Doc. #129

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

WILLIAM B. WEINBERGER, Plaintiff, v. UOP, INC., THE SIGNAL COMPANIES, INC., SIGCO INCORPORATED, LEHMAN BROTHERS KUHN LOEB, INC. CHARLES S. ARLEDGE, BREWSTER L. ARMS, ANDREW J. CHITIEA, JAMES V. CRAWFORD, JAMES W. GLANVILLE, RICHARD A. LENON, JOHN O. LOGAN, FRANK J. PIZZITOLA, WILLIAM J. QUINN, FORREST N. SHUMWAY, ROBERT S. STEVENSON, MAYNARD P. VENEMA, WILLIAM E. WALKUP and HARRY H. WETZEL, Defendants.	)	Civil Action No. 5642

PLAINTIFF'S OPENING POST-TRIAL BRIEF
ON REMEDY

William Prickett
PRICKETT, JONES, ELLIOTT
& KRISTOL
1310 King Street
Wilmington, Delaware 19899
Attorneys for Plaintiff

Hand Served
8-18-80
Mr. Payson
(Mr. Halket c/o Mr. Payson)
Mr. Balotti
Mr. Sparks

TABLE OF CONTENTS

TABLE OF CITATIONS

NATURE OF THESE PROCEEDINGS

This is a class action brought by the plaintiff against the corporate defendants. The case was tried to the Court commencing on May 19th and concluded on June 3rd, 1980. At the outset of the trial, the plaintiff served and filed Plaintiff's Pre-Trial Brief on Remedy. The defendants did not file any pre-trial briefs or memoranda on remedy.

The plaintiff incorporates and relies on his Pre-Trial Brief in this, his Post-Trial Brief on Remedy.

QUESTIONS PRESENTED

I. DOES NOT THIS COURT HAVE THE EQUITABLE POWER TO FASHION A REMEDY TO MAKE THE PLAINTIFF CLASS WHOLE?

II. DOES NOT THE FAILURE OF THE DEFENDANTS TO CALL ANY WITNESS FROM LEHMAN BROTHERS SHOW THAT LEHMAN BROTHERS' POSITION IS INDEFENSIBLE?

III. IS NOT THE $21.00 TENDER AND DIRECT PURCHASE PRICE OF $21.00 IN 1975 IRRELEVANT TO THE VALUE OF THE MINORITY SHARES IN 1978?

IV. HAS NOT THE PLAINTIFF PROVED THAT THE VALUE OF THE SHARES WAS NOT LESS THAN $26.00 PER SHARE?

V. HAVE NOT THE DEFENDANTS FAILED TO CARRY THEIR BURDEN OF PROOF THAT THE UOP MINORITY SHARES WERE FAIRLY VALUED AT $21.00?

ARGUMENT

I. THIS COURT HAS JURISDICTION TO FASHION A REMEDY TO MAKE THE PLAINTIFF CLASS WHOLE

Paragraph 17 of the complaint is as follows:

> "17. The plaintiff has no adequate remedy at law."

The defendants' answer is:

> "17. Denied."

The plaintiff's Amended Complaint requests the following relief:

> "1. That the Court enter an order enlarging the class to include all outside stockholders of UOP as of May 28, 1978.
>
> "2. Rendering judgment for the plaintiff and the class for the losses incurred by the class as a result of the acts of the defendants.
>
> "3. Awarding the plaintiff the costs and expenses of this litigation, including reasonable attorneys' fees.
>
> "4. Granting such other and further relief as may be just, including rescission, if appropriate, or rescissionary damages."

The Plaintiff's Pre-Trial Brief on Remedy points out that the equitable powers of this Court enable it to fashion the appropriate remedy to make the plaintiff class whole (pg. 15-22). Specifically, this Court can:

> "1. Order recission;
>
> "2. Order that Signal issue shares of its own stock to compensate UOP's minority shareholders for the difference between $21.00 and the true value of their UOP stock;
>
> "3. Order that UOP stockholders be given a portion of Signal's business in the form of a new venture;

"4. Order the distribution to UOP's minority shareholders of certain UOP's assets (including excess liquidity and timberland) which do not contribute significantly to its earning power;

"5. Order monetary award in the amount that bona fide arm's length negotiations would have produced as a per share price in this transaction;

"6. Order an award of monetary damages for the true value of UOP's stock; or,

"7. Award other appropriate relief pursuant to its equitable powers."

Though the suit was filed on July 6, 1978, about two weeks after the merger of May 26, 1978, and has been diligently pursued by the plaintiff since that time, more than two years have expired since the time of the cash-out merger of the minority shareholders of UOP. Since this was a cash merger, rescission remains a viable alternative though the defendants may try to establish insurmountable practical problems. The solution may be for the Court to order Signal to pay the minority shareholders of UOP for the difference between the cash-out price and the fair value of the minority UOP shares by:

(a) Issuing Signal common stock from Signal's treasury (if there is sufficient common stock in the Signal treasury), or

(b) Issuing a new special class of Signal common stock to the minority shareholders of UOP.

This would give the minority shareholders what they were deprived of -- an equity position in the total enterprise of which Signal had entirely taken over for itself by cashing out the minority shareholders of UOP. The UOP shareholders would have an equity interest as of the time of the Court's order that would reflect the "ups and downs" of Signal (including UOP) since the time of the merger. It would also be in accordance with the strong admonition of Vice Chancellor Hartnett in _Tanzer v. International General Industries, Inc._, Del. Ch., 402 A.2d 382, 391 (1979), that, in cases of mergers that eliminate minority stockholders, the minority be given an equity interest in the surviving entity. It, however, may in the end be simpler and more desirable from the minority's point of view to award monetary damages to the minority shareholders of UOP based on the diference between the merger price and the value of the shares, plus interest. Of course, in order for the Court to determine the _extent_ of the remedy required to make the plaintiff class whole (short of rescission) it is necessary for the Court to make an initial determination as to the true value of the minority shares of UOP as of the time of the merger. Hence, the plaintiff (while by no means suggesting that the plaintiff's remedy of choice will be money damages) will go forward in the balance of this brief and show why the record establishes that the value of the minority shares was not less than $26.00 per share.

Finally, _Schreiber v. Bryan_, Del. Ch., 396 A.2d 513 (1978), makes it clear that the defendants had the burden of proving that the $21.00 merger price was fair. Nevertheless, the plaintiff class has not relied on that advantage that they had as the trial opened: instead, they have gone forward and affirmatively established that the fair value of the minority shares of UOP was not less than $26.00 per share.

* * *

This Court has the equitable power to fashion the appropriate remedy to make the plaintiff class whole. To determine the extent of the remedy chosen will require a determination by the Court of the true value of the minority shares of UOP at the time of the cash-out merger.

II. THE FAILURE OF THE DEFENDANTS TO CALL ANY WITNESS FROM LEHMAN BROTHERS SHOWS THAT LEHMAN BROTHERS' POSITION IS INDEFENSIBLE

Conspicuous by his absence at the trial was Mr. Glanville, a director of UOP (Note) and a managing partner of Lehman Brothers at the time of the cash-out merger in 1978. Mr. Glanville had been represented to the UOP directors and to the minority stockholders as the person uniquely qualified to give a fairness opinion on the cash-out merger price of $21.00 (EX U-7). Of course, it may be that Mr. Glanville was not called by the defendants as a live witness at trial because Mr. Glanville, on deposition, had admitted that the basis for his opinion was simply that the merger price included 50% premium above market (Glanville 114-118). Or it may have been because Mr. Glanville was the person who directed the preparation of the 1976 memorandum advising Signal that it would be in Signal's best interest to cash-out the minority stockholders in 1976 for up to $21.00 a share. Of course, Mr. Glanville claimed that he did not remember having ordered the preparation of the memorandum (Glanville 24-25).

It was represented by counsel for Lehman Brothers off the record that Mr. Glanville had back trouble (TR 593). On

---

Note: Since Mr. Glanville was a director of UOP, his knowledge and activities are attributable to UOP, including, of course, the existence of LB-40, the memo he directed be prepared advising Signal in 1976 that it would be in Signal's best interest to cash out the minority for up to $21.00 per share.

June 3, 1980, counsel for Lehman Brothers stated (TR 1026-7):

> "MR. BALOTTI: Good morning, your Honor.
>
> "At the close of last Friday's session after we went off the record I told the Court that we would not be calling Mr. Glanville <u>as a defendant</u> in this action, and that I was informed that Mr. Glanville was entering the hospital today.
>
> "<u>To the best of my knowledge, that is still accurate, and I stated that that was one of the factors which influenced our decision not to call Mr. Glanville</u>. My recollection is that Mr. Prickett took issue with my remarks, and invited me to make them on the record, and I am doing so this morning. Thank you.
>
> "THE COURT: Any comment on the record in response to that, Mr. Prickett?
>
> "MR. PRICKETT: Yes, your Honor.
>
> "I think Mr. Balotti missed the point. After we had gone off the record on Friday he did suggest that Mr. Glanville was going into the hospital. I didn't take issue with that. I simply said that it should be made on the record because the defendants are tendering as the reason why Mr. Glanville is not appearing as a witness in this case is because of medical reasons.
>
> "I said that if Mr. Balotti would state as a fact as an officer of the court that in fact his client was going into the hospital, though we really don't know whether it's optional or what it is, we know he's in the hospital, and I accept that as correct to the best of his attorney's knowledge, and we now know that for some reason Mr. Glanville is going in the hospital today, and won't be here for trial. (Note)
>
> "THE COURT: Very good."

Note: If Mr. Glanville were only temporarily indisposed, the plaintiff would have made every reasonable accommodation to Mr. Glanville to make it possible for him to present his live testimony, almost at his personal convenience, as indeed was done at this very trial with other witnesses.

There was no elucidation by counsel or by an affidavit of Mr. Glanville, much less by his doctor or the hospital, as to whether Mr. Glanville's hospitalization was optional or mandatory, serious or not serious, whether his stay was going to be prolonged or whether he would be out of the hospital the very same day. The point is that no full or satisfactory explanation having been given for the defendants having failed to call Mr. Glanville, the Court as trier of fact may draw adverse inferences from Mr. Glanville's absence. Richard v. Jones, 16 Del. Ch. 227, 142 A. 832 (1928); Gammel v. Candler-Hill Corp., Del. Supr., 103 A.2d 228 (1954); Jett v. Texas Co., 73 F.Supp. 699 (D.Del. 1947); Anno. 5 ALR 2d 893, 907-908 (1949).

But the situation gives rise to further questions and inferences. First, Lehman Brothers is a large prestigious New York investment banking firm. (Denison v. Fibreboard, supra.) Mr. Glanville was only one of the senior executives. Assuming that Mr. Glanville was indisposed, any one of a number of the other managing partners of Lehman Brothers could have made themselves familiar with the opinion that was expressed on behalf of Lehman Brothers and come to Delaware to defend the Lehman Brothers opinion which had been given to the minority stockholders. Another Lehman Brothers executive could also have tried to explain how Lehman Brothers could prepare an opinion in 1976 that it was in Signal's best interest to cash out the minority at $21.00 and two years later, when the financial picture of UOP had dramatically improved, prepare an opinion for the minority advising them that $21.00 was a fair price for these same shares. No such managing partner of Lehman Brothers testified at trial. The inference that flows from the foregoing is that Lehman Brothers could not take the risk of defending their position in the Courts of Delaware by exposing one of their managing partners to further questions about the contradictory 1976 and 1978 opinions on the value of the minority shares of UOP.

However, Lehman Brothers' present position is even worse. There were four other Lehman Brothers employees who directly participated in the two opinions dealing with value of the minority shares of UOP. Mr. Schwarzman headed the three-man team that was supposed to have done the backup and research that was recited in the opinion letter as the basis for the "fairness" opinion (EX U-7-D-1). Mr. Schwarzman was not called. The two Lehman Brother employees who actually did the work on the report over the weekend before it was delivered, Mr. Pearson and Mr. Seegal, were not called. Finally, Mr. Altman, a former employee of Lehman Brothers and the man who, with Mr. Seegal, had had a hand in the preparation of LB-40, the memorandum advising Signal in 1976 that a cash-out of the minority shareholders at anything up to $21.00 would be advantageous to Signal, was not called. The failure to call any of the foregoing employees gives rise to a host of adverse inferences which the Court as the trier of fact should draw.

However, the most glaring deficiency in the defense so far both as liability and remedy are concerned is the total absence of any explanation as to how Lehman Brothers could decide and draw up an opinion that it was in the best interest of Signal to cash-out the minority stockholders of UOP at $21.00 in 1976 (the nadir of the financial fortunes of UOP) and two years later decide and issue another opinion advising the minority stockholders that it was in their best interest to be cashed out at $21.00. The point is not simply the failure to reveal the existence of the report as Lehman Brothers (and particularly Mr. Glanville, a director of UOP) was obligated to do. The very heart of the question is how to reconcile or explain the two obviously conflicting opinions. The Court in this situation need not draw adverse inferences: it should simply decide that if, in the privacy of its own research department, Lehman Brothers came to the conclusion that the value of the minority shares was worth $21.00 to Signal in 1976, then in view of the changed and improved situation, these same shares were worth not less than $26.00 to Signal in 1978.

* * *

The failure to call Mr. Glanville or indeed any Lehman Brothers' managing director or other employee gives rise to the adverse inference that the Lehman Brothers position was in fact indefensible and that the value of the minority shares was not less than $26.00 in 1978.

III. THE 1975 TENDER AND DIRECT PURCHASE PRICE OF $21.00 IS IRRELEVANT TO THE VALUE OF THE MINORITY SHARES IN 1978

At the time Signal decided to cash out the minority shareholders of UOP, the defendants owed the minority shareholders the fiduciary duty not only of complete candor but fairness. Mr. Walkup, Chairman of the Board of Signal, admitted that the minority shareholders of UOP were entitled to be paid the fair value of their UOP shares (TR 1693; 1706-1707). The defendants have admitted, inter alia, in their Rule 41 argument (TR 990, et seq.), that no arm's length bargaining to arrive at a negotiated price was possible because Signal and UOP were both wearing "two hats" (TR 998, et seq.; 1682; 1710). The defendants claim, however, that they made a determination that $21.00 was a fair price for the minority shares: neither Signal (TR 1678; 1696-7) nor the management (TR 1504, et seq.; Crawford 62) nor the Board of UOP (EX U-298) made any determination whatsoever as to the value of the minority shares. Rather, Signal's inner management first determined that the cash-out of the minority shareholders of UOP would be economically advantageous to Signal at any price, up to and including $24.00 per share (TR 1670; 1678-79). Signal then announced a price range of $20.00 to $21.00 and got prompt agreement that the price range was "generous" from Mr. Crawford, himself a Signal director, but also the President and Chief Executive Officer of UOP (TR 1507; 1711). Third (aside from repeatedly misrepresenting that there were "negotiations" between Signal and UOP relating to the merger price), the defendants justified the ultimate $21.00 cash-out price because $21.00 was also the price of Signal's 1975 tender offer and Signal's 1975 direct purchase of UOP treasury shares (TR 1698, 1707; EX U-298; EX U-7). (The defendants and their expert, William Purcell of Dillon, Read, also said that the $21.00 price was justifiable on "psychological" grounds (TR 1142, 1707; Crawford 68; Purcell 198-200).).

Mr. Walkup testified in his direct examination at trial (TR 1652):

> "A. Yes. I knew that the 1975 acquisition of the 50.5 percent was greatly oversubscribed. So that was to me a clear indication of how the market reacted to it at that time. We tendered for 4.3 million and 7.8 million shares were tendered, so we had to prorate them back. And I felt that the $21 price was certainly a very generous price."

However, Mr. Walkup was forced to concede on cross-examination that the amounts that had been offered and paid in the 1975 tender and the 1975 direct payment were irrelevant to a minority stockholder whose interest it was to obtain the 1978 fair value for his UOP shares which Signal was expropriating (TR 1706):

> "Q. Oh, sure. He paid market value. But in a merger in '78, he would be interested not in what was paid in '75 either by Signal for direct shares or Signal in a tender offer. He would be interested in the fair value of his shares, isn't that right?
>
> "A. Yes. The answer is yes.

"Q. And he's entitled to that?

"A. Exactly."

Mr. Kenneth Bodenstein confirmed the obvious: that the fact that Signal had made a tender offer at $21.00 in 1975 and also a direct purchase at $21.00 offer price in 1975 had no bearing at all on the value of the minority shares in 1978. These were three totally different transactions (TR 319-321). In spite of the foregoing, Mr. Purcell, the defendants' expert said that the results of the two 1975 transactions were taken into consideration by him in determining the value of the minority shares of UOP in 1978! (TR 1142).

* * *

Though the defendants had a fiduciary obligation to deal fairly with the minority, none of them made any attempt to determine the 1978 value of the minority shares. Instead, they justified the $21.00 cash-out merger price on the totally irrelevant ground that it was the same figure that had been offered by Signal after negotiation in the 1975 tender offer and the 1975 direct purchase.

IV. THE PLAINTIFF PROVED THAT THE VALUE OF THE MINORITY SHARES WAS NOT LESS THAN $26.00 PER SHARE

A. The Plaintiff's Proof

The plaintiff retained Kenneth Bodenstein, C.F.A. of Duff & Phelps to provide a financial analysis of the worth of the stock of UOP. Mr. Bodenstein's academic (MBA Columbia), professional (Chartered Financial Analyst) and practical qualifications (twenty years experience) are impressive. His work in preparation for the presentation of an understandable report was detailed and thorough.

There are several overall points that should be kept in mind. First, Mr. Bodenstein made it repeatedly clear that his professional opinion on the value of the shares of UOP would be precisely the same no matter whether the work had been undertaken at the request of Signal, a third party or the minority shareholder (TR 137, 144). Second, Mr. Bodenstein was not trying ex post facto to justify a price that had already been acted on in 1978: he was asked and did determine the value of UOP as a company in 1978 (TR 140, et seq.). Third, Mr. Bodenstein was consistently conservative at each and every stage of all of his analyses. Thus, the value of not less than $26.00 per share is a minimum figure since it itself is a conservative summation of many different analyses, each of which was itself conservatively calculated (TR 248, 255, 262, 286, 469, 477). An example of Mr. Bodenstein's consistently conservative approach is his postulate of "no growth" for UOP observed in all three discounted cash flow analyses (TR 249). Also, in this connection, Mr. Bodenstein, in line with his conservative approach, made his determination as of the date of the announcement of the merger, February 28, 1978, rather than the date of the vote on the merger, May 26, 1978 (TR 372). Mr. Bodenstein testified (TR 372):

> "There was a general appreciation in the market indexes of around 13%."

Mr. Bodenstein testified that there was nothing in the merger agreement that would reflect the general market rise between February 28, 1978, and May 26, 1978 (TR 373). Not only was there nothing in the agreement but the effect of the announcement of the merger agreement would cap the market or put a ceiling on it (TR 374). (Note) Fourth, Mr. Bodenstein's report and his responses on direct and cross-examination prove that the minimum value of not less than $26.00 was not simply his "feeling" that this was a "fair" figure (TR 1462), or an intuitive on-the-spot determination made without research or calculations (Glanville 117-118) or a solemn but unexplained "opinion" (TR 1133). Rather, it was a thoroughly professional evaluation based on numerous

---

Note: Mr. Bodenstein, as part of his conservative approach, did not include anything in connection with the obvious undervaluation of the patents and royalties which were all carried on UOP's balance sheet at only $2,285,000.00. Obviously, an appraisal of their value should have been made (TR 367; also Haskins & Sells' Cost Analysis of UOP's assets, including patents and royalties, EX S-360, pg. 35).

detailed and rational financial analyses. Mr. Bodenstein's method was to utilize many different analysis techniques and determine objectively the range of value that each technique provided. He analogized his approach as being similar to delineating as many of the spokes of a wheel as possible to see what the hub of the wheel (or what the price range) would be (TR 145). All of the "spokes" were clearly and openly delineated at trial. Thus, the record shows how the plaintiff has proved that the minority shares were worth not less than $26.00 per share.

B. There Is No Dispute That UOP's Financial Condition Improved Dramatically After 1976

At the outset of his testimony, Mr. Bodenstein testified that his examination of the financial records of UOP indicated that following the disastrous Come-By-Chance Refinery write-off of $31 million in 1976, there was a "dramatic" improvement in all aspects of UOP's financial condition: UOP's earnings (after the $31,000,000.00 write-off) went from $23.6 million in 1976 to $31.4 million in 1977 (TR 190). To Mr. Bodenstein, the significance of the $31 million earnings of UOP in 1977 was that they not only demonstrated an increasing trend but were in themselves at record levels (TR 180):

> "Well the significance, in one instance, it was a strong trend upward from the '75 unusual year. The other, the significant item to the thirty-one ($31 million) is that, as you look at the column, it is the highest in the last five-year period."

Mr. Bodenstein then turned to the importance of UOP's improving financial results from the point of view of continuing operations. He said (TR 181):

> "Q. Why is that so important in a financial analyst's view?
>
> "A. Well, we look at that line from continuing operations before taxes and extraordinary items because that is really the true measuring stick of management. It is before the whims of Congress to raise or decrease taxes. Taxes has a third-party hand in it. This is a result from operations, from continuing operations. <u>These are the earnings that the buyer is going to buy</u>."

Mr. Bodenstein pointed out that the 1977 earnings from continuing operations had reached the highest level and that the upward trend was continuing in 1978 (TR 182):

> "A. It just again shows a record of the 1977 41.8 million was the highest in this period of time. And, if I recollect, the highest the company had made. And the performance was continuing into the first quarter of '78."

Mr. Bodenstein also noted that earnings per share increased in 1977 (TR 182):

> "A. The earnings per share is the recorded figures from the company's annual report. It is showing that earnings per share were at 2.7 for a share, up from 2.06 in '76, and approximating 2.78 as of 1974. And the reason the earnings-per-share growth is not as dramatic as the growth in earnings from continuing operations is that as a result of the 1975 purchase of Signal of 1.5 million shares, it increased the number of shares outstanding and, therefore, dilutes the earnings per share."

The reason revenues as such were not quite as high in '77 as they had been in '74 is because, as Mr. Bodenstein explained, there had been a shift by UOP to those divisions that had a greater capability for making a profit. Thus, though revenues were not quite as high as in 1974, profits were higher (TR 187):

> "Well, that type of analysis of mix and looking at the profit margins of profit groups, obviously the higher profit margin provides a higher quality of earnings, and the trend towards this provides an analyst comfort that this company is moving in the right direction."

The comparison between the first quarter of '77 and the first quarter of '78 showed continued improvement in results (TR 189):

> "Q. Okay. Now, in comparing the first quarter of '77 with the first quarter of '78, does it reflect any improvement in the first quarter results measured against first quarter results of the prior year?
>
> "A. Yes.
>
> "Q. And does that have any special significance for you in terms of the quantitative and qualitative analysis you are making?
>
> "A. It just provides the input that business is going along as good as ever.

Mr. Bodenstein made an examination and analysis of the balance sheet of UOP from 1975 through the first quarter of 1978. He testified that there were "tremendous" changes in that period: UOP changed from having a heavy load of short and long term debt to having virtually no short term debt, greatly reduced long term debt, unused bank credit and about $50 million in cash (TR 193):

> "Okay. And what is the answer to the question?
>
> "A. The answer is that from year end '75 through the period in question, the company had made a substantial turnaround in its financial position. Number one, its working capital increased substantially from approximately $92,000,000 at the end

of '75 to the area of $163,000,000 at the end of '77. The cash position went from $24,000,000 to $73,000,000. At the same time, and most important, the short term bank loans, which was at $55,000,000 at the end of '75, reduced to one and a half million.

"So there was a dramatic change in the company's -- from becoming a borrower to banks on a short term basis, it turns around and was able to reduce that debt to practically zero. It increased its working capital and cash position -- and cash as a part of working capital substantially. Its long term debt and lease obligations declined from around $90,000,000 to $85,000,000 and of importancy on that line, I think the long term debt represented something like $65,000,000 out of that $85,000,000. The rest are long term lease commitments which now have to be recorded as long term liability.

"And so from a financial analyst's view, this company was making tremendous strides not only in improving their financial position, but had achieved it dramatically."

Mr. Bodenstein testified that, as of 1977, there was no longer any financial justification for Signal's 1975 infusion of capital (TR 195):

"Q. Well, does the turnaround in the balance sheet position that you have been talking about relate to the infusion of capital by Signal?

"A. Well, to an extent, yes. But as I said, there was a reduction of some 55, or let's say 50 million in bank loans, an increase of cash of another 50, so that's a hundred million dollars. Signal's contribution in its purchase of treasury shares was only .5 times 21, which is around 32-1/2 million.

"So to some extent there was some liquidity given to the company by that purchase, but the majority of it was self-generated by the business, obviously.

"Q. And in '77 was there any necessity for the 31.5 million dollars of cash capital infusion which Signal had made?

"A. Not as of '77 there wasn't." (Note)

In conclusion, there was no dispute between the parties (and their experts) that the actual financial results for UOP showed radical improvement after the 1975 write-off and the 1978 merger. PX 11 illustrates UOP's financial results.

U O P (PX 11) 1974 to 1977	(000's)		Receivable		12/31/77 139,000 3/31/78 172,000
	12/31/74	12/31/75	12/31/76	12/31/77	3/31/78
CASH & MRKT SECURITIES	$25,228	$23,779	$53,952	$72,979	46,000
WORKING CAPITAL	114,807	91,849	137,585	162,829	168,000
CURRENT RATIO	1.74	1.93	1.93	1.95	1.99
(Short Term Debt) BANK LOANS	48,970 54,000	53,708 58,000	2,380 7,000	1,571 8,000	1.500 8,000
LONG TERM DEBT & LEASE OBLIGATIONS	92,904 79,000	89,545 75,000	89,382	84,799	8,200
SHAREHOLDERS EQUITY	193,939	182,689	203,702	227,914	237,000
BOOK VALUE PER SHARE	19.43	15.91	17.74	19.86	20.67

Note: It should be noted that in cashing out the minority, Signal was repatriating, so to speak, the $31.5 million that it had invested in UOP in 1975. As Mr. Bodenstein testified, the excess liquidity (i.e., cash which a 100% owner, such as Signal turned out to be) could at the 100% owner's option be taken out of the business without hurting the income stream which UOP was producing (TR 211, et seq.).

Specifically, Mr. Purcell agreed that this exhibit correctly summarizes UOP's financial situation (TR 1302-1319) and it was admitted without objection. (Note)

C. Comparable Analyses Showed That the Value of the Shares of the Minority of UOP Was Worth Between $24.65 and $27.30 Per Share

After analyzing and determining that the market was fairly valuing the shares of UOP based on UOP's financial performance (P/E ratio, currient yield, dividend percent payout) (TR 326-328), Mr. Bodenstein did a financial analysis of UOP as a whole by comparing it with other companies of similar size (TR 323). He gave the reasons why UOP as a whole was valued (TR 328):

> "Well, since we are valuing this company for 100-percent ownership or for sale, we then look at comparable situations that were happening in the marketplace at the same time or during the same period. So therefore, we looked at the major acquisitions and mergers being enacted during that period. We selected the year June 1st, '77, I think, through the May period of '78.
>
> "Q. And what are you attempting to determine in that comparison?
>
> "A. We are seeking to determine what value the marketplace is paying for 100-percent ownership."

Note: Mr. Purcell suggested some different numbers and these were noted on PX 11 and circled: these differences are relatively slight and in any case do not affect the overall significance of PX 11 -- that from 1976 - 1978 UOP's financial performance showed marked, significant and continued improvement.

After indicating that the comparative criteria had to be mergers of over $100 million that took place in the same general time frame as the Signal merger, Mr. Bodenstein pointed out that there was a critical difference between acquisitions for 100% control and acquisitions for less than 100% control (TR 330):

> "It is the difference we described between the '75 and '78 type of transaction of The Signal-UOP. In 100-percent control you are receiving the minority shares' rights to future participation in the company. In a lesser acquisition of size, where you are seeking only 20-percent control or 30-percent or 40 or 50 or 60, you are providing the choice to remain a shareholder of the company to that minority shareholder. Those that wish to tender, can. Those that wish to remain participant in the company have the right to remain."

Mr. Bodenstein then measured what the marketplace had done in comparable situations (TR 331):

> "Again, to get the feel for what the marketplace was paying in terms of price-earnings ratios, market-to-book values, we value for that 100-percent attribute.
>
> "Q. And then when you got a feel for what the market would do, would you apply that to the price of UOP, which you determined was reasonable, and then see what the total price for UOP should have been?
>
> "A. Well, with the three major variables we would conclude what we felt was a reasonable price for value for UOP and then test it against the results of our comparable analysis in this acquisition area."

Mr. Bodenstein defined premium (TR 332):

> "It is the difference between the offer price from the poor [prior] minority price divided -- that's the dollar value. And we divide the original minority price into that, and you get a percentage premium."

Mr. Bodenstein described the term minority price as the market price being paid for minority positions in a company such as UOP in trades, for example, over the New York Stock Exchange (TR 333).

Mr. Bodenstein described what the seller sells and that the buyer gets for "premium" (TR 335):

> "These are the attributes of 100-percent control. And the seller is giving up -- the main attribute in his future participation in the growth of the company in terms of future appreciation in earnings and dividends. The buyer is getting 100-percent control, 100-percent voting control, 100-percent right to dividends, 100-percent control of deciding where the business goes and where it dosn't go."

By looking at comparable transactions, one can determine what value the marketplace is placing on the attributes that the seller is giving up and the buyer is acquiring (TR 336). Of course, a transaction is only comparable where 100% ownership is successfully acquired(TR 337).

Mr. Bodenstein testified that in making an analysis of premium it was vital to determine the market price unaffected by the merger in which the amount of premium is being measured (TR 348). There is what is commonly known in securities vernacular as "noise" resulting from leaks, rumors or almost simultaneous bids from other would-be acquirors (TR 350, et seq.). Mr. Bodenstein testified as to how "noise" is filtered out: by determining through analysis when the trading on the market of minority shares was unaffected by leaks, rumors or anticipation by the market of the merger or acquisition (TR 354). In doing his comparative analysis of premiums, Mr. Bodenstein determined the unaffected market or minority price of each of the comparables chosen, to make sure that market price was not being run up in price or volume based on advance knowledge or market premonition of the merger. Having done this, he determined the average as well as the median of premiums paid in the comparable mergers (i.e, those involving successful $100 million acquisitions of 100% control (TR 360). Specifically, Mr. Bodenstein testified as follows (TR 360):

> "Q. If the last line of Page 16, Plaintiff's for Identification No. 3, the Duff & Phelps report, were not there, what could you use the chart for? How could you utilize this chart in advising either Signal if they were selling or buying, or anybody, if they are using this?
>
> "A. Well, as we do, we would be advising the buyer or seller that at this period of time the average or median premiums for acquisition of 100-percent control were the area of 70 to 75-percent or between 70 and 80. These numbers aren't to be used as exact numbers. They are used to give us a feeling of order of magnitude. <u>So we would say that the area of average and median is in the area of 70 to 80 percent</u>."

Based on his analysis of the premium paid in comparable transactions, Mr. Bodenstein showed that a prospective buyer or a prospective seller should have been told that the proper premium for the acquisition of 100% control of UOP was between 70% to 80% of the market price (TR 361).

The UOP minority shareholders actually received a premium of only 42%. If an 80% premium had been paid, the UOP shareholders would have received not less than $27.30. (Note)

Note: Signal's timing was exquisite: it announced the merger when the price was as low as it was during the entire month of February 1968 (EX U-7).

D. Discounted Cash Flow Method, 1977 Applied to UOP Showed the Minority Shares Were Worth Between $25.21 and $28.09

Mr. Bodenstein testified that the discounted cash flow method is an accurate and long recognized method by which he, other chartered financial analysts and others knowledgeable in financial matters commonly use to determine the value of a business as a whole (TR 148-49). The basic concept of the discounted cash flow is simply an analysis of the "cash generating capability of a company as a going concern" (TR 152). The analysis determines what amount of free cash the business will throw off since this is what a buyer (or a 100% owner) can take out of the business (TR 151). Mr. Bodenstein explained the discounted cash flow method one step at a time. It was therefore made clear how the discounted cash flow method works in general and specifically what the analysis shows when it was applied to UOP's 1977 financial results. Thus, the use of the discounted cash flow method did not represent a "rabbit out of the hat": the calculations were done before the Court and appear fully in the record of the trial of this case.

The 1977 discounted cash flow analysis of UOP involved the financial figures of 1977, a closed year for UOP and simply applying the method to see what the result would be. First, however, Mr. Bodenstein made it clear that depreciation (and certain other items, such as deferred taxes) is a cash item (TR 154):

"Depreciation is an allowable expense by accounting principles and by the IRS. And therefore, it is an allowable deduction but it is a non-cash outlay. And therefore it produces cash to the company or to the owner."

The following diagrams illustrate the testimony showing why depreciation produces cash to the owner (PX 1):

DEPRECIATION AS CASH GENERATING ITEM

Sales		$1,000
	Labor Cost	200
	Raw Materials	300
	Depreciation	200
	Interest	100
Income before taxes		$ 200
	Taxes at 50%	100
Net Income		$ 100

Cash Flow Analysis

Cash In	Sales		$1,000
Cash Out	Labor Cost		200
	Raw Materials		300
	Interest		100
	Taxes		100
Net Cash Throw-off			$ 300
Net Income	$100		
Depreciation	200		$ 300

(PX 2):

"CASH FLOW ANALYSIS

"In evaluation of capital investment projects and/or acquisition analysis, cash flow analysis plays an important role, because annual net income from operations alone does not indicate how much net free cash is produced. This results from certain expenses, such as depreciation and deferred taxes, which do not require the use of cash on one hand offset by cash requirements for capital expenditures and long-term debt retirements. To illustrate:

"To net income from operations of:		10
1) Add non-cash expenses		
Depreciation, amoritization	3	
Deferred incomes taxes	2	5
Cash Produced from Operations		15
2) Subtract cash used but not expensed		
Capital expenditures	2	
Long-term debt retirement	1	3
Net Free Cash Throw-Off available for dividends		12 "

Having made these two preliminary points clear, Mr. Bodenstein then applied and illustrated the applied discounted cash flow method to the operations of UOP for the year 1977 (TR 201-207, PX 4):

" UOP

Cash Flow - 1977

Sources		In Millions
Income before extraordinary items		$ 24.3
Depreciation		15.0
Deferred income taxes		2.3
Cash flow from operations		$ 41.6
Uses		
Additions for plant and equipment		16.3
Long-term debt payment (net)		4.5
Cash requirements		$ 20.8
Net free cash from operations		$ 20.8
	7.5%[1]	8.5%[2]
Present value of net free cash	$277.3	$244.6
Excess liquidity	37.0	37.0
Extraordinary items	7.0	7.0
	$321.3	$288.6
Per share basis	$28.09	$ 25.21

[1]High side of discount range found in sample of 1977/1978 acquisitions

[2]Average Moody's Industrial Bond yeidl average: February, 1978"

Two alternate discount rates were used. The 8.5% rate is (TR 207):

> "The rate that bondholders were accepting for high grade industrial bonds at the time. This is a conservative approach because a bondholder at the time has no increase in principal. ***"

The 7.5% discount rate based on an analysis of comparable acquisitions of $100.00 or more in late 1977 and the spring of 1978 (TR 208):

> "We apply this technique to those acquisitions to find out what those buyers -- what rate they were assuming in discounting those companies free cash flows and what we did on a very conservative basis was to use the high end of that range which was 7 and 1/2 percent."

Mr. Bodenstein then analyzed the excess liquidity and determined that there was excess liquidity in the amount of $37 million (TR 209, et seq.). Mr. Bodenstein defined excess liquidity (TR 211) as "the working capital that is not required to generate the earnings of the business from its operations". He determined that UOP had excess liquidity by two disparate methods. First, from an examination of the UOP balance sheet (TR 211):

> "Obviously from the balance sheet, we could see a flow of how much cash is invested into short term marketable securities, and on a consistent basis year after year. Obviously, there is an area where you could assume that it is not working in the operation of the business."

In additon, he did a comparison between UOP and comparable acquisition companies (TR 212).

As to excess liquidity, the "unused cash" or cash that is not being invested in income producing facilities of the company, Mr. Bodenstein did not pick a number out of the hat and simply call it excess liquidity. It was demonstrated that UOP was carrying a large amount of cash, had unused bank credits and had very little short term debt (TR 209). He showed that there was between $50 million to $65 million of excess liquidity in the company -- that is, money that could be taken out without affecting the income producing capabilities of UOP (TR 260). All Mr. Purcell could say was that he could reach "... no general conclusion ..." on the question as to whether UOP had excess liquidity (TR 1089). This excess cash could be kept and used for further expansion (TR 1462) and that is precisely what in fact was done: Mr. Crawford proudly confirmed that UOP had excess liquidity and that he kept it and used it for a UOP capital expansion without borrowing. Besides meeting all of his needs for cash, he had squirrelled away cash for the projected 1978-79 capital expansion out of this cash (TR 1601):

> "Q. So that what you had to do was to squirrel away enough to provide for your future expansion, at the same time servicing all the current needs of the business, trade, inventory, reserves for customers' money and all that; isn't that correct?
>
> "A. Yes.
>
> "Q. But the situation was such that by prudent management you were able to finance future expansion in '78 or '79 through accumulations of current assets; isn't that right?
>
> "A. No. Through accumulation of cash.
>
> "Q. Cash; okay."

Mr. Bodenstein, as has been indicated, was most conservative. He did not "swell" the ultimate value figure by including all of the excess cash. Rather, after determining that the excess cash was between $50 million and $60 million, he only included $37 million as the conservative amount of additional dollars that should have been shared by Signal with the minority shareholders.

UOP's vast timberlands amounting to about 290,000 acres were carried at their original historical costs ($11,157,000.00) on UOP's balance sheet (or about $38.35 an acre (TR 264, 1179; EX U-7-29). The only justification for not valuing these assets at their actual value rather than their cost value was because Signal did not intend to sell the assets (TR 1459). These timberlands were not creating any income and should have been appraised so that the minority stockholders would receive their share of these assets that were not producing income (TR 266-268). No appraisal had been made of the actual value of these lands (TR 269). Mr. Bodenstein conservatively valued these vast timberlands. $100.00 to $200.00 an acre was in itself a conservative range of value to place on these timberlands based on his experience (TR 284-285). However, again to err on the side of caution, he included the timberlands at only $70.00 per acre for valuation purposes. Mr. Bodenstein concluded that a conservative but realistic range for the actual value of UOP's timberland was between $30 million and $50 million. (Note)

Note: The defendants had the duty of fairness to the minority shareholders at the time of the merger and this included obtaining appraisals where necessary to obtain current rather than historic values. At trial, the defendants had the burden of proof to show the $21.00 price was fair since the defendants introduced no evidence on the real value of the timberlands and, thus, the conservative value of $70.00 should be accepted. This Court could, as part of the appropriate remedy, order that there be an appraisal made of the value of UOP's timberlands.

Mr. Bodenstein combined the conservative determination of the excess liquidity with the conservative determination of the value of the timberlands and then to be almost triply cautious, further cut the combined figure in half (TR 286):

> "Q. So that both as to the excess liquidity and the timberland calculation you took a conservative figure, combined them and then took the conservative figure; is that correct?
>
> "A. That's correct.
>
> "Q. Now, why did you each time in the three steps take the most conservative approach?
>
> "A. Well, one, hopefully, that's the way we approach problems; and, two, just to be sure that we are not overstating the facts.
>
> "Q. And so that the combination of the three conservative assumptions results in only a figure of $50,000,000?
>
> "A. Yes."

The discounted cash flow analysis for 1977 showed that the value of the minority shares was between $25.21 and $28.09.

Exhibit 5 is based on the 1978 budget of UOP (TR 238). Of course, by the time of the merger, May 26, 1978, half of the 1978 budget had taken place (TR 238). Mr. Bodenstein found that UOP's management had always done an excellent job at making up a budget (TR 239) -- they were within plus or minus 10% of their estimate (TR 240). At the annual meeting, Mr. Crawford reported that UOP was on budget (TR 242). The steps of the analysis are essentially the same as those used for 1977 (and previously discussed) except that, instead of using the 7.5% or 8.5% discount factor which had been used in the "closed" year of 1977 discounted cash flow analysis, a 10% discount factor was used to reflect the risk of the possibility that something adverse might happen to UOP in the balance of 1978.

The discounted cash flow analysis, when applied to UOP's 1978 budget figures, established that the value of the UOP minority shares was $27.16.

F. The Discounted Cash Flow Analysis of UOP's Five-Year Business Plans For 1978-1982 Established That the Value of the Minority Shares Was $30.50

Mr. Bodenstein, following his deposition and as a result of pointed questions by the attorney for Signal, was requested to make a discounted cash flow analysis of "UOP's Cash Flow Analysis 1978 Five-Year Business Plan (Basic) in Millions)" (EX U-400), submitted by Mr. Crawford to Mr. Arledge on April 28, 1978 on a Signal Companies' form (TR

456-462). This plan includes an income statement, a balance sheet and an application and uses statement. There are three approaches: "basic", "optimistic" and "pessimistic". Because of limited information in the "scenarios" of optimistic and pessimistic approaches, Mr. Bodenstein only analyzed the "basic" or Mr. Crawford's expected plan (TR 465).

PX 7 is the discounted cash flow analysis based on UOP's five-year projection:

"U O P

Cah Flow Analysis

1978 Five-Year Business Plan (Basic)
(In Millions)

Year	Dividends	Increase In Cash	Free Cash Throw-Off
1978	$ 9.1	—	$ 9.1
1979	9.1	—	9.1
1980	11.3	$ 6.5	17.8
1981	13.7	9.1	22.8
1982	16.7	28.6	45.3

1983 Residual Value: 1982 Free Cash Throw-Off of $45.3 maintained into future (no growth) and discounted back at 10% rate $453.0

Year	Free Cash Throw-Off	Discounted at 12%
1978	$ 9.1	$ 8.1
1979	9.1	7.3
1980	17.8	12.7
1981	22.8	14.5
1982	45.3	25.7
1983	453.0*	229.7

TOTAL PRESENT VALUE --- $298.0 or $25.94 per share

*Residual Value in 1983

NOTE: Alternate valuation approach to 1983 residual value is to capitalize 1982 earnings of $55.7 at 10 times, or $557.0. Substituting this figure in 1983 results in a total present value of $350.3 or $30.59 per share.

Mr. Bodenstein testified (TR 475):

> "Now what I did here was just revert back to my analysis I did for '77 and '78, assume that as of 1982 -- I am assuming there is no further growth in this company but that the cash throw-off stays at 45.3 (million dollars) forever. Again, a very, very conservative approach. And saying that in the year 1982, as best as we -- and I feel it is a very conservative value -- that at a conservative value the residual value of UOP based on this management's expected performance which I feel is reasonable would be worth 453 million dollars."

Mr. Bodenstein then discounted that figure by a 12% factor (TR 478). Mr. Bodenstein testified that the five-year future projections were important becase (TR 483):

> "When a buyer goes into a company, it doesn't sit and look at the history. When a buyer sits with a potential acquiror, he sits down with him and says 'what are your plans?' You know the first thing we do when we go in if we represent a buyer, when we have the opportunity to work with the seller, is to ask 'what are your plans? let's see it.' And we spend days and days sitting with management, reviewing this to make sure that we are satisfied with his numbers and if we are we look at that."

The application of the discounted cash flow method to UOP's five-year projections shows that the value of the minority shares of UOP had a value of $30.59 per share.

* * *

Though the defendants have the burden of proof, the plaintiff established at trial by a variety of different analyses that the value of the minority shares of UOP was worth not less than $26.00 per share.

V. THE DEFENDANTS HAVE FAILED TO CARRY THEIR BURDEN OF PROVING THAT THE UOP MINORITY SHARES WERE FAIRLY VALUED AT $21.00

A. The Defendants' Recently Recruited Expert Relied on His Firm's Prestige Rather Than Financial Analysis In Trying to Justify the $21.00 Paid in 1978

In spite of the fact that the defendants had the burden of proof to prove the fairness of the $21.00 merger price since they stood on both sides of the transaction, Schreiber v. Bryan, supra, the defendants did not make any serious effort to carry that burden. First, as has been shown, the defendants deliberately chose not to call any representative from Lehman Brothers, the expert whose fairness opinion had been the defendants' principal justification at the time of the merger (in spite of the fact that Lehman Brothers was itself a named and appearing defendant in the lawsuit). Instead, William Purcell of Dillon, Read was retained, in March or April, 1980. At the outset, several things should be noted. First, though the case was tried to the Court, the defendants obviously seek to have acceptance of Mr. Purcell's opinions by recitations based on the prestige of and dollar volume of Dillon, Read (TR 1050-51). Denison v. Fibreboard, supra.) Second, it should be noted that Mr. Purcell was not asked to give an opinion on what the fair price of the minority shares of UOP in 1978 was: rather, he was asked to come in to defend the $21.00 price that was actually paid (TR 1054). (In this connection, Mr. Purcell did not even come up with a range -- he simply said flatly that $21.00 was fair.) Third, Mr. Purcell did not defend the Lehman Brothers opinion nor Mr. Glanville's methodology in the report: on the contrary, Mr. Purcell disdainfully said that neither he nor Dillon, Read would ever approach the problem as Mr. Glanville had done (Purcell 104-105). Thus, Mr. Purcell, the defendants' only expert, agrees that the Glanville opinion on which the directors of UOP recited they relied was not a valid basis for finding $21.00 fair. Finally, it should be noted that the Purcell elaborate but superficial report was not available to the UOP Board as justification for the merger in 1978: rather, it was prepared for trial in 1980 as an after the fact justification.

At the time that Mr. Purcell was examined on his deposition, he knew that Mr. Bodenstein had employed the discounted cash flow method as one of the techniques to measure and determine what the fair value of the minority shares of UOP was. (Mr. Purcell's deposition was taken on May 8, 1980: the deposition of Mr. Bodenstein had been taken in Chicago on April 21, 1980.) Also, at trial Mr. Bodenstein, being a witness for the plaintiff, had testified before Mr. Purcell was called. Daily copy was available. Thus, when Mr. Purcell came to the stand, the record showed that Mr. Bodenstein had made an analysis using the discounted cash flow method based on 1977, 1978 and UOP's five-year projection to measure and determine the fair value of the minority stock. Mr. Purcell did not utilize the discounted cash flow method (TR 1149). The plaintiff believes that the Court can draw adverse inferences from Mr. Purcell's failure to advise this Court what his calculation by the discounted cash flow method would have shown -- that is, that if he had used the discounted cash flow method. he would have found that the outcome would have been adverse to his ultimate opinion that $21.00 was fair. Mr. Purcell gave as the reasons why he did not use the discounted cash flow method was because the method is only appropriate where one is valuing the company from the point of view of a 100% owner (TR 1146). Mr. Purcell said that he agreed that the discounted cash flow method was a good way of determining the value of 100% of the company since the 100% owner could control all of the variables (TR 1154). Of course, as Mr. Bodenstein explained, since this cash-out merger was making Signal the 100% owner of UOP, the discounted cash flow method was uniquely appropriate to measure the value of what Signal was getting and conversely what the minority was being made to give up.

B. The Defendants' Expert Simply Gave His Personal Opinion Rather Than a Judgment Based on Financial Analysis on the 1978 $21.00 Price

Mr. Purcell submitted a superficially elaborate thirty-eight page report crammed full of figures with a number of official looking exhibits (DX 40-C). Actually, a review of this document shows there is a great deal of chaff but very little wheat (i.e., real financial analysis of the value of the minority shares of UOP in 1978). Actually, the report first purports to look at the market value of the UOP shares. It then formally determines that at $14.50, the market is fairly valuing UOP (TR 1077). ("The mountain labored and brought forth a mouse.")

Mr. Purcell then "studies" the investment value of the UOP shares. Again, after an elaborate presentation of a veritable panoply of financial figures, Mr. Purcell concludes that the investment value of the UOP shares is about $15.30 (TR 1125).

The next step was a consideration of the net asset values. Here, Mr. Purcell says that he paid little attention to it because there was no attempt or thought of liquidating UOP either by UOP itself or by its new 100% owner, Signal (TR 1127-1131). Mr. Purcell avoided any consideration as to whether there were undervalued assets by simply saying that this was of no significance because there was not going to be any liquidation (TR 1132). Of course, the significance, as was pointed out by Mr. Bodenstein, is the fact that, in this situation, the new 100% owner, Signal, acquired not only the assets that were producing the stream of income but also became 100% owner of the undervalued assets, such as the timberlands as well as the excess liquidity. These were assets which, at its sole option, the new 100% owner could extract without affect on the income stream for its own purposes without having shared it with the minority shareholders.

Next, Mr. Purcell testified that what was referred to as the "structure of the transaction" showed that the price of $21.00 was fair. Mr. Purcell testified as to what he meant by the phrase (TR 1082-1083):

> "It was our opinion that UOP's shareholders by their actions seemed to express a very strong consensus that $21 per share was an attractive price at which to sell their common shares. As we point out on Page 5 of our report, in connection with the May 26, 1978 annual meeting of stockholders, 92 percent -- actually, 92.1 percent -- of the shares represented at the meeting, excluding those owned by Signal, voted in favor of the proposed merger with Signal at the cash price of $21 per share.
>
> "Secondly, during April and May of 1975, in response to Signal's then current tender offer, the shareholders responded by selling approximately 78 percent of all UOP common shares then outstanding at the $21 price, despite the fact that Signal had indicated that they would take only a maximum of approximately 43 percent of the total shares then outstanding. As a result, Signal purchased on a pro rata basis only about 55 percent of the shares and returned the remaining shares to the UOP shareholders.
>
> "So those two factors had some meaning for us."

Of course, Mr. Purcell had to agree that the significance of a majority to the minority procedure was dependent on full disclosure (TR 1254). Mr. Purcell was, of course, a prisoner in this situation: he had already committed to give the defendants an opinion that all the material facts had been disclosed. As has been shown elsewhere, the defendants were guilty of misrepresentations and omissions. Furthermore, Mr. Purcell seems to believe that the active efforts not only of Signal but of UOP's management to persuade the minority stockholders to vote in favor of Signal's cash-out merger is in itself an indication that the merger price is fair (TR 1258-1260). In closing, Mr. Purcell did admit that the "psychological" aspect arising from the 1975 transaction had nothing to do with the value in 1978 of the minority shares (TR 1268).

Mr. Purcell, in his report and in his testimony, has simply listed a host of financial facts under the headings of market value, investment value, asset value and structure of the transaction. At trial, having repeated almost verbatim what is in his report and without any analysis at all of the value of the minority shares, he simply quoted his own report, saying (TR 1133):

> "Q. Based on your consideration of the market value of UOP shares, the structure of the transaction, the investment value including all of the elements you considered in determining investment value and the net asset value, what did you conclude with respect to the adequacy or fairness of the $21 per share merger terms?
>
> "Q. Well, as we state on Page 17:
>
> "'In summary, on the basis of all the information set forth herein in considering factors we deemed relevant, it is our opinion that the offer of $21 in cash per share was fair and equitable from a financial point of view to the holders of common stock of UOP other than Signal.'"

C. In Addition to the Lack of Analysis, Mr. Purcell's Credibility is Suspect Because It Came Out at Trial That He Was In Error on Four Important Points

1. Dillon, Read's Calculation of the Amount and Percentage of Premium Was Based on the Misconception of the Appropriate Measuring Date

Mr. Purcell's whole fairness conclusion rests on his determination that the premium paid was appropriate when measured by the premium paid in comparative transactions. The difference between the market price and the merger price is the premium price (TR 1134). Therefore, premium was critical to Mr. Purcell's conclusion. Mr. Purcell had a Mr. Daum and Mr. Read prepare Exhibit 6 and 7 of the Dillon, Read Report (DX 40; TR 1346). What Mr. Daum and Mr. Read did was to select comparable companies involved in $100 million mergers and determine the percentage of premium. Mr. Bodenstein made an analysis of premiums paid in the comparable period. Mr. Bodenstein's figure showed that the average or median premium was in the range of 70 to 80%. Mr. Daum and Mr. Read concluded that the average or median range was 35% (DX 40, Ex. 6; EX 7). The difference between the two reports is not only significant but is critical to Mr. Purcell's entire conclusion since his conclusion is totally dependent on the amount of the premium.

Mr. Daum and Mr. Read selected as the date for the determination of the market price the day before the announcement of the merger (TR 1347). They selected this date whether the record showed that there were leaks, rumors or other previous offers or news of offers that in fact drove the price and volume of the stock up beyond normal records of price and volume for the stock (TR 1349-1350). Thus, "noise" by way of leaks, rumors and other material was not filtered out in the Dillon, Read premium determination (TR 1352) but simply blindly accepted the price on the day before the official announcement as the means of measuring premium. This blind selection of the date of the official announcement clearly minimizes the amount of premium (TR 1352).

Obviously, the correct way to measure premium is to measure the difference between the merger price and the price of the security before it goes up in anticipation by way of leaks, rumors or other information towards the merger price (TR 1352). Again, Mr. Purcell had ample warning of the analysis made by Mr. Bodenstein of each merger transaction selected by Mr. Daum (PX 6). Mr. Purcell simply stuck to the concept that premium was simply the difference between the merger price and the price on the day before the official announcement of the merger regardless of what the published record showed had been the gyrations in volume and price before the official announcement (TR 1356). In short, the analysis of premium by Mr. Bodenstein was another exercise in comparative analysis which confirmed the fact that the value of the minority stock of UOP was worth not less than $26.00. Conversely, the mechanical way that Mr. Daum had analyzed premium for Mr. Purcell vitiates the entire basis for the one approach that Mr. Purcell gave to the Court in seeking to justify in 1980 the 1978 merger price of $21.00 per share.

2. Mr. Purcell Did Not Allocate Any of the Undervalued Assets of UOP to the Minority Shareholders Simply Because Mr. Crawford Said That There Were No Undervalued Assets

Mr. Purcell's report states (TR 1205-126):

"'The concept of book value was also useful in terms of studying a company's asset structure. Some companies have assets on their books at a very low cost basis or almost completely depreciated which have a present value far above their stated values (for example, mineral properties or securities carried at cost vs. market value). In such case the investment value of the company could be affected by a more thorough analysis of such assets.'

"I take it from what you say that the analysis of net assets is of paramount importance where there is a liquidation, but it also may be important if there are undervalued assets even when you're approaching the situation from the ongoing point of view. Is that correct?

"A. If such assets were readily saleable, or were of the nature that in our opinion would affect the investment value of the company."

In spite of the foregoing and in spite of the fact that Mr. Bodenstein had pointed out that UOP's vast timberlands were being carried at about $40.00 an acre, Mr. Purcell did not suggest that there be an appraisal obtained for the timberlands.

Mr. Purcell said that he determined from his due diligence visit that UOP had no intention of liquidating UOP of its assets (TR 1131). Of course, the question was not whether Signal was going to liquidate assets, such as the timberlands, but the fact that Signal was in fact acquiring 100% of UOP and that would then give it the right to liquidate or sell or retain for further appreciation UOP's undervalued assets. Second, Mr. Purcell depended on Mr. Crawford (rather than Mr. Shuman, Chief Financial Officer of UOP, TR 1198), who told him virtually on the eve of trial that there were no undervalued assets on the balance sheet of UOP (TR 1173; 1181; 1207). Mr. Purcell agreed that if there were non-income producing properties, it would be important to have an appraisal made (TR 1174). Mr. Purcell, though he calculated that UOP's 290,000 acres of timber were being carried at $38.35 per acre, still claimed that these were not "significant assets"(TR 1196). The plain fact of the matter is that UOP's timberlands were grossly undervalued (though correctly carried for accounting or bookkeeping purposes at their historical cost). If UOP had been sold as a whole to a third party, clearly Signal and the minority shareholders should have shared pro rata in the true value of these non-income producing undervalued assets. In the same way, since Signal was itself electing to take over the shares of the minority and would end up as a 100% owner of UOP, including the understated assets, clearly a present value should have been put upon such assets. Mr. Purcell's total refusal to consider the true value of UOP's timberlands is another example of his incredibility.

In this situation, the burden of proof is important: it was up to the defendants to prove the appropriate value for the undervalued assets, such as timber. In the absence of such proof, Mr. Bodenstein's conservative valuation on the timberlands should be accepted.

3. Mr. Purcell's Original Report Contained Two Major Errors in the Section Suggesting That UOP's Minority Shareholders Sell Their UOP Stock and Buy Signal Stock

As has been shown in Tanzer v. International, supra, Vice Chancellor Hartnett strongly suggested that in a cash-out merger, or in a merger that eliminates the minority, they be given an equity interest in the surviving corporation. Mr. Walkup said that no consideration was given to a stock-for-stock deal though he as a UOP director recognized that a stock-for-stock deal would be advantageous to the minority stockholders. The advantage to the minority includes the fact that they would have shared in the 13% rise that the market in general enjoyed between February and May and the spectacular rise from $28.00 to $39.00 that Signal stock underwent during that period. Mr. Walkup said that it simply was not in Signal's best interest for a stock-for-stock deal (TR 1684-1685).

In his original report, Mr. Purcell "volunteered" that the UOP stockholders take their UOP stock and sell it and then invest the funds in Signal stock (Purcell 220). Mr. Purcell's original report (as he acknowledged) contained two serious errors (TR 1370). The first error was in using $21.00 as the figure UOP shareholders could realize from the sale of their UOP stock (TR 1372). The second error was on the other side of the evaluation: the original report postulates that the minority shareholders could obtain Signal stock at $30.00 though the fact is that Signal stock had risen to $39.00 by the time of the merger (Purcell 215).

Mr. Purcell never did answer the question as to why it would not have been advantageous for the stockholders of UOP to have received a stock-for-stock deal (TR 1374-1475).

4. Mr. Purcell's Attempted Assertion That the Material Furnished to the Minority Shareholders Contains No Material Misrepresentations or Omissions Has Been Totally Disproved by the Evidence

Mr. Purcell's attempt to assert that there was nothing material omitted or misrepresented has fallen flat. The defendants, concerned with the omissions and misrepresentations that came out during discovery, not only called Mr. Purcell as a relief pitcher on damages but have got him to say in his report that there was nothing material misrepresented or omitted in the proxy statement (TR 1376). Over the plaintiff's objection (TR 1058), the witness, Mr. Purcell, was permitted to testify that, in his opinion as an investment banker, he saw nothing that had been omitted or misrepresented in the proxy statement (TR 1147). He even attempted to put himself not in the position of an investment banker but in the position of a stockholder to say that this was true, but the Court restrained him from stepping into the shoes of the stockholders and only allowed him to testify from the point of view of an investment banker (TR 1143).

There are several comments on Mr. Purcell's attempts to be helpful to the defendants in this situation. First, Mr. Purcell, with the Court's permission, was in fact testifying on the ultimate question. The question at issue before the Court is whether in fact there were material misrepresentations and omissions.

The evidence deals with these misrepresentations and omissions and their materiality. The ancient policy against testifying on the ultimate question, though modified by the adoption of Rule 705, was designed to prevent "oath helpers" from solemnly assuring the Court on the ultimate question which, in the end, the Court has to decide. Mr. Purcell was just such a witness. However, Mr. Purcell forfeited his credibility by trying, in the face of the misrepresentations and omissions already in the record, to state that everything material to the consideration of the cash-out merger by the minority stockholders was stated in the proxy.

* * *

Mr. Purcell, the recently recruited replacement damage expert for the defendants, did only a superficial job in defending the $21.00 price of the 1978 merger. His elaborate report is devoid of different methods of comparative analysis. In the end, the Court was simply asked to accept on faith and because of the prestige of his firm that $21.00 was in fact a fair price. In point of fact, his whole opinion depends on the adequacy of the premium. The falacy in Mr. Daum's and Mr. Read's method of calculating percentage of premium in comparable situations stands unrebutted. Finally, Mr. Purcell's credibility as a witness as a whole has been cut out from under him by his own attempt to assert in the face of the record that there were no material misrepresentations or omissions to the minority stockholders of UOP.

CONCLUSION

In order to determine the appropriate remedy in this case, the Court necessarily is going to have to decide the value of the minority shares of UOP in 1978. On this issue, the defendants, since they stood on both sides of the transaction, have had the burden of proof. However, the plaintiff's position does not depend on showing that the defendants have failed to sustain their burden of proof nor indeed on the adverse inferences that the Court can and should draw against the defendants. Rather, the case rests on the facts as to value as determined from the analysis presented and fully explained by Kenneth Bodenstein, CFA of Duff & Phelps. His testimony is uncontradicted that the value of the minority shares as of the time of the 1978 merger was not less than $26.00 per share.

The best that the defendants could do was to call William Purcell of Dillon, Read. However, Mr. Purcell made no financial analyses to defend the $21.00 price. He simply assembled and recited at length the financial facts and then flatly told the Court that he concluded that the price was fair. In doing so, his subordinates miscalculated the percentage of premium in comparable cases, he overlooked or disregarded any of the undervalued assets of UOP and disregarded the excess cash or liquidity that UOP enjoyed. He made flat factual errors in attempting to justify the absence of a stock-for-stock deal. His crowning error was to try to assert to the Court on the ultimate question of liability that there were no material misrepresentations and omissions.

The Court should determine that the stock of the minority was worth not less than $26.00 per share as of the time of the 1978 merger. The Court should then determine the remedy that is most appropriate to make the plaintiff class whole, including rescission, monetary damages or the requirement that Signal make the minority class whole by issuing Signal treasury or new Signal stock representing the difference between the value of the shares and Signal's merger price of $21.00.

PRICKETT, JONES, ELLIOTT &
KRISTOL

By ______________________
William Prickett
1310 King Street
Wilmington, Delaware 19899
Attorney for Plaintiff

August 18, 1980

E. The Plaintiff's Discounted Cash Flow Analysis of the 1978 Budget of UOP Resulted in a Figure of Not Less Than $27.16 as Value of the Minority Shares

PX 5:

"UOP

Cash Flow - 1978

Sources		In Millions
Income before extraordinary items		$ 30.0
Depreciation		16.5
Deferred income taxes		3.0
Cash flow from operations		$ 49.5
Uses		
Additions for plant and equipment		17.5
Long-term debt payment (net)		7.1
Cash requirements		$ 24.6
Net free cash from operations		$ 24.9
Present value of net free cash streams discounted at 10%		$250.0
Excess liquidity and timberland cushion		50.0
		$300.0
Per share basis		$ 26.20
Non-operating cash flow:		
Tax loss carryforward	$ 6.0	
Other	5.0	0.96 per share
	$11.0	
		$ 27.16