SUPPLEMENTAL MATERIALS

FOR

BUSINESS PLANNING FOR MERGERS AND ACQUISITIONS

(Fourth Edition, Carolina Academic Press 2015)

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Developments from January 1, 2015 through July 31, 2018
[To Be Updated Periodically]

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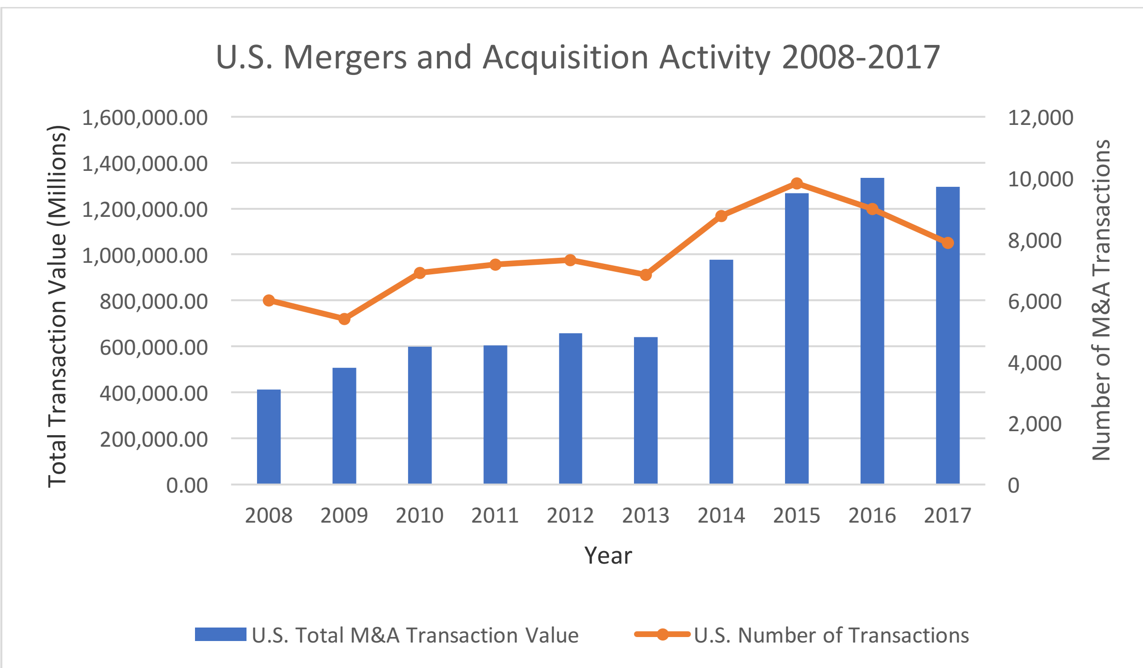
I. CHAPTER 1, INTRODUCTION

A. Pages 22 to 25, The Current M&A Scene: 2018

Pages 22 to 25, New Sec. 1.8. Replace Sec. 1.8, The Current M&A Scene with the following:
New Sec. 1.8. **The Current M&A Scene: 2018**

Graph 1-1 shows the state of play in the U.S. M&A marketplace from 2008 to 2017. There was a steady climb in both deal value and number of deals through 2015. However, in 2016 there was a drop in the number of deals, accompanied by a slight increase in value of deals. For 2017 there was a decrease in both the number of deals and the value of deals.

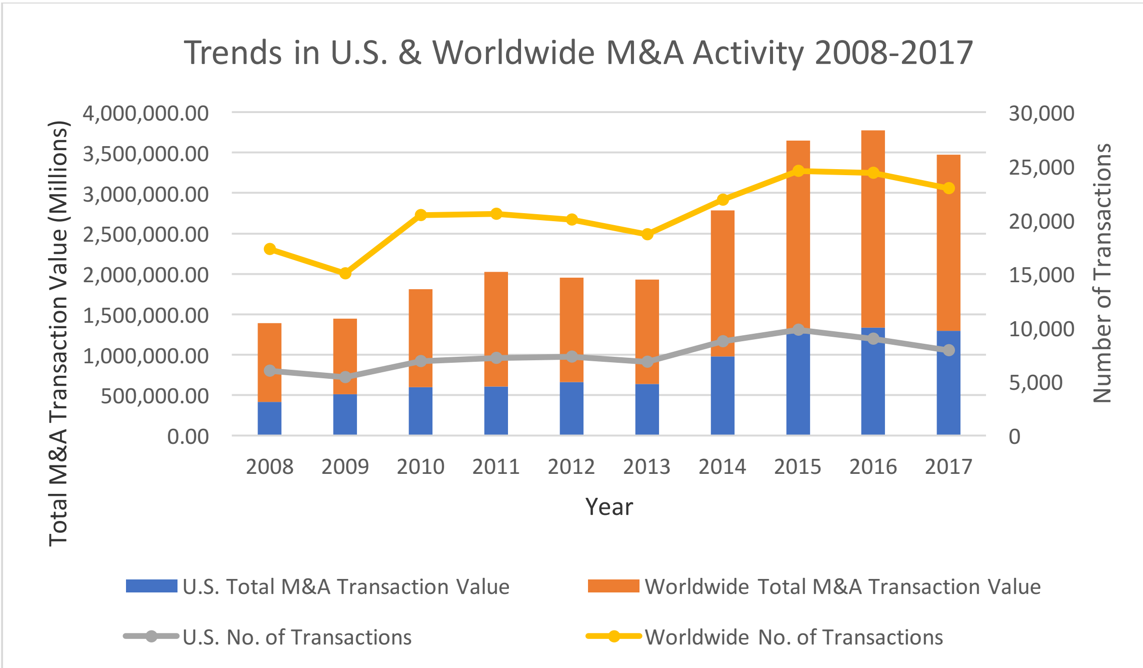
Graph 1-1



Source: Fact Set Idea Screening M&A Database, as of August 2018

A similar pattern is shown in Graph 1-2 with regard to worldwide M&A activity from 2008 through 2017.

GRAPH 1-2



Source: Fact Set Idea Screening M&A Database, as of August 2018

It would appear that the falloff from 2016 to 2017 was just a pause, for we seem to be back in a hot M&A market. For example, one July 2018 analysis of the market presents the following rosy picture for 2018:

> Multibillion dollar deals that will reshape the health-care and media industries have set 2018 on course to be the biggest year on record for global M&A. Now, after an unprecedented five years of bumper activity, dealmakers are starting to sound a note of caution.
>
> Companies announced $2.1 trillion of transactions in the first half of 2018, putting this year on track to beat 2007's $4.1 trillion total[.] * * * Twenty-four acquisitions valued at more than $10 billion bolstered the numbers, the data show, including Takeda Pharmaceutical Co.'s $62 billion purchase of Shire Plc and T-Mobile US Inc's $26.5 billion takeover of Sprint Corp.
>
> As the M&A juggernaut rolls on, some advisers are starting to ask how much longer the delirium can continue. Unlike the 2000 dot-com bubble or 2007's subprime-mortgage

crisis, though, this time there's no one clear threat looming. Instead, a myriad of warning signs are cited as potential hazards.[1]

The next update of chapter 1 will have a more complete analysis of recent developments in the M&A marketplace.

II. CHAPTER 2, VOTING AND DISSENTING IN MERGERS, ASSET ACQUISITIONS, AND COMPULSORY SHARE EXCHANGES

A. Page 50, New Sec. 2.10.Ea. Post 2015 Amendments to the Delaware General Corporation Law

Page 50, New Sec. 2.10.Ea. Add at the bottom of the page the following:
New Sec. 2.10.Ea. **Post 2015 Amendments to the Delaware General Corporation Law**

1. Introduction

Annually, the Corporate Council of the Corporation Law Section of the Delaware State Bar Association (Del Corp Council) proposes various amendments to the Delaware General Corporation Law. The Delaware legislature generally amends the DGCL in accordance with the proposals. A short "Synopsis" is attached to the proposals. This section sets out some of the parts of the post-2015 summaries addressing merger related provisions of the DGCL.

Whenever a client faces a corporate law issue, it is necessary for the attorney to be sure that he or she is focusing on the current statute; this is particularly true in Delaware, which generally has annual amendments to the DGCL and other business statutes.

2. The Del Corp Council's 2016 Proposed Changes to the DGCL Relating to Mergers

Section 7 amends Section 251(h) in several respects. It clarifies that Section 251(h) is applicable to a constituent corporation that has a class or series of stock that is listed on a national securities exchange or held of record by more than 2,000 holders immediately prior to the execution of the agreement of merger, even if not all classes or series of stock of such constituent corporation are so listed or held. Relatedly, Section 7 clarifies that the offer contemplated by paragraph (2) (the "Offer") may be effected through separate offers for separate classes or series of stock.

The amendments to Section 251(h) also clarify that the Offer may be conditioned on the tender of a minimum number or percentage of the shares of the stock of the constituent corporation, or of any class or series thereof.

Section 7 permits, for purposes of determining whether the requirement in paragraph (3) (the "Statutory Minimum Tender Condition") is satisfied, the inclusion of shares of stock of the constituent corporation held by any person that owns, directly or indirectly, all of the outstanding

[1] Nabila Ahmed, Ruth David and Aaron Kirchfeld, *Record M&A Activity Has Dealmakers Wondering How Long It'll Last*, Bloomberg BNA, Mergers & Acquisitions Law Report (July 16, 2018).

stock of the corporation making the Offer (the "Offeror"), or that is a direct or indirect wholly-owned subsidiary of such person or persons or of the Offeror (such owners and such subsidiaries, collectively, the "Offeror Affiliates"). Section 251(h), as amended, similarly permits shares of stock of the constituent corporation that are the subject of a written agreement requiring such shares to be transferred, contributed or delivered to the Offeror or any Offeror Affiliate in exchange for stock or other equity interests in the Offeror or any Offeror Affiliate to be counted for purposes of determining satisfaction of the Statutory Minimum Tender Condition, so long as such shares are in fact so transferred, contributed or delivered prior to the effective time of the merger (such shares in fact so transferred, contributed or delivered, "Rollover Stock").

Further, Section 7 provides that Rollover Stock and shares of the constituent corporation held by such constituent corporation in treasury, by any direct or indirect wholly-owned subsidiary of such constituent corporation, or by the Offer or Offeror Affiliates are excluded from the requirement that they be converted in the merger into, or into the right to receive, the same consideration paid in the Offer.

Finally, Section 7 clarifies the methods by which shares of stock of the constituent corporation may be "received" for purposes of the Statutory Minimum Tender Condition. With respect to certificated shares, such shares will be "received" upon physical receipt.

Section 8. The amendment to Section 262(c) is intended to clarify that where a provision of the certificate of incorporation confers appraisal rights where those rights otherwise do not exist, an appraisal proceeding must be dismissed under the new provisions of subsection (g) of Section 262, if applicable.

Section 9. The amendments to Section 262(d) conform to Section 251(h) as amended.

Section 10. The amendment to Section 262(g) limits the availability of a judicial determination and award of fair value where the corporation's shares had been traded on a national securities exchange. In that circumstance appraisal rights are essentially precluded unless the dispute with regard to valuation is substantial and involves little risk that the petition for appraisal will be used to achieve a settlement because of the nuisance value of discovery and other burdens of litigation. In a short-form merger under Section 253 or Section 267, however, there is no requirement of approval by the corporation's board of directors and therefore no obligation on the part of directors to approve and recommend the merger, and appraisal may be the only remedy. Accordingly, the limitation in new subsection (g) also is not applicable to mergers accomplished pursuant to Section 253 or Section 267.

[The amended section 262(g) reads as follows:

> If immediately before the merger or consolidation the shares of the class or series of stock of the constituent corporation as to which appraisal rights are available were listed on a national securities exchange, the Court shall dismiss the proceedings as to all holders of such shares who are otherwise entitled to appraisal rights unless (1) the total number of shares entitled to appraisal exceeds 1% of the outstanding shares of the class or series eligible for appraisal, (2) the value of the consideration provided in the merger or

consolidation for such total number of shares exceeds $1 million, or (3) the merger was approved pursuant to § 253 or § 267 of this title.]

Section 11. The amendment to Section 262(h) provides an option to the surviving corporation to pay to the stockholders seeking appraisal a sum of money, the amount of which is to be determined in the sole discretion of the surviving corporation, at any time before judgment is entered in the appraisal proceeding, with the result of avoiding the need to pay subsequently accruing interest on that sum. There 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. Where one or more stockholders' entitlement to appraisal is contested in good faith, the corporation may elect to pay such amount only to those stockholders whose entitlement to appraisal is uncontested.

3. The Del Corp Council's 2017 Proposed Changes to the DGCL Relating to Mergers

The amendments deal with, inter alia, the following matters: (1) The "Blockchain" or "Distributed Leger" Technology for Maintenance of Corporate Records, (2) Stockholder Consents under Section 228, (3) Merger Amendments, (4) Effective Time of Section 203 "Opt-Out," and (5) Annual Reports. Only the merger related amendments are discussed further here, and the Synopsis of these amendments provides:

Section 4. Sections 12 through 35 of this Act amend the provisions on mergers and consolidations in subchapter IX of chapter 1 of Title 8. Sections 254, 263 and 264 are amended to permit mergers of Delaware corporations with joint-stock or other associations, limited liability companies and partnerships formed or organized under the laws of a non-US jurisdiction. Sections 252, 253, 258 and 267 are amended to use the term "foreign corporation" (as such term is defined in Section 371(a)) to refer consistently to mergers with a corporation organized under the laws of any jurisdiction other than the State of Delaware. Sections 255 and 256 are amended to clarify how membership interests in a non-stock corporation may be treated in a merger and, as a result, redundant language to this effect in Section 257 is eliminated. All sections relating to mergers are amended to conform language to eliminate inconsistencies. The term "organized" is used with respect to corporations and refers to the method by which a corporation is formed, incorporated, created or otherwise comes into being under the laws governing its internal affairs. The term "formed" is used with respect to non-corporate entities and includes the method by which a non-corporate entity is formed, created or otherwise comes into being under the laws governing its internal affairs. Both terms are used with respect to joint stock associations given that the manner in which they are characterized may, depending upon the law at issue, include attributes of both "organized" and "formed". The clarification of the terms used to refer to corporations and non-corporate entities and the elimination of the term "existing" from Section 251 are for clarification purposes only and do not change the intent of such sections prior to the amendments. Each of the statutes on mergers and consolidations involving Delaware corporations and non-Delaware entities are amended to provide that such mergers and consolidations are permitted so long as the laws of the applicable non-Delaware jurisdictions do not prohibit the transaction. These amendments change provisions of Sections 252, 253, 256 and 258 that permitted these mergers and consolidations under Delaware law only if the applicable non-Delaware law "permitted" the transaction and change the language of Sections 254, 263, 264 and 267 from not "forbid" to not "prohibit". The amendments are intended to further facilitate mergers and consolidations of Delaware corporations with non-Delaware entities.

4. The Del Corp Council's 2018 Proposed Changes to the DGCL Relating to Mergers

Section 4. Sections 9 and 10 of this Act amend Section 262. The amendments to Section 262(b) will apply the "market out" exception to the availability of statutory appraisal rights to "intermediate form" mergers effected pursuant to Section 251(h). As currently drafted, Section 262(b)(3) provides that, if all of the stock of a subsidiary Delaware corporation party to a merger effected pursuant to Section 251(h) are not owned by the parent immediately prior to the merger, appraisal rights will be available for the shares of the subsidiary Delaware corporation, whether or not the market out exception would otherwise apply to an analogous "long form" merger, effectively ensuring that the market out exception will not be available to any exchange offer effected pursuant to Section 251(h). As amended, Section 262(b) will provide that, in the case of a merger pursuant to Section 251(h), appraisal rights will not be available for the shares of any class or series of stock of a target corporation that were listed on a national securities exchange or held of record by more than 2,000 holders as of immediately prior to the execution of the agreement of merger, so long as such holders are not required to accept for their shares anything except (i) stock of the surviving corporation (or depository receipts in respect thereof), (ii) stock of any other corporation (or depository receipts in respect thereof) that at the effective time of the merger will be listed on a national securities exchange or held of record by more than 2,000 holders, (iii) cash in lieu of fractional shares or fractional depository receipts in respect of the foregoing, or (iv) any combination of the foregoing shares of stock, depository receipts and cash in lieu of fractional shares or fractional depository receipts.

The changes to Section 262(e) effect a technical clarifying change with respect to the statement required to be furnished by the surviving corporation thereunder. Currently, Section 262(e) requires the surviving corporation to provide, upon request and subject to specified conditions, a statement to dissenting stockholders setting forth the aggregate number of shares that were not voted in favor of the merger or consolidation and as to which demands for appraisal have been received, and the aggregate number of holders of such shares. The changes to Section 262(e) give recognition to the fact that, in the case of a merger effected pursuant to Section 251(h), no shares are "voted" for the adoption of the agreement of merger. Instead, if a requisite number of shares of a target corporation are tendered for purchase or exchange in a tender offer satisfying the requirements of Section 251(h), the merger of the target corporation may be effected without a vote of its stockholders. The amendment to Section 262(e) thus clarifies that the statement provided pursuant thereto in connection with a merger effected under Section 251(h) must set forth the relevant shares not tendered for exchange or purchase rather than the shares not voted for the 346 merger.

B. Page 57, New Sec. 2.10.Ia. Delaware Supreme Court's August 2017 Appraisal Decision in *DFC*

Page 57, New Sec. 2.10.Ia. Add before Section J the following:
New Sec. 2.10.Ia. **Delaware Supreme Court's August 2017 Appraisal Decision in *DFC: The Impact of Deal Price***

DFC Global Corp. v. Muirfield Value Partners, L.P.
Delaware Supreme Court, 2017**,** 172 A. 3d 346
[This is a long and complex decision and this is principally the court's introduction.]

Opinion
STRINE, Chief Justice:
In this appraisal proceeding involving a publicly traded payday lending firm purchased by a private equity firm, the respondent argues that we should establish, by judicial gloss, a presumption that in certain cases involving arm's-length mergers, the price of the transaction giving rise to appraisal rights is the best estimate of fair value. We decline to engage in that act of creation, which in our view has no basis in the statutory text, which gives the Court of Chancery in the first instance the discretion to "determine the fair value of the shares" by taking into account "all relevant factors." As this Court previously held in Golden Telecom, Inc. v. Global GT LP, that language is broad, and until the General Assembly wishes to narrow the prism through which the Court of Chancery looks at appraisal value in specific classes of mergers, this Court must give deference to the Court of Chancery if its determination of fair value has a reasonable basis in the record and in accepted financial principles relevant to determining the value of corporations and their stock.

On the record before us, however, the respondent has made two convincing case-specific arguments why the Court of Chancery's determination of fair value cannot be sustained on appeal. For starters, the respondent notes that the Court of Chancery found that: 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. Although 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. But, despite its own findings about the adequacy of the market check, the Court of Chancery determined it would not give more than one-third weight to the deal price for two reasons.

The first reason was that there were regulatory developments relevant to the company being appraised and, therefore, the market's assessment of the company's value was not as reliable as under ordinary conditions. The respondent argues that this finding was not rationally supported by the record. We agree. The record below shows that the company's stock price often moved over the years, and that those movements were affected by the potential that the company's industry—payday lending and other forms of alternative consumer financial services—would be subject to tighter regulation. The Court of Chancery did not cite, and we are unaware of, any academic or empirical basis to conclude that market players like the many who were focused on this company's value would not have examined the potential for regulatory action and factored it in their assessments of the company's value. Like any factor relevant to a company's future performance, the market's collective judgment of the effect of regulatory 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 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.

The Court of Chancery also found that it would not give dispositive weight to the deal price because the prevailing buyer was a financial buyer that "focused its attention on achieving a certain internal rate of return and on reaching a deal within its financing constraints, rather than on [the company's] fair value." 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. For these reasons, we remand to the Court of Chancery to reconsider the weight it gave to the deal price in its valuation analysis.

The next issue in the respondent's appeal involves the Court of Chancery's discounted cash flow analysis. When the respondent pointed out in a reargument motion that the Chancellor's discounted cash flow model included working capital figures that differed from those the Chancellor expressly adopted in his post-trial opinion, the Chancellor corrected his clerical error. This would have resulted in the discounted cash flow model yielding a fair value figure lower than the deal price. But, instead of stopping there, at the prompting of the petitioners, the Court of Chancery then substantially increased its perpetuity growth rate from 3.1% to 4.0%, which resulted in the Court of Chancery reaching a fair value akin to its original estimate of the company's value. But, no adequate basis in the record supports this major change in growth rate. During the two decades before the merger leading to this appraisal, the company experienced rapid growth. The growth of the payday lending industry and its effect on poor borrowers during this period was a large driver of the regulatory reforms that the company faced, reforms that would require the company to write more loans to make the same profits as in the past. As it was, the record suggested that the management projections used in the Court of Chancery's original discounted cash flow model were optimistic and designed to encourage bidders to pay a high price. Those projections hockey stick up at the last two years, and therefore more working capital was required to sustain those increases, and that doesn't even account for the likelihood that regulatory changes required more loans (i.e., working capital) to make the same profits as in the past. During the sales process, the company had to revise its aggressive projections downward, as it was not keeping pace with them. Even after revising them downward, the company fell short of meeting them weeks after the transaction closed. Given the nature of the projection's outyears, the fact that the industry had already gone through a period of above-market growth, and the lack of any basis to conclude that the company would sustain high growth beyond the projection period, the record does not sustain the Court of Chancery's decision to substantially increase the company's perpetuity growth rate in its discounted cash flow model after reargument.

On cross-appeal, the petitioners argue that the Court of Chancery abused its discretion by giving weight to its comparable companies analysis, and that the only correct weighting of relevant factors would have given primary, if not sole, weight to the discounted cash flow model. We disagree. The comparable companies analysis used by the Chancellor was supported by the record; this was a rare instance where both experts agreed on the comparable companies the Court of Chancery used and so did several market analysts and others following the company. Thus, giving weight to a comparable companies analysis was within the Chancellor's discretion. Finally, the Court of Chancery's decision to give one-third weight each to the deal price, the discounted cash flow valuation, and the comparable companies valuation was not explained. Given the Court of Chancery's findings about the robustness of the market check and the substantial public information available about the company, we cannot discern the basis for this allocation. On remand, if the Court of Chancery chooses to use a weighting of different valuation methodologies to reach its fair value determination, the court must explain its weighting in a manner supported by the record before it.

For these reasons, we reverse and remand the Court of Chancery's ruling. On remand, the Chancellor should reassess the weight he chooses to afford various factors potentially relevant to fair value, and he may conclude that his findings regarding the competitive process leading to the transaction, when considered in light of other relevant factors, such as the views of the debt markets regarding the company's expected performance and the failure of the company to meet its revised projections, suggest that the deal price was the most reliable indication of fair value.

C. Page 57, New Sec. 2.10.Ib. Delaware Supreme Court's December 2017 Appraisal Decision in *Dell*

Page 57, New Sec. 2.10.Ib. Add after sec 2.10Ia the following:
New Sec. 2.10.Ib. **Delaware Supreme Court's December 2017 Appraisal Decision in *Dell***

Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.
Delaware Supreme Court, 2017, 177 A.3d 1

[This is a long and complex decision and the portions of the opinion set out here come principally from the Court's summary. The portion of this opinion addressing the Chancery Court's DCF analysis is in Chapter 7 of this Supplement, which deals with Valuation.]

VALIHURA, Justice:

The petitioners left standing in this long-running appraisal saga are former stockholders of Dell Inc. ("Dell" or the "Company") who validly exercised their appraisal rights instead of voting for a buyout led by the Company's founder and CEO, Michael Dell, and affiliates of a private equity firm, Silver Lake Partners ("Silver Lake"). In perfecting their appraisal rights, petitioners acted on their belief that Dell's shares were worth more than the deal price of $13.75 per share—which was already a 37% premium to the Company's ninety-day-average unaffected stock price.

Our appraisal statute, 8 Del. C. § 262, allows stockholders who perfect their appraisal rights to receive "fair value" for their shares as of the merger date instead of the merger consideration. The appraisal statute requires the Court of Chancery to assess the "fair value" of such shares and, in doing so, "take into account all relevant factors." The trial court complied: it took into account all the relevant factors presented by the parties in advocating for their view of fair value—including Dell's stock price and deal price—and then arrived at its own determination of fair value.

The problem with the trial court's opinion is not, as the Company argues, that it failed to take into account the stock price and deal price. The trial court did consider this market data. It simply decided to give it no weight. But the court nonetheless erred because its reasons for giving that data no weight—and for relying instead exclusively on its own discounted cash flow ("DCF") analysis to reach a fair value calculation of $17.62—do not follow from the court's key factual findings and from relevant, accepted financial principles.

"When reviewing a decision in a statutory appraisal, we use an abuse of discretion standard and grant significant deference to the factual findings of the trial court. This Court 'will accept [the Court of Chancery's] findings if supported by the record . . . .'" 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."

Here, the trial court gave no weight to Dell's stock price because it found its market to be inefficient. But the evidence suggests that the market for Dell's shares was actually efficient and, therefore, likely a possible proxy for fair value. Further, the trial court concluded that several features of management-led buyout ("MBO") transactions render the deal prices resulting from such transactions unreliable. But the trial court's own findings suggest that, even though this was an MBO transaction, these features were largely absent here. Moreover, even if it were not possible to determine the precise amount of that market data's imperfection, as the Court of Chancery concluded, the trial court's decision to rely "exclusively" on its own DCF analysis[3] is based on several assumptions that are not grounded in relevant, accepted financial principles.

We REVERSE, in part, and AFFIRM, in part, and REMAND for these reasons and those that follow. In addition, for reasons discussed in Section IV, we REVERSE and REMAND the Court of Chancery's decision concerning the allocation of fees and costs among the appraisal class. * * *

[Notwithstanding the Court's rejection of the use of the DCF methodology, the Court discussed several issues associated with the Chancery Court's DCF analysis. That discussion is included in Chapter 7 of this Supplement, which addresses valuation issues.]

B. The Court of Chancery's Reasons for Disregarding Deal Price Do Not Follow from the Record

The Company recasts the Court of Chancery's fair value opinion as creating several bright-line rules, including that the court must assign no weight to the deal price if: (i) it is not the "best" evidence of fair value; (ii) the court cannot "quantify the exact degree of the sale process mispricing"; or (iii) the transaction is an MBO. And the Company argues that each such rule is flawed. Setting aside whether the Court of Chancery's opinion actually purports to assert these more generalized propositions, we agree with the Company's core premise that, on this particular record, the trial court erred in not assigning any mathematical weight to the deal price. In fact, the record as distilled by the trial court suggests that the deal price deserved heavy, if not dispositive, weight.

On the other hand, we also agree with the petitioners that there is no requirement that the court assign some mathematical weight to the deal price, and that the court fulfilled its statutory obligation to take into account the deal price. The trial court's thorough examination of Dell's stock market dynamics and sale process demonstrates its consideration of these factors. But we reverse because there is a dissonance between the key underpinnings of the decision to disregard the deal price and the facts as found, and this dissonance distorted the trial court's analysis of fair value.

The three central premises that the Court of Chancery relied upon to assign no weight to the deal price were flawed. First, the court believed that a "valuation gap" existed between Dell's stock price and the Company's intrinsic value, and this conclusion — contrary to the efficient market hypothesis—led it to hypothesize that the bidding over Dell as a company was anchored at an artificially low price that depressed the ultimate deal price below fair value. Second, the court suggested that the lack of strategic buyers in the sale process—and, accordingly, the involvement of only private equity bidders—also pushed the deal price below fair value. Third, the court concluded that several factors endemic to MBO go-shops further undercut the deal price's credibility. We consider each of these premises in turn and find them untenable in view of the Court of Chancery's own findings of fact as considered in light of established principles of corporate finance. Without these premises, the trial court's support for disregarding the deal price collapses. Accordingly, the trial court's reliance on them as a basis for granting no weight to the market-based indicators of value constituted an abuse of discretion meriting reversal. * * *

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 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. "[O]ne 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." * * *

III. Fair Value Conclusion

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. That said, we give the Vice Chancellor the discretion on remand to enter judgment at the deal price if he so chooses, with no further proceedings. If he decides to follow another route, the outcome should adhere to our rulings in this opinion, including our findings with regard to the DCF valuation. If he chooses to weigh a variety of factors in arriving at fair value, he must explain that weighting based on reasoning that is consistent with the record and with relevant, accepted financial principles. * * *

D. Page 57, New Sec. 2.10.Ic. Application of the Delaware Supreme Court's Decisions in *DFC* and *Dell*—Chancellor Laster's January 2018 Decision in *Aruba*

Page 57, New Sec. 2.10.Ic. Add after new sec 2.10b the following:
New Sec. 2.10.Ic. **Application of the Delaware Supreme Court's Decisions in *DFC* and *Dell*—Chancellor Laster's January 2018 Decision in *Aruba***

Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.,
Delaware Court of Chancery, Jan. 26, 2018, 2018 Del. Ch. LEXIS 52.

[The discussion here does not include the court's DCF analysis. That analysis is included in Chapter 7 of this Supplement, which deals with Valuation.]

MEMORANDUM OPINION

LASTER, V.C.

In May 2015, Hewlett-Packard Company ("HP") acquired Aruba Networks, Inc. ("Aruba" or the "Company"). The transaction was governed by an Agreement and Plan of Merger by and among Aruba, HP, and Aspen Acquisition Sub., Inc., a wholly owned subsidiary of HP. Under the merger agreement, each share of Aruba common stock was converted into the right to receive consideration of $24.67 per share, subject to the holder's statutory right to eschew the merger consideration and seek appraisal. The petitioners perfected their appraisal rights and litigated this statutory appraisal proceeding. This is the court's post-trial decision on the issue of fair value.

The Delaware Supreme Court's decisions in Dell and DFC endorse using the market price of a widely traded firm as evidence of fair value. As in Dell and DFC, the market for Aruba's shares exhibited attributes associated with the premises underlying the efficient capital markets hypothesis. Under Dell and DFC, these attributes provide sufficient evidence of market efficiency to make Aruba's stock price "a possible proxy for fair value." Aruba's thirty-day average unaffected market price was $17.13 per share.

The Delaware Supreme Court's decisions in Dell and DFC endorse using the deal price in a third-party, arm's-length transaction as evidence of fair value. When evaluating the reliability of the deal price, a trial judge must remember 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; 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.

Put differently, "[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."

In this case, the merger was an arm's-length transaction that provided stockholders with consideration of $24.67 per share. By definition, it provided stockholders with "fair compensation" in the sense of "what would fairly be given to them in an arm's-length transaction." The petitioners proved that the Company's negotiators might have done better, but there is no reason to believe that they left any of Aruba's fundamental value on the bargaining table. When the merger consideration of $24.67 per share is compared to the unaffected market price of $17.13 per share, it is not possible to say that Aruba's stockholders were exploited. The deal price therefore provides reliable evidence of fair value.

The Dell and DFC decisions recognize that a deal price may include synergies, and they endorse deriving an indication of fair value by deducting synergies from the deal price. The respondent's expert cited a study that provides data on the base rates at which targets successfully extract a share of anticipated synergies from acquirers. Using that data, this decision arrives at a midpoint valuation indication for Aruba of $18.20 per share. I personally believe that Aruba's negotiators did not extract as great a share of the synergies as they might have, which suggests that deal-price-less-synergies figure is slightly higher.

The Dell and DFC decisions caution against relying on discounted cash flow analyses prepared by adversarial experts when reliable market indicators are available. The decisions teach that discounted cash flow models should be "used in appraisal proceedings when the respondent company was not public or was not sold in an open market check." 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." In this case, the discounted cash flow analysis prepared by the petitioners' expert generated a value of $32.57, which was inconsistent with the market evidence. The discounted cash flow analysis prepared by the respondent's expert generated a value of $19.75, nestled nicely between the unaffected market price and the deal price. Its methodological underpinnings, however, provided cause for concern, as did the meandering route by which the expert arrived at his final figure. I do not rely on the discounted cash flow valuations.

The two most probative indications of fair value are Aruba's unaffected market price of $17.13 per share and my deal-price-less-synergies figure of approximately $18.20 per share. In the context of this case, the unaffected market price provides the most persuasive evidence of fair value. My deal-price-less-synergies figure suffers from two major shortcomings.

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 complex matters and could be wrong. More broadly, the baseline data about the manner in which buyers and sellers allocate synergies could reflect sampling or measurement errors. both "aris[e] 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.

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. Aruba's unaffected market price provides the most persuasive evidence of fair value.

By awarding fair value based on the unaffected market price, this decision is not interpreting Dell and DFC to hold that market price is now the standard for fair value. Rather, Aruba's unaffected market price provides the best evidence of its going concern value.21 The fair value of Aruba is $17.13 per share. * * *

A. The Unaffected Market Price

The Delaware Supreme Court's recent decisions in 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,[2] then the unaffected

[2] [Original footnote 257] By "traditional," I mean a framing of the efficient capital markets hypothesis consistent with Eugene Fama's seminal work and its baseline Chicago-school assumptions. See Eugene F. Fama, Efficient Capital Markets: A Review of Theory and Empirical Work, 25 J. Fin. 383 (1970).

trading price provides evidence of the fair value of a proportionate interest in the company as a going concern. That evidence is more reliable than the single estimate of any one individual, be he a knowledgeable market participant, corporate insider, valuation professional, or trial judge. Under this standard, Aruba's unaffected market price provides persuasive evidence of fair value.

1. The Efficient Capital Markets Hypothesis

Both Dell and DFC endorse the efficient capital markets hypothesis and its predictions about the reliability of market prices. In DFC, the Delaware Supreme Court stated that "real world transaction prices can be the most probative evidence of fair value even through appraisal's particular lens." The high court observed that "[m]arket prices are typically viewed superior to other valuation techniques because, unlike, e.g., a single person's discounted cash flow model,

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At the trial court level in Dell, I cited some points of entry into a significant and growing body of literature that raises question about the assumptions undergirding the traditional model, which suggest a need for greater nuance. See In re Appraisal of Dell, Inc. (Dell Trial Fair Value), 2016 Del. Ch. LEXIS 81, 2016 WL 3186538, at *25 n.16 (Del. Ch. May 31, 2016), rev'd in pertinent part sub nom. Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd, A.3d , 2017 Del. LEXIS 518, 2017 WL 6375829 (Del. Dec. 14, 2017). In the legal field, much of this work has responded to the United States Supreme Court's relatively high-level framing of the efficient capital markets hypothesis as the cornerstone for using the fraud-on-the-market theory to create a presumption of reliance in securities fraud actions. See Basic Inc. v. Levinson, 485 U.S. 224, 241-42, 243-44, 246, 108 S. Ct. 978, 99 L. Ed. 2d 194 (1988). The field of behavioral economics has yielded particularly powerful insights. See, e.g., Donald C. Langevoort, Theories, Assumptions, and Securities Regulation: Market Efficiency Revisited, 140 U. Pa. L. Rev. 851 (1992); Larry E. Ribstein, Fraud on a Noisy Market, 10 Lewis & Clark L. Rev. 137 (2006); Jeff Schwartz, Fairness, Utility, and Market Risk, 89 Or. L. Rev. 175 (2010). Noise trading theory and chaos theory have yielded additional insights. See, e.g., Lawrence A. Cunningham, From Random Walks to Chaotic Crashes: The Linear Genealogy of the Efficient Capital Markets Hypothesis, 62 Geo. Wash. L. Rev. 546 (1994); Lawrence A. Cunningham, Capital Market Theory, Mandatory Disclosure, and Price Discovery, 51 Wash & Lee L. Rev. 843 (1994); Andrei Schleifer & Lawrence H. Summers, The Noise Trader Approach to Finance, 4 J. Econ. Persp. 19 (1990).

Perhaps future appraisal litigants will retain experts on market efficiency, as is common in federal securities actions, and maybe future appraisal decisions will consider subtler aspects of the efficient capital markets hypothesis. This decision does not provide any opportunity for doing so. In its supplemental submissions on the implications of Dell and DFC, the petitioners alluded to potential objections to the Delaware Supreme Court's framing of the efficient capital markets hypothesis, but they did not develop those objections in any meaningful way. Absent a case-specific expert opinion supported by credible evidence and the weight of social-science research, I do not believe a trial judge has the flexibility to disregard the Delaware Supreme Court's framing of the efficient capital markets hypothesis.

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." The court added that, from the perspective of economics, when the subject company's shares are "widely traded on a public market based upon a rich information base," then the fair value of a proportionate interest in the company as a going concern would "likely be best reflected by the prices at which [the] shares were trading as of the merger."

In Dell, the Delaware Supreme Court stated 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." The court explained that, when the market for a company's stock has attributes associated with efficient trading, the stock price reflects the judgments of many stockholders about the company's future prospects, based on public filings, industry information, and research conducted by equity analysts. In these circumstances, 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.

The court concluded that, when the market for a company's shares has the requisite attributes, the stock price is "likely a possible proxy for fair value."[3]

Under Dell and DFC, the critical question is whether the market for the subject company's shares has attributes associated with market efficiency. In Dell, the high court described the relevant attributes as follows: "A market is more likely efficient, or semi-strong efficient, if it has many stockholders; no controlling stockholder; highly active trading; and if information about the company is widely available and easily disseminated to the market."

In both Dell and DFC, the Delaware Supreme Court found that the market for the subject company's shares had the necessary attributes. The Dell decision described the market for Dell's stock as follows:

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. Based on these metrics, the record suggests the market for Dell stock was semi-strong efficient, meaning that the market's digestion and assessment of all publicly available information concerning Dell was quickly impounded into the Company's stock price. For example, on

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[3] [Original footnote 264] 2017 Del. LEXIS 518, [WL] at *1 (reversing trial court's fair value determination because, among other reasons, "[h]ere, the trial court gave no weight to Dell's stock price because it found its market to be inefficient. But the evidence suggests that the market for Dell's shares was actually efficient and, therefore, likely a possible proxy for fair value.").

January 14, 2013, Dell's stock jumped 9.8% within a minute of Bloomberg breaking the news of the Company's take-private talks, and the stock closed up 13% from the day prior—on a day the S&P as a whole fell 0.1%.

The DFC decision described the market for DFC's stock in similar, albeit more abbreviated, terms:

DFC's shares were traded on the NASDAQ exchange from 2005 until the merger. Throughout its history as a public company, the record suggests that DFC never had a controlling stockholder, it had a deep public float of 39.6 million shares, and, it had an average daily trading volume just short of one million shares. DFC's share price moved sharply in reaction to information about the company's performance, the industry, and the overall economy . . . .

The high court later noted that "DFC's stock was listed on a major U.S. exchange, traded actively, and had moved sharply over the years when the company was poised for growth or facing dimming prospects."

In neither case did an expert render an opinion on market efficiency, as is common in federal securities law actions when a plaintiff seeks to invoke the presumption of reliance associated with the fraud-on-the-market theory.[4] Nor was all of the market evidence part of the trial record. In DFC, the Delaware Supreme Court cited record evidence for some of the information about DFC's stock profile; it drew other information from DFC's public filings with the SEC or from an expert report addressing valuation issues. In Dell, the Delaware Supreme Court similarly drew much of the market-related information from public filings with the SEC or from an expert report addressing valuation issues.

In this case, as in *Dell* and *DFC*, no expert offered an opinion, pro or con, on whether the subject company's shares traded in an efficient market. During trial, the parties did not emphasize the attributes of the market for Aruba's common stock. Nevertheless, information drawn from sources comparable to those the Delaware Supreme Court used in Dell and DFC indicates that

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[4] [Original footnote 269] See, e.g., Amgen Inc. v. Conn. Ret. Plans & Tr. Funds, 568 U.S. 455, 471 n.6, 133 S. Ct. 1184, 185 L. Ed. 2d 308 (2013) (noting trial court relying on "unchallenged expert report . . . expressly found that the market for Amgen's stock was efficient"); IBEW Local 98 Pension Fund v. Best Buy Co., Inc., 818 F.3d 775, 779 (8th Cir. 2016) (noting "plaintiffs submitted a report by their expert" to support their "motion for class certification [which] relied on Basic's fraud-on-the-market presumption"); Schleicher v. Wendt, 618 F.3d 679, 682 (7th Cir. 2010) ("A financial economist concluded, in an expert report that the district judge credited, that the market for Conseco's shares was efficient . . . and that investors therefore can use the fraud-on-the-market doctrine as a replacement for person-specific proof of reliance and causation."). See generally 7AA Charles Alan Wright, Arthur R. Miller & Mary Kay Kane, Federal Practice and Procedure § 1781.1 (3d ed. 2005).

the market for Aruba's common stock had basic attributes consistent with what the high court found sufficient in those decisions:

• Aruba's shares traded on the NASDAQ through the date of the merger under the symbol ARUN.

• Aruba did not have a controlling stockholder.

• Aruba made public filings in compliance with the disclosure requirements imposed by federal securities laws.

• Thirty-three securities analysts covered Aruba.

• Aruba's weekly trading volume was 9.5 million shares or 8.7% of total shares outstanding.

• Aruba's bid-ask spread was 0.055%.

The following table compares the numerical attributes of Aruba's common stock with the comparable attributes for the subject companies in Dell and DFC.

	DFC	**Dell**	**Aruba**
Market Cap.	$375 million	$20 billion	$2.5 billion
Shares in public float	37.5 million	1.45 billion	104 million
Public float as % of outstanding	95%	85%	96%
Bid-ask spread	0.098%	0.08%	0.055%
# of analysts	10	33	33

Given these attributes, Aruba's stock price is "likely a possible proxy for fair value."

In addition, as in Dell, there is evidence that the Company's stock price reacted quickly to the release of news about the Company.

• When Aruba announced Project Greyhound after the market closed on August 26, 2014, the stock price rose by 5% the next day, closing at $21.26 on a day when the S&P 500 was stagnant.

• When Aruba announced its first quarter fiscal year 2015 earnings after the market closed on November 20, 2014, Aruba's stock price dropped by 14% on November 21 on a day when the S&P 500 was up 0.5%.

• When Bloomberg News reported that HP was in talks to buy Aruba on February 25, 2015, Aruba's stock price rose 21%. The news came out at 3:02 p.m. and, within one minute, Aruba's stock price had increased 12.7%. By 3:11 p.m., the price had increased to $22.86, before closing at $22.24 at 4 p.m. The same day, the S&P 500 decreased 0.1%.

• When Aruba announced its second quarter fiscal year 2015 earnings after the market closed on February 26, 2015, the stock price increased the next day by 9.7%. That same day, the S&P 500 decreased by 0.3%.

• When the merger was confirmed and the merger price of $24.67 announced on March 2, 2015, the stock price decreased slightly to close at $24.65.

Obviously, these are anecdotal observations and not event studies, but they compare favorably with the Dell court's observation that Dell's share price "quickly reflected the market's view on breaking developments," citing, as an example, that "on January 14, 2013, Dell's stock jumped 9.8% within a minute of Bloomberg breaking the news of the Company's take-private talks, and the stock closed up 13% from the day prior—on a day the S&P 500 as a whole fell 0.1%."278 Similar evidence in this case reinforces the conclusion that Aruba's stock price leading up to the merger is "likely a possible proxy for fair value." * * *

4. The Conclusion Regarding The Market Price Evidence

Aruba's thirty-day average unaffected market price was $17.13. Viewed within the framework established by *DFC* and *Dell*, Aruba's market price provides reliable evidence of the going concern value of the firm.

B. The Deal Price

The Delaware Supreme Court's recent decisions in *DFC* and *Dell* hold that when a widely held, publicly traded company has been sold in an arm's-length transaction, the deal price has "heavy, if not overriding, probative value." Applying that standard in this case, the merger price carries heavy weight, although the inclusion of elements of value arising from the merger requires adjustments to generate an indication 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.

3. Deducting Synergies

Under Dell and DFC, the deal price in this case has substantial probative value. But the evidence shows that the deal generated significant synergies. Under the DFC decision, it is to be assumed that HP shared some of those with Aruba's stockholders. 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." * * *

C. The Experts' Analyses

Both sides submitted opinions from valuation experts. Both experts used the discounted cash flow methodology to value Aruba. Both experts believed that the discounted cash flow methodology provided the best approach for determining the fair value of the Company. **[The discussion of these DCF analyzes, both of which were rejected by the court are discussed in Chapter 7 of this Supplement.]** * * *

D. Weighing the Valuation Methodologies

This decision has discussed each of the relevant methods of valuation that the parties presented. Under the statute, the court must make a point estimate of fair value measured in dollars and cents. When determining fair value, "[t]he 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."

The forceful discussion of the efficient capital markets hypothesis in Dell and DFC indicates that Aruba's unaffected market price is entitled to substantial weight.

[C]orporate 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 . . . .

"Market 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." "[I]n many circumstances a property interest is best valued by the amount a buyer will pay for it" and "a well-informed, liquid trading market will provide a measure of fair value superior to any estimate the court could impose."

In this case, because Aruba's shares "were widely traded on a public market based upon a rich information basis," the fair value of the petitioners' shares "would, to an economist, likely be best reflected by the prices at which their shares were trading as of the merger." Aruba had "a deep base of public shareholders" and "highly active trading," so "the price at which its shares trade is informative of fair value." The unaffected thirty-day average market price of Aruba's stock was $17.13 per share.

Dell and DFC teach that the deal price is also entitled to substantial weight. "In economics, the value of something is what it will fetch in the market. That is true of corporations, just as it is true of gold." For a court to give weight to the deal price, it need not be the most reliable evidence of the Company's value as a going concern. This court has authority "to determine, in its discretion, that the deal price is the most reliable evidence of fair value . . . , and that's especially so in cases . . . where things like synergy gains or minority stockholder discounts are not contested."

The deal price in this case resulted from an arm's-length transaction involving a publicly traded company without a controlling stockholder. The deal price in this case contained synergies, so it logically exceeded fair value. There is also the fact that the petitioners failed to identify a bidder who would pay more than HP. "Fair value entails at minimum a price some buyer is willing to pay . . . ." Taken together, these propositions indicate that the deal price in this case operates as a ceiling for fair value.

The *Dell* and *DFC* decisions recognize that a deal price may include synergies and endorse deriving an indication of fair value from the deal price by deducting synergies. In this case, the evidence shows that the deal generated significant synergies. Using the low-end synergy range implies a standalone value of $21.08 per share. Using the high-end synergy range implies a standalone value of $15.32 per share. This decision has adopted the midpoint of $18.20 per share as its deal-price-less-synergies value.

This decision does not give any weight to the discounted cash flow analyses. As in Dell, "this appraisal case does not present the classic scenario in which there is reason to suspect that market forces cannot be relied upon to ensure fair treatment of the minority." Discounted cash flow models are "often used in appraisal proceedings when the respondent company was not public or was not sold in an open market check."

The reason for that is not that an economist wouldn't consider the best estimate of a private company's value to be the price it sold at in an open sale process of which all logical buyers were given full information and an equal opportunity to compete. Rather, the reason is that if such a process did not occur, corporate finance instructs that the value of the company to potential buyers should be reflected in its ability to generate future cash flows.

"But, a single person's own estimate of the cash flows are just that, a good faith estimate by a single, reasonably informed person to predict the future. Thus, a singular discounted cash flow model is often most helpful when there isn't an observable market price." 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."

Marcus's discounted cash flow valuation of $32.57 per share diverged substantially from market indications. His figure is nearly double Aruba's thirty-day average unaffected market price of $17.13. It is approximately 32% higher than the deal price of $24.67 per share. In a transaction involving a financial buyer that could be expected to generate few if any combinatorial synergies, the Delaware Supreme Court recently emphasized the lack of reliability of a discounted cash flow analysis that yielded a result that was 40% over the deal price. The transaction in this case generated substantial synergies.

Dages's initial discounted cash flow valuation of $19.85 and revised discounted cash flow valuation of $19.75 fell nicely between the unaffected market price and the deal price. His figures also landed close to HP's standalone discounted cash flow valuation of $18.98 and Barclay's standalone discounted cash flow valuation of $19.93. The relative lack of methodological rigor in the analysis, however, creates cause for concern about the strategic selection of inputs to channel the result into this range.

The two probative indications of value in this case are the unaffected market price of $17.13 and the deal-price-less-synergies value of approximately $18.20 per share. Using these indicators nevertheless carries conceptual difficulties because "[t]he time for determining the value of a dissenter's shares is the point just before the merger transaction 'on the date of the merger.'" 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.

The unaffected market price provides direct evidence of the collective view of market participants as to Aruba's fair value as a going concern during the period before the announcement of the transaction, which could be different than Aruba's fair value as of closing. The same disconnect exists for the deal price, which provides evidence of how the parties to the merger agreement valued Aruba during the price negotiations, which could be different than Aruba's fair value as of closing. Addressing a similar issue in the Union Illinois case, Chief Justice Strine described the temporal gap as a "quibble" and "not a forceful objection," noting that "[t]he negotiation of merger terms always and necessarily precedes consummation." Observing that "[n]othing in the record persuades me that [the company] was more valuable by [closing] than it was when the Merger terms were set," he continued to use the deal price as an indicator of value. Similarly in this case, neither side proved that Aruba's value had changed materially by closing, so this decision sticks with the unaffected market price and the deal price less synergies.

The difficult question is how to choose between, weigh, or otherwise exercise my discretion non-abusively when evaluating the two probative valuation indications. The unaffected market price provides a direct measure of the collective judgment of numerous market participants about Aruba's value as a going concern. The deal price less synergies provides an indirect measure with two significant sources of uncertainty. One is the problem of measurement error. Under the traditional view of the efficient capital markets hypothesis, errors are randomly distributed and cancel out. My deal-price-less-synergies figure could have errors at multiple levels. To cite just a few, I may have erred when making my case-specific allocation of synergies to the sell-side. I might have misinterpreted the information that Aruba's expert cited, or that data itself could contain sampling and measurement errors. The size of the original synergy estimates might also be off, as could any number of individual estimates that added up to the overarching estimates. After all, they were necessarily predictions about complex matters. Perhaps errors at one level might counterbalance errors at another, but there is no way to know, and the smaller number of judgments involved (compared to the number of trades generating the market price) makes it more likely that the errors could skew the figure, just like a small and undiversified portfolio can produce extreme results. The Delaware Supreme Court's expressed preference in Dell and DFC for market indicators over discounted cash flow valuations counsels in favor of preferring market indicators over the output of a similarly judgment-laden exercise of backing out synergies.487

The other difficulty is that my deal-price-less-synergies figure continues to incorporate an element of value resulting from the merger. When an acquirer purchases a widely traded firm, the premium that an acquirer is willing to pay for the entire firm anticipates incremental value both from synergies and from the reduced agency costs that result from unitary (or controlling) ownership. Like synergies, the value created by reduced agency costs results from the transaction and is not part of the going concern value of the firm. The value belongs to the buyer, although the seller may extract a portion of it through negotiations. Eliminating shared synergies therefore only goes part of the way towards eliminating "any element of value arising from the accomplishment or expectation of the merger." A court also must eliminate the share of value that accrues from the reduced agency costs.

For Aruba, using its unaffected market price provides the more straightforward and reliable method for estimating the value of the entity as a going concern. I could strive to reach the same endpoint by backing out shared synergies and a share of value for reduced agency costs, but both steps are messy and provide ample opportunities for error. For Aruba, the unaffected market price provides a direct estimate of the same endpoint. Rather than representing my own fallible determination, it distills "the collective judgment of the many based on all the publicly available information about a given company and the value of its shares." "[T]he price produced by an efficient market is generally a more reliable assessment of fair value than the view of a single analyst," particularly when a trial judge is playing the analyst's role.

This approach does not elevate "market value" to the governing standard under the appraisal statute. The governing standard for fair value under the appraisal statute remains the entity's value as a going concern. For Aruba, the unaffected public market price provides the best evidence of its value as a going concern.

In this case, the best evidence of Aruba's fair value as a going concern, exclusive of any value derived from the merger, is its thirty-day average unaffected market price of $17.13 per share. I recognize that no one argued for this result. I also recognize that the resulting award is lower than Aruba's proposed figure of $19.75 per share. That figure relied on its expert's discounted cash flow analysis, which this decision has found unpersuasive.

"When . . . none of the parties establishes a value that is persuasive, the Court must make a determination based on its own analysis." The appraisal statute requires that "the Court shall determine the fair value of the shares." This means that I must reach my own, independent determination of fair value. That determination is $17.13 per share.

III. CONCLUSION

The petitioners are awarded $17.13 per share. The legal rate of interest, compounded quarterly, shall accrue on this amount from the date of closing until the date of payment. The parties shall cooperate in preparing a final order. If the parties identify additional issues that need to be resolved, they shall submit a joint letter within two weeks that explains the issues and recommends a schedule for bringing this case to conclusion, at least at the trial court level.

III. CHAPTER 3, FIDUCIARY DUTIES IN M&A GENERALLY AND IN USING POISON PILLS: DELAWARE WITH A QUICK LOOK AT PENNSYLVANIA, THE MODEL ACT, AND THE ALI'S PROPOSALS

A. Page 174, New Sec. 3.15.I. Delaware Supreme Court's Decision Applying the Business Judgment Rule in a Stock for Stock Merger, Even with KKR as the Managing Shareholder

Page 174, New Sec 3.15.I. Add before Sec. 3.16, the following:

New Sec. 3.15.I. **Delaware Supreme Court's Decision Applying the Business Judgment Rule in a Stock for Stock Merger, Even with KKR as the Managing Shareholder**

CORWIN V. KKR FIN. HOLDINGS LLC
Delaware Supreme Court, 2015, 125 A.3d 304.

STRINE, Chief Justice:

In a well-reasoned opinion, the Court of Chancery held that the business judgment rule is invoked as the appropriate standard of review for a post-closing damages action when a merger that is not subject to the entire fairness standard of review has been approved by a fully informed, uncoerced majority of the disinterested stockholders. For that and other reasons, the Court of Chancery dismissed the plaintiffs' complaint. In this decision, we find that the Chancellor was correct in finding that the voluntary judgment of the disinterested stockholders to approve the merger invoked the business judgment rule standard of review and that the plaintiffs' complaint should be dismissed. For sound policy reasons, Delaware corporate law has long been reluctant to second-guess the judgment of a disinterested stockholder majority that determines that a transaction with a party other than a controlling stockholder is in their best interests.

I. The Court Of Chancery Properly Held That The Complaint Did Not Plead Facts Supporting An Inference That KKR Was A Controlling Stockholder of Financial Holdings

The plaintiffs filed a challenge in the Court of Chancery to a stock-for-stock merger between KKR & Co. L.P. ("KKR") and KKR Financial Holdings LLC ("Financial Holdings") in which KKR acquired each share of Financial Holdings's stock for 0.51 of a share of KKR stock, a 35% premium to the unaffected market price. Below, the plaintiffs' primary argument was that the transaction was presumptively subject to the entire fairness standard of review because Financial Holdings's primary business was financing KKR's leveraged buyout activities, and instead of having employees manage the company's day-to-day operations, Financial Holdings was managed by KKR Financial Advisors, an affiliate of KKR, under a contractual management agreement that could only be terminated by Financial Holdings if it paid a termination fee. As a result, the plaintiffs alleged that KKR was a controlling stockholder of Financial Holdings, which was an LLC, not a corporation.

The defendants filed a motion to dismiss, taking issue with that argument. In a thoughtful and thorough decision, the Chancellor found that the defendants were correct that the plaintiffs' complaint did not plead facts supporting an inference that KKR was Financial Holdings's controlling stockholder. Among other things, the Chancellor noted that KKR owned less than 1% of Financial Holdings's stock, had no right to appoint any directors, and had no contractual right to veto any board action. Although the Chancellor acknowledged the unusual existential circumstances the plaintiffs cited, he noted that those were known at all relevant times by investors, and that Financial Holdings had real assets its independent board controlled and had the option of pursuing any path its directors chose.

In addressing whether KKR was a controlling stockholder, the Chancellor was focused on the reality that in cases where a party that did not have majority control of the entity's voting stock was found to be a controlling stockholder, the Court of Chancery, consistent with the instructions of this Court, looked for a combination of potent voting power and management control such that the stockholder could be deemed to have effective control of the board without actually owning a majority of stock. Not finding that combination here, the Chancellor noted:

> Plaintiffs' real grievance, as I see it, is that [Financial Holdings] was structured from its inception in a way that limited its value-maximizing options. According to plaintiffs, [Financial Holdings] serves as little more than a public vehicle for financing KKR-sponsored transactions and the terms of the Management Agreement make [Financial Holdings] unattractive as an acquisition target to anyone other than KKR because of [Financial Holdings]'s operational dependence on KKR and because of the significant cost that would be incurred to terminate the Management Agreement. I assume all that is true. But, every contractual obligation of a corporation constrains the corporation's freedom to operate to some degree and, in this particular case, the stockholders cannot claim to be surprised. Every stockholder of [Financial Holdings] knew about the limitations the Management Agreement imposed on [Financial Holdings]'s business when he, she or it acquired shares in [Financial Holdings]. They also knew that the business and affairs of [Financial Holdings] would be managed by a board of directors that would be subject to annual stockholder elections.
>
> At bottom, plaintiffs ask the Court to impose fiduciary obligations on a relatively nominal stockholder, not because of any coercive power that stockholder could wield over the board's ability to independently decide whether or not to approve the merger, but because of pre-existing contractual obligations with that stockholder that constrain the business or strategic options available to the corporation. Plaintiffs have cited no legal authority for that novel proposition, and I decline to create such a rule.

After carefully analyzing the pled facts and the relevant precedent, the Chancellor held:

> [T]here are no well-pled facts from which it is reasonable to infer that KKR could prevent the [Financial Holdings] board from freely exercising its independent judgment in considering the proposed merger or, put differently, that KKR had the power to exact retribution by removing the [Financial Holdings] directors from their offices if they did not bend to KKR's will in their consideration of the proposed merger.

Although the plaintiffs reiterate their position on appeal, the Chancellor correctly applied the law and we see no reason to repeat his lucid analysis of this question.

II. The Court of Chancery Correctly Held That The Fully Informed, Uncoerced Vote Of The Disinterested Stockholders Invoked The Business Judgment Rule Standard Of Review

On appeal, the plaintiffs further contend that, even if the Chancellor was correct in determining that KKR was not a controlling stockholder, he was wrong to dismiss the complaint because they contend that if the entire fairness standard did not apply, Revlon did, and the plaintiffs argue that they pled a Revlon claim against the defendant directors. But, as the defendants point out, the plaintiffs did not fairly argue below that Revlon applied and even if they did, they ignore the reality that Financial Holdings had in place an exculpatory charter provision, and that the transaction was approved by an independent board majority and by a fully informed, uncoerced stockholder vote. Therefore, the defendants argue, the plaintiffs failed to state a non-exculpated claim for breach of fiduciary duty.

But we need not delve into whether the Court of Chancery's determination that Revlon did not apply to the merger is correct for a single reason: it does not matter. Because the Chancellor was correct in determining that the entire fairness standard did not apply to the merger, the Chancellor's analysis of the effect of the uncoerced, informed stockholder vote is outcome-determinative, even if Revlon applied to the merger.

As to this point, the Court of Chancery noted, and the defendants point out on appeal, that the plaintiffs did not contest the defendants' argument below that if the merger was not subject to the entire fairness standard, the business judgment standard of review was invoked because the merger was approved by a disinterested stockholder majority. The Chancellor agreed with that argument below, and adhered to precedent supporting the proposition that when a transaction not subject to the entire fairness standard is approved by a fully informed, uncoerced vote of the disinterested stockholders, the business judgment rule applies. Although the Chancellor took note of the possible conflict between his ruling and this Court's decision in Gantler v. Stephens, he reached the conclusion that Gantler did not alter the effect of legally required stockholder votes on the appropriate standard of review. Instead, the Chancellor read Gantler as a decision solely intended to clarify the meaning of the precise term "ratification." He had two primary reasons for so finding. First, he noted that any statement about the effect a statutorily required vote had on the appropriate standard of review would have been dictum because in Gantler the Court held that the disclosures regarding the vote in question—a vote on an amendment to the company's charter—were materially misleading. Second, the Chancellor doubted that the Supreme Court would have "overrule[d] extensive Delaware precedent, including Justice Jacobs's own earlier decision in *Wheelabrator*, which involved a statutorily required stockholder vote to consummate a merger" without "expressly stat[ing] such an intention."

On appeal, the plaintiffs make Gantler a central part of their argument, even though they did not fairly present this point below. They now argue that Gantler bound the Court of Chancery to give the informed stockholder vote no effect in determining the standard of review. They contend that the Chancellor's reading of Gantler as a decision focused on the precise term "ratification" and not a decision intended to overturn a deep strain of precedent it never bothered to cite, was incorrect. The plaintiffs also argue that they should be relieved of their failure to argue this point fairly below in the interests of justice.

Although we disagree with the plaintiffs that this sort of case provides a sound basis for relieving a sophisticated party of its failure to present its position properly to the trial court, even if we agreed it would not aid the plaintiffs. No doubt Gantler can be read in more than one way, but we agree with the Chancellor's interpretation of that decision and do not accept the plaintiffs' contrary one. Had Gantler been intended to unsettle a long-standing body of case law, the decision would likely have said so. Moreover, as the Chancellor noted, the issue presented in this case was not even squarely before the Court in Gantler because it found the relevant proxy statement to be materially misleading. To erase any doubt on the part of practitioners, we embrace the Chancellor's well-reasoned decision and the precedent it cites to support an interpretation of Gantler as a narrow decision focused on defining a specific legal term, "ratification," and not on the question of what standard of review applies if a transaction not subject to the entire fairness standard is approved by an informed, voluntary vote of disinterested stockholders. This view is consistent with well-reasoned Delaware precedent.

Furthermore, although the plaintiffs argue that adhering to the proposition that a fully informed, uncoerced stockholder vote invokes the business judgment rule would impair the operation of *Unocal* and *Revlon*, or expose stockholders to unfair action by directors without protection, the plaintiffs ignore several factors. First, *Unocal* and *Revlon* are primarily designed to give stockholders and the Court of Chancery the tool of injunctive relief to address important M & A decisions in real time, before closing. They were not tools designed with post-closing money damages claims in mind, the standards they articulate do not match the gross negligence standard for director due care liability under *Van Gorkom*, and with the prevalence of exculpatory charter provisions, due care liability is rarely even available.

Second and most important, the doctrine applies only to fully informed, uncoerced stockholder votes, and if troubling facts regarding director behavior were not disclosed that would have been material to a voting stockholder, then the business judgment rule is not invoked. Here, however, all of the objective facts regarding the board's interests, KKR's interests, and the negotiation process, were fully disclosed.

Finally, when a transaction is not subject to the entire fairness standard, the long-standing policy of our law has been to avoid the uncertainties and costs of judicial second-guessing when the disinterested stockholders have had the free and informed chance to decide on the economic merits of a transaction for themselves. There are sound reasons for this policy. When the real parties in interest—the disinterested equity owners—can easily protect themselves at the ballot box by simply voting no, the utility of a litigation-intrusive standard of review promises more costs to stockholders in the form of litigation rents and inhibitions on risk-taking than it promises in terms of benefits to them. The reason for that is tied to the core rationale of the business judgment rule, which is that judges are poorly positioned to evaluate the wisdom of business decisions and there is little utility to having them second-guess the determination of impartial decision-makers with more information (in the case of directors) or an actual economic stake in the outcome (in the case of informed, disinterested stockholders). In circumstances, therefore, where the stockholders have had the voluntary choice to accept or reject a transaction, the business judgment rule standard of review is the presumptively correct one and best facilitates wealth creation through the corporate form.

For these reasons, therefore, we affirm the Court of Chancery's judgment on the basis of its well-reasoned decision.

B. Page 184, New Sec. 3.16.Ea. N.Y. Follows *MFW*

Page 57, New Sec. 3.16.Ea. Add before Section F the following:
New Sec. 3.16.Ea. ***N.Y. Follows MFW***

Matter of Kenneth Cole Prods., Inc,
N.Y. Ct of Appeals, May 5, 2016, 2016 N.Y. LEXIS 1059 .

Opinion
STEIN, J.:

In this shareholder class action challenging a going-private merger, we adopt the standard of review recently announced by the Delaware Supreme Court, in reviewing challenges to going-private mergers, New York courts should apply the business judgment rule as long as certain shareholder-protective conditions are present; if those measures are not present, the entire fairness standard should be applied. Applying the MFW standard to the case before us, we affirm the dismissal of the complaint.

I.

Kenneth Cole Productions, Inc. (KCP) is a New York corporation that designs and markets apparel, footwear, handbags and accessories. KCP was organized with two classes of common stock. As of June 2012, there were approximately 10,706,723 outstanding shares of Class A stock, which were traded on the New York Stock Exchange. Each Class A share entitled the holder to one vote, and defendant Kenneth D. Cole held approximately 46% of these shares. As of June 2012, there were approximately 7,890,497 outstanding shares of Class B stock, all of which were held by Cole. Class B shares entitled the holder to 10 votes, giving Cole approximately 89% of the voting power of the KCP shareholders. At the time in question, KCP's board of directors consisted of Cole and the other individual defendants herein. Defendants Michael J. Blitzer and Philip R. Peller were elected by Class A shareholders. Notably, defendants Denis F. Kelly and Robert C. Grayson held directorships voted on by both Class A and Class B shareholders, effectively giving Cole sole authority to fill these positions.

At a meeting held in February 2012, Cole proposed a going-private merger by informing KCP's board of his intention to submit an offer to purchase the remainder of the outstanding Class A shares and, in effect, take the publicly-traded company private. After making this announcement, Cole left the meeting, and the board established a special committee to consider the proposal and negotiate any potential merger. The special committee consisted of directors Grayson, Kelly, Blitzer and Peller. On February 23, 2012, Cole made an initial offer of $15.00 per share. The offer was conditioned on approval by (1) the special committee, and, then, (2) a majority of the minority shareholders. At that time, Cole indicated that he had no desire to seek any other type of merger and, as a stockholder, would not approve of one. He also stated that, if the special committee did not recommend approval or the stockholders voted against the proposed transaction, his relationship with KCP would not be adversely affected.

Within a few days of Cole's announcement, several shareholders, including plaintiff Erie County Employees Retirement System, commenced separate class actions alleging, among other things, breach of fiduciary duty by Cole and the directors. The committee retained legal counsel and a financial advisor, and proceeded to negotiate the terms of the going-private merger with Cole. The committee asked Cole to increase his offer several times, which he ultimately raised to $15.50 and then $16.00. Within a week of the $16.00 offer, Cole reduced his offer to $15.00, citing the alleged recent emergence of problems in the company and the economy. Finally, after months of negotiations, the special committee again asked Cole to increase his offer and, thereafter, approved Cole's offer of $15.25 for each outstanding share of Class A stock, which it recommended to the minority shareholders. Although the shareholder vote apparently occurred after an amended complaint was filed in this action, and is not mentioned therein, 99.8% of the minority shareholders voted in favor of the merger.

In the amended complaint, plaintiff sought, among other things, (1) a judgment declaring that Cole and the directors had breached the fiduciary duties they owed to the minority shareholders, (2) an award of damages to the class, and (3) a judgment enjoining the merger. Defendants separately moved to dismiss the complaint on the ground that it failed to state a cause of action.

Supreme Court granted defendants' motions and dismissed the complaint. The court determined that the complaint "fail[ed] to set forth facts demonstrating a lack of independence on the part of any of the . . . individual defendants." Further, the court held that "the complaint d[id] not adequately allege any facts that, if true, demonstrate[d] that the decision not to seek other bids constituted a breach of fiduciary duty," as "plaintiff[] acknowledge[d] that the special committee negotiated with Cole over a period of months and obtained an increase in the price he would pay . . . where the original price represented a premium over the stock's most recent selling price." Ultimately, the court reasoned that, "absent a showing of specific unfair conduct by the special committee, the [c]ourt will not second guess the [special] committee's business decisions in negotiating the terms of [the] transaction." The court further held that "the complaint d[id] not contain adequate statements regarding a breach" of Cole's fiduciary duty. Plaintiff appealed, on behalf of itself and the class.

The Appellate Division affirmed, holding that, "[c]ontrary to plaintiff's claim, the motion court was not required to apply the 'entire fairness' standard to the transaction". The Court noted that, unlike in Alpert v 28 Williams St. Corp. , "the merger in the case at bar required the approval of the majority of the minority (i.e., non-Cole) shareholders". In addition, Cole, an interested party, "did not participate when [KCP]'s board . . . voted on the merger," and plaintiff did "not allege that the remaining members Matter of Kenneth Cole Prods., Inc of the board . . . were self-interested". The Court held that "there [were] no allegations sufficient to demonstrate that the members of the board or the special committee did not act in good faith or were otherwise interested "This Court granted plaintiff leave to appeal.

II.

The primary issue before us is what standard should be applied by courts reviewing a going-private merger that is subject from the outset to approval by both a special committee of independent directors and a majority of the minority shareholders. Plaintiff urges that we apply the entire fairness standard, which places the burden on the corporation's directors to demonstrate that they engaged in a fair process and obtained a fair price. Defendants seek application of the business judgment rule, with or without certain conditions. We are persuaded to adopt a middle ground. Specifically, the business judgment rule should be applied as long as the corporation's directors establish that certain shareholder-protective conditions are met; however, if those conditions are not met, the entire fairness standard should be applied.

We begin with the general principal that courts should strive to avoid interfering with the internal management of business corporations. To that end, we have long adhered to the business judgment rule, which provides that, where corporate officers or directors exercise unbiased judgment in determining that certain actions will promote the corporation's interests, courts will defer to those determinations if they were made in good faith. The doctrine is based, at least in part, on a recognition that: courts are ill equipped to evaluate what are essentially business judgments; there is no objective standard by which to measure the correctness of many corporate decisions (which involve the weighing of various considerations); and corporate directors are charged with the authority to make those decisions. Hence, absent fraud or bad faith, courts should respect those business determinations and refrain from any further judicial inquiry. We have, therefore, held that the substantive determination of a committee of disinterested directors is beyond judicial inquiry under the business judgment rule, but that "the court may inquire as to the disinterested independence of the members of that committee and as to the appropriateness and sufficiency of the investigative procedures chosen and pursued by the committee".

A freeze-out merger is typical of situations in which a director's loyalty may be divided or compromised, thereby calling into question the applicability of the business judgment rule. In such a merger, the majority stock owner or group in control attempts to freeze out the interests of minority shareholders. There are three main types of freeze-out mergers: (1) two-step mergers, in which an outside investor purchases control of the majority shares of a target company, then uses that control to merge the target with a second company, thereby freezing out the minority shareholders of the target and forcing a cash-out of their shares; (2) parent-subsidiary mergers; and (3) going-private mergers, in which the majority shareholder seeks to remove public investors and gain ownership of the entire company.

This Court's seminal decision regarding freeze-out mergers is Alpert v 28 Williams St. Corp. In that case, we recognized that, where there are common directors or majority ownership between the parties involved in a transaction, "the inherent conflict of interest and the potential for self-dealing requires careful scrutiny of the transaction". In reviewing a two-step merger in Alpert, we held that while, "[g]enerally, the plaintiff has the burden of proving that the merger violated the duty of fairness, . . . when there is an inherent conflict of interest, the burden shifts to the interested directors or shareholders to prove good faith and the entire fairness of the merger". This "entire fairness" standard has two components: fair process and fair price. The fair process aspect concerns timing, structure, disclosure of information to independent directors and shareholders, how approvals were obtained, and similar matters. The fair price aspect can be measured by whether independent advisors rendered an opinion or other bids were considered, which may demonstrate the price that would have been established by arm's length negotiations. Considering the two components, the transaction is viewed as a whole to determine if it is fair to the minority shareholders.

In Alpert, we specifically stated that we were not deciding whether the circumstances that would satisfy fiduciary duties in a two-step merger would be the same for other types of mergers. Thus, that decision is not dispositive of the standard for reviewing a going-private merger, such as the one now before us. The present case is also distinguishable because, in Alpert, there was no independent committee and no minority shareholder vote.

The parties here debate whether we should apply the entire fairness standard, as in Alpert, or, alternatively, whether we should adopt the test recently established by the Delaware Supreme Court in Kahn v M & F Worldwide Corp. (MFW). In MFW, a controlling shareholder sought to purchase all of the shares of stock and take the corporation private, but made the proposal contingent from the outset upon two shareholder-protective measures — negotiation and approval by a special committee of independent directors, and approval by a majority of shareholders that were unaffiliated with the controlling shareholder (see id. at 638). As in the case before us, the controlling shareholder also made it clear that it was not interested in selling any of its shares, would not vote in favor of any alternative sale or merger and, if the merger was not recommended, its future relationship with the company — including its desire to remain a shareholder — would not be adversely affected.

In MFW, the question before the Delaware Supreme Court was framed as "what standard of review should apply to a going private merger conditioned upfront by the controlling stockholder on approval by both a properly empowered, independent committee and an informed, uncoerced majority-of-the-minority vote" (id. at 639 [internal quotation marks omitted]). We are presented with the same question here. In prior cases, the Delaware Supreme Court had applied the entire fairness standard when reviewing mergers with interested directors, although the court had created a burden shift — placing the burden on the objecting minority shareholders — in situations in which the interested director required approval by an independent committee or a majority of the minority shareholders; Kahn v Tremont Corp., . Never before had that Court addressed a situation in which both of those protections were present.

The Delaware Supreme Court opined in MFW that the opportunity for review under the business judgment rule — as opposed to the entire fairness standard — created a strong incentive for controlling shareholders to provide a structure for freeze-out mergers that is most likely to protect the interests of minority shareholders, because when both protections are in place, the situation replicates an arm's length transaction and supports the integrity of the process. That Court ultimately held that "business judgment is the standard of review that should govern mergers between a controlling stockholder and its corporate subsidiary, where the merger is conditioned ab initio upon both the approval of an independent, adequately-empowered Special Committee that fulfills its duty of care; and the uncoerced, informed vote of a majority of the minority stockholders". The Court articulated a number of reasons for the adoption of this new standard, including that: where the controlling shareholder clearly disabled itself from using its control to dictate the outcome, the merger acquired the characteristics of "third-party, arm's length mergers" that are reviewed under the business judgment rule; "the dual procedural protection merger structure optimally protects the minority stockholders in controller buyouts"; it is consistent with the tradition of courts deferring to informed decisions by impartial directors, especially when approved of by disinterested and informed stockholders; and it will provide an incentive to create structures that best protect minority shareholders. The standard was summarized as follows:

> "in controller buyouts, the business judgment standard of review will be applied if and only if: (i) the controller conditions the procession of the transaction on the approval of both a Special Committee and a majority of the minority stockholders; (ii) the Special Committee is independent; (iii) the Special Committee is empowered to freely select its own advisors and to say no definitively; (iv) the Special Committee meets its duty of care in negotiating a fair price; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority".

We now adopt that standard of review for courts reviewing challenges to going-private mergers. The standard set forth in MFW reinforces that the business judgment rule is our general standard of review of corporate management decisions, and is consistent with this Court's statement in Auerbach that the substantive determination of a committee of disinterested directors is beyond judicial inquiry under the business judgment rule, but that courts "may inquire as to the disinterested independence of the members of [a special] committee and as to the appropriateness and sufficiency of the investigative procedures chosen and pursued by the committee". While the business judgment rule is deferential to corporate boards, minority shareholders are sufficiently protected by MFW's conditions precedent to the application of that standard in going-private mergers. Overall, the MFW standard properly considers the rights of minority shareholders — to obtain judicial review of transactions involving interested parties, and to proceed to trial where there is adequate proof that those interests may have affected the transaction — and balances them against the interests of directors and controlling shareholders in avoiding frivolous litigation and protecting independently-made business decisions from unwarranted judicial interference.

According to the Delaware Supreme Court, for purposes of this rule, a complaint is sufficient to state a cause of action for breach of fiduciary duty — and the plaintiff may proceed to discovery — if it alleges "a reasonably conceivable set of facts" showing that any of the six enumerated shareholder-protective conditions did not exist. Conclusory allegations or bare legal assertions with no factual specificity are not sufficient, and will not survive a motion to dismiss (see conclusory allegations that two directors control the remaining directors are insufficient; a complaint must contain specific allegations of coercive power over others or that interested or controlled directors constitute a majority). Mere speculation cannot support a cause of action for breach of fiduciary duty. If the pleading requirements are met, in order to defeat summary judgment, a plaintiff must then demonstrate that there is a question of fact as to the establishment or efficacy of any of the enumerated conditions designed to protect the minority shareholders. Finally, if the evidence demonstrates that any of the protections were not in place, then the business judgment rule is inapplicable and the entire fairness standard applies.

Reviewing the complaint here under the MFW standard, we conclude that the courts below properly determined that the allegations do not withstand defendants' motions to dismiss.

Plaintiff did not sufficiently and specifically allege that any of MFW's six enumerated conditions were absent from the merger here. Beginning with the first condition, plaintiff concedes that Cole conditioned the merger, from the outset, upon approval by both a special committee of independent directors and a majority of the minority shareholders.

Next, in challenging the independence of the special committee, plaintiff alleged that Cole and/or his personally selected directors were responsible for nominating and electing the committee members to KCP's board. In this regard, the question is whether a director is beholden to the controlling party or so under that party's influence that the director's discretion would be compromised. Friendships, traveling in the same circles, some financial ties, and past business relationships are not enough to rebut the presumption of independence; the ties must be material in the sense that they could affect impartiality (see id. at 649). None of the allegations of the complaint, even if true, indicate that any of the members of the special committee engaged in fraud, had a conflict of interest or divided loyalties, or were otherwise incapable of reaching an unbiased decision regarding the proposed merger.

As to the third MFW condition, the complaint does not allege that the special committee lacked the freedom to reject Cole's offer or was prevented from hiring its own advisors, nor does it dispute that the committee did, in fact, select its own financial advisors and legal counsel. Plaintiff's speculation that the committee merely submitted to Cole's wishes is insufficient to state a cause of action for breach of fiduciary duty, particularly in view of Cole's statement at the time of his initial proposal that, if the committee did not recommend approval or the minority shareholders did not vote in favor of the proposed transaction, such a determination "would not adversely affect [his] . . . relationship" with KCP.

Turning to the fourth condition, while the complaint contains various allegations suggesting that the special committee could have been more effective in negotiating a higher buy-out price, none of those allegations are sufficient to support more than conclusory assertions that the committee failed to meet its duty of care in negotiating a fair price. Significantly, the complaint fails to allege any basis to conclude that the committee had an incentive to accept an inadequate price without meaningful negotiations or that it engaged in any unfair conduct. Additionally, the final price of $15.25 per share was higher than the original offer, was within the range of value determined by the committee's independent financial analysts, was recommended by the committee's independent legal counsel and financial advisors, and was higher than the stock's price prior to Cole's announcement that he intended to take the company private.

Regarding the fifth condition, the complaint lacks any specific challenges to the information contained in, or allegedly omitted from, the proxy statement provided to the minority shareholders prior to the vote, such that it could be said that the shareholders were not informed. Finally, plaintiff did not allege any coercion of the minority shareholders in relation to the vote.

Because plaintiff has not sufficiently alleged that any of the six enumerated MFW conditions were absent, the business judgment standard of review applies to the transaction at issue. Pursuant to that standard, absent fraud or bad faith, we defer to the determinations of the special committee and the KCP board of directors in recommending and approving the merger.

Inasmuch as no fraud or bad faith has been alleged here, the complaint was properly dismissed. Accordingly, the Appellate Division order should be affirmed, with costs.

* * * *

Order affirmed, with costs. Opinion by Judge Stein. Judges Pigott, Rivera, Abdus-Salaam, Fahey and Garcia concur. Chief Judge DiFiore took no part.

IV. CHAPTER 5, INTRODUCTION TO THE TAX ASPECTS OF MERGERS AND ACQUISITIONS

A. Page 395, New Sec. 5.3.C. Introduction to the 2017 Tax Cuts and Jobs Act (TCAJA)

Page 1, New Sec. 5.3.C. Add the immediately before Section 5.4 the following:
New Sec. 5.3.C. **Introduction to the 2017 Tax Cuts and Jobs Act (TCAJA)**

The 2017 Tax Cuts and Jobs Act (TCAJA) amended many of the provisions of the Internal Revenue Code, including many provisions that impact domestic and international operations of the four principal ways of operating a business: (1) sole proprietorship, including single member LLC; (2) partnership, including multimember LLCs; (3) S corporation; and (4) C corporation. Many of the changes have an impact on mergers and acquisitions.

This section merely hits the most salient of the changes made by the TCAJA that impact domestic M&A. A discussion of most of the generally significant domestic related business provisions of the TCAJA are discussed in the August 2018 supplement to Thompson, *Corporate Taxation Through the Lens of Mergers and Acquisitions*. Also, the most significant international related business provisions of the TCAJA are discussed in the August 2018 Supplement to Thompson, *U.S. International Tax Planning and Policy*. Both Supplements and books are available through Carolina Academic Press.

The following is a list of some highpoints relating to the impact of the TCAJA on domestic M&A:

- The TCAJA made no significant direct changes to subchapter C of the Code, including the provisions governing tax-free reorganizations and taxable acquisitions.
- The TCAJA lowered the tax rate on all C corporations to a flat 21%, a significant reduction from the previous top 35% rate.
- The maximum individual rate for ordinary income is 37%; however, the TCAJA enacted section 199A, which gives certain taxpayers a 20% deduction from their qualified business income, which is generally active business income. For individuals in the 37% bracket for ordinary income, the deduction will lower their effective tax rate on their qualified business income to close to 29%.
- The TCAJA made no changes to the taxation of an individual's long term capital gains (*i.e.*, net capital gain) and dividends, so the maximum rate on these items continues to be 23.8%.

- As a result of the corporate rate going down to 21%, while the maximum individual rate on dividends and capital gains stays at 23.8%, there can be an incentive for corporations to retain earnings. This will likely put pressure on the accumulated tax and the personal holding company tax, both of which are designed to fight against accumulations of income in corporations.
- The TCAJA enacted bonus depreciation, which will allow for full deductibility of the cost of certain personal property. This provision may make taxable asset acquisitions more attractive.
- On the other hand, the TCAJA enacted a 30% limit on the deductibility of business interest. This will likely have the effect of deterring some leveraged buyouts.

V. CHAPTER 7, MODERN VALUATION TECHNIQUES IN M&A

A. Page 483, New Sec. 7.12a. The Delaware Supreme Court's Discussion of Certain Elements of the DCF Methodology Used by the Court of Chancery in *Dell*

Page 57, New Sec. 7.12a. Add before Sec 7.13 the following:
New Sec. 7.12a. **The Delaware Supreme Court's Discussion of Certain Elements of the DCF Methodology Used by the Court of Chancery in *Dell***

Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.
Delaware Supreme Court, 2017, 177 A.3d 1

[This is the portion of the Supreme Court's decision addressing the Chancery Court's DCF analysis. The portion addressing the appraisal action generally is in Chapter 2 of this Supplement.]

VALIHURA, Justice:

[In this case Vice Chancellor Laster applied a DCF analysis in appraising the stock of Dell. As noted in the excerpt from this decision in Chapter 2, the Supreme Court "REVERSE[D], in part, and AFFIRM[ED], in part, and REMAND[ED]." In remanding the Court left open the possibility that the Vice Chancellor could revisit the DCF mythology, and the Court discussed several aspects of that methodology , which are set out here.]

i. Tax Issues

We note at the outset that the Company challenges the Court of Chancery's treatment of somewhat novel tax issues. These issues involve highly fact-specific, subjective determinations—the outcomes of which can cause wide differences in the ultimate DCF valuation. The parties have focused proportionately little attention on these issues before this Court, adding to our inclination to defer to the trial court, or remand for further consideration, where the record before us is not sufficiently developed on these complex, technical issues.

a. Terminal Period Tax Rate

Dell argues that the Court of Chancery abused its discretion in using Dell's 21% effective tax rate, rather than the top marginal tax rate under U.S. law (and an addition for state taxes) in its model's terminal period. But this effective tax rate reflected the Company's operative reality as of the merger date, and the evidence supports the Court of Chancery's decision that this operative reality was likely to continue. There is precedent favoring adopting tax rates consistent with the operative reality of the company under consideration. The 21% tax rate is just that—in line with Dell's history and apparently consistent with its tax-paying future. For example, Dell paid effective tax rates ranging from 16.5% to 29.2% in the five years before the Merger—including an average of 18.5% in the three years preceding the Merger—so 21%, the tax rate selected by management, is right in the ballpark. JPMorgan and Evercore also used a tax rate of 21% in the terminal periods of their own DCF calculations.

In contrast, in advocating that we apply the marginal tax rate of 35% plus 0.8% for state taxes to all Dell's earnings in the terminal period, the Company urges us to adopt a tax rate that Dell never paid and has no plans of paying. Given the ample reasons to apply the 21% effective tax rate to the terminal period, the Court of Chancery did not abuse its discretion.

b. Deferred Taxes

We find that the Court of Chancery erred in its conclusion that the effective tax rate accounted for the inevitable taxes that the Company would have to pay upon repatriating its foreign earnings and profits and, thus, remand for further consideration of what repatriation deduction is necessary.

Cash flows need to be available to stockholders in order to add value as part of a company's going concern. And, to be available to stockholders, the cash needs to be in the United States. Further, in order to be in the United States, foreign earnings and profits must be subjected to taxation when they return to the country, i.e., upon repatriation.

The trial court's free cash flow projections in its DCF valuation include all earnings, both domestic and foreign. The Court of Chancery's model also applied the same effective tax rate to all of those cash flows because, indeed, the effective tax rate is the aggregate tax rate covering both domestic and foreign earnings: it is lower than the statutory marginal tax rate to account for the lower tax rates applied to income earned abroad, adjusted against the proportion of income coming from each of the respective foreign jurisdictions.

But the Court of Chancery's analysis cannot end there. Though the effective tax rate accounts for the disparate tax treatment of Dell's income in various jurisdictions, including various tax holidays, it does not account for the tax consequence upon repatriation, as the Court of Chancery believed. Thus, to cure the existing asymmetry in the Court of Chancery's model, i.e., the model's inclusion of foreign earnings and profits in cash flow without any corresponding tax consequences upon repatriation, the Company is right that the model needs to account for the additional, previously-unaccounted-for tax consequence of repatriation.

However, the Company's proposed $2.24 billion deduction appears excessive as it assumes tax rates of over 30% upon repatriation. Dell's operative reality shows that the Company has never paid close to that rate when repatriating foreign earnings and profit and had no plans to repatriate vast amounts of money in the foreseeable future. In fact, in the past twenty years, Dell only repatriated "significant" amounts of such earnings during repatriation tax holidays and never paid more than 5.25% on such earnings and profit. Thus, contrary to the Company's proposal, it seems consistent with its operative reality to assume that Dell would only repatriate such earnings and profit when it would be subject to as little tax as possible, signaling that the Company's proposed $2.24 billion deduction is too big.

We remand this issue for further consideration given that the effective tax rate does not account for the future cost of repatriating Dell's foreign earnings. On remand, if the Court of Chancery decides to rely upon a DCF as part of its award, it has the discretion to seek additional input from the parties, and from a court-appointed expert, to resolve this issue. We do not dictate any outcome other than that the court's treatment of Dell's foreign earnings must include its corresponding tax consequences. That is, if the Court of Chancery chooses to include foreign earnings in its analysis, it should adjust its model to include some rational tax consequence upon repatriation. Otherwise, the court should exclude those earnings, consistent with its own assumption that they will be reinvested abroad indefinitely and thus never available to pay the Company's stockholders.

c. FIN 48

Dell's final tax argument on appeal is that the Court of Chancery abused its discretion by reducing its calculation by only $650 million instead of $3.01 billion to account for possible tax liability that the Company could face if tax authorities ultimately disagree with its positions on certain tax issues.

This is a complicated issue for many reasons, not the least of which is the absence of guidance in respected valuation treatises as to how to account for a so-called FIN 48 reserve when conducting a DCF valuation. FIN 48 is the Financial Accounting Standards Board interpretive statement that requires companies to create a reserve to account for tax benefits that are too uncertain to be recognized in a company's financial statements.

Applying this guidance, Dell created a $3.01 billion FIN 48 reserve based on its view that it was more likely than not that $3.01 billion would be due if Dell's positions on certain tax issues were contested. But, in its DCF valuation, the Court of Chancery only subtracted $650 million from its enterprise value, not the full $3.01 billion. On appeal, Dell argues that this was error because the Court of Chancery misunderstood the FIN 48 standard and therefore failed to include the full reserve amount.

Dell is correct as to one part of its argument. In its decision, the trial court collapsed the two-step process for creating this reserve by stating that the FIN 48 reserve "measures the tax payment a company expects to pay if a taxing authority disagrees with its position even though it thinks it is more likely than not that its position is correct." In fact, as the first step in creating the FIN 48 reserve, a company recognizes "the financial statement effects of a tax position when it is more likely than not, based on the technical merits, that the position will be sustained upon examination."203 Then, as the second step, a company must maintain as a liability on its balance sheet "unrecognized tax benefits, which are the differences between a tax position taken or expected to be taken in a tax return and the benefit recognized . . . ."

But the problem for Dell is that the error of the Court of Chancery does not translate directly into reversible error for an important reason. There is no agreement in the record that all of a FIN 48 reserve should be deducted when conducting a DCF analysis, and Dell has not cited corporate finance literature supporting its argument that the entirety of a FIN 48 reserve must be deducted. To be fair, Dell has cited corporate finance literature saying that the potential for tax liability has to be considered in calculating enterprise value. But, assuming that is right, Dell did not present a persuasive way of doing so when, as under FIN 48, the reserve is dealing with probabilities and, therefore, there is a need to decide on the amount of the reserve to be deducted. In fact, Dell's own expert testified that the question of how to treat FIN 48 reserves was not a common one and that he was unaware of any appraisal treatise that directs appraisers to deduct all of a FIN 48 reserve when calculating enterprise value. By definition, a reserve based on a more likely than not standard has a fairly large degree of uncertainty. And, there was factual testimony here that provided a factual basis for the Court of Chancery's determination to deduct only $650 million.

In his trial testimony, Dell's CFO spoke directly to the likelihood that Dell would face liability on the reserved amounts. That testimony indicated that, between 2013 and 2018, $650 million was the amount of Dell's FIN 48 reserve that was most likely to come due. Given that there is uncertainty in the valuation literature and the record about the extent to which a FIN 48 reserve should be deducted from enterprise value, we cannot find that the Court of Chancery's decision to deduct only the $650 million that was most likely to come due in the near future was an abuse of discretion.

Not only that, but there is evidence in the record that the Company's calculation of its effective tax rate took into account the FIN 48 reserve. Thus, by deducting the portion of the FIN 48 reserve that the record evidence showed was most likely to come due, and adopting an effective tax rate based in part on consideration of the issues addressed by the reserves, the Court of Chancery's decision was grounded in the record.

We are reluctant to speak broadly about this issue because the record below and before us is devoid of reliable guidance about how FIN 48 reserves should be treated in the calculation of a DCF. The unreliability of the record and our duty to respect the difficult task of trial judges in these cases leaves us unprepared to disturb the Court of Chancery's ultimate finding on this issue, despite its misstatement of the FIN 48 standard.

ii. Cross-Appeals

Petitioners cross-appealed alleging that, to the extent the Court of Chancery erred in formulating its DCF, it did so by adopting the revisions that Dell's expert applied to the BCG 25% Case projections and including deductions for working capital and restricted cash. We find that these choices do not amount to an abuse of discretion.

a. Projection Adjustments

The Court of Chancery did not abuse its discretion in adjusting the BCG 25% Case projections, which it factored into one of the two DCF calculations that it later averaged to arrive at its final determination of fair value. Though petitioners argue that the BCG 25% Case underestimated cost savings, both experts agreed that it was largely reliable.211 Petitioners' attorney also conceded at oral argument that "[e]veryone agrees that th[e] BCG 25% Case] is the best set of projections."

Petitioners also question the decision of Dell's expert, Hubbard, to update the projections to reflect the latest pre-Merger IDC report (August 2013) that suggested PC sales would continue to decline even further than anticipated industry-wide. Given that BCG had previously adjusted its projections to account for new IDC forecasts, it would seem to make sense that the projections as of the date of the Merger would need to include the most recent figures.

But petitioners argue that the projections' creator, Lutao Ning of BCG, testified at trial that one could not simply swap out old IDC data for new figures and that, regardless, the IDC numbers only corroborated the accuracy of BCG's projections because the projections forecasted such declines. We defer to the Court of Chancery's assessment of this testimony and its decision to adjust for the latest IDC report, especially since the trial court attempted to balance the "likely somewhat conservative" Adjusted BCG 25% Case against the "likely somewhat optimistic" adjusted Bank Case projections in the court's final fair value determination. It averaged two DCF valuations using all the same inputs other than these two sets of projections in arriving at its final fair value figure. This choice, which is unchallenged, was designed to minimize any over-pessimism in tweaking the IDC numbers. The Court of Chancery had logic for its adjustment to the projections, and this adjustment did not amount to an abuse of discretion.

b. Cash

Petitioners also challenge the Court of Chancery's deductions of $3 billion for working capital and $1.2 billion for restricted cash from Dell's enterprise value. Neither of these judgment calls amounts to an abuse of discretion.

Dell's CFO testified that the Company needed at least $5 billion in working capital to support its operations (including $2 billion restricted cash), and documentary evidence corroborates this view. It was reasonable for the Court of Chancery to believe this evidence supported the working capital deduction. Dell's CFO testified that the Company needed cash on hand to accommodate "seasonality" and "geographical friction," and the Court of Chancery did not abuse its discretion in crediting this testimony.

The Court of Chancery also did not abuse its discretion in deducting $1.2 billion of the $2 billion deduction for restricted cash advocated by the Company. The trial court did not deduct $0.8 billion of that total because evidence showed it had become unrestricted before the Merger and thus could no longer be counted among the restricted pool. There was some evidence at the time of the Merger that some Chinese regulations that restricted much of the cash were changing so as to allow Dell to access it and thus also eliminate the need for a portion of the remaining $1.2 billion deduction. But the record does not specify how much capital was likely to become unrestricted. Thus, we defer to the Court of Chancery's judgment in declining to shrink the deduction even further in light of the sparse record on restricted cash.

III. Fair Value Conclusion

[On remand, if the Vice Chancellor] decides to follow another route, the outcome should adhere to our rulings in this opinion, including our findings with regard to the DCF valuation. * * *

B. Page 483, New Sec. 7.12b. Vice Chancellor Laster's DCF Analysis in Aruba, Post-*Dell*

Page 483, New Sec. 7.12b. Add after the new Sec 7.12a the following:
New Sec. 7.12b. **Vice Chancellor Laster's DCF Analysis in Aruba, Post-*Dell***

[The discussion here does not include the court's general appraisal analysis, which led it to conclude that the pre-deal trading price was the fair value. That analysis is included in Chapter 2 of this Supplement, which deals with Voting and Dissenting.]

Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.,
Delaware Court of Chancery, Jan. 26, 2018, 2018 Del. Ch. LEXIS 52.

MEMORANDUM OPINION

LASTER, V.C.

[As indicated in Chapter 2,] Hewlett-Packard Company ("HP") acquired Aruba Networks, Inc. ("Aruba" or the "Company") for $24.67 per share and several shareholders moved to have their shares in Aruba appraised. The discussion here focuses principally on the court's DCF analysis.] The petitioners perfected their appraisal rights and litigated this statutory appraisal proceeding. This is the court's post-trial decision on the issue of fair value.] * * *

C. The Experts' Analyses

Both sides submitted opinions from valuation experts. Both experts used the discounted cash flow methodology to value Aruba. Both experts believed that the discounted cash flow methodology provided the best approach for determining the fair value of the Company. The respondent's expert, Kevin Dages, said so explicitly: "It is my opinion that Aruba's standalone fair value is most accurately measured using a [discounted cash flow] analysis based on the Management Projections." The petitioners' expert, Paul Marcus, expressed his view implicitly by relying exclusively on the discounted cash flow approach.

The discounted cash flow methodology is a valuation technique that the financial community generally accepts and that this court frequently uses in appraisal proceedings. "While the particular assumptions underlying its application may always be challenged in any particular case, the validity of [the discounted cash flow] technique qua valuation methodology is no longer open to question." 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."

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.

The Delaware Supreme Court has recently cautioned that "[a]lthough widely considered the best tool for valuing companies when there is no credible market information and no market check, [discounted cash flow] 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."

1. Marcus's Valuation Opinion

Marcus used a discounted cash flow analysis to opine that the Company's fair value at closing was $32.57 per share. His model generally adhered to the valuation literature and the teachings of the Delaware courts. From a methodological perspective, his model appears sound.

As a source of estimated future cash flows, "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."[5] Marcus used the February Projections, which covered the fiscal years 2015-2017. The February Projections had their roots in management's three-year plan, prepared in the ordinary course of business and with input from the Aruba Board. Management completed an iteration of its three-year plan in summer 2014. Management updated the plan in October 2014. In February 2015, management revised the plan to reflect intervening results and to adopt more conservative assumptions. To cover the final two

[5] [Originally footnote 417] Doft & Co. v. Travelocity.com Inc., 2004 Del. Ch. LEXIS 75, 2004 WL 1152338, at *5 (Del. Ch. May 20, 2004); see also Cede & Co. v. Technicolor, Inc., 2003 Del. Ch. LEXIS 146, 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. Experts who then vary from management forecasts should proffer legitimate reasons for such variance.") (footnote omitted)), rev'd in part, aff'd in part, 884 A.2d 26 (Del. 2005); Gray v. Cytokine Pharmasciences, Inc., 2002 Del. Ch. LEXIS 48, 2002 WL 853549, at *8 (Del. Ch. Apr. 25, 2002) (finding "litigation-driven projections to be unreliable" because "[a]ny other result would condone allowing a company's management or board of directors to disavow their own data in order to justify a lower valuation in an appraisal proceeding").

years of his projection period, Marcus used an extension of the February Projections that Qatalyst prepared working in conjunction with Aruba management. Qatalyst used the same projections as the basis for the fairness opinion that it delivered to the Aruba Board. Aruba also used the same projections in the proxy statement for the deal. Marcus adopted management's estimates for the cost of stock-based compensation and Aruba's tax rates.[6]

The projections resulted in Aruba having a high compound annual growth rate ("CAGR") of 10% at the end of the projection period. To normalize Aruba's high growth and transition the Company into a steady state, Marcus added a second, five-year stage to create a three-step discounted cash flow model. During the added second stage, he stepped down the growth rate to reach his terminal, third-stage growth rate of 3.5% per year. Delaware decisions and the valuation literature support this approach.[7] Like Marcus, HP used a three-stage discounted cash flow method when valuing Aruba.

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[6] [Original footnote 426] The Company had projected a tax rate of 4% for 2015 and 2016 and 25% thereafter. See JX 475 at 1 (email from Galvin to Qatalyst suggesting "I would do 4% thr[ough] 17; then do 25% thereafter"). Management attributed the rate to the Company's stockpile of valuable net-operating loss credits or "NOLs" from its early, pre-profit days. Due to those credits, the Company had a cash tax rate of only 3.2% and 3.1% in 2013 and 2014, respectively. The Company anticipated it had enough credits remaining to continue paying low taxes through at least 2016. JX 506 at 1 (internal email summarizing available net-operating loss credits and approximate use rates as of February 2015); see also JX 895 at 93 (2014 10-K: "As of July 1, 2014, the Company's federal loss carryforwards for income tax purposes were approximately $131 million with expiration dates starting in 2028."). Based on this evidence, Marcus adopted the Company's estimates. See Marcus Opening Report Ex. 7-1.

Aruba instructed Qatalyst to use the same tax figures that Marcus ultimately adopted. See JX 654 (Qatalyst working spreadsheet indicating Galvin provided tax rates); Marcus Tr. 46-47; Galvin Tr. 622.

[7] [Original footnote 428] See, e.g., DFC, 172 A.3d at 380 ("Indeed, if the record unambiguously supported the proposition that DFC was to continue a new spurt of growth past 2018, it would have been more appropriate to project out to a point where steady-state growth began. By doing that, the appraiser would have to assess with discipline the next period after the projections end and also the potential that the period might be negative, as well as that another period of above-market growth might be followed by a terminal growth rate more like inflation than the risk-free rate." (footnote omitted)); Prescott Group Small Cap, L.P. v. Coleman Co., Inc., 2004 Del. Ch. LEXIS 131, 2004 WL 2059515, at *29 (Del. Ch. Sept. 8, 2004) (Jacobs, J.) ("At the time of the merger, Coleman was projecting a 16% growth in sales for year 2002, which represented a return to Coleman's prior operating levels. Dr. Kursh utilized a three stage model because he did not believe a 16% growth rate was sustainable long-term." (footnote omitted)); Robert W. Holthausen & Mark E. Zmijewski, Corporate Valuation Theory,

Marcus calculated Aruba's weighted average cost of capital ("WACC") using the capital asset pricing model ("CAPM").[8] "Under CAPM, the cost of equity capital is the risk-free rate of return plus the subject company's risk. The subject company's risk is determined by multiplying the equity risk premium for the market by the company's beta." Marcus used a risk-free rate of 2.75%, based on the twenty-year U.S. Treasury maturity rate, and a supply-side equity risk premium of 6.19%. Marcus drew these figures from reliable sources, and Dages used the same risk-free rate and a virtually identical supply-side equity risk premium. Marcus calculated a beta for Aruba of 0.91, which he derived by giving one-third weight to Aruba's two-year, weekly, raw beta (0.81) and two-thirds weight to the two-year, weekly, raw, unlevered betas of a group of peer companies (1.11). Court of Chancery precedent supports the blended approach,[9] and the

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Evidence & Practice 216 (2014) ("We would prepare detailed year-by-year forecasts for the company until the company reaches steady state. You may need to value a company's cash flows for five years, ten years, or longer if the company is far from becoming a stable mature company as of the valuation date."); Shannon P. Pratt & Alina V. Niculita, Valuing a Business 219 (5th ed. 2008) ("The appropriate length of the forecast period should be until that variability stops; at the point in time that the company expects normalized or level growth, the terminal value is calculated.").

[8] [Original footnote 430.] In calculating his WACC, Marcus used an all-equity capital structure. He noted, however, that evidence in the record suggested that Aruba would have issued $300 million in convertible debt if HP had not made its approach. See, e.g., PTO ¶ 51, JX 224 (Aruba Board subcommittee minutes); JX 325 (email from Galvin relaying conversation with Barclays banker wherein banker suggested executing the convertible offering). The debt would have reduced Aruba's WACC and been a positive signal to the equity markets. Marcus Opening Report ¶ 223. The decision to maintain Aruba's all-equity capital structure could be seen as a valuation consequence that resulted from the expectation of the merger, although one that had a negative effect on Aruba's stockholders by depriving them of the value generated by a lower-cost capital structure. Cf. 8 Del. C. § 262(h) (instructing Court of Chancery to exclude "any element of value arising from the accomplishment or expectation of the merger"). The petitioners have not made this argument, so this decision does not consider it.

[9] [Original footnote 435.] See Merion Capital, L.P. v. 3M Cogent, Inc., 2013 Del. Ch. LEXIS 172, 2013 WL 3793896, at *18 (Del. Ch. July 8, 2013) ("[O]ne 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 . . . ."); Golden Telecom Trial, 993 A.2d at 524 ("I find that a beta that gives 2/3 weight to the Bloomberg historic raw beta of 1.32 and 1/3 weight to the 1.24 industry beta is the best approach to this DCF analysis.").

valuation literature supports the selection of a two-year period for Aruba.[10] He then added the fifth-decline size premium.[11] These calculations resulted in a 10% WACC.[12]

To calculate value for the terminal period, Marcus used the Gordon Growth Model. "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." As noted, Marcus selected a perpetuity growth rate of 3.5%. He believed it was reasonable to assume that Aruba would grow at the rate of the overall economy, but to be conservative he selected a growth rate approximately

[10] [Original footnote 436.] Holthausen & Zmijewski, supra, at 300 ("Using more recent data might better reflect a company's current (and more forward-looking) systematic risk."); Tim Koller, Marc Goedhart & David Wessels, Valuation: Measuring and Managing the Value of Companies 247 (5th ed. 2010) (noting that "changes in corporate strategy or capital structure often lead to changes in risk for stockholders" and that, where that occurs, "a long estimation period would place too much weight on irrelevant data"); Shannon P. Pratt & Roger J. Grabowski, Cost of Capital: Applications and Examples 208 (5th ed. 2014) (noting that five-years is more common but where "business characteristics change during the sampling period . . . it may be more appropriate to use a shorter sampling period. However, as the sampling period used is reduced, the accuracy of the estimate is generally reduced."); id. at 224 (recommending that "[i]f the underlying fundamentals of the business have changed, a more recent period should be used in developing a beta estimate"). Aruba had grown significantly during the years preceding the merger. See PTO ¶ 77. Aruba's expert agreed that he typically uses a two-year weakly raw beta when calculating WACC. Dages Tr. 793; Dages Dep. 432.

[11] [Original footnote 437] Marcus Opening Report ¶ 230. "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." Gearreald v. Just Care, Inc., 2012 Del. Ch. LEXIS 91, 2012 WL 1569818, at *10 (Del. Ch. Apr. 30, 2012). Dages disputed the applicability of a size premium at all because, "in [his] experience, a size premium is rarely applied to midor larger-cap companies" and "Aruba did not share the characteristics that researchers have hypothesized for returns in excess of what is predicted by the CAPM." Dages Rebuttal Report ¶ 32. He further argued that Aruba properly belonged in the sixth rather than fifth decile. Id.

[12] [Original footnote 438.] Dages used a WACC of 11%. Dages observed that all three deal advisors and two research analysts used higher WACCs. Dages Opening Report Ex. 18; Dages Rebuttal Report ¶ 31.

at the midpoint of the risk-free rate (2.75%) and nominal GDP growth rate, as predicted by reliable, oft-cited studies (4.3%).[13]

Marcus sensitized his valuation for discount rates of 9.5% to 10.5% and terminal growth rates of 3.0% to 4.0%, generating a valuation range for $29.16 to $36.93. The midpoint, based on a discount rate of 10% and a terminal growth rate of 3.5%, was $32.57.

My primary concerns with Marcus's opinion are his beta and the contrast between his valuation and market indicators. Marcus's raw and blended betas were both lower than one, indicating that Aruba, a relatively young and growing technology company, exhibited less volatility than the market as a whole.[14] Although the data supported the low beta, no one could offer a good explanation as to why the number was so low.[15] Marcus's beta of 0.91 also fell roughly 20% below the median two-year adjusted beta of companies in Aruba's peer group and approximately 35% below Aruba's five-year adjusted weekly beta. That said, Aruba's low beta was not unique. The bankers' fairness presentations identified other networking and WiFi companies that had betas of less than 1.

Marcus's valuation outcome diverged significantly from market indications. His valuation of $32.57 is

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[13] [Original footnote 441.] Marcus Opening Report ¶¶ 232-235. Marcus did not clarify why he adopted the risk-free rate rather than the projected rate of inflation as the floor for his terminal growth rate. As discussed in addressing Dages's report below, some of this court's precedent suggests adopting the risk-free rate as a ceiling for a company's long-term sustainable growth rate. This court's precedents support adopting the rate of inflation as a floor for a company's long-term growth rate. See Golden Telecom Trial, 993 A.2d at 511-12 ("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."); see also Owen v. Cannon, 2015 Del. Ch. LEXIS 165, 2015 WL 3819204, at *25 (Del. Ch. June 17, 2015) ("I find that it is appropriate under Golden Telecom to calculate the terminal growth rate as a premium to inflation."). The distinction does not alter the outcome in this case, and this decision expresses no view on the issue.

[14] [Original footnote 443.] Dages Tr. 747; see also Pratt & Grabowski, supra, at 194 ("Many high-tech companies are good examples of stocks with high betas. . . . The classic example of a low-beta stock would be a utility that has not diversified into riskier activities.").

[15] [Original footnote 444.] See, e.g., Dages Tr. 790-91 ("I don't see a basis for getting comfortable with a beta that is that low given this company, its position in the industry, and what I've heard about the challenges it's facing. Especially when I look at the peers and they are all up over 1. And I look at them, and they are well over 1 in a longer time period.").

• approximately 32% higher than the deal price of $24.67;

• approximately 39% higher than the mean of the last batch of unaffected analyst price targets at $23.4;

• approximately 21% above the mean of the midpoints of the final valuations prepared by all three advisors at $26.57; and

• nearly double Aruba's thirty-day average unaffected market price of $17.13 per share.

Despite its seemingly [*94] sound methodology, these market indicators combine to create significant doubt regarding the reliability of the Marcus discounted cash flow analysis and its resulting valuation.

2. Dages's Valuation Opinion

Dages rendered several different valuation opinions. They produced relatively stable outputs but changed substantially in their inputs. Dages also made a significant judgment call by selecting a WACC from a menu of possibilities, rather than calculating a beta to generate a WACC as contemplated by CAPM.

In his opening report, Dages opined that the standalone fair value of Aruba was $19.85 per share, which he derived using a discounted cash flow methodology. Like Marcus, Dages used the February Projections with the two-year extension prepared by Qatalyst with management's input. Unlike Marcus, who used management estimates for stock-based compensation and tax rates, Dages used a stock-based compensation figure from Barclays, and his own estimate of Aruba's effective tax rate.[16] Despite recognizing the issue raised by Aruba's high growth rate at the end of the projection period, Dages used a traditional two-stage model rather than a three-stage model. For his terminal value, Dages explained the principles used when selecting a long-term growth rate in much the same terms as Marcus, but then chose the risk-free rate (2.75%) because "some financial economists caution that the risk-free rate . . . should serve as the ceiling for a stable, longterm growth rate" and this court had used that rate in "a recent opinion."[17]

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[16] [Original footnote 452.] See id. ¶ 115 (using tax rate of 30%). Dages stated in his report that "[t]he 30.0 percent tax rate is based on the effective tax rate used by Aruba in the Management Projections." Id. At trial, he admitted that this was an error. See Dages Tr. 732-33; 812-15.

[17] [Original footnote 455.] See id. ¶ 110. Dages's report did not cite the financial economists or the opinion. Presumably, he was referring to the DFC trial-level opinion, where he also served as an expert. There, Chancellor Bouchard adopted the risk-free rate as a ceiling in reliance on Dages's identical suggestion "that some financial economists view the risk-free rate as the ceiling for a stable, long-term growth rate." DFC Trial, 2016

For his discount rate, Dages started out using CAPM to develop a WACC. He used the same risk-free rate as Marcus (2.75%) and a supply-side equity risk premium that was substantially similar to Marcus's (6.21%). On the issues of a beta and size premium, however, Dages punted. He described a variety of possible betas, including (i) raw and adjusted betas for Aruba derived using two years of weekly measurements, five years of weekly measurements, and five years of monthly measurements, and (ii) raw and adjusted betas for peer companies derived using the same measuring periods. Rather than selecting a beta, Dages used the various candidates to generate nine possible WACCs. He then added into the mix the WACCs used by the three financial advisors and WACCs from two analysts, for a total of fourteen possibilities. After surveying these, he chose a WACC of 11%. His WACC implied a beta of 1.33. This court has criticized similarly unstructured approaches to valuation inputs.[18]

Del. Ch. LEXIS 103, 2016 WL 3753123, at *17. In that case, Dages had also acknowledged that "one suggested ceiling for a company's perpetuity growth rate is nominal GDP." 2016 Del. Ch. LEXIS 103, [WL] at *18; see also Golden Telecom Trial, 993 A.2d at 511 ("Generally, once an industry has matured, a company will grow at a steady rate that is roughly equal to the rate of nominal GDP growth."). Dages conceded that a 4.5% perpetuity growth rate, substantially above the 3.14% risk-free rate calculated in that case, was "at the high end of the reasonable range of long-term growth rates." DFC Trial, 2016 Del. Ch. LEXIS 103, 2016 WL 3753123, at *18. On appeal, the Delaware Supreme Court stated that the risk-free rate "is viewed to be the ceiling for a stable, long-term growth rate." DFC, 172 A.3d at 383. The idea that a company in a steady state will grow more or less in line with the average rate of the broader economy has intuitive appeal. See 3M, 2013 Del. Ch. LEXIS 172, 2013 WL 3793896, at *21 (quoting Golden Telecom for the proposition that "the rate of inflation is the floor for a terminal value" and noting that "a terminal growth rate should not be greater than the nominal growth rate for the United States economy"). Because the experts did not develop the issue further, and because resolving it is not necessary to decide this case, this decision expresses no opinion on the matter.

[18] [Original footnote 462.] See In re Orchard Enters., Inc., 2012 Del. Ch. LEXIS 165, 2012 WL 2923305, at *17 (Del. Ch. July 18, 2012) (Strine, C.) (expressing the court's preference for "the more academically and empirically-driven CAPM model when that can be applied responsibly" and noting that it involves "less (but still more than comfortable) amounts of subjectivity"); Del. Open MRI, 898 A.2d at 338 (questioning the use of the build-up method with its concept of "company-specific risk" and observing "[t]he calculation of a company specific risk is highly subjective and often is justified as a way of taking into account competitive and other factors that endanger the subject company's ability to achieve its projected cash flows. In other words, it is often a back-door method of reducing estimated cash flows rather than adjusting them directly. To judges, the company specific risk premium often seems like the device experts employ to bring their final results into line with their clients' objectives, when other valuation inputs fail to do the trick."); Andaloro, 2005 Del. Ch. LEXIS 125, 2005 WL 2045640, at *12 n.49 (criticizing expert who "spiraled" into a terminal growth rate "through an incomprehensible 'iterative process'" and finding that "[r]ather than a reasoned exercise in

After I issued an evidentiary ruling precluding Dages from rendering an opinion on stock-based compensation, Dages changed course and relied at trial on a set of projections that he had created himself using industry growth rates and referenced in a footnote in his opening report.[19] When he ran his discounted cash flow model with those projections and management's figures for stock-based compensation expense, his model generated a value of $19.45 per share, forty cents below his original opinion. At trial, Dages revised his view on Aruba's tax expenses and agreed with management's use of a 4% tax rate for 2015 and 2016, although he continued to endorse the use of a 30% tax rate for subsequent years rather than management's rate of 25%.[20] This modification added thirty cents per share to his valuation, resulting in a figure of $19.75 per share. Serendipitously, that result fell just ten cents below the valuation in his opening report, although reached using substantially different inputs. This is the fair value figure that Aruba endorsed at post-trial argument.

Dages's final opinion of $19.75 per share comported with market evidence by falling between the unaffected market price and the deal price. Its methodological underpinnings, however, provided cause for concern, as did the meandering route by which Dages arrived at this figure.

D. Weighing the Valuation Methodologies

This decision has discussed each of the relevant methods of valuation that the parties presented. Under the statute, the court must make a point estimate of fair value measured in dollars and cents. When determining fair value, "[t]he 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."

The forceful discussion of the efficient capital markets hypothesis in Dell and DFC indicates that Aruba's unaffected market price is entitled to substantial weight.

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applied social science, [the expert] appears to have channeled inspiration, more like a great songwriter than a valuation expert").

[19] [Original footnote 463.] Dages Tr. 760-61 ("Q. So to be clear, your opinion, when you originally opined, was the February revenue projections; right? A. Correct."); id. at 767 ("Q. So you didn't just swap out the Dell'Oro projected growth rates for the industry for management's. You created your own industry projections. A. Correct."); id. at 772 ("Q. Now, in fact, you don't have any expertise that would allow you to determine whether Dell'Oro's industrywide growth rates are a reasonable proxy for Aruba's expected future performance, do you? A. No. No independent expertise, no.").

[20] [Original footnote 464.] Dages Tr. 751, 813. In light of other evidence in the record, the cash tax rate is more persuasive. See Galvin Dep. 296 (stating that management provided the cash tax rate); JX 548 (Qatalyst spreadsheet showing management's cash tax rates); JX 654 (Qatalyst projections using management's cash tax rate); see also Dages Tr. 815 (testifying that cash tax rate is typically more accurate than effective tax rate).

[C]orporate 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 . . . .[21]

"Market 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." [22] "[I]n many circumstances a property interest is best valued by the amount a buyer will pay for it" and "a well-informed, liquid trading market will provide a measure of fair value superior to any estimate the court could impose." [23]

In this case, because Aruba's shares "were widely traded on a public market based upon a rich information basis," the fair value of the petitioners' shares "would, to an economist, likely be best reflected by the prices at which their shares were trading as of the merger." Aruba had "a deep base of public shareholders" and "highly active trading," so "the price at which its shares trade is informative of fair value." The unaffected thirty-day average market price of Aruba's stock was $17.13 per share.

Dell and DFC teach that the deal price is also entitled to substantial weight. "In economics, the value of something is what it will fetch in the market. That is true of corporations, just as it is true of gold." For a court to give weight to the deal price, it need not be the most reliable evidence of the Company's value as a going concern. This court has authority "to determine, in its discretion, that the deal price is the most reliable evidence of fair value . . . , and that's

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[21] [Original footnote 466.] DFC, 172 A.3d at 370; accord Dell, 2017 Del. LEXIS 518, 2017 WL 6375829, at *17 (explaining that, when a market is efficient, "a company's stock price reflects the judgments of many stockholders about the company's future prospects, based on public filings, industry information, and research conducted by equity analysts. In these circumstances, 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" (internal quotation marks and footnotes omitted)).

[22] [Original footnote 467.] DFC, 172 A.3d at 369-70; see also Dell, 2017 Del. LEXIS 518, 2017 WL 6375829, at *17 ("[T]he 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.").

[23] [Original footnote 468.] Applebaum, 812 A.2d at 890 (Del. 2002); see also Dell, 2017 Del. LEXIS 518, 2017 WL 6375829, at *15 n.108 (citing Applebaum); DFC, 172 A.3d at 369 & n.116 (quoting Applebaum).

especially so in cases . . . where things like synergy gains or minority stockholder discounts are not contested." [24]

The deal price in this case resulted from an arm's-length transaction involving a publicly traded company without a controlling stockholder. The deal price in this case contained synergies, so it logically exceeded fair value. There is also the fact that the petitioners failed to identify a bidder who would pay more than HP. "Fair value entails at minimum a price some buyer is willing to pay . . . ." Taken together, these propositions indicate that the deal price in this case operates as a ceiling for fair value.

The Dell and DFC decisions recognize that a deal price may include synergies and endorse deriving an indication of fair value from the deal price by deducting synergies. In this case, the evidence shows that the deal generated significant synergies. Using the low-end synergy range implies a standalone value of $21.08 per share. Using the high-end synergy range implies a standalone value of $15.32 per share. This decision has adopted the midpoint of $18.20 per share as its deal-price-less-synergies value.

This decision does not give any weight to the discounted cash flow analyses. As in Dell, "this appraisal case does not present the classic scenario in which there is reason to suspect that market forces cannot be relied upon to ensure fair treatment of the minority." Discounted cash flow models are "often used in appraisal proceedings when the respondent company was not public or was not sold in an open market check."

The reason for that is not that an economist wouldn't consider the best estimate of a private company's value to be the price it sold at in an open sale process of which all logical buyers were given full information and an equal opportunity to compete. Rather, the reason is that if such a process did not occur, corporate finance instructs that the value of the company to potential buyers should be reflected in its ability to generate future cash flows.

"But, a single person's own estimate of the cash flows are just that, a good faith estimate by a single, reasonably informed person to predict the future. Thus, a singular discounted cash flow model is often most helpful when there isn't an observable market price." 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."

Marcus's discounted cash flow valuation of $32.57 per share diverged substantially from market indications. His figure is nearly double Aruba's thirty-day average unaffected market price of $17.13. It is approximately 32% higher than the deal price of $24.67 per share. In a transaction involving a financial buyer that could be expected to generate few if any combinatorial

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[24] [Original footnote 473.] Id. at 367; see also Dell, 2017 Del. LEXIS 518, 2017 WL 6375829, at *16 ("In fact, the record as distilled by the trial court suggests that the deal price deserved heavy, if not dispositive, weight.").

synergies, the Delaware Supreme Court recently emphasized the lack of reliability of a discounted cash flow analysis that yielded a result that was 40% over the deal price.[25] The transaction in this case generated substantial synergies.

Dages's initial discounted cash flow valuation of $19.85 and revised discounted cash flow valuation of $19.75 fell nicely between the unaffected market price and the deal price. His figures also landed close to HP's standalone discounted cash flow valuation of $18.98 and Barclay's standalone discounted cash flow valuation of $19.93. The relative lack of methodological rigor in the analysis, however, creates cause for concern about the strategic selection of inputs to channel the result into this range.

The two probative indications of value in this case are the unaffected market price of $17.13 and the deal-price-less-synergies value of approximately $18.20 per share. Using these indicators nevertheless carries conceptual difficulties because "[t]he time for determining the value of a dissenter's shares is the point just before the merger transaction 'on the date of the merger.'"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.

The unaffected market price provides direct evidence of the collective view of market participants as to Aruba's fair value as a going concern during the period before the announcement of the transaction, which could be different than Aruba's fair value as of closing. The same disconnect exists for the deal price, which provides evidence of how the parties to the merger agreement valued Aruba during the price negotiations, which could be different than Aruba's fair value as of closing. Addressing a similar issue in the Union Illinois case, Chief Justice Strine described the temporal gap as a "quibble" and "not a forceful objection," noting that "[t]he negotiation of merger terms always and necessarily precedes consummation." Observing that "[n]othing in the record persuades me that [the company] was more valuable by [closing] than it was when the Merger terms were set," he continued to use the deal price as an indicator of value. Similarly in this case, neither side proved that Aruba's value had changed materially by closing, so this decision sticks with the unaffected market price and the deal price less synergies.

The difficult question is how to choose between, weigh, or otherwise exercise my discretion non-abusively when evaluating the two probative valuation indications. The unaffected market price provides a direct measure of the collective judgment of numerous market participants about Aruba's value as a going concern. The deal price less synergies provides an indirect measure with

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[25] [Original footnote 481.] DFC, 172 A.3d at 362; cf. Lender Processing, 2016 Del. Ch. LEXIS 189, 2016 WL 7324170, at *33 ("The proximity between [the discounted cash flow] outcome and the result of the sale process is comforting."); Ancestry.com, 2015 Del. Ch. LEXIS 21, 2015 WL 399726, at *23 ("The DCF valuation I have described is close to the market, and gives me comfort that no undetected factor skewed the sales process.").

two significant sources of uncertainty. One is the problem of measurement error. Under the traditional view of the efficient capital markets hypothesis, errors are randomly distributed and cancel out.[26] My deal-price-less-synergies figure could have errors at multiple levels. To cite just a few, I may have erred when making my case-specific allocation of synergies to the sell-side. I might have misinterpreted the information that Aruba's expert cited, or that data itself could contain sampling and measurement errors. The size of the original synergy estimates might also be off, as could any number of individual estimates that added up to the overarching estimates. After all, they were necessarily predictions about complex matters. Perhaps errors at one level might counterbalance errors at another, but there is no way to know, and the smaller number of judgments involved (compared to the number of trades generating the market price) makes it more likely that the errors could skew the figure, just like a small and undiversified portfolio can produce extreme results. The Delaware Supreme Court's expressed preference in Dell and DFC for market indicators over discounted cash flow valuations counsels in favor of preferring market indicators over the output of a similarly judgment-laden exercise of backing out synergies.

The other difficulty is that my deal-price-less-synergies figure continues to incorporate an element of value resulting from the merger. When an acquirer purchases a widely traded firm, the premium that an acquirer is willing to pay for the entire firm anticipates incremental value both from synergies and from the reduced agency costs that result from unitary (or controlling) ownership.[27] Like synergies, the value created by reduced agency costs results from the transaction and is not part of the going concern value of the firm.[28] The value belongs to the buyer, although the seller may extract a portion of it through negotiations.[29] Eliminating shared synergies therefore only goes part of the way towards eliminating "any element of value arising

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[26] [Original footnote 486.] See Ronald J. Gilson & Reinier H. Kraakman, The Mechanisms of Market Efficiency, 70 Va. L. Rev. 549, 581 (1984). Behavioral economics, noise theory, and chaos theory may provide reasons to question this assumption, but for the reasons already stated, I do not believe that a trial court has the flexibility to disregard the Delaware Supreme Court's framing of the efficient capital markets hypothesis.

[27] [Original footnote 488.] See Rationalizing Appraisal, supra, at 1038, 1049.

[28] [Original footnote 489.] See Rationalizing Appraisal, supra, at 1023-24, 1038, 1046-54, 1067; Implicit Minority Discount, supra, at 30-36, 52; Fair Value of Cornfields, supra, at 139-41.

[29] [Original footnote 490.] See Control Premiums, supra, at 866-71; Rationalizing Appraisal, supra, at 1052-53; Implicit Minority Discount, supra, at 35, 52.

from the accomplishment or expectation of the merger."[30] A court also must eliminate the share of value that accrues from the reduced agency costs.[31]

For Aruba, using its unaffected market price provides the more straightforward and reliable method for estimating the value of the entity as a going concern. I could strive to reach the same endpoint by backing out shared synergies and a share of value for reduced agency costs, but both steps are messy and provide ample opportunities for error. For Aruba, the unaffected market price provides a direct estimate of the same endpoint.[32] Rather than representing my own fallible determination, it distills "the collective judgment of the many based on all the publicly available information about a given company and the value of its shares. "[T]he price produced by an efficient market is generally a more reliable assessment of fair value than the view of a single analyst," particularly when a trial judge is playing the analyst's role.

This approach does not elevate "market value" to the governing standard under the appraisal statute. The governing standard for fair value under the appraisal statute remains the entity's value as a going concern. For Aruba, the unaffected public market price provides the best evidence of its value as a going concern.

In this case, the best evidence of Aruba's fair value as a going concern, exclusive of any value derived from the merger, is its thirty-day average unaffected market price of $17.13 per share. I recognize that no one argued for this result. I also recognize that the resulting award is lower

[30] [Original footnote 491.] 8 Del. C. § 262(h).

[31] [Original footnote 492.] See Rationalizing Appraisal, supra, at 1055 (explaining that, for an acquisition of a widely held firm, "the firm's going concern value can be estimated . . . as the actual purchase price minus synergies minus control value"). Failing to make this adjustment would treat the value of the firm as greater than the aggregated value of individual shares, which is the same analytical misstep reflected in the concept of the implicit minority discount. See Control Premiums, supra, 854-59 (explaining conflict between efficient capital markets hypothesis and implicit minority discount); Implicit Minority Discount, supra, 53 (explaining logical equivalence between correcting for a non-existent implicit minority discount and introducing a "'third-party sale value lite' standard in lieu of the traditional 'proportionate share of going concern value' standard").

[32] [Original footnote 493.] See Control Premiums, supra, at 858-59 ("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."); Implicit Minority Discount, supra, at 52 ("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 that going concern value . . . ."); see also Rationalizing Appraisal, supra, at 1033-34.

than Aruba's proposed figure of $19.75 per share. That figure relied on its expert's discounted cash flow analysis, which this decision has found unpersuasive.

"When . . . none of the parties establishes a value that is persuasive, the Court must make a determination based on its own analysis."[33] The appraisal statute requires that "the Court shall determine the fair value of the shares."[34] This means that I must reach my own, independent determination of fair value.[35] That determination is $17.13 per share.

III. CONCLUSION

The petitioners are awarded $17.13 per share. The legal rate of interest, compounded quarterly, shall accrue on this amount from the date of closing until the date of payment. The parties shall cooperate in preparing a final order. If the parties identify additional issues that need to be resolved, they shall submit a joint letter within two weeks that explains the issues and recommends a schedule for bringing this case to conclusion, at least at the trial court level.

VI. CHAPTER 8, INTRODUCTION TO THE ANTITRUST LAW ASPECTS OF MERGERS AND ACQUISITIONS

A. Page 570, New Sec. 8.25.Ca. *Staples, Office Depot*, Blocked Again

Page 570, New Sec. 8.25.Ca. Add before Section D the following:
New Sec. 8.25.Ca. *Staples, Office Depot*, Blocked Again

FTC v. Staples, Inc.
U.S. District Court, D.C, May 10, 2016, U.S. Dist. LEXIS 64909

Drawing an analogy to the fate of penguins whose destinies appear doomed in the face of uncertain environmental changes, Defendant. Staples Inc: ("Staples") and Defendant Office Depot, Inc. ("Office Depot") (collectively "Defendants") argue they are like "penguins on a

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[33] [Original footnote 496.] Cooper v. Pabst Brewing Co., 1993 Del. Ch. LEXIS 91, 1993 WL 208763, at *8 (Del. Ch. June 8, 1993) (citing In re Shell Oil Co., 607 A.2d 1213 (Del. 1992)); accord Del. Open MRI Radiology Assocs. P.A. v. Kessler, 898 A.2d 290, 310-11 (Del. Ch. 2006). See generally Appraisal Rights, supra, at A-89 to A-90 ("If both parties fail to meet the preponderance standard on the ultimate question of fair value, the Court is required under the statute to make its own determination.").

[34] [Original footnote 497.] 8 Del. C. § 262(h).

[35] [Original footnote 498.] Dell, 2017 Del. LEXIS 518, 2017 WL 6375829, at *13 ("In reality, the burden falls on the trial judge to determine fair value, using all relevant factors." (internal quotation marks and alterations omitted)).

melting iceberg," struggling to survive in an increasingly digitized world and an office-supply industry soon to be revolutionized by new entrants like Amazon Business. . . . Charged with enforcing antitrust laws for the benefit of American consumers, the Federal Trade Commission ("FTC") and its co-plaintiffs, the. Commonwealth of Pennsylvania and the District of Columbia, commenced this action in an effort to block Defendants' proposed merger and alleged that the merger would "58liminate[e] direct competition between Staples and Office Depot" resulting in "significant harm" to large businesses that purchase office supplies for their own use. . . . The survival of Staples' proposed acquisition of Office Depot hinges on two critical issues: (1) the reliability of Plaintiffs' market definition and market share analysis; and (2) the likelihood that the competition resulting from new market entrants like Amazon Business will be timely and sufficient to restore competition lost as a result of the merger.

Subsequent to Defendants' announcement in February 2015 of their intent to merge, the FTC began an approximate year-long investigation into the $6.3 billion merger and its likely effects on competition. . . . On December 7, 2015, by a unanimous vote, the FTC Commissioners found reason to believe that the proposed merger would substantially reduce competition in violation of Section 7 of the Clayton Act and Section 5 of the FTC Act. . . . That same day, Plaintiffs commenced this action seeking a preliminary injunction pursuant to Section 13(b) of the FTC Act, 15 U.S.C. § 53 (b) to enjoin the proposed merger until the FTC's administrative proceedings are complete. * * *

At the conclusion of Plaintiffs' case, Defendants chose not to present any fact or expert witnesses, arguing that Plaintiffs failed to establish their prima facie case. . . . And, although entitled to a trial on the merits before an Administrative Law Judge at the FTC, Defendants indicated that they will not proceed with the merger if Plaintiffs' motion is granted. . . . Upon consideration of the evidence presented during the hearing, the parties' proposed findings of fact and conclusions of law, and the relevant legal authority, the Court concludes that the Plaintiffs have established their prima facie case by demonstrating that Defendants' proposed merger is likely to reduce competition in the Business to Business ("B-to-B") contract space for office supplies. Defendants' response relies in large part on the prospect that Amazon Business will replace any competition lost because of the merger. Although Amazon Business may transform how some businesses purchase office supplies, the evidence presented during the hearing fell short of establishing that Amazon Business is likely to restore lost competition in the B-to-B space in a timely and sufficient manner. For the reasons discussed in Section IV infra, Plaintiffs' Motion for Preliminary Injunction is GRANTED. * * *

Plaintiffs have met their burden of showing that the merger would result in "undue concentration" in the relevant market of the sale and distribution of consumable office supplies to large B-to-B customers in the United States. The relevant HHI [see the discussion of the HHI in the enforcement standards section of this chapter] would increase nearly 3,000 points, from 3270 to 6265. These HHI numbers far exceed the 200 point increase and post-merger concentration level of 2500 necessary to entitle Plaintiffs to a presumption that the merger is illegal. The Court rejects Defendants' arguments in opposition to Dr. Shapiro's market analysis for the reasons discussed in detail in Section IV.F supra. Nevertheless, to strengthen their prima facie case, Plaintiffs presented additional evidence of harm[.] * * *

Defendants' sole argument in response to Plaintiffs' prima facie case is that the merger will not have anti-competitive effects because Amazon Business, as well as the existing patchwork of local and regional office supply companies, will expand and provide large B-to-B customers with competitive alternatives to the merged entity. . . Plaintiffs argue that there is no evidence that Amazon or existing regional players will expand in a timely and sufficient manner so as to eliminate the anticompetitive harm that will result from the merger. . . . For the reasons discussed below, Defendants' argument that Amazon Business and other local and regional office supply companies will restore the competition lost from Office Depot is inadequate as a matter of law.

B. Page 603, New Sec. 8.40.A. The *AT&T-Time Warner* Vertical Merger

Page 603, New Sec. 8.40.A. Add before Part V the following:
New Sec. 8.40.A. **The *AT&T-Time Warner* Vertical Merger**

United States v. AT&T Inc.,
U.S. District Court, D.C. (June 12, 2018, 2018 U.S. Dist. LEXIS 100023 .

MEMORANDUM OPINION

If there ever were an antitrust case where the parties had a dramatically different assessment of the current state of the relevant market and a fundamentally different vision of its future development, this is the one. Small wonder it had to go to trial!

On November 20, 2017, the U.S. Department of Justice's Antitrust Division brought this suit, on behalf of the United States of America ("the Government" or "the plaintiff"), to block the merger of AT&T Inc. ("AT&T") and Time Warner Inc. ("Time Warner") as a violation of Section 7 of the Clayton Act, 15 U.S.C. § 18. The Government claims, in essence, that permitting AT&T to acquire Time Warner is likely to substantially lessen competition in the video programming and distribution market nationwide by enabling AT&T to use Time Warner's "must have" television content to either raise its rivals' video programming costs or, by way of a "blackout," drive those same rivals' customers to its subsidiary, DirecTV. Thus, according to the Government, consumers nationwide will be harmed by increased prices for access to Turner networks, notwithstanding the Government's concession that this vertical merger would result in hundreds of millions of dollars in annual cost savings to AT&T's customers and notwithstanding the fact that (unlike in "horizontal" mergers) no competitor will be eliminated by the merger's proposed vertical integration.

Not surprisingly, the defendants, AT&T, Time Warner, and DirecTV, strongly disagree. Their vision couldn't be more different. The video programming and distribution market, they point out, has been, and is, in the middle of a revolution where high-speed internet access has facilitated a "veritable explosion" of new, innovative video content and advertising offerings over the past five years. Trial Tr. ("Tr.") 1397:1-4 (Montemagno (Charter)). Vertically integrated entities like Netflix, Hulu, and Amazon have achieved remarkable success in creating and providing affordable, on-demand video content directly to viewers over the internet. Meanwhile, web giants Facebook and Google have developed new ways to use data to create effective — and lucrative — digital advertisements tailored to the individual consumer.

As a result of these "tectonic changes" brought on by the proliferation of high-speed internet access, video programmers such as Time Warner and video distributors such as AT&T find themselves facing two stark realities: declining video subscriptions and flatlining television advertising revenues. Id. at 3079:18 (Bewkes (Time Warner)). Indeed, cost-conscious consumers increasingly choose to "cut" or "shave" the cord, abandoning their traditional cable- or satellite-TV packages for cheaper content alternatives available over the internet. At the same time, Facebook's and Google's dominant digital advertising platforms have surpassed television advertising in revenue. Watching vertically integrated, data-informed entities thrive as television subscriptions and advertising revenues declined, AT&T and Time Warner concluded that each had a problem that the other could solve: Time Warner could provide AT&T with the ability to experiment with and develop innovative video content and advertising offerings for AT&T's many video and wireless customers, and AT&T could afford Time Warner access to customer relationships and valuable data about its programming. Together, AT&T and Time Warner concluded that both companies could stop "chasing taillights" and catch up with the competition. 2/16/18 Hr'g Tr. 34:16 [Dkt # 67]. Those were the circumstances that drove AT&T, a distributor of content, and Time Warner, a content creator and programmer, to announce their historic $108 billion merger in October 2016 (the "proposed merger" or "challenged merger"). Those are the circumstances that cause them to claim today that their merger will increase not only innovation, but competition in this marketplace for years to come.

Section 7 of the Clayton Act assigns this Court the "uncertain task" of weighing the parties' competing visions of the future of the relevant market and the challenged merger's place within it. Nothing less than a comprehensive inquiry into future competitive conditions in that market is expected. And the Government has the burden of proof to demonstrate that the merger is likely to lessen competition substantially in that uncertain future.

Since announcing the transaction in late October 2016, defendants have delayed closing on the merger agreement for about 18 months as a result of the Government's investigation and suit. The deal is now set to expire if not consummated on or before June 21, 2018 — a turn of events that would require AT&T to pay Time Warner a "break-up fee" of $500 million. The parties have engaged in a highly accelerated discovery schedule to prepare themselves to try this case in March and April of this year. The trial itself lasted nearly six weeks. Both sides put on a case-in-chief and the Government put on a rebuttal case as well. At the conclusion of the trial, I advised the parties I would issue a ruling, if not an opinion, no later than June 12, 2018 so that the losing side would have the agreed-upon time remaining to pursue its appellate rights before the merger or the $500 million break-up fee went into effect.

The following is the Court's Opinion. Initially, I provide context for this suit by reviewing the background of the video programming and distribution industry, the proposed merger, and the procedural history of this case. Thereafter, I discuss the legal standards governing a suit under Section 7 of the Clayton Act, emphasizing in particular the considerations at play in evaluating vertical mergers. With that in place, I next analyze each of the Government's three theories of harm to competition, balancing, as appropriate, the conceded proconsumer benefits of the merger with the consumer harms alleged and the evidence offered to support them. Ultimately, I conclude that the Government has failed to meet its burden to establish that the proposed "transaction is likely to lessen competition substantially."

As such, based on that conclusion, and for all the reasons set forth in greater detail in this Opinion, the Court DENIES the Government's request to enjoin the proposed merger. * * *

[The court set out the following guide to the Antitrust Analysis of Vertical Mergers:]

C. Antitrust Analysis of Vertical Mergers

In the typical horizontal merger case under Section 7, the Government's path to carrying its prima facie burden is clear: by putting forward statistics to show that the proposed "merger would produce a firm controlling an undue percentage share of the relevant market, and would result in a significant increase in the concentration of firms in that market," the Government triggers a "'presumption' that the merger will substantially lessen competition." (internal quotation marks and alterations omitted).

In this case, however, the "familiar" horizontal merger playbook is of little use. That is, of course, because the proposed transaction between AT&T and Time Warner is a vertical merger — i.e., one that involves "firms that do not operate in the same market" and thus "produce[s] no immediate change in the level of concentration in any relevant market." Dept. of Justice & Fed. Trade Comm'n, Non-Horizontal Merger Guidelines § 4.0 (June 14, 1984) ("Non-Horizontal Merger Guidelines"). The parties therefore agree that in this case "there is no short-cut way to establish anticompetitive effects, as there is with horizontal mergers." Joint Statement on the Burden of Proof at Trial ("Joint Statement") 3 [Dkt. # 87]; see 4A Areeda & Hovenkamp, Antitrust Law ¶ 1000a ("[T]he basic economic reason for limiting horizontal mergers is well-founded and rather generally accepted: horizontal mergers increase market concentration, and high market concentration can substantially lessen competition among rivals, particularly with respect to price. Unfortunately, there is no comparable theoretical basis for dealing with vertical mergers.").

With no presumption of harm in play, the Government concedes that, to satisfy its burden here, it must make a "fact-specific" showing that the effect of the proposed merger "is likely to be anticompetitive." Joint Statement 3-4. Such a showing is "necessarily both highly complex" and "institution specific." David T. Scheffman & Richard S. Higgins, Vertical Mergers: Theory and Policy, see also Gov't PCOL ¶ 25 (collecting sources for proposition that "vertical mergers are judged on a case-by-case basis" based on consideration of "case-specific evidence of a danger of future competitive harm"). Of particular relevance here, the Government states that a vertical merger may "act as a clog on competition" by giving the merged firm "control of a competitively significant supplier." Gov't PCOL ¶ 46. Such a situation would occur, the Government continues, if the merged firm were to withhold a source of supply from its rivals or otherwise foreclose access to the source "on competitive terms," such as by causing its rivals to "pay[] more to procure necessary inputs," which in turn could "harm[] competition and consumers." Id. ¶¶ 46, 57-58 (emphasis omitted).

Further complicating the Government's challenge is the recognition among academics, courts, and antitrust enforcement authorities alike that "many vertical mergers create vertical integration efficiencies between purchasers and sellers." Michael H. Riordan & Steven C. Salop. Evaluating Vertical Mergers: A Post-Chicago Approach. The proposed merger reflects that principle: the

Government's chief economic expert, Professor Shapiro, predicts that the merger, if consummated, would lead to 5352 million in annual cost savings on the part of AT&T's customers. See Tr. 2252:19-21 (Shapiro); infra pp. 66-68; see also Gov't PFOF ¶¶ 222-223 (EDM effect is "generally accepted as a potential procompetitive benefit resulting from vertical mergers").

As the Government also notes, the "principal objective of antitrust policy is to maximize consumer welfare by encouraging firms to behave competitively." Gov't PCOL ¶ 4 (emphasis and internal quotation marks omitted)); see id. ("Section 7 proscribes mergers with the potential to harm the competitive process, and thereby result in harm to consumers, including higher prices . . . ."). As such, any proper assessment of a proposed merger, Professor Shapiro testified, must consider both the positive and negative "impact[s] on consumers" by "balancing" the proconsumer, "positive elements" of the merger against the asserted anticompetitive harms. See Tr. 2182:12-20, 2253:4-5 (Shapiro); see also id. at 2461:22-2462:5 (Carlton) ("Well, Professor Shapiro is looking at the [e]ffects on consumer prices. That seems the right thing to do. . . .[W]e want to see what's going to be the result on the end price that consumers pay."); cf. Gov't PFOF ¶ 223 (discussing fact that Professor Shapiro accounted for EDM effects). In view of that "somewhat different" analysis applicable to vertical mergers, Tr. 2182:16-18 (Shapiro), it is perhaps little surprise that the Department of Justice's Non-Horizontal Merger Guidelines recognize that vertical mergers "are less likely than horizontal mergers to create competitive problems," Non-Horizontal Merger Guidelines § 4.

Given all of the competing considerations at play, "the analysis of vertical mergers" has been described as "much more complex than the analysis of horizontal mergers." Scheffman & Higgins, Vertical Mergers. Things are made more difficult still by the lack of modern judicial precedent involving vertical merger challenges — a dearth of authority that is unsurprising, considering that the Antitrust Division apparently has not tried a vertical merger case to decision in four decades ! See Defs.' Proposed Conclusions of Law ("Defs.' PCOL") ¶ 32 [Dkt. # 120]; 2/16/18 Hr'g Tr. 13:24-14:1.

To sum up, the Court accepts that vertical mergers "are not invariably innocuous," but instead can generate competitive harm "[i]n certain circumstances." Non-Horizontal Merger Guidelines §§ 4, 4.2; Gov't PCOL ¶ 22.20. The case at hand therefore turns on whether, notwithstanding the proposed merger's conceded procompetitive effects, the Government has met its burden of proof of establishing, through "case-specific evidence," that the merger of AT&T and Time Warner, at this time and in this remarkably dynamic industry, is likely to substantially lessen competition in the manner it predicts. Gov't PCOL ¶ 25. Unfortunately for the Government, for the following reasons, it did not meet its burden.

VII. CHAPTER 9, HART-SCOTT-RODINO PRE-MERGER NOTIFICATION

A. Page 616, New Sec. 9.6.Ba. Notification Thresholds for 2018

Page 616, New Sec. 9.6.Ba. Add before sec 9.7 the following:
New Sec. 9.6.Ba. **Notification Thresholds for 2018**

FTC Press Release: FTC Announces Annual Update of Size of Transaction Thresholds for Premerger Notification Filings
(January 26, 2018)

For 2018, the size-of-transaction threshold for reporting proposed mergers and acquisitions under Section 7A of the Clayton Act will adjust from $80.8 million to $84.4 million. * * *

The FTC revises the thresholds annually, based on the change in gross national product. The revised thresholds under Section 7A of the Clayton Act will apply to all transactions that close on or after the effective date of the notice, which is 30 days after its publication in the Federal Register. The thresholds for Section 8 of the Clayton Act become effective upon publication in the Federal Register. A complete listing of current thresholds can be found on the FTC's website, and will be updated once the revised thresholds are published in the Federal Register. * * *

B. Page 628, New Sec. 9.8a. No Payment of Money Required

Page 628, New Sec. 9.8a. Add before sec 9.9 the following:
New Sec. 9.8a. **No Payment of Money Required**

Premerger Notification Office Staff, HRS Blog, You don't have to write a check to acquire an HSR-reportable interest
(May 15, 2018)
Available at https://www.ftc.gov/news-events/blogs/competition-matters/2018/05/you-dont-have-write-check-acquire-hsr-reportable.

If your HSR compliance program tracks only those acquisitions that require a payment, you may miss a variety of reportable acquisitions, leading to liability and fines for failures to file. In most situations, you have to file notification under the Hart-Scott-Rodino Act before you pay to purchase voting securities, assets, or certain non-corporate interests. As a result, many HSR compliance programs kick in when someone has to write a check. Below we flag some examples of situations in which you may need to file – a compliance program that won't catch these isn't doing its job.

Exchange of one type of interest in a company for another
Acquisition of some kinds of interests in companies are reportable, while others are not. If you exchange one type of interest for another, that acquisition may be subject to HSR reporting and waiting requirements even though you're exchanging one interest for another in the same company. For example, in 2013 Berkshire Hathaway exchanged convertible notes of USG Corporation for voting securities of USG Corporation. Even though both interests were in the same company, the conversion required an HSR filing. But Berkshire Hathaway's compliance program missed it, and Berkshire Hathaway paid a civil penalty for the violation.

Backside acquisitions
When one corporation buys another, consideration often comes in the form of voting securities of the buyer. For example, Corporation A may buy Corporation B for cash and a certain number of shares in Corporation A. The payment of Company A shares to the target's shareholders is known as a "backside transaction." If you hold shares of company B and will end up holding

shares of A as part of a backside transaction, you may have to file and observe the waiting period before acquiring these new shares.

Consolidations and acquisition of shares in Newco
In a Consolidation, when Corporation A and Corporation B combine under a Newco that will be its own ultimate parent entity, the shareholders of A and B may receive voting securities of Newco in exchange for their shares in A or B. Similar to backside transactions, if you are going to receive shares of Newco, you may have to file for the acquisition even though no money changed hands and you took no direct action to cause the acquisition or to exchange the shares.

Reorganization
When a partnership or LLC reorganizes into a corporation, or vice versa, you might have a reportable acquisition of voting securities or non-corporate interests as a result. For example, suppose partnership P plans to reorganize to become corporation C and distribute a different number of voting securities in C to partners of P in exchange for their partnership interests. If you are a partner, you may have to file and wait before you receive shares of C, even though you are not writing a check and did not take any action to effect the reorganization.

Employee compensation
Employees, particularly executives, may receive a portion of their compensation in the form of voting securities of the company they work for, and these stock awards may be reportable events. For example, if you know that you will receive voting securities or restricted share awards (RSAs) from your employer that entitle you to vote the shares and receive dividends, you may have to file and observe the waiting period before you receive them. On the other hand, if you acquire restricted stock units (RSUs), which do not carry the right to vote, you may have to file and wait not before you receive them, but before the shares vest. For example, in 2007 Brian L. Roberts, the Chief Executive Officer of Comcast Corporation, paid a civil penalty because he failed to file and wait before RSUs he had received vested and resulted in him holding voting securities above the HSR reporting threshold.

An effective HSR compliance program requires a robust mechanism to track the companies in which you hold an interest, but must also take into account how those interests may change or grow over time. Limiting an HSR analysis to situations where a check will cross the table can result in the failure to file for reportable acquisitions and substantial penalties.

VIII. CHAPTER 26, INTERNATIONAL ACQUISITIONS

A. Page 1066, New Sec. 26.3.A. UNCTAD's Evaluation of M&A in 2017 and Predictions for 2018

Page 616, New Sec. 26.3.A. Add before Part II the following:
New Sec. 26.3.A. **UNCTAD's Evaluation of M&A in 2017 and Predictions for 2018**

UNCTAD, January 2018 *Global Investment Trends Monitor*: Global FDI Flows Slipped Further in 2017

(Jan 2018)

[The following are some of the highlights from the report relating to foreign direct investment (FDI).]

- Global [FDI] fell by 16% in 2017, to an estimated US$1.52 trillion . . ., from a revised US$1.81 trillion in 2016 – a stark contrast to other macroeconomic variables, such as GDP and trade growth, which saw substantial improvements in 2017.
- A slump in FDI flows to developed countries (-27%) was the principal factor behind the global decline. A strong decrease in flows was reported in Europe (-27%) as well as in North America (-33%) mainly due to a return to prior levels of inflows in the United Kingdom and the United States after spikes in 2016. This decline was tempered by an 11% growth in flows to other economies, principally Australia.
- FDI to developing economies remained stable, at an estimated US$653 billion, 2% more than the previous year. Flows rose marginally in developing Asia and Latin America and the Caribbean, and remained flat in Africa. Developing Asia regained its position as the largest FDI recipient region in the world, followed by the European Union and North America.
- FDI to the transition economies declined by 17% to an estimated US$55 billion, mainly due to a drop in the Russian Federation and lackluster inflows across most of the Commonwealth of Independent States (CIS).

[The following are some of the highlights from the report relating to cross-border M&A and greenfield investments during 2017.]

- After three years of growth, cross-border merger and acquisitions (M&As) declined 2017. Their growth already slowed in 2016; in 2017, they contracted by 23%, to US$666 billion. However, this still represented the third highest level since 2007.
- Preliminary data on the value of announced greenfield FDI projects show a decline of 32% to US$571 billion (-17% in number of projects), their lowest level since 2003. If confirmed, the drop in greenfield project announcements would be negative indicator for the longer term. Of particular concern is the near halving of the value of project announcements in developing economies, although the fall in project numbers was limited to 23%.

[The following is a highlight from UNCTAD's assessment, as of early 2018, of what is likely to be the state of global FDI in 2018.]

- Higher economic growth projections, trade volumes and commodity prices would normally point to a potential increase in global FDI in 2018. However, elevated geopolitical risks and policy uncertainty could have an impact on the scale and contours of any FDI recovery in 2018. In addition, tax reforms in the United States are likely to significantly affect investment decisions by United States MNEs, with consequences for global investment patterns.