ANALYSES OF AND TAKEAWAYS FROM RECENT DELAWARE VALUATION DECISIONS[1]

GILBERT E. MATTHEWS
Sutter Securities Financial Services, Inc.

The year 2019 was another active period for valuation cases in the Delaware courts, and the activity has continued into 2020. The Supreme Court reversed one 2018 Court of Chancery decision in 2019 and affirmed another. Four valuation cases were decided by the Court of Chancery in 2019 and four more in early 2020; these decisions are discussed below.

Most Delaware valuation cases are statutory appraisals. Exhibit 1 shows that since 2006, transaction price has been the dominant metric in appraisals in arm's-length transactions, while most appraisals in related party transactions have been determined using discounted cash flows (DCF). From 2013, only two appraisals in arm's-length transactions (*AOL Inc.*[2] and SourceHOV, discussed below) were based on the court's DCF calculation; the others which used DCF considered it only as confirmatory of the valuation based on transaction price.

Aruba Networks

The most significant 2019 decision was the Supreme Court's reversal of the Court of Chancery's decision in *Aruba Networks*. Aruba had been acquired in an arm's-length transaction. Vice Chancellor Travis Laster had valued it at "unaffected market price" – the average price during the 30 days prior to a news article that leaked the pending transaction.[3] He appraised the company at 69.4% of the deal price.

Subsequent to trial, the Supreme Court issued an opinion reversing Laster's decision in *Dell*,[4] in which he had relied on DCF and rejected market value. Laster then requested "supplemental briefing on 'the market attributes of Aruba's stock' in part because he 'learned how many errors [he] made in the *Dell* matter.'"[5] Neither petitioners nor respondent had discussed unaffected market price at trial. The respondent argued for unaffected market price in its subsequent post-trial brief. Laster's decision concluded that "Aruba's

1 This article, which was previously published as "Highlights of 2019 Delaware Valuation Decisions," in Business Valuation Update, Vol.25: No.11 (November 2019), reprinted with permission, and also posted on Harvard Law School Forum on Corporate Governance (Jan. 12, 2020) [available at https://corpgov.law.harvard.edu/2020/01/12/delaware-appraisal-decisions/]; it is updated to include decisions through April 2020.

2 *In re Appraisal of AOL Inc.,* 2018 WL 1037450 (Del. Ch. Feb. 23, 2018); *modified*, 2018 WL 3913775 (Del. Ch. Aug. 15, 2018). In this case, the Court concluded that the sale process was compromised by the seller's commitment to a single buyer, making the negotiated transaction price unreliable as a measure of value.

3 *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.,* 2018 Del. Ch. LEXIS 52 (Del. Ch. Feb. 15, 2018) *("Aruba I"); rev'd,* 210 A.3d 128 (Del. 2019) *("Aruba II"). Aruba I* was discussed by the author in *Business Valuation Update,* October 2018.

4 *In re Appraisal of Dell Inc., 2016 Del. Ch. LEXIS 81 (May 31, 2016); rev'd, Dell Inc. v. Magnetar Global Event Driven Master Fund Ltd,* 2017 Del. LEXIS 518 (Del. Dec. 14, 2017).

5 *Aruba II* at 131, quoting the Court's letter to the parties.

Exhibit 1: Valuation Methods Used in Delaware Appraisal Decisions							
	Number of Valuations	DCF or similar	Comparable Companies	Comparable Transactions	Asset Value	Transaction Price	Unaffected Mkt. Price
	Arm's-Length Transactions						
1998-2005	2	2	0	0	0	1	0
2006-2013	4	3	1	0	0	2	0
2014-1Q 2020	16	7	2	1	0	13	1
Total	22	12	3	1	0	16	1
	Related Party Transactions						
1998-2005	14	8	7	4	0	0	0
2006-2013	7	7	1	1	1	0	0
2014-1Q 2020	9	9	0	0	0	0	0
Total	30	24	8	5	1	0	0
Note: Some decisions used more than one method.							

unaffected market price provides the best evidence of its going concern value."[6]

The Vice Chancellor had noted that:

> Aruba management knew internally that Aruba was having an excellent quarter and would beat its guidance. But…[it] time[d] the announcement of the merger to coincide with the announcement of Aruba's February 2015 earnings.[7]

Nonetheless, he concluded:

> [T]he record does not provide a persuasive reason to question the reliability of Aruba's trading price based on the decision by Aruba management to bundle together two pieces of information.[8]

The Supreme Court disagreed, concluding that the not-yet-disclosed information had indeed affected the public market:

> HP [the buyer]…had material, nonpublic information that, by definition, could not have been baked into the public trading price. …In particular, HP had better insight into Aruba's future prospects than the market because it was aware that Aruba expected its quarterly results to exceed analysts' expectations.[9]

The Supreme Court criticized the Court of Chancery's decision that the unaffected market price was fair value:

> The lack of a developed record on whether the stock price was an adequate proxy for fair value buttresses our holding that the Court of Chancery abused its discretion by awarding the thirty-day average unaffected market price of $17.13 per share.[10]
>
> Due to requirements for SEC review and a shareholder vote, an acquisition of public companies cannot close until well after the announcement of a transaction. The Supreme Court pointed out that the Delaware appraisal statute requires that the company be valued at the closing date:
>
> Although §262 requires the Court of Chancery to assess Aruba's fair value as of "the effective date of the merger," the Court of Chancery arrived at the unaffected market price by averaging the trading price of Aruba's stock during the thirty days before news of the merger leaked, which was three to four months prior to closing.[11]

The Supreme Court directed a final judgment that petitioners be awarded $19.10 per share, which was Aruba's estimate of the deal price ($24.67) minus synergies. It agreed with Laster's conclusion that the transaction price included substantial synergies.[12] The Supreme Court noted that the $19.10 valuation, which was 77.4% of the deal price and 11.5% above the unaffected market price, "was corroborated by… Aruba's [expert's] DCF, comparable companies, and comparable transactions analyses."[13]

PLX Technology

In this fiduciary duty case, a hedge fund's representative who was a director of the publicly traded company, among other things, had conversations with the buyer and its investment banker that were not disclosed to

6 *Aruba I* at *4.
7 *Aruba I* at *63.
8 *Aruba I* at *66.
9 *Aruba II* at 139.

10 *Aruba II* at 140.
11 *Aruba II* at 132.
12 Laster concluded that the transaction prices minus synergies was $18.20 per share. [*Aruba I* at *45.]
13 *Aruba II* at 142.

other board members. The Court of Chancery agreed with plaintiffs that the hedge fund had aided and abetted breaches of the board's duties to shareholders. However, Vice Chancellor Laster rejected the plaintiffs' claim that the $6.50 deal price was unfair. He concluded that plaintiffs "were unable to prove that the breaches resulted in damages."[14]

Laster determined that the projections used by the plaintiffs' expert in his DCF calculations were flawed in three respects:

1. The projections included "a new line of business involving a new set of customers with a new set of requirements" and "evidence at trial did not give [the Court] sufficient confidence to base a damages award on this element of the projections."[15]
2. "PLX management had a track record of missing its projections."[16]
3. "[B]idders do not appear…to have believed that [the projection] supported valuations in the range that [plaintiffs' expert] posited…If the projections were sufficiently reliable to support a credible valuation of $9.82 per share, then it seems likely that another buyer would have competed."[17]

Also, Laster concluded that plaintiffs' expert's discount rate was too low. He faulted expert's beta because it was based on daily returns rather than weekly or monthly returns, thereby reducing beta:

> "[W]hen the return interval is shortened, the following occurs: Securities with a smaller market value than the average of all securities outstanding (the market) will generally have a decreasing beta, whereas securities with a larger market value than the average of all securities outstanding will generally have an increasing beta."[18]

Defendants' expert did not fully credit management's projections for the new line of business and his DCF calculation valued PLX at less than the transaction price.[19] The Court agreed that the deal price exceeded going-concern value:

> Although flawed from a fiduciary standpoint, the details of the sale process that the Board conducted and the nature of the synergistic deal with Avago that it generated means that the plaintiffs received consideration that exceeded the value of the Company on a stand-alone basis.[20]

The Supreme Court affirmed the trial court's decision that plaintiffs failed to prove that they suffered damages.

Trussway

In February 2019, a shareholder who was squeezed out of Trussway Holdings, Inc., a private company, was awarded an amount 5% higher than the merger value. Vice Chancellor Sam Glasscock III determined fair value solely on his DCF calculation, rejecting petitioner's expert's comparable company analysis because the "supposed 'comparable companies' are too divergent from [Trussway], in terms of size, public status, and products, to form meaningful analogs for valuation purposes."[21]

The Court averaged DCF calculations based on two periods: a nine-year management projection and the first five years of that projection. It described the five-year period as "more standard."[22] (However, the reason it is "more standard" does not stem from valuation theory, but simply reflects the fact that that few companies make projections beyond five years.) The valuation based on the five-year period was 15% lower than the valuation based on the nine-year period.

The management projections included "strategic initiatives" that included, among other things, selling new products to be added to the company's product line and gaining additional market share through sales to market segments in which the company did not yet participate.[23] Both experts adjusted their valuations to reflect their concerns that the longer-term projections were optimistic. Petitioner's expert increased his discount rate by 1% after the first five years, and respondent's expert gave 25% weight to the nine-year projection and 75% weight to the five-year period.[24]

In using the five-year period, the Court effectively substituted the 2.3% perpetual growth rate (as to which both experts agreed) for the higher growth rate that management expected in the final four years. The Court agreed with the experts' view that that an adjustment should be made to a value based on the nine-year projection, and it explained its decision to give partial weight to the shorter period:

> Of more concern to me is Trussway management's ability (or that of any human prognosticator) to accurately predict corporate performance nine years out, particularly concerning new facets of

14 *In re PLX Technology Inc. S'holders Litig.*, 2018 WL 5018353 (Del. Ch. Oct. 16, 2018) at *56*; aff'd,* 211 A.3d 137 (2019).
15 *Id.* at *52.
16 *Id.*
17 *Id. at *53.*
18 *Id.* at *54, quoting Gabriel Hawawini, "Why Beta Shifts as the Return Interval Changes," *Fin. Analysts J.,* May-June 1983 at 73.
19 *Id.* at *52.
20 *Id.* at *56.
21 *Hoyd v. Trussway Holdings LLC,* 2019 WL 994048 (Del Ch. Feb. 28, 2019) at *5.
22 *Id.* at *7.
23 *Id.* at *2.
24 *Id.* at *6.

a business. I am also aware that there is a degree of huckster's optimism in these predictions.[25]

Jarden

The *Jarden* decision in July 2019 determined the appraisal price in an arm's-length transaction solely on the unaffected market price, the closing price immediately before *The Wall Street Journal* published rumors of the transaction.[26] Vice Chancellor Joseph Slights III relied on "expert testimony…including an event study that analyzed the market's response to earnings and other material announcements."[27] He noted that (i) Jarden had no control shareholders, (ii) 94% of its shares were in the public float, (iii) the bid-ask spread was only 0.02%, and (iv) approximately 20 analysts had published reports on Jarden in the year prior to the merger.[28] He also concluded that the unaffected market price was not "stale" on the closing date.[29]

Petitioners' expert posited that the market price was depressed by a "conglomerate discount." The Court rejected this argument, noting that "it is not clear that this notion [of a conglomerate discount] is accepted within the academ[ic community] or among valuation professionals."[30]

The Court concluded that the transaction price was not an applicable valuation standard in this situation, explaining:

> I place less weight on this market-based valuation approach in this case because the sales process was not well-conceived or well-executed and the expert analysis of the transaction synergies raised more questions than it answered.[31]

Even though the Court agreed with petitioners' claim that the negotiating approach of Jarden's Executive Chairman "may well have set an artificial ceiling on what Newell was willing to pay,"[32] it nonetheless based its valuation on unaffected market price ($48.31), which was 18.4% *less* than the deal price ($59.21).

The Vice Chancellor dismissed the petitioners' valuation based on comparable companies, saying, "After considering the evidence, I am satisfied that Petitioners' comparable companies analysis is not credible because Jarden had no reliable comparables."[33] Several other decisions in recent years have similarly rejected expert testimony utilizing the comparable company method.[34]

Slights noted that his valuation was confirmed by his DCF calculation and by "the most reasonable estimate" of "the Merger price less synergies."[35] In his DCF calculation, he used the midpoint of the experts' inflation and GDP growth estimates as the perpetual growth rate,[36] an approach often used by the Court of Chancery.

This decision is being appealed by petitioners.[37]

Columbia Pipeline

An August 2019 decision by Vice Chancellor Laster based appraisal value in an arm's-length transaction solely on the deal price.[38] Deal price has become the predominant standard of value in appraisals of companies acquired in arm's-length transactions.

The Vice Chancellor rejected petitioners' claim that the company's value increased between signing and closing.[39] He also rejected the unaffected market price as a measure of value in this case[40] and rejected its DCF analysis.

Petitioners' DCF valuation was 24% over the deal price and 57% over unaffected market. Laster rejected their DCF analysis as contrary to contemporaneous market evidence:

> [Expert]'s opinion that the value of Columbia materially exceeded the deal price conflicts with the market behavior of other potential strategic acquirers who had shown interest in Columbia, and who did not step forward to top TransCanada's price.[41]

He also expressed concern about the terminal value calculated by petitioners' expert:

> [T]he terminal value represented 125% of his valuation of Columbia. . .. This court has questioned the utility of a DCF in a case where the terminal value represented 97% of the result, finding that "[t]his back-loading highlights the very real risks" presented by using that

25 *Id.* at *6.

26 *In re Appraisal of Jarden Corp.,* 2019 WL 3244085 (Del. Ch. July 19, 2019) at *28-*29; *modified*, 2019 WL 4452209 (Sept.16, 2019). The Court defined unaffected market price as a single price rather than an average over a period of time. [*Id*. at *19-*20.]

27 *Id*. at *2.

28 *Id.* at *27.

29 *Id.* at *31.

30 *Id.*

31 *Id.* at *26.

32 *Id*. at *24.

33 *Id.* at *3.

34 *E.g.*, in the past five years, *Domain Associates, Inc. v. Shah,* 2018 WL 3853531 (Del. Ch. Aug. 13, 2018) at *18; *Blueblade Capital Opportunities LLC v. Norcraft Cos., Inc.,* 2018 WL 3602940 (Del. Ch. July 27, 2018) at *28; *In Re Appraisal of SWS Group, Inc.,* 2017 Del. Ch. LEXIS 90 (Del. Ch. May 30, 2017); at *31-*32, *aff'd*, 181 A.3d 153 (Del. 2018); *In re ISN Software Corp. Appraisal Litig.,* 2016 Del. Ch. LEXIS 125 (Del. Ch. Aug. 11, 2016) at *9, *aff'd, ISN Software Corp. v. Ad–Venture Capital Partners, L.P.,* 173 A.3d 1047 (Del. 2017); *Dunmire v. Farmers & Merchants Bancorp of Western Pa., Inc.,* 2016 Del. Ch. LEXIS 167 (Nov. 10, 2016) at *30; *Merlin Partners LP v. AutoInfo, Inc.,* 2015 Del. Ch. LEXIS 128 (Del. Ch. Apr. 30, 2015) at *32.

35 *Id. at *50.*

36 *Id. at *32.*

37 Delaware Cases to Watch in 2020, Law360, Jan. 1, 2020, *available at* www.law360.com/articles/1229419/delaware-cases-to-watch-in-2020.

38 *In re Appraisal of Columbia Pipeline Group, Inc.*, 2019 WL 3778370 (Del. Ch. Aug. 12, 2019) at *43.

39 *Id.*

40 *Id.* at *49.

41 *Id.* at *50.

Continued from p.29

> methodology and "undermin[ing] the reliability of applying the DCF technique."[42]

Laster observed, "The wide swings in output that result from legitimate debate over reasonable inputs undermine the reliability of [petitioner's expert]'s DCF model."[43]

He did not reduce the price for synergies, noting that the synergy adjustment proposed by respondent was excessive:

> [Respondent] did not meet its burden of proof. [It] likely could have justified a smaller synergy deduction, but it claimed a larger and unpersuasive one. This decision therefore declines to make any downward adjustment to the deal price.[44]

Stillwater Mining

A second August 2019 decision by Laster also ruled that appraisal value in an arm's-length transaction was the deal price.[45] He rejected trading price, given the availability of "a market-tested indicator like the deal price."[46] He also rejected DCF in this case:

> The legitimate debates over [contested] inputs and the large swings in value they create undercut the reliability of the DCF model as a valuation indicator.[47]

Laster determined that the trading price was not a measure of fair value because it was impacted by inadequate disclosure of Stillwater's reserves. He observed that SEC limitations on disclosure of reserves that did not rise to the "probable" level affected the viability of trading price as a valuation indicator:

> [The SEC did] not permit a mining company to disclose information about inferred resources, which are mineral deposits where the quantity, grade, and quality "can be estimated" based on "geological evidence," "limited sampling," and "reasonably assumed, but not verified, geological and grade continuity."[48]

Stillwater is the only U.S. source of "platinum group metals," palladium, platinum and rhodium. The Vice Chancellor observed, "Between signing and closing, the prices of palladium and platinum increased materially, with a direct effect on Stillwater's value."[49] He did not adjust his appraisal for this price movement because petitioners did not argue for it or quantify its effect on value.

> [W]hether to adjust the deal price for an increase in value between signing and closing presents numerous difficult questions. In this case, the petitioners did not argue for an adjustment to the deal price, and so the parties did not have the opportunity to address these interesting issues. . .. The petitioners accordingly failed to prove that the deal price should be adjusted upward to reflect a change in value between signing and closing.[50]

UIP Companies

Delaware courts have seldom accepted company-specific premiums in determining cost of capital. Former Chief Justice Leo Strine, Jr., wrote in 2006, "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."[51] However, Vice Chancellor McCormick ruled in a shareholder dispute in January 2020 that special circumstance merited the application of this factor to reduce the value of a small private real estate management company:

> Given UIP's unique circumstances as almost wholly dependent on the SPEs [special purposes real estate entities] and [UIP's two principals] for its revenue, the Court finds that Defendants have met their burden of showing that a specific-company risk premium is necessary in this case.[52]

SourceHOV Holdings

Five minority shareholders in SourceHOV filed for appraisal when the company engaged in a three-way merger with another private company and a Nasdaq-listed SPAC (special purpose acquisition company).

Both experts agreed that the income approach was the only appropriate valuation methodology because there were no adequate guideline companies or transactions and there was no market check on the deal price process. Petitioners' expert used both DCF and Capital Cash Flow (CCF). Vice Chancellor Slights noted:

> CCF is a variation of DCF that is better suited to value future cash flows where a company's capital structure is expected to change. Ultimately, a traditional DCF and CCF are "algebraically equivalent."[53]

Respondent's expert used an adjusted present value DCF model that the Court said was "functionally the

42 *Id.* at *51, quoting *Union Ill. 1995 Investment LP v. Union Finl. Group, Ltd.*, 847 A.2d 340, 361 (Del. Ch. 2003).

43 *Id.* at *52.

44 *Id.* at *45.

45 *In re Appraisal of Stillwater Mining Co.*, 2019 WL 3943851 (Del. Ch. Aug. 21, 2019) at *50.

46 *Id.* at *59.

47 *Id.* at *61.

48 *Id. at *58,* quoting the SEC's *Industry Guide 7* [17 C.F.R. 229.801(g)]. *Industry Guide 7* was rescinded on Oct. 31, 2018 [www.sec.gov/corpfin/secg-modernization-property-disclosures-mining-registrants].

49 *Id.* at *48.

50 *Id.* at *50.

51 *Del. Open MRI Radiology Assocs. v. Kessler*, 898 A.2d 290, 339 (Del. Ch. 2006).

52 *Coster v. UIP Cos., Inc.*, 2020 WL 429906 (Del. Ch. Jan.28, 2000) at *25.

53 *Manichaean Capital, LLC v. SourceHOV Hldgs., Inc.*, 2020 WL 496606 (Del. Ch. Jan. 30, 2020) at *12. *See* Richard A. Ruback, "Capital Cash Flows: A Simple Approach to Valuing Risky Cash Flows," 31(2) *Financial Mgt.* 85 (2002).

same as [the] CCF model."[54] The principal differences between the two analyses were (i) the calculation of beta, (ii) the small company premium, (iii) debt load projections, and (iv) the projection on which the analysis was based; the fourth difference was not material.

Petitioners' expert determined beta based on the betas of 19 publicly traded guideline companies. Respondent's expert calculated beta based on the yield on SourceHOV's debt. The Court rejected the beta based on the company's debt, describing it as "methodologically novel" and unsupported by academic literature.[55]

Petitioners' expert based his small stock premium of 2.08% on the 8th decile in Duff & Phelps' 2017 Valuation Handbook, while respondent's expert used the 9th decile's 2.68%. Both cited the market price of shares of the surviving company. The latter argued that this price included synergies. The Court was "persuaded the 2.68% size premium is more accurate on this record."[56]

Respondent's expert predicted that SourceHOV would have retired all its debt when it matured in 2020, thereby lowering its tax saving from interest deductions. The Court rejected this premise.

The expert's valuations were $5,079 per share and $2,817 per share, respectively. The Court accepted all of the petitioners' report other than the small stock premium and appraised SourceHOV at $4,591 per share.

The Court commented favorably on an adjustment in the petitioners' report that favored the respondent, whose forecast included depreciation substantially in excess of capital expenditures:

> This forecast led to "depreciating and amortizing more asset value than [SourceHOV] even ha[d] on the books [brackets in original].". If [petitioners' expert] had accepted this high level of depreciation and amortization …, the result would have been to increase SourceHOV's value in a DCF analysis. Instead, to account for his concern that depreciation and amortization forecasts were too high, [he] made a Respondent-friendly adjustment to provide a more accurate calculation.[57]

In the past, the Court of Chancery has sometimes erred by accepting terminal value calculations in which depreciation materially exceeded capex.[58]

54 *Id.* at *14.
55 *Id.* at *21.
56 *Id.* at *27.
57 *Id.* at *25.
58 *In re Emerging Communications, Inc. Sh'h's Litig.*, 2004 Del. Ch. LEXIS 70 (Del. Ch. May 3, 2004) at *57, n.56; *Lane v. Cancer Treatment Centers of America, Inc.*, 2004 Del. Ch. LEXIS 108 (Del. Ch. July 30, 2004) at *111.

Panera Bread

A January 2020 decision appraised Panera Bread, which had been taken private in a negotiated transaction. Both experts valued the company using DCF, comparable companies, and comparable transactions. However, respondent's expert testified that he viewed his calculations as corroborative of his deal-price-minus-synergies valuation and gave no independent weight to them.

Vice Chancellor Zurn pointed out several flaws in petitioners' expert's DCF analysis but did not criticize respondent's expert's DCF.[59] He rejected both experts' comparable transaction analyses because "neither sample size is reliable enough to afford it weight."[60] He criticized the comparable companies selected by each expert and stated:

> Neither expert presents a reliable empirical analysis to show a suitable peer group; both sets have material weaknesses. For that reason, I do not find comparable companies as a fair measure of value. Instead, I view both parties' comparable companies analyses as an attempt to corroborate their preferred valuation.[61]

The Court accepted the testimony of respondent's expert that the deal price of $315 per share included synergies of $11.56 per share.[62] However, the company had prepaid the full $315 to the dissenters in order to avoid paying interest on the award, and the Vice Chancellor ruled that Delaware law did not authorize him to order a refund of the difference.[63]

Real Time Cloud Services

This March 2020 decision addressed a dispute between partners in of a small accounting services firm. Defendants' expert based his valuation on the company's internal financial statements, while plaintiff's expert used financial statements "recreated" for purposes of the litigation that were inconsistent with the company's records and the plaintiff's own tax returns.[64] The Court based its valuation on the defendants' report, adjusted to use the higher growth rate posited by the plaintiff.[65]

Expert Witness Testimony

The Court of Chancery often rejects not only expert testimony that is not persuasive, but also testimony that is not supported in the valuation literature, e.g., the conglomerate discount rejected in *Jarden* and

59 *In re Appraisal of Panera Bread Co.*, 2020 WL 506684 (Del. Ch. Jan. 31, 2020) at *40-*41.
60 *Id.* at *43
61 *Id.* at *42.
62 *Id.* at *40.
63 *Id.* at *44.
64 *Zachman v. Real Time Cloud Services, LLC*, 2020 WL 1522840 (Del. Ch. Mar. 31, 2020).at *16-*17.
65 *Id.* at *17.

Continued from p.31

the beta based on daily price changes rejected in *PLX Technology.*

The Court on several occasions has criticized experts who overreach in their valuations. As discussed above, it faulted the petitioners' expert's DCF analysis in *Columbia Pipeline* as contrary to market evidence. Also, the respondent's expert in *Columbia Pipeline* was deemed to have been unpersuasive as to the amount of synergies included in the transaction price; the Court commented that respondent "likely could have justified a smaller synergy deduction."

On the other hand, the absence of testimony on relevant valuation issues can be harmful. Because there was no testimony as to the impact of increased palladium and platinum prices prior to closing in *Stillwater Mining*, the Court was unable to quantify impact of this change on the appraised value. In a 2018 case, Chancellor Andre Bouchard declined to consider respondent's post-trial argument for valuing the company at unaffected market price because the issue had not been discussed at trial.[66]

In both *Columbia Pipeline* and *Stillwater Mining*, Laster quoted a 2016 opinion:

> An argument may carry the day in a particular case if counsel advance it skillfully and present persuasive evidence to support it. The same argument may not prevail in another case if the proponents fail to generate a similarly persuasive level of probative evidence or if the opponents respond effectively.[67]

He added in both decisions:

> Likewise, the approach that an expert espouses may have met "the approval of this court on prior occasions," but may be rejected in a later case if not presented persuasively or if "the relevant professional community has mined additional data and pondered the reliability of past practice and come, by a healthy weight of reasoned opinion, to believe that a different practice should become the norm."[68]

The valuation approaches that the Court of Chancery will accept necessarily depend on the facts of the specific case.

> The appraisal exercise is, at bottom, a fact-finding exercise, and our courts must appreciate that, by functional imperative, the evidence, including expert evidence, in one appraisal case will be different from the evidence presented in any other appraisal case. Different evidence, of course, can lead to different decision paths and different outcomes.[69]

Conclusion

These recent cases demonstrate the importance of high quality expert testimony in valuation litigation. Although each decision is fact-specific, experts should be familiar with past practice in the Court of Chancery and with the its interpretation of fair value and operative reality. Experts should be careful to utilize practices that are supported in the academic and valuation communities and should be aware of current developments in the profession. Columbia Pipeline's criticism of petitioners' DCF calculation and of respondent's synergies claim are warnings against overreaching, while the Court's inability in that case to determine the market impact of higher product prices shows how the absence of relevant testimony can impact a decision.

In the past, event studies were often used in other types of security cases but not in appraisals. The current focus on deal prices and historical market prices in arm's-length transactions has necessitated testimony on event studies in appraisal cases where the Court relies on market factors rather than corporate valuations.

In recent cases, many experts have not used comparable companies and comparable transactions. This may be a consequence of the Court of Chancery's frequent rejection of these approaches. Nonetheless, these valuation methods are widely used in the investment community. Comparable companies are frequently used in research reports, and both approaches are commonly included in investment bank presentations to corporate clients and in fairness opinions. In investment bank fairness opinions issued in connection with the acquisitions of companies that were appraised in Delaware since 2010, 97% used comparable companies and 76% used comparable transactions as a valuation method. Chancellor William B. Chandler III wrote in 2011:

> [I]t is preferable to take a more robust approach involving multiple techniques – such as a DCF analysis, a comparable transactions analysis (looking at precedent transaction comparables), and a comparable companies analysis (looking at trading comparables/multiples) – to triangulate a value range, as all three methodologies individually have their own limitations."[70]

66 *In re Appraisal of Solera Holdings, Inc.*, 2018 WL 3625644 (Del. Ch. July 30, 2018) at *32.

67 *Merion Capital L.P. v. Lender Processing Services, L.P.*, 2016 WL 7324170 (Del. Ch. Dec. 16, 2016) at *16.

68 *Columbia Pipeline* at *16 *and Stillwater Mining* at *20, quoting *Global GT v. Golden Telecom, Inc.*, 993 A.2d 497, 517 (Del. Ch. 2010); *aff'd*, 11 A.3d 214 (Del. 2010).

69 *Jarden* at *1.

70 *Muoio & Co. v. Hallmark Entm't Invs. Co.*, 2011 Del. Ch. LEXIS 43 (Mar. 9, 2011) at *83-*84.

Comparable transactions can be useful in appraisals when they can be adjusted for the impact of synergies. Experts should continue to use comparable companies when they deem it appropriate and should explain to the Court the basis for their selection of the comparables and why they are relevant to the subject company.

ABOUT THE AUTHOR

Gilbert E. Matthews, CFA
Sutter Securities Financial Services, Inc.

Mr. Matthews has been a Senior Managing Director of Sutter Securities in San Francisco since 1995. He previously was with Bear Stearns in New York for 35 years, where he was a general partner and Senior Managing Director. He has testified as an expert witness in numerous Federal and state courts and has written several book chapters and numerous articles on fairness opinions, corporate valuations and litigation relating to valuations and appraisals.