IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

ALDEN SMITH,

Plaintiff,

v.

JAY A. PRITZKER, ROBERT A. PRITZKER, JEROME W. VAN GORKOM, BRUCE S. CHELBERG, WILLIAM B. JOHNSON, JOSEPH B. LANTERMAN, GRAHAM J. MORGAN, THOMAS P. O'BOYLE, ROBERT W. RENEKER, W. ALLEN WALLIS, TRANS UNION CORPORATION, a Delaware corporation, THE MARMON GROUP, INC., a Delaware corporation, GL CORPORATION, a Delaware corporation, and NEW T CO., a Delaware corporation,

Defendants.

Civil Action No. 6342

BRIEF OF DEFENDANTS JAY A. PRITZKER, ROBERT A. PRITZKER, THE MARMON GROUP, INC., GL CORPORATION AND NEW T CO. IN OPPOSITION TO PLAINTIFF'S APPLICATION FOR A PRELIMINARY INJUNCTION

MORRIS, NICHOLS, ARSHT & TUNNELL
Lewis S. Black, Jr.
A. Gilchrist Sparks III
Richard D. Allen
John F. Johnston
1105 North Market Street
Post Office Box 1347
Wilmington, DE 19899
(302) 658-9200
Attorneys for Defendants Jay A. Pritzker, Robert A. Pritzker, The Marmon Group, Inc., GL Corporation and New T Co.

January 29, 1981

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NATURE AND STAGE OF PROCEEDINGS

This action was commenced on December 19, 1980 by Alden Smith ("Smith"), a holder of common stock of Trans Union Corporation ("TU"), seeking to enjoin the proposed merger into TU of New T Co. ("NTC"), an indirect wholly-owned subsidiary of GL Corporation ("GL"). GL is owned beneficially by certain members of the Pritzker family of Chicago (the "Pritzkers"). TU, NTC and GL are each Delaware corporations, and each is named as a defendant. Also named as defendants are The Marmon Group Inc. ("Marmon") (a subsidiary of GL), Jay A. and Robert A. Pritzker, both of whom are directors and officers of Marmon, and eight of TU's ten directors. Answers denying the material allegations of the Complaint were filed by TU, GL, NTC, and Marmon on January 14, 1981. Motions to dismiss were filed by the individual defendants on January 19, 1981.

Pursuant to order of the court, as modified by agreement of counsel, expedited discovery was taken by all parties. Documents were produced to plaintiff by TU, GL, NTC and Marmon on January 9, 1981. Thereafter, between January 14 and January 26, the individual defendants and certain others were deposed as follows: Jay A. Pritzker ("J. Pritzker") on January 14; Robert A. Pritzker ("R. Pritzker") on January 15; William D. Browder ("Browder"), on January 16 and 18; Jerome W. Van Gorkom ("Van Gorkom") on January 19; Thomas P. O'Boyle ("O'Boyle") on January 20; Graham J. Morgan ("Morgan") and Sidney A. Bonser ("Bonser") on January 21; Robert W. Reneker ("Reneker") and W. Allen Wallis ("Wallis") on January 22; Bruce S. Chelberg ("Chelberg") on January 23; Joseph B. Lanterman ("Lanterman") on January 24; and William B. Johnson ("Johnson") on January 26. Plaintiff Smith was deposed on January 15.

On January 19, 1981, TU sent to all stockholders of record as of December 19, 1980, a Proxy Statement ("Proxy Statement") (Ex. A to the Affidavit of William B. Moore, hereafter "Moore Aff.") relating to the proposed merger and on January 27, 1981, TU sent a Supplement to Proxy Statement ("Proxy Supp.") (Ex. B to Moore Aff.) to such persons.

On January 28, 1981, plaintiff served and filed, without leave of court or all parties, an amended complaint; among the amendments was the addition of Bonser and Browder as defendants. Late on January 28, plaintiff also filed his 105 page brief in support of his application for a preliminary injunction.

This is the brief of defendants GL, NTC, Marmon, and Jay A. Pritzker and Robert A. Pritzker in opposition to plaintiff's motion.

STATEMENT OF FACTS

A. Introduction

The proposed merger, which is scheduled to be voted upon by the stockholders of TU at a special meeting to be held on February 10, 1981, provides for the payment to each stockholder of TU (other than NTC) of $55 in cash for each share of common stock held. The closing sales price of TU's common stock on the New York Stock Exchange ("NYSE") on September 19, 1980 (the last trading date prior to the announcement of the proposed merger) was $37.25. Thus, the proposed merger offers to stockholders a premium of $17.75 (an aggregate premium to the holders of TU's 12,512,956 shares of more than $222,000,000), or more than 47%, over the last closing price on the NYSE before the announcement of the proposed merger. The $55 merger price also represents a premium of $21.12, or more than 62%, over the average of the high and the low prices at which the shares traded on the NYSE in 1980 before the proposed merger was announced. Moreover, as discussed in detail hereafter, TU has, with the assistance of its investment banker, Salomon Brothers, sought actively for more than three months to solicit offers more favorable to its stockholders than the $55 per share cash offer provided in the proposed merger. Not one firm offer at a price equal to or higher than $55 per share has been forthcoming.

Plaintiff, who for reasons arising out of his unique federal income tax position does not wish to see the proposed merger consummated, has mustered every weapon in his arsenal in an effort to deny to TU's stockholders the right to make their own investment decision with respect to the proposed merger.* Notwithstanding that he was told by TU's senior legal officer prior to the filing of the complaint in this action that the Pritzker interests did not intend to vote the 1,000,000 shares which they had contracted to purchase (Smith 212-217) and was given access to the merger documents (Smith 193), plaintiff's claim of irreparable injury in the complaint is premised upon factually erroneous allegations that the 1,000,000 shares would be voted in favor of the proposed merger. (Complaint ¶39).**

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* Of the 12,512,956 shares of TU common stock outstanding and entitled to vote upon the proposed merger, Pritzker interests own beneficially only 110,266 shares (less than 1% of the shares entitled to vote on the proposed merger). Such shares have been held for more than ten years by certain trusts for the benefit of certain members of the Pritzker family. (J. Pritzker 12). Accordingly, the Pritzker interests are in no position to dictate the outcome of the vote on the proposed merger.

** In a further effort to block the proposed merger at any cost, on November 24, 1980 plaintiff, solely on the advice of counsel, purchased 100 shares of Marmon preferred stock and has subsequently given consideration to bringing a derivative suit on behalf of Marmon. (Smith 36-40, 52-54).

Having now been compelled by the objective facts to abandon the baseless theory upon which injunctive relief was initially sought, plaintiff has turned to an attack upon the sufficiency of the business judgments made by TU's directors in approving the proposed merger, seeking in large part to build a new case upon the varying recollections of TU's ten directors with respect to details of meetings and events occurring as much as four months ago. In order to set the record straight and to consider recent developments, TU's directors, at the regularly scheduled directors meeting held on Monday of this week, reviewed all facts relating to the proposed merger and unanimously reaffirmed their recommendation that the merger be approved.

As the following review of the largely undisputed facts of record will demonstrate, plaintiff's pending application for a preliminary injunction, whereby he asks this Court to substitute its business judgment for that of TU's directors and stockholders, must be denied.

B. The Parties

1. Plaintiff

The plaintiff, B. Alden Smith, is the record and beneficial owner of 54,061 shares of common stock of TU (Smith 64, 69). Smith acquired substantially all of the shares of TU which he presently owns as a result of the sale of his company, Smith & Loveless Inc., to TU in 1959. In that sale Smith and his partner, Compre Loveless, each received 50,000 shares of TU common stock. (Smith 12-18). Subsequently, TU stock was split two and one-half for one, giving to Smith and Loveless a total of 125, 000 shares each. (Smith 64).

In the early 1960's Smith read in Fortune Magazine of a tax avoidance gimmick known as "selling short against the box" whereby he could realize the market value of his TU stock while deferring indefinitely the payment of any federal capital gains tax on the transaction. (Smith 344-345). Essentially, the "short against the box" technique permits a stockholder to create a perfect hedge by depositing with a broker the same number of shares which are sold short, as security for the open contractual obligation to deliver shares under the short sale contract. Smith discussed the technique with his former partner, Loveless, and both made a decision about the same time in the early 1960's to sell a portion of their TU stock short against the box. (Smith 344-346). The effect of the transaction was summarized in a series of responses by Smith to questions posed at his deposition:

> Q. Do I understand correctly that the economic effect of that was to put a certain amount of cash in your pocket in the 1960's, that you have never had to pay taxes on up to now?
>
> A. It was a hedging position, a means of avoiding taxes.

Q. But my question was, did it enable you to put a certain amount of cash in your pocket in the 1960's?

A. It did.

Q. And not realize a gain on it and pay tax?

A. It did. It delayed the tax.

(Smith 346).

From his short sales against the box of 50,000 shares of TU common stock in the early 1960's Smith received cash in the total amount of $767,392. (Smith 111). The capital gains taxes payable with respect to that transaction and which were avoided by reason of the short against the box technique are $214,800. (Smith 112). However, if the proposed merger is consummated, Smith's offsetting long and short positions in TU common stock would be liquidated and the $214,800 capital gains tax which he has avoided paying for more than 15 years would become due and payable. (Smith 112). Smith, having "locked in" his gain by creating a hedge and by avoiding the payment of capital gains taxes by employing the "short against the box" technique, was thereafter totally unconcerned with the market price for TU common stock. His only interest was to insure that no transaction occur, such as the proposed merger, which would upset his tax avoidance gimmick and cause him to pay his taxes. It is Smith's undisclosed peculiar tax posture, arising from his hedge of TU stock, which motivates his selfish desire to have this Court enjoin the proposed merger.*

Given the foregoing, it is abundantly clear that Smith does not represent the interests of TU's other stockholders in seeking to enjoin the proposed merger. His economic interest in the proposed transaction is completely _sui generis_, arising out of his own personal tax situation, and any complaint on his part with respect to the terms of the proposed merger must be assessed in that light.**

In short, this suit is the effort of one TU stockholder to block the proposed merger in order to facilitate his own peculiar tax plans and, among other things, to further defer the payment of $214,800 in capital gains taxes on cash received by him more than 15 years ago. He would seek this end while denying to TU's stockholders the right to make their own investment decision as to whether to

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* Smith holds an additional 54,061 shares of TU stock in a "long" position. Again, because of another peculiar tax posture (arising out of an unrelated capital gain on the sale of an orange grove), it is not necessarily in Smith's economic interest either for the market price for such stock to increase or for him to accept the substantial premium offered in the proposed merger. In fact, Smith candidly testified that he would, for reasons peculiar to his tax posture, benefit currently if the price of TU stock were to fall. (Smith 114).

** Not surprisingly, Smith's former partner, Compre Loveless, who is also "short against the box" in TU stock, has agreed to assist Smith in the financing of this lawsuit. (Smith Ex. 22).

accept the aggregate premium over market offered in the proposed merger in excess of $222,000,000.

2. TU and Its Directors

The common stock of TU or its predecessor and principal subsidiary, Union Tank Car Company, has been traded on the NYSE for more than 60 years. (Proxy Statement, p. 2). As of December 19, 1980 (the record date for the special meeting to consider the proposed merger), there were 12,512,956 shares of TU common stock issued and outstanding. (Proxy Statement, p. 1). TU is a diversified holding company whose operations are conducted entirely through its subsidiaries. The principal activity of TU is the leasing of railway tank cars and other rail cars to shippers of bulk liquid, compressed gas, and powdered, pelletized or dry products in the United States, Canada, Mexico and Great Britain. (Proxy Statement, p. 23). In addition, other subsidiaries of the company are engaged in general leasing, water and waste treatment, distribution activities, real estate development and information services. (Proxy Statement, pp. 23-24).

For the period 1975 through September 19, 1980, the date the proposed merger was announced, the stock of TU has traded on the NYSE between a low of $24-1/4 and a high of $39-1/2. The high at which such stock traded in 1980 was $38-1/4, the low was $29-1/2, and the closing sale price on September 19, 1980 was $37.25. (Proxy Statement, pp. 5-6).

According to TU, as of the record date for the proposed merger no person beneficially owned 5% or more of the outstanding common stock of TU. (Proxy Statement, p. 2).

In addition to naming TU as a defendant, the amended complaint names all of TU's ten directors as defendants. Of the defendant directors, five are outsiders who are neither officers nor employees of TU. See pp. 14-15, infra.

3. The Pritzker Defendants

Notwithstanding that GL, Marmon, NTC and the Pritzkers do not control TU, did not seek out the proposed merger, and were in no position to exert improper influence over TU, plaintiff has named each of them as defendants. No effort whatsoever is made in the complaint to state a claim against GL, Marmon or NTC. However, at paragraph 38 of the complaint plaintiff states as follows with respect to defendants Jay A. and Robert A. Pritzker:

> 38. The defendant officers and directors of TUC and the Pritzkers have fraudulently conspired to manipulate the corporate machinery of TUC to enrich themselves at the expense of TUC and the Public Stockholders. As a result of the conspiracy to affect the merger, TUC officers and directors will be able to exercise their stock options while the Pritzkers will reap an automatic $17 million profit and will have the benefit of the investment tax credits of

> TUC. On the other hand, many Public Stockholders will be faced with enormous tax liabilities and TUC itself will be saddled with large new debt, arising solely out of the proposed transaction.

Notwithstanding that plaintiff's counsel has taken 13 depositions and reviewed thousands of documents in connection with this proceeding, not one fact has come to light to support plaintiff's claim that the Pritzkers somehow "fraudulently conspired" with TU. Moreover, plaintiff's claims that the Pritzkers will reap "an automatic $17 million profit" and that TU "will be saddled with large new debt" as a result of the proposed merger are factually incorrect. See pp. 26-27, infra. In short, while the Pritzkers, NTC, GL and Marmon are named as defendants in this lawsuit, there is no claim against them.*

C. Events Leading Up to the Merger Proposal

In complete contrast to plaintiff's unsupported claims of fraud and conspiracy against the Pritzkers, the

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* The Pritzkers have moved to dismiss this action as to them on the ground, among others, that the purported service of process on them under 10 Del. C. §3114 is improper since the one allegation in the complaint against them is not based on actions by them as directors. See Hana Ranch, Inc. v. J. Gordon Lent, C.A. No. 6255, unreported opinion (Del. Ch., October 10, 1980).

uncontroverted facts show clearly that the genesis of the proposed merger was the product of arm's length discussions and negotiations initiated at the behest of J. W. Van Gorkom, chief executive officer of TU, with Jay A. Pritzker. (J. Pritzker 26-35; Van Gorkom 16). Throughout these negotiations and discussions, which spanned the period from September 13 through September 19, Van Gorkom was very concerned that there would be leaks and market disruption in the trading of TU stock (J. Pritzker 30, 33). Accordingly, he limited the involvement of TU personnel in the initial discussions with GL to Bruce Chelberg, TU's president, and Carl Peterson, TU's controller (J. Pritzker 29-30). In addition, TU made representatives of The Boston Consulting Group available to GL. (J. Pritzker 33-34).

At the conclusion of its investigation, GL determined to pursue the acquisition of TU. On Friday, September 19, counsel for GL delivered to counsel for TU draft merger documents which were then the subject of negotiations between counsel for GL and counsel for TU. During the course of such negotiations Jay Pritzker indicated that the merger proposal would be open and available for acceptance only until September 21, 1980. His reason for the imposition of such a condition was based upon his experience that leaks of the existence of such negotiations not only adversely affected uninformed stockholders but also tended to adversely affect the likelihood of successful negotiation. (J. Pritzker Aff. ¶2).

In addition to the requirement that its merger offer be accepted by TU by September 21, 1980, GL also conditioned its merger offer on the agreement of TU to issue to GL, or its designee, 1,000,000 newly issued shares of the common stock of TU. This arose because of the unusual circumstance which Van Gorkom attached to his initial solicitation of Pritzker's interest. Van Gorkom said that he wanted to be free to entertain a better offer than $55 per share should such an offer be made some time after announcement of the proposed merger. Pritzker said that he was not willing to be a "stalking horse" for TU. (J. Pritzker 28). This impasse was solved by Van Gorkom's agreement that TU would issue 1,000,000 shares to TU. This stockholding would permit GL to derive benefit from the making of the merger offer after paying its costs (including those incurred in obtaining and maintaining financing commitments for the merger even if another entity ultimately topped GL's bid. (J. Pritzker 28; Pritzker Aff. ¶3). A price of $38 in cash for each of the 1,000,000 shares was agreed upon. (Pritzker Aff. ¶3). Both the number of shares and the price paid (which was $0.75 above market) were the subject of negotiations between Jay

Pritzker and Van Gorkom, wherein Pritzker had initially sought 1,750,000 shares at market and reluctantly acceded to Van Gorkom's demand for a higher price and a lesser number of shares, although he thought it to be inadequate. (J. Pritzker 29).

D. Actions of Trans Union With Respect to the Proposed Merger

1. The TU Board of Directors

The TU Board of Directors consists of ten members, five of whom are employees of TU ("the inside directors") and five of whom are not employees ("the outside directors"). The inside directors are: (1) Jerome Van Gorkom, Chairman and Chief Executive Officer of TU, and a Director since 1957; (2) Bruce S. Chelberg, President and Chief Operating Officer of TU, and a Director since 1978; (3) William B. Browder, Senior Vice President-Law of TU and a Director since 1954; (4) Sidney H. Bonser, Executive Vice President of TU and a Director since 1969; and (5) Thomas P. O'Boyle, Senior Vice President-Administration of TU and a Director since 1968.

The five outside directors of TU are unusually experienced businessmen. In addition, they have wide-ranging experience on the Boards of other corporations. Robert W. Reneker is the retired Chairman of Esmark, Inc.

and has been a Director of TU since 1971. (Reneker 9). Mr. Reneker presently serves on the Boards of Directors of General Dynamics Corporation, Morton-Norwich, The Chicago Tribune, Jewel Corporation, United States Gypsum Company, and Money Mart Assets. (Reneker 10).

Joseph B. Lanterman is the retired Chairman of Amsted Industries, Inc. and has been a Director of TU since 1976. (Lanterman 3, 8-9, 13). Mr. Lanterman presently serves on the Boards of Directors of International Harvester Company, Peoples Energy Corporation, Illinois Bell Telephone Co., Kemper Insurance, The Midwest Stock Exchange, A. E. Staley Manufacturing Company, the Illinois Central Railroad, and Harris Bank and Trust Company. (Lanterman 10-11).

W. Allen Wallis is Chancellor of the University of Rochester and a former Dean of the Graduate School of Business of the University of Chicago; he has been a Director of TU since 1962. (Wallis 12-14). Mr. Wallis presently serves on the Boards of Directors of Bausch & Lomb, Eastman Kodak Company, Lincoln First Bank, Rochester Telephone Company, McMillan Company, Metropolitan Life Insurance Company, and the Standard Oil Company. (Wallis 18, 21).

Graham J. Morgan is the Chairman and Chief Executive Officer of United States Gypsum Company and has been a Director of TU since 1979. (Morgan 5-6). Mr. Morgan presently serves on the Boards of Directors of IC Industries, Inc., and the Illinois Central Gulf Railroad. (Morgan 21).

William B. Johnson is Chairman and Chief Executive Officer of IC Industries, Inc., and has been a Director of TU since 1969. (Johnson 6, 10).

Both by reason of their service on the Board of TU, a company which has made numerous corporate acquisitions, and by reason of their extensive business experience and service on other boards, the Directors of TU are familiar with and knowledgeable concerning the subject of corporate acquisitions.

2. <u>The September 20, 1980 special meeting of the TU Board of Directors</u>

On Saturday, September 20, 1980, a special meeting of the Board of Directors of TU was held to consider the proposed merger. (Browder Ex. 2). All board members were present except O'Boyle. (<u>Id</u>.) Also present were Carl W. Peterson, Senior Vice President-Controller of TU, Donald B. Romans ("Romans"), Executive Vice President-Finance of TU, William B. Moore, Secretary and General Counsel of TU, and James J. Brennan, a partner in the law firm of Sidley & Austin, outside counsel to TU. (Browder 78, 83).

At the last previous meeting of the Board in August, the Board had received a report of The Boston Consulting Group, Inc., which had been retained to conduct an extensive study of TU. (Van Gorkom 13-14). The Board had also reviewed at its August meeting a Five-Year Forecast which had been prepared by management. (Van Gorkom 13-14). Hence, the Board had been fully updated on the most recent information relating to the operation and prospects of TU.

The September 20, 1980 meeting began with a presentation by Van Gorkom concerning the merger proposal in which he discussed his reasons for approaching Pritzker, his original and subsequent meetings with Pritzker, and the substance of the merger proposal which evolved from those discussions. (Reneker 37-38). Following Van Gorkom's presentation, the Board discussed the merger proposal at length, focusing generally on its terms and particularly on, among other things, the proposed price, the proposed sale to GL or its designee of the one million shares of TU common stock, the effect of other offers, and whether there was a need for expert advice. (Chelberg 129-130).

With respect to the price of $55 per share to be paid to TU stockholders, a number of factors, including the following, were considered significant by the Board. First, such price reflected a premium of more than 46% over the most recent price at which TU stock had traded (Browder 86-87; Morgan 61), and the premium was viewed as comparable to the premiums paid in other acquisitions. (Chelberg 92; Browder 168). Second, for some time prior to September 20, Romans had been studying the stock of TU in an attempt to assess its value. In response to questions directed to him by the Board, Romans said that he could not say that the $55 price was unfair and that, in fact, it was within the range which he had determined represented, at least in his view, the value of the stock.* (Bonser 26-27; Reneker 67; Wallis 66; Chelberg 154; and Lanterman 55).

Although the Board was advised by counsel that there was no legal requirement to obtain a "fairness opinion" from an investment banker, the Board considered whether it ought to seek such an opinion. (Chelberg 148-49). While, as a practical matter, there was not time to obtain such an opinion if the existing offer were to be accepted, the Board concluded that such an opinion in all events was unnecessary for two reasons. First, the price offered, as noted, reflected a substantial premium over the market price. Second, it was the view of most Board members that the market would provide the best gauge as to the fairness of the price, and if the $55 price was low, other offers would be received. (Browder

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* Romans apparently had initially determined that the value of TU stock was in the range of $50-$60 and later concluded that the range might be as high as $55-$65. (Bonser 26-27).

249, 252; Wallis 74; Chelberg 162, 166-67).* Hence, the Board considered the $55 per share offer as a "floor" which would guarantee a good price to the stockholders but not preclude an even better price. (Reneker 81-82; Browder 280). On the basis of all of these factors, the Board concluded that TU stockholders ought to be given the opportunity to accept or reject the proposal.

The Board understood that acceptance of the Pritzker proposal did not foreclose the receipt and acceptance of other offers. (J. Pritzker 82; Chelberg 121-22; Van Gorkom 218). Consistent with its desire not to discourage a more favorable offer, however, the Board insisted on at least one modification to the merger proposal. As presented, the proposal would have prohibited TU from providing to prospective offerors confidential information of the type made available to the Pritzkers. Because it believed that such a provision might discourage other offers, the Board directed that the provision be deleted. (Browder 135; Chelberg 135, 172-73).

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* This view was subsequently confirmed by TU's investment banker. Mr. Chelberg testified that, in the opinion of Salomon Brothers

> "the Pritzker offer would excite others, especially other investment banking houses who would be contacting clients they represented . . . ." (Chelberg 167).

The Board also extensively discussed the provision of the merger proposal which permitted GL to purchase one million shares of TU stock (Morgan 74). While such a feature was not common, neither was it unheard of. (Chelberg 100). Indeed, Chelberg simply considered it a variation on the fairly common practice of an offeror buying a substantial block of stock in the market before making a tender offer or merger proposal. (Chelberg 101). In all events, the Board viewed the term as a condition of the offer (Morgan 72), and concluded that it appeared reasonable (Wallis 53) and appropriate since the Pritzker offer had the effect of establishing a "floor" for the stock at a level almost 50% above the market price. (Reneker 55). However, the Board insisted that the issuance of the shares be conditioned on GL receiving financing commitments and therefore becoming obligated to proceed with the proposed merger. (J. Pritzker Aff. ¶3).

Finally, the Board understood that the merger proposal had to be acted on promptly. (J. Pritzker Aff. ¶2; Reneker 68). No Board member present at the meeting testified that he needed either additional time in which to consider the matter or additional information on which to base a decision. A voice vote was taken with all directors voting in favor of the proposed merger and no director voting against the proposal or abstaining.*

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* One of the inside directors, Sidney Bonser has since stated that he did not vote on the merger proposal but, rather, did not respond when the voice vote was taken. (Chelberg 175). Mr. Bonser, however, subsequently approved the minutes of the September 20 meeting, which do not reflect that any Board member abstained.

3. Amendment of the merger agreement and events leading thereto

During the first weeks following Board approval of the proposed merger, several members of TU senior management indicated concern about the desirability of the merger. The principal objections concerned the price to be offered to stockholders, which was said to be inadequate in light of the underlying value of TU stock, the prospect of TU becoming a privately held company, the prospect of having to work for the Pritzkers, and the effect of the proposed merger on future operations. (Browder 227; Chelberg 186-87).* Certain members of senior management stated that they would resign from the company if the proposed merger was approved. (Browder 250-51, 256-58).

Upon learning of such objections to the proposed merger, Van Gorkom approached Jay Pritzker to discuss the matter. They agreed that the merger agreement should be modified in two respects: (1) to permit TU to solicit actively through an investment banker other potential offerors; and (2) to extend to February 1981 the time for submis-

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* Besides the expressed objections, the opposition to the proposed merger of certain members of management -- particularly Bonser, Romans and O'Boyle -- apparently related to their desire to participate in a leveraged buyout of TU (see "KKR" pp. 31-34, <u>infra</u>), after which they expected to assume top management positions in TU (Bonser 102-04; Van Gorkom 199-200). Bonser, for instance, acknowledged that he expected to be President of TU after such an acquisition. (Bonser 102-03).

sion of the proposed merger to the TU stockholders so as to allow additional time for such an active solicitation. (Van Gorkom 217, 224). Jay Pritzker did not view the first of these changes as particularly significant, since he believed that the initial announcement of the proposed merger had been sufficient to arouse the interest of anyone seriously interested in acquiring TU. (J. Pritzker 50-51, 79). The second change, however, was very significant to him since it in effect tied his hands for almost four months while guaranteeing to TU the benefit of a "floor" for that period. (J. Pritzker 50). Nevertheless, Jay Pritzker agreed to the amendments. (J. Pritzker 50).

On October 4, 1980, a meeting of TU senior management was held to discuss the proposed changes. Van Gorkom described the proposed amendments to those present, after which there was extended discussion. (Van Gorkom 220; Browder 262-66; Chelberg 204, 206-07). In light of the proposed changes, those officers who had threatened to resign withdrew such threats and agreed to stay with TU for a period of at least six months following any merger. (Van Gorkom 220).*

On October 8, 1980, the TU Board held a special meeting to consider the proposed amendments; again, all

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* Even Romans, one of the strongest opponents of the proposed merger, conceded that the investment banker chosen would have adequate time in which to search for a better offer. (O'Boyle 89).

directors were present except O'Boyle. (Browder 266, 270-71). Van Gorkom described in detail the circumstances leading to the proposed amendments. After discussion, the Board voted unanimously to approve the amendments. Thereafter, the Board considered the hiring of an investment banker to conduct a search for a better offer; it ultimately was decided to retain Salomon Brothers, which previously had performed certain investment banking services for TU. (Browder 276-78).

Finally, the Board again considered the desirability of seeking a "fairness opinion" from an investment banker. The Board decided that such an opinion was unnecessary in light of the active search for other offers that was to be made. (Browder 280-81).

4. The Principal Terms of the Proposed Merger

Plaintiff, in his brief, singles out three aspects of the Agreement and Plan of Merger, the Supplemental Agreement, and the September 20, 1980 letter agreement, all as amended as of October 10, 1980 (hereafter referred to collectively as the "Agreements"), in his effort to establish that the actions of the board of directors of TU in connection with the merger were unreasonable. In each case, plaintiff's brief either deliberately mischaracterizes the nature of the Agreements or evidences a misunderstanding of their import. Most striking, however, is the fact that plaintiff's brief would have the Court overlook the essential term of the Agreements, namely that they provide to TU's stockholders the opportunity to realize $55 in cash for each share of stock held by them which, as previously noted, is a premium of in excess of 62% over the average high and low market prices for TU common stock for the eight and one-half month period immediately prior to the announcement of the proposed merger on September 19.

Plaintiff's first attack upon the terms of the Agreements is directed at the provisions defining TU's rights vis-a-vis alternative offers. (PB 36-37). Contrary to the suggestions made by plaintiff, the Agreements make clear that TU may solicit, receive and accept <u>any</u> offer from a third party providing for a merger, a consolidation, a sale of substantially all of TU's assets, or an exchange of more than 45% of the then outstanding stock of TU (with a commitment by the offeror to acquire promptly the balance of such Common Stock by merger or otherwise). The only condition imposed upon such acceptance is that it not preclude submitting the proposed merger to the stockholders of TU for their approval (unless it has previously been terminated) and that TU submit the proposed merger to the stockholders for their approval at or prior to the time such alternative proposals are so submitted. (Supplemental Agreement Section 2.03(a), at Proxy Statement I-15 - I-16). In other words, GL has bargained not for the right to impose conditions upon alternative offers, but only for the right to present its own offer, with or without the recommendation of TU's directors, to TU's stockholders for their consideration.

In addition, under the limiting conditions misleadingly focused upon by plaintiff, the Agreements permit TU to defeat even GL's right to present the Agreements to TU's stockholders in the event that there exists a definitive agreement for a merger, consolidation, sale of assets or purchase or exchange of TU common stock which is, in the opinion of TU's directors, more favorable to the stockholders of TU than the Agreements. (Agreement and Plan of Merger, Article V(e), Proxy Statement I-17). Accordingly, it is clear that any bidder for TU may come forward freely with an offer containing whatever conditions such bidder may seek to impose and TU may accept that offer. Obviously, if that occurs and the offer is in fact better than that submitted by GL, TU's stockholders will reject the Agreements and TU will be free to consummate such an alternative transaction.

Second, plaintiff's brief attacks the condition imposed by the Agreements that TU issue 1,000,000 newly issued shares of its common stock to GL or its designee as being both a chilling factor with respect to other bidders for TU and a waste of TU's assets. Again, plaintiff's statements fail to accurately portray the financial realities of the 1,000,000 share issuance.

Pursuant to the Agreements, the issuance of the 1,000,000 shares was conditioned upon GL obtaining financing for the proposed merger by October 10, 1980, which commitments were obtained on October 8, 1980 (Pritzker Aff. ¶3). Thereafter, GL designated Canadian Imperial Bank of Commerce Trust Company (Bahamas) Ltd., as trustee of certain trusts for the benefit of members of the Pritzker family (the "Trusts"), as GL's designee to purchase such 1,000,000 shares (Pritzker Aff. ¶3). The 1,000,000 shares of TU common stock were acquired by the Trusts on Wednesday, January 28, 1981 (Pritzker Aff. ¶5).

In the event the proposed merger is consummated, it is anticipated that the Trusts will transfer such 1,000,000 shares to GL in consideration for a $38 million note of GL. GL would thereafter contribute such 1,000,000 shares to NTC, and such shares would be cancelled in the merger. (Pritzker Aff. ¶5). In such case, the Trusts would not profit. If the proposed merger is not consummated and some other entity acquires TU, such 1,000,000 shares would be "sold" by the Trusts to the acquiror of TU and the profit, if any, would be the property of the Trusts. If the proposed merger is not consummated and TU is not so acquired, the Trusts would be free to either hold or dispose of such 1,000,000 shares, but would bear the risk that such shares would decline in value to a level at or below that at which they were purchased. (Pritzker Aff. ¶5). Thus, the only way in which the Trusts benefit from the 1,000,000 share issuance is if the proposed merger does not go through, and then only to the extent that the price of the shares or the amount of a competing offer for TU common stock exceeds the price at which the Trusts purchased the shares. It is therefore altogether incorrect and no more than pure speculation to suggest, as plaintiff does, that the Trusts will in fact realize a benefit of $17 million or better on the 1,000,000 share transaction.

Plaintiff has similarly mischaracterized the effect of the 1,000,000 share transaction upon potential bidders by ignoring the fact that TU is today $38 million richer by reason of Trusts' purchase of the TU stock. Accordingly, any bidder who would top the GL offer would be not at a $55 million disadvantage, as suggested by plaintiff, since it would acquire a TU having an additional $38 million.

Finally, plaintiff attacks that portion of the Agreements which require that TU purchase for the difference between the option price and $55 per share from the holders thereof all outstanding stock options. Obviously, this provision was insisted upon by GL so that, at the conclusion of the proposed merger, it would own all the common stock of TU without any outstanding contractual right on the part of an option holder to assume a minority position. It does not, as plaintiff suggests, constitute a gift to optionees but instead is a necessary payment to buy out their valuable contractual rights, be they vested or <u>in futuro</u>, to become stockholders of TU. The fallacy in plaintiff's suggestion that this constitutes a waste of TU's assets is that such a settlement of the contractual rights held by such optionees will be effected only if the proposed merger is consummated, in which case the economic impact of the transaction will fall entirely upon GL and its wholly-owned subsidiary, as the sole stockholder of TU after the proposed merger is consummated.

Moreover, any suggestion that the directors were motivated by the purchase of these options is contradictory to the facts of record. Only four of the nine directors in attendance at the September 20 meeting were optionees and, more importantly, the subject of the handling of the options was not addressed until after agreement in principle on the merger had been reached. (Browder 316).

5. The Salomon Brothers search for other offers

Following the October 8 Board meeting, the investment banking firm of Salomon Brothers was retained by TU to search for a better offer than the proposed merger. As described by Jay F. Higgins, the partner in charge of the Mergers And Acquisitions Department of Salomon Brothers, the mandate of Salomon Brothers was to do "whatever possible to see if there is a superior bid in the market place over a bid that is on the table for Trans Union." (Higgins 71).

The retention agreement between TU and Salomon Brothers provided to Salomon Brothers an enormous financial incentive to obtain a better offer. Specifically, if the proposed merger ultimately was consummated, the agreement provided that "Salomon shall be paid the amount of $500,000 and shall not be entitled to any reimbursement of expenses . . ." (R. Pritzker Ex. 4). On the other hand, the agreement provided:

> "If any Sale Transaction not involving an entity controlled by the Pritzker Family is consummated, Salomon shall be paid a fee equal to 3/8 of 1% of the

> aggregate fair market value of the consideration received by the Company, in the case of the sale of assets, or by the stockholders of the Company, in the case of a merger or consolidation or an exchange for or purchase of the Common Stock, and Salomon shall in addition be entitled to reimbursement of expenses. . . ." (Id.)*

Hence, if the proposed merger was consummated, Salomon Brothers would receive a total of $500,000. If, however, it obtained a proposal involving, for instance, even $56 per share for TU stockholders -- one dollar above the Pritzker offer -- Salomon Brothers would receive a fee of approximately $2.65 million plus disbursements.

Understandably in light of that incentive, Salomon Brothers conducted a thorough and extensive search for a better offer. It assembled a team consisting of "several important Salomon Brothers' partners or employees" (Higgins 76) and involving about 50 Salomon Brothers' employees altogether. (Higgins 13). After preparing a detailed written brochure concerning TU,** Salomon Brothers made oral presentations, by telephone or personal visit, to over 150 companies

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* The agreement also provided that if a merger with Pritzker interests at a higher price ultimately was consummated, Salomon Brothers would receive a fee based on 3/16 of 1% of the total consideration.

** The written presentation stressed that the TU Board "has not placed any limitation on the form of the offer or the type of consideration involved. . . and a tax free transaction would be viewed very favorably." (Higgins Ex. 2 at 3-4).

which it had identified as potential offerors. (Higgins 76-7). Despite this extensive search, only one company, General Electric Company ("GE"), showed sustained interest in making a better offer for TU and GE ultimately decided not to make an offer.

In the course of the Salomon Brothers search, no company contacted by Salomon Brothers indicated that there was insufficient time in which to consider an offer for TU (Higgins 131-32)* and no company contacted expressed concern about the feature of the proposed merger permitting GL to acquire one million shares of TU. (Higgins 122).

6. KKR

During the period following Board approval of the merger proposal, several members of TU senior management -- particularly Bonser, Romans, and O'Boyle -- investigated an acquisition of TU by means of a "leveraged buyout." In rough terms, the plan called for a group of investors, including interested members of TU management, to contribute a relatively small amount of equity and to borrow most of the funds needed to purchase the stock of TU, using as the security for such loans solely the assets or stock of TU.

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* Since the Pritzkers, without the assistance of an investment banker, were able to make a firm offer for TU less than one week after first considering the matter, it seems obvious that time would not have been a problem to a company with a serious interest in TU.

Romans and Bonser had contacted Kohlberg, Kravis, Roberts and Company ("KKR"), an organization that specialized in organizing leveraged buyouts.

The possibility of such a leveraged buyout first came to the attention of the Board at the October 8 meeting. The Board directed Van Gorkom to participate in discussions or meetings with KKR representatives. (Wallis 121-22). Van Gorkom thereafter twice traveled to New York concerning a possible KKR proposal; on the first trip he met with KKR representatives and on the second trip he met with representatives of Continental Bank and Prudential Insurance Company, both of which were prospective lenders. (Van Gorkom 237).

On December 2, 1980, Mr. Kravis of KKR, along with Romans, came to Van Gorkom's office and delivered to Van Gorkom a two-page letter stating that KKR was offering to purchase all Trans Union stock for $60 per share, subject to obtaining financing commitments. (Van Gorkom 249-51; Chelberg 224, 238). Kravis requested that a press release announcing the offer be issued in order to "cool off" other prospective bidders. (Van Gorkom 251; Chelberg 231-32).

Van Gorkom advised Kravis and Romans that he did not consider the letter to be an offer given the contingency for financing.* Van Gorkom also stated that he felt it would be inappropriate to issue a press release (since such a release might have exactly the effect desired by Kravis -- "cooling off" any other interested company then considering an offer in excess of $55 per share). (Van Gorkom 251). Van Gorkom said, however, that he would consult counsel to see if, under the circumstances, a public announcement was required. (Chelberg 232).

Because a regular meeting of the Board of Directors of TU was scheduled for the afternoon of December 2, Van Gorkom and Chelberg met with James Brennan of Sidley & Austin to discuss presenting the KKR proposal to the Board. However, in the midst of that meeting (and about three hours after Van Gorkom's meeting with Kravis and Romans), Kravis telephoned Van Gorkom to advise him that the offer was being withdrawn. (Chelberg 239-41).

Later in December, Van Gorkom and Chelberg met with Kravis to discuss the reasons for the withdrawal of the KKR proposal. (Chelberg 249-50). In essence, Kravis said

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* While the offer of GL also had been contingent on the receipt of financing, Van Gorkom perceived significant differences between the two proposals. Van Gorkom had spoken to prospective lenders to the Pritzkers and, in light of those conversations and his knowledge of the assets of the Pritzkers, was confident that the needed financing would be obtained. In contrast, the KKR group had been put together solely for the purpose of this transaction and, thus, had no established credit. Moreover, KKR still lacked about $35 million in equity contributions. (Van Gorkom 252).

that the principal equity contributor had decided not to participate for a variety of reasons, principally related to the division in management resulting from the fact that certain members of management were to participate in the proposal while others were not. (Chelberg 253-55).

As recently as Saturday, January 24, Van Gorkom and Chelberg again met with representatives of KKR to see if the KKR proposal could be revived. They were advised that it could not. (TU Proxy Supp.).

7. TU Board of Directors meeting of January 26, 1981

A regularly scheduled meeting of the TU Board was held on Monday, January 26, 1981. As set forth in the affidavit of William B. Moore, the Board reviewed and considered a number of matters elicited in the course of the two weeks of discovery which has occurred in this case, and of which plaintiff appears to complain. As the affidavit further recites, after a thorough re-examination of the merger proposal in light of these matters, the Board unanimously voted to recommend the Pritzker merger proposal to the stockholders of TU.

The following day a supplemental proxy was sent to all stockholders of TU advising them, among other things, of the various matters considered by the Board at the January

26 meeting, of the Board action taken at that meeting, and of the status of other possible offers.

E. <u>Duff and Phelps Report is Premised On Assumptions Which Are Contradicted By Objective Facts of Record</u>

Plaintiff has submitted a report prepared by Duff and Phelps, Inc. ("Duff and Phelps") concluding that the value of TU stock is in the range of $65-$70. Apart from the shortcomings of the analysis on which that conclusion is based, discussed <u>infra</u>, many of the factual assumptions on which that report is premised are contrary to the objective facts of record in this case.

While conceding, as it must, that market price ordinarily is the best indicium of value, Duff and Phelps arbitrarily disregards the market price at which TU stock traded prior to the announcement of the proposed merger by simply asserting, without support, that the market was not "duly informed" about TU. (Duff and Phelps Report at 16). The fact is that TU, during the past year, made conscientious efforts to "duly inform" the investment community about TU through presentations to members of that community by senior management. (Chelberg 76-81, Ex. 1). Hence, if anything, the investment community was probably better informed about TU than about most companies.

Duff and Phelps seeks to ignore the efforts of Salomon Brothers by pointing to supposed obstacles forced on them. First, Duff and Phelps asserts that, given the complexity of TU, a potential purchaser simply did not have time to study TU and make a decision. To begin with, Duff and Phelps was retained only two and one-half weeks ago, and yet now purports to have conducted a thorough examination of TU; prospective purchasers had three to four months to analyze the Company. Moreover, GL, the only company to make an offer, was able to do so within one week of being approached by TU, and without the benefit of the efforts of Salomon Brothers. Finally, no company contacted by Salomon Brothers indicated that there was insufficient time to consider the matter. (Higgins 131-32).

Duff and Phelps also claims that the approval of the Pritzker proposal "capped the market," inhibiting other bidders, because "a new potential acquiror would have no reason to expect a friendly reception." (Duff and Phelps Report at 24). Whatever validity there might be to that proposition in the abstract, it cannot sensibly be applied in a situation where, as here, the company to be acquired actually engages in an extensive solicitation of other offers.

Duff and Phelps claims also that "Salomon Brothers imposed a condition on new bidders that they bid by January

1, 1981." Again, the testimony of the Salomon Brothers representative is to the contrary (Higgins 130) and indeed the sustained contacts with GE extending into late January demonstrate that there was no arbitrary deadline of January 1.

Next, Duff and Phelps claims that the issuance of the one million shares to the Trusts also discouraged other offers because a company offering $56 per share would have to expend $68 million more. (Duff and Phelps Report at 26). They ignore, however, that TU would have an additional $38 million in cash by reason of the sale of the stock. More importantly, the testimony of record is that no company contacted by Salomon Brothers expressed any concern about that feature of the Pritzker proposal. (Higgins 122).

The indisputable fact is that a very highly motivated, very highly regarded investment banking firm made an intensive three month search for a better offer and found no such offer. There can be no better indication of the fairness of the Pritzker proposal.

Finally, it is apparent from the deposition of Duff and Phelps that its analysis was less than complete and less than objective. Milton L. Miegs ("Miegs"), the employee who conducted the analysis, admitted that plaintiff's counsel had reviewed drafts of the Duff and Phelps report and made suggestions and additions (Miegs 141). Additionally, while the report opines at length on the performance of the TU Directors, Miegs read only the transcripts of the depositions of two Board members, Messrs. Van Gorkom and Chelberg, and did not bother to review the depositions of the other TU Board members. (Miegs 14). Lastly, and most importantly, Miegs was unaware that less than three years ago Duff and Phelps had been retained by TU to evaluate the value of certain TU stock to be issued in an acquisition; at that time Duff and Phelps relied almost exclusively on market value to assess the stock and concluded:

> "We are of the opinion that Trans Union's market performance over the next several years will continue to reflect the market volatility and the past cautious attitude of the investment community toward the company. Based on the historical pattern, it appears that an area of price support for Trans Union common shares could be found in the low 20s, based mainly on the stability and growth potential of the company's dividend." (Miegs 151-52, Ex. 6).

F. Plaintiff's Statement Of Facts

Plaintiff devotes about 40 pages of his brief to describing his perception of the merger proposal and the circumstances out of which it arose. While plaintiff's selected culling from the deposition testimony permits him to draw an imaginative picture of those events, it is a picture at odds with the actual events and it is a picture with which defendants disagree in numerous respects. Since, however, the TU Board has now reviewed the entire merger proposal in light of the actions and inactions of which plaintiff appears to complain and has concluded unanimously that the merger proposal is in the best interests of TU stockholders, factual disputes as to events preceding the recent Board meeting are no longer relevant.

Nevertheless, we do note in passing several particularly far-fetched assertions of plaintiff:

(1) On page 16 of his brief, plaintiff suggests that Van Gorkom, after learning that Romans and Bonser were working "night and day" on a leveraged buyout of KKR and after learning that Romans and Bonser wanted to replace him and Chelberg as the top officers in the company, "wasted no time" and immediately sought out J. Pritzker. What plaintiff overlooks is that the testimony of Van Gorkom cited in support of those assertions reflects that Van Gorkom learned of the actions and aspirations of Romans and Bonser subsequent, not prior, to the approval by the Board of the Pritzker proposal. Thus, the causal relationship plaintiff suggests is without any record support.

(2) On page 40, in describing the collapse of the KKR proposal, plaintiff says:

> "The key person in the operation of Union Tank was Mr. Jack Kruizenga. He actually ran Union Tank (Van Gorkom 199). He was a member of management participating in the KKR proposal (Van Gorkom 266). Both Mr. Van Gorkom and Mr. Robert Pritzker had individually had conferences with this key man (Van Gorkom 198; Robert Pritzker 38-45). Mr. Kruizenga withdrew and the KKR deal fell apart."

Obviously plaintiff seeks to suggest that Kruizenga withdrew from the KKR deal after being confronted by Van Gorkom and Robert Pritzker. An examination of the record references cited by plaintiff, however, discloses that the "conferences" referred to occurred, in the case of Robert Pritzker, in mid-September, and in the case of Van Gorkom in late September, long before the collapse in December of the KKR proposal. Again, only plaintiff's imagination, and not facts of record, support plaintiff's claims.

(3) In arguing that the 1 million share agreement had an inhibiting effect on other prospective offerors, plaintiff twice claims that one such effect was that "the Pritzkers would be using '92¢ dollars' as opposed to '100¢ dollars' which any alternative bidder would have to utilize." (Plaintiff's Brief at 36, 62). This superficial analysis ignores the fact that any such offeror would be buying a company with $38 million more in cash received from the purchase of the shares. When that is considered, the actual

figures in plaintiff's analysis, assuming the analysis has any relevance, would be "98¢" versus "100¢."

(4) Plaintiff repeatedly notes that Salomon Brothers has not opined on the fairness of the merger price and repeatedly suggests that Salomon Brothers refused to give such an opinion (e.g. "Salomon Brothers at the time specifically declined and significantly declined to make any statement on the fairness of the Pritzker merger proposal." PB-34). The fact, of which plaintiff is well aware, is that the TU Board determined that no such opinion was needed, and Salomon Brothers has never been asked for such an opinion.

ARGUMENT

I. PLAINTIFF BEARS THE BURDEN OF ESTABLISHING THE PROBABILITY OF ULTIMATE SUCCESS ON THE MERITS AND THE EXISTENCE OF IMMINENT, IRREPARABLE INJURY WHICH OUTWEIGHS POTENTIAL INJURY TO DEFENDANTS AND TO PLAINTIFF'S FELLOW STOCKHOLDERS IF THE RELIEF SOUGHT IS GRANTED

Preliminary injunctive relief is an extraordinary remedy and is not casually or routinely granted. Petty v. Penntech Papers, Inc., Del. Ch., 317 A.2d 140 (1975). The exacting two-part test to be applied in deciding an application for preliminary injunctive relief is familiar to the Court. As Chancellor Quillen wrote in Gimbel v. Signal Companies, Inc., Del. Ch., 316 A.2d 599, 602, aff'd, 316 A.2d 619 (1974):

> The Court must ask itself two familiar questions. [They are:]...
>
> * * *
>
> "Has the plaintiff satisfied the Court that there is a reasonable probability of his ultimate success on final hearing?"...
>
> * * *
>
> "Has the plaintiff satisfied the Court that he will suffer irreparable injury if the Court fails to issue the requested preliminary injunction?"

Moreover, the second question must be considered in light of potential harm to the defendant:

> In the exercise of sound judicial discretion in the award or denial of a preliminary injunction, the Court should balance the conveniences of the

> parties and the possible injuries to them according as they may be affected by the granting or the withholding of the injunction.

Id. Accord, Petty v. Penntech Papers, Inc., Del. Ch., 347 A.2d 140, 141 (1975).

Plaintiff's brief cites no case, and we are aware of none, in which this Court has enjoined an arm's length merger. On the basis of the present record, it is clear that plaintiff has not made and cannot make the necessary showing that would entitle him to the drastic relief involved in enjoining the merger proposed here. As demonstrated in Section II, infra, the enormous potential harm to plaintiff's fellow stockholders, not to mention the harm to the Pritzkers, that would result from the entry of a preliminary injunction greatly outweighs any conceivable harm from the merger to plaintiff or any "class" of stockholders of TU situated similarly to plaintiff.* Moreover, as demonstrated in Section III, infra, plaintiff cannot demonstrate any reasonable probability of ultimate success in meeting the very strict "fraud or constructive fraud" test which should be applied to this merger.

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* As already discussed, plaintiff's opposition to the merger is based upon his peculiar tax situation which makes his aims practically unique among TU stockholders. See Section II.B, infra.

II. <u>THE ENORMOUS POTENTIAL HARM TO TRANS UNION STOCKHOLDERS AND TO THE PRITZKER INTERESTS WHICH WOULD RESULT FROM AN ENJOINING OF THE MERGER FAR OUTWEIGHS ANY HARM TO PLAINTIFF OR ANY CLASS OF TRANS UNION STOCKHOLDERS SIMILARLY SITUATED WHICH COULD CONCEIVABLY RESULT FROM THE MERGER</u>

In assessing whether plaintiff has carried his burden of demonstrating irreparable injury, the Court must weigh the potential injury to plaintiff's fellow stockholders and to the Pritzker interests if the merger is enjoined against the plaintiff's assertions of injury to him which would result from the consummation of the merger.

A. <u>A Preliminary Injunction Would Result in Enormous Harm to Plaintiff's Fellow Stockholders and to the Pritzker Interests</u>

The proposed merger affords a premium to the TU stockholders of over $222 million. This represents the aggregate value of the cash consideration offered in the merger over the market price for TU shares on the day before the merger was announced. A preliminary injunction would, as a practical matter, eliminate the possibility of this merger. The March 31, 1981 time limit for consummation of the merger set by the Pritzkers would expire. This time limit is, in turn, dictated by the identical cut-off date of their commitment for favorable (14% interest) financing. The TU stockholders would be left with only the speculation, or hope, that a better offer would emerge.

It is idle to speculate at a time when the prime rate is 20% that the Pritzkers or any other potential buyer could arrange for financing at two-thirds of prime. If the existing commitments expire, at the very least the proposed merger will be abandoned. (Pritzker Aff. ¶7).*

Hence, plaintiff's claim that an injunction will cause the Pritzkers no harm (PB 103) is the rankest speculation. And the harm that may befall TU's stockholders if the only merger offer extant goes away seems readily apparent. In short, the GL offer will not survive a preliminary injunction, which would irreparably alter the status quo to the detriment of both TU's stockholders and GL.

On the other hand, the benefits of the present offer are obvious. The price to be paid represents a premium of 62% over the average of the high and low at which TU's shares traded in 1980 before the merger was announced and of about 47% over the last closing price before the announcement. If the opportunity represented by this merger is terminated by the Court through the issuance of an injunction and the price returns thereafter to the $37.25 price on

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* As Jay Pritzker testified at his deposition, GL's offer was premised upon the interest rate commitments available in late September. (J. Pritzker 32). Given those interest rates Jay Pritzker concluded "that we could afford to pay $55 but that we could not afford to pay any more". (J. Pritzker 87).

September 19, 1980, the last trading date before the announcement of the merger, the stockholders of TU will have lost $17.75 per share for each of 12,512,956 shares, or a total of approximately $222,104,969. Even if the price per share only falls to $45-$46 -- a range suggested by the plaintiff in his deposition (Smith 292) -- the lost opportunity to TU's stockholders would still be on the order of at least $112,616,604.

In addition, the interests of the Pritzkers in not being deprived of a valuable business opportunity are entitled to be weighed against the plaintiff's. The Pritzker interests have negotiated at arm's length and in good faith for the proposed merger, have incurred substantial costs, and have tied up substantial sums of money in order to be able to consummate the merger on bargained for terms on an agreed upon time schedule. There is absolutely no evidence of any wrongdoing on their part.

Neither the Pritzker interests nor the stockholders of TU should be deprived of the opportunity represented by the present merger on the basis of plaintiff's speculation that better offers will emerge if the Court is willing to enjoin the present merger. If the merger is not enjoined the TU stockholders will be able to decide for themselves whether or not the proposed merger should be consummated. As this Court noted in <u>Weinberger v. United Financial Corp.</u>

of California, Del. Ch., 405 A.2d 134, 137 (1979), "the rights of those stockholders... who wish to take advantage of the merger price offered must be taken into account". The stockholders of TU entitled to vote on the merger (with the exception of the less than 1% of TU shares owned by the Trusts) are in no way affiliated with the Pritzker interests and have been fully informed in TU's original and supplementary proxy materials about possibilities for other mergers on other terms. Assuming that they vote to accept the terms of the merger rather than rely upon a speculative hope of something better, the Court should not veto that decision on the basis of the harm asserted by a plaintiff who is representative of at best a small segment of TU stockholders.

B. The Peculiar Harm Asserted by Plaintiff Provides No Basis for the Drastic Relief Sought

Plaintiff purports to bring this action on behalf of a class of all stockholders of TU. He has not, however, moved for class certification and, on the basis of the present record, is clearly not representative of the stockholders of TU. Indeed, the present record suggests that he has a very unusual investment strategy with respect to his

TU stock -- one which is apparently representative of a class consisting only of himself and Compre Loveless, his partner. Although there is presumably some price which would be high enough to cause him to prefer a merger to no merger, there is no basis in the record to believe that there is any possibility of a merger with terms sufficiently favorable that he would prefer it to no merger. This is, of course, in direct opposition to the interests of the vast majority of his fellow stockholders and results from his continuing endeavor, begun more than 15 years ago, to avoid paying capital gains taxes of $218,800. Hence, the Court should be exceedingly wary of his assertions concerning the possibilities of other offers since his interests would best be served by blocking the present merger in the hope that such offers <u>will</u> <u>not</u> be forthcoming.

Plaintiff purports to be concerned about (1) the tax consequences which the merger will have for certain TU stockholders who have a low basis and (2) the price which is being offered. As to the first concern, there is no indication in the record that such consequences would be sufficient to cause any substantial number of stockholders to oppose the present merger. But, more importantly, even to the extent that there are TU stockholders who, like plaintiff, have a tax position which makes the present merger unattractive, the Court should not be asked to intervene on their behalf to the detriment of the other stockholders in order to provide them something that they cannot accomplish through the use of their votes against the merger. See Marks v. Wolfson, Del. Ch., 188 A.2d 680, 687 (1963).

The stockholder vote which is to take place on February 10, 1981, will, of course, be the best evidence of the strength of the competing interests of the various TU stockholders. If a majority of TU stockholders prefer to accept the sizable premium offered by the present merger, albeit on a "taxable" basis, the Court should not lend its aid to the disgruntled minority. The fact that the tax laws may have different effects on the various stockholders of TU does not provide a basis for the dissatisfied minority to invoke the aid of this Court. As the court noted in Marks v. Wolfson, supra, 188 A.2d at 687, any "injustice" which plaintiff believes may result from differing tax treatment is not a matter for "judicial correction" by this Court.*

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* Plaintiff does not cite Marks, supra, but does cite Lewis v. Great Western Corp., Del. Ch., No. 5397, September 15, 1977, 3 Del.J.Corp.L. 583 (1978) to suggest that the Court should take cognizance of the disparate tax interests of TU's stockholders. However, Great Western was an "interested" merger case in which the burden was on the defendants to prove the "entire fairness" of the transaction. Moreover, the "unfairness" alleged with respect to the tax consequences involved there was that the entire class on whose behalf the

(Cont'd)

Plaintiff's concern about undervaluation of his TU stock is answered directly in Weinberger v. United Financial Corp. of California, Del. Ch., 405 A.2d 134, 137 (1979):

> Nor has [plaintiff] demonstrated the threat of irreparable injury as a result of failure to obtain the entry of a preliminary injunction [citing Gimbel, supra], as plaintiff and other dissenting stockholders are not only entitled to a fair hearing but to an appraisal.

Plaintiff has made no showing that any damage which he might be awarded after a final hearing (whether in the present action or an appraisal proceeding) could not be compensated in damages at such time as he has proven a right to damages. Relegating plaintiff to such a remedy is particularly appropriate where, as here, the alternative is to eliminate the possibility of a merger which the majority of TU's stockholders must view as beneficial, and endorse by their votes, in order for the merger to proceed. Weinberger v. United Financial Corp. of California, supra.

(Footnote continued from preceding page)

injunction was sought was to be deprived of its equity position in the company and given, not cash, but rather a debt instrument (which would be a taxable event) without giving them any cash to pay the tax and with some possibility that their debt securities could be liquidated only at a large discount. Like the claim rejected in Marks and unlike that in Great Western, plaintiff's claim in this case is one of discriminatory tax treatment arising from the fact that the merger will have varying tax consequences for the various TU stockholders. Such a claim could, of course, be made in any cash merger.

III. PLAINTIFF CANNOT CARRY HIS BURDEN OF DEMONSTRATING A REASONABLE PROBABILITY OF SUCCESS ON THE MERITS

A. The "Fraud or Constructive Fraud" Test to Be Applied to Third Party Mergers Cannot be Met Where the Merger Price Constitutes a Substantial Premium over Market, Was Negotiated at Arm's Length and Where Competing Offers Have Actively Been Sought

Plaintiff apparently has abandoned his allegation that the proposed merger is the product of a conspiracy. In fact, it is a classic "third party" or "arm's length" merger uncomplicated by any interests which stand on both sides of the transaction. Plaintiff does maintain that TU's board, including its independent directors and notwithstanding their wide business experience, breached its fiduciary duty in approving and recommending the merger. This assertion will not stand up, as demonstrated at III.B, _infra_. Hence, for purposes of his motion to enjoin the merger plaintiff must show a reasonable probability of success in convincing the Court that the merger agreement is so grossly unfair to the TU stockholders as to constitute a constructive fraud. _See generally_ E. Folk, The Delaware General Corporation Law, §251,4c (1972) at 339-341; Nathan & Shapiro, Legal Standard of Fairness of Merger Terms Under Delaware Law, 2 Del.J.Corp.L. 44, 45 (1977) (in arm's length mergers a court will not substitute its judgment for that of board of directors unless the terms of the merger are "so patently unfair as to shock the conscience of the court").

This Court recently had the occasion to apply the constructive fraud test in Weinberger v. United Financial Corp. of California, Del. Ch., 405 A.2d 134 (1979). Relying in part upon "the rights of those stockholders of United Financial Corporation who wished to take advantage of the merger price offered", the Court held that:

> In short, the substantial premium over market price proposed to be paid to those stockholders who elect to participate in the pending merger, namely 77.8%, cannot be said to be grossly unfair, constitute a conscious abuse of discretion, or be deemed to be a constructively fraudulent act on the part of the board of directors of United Financial Corporation. Accordingly, I am not satisfied that plaintiff has demonstrated a reasonable probability of ultimate success after final hearing....

405 A.2d at 137 (emphasis added). As in Weinberger, supra, given the "substantial premium over market price" available here, it is obvious that none of the terms which the Chancellor used to describe the "constructive fraud" test can be applied to the present transaction.

Moreover, the facts of the present case present even a lesser probability of success on the merits than did the facts in Weinberger in that here, unlike the facts recited in Weinberger, the $55 merger price has faced a market test for a period of four months during which time a large New York investment banking firm with a substantial self-interest in finding a better offer has been unable to generate anything but speculation that other offers _might_ be available at some undefined time in the future.

In _Abelow v. Symonds_, Del. Ch., 184 A.2d 173, 178 (1962), _aff'd_, 189 A.2d 675 (1963), this Court noted that arm's length bargaining is the best method of arriving at a fair selling price: "[A]rm's length bargaining between a willing buyer and seller is a time tested method of arriving at a fair selling price for corporate assets...." _See also_ _Alcott v. Hyman_, Del. Ch., 184 A.2d 90, 95 (1962), _aff'd_, Del. Supr., 206 A.2d 501 (1965) ("Arm's length bargaining is a time tested method of arriving at a fair price"). For this same reason, the Court should give no weight to the hastily prepared Duff & Phelps speculations as to the value of TU's stock.

It is also worth noting that the $55 price in the proposed merger is well within all of the various "ranges" of fair prices discussed in the various depositions taken by plaintiff in this action. The acceptance or rejection of prices within those ranges was clearly a matter for the exercise of the directors' business judgment. As Vice Chancellor Brown recently stated in _Kaplan v. Goldsamt_, Del. Ch., 380 A.2d 556, 568 (1977), relying _inter alia_ on _Cole v. National Cash Credit Association_, a "third party" merger case:

> In the area of valuation, wide discretion is allowed to the directors, and as long

> as they appear to act in good faith, with honest motives, and for honest ends, the exercise of their discretion will not be interfered with by the courts. Muschel v. Western Union Corp., Del. Ch., 310 A.2d 904 (1973); Cole v. National Cash Credit Association, 18 Del. Ch. 47, 156 A. 183 (1931). The presumption of sound business judgment reposed in the board of directors will not be disturbed if any rational business purpose can be attributed to its decision. Sinclair Oil Corporation v. Levien, Del. Supr., 280 A.2d 717 (1971); accord, Gimbel v. Signal Companies, Inc., Del. Ch., 316 A.2d 599, aff'd, Del. Supr., 316 A.2d 619 (1974).

Notwithstanding Salomon's efforts and the arm's length origin of the merger proposal, plaintiff argues, based on the Duff & Phelps report, that the proposed merger is "unfair to TU's stockholders" (PB 67). The legal standard which he seeks to apply, without citation to any authority, is that the defendants have the burden of establishing the fairness of the transaction. (PB 67). Given the applicable "constructive fraud" standard in this arm's length merger, plaintiff's claim that the price is "unfair" is irrelevant as a matter of law. Further, the Duff & Phelps report is premised almost entirely upon a discounted cash flow analysis which has been found by this Court to be inherently speculative and therefore unacceptable for valuation purposes. See Frick v. American President Lines, Ltd., Del. Ch., C.A. 3766 (Letter Opinion dated June 19, 1975), and was not relied upon by Duff & Phelps in arriving at the radically lower conclusion as to the value of TU's stock which appears in their 1978 report which they prepared at TU's behest.

Finally, whatever the appropriate standard, the Duff & Phelps report is simply insufficient on its face to raise any real question about the fairness of the price. The indisputable facts of record are: (1) the price represents a significant premium over the market price at which the stock was traded prior to the merger; (2) an extensive search for a better offer was made by a prestigious investment banking firm, highly motivated by the terms of its retention;* (3) no other offer has been forthcoming and (4) the only expressions of interest have been in the range of $60 per share or less. In light of these facts, it cannot be said that the price being paid is unfair, let alone grossly unfair. On the present record, it is simply inconceivable that plaintiff will be able to demonstrate that the terms of the merger are "grossly unfair, constitute a conscious abuse of discretion, or be deemed to be a constructively fraudulent act on the part of the board of directors". Weinberger v. United Financial Corp. of California, supra, 405 A.2d at 137.

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* As previously noted, while Duff & Phelps speculates that time constraints and the terms of the Pritzker proposal discouraged other offers, such speculation is contradicted by facts of record, namely that no company contacted by Salomon Brothers gave any indication that there was insufficient time or gave any indication that the 1,000,00 share feature was of concern. (Higgins 122, 130-131).

B. The TU Directors Gave Repeated and <u>Adequate Consideration to the Proposed Merger</u>

Plaintiff's primary contention is that the defendant directors breached their fiduciary duty of due care in that they made an "uninformed" business decision to recommend to the stockholders that the merger be accepted (PB 53-67). contrary to plaintiff's assertions, the plain facts are that at September 20 the TU Board was very much apprised of TU's prospects in light of its consideration in August of the Boston Consulting Group study and the Five-Year Forecast and that it accepted an offer that was within a range that even Romans viewed as reasonable and was structured in such a way that it enabled TU to obtain a better offer if one were available.

Much of plaintiff's argument concerning the TU Board's alleged acceptance of a bad deal appears to center around the wholly unsupported premise that four months on the auction block was not long enough to obtain better offers. The only plausible evidence of record is in direct contradiction to this premise. Mr. Higgins, of Salomon Brothers, testified that the amount of time was not a factor in the failure to obtain a better offer. (Higgins 131-132).

Plaintiff's only response was the Duff & Phelps opinion that four months was not long enough for an acquiring company to analyze a complex company like TU. <u>See</u> Duff &

Phelps Report at 23-26. Even ignoring the fact that the Pritzker interests were able to analyze the company in the one-week period between September 14 and September 20, the opinion is particularly lacking in credibility in that Duff & Phelps was retained only two and one-half weeks before the date of its report which purports to instruct the Court on the true value of TU.

Between the time that the original arm's length bargain arrived at between Jay Pritzker and Van Gorkom was approved by TU's board of directors on September 20 and the board's unanimous decision to recommend the merger to the stockholders at the directors' meeting on January 26, the directors had occasion to weigh the present offer against other possible offers. Of course, as other offers became more or less likely, their evaluations of the present offer varied to some extent as did their recollections at their depositions of the details of what occurred at the directors' meetings which took place over that four-month period. Plaintiff has made much of scattered expressions of opposition to the merger made at various times and for various reasons by two of TU's ten directors and by certain members of its management. However, any possible theory of liability based upon the manner by which TU and its directors went about the task of evaluating the merger proposal has been ruled out by the disclosures and discussions at the January 26 meeting.

At that meeting, as described in the affidavit of William Moore, TU's secretary and general counsel, the events of the period from September 20 to January 26 were discussed and all material information which plaintiff has unearthed in discovery was fully considered and discussed. After such discussions, and with knowledge that they were free to alter their recommendation with respect to the merger, TU's directors unanimously recommended that its stockholders vote in favor of the proposed merger

In Muschel v. Western Union Corp., Del. Ch., 310 A.2d 904 (1973), plaintiffs argued that the merger in question there should be enjoined because the Western Union board had not considered the various materials which plaintiffs contended were material to their decision. Defendants submitted an affidavit stating that a meeting had been held the prior day and that all matters raised by plaintiffs were considered and that after full review, discussion and consideration the directors had unanimously voted to approve the merger. The Court noted that insofar as the application for an injunction rested on the refusal of the board to meet and consider withdrawing from the merger agreements on the basis of the facts deemed material by plaintiffs, "it seems to have vanished with the meeting". 310 A.2d at 909. Similarly, to the extent that plaintiff's argument is based upon an alleged failure by TU's Board fully to consider matters which plaintiff deems relevant, the relevance of any such claims have "vanished" with the January 26 meeting.

Finally, the full consideration which the board gave this matter from September 20 to January 26 and the fact that the market was tested distinguishes the two cases upon which plaintiff relies.

In Signal v. Gimbel, Del. Ch., 316 A.2d 599, 612, aff'd, 316 A.2d 619 (1974), as the quote from the case at page 56 of plaintiff's brief reveals, "[t]here was no effort made to determine if other companies would offer a higher price". In the present case, of course, there have been intensive efforts by Salomon Brothers to make just such a determination. More importantly, however, Signal does not stand for the proposition for which plaintiffs cite it. The Signal Court found that, notwithstanding the haste within which the directors there had to act, they could not be said "to have passed an unintelligent and unadvised judgment". 316 A.2d at 615. The Court held that:

> The ultimate question is not one of [the] method [by which the directors reached their decision] but one of value.

Id. The Court found that the evidence of value which was offered was of such a magnitude "to suggest that someone may be dead wrong". Id. at 617. As noted, supra, Section III.A, plaintiff cannot demonstrate any reasonable probability of success in establishing a gross disparity in value sufficient to allow the Court to second guess the directors' business judgment.

Similarly, in Thomas v. Kemper, Del. Ch., C.A. No. 4138 (1973), as revealed in the quote on page 59 of plaintiff's brief, "It was readily apparent that at least one other group was not only interested in acquiring the Sugarland's lands... but was willing to top White and Hill's offer as to cash". (emphasis added).

In Weinberger v. United Financial Corp., supra, the Court distinguished Thomas v. Kemper on the ground that, in Weinberger, as in the present case and unlike Thomas, "there [was] no evidence of a firm offer of a greater amount". 405 A.2d at 136. In Thomas, the "fundamental error of business judgment" upon which relief was premised was the directors' "insistence in continuing to deal solely with White and Hill... after it was readily apparent" that there was a better offer available... Thomas, supra, at 12, Plaintiff's Exhibit 23, pp. 5-6. Hence, the TU Board's continuing and repeated consideration of the merger and of the possibilities of other offers completely distinguishes this case from Thomas.

Plaintiff makes much of the fact that the directors were not informed in advance by Van Gorkom about the subject of the September 20 meeting and the fact that the deal required prompt acceptance. They overlook the fact that Van Gorkom had insisted from the very beginning of negotiation with the Pritzkers that TU had to be allowed to obtain other offers and that the merger price was to provide a floor for other offers (J. Pritzker 27-28). Under those circumstances, a prompt decision did not foreclose, and, indeed, was designed to prompt, other offers. Moreover, the Board continued to reevaluate and reconsider the proposed merger through Monday of this week when they once again, after much discussion, voted unanimously to recommend the merger. They clearly have dutifully exercised their business judgment with respect to the merger.

For purposes of the present motion, the Court should assume that the stockholders of TU will approve the merger. As the Court noted in Abramson v. Nytronics, Inc., S.D.N.Y., 312 F.Supp. 512, 527 (1970)(applying Delaware law), it is "appropriate" to assume that the transaction will be approved because "if the proposal is defeated by the stockholders, plaintiff's case is rendered moot".

The supplement to the proxy statement which was sent to the stockholders fully described and discussed the basis for the board's recommendation that the stockholders approve the merger. To the extent that any basis whatsoever could remain after the January 26 meeting for complaint about either the basis of the baord's recommendation or the process by which that recommendation was reached, such complaint will be rendered moot by approval of a majority of TU stockholders who have full knowledge of all material facts. As the Supreme Court noted in Michelson v. Duncan, Del. Ch., 407 A.2d 211, 224 (1979):

> [T]he entire atmosphere is freshened and a new set of rules invoked where formal approval has been given by a majority of independent, fully informed stockholders.... [Quoting Gottlieb v. Hayden Chemical Corp., Del. Ch., 91 A.2d 57, 59 (1952)]

Indeed, stockholder approval will limit the Court's review after a final hearing to the standards set by the business judgment rule. As the Court stated in Lewis v. Hat Corp. of America, Del. Ch., 150 A.2d 750, 753-54 (1959):

> The complaint centers on the alleged impropriety of the acquisition of the properties of Champ Hats by Hat Corporation and ignores the fact that this basic transaction was fully disclosed to the stockholders and ratified by them.
>
> * * *
>
> It is clearly established in Delaware that stockholders ratification of corporate action which is not per se void renders such action immune from minority stockholder attack.... It is well established that it is not the proper

> function of this Court to overturn a business transaction duly ratified by the stockholders absent a showing of fraud, a gift of assets, illegality or ultra vires action....

And, as the Court stated in Michelson v. Duncan, Del. Ch., 386 A.2d 1144, 1155 (1978), aff'd in part, rev'd in part on other grounds, 407 A.2d 211 (1979):

> If the stockholders, after receiving a disclosure of all germane facts given with complete candor, cannot ratify an act by the Board of Directors not constituting a gift or waste of corporate assets, corporate democracy is meaningless.

As already discussed, it is inconceivable on the present record that plaintiff will be able to demonstrate that the terms of the merger constitute "constructive fraud" which he must do to prevail in a suit, like this one, involving an arm's length merger. Accordingly, any claim by plaintiff of a probability of success on the merits of his attack upon the directors' exercise of business judgment must be rejected.

IV. TU'S PROXY MATERIALS MAKE DISCLOSURE OF ALL INFORMATION A REASONABLE STOCKHOLDER WOULD CONSIDER IMPORTANT IN MAKING AN INFORMED JUDGMENT CONCERNING THE PROPOSED MERGER

In Kaplan v. Goldsamt, Del. Ch., 380 A.2d 556, 565-66 (1977), this Court summarized the nature of a Delaware corporation's disclosure obligations to its stockholders:

> [W]hile a corporation must adequately inform shareholders as to matters under consideration, the requirement of full disclosure does not mean that a proxy statement must satisfy unreasonable or absolute standards. Many people may disagree as to what should or should not be in such a statement to shareholders, and as to alleged omissions the simplest test (sometimes difficult of application) is whether the omitted fact is material. Kaufman v. Shoenberg, 33 Del.Ch. 211, 91 A.2d 786 (1952). There is obviously no requirement to include insignificant information. Compare Baron v. Pressed Metals of America, Del.Supr., 35 Del.Ch. 581, 123 A.2d 848 (1956); American Hardware Corporation v. Savage Arms Corporation, 37 Del.Ch., 10, 135 A.2d 725 (1957). Provided that the proxy statement viewed in its entirety sufficiently discloses the matter to be voted upon, the omission or inclusion of a particular item is within the area of management judgment. Schiff v. RKO Pictures Corp., 34 Del.Ch. 329, 104 A.2d 267 (1954).

This long standing view of the Delaware courts comports with the recent expression of the United States Supreme Court in TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 96 S.Ct. 2126, 48 L.Ed.2d 757 (1976) wherein it

> was stated that in order for an omission to be material,
>
> "...there must be a substantial likelihood that the disclosure of the fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." Id., 96 S.Ct. at 2133.

Plaintiff, in a twelfth hour attempt to divert the Court's attention from the simple fact that this is an arm's length merger which is being presented in good faith to TU's stockholders for their consideration, has sought to amend his complaint to add what he characterizes as a "litany" of alleged undisclosed and misstated material facts. Even a cursory review of those allegations, however, makes clear that such alleged "facts" are either adequately disclosed in TU's original proxy materials, are disclosed in TU's supplemental proxy materials which "crossed" with plaintiff's amendment to his complaint, or are simply not material.

While the brief lists 17 alleged nondisclosures or misstatements, plaintiff discusses in his brief only two. First, he claims that the record shows the presence of undisclosed tax benefits to GL, the omission of which in TU's proxy materials is misleading to stockholders. In doing so, he chooses to overlook the disclosure in TU's proxy statement that GL "should be able to take greater advantage of the tax benefits inherent in Trans Union's operations by utilizing taxable income generated by other members of the GL consolidated tax group" (p. 12) and that TU's leasing operations are "dependent to a large extent upon general conditions such as levels of economic activity, interest rates, inflation and federal income tax laws" (p. 3). Moreover, TU's September 26, 1980 supplement to its proxy statement contains the following disclosure at page 2:

> For several years, the Board of Directors and management of Trans Union have considered and assessed a future course for the Company with particular emphasis on how to utilize the investment tax credit and other "tax benefits" inherent in the Company's principal operations, the leasing of railroad tank cars. While the Company's net income has more than doubled over the past ten years and the outlook for future growth is favorable, the Company's taxable income has been insufficient for it to obtain optimum benefit from the utilization of such "tax benefits". Accordingly, management gave consideration to acquiring other companies in order to generate additional taxable income, and some members of management gave consideration to the sale of the Company upon favorable terms to an entity more able to utilize such "tax benefits". The Chairman of the Board of the Company, Mr. Jerome W. Van Gorkom, and certain other members of the Board of Directors and management of the Company believed that the Company's inability to optimize the use of such "tax benefits" would be exacerbated if current proposals to change the federal income tax laws, as they relate to accelerated depreciation, were enacted.

In short, there is no basis for plaintiff's claim of undisclosed tax benefits.*

Similarly, plaintiff's claim that TU has failed adequately to disclose the projections contained in TU's business plan prepared in July, 1980 is without merit. TU's proxy statement, at page 3, discloses that such projections were furnished to GL and to other potential acquirors and that such projections indicate that TU's net income might increase to approximately $153 million in 1985 (Proxy Statement, p. 3). This disclosed projection is almost three times the net income of $58,248,000 reported by TU as its net income for December 31, 1979, and is certainly sufficient to place TU's stockholders on notice that there is a basis for the belief of the Board of Directors, stated at page 3 of the proxy statement, that TU's prospects for future earnings growth are "excellent". Notwithstanding this candid disclosure of projected earnings, plaintiff would have TU go further to provide to stockholders projections of cash flow. In Securities Act Release No. 5377, CCH Fed.Sec.L.Rep. ¶72,164 (a copy of which is attached to this brief as an exhibit),

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* Of course, plaintiff also ignores the fact that TU's consolidated financial statements, which set forth the exact amount of TU's deferred federal income taxes and investment tax credits, are a part of TU's proxy statement.

the Securities and Exchange Commission made clear that the type of disclosure sought by plaintiff decreases the credibility of conventional financial statements as a measure of business activity and tends to create confusion among stockholders:

> The variation in form and purposes of such data creates confusion. The term "Cash Flow" and similar formulations such as "Earnings Before Non-Cash Charges", "Adjusted Net Income", "Net Operating Income" and "Operating Funds Generated" do not have precise definitions and may mean different things to different people. In addition to this definitional problem, there are different purposes for presenting these data...
>
> While differing definitions and purposes are basic sources of confusion investors and registrants are experiencing with "cash flow" data, the presentation of such data on a per share basis confounds this confusion.

CCH Fed.Sec.L.Rep. ¶72,164 at 62,325. After noting that "it is not clear that the simple omission of depreciation and other non-cash charges deducted in the computation of debt income provides an appropriate alternative measure of performance for an industry either in theory or in practice", the Commission goes on to state:

> This problem was recognized by the Accounting Principles Board in Opinion No. 19 where it was noted that "the amount of working capital or cash provided from operations is not a substitute for or an improvement upon properly determined net income as a measure of results of operations....

> If accounting net income computed in conformity with generally accepted accounting principles is not an accurate reflection of economic performance for a company or an industry, it is not an appropriate solution to have each company independently decide what the best measure of performance should be and present that figure to its shareholders as Truth. This would result in many different concepts and numbers which could not be used meaningfully by investors to compare different candidates for their investment dollars.

CCH Fed.Sec.L.Rep. ¶72,164 at 62,326. Finally, after noting that the major problem in the presentation of cash flow data is that of investor understanding, the Commission concludes as follows:

> Sales, current assets, funds flow, total assets, cash and other similar figures cannot logically be related to the common shareholder without adjustment. These are aggregate data which are of great importance to analyst and management alike in understanding the operations of the total economic entity, but they are not items which accrue directly to the benefit of the owner of a part of the common equity. Charges and claims must be considered before the owner is benefited.

CCH Fed.Sec.L.Rep. ¶72,164 at 62,328.

To the extent a sophisticated stockholder is concerned with the general cash flow position of TU, historical information is available in TU's source and use of funds analysis in its financial statements. As is clear from the above-quoted SEC release, for TU to have gone beyond that disclosure and the narratives with respect to "tax benefits" set forth in its proxy materials to present to stockholders projected cash flows would have been inherently confusing and misleading to such stockholders. Far from failing to make appropriate disclosure as plaintiff suggests, TU has adhered to the Securities and Exchange Commission's guidelines and has made the appropriate disclosures with respect to cash flow.

Plaintiff's remaining litany of alleged nondisclosures and misstatements is so insubstantial as to not even merit treatment in his own brief. With reference to the numbered paragraphs at pages 88 through 91 of his brief, all such alleged nondisclosures and material misstatements fall into the following broad categories:

a. Allegations with respect to alleged inadequate disclosure of "tax benefits", cash flows and projections, already discussed in detail above and shown to be either disclosed insofar as they exist and are material or to be not appropriate subjects for disclosure (¶¶ 1-6, 16).

b. Allegations that the 1,000,000 share transaction is not adequately disclosed, when in fact it is discussed in detail at page 2 of the Proxy Statement and the agreement giving rise to the purchase is set forth in full at Appendix 1 to said Statement (¶¶ 7-9, 13).

c. Allegations that the proxy statement fails to disclose advantageous income tax consequences available to the Trusts arising out of the 1,000,000 share transaction and their status as Bahamian residents, a fact which is logically irrelevant to any assessment by stockholders of the merits or demerits of the proposed merger (¶¶ 10-11). See Pritzker Aff. ¶6.

d. Allegations of nondisclosure of facts which either are trivial, inaccurate, or, in the case of those which are material, are fully disclosed in TU's original or supplemental proxy materials (¶¶12, 14, 15, 17). See Pritzker Aff. ¶4.

In short, the product of TU's extraordinary efforts to keep its stockholders informed with respect to the details of the merger, including the issuance of its supplemental proxy materials which literally place the stockholders "in the board room", should be commended, not excoriated, and cannot be the basis for a claim that the merger vote should be enjoined.

CONCLUSION

For the reasons stated herein, and in the Affidavit of Jay A. Pritzker filed herewith, plaintiff's application for preliminary injunctive relief should be denied.

MORRIS, NICHOLS, ARSHT & TUNNELL

A. Gilchrist Sparks

Lewis S. Black, Jr.
A. Gilchrist Sparks, III
Richard D. Allen
John F. Johnston
1105 North Market Street
P.O. Box 1347
Wilmington, Delaware 19899
(302) 658-9200

Attorneys for Defendants
Jay A. Pritzker, Robert A.
Pritzker, The Marmon Group,
Inc., GL Corporation and
New T Co.

January 29, 1981

EXHIBIT A

lists and standard product catalogs, and reports to stockholders should also not be considered advertising costs for purposes of this rule.

It is recognized that the distinction between advertising costs and other selling expenses is frequently not clear cut. Where the guidance set forth herein is not sufficient to enable the registrant to determine the appropriateness of including or excluding certain classifications of significant costs, disclosure of the type of costs included or excluded from the caption will be a satisfactory solution.

Under Item 8, Research and development costs, all costs charged to expense as incurred in the current period for the benefit of the company in these account classifications should be reported. These would include company sponsored projects of pure and practical research as well as the development of new products or services or new or better production machinery and equipment and for the improvement of existing products and services. The amortization of deferred research and development costs should not be included herein since this amount is described in Item 3 of the schedule.[1]

PART B—CORRECTIONS, CLARIFICATIONS AND EDITORIAL CHANGES

(The text of the amendments of Rules 1-02, 3-15, 5-02-23, 5-03-17, 5-04, 9-05, 12-02, 12-04, 12-06, 12-13, 12-16, 12-42 and 12-43 of Regulation S-X is omitted.)

The amendments to Regulation S-X are adopted pursuant to authority conferred on the Securities and Exchange Commission by the Securities Act of 1933, particularly Sections 6, 7, 8, 10 and 19(a) thereof; the Securities Exchange Act of 1934, particularly Sections 12, 13, 15(d) and 23(a) thereof; the Public Utility Holding Company Act of 1935, particularly Sections 5(b), 14 and 20(a) thereof; and the Investment Company Act of 1940, particularly Sections 8, 30, 31(c) and 38(a) thereof.

By the Commission.

—Footnote—

* The effective date of the requirement for compensating balance disclosure was deferred to cover periods beginning on or after December 30, 1972 (Accounting Series Release No. 136).

[1 This paragraph was rescinded in Accounting Series Release No. 178, October 9, 1975.—CCH.]

[¶ 72,164]

RELEASE NO. 142

March 15, 1973, 38 *F.R.* 9159; *Securities Act Release No.* 5377, *Exchange Act Release No.* 10041.

Reporting Cash Flow and Other Related Data.

Introduction

The Commission has recently received preliminary registration statements which include "cash flow per share" data in the narrative section of the prospectus. Use of such data has also been noted in annual reports to shareholders, particularly in the "Financial Highlights" or "President's Letter" section. These and other means of presenting financial data appear designed to decrease the credibility of conventional financial statements as a measure of business activity.

The variation in form and purposes of such data creates confusion. The term "Cash Flow" and similar formulations such as "Earnings Before Non-Cash Charges," "Adjusted Net Income," "Net Operating Income" and "Operating Funds Generated" do not have precise definitions and may mean different things to different people. In addition to this definitional problem, there are different purposes for presenting these data. One is to present an apparent alternative to net income as a measure of performance. A second is to present information about liquid or near-liquid assets provided by operations which may be available for reinvestment or distribution to shareholders.

While differing definitions and purposes are basic sources of the confusion investors and registrants are experiencing with "cash flow" data, the presentation of such data on a per share basis compounds this confusion.

Numerous questions have been received in regard to the Commission's policy in these matters. This release is being issued to outline the Commission's views.

"Cash Flow" as a Proxy for Income Measurement

One of the principal reasons given for presenting "cash flow" is that the income measurement model currently prescribed by generally accepted accounting principles does not accurately reflect the economic performance of certain types of companies, typically those with substantial assets which arguably do not depreciate or require replacement. While the Commission recognizes that there are problems of income measurement for some industries, the unilateral development and presentation on an unaudited basis of various measures of performance by different companies which constitute departures from the generally understood accounting model has led to conflicting results and confusion for investors. Additionally, it is not clear that the simple omission of depreciation and other non-cash charges deducted in the computation of net income provides an appropriate alternative measure of performance for any industry either in theory or in practice. This problem was recognized by the Accounting Principles Board in Opinion No. 19 where it was noted that "the amount of working capital or cash provided from operations is not a substitute for or an improvement upon properly determined net income as a measure of results of operations . . . ."

If accounting net income computed in conformity with generally accepted accounting principles is not an accurate reflection of economic performance for a company or an industry, it is not an appropriate solution to have each company independently decide what the best measure of its performance should be and present that figure to its shareholders as Truth. This would result in many different concepts and numbers which could not be used meaningfully by investors to compare different candidates for their investment dollars.

Where the measurement of economic performance is an industry-wide problem, representatives of the industry and the accounting profession should present the problem and suggested solutions to the Financial Accounting Standards Board which is the body charged with responsibility for researching and defining principles of financial measurement. Until new and uniform measurement principles are developed and approved for an industry, the presentation of measures of performance other than net income should be approached with extreme caution. Such measures should not be presented in a manner which gives them greater authority or prominence than conventionally computed earnings.

Where management believes that the existing conventional income model does not present the results of operations realistically or fully, an explanation of the reasons and a description of possible alternatives which might be used to measure results may be presented to shareholders and potential investors to supplement conventional financial data. The presentation of additional data in tabular form is also acceptable. Such tables should be accompanied by a careful explanation of the data presented. The adding together of figures derived by different measurement techniques (such as net income and cash flow) should be avoided as should per share data relating to measures other than net income (see discussion below). In addition, when various measurement models are used for different lines of business, there should be a consistent application of such models to all similar segments of the firm's operations. Also, results for all segments included in consolidated statements of net income should be included in any tabular or summary presentation.

Annual reports to shareholders as well as filings with the Commission should include explanations and data as discussed above whenever measurement models other than conventionally computed income are used. Such additional information and data would typically be presented in the "Financial Highlights," the "President's Letter," or the text of the report and should not be presented without also presenting net income. Terms such as "Net Operating Income" which leave the impression that a figure other than net income is really income should not be used.

In cases where a measurement problem exists for an individual company rather than in an entire industry, a solution already exists in the procedures of the accounting profession. Under the newly adopted Code of Ethics of the American Institute of CPA's, an auditor is permitted to render an opinion approving statements prepared even though they deviate from the principles adopted by the Accounting Principles Board (or its successor body) if he believes and can support the assertion that due to unusual circumstances the financial statements would otherwise be misleading. Under such circumstances, full disclosure must be made by both company and auditor, and the basic statements must be prepared in accordance with the principles determined to present operating results most meaningfully. In such cases, the staff of the Commission will naturally consider the circumstances which gave rise to the situation, but it will normally give great weight to the judgment of the registrants and their independent accountants.

The above discussion is designed to assist companies which believe the conventional income measurement model is unsatisfactory in providing disclosure which is useful and not misleading. This discussion is not intended to support or reject any particular new measurement model and the Commission strongly urges the accounting profession and other interested parties to consider the development of new techniques for the measurement of results in industries where the current model seems deficient.

"Cash Flow" as a Measurement of Funds Generated from Operations

A second basic reason for highlighting cash or funds generated from operations data in financial summaries is to show the liquid or near-liquid resources generated from operations which may be available for the discretionary use of management. Analysts have suggested that this is a useful measure of the ability of the entity to accept new investment opportunities, to maintain its current productive capacity by replacement of fixed assets and to make distributions to shareholders without drawing on new external sources of capital.

While presentation of "funds generated from operations" is useful, these data should be considered in the framework of a source and application of funds statement which reflects management's decisions as to the use of these funds and the external sources of capital used. The implication of a presentation which shows only the funds generated from operations portion of a funds statement is that the use of such funds is entirely at the discretion of management. In fact certain obligations (e.g., mortgage payments) may exist even if replacement of non-depreciating assets is considered unnecessary. Therefore presentation of one part of a funds statement should be avoided.

The Commission has also noted situations where investors were misled by cash distributions which were in excess of net income and were not accompanied by disclosure indicating clearly that part of the distribution represented a return of capital. To highlight this fact in cases where funds distributed exceed net income, the Commission developed the "Funds Generated and Funds Disbursed" statement in Form 7-Q which begins with the caption "Income (Loss) Before Realized Gain or Loss on Investments." From that amount the first deduction is "Cash Distributed to Shareholders." The statement then provides for adding non-cash charges and deducting debt repayments to arrive at the "Excess (Deficiency) of Funds Generated Over Distributions." This indicates whether operations generated the cash to make distributions or whether distributions are made from borrowing or other sources.

Cash flow presentations designed to reflect the liquid assets or working capital generated by the firm should be consistent with the principles outlined in this section.

Per Share Information

Many of the problems outlined above are accentuated when "cash flow" data is presented on a per share basis. Most importantly, such a presentation emphasizes the implication that cash flow is more meaningful than net income as a measure of performance, particularly when a per share figure is included in the "Financial Highlights" section of a report.

The first major problem in the presentation of cash flow per share data is that of investor understanding. Investors over many years have grown accustomed to seeing operating per share data computed only in the case of net income. Accounting authorities have considered and largely settled the measurement problems associated with the presentation of net income on a per share basis. If other data are presented in this way, there is a danger that the investor will think that what he is seeing is the conventional accounting measure of earning power when in fact this is not the case. In a number of reports, cash flow per share data have been presented in such a manner as to lead to this inference despite the strong recommendation of the Accounting Principles Board in Opinion No. 19 that "isolated statistics of working capital or cash provided from operations, especially per share amounts, not be presented in annual reports to shareholders." Such presentations run a high risk of materially misleading investors and companies are urged to avoid this type of disclosure.

Beyond the problem of understandability is the question of relevance. The investment community generally recognizes the relevance of "earnings per share" as a measure of the historically achieved earning power of an economic entity in terms of a unit which is being bought, sold and quoted in the market place, the share of common stock. The earning power represented by that share has generally been considered a significant element in the determination of its worth. Net income, as a measure of ultimate result, may reasonably be interpreted on a per share basis since no significant claims stand between it and the common stock owner. Where there are senior equity claims, these are deducted before computing the per share figure. Dividends are similarly logically presented in terms of the individual share, as are net assets.

Significant questions as to relevance arise, however, when other data are presented on a per share basis. Sales, current assets, funds flow, total assets, cash and other similar figures cannot logically be related to the common shareholder without adjustment. These are aggregate data which are of great importance to analysts and management alike in understanding the operations of the total economic entity, but they are not items which accrue directly to the benefit of the owner of a part of the common equity. Charges and claims must be considered before the owner is benefited. To reflect such items on a per share basis may mislead the unsophisticated, since there is an implication that the shareholder is directly affected. In fact, such data are only meaningful from an operating viewpoint and not from that of an external investment unit.

Accordingly, per share data other than that relating to net income, net assets and dividends should be avoided in reporting financial results.

Conclusion

In this release, the Commission has reiterated and explained its view as expressed to individual registrants for many years that certain approaches to "cash flow" reporting may be misleading to investors. All registrants are urged to examine their reporting practices in light of the problems and guidance set forth in this release and to amend them where appropriate.

The Commission recognizes that reporting financial results cannot be a static phenomenon, and it continues to examine its views and policies to determine in what respects change is desirable. In this connection, it welcomes comments and suggestions regarding its policies from registrants and other knowledgeable parties. If any parties have comments on the views and policies set forth in this release, they should be addressed to the Chief Accountant of the Commission.

By the Commission.

[¶ 72,165] **RELEASE NO. 143**

March 20, 1973.

Findings and Order Imposing Remedial Sanction *In the Matter of Robert Lynn Burroughs.*

In these proceedings pursuant to Rule 2(e) of the Commission's Rules of Practice to determine whether Robert Lynn Burroughs, an accountant, should be temporarily or permanently denied the privilege of appearing or practicing before the Commission,[1] he submitted an offer of settlement.

Under the terms o. the offer, respondent, solely for the purpose of these proceedings and without admitting or denying the allegations of the order for proceedings, consented to findings in accordance with the allegations in that order and to the entry of an order censuring him.

After due consideration of the offer of settlement and upon the recommendation of its staff, the Commission determined to accept such offer.

On the basis of the order for proceedings and the offer of settlement, it is found that:[2]

1. Respondent, an employee of a public accounting firm, participated, under the supervision of a partner in the firm, in the audit of the records of a registered broker-dealer.

2. In connection with such audit and the certification of the broker-dealer's financial statement as of September 30, 1971, which was filed with the Commission on Form X-17a-5 pursuant to Rule 17a-5 under the Securities Exchange Act of 1934, respondent failed to comply with generally accepted

EXHIBIT B

COURT OF CHANCERY
OF THE
STATE OF DELAWARE

WILLIAM MARVEL
VICE-CHANCELLOR

June 18, 1975

COURT HOUSE
WILMINGTON, DELAWARE

68

William O. LaMotte, Esquire
1105 North Market Street
Charles Crompton, Jr., Esquire
350 Delaware Trust Building

Re: Frick v. American President Lines, Ltd., C.A. 3766
Submitted: April 21, 1975

This is the Court's decision on certain contested evidentiary rulings made by the Court-appointed appraiser in this case in pending proceedings before him. He has not, of course, at this stage reached a decision on the ultimate question to be decided in this litigation, namely the value of shares of stock of American Mail Lines upon its merger into American President Lines.

The evidentiary rulings in dispute are concerned with the admissibility of the following proffered exhibits.

(1) Petitioners' exhibits 25 through 30,[1] which are revisions 24029 of general order 82 of the Maritime Administration, United States Department of Commerce.

(2) Petitioners' exhibits 42 through 47, which are hull and machinery as well as war risk insurance policies issued to American Mail Lines and covering seven of such company's fleet of ten vessels which were admitted.

(3) Petitioners' exhibit 39, entitled "Projected Value of Discounted Cash Flows" and the testimony of its sponsor, Robert L. Bryant, which were excluded.

(4) Part of petitioners' exhibit 10A, which is a memorandum of W. B. Fowler, chairman of AML's board of directors,

1 Exhibits 25 and 26 were ultimately admitted and 27 through 30 exclud(

addressed to R. E. Benedict, president of AML, containing a purported opinion of a witness who did not testify at the appraisal hearing, which was excluded.

(5) A portion of testimony of defendant's witness Frank Pomery setti forth the earnings of American Mail Lines for the fiscal year 1973, which was exclude

Petitioners' exhibits 25-30 are revisions of general order 82 promulgated by the Maritime Administration, United States Department of Commerce. Each of the revisions sets forth the respective values, which, in the opinion of MarAd's Ship Valuation Committee, would be deemed to constitute just compensation for the numerous vessels listec including those of AML, in the event of their requisition for use by the United States. See section 902(a) of the Merchant Marine Act, 1936, 46 U.S.C. §1242(a). The values listed in the revisions also represent the maximum amount of claims which the United States would be compelled to pay under the insurance binders or policies issued by it pursuant to Title XII of the Act, 46 U.S.C. §§1281-1294 in the event of total loss of an insured vessel by reason of enumerated war risks.

Each revision of general order 82 sets forth a valuation which is effective for a six month period. The revisions, taken collectively, cover the period from the beginning of 1971 to the end of 1973. Each of the revisions purports to set forth a "*** current domestic market value as determined by the Maritime Administration." §309.3(c). However, no member of the MarAd Ship Valuation Committee testified at the appraisal hearing, and the only testimony concerning the basis for the determination of values by such committee was elicited by the petitioners upon cross-examination of defendant's witness, George Kurfehs, who testified that non-governmental data were utilized to assist in the formulation of the values listed in exhibit 25-30. He further testified that he did not believe that the time and effort expended by the persons who had assembled such outside data was substantial.

However, the appraiser admitted petitioners' exhibits 25 and 26 as evidence of the Ship Valuation Committee's "findings" on the value of the vessels for the purposes of requisition and insurance. The appraiser held further, that:

> "***value does become a factor affecting the amount of just comepnsation to be paid should the vessel be taken by the United States government for military use in a time of national emergency. At the time of the merger in question, the state of national emergency which had been proclaimed by President Truman in 1950 (15 Fed. Reg. 9029) had not been rescinded. American Maritime Assoc. v. Stans, (U.S.D.C., D.C., 1971) 329 F.Supp. 1179, 1183. Under such circumstances, I think that the finding by the MarAd Ship Valuation Committee of the value of the vessel to be used in determining the amount payable as just compensation is a factor which would affect the market value of the vessel."

I am of the opinion that the above reasons support a finding of relevancy of the Ship Valuation Committee's findings as to determination of the current market value of the vessels in question.

The appraiser adopted the same reasoning in determining that the amount of war risk insurance obtainable on a vessel is relevant to a determination of the market value, citing De La Rama Steamship Company v. United States (U.S.D.C., S.D.N.Y., 1950) 92 F.Supp. 243, 254, aff'd (2d Cir. 1953) 206 F.2d 651, 655. I agree.

However, I am satisfied that the appraiser erred when he accepted the Committee's findings as evidence of the current domestic value of the vessels in question. Defendant's objections to the proffered evidence as hearsay, in my opinion, were valid.

Petitioner's contend, and the appraiser agreed, that the Committee's valuation fell within the exception to the hearsay rule for government records and documents. I disagree.

The policy underlying the government records exception is found in Wigmore on Evidence, vol. 5 §1632 at 618 as follows: "When it is a part of the duty of a public officer to make a statement as to a fact coming with in his official cognizance, the great probability is that he does his duty and makes a correct statement." (Chadbourn rev. 1974). However, Wigmore goes on to note at 5 Wigmore, Evidence §1672 at 817, 818:

> "....a record of a primary fact made by a public officer in the performance of official duty is or may be made by legislation competent 'prima facie' evidence as to the existence of that fact; but....records of investigations and inquiries conducted, either voluntarily or pursuant to requirement of law, by public officers concerning causes and effects and involving the exercise of judgment and discretion, expressions of opinion, and making conclusions are not admissable as evidence as public records."

See also Federal Rules of Evidence. P.L. 93-595, 88 Stat. 1926 (January 2, 1975), Rule 803(8), 88 Stat. 1940.

Value is not, in my opinion, a primary fact in the absence of a readily ascertainable market quotation derived from active trading in the subject property. Further, it is clear that the determination of the Committee was based upon the judgment of outside experts and not by government officials acting pursuant to their duly authorized duties.

Defendant having been deprived of the opportunity to cross-examine the petitioners' witness either as to the method utilized to calculate vessel values, or to explore the accuracy of estimates of subsequent open market sales, or to determine the expertise of the individuals who determined them, I am of the opinion that the values of the MarAd Ship Valuation Committee are not sufficiently reliable and trustworthy to call for the disregarding of the right of cross-examination. Accordingly the Committee's valuations will be limited in use by the appraiser to a determination of requisition and war risk compensation and the limited effect such elements have on market value.

The appraiser also excluded petitioners' exhibits 27-30 in their entirety. It is clear that under Delaware law the value to be determined is the value as of the date of merger,[2] in the present case, August 18, 1971. Therefore, the Committee's valuations for the period subsequent to the merger, taken in the above context, bear no relationship to the market value of stock of AML prior to the merger and were properly excluded.

Petitioners' exhibits 42-47 are, as noted above, hull and machinery insurance policies as well as war risk insurance policies issued to AML by various insurers for the twelve month period beginning June 1, 1971. Each such exhibit discloses the amount at which each of seven of AML's ten vessels was valued and insured. Exhibits 45 and 46 list in the case of five insured vessels values equal to the book value of such vessels as of June 1, 1971 and for two other vessels insured values approximately equal to the values determined by MarAd pursuant to general order 82. Exhibits 42 and 47, on the other hand, contain amended values for all seven vessels which are all approximately equal to general order 82 values. Such amendments were made pursuant to a change in the insurance requirements of MarAd. The hull and machinery insurance was previously required to be in an amount of no less than the highest of (a) general order 82 value, (b) 110% of mortgage indebtedness or (c) book value. The change eliminated consideration of book value in reaching a determination as to insured value.

2 8 Del. C. §262(b).

Petitioners contend that the defendant accepted the values set forth in MarAd's general order 82 by reason of its failure to challenge such values. However, the appraiser held that neither the appropriate authorities or inferences to be drawn from the record support such a contention. I agree.

The appraiser having admitted into evidence petitioners' exhibits 42-47 on the theory that insurance placed and accepted upon a vessel is relevant as an indication of a minimum valuation, I accept such rulings, believing such determination of the appraiser to be within the "range of reason". As stated in De La Rama Steamship Company v. United States, 92 F. Supp. 243 (S.D.N.Y. 1950), aff'd, 206 F.2d 651 (2d Cir. 1953) at 251 that:

> "In the absence of such a market [for the sale of a vessel], the basis of valuation must be a composite one based on such factors as reconstruction cost less depreciation, the manner in which the vessel had been kept up, appraisals for insurance purposes, earning capacity, original cost where appropriate, extent of demand compared to supply, the amount of war risk insurance obtainable, restrictions to which ships were subject, and so forth."

The court in such case based its ruling upon the theory that "***while a vessel may be underinsured, it is unlikely that it would or could be over-insured, and therefore insurance valuations have some relevance on the question of minimum valuation." 92 F. Supp. at 254. 3 The appraiser, relying upon the De La Rama Steamship case, properly admitted into the record the above exhibits for the limited purpose of their proof of minimum value.

I believe it is clear that an additional factor in connection with the opposing contentions have made acceptance of the insurance policy by the insurers required. Standard practice in the insurance business mandates insurance at or below the appraised value. The defendants' inability to cross examine the experts responsible for the appraisal upon which the insurance policies were based is a matter which, in this instance, goes, in my opinion, to the weight of the evidence not to its admissabilit;

Petitioners' exhibit 39 sets forth a range of "discounted cash flow" values for AML stock as calculated by petitioners' witness Robert L. Bryant. Such witness formulated these values by adding up the cash flows projected for AML for the years 1972 through 1986, by discounting that sum by a selective percentage factor, and by dividing the discounted total projected cash flow by the number of shares of AML stock outstanding at the time of the merger. For the years through 1975, Mr. Bryant based his projection upon the figures appearing in AML'l five year plan, and by extrapolating his projections for those years forecast cash flows for the years 1976 through 1986.

The defendant objected to the introduction of the proposed exhibit and the accompanying testimony of Mr. Bryant for the reasons that (1) the discounted cash flow valuation is not relevant or material to valuation in an appraisal proceeding and (2) such projections of cash flow were too conjectural and speculative. The appraiser upheld the objections and granted a motion to strike the proffered exhibit and testimony thereon on the basis of the above. I agree.

The purpose of an appraisal proceeding and the duties of the appraiser thereunder are set forth in Tri-Continental Corporation v. Battye., Del. Supr. Ct., 74 A.2d 71, 72 (1950) as follows:

> "The basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him, viz., his proportionate interest in a going concern. By value of the stockholder's proportionate interest in the enterprise is meant the true or intrinsic

> value of his stock which has been taken by the merger. In determining what figure represents this true or intrinsic value, the appraiser and the courts must take into consideration all factors and elements which reasonably might enter into the fixing of value. Thus, market value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or which could be ascertained as of the date of merger and which throw any light on future prospects of the merged corporation are not only pertinent to an inquiry as to the value of the dissenting stockholders' interest, but must be considered by the agency fixing the value."

Petitioners contend that the discounted cash flow is relevant an material to the extent that it represents a "factor" or "element" that may "reasonably...enter into" the appraiser's determination of the "true or intrinsic value of [petitioners'] stock." 74 A.2d at 71, 72. And there is no doubt but that cash flow, that is, net profits after taxes plus non-cash charges, such as depreciation, depletion, and amortization, have become important factors in the valuation of a going concern for the purpose of acquisition. This is not to say, however, that the technique is appropriate for the purposes of appraisal.

Petitioners contend that the value of their stock at the date of .e merger was necessarily tied in whith the future prospects of AML, and certain Delaware decisions have held that future prospects are indeed of vital concern in an appraisal proceedings. See Universal City Studios, Inc. v. Francis I. duPont & Co., Del. Supr.Ct., 334 A.2d 216 (1975); In re Olivetti Underwood Corp., Del. Ch., 246 A.2d 800 (1968); Sporborg v. City Specialty Stores, Del. Ch., 123 A.2d 121 (1956); Application of Delaware Racing, Del. Supr. 213 A.2d 203 (1965).

However, the fact that the courts have sought to take into consideration the future prospects of a corporation does not give validity to all means designed to forecast such prospects. The accounting technique known as cash flow analysis seeks to utilize presently available information so as to project future income flow to the corporation. However, mere projections of future earnings have been looked upon with disfavor in Delaware as speculative. See Levin v. Midland-Ross Corp., Del. Ch., 194 A.2d 50, 57 (1963), Cottrell v. Pawcatuck, Del. Supr. Ct., 128 A.2d 225, 231 (1956) and David J. Greene & Co. v. Dunhill International, Inc. Del. Ch. 249 A.2d 427, 433 (1968).

Thus, the cash flow technique sought to be invoked here is, in my opinion, overly speculative for the same reasons, i.e. that it rests upon events which have not been shown to be reasonably probable of happening. See Olson v. United States, 292 U.S. 246, 257 (1934). Compare Korf v. Fleming, Iowa Supr. Ct., 32 N.W. 2d 85, 96 (1948), and Brooklyn Eastern Dist. Terminal v. City of New York, 139 F.2d 1007, 1013 (2d Cir)(1944) cert. den., 322 U.S. 747.

Furthermore, it is apparent that the cash flow analysis is limited in its usefulness as a projection by the very fact that its validity rests upon the financial techniques of a few experts. Accordingly, when the Delaware courts have been confronted with the task of ascertainin the effect of future prospects on the present value of a stock in the absence of an open market, they have turned their attention to aggregate figures. Thus, the capitalization rate for a company is often determined by compiling a weighted price-earnings ratio from a study of the open market price of shares by comparable businesses in the same or similar industry. This figure, which is, in effect, an open market estimation of the future prospects of such business, negatives the factor of individual speculation. This ratio is then applied to the past earnings record of the subject company to determine the market price that the company could reasonably expect to obtain.

I am of the opinion that the appraiser's decision rejecting the admission of petitioner's exhibit 39 and the accompanying testimony was correct and in accord with the law of this state.

Petitioner's exhibit 10A is a memorandum from W. B. Fowler, who was then chairman of AML's board of directors, to R. E. Benedict, who was then AML's president. The exhibits penultimate paragraph informs Benedict of a brief meeting with "Dan Banks of Blythe & Co." to discuss information pertinent to the valuation of AML stock. Fowler then writes, "Banks, as I see it, feels that Lehman Brothers are being a little too tight when they say that the fair value of AML is $40 per share." The appraiser struck this portion of petitioners' exhibit 10A stating:

> "The petitioners' argue that the above quoted portion is admissible for two reasons. First, it is contended that such portion of petitioners' exhibit 10A proves what APL and AML believed to be the share valuation for AML stock. The above quoted language simply cannot support that conclusion. Banks was not an employee of either AML or APL. The above quoted portion does not state what Fowler or Benedict believed. Rather, it states what Fowler perceived Banks to believe. Certainly, this cannot be molded into evidence as proof of what APL or AML thought to be true.
>
> Second, petitioners submit that the above quoted portion is admissible to show the truth of the statement that Banks thought $40 per share to be a "little too tight." I cannot agree. Such evidence of mental attitude is inadmissible as hearsay. Children's Bureau v. Nissen, Del. Super., 29 A.2d 603 (1942). I am also unpersuaded by the petitioners' argument that the perception of Mr. Fowler is so trustworthy as to make the hearsay rule inapplicable."

The appraiser's views are well taken and, in my judgment, in accord with established precedent. There is no error.

Defendant's witness, Frank Pomeroy, testified that for the first nine months of 1973 AML suffered a net loss of $819,600. This testimony was offered by defendant for the sole purpose of impeaching petitioners' projections of financial results for the years 1973, 1974 and 1975 contained in the AML five year plan. The testimony was deemed inadmissible by the appraiser since an attempt to use evidence arising subsequent to the merger to impeach documentary evidence existing before the merger offends the express mandate of 8 Del. C. §262(b) that the value of a dissenting shareholder's stock shall be determined as of the effective date of the merger, "*** exclusive of any element of value arising from the expectation or accomplishment of the merger..." See Tri-Continental Corp. v. Battye., supra.

I agree. The proffered proof of earnings for the fiscal year 1973 is inadmissible under 8 Del. C. §262(b), and it was not error for the appraiser to strike such tender of proof from the record.

An appropriate form of order may be submitted in conformity with the above.

WM/ch

c: Register in Chancery