt to achieve the best outcome possible.").

[151] *Id.* at ¶ 8.

[152] *See* JX 87 (Hausman Report) ¶ 16; JX 91 (Hausman Rebuttal) ¶ 3; Tr. 660 (Hausman).

153 JX 91 (Hausman Rebuttal) ¶ 2; *see id.* at ¶ 3 ("I find it remarkable that Mr. Schechter makes no reference in his report to these prior market valuations. The market knew Crown was for sale and Hallmark was a 'motivated seller.' Yet no offer came within a factor of three of Mr. Schechter's valuation."); *see also id.* at n. 9 ("Fox made the only actual offer, and its offer is only about 1/6 of Mr. Schechter's valuation.").

154 *Id.* at ¶ 12 ("[T]he discrepancy between Crown's market valuation and Mr. Schechter's valuation implies that a potential buyer could earn over $1.8 billion by buying Crown (the difference between Mr. Schechter's $2.95 billion valuation and the $1.13 billion market valuation). This type of opportunity is rarely missed by Wall Street. Thus, even given the characteristics of Hallmark owning a substantial share of Crown, I do not find it plausible that a buyer would miss the opportunity of an expected return of approximately 160% if Mr. Schechter's valuation was accurate. This analysis makes his valuation especially implausible given Hallmark's demonstrated willingness to sell Crown over the 2005–2009 period.").

155 JX 87 (Hausman Report) ¶ 16 ("Given the value of the debt at $1.1 billion before the recent recapitalization, and reviewing the above approaches and outcomes, I do not find that the value of the Crown common stock was positive. That is, after the debt is paid off there would not be any residual value for common equity owners.").

156 *Id.* at n. 9 ("My conclusion is also consistent with the Evercore valuation of Crown as of December 2009 of $1.025 billion.").

157 *Kleinwort Benson Ltd. v. Silgan Corp.,* 1995 WL 376911, at *5 (Del.Ch. June 15, 1995); *see, e.g., Doft & Co. v. Travelocity.com Inc.,* 2004 WL 1152338, at *5 (Del.Ch. May 20, 2004) ("Delaware law clearly prefers valuations based on contemporaneously prepared management projections because management ordinarily has the best first-hand knowledge of a company's operations."); *In re Emerging Commc'ns, Inc. S'holders Litig.,* 2004 WL 1305745, at *14 (Del.Ch. May 3, 2004) ("This Court has consistently expressed a preference for the most recently prepared management projections available as of the merger date. The Court has also been skeptical of *ex post* adjustments to such projections.").

158 *Cede & Co. v. JRC Acquisition Corp.,* 2004 WL 286963, at *2 (Del.Ch. Feb.10, 2004) ("[T]his Court prefers valuations based on management projections available as of the date of the merger and holds a healthy skepticism for post-merger adjustments to management projections or the creation of new projections entirely. Expert valuations that disregard contemporaneous management projections are sometimes completely discounted."); *see, e.g., Taylor v. Am. Specialty Retailing Group, Inc.,* 2003 WL 21753752, at *2 (Del.Ch. July 25, 2003) ("Significantly, Kern's valuation lacks credibility because, ... he ignored a contemporaneous set of projections prepared by Dunham's management, choosing instead to rely on far more pessimistic assumptions of Dunham's future prospects that he prepared on his own.").

159 *In re Emerging Commc'ns,* 2004 WL 1305745, at *15 (explaining that "[e]xperts who ... vary from management forecasts should proffer legitimate reasons for such variance" and finding that the expert in that case had failed to provide "legitimate reasons" for modifying management's projections).

160 JX 86 (Schechter Report) at 37–39 ("I found several areas of the forecasts to be lower than I would expect;" "I find this estimate to be very low;" "The forecasts used in the Morgan Stanley valuation are very low."). Using his own approach, Schechter calculated the revenues to surpass management's projections by $26 million (8%) in 2011, $69 million (19%) in 2012, and $75 million (18%) in 2013. *Compare* JX 86 (Schechter Report) at Ex. 4, *with* JX 559 (Crown 5 Year Plan) at SC0000018.

161 *See* Tr. 508–09 (Stewart).

162 *Id.* at 520.

163 *Id.* at 509–510 ("[L]ike any business, it's very difficult to predict the forecasted performance of the organization ... forward-looking forecasts are obviously dependent on advertising revenue which is driven by ratings, and those ratings are very difficult to predict for extended periods beyond three to four years.").

164 JX 91 (Hausman Rebuttal) ¶ 20 n. 32 ("An example might be useful to demonstrate how uncertainty increases the further one predicts into the future. The prediction for 2024 has approximately 4.7 times as much uncertainty (variance) as the prediction for 2010. Now values further into the future have less weight in the DCF because of discounting. But even after discounting, the predictions for 2022–2024 will contribute

approximately the same amount to the DCF valuation as the 2010 prediction. Yet, the discounted prediction from 2022–2024 will still have over 4 times as much uncertainty as the 2010 prediction since the ratio of the variance is approximately 4.3.").

[165] *See, e.g.,* Tr. 187 (De Rose) ("We used the projections provided to us by management at Crown. It's our customary practice to rely on management projections."); Tr. 255(Lee) ("We rely on management's judgment and believe that as the operators of the company, they are in the best position to evaluate how the company will perform and are in the best position to prepare a business plan .").

[166] Tr. 963 (Hamada) ("Q. [Y]ou didn't give any opinion at all on the appropriate lengths of a projection period for a DCF analysis of Crown; did you? A. What would be an appropriate length of time or optimal length of time? No, I did not.").

[167] JX 91 (Hausman Rebuttal) ¶ 2.

[168] *In re Zenith Nat'l Ins. Corp. S'holders Litig.,* C.A. No. 5296–VCL, Tr. at 117 (Del. Ch. Apr. 22, 2010); *see also* *Gray v. Cytokine Pharmasciences, Inc.,* 2002 WL 853549, at *7 (Del.Ch. Apr.25, 2002) ("Davis's valuation reached conclusions as to value that are so high that they draw into question both his qualifications and his independence. Davis's valuation is off the charts. Davis's valuation, ..., more than doubles the results reached by Merrill Lynch and Lehman Brothers. Davis's going concern value is also more than four times higher than any offer PSI's board received when attempting to sell the Company.").

[169] *Gray,* 2002 WL 853549, at *7–8 (finding that "the extraordinary variance from [earlier] indications of value" the board had received when attempting to sell the company was "unexplained").

[170] *Id.* at 8 ("In sum, when compared to other indications of value, [plaintiff's expert's] valuation is such an outlier that it casts doubt on its reliability, quite apart from its exact assumptions and methodologies.").

[171] Tr. 50 (Schechter); *but see* 763 (Griffith) ("[W]e wouldn't have extended the standstill. I think we would have no choice but to pursue bankruptcy or foreclosure."); 819–20 (Hall) ("Q. So bankruptcy was an option? A. It was an option, and probably the only option, and we were prepared to take forward if this did not take place.").

[172] Tr. 12–13 (Schechter).

[173] *Cede & Co. v. JRC Acquisition Corp.,* 2004 WL 286963, at *2 (Del.Ch. Feb.10, 2004) (quoting *Ryan v. Tad's Enters., Inc.,* 709 A.2d 682, 702 (Del.Ch.1996)).

[174] *Hanover,* 2010 WL 3959399, at *2 ("Although there is no single preferred or accepted valuation methodology under Delaware law that establishes beyond question a company's value, there are commonly accepted methodologies that a prudent expert should use in coordination with one another to demonstrate the reliability of its valuation. If a discounted cash flow analysis reveals a valuation similar to a comparable companies or comparable transactions analysis, I have more confidence that both analyses are accurately valuing a company.").

[175] JX 89 (Lee Rebuttal Report) at 6 ("While DCF valuation is a theoretically sound and commonly used valuation methodology, it is highly sensitive to the numerous underlying assumptions, including but not limited to the cash flow projections, terminal value calculation, and WACC. Furthermore, a DCF valuation values the 'fundamental' or 'intrinsic' value of an enterprise and as such, may not reflect certain market dynamics or synergies that an acquirer may enjoy. Consequently, the theoretical DCF valuation analysis may misrepresent what a buyer would actually pay for a business."); JX 92 (De Rose Rebuttal Report) at 5 ("Though the DCF is a generally accepted valuation methodology, it is typically general industry practice to employ the use of several methods—based on available data—in order to triangulate a conclusive valuation opinion.").

[176] *Hanover,* 2010 WL 3959399, at *2; JX 89 (Lee Rebuttal Report) at 7 n. 11 (citing Niso Abuaf, *Valuing Illiquid Equity Securities in Light of the Financial Crisis of 2007–2009,* 20 Journal of Applied Finance 110, 113 (2010) ("Most practitioners triangulate among the three approaches. Triangulation shows scientific humility and legal prudence. That is, if we do not know what the truly correct approach is, we might as well be non-dogmatic and consider all the reasonable approaches, cross-check them against each other, and estimate the final result by quoting a range and not a point estimate."); Conroy & Harris, *Valuing Assets in Financial Markets* 5 (2007) ("Triangulation of value estimates is common in practice and also very useful as any method has its flaws.")). Trading comparables/multiples in the comparable companies analysis informs "what equity investors were

willing to pay for similar assets, based on facts and circumstances at the time of the analyses .” *Id.* Precedent transaction comparables in the comparable transactions analysis reflects “the value buyers were willing to pay for similar assets, including potential synergies, control premia, and other factors relevant to the period when such assets were acquired.” *Id.* In sum, this market approach is premised on the concept that “the value of a business can be determined by reference to ‘reasonably’ comparable guideline companies for which values are known because either (i) they are publicly traded (comparable companies analysis), or (ii) they were recently bought or sold in a transaction, the terms of which were publicly disclosed (comparable transactions analysis).” JX 92 (De Rose Rebuttal Report) at 5.

[177] JX 86 (Schechter Report) at 31–32.

[178] *Id.*

[179] 2010 WL 3959399, at *2.

[180] Hamada, in his deposition, admitted that he could have offered his rebuttal report before the opening expert report was filed. Hamada Dep. 18–20, 23–25. Hamada had not read the Hausman Rebuttal Report before his deposition although he conceded at trial that “it was certainly important enough for me to read.” Tr. 937 (Hamada). Moreover, Hamada's cross-examination revealed that he had not discovered any real flaw in Hausman's criticism of Schechter's DCF analysis. Tr. 950–52 (Hamada).

[181] *Id.* at 940.

[182] *Id.*

[183] *Id.* (“But in this assignment they would have never hired me as an expert in the cable television industry. So I would not be able to adequately evaluate the contents of those offers and so forth because I don't know that industry well enough.”).

[184] Tr. 974 (Hamada).

[185] Tr. 942 (Hamada).

[186] *Id.*

[187] Tr. 943 (Hamada).

[188] Hamada explained there are two accepted approaches to calculate a firm's WACC—an industry approach and a firm-specific approach. Tr. 904–05 (Hamada); JX 88 (Hamada Rebuttal) ¶¶ 6–8. Hamada opined that the correct calculation of WACC under the industry approach requires that a cost of equity and a cost of debt based on industry inputs must be weighted with an industry-average capital structure. Under the firm-specific approach, the firm-specific cost of equity and the firm-specific cost of debt must be weighted with a firm-specific capital structure. Hamada insists that calculating a firm's WACC using an industry-average capital structure with firm-specific costs of equity and debt is methodologically inappropriate and results in an incorrect WACC calculation. *Id.* at ¶¶ 6–10; Hamada Dep. 151–56.

[189] *See* Tr. 914 (Hamada), 324(Lee); *see also* Special Committee Defs.' Answering Post–Trial Br. 60 n. 39.

[190] Hamada Dep. 159; Tr. 977 (Hamada).

[191] JX 74 (Morgan Stanley Feb. 25, 2010 Presentation) at 35–37.

[192] Hamada explained that the “cliff-like drop” in the terminal year is evident with Morgan Stanley's selected perpetuity growth rates—22.3% free cash flow growth in the final year of the projections going out only 3½ years and then dropping immediately to only 1–3% growth in perpetuity. JX 88 (Hamada Rebuttal) ¶¶ 15–16.

[193] *See, e.g.,* Tr. 312(Lee) (“[I]t's typical to have a difference, a spread between the growth rate that's implied by management's projections and then the perpetual growth rate that you apply using the perpetual growth rate methodology. I think that's the case in every DCF that I've done, so it wasn't unusual and wasn't something that we viewed as highly suspect.”); Kindler Dep. 67 (“Having reviewed many of these I cannot imagine a single case where the perpetuity growth rate is not significantly below the growth rate in the last years.”). Moreover, Morgan Stanley's perpetuity growth rates were consistent with industry practice. JX 89 (Lee Report) at 17.

[194] Perpetuity growth rates implied by Morgan Stanley's exit multiple calculation actually were higher than the perpetuity growth rate Schechter used. Hamada, however, altered the WACC Morgan Stanley estimated and then argued that Morgan Stanley's exit multiples created a cliff-like drop. Morgan Stanley estimated a WACC nearly 50% higher than the WACC that Hamada assumed in his criticisms of Morgan Stanley's exit

multiple calculation. Tr. 966–69 (Hamada) (“Q. [I]n your report, your analysis of the cliff-like drop assumes that Morgan Stanley estimated Crown's WACC to be 9 percent; doesn't it? A. Just the same as the number right above 13.2 percent on page 34. Q. But Morgan Stanley did not estimate Crown's WACC to be 9 percent; did it? A. They should have.”).

[195] Tr. 948 (Hamada).

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United States District Court, S.D. Florida.

SECURITIES AND EXCHANGE
COMMISSION, Plaintiff,
v.
BANKATLANTIC BANCORP, INC.
and Alan B. Levan, Defendants.

Case No. 12-60082-CIV-SCOLA/OTAZO-REYES
|
Signed 11/14/2013

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ORDER RE: D.E. 148, 155, 159 & 156

ALICIA M. OTAZO-REYES, UNITED STATES MAGISTRATE JUDGE

***1** THIS CAUSE came before the Court upon the following motions: (1) Plaintiff's Daubert Motion to Exclude the Opinion and Testimony of John J. Huber ("Huber") (hereafter, "Huber Motion") [D.E. 148]; (2) Plaintiff's Daubert Motion to Exclude the Opinion and Testimony of Christopher M. James ("James") (hereafter, "James Motion") [D.E. 155]; (3) Plaintiff's Daubert Motion to Exclude the Testimony of Linda A. MacDonald ("MacDonald") (hereafter, "MacDonald Motion") [D.E. 159] (collectively, "Plaintiff's Daubert Motions"); and (4) Defendants' Motion in Limine to Exclude the Opinions and Testimony of Expert Witness Lynn E. Turner ("Turner") (hereafter, "Turner Motion" or "Defendants' Daubert Motion") ([D.E. 156]).[1]

Plaintiff's Daubert Motions and Defendants' Daubert Motion were referred to the undersigned by the Honorable Robert N. Scola, Jr., United States District Judge, "*to be heard and determined* in accordance with [ ] 28 U.S.C. § 636(b)(1)(A) and Rule 1(c) of the Local Magistrate Judge Rules" [D.E. 169]. The undersigned held an evidentiary hearing on the motions, which took place on September 23-25, 2013. For the reasons stated below, the undersigned hereby DENIES the Huber Motion, the MacDonald Motion and the Turner Motion; and GRANTS IN PART and DENIES IN PART the James Motion.

I. FACTUAL AND PROCEDURAL BACKGROUND[2]

Defendant BankAtlantic Bancorp, Inc. ("Bancorp" or "BBX") is a publicly traded company. During 2006 and 2007, Bancorp was the holding company for BankAtlantic, a federal savings bank offering consumer and commercial banking and lending services throughout Florida. Bancorp's common stock is listed on the New York Stock Exchange and registered with the Securities and Exchange Commission ("SEC" or "Plaintiff") under Section 12(b) of the Securities and Exchange Act of 1934 (hereafter, "Exchange Act"), 15 U.S.C. § 78*o*(b). Defendant Alan Levan ("Levan") is the Chairman of the Board and CEO of Bancorp, and in 2007 he was also the Chairman of BankAtlantic.

In 2007, BankAtlantic was one of Florida's largest commercial banking and lending institutions with $1.5 billion in its commercial real estate loan portfolio. Approximately $533 million of this portfolio consisted of loans in BankAtlantic's commercial residential real estate land acquisition and development portfolio ("Commercial Residential Portfolio" or "Portfolio"). The loans in the Portfolio consisted of Builder Land Bank ("BLB") loans and non-BLB loans.[3] In managing the Portfolio, Bancorp assigned to the loans, and reassigned as necessary, internal grades of 1 to 13, based on their individual creditworthiness. Grades 10-13 were considered non-passing grades.

***2** The SEC brings this action against Bancorp and Levan (collectively, "Defendants") for alleged securities laws violations, arising from: (1) Defendants' public disclosures regarding the health of the Commercial Residential Portfolio; (2) Bancorp's accounting treatment of a portion of the Portfolio; and (3) Bancorp's maintenance of internal controls. The SEC alleges the following as to each of these three violation categories.

1. Public Disclosures:

The SEC alleges that Defendants failed to provide appropriate disclosures in the Management Discussion and Analysis ("MD&A") section of Bancorp's Forms 10-Q for the first and second quarter of 2007.[4] The SEC also alleges that Defendants made material misrepresentations during Bancorp's first and second quarter earnings conference calls in 2007.[5] According to the SEC, Defendants had knowledge of serious problems within BankAtlantic's Commercial Residential Portfolio during the first two quarters of 2007, yet did not disclose those problems until the third quarter of 2007. The SEC further alleges that Defendants, by misrepresentations and omissions, failed to alert investors to a known trend of loan extensions and internal loan downgrades in the Commercial Residential Portfolio.

2. Accounting:

The SEC alleges that Defendants committed accounting fraud violations in connection with Bancorp's 2007 Form 10-K.[6] According to the SEC, Bancorp engaged an investment bank, JMP Securities, Inc. ("JMP"), in 2007 to sell some of the problem loans in the Commercial Residential Portfolio (the "JMP Loans"), yet Bancorp did not reclassify the JMP Loans from "held-for-investment" to "held-for-sale" in accordance with Generally Accepted Accounting Principles ("GAAP"). As a result, Bancorp avoided writing down the JMP Loans to the lower of cost or fair value and reporting a materially significant loss for 2007 in the Form 10-K.

3. Controls:

The SEC alleges that Bancorp failed to maintain or follow adequate internal Disclosure Controls and Procedures ("DC&P") in violation of Section 13(b)(2) of the Exchange Act, 15 U.S.C. § 78m(b)(2). According to the SEC, the DC&P that were maintained by Bancorp were usurped by Levan, were never properly in place, or failed.

Defendants have retained MacDonald, James and Huber, all of whom are nonscientific expert witnesses, to testify at trial concerning these allegations of securities laws violations. The SEC has retained a single nonscientific expert witness, Turner, for the same purpose. In their respective Daubert Motions, Plaintiff and Defendants do not challenge the overall professional qualifications of these expert witnesses.[7] However, each side argues that the other's proposed expert testimony raises serious concerns about: the reliability of the testimony; whether the testimony will assist the trier of fact; and whether the testimony will invade the province of the Court to instruct the jury.

II. LEGAL STANDARDS

***3** A party who seeks to admit expert testimony bears the burden of laying the proper foundation for its admissibility by a preponderance of the evidence. Allison v. McGhan Med. Corp., 184 F.3d 1300, 1306 (11th Cir. 1999). Thus, before expert testimony may be admitted as evidence at trial pursuant to Rule 702 of the Federal Rules of Evidence, the district court must act as a gatekeeper and screen the proffered evidence. Daubert v. Merrell Dow Pharm., Inc., 509 U.S. 579, 597 (1993). In the Eleventh Circuit, this gatekeeping function must be performed as follows:

> [I]n determining the admissibility of expert testimony under Rule 702, [the court must] engage in a rigorous three-part inquiry [and] must consider whether: (1) the expert is qualified to testify competently regarding the matters he intends to address; (2) the methodology by which the expert reaches his conclusions is sufficiently reliable as determined by the sort of inquiry mandated in *Daubert*; and (3) the testimony assists the trier of fact, through the application of scientific, technical, or specialized expertise, to understand the evidence or to determine a fact in issue.

United States v. Frazier, 387 F.3d 1244, 1260 (11th Cir. 2004) (citing City of Tuscaloosa v. Harcros Chems., Inc., 158 F.3d 548, 562 (11th Cir. 1998)). Seealso, McCorvey v. Baxter Healthcare Corp., 298 F.3d 1253, 1257 (11th Cir. 2002) (The gatekeeping function requires the trial court "to conduct an exacting analysis of the proffered expert's methodology" to ensure it meets the standards of admissibility under Daubert.).

However, a "district court's gatekeeper role under Daubert is not intended to supplant the adversary system or the role of the jury." Maiz v. Virani, 253 F.3d 641, 666 (11th Cir. 2001) (citing Allison, 184 F.3d at 1311). Rather, "[v]igorous cross-examination, presentation of contrary evidence, and careful instruction on the burden of proof are the traditional and appropriate means of attacking shaky but admissible evidence." Allison, 184 F.3d at 1311.

A. First Daubert Inquiry – Expert's Qualifications

"While scientific training or education may provide possible means to qualify [an expert], experience in a field may offer another path to expert status." United States v. Masferrer, 367 F. Supp. 2d 1365, 1372 (S.D. Fla. 2005) (citing Frazier, 387 F.3d at 1260-61). "[I]f the witness is relying solely or primarily on experience, then the witness must explain how that experience leads to the conclusion reached, why that experience is a sufficient basis for the opinion, and how that experience is reliably applied to the facts." United States v. Augustin, 661 F.3d 1105, 1125 (11th Cir. 2011) (citing Frazier, 387 F.3d at 1261). In this case, all of the proffered experts are nonscientific and rely primarily on their experience in their respective professional fields to justify their opinions. Therefore, although the experts' overall professional qualifications have not been challenged, those qualifications are a factor to take into consideration when assessing the reliability of their opinions. Augustin, 661 F.3d at 1125; Frazier, 387 F.3d at 1261.

B. Second Daubert Inquiry – Reliability of Expert's Opinion

"For nonscientific expert testimony, the trial judge must have considerable leeway in deciding in a particular case how to go about determining whether particular expert testimony is reliable." Am. Gen. Life Ins. Co. v. Schoenthal Family, LLC, 555 F.3d 1331, 1338 (11th Cir. 2009) (citing Kumho Tire Co., Ltd. v. Carmichael, 526 U.S. 137, 152 (1999)). Thus, "[a] district court may decide that nonscientific expert testimony is reliable based upon [the expert's] personal knowledge or experience." Schoenthal, 555 F.3d at 1338 (citing Kumho, 526 U.S. at 150). In the context of nonscientific experts, therefore, the main purpose of the Daubert reliability inquiry is to determine whether the expert who is "basing testimony upon professional studies or personal experience, employs in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field." McClain v. Metabolife Int'l, Inc., 401 F.3d 1233, 1255 (11th Cir. 2005) (citing Kumho, 526 U.S. at 152).

C. Third Daubert Inquiry – Helpfulness/Relevance of Expert's Testimony

***4** "To be admissible, expert testimony must assist the trier of fact to understand the evidence or to determine a fact in issue. This condition goes primarily to relevance."Johnson v. Bush, Case No. 00-3542-CIV, 2002 WL 34355950, at *1 (S.D. Fla. Apr. 19, 2002). Put another way, the proposed testimony must "fit" the case. Id. Seealso, Allison, 184 F.3d at 1312 ("[T]he court must ensure that the proposed testimony is relevant to the task at hand, i.e., that it logically advances a material aspect of the proposing party's case.").

"[E]xpert testimony is admissible if it concerns matters that are beyond the understanding of the average lay person." Frazier, 387 F.3d at 1262. However, "[p]roffered expert testimony generally will not help the trier of fact when it offers nothing more than what lawyers for the parties can argue in closing arguments." Id. at 1262-63.

"An opinion is not objectionable just because it embraces an ultimate issue." Fed. R. Evid. 704(a). In the Eleventh Circuit, "an expert may offer opinion testimony on an ultimate issue of fact, Fed. R. Evid. 704, [but] an expert may not [ ] merely tell the jury what result to reach." United States v. Caro, 454 Fed.Appx. 817, 843 (11th Cir. 2012) (citing Montgomery v. Aetna Cas. & Sur. Co., 898 F.2d 1537, 1541 (11th Cir. 1990)). Further, " 'while an expert may testify as to his opinion on an ultimate issue of fact, [he or she] may not testify to the legal implications of conduct; the court must be the jury's only source of law.' " Dubiel v. Columbia Hosp. (Palm Beaches) Ltd. P'ship, Case No. 04-80283-CIV, 2005 WL 5955691, at *5 (S.D. Fla. Jan. 11, 2005) (citing Montgomery, 898 F.2d at 1541).

While an expert may opine "as to whether one party or another acted in compliance with industry standards, an expert cannot permissibly opine on whether a party had a right to do what it did under *legal* standards. Instead, this area is reserved for the Court." R&R Int'l, Inc. v. Manzen, LLC, Case No. 09-60545-CIV, 2010 WL 3605234, at *19 (S.D. Fla. Sept. 12, 2010). Seealso, United States v. Long, 300 Fed.Appx. 804, 814-16 (11th Cir. 2008) (finding it admissible for a forensic expert witness to testify that the actions of the defendant "bore the hallmarks of a Ponzi Scheme" because it "was a factual, and not a legal conclusion," but excluding an expert who used the language "artifice or scheme to defraud").

III. THE EVIDENTIARY HEARING

On September 23-25, 2013, the undersigned heard the testimony of MacDonald, James, Huber and Turner regarding their proposed expert opinions. Defendants tendered MacDonald on the subject of Defendants' alleged failure to reclassify the JMP Loans from “held-for-investment” to “held-for-sale pursuant to GAAP;” James on the subjects of Defendants' alleged failure to provide appropriate disclosures in the MD&A section of Bancorp's 2007 first and second quarter Forms 10-Q and Defendants' alleged misrepresentations during the 2007 first and second quarter earnings conference calls; and Huber on the subjects of Bancorp's allegedly inadequate DC&P and misleading public disclosures.[8] The SEC tendered Turner as its sole expert witness with respect to all of these issues.

By agreement of the parties, the initial and rebuttal report of each expert were deemed to constitute that expert's direct examination. See Order Setting Evidentiary Hearing [D.E. 216]. Thus, the live testimony at the evidentiary hearing was limited to cross-examination and re-direct examination of each witness. Having considered the expert witnesses' proposed trial testimony (as expounded at the Daubert Evidentiary Hearing), the pertinent portions of the record and the applicable law, the undersigned concludes with regard to Defendants' experts that MacDonald and Huber satisfy the Daubert requirements and that James also satisfies them, except for two of his opinions. The undersigned also concludes that the SEC's expert, Turner, passes muster under Daubert.

IV. MACDONALD

***5** At trial, MacDonald would offer the following opinions: (1)Defendants were not required by GAAP to reclassify the JMP Loans from “held-for-investment” to “held-for-sale;” and (2) even if the loans had to be reclassified as “held-for-sale,” the resulting write down of the loans should not be calculated using the fair value approach proposed by the SEC's expert. McDonald Expert Report [D.E. 171-20 at ¶ 10].

A. Reclassification of the JMP Loans

MacDonald began her analysis by evaluating the relevant GAAP principles applicable to determining whether the JMP Loans should have been reclassified from “held-for-investment” to “held-for-sale.” Id. at ¶¶ 11-17. The first GAAP source she consulted was the American Institute of Certified Public Accountants' Statement of Position 01-6 (“SOP 01-6”). See Transcript of Daubert Evidentiary Hearing on September 23, 2013 (hereafter, “Trans. 9/23”) [D.E. 243 at 10, 24-25]. According to MacDonald, SOP 01-6 provides that loans previously classified as “held-for-investment” should be reclassified as “held-for-sale” at the lower of cost or fair value only after a decision has been made to sell them. MacDonald Expert Report [D.E. 171-20 at ¶ 12]. Because SOP 01-6 does not explain how to determine whether “a decision to sell” has been made, Trans. 9/23 [D.E. 243 at 11], MacDonald then turned to Financial Accounting Standard 144 (“FAS 144”) for further guidance. MacDonald Expert Report [D.E. 171-20 at ¶ 13].[9]

Although FAS 144 does not pertain to loans, Trans. 9/23 [D.E. 243 at 15], MacDonald, as the primary author of FAS 144, reasoned by analogy from that source because there was a void in GAAP with respect to loans, and FAS 144 supplied guidance for long-lived assets, the most analogous asset to loans. Id. at 56-60. According to MacDonald, FAS 144 provides that intent to sell is not sufficient to classify a long-lived asset as “held-for-sale.” MacDonald Expert Report [D.E. 171-20 ¶ 14].

In MacDonald's opinion, the factual record did not reflect that Bancorp, through Levan or otherwise, had made a decision to sell the JMP Loans. Id. at ¶ 18. Specifically, MacDonald opined that Bancorp's engagement with JMP regarding the JMP Loans constituted a market test and not a decision to sell. Id. at ¶¶ 19-50.[10] MacDonald testified that, under FAS 144, when “there [are] indicia that you are test marketing [ ] long-lived assets, you will not call it Held-for-Sale even if all of the other conditions [for a sale] are met.” Trans. 9/23 [D.E. 243 at 60]. When asked whether a jury could just as easily undertake the same review of the record that she had conducted to reach her conclusions, MacDonald responded that her review had been conducted through the lens of her understanding of GAAP, and based on her professional experience. Id. at 23.

B. The SEC's Expert's Fair Value Approach

According to MacDonald, even if the JMP Loans should have been reclassified as “held-for-sale,” the fair value approach utilized by the SEC's expert was not valid under GAAP. MacDonald Expert Report [D.E. 171-20 at ¶¶ 51-83]. MacDonald looked to FAS 157, which addresses fair value measurements, for guidance on determining fair value. Id. at 53-54.[11] FAS 157 defines fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." Trans. 9/23 [D.E. 243 at 64]. Thus, an orderly transaction is one of the bases for determining fair value. Id. at 65.

***6** In MacDonald's opinion, bids in a proposed sales transaction that reflect distressed pricing cannot qualify as a measurement of fair value under FAS 157 because the sale would not constitute an "orderly transaction." MacDonald Expert Report [D.E. 171-20 at ¶ 75]. MacDonald further testified that, for purposes of reclassifying the JMP Loans as "held-for-sale," the applicable fair value "measurement date" under FAS 157 would have been December 31, 2007. Trans. 9/23 [D.E. 243 at 30]. However, all of the bids relied upon by the SEC were received at some point after that date, MacDonald Expert Report [D.E. 171-20 at ¶¶ 55-63], and, in any event, an unaccepted offer cannot form the basis for a transaction date. Trans. 9/23 [D.E. 243 at 65-66],[12]

MacDonald testified that the SEC's proposed approach for determining fair value of the JMP Loans was missing a number of steps required under GAAP. Id. at 38-39. Though MacDonald admitted that she did not undertake these steps herself, including reviewing the underlying appraisals, performing a discounted cash flow analysis or confirming the findings of Bancorp's external auditors, id. at 40-44, she saw no signs that the SEC's expert, Turner, who actually valued the JMP Loans, carried out any of these tasks when computing their fair value. Id. at 66-68.[13] According to MacDonald, the only two bids upon which Turner relied, which were received after the measurement date in a disorderly transaction, could not provide a legitimate basis to determine fair value under GAAP. Id.

C. Challenges to MacDonald's Opinions

The SEC challenges the reliability and helpfulness/relevance of MacDonald's opinions. As to reliability, the SEC argues (i) that MacDonald's first opinion on GAAP compliance is not reliable because she applied no real methodology and did nothing more than weigh the factual evidence, which is a task solely reserved to the jury, and (ii) that her second opinion is not reliable because she failed to carry out her own valuation of the JMP Loans. MacDonald Motion [D.E. 159 at 3]. As to helpfulness/relevance, the SEC argues (i) that MacDonald's first opinion on GAAP compliance is ultimately a legal conclusion, which is improper and intrudes on the Court's role; and (ii) that in rejecting the SEC's expert's determination of fair value in her second opinion, MacDonald reached an improper legal conclusion and provided no coherent alternative theory of her own. Id.

1. Reliability

Because MacDonald is a nonscientific expert, consideration of her qualifications is part of the inquiry into the reliability of her methodology. Augustin, 661 F.3d at 1125; Frazier, 387 F.3d at 1261. MacDonald is a Certified Public Accountant with over thirty years of professional experience in financial accounting and reporting, including her present position as a Senior Managing Director in the forensic and litigation consulting practice of FTI Consulting, Inc. and as a past Director of the Financial Accounting Standards Board ("FASB"). MacDonald Expert Report [D.E. 171-20 at ¶¶ 4-8]. MacDonald also worked at the SEC's Enforcement Division on investigations into fraud and GAAP violations associated with public companies' financial statements. Id. at 6.

(i) MacDonald's first opinion on GAAP compliance

***7** The SEC contends that MacDonald applied no real methodology and did nothing more than a jury would do with respect to this opinion. However, as discussed above, MacDonald testified that she consulted the GAAP guidance that she found to be relevant to the classification of loans as "held-for-sale;" applied that guidance, viewed through the lens of her extensive experience in financial accounting and reporting, to the factual record; and opined that the JMP Loans were correctly classified under GAAP as "held-for-investment" rather than "held-for-sale." Because her methodology was informed by and conducted in accordance with her professional experience, MacDonald's opinion as a nonscientific expert meets the Daubert reliability prong. Schoenthal, 555 F.3d at 1338; McClain, 401 F.3d at 1255. Moreover, because she applied her professional experience to formulate her opinion, MacDonald did not just weigh the facts as a lay jury would.

(ii) MacDonald's second opinion on fair value

The SEC challenges MacDonald's second opinion as unreliable because, while criticizing the SEC's expert's valuation, she did not perform one herself. However, the impact of such failure simply goes to the weight to be given by the jury to MacDonald's opinion, rather than its admissibility. Rosenfeld v. Oceania Cruises, Inc., 654 F.3d 1190, 1193 (11th Cir. 2011) ("[I]n most cases, objections to the inadequacies of a study are more appropriately considered an objection going to the weight of the evidence rather than its admissibility.").

2. Helpfulness/Relevance

The SEC also seeks to exclude both of MacDonald's opinions under the helpfulness/relevance inquiry as improper legal conclusions.

(i) MacDonald's first opinion on GAAP compliance

The SEC argues that MacDonald's first opinion constitutes an impermissible legal opinion because the "clear risk here is the jury will likely confuse MacDonald's opinion that the Defendants followed GAAP as a determinative conclusion, if not exactly the same as, finding the Defendants did not violate the federal securities laws." MacDonald Motion [D.E. 159 at 7]. However, expert testimony as to the interpretation of GAAP and its application to the facts of a case is permissible and does not, without more, constitute improper legal conclusions. Seee.g., In re Novatel Wireless Sec. Litig., Case No. 08cvl689, 2011 WL 5827198, at *3 (S.D. Cal. Nov. 17, 2011) (admitting expert testimony of "whether Defendants complied with SEC and GAAP requirements" but excluding testimony about what their contracts permitted); S.E.C. v. Leslie, Case No. C 07-3444, 2010 WL 2991038, at *7-9 (N.D. Cal. July 29, 2010) (admitting expert's interpretation of GAAP but excluding testimony about judicial opinions and Securities Exchange Rule quotations); S.E.C. v. Retail Pro, Inc., No. 08cv1620, 2011 WL 589828, at *4 (S.D. Cal. Feb. 10, 2011) (finding that evidence regarding GAAP and revenue recognition was a proper basis for expert testimony). Therefore, so long as MacDonald's testimony does not veer into the subject of securities laws violations, her opinion that GAAP did not require Defendants to reclassify the JMP Loans from "held-for-investment" to "held-for-sale" is not impermissible, even if GAAP compliance is an element of the securities laws violations alleged by the SEC.

Further, the Eleventh Circuit has "recognized that an instruction may be used to prevent a jury from placing too much weight on an expert's legal conclusions." Maiz, 253 F.3d at 667. Seealso, United States v. Gold, 743 F.2d 800, 817 (11th Cir. 1984) (upholding the district court's decision to admit expert testimony about an ultimate legal issue in the case because the court was "careful to instruct the jury about the weight that should be given expert testimony such as [this]"). Indeed, the Eleventh Circuit has ruled that in such instances "[i]f the district court takes a curative measure, [the appellate] court will reverse only if the evidence is so prejudicial as to be incurable by that measure." United States v. Pacheco, 426 Fed.Appx. 832, 835 (11th Cir. 2011). Thus, the SEC may seek an appropriate curative instruction to alleviate its concerns regarding the weight the jury may place on MacDonald's opinion regarding GAAP compliance.

(ii) MacDonald's second opinion on fair value

***8** The SEC argues that MacDonald's second opinion "attempts to 'rule' on the adequacy of support for the [SEC]'s 'held-for-sale' claim, and, in doing so, seeks to reach an impermissible legal conclusion." MacDonald Motion [D.E. 159 at 10]. However, MacDonald's criticism of Turner's approach to computing the fair value of the JMP Loans is neither a "ruling" nor an "impermissible legal conclusion." Novatel, 2011 WL 5827198, at *3; Leslie, 2010 WL 2991038, at *7; Retail Pro, 2011 WL 589828, at *4. Moreover, the SEC may seek an appropriate curative instruction to alleviate its concerns regarding the weight the jury may place on MacDonald's opinion regarding the SEC's proposed fair value calculation. Maiz, 253 F.3d at 667; Gold, 743 F.2d at 817; Pacheco, 426 Fed.Appx. at 835.

Therefore, the MacDonald Motion is denied.

V. JAMES

At trial, James would offer the following opinions relating to Defendants' public disclosures: (1) the credit market crisis unexpectedly and negatively impacted real estate prices and market conditions for lenders beginning in the third quarter of 2007; (2) The MD&A disclosures in Bancorp's 2007 first and second quarter Forms 10-Q were consistent with regulatory requirements and industry practice; (3) Bancorp's loan performance during that time was consistent with Defendants' specific disclosures as well as the market trends they disclosed; and (4) several analysts thought that Bancorp was conservative in disclosing negative trends and addressing problem loans. James Expert Report [D.E. 155-1 at 2-4]. James testified that, in preparing his expert report, he "followed the same procedures that [he] does in his research ... [and] that are commonly used by economists" and that those procedures are the same as "the scholarly standard and the scientific standard that [are] applied when [he does his] own published research." Transcript of Daubert Evidentiary Hearing on September 24, 2013 (hereafter "Trans. 9/24") [D.E. 244 at 187, 196].[14]

A. The credit market crisis

According to James, the credit markets dramatically and unexpectedly declined in August 2007 and the real estate sector deteriorated significantly amid this crisis. James Expert Report [D.E. 155-1 at ¶¶ 19-46]. James opined that Florida was more affected by the real estate downturn than almost all other states. Id. at ¶ 39. When asked why he focused on trends in the Florida real estate market when the SEC did not allege such a trend in its complaint, James responded that Defendants' "disclosing their business and its exposure to the real estate market [was], in [his] opinion, disclosing an important trend that is common to their business model and the loans they make." Trans. 9/24 [D.E. 244 at 168-69].

B. Consistency of disclosures with regulatory requirements and industry practice

According to James, Defendants' public disclosures were adequate in that they disclosed: (1) known trends in the real estate market and the risks in BankAtlantic's loan portfolio; (2) the fact that problem loans existed throughout the portfolio; (3) risks consistent with regulatory requirements; and (4) risks that were more comprehensive than those of most comparable banks. James Expert Report [D.E. 155-1 at ¶¶ 47-84], The SEC asked James whether he was aware of any evidence supporting Defendants' non-disclosure of Bancorp's internal loan grades. Trans. 9/24 [D.E. 244 at 172-77]. James responded that he relied on the deposition testimony of bank employees, id., and his own experience as a director of a bank for 16 years in concluding that this type of information is not commonly disclosed because such level of disclosure is discouraged by bank regulators. Id. at 197-98. The SEC also questioned whether James had actually compared Bancorp's disclosures with the other banks' disclosures in terms of what was happening in their loan portfolios, and, in particular, their own internal loan grades. Id. at 176-77. James responded that he did look at the other banks' disclosures, but acknowledged that, because internal loan grades are not generally publicly available, he was not able to review them. Id.[15]

C. Consistency of Bancorp's loan performance with Defendants' specific disclosures and the market trends they disclosed.

***9** According to James, Bancorp's actual loan performance was consistent with Defendants' specific disclosures as well as the market trends they disclosed. James Expert Report [D.E. 155—1 at ¶¶ 85-91]. In formulating this opinion, James reviewed the deterioration of BankAtlantic's Commercial Residential Portfolio through the fourth quarter of 2008. Id. at ¶¶ 85-86. James also looked to performance data for the loan portfolios of other, purportedly similarly situated Florida and non-Florida banks through the fourth quarter of 2008. Id. at ¶¶ 87-91. After noting that Defendants reported worse than average losses in the third quarter of 2007, James observed that most of the other banks he considered eventually reported similar losses to Bancorp's and caught up to Bancorp's reported losses by the end of 2008. Id. at ¶¶ 86-91. Based on these observations, James concluded that, "throughout the first half of 2007 [Defendants] warned about the negative market trend" and that "[t]he losses [Bancorp] reported in [the third quarter of 2007] therefore can be described as the realization of a disclosed risk, the magnitude of which was unforeseeable by most market[ ] participants" and "in line with that experienced by comparable banks." Id. at ¶ 85. To put it in simpler terms, the gist of this third opinion by James is that the events that occurred after the first and second quarters of 2007, both with respect to Bancorp's and other banks' loan performances, show that Defendants' public disclosures in those two quarters were "par for the course."

D. Analysts' Reports

According to James, several analysts indicated that Bancorp was conservative in disclosing negative trends and problem loans in 2007, that Bancorp recognized the negative trend in Florida real estate, and that Bancorp was one of the most proactive banks in addressing and disclosing market concerns and regarding the deterioration of Bancorp's real estate loan portfolio. Id. at ¶¶ 92-100. In support of these observations, James quoted and summarized the underlying analysts' reports. Id. When challenged regarding his "expertise in reading an analyst's report and providing a one-sentence summary" of it, Trans. 9/24 [D.E. 244 at 186], James acknowledged that he did not possess such expertise, but explained that those reports are of the same type as those on which he would rely in his published research. Id.

E. Challenges to Janies' Opinions

The SEC objects to James testifying on the grounds that: (1) James' opinion that the credit crisis unexpectedly and negatively impacted real estate prices and market conditions for lenders beginning in the third quarter of 2007 is irrelevant, based on flawed methodology, and will confuse the jury; (2) James' opinion that Defendants' disclosures appear consistent with regulatory requirements and industry practice is a legal opinion that improperly invades the province of the Court and jury, and is also irrelevant and unreliable; (3) James' opinion that Bancorp's loan performance was consistent with Defendants' specific disclosures and the market trends they disclosed is irrelevant and unreliable; and (4) James' opinion reporting the contents of analysts' reports regarding Bancorp's disclosures is hearsay. James Motion [D.E. 155 at 5-18]. Thus, the SEC's challenges to James' opinions fall into three categories: the reliability of James' methodology; the helpfulness/relevance of his opinions; and, as to the fourth opinion, that it is hearsay.

1. Reliability

Because James is a nonscientific expert, consideration of his qualifications is part of the inquiry into the reliability of his methodology. Augustin, 661 F.3d at 1125; Frazier, 387 F.3d at 1261. James is the William H. Dial/Sun Bank Eminent Scholar and Professor of Finance and Economics at the University of Florida, as well as a visiting scholar at the Federal Reserve Bank of San Francisco. James Expert Report [D.E. 155-1 at 1]. James has authored or co-authored numerous peer-reviewed articles on economics and banking. Id. at App. A. In 1995 and 1998, James served as a consultant to the Federal Reserve Board of Governors. Id. Additionally, from 1989 to 2006, James served on the Board of Directors and the Advisory Board to SunTrust Banks of Florida. Id. James testified that the methodology for all of his opinions was grounded in the same level of intellectual rigor that undergirds the work of professional economists in the field. Trans. 9/24 [D.E. 244 at 187, 198]. Hence, the SEC's challenge to the reliability of James' methodology fails. SeeMcClain, 401 F.3d at 1255 (an expert basing testimony upon professional studies or personal experience must employ in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field); Maiz, 253 F.3d at 665-66 (finding an economists' theories and methodology sufficiently reliable where his model was not unusually complex and his use of a broad-based index to estimate the performance of U.S. real estate was not without foundation).

2. Helpfulness/Relevance

***10** The SEC challenges the helpfulness/relevance of James' first three opinions.

(i) James' first opinion on the credit market crisis

The SEC argues that this opinion is not relevant because it will not help the trier of fact understand a fact in issue, as there is no requirement for the SEC to prove loss causation. Plaintiff's Reply Memorandum in Support of its Daubert Motion to Exclude the Opinion and Testimony of Christopher M. James (hereafter, "James Reply") [D.E. 201 at 4], In order to prevail on its securities fraud claims, the SEC must show that Defendants knowingly, willingly or recklessly made untrue statements or omissions of material fact. See Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5.[16] Significantly, the SEC must show that the allegedly misleading statements or omissions made by Defendants were *material.*Basic, Inc. v. Levinson, 485 U.S. 224, 231 (1988). A fact is material where there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." Basic, 485 U.S. at 231-32. The credit market crisis' impact on real estate prices and market conditions for lenders would arguably have been part of the "total mix" of information considered by reasonable investors in the first half of 2007. Therefore, James' first opinion is not unhelpful or irrelevant.

(ii) James' second opinion on consistency of disclosures with regulatory requirements and industry practice.

The SEC argues that James' second opinion is an impermissible legal opinion and that disclosures made by other banks are irrelevant to whether Defendants made adequate disclosures. James Motion [D.E. 155 at 9]. However, in addition to materiality, the SEC must prove scienter by showing that Defendants acted with, at a minimum, severe recklessness, when making the alleged misleading statements or omissions in their public disclosures. Mizzaro v. Home

Depot, Inc., 544 F.3d 1230, 1238 (11th Cir. 2008). Severe recklessness is "not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and that present[s] a danger of misleading buyers or sellers which is either known to the defendant or is so obvious that the defendant must have been aware of it." Id. Adherence to, or departure from, industry standards can be probative of whether ordinary care was observed in conducting business. Messer v. E.F. Hutton & Co., 847 F.2d 673, 677-78 (11th Cir. 1988). Because James' opinion on regulatory requirements and industry standards goes to an element of the SEC's securities fraud claims, it is not irrelevant. Allison, 184 F.3d at 1312. [17]

***11** Moreover, expert testimony on regulatory requirements and industry practices is permissible and does not, without more, constitute improper legal conclusions. Novatel, 2011 WL 5827198, at *3; Leslie, 2010 WL 2991038, at *7; Retail Pro, 2011 WL 589828, at *4. Therefore, so long as James' testimony does not veer into the subject of securities laws violations, his second opinion is not impermissible. And the SEC may seek an appropriate curative instruction to alleviate its concerns regarding the weight the jury may place on James' second opinion. Maiz, 253 F.3d at 667; Gold, 743 F.2d at 817; Pacheco, 426 Fed.Appx. at 835.

(iii) James' third opinion on consistency of Bancorp's loan performance with Defendants' specific disclosures and the market trends they disclosed.

As noted above, James' third opinion is, essentially, that the events that occurred after the first and second quarters of 2007, both with respect to Bancorp's and other banks' loan performances, show that Defendants' public disclosures in those two quarters were "par for the course." The SEC contends that this opinion is irrelevant and unreliable. According to the SEC, the opinion would mislead or confuse the jury because the performance of other banks is not relevant to the SEC's claims, and because, without access to the other banks' internal loan portfolios, any such comparisons would be unreliable. James Motion [D.E. 155 at 15-16]. Defendants counter that the fact that comparable banks eventually reported the same types of losses as Bancorp, demonstrates that Bancorp responded more aggressively to the crisis by reporting those losses in the third quarter of 2007, and that "[s]uch evidence undercuts any claim that there was any intention to mislead investors," which is critical for the establishment of scienter. Defendants' Memorandum in Opposition to Plaintiff's *Daubert* Motion to Exclude the Testimony of Christopher M. James (hereafter, "James Response") [D.E. 178 at 20, 23]. Defendants also argue that specific knowledge of the comparable banks' internal loan portfolios was unnecessary since the loans in question were not an "exotic type of loan only made by [Bancorp]." Id. at 24.

The undersigned fails to see how James' third opinion, which is wholly predicated on after-the-fact events involving not only Bancorp but other banks, would be relevant to rebutting the element of scienter in the SEC's securities fraud claims. Additionally, Defendants failed to meaningfully address the SEC's contention that the data from other banks utilized by James is incomplete, given his lack of access to those banks' internal loan portfolios. Therefore, the undersigned agrees that James' third opinion is both irrelevant and unreliable and finds that it should be excluded. [18]

3. Hearsay Objection

The SEC argues that James' fourth opinion does nothing more than recite the contents of analysts' reports regarding Bancorp's disclosures, hence is inadmissible hearsay. James Motion [D.E. 155 at 16-18]. Defendants contend that James' opinion and the analysts' reports are admissible under Fed. R. Evid. 703, which provides:

> An expert may base an opinion on facts or data in the case that the expert has been made aware of or personally observed. If experts in the particular field would reasonably rely on those kinds of facts or data in forming an opinion on the subject, they need not be admissible for the opinion to be admitted. But if the facts or data would otherwise be inadmissible, the proponent of the opinion may disclose them to the jury only if their probative value in helping the jury evaluate the opinion substantially outweighs their prejudicial effect.

***12** Fed. R. Evid. 703. Seealso, Royale Green Condo. Ass'n, Inc. v. Aspen Specialty Ins. Co., Case No. 07-CIV-21404, 2009 WL 2208166, at *2 (S.D. Fla. July 24, 2009) (admission of hearsay evidence through an expert creates a danger that the testifying expert will serve as a conduit for the opinions of others).

Defendants argue that, James, as an expert, was entitled to rely on the analysts' reports in forming his own opinion notwithstanding their hearsay status. James Response [D.E. 178 at 19]. Defendants further argue that the reports may be disclosed directly to the jury "because...they are a contemporaneous assessment...that directly undercut[s] the SEC's theory of fraud." Id. at 19-20. As noted above, James did testify that these analysts' reports are of the type that he would rely on in his own research. However, James' purported fourth opinion consists of nothing more than a summary of the analysts' reports. James Expert Report [D.E. 155-1 at ¶¶ 92-100]. Because James did not actually render an opinion, the probative/prejudicial prong of Rule 703 does not come into play and Defendants' attempt to gain admissibility of the hearsay analysts' reports through Rule 703 to rebut the SEC's securities fraud claims fails.

Therefore, the James Motion is denied as to his first and second opinions but granted as to the third and fourth ones.

VI. HUBER

At trial, Huber would offer the following opinions: (1) during the relevant period, Bancorp's relevant DC&P were adequate under the circumstances; and (2) Bancorp's disclosures in its 2007 first and second quarter Forms 10-Q concerning known trends or uncertainties were adequate under the circumstances, and the statements made during the 2007 first and second quarter earnings conference calls were not misleading. Huber Expert Report [D.E. 148-1 at 13].

A. Adequacy of Bancorp's relevant DC&P.

According to Huber, during the period in question, Bancorp's relevant DC&P were adequate under the circumstances. Huber Expert Report [D.E. 148-1 at ¶¶ 22-69], Huber further opined that adjustments made by Bancorp to its DC&P during the period from January 1 through November 9, 2007 enabled Bancorp to respond to evolving market conditions, id. at ¶¶ 27-52; that Bancorp's DC&P incorporated reviews conducted by external third parties, id. at ¶¶ 53-58; that Bancorp's public disclosures were drafted in an atmosphere of open communication and cooperation, id. at ¶¶ 59-62; and that Bancorp's internal certification process by its senior management provided an additional check to ensure that its DC&P were complete and accurate. Id. at ¶¶ 63-68. Huber also opined that Bancorp had adequate DC&P in place before the credit crisis, and that Bancorp was proactive in adjusting and adapting its DC&P to address the downturn in the Florida real estate market. Id. at ¶¶ 27-52. "As conditions deteriorated in 2007, [Bancorp] enhanced its processes ... and senior ... executives were proactive and ordered measures to refine [Bancorp's] disclosure, controls and procedures as conditions deteriorated." Id. at ¶ 15. In concluding that the DC&P were adequate throughout the crises, Huber thoroughly analyzed Bancorp's formal and informal credit approval and loan monitoring functions. Id. at ¶¶ 53-68.

B. Adequacy of Defendants' disclosures

***13** Huber testified that the existence of adequate DC&P would also be relevant to determining whether there was intent to deceive or mislead by Defendants in their public disclosures, and that, in this case, the DC&P "facilitate[d]...disclosure being made." Transcript of Daubert Evidentiary Hearing on September 25, 2013 (hereafter "Trans. 9/25") [D.E. 245 at 61-62]. Huber further testified, in response to various examples posed by Defendants' counsel, that the public disclosures made by Defendants matched the internal commentary at Bancorp. Id. at 68-81, 85.

According to Huber, Bancorp's disclosures in the 2007 first and second quarter 10-Q's regarding known trends or uncertainties in BankAtlantic's Commercial Residential Portfolio were adequate under the circumstances. Huber Expert Report [D.E. 148-1 at ¶¶ 68-87], Huber further opined that, considering the total mix of information, Defendants' disclosures in the 2007 first and second quarter earnings conference calls were not misleading, id. at ¶¶ 88-103, and that "disclosing downgraded and extended loans could have confused, rather than informed, investors." Id. at ¶ 17. Huber clarified that his opinion reflects how he, as a professional who works in the field of disclosure, would have advised management to disclose the trend it identified, and such level of disclosure would have been preferable because it was more general and easily understood by investors than "complex specifics that might be included within the general." Trans. 9/25 [D.E. 245 at 43-46]. [19]

The SEC asked Huber to confirm his opinion that management did not appear to believe that extensions or downgrades in the first and second quarters constituted a known trend requiring disclosure, id. at 52, and his opinion that the total mix of information indicated that Levan did not intentionally mislead investors during the first and second quarter earnings conference calls. Id. at 53. Huber confirmed his opinions, and indicated that they were based on his experience as an expert in the field of securities disclosure, combined with his review of the record. Id. at 52-55.

C. Challenges to Huber's Opinions

The SEC objects to Huber's methodology based on how Huber structured his team of assistants, how he divided the work, and for "not analyzing much of the material he purported to base his conclusions on." Huber Motion [D.E. 148 at 9]. The SEC further contends that Huber offers no sound methodology for his conclusions and that those conclusions are nothing more than a biased recitation of facts. Id. at 1, 4. Finally, the SEC argues that Huber's testimony will confuse the jury as it is nothing more than a legal opinion. Id. at 1. As with MacDonald and James, the SEC challenges the reliability and helpfulness/relevance of Huber's testimony.

1. Reliability

Because Huber is a nonscientific expert, consideration of his qualifications is part of the inquiry into the reliability of his methodology. Augustin, 661 F.3d at 1125; Frazier, 387 F.3d at 1261. Huber is currently a Senior Managing Director at FTI Consulting, Inc. Huber Expert Report [D.E. 148-1 at App. A]. Huber previously served as Deputy Director and Director of the SEC's Division of Corporation Finance and was responsible for the Division's rule-making program. Id.[20] Huber was also a senior partner at Latham & Watkins, LLP, where he advised clients on securities regulation issues, including compliance with securities laws and internal control over financial reporting. Id. Huber is an editor of ThePractitioner's Guide to theSarbanes-Oxley Act, published by the American Bar Association in 2004. Id.

***14** With regard to Huber's use of assistants, how he divided the work between himself and his staff, and the extent of his own personal analysis of the materials underlying his opinions, Huber testified at his deposition that he closely supervised the work of his team of two certified public accountants, that he did his own review of the documents as needed, that he conducted research independently of his team, and that he and his team generated over twenty drafts of his expert report. Huber Deposition pp. 29-32 [D.E. 171-1 at 30-33]. This testimony refutes the SEC's contention that Huber's expert work was not his own.

The SEC's argument that Huber simply recites the facts in the record and provides no explanation for his conclusions is similarly refuted by Huber's testimony. At the Daubert Evidentiary Hearing, Huber explained his reasoning for extensively quoting portions of the record in his expert report as being in keeping with his methodology for writing disclosures in his professional practice. Seee.g., Trans. 9/25 [D.E. 245 at 20-21] (explaining that in writing disclosures he balances "yes or no with respect to putting out all of the facts in a true, accurate, and complete fashion"). At his deposition, Huber testified that his opinion regarding the adequacy of the changes in Bancorp's DC&P was based on his experience in private practice doing DC&P and restatement work, participating in panels with SEC officials, and testifying at SEC hearings. Huber Deposition pp. 104-05 [D.E. 171-2 at 27-28]. Huber also laid out the twelve factors that he used in deriving his conclusions regarding Bancorp's DC&P. Huber Deposition pp. 122-28, 145-46 [D.E. 171-2 at 45-51, 68-69]. Further, with respect to his opinion on the adequacy of Defendants' disclosures in the 2007 first and second quarter Forms 10-Q, Huber described in his expert report his analysis of the SEC regulation on MD&A and its application to the facts of this case. Huber Expert Report [D.E. 148-1 at ¶¶ 69-75]. Similarly, with respect to his opinion regarding the first and second quarter earnings conference calls, Huber outlined his familiarity and experience with the informality of those calls and the importance of considering their content in light of the total mix of information, and explained how he considered these factors in forming his opinion. Id. at ¶¶ 89-103.

Based on the foregoing, the undersigned finds sufficient record support for Huber's methodology of applying his professional experience to the facts of this case. Because his methodology was informed by and conducted in accordance with his experience, Huber's opinion as a nonscientific expert meets the reliability prong. Schoenthal, 555 F.3d at 1338; McClain, 401 F.3d at 1255.

2. Helpfulness/Relevance

The SEC seeks to exclude Huber's opinions under the helpfulness/relevance inquiry as improper legal conclusions on the grounds that they embrace an ultimate legal issue and would tell the jury how to decide the case. Huber Motion [D.E. 148 at 15-17]. However, expert testimony as to the interpretation of the SEC's requirements relating to DC&P and public disclosures and the application of those requirements to the facts of a case, does not, without more, constitute improper legal conclusions. Novatel, 2011 WL 5827198, *3; Leslie, 2010 WL 2991038, at *7; Retail Pro, 2011 WL 589828, at *4. Therefore, so long as Huber's testimony does not veer into the subject of securities laws violations, his opinions regarding the adequacy of Bancorp's DC&P and Defendants' public disclosures are not impermissible legal opinions. And the SEC may seek an appropriate curative instruction to alleviate its concerns regarding the weight the jury may place on Huber's opinions. Maiz, 253 F.3d at 667; Gold, 743 F.2d at 817; Pacheco, 426 Fed.Appx. at 835.

***15** Therefore, the Huber Motion is denied.

VII. TURNER

At trial, Turner would provide the following opinions: (1) during the first and second quarters of 2007, a material downward trend related to loan quality existed within BankAtlantic's Commercial Residential Portfolio that was not adequately disclosed in the MD&A section of Bancorp's 10-Q's and the earnings conference calls for those quarters; (2) Bancorp's lack of disclosure of this trend failed to inform the investing public of the negative developments; (3) Bancorp incorrectly categorized certain loans as "held-for-investment;" and (4) due to the failure to appropriately report certain loans at market value, Bancorp's assets and income before taxes were overstated by $53 million for the year ended December 31, 2007. Turner Expert Report [D.E. 162-3 at ¶¶ 19-24, 113-16],

A. Turner's Methodology.

At the Daubert Evidentiary Hearing, Defendants questioned the number of hours that Turner devoted to the preparation of his expert report and asked him to confirm the fact that 8 days before his expert report was due, he had billed only 3 hours to the SEC. Trans. 9/24 [D.E. 244 at 20, 56-57], Turner confirmed this fact, id., and the additional fact that, in total, he only billed the SEC 38 hours for the preparation of his expert report. Id. at 21. Turner explained that he worked many additional hours that he did not bill out of "a notion of public service." Id. [21]

Defendants also questioned Turner's independence, given that he was donating time to one party in the case. Trans. 9/24 [D.E. 244 at 21]. Turner responded that "just because you don't bill for all your hours doesn't mean that you're not independent" and that other members of his accounting profession do not see providing this type of public service to be in conflict with their independence. Id. at 22. Turner also stated that he makes it clear on any engagement that his opinions are his own, and that he also takes his ethical responsibilities seriously. Id. at 103-05. [22]

In response to an inquiry as to how many hours he actually spent on the engagement, Turner testified, "I don't recall.... I can tell you it was a fair amount of hours." Id. at 22-23. Turner further testified that he approaches the task of providing an expert opinion in the same manner as preparing for an audit. Id. at 24-25, 106-07. Turner explained that "[y]ou plan it up front. You direct the staff as to what you want... and then it becomes an iterative process.... At the end of the day ... the audit is signed by the audit partner. It is [his] opinion, ... not the opinion of the staff." Id. at 25. [23]

B. Defendants' disclosures.

***16** At the Daubert Evidentiary Hearing, Turner agreed with the proposition that a "collapsing Florida real estate market" was a negative trend, but explained that "if you've got, in a particular part of your loan portfolio ... some significant positive or negative trends ... you would need to say that ... the disclosure needs to run to the particulars of the company, not a broad general [statement of] what's happening to everyone." Id. at 43, 45. Turner opined that Defendants' disclosure of the real estate market trend was not sufficient for MD&A purposes because one has "to put [the disclosure] in the context of what's going on in that particular bank so that the investors can see the bank through the eyes of management." Id. at 121. [24] Turner stated, "The cause of [Bancorp's loss] was ... I wouldn't say just the Florida real estate market. Certainly that might have been part of the cause." Id. at 53.

According to Turner, the disclosure in Bancorp's 2007 first quarter 10-Q that non-BLB Loans were "of relatively lower risk than the [BLB] loans" did not correctly identify the trend with respect to the non-BLB loans, albeit he acknowledged that he had not reviewed Bancorp's 2007 third quarter losses to determine if they matched Defendants' earlier disclosures with respect to both the BLB and the non-BLB Loans. Id. at 48-49, 52. Defendants' counsel asked Turner whether Bancorp had to disclose individual internal loan downgrades and extensions. Id. at 57. In response, Turner explained that, though trends of downgrades or extensions in a portfolio should be described, it was not necessary to mention specific loans. Id. at 58. Finally, Defendants' counsel asked Turner if he was aware that banking regulators "unanimously objected to disclosure of internal loan grades." Id. at 60. Turner confirmed his understanding that bank regulators "didn't like to see the loan grades disclosed," id. at 61, but added that companies would still need to disclose the general trend of these occurrences. Id. at 116.

C. Reclassification of the JMP Loans

In his testimony, Turner explained his reliance on two offers for establishing his valuation of the JMP Loans. Id. at 75. Turner clarified that there were actually 6 bids and that he used the 2 highest ones in computing the fair value of the JMP Loans, but could not recall whether these two bids were oral or written or when they were received. Id. at 75-76.

Defendants' counsel asked Turner whether the market was "orderly" at the December 31, 2007 measurement date. Id. at 81. Turner did not respond directly, but opined that, under FAS 157, an orderly transaction is a transaction in which information is available to the buyer and seller to make an informed bid at a fair price. Id. at 82. In response to Defendants' contention that one of the bids he relied on was from a vulture fund looking for distressed sales in a market under duress, id. at 83-84, Turner disagreed with Defendants' understanding of the term "duress," and explained that, in the context of a FAS issued by the FASB, duress is a term of art that refers only to involuntary sale or liquidation, as in bankruptcy. Id. at 84.

Turner testified that, in opining that Bancorp had made a decision to sell the JMP Loans, he relied, as would an auditor in private practice, on the engagement letter between Bancorp and JMP because it was a legal agreement. Id. at 86. Defendants' counsel asked Turner if someone else could read the contract language of the engagement letter as meaning something other than that Bancorp was offering the JMP Loans for sale. Id. at 92. Turner responded that, as a former CFO and corporate executive, he could only read it as a decision to sell loans. Id.

***17** Turner testified that he was not asked to opine regarding the fact that Bancorp still failed to properly account for the JMP Loans in the first quarter of 2008 because "[w]hat [Bancorp] did in the first...quarter [of 2008], at least in [his] mind, [wasn't] relevant to whether they did the accounting right at the end of the fourth quarter of [2007]." Id. at 74-75.

D. Challenges to Turner's Opinions

Defendants argue that Turner must be precluded from offering expert testimony at trial on several grounds. First, Defendants argue that Turner did not employ any intellectual rigor in reaching his conclusions. Turner Motion [D.E. 156 at 2]. Specifically, Defendants contend that Turner lacks the qualifications to opine regarding the Florida real estate market; that he billed only 38 hours for the generation of his expert report; that he improperly relied on unqualified assistants to conduct the underlying research and draft the report; and that he used his team's research to support his preconceived conclusions in favor of the SEC. Defendants' Reply Memorandum in Further Support of Their Motion in Limine to Exclude the Opinions and Testimony of Lynn E. Turner (hereafter, "Turner Reply") [D.E. 211 at 1-3].

Second, with respect to the "held-for-sale" issue, Defendants argue that Turner's opinions that Bancorp intended to sell the JMP Loans in the fourth quarter of 2007 and that a sufficiently orderly market existed for Bancorp to sell loans at that time; and his calculation of the fair value of the JMP Loans in the fourth quarter of 2007, must all be excluded because they are unreliable. Turner Motion [D.E. 156 at 2].

Third, Defendants argue that Turner's opinions on what a law or regulation says or means cannot be presented to a jury because they are improper legal conclusions and it is the exclusive function of the Court to address, resolve, and instruct on matters of law. Id.

Fourth, in challenging Turner's opinions that during the first and second quarters of 2007, a material downward trend related to loan quality existed within BankAtlantic's Commercial Residential Portfolio that was not adequately disclosed in the MD&A section of Bancorp's 10-Q's and the earnings conference calls for those quarters and that Bancorp's lack of disclosure of this trendfailed to inform the investing public of the negative developments, Defendants parse these two opinions into the following list of sub-opinions, which they argue must be excluded as a matter of law:

a. His opinion that BBX violated securities laws by failing to disclose changes in internal loan grades (it is an undisputed fact that the vast majority of publicly reporting banks declined to publish loan grades at the urging of all federal bank regulators and it is undisputed that disclosing the substance of what would be learned from internal loan grades, which BBX did, is perfectly appropriate);

b. His opinion that changes in internal loan grades for some land loans constituted a trend requiring disclosure;

c. His opinion that BBX was required to disclose the number and amount of loan extensions in the first and second quarter of 2007 (the vast majority of financial institutions do not make such disclosures and Turner has no knowledge of the condition of the loans that were extended thus he fails to provide any connection between a loan extension and an increased risk of loss);

***18** d. His opinion that non-BLB commercial real estate loans were just as risky as BLB loans and that the market should have been told as much (it is indisputable that the risk was not the same and the Company correctly weighed the relative risks and advised the market accordingly and timely);

e. Any opinion that the Company failed to disclose "crumbling creditworthiness of the loans within BankAtlantic's commercial real estate land acquisition and development portfolio in Q 1 and Q2 of 2007";

f. His opinion that a company can be guilty of violating securities laws for failing to include in a Form 10-Q information disclosed in an earnings conference call (Turner's opinion is nothing but a legal conclusion and an incorrect one at that); and,

g. His opinion regarding BBX's and Levan's alleged intent to defraud or deceive (another's intent is not a proper subject of expert testimony).

Id. at 3-4.

In their first and second arguments, Defendants challenge the reliability of Turner's opinions. In their third argument, they challenge their helpfulness/relevance. Defendants' fourth argument is predicated on parsing Turner's opinions that Defendants failed to disclose a material downward trend in the quality of BankAtlantic's Commercial Residential Portfolio and that the lack of disclosure of this trend failed to inform the investing public of the negative developments.

1. Reliability

Because Turner is a nonscientific expert, consideration of his qualifications is part of the inquiry into the reliability of his methodology. Augustin, 661 F.3d at 1125; Frazier, 387 F.3d at 1261.Turneris currently a Managing Director at LitiNomics. Turner Expert Report [D.E. 162-3, Ex. C, at 60]. Turner has over thirty-five years of business, regulatory and academic experience concerning accounting, auditing and financial reporting matters. Id. From 1996 to 1998, Turner was Vice President and CFO of a high-technology semiconductor and storage systems manufacturing company. Id. From July 1998 to August 2001, he served as Chief Accountant for the SEC. Id. From 2001 until 2003, he was as a professor at Colorado State University where he taught courses in accounting and auditing, including MBA-level classes, Id.

(i) Turner's intellectual rigor

Defendants first challenge Turner's lack of qualifications to opine regarding the Florida real estate market. In response, the SEC argues that Turner's expertise in the Florida housing market is irrelevant because the "true trend at issue in this case" is not the Florida real estate market, but the "crumbling creditworthiness within the [Commercial Residential] Portfolio as reflected by the multiple loan downgrades and extensions." Response in Opposition re Defendants' Motion in Limine to Exclude the Opinions and Testimony of the SEC's Expert Witness Lynn B. Turner (hereafter, "Turner Response") [D.E. 186 at 15]. However, as discussed above with respect to James, the collapse of the Florida real estate market is not irrelevant to the SEC's claims. Further, at the Daubert Evidentiary Hearing, Turner testified that, while he did not believe that Bancorp's loss was just due to the downturn in the Florida real estate market, that factor might have been part of the cause. But the fact that Turner is not versed in the Florida real estate market does not merit striking him as an expert as Defendants contend; it simply goes to the credibility and weight of his testimony. Rosenfeld, 654 F.3d at 1193 ("[I]n most cases, objections to the inadequacies of a study are more appropriately considered an objection going to the weight of the evidence rather than its admissibility."). Defendants also challenge Turner's reliability based on his having billed the SEC for only 38 hours of his time and for the way he utilized his assistants in rendering his expert report. But Turner testified extensively as to the hours he billed, the independence of his opinion, and the preparation of his expert report in the same fashion as he would conduct an audit. Based on the foregoing, the undersigned finds sufficient record support for Turner's methodology of applying his professional experience to the facts of this case. Because his methodology was informed by and conducted in accordance with his experience, Turner's opinion as a nonscientific expert meets the reliability prong. Schoenthal, 555 F.3d at 1338; McClain, 401 F.3d at 1255.

(ii) The held-for-sale issue

***19** Defendants argue that Turner's opinions with respect to this issue are unreliable. At the same time, Defendants are attacking those opinions through their own expert on this issue, MacDonald. Therefore, rather than exclude Turner's opinions as Defendants propose, the Court should defer to the jury the task of weighing the testimony of these two opposing experts. Allison, 184 F.3d at 1311 ("Vigorous cross-examination, presentation of contrary evidence, and careful instruction on the burden of proof are the traditional and appropriate means of attacking debatable but admissible evidence.").

2. Helpfulness/Relevance

Defendants argue that Turner's opinions on what a law or regulation says or means cannot be presented to a jury as it is the exclusive function of the Court to address, resolve, and instruct on matters of law. However, expert testimony on legal and regulatory requirements is permissible and does not, without more, constitute improper legal conclusions. Novatel, 2011 WL 5827198, *3; Leslie, 2010 WL 2991038, at *7; Retail Pro, 2011 WL 589828, at *4. Additionally, because securities laws constitute a complex topic that is outside the understanding of the average juror, courts have allowed the testimony of experts in this area. Seee.g., S.E.C. v. Big Apple Consulting U.S., Inc., No. 6:09-cv-1963-Orl-28GJK, 2011 WL 3753581, at *4 (M.D. Fla. Aug. 25, 2011) (acknowledging that testimony by securities experts is often admitted to assist the jury in understanding complex securities terms, practices and regulations); S.E.C. v. Sky Wav Global, LLC, Case No. 8:09-cv-455-T-23TBM, 2010 WL 5058509, at *4 (M.D. Fla. Dec. 6, 2010) (attorneys can testify in securities cases and offer opinions on securities industry customs and practices).

Therefore, so long as Turner's testimony does not veer into the subject of securities laws violations, his opinions are not impermissible legal opinions. And the SEC may seek an appropriate curative instruction to alleviate its concerns regarding the weight the jury may place on Turner's opinions. Maiz, 253 F.3d at 667; Gold, 743 F.2d at 817; Pacheco, 426 Fed.Appx. at 835. Moreover, given that MacDonald, James and Huber will be permitted to testify regarding Defendants' conduct vis-a-vis SEC laws and regulations, it would be unfair to exclude Turner. United States v. Lankford, 955 F.2d 1545, 1552 (11th Cir. 1992) ("It is an abuse of discretion to exclude the otherwise admissible opinion of a party's expert on a critical issue, while allowing the opinion of his adversary's expert on the same issue.").

3. Parsing of Turner's Disclosure Opinions

As noted above, Defendants' fourth argument is predicated on parsing Turner's opinions that Defendants failed to disclose a material downward trend in the quality of BankAtlantic's Commercial Residential Portfolio and that the lack of disclosure of this trend failed to inform the investing public of the negative developments.

With regard to trends in the Commercial Residential Portfolio, Defendants challenge the following: Turner's purported opinion that Bancorp violated securities laws by failing to disclose changes in internal loan grades; his opinion that changes in internal loan grades for some land loans constituted a trend requiring disclosure; and his opinion that Bancorp was required to disclose the number and amount of loan extensions in the first and second quarter of 2007. However, Turner explained at the Daubert Evidentiary Hearing that, though trends of downgrades or extensions in a portfolio should be described, it was not necessary to mention specific loans. Turner also confirmed his understanding that bank regulators did not like to see loan grades disclosed, but opined that companies would still need to disclose the general trend of these occurrences. To the extent that Defendants disagree with these opinions, they will have the opportunity to challenge them at trial. Allison, 184 F.3d at 1311 ("Vigorous cross-examination, presentation of contrary evidence, and careful instruction on the burden of proof are the traditional and appropriate means of attacking debatable but admissible evidence.").

***20** Defendants also challenge Turner's opinion that non-BLB commercial real estate loans were just as risky as BLB loans and that the market should have been told as much because, according to Defendants, it is indisputable that the risk was not the same and Bancorp correctly weighed the relative risks and advised the market accordingly and timely. Here, Defendants are simply disagreeing with Turner's opinion and they will be able to do so at trial. Allison, 184 F.3d at 1311.

Defendants seek to exclude any opinion that Bancorp failed to disclose "crumbling creditworthiness" of BankAtlantic's Commercial Residential Portfolio. However, this argument has been forestalled by Judge Scola's ruling that "crumbling creditworthiness" does not constitute a new and unpleaded claim. See Omnibus Order on Pending, Non-Referred Motions in Limine [D.E. 242 at ¶ 6].

Defendants argue that Turner should not be allowed to opine that a company can be guilty of violating securities laws for failing to include in a Form 10-Q information disclosed in an earnings conference call because this is nothing but a legal conclusion and an incorrect one at that. Initially, it is not clear from Turner's expert report that he intends to opine on violations of securities laws. In any event, as more fully discussed above, expert testimony on legal and regulatory requirements is permissible, particularly in such a complex area as securities laws.

Finally, Defendants seek to exclude Turner's purported opinion regarding BBX's and Levan's alleged intent to defraud or deceive because another's intent is not a proper subject of expert testimony. However, Defendants have not pointed to any particular statement by Turner indicating that he is intending to proffer any such testimony.

Therefore, the Turner Motion is denied.

VIII. CONCLUSION

Having considered the parties' arguments and the applicable law, the undersigned concludes that MacDonald, James, Huber and Turner may provide expert testimony at trial within the parameters discussed herein. Accordingly, it is

ORDERED AND ADJUDGED that:

1. The MacDonald Motion [D.E. 159] is DENIED.

2. The James Motion [D.E. 155] is DENIED as to James' first and second opinions and GRANTED as to James' third and fourth opinions.

3. The Huber Motion [D.E. 148] is DENIED.

4. The Turner Motion [D.E. 156] is DENIED.

DONE AND ORDERED in Chambers at Miami, Florida this 14th day of November, 2013.

All Citations

Not Reported in Fed. Supp., 2013 WL 12009694

Footnotes

[1] The undersigned will issue a separate Order on Plaintiff's Daubert Motion to Exclude the Testimony of David Friedman and Jeff Mindling [D.E. 149].

[2] A detailed factual recitation is found in Judge Scola's Omnibus Order on Summary Judgment [D.E. 234 at 2-11].

[3] BLB loans were loans made to land investors after they had sold to homebuilders options to purchase lots in the land holdings. For non-BLB loans, the land investors did not have pre-loan option contracts.

[4] Form 10-Q is a report that must be filed by publicly traded companies for each of their first three fiscal year quarters. Seehttp://www.sec.gov/answers/form10q.htm (last visited on October 31, 2013). "The Form 10-Q includes unaudited financial statements and provides a continuing view of the company's financial position during the year." Id.

[5] “The earnings conference call is a way for companies to relay information to all interested parties, including institutional and individual investors, as well as buy– and sell-side analysts.” Seehttp://www.investopedia.com/ask/answers/04/052104.asp (last visited October 31, 2013).

[6] Form 10-K is an annual report that must be filed by publicly traded companies. Seehttp://www.sec.gov/answers/form10k.htm (last visited on October 31, 2013). “The annual report on Form 10-K provides a comprehensive overview of the company's business and financial condition and includes audited financial statements.” Id.

[7] Defendants do object to Turner's lack of expertise in a particular area, as more fully discussed below.

[8] Judge Scola has ruled that certain statements made by Levan during the second quarter earnings conference call were false as a matter of law. See Omnibus Order on Summary Judgment [D.E. 234 at 12-15],

[9] The FAS promulgated by the Financial Accounting Standards Board (“FASB”) were the highest GAAP authority in 2007 and 2008. Trans. 9/23 [D.E. 243 at 54].

[10] In MacDonald's view, the following are indicia of a decision to sell: “the plan of sale must be approved by management having the authority to take such action;” the “actions needed to complete the plan of sale ... must be initiated;” and “the actions needed to complete the plan of sale must indicate that it is unlikely that... the plan will be withdrawn.” [Id. at ¶ 14].

[11] MacDonald testified that she had led the team that developed FAS 157 and that she was the primary author for the final rule. Trans. 9/23 [D.E. 243 at 64],

[12] Additionally, MacDonald opined that, while an orderly transaction is fundamental to a determination of fair value, there would be no orderly transaction where only six out of fifty potential bidders responded to JMP's solicitation and at least three of those bids contemplated distressed debt pricing. Id. at 65-66.

[13] While MacDonald conceded on cross-examination that there is no mathematical formula to determine fair value, Trans. 9/23 [D.E. 243 at 34], she clarified that, under GAAP, one is expected to conduct a comprehensive approach and that, while a certain amount of artistry is involved in the process, it has more to do with the precision of the valuation rather than the methodology used in conducting the valuation. Id. at 67-68.

[14] In response to repeated inquiries into the methodology underlying his market observations, James explained that methodology in detail and occasionally corrected SEC's counsel's articulation of it. Trans. 9/24 [D.E. 244 at 150-68].

[15] Judge Scola has ruled that evidence that the Office of Thrift Supervision prohibits the disclosure of internal loan grades in the MD&A section of 10-Q's is admissible because it is relevant and material to Defendants' overall state of mind. See Omnibus Order on Pending, Non-Referred Motions in Limine [D.E. 242 at ¶ 10(F)].

[16] Thus, the SEC's burden here is different from that of plaintiffs in a private securities class action that was based on the same events, namely, Hubbard v. BankAtlantic Bancorp, Inc., 688 F.3d 713 (11th Cir. 2012). There, in addition to the foregoing elements, plaintiffs needed to prove loss causation and damages. Id. at 725.

[17] Judge Scola has ruled that testimony comparing Bancorp's disclosures and performance to that of other banks will only be admissible at trial to rebut scienter to the extent that Levan or anyone else at Bancorp knew of the disclosures and performance of other banks and relied upon that knowledge in their activities and decision-making process. See Omnibus Order on Pending, Non-Referred Motions in Limine [D.E. 242 at ¶ 10(E)]. Logically, James' second opinion is subject to this same restriction.

[18] Although the undersigned has found that James utilized an acceptable overall methodology, this particular opinion is unreliable due to the lack of complete data.

[19] Huber repeatedly characterized Defendants' disclosures regarding Bancorp's loan exposure in the deteriorating Florida real estate market as “putting up a flare,” that is, warning the market of a serious issue. Trans. 9/25 [D.E. 245 at 64-66, 78].

[20] The Division of Corporation Finance is the division that: drafts the SEC's rules concerning disclosure by companies that report to the SEC; provides interpretive guidance concerning disclosure by public

companies; and reviews and comments on filings by public companies. Seehttp://www.sec.gov/divisions/corpfin/cfabout.shtml (last visited on October 31, 2013).

[21] Turner testified that public service is "near and dear to [his] heart" and "an important thing in this country." Trans. 9/24 [D.E. 244 at 109]. Furthermore, Tuner provided a sworn declaration attesting to the appropriateness of the time billed and the reliability of his methodology. [D.E. 186-1 at ¶¶ 4-13].

[22] Turner further explained that he doesn't care about his billable hours because he has done "very well in life" and "just enjoy[s] what [he's] doing." Id. at 108.

[23] Turner added that, for professional accountants practicing in the field, in a typical audit staffing, only "about five percent" of the total time billed by the team on the project is billed by the audit partner. The rest of the time is billed by an "audit manager" and "by other staff." Id. at 106.

[24] According to Turner, a bank should disclose in its MD&A concerns about creditworthiness within the respective subsections of its loan portfolios. Id. at 115.

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207 N.C.App. 749
Unpublished Disposition
NOTE: THIS OPINION WILL NOT APPEAR IN A PRINTED VOLUME. THE DISPOSITION WILL APPEAR IN THE REPORTER.
Court of Appeals of North Carolina.

STATE of North Carolina
v.
Adrian Lee BULLOCK.

No. COA10–320.
|
Nov. 2, 2010.

***1** Appeal by Adrian Lee Bullock from judgment entered 24 June 2009 by Judge Abraham P. Jones in Durham County Superior Court. Heard in the Court of Appeals 14 September 2010.

Attorneys and Law Firms

Attorney General Roy Cooper, by Assistant Attorney General Margaret A. Force, for the State.

William D. Spence for defendant appellant.

Opinion

HUNTER, JR., ROBERT N., Judge.

Adrian Lee Bullock ("defendant") was convicted of statutory rape and taking indecent liberties with a child and appeals on numerous grounds. For the following reasons, we find no reversible error.

I. Factual and Procedural Background

Defendant was indicted for statutory rape or sexual offense of a person who is fifteen years old, second-degree kidnapping, and taking indecent liberties with a child. At trial, the State first offered the prosecuting witness, Sarah, who was fifteen at the time of the alleged crime.[1] She testified as follows. On Wednesday, 18 July 2007, she was walking her dog when she saw defendant, her neighbor, spraying for ants in his yard. Defendant stated he was out of ant killer, and Sarah traveled to her residence where she obtained some ant killer for him. When she returned to defendant's residence, defendant grabbed Sarah's arm, pulled her into his residence, and led her to his bedroom. There, defendant forced Sarah onto his bed, and inserted his penis into her vagina over her objections. Sarah did not mention oral sex during her testimony. She saw and heard the *Jerry Springer Show* on defendant's television during the encounter. She stated defendant had black sheets on his bed, there was a Playstation video game console on his floor, and there were several pictures on the table next to his bed. Sarah testified that when the sexual encounter was over, she walked out of defendant's bedroom, out of the residence, and returned to her own residence where she immediately took a shower. After the shower, she called her friend Jessica, who suggested Sarah tell her parents about the incident. Sarah also called her grandmother who demanded she do the same by Saturday. Sarah told her father about the incident that Friday.

Sarah's father called the Durham County Sheriff's Department, and Sarah was taken to the emergency room. At the hospital, she was interviewed by Dr. Anne–Caroline Norman. After meeting with Dr. Norman, she was interviewed and examined by Dr. Karen St. Claire. Dr. Aditee Narayan testified for the State at trial because Dr. St. Claire was out of town. Dr. Narayan testified she had examined Dr. St. Claire's medical evaluation report; she discussed the findings, stating the report revealed a bruise to the hymen and abrasions extending from the outer part of the hymen through the floor of the vagina. Dr. Narayan testified these injuries were "consistent with an injury that happened a few days prior [to the examination]." She also testified the injuries were consistent with the "history of the sexual assault that [Sarah] provided."

***2** Donna Stanley, a licensed clinical social worker who had been Sarah's therapist for fourteen months following the incident, testified about Sarah's mental state following the encounter with defendant. She stated Sarah had exhibited various symptoms, such as flashbacks and depression, but had gradually improved. She also testified that Sarah had experienced crying spells and dreams about the alleged rape. Stanley commented that Sarah had an impressive memory: "She had an amazing memory. The details were consistent over the whole fourteen months, which is almost like a photographic memory."

Defendant testified and denied raping or assaulting Sarah, but admitted her description of his bedroom was correct. His wife, who was not home during the incident, testified she telephoned and spoke with defendant on the day of the incident around 11:20 a.m. for at least twenty to twenty-five minutes and that nothing seemed out of the ordinary. She also testified that after being notified of Sarah's allegations, defendant appeared to be shocked, upset, and puzzled.

A biologist testified Sarah's undergarments, as well as tests taken from Sarah's person, did not reveal the presence of semen. Another expert could find no transfer of hair from defendant to Sarah. Dr. Norman testified that, when she interviewed Sarah at the emergency room, Sarah stated defendant had performed oral sex on her. Scott Bradsher, the coordinator for the local television station, testified the *Jerry Springer Show* ran in the area from 12:00 p.m. to 1:00 p.m. on the date of the encounter, but conceded the footage Sarah claimed to have seen and heard could have been a recording.

The jury found defendant guilty of statutory rape and taking indecent liberties, but not guilty of second-degree kidnapping. He was sentenced to a concurrent active term of 316 to 389 months on the statutory rape conviction and 25 to 30 months on the indecent liberties charge. He gave oral notice of appeal in open court and appealed to this Court.

II. Jurisdiction

Defendant appeals as a matter of right pursuant to N.C. Gen.Stat. § 15A–1444(a) (2009). We have jurisdiction over his appeal pursuant to N.C. Gen.Stat. § 7A–27(b) (2009).

III. Analysis

Defendant appeals both convictions. His argument can be summarized as follows: (1) it was plain error to admit portions of Dr. Narayan's and Dr. St. Claire's expert testimony and portions of Stanley's and Dr. St. Claire's non-expert testimony; (2) the trial court committed reversible error by denying defendant's motions to dismiss at the close of all the evidence; and (3) the trial court committed reversible error by failing to intervene *ex mero motu* during the State's closing argument. After careful review, we conclude the trial court did not commit reversible error.

A. The Testimonial Evidence

Defendant argues the admission of Dr. Narayan's expert testimony, Dr. St. Claire's expert testimony, Dr. St. Claire's non-expert testimony, and Stanley's non-expert testimony impermissibly bolstered Sarah's credibility. Defendant failed to object at trial, so we review for plain error. N.C. R.App. P. 10(a)(4).

***3** When a defendant fails to object at trial, plain error review requires him to meet a heavy burden on appeal:

> [T]he plain error rule ... is always to be applied cautiously and only in the exceptional case where, after reviewing the entire record, it can be said the claimed error is a “fundamental error, something so basic, so prejudicial, so lacking in its elements that justice cannot have been done,” or “where [the error] is grave error which amounts to a denial of a fundamental right of the accused,” or the error has “ ‘resulted in a miscarriage of justice or in the denial to appellant of a fair trial’ “ or where the error is such as to “seriously affect the fairness, integrity or public reputation of judicial proceedings” or where it can be fairly said “the instructional mistake had a probable impact on the jury's finding that the defendant was guilty.”

State v. Odom, 307 N.C. 655, 660, 300 S.E.2d 375, 378 (1983) (alteration and footnotes omitted in original) (quoting *United States v. McCaskill,* 676 F.2d 995, 1002 (4th Cir.1982)). To amount to plain error, the error in question must have “tilted the scales,” causing the jury to rule against the defendant. *State v. Black,* 308 N.C. 736, 741, 303 S.E.2d 804, 807 (1983).

1. The Expert Testimony

North Carolina Rule of Evidence 702(a) addresses the admissibility of expert testimony:

> If scientific, technical or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion.

N.C.R. Evid. 702(a). However, expert testimony is not admissible to vouch for a witness's credibility. *State v. Heath,* 316 N.C. 337, 342, 341 S.E.2d 565, 568 (1986). This limitation on expert testimony is derived from the application of North Carolina Rules of Evidence 608(a) and 405(a). Rule

608(a) states that the credibility of a witness may be attacked or supported by reputation or opinion evidence as provided by Rule 405(a). N.C.R. Evid. 608(a). Rule 405(a) states that "[e]xpert testimony on character or a trait of character is not admissible as circumstantial evidence of behavior." N.C.R. Evid. 405(a). Our courts have concluded that, when read together, Rules 608 and 405 prohibit experts from testifying as to a witness's credibility. *Heath,* 316 N.C. at 342, 341 S.E.2d at 568; *see also, e.g., State v. Bailey,* 89 N.C.App. 212, 219, 365 S.E.2d 651, 655 (1988) ("[T]he testimony of an expert to the effect that a prosecuting witness is believable, credible, or telling the truth is inadmissible evidence.").

In sexual abuse cases, there is an inherent conflict between (1) the need for expert medical testimony that tends to establish whether abuse has occurred and (2) the prohibition on admitting that very testimony for the purpose of bolstering a victim's credibility. Our courts have developed a significant body of case law attempting to reconcile these competing interests. An expert may not testify that sexual abuse has "*in fact* " occurred without a foundation of physical evidence supporting that opinion. *State v. Stancil,* 355 N.C. 266, 266–67, 559 S.E.2d 788, 789 (2002) (per curiam). Nor may an expert rely solely on interviews with a child as a basis for testifying that the child was "sexually abused." *State v. Grover,* 142 N.C.App. 411, 419, 543 S.E.2d 179, 183–84 (citing *State v. Dick,* 126 N.C.App. 312, 315, 485 S.E.2d 88, 90, (1997)), *aff'd per curiam,* 354 N.C. 354, 553 S.E.2d 679 (2001). But "it is ... well-settled that testimony based on the witness's examination of the child witness and expert knowledge concerning the abuse of children in general is not objectionable because it supports the credibility of the witness or states an opinion that abuse has occurred." *Dick,* 126 N.C.App. at 315, 485 S.E.2d at 89; *accord In re Butts,* 157 N.C.App. 609, 617, 582 S.E.2d 279, 285 (2003) ("[O]therwise admissible expert testimony is not rendered inadmissible merely because it enhances a witness's credibility."). Furthermore, "an expert witness may testify, upon a proper foundation, as to the profiles of sexually abused children and whether a particular complainant has symptoms or characteristics consistent therewith." *Stancil,* 355 N.C. at 267, 559 S.E.2d at 789 (citing *State v. Hall,* 330 N.C. 808, 818, 412 S.E.2d 883, 888 (1992); *State v. Aguallo,* 322 N.C. 818, 822–23, 370 S.E.2d 676, 678 (1988); *State v. Kennedy,* 320 N.C. 20, 32, 357 S.E.2d 359, 366 (1987)).

***4** Defendant contends the physical evidence was insufficient to support Dr. Narayan's testimony. He argues that, "in effect," Dr. Narayan testified that "the physical examination of [Sarah] was consistent with her being pulled into the defendant's house and raped by him." Defendant also claims Dr. Narayan's testimony "indicated that defendant was the very one who had assaulted [Sarah]."

Defendant's account mischaracterizes the record. Dr. Narayan's opinion was based on Dr. St. Claire's report, so before giving her opinion, Dr. Narayan related the details of that report. The report contained Sarah's case history, including the allegations of rape. After discussing the results of the physical examination Dr. St. Claire had performed, and describing the general symptoms of child sexual abuse, the following exchange occurred:

> Q. Based on your review of the medical record in this case and Dr. St. Claire's interview and examination, are you able to form an expert opinion regarding the cause of the genital injury?
>
> A. Yes.
>
> Q. What is your expert opinion?
>
> A. Based on the information documented, it is most consistent—it is determined that her physical exam findings, which we discussed already, are consistent with the history of sexual assault that she provided.

Dr. Narayan's reference to "the history of sexual assault ... [Sarah] provided" clearly refers to the sexual act itself. She was testifying as to "the cause of the genital injury"—not the events leading up to the cause of the genital injury. She did not testify that Sarah's account of the sexual assault, or the events surrounding it, were accurate. Nor did she state that she believed Sarah or that Sarah's story was credible.

This reading falls in line with our Supreme Court's decision in *State v. Aguallo.* There, the expert witness testified the victim's hymen had been lacerated. *Aguallo,* 322 N.C. at 822, 370 S.E.2d at 678. When asked whether the victim's injuries were consistent with what the victim had told her, the expert replied, "I felt it was consistent with her history." *Id.* The Court provided the following analysis:

> Essentially, the doctor testified that the physical trauma revealed by her examination of the child was consistent with the abuse the child alleged had been inflicted upon her.

> We find this vastly different from an expert stating on examination that the victim is "believable" or "is not lying." The latter scenario suggests that the complete account which allegedly occurred is true, that is, that this defendant vaginally penetrated this child. The actual statement of the doctor merely suggested that the physical examination was consistent with some type of penetration having occurred. The important difference in the two statements is that the latter implicates the accused as the perpetrator of the crime by affirming the victim's account of the facts. The former does not.

Id.

Considering Dr. Narayan's testimony in context, it is apparent defendant's reliance on several post-*Aquallo* decisions, is misplaced. In *State v. O'Connor,* this Court held it was error to admit a portion of an expert's written report that explicitly stated a victim's allegations of sexual assault were credible. 150 N.C.App. 710, 712, 564 S.E.2d 296, 297 (2002). The mistake by the trial judge constituted *plain error* "because there was no physical evidence of abuse and the State's case was almost entirely dependent" on the victim's credibility. *Id.* Here, Dr. Narayan did not explicitly endorse Sarah's allegations as credible.

***5** Defendant also relies on *State v. Couser,* which is distinguishable. There, a physician testified "that her diagnosis of the victim was 'probable sexual abuse.' " State v. Couser, 163 N.C.App. 727, 729, 594 S.E.2d 420, 422 (2004). We held the trial court erred by admitting that testimony because there was an insufficient basis for the expert's conclusion. On cross-examination, the testifying expert admitted the abrasions forming the basis of her opinion "were not diagnostic nor specific to sexual abuse." *Id.* at 730, 594 S.E.2d 420, 549 S.E.2d at 422. We held it was *plain error* because the State's only direct evidence was the victim's testimony, which was corroborated by other witnesses. *Id .* at 731, 594 S.E.2d at 423 (distinguishing *Stancil*). Unlike the physician in *Couser,* Dr. Narayan did not state Sarah was the probable victim of sexual abuse—only that the physical evidence was *consistent* with the sexual penetration described by Sarah. There was plenty of evidence for that conclusion. Therefore, *Couser* does not provide a basis for us to conclude the trial court below committed error.

Defendant's reliance on *State v. Streater* is also misplaced. In that case, the expert testimony amounted to an impermissible opinion regarding the victim's credibility because there was no physical evidence supporting the expert's conclusion that his findings were consistent with the victim's account of the sexual assault. State v. Streater, 197 N.C.App. 632, ––––, 678 S.E.2d 367, 374 (2009) (explaining the expert "testified that there was no physical evidence of anal penetration"). We concluded the trial court committed *plain error* because the victim's testimony was the only direct evidence implicating the defendant on the charge of first-degree sexual offense. Here, there was physical evidence supporting Dr. Narayan's conclusion. We find no error, let alone plain error, in the admission of Dr. Narayan's testimony.

Defendant contends the admission of the following expert testimony by Dr. St. Claire amounted to plain error:

> I had a detailed history from [Sarah], with her telling me what had happened. I felt that these genital injuries were consistent with trauma and with the history that she had provided. Although they are not specific for sexual trauma, they certainly are consistent with that, in particular, the bruising on the hymen[,] and felt that these [injuries] were consistent with the history of a sexual assault that she provided.

In addition to making the same arguments we have already discussed above, which we reject in this context as well, defendant claims this testimony is baseless because there was no evidence of vaginal intercourse. This contention, of course, ignores the substantial physical evidence of recent bruising and abrasions. Furthermore, Dr. St. Claire's testimony that the genital injuries *could* be caused by other sources does not conflict with her testimony that the injuries are *consistent* with a history of sexual assault. *Cf.* State v. Ewell, 168 N.C.App. 98, 103, 606 S.E.2d 914, 918 (2005) (stating that testimony indicating a child exhibits characteristics consistent with abuse is admissible " 'to inform the jury that the lack of physical evidence of abuse is not conclusive that abuse did not occur' " (quoting *State v. Bush,* 164 N.C.App. 254, 258, 595 S.E.2d 715, 718 (2004))). Therefore, we conclude it was not error, and certainly not plain error, to admit Dr. St. Claire's expert testimony.

2. The Non-expert Testimony

***6** Defendant next argues admitting Donna Stanley's and Dr. St. Claire's non-expert testimony was plain error because it impermissibly bolstered Sarah's testimony. Stanley, a licensed social worker who was Sarah's therapist for fourteen months after the offense occurred, testified as a non-expert witness. In an attempt to explain why Sarah did not immediately report the encounter with defendant, and to gauge the effect of the incident on Sarah, the State questioned Stanley regarding Sarah's interaction with her parents. In the course of that discussion, Stanley indicated Sarah's parents had been supportive since the incident. When asked whether this was "clinically significant," Stanley replied as follows: "Yes. It's extremely helpful in healing a rape victim to be believed. If her parents did not doubt [her story], they believed, and showed it in action by going to the police and doing what they needed to do to address it." Defendant argues this testimony amounted to plain error, not because it skirted the line between lay and expert opinion, but because it conveyed a message that Stanley and Sarah's parents believed Sarah's account of the incident. Defendant also contends the admission of similar remarks on the subject of Sarah's memory made by Dr. St. Claire and Stanley constituted plain error. Stanley stated that over the course of fourteen months, the details of Sarah's story had remained the same, remarking that "she had an amazing memory." Dr. St. Claire made similar comments.

Lay witness opinion testimony must be limited to "those opinions or inferences which are (a) rationally based on the perception of the witness and (b) helpful to a clear understanding of his testimony or the determination of a fact in issue." N.C.R. Evid. 701. Therefore, a non-expert witness is prohibited from vouching for the veracity of another witness. *See* *State v. Robinson,* 355 N.C. 320, 334–35, 561 S.E.2d 245, 255 (2002) (applying Rule 701). Of course, lay opinion testimony is not automatically inadmissible simply because it also favorably reflects on the credibility of another witness. *See* *Dick,* 126 N.C.App. at 315, 485 S.E.2d at 89 (stating this rule in the context of expert testimony); *In re Butts,* 157 N.C.App. at 617, 582 S.E.2d at 285 (same).

We express no opinion as to whether the admission of each of these three pieces of evidence was error, because even assuming it was, it would not rise to the level of *plain error.* There were numerous witnesses whose testimony *permissibly* bolstered Sarah's credibility. As discussed above, the expert testimony, which was properly admitted, likely had an incidental benefit to Sarah's credibility. Furthermore, defendant admitted Sarah had accurately described his bedroom. Thus, the jury had numerous occasions to judge Sarah's credibility independent of the allegedly improper testimony. Consequently, defendant has failed to establish either Stanley's or Dr. St. Claire's non-expert testimony "tilted the scales," causing the jury to rule against him.

B. Defendant's Motions to Dismiss

***7** Defendant next argues the trial court erred by failing to grant defendant's motions to dismiss the charges of statutory rape and indecent liberties. We disagree. The denial of a motion to dismiss for insufficient evidence is reviewed *de novo* on appeal. *State v. Bagley,* 183 N.C.App. 514, 523, 644 S.E.2d 615, 621 (2007) (citing *Shepard v. Ocwen Fed. Bank, FSB,* 172 N.C.App. 475, 478, 617 S.E.2d 61, 64 (2005)). When confronted with a motion to dismiss, the trial court must determine whether there is substantial evidence of each essential element of the offense charged and of the defendant being the perpetrator. *State v. Crawford,* 344 N.C. 65, 73, 472 S.E.2d 920, 925 (1996) (citing *State v. Vause,* 328 N.C. 231, 236, 400 S.E.2d 57, 61 (1991)). Substantial evidence has been defined as the amount of relevant evidence reasonably needed to support a conclusion. *Vause,* 328 N.C. at 236, 400 S.E.2d at 61. The evidence, which may be direct or circumstantial, must be viewed in the light most favorable to the State, giving the State the benefit of every reasonable inference. *State v. Barden,* 356 N.C. 316, 351, 572 S.E.2d 108, 131 (2002) (citing *State v. Lucas,* 353 N.C. 568, 581, 548 S.E.2d 712, 721 (2001); *State v. Locklear,* 322 N.C. 349, 358, 368 S.E.2d 377, 382–83 (1988)).

1. The Statutory Rape Charge

A person is guilty of statutory rape if he or she "engages in vaginal intercourse or a sexual act with another person who is 13, 14, or 15 years old and the defendant is at least six years older than the person, except when the defendant is lawfully married to the person." N.C. Gen.Stat. § 14–27.7A(a) (2009). Defendant claims his motion should have been granted because the district attorney failed to address whether defendant was married to the victim. He concedes, however, that he testified he was married to his wife, Kitoria Downey, for approximately five years, which overlaps with the date of the crime. Therefore, there was substantial evidence that defendant and Sarah were not married.

Defendant also argues there was insufficient evidence that he engaged in vaginal intercourse with Sarah. As a general rule, the testimony of a single witness is sufficient to defeat a motion to dismiss. *State v. Vehaun,* 34 N.C.App. 700, 704, 239 S.E.2d 705, 709 (1977). This rule does not apply, however, "when the only testimony justifying submission of the case to the jury is inherently incredible and in conflict with the physical conditions established by the State's own evidence." *State v. Wilson,* 293 N.C. 47, 51, 235 S.E.2d 219, 221 (1977) (citing *State v. Miller,* 270 N.C. 726, 731, 154 S.E.2d 902, 905 (1967)). Defendant contends the exception applies because there was conflicting testimony as to whether Sarah could have seen and heard the *Jerry Springer Show* on defendant's television. A representative of the local television station with exclusive rights to run the *Jerry Springer Show* testified that the program was not scheduled to run until an hour after the time Sarah testified she was forced into defendant's residence, although the representative admitted the show could have been a recording. Sarah accurately described defendant's room, correctly testifying there were black sheets on his bed, a Playstation video game console on his floor, and several pictures on his table. Viewed in the light most favorable to the State, the *potential* misidentification of a daytime talk show during a forced sexual encounter does not make Sarah's testimony "inherently incredible." We find no error in the trial court's denial of defendant's motion to dismiss.

2. The Indecent Liberties Charge

***8** A person that is at least sixteen years old and at least five years older than the victim is guilty of taking indecent liberties with a child if he "[w]illfully takes or attempts to take any immoral, improper, or indecent liberties with any child of either sex under the age of 16 years for the purpose of arousing or gratifying sexual desire." N.C. Gen.Stat. § 14–202.1(a)(1) (2009). Defendant first argues there was not substantial evidence that he acted for the purpose of arousing or gratifying a sexual desire. His argument lacks merit because a jury may infer from a defendant's actions that his purpose was to arouse himself or gratify his sexual desire. *See* *State v. Rogers,* 109 N.C.App. 491, 505–06, 428 S.E.2d 220, 228–29 (1993) (permitting an inference that the defendant intended to arouse himself or gratify his sexual desire); *State v. Slone,* 76 N.C.App. 628, 631, 334 S.E.2d 78, 80 (1985) (same). Sarah testified defendant grabbed her, forced her into his home, and then raped her. This testimony alone is sufficient to defeat a motion to dismiss, even without corroboration.

Defendant also argues his motion to dismiss should have been granted because a conviction on statutory rape and indecent liberties charges arising from the same transaction violates the double jeopardy clause. Defendant has abandoned this argument because he failed to raise double jeopardy in his assignments of error. *See* *State v. Bell,* 359 N.C. 1, 27–28, 603 S.E.2d 93, 111–12 (2004) (declining to review a double jeopardy argument when defendant failed to object on double jeopardy grounds at trial and failed to address double jeopardy in his assignments of error); *State v. Wiley,* 355 N.C. 592, 615, 565 S.E.2d 22, 39 (2002) ("It is well settled that an error, even one of constitutional magnitude, that defendant does not bring to the trial court's attention is waived and will not be considered on appeal."); *State v. Hamilton,* 351 N.C. 14, 22, 519 S.E.2d 514, 519 (1999) ("Our scope of appellate review is limited to those issues set out in the record on appeal.").

C. The State's Closing Argument

Finally, defendant argues the trial court should have intervened *ex mero motu* during the State's closing argument when his trial counsel failed to object to the prosecutor's credibility-related statements and allegedly emotionally charged argument. We conclude the trial court's failure to intervene does not necessitate a new trial. To constitute reversible error, "the prosecutor's remarks must be both improper and prejudicial. Improper remarks are those calculated to lead the jury astray." *State v. Jones,* 355 N.C. 117, 133, 558 S.E.2d 97, 107–08 (2002). But when a defendant fails to object during the State's closing argument, he has a heavier burden of persuasion on appeal:

> [The] defendant must show that the alleged impropriety was so gross that the trial court abused its discretion in not correcting the arguments *ex mero motu.* Under this standard, only an extreme impropriety on the part of the prosecutor will compel this Court to hold that the trial judge abused his discretion in not recognizing and correcting *ex mero motu* an argument that defense counsel apparently did

> not believe was prejudicial when originally spoken.

***9** *Wiley,* 355 N.C. at 620, 565 S.E.2d at 42 (citations and internal quotation marks omitted).

Generally, "counsel possesses wide latitude to argue facts in evidence and all reasonable inferences arising from those facts." *Id.* at 620, 565 S.E.2d at 42. While attorneys may not express their personal opinions, they may argue the jury should not believe a particular witness. *State v. Augustine,* 359 N.C. 709, 725, 616 S.E.2d 515, 528 (2005) (citing *State v. Jones,* 358 N.C. 330, 350, 595 S.E.2d 124, 137 (2004); *State v. Golphin,* 352 N.C. 364, 455, 533 S.E.2d 168, 227 (2000)); *see also* N.C. Gen.Stat. § 15A–1230(a) (2009) (forbidding attorneys from expressing "personal beliefs as to the truth or falsity of evidence"). A prosecutor may give the jury "reasons to believe the state's witnesses," *Wiley,* 355 N.C. at 622, 565 S.E.2d at 43, and may "argue that the State's witnesses are credible," *Augustine,* 359 N.C. at 725, 616 S.E.2d at 528. Statements during closing argument "must be considered in the context in which the remarks were made and the overall factual circumstances to which they referred." *Id.* (citation and internal quotation marks omitted).

Defendant argues a litany of the prosecutor's comments were grossly improper because the prosecutor impermissibly inferred and explicitly stated defendant and his wife were lying. These statements include the following: "Frankly, unless you choose to believe the made-up testimony of the defendant and his wife, then the testimony is uncontradicted"; "Now, then we spoke to Kitoria Downey, the co-master conspirator, with her husband, who's been practicing every day, engaged in a dialogue to try to thwart you and try to hide the truth from you"; and, "That's part of the lie, part of the misrepresentation."

We recently found it was not reversible error when a trial judge failed to intervene *ex mero motu* after the following prosecutorial comments:

> You can look at that statement and when you do you know that when Detective Ward got up there on the stand and said we didn't believe him, you can see why, because it's in that statement. He was lying.... But later he found out that this statement means he's guilty of kidnapping, robbery, sex offense and murder. What can he do? Well, somehow he's got to get rid of this statement, this statement that he gave of his own free will.
>
> ...
>
> He's had four year[s], ladies and gentlemen, to think about what he would say. He's had access to all the [d]iscovery, the complete investigation. And he used that to craft this story because that's what he told you when he took the stand, he told you a story.

State v. Sanders, 201 N.C.App. 631, ––––, 687 S.E.2d 531, 538, *disc. review denied,* 363 N.C. 858, 695 S.E.2d 106 (2010). After reviewing the record and the context in which the prosecutor's statements were made, we conclude that while the prosecutor's credibility-related statements certainly bordered on impropriety, they were not so grossly improper that the trial court committed reversible error by failing to intervene *ex mero motu. Cf. State v. Roache,* 358 N.C. 243, 300, 595 S.E.2d 381, 418 (2004) (admonishing "counsel to refrain from suggesting that the expert's opinion testimony has been bought or is perjured for compensation," but nevertheless determining counsel's comments were not grossly improper).

***10** Defendant also contends the following statement was improper because it invited the jurors to decide the case based on emotion and sympathy: "You really didn't need but one witness, and she's the first one I called to the stand. Do not tell [Sarah] that you do not believe her." Defendant argues this case is distinguishable from several North Carolina Supreme Court cases where there was significant evidence against the defendants and the Court suggested the prosecutors' comments were inappropriate, but did not justify new trials. *See id.* at 297–98, 595 S.E.2d at 416 (ruling prosecutor's comments were improper but did not necessitate a new trial given the overwhelming evidence against defendant); *State v. McCollum,* 334 N.C. 208, 224–25, 433 S.E.2d 144, 152–53 (1993) (ruling defendant was not denied due process by prosecutor's comments asking jurors to imagine the victim was their child when the evidence against defendant was overwhelming); *State v. Boyd,* 311 N.C. 408, 418, 319 S.E.2d 189, 197 (1984) (expressing displeasure with the prosecutor's comments, but concluding they were not grossly improper and noting there was substantial evidence against defendant). He claims this case is distinguishable because there is not overwhelming evidence against him.

His argument fails because the prosecutor's comments were not improper in this respect as they did not invite the jurors to decide the case based on emotion and sympathy. The prosecutor's comments were not a blatant appeal to the juror's emotions; rather, the prosecutor suggested the jury was confronted with conflicting accounts of what transpired and encouraged the jury to side with Sarah's version. A closing argument is not impermissible merely because it may provoke an emotional response. *Cf., e.g., In re Butts,* 157 N.C.App. at 617, 582 S.E.2d at 285 (2003) (stating that otherwise admissible expert testimony is not inadmissible because it incidentally enhances a witness's credibility). Therefore, the trial court did not commit reversible error by failing to intervene.

IV. Conclusion

No reversible error.

Judges HUNTER, ROBERT C., and WALKER concur.

Report per Rule 30(e).

All Citations

207 N.C.App. 749, 701 S.E.2d 403 (Table), 2010 WL 4290134

Footnotes

[1] Pseudonyms are used to conceal the identity of the victim.

End of Document

2003 WL 21017456

UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Superior Court of North Carolina, Mecklenburg County, Business Court.

SUNBELT RENTALS, INC., a North Carolina corporation, Plaintiff,
v.
HEAD & ENGQUIST EQUIPMENT, L.L.C., d/b/a Hi-Lift, Robert Hepler, Douglas Kline, Michael Quinn, Gregg L. Christensen, Patrick C. Muldoon, Michele U. Dougherty and Brian W. Pearsall, Defendants.

No. 00-CVS-10358.
|
May 2, 2003.

{1} This case highlights a basic duality in our economic system and the business laws which govern that system. Our system is dependent on both competition and ethics. The preservation and promotion of fair competition is one of the primary goals of our business laws. Competition fuels the engines of our economic system. Without it, productivity gains, innovation, efficiency and economy would be severely diminished; employees would have fewer opportunities for betterment; investors would receive smaller returns on their capital; and consumers would pay more for their purchases. Competition, like any fuel not properly contained and utilized, can become destructive. To insure that competition is beneficial instead of destructive, our business laws impose certain constraints on competition. One of the key mechanisms for imposing those constraints is state unfair competition laws. In this case, the Court is called upon to determine whether certain conduct of the defendants is outside the bounds of fair, ethical competition, and thus violates North Carolina's Unfair and Deceptive Trade Practices Act ("U.D.T.P.A."), N.C.G.S. § 75-1.1. The Court concludes that in certain instances the competitive actions of the defendants have exceeded the bounds of fair and ethical competition and thus violated that statute. Plaintiffs have been damaged in the amount of five million dollars, which amount is trebled pursuant to the statute.

{2} Drawing that boundary and determining appropriate damages for the out of bounds activity has been difficult in this case. The primary difficulties arise from (1) the failure of the plaintiff corporation to take even the most rudimentary steps to protect itself from the very competition about which it now complains, (2) the highly competitive nature of the aerial work platform leasing industry, (3) the key role service and people play in an industry characterized by a uniformity of physical product, (4) the failure of the defendants to testify fully and truthfully, and (5) the overlapping impact of both fair and unfair competition on the damages issues.

{3} The Court has previously granted summary judgment in favor of all defendants on the plaintiff's claims for breach of fiduciary duty and aiding and abetting breach of fiduciary duty. See Sunbelt Rentals, Inc. v. Head & Engquist Equipment, L.L.C., 2002 NCBC 4 (No. 00 CVS 10358, Mecklenburg County Super. Ct. July 10, 2002) (Tennille, J.) Additionally, at the close of plaintiff's evidence the Court granted Defendants Patrick Muldoon and Michele Dougherty's motion to dismiss plaintiff's claims against them pursuant to Rule 41(b).

Attorneys and Law Firms

Parker, Poe, Adams & Bernstein, L.L.P., by Edward B. Davis, Deborah L. Edney, William L. Rikard, Jr., and Eric D. Welsh, for plaintiff.

Helms Mulliss & Wicker, P.L.L.C., by Marna M. Albanese, Irving M. Brenner, and Paul M. Navarro, for defendants.

ORDER AND OPINION

BEN F. TENNILLE, Special Superior Court Judge for Complex Business Cases.

I.

FINDINGS OF FACT

***1** {4} The following Findings of Fact are entered after 10 days of trial without a jury, hearing 28 live witnesses, reviewing deposition designations for 47 other witnesses covering thousands of pages, and reviewing written discovery responses and over 600 exhibits.

Parties

{5} Plaintiff Sunbelt is a North Carolina corporation that rents construction and industrial equipment. It does business throughout the United States, including Mecklenburg County, North Carolina, where it has a place of business. On April 20, 2000, Sunbelt announced the purchase of BET Plant Services, Inc. ("Plant Services"), including its division BPS Equipment Rental and Sales ("BPS"). The purchase was consummated on June 1, 2000. BPS had been in the business of renting, selling and installing construction and industrial aerial work platform equipment and scaffolding since 1939. Prior to its acquisition by Sunbelt, BPS was headquartered in Jacksonville, Florida, and operated 24 branches located throughout the southeast and south central United States.

{6} Defendant Head & Engquist Equipment, L.L.C. ("H & E") is a Louisiana corporation doing business in various states throughout the United States, including North Carolina, where one of its divisions, Hi-Lift ("Hi-Lift"), has a branch. Hi-Lift competes with Sunbelt in the AWP leasing business.

{7} Defendant Robert Hepler ("Hepler") is a citizen and resident of Florida and served as president of BPS and as a director and officer of Plant Services from 1992 until his employment ended on December 14, 1999. After leaving his position at BPS, Hepler was employed as president of H & E's Hi-Lift division. Hepler performs essentially the same duties and responsibilities as president of the Hi-Lift division as he did as president of BPS.

{8} Defendant Douglas Kline ("Kline") is a citizen and resident of Florida, and from 1992 until the end of his employment on December 14, 1999, Kline served as vice president of finance and chief financial officer of BPS. Kline joined the Hi-Lift division as its executive vice-president and chief financial officer as part of a package agreement he and Hepler made with H & E. Kline performs essentially the same duties and responsibilities for Hi-Lift as he did as chief financial officer for BPS.

{9} Defendant Michael Quinn ("Quinn") is a citizen and resident of Georgia. From 1989 until January 5, 2000, he was a member of the BPS senior management team, acting primarily as product manager for BPS and its predecessor companies. At one time he was branch manager of the BPS Atlanta branch. On January 5, 2000, Hi-Lift employed Quinn as its product manager and as vice president for its Eastern region. Quinn performs essentially the same duties and responsibilities for Hi-Lift as he performed for BPS.

{10} Defendant Gregg Christensen ("Christensen") is a citizen and resident of Texas. Christensen was director of operations at BPS's Western division from approximately 1992 until he left that position on January 14, 2000. He also was branch manager for the BPS Dallas branch until November 1999. After leaving BPS, Christensen became Hi-Lift's vice president for its Western division. Christensen performs essentially the same duties and responsibilities for Hi-Lift as he performed for BPS.

***2** {11} Defendant Brian W. Pearsall ("Pearsall") is a citizen and resident of Mecklenburg County, North Carolina. He was the branch manager for BPS in Charlotte, North Carolina until June 2000 and assumed the same position with Hi-Lift when he left BPS. He is Rob Hepler's brother-in-law.

{12} Rentokil Initial plc ("Rentokil") is a British company which obtained ownership of Plant Services in connection with a hostile takeover in approximately 1997. James Wilde ("Wilde") was the manager of Rentokil responsible for oversight of BPS after the Plant Services acquisition. Hepler and Kline reported to Wilde when Rentokil owned Plant Services and they were employed by BPS. Rentokil is not a party to this litigation.

The Equipment Rental Industry

{13} Before providing an overview of this case, it is helpful to outline the challenges and general practices in the equipment rental industry. This action is concerned principally with equipment rentals of aerial work platforms ("AWP"). AWP equipment consists of boom lifts, scissor lifts, push-around lifts (smaller non-motorized lifts) and reach forklifts. Boom and scissor lifts come in a wide range of models, sizes and functions; they are substantial pieces of equipment that cost thousands of dollars each and encompass a broad variety of devices designed to lift workmen off the ground to do work on jobs that otherwise would be very difficult to reach. Sometimes included within this class of equipment are "swing stages" and "mast climbers," equipment used to climb alongside buildings and other structures. Hi-Lift purports to operate exclusively in the AWP business.

{14} The business is highly specialized. If not delivered, handled or operated properly, AWP equipment can cause substantial injury and even death. Thus, the nature of the industry is such that its workmen and sales people must be highly trained in the mechanics, applications and operations of the equipment.

{15} The larger equipment rental companies typically purchase or lease equipment from a limited number of manufacturers. As of the fall of 1999, the two primary manufacturers of AWP equipment in the United States were JLG Industries (McConnellsburg, Pennsylvania) and Genie Industries (Redmond, Washington). JLG and Genie (and other secondary manufacturers) sell boom lifts, scissor lifts and other AWP equipment in certain standard sizes with various options such as two-wheel drive or four-wheel drive. Thus, the competitors in this industry offer, for all practical purposes, the same or very similar equipment to potential customers. As a result, prices tend to be set by the marketplace, and service and equipment availability have become significant factors affecting the success of the businesses in the area.

{16} AWP managers and salespeople know, from experience or simply by asking their customers, what type of equipment is needed by the different types of contractors for particular jobs. For example, electrical contractors will often use smaller scissor lifts or push-around lifts that can fit through interior doorways, while glass manufacturers working on the outside of buildings need taller boom lifts which can range up to 120 feet in height. Knowledge of the company's customer base contributes to higher utilization of equipment and better selection of the “fleet mix” for a particular market. Such information allows a business to invest in certain machines that yield better rates and profits. A new market entrant has a significant advantage if it has access to that information. With such information, a new entrant can maximize its initial fleet investment with little risk, perhaps saving millions of dollars, and can accurately project an operating budget.

***3** {17} The potential customers for AWP equipment are general construction contractors, subcontractors (such as electrical, glass and painting companies) and other industrial or commercial businesses that need equipment to work “in the air.” These customers are typically identified through numerous public sources-including the yellow pages, business directories and publications (such as Dodge Reports and PEC Reports that list various pending construction sites and related contractors)-and through on-jobsite trailers and direct contacts with contractors. It may be more difficult to determine which industrial customers are in the rental market, although the types of users-airlines, for example-are easy to determine.

{18} These public directories, reports and other sources not only provide the name of potential customers but also the customer's address, phone number and the name of the person to contact. The Dodge Reports and PEC Reports go further, providing detailed information about construction projects (Dodge) and industrial plants (PEC).

{19} Long-term rental contracts are rare. Companies typically rent for periods ranging from a day to a month, with weekly rentals being the most common. Even with longer term rentals, the customer is given the opportunity to return the equipment prior to the end of the rental period, paying only for the time rented.

{20} Rental companies primarily use outside sales representatives to sell and rent AWP equipment. These salesmen typically visit job sites or company offices to attempt to rent equipment. Customer rental decisions are made on varying factors, including price, the relationship between the customer and the sales person, availability of equipment on the customer's schedule, customer service, perceived dependability of the equipment and other considerations particular to the customer. Many customers do business with more than one company to maintain the flexibility and price competitiveness offered by having multiple sources of equipment.

{21} The personal relationship between the outside salesman and the customer is particularly important for success in this industry. Many salesmen have been calling on the same customers for many years and naturally develop close personal and/or professional relationships that increase the likelihood that the customer will rent from the salesman's company, other factors being equal. The hiring of salesmen from competitors to take advantage of these customer relationships is not unusual in the industry. It would be unusual, however, for an entire sales force to leave an office at the same time and go to the same competitor and unusual for the majority of salespeople in a number of offices to leave and go to work for the same competitor at the same time.

{22} Nothing in the history of the industry is indicative of mass departures of personnel from one branch to a competitor's branch. The departure of a number of core-positional people at various levels of the branch organization, at approximately the same time, to a competitor, has a major detrimental impact on a branch and can adversely affect the performance of the branch. Personnel changes usually occur as one- or two-person departures at a time.

***4** {23} In terms of price, historical prices have limited value. Prices are quoted and then negotiated between the outside sales representative and the customer or over the telephone with inside sales coordinators. While salesmen would like for prices to remain "confidential," they understand and expect that prices will become known in the market. Customers do not consider quoted prices to be confidential and often reveal price sheets and quoted prices of competitors to obtain more favorable terms. AWP rental companies occasionally quote good customers a fixed price for a job or period of time; these arrangements would constitute confidential information. "Sealed bids" or other formal bidding processes are rarely used. Recent consolidation in the industry has made pricing extremely competitive and has created several large competitors.

{24} Well-run companies in the equipment rental business study their markets and customers and gather various financial, sales and marketing information. This information includes average rental rates, construction information, fleet mix records, revenue per employee, utilization rates and other measures of operations. This information is shared with employees to improve their performance. It is not generally shared with competitors. Most of the information is based on a company's experience and is the type of information that employees would have some general knowledge about and retain. Such information takes some time to accumulate.

{25} Efforts to protect that information exists in the AWP rental industry include obtaining covenants not to compete, placing a general confidentiality policy statement in an employee handbook and limiting access to the information.

{26} The industry has grown considerably over the last five to seven years through "greenfield" startups-startup branches in a market where there has been no prior presence-and, more significantly, through consolidation. As part of the industry consolidation, larger companies have expanded by purchasing smaller companies rather than through greenfield operations. In these acquisitions, the tangible and intangible assets of a branch or multiple branches are acquired, including, importantly, the entire human resource components and goodwill of the company. Consolidation has caused competition to increase and margins to fall. In the year 2000, acquiring companies were paying multiples of five to seven times EBITDA for the acquired company or branch.

{27} The industry has historically been in short supply of trained, qualified branch managers, sales persons, mechanics, inside sales coordinators, drivers and other related positions. Businesses that are able to retain those personnel develop a considerable competitive advantage based on the investment those businesses make in the employees' training, experience and customer relationships.

{28} In a typical mature AWP business, the human resource component includes a branch manager, outside sales representatives, an inside sales coordinator, credit manager, service manager, branch administrator, mechanics (both inside as well as field mechanics) and drivers. In a typical greenfield situation, hiring all these personnel and achieving a satisfactory level of competent employees takes months. The employment of a number of experienced trained people for these positions within a short time frame (30 days or less) is atypical for this industry. In fact, such employment is inconsistent with normal marketplace employment activity.

***5** {29} In the industry, the most important business component is the branch office. Consequently, the branch manager position is one of critically important leadership in that this person is responsible for the total operation of each branch. He or she is also responsible for the development of confidential information about branch operations, its equipment fleet, its customers and employees and other related branch activities. Significantly, a branch manager must be sufficiently familiar with the branch's customers to be able to deal with customers upon the departure of a sales person and thus ensure continuity in the relationship between the branch and its customers.

{30} A branch manager has "very unique, very useful knowledge" of all personnel in the branch: competency levels, work ethics, salary/compensation, customer relationships and other personnel related matters. He or she is intimately involved in supervising a branch's sales force and in effect operates as a sales manager for each sales force. He or she must also supervise the service side of the branch, including the service manager, the mechanics and drivers.

{31} The individuals working for the branch manager-sales personnel, mechanics and other service related personnel-must act *interdependently* to deliver the equipment *and* service to customers. Sales personnel are the conduit through which businesses (branches) have relationships with customers. As stated by a customer called by defendant as a witness, sales personnel are the "face person" for the relationship with the customer. The service manager, mechanics and drivers all support the relationship with the customer by initial delivery of the equipment, training a customer in the operation of the equipment, regular maintenance of the equipment and prompt field repair of the equipment in the event of breakdowns. Service personnel have frequent and close contact with customers. The AWP business requires a high service component and the presence of a strong team effort.

{32} All AWP personnel undergo regular training. Sales personnel, for example, have to know the uses of the equipment and the most advantageous applications of it. Inside sales coordinators need to know equipment applications to provide appropriate advice to customers. The mechanics and service personnel have to be able to maintain and deliver the equipment to the satisfaction of customers, including OSHA-required familiarization.

Overview

{33} Before discussing the detailed Findings of Fact, a general overview of the core facts is helpful.

{34} Defendants Hepler and Kline were employed by BPS. They played significant roles in the creation of a successful business at BPS renting aerial work platforms to construction companies and industrial users both before and during the time it was owned by Rentokil. BPS had rental locations in several key markets in the Southeast, including Atlanta, Charlotte, Tampa-Fort Myers, Orlando, Dallas and Houston. When Rentokil decided to sell BPS in 1999, it did not consult with or inform Hepler and Kline of the decision and did not offer them any inducement to stay with the company through consummation of any sale. Neither had a contract that restricted his employment by a competitor.

***6** {35} Accordingly, Hepler and Kline devised a business plan that envisioned competing directly with BPS in its key branches in the Southeast. A successful AWP leasing business required two key ingredients: capital and the right people.

{36} At the heart of the plan was the conversion of the employee base of the targeted BPS branches and key BPS management in addition to Hepler and Kline. With the conversion of those key employees came all the information necessary to ramp up a greenfield operation more rapidly than would normally occur. The branch managers were thoroughly knowledgeable about the business of each branch, including the employee base, competition and pricing in the local market, the fleet mix, the customer base, and every other aspect of the local operation. The service employees were already trained and knew the equipment, customers, job sites and safety requirements. The salesmen knew the customers, the locations of current and upcoming jobs, and the prevailing market prices for the equipment to go on the jobs. The credit managers knew the credit history of the customer base. Each employee brought with him or her the knowledge of the systems, information and records necessary to the smooth functioning of an AWP rental operation. Concomitantly, the departure of each of those employees left BPS with a void, which impacted its ability to compete in the local market in the short term. Significantly, not one of the employees hired by H & E, including Hepler and Kline, had any form of contract containing a restrictive covenant or a covenant not to compete.

{37} Capital was required to purchase or lease the significant amounts of large and expensive equipment that constituted the lease products of the business and to fund other startup costs. H & E provided the capital and financial backing to bring the business plan to fruition. During the six-month period between their departure from BPS and the closing of its sale to Sunbelt, Hepler and Kline together with the other defendants successfully enticed significant numbers of the key management and skilled employees of the targeted branches to leave and join the new venture with H & E. That six-month period was one of extreme vulnerability for BPS, but a vulnerability of BPS's own creation.

{38} Three factors, discussed more fully below, have entered into the determination that defendants' actions-which when taken alone or in isolation might not have been outside the bounds of fair competition-when viewed collectively crossed over the boundary. First is the use of then BPS managers to accomplish the raid on BPS employees. Second is the magnitude of the raid. Third is the coordinated timing of the departures.

BPS and Its Operations

{39} Five companies acquired by Plant Services were consolidated into BPS in approximately 1993 to 1994. These included Hepler Hi-Lift, which Defendant Hepler founded, and four other companies: Able Equipment Company, Safe-

T-Green, Booms and Scissors, and Florida Contractor Rentals and Sales.

***7** {40} Defendant Kline was the chief financial officer for Safe-T-Green and in 1994 was moved to BPS headquarters in Jacksonville, Florida to become the chief financial officer for BPS, working directly under Hepler.

{41} Under Hepler and Kline, BPS had a senior management team which included: Doug Guy, director of Eastern operations; Christensen, director of Western operations; Jeff Stachowiak, director of marketing, sales and safety; John McGraw, director of scaffolding; and Mike Quinn, product manager.

{42} During Hepler's tenure as president, the senior management team met regularly, at least once per month. At its meetings, the senior management team discussed customers, mechanic availability, sales personnel, equipment utilization, safety, marketing, product mix, average rental rates, planning and other matters. Branches were regularly evaluated branch-by-branch. Senior management regularly shared BPS marketing, customer and internally developed information. This information included head counts, salary information, pricing, organizational structure, financial projections and forecasts, cost information, branch budgets and customer information, including the identity, contacts and requirements of its rental customers, pricing in effect for those customers and fleet utilization information by branch. Senior management knew that this information was confidential.

{43} Defendants Hepler and Kline managed the day-to-day affairs of BPS, made strategic decisions, developed and implemented budgets and hired and fired employees. Hepler was involved in all levels of the business. He frequently visited branches, discussed up and coming job sites and sales personnel and was actively involved with customers. Kline was involved in all aspects of the business as the result of his financial responsibilities. In particular, he was extensively involved with branch managers in budgeting. Hepler and Kline were highly compensated. Hepler was paid a salary of $260,000 in 1999, and Kline was paid a salary of $160,000 to manage 24 branch operations throughout the Southeast and South Central United States. They had access to and knowledge of BPS's confidential business information.

{44} Defendant Christensen, as Western regional manager for BPS, was closely involved in personnel issues, budgets, fleet mix and management of the branches for which he was responsible. He was directly involved in the BPS Texas branches and, in fact, managed the Dallas branch for several years. He had access to all of BPS's confidential business information related to his geographic area of responsibility.

{45} Defendant Quinn was involved in a variety of senior management issues, including budgets and, most importantly for him, fleet management. He was intimately involved with fleet utilization, equipment ordering, scheduling delivery dates, and equipment movement. Transferring equipment between branches facilitated utilization. He had access to and knowledge of BPS's confidential business information.

***8** {46} BPS placed special emphasis on its branches and branch managers. Among its most experienced branch managers at the end of 1999 were: Mark Alexander (“Alexander”) (9 years, 7 months) (Atlanta); Duke Drennan (“Drennan”) (18 years, 7 months) (Orlando); Beare Jones (“B.Jones”) (20 years, 5 months) (Tampa/Fort Myers); Abe Farrington (“Farrington”) (5 years, 3 months) (Dallas); David Hobbs (“Hobbs”) (4 years 3 months) (Charleston, South Carolina); and Defendant Pearsall (13 years) (Charlotte). These branch managers dominated their branches, recruited, hired, reviewed and fired employees, set salaries, trained and certified employees, set prices and rates for customers in their markets, developed confidential information for their respective markets, prepared budgets for their branches and carried out the multiple other business and leadership duties and responsibilities expected of a branch manager. The branch managers were in continuous contact with senior management.

{47} Branch managers regularly made presentations to their peers about their branch operations with emphasis on the keys to success they had found in operating their branches. For example, Alexander made a presentation to the BPS branch managers in June 1999, in which he emphasized:

> (a) the longevity and experience of his sales staff (“60 years of combined experience”);
>
> (b) the branch's interdependence of its personnel and its emphasis on team work; and
>
> (c) the Atlanta branch's success in retaining customers. (“WE DON'T LOSE CUSTOMERS.”)

{48} In order to protect its information, BPS implemented an employee handbook containing a section on confidential information. In fact, developing the handbook was the direct responsibility of Defendant Kline, who rewrote, in his own handwriting, that section of the handbook dealing not only with confidentiality but also with employee loyalty. Each BPS employee was required to acknowledge receipt of the handbook in writing. Virtually all of the BPS/Sunbelt employees who left to become employed by H & E signed such an acknowledgment. Hepler and Kline have both separately acknowledged the presence of trade secrets in this industry. Additionally, some defendants and many of their H & E employees also admitted that certain information is confidential and is not to be shared with competitors.

{49} BPS's business information was treated as confidential when discussed by senior management. Efforts were made to protect it at the branches. For example, the war rooms had the information taken down from the walls when outside people came in. Pricing was kept in special books. Branch managers (e.g.Pearsall) had specific rules about file removal from the branch office. Passwords were required and given to only certain personnel with respect to the BPS computer system. Salesmen's information was limited to customers for which they had responsibility. Only branch managers had access to information on all branch customers. Salary information was kept under lock and key at the branches.

***9** {50} Based on senior management discussions, the individual defendants were acutely aware that BPS lacked depth in a number of its human resource requirements. BPS senior management had frequently discussed that it did not have sufficient human resource reserves for its sales people. The individual defendants were acutely aware of the intense competitive pressures regarding qualified experienced mechanics and drivers and knew that those positions were in short supply in all of their markets. As a result, Defendants Hepler, Kline, Quinn, Christensen and H & E knew that the branches from which they successfully recruited BPS personnel *en masse* would be seriously harmed by those departures and that those branches would not have sufficient human resources to compete effectively with H & E until the departed employees could be replaced and trained.

{51} Over the years at BPS, the branch managers developed close personal and professional relationships with many of their long-time employees, who in turn formed close relationships among themselves; there are examples of shared family relationships as well, with fathers, wives, sons or brothers working in the same branch. These relationships often mirrored those more commonly found in a family-run business.

{52} Outside sales representatives usually reported directly to the branch manager, as did the inside sales coordinators. The inside sales coordinators were responsible for taking orders over the phone from customers, both those who had been solicited by the outside salesmen and others who called in to shop for prices over the telephone. The inside sales coordinators were also responsible for scheduling deliveries and dispatching drivers to deliver and pick up equipment which had been called “off rent.” Larger branches had service managers who reported to the branch manager. The service managers were responsible for supervising the mechanics (both shop mechanics and field mechanics), the parts department, the shop foreman and, to a limited extent, the drivers.

{53} The branch administrative personnel-i.e., the branch administrator, credit department employees and receptionist-also ultimately reported to the branch manager. Each of the branch employees served an important function at the branch and participated in training appropriate to his or her position. Training for mechanics was handled primarily through on-the-job experience and training classes provided by the manufacturers. The safety concerns surrounding use of the equipment made trained mechanics critical. Salesmen, to the extent they were not already experienced in the industry, were trained through experience and advice from the branch manager and fellow sales representatives. Drivers with no experience were trained through manufacturer classes, training videos and practice at the branch location. The process of training drivers typically took no more than two to three weeks.

{54} In addition to routine sales efforts, sales duties at the branch level consisted of assigning salesmen to territories, identifying target customers, creating “war rooms” to further identify ongoing and potential jobsite and customer opportunities, and discussing competitive pressures. Sales meetings among the sales representatives and the branch manager were sometimes held to discuss sales efforts throughout the branch.

***10** {55} Rental contract records were maintained both in the company's computer database and in “hard copy” files maintained at the branches. The rental contracts typically included the name, address and telephone number of the customer; the name and contact information of the customer who had rented the equipment; the price at which the equipment was being rented; the expected term of the rental;

and often directions to the job site where the equipment was to be used. Sometimes hand tickets were prepared which included varying amounts of the information found on the typical printed rental contract. The rental contracts were delivered to the job site with the equipment, and a contract copy was left with the customer.

{56} As of the end of 1999, BPS included the following among its southeastern and Texas branch locations: Atlanta, Tampa, Fort Myers, Orlando, Miami, Jacksonville, Charlotte, Raleigh, Charleston, Richmond, Dallas, Houston and Austin. BPS had additional branches in Arizona, California and Nevada. By virtue of his presidency at BPS and prior experience with his own business, Hepler had extensive knowledge of the AWP market in each of these cities.

{57} Hepler also had long-standing personal relationships with many of the BPS branch managers. As of January 2000, the branch manager of the Atlanta branch was Mark Alexander. Hepler had known Alexander, either as a competitor or as one of the BPS branch managers, since the early 1990's. They were personal friends in addition to their professional relationship. Alexander was also close to Quinn.

{58} The branch manager of the Tampa and Fort Myers, Florida branches as of January 2000 was Beare Jones (“Jones”). Hepler and Jones were extremely close friends. Jones has worked for either Hepler or Hepler's father in the equipment rental business for nearly forty years. At the age of seven or eight, Hepler, now 46 years old, began working in his father's business with Jones.

{59} The long-time BPS branch manager for Charlotte was Defendant Brian Pearsall. Pearsall is, as noted above, Hepler's brother-in-law. Hepler and Pearsall had worked together for over ten years as of January 2000.

{60} The BPS branch manager for Charleston, South Carolina in January 2000 was David Hobbs (“Hobbs”). Hobbs started as a BPS employee in the BPS Jacksonville office and developed a close relationship with Hepler as he was promoted through various positions at the Jacksonville branch and later to the position of branch manager in Charleston.

{61} The branch manager for the BPS Orlando branch at the beginning of 2000 was Duke Drennan (“Drennan”). While not as close personally to Drennan as he was to the other branch managers discussed above, Hepler had known and worked with Drennan for over ten years as of January 2000.

{62} Hepler also had close personal relationships with BPS employees below the branch manager level and frequently played golf with the salesmen.

***11** {63} In summary, Hepler and Kline were in an ideal position to recruit BPS employees to go to work with H & E. No BPS employee was restrained by a restrictive covenant.

{64} The announcement that Plant Services was for sale caused uncertainty and insecurity among the BPS employees. When it had previously attempted to sell Plant Services, Rentokil had purchased some protection against this vulnerability by contracting with Hepler and Kline to stay on through a transition with a new owner. In 1999 Rentokil elected not to purchase that same protection, leaving Hepler and Kline to go to work for a competitor at the time BPS would be most vulnerable. Rentokil was either unaware or unconcerned about the close relationship between Hepler and Kline and the branch managers.

{65} Insecurity among the BPS employees was understandable. The possibility existed that BPS would be purchased by a large competitor who would close branches and consolidate management practices. Four of the key managers who had guided the company to success had left abruptly and without explanation.

{66} Not until the problems posed by Hi-Lift were apparent did Sunbelt/BPS offer “loyalty contracts” to some of the BPS managers. Sunbelt's president, Bruce Dressel (“Dressel”), visited nine BPS branches and discussed with BPS branch managers Sunbelt's desire that they stay with BPS and work for Sunbelt. Drennan assured Dressel he was “on board” with the Sunbelt acquisition. Jones did not commit but gave no indication that he would not be staying. Defendant Pearsall accepted Sunbelt's invitation to attend Vendorfest.

{67} Rentokil elected not to spend any money to protect itself against loss of employees during the period of time BPS was for sale, despite the fact that its two key employees had left to join a company that would compete with BPS. That fact was clearly known to Sunbelt when it elected to purchase BPS. In fact, Dressel chided Wilde for his failure to keep Hepler and Kline on board during the transition.

H & E and Hi-Lift and Its Operations

{68} H & E has been in existence since the 1960's and built a reputation in the Gulf region in the crane and dirt movement business. At some point in the 1990's, H & E entered the rental business by acquiring a small fleet of equipment from Grove Manufacturing ("Grove"), another but smaller manufacturer of equipment. H & E was not very successful with its fleet. It apparently had a fleet of approximately 1,000 to 1,200 units spread across at least five locations, including Gonzales, Louisiana; Memphis, Tennessee; and Houston, Dallas and San Antonio, Texas. The fleet in Dallas was only about 250 units, and the fleet in Houston approximately 300 units. Engquist himself described H & E's fleet, which operated out of locations that also had the crane and dirt moving business intermixed, as a problem and "struggling." The Memphis and Gonzales branches, even though in "major markets," were later closed. The Court notes that, during the events of this litigation, H & E provided *no* evidence that it opened any branch under the Hi-Lift name in any location other than those in which BPS had an existing branch, and that it closed the Memphis and Gonzales AWP operations, two markets in which BPS had no presence.

***12** {69} While H & E had a minor AWP presence in Dallas, Houston and San Antonio, the evidence that the fleet was struggling suggests that H & E's efforts were not formed or based on any highly developed business information. Hi-Lift had no market presence and no market information of its own about Atlanta, Charlotte, Tampa/Fort Myers or Orlando. The Grove AWP equipment these branches used was not nearly as widely used as the Genie and JLG equipment. Thus, customers were more familiar with and wanted Genie and JLG equipment. Quinn was exceptionally knowledgeable with respect to the purchasing of that equipment.

{70} In mid-1999, H & E was purchased in part by an investment group, Bruckmann, Rosser and Sherrill ("BRS").[1] At about the same time, ICM (located in Salt Lake City) was also purchased by BRS, thus linking H & E and ICM. In fact, this common owner considered from the outset merging the two companies. The Court further notes that the boards of directors of ICM and H & E met jointly, and Gary Bagley ("Bagley"), C.E.O. and president of ICM, was a member of H & E's board of directors in part of 2000 and part of 2001. Further, Hepler testified that he and Kline spent a day in Jacksonville with Earl Rose, branch manager, conferring about business plans to open locations in the Northwest based on the Hi-Lift plan he and Bagley had been discussing.

{71} The broader picture for Hi-Lift and its investors is clear. H & E and ICM each had an AWP business that would benefit from the experienced management that Hepler, Kline, Quinn and Christensen could provide. When Hepler and Kline were hired, a plan was in place pursuant to which H & E would open AWP rental operations in Charlotte, Atlanta, Orlando and Tampa Bay-Fort Myers, and the former Grove-dominated AWP operations in Dallas and Houston would be converted to Genie and J & G equipment and run similar to the BPS branches in those locations. It is also apparent that there was at a minimum the likely prospect of some combination of the H & E and ICM AWP business so as to produce a company with coast-to-coast branches capable of competing with the largest players in the market. That likelihood has come to fruition with the merger of H & E and ICM and the creation of an AWP division encompassing the branches of both ICM and H & E.

{72} If carried out in a fair manner, it was a well-conceived and perfectly legitimate business plan. H & E had every right to compete with BPS Sunbelt in a fair manner, and, given the experience of its management and the capital resources of its financial backers, it would have been a formidable competitor under any circumstances. The Court does not find that the existence of such a plan was an unfair trade practice. The plan was a perfectly proper competitive strategy. The defendants were free to compete fairly with BPS in any market. BPS and its owners had the ability to provide some protection against that competition and elected not to pay the price to do so.

***13** {73} The implementation of the consolidation and expansion plan is where the activities occurred which give rise to liability in this action. In their testimony, defendants contended that no plan existed to raid BPS at specific locations and that the defections which occurred were unsolicited and unplanned. The Court, as finder of fact, does not find that testimony credible.

{74} Hi-Lift hired Hepler, Kline, Quinn and Christensen at salaries that were commensurate with the development of a large organization such as has been developed by Hi-Lift. Quinn provided the necessary purchasing expertise for such a large operation and expansion, and Christensen provided the West Coast management necessary since Hepler and Kline wanted to stay on the East Coast.

{75} Hepler and the branch managers testified that there were no prior discussions or solicitation of personnel. The Court finds that testimony is not credible and that those activities did take place. What *actually* happened is a clear indication that these activities occurred. In the cases of the Charlotte, Atlanta, Orlando, and Tampa-Fort Myers branches, a pattern of lining up salesmen and other key employees to leave at the same time is apparent.

{76} In each instance, the branch manager was offered compensation, including a signing bonus that was in excess of his or her BPS compensation or covered the bonus he or she would have gotten from BPS/Sunbelt for signing a loyalty contract. The branch manager then recruited the key or skilled employees (sometimes referred to as the “A Team”) needed to open quickly. These key employees included the most experienced outside sales people, the inside sales person, the service manager, experienced mechanics and drivers, and the administrative or credit manager. While the detailed information about the branches was useful, it was not necessary because the recruited employees brought all their knowledge and skills with them. Had H & E opened a greenfield office in one of the locations, many employees might have switched over in time. It is also possible that BPS could have made them counter offers from which they would have benefited and for which they would have stayed. That did not happen because of the wrongful conversion of employees by Hepler and the branch managers.

{77} The fact that there was no effort to fill these new positions outside BPS is a strong indicator that the branch managers knew who was lined up to leave. The ability of Hi-Lift to begin operations at a level and at a speed far in excess of those normally associated with a greenfield is indicative of the value these key, skilled, core employees brought with them.

{78} The fact that each of the new H & E locations at former BPS branches were opened before Sunbelt consummated its purchase of Plant Services is a clear indication that H & E rushed to open these branches while BPS was in the transition period and most vulnerable to a raid on its employees.[2] The timetable contributed to the need to use the branch managers as recruiters prior to the establishment of a Hi-Lift branch.

***14** {79} Most of the individual acts standing alone would not have risen to the level of unfair competition or an unfair trade practice. For example, if BPS salesman Ken Farris had voluntarily left BPS and gone to work for United Rentals in Atlanta, he could have called on his old customers, used his past knowledge and experience with respect to the type of equipment they used and even promised to meet or beat BPS prices, knowing full well the BPS price structure, including specific prices for particular customers on a known job site.

{80} Hepler and Kline were free to go to work for a competitor. In doing so, they were not restricted from directing the sales people of the new employer to call on customers whom Hepler and Kline knew to be former BPS customers or from using the knowledge and skills they gained while working in the industry.

{81} The critical issues arise from both the expansive nature and the cumulative effects of the H & E actions. In the context of an industry in which service may be the significant business determinant and trained employees are not plentiful, the consequences of a secret wholesale raid on a competitor's employees are clearly discernable in advance. The competitor's revenue is likely to be impacted by the inability to service customers in a normal businesslike manner.

{82} The Court finds that defendants used the BPS branch managers, while they were still employed by BPS, to recruit employees to leave BPS branches in a concerted and orchestrated manner, which had the dual effect of temporarily immobilizing the BPS branch and permitting Hi-Lift to fill the void so created to appropriate BPS's business to Hi-Lift, at least temporarily.

Hepler/Kline Decision to Leave BPS

{83} The past history of the first attempted sale of Plant Services is instructive. Plant Services had been put on the market for sale in 1998. During the process of that potential sale, Hepler and Kline were intimately involved in the preparations for sale. Pursuant to an agreement with Rentokil, Plant Services' parent, Hepler stood to make as much as four times his salary if the sale was completed-Kline, a lesser amount. As a result, Hepler and Kline did not consider departing BPS in 1998.

{84} As part of the process, Hepler and Kline made confidential presentations for Plant Services about BPS. One of those presentations was made to Bagley, a representative of ICM, a business in the Northwest that had some AWP operations.

{85} No sale was made in 1998, although Ripplewood/ICM was discussing offering $800 million for Plant Services.

{86} Rentokil decided in 1999 to put Plant Services back on the market; however, they handled the matter very poorly. In August 1999, Hepler and Kline learned of the proposed sale before they were informed of it by Rentokil management. Hepler and Kline reacted negatively to the proposed sale of BPS. In fact, Hepler described himself as being quite angry about the sale. Their reaction was understandable, given the 1998 arrangement and the contribution they made to BPS and the way they found out about the sale.

***15** {87} After learning of the proposed sale of Plant Services, Hepler and Kline communicated with each other about their dissatisfaction and their intention to leave BPS. However, they did not communicate their displeasure and desire to leave to their superiors at Rentokil.

{88} Hepler worked out a potential consultancy with Genie Industries, one of the principal suppliers of equipment to BPS. Kline had no such prospects, and only had an interview lined up which did not get past a video interview. Hepler apparently made inquiry of Genie during this time as to whether it would support a new venture put together by Hepler and Kline.

{89} According to Hepler, he received a call from a potential investor named Bob Williams ("Williams") in August 1999, in response to which he and Kline developed a very specific business plan for Aerial Equipment Specialists (the "AES Plan"). This business plan:

(a) Stated that the management of BPS was committed to the plan:

> "The majority of the management team is committed to AES.... The five senior managers (CEO, CFO, Director of Operations, Product Director and Director of Marketing) have worked together as a team for over six years...."

(b) Stated that specific fleet mixes for the specifically identified markets:

> "We have developed a fleet mix for each of the proposed branches, which will coincide with the needs of the local rental market.... The equipment mix, as well as the option list, was formulated by experience in each of these markets to maximize utilization."

(c) Emphasized customer targeting as BPS had done in the past:

> "[W]e target ... those customers for the following reasons:
>
> • [T]hey ... understand the added value concept of providing exactly what the customer needs.
>
> • [T]hey are more responsible and less abusive to our products.
>
> • These customers tend to be established and will pay for services rendered promptly...."

(d) Identified seven geographical locations where the company would do business;

(e) Specified employee compensation and other equipment formulae for the branches;

(f) Set forth specific operating ratios (e.g. AWP's per delivery driver, sales person and mechanic);

(g) Made projections and forecasts for each location; and

(h) Included average monthly rental rates for each of the seven branches cited, which were then used to develop the rental revenue in the financial model.

{90} The branch locations, employee compensation and other aspects of the AES Plan are strikingly similar to the plan defendants actually implemented at H & E. The Court concludes that Kline must have used BPS information in formulating the AES plan. The information in the AES Plan was accessible to Kline from BPS information. It is not information that anyone could carry in his head. For instance, the average monthly rental rates set forth for each market and for each product group in the AES Plan are different, and as the AES Plan itself states, "[were] formulated by experience in each of these markets to maximize utilization." More specifically, there are 20 products listed (12 booms and 8 scissors) and 7 markets; in other words, 140 different individualized average rental rates were quoted in the AES

Plan. Thus, inclusion of such information in the AES Plan manifests defendants' intentions, from at least August 1999, to take advantage of information developed by BPS. Kline admitted that at the time the AES Plan was prepared, he had access to average rental rates for the BPS branches in Atlanta, Charlotte, Orlando, Dallas, Houston and Tampa, and that gross margins were based upon his experience at BPS. However, given the commodity nature of the equipment and the highly competitive market, it was probably not difficult to project margins.

***16** {91} In testifying at trial about the AES Plan, Hepler gave very contradictory testimony. On one day, he testified he knew nothing about the information contained under operating ratios, contending that Kline alone had put together that information. The next day, however, Hepler testified that he did know about those ratios and that they were just generic.

{92} After the development of the AES Plan, Hepler and Kline sent the plan to Williams and made presentations of it to at least two other investors, one involving a trip to South Bend, Indiana. In those presentations, Hepler and Kline did not qualify the specific declarative representations contained in the plan.

{93} At least as early as October 19, 1999, Defendants Hepler and Kline began consulting with attorneys about their activities. Hepler and Kline gave their attorneys earlier employment agreements for review. On October 25, 1999, they submitted the BPS Employee Handbook and the AES Plan for review. They specifically conferred with their attorneys regarding “potential litigation issues.”

{94} According to Hepler, he and Kline had decided to resign from BPS on the evening of November 10th in Houston. Because this dinner with James Wilde was canceled, however, they did not resign.

{95} According to Hepler, sometime before November 11, 1999, he received a call from Gary Bagley at ICM inquiring about his status. Bagley was aware that Plant Services was again for sale, but ICM was not approaching Plant Services. As a result of this and follow-up calls, Hepler arranged to meet Bagley in Dallas, Texas on November 11, 1999, after having a budget meeting in Houston with Hepler's BPS superiors on November 10, 1999. Bruckmann and Bagley traveled to this meeting from California and Utah, respectively, to meet Hepler. Conversations between Bagley and Hepler indicate that there would be no need for ICM to bid for Plant Services. By hiring Helper and Kline, ICM would be able to benefit from their implementation of the AES Plan at much less cost than an acquisition of Plant Services.

{96} Bruce Bruckmann, whose investment group owned H & E, attended the November 11, 1999 meeting between Hepler and Bagley in Dallas. Kline was not present. Defendants characterized the meeting as an “employment interview.” Hepler testified at his deposition that, even though he had not discussed the proposition with Kline, he told Bagley and Bruckmann that he was not interested in a position unless Kline was also offered a position. Hepler and Kline had consulted their attorney about the interview in advance of it.

{97} Immediately after the November 11, 1999 Dallas meeting, Defendants Hepler and Kline *both* called James Wilde, chairman and president of Plant Services and regional managing director of Rentokil, to resign from BPS. Defendants said nothing about their competitive plans and activities. Wilde would not accept their resignations without meeting with them. Defendants Hepler and Kline, without Wilde's knowledge, proceeded to tell other BPS senior management that they intended to leave.

***17** {98} Shortly after the November 11, 1999 meeting with Bagley and Bruckmann, Hepler began a series of telephone calls with Bagley. These telephone calls led to a meeting in Dallas on November 23, 1999, attended by Hepler, Kline, Bruckmann, Bagley, Hal Rosser of Bruckmann Rosser, and others. The meeting took place at the Admiral Club at the Dallas Airport. Engquist met Helper and Kline for the first time at this meeting. After approximately two hours of discussion, Hepler and Kline were offered employment at H & E at salaries of $300,000 and $200,000, respectively. These salaries were more in line with salaries for managing a nationwide AWP operation, not just H & E's AWP operation.

{99} Engquist testified that he hired Hepler and Kline in order to address problems with H & E's fleet, which consisted of Grove equipment. Thus, Hepler and Kline were offered a $500,000 compensation package, an amount greater than their BPS compensation, to take over an aging fleet that was approximately a tenth the size of the BPS fleet.

{100} Significantly, Engquist was concerned about the availability of personnel in the business and at this meeting specifically “questioned” whether Hepler and Kline would be able to obtain the “right people” to grow the business. Hepler responded that he was confident that he could. Hepler and Kline's disproportionate compensation for the H & E fleet, Engquist's statements regarding the "right people," Bruckmann's repeated involvement in meeting with Hepler and the large contingency of personnel in attendance at the November 23 meeting in Dallas, the AES Plan and the subsequent hiring of Quinn and Christensen at salaries in excess of $100,000 each confirm that defendants intended to expand H & E with BPS personnel, and on a scope with the AES plan. Engquist remained involved in the decision-making process that led to the hiring of Christensen, Quinn, Alexander and Hobbs and signed off on the employment of numerous other BPS employees, including Abe Farrington, Beare Jones, Duke Drennan, Brian Pearsall, Steve Mathews, Ken Moon and Dan Franz.

{101} Hepler and Kline did not accept the job offers on the spot, contending that they had agreed to meet in person with Wilde before anything happened on their resignations. Eight days later, on December 1, 1999, when James Wilde was again in the United States in Jacksonville, they officially resigned and at Wilde's request submitted written resignations. Wilde asked Hepler and Kline to stay on to sell BPS, or stay at least for a longer notice period. Hepler and Kline, after conferring with Engquist, refused. They gave BPS only two weeks' notice. A public announcement was made of their resignations on December 1, 1999.

{102} During the notice period, Hepler and Kline had several discussions with their attorneys. On December 14, 1999, before flying to Baton Rouge that night to begin their employment at Hi-Lift, they consulted with their attorney about litigation risks, solicitation of BPS employees, and consultations with H & E concerning the same. Defendant Kline testified in his deposition that on December 15th, after discussion of BPS solicitation of employees came up, Hepler and Kline and Engquist had a conversation with H & E's attorney, Ashley Moore.

***18** {103} Hepler and Kline both have testified in deposition and Hepler at trial about going to Baton Rouge on December 15th. On the afternoon of December 15, 1999, Engquist suggested that they fly to Dallas the next day to review the H & E AWP fleet at Martin Equipment. After that suggestion, according to Engquist, Hepler and Kline began conversations with Engquist about the employment of Defendants Quinn and Christensen.

{104} As described by both Hepler and Kline in deposition, and by Hepler at trial, Hepler and Kline raised the issue of employment of Quinn and Christensen with Engquist because they needed Quinn to "manage the fleet" and Christensen to manage the western operations, particularly the branches in Texas for H & E where Christensen had worked for BPS. They further testified that on December 15th they discussed compensation in excess of $100,000 each for Christensen and Quinn and that Engquist was agreeable to that compensation. In their testimony, they suggested that Engquist meet Quinn and Christensen in Dallas the next day before making any final decision.

{105} Hepler testified that he had had no contact with Christensen and Quinn about getting together in Dallas until after the December 15th discussion with Engquist. In this, Kline's deposition testimony and Hepler's trial testimony directly conflict with the testimony of their co-defendant, Quinn. Quinn testified in his deposition that when he was first contacted by telephone by Hepler to tell him that Hepler was *going to* work for H & E, Hepler wanted to talk to him about employment at H & E, and would be contacting him again. Quinn further testified that shortly thereafter he received another call from Hepler setting up a meeting in Dallas "within the next *week or so.*" Quinn's travel itinerary shows that on December 9th he had already booked a flight from Florida to Dallas arriving in the Dallas airport at 2:30 p.m. December 16th. This timing supports Quinn's testimony that the Dallas meeting was arranged several days in advance. Further evidence that Quinn was conspiring with Hepler is found in Quinn's testimony that he accepted employment with H & E without a specific compensation offer even though Quinn expressed doubts about Hi-Lift.

{106} Defendants did not present Defendant Quinn for testimony at trial. Nor did they call Defendant Pearsall, Drennan, Jones, Shelly Parnell, or others whose deposition testimony contradicted Hepler, Kline or Engquist.

{107} Immediately upon Hepler's return from Christmas vacation, he proceeded to recruit additional BPS employees.

{108} Hepler and Quinn traveled to Atlanta on January 6, 2000 to meet with Alexander; Alexander was the Atlanta branch manager, BPS's largest branch and among its most successful. Notwithstanding Hepler's testimony that H & E had no definite plan at this time to open in Atlanta, Hepler and Quinn sought assurances that Alexander would be "available when it came time to leave." Hepler's testimony about this meeting is not credible.

***19** {109} The very next day, Hepler and Quinn had breakfast with Gary Maner, BPS's national service manager. At that time, they offered him employment to head up the rebuild facility for H & E, the same initiative that BPS was supposed to have achieved as a strategic initiative in 1999. This is another example of Hepler and Quinn's use of knowledge of BPS's business plan for the immediate benefit of Hi-Lift.

{110} On January 9, 2000, Hepler, Kline and Quinn flew to Seattle, Washington to meet with Genie Industries, the major supplier of AWP equipment and according to the AES Plan the "preferred supplier." According to Hepler and Engquist, who later joined the other defendants, the purpose of this meeting was to become acquainted with Genie, with whom H & E had nothing but a casual business relationship at that time. According to Hepler, H & E was able to convince Genie that it was a sufficient size player to obtain very favorable pricing and terms on equipment. Even though it was only three days after his Atlanta recruiting efforts, Hepler testified that an Atlanta branch was not discussed as a real possibility at that point with Genie. Engquist, however, testified that they had committed to Genie that Hi-Lift would open a branch in Atlanta. For this reason and other reasons, the Court again finds Hepler's testimony not to be credible.

{111} Thereafter, H & E set about communicating with JLG, another major AWP equipment manufacturer, about orders to be placed with JLG. Hepler testified that with respect to both entities, they were able to achieve contracts that would allow them to move equipment around freely, cancel and substitute orders and do other things that minimized the financial risks of purchase orders to either manufacturer. There were serious discrepancies between Hepler's testimony and the contracts themselves.

{112} Based on the quantity of equipment ordered by Quinn on behalf of H & E, substantial thought had to go into the ordering of the right kind of units. Utilization reports constitute a substantial competitive advantage and are based on knowledge of different marketplaces and their respective needs. A review of plaintiff's exhibit 522 shows that an Atlanta fleet does not fit Charlotte and a Charlotte fleet does not fit Atlanta. For example, Charlotte has 3 times (19) more 90-foot booms than Atlanta (6). Thus, the Court concludes that this type of information about fleet mix is a significant competitive advantage and gives a competitor an advantage if it knows the requirements of specific markets in general and specific customers in particular. Accordingly, allocation of dollars to purchases of specific equipment is indeed critical. The immediate, high utilization rates and profits achieved by H & E as its branches opened confirm that H & E used confidential information from BPS to establish and set up their fleets in each of the markets in which it opened, just as Defendants Hepler and Kline stated in the AES plan and as Quinn and Christensen did every day for BPS.

***20** {113} Examples of the Court's concern with respect to credibility include, but are not limited to, the following examples:

> (a) Hepler specifically testified that at the January 6, 2000 dinner in Atlanta he did not solicit or recruit the BPS personnel present for H & E. He is flatly contradicted by Quinn on several points, including the following:
>
> > Q: Did Mr. Hepler tell each of these gentlemen [Messrs. Alexander, Leavell, Cornett, Franz and Brown] that he would like to employ them in his new venture?
> >
> > A: I don't know that it was told specifically to each on individually. I don't recall *how he worded it other than he would like to have all of them with this to be part of this new venture.* (Emphasis added.)

(b) Engquist testified:

> Q. Mr. Engquist, in your experience, how quickly could JLG deliver equipment to the H & E branch?
>
> ...
>
> Q. For example if you ordered something on Thursday when would it get there?
>
> A. It would probably get there *Monday, Tuesday.* They had availability of equipment.

Defendants' order log sets forth the order date and the receipt date for all of H & E's AWP equipment orders to JLG and Genie. A casual review shows that occasionally each manufacturer did deliver on a few days' notice. However, a more thorough review reveals that Engquist grossly exaggerated delivery times. The average time from order date to actual receipt based on Defendant H & E's *own* documents shows that the *average delivery time* of Genie was 28.9 days and JLG 44.5 days-vastly different than "Thursday" to "Monday or Tuesday." Additionally, H & E's initial orders for Atlanta, for the period from February 25 through April 15, 2000, totaled 467 units comprised of over 30 different product models (including options)-a very large order, apparently intended for more branches than just Atlanta. Approximately 1650 rental items were ordered as reflected by the log, comprised of approximately 58 different JLG models and 42 different Genie models (including options). The two most popular such models appear to be models 1932E2 (208 were ordered) and 2032E2 (121 were ordered). These models' popularity suggests that they are staples in a fleet, yet their average delivery times were each 54 days from the date of order. These delivery times, based on H & E's order log, confirm the testimony of Guy Ramsey, the industry expert, on lead times.

> (c) Hepler's expense reports concerning the February 22, 2000 breakfast in Fort Myers directly contradict his testimony about soliciting salesmen with Jones.

{114} The defendants used their knowledge of BPS information in the hiring and recruitment of personnel. In virtually all cases, employees hired from BPS by H & E occurred after salary increases were offered. Hepler, Kline, Quinn, Christensen and Pearsall used their knowledge of the skills, training, experiences and relationships of BPS employees in selecting and hiring those employees.

{115} BPS's accumulated confidential information concerning its average rental rates, average rental rates per type of equipment, utilization reports per type of equipment, salary information, employee revenue by headcount and similar information had significant value to BPS was developed over several years, was not readily available in the marketplace and could not be easily obtained through legitimate means without great cost. Defendants used their knowledge of that BPS information in the Hi-Lift business plan.

The H & E Branches

***21** {116} The Court will now review each H & E branch in the order that evidence was presented. The Court finds that the evidence confirms a common pattern in H & E's opening of a number of the branches that had known intentional adverse consequences on the corresponding BPS branch. The pattern can be summarized as follows:

(a) Hepler, Kline and Engquist decide to open a branch in a particular market.

(b) Hepler, using his past relationship with, and knowledge of, BPS's branch managers, and with the assistance of Quinn and/or Christensen, recruits the BPS branch managers.

(c) Hepler, with Engquist's approval, employs the BPS branch manager and directs that he recruit and employ on behalf of H & E the best BPS personnel from his branch.

(d) The BPS branch manager, using his prior relationship and knowledge of BPS employees' skills, salary, relationships and training, recruits selected BPS employees to come to work for H & E. The branch manager first recruits the branch's top sales personnel and service manager, and may recruit mechanics and drivers, although, this is usually done by the recruited service manager. Based upon the timing and nature of the departures, the Court finds that many of the employees were recruited by branch managers while the branch managers were still employed by BPS.

(e) Hepler, either meets directly, or communicates by telephone, with many of those BPS employees in the recruiting process, especially the salesmen.

(f) The branch manager, sales personnel, service manager and some of the branch personnel all leave at about the same time to open an H & E branch in the same geographical area, with little or no notice to BPS. Shortly thereafter, the departing BPS employees are followed by other recruited mechanics, drivers and other personnel.

(g) The H & E branch opens based on financial and fleet information put together by Kline, Quinn and Christensen and has immediate business. The financial and fleet information is based on confidential information gained during their employment with BPS.

(h) On behalf of H & E, the sales representatives are immediately in the market and soliciting customers, but do not have H & E pricing information or H & E promotional materials. Notwithstanding that, they are able to secure significant numbers of rental contracts for H & E immediately.

(i) The BPS branch is left in a weakened state. The branch does not have sufficient trained, knowledgeable human resources to respond to H & E's competition, address relationships with customers, or perform the routine service necessary to support the branches relationships with its customers. BPS is required to rush other personnel resources to the branches to react to the emergency.

{117} Based on this pattern, and as will be shown more explicitly in the following findings for each branch, the Court makes these summary findings:

(a) Hepler's testimony as to the circumstances of his meetings and communications with BPS personnel are contradicted by the recruited employees' testimony, further discrediting Hepler's credibility. Hepler is not a credible witness.

***22** (b) The fact that each new branch had "80%" utilization within weeks of opening is circumstantial evidence that H & E used BPS's confidential information to tailor its branches' rental fleets without spending the necessary time, money and effort to develop the information itself. The utilization rate is also circumstantial evidence that a higher percentage of the BPS customer base was converted to H & E in the short term.

(c) In view of the circumstances of this pattern, the Court finds, in the short term, that were it not for H & E's interference with BPS employer relationships, and subsequent solicitation of BPS customers, those customers would have continued doing business with Sunbelt, or, at least, that Sunbelt would have been able to fairly compete for those customers' business, an opportunity they were not afforded after H & E's orchestrated conversion of BPS employees, customers and information.

(d) BPS, under Hepler and Kline, had built very strong customer relations at the branch level. It would have been natural for those customers to continue doing business with BPS, subject to normal competitive pressures. A new start-up such as H & E could have been expected to take some customers or some business of some customers over time. The mass exodus of key sales employees in each branch with intimate knowledge of the BPS customer base permitted H & E to effectively solicit the business of that customer base while BPS was trying to rebuild its sales force. Organized defection of service people, mechanics, drivers, inside sales reps and credit manager adversely impacted BPS's ability to service its existing customers, thereby facilitating the conversion of their short term business by H & E. The loss of each branch manager left the branch leaderless and adversely impacted the branch's ability to recover from the other defections. The combined departure of the key employees both took from BPS and transferred to H & E a vast amount of collective knowledge about the business and customers of the branch. That combination gave H & E a competitive advantage it would not have possessed without the organized and orchestrated defections.

Charlotte

{118} The Charlotte Hi-Lift branch opened on or before June 5, 2000, with the following staff from BPS: a branch manager (Brian Pearsall); an inside sales coordinator (William Huntley); a service manager (Pat Muldoon); a branch administrator (Michele Dougherty); a sales representative (Ken Farris); and a driver (Frank Evans). Within a week the H & E Charlotte branch added a BPS master mechanic (Lennie Merrington). Each of these employees came from BPS.

{119} Although the possibility of a Charlotte greenfield was part of the original AES Plan and was discussed at the H & E board meeting on February 10, 2000, and although a pro-forma was drawn up for Charlotte by May 9, 2000 and Pearsall was Hepler's brother-in-law, the defendants claim that there was no plan to open the Charlotte branch in 2000 until a "chain of events" took place in late May 2000 with Pearsall wanting to leave BPS. Defendants' position is not credible. Although defendants made plans as early as May to open a Charlotte branch, it was the last branch opened. Clearly, defendants felt they could rely on Pearsall to convert himself and other employees to H & E. It was obviously completed in a rush so that it was done before Sunbelt took over and had an opportunity to create a relationship with the employees.

***23** {120} Defendants' documents and their own witness show that:

(a) Engquist testified that a decision to open was made by May 9, 2000, because a branch manager, specifically Brian Pearsall, was available;

(b) Delores Kline, a real estate agent and the wife of Doug Kline, flew to Greensboro, North Carolina on May 9, 2000 (coincidentally the same day Engquist, Hepler and Doug Kline were in Atlanta discussing the Charlotte pro forma), and spent May 9-11, 2000 in Charlotte looking for a site for the H & E Charlotte branch;

(c) Delores Kline's notes indicate she was looking for licensing reciprocity in North Carolina in October or November 1999;

(d) Engquist signed the certificate to do business in North Carolina on February 25, 2000;

(e) Hepler discussed opening in Charlotte with Earl Rose on April 17, 2000; and

(f) 159 pieces of AWP equipment, ordered as early as May 22, 2000, arrived in Charlotte between June 6, 2000 and the end of June 2000.

{121} Meanwhile, Pearsall, Hepler's brother-in-law and BPS's Charlotte branch manager, denied in his deposition knowing about the plan to open an H & E branch in Charlotte until Saturday or Sunday, May 27-28, 2000. Hepler claimed in his deposition that Pearsall called him at home after Pearsall had a discussion with Bruce Dressel at Sunbelt's Vendorfest, which was held over Memorial Day weekend in May 2000, and that this call, which occurred on either May 27 or 28, 2000, was the beginning of the chain of events which led to the opening of H & E's Charlotte branch-eight days later with a facility and a full staff.

{122} Pearsall, although a resident of Charlotte, did not testify at trial and was present in Court several days. In his deposition, he stated that he called Hepler and "told him that I wasn't going to, I couldn't work for Sunbelt and at that time he [Hepler] asked me if I could, if I wanted to work with, with H & E." Hepler, on the other hand, testified at trial that Pearsall called Hepler "and said could you hire me? I would like to come to work for you."

{123} In fact, Pearsall and Hepler had been in regular communication from as early as January 14, 2000. Between January 14, 2000 and March 18, 2000, Hepler called Pearsall at least eight times, including three phone calls Hepler made to the BPS Charlotte office totaling approximately 37 minutes. In view of the events occurring by May 9, it is highly improbable that Hepler and Pearsall had no discussion of a Charlotte branch before May 27 or 28.

{124} The Court does not find the testimony, by deposition, or in person, of either Hepler or Pearsall to be credible when taken in light of the totality of the evidence. Moreover, Pearsall's failure to testify calls into question his ability to rebut the testimony of several Charlotte branch witnesses about his statements and activities.

{125} Pearsall turned in an oral resignation on May 30, 2000 and a written resignation on May 31, 2000. Pearsall said he talked to Hepler again on the night of May 30, 2000, but not again until at least June 5, 2000. In his written resignation, Pearsall agreed to work a two-week notice.

***24** {126} As part of, or in lieu of, that notice, Pearsall agreed to help manage the inventory of the Charlotte branch, which was to be conducted in conjunction with the acquisition of BPS by Sunbelt, during the week and weekend, following Memorial Day. Traditionally, James "Rocky" Busic was in charge of the inventory for the scaffolding side of the Charlotte branch. Although the May 2000 inventory was not a regularly scheduled inventory and Busic had scheduled vacation during that time, Busic approached Pearsall and asked to reschedule his vacation for the July 4, 2000 weekend so that he could participate in the inventory. Pearsall insisted that Busic take his scheduled vacation and said to Busic "[W]hy do you care about this inventory? They [Sunbelt] don't care anything about you."

{127} At Pearsall's insistence Busic took his vacation, only to return 8 days later on June 5, 2000, to find the branch in a state of "chaotic disorder." Pearsall did not help with the inventory as promised and left inexperienced BPS employees to do the inventory. Busic was forced to re-do the inventory a few months later, spending three days rather than the usual four hours doing the inventory because it had not been done accurately in May 2000.

{128} Pearsall also incited the BPS employees, apparently in an effort to rally them to the H & E side, or any side other than BPS, by repeatedly disparaging Sunbelt to other BPS employees. Pearsall told BPS employees, while he was still employed at BPS, that Sunbelt "was not a company you want to work for," were "dirt bags," "didn't have a good reputation about their people," that the BPS employees might "want to find another job," that the branch would be run into the ground within "30 to 60 days," and that Sunbelt "was buying all the assets [of BPS] and not necessarily the people."

{129} Defendants hired at least five BPS/Sunbelt employees for the H & E branch in Charlotte immediately before the date of Sunbelt's acquisition; they solicited and tried to hire several more. Pearsall directed many of the "key" Charlotte BPS employees to leave BPS immediately. While still a BPS branch manager and on site at the BPS Charlotte branch, Pearsall offered jobs at H & E to two salesmen

(Farris and Huntley), the service manager (Muldoon) and the branch administrator (Dougherty), all of whom claim to have accepted on the spot, and three of whom Pearsall immediately sent to work for H & E. Engquist and Hepler testified that this very conduct would be improper.

{130} Farris and Muldoon, the top salesman of the entire BPS organization and the Charlotte branch manager respectively, turned in their resignations on May 30, 2000. Pearsall directed Farris to leave the same day he resigned. He told Muldoon to leave on the morning of June 1, 2000, prior to Muldoon working a two-week notice and the same day Sunbelt acquired BPS.

{131} Likewise, although Huntley's resignation letter offered a notice period, Huntley never returned to BPS after May 31, 2000. Instead, he showed up for work at H & E on June 5, 2000, and immediately began calling on BPS customers. Pearsall testified in his deposition that he told Huntley to make a clean break and leave immediately a discussion Engquist admitted was improper, particularly for a manager who was also departing for the same competition.

***25** {132} Bruce Funderburgh was approached by Pearsall approximately 2 to 2½ weeks prior to the acquisition of BPS by Sunbelt. This solicitation was well before Pearsall claims to have called Hepler regarding a job at H & E (on May 27 or 28, 2000), and in fact coincides more logically with Ms. Kline's visit to Charlotte to secure a location for the Charlotte H & E branch in early May 2000. In that conversation, Pearsall told Funderburgh that he was going to start a new H & E branch and that several other BPS employees, including Muldoon, Dougherty, Frank Evans, and Ken Farris, would be going with Pearsall to H & E. The Court finds Mr. Funderburgh's testimony to be credible.

{133} At trial and in his deposition, Hepler testified that he had no discussion with Pearsall about hiring any other BPS employees until Pearsall worked out his notice and came on board with H & E, despite the fact that Pearsall did not come on board with H & E until at least June 5, 2000. By that time, at least four other BPS employees had been recruited and put to work as H & E employees by Pearsall and Hepler.

{134} The Court finds that, contrary to his testimony, Hepler knew of and was involved with Pearsall's recruitment of BPS employees. Hepler spoke to Farris on the day Farris resigned and was fully aware that Pearsall was recruiting BPS employees at that time, which was long before Pearsall left BPS on June 5, 2000. Specifically, the Court finds that on May 30, 2000, after instructing Farris to leave BPS immediately, Pearsall instructed him to call Hepler. Furthermore, Farris spoke to Hepler in Jacksonville at that time for the purpose of organizing the start up of the Charlotte branch six days later.

{135} Further undermining Hepler and Pearsall's testimony concerning the timing of the opening of the Charlotte H & E branch and their recruitment efforts, Patrick Muldoon, the BPS service manager for Charlotte, was also involved in helping to solicit employees for H & E long before he left BPS. Muldoon solicited Rick Bailey, the BPS shop foreman at the time, well before the end of May 2000:

> Q: “You had been talking about H & E moving into the area with Mr. Bailey over a period of weeks prior to the time you left, hadn't you?”
>
> A: “It may have been weeks because we knew about H & E coming to the area opening branches. It may have been weeks before that, yes.”

{136} Muldoon told Bailey that Pearsall and several others would be starting a new H & E branch in Charlotte and that it was going to be a smaller operation but that “basically, everything would stay the same ... [that they] would be doing the same thing in a different place.” Muldoon also suggested that Bailey go look at the H & E branch a week or so before he left.

{137} Muldoon also solicited Lennie Merrington, a master mechanic, on behalf of H & E. Merrington came to work at H & E on June 9, 2000, despite the fact that his official termination date from BPS was not until June 19, 2000.

***26** {138} Later, Muldoon, on his last day of work at BPS, solicited Ron Chambers, a road mechanic who worked on customer owned machines, to come and work at H & E. Muldoon asked Chambers for his phone number and told him that they were “going to try and keep ... the A Team together.” Muldoon subsequently called Chambers at home, offered him a position at H & E, and told him that they were going to pick up two service trucks for the Charlotte H & E branch.

{139} Pearsall also, either directly or indirectly, solicited the employment of BPS road mechanics Milton Turner and Ron Chambers, and shop mechanics Reggie Gill and Bill Mann.

{140} Plaintiff called a number of Sunbelt BPS employees who testified, and demonstrated by the fact that they stayed on and gave Sunbelt an opportunity to compete for their talents, that the timing of the recruitment had significance.

{141} All in all, when the smoke from Pearsall's departure had cleared, at least nine of the BPS employees had left and gone to H & E before the first week of Sunbelt's ownership of BPS was over. If Pearsall had been successful in employing each of the employees he solicited or who were solicited on his behalf, the AWP side of the Charlotte BPS branch would have lost more than 15 employees.

{142} The Court finds that Pearsall used his position and influence over the employees of BPS and his knowledge as to their skills, salary and training to sow the seeds of fear and doubt with respect to Sunbelt and use that fear and doubt to solicit them for the new H & E branch and interfere with their relationships with BPS and Sunbelt. The Court further finds that without Pearsall's disparagement of Sunbelt and his insistence that the employees leave immediately, before Sunbelt could come in and fairly compete and bargain for their continued employment, some, if not all, of the employees who left for H & E would have remained in the employ of Sunbelt, at least for a sufficient period of time for Sunbelt to compete for their employment on a level playing field or assist in training their replacements. Their continued presence would have eliminated many customer problems.

{143} Further, without his “inside” position with respect to the employees, the Court doubts that Pearsall would have been able, particularly without any increase in salary, and in the guise of a “lateral” move, to convince so many long-term employees to leave BPS.

{144} The impact of the departure of these employees on the Charlotte branch was significant, as the remaining employees were required to take on additional responsibilities and work long hours to try to compensate for the departures. The branch was unable to get equipment out to customers on a timely basis because of the lack of trained personnel, including mechanics and drivers; equipment out on rent sat for prolonged periods after it was off rent because of the lack of availability of truck drivers to pick up the equipment.

***27** {145} Customer complaints increased significantly. Sunbelt did not have a viable sales force in the field to counter H & E's sales effort in Charlotte. This situation exacerbated customer confusion.

{146} Once Pearsall had taken a full complement of employees and information to start the H & E branch, he left the BPS office in a state of chaos and disorder, without proper documentation, without a proper inventory having been conducted, and without enough information for the remaining BPS employees and new Sunbelt employees to service and deal with BPS customers. These actions of defendants caused BPS/Sunbelt to lose customers. The Court finds his actions, and the actions of H & E and Hepler in their support, were intended to put the BPS branch in a state where it could not properly compete for either its employees or its customers in the early days of the H & E Charlotte branch.

{147} Having left the branch in a state of disorder, Pearsall and the other former BPS employees immediately targeted BPS customers.

{148} Farris and Huntley called on, and solicited orders from, BPS customers within the first 48 hours of their resignations from BPS. Both acknowledged that they were put immediately back into their former BPS territories by H & E, that they had no literature, equipment, or pricing information for H & E, but that they were able to secure orders for H & E immediately. Huntley immediately called on Universal Drywall, a BPS customer; Freeman Mechanical, a BPS customer; Davis Erecting, a BPS customer; Delta Electric, a BPS customer; and Drywall Carolina, a BPS customer.

{149} The Court finds that much of Huntley's testimony was not credible. His trial testimony was contradicted by his deposition testimony, and both were contradictory at times.

{150} Farris immediately went to BPS Charlotte's largest job site-Corning in Midland, North Carolina, and began calling on customers of BPS at that site. Mr. Farris obtained orders from BPS customers, on behalf of H & E, as early as June 1, 2000, before the H & E branch was open. In fact, Kline's June 2000 e-mail to Bruckmann confirms that defendants' expected Farris to switch over the Corning customers.

{151} Farris also acknowledged that he had no pricing or other H & E information when he went to call on BPS customers. In fact, Farris called on BPS customers on behalf of H & E *while he was still employed by BPS.* Farris testified that he began his employment with H & E on May 31, 2000, and he submitted his letter of resignation to BPS on May 31, 2000, but he also acknowledged that he solicited customers at the Corning site on behalf of H & E on May 30, 2000.

{152} Further, Farris's acknowledgment of receipt of the H & E policy handbook is dated May 31, 2000 and is signed by Brian Pearsall as Farris's H & E supervisor, despite the fact that Pearsall was still employed by BPS on May 31, 2000.

{153} Farris obtained orders from the following BPS customers within a week of H & E's opening: Interstate Electric (order date 6/6/00); Rental Supply (order 6/7/00); Capital City Steel Erectors Supply (price quoted was “off the seat of [his] pants); Gulf State Electric, Supply (order 6/6/00); Environmetrics (order 6/7/00); Howard Brothers Electric. Farris's relationships with these customers were developed while he was employed at BPS.

***28** {154} The Court finds that many of these customers from which BPS lost business had long standing relationships with BPS. These customers would have given Sunbelt the opportunity to compete fairly for their business with H & E, an opportunity that H & E's actions may have prevented in some cases.

{155} H & E's new Charlotte employees could not, at least in the beginning, have used the “Dodge” reports to find and secure new customers for H & E. The new H & E branch did not have credit applications and related paperwork when it began taking rental contracts. Credit information is an essential part of doing business when dealing with expensive equipment like the kind at issue here. The only way H & E could have done business was in reliance on the BPS credit information known to the former BPS employees hired by H & E.

{156} Therefore, the Court finds that H & E used customer information brought to it by the BPS employees it brought on board immediately-including pricing information, customer information, credit information and information related to prospective and upcoming jobs-in order to solicit and secure jobs.

{157} The Court finds that there was sufficient evidence to show that BPS considered the compilation of its customer information, which took considerable time, money and effort to compile, to be confidential. Further, the Court finds that BPS took reasonable efforts to maintain the confidentiality of that information, including maintaining passwords on the computer system, not giving each employee a password, shredding of confidential documents, and requiring each employee to sign an employee handbook with a confidentiality provision.

{158} Finally, the Court also finds that the BPS employees who left *en masse* and went to H & E had an opportunity to acquire and know the confidential information and to use it at H & E.

Orlando

{159} The Orlando Hi-Lift branch opened on or about May 22, 2000, with the following staff from BPS: a branch manager (Wellington “Duke” Drennan); BPS's complete AWP outside sales staff (Jay Kiefer, Mark Stuckie and Jeff Hansen); a shop foreman (Michael Waldrop); mechanics (Todd Chesser and Scott Waldrop); a credit manager (Patricia Uddo); a branch administrator (Brenda Drennan); and a driver (Henry Garver). Shortly thereafter, the H & E Orlando branch added an inside sales coordinator (Andrea Ussery) and another driver (Donald Henderson).

{160} After a conversation with Hepler at the 1999 national sales meeting in Dallas, Duke Drennan (“Drennan”), the BPS Orlando branch manager, told some of his employees that Hepler might start a company of his own and that this might be a possibility for future employment. The employees to whom Drennan made these comments-Jay Kiefer (“Kiefer”), Mark Stuckie (“Stuckie”), Jeff Hansen (“Hansen”), Patty Uddo (“Uddo”), Peter Casey (“Casey”), Brenda Drennan (“B.Drennan”), Steve Hicks (“Hicks”) and Andrea Ussery (“Ussery”)-all later left BPS to work for H & E.

***29** {161} Hepler called Drennan at the BPS Orlando branch in March 2000. Drennan testified that he likely informed Kiefer, Stuckie, Hansen, Uddo, Casey and Hicks of this conversation with Hepler. Hepler's telephone records reflect an eight-minute telephone call to the BPS Orlando branch on March 29, 2000.

{162} Drennan resigned from BPS on April 29, 2000 and left BPS on May 4, 2000. Drennan's employment offer from Hepler included a salary of $105,000, higher than his salary at BPS, as well as a $25,000 signing bonus.

{163} Hepler's H & E expense records reflect meetings with Drennan in April 2000 to discuss H & E, including Tampa and Orlando branch locations and operations. These records reflect such meetings prior to Drennan's resignation from

BPS. For example, Drennan, while still employed by BPS, again had dinner with Hepler on April 13, 2000 at Christine's restaurant in Orlando along with Delores Kline and Mike Quinn. Hepler, Quinn and Delores Kline were in Orlando to look at potential properties for an H & E facility in the area.

{164} All of the employees that Drennan solicited on behalf of H & E in April, May or June of 2000 were BPS employees.

{165} While still a BPS Orlando branch manager, Drennan did the following:

(a) In April 2000, Drennan, after conferring with Hepler, invited BPS employees Kiefer, Stuckie, Hansen, Uddo and Ussery to have dinner with him and Hepler. Drennan met with these employees separately at BPS, informed them of his intent to leave BPS if Hepler offered him a job at H & E, and invited each individual to attend the dinner at the Orlando Ale House.

(b) Drennan testified that at this dinner Hepler discussed the prospect of H & E opening a facility in the Orlando area. Hepler ended the dinner by saying he would further explore the possibility and it was agreed that they would continue the discussion in the future. Of course, Hepler testified that they did not discuss the possibility of an H & E Orlando branch at this dinner. Drennan's testimony contradicts Hepler's testimony about this dinner. The Court finds that Hepler's testimony is not credible and he used this meeting to recruit BPS employees to H & E with Drennan's assistance.

(c) Prior to the Orlando Ale House dinner, Ussery never heard anyone at the BPS branch express a desire to leave BPS. He testified: "[W]e all loved working there." The pending sale of BPS was a subject of curiosity, but not a great concern: "We had already gone through a sale one time, and nothing changed. It was just curiosity. Everybody was just curious."

(d) Drennan admits that he openly criticized BPS in conversations with his employees and discussed his plans with regard to Rob Hepler.

(e) Drennan, following the April 2000 meeting with Hepler, assisted BPS employees Kiefer, Stuckie, Uddo, Hansen and Ussery in communicating with Hepler regarding employment with H & E and the details of such employment. Hepler authorized Drennan, prior to Drennan leaving BPS, to offer employment with H & E to BPS employees and set their H & E salaries. Drennan did just that, discussing H & E employment with BPS employees while still the BPS Orlando branch manager of. The salaries Drennan offered on behalf of H & E were consistently higher than the salaries Drennan paid such employees at BPS. Defendants, with the assistance of Drennan, recruited and hired 12 BPS employees required for H & E's start up (17 total).

***30** (f) Drennan talked to Kiefer, who already had resigned from BPS, about setting up a boom for an H & E customer and contacting the necessary personnel to help place the boom on the job site for the customer. Drennan gave Kiefer the authority to get help with the boom and referred Kiefer to Mike Quinn. The boom was on the customer's job site before Drennan left BPS.

(g) Drennan, upon being asked by one of his BPS employees if he would hire her boyfriend to come work for H & E, told her that he could not approach any employees but it was all right if employees approached him. The BPS employee in question subsequently approached Drennan at BPS, and Drennan offered him a job at H & E. Clearly, Drennan knew that recruiting for his employer's competitor was wrong.

{166} Drennan took confidential business files of BPS with him to H & E, including BPS monthly goals, rental revenue information, salary/wage reports and a spreadsheet reflecting average salaries, and returned those files only after the lawsuit was filed.

{167} Not only did Drennan take confidential files and solicit other BPS employees while he was employed at BPS, he also encouraged at least one employee to bring valuable, confidential BPS information and documents with him.

{168} In late March 2000, Drennan solicited Rick Breinlinger ("Breinlinger") at the BPS branch. Drennan first approached Breinlinger at the BPS branch and told Breinlinger that he was moving to another company where he would be working with Hepler and wanted Breinlinger to come with him. Drennan said that other BPS employees were also going with him and that Breinlinger was not to say anything to anybody. Drennan said that he would get back to Breinlinger about the details, which he did. He called Breinlinger at home and invited Breinlinger to his house to discuss the details of the H & E offer. Breinlinger met with Drennan at his house on a Sunday afternoon, at which time they discussed the position, salary and vacation time H & E, through Drennan, was offering Breinlinger. At this meeting they also discussed the location of the H & E facility and other BPS employees who Drennan had solicited from BPS. Drennan asked about Breinlinger's BPS service log book, which contained detailed information about customer contact information, how such customers conducted business, and repairs performed for customers. He told Breinlinger to bring the service log book with him to H & E. Drennan reiterated at this time the importance of keeping the matter quiet and not discussing it with anyone. Drennan ultimately retracted the H & E offer when Breinlinger refused to leave BPS without giving a two week notice. Drennan admits he solicited Breinlinger to leave BPS to work for H & E.

{169} Defendants did not call Drennan as a witness to rebut or deny Breinlinger's testimony.

{170} H & E salesmen in Orlando were not provided any guidance or parameters with regard to pricing on behalf of H & E. H & E Orlando did not even compile price lists until 2001. Prior to that time, H & E salesmen were expected to quote prices to customers based on “information in their head.” Drennan has never spoken with Hepler or anyone else in Hi-Lift's corporate office about pricing. He has always set the prices for his branch.

***31** {171} The territories covered by H & E salesmen were territories that they had covered on behalf of BPS, and they immediately called on the customers and job sites based on information acquired while employed by BPS. For example, as soon as Kiefer resigned from BPS, he called on R.C. Aluminum, a BPS customer at the Hard Rock Café job site, a major project that he covered for BPS. Regarding the order he received from R.C. Aluminum that first day, Kiefer testified, “I didn't write it up at all. I mean, I knew the account and knew R.C. Aluminum, the job.” He did not even ask for a credit application from R.C. Aluminum, despite H & E's alleged policy of obtaining a credit application from every customer. On behalf of H & E, Kiefer called on every trailer on the Hard Rock job site, each of which he had called on for BPS.

{172} Drennan admits, and H & E business records show, that he has personally entertained and solicited former BPS Orlando customers on behalf of H & E.

{173} The departure of Drennan and other BPS employees in such a short period of time left the BPS Orlando branch understaffed, lacking experienced personnel, unable to service customers as it had prior to H & E's raid on the branch, and caused the branch to lose considerable business from longstanding customers. Further, without Kiefer, Stuckie and Hansen, its entire AWP sales force, the branch's business slowed considerably, and many of its high volume customers began calling BPS equipment off rent and stopped renting equipment from BPS.

Tampa-Fort Myers

{174} Prior to May 2000, H & E did not have a presence in the Tampa-Fort Myers market. The H & E branches established in Tampa-Fort Myers were greenfields.

{175} The Tampa and Fort Myers Hi-Lift branches opened on or before May 8, 2000 and June 5, 2000, respectively, and were staffed with the following BPS personnel: a branch manager (Beare Jones); sales reps (John Andrachak, John Breadmore, Wade Bercaw, Scott Strawn, Jason Jones and Brian Ditoro); a service manager (Doug Ashmore); inside sales coordinator (Bonnie Quasnick); drivers (James George, Jonathan Brunelle, and Charles Heim); an officer manager (Belinda Harrison); a shop foreman (Ronald Good); field mechanics (Timothy Poole, Billy Marshall, and John Clark); an erector superintendent (Nicholas Cooper); a shop mechanic (John Taylor); erector foremen (Leon Beebe, Scott Price, and Mark Roesler); and erectors (Larry Brown, Charles Cansdale, and Eric Ruzycki). Each of these employees were hired from BPS.

{176} The market for trained and experienced drivers, mechanics and salesmen in Fort Myers and Tampa in 2000 was very tight. Trained and experienced employees were then difficult to locate in these markets.

{177} BPS had existing branches in Tampa and Fort Myers in January 2000. BPS had opened up the Tampa branch in or about 1996 as a greenfield. Hepler testified about the steps undertaken at the time to create that greenfield. None of those steps were repeated when H & E opened up its Tampa branch in May 2000. Instead of placing advertisements in the newspaper for employees, H & E used secret meetings with Hepler, branch manager Beare Jones and service manager Doug Ashmore to solicit employees. Instead of building slowly as business warranted, H & E opened with a full complement of employees.

***32** {178} Jones claims that when he learned of Defendant Hepler's December resignation he was “shocked” by the news, that it “stopped [his] heart,” and that, despite the fact that Hepler was like a brother to him, he did not speak to him at all for 60-90 days after Hepler departed.

{179} The evidence shows that contrary to his sworn testimony, Jones spoke with Hepler repeatedly throughout the time period prior to Hepler leaving BPS for H & E, including three times on January 3, 2000, a thirteen minute conversation on January 13, two conversations on January 18 (4 and 6 minutes respectively), an eleven minute call on February 17, three calls on February 21, two calls on March 29 (including a seven minute call), an April 4 call for twelve minutes, a thirty-five minute call on April 11 and three calls on April 12. For this and other reasons stated below, the Court does not find Jones's testimony credible and notes that he did not testify at trial. Jones, Hepler and Hepler's father had been close friends and business associates for decades.

{180} On February 22, 2000, a meeting occurred in Fort Myers attended by Hepler, Jones and the BPS sales staff in Fort Myers and Tampa. H & E's business records reflect that the purpose of the meeting was to "discuss H & E employment offer with Jones and sales staff." Hepler submitted that receipt for his breakfast to his employer and was reimbursed for the expenditure as a proper business expense. Moreover, Hepler's attempt to excuse the clear statements on the H & E expense report for this meeting by laying blame on his secretary is not credible. Ms. Parnell's testimony is clear that she always tried to be accurate, took the information that was given to her by Hepler to place on the report, did not add her own musings, and had no reason to believe that the information was inaccurate. Hepler also admitted that he never called anyone in Baton Rouge and told them anything was inaccurate or needed to be changed in the report.

{181} Jones admitted that he invited BPS employees to attend the meeting with Hepler on February 22, 2000. Former BPS employees Wade Bercaw, Scott Strawn, John Andrachak and John Breadmore all met at this early morning breakfast meeting in Fort Myers. Their claim that it was a casual, non-business breakfast among old friends is not credible. Kevin White, branch manager of Sunbelt in Fort Myers, testified that Bercaw stayed with him in Fort Myers the previous night and explicitly told him that he would be meeting with Jones, Hepler, Andrachak, Breadmore and Strawn the next day about starting a new business in Florida. White was credible, and his testimony is confirmed by H & E's business records. His testimony is also confirmed, in part, by Bercaw, who testified that he knew the night before the meeting that Hepler, Jones, Andrachak and Strawn would be there and that it would be held at the Shoney's. White also testified that in a later conversation he was told by Bercaw that he was offered a job by Hepler at that breakfast. White's testimony is also confirmed by the fact that Bercaw telephoned him some months later, after learning that White had disclosed this meeting to Sunbelt's CFO, to express his displeasure with the fact that he had disclosed this clandestine meeting. The Court finds White's testimony credible. Bercaw's testimony, denying that the purpose of the meeting was for employment, is not credible.

***33** {182} The testimony of Hepler and Jones regarding this February 22 meeting is inconsistent in significant respects. Hepler testified several times that he knew nothing about the fact that others would attend this breakfast meeting until the morning when Jones picked him up. Jones testified, however, that he discussed having these people attend when Hepler first called him to tell him he would be traveling to Fort Myers, several days before the breakfast meeting occurred. Hepler and Jones are not credible in their denials as to the purpose of the meeting. Hepler recruited Jones to H & E, and then, with Jones's assistance while Jones was still a BPS employee, readily recruited other BPS employees for H & E.

{183} Jones had knowledge of Hepler's efforts to start new branches in Tampa and Fort Myers for H & E and was an active participant in a plan to hire BPS employees to go to H & E in Tampa and Fort Myers and to start-up the new branches.

{184} In the span of thirty days, Jones, Bonnie Quasnick (the Tampa inside sales coordinator) and Hepler solicited and hired 25 experienced BPS employees from BPS's Tampa and Fort Myers branches; over 90 percent of the H & E work force came from the Tampa and Fort Myers BPS branches. Jones testified that as the H & E branch manager, he would have a say in the employees and structure of the branch and admitted that outside sales persons, inside sales persons and the service manager are essential to a new branch. Jones reviewed these employees while at BPS, was knowledgeable of their BPS salaries and knew these employees to be good performers These employees were hired for similar positions at H & E and offered a salary increase to leave BPS. As of January 1, 2001, twenty-six of H & E's 35 employees in Tampa/Fort Myers were former BPS employees.

{185} Jones's denials of knowledge and involvement in the defendants' plan to recruit employees *en masse* from BPS to H & E and switch customers are not credible.

(a) Evidence shows that at the time Jones filled out his application for employment with H & E he listed the position as branch manager for Tampa *and* Fort Myers and he also indicated that he would *not* relocate from Fort Myers.

(b) Jones also claimed to have been dissatisfied with BPS after Hepler left. Nevertheless, H & E gave him a $14,000 salary increase and a $25,000 sign-on bonus to leave BPS to go to work for H & E.

(c) Jones claims that at the time he resigned there was no BPS plan to open a Fort Myers branch, only a Tampa branch. In addition to the admission on his H & E application, Jones hired two employees, Andrachak and Breadmore from the BPS Fort Myers branch-both of whom indicated in their H & E employment application that they would not relocate from Fort Myers.

(d) Jones testified that he had no involvement in the location of the H & E branch in Tampa. Kline also denied having spoken with Jones when he went to Tampa in February 2000. Evidence shows, however, that Jones was in contact with Defendant Kline right before Kline' February 27 trip to Tampa and signed a letter of intent for the rental of property for the H & E Hi-Lift branch.

***34** (e) While still a BPS employee, Jones also met with Hepler on April 26, 2000, to discuss “Tampa operations,” and he met with Hepler on May 17, after he had resigned, to finalize the recruitments of Breadmore, Andrachak and Quasnick.

(f) Moreover, defendants' action in ordering AWP equipment for Tampa confirms the prearranged plan. On March 31, 2000, defendants placed an order for 99 units for Tampa with JLG. As confirmed by the events in almost each location, defendants would not have placed such an order without the branch manager (Jones) in place.

{186} BPS employees in Tampa were also recruited by Doug Ashmore, the former BPS service manager under Jones. Billy Marshall, Ron Good and Timothy Poole, all experienced service mechanics, worked under Ashmore. Ashmore testified that it was important to the business to have experienced mechanics. All three of these mechanics were hired the same day by H & E; Good and Poole left BPS without notice in the early morning hours on June 1. Sunbelt did not have the opportunity to speak with these employees about continued employment at the branch.

{187} Ashmore denied, under oath, that he solicited any employees to leave BPS for H & E while employed at BPS. Billy Dobbs, who Ashmore claims is a trusted friend and worked under Ashmore, testified that Ashmore solicited him as part of the “chosen few” for H & E while Ashmore was still with BPS. Dobbs also testified that the mechanics agreed that they would leave early in the morning, Monday, June 1, without notice. Libby Oleson, an assistant to the inside sales coordinator and Quasnick, also testified that she had conversations with Ashmore during the time he was employed by BPS. These conversations show that he had been coordinating with Jones regarding the solicitation of BPS employees for the new H & E branch.

{188} The testimony of other former BPS employees in Tampa and Fort Myers, now H & E employees, is not credible, and further supports a finding that the defections were planned and orchestrated while the current H & E employees were still BPS employees.

(a) Andrachak and Breadmore, former BPS sales representatives from the BPS Fort Myers branch, and now H & E employees, testified that they resigned from BPS without a job offer from defendants. Breadmore was the sole breadwinner for the family, and he and his wife required insurance through his work. Both testified that, although they did not know the purpose of their trip to Tampa, they traveled two and half hours from Fort Myers to Tampa to meet with Jones and Hepler and while in Tampa they were offered a job, which they accepted. At the time they accepted the offer, they supposedly did not know anything about the job or where it would be located, even though they were not willing to move from Fort Myers. Finally, although testifying that when they left BPS they did not have an offer in hand, their employment applications with H & E state that the reason they left BPS was for a “new” or “better” job.

***35** (b) Andrachak's employment termination date with BPS was May 26, yet Andrachak submitted an expense report to H & E for reimbursement of expenses incurred beginning May 15.

(c) Similarly, Quasnick's last day of work at BPS was May 22, 2000 (with a termination date of June 2), yet she signed her both her W-4 and H & E employment application on May 19, 2000. The May 19 date on her employment application was crossed out and changed to May 22. Quasnick testified that she did not start at H & E until May 23, 2000. She also testified that when she spoke with Hepler and Jones at dinner prior to her resigning, there was no discussion of Strawn and Bercaw. Jones testified that he told Quasnick at that dinner that he had been speaking with Strawn and Andrachak.

(d) Ashmore filled out his H & E application for employment on May 22 and signed his H & E employee handbook acknowledgment on May 25. Ashmore, however, continued working at BPS until two days after Jude Yimin of Sunbelt had arrived at the branch, all the time soliciting BPS employees to leave the branch for H & E.

{189} After successfully bringing over the BPS employees, defendants immediately began building a revenue stream by targeting longstanding customers of BPS in Tampa and Fort Myers and "switching" them over to H & E. Evidence shows, and Jones admits, that efforts were made by H & E to switch customers from BPS to H & E almost immediately following the departure of the BPS employees to H & E. The evidence also shows that BPS had longstanding customers in Fort Myers (customers of BPS as early as 1994 and 1995 when White was employed at BPS) and Tampa and that relationships between sales representatives with customers was fostered by BPS. In May and June 2000, the BPS branches experienced a decline in AWP lease contracts while H & E experienced a concurrent rise in contracts with these same customers.

{190} Substantial evidence shows that pricing and customer contact information at the branches was confidential information, although customers themselves did not treat pricing as confidential. White testified that he understood that the BPS branch had special or preferred pricing for customers, based on a number of factors, including volume of business given by that customer, and that this information was confidential when he was an outside salesman at the BPS Fort Myers branch under Jones in 1994-95. Bercaw admitted to using special pricing at BPS, which was exclusive for the customer and maintained for at least six months. In addition, the BPS employees who went to H & E signed acknowledgments of the BPS, and later the H & E handbooks, which contained confidentiality sections.

{191} In 2000, BPS was the largest rental company in Fort Myers. By taking BPS employees and leaving the BPS branch in disarray, H & E was able to rapidly gain market share in the Fort Myers' market and BPS lost market share in Tampa at a fast rate.

{192} The massive departure of employees from BPS to H & E in such a short period of time left the BPS (now Sunbelt) branches in Fort Myers and Tampa in a total state of disarray. The H & E employees involved in the solicitation of these employees were indifferent to the impact of their actions on the BPS branches.

***36** {193} The evidence shows that at the time that H & E was contacting BPS customers, BPS was not in a position to compete in the marketplace. Salesmen are vital to the business and act as the company representative with the customer. With the mass exodus of employees from the BPS Fort Myers and Tampa branches, BPS did not have experienced outside sales representatives who knew the customer base and contacts to call on customers and present the facts concerning the acquisition. At the same time, however, H & E had their sales force (the former BPS sales team) in the field immediately calling on customers.

{194} Defendants' conduct was undertaken for the purpose of harming BPS/Sunbelt and gaining a competitive advantage over Sunbelt in the Tampa/Fort Myers markets. In summary, the Court finds the following facts:

(a) Over 90 percent of the H & E employees in Tampa and Fort Myers came from BPS and were hired in a thirty-day period, leaving the BPS branches with virtually no employees. Given Hepler's experience and past involvement in starting up a greenfield branch in Tampa and his knowledge of BPS personnel vulnerabilities, Hepler knew that defendants' actions would have a debilitating effect on the Sunbelt's ability to compete.

(b) Hepler arranged a meeting in February 2000 for the purpose of discussing the opening of branches in Tampa and Fort Myers This meeting was attended by the same BPS employees who became the first employees of H & E. Defendants' and their witnesses' denials that the meeting was for the purpose of recruitment are not credible.

(c) The speed by which H & E established itself in Fort Myers and Tampa, a market in which BPS had significant market share, demonstrates that H & E's actions were calculated as part of a plan. By year-end 2000, H & E had profitable branches in Tampa and Fort Myers.

(d) Just as Sunbelt was undertaking efforts to recover in Fort Myers by hiring Kevin White as the branch manager, Jones made a threatening comment to him to discourage his taking a job with BPS. Hepler telephoned White to offer him a position in Texas. White had not spoken with Hepler in six years and had not been talking with him about a position in Texas. In fact, White had had no experience in Texas. The only apparent reason for offering him a job was to keep experienced employees from going to work for Sunbelt in Fort Myers.

(e) Jones denied that he did anything intentional to harm Sunbelt. He testified that proof of his contention was that he had not gone after ICM, the largest industrial customer of BPS in Tampa and a customer that Bercaw described as having a verbal, exclusive partnership with BPS/Sunbelt. In fact, not more than a week after Bercaw started at H & E, he was calling on ICM trying to obtain their business with the full knowledge and support of Jones. When shown his deposition testimony at trial, Bercaw reluctantly admitted that he was trying to establish the same type of verbal, exclusive partnership with ICM that BPS/Sunbelt enjoyed. Contrary to his sworn testimony, Jones personally went after ICM's business; he just wasn't successful in his efforts.

***37** {195} As a direct and proximate result of defendants' actions, the BPS/Sunbelt branches in Tampa and Fort Myers were left in a debilitated state.

(a) Experienced employees in the branches, such as Andrachak (outside sales), Breadmore (outside sales), Strawn (outside sales), Bercaw (outside sales), Jason Jones (inside sales), Bonnie Quasnick (inside sales), Brian Ditoro (inside sales), Doug Ashmore (service mechanic), Ron Good (mechanic) and Tim Poole (mechanic), were gone to H & E within days of each other.

(b) In Fort Myers, the only remaining outside salesman, Tim Kennedy, was moved to the branch manager position, leaving no outside sales staff until the branch hired Scott Williams, who had no experience with AWP rentals, and Frank Hight, who was later terminated for poor performance.

(c) In Tampa, the only remaining AWP outside salesman, Dennis Carpenter, had only recently moved into that position from his prior position as a driver, and he had no AWP sales experience. BPS/Sunbelt filled the inside sales/dispatch position in Fort Myers with a person who sold copiers and had no AWP experience.

(d) Drivers and mechanics were hired with no AWP experience.

(e) As Billy Dobbs testified, positions were filled with just “warm” bodies, sometimes by family members who had no training or experience with AWP's. Libby Oleson moved into the inside sales coordinator position, to replace Quasnick, although at the time Ms. Oleson had no experience in crucial aspects of the job such as setting prices and giving advice regarding the type of AWP equipment best suited to a customer's job. Jeff Brown, who was hired in July 2000 to act as an AWP outside salesman in Tampa, could not take on his sales responsibilities for the first several months because he had to assume other responsibilities-such as assisting Ms. Oleson with the inside sales function, handling field service problems and advising customers on rental needs-caused by the rapid departures of BPS employees for the H & E branches.

(f) It took the Sunbelt Tampa branch two and a half years to rebuild its sales staff with experienced sales people.

{196} As a direct and proximate result of the massive departure of BPS employees to H & E in May 2000, the Fort Myers and Tampa branches experienced significant problems with the operation of its business that caused it to lose customers.

(a) Response time for servicing equipment in the field increased from a matter of hours before the departures to sometimes days. Similar difficulties were encountered in Tampa.

(b) AWP equipment was not serviced or timely delivered, and customers called in to order equipment off rent when the jobs had not been completed.

(c) AWP equipment in Fort Myers could not be located for months.

(d) Due to the absence of drivers, equipment was not picked up in a timely manner in Tampa, causing additional customer complaints and loss of business.

(e) Employees in the BPS/Sunbelt branch in Tampa worked long shifts, sometimes 14 to 15 hour days, to keep the branch open.

Dallas

***38** {197} As of the beginning of 2000, Defendant H & E did not have a branch in Dallas, Texas that specialized in the sale or rental of equipment. In establishing the budget for the Dallas branch, H & E employees treated it as a greenfield.

{198} The Dallas Hi-Lift branch opened no later than March 20, 2000 and, within two days of the opening, had the following staff from BPS: a branch manager (Abe Farrington), a service manager (Jeff Billups), outside sales reps (Steve Matthews and Ken Moon), mechanics (Tim Green and Tony Herriage) and a driver (Darrell Herriage). Within two weeks, H & E added another BPS mechanic (Allen Green) and in the next two months, another BPS mechanic (Curtis Billups) and a BPS driver (Chris Brown).

{199} Christensen, a senior member of the BPS management team, worked out of the Dallas branch and worked closely with Abe Farrington ("Farrington"), who in 1999 became the BPS Dallas branch manager. Christensen left his employment with BPS on January 14, 2000.

{200} In January 2000, BPS had many experienced and trained employees in the key positions in its Dallas branch. Farrington had been employed by BPS since December 1994 and had been the branch manager since early 1999. Farrington oversaw the other employees of the branch. Jeffrey Billups had been employed at BPS since May 1996. Steve Matthews, an outside AWP sales representative, and Ken Moon, the outside AWP sales representative for industrial accounts, had been employed by BPS since April 1997 and January 1999, respectively. Thomas Green, Allen Green and Tony Herriage were trained AWP mechanics that had been employed at BPS since May 1997, October 1996 and April 1997, respectively. Darrell Herriage, an experienced AWP driver, had been employed at BPS since May 1997. Each of these BPS employees was solicited by Christensen or Farrington and left BPS for employment at H & E in March or April 2000.

{201} In a span of 35 days, all of these BPS employees were on the payrolls at H & E. With one exception, each BPS employee was offered more money to go from BPS to H & E. For example, Farrington, who accepted employment with H & E no later than March 4, received a $5,000 increase to join H & E as its Dallas branch manager. The fact that H & E had to pay more for these employees to go to H & E belies defendants' contention that these employees left out of concern over their future employment at BPS. Indeed, Matthews testified that he was satisfied with his job at BPS. All of these BPS employees were placed in positions at H & E that were similar to those they held at BPS.

{202} Christensen also attempted to recruit other BPS employees who did not leave BPS for H & E. For example, Christensen attempted to create a suspended scaffolding department by recruiting Monty Huffman of BPS to join H & E. Christensen intended Huffman to then recruit the two other employees that worked under him at BPS, Robert Landry and Larry Sible. Huffman, Landry, nor Sible left BPS for H & E. H & E did not thereafter, independently, develop a suspended scaffolding business because, as Christensen testified, Mr. Huffman declined his offer and stayed with BPS/Sunbelt. The team of Christensen and Farrington solicited and hired other BPS employees to join H & E during the period of April through September 2000. During that period, they hired six additional BPS employees for the new H & E Branch.

***39** {203} Hepler and Christensen had conferred with respect to planning a new venture. For example, following Hepler's trip to meet with Rentokil personnel in the United Kingdom in August 1999, the National Sales Meeting occurred for BPS. Christensen and Hepler attended this meeting. During a break at this meeting, Christensen and Hepler took Linda Gomez, an outside AWP salesperson, to the side and asked her about the largest projects going on in the Dallas market and for her thoughts on where to locate a new branch. At the time, Hepler was aware that Rentokil was putting BPS up for sale and BPS was not opening a new branch in Dallas. Hepler's comment about a new branch could only relate to a new business venture and one about which Christensen knew.

{204} At the same time Hepler and Kline were taking steps to market their new company to prospective investors and meeting with Bruce Bruckmann, John Engquist and Gary Bagley, operations in the Dallas branch began to suffer, providing some circumstantial evidence that attention was diverted from operating the business to the development of a new company. These operational problems increased in December 1999.

{205} Hepler announced his resignation to BPS employees on December 1, 1999 and continued his employment with BPS until December 14, 1999. In his testimony, Christensen attempted to minimize his contacts with Hepler, but telephone records show that Christensen called BPS headquarters in Jacksonville and had lengthy conversations during this period in which Hepler was still employed at BPS. Beginning on December 15 (after Hepler left BPS), Christensen directed his calls to Hepler's cell phone, calling him on numerous occasions leading up to Christensen's termination of his employment with BPS. Telephone records also show that at the same time Christensen was calling the Jacksonville headquarters following Hepler's announced resignation, he also made calls to Farrington and Quinn.

{206} Hepler met with Christensen on December 16, 1999 in Dallas, Texas with John Engquist, purportedly to discuss his employment with H & E. Christensen received a $20,000 salary increase to $125,000 to join H & E and a $25,000 sign-on bonus. Telephone records show that after this meeting, Christensen, Hepler and Quinn had numerous telephone calls with each other and that Christensen continued to call the BPS branch in Dallas. Again, Christensen in his testimony attempted to minimize these contacts. Telephone records show at least 18 calls between Hepler and Christensen during the period of December 15 to January 14, the date Christensen left his employment with BPS.

{207} On January 11, 2000, prior to his January 14 termination date, Christensen telephoned Delores Kline and then began working with her to identify suitable properties in Dallas for the new Hi-Lift branch. These efforts led to Defendant Kline signing a letter of intent for the rental of property in Dallas on February 11, 2000.

***40** {208} No later than January 18, 2000, Defendant Hepler had directed Christensen to begin soliciting experienced BPS employees for the new Hi-Lift branch in Dallas. It was "challenging" to find skilled employees in the Dallas marketplace. Christensen quickly looked to the BPS Dallas branch for these employees. Christensen and Farrington had access to confidential salary information for employees in the BPS Dallas branch.

{209} Christensen never obtained the services of headhunters or placed advertisements in newspapers, but instead used BPS as his primary source for employees. On several occasions in February and March 2000, Christensen met with groups of BPS employees for lunch and dinner recruitment meetings. One such meeting was attended by six BPS employees. Another lunch was attended by three of BPS's outside sales personnel. No persons other than these BPS employees and Christensen were invited or attended these exclusive meetings. The exclusive nature of these group recruitment efforts strongly supports the finding that these meetings were not open to the general public but were part of a plan to seek mass departures of employees from BPS. Christensen interviewed no "candidates," other than Farrington, for the Dallas branch manager slot. Through Christensen and Farrington, defendants recruited and hired nine key BPS employees in Dallas, including its branch manager, service manager, several mechanics and two of its outside salesmen. During at least at one of these meetings, Christensen expressed his negative view of Rentokil's ownership of BPS. All of this conduct is outside the norm of recruitment effort in this industry.

{210} Pricing appeared to have more significance in the Texas market than in other BPS markets. In January 2000, BPS had customers with whom it had longstanding relationships, including Potter Concrete, Mills Electrical, Barnsco, Term Sheetmetal, Walker Engineering, Oak Cliff Glass and Electric, Drywall Interiors, Haley Greer, North Star Fire Protection and Ram Steel. Prior to that time, BPS personnel, including Christensen and Farrington, made presentations to BPS customers to establish special relationships whereby preferential pricing would be provided to these customers and, in return, the customer would provide 100 percent of its business to BPS. One example of such a presentation was that made to Mills Electric. These presentations led to the formation of a "gentleman's agreement" between the customer and BPS. BPS had every expectation that based on these agreements that it would continue to do business with these customers in the future. Among the customers for which these "gentleman's agreements" were established was Mills Electric and Ram Steel, both of which were in the top five customers for the BPS branch in rental volume in 1999.

{211} The preferential pricing set by BPS for these customers was considered confidential at BPS. Customer contact information was also considered confidential at the BPS branch and gave BPS a competitive advantage over the competition. Christensen told Linda Gomez on various occasions that the pricing was to be hand delivered to insure that the customers understood that the pricing was to be held in confidence. Linda Gomez testified that in her experience customers honored that request and did not share this preferential pricing with BPS competitors under this "gentleman's agreement." Preferential pricing remained in place for a year and then was reviewed to determine whether it should be adjusted. Gomez testified that the special pricing gave BPS a competitive advantage over the competition. Christensen admitted that he would not share any information with a competitor and would not disclose BPS customer information so that it loses its confidentiality and Farrington admitted that he encouraged sales representatives not to disclose pricing to the competition. Christensen, Farrington and Matthews each acknowledged their receipt of the BPS handbook which contained the confidentiality section.

***41** {212} The Court finds Ms. Gomez's testimony to be credible. The Court also notes that Christensen and Farrington did not testify at trial to rebut plaintiff's evidence.

{213} Evidence shows that the defendants engaged in improper conduct intended to gain unfair advantage over BPS. After Farrington and other BPS employees left for H & E, BPS discovered confidential information missing from the branch. Farrington maintained a binder of preferential pricing in his office. Following his departure, that binder could not be located. Matthews produced in discovery customer contact information that he took with him from BPS-despite being told by Christensen not to take any BPS documents with him. Matthews left binders containing only blank pieces of paper when he was required to leave information concerning customer contacts and new job starts. Customer profiles maintained by Gloria Silva could not be located at BPS within a week after she left BPS for H & E. In addition, Matthews' cell phone, paid for by BPS, was programmed to forward incoming calls to him when employed at H & E. The cell phone could not be disabled because the phone had been locked out and the access code was unknown.

{214} Mathews resigned from BPS without giving any notice on March 20 and joined a sales meeting with Farrington at H & E that day. Matthews also that day called on BPS customers, including Drywall Interiors, and admitted that he had no pricing information from H & E. Christensen called on Mills Electric and Haley Greer after the H & E branch opened, and Matthews immediately sought after other BPS customers, such as Oak Cliff Glass.

{215} Following the departures of Farrington and the other BPS employees to H & E in March 2000, longtime customers of BPS, including Potter Concrete, Ram Steel, Mills Electric, Cherry Paint, Gorman & Associates, Williams Insulation, and Oak Cliff Glass, stopped doing business with BPS and instead placed their AWP rental orders with H & E. The speed at which H & E switched long time customers of BPS to H & E is shown by the decline in contracts with Oak Cliff Mirror & Glass, Potter Concrete and Williams Insulation in March and April 2000 and the concurrent rise in contracts with those customers at H & E. The evidence shows that BPS had “gentleman's agreements” with these customers and reasonable expectations of continuing to do business with these customers prior to defendants' solicitation of the BPS employees to H & E and related conduct. Indeed many of the BPS customers that were lost to H & E were customers with whom Linda Gomez, not Mathews or Moon, had established relationships belying the suggestions that customers simply followed the sales representatives to H & E.

{216} The rapid departures of Farrington, Billups and the other BPS employees to H & E's Hi-Lift branch in Dallas had a debilitating effect on the BPS branch in Dallas, including the loss of longstanding customers. With the departure of Farrington, Matthews and Moon, the outside AWP sales presence was reduced to one experienced and trained AWP salesperson, Ms. Gomez. Mr. Lane, an outside AWP salesman, had to assume duties as the new branch manager. Besides Gomez, the only other AWP outside salesman was Scott Douglas, an apprentice with little experience. Equipment was not serviced and delivered in a timely manner, leading to customer dissatisfaction. As a result of the defendants' conduct, some longtime customers of the BPS Dallas branch stopped placing orders with BPS/Sunbelt.

***42** {217} While BPS business was suffering, the Dallas Hi-Lift branch grew rapidly. It was profitable in 2000. Christensen and Farrington received bonuses for their performance in 2000 because the company exceeded the plan for 2000.

{218} There is evidence that the same pattern of conduct found at other branches existed at the Dallas branch. The Court finds the following:

(a) Telephone records indicate that Hepler and Christensen called the BPS Dallas branch after Christensen tendered his resignation, but prior to his leaving BPS, at a time when Farrington was employed at BPS. Farrington did not deny that he spoke with Christensen on the telephone at the BPS branch at the time in question.

(b) Christensen met with Farrington on at least two occasions before Farrington left BPS. On the first such known occasion, they discussed when Farrington would need to leave BPS, which suggests that the preliminary discussions had long passed.

(c) Christensen used BPS as his primary personnel source for the Hi-Lift Dallas branch.

(d) Christensen testified that risk and uncertainty exist with starting a new company and that he considered that

> uncertainty in deciding to accept employment with H & E. One of those risks was establishing itself by reputation, "the new-guy-on-the-block syndrome." Christensen admitted that he brought employees from BPS to make the company profitable and that that gave him greater comfort with his decision to go to H & E.
>
> (e) Farrington testified that he reviewed the property then used by Martin Equipment, another division of H & E, to determine whether it could be used for the Hi-Lift operations, and that his assessment was that it would not work. He further testified that afterward he met with Delores Kline to identify another location for the branch, which turned out to be the branch that Hi-Lift operates out of in Dallas. Farrington testified that none of this occurred while he was employed by BPS. Farrington's last day with BPS was either March 14 or 17, 2000. If Farrington were correct, then work on identifying this new property would had to have occurred after March 14. H & E, however, signed a letter of intent with respect to the lease of this property on *February 11, 2000.*

{219} Farrington testified that prior to resigning on March 4, he did not know that Christensen was meeting with other BPS employees, and he denied having any role in the recruitment of BPS employees while he was himself employed by BPS. Indeed, Farrington admitted that it would have been improper for him to solicit employees while employed by BPS. Yet, an H & E expense record filled out by Christensen shows that Farrington met with Christensen and Billups *together* on March 3, 2000 (while Farrington was the branch manager of BPS). When confronted with this document, Farrington admitted that maybe he was "in the same building" with Billups but that he had nothing to do with his recruitment. Reluctantly, Farrington admitted that he was aware that Christensen was discussing Billups going to H & E. Christensen testified that he met with both Farrington and Billups together and it was at this lunch that they discussed when Farrington would leave BPS for H & E.

Houston and San Antonio

43** {220} ***Houston. As with Dallas, Christensen was intimately involved in the solicitation of employees for the new H & E Hi-Lift branch in Houston, Texas.

{221} H & E had a small fleet in Texas at its South Texas Equipment subsidiary. South Texas was better known as a crane and earth moving equipment company than a AWP rental company. Prior to 2000, the South Texas fleet consisted largely of aging Grove equipment. Utilization of the Grove fleet did not meet Engquist's expectations. Because of its Grove fleet, the South Texas AWP mechanics had not attended special training by Genie or JLG prior to January 2000. Christensen testified that when he first met with John Engquist he was told that H & E had not been very successful in the rental market and that is why they were looking to bring on Hepler, Kline, Quinn and himself: to develop a new H & E rental division.

{222} The Houston branch manager, Rodriguez, testified that Engquist did not speak to him prior to November 1, 1999 about expanding the operations in Houston or opening up in other markets. Rodriguez's testimony confirms that the creation of the H & E Hi-Lift division was only explored after Hepler and Kline approached Bruckmann, Bagley and Engquist.

{223} In February and March 2000, Christensen met with BPS employees in Houston for the purpose of soliciting them to H & E. Christensen, later with the assistance of Rodriguez, solicited and hired eight experienced BPS employees to the Houston branch, nearly one-third of the H & E work force in Houston. The former BPS employees were hired for similar positions at H & E and, with one exception, were given pay increases to go to H & E. No headhunters nor advertisements in newspapers were used for building the new Hi-Lift branch.

{224} H & E expanded its customer base rapidly in 2000 concurrent with its hiring of employees from BPS. Significantly, no contracts were produced by H & E for many customers at the branch until the period after April 2000. H & E's business with Brown & Root nearly tripled between January and April 2000. By October 2000, after hiring eight employees from BPS, H & E doubled its rental revenue in Houston from the same time the prior year.

{225} ***San Antonio.*** Hepler, with Christensen's assistance and input, solicited David Hobbs, BPS's branch manager in Charleston, South Carolina for a new Hi-Lift branch in Texas. Hobbs received a substantial pay increase-$20,000, plus a $27,000 moving expense payment-to leave BPS for H & E. The day after Christensen left BPS, he traveled to Jacksonville to meet with Hepler and Rodriguez and then traveled to Savannah, Georgia to meet with Hobbs and Alexander. Hepler had given Christensen responsibility for soliciting Hobbs. Following the meeting with Hobbs in Savannah, Hepler and Christensen continued their conversations with Hobbs to solicit him to H & E, and Christensen kept Hepler abreast of his progress. Hobbs was on board quickly though, and signed H & E employment forms in late January 2000 indicating his acceptance of employment at that time. Then Christensen, with Hobbs' assistance, solicited Gloria Silva (Ysassi) from BPS to H & E.

***44** {226} The recruitment of Hobbs is a good example of the difficult interplay of fair and unfair competition. If nothing else had happened, the hiring of David Hobbs to leave BPS in Charleston and move to a new Hi-Lift branch in San Antonio would not be a problem. The same could be said of the hiring of Gloria Silva (Ysassi) to be credit manager in San Antonio. Standing alone, each hire would not provide grounds for an unfair trade practices claim. When put in the context of the overall raid of BPS employees, the two hires provide additional evidence of a deliberate effort to orchestrate mass defections from BPS to H & E and to appropriate the intellectual knowledge base of Sunbelt.

{227} While having some minor impact, the defendants' actions in the Houston-San Antonio market were not as devastating as the actions taken in the other BPS branch markets targeted by H & E. They are evidence, however, of the pervasive effort of H & E to siphon off most of the key employees of BPS.

Atlanta

{228} The Atlanta Hi-Lift branch opened on or about March 15, 2000. The following BPS personnel were either on-board at the opening or working with Hi-Lift within two weeks of opening: a branch manager (Mark Alexander); a full AWP outside sales staff (David Leavell, Bill Kenyon, Dan Franz and James Cornett); a service manager (James Brown); a shop foreman (Dan McMahan); mechanics (Paul Fredrickson, Michael Mullen and Roger Dempsey); a credit manager (Andrew Warshaw); a parts coordinator (Clinton McMahan); and drivers (Nathaniel West and David Waddell). Shortly thereafter, the Atlanta Hi-Lift branch added an administrative assistant (Rhonda Rathel). Each of these employees was hired from BPS.

{229} Hepler and Quinn arranged to meet with Alexander, the nine-year existing manager of the BPS Atlanta branch, on January 6, 2000 to begin the plan leading to the opening of the H & E Atlanta branch. At lunch, Hepler told Alexander he wanted to open an H & E branch in Atlanta and wanted assurance that Alexander would consider becoming the branch manager. Alexander was given responsibility for hiring employees at the new H & E branch.

{230} A dinner was arranged that night with four long-term BPS employees that worked under Alexander at the Atlanta branch: Atlanta's two most successful salesmen, David Leavell ("Leavell") and Jim Cornett ("Cornett"), the Atlanta service manager James Brown ("Brown") and Alexander's "right-hand man at the branch," Dan Franz ("Franz"), the scaffolding manager. Hepler and Alexander claim that the dinner was Alexander's idea to get old friends together and deny that recruitment was. This testimony sharply conflicts with co-defendant Quinn's testimony that Hepler set this dinner up to recruit these BPS employees for H & E. Once again, Hepler's credibility is at issue, and for the multiple contradictions between Hepler and other sworn testimony, the Court again finds Hepler is not credible.

***45** {231} Quinn testified that the dinner was arranged for the express purpose of recruiting BPS employees to come work for H & E. Hepler's only explanation when confronted at trial with Quinn's testimony was that Quinn's recollection was inaccurate. Alexander admits that he falsified his expense report for this Atlanta dinner (to hide the fact that Hepler and Quinn attended) and submitted it to BPS for payment. The fact that similar meetings were held with the key employees in other branches with the branch managers present indicates a pattern of using the branch managers to solicit, plan and organize the defections.

{232} H & E business records show that employee benefits information was requested for Mark Alexander on January 7, 2000, and that insurance networks were already in place for the Atlanta employees.

{233} Hepler subsequently arranged a meeting with Alexander in Savannah on January 20, 2000, at which time Hepler showed Alexander a detailed business plan for the Hi-Lift division that contained projections for all branches. Regarding the plan he reviewed with Hepler on January 20, Alexander testified: "[Hepler] and Doug [Kline] had put together a one-year-I believe a one-year, three-year, five-year growth plan and that the return on investment was very, very achievable. I asked to look at it. He showed it to me, pulled it out of his briefcase, and the numbers I saw were achievable in my opinion." Hepler denies showing Alexander a business plan that night and, when confronted at trial with Alexander's testimony, claimed that Alexander's recollection was inaccurate. Defendants did not call Alexander as a witness.

{234} Hepler assured Alexander on January 20 that the necessary capital was available for the H & E start-up. With respect to capital, Hepler explained to Alexander "that it was all arranged, that not all of it was one hundred percent secured yet and some of that was contingent upon the fact the we come out-*that Hi-Lift come out of the box pretty strong.* But that he was confident that that wasn't going to be a problem." (Emphasis added.) That evidence confirms at least the need for swift conversion of the necessary BPS employee base.

{235} At the Savannah meeting, Hepler offered Alexander a job as the Atlanta branch manager, which Alexander accepted at that time. Alexander's salary would increase from $103,500 at BPS to $105,000 at H & E, and he also received a $25,000 signing bonus. Alexander assured Hepler that he could hire the necessary people for the branch. When asked at deposition who he had in mind that night to recruit, Alexander immediately responded with eleven names, all of whom he hired from BPS for the Atlanta startup.

{236} The next day, January 21, 2000, Alexander resigned from BPS and immediately spoke with Brown about his resignation. Alexander used Brown as an inside source to set up meetings and solicit BPS employees. Brown expressed to at least one BPS employee (Galvond) his intent to harm BPS by gutting the BPS branch to the ground. Brown not only solicited BPS employees on behalf of H & E he also, while still employed by BPS, encouraged at least one BPS employee to take confidential BPS files and information home with him in anticipation of leaving BPS to work for H & E. Brown also indicated to Galvond that his reason for taking his BPS laptop computer home with him each night was for the purpose of compiling confidential BPS information for use at H & E.

***46** {237} Alexander arranged a lunch with Brown on February 8, 2000, prior to Brown's resignation from BPS. At this lunch Brown showed Alexander a list of BPS employees Brown wanted to recruit from BPS to work for H & E. Brown told Alexander at this lunch that the instability at BPS caused by Alexander's resignation would help his efforts to recruit BPS employees for H & E. Alexander testified in deposition that it would be improper for Brown to recruit BPS employees for H & E while still employed at BPS.

{238} While still employed by BPS, Alexander spent time with Doug and Delores Kline trying to locate a facility for H & E to open its Atlanta branch. A factor Alexander considered in locating a facility for H & E was to find a location that would make it easier to recruit BPS employees.

{239} When Brown began his employment with H & E, he told Alexander that he had already been in contact with several BPS employees he was recruiting for H & E and undertook the role of overseeing recruitment of employees for H & E. Alexander gave him authority to make employment offers on behalf of H & E.

{240} Between late February and early April 2000, at least 13 more BPS employees solicited by Alexander and Brown left BPS and began work with H & E. On opening day, every employee of H & E's Atlanta branch had been hired from BPS.

{241} The H & E branch in Atlanta was virtually identical to the former BPS Atlanta branch with respect to its employees, customer base and structure. In addition to all employees being former BPS employees, employees' responsibilities at H & E were virtually the same as at BPS. Former salesmen were assigned the same territories at H & E that they had at BPS, called on BPS customers and based pricing on information and experience acquired at BPS. In effect, H & E's Atlanta branch operated as the former BPS branch-used the *same* employees to conduct the *same* business with the *same* customers.

{242} Only ninety days after Hepler and Kline departed from BPS, on or about March 23, 2000, H & E opened a greenfield branch in Atlanta, where it previously had no operations, with all the necessary employees to sell, service and deliver equipment.

{243} In building a fleet for H & E's Atlanta branch, Quinn placed orders based on information and knowledge acquired at BPS concerning the Atlanta market instead of conducting market studies and evaluations, a process that Hepler testified is necessary for any greenfield operation.

{244} Cornett testified in deposition that he covers the same territory for H & E that he covered for BPS and is still using his BPS customer list at H & E. Cornett admitted that he likely called on BPS's biggest customers first, with no pricing information or marketing materials from H & E. Alexander admitted that he did not establish rental rates for H & E's Atlanta branch until July 2000, four months after the branch opened. Prior to that point, salesmen priced equipment based on past experience, with no guidance from H & E. When Leavell began his employment with H & E, there were no meetings in which the sales staff discussed rental rates, sales strategy or marketing strategy-Alexander simply instructed the salesmen to go do their jobs. Leavell took with him to H & E, however, notes that he had taken at BPS regarding BPS customers, including contacts.

***47** {245} Further evidence that H & E's Atlanta branch as well as other AWP branches operated as the former BPS branch is a June 12, 2000 H & E memo from Mark Alexander to "All branch managers," copied to Defendants Kline, Quinn and Christensen, in which Alexander, stated:

> Last Tuesday I had a meeting with Jeff Farmer with MLS & Assoc. I know the entire former BPS crowd remembers that MLS was our printing supplier for many years.... The good news for us is that ... [MLS] has all of the marketing brochures we ever produced and none of this is copyrighted or trademarked.... Jeff and I have another meeting tomorrow at which time he is going to bring the first draft of the monthly order form we were receiving every month from MLS. By the end of the week you should be receiving this form by fax at your branch.

{246} The loss of its branch manager and key personnel to H & E in such a short period of time caused turmoil in the BPS Atlanta branch. BPS was forced to bring in personnel from other branches in order to deal with the situation; they were unable to respond to customer needs and requests in a timely fashion; the condition of equipment in the yard suffered; and customers began calling BPS equipment off rent at a high rate. As a result, BPS lost a significant amount of business, and the volume of equipment being rented slowed considerably because BPS lacked qualified people to rent it, lacked qualified people to repair it, and lacked qualified people to deliver it.

{247} Despite being a greenfield operation in a market in which H & E previously had no presence, the H & E start-up branch in Atlanta did not struggle but was profitable by July 2000, exceeding the budgets that had been set for it by year-end. Reflecting the existence of and execution of the Plan, while Sunbelt's revenue at the Atlanta branch from the BPS customers was dropping dramatically (often to zero), H & E's revenue from these same customers rose from zero to hundreds of thousands of dollars.

H & E Today

{248} As the result of the employment activity by Defendants Hi-Lift, Hepler, Kline, Quinn and Christensen, Hi-Lift is substantially different today than H & E's aerial work platform division was as of December 31, 1999. Not only was the H & E AWP fleet aging, it had not been very productive for H & E. As of December 31, 1999, H & E's AWP fleet had only generated rental revenue of $7.2 million, a gross profit of only $2.5 million and a pre-tax loss of $289,000. The results of H & E's employment of Hepler, Kline, Christensen and Quinn and their conspiratorial activities, were that Hi-Lift realized $23.4 million dollars in rentals by December 31, 2000, a gross profit of $16.9 million and a pre-tax profit of $3.4 million. This profit occurred notwithstanding that two of the branches in the Hi-Lift division did not open until the middle of March 2000, followed by two more in May and one in June. Thus, through the opening of branches where Hi-Lift had no prior presence and the employment of BPS personnel at those branches and the "struggling" branches which H & E operated in Texas, Hi-Lift achieved over three times the rental revenues it previously had and turned a loss into a substantial profit. The turnaround totaled $3.7 million in one year.

***48** {249} Even more remarkable is the speed at which Hi-Lift achieved profit before taxes (and before corporate allocations) and exceeded budget/projections. By July 14, 2000, Defendant Kline reported that Hi-Lift had $153,000 profit before taxes in June (before corporate allocations) and had exceeded the budget/projection for the time-frame. Further, Kline reported that Charlotte utilization, which was at 58 percent, was not alarming because of Hi-Lift's expectation that the "Corning job would utilize most of the remaining equipment very shortly."

{250} Similarly, a month later, Kline further reported that the Hi-Lift division had achieved $613,000 in profit before taxes (and before corporate allocations) and that "all branches were profitable in July." As significantly, as Kline had reported in June, utilization by branch and across the entire fleet was extraordinarily high. By July 26, the Charlotte fleet, six weeks after opening, was at a 74 percent utilization level and quickly moved to 80 percent. Hi-Lift had 2,746 units in the fleet as of August 9th and a 79 percent utilization for the entire fleet.

{251} Hi-Lift rentals increased by $30.8 million, or 130 percent, to $55.4 million in fiscal year 2001 over fiscal year 2000. Thus, in fiscal year 2001, Hi-Lift had almost eight times the revenue it had as of December 31, 1999. As stated by an industry expert, such results are "astounding." Moreover, the Court finds that these results confirm a number of points including:

(a) The mass departures severely injured Sunbelt, a result that could only have been intended by defendants or the product of callous disregard for the consequences.

(b) Sunbelt/BPS confidential business information was used by defendants; otherwise, their personnel could not have been assembled so much business so quickly and efficiently.

(c) Sunbelt's expected repeat business was quickly and effectively appropriated by defendants.

(d) Defendants' activities were unfair, unethical and anticompetitive.

(e) The actions resulted in a dramatic $3.7 million turnaround in performance in one year.

II.

CONCLUSIONS OF LAW

{252} Truth matters.

{253} To the extent there may have developed in the business community a sense that in business litigation it is acceptable to render less than truthful testimony, that trend is one which must be reversed. The primary business of the courts is ascertaining the truth. Those who impede that work by providing less than complete, honest testimony should not be surprised to find their conduct unrewarded by the legal system. Every witness who takes an oath is compelled to tell the truth, the whole truth and nothing but the truth. Those who fail to honor that oath leave all their credibility on the courthouse steps. A healthy economic system requires a strong legal system that permits, promotes and protects fair competition while prohibiting and punishing conduct that threatens the vitality of that competitive system. Finding the truth is an essential part of the work of our legal system. Every witness is compelled to cooperate fully and truthfully in that search.

***49** {254} The Court, as Finder of Fact, had the opportunity to judge the testimony of the live witnesses firsthand. That is significant in this case where the testimony of defendants and the inferences to be drawn from their actions are in conflict. Defendants chose not to present live testimony from Defendants Kline, Christensen, Quinn and Pearsall, nor did branch managers Jones, Drennan and Alexander appear live. The Court has reviewed their proffered deposition testimony. The Court finds credibility issues as to defendants' witnesses with respect to two key subject areas: the existence of a plan to raid BPS at its key branches in an orchestrated manner and the use of the branch managers to do so. In both subject areas, the uncontroverted actions speak louder than words of denial. On numerous occasions, Mr. Hepler's testimony was contradicted by his own employees, his own documents or the credible testimony of others.

{255} Sunbelt has the burden on each of its claims of proving by "the greater weight of the evidence" that defendants' actions caused the damages that Sunbelt claims were the result of the massive departure of its employees and consequent conversion of customers and trade secrets. Sunbelt need not have a particular quantity of evidence in order to prove its claims; it must simply show that, considering all of the evidence, the facts necessary to find in its favor are more likely than not to exist. *See, e.g.,* *Joyner v. Garrett,* 279 N.C. 226, 236, 182 S.E.2d 553, 560 (1971) (holding that the law relating to burden of proof is equally applicable to jury and non-jury trials).

{256} As a general matter, the Court notes that the failure of four defendants, and a number of H & E employees who figure prominently in defendants' plan and conspiracy, to testify at trial in a civil matter is a "pregnant circumstance" for the Court to consider. *Jacobs v. Locklear,* 65 N.C.App. 147, 150, 308 S.E.2d 748, 750 (1983); *see also* *Ledford v. Emerson,* 141 N.C. 596, 54 S .E. 433 (1906) (finding that failure of defendant to testify was legitimate subject of comment before the jury); *Allred v. Demuth,* 890 S.W.2d 578, 581 (Ark.1994) (holding that failure to testify gives rise to presumption that the testimony would have been against the party's interest); *Keith v. Burlington Northern Railroad Co.,* 889 S.W.2d 911, 918 (Mo.Ct.App.1995) (permitting an unfavorable inference against party who fails to testify).

{257} In this case, considering the totality of the evidence, the Court may and does draw an adverse inference from the fact that Defendants Kline, Christensen, Quinn, Pearsall (who sat through several days of testimony in this Court), and other prominent H & E employees failed to testify at trial. However, that adverse inference was but one factor considered by the Court in reaching its decision, which would have been the same without the inference.

{258} Because the law makes no distinction between the weight to be given to either direct or circumstantial evidence, and no greater degree of certainty is required of circumstantial rather than direct evidence, the Court has also afforded equal weight to direct and circumstantial evidence presented at trial and through depositions and exhibits. *See, e.g.,* N.C.P.I.-Civil 101; *Patton v. Dail,* 252 N.C. 425, 428, 114 S.E.2d 87, 90 (1960) (holding that a fact in controversy may be established by circumstantial evidence); *Byrd's Lawn & Landscaping, Inc. v. Smith,* 142 N.C.App. 371, 377, 542 S.E.2d 689, 693 (2001) (finding that circumstantial evidence was sufficient to support finding of trade secret misappropriation).

***50** {259} Additionally, certain behaviors which may be benign or innocuous when standing alone, but which acquire a different meaning when placed in a larger context, may allow the Court, in light of the totality of the facts and circumstances, to reasonably infer that illegal conduct occurred in this case. *See Terry's Floor Fashions, Inc. v. Burlington Indus., Inc.,* 568 F.Supp. 205, 210 (E .D.N.C.1983).

{260} In summary, the Court finds that the tortious interference claims are subsumed in the U.D.T.P.A. claim, and that defendants (1) violated N.C.G.S. § 75-1.1, (2) misappropriated trade secrets, and (3) committed civil conspiracy. Damages for tortious interference, misappropriation, and civil conspiracy are subsumed under the U.D.T.P.A. damages. Plaintiff has been damaged by defendants' unfair and deceptive behavior in the amount of five million dollars; these damages are to be trebled under N.C.G.S. § 75-16.1.

U.D.T.P.A.

{261} To establish a violation of N.C.G.S. § 75-1.1, a plaintiff must show: (1) defendant committed an unfair or deceptive act or practice; (2) the action in question was in or affecting commerce; and (3) the act proximately caused injury to plaintiffs. *E.g., Dalton v. Camp,* 353 N.C. 647, 656, 548 S.E.2d 704, 711 (2001); *Becker v. Graber Builders, Inc.,* 149, N.C.App. 787, 794, 561 S.E.2d 905, 910 (2002). Plaintiff has fulfilled each of those requirements.

{262} Whether an act is unfair or deceptive is a question of law for the Court to determine. *Gray v. N.C. Ins. Underwriting Ass'n,* 352 N.C. 61, 68, 529 S.E.2d 676, 681 (2000).

{263} Although certain acts, standing alone, may evoke the action, a claim for unfair and deceptive trade practices pursuant to N.C.G.S. § 75-1.1 is an independent claim that stands alone as a distinct action and is not derivative. *See, e.g., Bhatti v. Buckland,* 328 N.C. 240, 400 S.E.2d 440 (1991) (finding that proof of fraud alone would establish that unfair and deceptive trade practices have occurred, no finding of “substantial aggravating circumstances”); *The Country Club of Johnson County v. U.S. Fidelity & Guaranty Co.,* 150 N.C.App. 231, 563 S.E.2d 269 (2002) (noting that a claim under N.C.G.S. § 75-1.1 is independent of other claims and affirming judgment on claim of unfair and deceptive trade practices alone); *Drouillard v. Keister Williams Newspaper Services, Inc.,* 108 N.C.App. 169, 423 S.E.2d 324 (1992) (holding that if a violation of the North Carolina Trade Secrets Protection Act satisfies the three prong test, then it would be a violation of N.C.G.S. § 75-1.1), *appeal dismissed and review denied,* 333 N.C. 344, 427 S.E.2d 617 (1993); *Bernard v. Central Carolina Truck Sales,* 68 N.C.App. 228, 230, 314 S.E.2d 582, 584 (1984) (“As previously stated, an action for unfair and deceptive acts or practices is a distinct action [and] ... creates a cause of action broader than traditional common law actions....”).

***51** {264} Whether an act or practice is unfair is determined on a case-by-case basis, and “the fair or unfair nature of particular conduct is to be judged by viewing it against the background of actual human experience and by determining its intended and actual effects upon others.” *United Laboratories v. Kuykendall,* 102 N .C.App. 484, 491, 403 S.E.2d 104, 109 (citations omitted), *aff'g,* 335 N.C. 183, 437 S.E.2d 374 (1993); *see Johnson v. Phoenix Mut. Insurance,* 300 N.C. 247, 262-63, 266 S.E.2d 610, 621 (1980) (finding that whether a trade practice is unfair or deceptive depends on the facts of each case.).

{265} A practice is unfair when it offends established public policy as well as when the practice is immoral, unethical, oppressive, unscrupulous, or substantially injurious to consumers. Johnson v. Phoenix Mut. Ins., 300 N.C. 247, 266 S.E.2d 610. The U.D.T.P.A. is "directed toward maintaining ethical standards in dealings between persons engaged in business, and [intended] to promote good faith at all levels of commerce. Unfair methods of competition [...] would not promote good faith...." Kuykendall, 102 N.C.App. at 491, 403 S.E.2d at 109 (citations omitted).

{266} One method of determining if actions are unfair or unethical is to look at those actions through the lens of equity. Faced with an *ex ante* rather than *ex post* review of the actions, what would a court of equity do faced with a request for injunction? Would a court enjoin defendants from using a competitor's branch managers to secretly hire away the competitor's employees and orchestrate their departure in a manner designed to impair the competitor and benefit the defendants? *See, e.g., Global Telesystems, Inc., v. KPNQwest,* 151 F.Supp.2d 478 (2001) (S.D.N.Y.); *Thal v. Polumbaum,* 196 Misc. 897, 900, 96 N.Y.S.2d 226, 230 (1949); *The Monitor Stove Co. v. The Williamson Heater Co ., 18 Ohio App. 352 (1923)*. Surely a court would not *ex ante* condone such behavior. If so, it should find the same behavior *ex post* to be unfair and unethical.

{267} BPS/Sunbelt and Hi-Lift were in competition in the AWP rental business, and the conduct which the Court has found to violate the U.D.T.P.A. was in and affected commerce as required by the statute.

{268} The surreptitious and intentional use of BPS employees to solicit other key employees while both the soliciting and solicited employees were still employed by BPS is an unfair trade practice. Defendants' attempts to conceal their mendacious behavior have failed. Their lack of credibility on this issue is a factor for the Court to consider in determining whether their actions constituted unfair trade practices. It is precisely the conduct which the Court has found to be unfair that was the subject of defendants' untruthful testimony. Defendants' lack of candor with respect to the solicitation of other employees by Hepler and the branch managers while the branch managers were still employed by BPS demonstrates their belief that such conduct was legally and ethically unacceptable. Indeed, Mr. Engquist and others so testified.

***52** {269} Defendants admit that they gave no consideration to the impact of their actions on the BPS branches at issue. In addition, defendants have admitted that they were in a position to understand the dire consequences of their actions on the raided branches. John Engquist admitted that the behavior of a branch manager in soliciting employees who reported to him and telling them to leave immediately would be improper behavior. Rob Hepler likewise admitted that such conduct was unethical. Undermining the entire structure of a branch by secretly soliciting key employees at various levels of the organization to leave *en masse* to H & E with the inevitable consequence of crippling the branch, and then using the same employees to blitz BPS customers for business with H & E is not ethical competitive behavior. Building fully functional and profitable greenfield branches in a matter of days, rather than months, through orchestrated, *en masse,* secret recruitment efforts by key insiders is not ethical behavior in competition.

{270} Competitor A may not use existing management employees of Competitor B to secretly solicit *en masse* defections to Competitor A's business while those managers or key employees are still employed by Competitor B, particularly where Competitor A knows that the coordinated *en masse* defections will impair Competitor B's ability to function and provide at least a temporary competitive advantage to Competitor A in the marketplace. Competitor A could openly solicit any employee of Competitor B who was not bound by a contract containing a restrictive covenant so long as the new employee does not use confidential business information and trade secrets of Competitor B. The employee could be offered more money. There would be no limit on the number hired. Here it is the surreptitious recruitment of *en masse* defections timed to disrupt Competitor B's business and take advantage of the employees' knowledge of confidential business information which crosses over the line of fair competition.

{271} The Court also considered the deliberate acts of disruption committed by the departing employees as well as the derogatory comments made by the branch managers and other key employees. Further, the manipulation of the employee departures in the form of mass resignations was also unfair and calculated to handicap BPS in such a way that Hi-Lift could take competitive advantage of the situation it had unfairly created. It eliminated the opportunity for BPS to compete for the employees on a level playing field.

{272} The Court is not holding that Hi-Lift could not hire BPS employees, be they executives, branch managers, salesmen or mechanics. Had Hi-Lift opened a branch office prepared for business and then advertised for employees, any BPS employee could have been solicited and hired. Prior to opening a branch office, Hi-Lift could have advertised in trade publications that it was seeking experienced employees. Any BPS employee could have chosen to respond to that advertisement. Indeed, many BPS employees may have applied for employment with Hi-Lift. In its haste and its effort to take advantage of BPS before Sunbelt could close its purchase, Hi-Lift overstepped the bounds of ethical and fair competition.

***53** {273} An example of activity by Hi-Lift that would not fall into the category of unfair trade practice was the hiring of David Chapman. He ran the Charleston branch for BPS and was a friend of Hepler. He was hired away from BPS to run the Houston branch for Hi-Lift. He did not hire any Charleston employees and was contractually free to work wherever he desired. Hi-Lift did not commit any unfair trade practice by hiring him, and his hiring had no adverse impact on the Charleston branch other than the loss of his personal experience. Hi-Lift did not have a competing branch in Charleston.

{274} The appellate court decisions dealing with unfair competition and conversion of business and employees demonstrate an awareness that competition is healthy and not to be unduly discouraged. Those decisions also evidence a desire to permit employees the greatest freedom of movement in order to maximize their job opportunities. *See, e.g., Dalton,* 353 N.C. 647, 548 S . E.2d 704; *Hiatt v. Burlington Industries, Inc.,* 55 N.C.App. 523, 529, 286 S.E.2d 566, 569, *disc. rev. denied,* 305 N.C. 395, 290 S.E.2d 365 (1982); *Long v. Vertical Technologies, Inc.,* 115 N.C.App. 598, 439 S.E.2d 797 (1994); *Fletcher, Barnhardt & White, Inc. v. Matthews,* 100 N.C.App. 436, 397 S.E.2d 81(1990), *disc. rev. denied,* 328 N.C. 89, 402 S.E.2d 411(1991). Nothing in this opinion should be read to depart from the trends evident in those decisions. Hepler and Kline were free to compete fairly, and each employee of BPS/Sunbelt was free to work for the employer he or she selected. The surreptitious way in which the BPS employees were solicited may have actually deprived them of the opportunity to see what Sunbelt would offer them to stay. None of the converted employees had the right to use BPS/Sunbelt confidential business information, but they could use the experience and contacts they had gained from years in the AWP business.

{275} The manner in which the branch managers were used was deceptive. That deception prevented fair competition for both employees and customers. The deceptive, secretive nature of defendants' actions differentiates this case from others where courts have found the hiring of competitor's employees to be acceptable.

{276} In *Peoples Sec. Ins. Co. v. Hooks,* our Supreme Court affirmed the 12(b)(6) dismissal of plaintiff employer's claim that its former employee had unlawfully interfered with the employment contracts of other employees. 322 N.C. 216, 367 S.E.2d 647 (1988). After quitting, defendant employee hired away many of his co-workers and subsequently assigned them to develop the same territory as they had worked with the plaintiff. Our Supreme Court looked to other jurisdictions for the proposition that "[t]he free enterprise system demands that competing employers be allowed to vie for the services of the "best and brightest" employees without fear of subsequent litigation for tortious interference." *Id.* at 222, 367 S.E.2d at 651 (citing *McCluer v. Super Maid Cook-Ware Corp.,* 62 F.2d 426 (10th Cir.1932); *Vincent Horwitz Co. v. Cooper,* 352 Pa. 7, 41 A.2d 870 (1945); *Diodes, Inc. v. Franzen,* 260 Cal.App.2d 244, 67 Cal.Rptr. 19 (1968); *Coleman & Morris v. Pisciotta,* 107 N.Y.S.2d 715, 279 A.D. 656 (1951)).

***54** {277} The clearest differences between the *Hooks* case and the case before this Court are the timing, subterfuge, and wrongful purpose. In *United Lab. v. Kuykendall,* the North Carolina Supreme Court clarified its ruling in *Hooks.*

> [I]n a recent decision, [this Court] held that in some situations a competitor may hire an employer's former employees without being liable for tortious interference with contract. In *Hooks,* plaintiff's employees had terminable at will contracts with plaintiff, had signed covenants not to compete, and subsequently went to work for one of plaintiff's competitors. This Court held that hiring the competitor's former employees and assigning them to the same territory they had worked in their prior employment was not a tortious interference with contract. We held in *Hooks* that a claim for tortious interference with contract would not lie where a defendant had only "offered the plaintiff's employees job opportunities which induced them to terminate their terminable at will contracts and, by locating these employees in their previously assigned territories, induced them to breach the non-competition clauses contained in their contracts with the plaintiff." We concluded that the fact that the plaintiff and defendant were in competition was sufficient to justify the defendant "in offering the plaintiff's employees new jobs and locating them in their previously assigned territory." In *Hooks,* however, we also emphasized that " '[t]he privilege [to interfere] is conditional or qualified; that is it is lost if exercised for a wrong purpose. In general a wrong purpose

> exists where the act is done other than as a reasonable and *bona fide* attempt to protect the interests of the defendant which is involved.' "

322 N.C. at 662, 370 S.E.2d at 387 (internal citations omitted).

{278} Defendants would like to avail themselves of the notion that competition justifies their actions. *See Childress v. Abeles,* 240 N.C. 667, 84 S.E.2d 176 (1954). However, defendants should have used lawful means to pursue their ends. *See, e.g., id .; Hooks,* 322 N.C. 643, 370 S.E.2d 375.

{279} Based on the above findings of fact, and pursuant to North Carolina law, there is extensive evidence showing that the actions of defendants were unfair, unethical, and immoral; those actions proximately caused Sunbelt's injury; those actions were of and affecting commerce; and, thus, the Court finds that these actions constitute unfair trade practices or unfair methods of competition under N.C.G.S. § 75-1.1.

Tortious Interference

{280} The Court will not deal with the tortious interference claims separately, as each is subsumed in the holding of unfair competition. If an appellate court were to find that defendants' conduct was not barred as unfair competition, it would be difficult to find that it was "tortious interference" since there would have been a determination that the competitive actions were fair and protected.

Trade Secrets

***55** {281} The application of the law of misappropriation of trade secrets is difficult to apply in this case because of the nature of the industry, the vast experience of the BPS/Sunbelt employees hired away by Hi-Lift and the difficulty of proving specific use of the information. Here, the use of confidential business information by Hi-Lift would have been coextensive with the unfair competition that the Court has found to exist by virtue of the unlawful *en masse* appropriation of the employee base. The damages for misappropriation would be included in the unfair trade practice damages for all practical purposes. *See Drouillard,* 108 N.C.App. 169, 423 S.E.2d 324.

{282} Under the North Carolina Trade Secrets Protection Act ("Trade Secrets Act"),

> "Trade secret" means business or technical information, including but not limited to a formula, pattern, program, devise, compilation of information, method, technique, or process that:
>
> 1. Derives independent actual or potential commercial value from not being generally known or readily ascertainable through independent development or reverse engineering by persons who can obtain economic value from its disclosure or use; and
>
> 2. Is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

N.C.G.S. § 66-152 (2001).

{283} The factors which trial courts should apply in determining whether information is properly classified as a trade secret have been clearly enunciated by the appellate courts. The six primary factors are: (1) the extent to which the information is known outside the business, (2) the extent to which it is known inside the business, (3) the measures taken to guard the secrecy of the information, (4) the value of the information to the business and to the competitor, (5) the expenditure of time and money in developing the information and (6) the ease or difficulty with which the information could properly be acquired or duplicated by others. *See Byrd's,* 142 N.C.App. at 375, 542 S.E.2d at 692; *State ex rel. Utilities Comm'n v. MCI Telecommunications Corp.,* 132 N.C.App. 625, 634, 514 S.E.2d 276, 283 (1999); *Wilmington Star News, Inc. v. New Hanover Regional Medical Center,* 125 N.C.App. 174, 182, 480 S.E.2d 53, 57, *appeal dismissed,* 346 N.C. 557, 488 S.E.2d 826 (1997).

{284} Applying these factors in specific factual situations, our courts have found a variety of information to constitute a trade secret. *See Byrd's,* 142 N.C.App. at 371, 542 S.E.2d at 689 (cost history information); *Wilmington Star News Inc.,* 125 N.C.App. at 174, 480 S.E.2d at 53 (price lists); *Barr-Mullin Inc. v. Browning,* 108 N.C.App. 590, 424 S.E.2d 226 (1993) (computer software); *Drouillard,* 108 N.C.App. 169, 423 S.E.2d 324 (customer lists, pricing formulas and bidding formulas).

{285} Under the Trade Secrets Act, "misappropriation" is defined as the "acquisition, disclosure, or use of a trade secret of another without express or implied authority or consent, unless such trade secret was arrived at by independent development, reverse engineering, or was obtained from another person with a right to disclose the trade secret." N.C.G.S. § 66-152(1). Plaintiff bears the initial burden of showing a *prima facie* case of misappropriation by introducing substantial evidence that the defendant: "(1) knows or should have known of the trade secret; and (2) has had a specific opportunity to acquire it for disclosure or use or has acquired, disclosed, or used it without the express or implied consent or authority of the owner." N.C.G.S. § 66-155. There is no specific requirement that plaintiff show that defendants have disclosed or used the trade secrets, only that they had a specific opportunity to acquire the trade secrets for use or disclosure. Once plaintiff establishes a *prima facie* case, the burden shifts to defendants to show that the trade secret was acquired properly.

***56** {286} There is seldom direct evidence of the use of confidential business information. There is evidence in this record that some documents containing confidential information were removed from branch offices. Certainly, the defendants in this case had access to all of BPS's business information; they built the business. In this instance it may be more important to look at what was not done and the business results. There is no evidence of a unified pricing structure for Hi-Lift. Many salespeople testified that they did not have prices when they began calling on customers. There were no restrictions placed on the sales people concerning use of BPS information. The sales people began calling on the same customers within days of leaving BPS and in some cases went after business that was based on special pricing arrangements. Credit decisions had to be based upon knowledge obtained at BPS, as there is no evidence of the independent development of credit information for the customers called upon at the outset. Indeed, there is little evidence of the independent development of information by Hi-Lift that one would expect in a normal greenfield operation. As previously noted, there was an advantage to Hi-Lift to get the new Hi-Lift branches open in the BPS markets before Sunbelt could close its transaction. The rapidity with which the old BPS customers were identified, called upon and converted to Hi-Lift, despite the lack of business information and guidance from Hi-Lift management, provides strong circumstantial evidence that at least some of BPS confidential information was used to solicit customers.

{287} The evidence shows that the individual defendants knew BPS/Sunbelt's trade secrets and had access to them, and each had the opportunity to acquire them for disclosure and use. Prior to appropriating BPS employees, *en masse,* H & E had *no customers* in North Carolina, Georgia, or Florida. Despite this fact, the "new" H & E operations made a significant profit in their first year of operation-based on their taking of BPS/Sunbelt employees, trade secrets and customers-and the BPS branches experienced a concurrent, substantial decrease in business. This occurrence alone is circumstantial evidence of the defendants' use and disclosure of BPS trade secret information. *See, e.g., Byrd's,* 142 N.C.App. at 377, 542 S.E.2d at 693 (finding that evidence defendant acquired several of plaintiff's customer contracts after opening a competing business was "sufficient circumstantial evidence to sustain a finding that defendant knew of the confidential information, had the opportunity to acquire it for his own use and did so.") Here, testimony supports that Defendant Pearsall misappropriated confidential customer information of BPS-testimony that Pearsall never rebutted. In addition, testimony of witnesses located in Tampa/Fort Myers, Dallas and Atlanta supports that confidential customer information was misappropriated by BPS employees who left and went to H & E. Indeed, in Tampa, identical confidential pricing was used by Ms. Quasnick after she went to H & E, and in Dallas, Steve Mathews took sales notes with him, even though he was purportedly instructed not to do so by Christensen.

***57** {288} Based on the above the Court finds that (1) BPS/Sunbelt's compilation of information, including its special pricing information, customer information (identity, contacts and requirements of its rental customers), personnel and salary information, organizational structure, financial projections and forecasts, utilization rates, fleet mix by market, capital and branch budget information, and cost information, when taken together constitutes trade secrets and (2) that the defendants misappropriated BPS/Sunbelt's trade secret information unlawfully.

Civil Conspiracy

{289} A claim for civil conspiracy "requires the showing of an agreement between two or more persons to do an unlawful act or to do a lawful act in an unlawful way that results in damage to the claimant." *See, e.g., Dalton v. Camp,* 138 N.C.App. 201, 213, 531 S.E.2d 258, 266 (2000), *rev'd on other grounds,* 353 N.C. 647, 548 S.E.2d 704 (2001).

{290} Sunbelt must also show an "overt act' committed by at least one conspirator in furtherance of the conspiracy. *Id.* at 212, 531 S.E.2d at 267.

{291} Circumstantial evidence is sufficient, in many cases, to prove an action for conspiracy. *See, e.g., id.* at 214, 531 S .E.2d at 267.

{292} In this case, the evidence presented at trial shows more than a mere suspicion or conjecture of an overarching unlawful plan for *en masse* departures of BPS employees and customers, the use of trade secrets, and the consequent stifling of BPS/Sunbelt's ability to effectively compete with H & E in the early stages of H & E's entrance into the markets at issue. The considerable shift of BPS employees and customers to H & E within a very short time period, the almost "instant" H & E greenfield branches that sprung up, and the use of certain BPS confidential information constitutes significant circumstantial evidence that the "raid" of BPS was planned and agreed to long in advance of its actual implementation.

{293} Plaintiff has shown sufficient circumstantial and direct evidence of an overall plan by H & E and Hepler, Kline and the other individual defendants, to cripple or eliminate BPS/Sunbelt as a competitor in the AWP business in at least seven markets. Many of the actions against BPS by the individual defendants were taken while each was still employed there. The strikingly similar pattern of taking the human resources from the branches through a "pyramid" scheme and the "secret" meetings held with Sunbelt employees supports a finding that there was an agreement. These actions are unlawful and constitute a conspiracy in furtherance of the acts as described above.

{294} In light of the Court's findings of fact, and the laws of North Carolina with respect to civil conspiracy, the Court finds that defendants agreed among themselves, while most were still employed by BPS, to do a lawful act-to compete and solicit employees-in an unlawful way, and that defendants' actions have caused significant damages to the plaintiff.

U.D.T.P.A. Damages and Attorney Fees

***58** {295} The Court concludes that BPS was damaged by conduct that the Court has found to violate the U.D.T.P.A. statute. Such conduct includes unfair actions of defendants in using the BPS/Sunbelt branch managers and other BPS/Sunbelt employees to recruit others to leave BPS/Sunbelt in a coordinated departure to staff new offices of Hi-Lift.

{296} The amount of damages plaintiff has proven was proximately caused by defendants' unlawful actions. *See, e.g., Process Components, Inc. v. Baltimore Aircoil Co.,* 89 N.C.App. 649, 652, 366 S.E.2d 907, 910 (1988) (finding that where plaintiff proves damage, amount of damages is for jury to decide).

{297} Sunbelt must show that the amount of damages it seeks is based upon a standard that will allow the Court to calculate the amount of damages with reasonable certainty, although it is not required to prove them to a mathematical certainty. *McNamara v. Wilmington Mall Realty Corp,* 121 N.C.App. 400, 407, 466 S.E.2d 324, 329 (1996) (citing *Olivetti Corp. v. Ames Business Sys., Inc.,* 319 N.C. 534, 547, 356 S.E.2d 578, 586 (1987)); *see also Byrd's,* 142 N.C.App. at 377, 542 S.E.2d at 693 (finding that law requires that the evidence establish a basis for the assessment of damages with a fair degree of probability, but lost profits are to be evaluated on a case-by-case basis).

{298} Plaintiff is entitled to receive damages that are the natural and probable result of the defendant's illegal actions, but they need not be exact. *See Roane-Barker v. Southeastern Hospital Supply Corp.,* 99 N.C.App. 30, 40, 392 S.E.2d 663, 669 (1990). Indeed, the United States Supreme Court has said that:

> Where the [wrongful conduct] itself is of such a nature as to preclude the ascertainment of the amount of damages with certainty, it would be a perversion of fundamental principles of justice to deny al. relief to the injured person, and thereby relieve the wrongdoer from making any amend for his acts. In such case, while the damages may not be determined by mere speculation or guess, it will be enough if the evidence shows the extent of the damages as a matter of just and reasonable inference, although the result by only approximate. The wrongdoer is not entitled to complain that they cannot be measured with the exactness and precision that would be possible if the case, which he alone is responsible for making, were otherwise.

Story Parchment Co. v. Patterson Parchment Co., 282 U.S. 555 (1931).

{299} This is a unique fact situation unlikely to be replicated. It is factually distinguishable from *Dalton v. Camp* and other similar cases. *See, e.g., Combs & Assocs. v. Kennedy,* 147 N.C.App. 362, 555 S.E.2d 634 (2001); *Dalton,* 353 N.C. 647, 548 S.E.2d 704; *Fletcher, Barnhardt & White, Inc. v. Matthews,* 100 N.C.App. 436, 397 S.E.2d 81. Defendants' behavior was closer to that of the employees in *Long v. Vertical Technologies, Inc.,* 115 N.C.App. 598, 439 S.E.2d 797, than it was to the employee's behavior in *Dalton.*

***59** {300} In *Long,* an employer fired two employees after discovering those employees had founded two companies while employed. The employees did not fully disclose their use of the employer's property to further the business of their new companies. Plaintiff employees sued the employer for, *inter alia,* wrongful discharge. After a bench trial, the trial court found for the employer as to the wrongful discharge claim and the employer's counterclaim for breach of loyalty and fiduciary duty. When our Court of Appeals affirmed the trial court's judgment, it stated:

> Manifestly, when a servant becomes engaged in a business which necessarily renders him a competitor and rival of his master, no matter how much or how little time and attention he devotes to it, he has an interest against his duty. It would be monstrous to hold that the master is bound to retain the servant in his employment after he has thus voluntarily put himself in an attitude hostile to his master's interests. (Citations omitted.)

Long, 115 N.C.App. at 604, 439 S.E.2d at 802 (quoting *In re Burris,* 263 N.C. 793, 795, 140 S.E.2d 408, 410 (1965)).

{301} In the case before this Court, defendants deliberately used key inside managers to orchestrate a plan of conversion of employees that would have the known and desired impact of disrupting BPS/Sunbelt's operations in a way that would provide a competitive advantage for Hi-Lift as it jump-started its new branches. The evidence in this record shows that, pursuant to their unlawful plan, defendants used BPS's time, resources, and trade secrets while they were still employees of the plaintiff.

{302} One of the keys to profitability in the AWP business is reaching a critical mass of business that can support the overhead and maximize fleet usage. Hepler and Kline were well aware of the need to get to that critical mass quickly because BPS had commissioned a specific study which showed the critical usage and revenue points at its branches. They referenced that target point in their business projections. Slowly building business through the usual methods associated with greenfield operations would have meant a significant delay in reaching the revenue and usage targets necessary for profitability. The secret wholesale raid on the BPS/Sunbelt employee base using the branch managers was designed to and did minimize the time required to reach the critical mass and was a key component in defendants' plan. As a result, profitability was achieved at a rate far swifter than the industry norm. The rapid achievement of high levels of revenue also facilitated borrowing and negotiating with equipment suppliers. Those factors provided the motivation to secretly use the branch managers and others to carry out the plan to convert the employee base and customer business quickly and by surprise.

{303} The focus on hitting the key BPS branches before a new owner could take control and make efforts to retain the employees and customers explains the need to use the branch managers to pre-position the departures. Nowhere was that more evident than the last minute actions relating to the Charlotte branch which occurred just before the Sunbelt closing. It is a fair inference that Charlotte was left until last because Mr. Hepler had the most confidence in the commitment of his brother-in-law to make the changeover.

***60** {304} Plaintiff's damages are based in part on the incremental profits it lost as a result of defendants' unethical and unlawful conduct and in part on the expenses resulting from the mass departures orchestrated by defendants. It is also based in part on the benefit Hi-Lift received.

{305} BPS/Sunbelt was damaged by the conduct the Court has found to violate the unfair trade practices statute. That conduct took place in commerce. BPS/Sunbelt lost employees it may not have otherwise lost. As a result, BPS/Sunbelt incurred expense in hiring and training new employees. It lost efficiency in its operation and lost business as a result of the disruption to its business and the advantage created for Hi-

Lift by having the old BPS salesmen out soliciting business when BPS/Sunbelt had its sales force suddenly depleted. BPS/Sunbelt thus experienced a loss of efficient use of its fleet for a period of time until it could get trained sales people and trained mechanics and drivers who could service its accounts. BPS/Sunbelt lost business, incurred expenses and thus lost profits as a result of defendants' unfair conduct. The majority of the damage occurred at the Atlanta, Charlotte, Orlando and Fort Myers-Tampa branches. The impact of the unfair competition was minimal at the Texas branches but existed to some extent.

{306} If the actions of the branch managers were not taken with the intent of disrupting Sunbelt's business, they were taken with the knowledge and callous disregard of the harm they would cause. The Court finds the actions were intended to disrupt Sunbelt's business.

{307} Conversely, Hi-Lift derived a substantial benefit from its unfair conduct. It's acquisition of a trained work force eliminated training costs and a learning curve for new employees and produced a safer operation. It obtained market information in the presence of the sales force, customer contacts and relationships, information on customer credit history, current pricing information, current fleet mix information, and an instant "team" useful to the efficient operation of an AWP rental business.

{308} Because of defendants' unlawful actions, Hi-Lift was able to start greenfield operations at a significantly faster pace and to appropriate the short-term business customers of BPS/Sunbelt because of the disability created by the coordinated mass departures. Hi-Lift created a profit of approximately $3.4 million in its first year, a unique and remarkable result attributable in large part to the wholesale appropriation of key BPS/Sunbelt employees and the knowledge base they brought with them.

{309} The damages which were proximately caused by those actions included loss of trained employees, the cost of replacing those employees, loss of customers and business due to inefficient service resulting from the loss of staff, loss of efficient use of its fleet in the affected branches, and general business disruption.

{310} BPS/Sunbelt was a sufficiently large organization that it could and did replace the lost employees, and its new employees were trained and had the equipment and tools to compete with Hi-Lift in the long run. Hi-Lift was entitled to compete fairly with BPS/Sunbelt. The success that the management team had at BPS was a clear indication of their capability, and they had sufficient capital backing. In the long term, it was clear that Hepler and Kline would provide stiff competition. BPS could have protected itself against that competition but did not. Accordingly, the Court finds that the compensable damages are limited to the short-term period of time and expenses it took BPS /Sunbelt to compensate for the actions which the Court has found to be unfair. For most of the positions, six months was an adequate period of time to hire and train new employees and have them on the job with competitive capabilities. Many could be hired and trained quicker. At that point the companies were on a fair competitive basis and it would not be unexpected that Hi-Lift would take some market share from BPS/Sunbelt. Therefore the Court has not attributed all lost customers to unfair competition.

***61** {311} There has been significant evidence that many of defendants' rentals made in its "new" markets were made to the same customers and in the same geographic areas as plaintiff's rentals would have been. *See* Roane-Barker, 99 N.C.App. at 40, 392 S.E.2d at 670. Since it could compete lawfully, at least some of those sales would have been made in any event. Accordingly, the Court has not accepted in full the damage calculation proffered by plaintiff's expert.

{312} The clear prospect that Hi-Lift would have taken some market share from BPS in their overlapping markets combined with the overlap of unfair competition and trade secret misappropriation makes the damage assessment more complicated. As a matter of public policy, the Legislature has endorsed that concept that damages can be determined by actual loss to the plaintiff or unjust enrichment of the defendant in the case of misappropriation of trade secrets. *See* N.C.G.S. § 66-154. That policy is equally applicable where the unfair trade practice and misappropriation claims: (1) intermingle, (2) support both claims, and (3) cause damage. For that reason, the Court has considered the profit derived by Hi-Lift from its unusually rapid expansion and achievement of profitability in the first year in determining damages.

{313} The plaintiff has been damaged in the amount of five million dollars by the unfair trade practices of defendants. This is the amount to be trebled in this case; it is the amount the Court concludes represents the actual damages in this case directly flowing from the Chapter 75 violations, including the use of confidential business information. The damages are based upon the number of employees unfairly appropriated by Hi-Lift, their value and the disruption and expense their coordinated departures inflicted on BPS/Sunbelt, as well as the benefit received by Hi-Lift. The damages result from actions in the Atlanta, Charlotte, Orlando and Tampa-Fort Myers markets for the most part, with some smaller allocation for the Texas markets. The extent of the appropriation is set out above in the Findings of Fact. The damages resulted from the coordinated efforts of all the defendants which were part of an overall strategy designed to hit BPS/Sunbelt during the transition period before a transaction could be closed between Rentokil and Sunbelt and to convert customers quickly to take advantage of profitable fleet utilization.

{314} Plaintiff is also entitled to its attorney fees pursuant to N.C.G.S. § 75-16.1 and § 66-152, and to treble damages pursuant to N.C.G.S. § 75-16 to -16.1 ("the presiding judge may, in his discretion, allow a reasonable attorney fee to the duly licensed attorney representing the prevailing party ... upon a finding ... that: (1) The party charged with the violation has willfully engaged in the act or practice, and there was an unwarranted refusal by such party to fully resolve the matter which constitutes the basis of such suit ...."); § 66-152 ("if willful and malicious misappropriation exists, the court may award reasonable attorney fees to the prevailing party"); § 75-16 ("If any person shall be injured or the business of any ... corporation shall be broken up ... or injured by reason of any act or thing done by any other person, firm or corporation in violation of the provisions of this Chapter, ... if damages are assessed in such case judgment shall be rendered in favor of the plaintiff and against the defendant for treble the amount fixed by the verdict.").

Trade Secrets and Damages

***62** {315} The Court has also not dealt separately with the damages for theft of trade secrets. There are several reasons for that omission. First, while there is some direct evidence of the purloining of documents or other written confidential information, the reality is that Hi-Lift hired the people from BPS/Sunbelt who had the expertise to run an AWP business effectively and they hired the salesmen who knew the customers and the market. Pricing information was of fleeting long-term value as the market was intensely competitive. Short-term pricing or special account pricing was of more value. Most of the information about fleet usage was in the heads of the key management people hired away. They knew the essential needs to get up and running, and, if they did not, the salesmen who were hired knew the customer requirements. Undoubtedly there were instances in which Hi-Lift salesmen simply charged what they knew the customer was paying BPS/Sunbelt, but the customer was free to provide them with that information in any event.

{316} The damages resulting from the use of trade secrets also were subsumed in the damages the Court has found to flow from the unfair competition. It was the orchestrated and deceptive solicitation of the employees who possessed the key information and value that caused the damages. The information on utilization rates by market, average rental rates by market, and customer information, including credit worthiness, constituted information which one or more of the individuals hired by Hi-Lift carried in their heads and were a part of their work experience. The total usurpation of that knowledge base by unfairly using insiders created the specific liability and damage. The use of the branch managers and department heads to recruit other "A Team" players could only have been accomplished by the use of confidential information about their skills and pay levels. Each employee unfairly solicited by defendants brought with him or her a piece of the BPS information bank needed to convert the customer base to Hi-Lift, at least on a short-term basis. It is clear that defendants did not "independently develop" the information used when each branch was started. There is no evidence that market surveys, pricing trend analyses, trade information, employee interviews, advertisements for employees or upcoming construction work information was gathered by anyone at H & E in any of the new markets. Rather, all that information was readily available because of the orchestrated changeover of BPS employees to Hi-Lift.

Laches

{317} The Court must also examine the defendants' defense of laches, as presented in this case.

{318} The Court finds plaintiff's claims are not barred by laches.

{319} The doctrine of laches requires a showing that: (1) the petitioner negligently failed to assert an enforceable right within a reasonable period of time, and (2) the propounder of the doctrine was prejudiced by the delay in bringing the action. *Costin v. Shell,* 53 N.C.App. 117, 120, 280 S.E.2d 42, 44 (1981) (citing *Builders Supplies v. Gainey,* 282 N.C. 261, 192 S.E.2d 449 (1972); *Rape v. Lyerly,* 287 N.C. 601, 215 S.E.2d 737 (1975)).

***63** {320} Laches is an equitable defense and is not available in actions at law; therefore plaintiff's legal claims should not be barred by laches. *Coppersmith v. Upton,* 228 N.C. 545, 548, 46 S .E.2d 565, 566 (1948) (quoting *U.S. v. Mack,* 295 U.S. 480 (1935)) ("The doctrine of laches ... is ordinarily regarded as an equitable defense, and it has been held that the plea is not tenable in a court of law and on a legal demand, 'the court being governed by the statute of limitations.' ")

{321} Laches is an affirmative defense and the burden of proof is on the party who pleads it. *Taylor v. Raleigh,* 290 N.C. 608, 622, 227 S.E.2d 576, 584 (1976).

{322} The facts and evidence show that the effects of defendants' plan did not emerge until months after Hepler and Kline's departure.

{323} Plaintiff did not delay in initiating its lawsuit; it did so as soon as defendants' plans were clear and when Sunbelt took over at a closing of the purchase transaction. Defendants, fully aware of BPS's transitional period between execution of the contract and closing, took full advantage of it.

{324} Defendants cannot show that they were prejudiced by plaintiff's alleged delay in the initiation of the lawsuit.

{325} The statute of limitations applicable to a misappropriation of trade secrets claim is three years. N.C.G.S. § 66-157. Plaintiff commenced this action well before the expiration of this period. *See, e.g., Creech v. Creech,* 222 N.C. 656, 663, 24 S.E.2d 642, 647 (1943).

Counterclaims

{326} In its counterclaim, Defendant H & E has alleged among other things that Sunbelt "resented H & E's lawful success," "wanted to avoid having to compete with H & E for employees and customers," that "[Sunbelt's complaint] allegations are patently false," and that therefore this action is a "sham, filed solely for purposes of interfering with H & E's relationships with its employees, customers and vendors."

{327} H & E further alleges that Sunbelt, by filing a lawsuit, "unlawfully sought to intimidate, harass and scare smaller H & E into wasting its resources and ceasing to lawfully recruit and hire Sunbelt's employees, pursue customers and otherwise compete with Sunbelt."

{328} Defendant H & E's allegations in its counterclaims are not supported by the evidence. The findings of fact recited above are more than sufficient to justify the filing of a lawsuit. Moreover, Defendant H & E has not produced evidence that it was prevented from pursuing, recruiting and hiring Sunbelt's employees, pursuing customers and otherwise competing with Sunbelt. To the contrary, the significant evidence is that Defendant H & E in fact continued and continues to hire Sunbelt employees, has enjoyed remarkable success with customers and has been extraordinarily profitable in short order.

{329} The Court must also determine the fate of Defendant H & E's counterclaim against plaintiff, which alleges that the filing of this lawsuit by Sunbelt is a "sham," and was done solely for the purpose of interfering with H & E's relationships with its employees, customers and vendors in violation of N.C.G.S. § 75-1.1.

***64** {330} Initially, the Court notes that Sunbelt's claims are immunized by the *Noerr-Pennington* doctrine, which is derived from the First Amendment right to petition the government and immunizes legislative, executive and judicial activity from antitrust liability, even if the activity is designed to eliminate competition. *See, e.g., United Mine Workers of Am. v. Pennington,* 381 U.S. 657 (1965) (holding that exercising the right to seek redress from the courts is immune from claims under state and federal anti-competitive statutes alleging injury resulting from the mere prosecution of the lawsuit).

{331} Sunbelt has a constitutional right to seek judicial redress of its injuries. Sunbelt's allegations in the Complaint were well grounded in law and fact, and the evidence presented at trial has shown that defendants orchestrated mass resignations of managers and employees of BPS and diverted business to H & E's new offices using confidential and proprietary information of BPS. Sunbelt has stated valid claims and, as a matter of law, cannot be held liable under Chapter 75 for any incidental effects the lawsuit may have had on H & E Hi-Lift's business. *See, e.g., Static Control Components, Inc. v. Darkprint Imaging, Inc.,* 2001 WL 293661 (M.D.N.C., Feb. 9, 2001); *Merck & Co., Inc. v. Lyon,* 941 F.Supp. 1443, 1447 (M.D.N.C.1996); *Byrd's,* 142 N.C.App. 371, 542 S.E.2d 689.

{332} Therefore, in light of the findings of fact as set forth above, the Court concludes that Sunbelt brought this suit with the realistic expectation that its claims would succeed against the defendants, that the suit was "reasonably calculated to elicit a favorable outcome," and that therefore the suit is immunized under the *Noerr-Pennington* Doctrine. *See* *Baltimore Scrap Corp. v. The David Joseph Co.,* 237 F.3d 394 (4th Cir.2001) ("If an objective party can conclude that the suit is reasonably calculated to elicit a favorable outcome, the suit is immunized under *Noerr,* and an antitrust claim premised on the sham exception must fail.").

{333} Nevertheless, the *Noerr-Pennington* Doctrine does contain a "sham" exception, and, in order to determine whether Defendant H & E can succeed on its counterclaim, the Court must determine if it has met the two prongs of that exception: (1) whether H & E has shown that no reasonable litigant could realistically expect success on the merits of the claims involved here; and (2) whether H & E has shown that Sunbelt *subjectively* lacked a reasonable belief that it could succeed on the merits and brought this case for an improper or malicious purpose. *See* *Professional Real Estate Investors, Inc. v. Columbia Pictures Industries, Inc.,* 508 U.S. 49 (1993) ("*PRE* ").

{334} Defendants have presented no facts or evidence to show that Sunbelt subjectively believed the lawsuit was anything but a valid and legal claim for damages caused by the defendants. Certainly there has been no evidence that this lawsuit was brought for any improper purpose. *See also,* *United States v. Ward,* 618 F.Supp. 884 (E.D.N.C.1985) ("A party to a lawsuit has a right to use the procedures of the courts to advocate its position, even if such activities cause direct injuries to competitors.... Only actions undertaken without a genuine intent to influence the outcome of the dispute being adjudicated are a sham.")

***65** {335} Furthermore, defendants have not presented evidence showing that the lawsuit is objectively baseless, or a "sham." Sunbelt's evidence of H & E's wrongful actions has been detailed and specific. As set forth above in the Court's findings of fact, Sunbelt has shown sufficient evidence for the Court to find defendants liable to Sunbelt for damages on its claims. Therefore, it follows that Defendant H & E has shown no evidence that Sunbelt's allegations are objectively baseless. *PRE,* 508 U.S. at 60. As such, H & E's counterclaim must be dismissed.

{336} For the reasons set forth above, Defendant H & E's counterclaim fails and is therefore dismissed.

III.

CONCLUSION

{337} The Court concludes that the application of treble damages is appropriate in this case. It is necessary to prevent defendants and others from profiting from unfair practices. Defendants' actions were deliberate and taken to gain business advantage. Rather than compete in a fair manner, defendants orchestrated the clandestine raid of BPS by the branch managers while the sale to Sunbelt was still pending. The massive nature of the raid facilitated the achievement of the critical mass necessary for profitability. Defendants have benefited from their actions, establishing a viable and profitable business overnight. While they would likely have been successful in the long run, their unfair practices accelerated and enhanced their success. The imposition of treble damages where unfair actions are taken to maximize profits serves the specific purpose for which the treble damage provisions were enacted. The fact that defendants tried to hide their actions by providing less than truthful testimony has also contributed to the Court's decision.

{338} Final judgment will not be entered in this matter until any motion for attorney fees has been heard. Plaintiff will have thirty days from today's date to file a motion for attorney fees with supporting documentation, and defendants will have thirty days after service to respond. The Court will then enter a judgment.

All Citations

Not Reported in S.E.2d, 2003 WL 21017456, 2003 NCBC 4

Footnotes

[1] Bruckman, Rosser and Sherrill ("BRS") is an equity investment partnership.

[2] The sale of Plant Services is discussed more fully elsewhere in this opinion.

End of Document

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Only the Westlaw citation is currently available.

UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Superior Court of Connecticut,
Judicial District of Litchfield.

TORRINGTON RESEARCH CO.
v.
Michael D. MARVIN et al.

No. CV064005175.
|
April 6, 2010.

Attorneys and Law Firms

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Opinion

ROCHE, J.

***1** In this appraisal action, the court is asked to determine the "fair value" of certain shares of common stock pursuant General Statutes §§ 33–855(4) and 33–871.

PROCEDURAL HISTORY

On October 4, 2006, the plaintiff, Torrington Research Company (hereinafter the company), a closely held corporation, commenced this appraisal action against the defendants, Michael D. Marvin, Lee Newberg, Heidi Newberg and Nancy Lawson, by filing a petition with this court. In its petition, the company alleges the following. On April 8, 2006, and at all pertinent times, Heidi Newberg, Lee Newberg, Michael Marvin and Nancy Lawson owned 51,200, 51,200, 204,167 and 5000 shares of the company's common stock, respectively. The company notified its shareholders on April 8, 2006, of a meeting that was to be held on April 19, 2006, "for the purpose of considering and authorizing the company to sell substantially all" of its assets pursuant to a written asset purchase agreement with the Bergquist Torrington Company (hereinafter Bergquist), a wholly owned subsidiary of the Bergquist Company. In that notice, the company provided its opinion that the proposed action would give rise to appraisal rights. As a result, the defendants and at least two other parties gave notice of their intention to seek appraisal rights.[1] At the special meeting, the shareholders approved the sale of "substantially all" of the company's assets to Bergquist, and on April 21, 2006, the sale occurred. On approximately May 1, 2006, the company served each defendant with an appraisal notice, and on July 12, 2006, it paid the defendants a sum equal to its estimate of the fair value of each share of the common stock. The company estimated the fair value at one cent, and thus, Heidi Newberg, Lee Newberg, Michael Marvin and Nancy Lawson were paid $524 .80, $524.80, $2092.72 and $51.25, respectively. The company also provided the defendants with financial information when it paid out its estimation of the fair value of the common stock.

On July 24, 2006, the defendants gave notice of their "dissatisfaction with the amount of the payment, rejected the offer and demanded payment of their stated estimate of the fair value of the shares," which they allege is $1.75 per share. As of the date of the filing of this petition, the parties were unable to agree upon the fair value of the company's common stock.[2] Thus, pursuant to General Statutes § 33–871, the company instituted this action and petitioned the court to determine the fair value of the shares pursuant to General Statutes §§ 33–855 through 33–872 and to enter a judgment for the "amount, if any by which the court finds the fair value of the defendant shareholders' shares, plus interest, exceed[s] the amount" already paid to the defendants.

Pursuant to § 33–871(d), this case was tried to the court without a jury on September 16, September 17, September 18 and October 29, 2009.[3] At trial, the parties submitted numerous exhibits, and the court heard testimony from Peter Turner, James Plewacki, Roger Dickinson and Heidi Newberg.[4] Neither the company nor the defendants called expert witnesses to testify as to appropriate valuation methods. On November 20, 2009, and November 23, 2009, respectively, the company and the defendants filed proposed findings of fact and post-trial memoranda. On December 11, 2009, the defendants filed a reply to the company's proposed findings of fact and supporting memorandum, and on December 16, 2009, the court heard post-trial arguments.

DISCUSSION

I

APPLICABLE LEGAL STANDARDS

***2** In *Welsh v. Independent Bank & Trust Co., 1 Conn.App. 14, 467 A.2d 941 (1983)*, cert. denied, 192 Conn. 801, 470 A.2d 1218 (1984), the only appellate level case in Connecticut that discusses the fair value of stock in an appraisal action, the court noted: "The basic concept of value under the appraisal statute ... is that the stockholder is entitled to be paid for that which has been taken from him ... his proportionate interest in a *going concern.* This is the true or intrinsic value of this stock which has been taken by the merger ... In determining fair value, a court may rely on a legally recognized measure of value which is supported by the subordinate facts. No single method of valuation will control in all cases ... It is within the discretion of the trier of fact to select the most appropriate method of valuation under the facts properly found by him ... Valuation is a matter of fact to be determined by the trier's independent judgment of what is just compensation. Thus, valuation rests largely within the discretion of the lower court."[5] (Citations omitted; emphasis added; internal quotation marks omitted.) *Id., at 16–17, 467 A.2d 941*.

Although the Appellate Court decided Welsh before the legislature adopted the definition of fair value, in § 33–855(4), the current statutes provide discretion to the trier of fact as it determines fair value. Section 33–871 provides in relevant part: "(a) If a shareholder makes demand for payment under section 33–868 which remains unsettled, the corporation shall commence a proceeding within sixty days after receiving the payment demand and petition the court to determine the fair value of the shares and accrued interest ... (d) The jurisdiction of the court in which the proceeding is commenced ... is plenary and exclusive. The court may appoint one or more persons as appraisers to receive evidence and recommend a decision on the question of fair value. The appraisers shall have the powers described in the order appointing them, or in any amendment to it ... There shall be no right to a jury trial. (e) Each shareholder made a party to the proceeding is entitled to judgment (1) for the amount, if any, by which the court finds the fair value of the shareholder's shares, plus interest, exceeds the amount paid by the corporation to the shareholder for such shares, or (2) for the fair value, plus interest, of the shareholder's shares for which the corporation elected to withhold payment under section 33–867."

The applicable definition of fair value is found in § 33–855(4) and provides: "Fair value means the value of the corporation's shares determined: (A) Immediately before the effectuation of the corporate action to which the shareholder objects, (B) using customary and current valuation concepts and techniques generally employed for similar businesses in the context of the transaction requiring appraisal, and (C) without discounting for lack of marketability or minority status except, if appropriate, for amendments to the certificate of incorporation pursuant to subdivision (5) of subsection (a) of section 33–856." (Internal quotation marks omitted.)

***3** The Supreme Court has identified at least two valuation methods of closely held businesses in other contexts. "While there are several different methods by which to determine the value of a closely-held corporation, these methods, and their variants, are of two general types: (1) capitalization of earnings, or the net present value of a future income stream; and (2) net asset value, or the present sale price of the business assets less its liabilities ... While these alternate methods of valuation frequently yield different results ... they purport at least in theory to obtain the same object, i.e., the market value of the business. That different methods of valuation may yield different results, depending upon what exactly is being valued, does not mean that the results of the alternate methods can simply be summed to determine total value. One or the other, or the combined weighted average of each, will produce the best approximation of market value." (Citations omitted.) *West Haven Sound Development Corporation v. West Haven, 201 Conn. 305, 329–30, 514 A.2d 734 (1986)*.

Connecticut's definition of fair value is derived from the Model Business Corporation Act's definition of fair value, which was adopted in Public Acts 2001, No. 01–199, § 15. The act's official comments indicate that its drafters endorse similar, if not identical, valuation approaches to those recognized by the Supreme Court. The comments provide in relevant part: "[F]air value is to be determined immediately before the effectuation of the corporate action, rather than, as is the case under most state statutes that address this issue, the date of the shareholders' vote. This comports with the purpose of this chapter to preserve the shareholder's prior rights as a shareholder until the effective date of the corporate action, rather than leaving the shareholder in an ambiguous state with neither rights as a shareholder nor [perfected] appraisal rights. The corporation and, as relevant, its shares are valued as they exist immediately before the effectuation of the corporate action requiring appraisal. *Accordingly, [the definition of fair value] permits consideration of changes in the market price of the corporation's shares in anticipation of the transaction, to the extent such changes are relevant.* Similarly, in a two-step transaction culminating in a merger, the corporation is valued immediately before the second step merger, taking into account any interim changes in value ... The new formulation in paragraph ii [which corresponds with § 33–855(4)(B)], which is patterned on section 7.22 of the Principles of Corporate Governance promulgated by the American Law Institute, directs courts to keep the methodology chosen in appraisal proceedings consistent with evolving economic concepts ...

"Modern valuation methods will normally result in a range of values [rather than a] particular single value. When a transaction falls within that range, 'fair-value' has been established. *Absent unusual circumstances, it is expected that the consideration in an arm's length transaction will fall within the range of 'fair value '* ... Section 7.22 of the ALI Principles of Corporate Governance also provides that in situations that do not involve certain types of specified conflicts of interest, *the aggregate price accepted by the board of directors of the subject corporation should be presumed to represent the fair value of the corporation, or of the assets sold in the case of an asset sale unless the plaintiff can prove otherwise by clear and convincing evidence.* That presumption has not been included in the definition of fair value ... because the framework of defined types of conflict transactions which is a predicate for the ALI's presumption is not contained in the Model Act. *Nonetheless ... a court determining fair value should give great deference to the aggregate consideration accepted or approved by a disinterested board of directors for an appraisal-triggering transaction.*" (Internal quotation marks omitted; emphasis added.) Model Business Corporation Act (American Bar Association) § 13.01(4), official comment (2008).

II

THE PARTIES' ARGUMENTS

***4** The company argues, *inter alia,* that the definition of fair value in § 33–855(4) precludes the court from considering the value of any appreciation or depreciation arising out of the transaction to which the dissenting shareholders object. The company argues that the statute precludes any adjustment for appreciation or depreciation because the definition of fair value is based on the time period "immediately before" the transaction to which the dissenting or minority shareholders object, which, in this case, is Bergquist's purchase of substantially all of the plaintiff's assets. Moreover, the company argues, "value must be taken to mean what the shares would be worth if the proposed change in the corporation had not occurred." Thus, the dissenting shareholders are entitled to the fair value of their interest in the specific "going concern" that existed before the transaction to which they object and no more. Although the company recognizes that the court has broad discretion in choosing a valuation method, it notes that the following factors are generally considered appropriate when determining the fair value of shares: earnings record, earnings prospect, capitalization of its earnings, dividend record, rate of dividends, probability/likelihood of future earnings and dividends, accumulated surplus earnings, the "basic condition" of the corporation, the market value of its stock, reserves for contingencies and requirements for and availability of working capital, value of assets, book value, liabilities, net asset value and liquidation value.

Additionally, the company argues, a threshold issue for the court is whether it was a "going concern." Since Connecticut has adopted the "going concern" standard, the company argues that "those methods of valuation geared to valuing a going business rather than those geared to valuing assets and liabilities in a theoretical liquidation circumstance would seem most appropriate." Moreover, the company argues, it was not a "going concern" as of April 21, 2006, since evidence and testimony reveal that it was insolvent and without significant earnings, but for the asset sale with Bergquist. In fact, the company argues, it would have filed for bankruptcy if the asset sale had not occurred. Even if there is evidence to support the fact that the company was a "going concern," the company argues that the "generally accepted factors" used in going concern valuations "negate any claim that [the company] had a positive value."[6] Thus, if the court finds that the company was a "going concern," the company suggests that a "reliable factor" upon which the court may use to determine the fair value of the stock is "the price paid by [Bergquist] for substantially all of the assets of [the company] plus the value of the assets retained by [the company] less the total amount of liabilities that [the company] had on April 21, 2006."

In the defendants' post-trial memorandum, they also note that the trial court has the discretion to accept certain testimony and valuation methods. Regarding the company's case, the defendants note that the company failed to provide any expert opinion on valuation and instead relied on "self-serving testimony of 'insiders' who benefitted from the dilution of value in the asset sale to justify the penny a share valuation." In contrast, the defendants rely on "historical prices" to estimate the fair value of the stock. The defendants also rely on General Statutes § 33–900 to argue that the court may take wrongful conduct into account when determining "fair value." The defendants claim that the company cannot refute the historical trend of the stock prices and suggest that Peter Turner's testimony that the company would have filed for bankruptcy in lieu of the asset sale is nothing more than "rank speculation." The defendants also claim that the company chose to ignore over six million dollars in assets allegedly reported to the Internal Revenue Service in 2006, which it had before the asset sale. Moreover, the defendants claim that the one cent valuation is "simply unrealistic" because it suggests that the company "could be purchased in its entirety for less money at that value than the price paid for the assets actually sold." Additionally, the defendants claim, the company failed to produce evidence at trial to justify "why Bergquist would overpay so much for its assets," and there is "no objective evidence ... that the company faced bankruptcy in 2006 any more than it did in 2004, when it sold its shares for [sixty-five cents per share]."

***5** The defendants also characterize the company's bankruptcy claim as an "obvious and disingenuous attempt to distract the court from the fact that [the company] chose to structure a sales transaction that assured it lacked liquidity to pay the defendants 'fair value' for their shares after the asset sale, which explains the penny valuation." The defendants claim that the company had "no intention of raising sufficient funds to avoid the asset sale" as of January 2006, the company did not seek out buyers other than Bergquist, and the fair value of the stock was "diluted" as a result of "dealing with an insider like Bergquist beginning in 2005, as opposed to a neutral buyer in the open market place." The defendants argue that the company's officers let Bergquist control the terms of the asset sale because those officers would receive substantial benefits as a result of the sale, unlike the defendants. Although the defendants' assertion that the one cent valuation is inconsistent with the historical trend of the share prices, they argue that even if the company's internal balance sheet is accurate, there is no reasonable basis for the one cent valuation, which they claim is thirteen cents a share under the net asset valuation methodology.[7] The defendants also allege that the company's transaction with Bergquist "has all the indicia of a fraudulent transfer" under General Statutes § 52–552e.

In a post-trial rebuttal memorandum dated December 11, 2009, the company argues, *inter alia,* that there is no evidence to support claims that any alleged, "self-serving" transactions impacted the fair value of the stock. On December 15, 2009, the defendants filed a reply memorandum in which they argue, *inter alia,* that the company ignores central concepts of "fairness" and "equity" that are essential to Connecticut's appraisal right statutes. The defendants urge the court to reject the company's various accounting principles because those methods were not explained through expert witness testimony, which the defendants claim is required. The defendants note: "In essence, [the company] is asking this court to do what no court has done in the past twenty years; find that minority shareholders' stock had no value immediately before the asset sale where the majority shareholders reaped valuable hidden benefits in the transaction." The defendants urge the court to find that the fair value of the stock is not less than eight cents per share, before accounting for the company's alleged wrongful conduct.

III

CONCLUSIONS OF LAW & FINDINGS OF FACT

A

Going Concern

Based on the applicable legal standards, the court agrees with the company's conclusion that a threshold determination is whether the company was of a "going concern" immediately before the effectuation of the corporate action to which the defendants object. Given that the Supreme Court has recognized that a "going concern value ... has been sometimes used to broadly encompass all those factors which contribute to the value of the enterprise apart from its physical assets"; *Gray Line Bus Co. v. Greater Bridgeport Transit District,* 188 Conn. 417, 422, 449 A.2d 1036 (1982); the court concludes that the company was of a "going concern." This conclusion is based on various testimony adduced at trial. Peter Turner, who was involved in the asset sale, testified that the company was a "synergistic" counterpart to Bergquist and that Bergquist saw potential value in the company's developing technology, which is one of the reasons

Bergquist was interested in acquiring the company's assets. Specifically, Turner testified that "Bergquist had a strong interest in our technology ... because of the synergies of the two products. They had, prior to these discussions, made an investment in the company, because they liked the technology substantially." Additionally, Turner testified that "Bergquist, just like [the company's] officers and directors and employees, realized that there was a technology that had a lot of potential, but we had not been able to capitalize or commercialize that potential. Bergquist didn't know if they could capitalize on commercializing that potential, but they were willing to take that risk." James Plewacki testified that Bergquist was "purchasing the business ... with the assumption that we were going to run it forward as a going concern." Plewacki also testified that there may have been some "nominal value" in the company's patents, and that the licensing agreement that Bergquist had with the company, which dated back to August, 2005, "tapped the expertise of the [company's] employees." Finally, Plewacki responded affirmatively when asked whether the primary reason or asset that Bergquist was interested in was the company's key employees. All of this testimony collectively establishes that the company had value apart from its physical assets. As a result, the company was of a "going concern" immediately before the asset sale.

B

Fair Value

***6** Since the court has concluded that the company was of a "going concern," the next question is the appropriate valuation method and the fair value of the stock at issue. Both parties concede that the court has the discretion to choose the most appropriate valuation based on the facts found at trial. Although the parties spend a great deal of time arguing as to whether either side was required to put on expert testimony at trial, nothing in the applicable statutes requires either party to put on expert testimony. Moreover, although the company argues that the defendants have the burden of proving that the fair value of the stock is contrary to the company's determination, it does not advance binding legal authority to support such a conclusion. Furthermore, the applicable statutes do not support this theory. Accordingly, the court is left to determine the fair value of the stock based on the evidence and testimony submitted at trial and the facts found.[8]

At the outset, it is noted that regardless of the valuation method chosen, the court will not take §§ 33–900 and 52–552e into account in determining the fair value of stock in this appraisal action, despite the defendants' arguments otherwise. The defendants rely on these statutes to argue that the court should take the company's "wrongful conduct" into account when determining fair value. Appraisal actions are governed by §§ 33–855 through 33–872. Section 33–900 governs fair value in the context of a dissolution action, not an appraisal action. Moreover, that section does not include a definition of fair value, unlike the appraisal section of the General Statutes. Additionally, § 52–552e, which pertains to the Uniform Fraudulent Transfer Act, is also irrelevant in the present matter. The defendants presented minimal, if any, evidence from which the court can conclude that fraudulent activity was behind or implicated in the valuation or the asset sale. Aside from Heidi Newberg's testimony, during which she suggested that the company's valuation was suspect and questioned the motivations behind the asset sale, the defendants never presented documentation or any other evidence from which the court may find that self-dealing or fraudulent activity was involved in the company's valuation of its stock or the asset sale. Instead, the defendants discussed these concepts in their post-trial memoranda. The court will not infer fraud or self-dealing in the absence of credible evidence.

Even if the court refuses to find wrongful conduct in the company's assessment of fair value, this does not mean that the court must accept the company's conclusion as to the stock's fair value. As already noted by the parties, the court has the discretion to chose the most appropriate valuation based on the facts found in this case.[9] Thus, based on the following exhibits, as well as supporting Connecticut case law, the official comments to the Model Business Corporation Act and the parties' recognition of this valuation method, the court concludes that the "net asset value" method, or the sale price of the business assets less its liabilities, is the most appropriate valuation method in the present matter. In determining the company's "net asset value," the court relies on the following exhibits, which are probative: plaintiff's exhibit 1 (the February 8, 2006 letter from Bergquist to the company outlining the terms of the asset sale), plaintiff's exhibit 4 (the asset purchase agreement between the company and Bergquist), plaintiff's exhibit 9 (the July 12, 2006 letters from the company to the defendants), plaintiff's exhibit 20 (the company's income statement for periods ending December 31, 2004, December 31, 2005 and April 21, 2006;

the company's balance sheets for the same period; and a statement of changes in the shareholders' equity from January 1, 2005 through April 21, 2006), and the defendant's exhibit Y (the 2006 corporate tax return). Additionally, the court relies on I.R.S. form 8594, which is included in defendant's exhibit Y, in which the plaintiff asserts that the total value of the assets transferred from the company to Bergquist was $6,881,851. The court concludes that this sale price includes the value of the earnout provision in the asset purchase agreement. Moreover, the court relies on the balance sheet contained within the plaintiff's exhibit 9 (the July 12, 2006 letters from the company to the defendants) in which the company's total liabilities are stated at $6,306,411. It is undisputed that the number of outstanding shares of stock immediately before the sale to Bergquist was 6,838,531 shares. Thus, the asset value coincides with the sale price as indicated in I.R.S. Form 8594.

CONCLUSION

***7** As a result of these probative exhibits, the court concludes that the sale price ($6,881.851) of the company, less its liabilities ($6,306,411) before the sale date and divided by the number of outstanding shares (6,838,531) results in a per share price of $.084 dollars per share. Thus, the value of Heidi Newberg's 51,200 shares is $4300.80, the value of Lee Newberg's 51,200 shares is $4300.80, the value of Michael Marvin's 204,167 shares is $17,150.028 and the value of Nancy Lawson's 5000 shares is $420. See addendum. Finally, the court must include 8% statutory interest for each year, per General Statute § 37.1. The asset sale occurred on April 21, 2006, almost four years ago. As a result, this adds: $1376.29 in interest to Heidi Newberg's shares, bringing her total stock value to $5677.80; $1376.29 in interest to Lee Newberg's shares, bringing his total stock value to $5677.80; $5488.01 in interest to Michael Marvin's shares, bringing his total stock value to $22,638.04; and $134.40 to Nancy Lawson's shares, bringing her total stock value to $554.40. See addendum. It is noted that the company has already paid Heidi Newberg, Lee Newberg, Michael Marvin and Nancy Lawson, $524.80, $524.80, $2092.72 and $51.25, respectively. Thus, the fair value, as found here, must be reduced by these amounts. As a result, Heidi Newberg, Lee Newberg, Michael Marvin and Nancy Lawson are entitled to an additional $5152.29, $5152.29, $20,545.32 and $503.15, respectively.

So Ordered.

Addendum

Name	# Shares	@ $.084	8% Interest*	Total	Already Paid	Owed
H. Newberg	51,200	$4,300.80	$1376.29	$5,677.09	$524.80	$5,152.2 9
L. Newberg	51,200	$4,300.80	$1376.29	$5,677.09	$524.80	$5,152.2 9
M. Marvin	204,167	$17,150.0 28	$5488.01	$22,638.04	$2092.72	$20,545.32
N. Lawson	5000	$420	$134.40	$554.40	$51.25	$503.15

All Citations

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Footnotes

[1] The other parties were: 1) John Haller; and 2) the estate of Stephen Marks and Abbie Marks. The estate of Stephen Marks and Abbie Marks filed a timely withdrawal of its intention to exercise its appraisal rights. The company paid John Haller $358.60 for the fair value of his stock. Haller is not named as a defendant because he “has given no notice of dissatisfaction with the amount of payment received, not rejected the offer of July 12, 2006, nor demanded payment of any sum other than that tendered.”

[2] Specifically, the company alleges, the parties were unable to agree on the fair value of the stock immediately before "and independently of the sale of substantially all of its assets to [Bergquist]," thereby suggesting that the court should not take the Bergquist sale into account, in any way, in determining fair value.

[3] Section 33–871(d) provides in relevant part: "There shall be no right to a jury trial."

[4] Turner was called as a witness by both the company and the defendants. Turner testified that, at the time of trial, his only relationship with the company was as a shareholder. During the asset sale, however, Turner was the company's president, chief operating officer and chief financial officer. Turner left the company in 2008 and sold his shares for seventy-five cents per share. The company called Plewacki as a witness, and he testified that he is a senior vice president and the chief financial officer of Bergquist. The defendants called Dickinson as a witness, and he testified that he was the chief executive officer, chairman and one of the founding members of the company. The defendants also called Heidi Newberg, one of the defendants. Newberg testified that she never worked for the company or Bergquist and that she is employed as a professor of physics and astronomy. Newberg testified that she and the other defendants invested in the company because her brother, Russell Marvin, was the company's chief technology officer at one point in time.

[5] "[G]oing concern value, [is] a term which has sometimes been used broadly to encompass all those factors which contribute to the value of the enterprise apart from its physical assets." (Internal quotation marks omitted.) *Gray Line Bus Co. v. Greater Bridgeport Transit District,* 188 Conn. 417, 422, 449 A.2d 1036 (1982).

[6] Specifically, the company argues: 1) it had no earnings for the years preceding April 21, 2006; 2) there is no evidence that it ever paid a dividend to its shareholders; 3) since no dividend was paid, there is no evidence of a rate that can be utilized to establish any value; 4) actual earnings were less than the expenses incurred throughout the five-year period preceding April 21, 2006; 5) in the first quarter of 2006, the company was without the financial resources to raise capital, make payroll, pay rent or to fund the performance of its then outstanding contracts; 6) in the absence of actual positive earnings, there is no capitalization factor that, applied to positive earnings, can produce a positive value; 7) the likelihood of accumulated surplus earnings as of April 21, 2006, was negative if that likelihood was to be based on actual past earnings and dividends paid; 8) the accumulated surplus earnings for the company were negative between 2002, and December 31, 2005; 9) the company's ability to sustain its operation for the five-year period prior to April 21, 2005, was dependent upon its ability to obtain loans and equity investments, and the company was unable to raise any equity from its January 6, 2006 stock offering, which also precluded the company from borrowing; 10) the company's current liabilities exceeded its assets, and the company had no reserves for contingencies; and 11) the "basic condition" of the company from December 31, 2003 through April 21, 2006, was that it was on the verge of "going under," which the defendants allegedly concede.

[7] The defendants define the "net asset value" from Black's Law Dictionary, as "the market value of a share in a mutual fund, computed by deducting any liabilities of the fund from its total assets and dividing the difference by the number of outstanding fund shares." Black's Law Dictionary (9th Ed.2009).

[8] Although Connecticut courts have not addressed the burden of proof in appraisal actions, one Delaware court has noted that: "In a statutory appraisal proceeding, both sides have the burden of proving their respective valuation positions by a preponderance of the evidence ... If neither party satisfies its burden, however, the court must then use its own independent judgment to determine fair value." *Dobler v. Montgomery Cellular Holding Co., Inc.,* 2004 WL 2271592 (Del.Ch. Sept.30, 2004), aff'd, 880 A.2d 206 (Del.2005).

[9] It is interesting to note, however, that in their briefs, both the company and the defendants identify a valuation method that is akin to the Supreme Court's "net asset value." The company recognizes that "the market value of its stock ... [the] value of assets, [the] book value, liabilities, [and the] net asset value" are all factors that the court may consider in valuing the stock of a closely held business in an appraisal action. Additionally, the company suggests that a "reliable factor" upon which the court may use to determine the fair value of the stock is "the price paid by [Bergquist] for substantially all of the assets of [the company] plus the value of the assets retained by [the company] less the total amount of liabilities that [the company] had on April 21, 2006." Likewise, the defendants identify the "net asset value" method, as defined in Black's Law Dictionary, in their post-trial memorandum.

[*] The interest owed was calculated by multiplying the total amount of the shares at $.084 by 8% over four years (April 2006–April 2010).

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United States District Court, E.D. Virginia,
Richmond Division.

VIRGINIA POWER ENERGY
MARKETING, INC., Plaintiff,
v.
EQT ENERGY, LLC, Defendant.

Civil Action No. 3:11cv630
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|
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ORDER

Robert E. Payne, Senior Judge

***1** Having reviewed EQT ENERGY, LLC'S MOTION TO EXCLUDE OPINIONS OF GEORGE BRIDEN AND MEMORANDUM IN SUPPORT (Docket No. 36), the response and the reply briefs, and having reviewed the report at issue, the Court finds as follows:

(1) The report is difficult to analyze because it lumps together factual assertions and opinions;

(2) The last sentence of the first paragraph and the entirety of the second paragraph under the heading "*2. The LOI*" express opinions on the intent of the parties and that is an improper subject for expert opinion evidence;

(3) The first paragraph under the heading "*3. Opinions*" is argument and will not be helpful to the finder of the fact in deciding a fact in issue or in understanding the evidence;

(4) The second paragraph under the heading "*3. Opinions*" expresses opinions on the intent of the parties and that is an improper subject for expert opinion evidence;

(5) The third paragraph under the heading "*3. Opinions*" expresses the witnesses' opinions on matters as to which the jury needs no assistance and as to which the opinion does not help the finder of the fact determine a fact in issue or understand any of the other evidence;

(6) The fourth paragraph under the heading "*3. Opinions*" expresses an opinion on the issue of good faith and is not a proper subject for expert opinion evidence. Nor would such an opinion assist the finder of fact to determine a fact in issue or to understand the evidence;

(7) The fifth paragraph under the heading "*3. Opinions*" discusses what the parties were aware of and draws conclusions and essentially makes arguments and comments upon bad faith in a way that is impermissible; and, for the foregoing reasons, the opinions therein will not assist the finder of the fact to determine a fact in issue or to understand the evidence and, in addition, the opinions therein are not the proper subject for expert opinion evidence;

(8) The sixth paragraph under the heading "*3. Opinions*" comments upon the materiality of the 4¢ rate differential which is an appropriate subject for expert opinion evidence;

(9) The penultimate paragraph under the heading "*3. Opinions*" is a comment upon the opinion of another expert and is nothing more than vouching for the opinion of the other expert (Guy Davis) and therefore is not a proper subject for expert opinion evidence.

For the foregoing reasons, it is hereby ORDERED that EQT ENERGY, LLC'S MOTION TO EXCLUDE OPINIONS OF GEORGE BRIDEN is granted in part and denied in part. The last sentence of the first paragraph and the entire second paragraph of the "The LOI" section will be excluded. All of the opinions expressed in the "Opinions" section, with the exception of the opinion in paragraph six relating to the materiality of the rate differential, will be excluded.

It appears that the section entitled "*1. Background*" and the remainder of the first paragraph of the "LOI" section contain some information which may be pertinent to the understanding of the industry and, if properly circumscribed and presented in a non-advocacy manner, might be admissible as industry practice evidence.

***2** It is further ORDERED that the facts and legal contentions are adequately presented in the materials before the Court and oral argument would not aid the decisional process.

It is so ORDERED.

All Citations

Not Reported in Fed. Supp., 2012 WL 13034278

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