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IN THE SUPREME COURT OF THE STATE OF DELAWARE

WILLIAM B. WEINBERGER, Appellant, 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, Appellees.	)	No. 58, 1981

SUPREME COURT OF THE STATE OF DELAWARE
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OPENING BRIEF OF APPELLANT
IN SUPPORT OF HIS APPEAL

On Appeal From the Court of Chancery
In and For New Castle County
Civil Action No. 5642

Hand Serve
4-16-81
Mr. Sparks
Mr. Bayson
Mr. Balotti

April 16, 1981

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EXPLANATORY NOTE ON REFERENCES, FORM AND THE ORDER ON PAGE LENGTH

The plaintiff will refer to pages of his Appendix thus "(A899)" and at times the document in question. Thus, for example, page references to the opinion of the Court below will appear thus: "(A1881, Op.)".

Pages of the trial transcript will be referred to as "(TR 889)" or by the name of the witness thus: "(Crawford 889)", or where the testimony is included in the appendix as "(A889 Walkup)".

Pages of deposition transcripts admitted in evidence will be referred to by the name of the deponent thus: "(Crawford Dep. 9)".

Exhibits will be referred to by the trial exhibit number. Thus, the plaintiff's exhibits which emanated from Signal are referred to solely by number as, for example, "(PX 5)"; exhibits emanating from Lehman Brothers are referred to as, for example, "(PX LB 5)"; and exhibits emanating from UOP are referred to as, for example, "(PX U-100-9)". In the course of the trial, the plaintiff introduced eleven exhibits which will be referred to as "(PX 1, Trial)", "(PX 2, Trial)". At times, for clarity, an exhibit will be briefly described as, for example: ("PX 298 - Minutes of the Executive Committee of the Board of Signal 2/28/78)".

The defendants collectively introduced forty-one exhibits at trial which will be referred to as, for example, "(DX 10)".

In quotations, matters in parentheses and underlining are added throughout unless otherwise noted.

On March 10, 1981, this Court approved counsel's waiver of Rule 14(d) governing page limitations of briefs.

PLAINTIFF'S STATEMENT OF THE NATURE OF THE PROCEEDINGS AND THE JUDGMENT AND ORDERS APPEALED FROM

A. Nature of These Proceedings

This derivative and class action was commenced on July 6, 1978, shortly after the merger complained of on May 26, 1978. Contemporaneously with the filing of the suit, the plaintiff began discovery. The plaintiff filed a voluntary dismissal, without prejudice, as to the individual defendants.

After briefing and argument, the Court below entered orders on April 26, 1979, dismissing the derivative counts and, while certifying the plaintiff as the class representative, limited the class "to those former stockholders of UOP who voted against the merger and/or who had not turned in their certificates in exchange for $21 per share payment".

The plaintiff asked for leave to take an interlocutory appeal from the lower Court's orders of April 26, 1979, dismissing the derivative count and limiting the class as set out above. The plaintiff's request for an interlocutory appeal from the foregoing orders was refused by this Court by order dated August 28, 1979. The plaintiff has renewed his appeal from the lower Court's orders of April 26, 1979.

After the original complaint was held to be legally insufficient by the Court, an amended complaint was served and filed and answered by all of the defendants.

After the completion of discovery, on May 21, 1980, and prior to the commencement of testimony, the plaintiff served and filed a motion to enlarge the class to include all of those stockholders of UOP as of the time of the merger. The Court below says in its opinion (A1882-3 Op.):

> "Subsequent to the completion of the trial, plaintiff also filed a motion whereby he seeks to enlarge the class so as to include all former shareholders of UOP as of the time of the merger other than Signal."

The Court below concluded in its opinion (A1960 Op.):

> "Judgment will be entered in favor of the defendants UOP and Signal as well as in favor of the defendant Lehman Brothers. <u>This decision makes it unnecessary to consider plaintiff's motion to enlarge the class</u>. An appropriate form of order may be submitted."

The plaintiff appeals from the Court's refusal to act on his motion to enlarge the class.

After trial and post-trial briefing, the Court handed down an opinion on February 9, 1981. A final judgment was entered on the opinion on February 19, 1981. The plaintiff appeals from the final order of the Court below.

B. <u>Summary of the Plaintiff's Argument</u>

(1) The Court below erred in dismissing the derivative count because UOP, in the merger, survived and remained an entity, and the Court below erred in originally limiting the plaintiff class to those UOP stockholders who voted against the merger and/or who did not turn their certificates in and the Court below erred in refusing to consider and grant

plaintiff's motion for the enlargement of the class to include all of the minority stockholders of UOP as of the date of the merger.

(2) The Court below erred in its interpretation of the law and in applying the law to the facts in connection with the fiduciary responsibilities of the defendants, vis-a-vis the minority stockholders in a cashout merger.

(3) The Court below erred in applying an appraisal standard in determining whether the cashout merger of the minority stockholders was intrinsically fair at a $21 price especially in view of the decision of this Court in Lynch.

(4) Since the record shows that the defendants failed to carry out their fiduciary obligations to the minority, the Court below erred in holding that the structuring of the vote on the merger so that it would essentially be ratified by a majority of the minority was significant.

STATEMENT OF FACTS

A. Signal's Acquisition of 50.5% of the Stock of UOP in 1975

In 1975, The Signal Companies, Inc. ("Signal") negotiated an arm's length tender and purchase for 50.5% of the common stock of UOP, Inc. ("UOP") (Logan Dep. 37, et seq.). Mr. James Glanville, a partner of Lehman Brothers Kuhn Loeb ("Lehman") and a director of UOP, assisted by Roger Altman, was retained by UOP for a fee of $450,000.00 to help Mr. Logan, President of UOP, in these negotiations. Mr. Rohatyn and Mr. Pizzitola of Lazard Freres advised Signal in the negotiations (Logan Dep. 39). In the final round of negotiations, UOP started by demanding $25; Signal countered, offering $19. In face-to-face bargaining, Signal and UOP finally settled on a compromise price of $21 (Logan Dep. 42-47, 53). (Note) Since UOP needed capital, the transaction was structured so that $30 million of treasury stock was purchased directly from UOP at $21 with the balance, in order to come up with 50.5%, coming from a successful tender at $21 to the public stockholders (Logan Dep. 49, 54). Mr. Glanville abstained from voting when the tender and purchase

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Note: The Court below characterizes this situation as "friendly negotiations" (A1884 Op.). However, as the lower Court then stated, this transaction was the result of "arm's length bargaining" (A1884 Op.) between knowledgeable equals, each advised by their own investment bankers. The original difference in the asking price ($25) and the price offered ($19) was six dollars ($6) or a total of $25,800,000.00 (i.e., $6 x 4.3 million shares).

came before the UOP Board: Lehman had a financial interest in the outcome arising out of the $450,000.00 fee it was getting from UOP (U-313).

Though Signal could have acquired 77% of the UOP stock, Signal deliberately limited its combined direct purchase and tender to 50.5% of the stock of UOP (A1885 Op.). 50.5% was designed to and did give Signal control of UOP: Signal's public filings thereafter stated that Signal had complete control of UOP (PX U-326). After obtaining control of UOP, Signal caused five members of its management to be elected to the UOP Board (Messrs. Shumway, Walkup, Arledge, Wetzel and Chitiea; PX U-7). UOP's Chief Executive Officer, Mr. Logan, was replaced by a long time Signal executive, Mr. Crawford; Mr. Crawford was also elected to the Signal Board (Crawford Dep. 14, 36; Logan Dep. 64). Mr. Crawford's appointment by Signal as Chief Executive Officer and President of UOP was a career and financial promotion for Mr. Crawford (Shumway Dep. 12-13).

In 1976, after Signal had acquired control of UOP, Mr. Glanville, a managing director of Lehman and a director of UOP, had Mr. Altman and Mr. Seegal, subordinates of his at Lehman, prepare a draft entitled "<u>Memorandum to Mr. Forrest Shumway - Confidential Draft - Considerations Relating to Signal Companies' Investment in UOP - Lehman Brothers Incorporated</u> - June 1976" (PX LB-40). This Memorandum advised Signal that Lehman, after research, had concluded that it would be advantageous for Signal to acquire the common stock of UOP still owned by minority stockholders at up to $21 per share (Seegal Dep. 19, et seq.): it was apparently never transmitted to Signal (A1918 Op.). Though the memorandum was prepared at the specific direction of Mr. Glanville, he denied having any recollection of it whatsoever at the time of his deposition (Seegal Dep. 20; Glanville Dep. 28).

B. Signal's Decision to Aquire the Balance of UOP Stock at $20 to $21

UOP suffered an unanticipated operating loss of $35 million in the Come-By-Chance Refinery venture in 1975, but, in January, 1978, UOP's President, Mr. Crawford, reported that UOP's net income in 1977 "was at a record level" (Ex. U-49).

The Court below says (A1887 Op.):

> "In the two years following UOP's disastrous 1975 performance, its fortunes steadily improved so that by the end of 1977 UOP's earnings and operating record had substantially neared its performance for 1974, the year immediately preceding Signal's acquisition of its majority interest."

Actually, 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 before the 1978 merger. PX 11 illustrates UOP's financial results. (Note)

Note: Mr. William K. Purcell of Dillon, Read suggested some slightly different numbers (Tr. 1305-1311): these were noted on PX 11, Trial and circled and do not affect the overall significance of PX 11, Trial -- that is from 1975-1978 UOP's financial performance showed marked, significant and continued improvement.

(PX 11, Trial)

UOP (PX 11) 1974 to 1977	(000's)		12/31/77 Receivable 3/31/78	139,000 172,000	
	12/31/74	12/31/75	12/31/76	12/31/77	3/31/78
CASH & MRKT SECURITIES	$ 25,228	$24,779	$ 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

From 1975 through January, 1978, Signal claimed to have considered many investment and merger possibilities in order to utilize its excess cash (Shumway Dep. 18-21). Though Signal said that its only two serious merger possibilities never "came to fruition" (A1888 Op.), Signal never disclosed the identity of these two companies nor the extent of Signal's efforts to make these acquisitions on a "friendly basis" (A1888 Op.). (Note) Mr. Shumway testified that the possibility of taking over the balance of the equity in UOP

Note: Mr. William Walkup, Chairman of Signal, jocularly testified on direct examination that Signal's acquisition by a cashout merger of the stock of UOP minority shareholders "... was the only game in town at the moment" (TR 1638).

first came up in January, 1978, when he conceived of the idea (Shumway Dep. 19-23).

In January, 1978, Mr. Shumway directed Signal's Chief Financial Officer, Mr. Chitiea, and Mr. Arledge, Signal's Vice President in charge of planning, to evaluate the economics from Signal's point of view of Signal's acquiring the interest of the minority shareholders by a cashout merger (Shumway 29). Mr. Chitiea and Mr. Arledge were also UOP directors (A1888 Op.). A detailed financial analysis was made by Messrs. Chitiea and Arledge of the economic benefits that would accrue to Signal from taking over the minority UOP stock (Shumway Dep. 29; PX 74; PX 248). Mr. Chitiea and Mr. Arledge then made a presentation to Signal management that showed (based on inside UOP financial information available to Signal as majority stockholder of UOP) that the acquisition of the minority's shares would be economically advantageous to Signal at any price up to $24 per share (Arledge Dep. 16-18; PX 74; PX 248; A1888 Op.). The foregoing information was never disclosed to UOP's minority shareholders (A1888 Op.). The analysis by Messrs. Arledge and Chitiea culminated in a firm decision by Signal senior management (Note) that it would be in Signal's best interest to take over the minority stockholders' common stock. Signal management decided to present the plan for a cashout merger of UOP's minority shareholders

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Note: Signal's management consisted of Mr. Walkup, Chairman of the Board; Mr. Shumway, the President; Mr. Chitiea, Vice President for Finance; Brewster Arms, Esquire, house counsel for Signal; and Mr. Arledge, Vice President for Planning (A1888 Op.). The foregoing were all Signal directors and all were also directors of <u>UOP</u> except Mr. Arms (TR 1644-1677).

at $20-$21 to the Executive Committee of Signal on February 28, 1978 (Shumway Dep. 28). The Court below says (A1890-1 Op.):

> "As a result of these and other factors which made the acquisition of 100 per cent ownership of UOP seem advisable from Signal's standpoint, and based upon the consensus that a price of $20 to $21 per share would be fair for Signal as well as for the minority shareholders of UOP, Signal's Executive Committee authorized its management 'to negotiate' with UOP 'for a cash acquisition of the minority ownership in UOP, Inc. with the intention of presenting a proposal to the Board of Directors of [Signal] on March 6, 1978.'"

The "consensus" referred to is a consensus of the Executive Committee of Signal which had been informed by Mr. Arledge and Mr. Chitiea that any price up to $24 would be advantageous to Signal. No one (and, specifically, no investment banker) had been asked at that point to evaluate the value of the minority shares from the point of view of UOP's minority stockholders (Shumway Dep. 24). Signal's UOP directors never suggested or considered a stock-for-stock merger because it was not in Signal's interest to do so (A1323-1327 Walkup).

Mr. Shumway testified as follows on reasons for and purpose of the acquisition of UOP minority shares (Shumway Dep. 43):

> "Q. And the first reason you presented, therefore, was that you didn't have alternatives on the horizon, the near horizon, that would require the cash or, I supposed, the credit of Signal so that you had the resources available to make that acquisition; is that right?
>
> "A. Yes.

As an alternative we always have other places we could put funds, but they didn't think they were as attractive as this.

"Q. But that's not what you said here. You said here, quote:

> '... no other major cash expenditures by this Corporation are anticipated in the near future,'

indicating that you had no other cash expenditures that would preclude that; is that what you meant by that?

"A. I don't know what the secretary meant.

"Q. Tell us what you meant.

"A. <u>What I meant was that we had the financial resources to make the acquisition, and it was the most viable alternative of other potential uses of that cash, in my opinion</u>."

C. Mr. Crawford, Signal's Designated President of UOP, Immediately Agreed to Signal's Plan, Including the Price

James Crawford, the Signal executive who, as noted, had been made President and Chief Executive Officer of UOP by Signal, was requested by Mr. Shumway, the President of Signal, to come from Chicago (the corporate headquarters of UOP) to Los Angeles (the corporate headquarters of Signal) for the meeting of the Executive Committee of Signal of Tuesday, February 28, 1978 (Crawford Dep. 36). Though Mr. Crawford had been elected a director of Signal in November, 1975, he did not ordinarily attend Executive Committee meetings (Crawford Dep. 37-38). He was not told in advance why he was being summoned (Crawford Dep. 38). When he arrived at Signal headquarters, Mr. Crawford met privately with Mr. Walkup, Chairman of the Board of Signal, and Mr. Shumway, Signal's President, in Mr. Shumway's office (Shumway Dep. 40). Mr. Crawford was told that, at the Executive Committee meeting to be held later that same day, Signal would "acquire" the 49.5% of the publicly held stock of UOP at a "range" of $20 to $21 (Crawford Dep. 41-42). Mr. Crawford stated that at the initial meeting with Mr. Shumway and Mr. Walkup he said he favored Signal's cashout merger and specifically stated that the price range of $20 to $21 was "generous" to the minority stockholders (Crawford Dep. 44). He made this statement without consulting his own management, the Board of UOP or any independent investment adviser (Crawford Dep. 44). Between the time of the original private meeting between Mr. Crawford and Messrs. Shumway and Walkup and the Executive Committee meeting later that day (February 28, 1978), Mr. Crawford did not consult with anyone (Crawford Dep. 47). Mr. Crawford attended the meeting of the Executive Committee of the Board of Signal; after Mr. Shumway had delineated Signal's decision to acquire the minority's stock by a cashout merger at a price of $20 to $21, Mr. Crawford stated to the Signal Executive Committee his unequivocal approval of Signal's proposed cashout merger of UOP's minority shareholders, including a price for the stock of the minority stockholders of $20 to $21 (PX 278). Mr. Crawford admitted that he never made any attempt whatsoever to obtain or negotiate for any additional consideration beyond the $20 - $21 which Signal management had already itself decided to pay the minority shareholders (Crawford Dep. 67). Nor did Mr. Crawford even inquire whether Signal would offer a tax-free exchange of the UOP stock for Signal's own stock and thus give the minority the opportunity to continue their equity participation in the Signal-UOP venture without adverse capital gains consequences (PX 278). Specifically, Mr. Crawford testified (Crawford Dep. 46):

> "Q. My question to you was not that. My question was: Did you ever attempt to get a nickel more for those stockholders?
>
> "A. Your question was: Did I attempt to get more than 20 or 21?
>
> "Q. Yes.
>
> "A. And I answered that question negatively.
>
> "Q. So in this meeting with Signal, Signal's President and Chief Executive Officer, you indicated that you felt that the offer was generous?
>
> "A. Yes."

The price range of $20-$21 originated with Mr. Forrest Shumway, President of Signal, the majority holder of UOP stock: it was not the product of research, study or consultation, nor was it the outgrowth of negotiations. Mr. Shumway himself never had any evaluation done to determine the <u>value</u> or <u>worth</u> of the minority shares: he simply felt that the price was "fair" to the minority shareholders of UOP (Shumway Dep. 55). The Court below found (A1936 Op.):

> "Moreover, I am satisfied that the primary factor considered by those concerned was the comparison of Signal's 1978 proposal with the situation prevailing at the time of the 1974 tender offer."

The price range of $20-$21 was initially presented to the management of Signal, i.e., Messrs. Walkup, Chitiea, Arledge and Arms. Messrs. Shumway, Walkup, Chitiea and Arledge were directors of UOP (PX U-7). None of them even suggested, as UOP directors, that the minority shareholders were entitled to a higher price (Chitiea Dep. 50). None of these UOP directors attempted to negotiate on behalf of the unrepresented outside stockholders of UOP for a better price or a stock-for-stock merger though they knew from the study made by Messrs. Chitiea and Arledge that any price up to $24 would be advantageous to Signal (A1888 Op.).

Brewster Arms, Esquire, house counsel of Signal, was present at the Executive Committee meeting of February 28, 1978. He alerted Messrs. Shumway, Walkup, Wetzel, Chitiea and Arledge to their obvious conflict of interest and of their fiduciary responsibilities (PX 278, Minutes of the Meeting of the Executive Committee of Signal 2/28/78):

> "Mr. Arms pointed out the fiduciary responsibilities of those persons who are common directors of both this company and UOP (namely, Messrs. Arledge, Chitiea, Crawford, Shumway, Walkup and Wetzel) and he commented particularly upon the unique role of Mr. Crawford as director of both companies and the President and Chief Executive Officer of UOP."

D. The Press Releases and Proxy Statement Stated That There Were Negotiations in Connection With the Price of $21

Immediately after the meeting of the Executive Committee of Signal on February 28, 1978, and before the meetings of the Boards of both UOP and Signal on March 6, 1978, there were two press releases published in connection with the proposed acquisition by Signal of the minority's shares. The first was a joint release of Signal and UOP dated February 28, 1978, which reads, in pertinent part (PX 146):

> "SIGNAL NEGOTIATING
> FOR UOP COMMON STOCK
>
> "The Signal Companies, Inc. and UOP, Inc. are conducting negotiations for the acquisition for cash by Signal of the 49.5% of UOP which it does not presently own, announced Forrest N. Shumway, president and chief executive officer of Signal, and James V. Crawford, UOP president.
>
> "Price and other terms of the proposed transaction have not yet been finalized and would be subject to approval of the boards of directors of Signal and UOP, scheduled to meet early next week, the stockholders of UOP and certain regulatory agencies. The close price of UOP's common stock (NYSE) on February 28, 1978, was $14.50 per share."

This press release was issued after Mr. Crawford had met first with Mr. Shumway and Mr. Walkup at which time he stated his agreement to the merger proposal and stated that the price range was "generous". It was also after he had stated the same thing at the Executive Committee meeting of Signal. It was issued before Mr. Crawford had talked to any of his directors (Crawford Dep. 41-42, 44, 47). No negotiations had taken place.

Two days later, on March 2, 1978, a second press release was issued by Signal (PX 110):

> "SIGNAL TO RECOMMEND
> PRICE OF $20-$21 FOR
> OUTSTANDING UOP SHARES
>
> "Forrest N. Shumway, President and Chief Executive Officer of The Signal Companies, Inc., announced today that Signal management will recommend to its directors for their approval a price in the range of $20 to $21 a share in the proposed acquisition of the outstanding 49.5% minority interest in UOP, Inc. (Note)
>
> "Last Tuesday the company announced it was conducting negotiations for Signal's acquisition of this interest. If Signal's directors approve, the offer will be presented to the UOP directors for their review and approval. Both boards are scheduled to meet Monday, March 6. A further announcement will be made following the meetings."

These press releases were published, inter alia, in The Wall Street Journal (PX U-49-110), The New York Times (LB-17), and The Daily Herald (PX U-49-146). The press releases were officially filed with the SEC by UOP as an amendment to its 13d (PX U-155).

There were several informal telephone calls some time between February 28, 1978 and March 6, 1978 (A1893 Op.) between Mr. Crawford and Mr. Shumway and Mr. Walkup. But at trial (as contrasted with discovery), it came out in the

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Note: Signal's management knew before the February 28, 1978 meeting that any price up to $24 would be advantageous to Signal but decided that a price range of $20-$21 would be "fair" to UOP's minority stockholders (PX 68-1, 2, 3; PX 74). Signal made no new decision prior to the issuance of this second press release.

cross-examination of Mr. Walkup that the "negotiations" on price between Signal and UOP consisted of one solitary phone call between Mr. Walkup and Mr. Crawford (TR 1718-19):

> "Q. Okay. So that we come down to the fact that there was one phone call where there was a discussion or negotiation on price, is that correct?
>
> "A. Yes.
>
> "Q. So far as that is concerned, Mr. Crawford said that the price had to be at the upper range, isn't that right? The upper end of the range?
>
> "A. I recall his telling me it had to be 21.
>
> "Q. No. Did Crawford ever ask you on behalf of the minority shareholders for anything more than 21?
>
> "A. No.
>
> "Q. Did he ever ask you for a delay in the time to consider the proposal?
>
> "A. No.
>
> "Q. Did he ever ask for a stock-for-stock deal?
>
> "A. Not to my knowledge.
>
> "Q. Did he ever ask you for consideration of payment of the dividend in the second quarter, or that part of it that would be attributable to the period before the date of the annual meeting?
>
> "A. Not as I recall.
>
> "Q. Did Mr. Crawford ever ask for a provision for an escalation to reflect increases in the general market price -- I'm sorry -- the New York Stock Exchange general price level?
>
> "A. No.
>
> "Q. Did he ever ask you for a provision for escalation in terms of the increase of the Signal stock?
>
> "A. No.

"Q. Did it ever occur to you as a fiduciary of the minority shareholders of UOP that terms along those four general points be considered?

"A. No." (Note)

After the meeting of the Boards of UOP and Signal on March 6, 1978, Signal issued a press release saying, in effect, that the price was the result of "negotiations" (PX 24). On March 7, 1978, UOP sent a letter to its minority stockholders stating that, on February 28, 1978, "both companies had announced negotiations were being conducted ..." (PX U-49-075).

The Notice of Annual Meeting and Proxy Statement 1978 states (PX U-7, page 3):

> "The price was determined <u>after</u> discussions between James V. Crawford, a director of Signal and Chief Executive Officer of UOP, and <u>officers</u> of Signal which took place during meetings on February 28, 1978, and in the course of <u>several</u> subsequent telephone conversations."

Note: The Court below found that what actually happened was (A1893 Op.):

> "During this period, Crawford also had several telephone contacts with Signal officials. In only one of them, however, was the price to be paid for the shares discussed. In a conversation with Walkup, Crawford advised that as a result of his communications with UOP's non-Signal directors, it was his <u>feeling</u> that the price to be paid would have to be at the top of the proposed range or $21 per share if approval of UOP's outside directors was to be obtained. Again, however, he did not seek any price higher than $21 per share."

(The foregoing statement is repeated verbatim at page 9 of the Proxy Statement.) However, on page 13 of the UOP Proxy, it was again represented that there had been negotiations (EX U-7, page 13):

> "On February 28, 1978, the last day of reported trading prior to the public announcement that UOP and Signal were conducting negotiations for the acquisition for cash by Signal of the 49.5% which it does not presently own..."

The original draft of the Proxy Statement stated there were "negotiations" leading to the price (PX U-82). However, when the SEC challenged UOP's claim that there had been "negotiations" and demanded details (PX U-82), UOP chose not to press its representation that the price had been determined after "negotiations": it substituted the word "discussions" (plural) (PX U-81; A1927 Op.). There were no press releases correcting the earlier releases that stated there were negotiations between Signal and UOP as to price nor did the Proxy Statement give any explanation of the reason for change from "negotiations" to "discussions".

E. The Retention of Lehman Brothers

After the February 28, 1978 meeting, Mr. Crawford returned to Chicago, and promptly got in touch by phone with Mr. James Glanville (Glanville Dep. 42). As previously pointed out, Mr. Glanville was a managing director of Lehman Brothers, a New York investment house (Glanville 4-7). Mr. Glanville had been a member of the Board of UOP for a number of years and, for a fee of $450,000.00, had helped UOP in the negotiations with Signal resulting in the acquisition by Signal of 50.5% of the UOP stock in 1975 (Glanville 12-22). Mr. Crawford asked Mr. Glanville whether Lehman could provide a fairness opinion for the Board and minority stockholders on the Signal acquisition of the minority's shares at $20 to $21 per share (Glanville 43). (Mr. Glanville made no mention of the fact that, in 1976, he had directed the preparation of a Memorandum addressed to the President of Signal advising that it was in Signal's interest at that time to buy out the minority stockholders at up to $21 per share (PX LB-40). Mr. Glanville stated that he could not remember if Mr. Crawford asked if Lehman had a conflict of interest (Glanville Dep. 43). (Note [1]) Mr. Glanville immediately replied that Lehman could give such an opinion (Glanville Dep. 43). Mr. Crawford noted at the time that Mr. Glanville had in fact said (Crawford Dep. 119-120):

> "Q. 'No problem with $21 - no negotiation'.
>
> Now, this being your note, what did that mean?
>
> "A. He said that his off-the-cuff reaction was that he would have no problem with $21 as a fair price. He didn't feel that it was necessary or proper to negotiate in order to increase that price. He was referring to the position that he might take as a member of the Board of Directors." (Note [2])

Note 1: At his deposition, Mr. Glanville claimed he had no memory at all of the 1976 Memorandum (PX LB-40) (Glanville 24-28).

Note 2: Neither Mr. Crawford nor Mr. Glanville ever explained how Mr. Crawford could ask whether Mr. Glanville could give an opinion on the fairness of $21 in view of the fact that it was only on March 6, 1978 that Signal determined that the price would be $21. In this connection, PX-70 dated 2/28/81 is a handwritten calculation of the advantages to Signal if the cashout price were $21.

Mr. Glanville quoted $250,000 as the price of the opinion (Glanville Dep. 43). Mr. Crawford stated that he expressed "total shock" by the price Mr. Glanville was demanding (PX U-71). Though Mr. Glanville claimed that his loyalty was to the stockholders of UOP (Glanville Dep. 45), the balance of the week was spent in active <u>negotiations</u> between Mr. Crawford and Mr. Glanville on the price that Lehman would charge for the fairness opinion (EX U-71). (Note)

Mr. Glanville had Mr. Schwarzman, Mr. Pearson and Mr. Seegal, subordinates of his at Lehman (Seegal 45), make a one-day "due diligence" visit on March 3, 1978 (Seegal 50) to UOP headquarters. Messrs. Schwarzman, Seegal and Pearson interviewed UOP's management: the bright future, both short and long range, of UOP (as to which Signal had advance private information) was confirmed: they were assured by

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Note: Mr. Glanville originally demanded $250,000 plus indemnification as the price for the Lehman "product" (Schwarzman Dep. 10). Mr. Crawford expressed "total shock" and proceeded to get the Lehman "product" he felt he needed by intense arm's length bargaining: it included the tactics that both sides necessarily use in arm's length bargaining to arrive at a final figure that both sides can agree to: shock (PX U-49-083), reminders of past favors (PX U-49-23), attempts to enlist others (PX U-49-23), promises of future benefits unrelated to the negotiations at hand (PX U-49-25-127), offers (PX U-49-23) and counter-offers (PX U-49-25-127). Mr. Crawford, by negotiation, got Mr. Glanville to agree to $150,000 rather than the $250,000 originally demanded (PX U-71). The Court below characterized the foregoing as "discussions" (A1892 Op.).

UOP management, UOP counsel and UOP's auditors that there would be no "surprises" (Seegal Dep. 53; Pearson Dep. 9-12). Back in New York, they did "a cursory two day review of publicly available statistical data ..." (A1927 Op.) as well as (and significantly) the 1976 Memorandum which Mr. Seegal and Mr. Altman had prepared at Mr. Glanville's direction in 1976 advising Signal's President that it would be in Signal's interest to purchase the minority shares in 1976 at up to $21 (PX LB-40; Seegal Dep. 19-29, 63). Mr. Schwarzman, the senior Lehman officer (aside from Mr. Glanville), saw the 1976 Lehman Memorandum but recognizing its significance, claimed he had deliberately not reviewed its contents (Schwarzman Dep. 19-25). Mr. Glanville did not participate in the "due diligence" visit nor did he review the report made of the visit (Seegal Dep. 79). He was in Vermont on the weekend of March 3-5 before the Chicago meeting of Monday, March 6, 1978 (Glanville Dep. 58; Schwarzman 17)): he was read a draft of the proposed Lehman fairness letter (Seegal Dep. 49). Mr. Schwarzman went to Florida after the due diligence visit (Schwarzman Dep. 34) and left the preparation of the draft of the Lehman opinion and statistical basis for the opinion to Mr. Seegal and Mr. Pearson (Seegal Dep. 79-80): actually, the final one-page basis for the fairness opinion was a comparison between UOP's 1975 results with its 1978 results. It was finally prepared by Mr. Pearson, less than one year out of business school, working alone, on Sunday, March 5, 1978 (Seegal Dep. 80;

Pearson 4; PX LB-5, Table I). Mr. Glanville never met with Mr. Seegal and Mr. Pearson: "They telephoned this impression [i.e., that $20 - $21 was fair] to Mr. Glanville who was spending the weekend in Vermont." (A1894 OP.). Mr. Glanville only met Mr. Schwarzman as they were flying out from New York to Chicago on March 6, 1978, the very morning of the Chicago meeting of UOP's Board (Glanville Dep. 70-71). He may have "glanced" at the paperwork on the plane trip from New York to Chicago (Glanville Dep. 73): he only "thumbed" through it, according to Mr. Schwarzman (Schwarzman Dep. 53).

Mr. Glanville made no determination of the value of the minority shares: his opinion was solely based on the fact that the price of the stock before the Signal announcement was in the area of $14.50 (Glanville Dep. 114) and $21 represented, therefore, the market price plus a fifty percent premium (Glanville Dep. 117-118):

> "Q. Did you yourself make any computation as to what the proper premium was in this case?
>
> "A. In my head -- first, I don't understand the expression proper premium. The premium in this case was about 50% and that was a calculation I did in my head when I first heard what the price level was.
>
> "Q. I see. So that when you first heard what the price was to be -- is that $21? --
>
> "A. 20 to 21.
>
> "Q. -- so that you did a calculation in your head that the premium was in the area of 50% and that sounded right to you based on what you knew?
>
> "A. That sounded appropriate, correct.

"Q. And therefore, if they had said, at that time, the price is 21, you could have said, that price is fair at that time?

"A. Correct, from that point of view.

"Q. And I take it that in this situation you did not make any written calculations at all?

"MR. HAGAN: What do you mean by 'written calculations'?

"Q. You didn't write anything down on any piece of paper, you yourself?

"A. No, sir." (Note[1])

The written Lehman opinion was delivered to the Board of UOP on March 6, 1978. (Note[2]) The first page simply recites the due diligence visit, the documents reviewed and disclaimers (including significantly the absence of any appraisal of UOP's assets). These are followed by a statement that Mr. Glanville who signed the letter for Lehman has been a director of UOP since 1972 and "<u>is familiar with the business and future prospects of UOP</u>" (PX U-7, pg. D-1-2). No basis or reasons for the opinion are given: the only

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Note 1: Actually, even under Mr. Glanville's approach, a price of $22 would have been more appropriate than $21 (i.e., $14.50 + 50% premium = $21.75).

Note 2: The Court below in effect found that Lehman was prepared to attest to the fairness of Signal's offer whether it was $20 or $21 (A1894 Op.): "The two (Glanville and Schwarzman) had with them the draft of a 'fairness opinion letter' in which the price had been left blank. Either during or immediately prior to the directors' meeting that followed [sic], the two page 'fairness' letter was typed in final form and the price of $21 was inserted."

operative part of the letter is the final sentence which states (PX U-7, pg. D-2):

> "On the basis of the foregoing, our opinion is that the proposed merger is fair and equitable to the stockholders of UOP other than Signal."

F. UOP Board Approval

Mr. Crawford readily agreed that the UOP Board would meet on March 6th, just three business days after Signal's acquisition program was first disclosed to him (Crawford Dep. 113). The Board of UOP and Signal both met on March 6, 1976: the two meetings were connected by telephone (PX 36).

Since Signal was the majority stockholder of UOP, it had determined the composition of the UOP Board (PX U-7). The UOP Board consisted of five Signal executives (Mr. Shumway, Mr. Walkup, Mr. Chitiea, Mr. Arledge and Mr. Wetzel) and seven other directors whom Signal nominated and elected (Mr. Pizzitola, Mr. Clements, Mr. Lenon, Mr. Quinn, Mr. Stevenson, Mr. Venema and Mr. Crawford, the former Signal executive whom Signal had installed as President and Chief Executive Officer). Mr. Walkup, Chairman of the Board of Signal and himself a director of UOP, appeared at the UOP Board meeting in Chicago and formally presented the Signal cashout merger proposal, including the price of $21 (PX 298). The UOP directors (who attended the March 6 meeting) received their first documentary information at the meeting itself (A1895 Op.; PX 298, Minutes of the Meeting of UOP's Board of March 6, 1978). Mr. Crawford urged UOP Board approval of Signal's cashout merger of UOP's minority shareholder (by first carefully explaining that the cashout merger would have no effect on UOP employees or customers) even before Mr. Walkup of Signal presented the Signal plan to the UOP Board (PX 298).

> "At the request of the Chairman, Mr. Crawford advised the Board that the proposed merger with Signal would appear to have minimal effect on UOP employees, their benefits and the UOP managers. He stated that some 250 employees have exercisable options to purchase UOP common stock and therefore an equitable arrangement would be needed for either an exchange of stock covered by such options or a buy-out based on the difference between the option prices and $21 per share. He was of the opinion that the proposed merger with Signal owning 100 percent equity in UOP would have a beneficial effect on its customers. He anticipates after the proposed merger becomes effective that the Board of Directors will be changed to an all-inside Board at an appropriate time. The proposed merger-offer will give UOP stockhholders an opportunity to accept or reject an approximate 45 percent increase in the market value of UOP common stock. He expects the stockholder response to be similar to the response received in Signal's 1975 tender offer for UOP common stock, which was over-subscribed.
>
> "Mr. Walkup then stated that Signal proposed in the cash-merger transaction to use funds on hand supplemented by short-term borrowings, which later could be changed to long-term loans. <u>He said UOP as a wholly-owned company would make an outstanding investment for Signal in that Signal's earnings would be increased</u>.
>
> * * *
>
> "<u>Mr. Walkup further stated that the $21 per share offering price was arrived at after comparing UOP's values in 1974 - 1975 with present values</u>. (Note) The market value of UOP common

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Note: Mr. Walkup thus reconfirmed that the price was not negotiated: it was arrived at after "comparing UOP's values in 1974 - 1975 with present values".

stock at the time the 1975 tender offer was made was $13.875 and a premium of 51 percent was offered to UOP stockholders at $21. The market value of said stock on February 28, 1978 was $14.50 - with a 45 percent premium in the $21 cash-merger offer.

* * *

"Mr. Walkup concluded by stating that he anticipated no problems in concluding the proposed transaction and that Signal desires to keep UOP employees whole and not penalize them because of the transaction. He also stated that he would answer any questions other Directors might have and that he would leave the meeting while the other Directors participating in the meeting made their evaluation of Signal's $21 per share offer."

The Board minutes then state (EX 298, pg. 4):

"The Chairman then presented to the Board for consideration the report of Lehman Brothers Kuhn Loeb with respect to the offer of $21 by Signal to the Corporation's stockholders.

"Mr. Glanville stated that he became familiar with UOP at the time its capital stock was first offered to the public in 1959. In addition, he has served as a Director of UOP since 1972 and he has had familiarity with UOP affairs for many years. <u>After he and his staff had reviewed what they believed to be pertinent financial and other materials, with complete cooperation of management of UOP, they concluded that the proposed merger offer is fair and equitable to the stockholders of UOP other than Signal</u>. Copies of said report were in each Director's book. For the information of Messrs. Lenon, Pizzitola and Stevenson, who were participating in the meeting by means of conference telephone, Mr. Glanville summarized and read verbatim <u>portions</u> <u>of</u> <u>his</u> <u>report</u> to the Board of Directors." (Note)

In spite of Mr. Crawford's request that the outside directors take the lead in evaluating the Signal "offer" (PX U-49-30), the proposal was not referred to a special committee of independent directors with the responsibility of considering the matter from the point of view of the minority stockholders (Clements 58). There was no suggestion that the proposal be taken under advisement, nor do the minutes reflect any questions by the directors (Clements 34-35; Pizzitola 31). Mr. Schwarzman, the senior Lehman officer who had headed Lehman's one-day due diligence and research effort and who knew of the existence and significance of the 1976 Memorandum (PX (LB-40), was present at the

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Note: The "report" referred to is simply the two-page letter of Lehman Brothers dated March 6, 1978 (PX U-49-092). That the "report" is not "Lehman Brothers Summary Data Counseling an Offer by Signal Companies, March 1978" (PX LB-5) is obvious from a casual examination of the contents of PX LB-5 -- it contains drafts, summaries of potential offer prices and fee information on other Lehman transactions.

The Court below stated (A1895 Op.):

> "In addition, they [the UOP Board] were presented with Lehman Brothers' fairness opinion letter, as to which Mr. Glanville made comments concerning the information which had gone into the preparation."

There is nothing in the record that provides a basis for suggesting Mr. Glanville made "comments as to the information which had gone into the preparation" of the opinion letter.

UOP Board meeting but made no presentation, volunteered nothing and was asked no questions: only Mr. Glanville spoke on behalf of Lehman (Schwarzman 53).

Mr. Clements believed it was the responsibility of Mr. Crawford to negotiate the best price for the minority (Clements Dep. 39). Mr. Arledge thought that "somebody" was negotiating for the minority shareholders because Signal's press releases recited that there were negotiations (Arledge Dep. 27; PX 146; PX 37, pg. 4). Mr. Pizzitola assumed Mr. Crawford had conducted negotiations because it was his responsibility to do so (Pizzitola Dep. 33). Even Mr. Glanville stated it was Mr. Crawford's responsibility to negotiate for the best price for the stock of the minority shareholders and assumed, without asking, that Mr. Crawford had done so (Glanville Dep. 92-96). There was no suggestion by the Board as a whole that there should be negotiations to better the price or terms, including a stock-for-stock tax-free exchange, for the minority shares (Glanville 92-96).

Signal's cashout merger of the minority shareholders of UOP was brought on for a vote both by the Signal Board and the UOP Board. Those persons who were both Signal directors and UOP directors (Messrs. Shumway, Walkup, Chitiea, Arledge and Wetzel) voted in favor of the merger as directors of Signal. The same persons abstained from voting for the merger as directors of UOP "on the advice of counsel" (Chitiea 55-57). However, all of the Signal-UOP directors who abstained affirmatively stated on the record that, but for the conflict of interest, they would have voted in favor of the proposal (PX U-278). Mr. Crawford, both a UOP and Signal director, did not abstain. (Note) A UOP press release dated March 6, 1978, said the action of the UOP Board was "unanimous" (PX U-49-099). A letter was sent to each minority stockholder on March 7, 1978, stating that there had been "unanimous" approval by the UOP Board of Signal's proposal (PX U-49-073). A similar letter was sent to UOP employees reciting unanimous action by the UOP Board (PX U-49-087). The minority stockholders were informed in the Notice and Proxy Statement that the Signal proposal had been laid before the UOP Board, that the Board had considered the proposal, that the Board had had the benefit of the opinion of Lehman Brothers, and that "Signal" directors on the UOP Board had abstained (but signified approval) (PX U-7, pg. 3).

G. Implementation of the Merger

UOP's management, without Board approval, retained Georgeson & Co., a professional stock solicitation company, to solicit proxies in favor of the Signal proposal (PX U-7, pg. 4).

Note: Mr. Pizzitola was an officer of Lazard Freres, Signal's investment banker: he did not abstain nor was it disclosed then or in the Proxy Statement that he was on the Board as a result of his affiliation with Signal (PX U-7). Mr. Crawford said Mr. Pizzitola was considered for the fairness opinion but rejected because of the conflict of interest since Lazard Freres were Signal's investment bankers (Crawford Dep. 155).

The Notice of Annual Meeting and Proxy Statement of UOP was prepared, circulated and sent out to the stockholders (PX U-7): it repeatedly urged the minority shareholders to vote in favor of the merger proposal of Signal (PX U-7, Introductory Letter, Notice, pg. 9, pg. 10), representing that the price had in effect been negotiated and was fair to the minority stockholders of UOP in the view of (1) UOP's management, (2) the Board, and (3) Lehman Brothers, a New York investment banking house (which had been retained and paid $150,000 for an independent opinion to the UOP Board and the minority stockholders that the terms of the Signal merger were fair to UOP's minority shareholders).

Since Signal stood on both sides of the proposed transaction because it held 50.5% of the UOP stock (PX U-7, pg. 4), the vote on the merger was structured so that (1) Signal would not vote its shares until after it was known whether a majority of the minority had approved and (2) there had to be a minimum of two-thirds of the outstanding stock voting to approve the merger (PX U-7; A1914).

There were angry letters of protest from stockholders of UOP to Mr. Crawford in regard to the price (PX U-49-10), the cashout (PX U-49-036), the lack of arm's length bargaining (PX U-49-043), the failure to offer a tax-free exchange of Signal stock for UOP stock (PX U-49-067), and the failure to increase the $21 price fixed March 6, 1978, when stock prices generally and Signal's stock in particular rose by about 25% on May 28, 1978 (PX U-49-023). Mr. Crawford sent bland answers to all such inquiries from UOP shareholders (PX U-49-035).

On February 28, 1978, UOP stock closed at $14.50. Pursuant to New York Stock Exchange regulations, trading was interrupted because of the announcement of "negotiations" (Purcell Dep. 233). When the stock reopened, it traded at $19.5/8 and, on May 26, 1978, the date of the annual meeting of UOP, the market price was $21 (Purcell Dep. 222-223). Mr. William Purcell of Dillon, Reed testified that normally after the announcement of a merger price range, the stock price rises to substantially the area of the price range and remains fairly constant at that figure but does not exceed it. The merger price "caps" the market (Purcell Dep. 224).

Mr. Purcell testified Signal stock was traded February 28, 1978, at about $28 (Purcell Dep. 221). Between that time and May 28, 1978, the date when the cashout merger of UOP was approved, Signal stock rose to about $39 (Purcell Dep. 221). Mr. Purcell testified that in the period from March 1, 1978 through May 26, 1978, the stock market as a whole rose by about 13% (Purcell Dep. 221). There was no stock-for-stock alternative which would have allowed UOP's minority shareholders to participate in the general rise of the stock market and the rise in the price of Signal stock (PX U-7, pg. C-1-18; A94-101).

The terms of the merger, moreover, did not make any provision for an increase in price to reflect any upward movement of the stock market (Purcell Dep. 225). Rather, the Signal proposal was based on the market price of $14.50, the lowest that UOP stock traded for the entire month of February, 1978 (PX U-7). In addition, the merger agreement did not provide for any update on the fairness of the transaction as of the time of closing, May 28, 1978, as contrasted with the time of the announcement of February 28, 1978 (Purcell Dep. 226). Mr. Purcell testified that he was familiar with merger agreements requiring a fairness opinion as of the time of closing (Purcell Dep. 227).

The Merger Agreement provided Signal with an "out": Signal could have backed out of the merger agreement prior to May 28, 1978, if the market had gone down simply by having an affirmative vote of both its Board and the Board of UOP, which Signal controlled (PX U-7). UOP had no such "out". The UOP minority stockholders were not paid of that portion of the second quarter dividend represented by the period from March 31 through May 28: the UOP Board voted to omit the dividend and Signal thus received 100% of the second quarter UOP dividend (PX 141).

H. May 26, 1978, the Date of the Stockholders' Meeting

On May 26, 1978, the meeting of stockholders of UOP took place (PX U-403; A1374-1447). A number of stockholders attended and raised questions about the entire merger. (Note [1]) A "script" had been prepared in advance of the meeting to field just such questions (PX 296). Bland, evasive answers were given to all stockholders' questions: there was no in depth explanation of how the cashout price was arrived at (A1375-1447). Both Mr. Glanville and Mr. Schwarzman attended the meeting (A1139, 1414). Mr. Schwarzman never said anything at the stockholders' meeting though he knew of the existence of PX LB-40, the 1976 Lehman draft opinion to Signal that stated that it was in Signal's interest to buy out the minority stockholders at any price up to $21. (Note [2]) The proxies having been mailed in prior to the stockholders' meeting, the outcome was a foregone conclusion. On that date, there were 11,488,302 UOP common shares outstanding. Signal owned about 5,800,000 and 5,688,302 were owned by minority shareholders (A1445). Only 56.4% of the 5,688,302 shares owned by minority shareholders were voted. Thus, 43.6% of the minority stockholders did

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Note 1: The price (A1392, 1402), Lehman's role (A1414), the absence of the second quarter UOP dividend (A1405), the fiduciary capacity of the directors (A1408), the reason why Signal did not purchase more stock in 1975 (A1411), the reason why Signal did not offer a stock-for-stock merger (A1402), the details of the SEC review (A1415).

Note 2: Significantly, after the suit was commenced, Mr. Glanville sent Mr. Schwarzman a note saying (PX LB-49):

> "Steve Schwarzman -- it looks like you will earn your fee."

not vote at all and 7.9% voted against the merger (A1897 Op.). In contrast, in 1975, there was a 78% subscription for the Signal tender (A1885 Op.). However, since the vote was sufficient to comply with the two requirements of the merger agreement, the merger was consummated before the end of the meeting of May 26, 1978 (A1445).

After the merger, Mr. Crawford received and acknowledged written congratulations from other Signal executives for having successfully carried out the merger and eliminated the minority shareholders of UOP. Mr. Crawford replied to the congratulatory letter from Mr. Roger W. Mullin, Jr., Chairman of the Board of Mack Trucks, Inc., another Signal subsidiary, on June 5, 1978 (PX U-49-4):

> "Dear Roger:
>
> "Thanks for your kind note.
>
> "The merger mechanics came off smoothly, with the independent shareholders voting more than 11 to 1 in favor of accepting Signal's offer.
>
> "Congratulations on Mack's outstanding performance. Everything seems to be going very well in Allentown. Sincerely,
>
> Your Blood Brother,
>
> J. V. Crawford"

I. The Parties' Experts

The plaintiff retained, as his damage experts, Mr. Alfred Hansen, C.F.A. and Mr. Kenneth Bodenstein, C.F.A. of Duff & Phelps, Inc., a Chicago appraisal firm (A663). After study and analyses, Duff & Phelps submitted a detailed report in which they concluded that the stock belonging to the UOP minority shareholders had a worth at the time of the merger of not less than $26 per share (A486-513). Both Mr. Hansen and Mr. Bodenstein were deposed by the defendants in Chicago in April, 1980 (Hansen Dep. 4-70; Bodenstein Dep. 4-398). Mr. Bodenstein testified at trial for three days explaining in detail why, based on several methods of comparable analysis including three different analyses based on the method used by business for evaluating the worth of 100% ownership (i.e., the discounted cash flow method), that the minority stock was conservatively worth not less than $26 per share (A639-1019).

The defendants did not rely on Mr. Glanville or Lehman Brothers for expert testimony on the value of the minority shares. Indeed, neither Mr. Glanville nor anyone from Lehman testified or even attended the trial (TR 1026). Instead, "for purposes of trial" (A-1955 Op.), in March, 1980, the defendants selected a new expert: Mr. William Purcell of Dillon, Read was retained to provide an opinion as to why Signal had been justified in paying only $21 per share to the minority in 1978 (A1179-1180). In his report (DX 40-C; A514-551) and in his testimony at deposition and at trial, Mr. Purcell used only one calculation for his ultimate conclusion: his sole method was that of a statutory appraisal plus a premium (DX 40-C; A1955 Op). (Note) Based on his calculations using this method, he concluded (not that the price was within an acceptable range) but rather that $21 was fair to the minority (A1958 Op.). Mr. Purcell testified that he did not rely on Mr. Glanville's approach or the reasons adopted by the UOP management and Board but he adopted their principal rationale that the price in 1978 was justified because certain of UOP's financial figures were comparable to those in 1975 (A1196). Mr. Purcell himself did not do the research and calculations on comparable premiums: rather, this was done by Mr. Daum and Mr. Reid, two juniors at Dillon, Read (A1062; DX 6; EX 6; EX 7). Mr. Daum and Mr. Reid selected the day before the announcement of the proposed merger as the base line for calculating the amount of premium (without attempting to determine whether leaks or anticipation by the market had resulted in increases in price of the market) (A1346). Prior to Mr. Purcell's testimony, Mr. Bodenstein had prepared and there had been introduced into evidence specific calculations as to each of Mr. Purcell's comparable mergers to show that without filtering "noise"

Note: Mr. Purcell testified that the discounted cash flow method was appropriate to determine 100% of the value of a company (A1045, 1051-1057), that B. Graham, D. Dodds & S. Cottle, Security Analysis (4th Ed. 1962) (hereafter "Graham and Dodd") explained the method (A1048) that Graham and Dodd were "pretty sound" (A1049), that he did not make such a calculation using that method even on a retrospective basis (A1057).

(i.e., the increase in price or value due to leaks or anticipation (A1943)) the percentage of premium would be incorrect (PX 6 Trial).

ARGUMENT

I. THE COURT BELOW ERRED IN DISMISSING THE DERIVATIVE COUNTS, IN LIMITING THE CLASS CERTIFIED, AND IN FAILING TO CONSIDER AND ACT ON PLAINTIFF'S MOTION THAT THE CLASS BE ENLARGED

After briefing and argument, the Court below, on April 26, 1979, entered orders on its opinions of April 3, and April 5, 1979, dismissing the derivative counts and certifying the class but limiting it "to those former stockholders who had voted against the merger and/or who had not turned in their certificates in exchange for $21 per share payment". The plaintiff's interlocutory appeal was dismissed by this Court. The plaintiff has renewed its appeal as to these two orders of the lower Court.

A. Dismissal of Derivative Count

The Court below dismissed (A215-220) the derivative count purportedly on the basis of Heit v. Tennaco, Inc., (D.Del. 1970) 319 F.Supp. 884; Braasch v. Goldschmidt, Del.Ch., 199 A.2d 760 (1964); and Beals v. Washington International, Inc., Del. Supr., 386 A.2d 1156 (1978). The plaintiff's basic position is (1) that the defendants, by carrying out the merger, should not be able to eliminate what would otherwise be a viable cause of action for the company in question, and (2) that UOP survived the merger and, therefore, the derivative counts should not have been dismissed (A146-214).

B. Limitation of Class to Those Who Voted Against the Merger and/or Who Had Not Turned Their Stock In

The plaintiff's original complaint was based on the public information available to the plaintiff and other outside stockholders (i.e., the press releases, UOP's letters to stockholders and the notice of the meeting). Based on this information, the plaintiff's attorneys drew up a complaint, and served and filed it promptly, challenging the merger. (Note) The Court below held, in effect, that those who had voted for the merger or who had turned their shares in were not dissatisfied with the merger and therefore could not be members of the class (A295-308). The lower Court's original decision limiting the class was incorrect for the reasons stated in plaintiff's Notice of Appeal of an Interlocutory Order (A328-340).

The plaintiff thereafter filed an amended complaint that in essence alleged breach of their fiduciary obligations by the defendants to all of the minority shareholders (A315). Prior to the commencement of the testimony, the

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Note: William J. Carney, "Fundamental Corporate Changes, Minority Stockholders and Business Purposes", (A.B.A.J. Vol. 1980 No. 1, pg. 73), (hereafter cited, for example, as "Carney supra"):

> "*** Courts often require the plaintiff to plead the unfairness with some particularity before the Court will reach the merits, which places a substantial burden of proof on the plaintiff at the onset of the case."

plaintiff filed a motion that the class be enlarged to include all minority stockholders as of the date of the merger on May 26, 1978 (A636). The plaintiff filed a post-trial brief in support of the motion for enlargement of the class. The defendants did not respond: rather, they said (Signal and UOP's Post-Trial Brief - September 19, 1980):

> "We respectfully suggest that the Court defer a determination on plaintiff's motion until after the merits of the case have been decided.

The Court below not only did not address itself to the plaintiff's motion for enlargement but stated that the plaintiff's motion for enlargement was filed after trial (A1966 Op.).

This Court should reverse the lower Court's decision dismissing the derivative count. If the Court reverses the lower Court, then the Court below should be directed to certify all of the minority stockholders of UOP as members of the class since, if there was a breach of fiduciary duty as to some of the minority stockholders, there was a breach as to all of them. To put it another way, if material facts were misrepresented or withheld from the minority shareholders, then acceptance of the merger terms by an affirmative vote or surrender of the stock is of no effect and the minority shareholders who voted in favor or who surrendered their shares should be included within the plaintiff class.

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The Court belowed erred not only in dismissing the derivative count of the original complaint but erred in not certifying as the class all of the minority stockholders of UOP. The Court should be reversed on both matters. A class consisting of all of the minority stockholders of UOP as of May 28, 1978 should be certified.

II. IN VIEW OF THE TRIAL RECORD AND THE APPLICABLE LAW, THE LOWER COURT'S DECISION EXONERATING ALL OF THE DEFENDANTS IS INCORRECT

The lower Court commenced by suggesting (A1903 Op.):

> "The decisions in Singer, Tanzer and Roland International have bred some uncertainty in this Court as well as, I think it fair to say, among members of the corporate bar concerning the present status of litigation wherein a cash out merger effectuated by a majority shareholder is attacked in a class action brought by a member of the cashed out minority. From a repeated reading of those decisions, I am not convinced that the situation has been complicated to the extent that at first it might appear."

The lower Court then sets out its interpretation of Singer and its conclusion (A1907 Op.):

> "Sterling, then, is the bedrock on which Singer, Tanzer and Roland International are built. It is still the law, and it is still the final word even if it appears on the evidence that there is no violation of anything new that has been announced in Singer and Tanzer. Thus, the analysis must turn to Sterling."

However, as will be shown, the lower Court, in interpreting the law and applying it, has managed to exculpate all of the defendants in a case which clearly offends the spirit and the letter not only of Singer v. Magnavox, Del. Ch., 379 A.2d 1121 (1977), Del. Supr., 380 A.2d 969 (1977); Tanzer v. Roland International Corporation, Del. Supr., 407 A.2d 1032 (1979), but Sterling v. Mayflower Hotel Corp., 93 A.2d 107 (1952), and Guth v. Loft, Del. Sup. 5 A.2d 191 (1971), as well. Specifically, the lower Court held, in applying what it conceives to be the law to the facts of this case:

(1) That an investment banker retained to give a fairness opinion for the benefit of the minority (and whose managing partner is himself a director) has no fiduciary obligation whatsoever to the minority shareholder.

(2) That all that this Court's requirement that a majority owner have a "bona fide purpose" means is that the merger be in the selfish best interest of the majority.

(3) That the fiduciary requirements of "complete candor" as clearly set out by <u>Lynch</u> are satisfied (a) even though the minority were repeatedly and falsely assured that the cashout merger price was arrived at by negotiation<u>s</u>, (b) even though the minority stockholders were misled as to what the investment banker giving the fairness opinion did and did not do and were not informed of its prior contradictory opinion, and (c) even though it was falsely represented to the minority that their Board was unanimously of the opinion that the price of $21 was fair.

(4) That, in spite of the <u>Singer</u>, <u>Mayflower</u> and <u>Guth</u> decisions, the majority stockholder of UOP, the directors of UOP (and UOP management) were entirely relieved of their fiduciary obligation to do their utmost to advance the interest of the minority because

they found themselves in a conflict of interest and could justify their whole course of conduct and misleading representations to the minority simply by asserting at trial that they thought that the cashout price was "fair" to the minority.

In this case, the lower Court's decision results in a dismissal of the case of the minority stockholders but, as is obvious, the effect of the lower Court's decision is a precedent which, unless reversed by this Court, will be to eviscerate not only Singer, supra, Tanzer, supra, and Najjar, supra, but will undercut Sterling, supra, and Guth, supra. However, as will be shown, the lower Court's entire approach to the majority-minority situation is not only incorrect but was specifically wrong in its interpretation of the meaning of each of the above decisions. (Note)

A. In View of the Record, the Court Below Erred in Exonerating the Defendant Lehman Brothers From Its Fiduciary and Legal Obligation to the Minority of UOP

The Court below begins by exonerating Lehman on the basis that plaintiff had failed to prove that Lehman had conspired with UOP (A1916 Op.):

Note: The opinion of the lower Court itself contains some intimations that the lower Court recognized that its approach was at variance with the decisions of this Court but hopes that this Court will in effect reverse its position as announced in Singer, Tanzer and Najjar and adopt the lower Court's approach when the Court below says (A1903 Op.): "I therefore offer my understanding of the effect of these decisions, and apply the conclusions to the facts of this case, with the hope that my interpretation is the correct one."

"Initially, I dispose of the charges against Lehman Brothers. Plaintiff says that Lehman Brothers conspired with Signal and it controlled UOP board of directors to deceive UOP's minority shareholders into voting to approve the terms of the merger. The basis of this assertion is that Lehman Brothers was actually working in the interests of Signal rather than UOP's minority in rendering its fairness opinion."

The plaintiff will show:

(1) That, since Lehman acted in Signal's interests rather than in the interests of the minority, Lehman is liable to the minority both on agency and fiduciary principles.

(2) That, since the basis of Lehman's opinion was not disclosed, Denison is applicable.

(3) That Lehman Brothers' 1976 Memorandum directed to Signal was material and should have been disclosed by Lehman especially since Mr. Schwarzman, an executive of Lehman, recognized its import.

(4) That, contrary to what the Court below holds, there was no separate Lehman opinion apart from that of Mr. Glanville.

1. Lehman is Liable to the Minority Under Agency and Fiduciary Principles

The record confirms that Lehman, through its managing director, Mr. Glanville, did act in the interests of Signal rather than the minority stockholders of UOP. The existence of Lehman's unrevealed 1976 opinion in draft form to Signal advising Signal to acquire the balance of the minority shares for any price up to $21, the alacrity with which it agreed to provide a requested fairness opinion at a price of either $20 or $21 based on the off-the-cuff reaction of Mr. Glanville, the poverty of its backup effort, hurriedly assembled by junior associates of Lehman, and the details of the intense haggling on the amount of the fee that Lehman would receive, all confirm that Mr. Glanville (and, hence, Lehman) was really concerned in forwarding the interests of Signal rather than providing an in depth considered evaluation of the worth of the shares of the minority stockholders of UOP. Indeed, there is not a scintilla of evidence that suggests that Lehman or Glanville did anything whatsoever for the minority shareholders.

Lehman is liable to the minority shareholders on two separate bases. First, Mr. Glanville was both a UOP director and a managing partner of Lehman. Lehman is legally responsible for Mr. Glanville's activities under agency principles. Mitchell v. Palmer, Del. Supr., 343 A.2d 620 (1975); Coca-Cola Co. v. Loft, Del.Ch., 167 A. 900 (1933), Aff'd. Del. Supr., 180 A. 927 (1935). Second, contrary to what the Court below holds, an investment banker retained to give a fairness opinion for the benefit of minority shareholders but whose action actually furthers the interests of the majority is liable to the minority. Laventhol, Krekstein, Horwath & Horwath v. Tuckman, Del. Supr., 372 A.2d 168 (1976). To put it another way, an investment banking house employed by the majority to give a fairness opinion to provide assurance to the minority stockholders that the offer by the majority is fair should have been held to the fiduciary standards of the majority itself. To hold otherwise and to exonerate the investment banker in this case will provide a judicial inducement to investment bankers to give the appearance of working for the minority but actually to further the interest of the majority (who will continue to control the corporation and provide additional investment banking business). (Note)

2. The Holding in Denison is Applicable to This Case

At a later point in its opinion, the lower Court distinguishes Denison Mines, Ltd. v. Fibreboard Corp., 388 F.Supp. 812 (D.Del. 1974), solely on the basis that Judge Stapleton's actual holding was that the Lehman Brothers opinion in Denison was not included in the Proxy Statement (A1931). Denison's primary significance for this case lies in the fact that Judge Stapleton pointed out the obvious importance of the opinion of an investment banking house to outside stockholders:

> "The reason this representation was made is obvious. Because of the independence of Lehman Brothers, as well as its reputation in the investment banking field, its opinion added persuasive support for management's view. In the context of this Proxy Statement, the Court

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Note: In the negotiations between Mr. Crawford and Mr. Glanville, Mr. Crawford pointedly reminded Mr. Glanville of the possibility of future Signal business (EX U-49-25-147).

> believes the impact of the reference to Lehman Brothers' opinion on a substantial number of stockholders would be difficult to overestimate."

Though in this case the Lehman fairness opinion was reprinted in the Notice and Proxy Statement, it does not state the reasons for the opinion: all it says is that, based on its analysis, the merger price is fair to the minority stockholders. Thus, the actual holding of Denison is applicable to this case.

3. Lehman's Failure to Disclose the Existence of Lehman's 1976 Opinion to Signal is a Violation of the Requirement of Complete Candor

The Court below held as a matter of law that PX LB-40, "Memorandum to Forrest Shumway - Confidential Draft, Considerations Relating to the Signal Companies' Investment in UOP - Lehman Brothers, Inc., June 1976" (hereafter referred to simply as "PX LB-40"), is legally nonsignificant (A1918-1919). The uncontradicted record shows: PX LB-40 was prepared at Mr. Glanville's specific direction by Mr. Altman and Mr. Seegal of Lehman Brothers in 1976; Mr. Seegal was made a member of the 1978 Lehman backup "team" because of his past familiarity with UOP (Seegal Dep. 44); the Lehman team saw and used PX LB-40 in connection with its backup work in March of 1978 (Seegal Dep. 61-67). Specifically, Mr. Schwarzman, head of the Lehman backup team, saw PX LB-40 in the week prior to March 6 and recognized its importance but stated on his deposition that he affirmatively decided not to look at its contents (though others did) because he knew and recognized its critical significance (Schwarzman Dep. 17-20).

The Court below says of PX LB-40 (A1917 Op.):

> "If it was the feeling of Lehman Brothers that UOP was a good investment for Signal in 1976 at $21 per share despite its poor 1975 performance, plaintiff wonders how Lehman Brothers could have seriously suggested in 1978 that $21 was a fair price to the minority in view of UOP's vastly improved performance in 1976 and 1977."

The plaintiff "wondered" about Lehman's inconsistent position when PX LB-40 first came to light during the discovery. This inconsistency was not explained at trial: neither Mr. Glanville nor any other managing partner nor indeed any employee of Lehman appeared or testified at trial (though Lehman was a named defendant) first to explain the inconsistency that the lower Court refers to and, second, to explain and justify the fairness opinion itself. The Lehman fairness opinion was one of the principal justifications for the recommendation of UOP's Board to the minority stockholders to vote in favor of the Signal proposal (PX U-7). The opinion of the Court below makes no mention of the failure of Mr. Glanville or any Lehman executive or employee to appear at trial nor does the Court below make any mention of the fact that, though the defendants at the time of the merger relied on Mr. Glanville's opinion, at trial they studiously avoided even mentioning it. Of course, the Court below did not draw any adverse inferences from the foregoing. Richard v. Jones, Del.Ch., 142 A. 832 (1928); Gammel

v. Chandler-Hill Corp., Del. Supr., 103 A.2d 228 (1954); Jett v. Texas Company, D.Del., 73 F.Supp. 699 (1947), Anno., 5 A.L.R. 2d, 893, 907-908 (1949).

4. The Failure to Disclose the True Basis of the Fairness Opinion Was a Violation of the Requirement of Complete Candor

At a later section of its opinion dealing with the defendants' non-disclosure, the Court said (A1932 Op.):

> "Finally, however it came about, UOP hired Lehman Brothers to render an opinion, and the opinion given was offered as being that of Lehman Brothers. I cannot see where UOP had any obligation to state or insinuate in any way in the proxy materials that the opinion was really the personal opinion of Glanville based on his initial reaction that the $20 to $21 price range was fair because it represented almost a 50 per cent premium over market. The evidence shows that other qualified persons at Lehman Brothers worked on the project and that a good deal of information was reviewed before the opinion letter was issued. In this context, I find no misrepresentations or lack of disclosure in the Proxy Statement reference to Lehman Brothers."

As the record shows, on being asked by Mr. Crawford, Mr. Glanville immediately stated his opinion: it was simply that since $21 represented a premium of about 50% over market, Signal's cashout price of $21 was fair to the minority (Crawford Dep. 119-120). The Court below states that Lehman (as apart from Mr. Glanville) was retained, did the work and gave the fairness opinion. The entire record, however, is flatly to the contrary.

Mr. Glanville was the only Lehman partner familiar with UOP: the minutes of the meeting of the Board of UOP of March 6, 1978, in pertinent part, state (PX 298, pg. 4):

> "Mr. Glanville stated that he became familiar with UOP at the time its capital stock was first offered to the public in 1959. In addition, he has served as a director of UOP since 1972 and he has had familiarity with UOP affairs for many years."

The opinion letter itself specifically recites the foregoing and goes on to state that Mr. Glanville is "familiar with the business and future prospects of UOP" (PX U-7, pg. D1-2). The Notice of Meeting and Proxy Statement also recite Mr. Glanville's special qualifications (PX U7, pg. 10, (A129); Appendix D, pg. 9, D-29 (A102)). In contrast, Mr. Schwarzman, the Lehman executive chosen to head up the Lehman backup team had no prior familiarity with UOP (Schwarzman Dep. 6). Mr. Seegal, though familiar with UOP, was only an associate (Seegal Dep. 6) and Mr. Pearson, the only other member of the team, was but one year out of business school (Pearson Dep. 4). Mr. Glanville was the Lehman representative who presented the opinion, who spoke at the meeting and who is supposed to have answered questions of the Board of Directors (PX 298; Schwarzman Dep. 52). Thus, the entire record indicates that Mr. Glanville was selected by Mr. Crawford in preference to Mr. Pizzitola or any other investment banker because of Mr. Glanville's personal familiarity with UOP. Mr. Glanville was the person represented both by the Board of UOP and to the stockholders as being specially knowledgeable (PX 298; PX U-7).

Lehman did not issue an independent opinion separate apart from Mr. Glanville. Rather, a backup team was formed in order to do the due diligence visit and provide a review of the statistical information and draft the formal opinion letter (Schwarzman Dep. 9-11). The backup simply consists of a one-page comparison of certain similarities between the financial status of UOP in 1974 and 1978: there is a total absence of comparative or critical analysis of the worth of the shares of the minority of UOP (PX LB-5). Thus, at the time, every effort was made both by Signal and Lehman to convince the minority stockholders that Mr. Glanville, a Lehman managing partner who had been a member of the Board of UOP since 1972, had special qualifications to give a fairness opinion. This was done to persuade the minority that someone especially knowledgeable had looked into the matter and was in a position to assure them that the price of $21 was fair. The lower Court's suggestion that Lehman, apart from Mr. Glanville, issued the fairness opinion simply will not hold water. The record made at the time simply does not substantiate the Court's holding that there is a Lehman opinion apart from Mr. Glanville's opinion. Furthermore, measured by the test of complete candor, it was false to represent to the minority stockholders that an independent banker had reviewed the matter and had concluded that the price of $21 was fair when the fact of the matter was that the opinion was simply Mr. Glanville's horseback reaction that the price of $21 was fair because it was 50% more than the market price.

B. The Interpretation of the Court Below of the Proper Business Purpose Rule Is Incorrect

1. Signal's Purpose was Solely to Promote Its Own Economic Best Interest

The Court below found that Signal's purpose in cashing out the minority was to promote Signal's own economic interest (1920 Op.):

> "The facts of the matter clearly indicate that Signal was motivated by its own economic interests, and thus those of its own shareholders, in determining to acquire the remaining 49.5 per cent interest in UOP. It had surplus cash as a result of the sale of its Signal Oil and Gas Company subsidiary in 1974. It had been looking for other places to invest this excess cash. It had attempted two other acquisitions or combinations during 1977, but the effort had been unsuccessful. By its own admission, in the early part of 1978 the acquisition of the balance of UOP's minority shares so as to give Signal 100 per cent ownership of UOP appeared to be the best investment opportunity then available to it." (Note)

Note: The Court below then goes on to list some other "purposes" which Signal later advanced to justify its appropriation of the minority's equity interest in UOP (A1920 Op.). The Court below did not base its decision on these alternative purposes, acknowledging that the plaintiff had established [as Signal was forced to acknowledge at trial (Walkup TR 1662, et seq.)] that all of these alternative reasons were "foreseeable" in 1975 when Signal acquired its majority position. (See Najjar, supra, pg. 1034, footnote 4.) Actually, these reasons are the very "subterfuges" that this Court alerted the lower Court to in scrutinizing a majority cashout of a minority (Tanzer v. International General Industries, Del. Supr., 379 A.2d 1121 at pg. 1124 (1977)). In Young v. Valhi, Del.Ch., 382 A.2d 1372 at pg. 1377 (1978), and in Kemp v. Angel, Del.Ch., 381 A.2d 241 (1977), the validity of such purposes was questioned. As to the alleged necessity of eliminating conflicts of interest, see William J. Carney, "Fundamental Corporate Changes, Minority Shareholders and Business Purposes", (A.B.A.J., Vol. 1980, No. 1, pg. 73 at pg. 108):

> "The great difficulty with this justification is that the conflict of interest was often created by the parent corporation when it began the takeover."

2. The Sterling Case Is Not Authority for the Lower Court's Decision

In arriving at its decision, the Court below first states that Singer, supra; Tanzer, supra; and Roland, supra, were nothing more than an affirmation of Sterling v. Mayflower Hotel Corp., Del. Supr., 93 A.2d 107 (1952) (A1913 Op.):

> "Singer reaffirms the basic principles of Sterling and specifically applies them to an interested merger situation in which the minority shareholders are being given a cash payment for their shares rather than a value-equivalent interest in the surviving corporation. The amplification which Singer seems to provide is its indication that the 'purpose' of the majority shareholder in seeking such a merger is a specific element or factor which must be considered in evaluating its fairness to the minority, and that if there is no purpose other than to rid the enterprise of its minority shareholders, it is a violation of the majority shareholder's fiduciary duty, and therefore wrong. ...
>
> "Tanzer goes further, and says that in evaluating the fairness to the minority, it is not necessarily wrong for a majority shareholder to merge out the minority in furtherance of its own private interests provided that its purpose is a bona fide one, and in this regard "bona fide" is used in the sense of not being a mere subterfuge to get rid of the minority. In other words, the bona fide nature of the majority shareholder's alleged purpose is now specifically made another element or factor which this Court must consider in scrutinizing the transaction for 'entire fairness' to the minority."

The Court below then quotes Sterling, supra, as authority for the proposition that a "bona fide" purpose is simply one in which the economic interest of the majority is served, saying (A1923 Op.):

"Mayflower [sic.] directors and stockholders have determined, not that [the Mayflower] venture should be terminated but that it should be integrated completely with the Hilton enterprise. Having made this decision they had the right to avail themselves of the means which the law provides for just such a purpose, subject always to their imperative duty to accord to the minority fair and equitable terms of the conversion ***" (Note)

* * *

"Thus the purpose in Sterling was to further the investment and business interests of the majority shareholder. There it was a voluntary rather than economically compelled decision on the part of a majority. Sterling is still the law."

The lower Court's interpretation of the meaning and effect of Sterling as it relates to the proper business purposes doctrine appears incorrect for several different

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Note: The lower Court holds that the underlined phrase "for just such a purpose" refers to the "purpose" of the majority in affecting the merger. The plaintiff believes that the lower Court is mistaken: what this Court was saying was that if the majority in Sterling made a legal and proper determination to affect a merger, they were free to use the means (i.e., the predecessor to 8 Del.C. §251) which the Delaware law afforded them in carrying out their decision.

reasons. (Note [1]) Besides the obvious fact that Sterling was decided twenty-five years before Singer, as the Chancellor and this Court made clear, Sterling was a stock-for-stock merger, not a cashout acquisition of a helpless minority who were being forever excluded from the enterprise. Rather, as Chancellor Hartnett in Tanzer v. International General Industries, Inc., Del.Ch., 402 A.2d 382 at 391 (1979), pointedly suggests be done (Note [2]), the Sterling

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Note 1: Though perhaps not strictly germane to the argument at this point, in Sterling, the Mayflower board not only had the proposed merger under consideration for over two years (in contrast to the present situation where the non-Signal UOP Board first heard of the proposed merger only three business days before the meeting when the Board "unanimously" approved Signal's proposal) but before voting on the merger, the Mayflower board had obtained an updated "forty page report including charts with a long appendix containing analyses of the pertinent financial data" (Sterling, supra, at pg. 110) from Standard Research Consultants, Inc.

The Chancellor noted, Sterling v. Mayflower Hotel Corp., Del.Ch., 89 A.2d 862 at 867 (1952):

> "Standard is a nationally known reputable firm having no interest in either Hilton or Mayflower. It took the assignment on the express condition that it would be permitted to exercise its own independent and unbiased judgment as to a fair plan of exchange."

Note 2: There is a real distinction between a genuine merger, tax-free, stock-for-stock transaction (i.e., Sterling) where the minority is given a continuing equity interest and a cashout acquisition where the majority forcibly expels the minority (i.e., this case) especially if (as the lower Court has in effect held) the measure of recompense is limited to statutory appraisal.

minority was given a continued equity participation in the ongoing enterprise. Specifically, this Court said in Sterling, supra, at pg. 112:

> "A merger ordinarily contemplates the continuance of the enterprise and of the stockholders' investment therein, though in an altered form; ***"

Moreover, in Sterling, there was, in effect, a cash alternative for those minority stockholders who no longer wished to participate in the ongoing enterprise. Second, a review of the lower Court's opinion and the opinion of this Court in Sterling shows that no question appears to have been raised as to whether Hilton had a proper business purpose for carrying out the merger (other than its own economic best interests). Finally, and determinative, is the fact that in Singer, supra, this Court held that the necessity of a proper business purpose was an issue of "first impression", thus negating Sterling as a proper basis for the lower Court's holding on the point (pg. 975):

> "The statute [8 Del.C. §251) is silent on whether a merger may be accomplished only for a valid business purpose but two recent unreported decisions seem to suggest that such a showing is required under Delaware law. See Pennsylvania Mutual Fund, Inc. v. Todhunter International, Inc., Del.Ch., C.A. No. 4945 (December 23, 1975). Neither decision was by this Court and the issue is one of first impression here."

3. The Advancement of the Majority's Economic Interest Does Not Constitute a Proper Business Purpose Neither as a Matter of Law Nor as a Matter of Logic

This brings the plaintiff to the ultimate question: is the lower Court's interpretation correct that a "bona fide purpose" (as the phrase appears in this Court's opinion in <u>Tanzer</u>) simply means proving that the economic best interest of the majority be served by the merger? (Note) The plaintiff believes not only is the Court below wrong insofar as what constitutes a bona fide purpose under the law as announced by this Court but the lower Court is wrong as a matter of logic.

In <u>Tanzer</u>, <u>supra</u>, after noting that a majority stockholder's right to act in its own interest was limited by its fiduciary duty to the minority, this Court made it clear that a "bona fide purpose" was one that was more than simply the majority's self-interest, saying:

> "Turning now to the Chancellor's opinion, he found that ...
>
> > "'The principal reason for the merger and evidently the other reason for the merger is to facilitate long term debt financing by IGI. He went on to conclude that: 'IGI has a legitimate and present and compelling business reason to be the sole owner of Kliklok. IGI is not freezing out the minority <u>just for the purpose of freezing out the minority</u>.'"

In <u>Tanzer</u>, the Vice Chancellor defined a "bona fide purpose" as one that was "legitimate", "present" and "compelling". Clearly, Signal's economic self-interest in acquiring the minority UOP interest comes within none of the

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Note: The Court below accepted (A1920 Op.) Signal's general assertions that the acquisition of the minority's interest in UOP was "the only game in town at the moment" (Walkup TR 1668-1672). Other considerations aside, Signal did not carry its burden of proof in showing it actually had no other alternatives (<u>Singer</u>, <u>supra</u>).

foregoing. See also, Najjar, supra, pg. 1034, footnote 4.

The lower Court's decision is not only legally incorrect, it is illogical. Under the lower Court's analysis, if a merger is neutral in effect (i.e., does not benefit the majority stockholder or the controling corporation), it is impermissible. But if the majority stockholder effects the purpose for its own selfish purpose, the merger is proper. Under this analysis, the only improper purpose would be if the majority went through the merger process for no reason whatsoever. But if the majority says "Let's eliminate the minority stockholders because we have nothing better to do with our excess cash", then the lower Court says the merger has a proper and valid business purpose. Obviously, any merger proposed by a majority stockholder is going to yield some benefit to the majority or the majority would not propose and carry out the merger in the first place. While Tanzer holds that the fact that the merger benefits the majority stockholder does not per se make the purpose of the merger improper, neither does it say that the fact that the merger benefits the majority make the purpose per se proper. By its ruling, the lower Court has turned a broad equitable principle into an inflexible and incongruous rule: as long as the majority stockholder has a selfish purpose for proceeding with the merger, the merger has a valid business purpose. (Cf. Justice Quillen's dissent in Roland, supra, 405 A.2d at 1038.)

The actual reason that the lower Court advances as justification for its holding is not based on law or logic but something quite different (A1922 Op.):

> "Logically extended, it means that if one company desires to obtain control of another through the tender offer device, it must get all of the outstanding shares through the offer, or forever hold its peace thereafter as to any consequences resulting from an acquisition of less than all outstanding shares. With a large, publicly-held company, such logic is unrealistic."

The Court below seems to believe that continued joint ownership of an enterprise by a majority and minority stockholder is simply unthinkable and unworkable: that is simply not correct. There is no corporate reason why a majority must eliminate a minority simply because it is in the majority's economic or selfish best interest to do so. Further, the Court below seems to think that the majority has some sort of inalienable right to oust the minority whenever the fortunes of the joint enterprise are such that it would be in the majority's economic best interest to take over the minority's interest. The lower Court has totally disregarded Najjar, in which this Court teaches that not even in a short form merger can the majority oust the minority absent a proper purpose (i.e., a legitimate and compelling business reason other than simply the economic benefit of the majority). The majority is not being harshly dealt with: it can not take over the position of strangers or third parties arbitrarily simply because it would be economically advantageous to do so. Similarly, there is no reason why, simply because it is beneficial to the majority, that it should be able to expropriate the property of its fellow owners of the enterprise, the minority.

Of course, corporate situations can and do change. If, as in _Tanzer_, _supra_, the situation changes and some legitimate and compelling need develops that requires that the majority take over the position of the minority, then clearly under _Tanzer_, _Singer_ and _Najjar_, the majority can merge out the minority (albeit they have to scrupulously observe the standards of fairness in doing so). To apply the foregoing to the present situation, if a situation were to develop in UOP where it became important and compelling for Signal to take over the interest of the minority, it could do so under the present law. (Note)

In summary, the Court below has found as a fact that Signal cashed out the minority shareholders of UOP because it was in Signal's own economic interest to do so. The lower Court's decision is at variance with this Court's decisions in _Singer_, _Tanzer_ and _Najjar_. _Sterling_ provides

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Note: Examples are not difficult to think of: (1) if defense contracts required single ownership, (2) if UOP needed loans from Signal, (3) if Signal proposed to split some of UOP's divisions and amalgamate them with other entities in the Signal complex, then Signal would have a real necessity for eliminating the separate minority ownership of UOP. Of course, as _Tanzer_, _supra_, makes clear, the present and fairest method of doing so not only tax-wise but in the interest of allowing a continuing equity interest to the the minority interest in the enterprise is a stock-for-stock transaction rather than a cashout merger.

no basis for the lower Court's decision. The decision of the lower Court should be reversed. To do anything else is to countenance the complete evisceration of the requirement of a proper business purpose in cashout mergers. It would sanction the casual cashout of a minority at any particular time when it is economically advantageous to the majority to do so.

C. Though The Court Below Failed to Utilize The Standard of "Complete Candor", the Record Shows the Defendants Were Guilty of Numerous Material Misrepresentations to UOP's Minority Shareholders

In Lynch v. Vickers Energy Corp., Del. Supr., 383 A.2d 278 (1977), this Court said:

> "Relying on Allied Chemical & Dye Corporation v. Steel & Tube Co., Del.Ch., 120 A. 486 (1923) and Epstein v. Celotex Corporation, Del. Ch., 238 A.2d 843 (1968), the Chancellor determined that Vickers, as the majority shareholder of Transocean, owed a fiduciary duty to plaintiff which required 'complete candor' in disclosing fully 'all of the facts and circumstances surrounding the' tender offer. 351 A.2d at 573. We agree with that statement of the law. Compare Singer v. The Magnavox Company, et al., Del. Supr., 380 A.2d 969 (1977); Lank v. Steiner, Del. Supr., 224 A.2d 242, 244 (1966), applying the 'special circumstance rule' to a director possessed of special knowledge withheld from a stockholder with whom he is negotiating for purchase of his stock; and Iroquois Industries, Inc. v. Lewis, Del. Supr., 318 A.1d 134 (1974)."

The record shows that the defendants were not "completely candid" with the minority shareholders of UOP. On the contrary, whether the various representations of the defendants are measured individually or whether the representations are measured collectively against the fiduciary standard that requires "complete candor", the defendants' conduct falls far short. In point of fact, the opinion of the Court below on this phase of the case consists largely of palliation, condonation and explanation of the misrepresentations of the defendants in flat contradiction of this Court's explicit directions that the applicable standard is "complete candor" on the part of the majority vis-a-vis the minority. To put it another way, the defendants' course of misrepresentations dug out through discovery in this case shows a clear pattern of that very sort of conduct by a majority shareholder in cashing out a minority that this Court held in Singer and subsequent cases would not be tolerated by the Courts of Delaware.

1. The Defendants Repeatedly Misepresented to the Minority Shareholders That There Had Been Negotiations as to Price

The record is too clear for contradiction that the defendants Signal and UOP repeatedly and consistently represented to the minority stockholders that there were "negotiations" between Signal and UOP in arriving at the price of $21. (PX 146, Press Release of February 28, 1978; PX 110, Press Release of March 2, 1978; PX 24, Press Release of March 6, 1978; PX U-49-075, Letter to Stockholders of March

7, 1978; EX U-7, Proxy Statement, pg. 13.) (Note) Furthermore, Signal never disclosed to the minority stockholders that Signal's studies showed that the cashout merger of UOP's minority shareholders would be profitable to Signal at any price up to $24.

The plaintiff proved at trial that the alleged negotiations as to price actually came down to one undated, undocumented phone call between Mr. Crawford and Mr. Walkup, Chairman of Signal. All that Mr. Crawford was supposed to have said was that it was his "feeling" that the price had to be at the upper end of Signal's $20 to $21 range if the outside UOP directors were to recommend the Signal proposal (A1893 Op.).

In the light of the foregoing record, the Court below summarily disposed of the fact that Signal (and UOP) repeatedly represented to the minority that there had been "negotiations" as to the price by holding that all the defendants meant by "negotiations" was "discussions".

Note: The Court below noted that in the Proxy Statement UOP was forced to withdraw the representation that the price had been negotiated, saying (A1927 Op.):

> "Initially, the word 'negotiations' had been used rather than the word 'discussions' in the original draft of the Proxy Statement. However, when the Securities and Exchange Commission sought the details of the 'negotiations' as part of its approval of the Proxy Statement, the term was deleted and the word 'discussions' substituted in its place."

"Plaintiff has his concept of what is meant by the term 'negotiations'. However, his interpretation is not the only one, nor is it necessarily the correct one.

"As defined in _Webster's Third New International Dictionary_, 'negotiate' means:

> 'to communicate or confer with another so as to arrive at a settlement of some matter; meet with another so as to arrive through discussion at some kind of agreement or compromise about something: come to terms esp. in state matters by meetings or discussions'.

"_Black's Law Dictionary_ (4th Ed.) defines 'negotiation' as follows:

> 'The deliberation, discussion or conference upon the terms of a proposed agreement; the act of settling or arranging the terms and conditions of a bargain, sale, or other business transaction'."

The Court below left out the first part of the definition of "negotiations" found in Black's Law Dictionary (4th Ed.):

> "Negotiation is process of submission and consideration of offers until acceptable offer is made and accepted. Gainey v. Brotherhood of Ry. and S. S. Clerks, Freight Handlers, Exp. & Station Emp., D.C. Pa., 275 F.Supp. 292, 300...
>
> "See also Negotiate."

Judge Sheridan held in _Gainey v. Brotherhood of Ry. and S.S. Clerks, Freight Handlers, Exp. & Station Emp._, D.C. Pa., 275 F.Supp. 292 at 300, that "negotiations" means:

> "'Negotiation is a process of submission and consideration of offers until an acceptable offer is made, and accepted'. United States v. John McShain, Inc., 1958, 103 U.S.App.D.C. 328, 258 F.2d 422, 424."

The Court below accepted the defendants' argument that the term "negotiation" is precisely synonymous with "discussions". This is the primary basis of the Court's decision on this point (A1929 Op.).

The Court below does go on to say (A1929 Op.):

> "Here, there were other matters that went into the makeup of the merger agreement other than price. As Crawford indicated at the initial meeting on February 28, 1978, there were employee stock options and incentive programs at UOP to be considered. Some assurance of the future employment prospects of key UOP personnel was also of concern."

Of course, provisions dealing with stock options and incentive plans for UOP executives were terms of the merger agreement but such matters were of no significance whatsoever to the minority shareholders since, by the very merger terms, they were being expelled from the business. To put it another way, the terms of the merger other than the cashout price are totally irrelevant so far as the minority shareholders are concerned. In addition, whether there was arm's length bargaining, negotiations, or merely "discussions" in connection with terms unrelated to the cashout price is also totally devoid of significance so far as the minority is concerned. (Note [1])

The Court then says (A1930 Op.): (Note [2])

> "In short, between February 28 and March 6 there were discussions and deliberations by both

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Note 1: The Court says (A1929 Op.):

> "In addition, as Signal points out, plaintiff conveniently overlooks the fact that UOP's 49.5 per cent minority was comprised of 5,688,302 outstanding shares. Thus the price range initially proposed by Signal of $20 to $21 per share involved a potential swing in the acquisition price of $5,688,302 depending upon whether an agreement was finally reached on the high figure, the low figure or something in between."

The plaintiff did not overlook that "fact". The "potential swing" has nothing to do with the value of the shares of the minority. The important fact is that Signal cashed out the minority at the "<u>conveniently</u>" low figure of $21 -- that is, $3 less than the $24, the price which Signal privately determined it could pay and still make a profit.

Note 2: The Court below said (A1930 Op.):

> "The proposal was made first to Crawford with the understanding that he would submit it to his directors for their reaction. He did so, he discussed it with them on an individual basis, and he then advised Walkup that he thought UOP's board would be receptive provided that the $21 figure was used."

What the Court below finds is further confirmation that there were no negotiations. There is nothing in the record so far as plaintiff knows that justifies the lower Court's finding that the Signal proposal was "privately" disclosed to Mr. Crawford to obtain the reaction of UOP directors. What it does show, however, is that Mr. Crawford was able to represent to Mr. Walkup of Signal what the "independent" members of the Board of UOP would probably do in regard to the Signal proposal (1) before the proposal of Signal was supposedly finalized, (2) before the Signal proposal was presented to the Board of UOP, and (3) before the Board of UOP had met.

> sides, and, to a limited degree, with each other concerning the terms of the merger agreement which was to be submitted to the boards of Signal and UOP on March 6 for their respective considerations."

Actually, as has been shown, the foregoing is not accurate as to the price (the only important matter in a cashout merger for the minority stockholders). As was finally admitted at trial, there was only one single phone conversation between Mr. Crawford and Mr. Walkup in which Mr. Crawford had expressed the "feeling" that Signal had to offer $21 if it wanted the approval of the independent UOP directors (A1893 Op.). That single phone conversation simply will not support the representations made <u>before</u> that single phone call and <u>after</u> that single phone call that Signal and UOP were conducting "negotiation<u>s</u>".

The Court concludes (A1930 Op.):

> "Plaintiff's view is that there can be no negotiation as to price unless one side first demands an amount in excess of the price range initially suggested by the other. But that is not necessarily required by the accepted definition of the term."

The Court below had previously accepted the defendants' view that the "accepted definition" of the term "negotiations" is interchangeable with the word "discussion<u>s</u>". As noted, the plaintiff disagrees; in plaintiff's view, the use of the word "negotiations" in arriving at a price is intended to and does convey the impression of arm's length bargaining with offers and counteroffers. Cf. <u>Abelow v. Symonds</u>, Del.Ch., 184 A.2d 173 (1967), on appeal, <u>Abelow v. Mid-States Oil Corp.</u>, Del. Supr., 189 A.2d 675 (1963); <u>Palley v.</u>

McDonnell Co., Del.Ch., 295 A.2d 762 (1972); Gimbel v. Signal Oil Cos., Inc., Del.Ch., 316 A.2d 399 (1974); Nathan and Shaprio, "Legal Standards of Fairness Under Delaware Law", 2 Del.J.Corp.Law, pg. 44. (Note) Also, to meet the standard of "complete candor", the defendants should, at a bare minimum, have informed minority stockholders that "negotiations" was being used to mean only "discussions". Second, even if one equates "negotiations" with "discussions" and holds that a fiduciary is under no obligation to "bargain" to obtain the best possible result for one's

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Note: When Signal and UOP were negotiating in 1975, and when Mr. Crawford and Mr. Glanville were negotiating on the price for Lehman's fairness opinion, there was arm's length bargaining with offers and counteroffers culminating in an acceptable compromise.

corporate cestui, (Note) the fact remains that Signal top management had originally decided on a price range of $20 to $21, that this range was accepted by Mr. Crawford and the

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Note: Toms, "Compensating Shareholders Frozen Out in Two-Step Mergers", Corporate Practice Commentator, Vol. 22, No. 4, Winter 1981 (Callaghan & Co.), pg. 489:

> "When a shareholder is asked by management to ratify a merger, he is advised by management -- his representative in fiduciary theory -- that the price for the entire company is a good one in light of the future prospects of the company. Guided by management's evaluation, he is less likely to be swayed by his personal circumstances. A shareholder confronted by a tender offer, however, is free of the pressures (and benefits) of the management-negotiated bargain. He can thus be expected to consider the tender offer only in light of his personal situation.
>
> "*** When the shareholder ratifies management's unitary bargain or its appraisal in a self-dealing merger (i.e., where the merger is with a controlling shareholder) he may do so secure in the knowledge that management has a fiduciary duty to bargain for or appraise the company's value on the shareholder's behalf to ensure that, based on all the information, including undisclosed information, in possession of management, the merger price fairly compensates the shareholder for the intrinsic value of his share in the company."

[The footnotes from the above quotation are omitted except footnote 29 which states "Brudney and Chirelstein, Fair Shares in Corporate Mergers and Takeovers, 88 Harv.L.Rev. 297 1974, acknowledge that a shareholder vote, where management controls the proxy machinery, is illusory. Fair Shares, supra, Note 6 at 300, 333. Voluminous literature supports this view. See Compensating Shareholders at 558, n. 29."]

Board of UOP without any "discussions" or any attempt to obtain "one nickel more" or obtain better terms (including a tax-free stock-for-stock transaction) for the UOP minority shareholders.

When measured by the standard of "complete candor", the representations by Signal and UOP in the press releases of February 28 and March 3, 1978, and in UOP's letter to its minority shareholders of March 6, 1978, misrepresented to the defendants that there were "negotiations" between the two of them as to the cashout price was a material fact. (Lynch v. Vickers, supra; Kaplan v. Goldsant, Del.Ch., 380 A.2d 557 (1977).) The fact that the Proxy Statement was changed after the SEC request for details on the alleged negotiations confirms that the defendants realized in fact that there had not been any "negotiations" as to price. The deliberate false impression conveyed by the two press releases and the letter should have been corrected. (Mitchell v. Texas Gulf Sulphur, 10th Cir., 446 F.2d 90 (1971), cert. denied, 404 U.S. 1004, rehearing denied, 404 U.S. 1064, cert. denied, 405 U.S. 918; Berland v. Mack, S.D.N.Y., 48 F.R.D. 121 (1969); SEC v. Great American Industries, Inc., 2nd Cir., 407 F.2d 453, 456 (1968).) The Court below erred in holding that there had not been a misrepresentation on a material fact of great importance to the minority stockholders -- that is, how the price of $21 had been arrived at.

D. The Defendants Misrepresented to the Stockholders, in the Light of the Requirement of Complete Candor That the Lehman Opinion Was Simply That of Mr. Glanville

[The plaintiff incorporates, but will not repeat, the material found in Section I, A, 3.]

E. It Was Misleading to Represent To the Stockholders That the Board of UOP Was Unanimous

The Court below said (A1933 Op.):

> "Finally, although it may be a technical point, I find no material misrepresentation in the fact that the vote of UOP's board to approve the terms of the merger was said to be unanimous. While it is true that not all of UOP's directors voted in favor of the merger due to the fact that five Signal-affiliated directors abstained, it is also true that none of UOP's directors voted against it or offered any opposition to the fairness of the proposal."

The vote of the UOP Board was not unanimous. Five members were advised they could not vote because, since they were also Signal directors, there was a conflict of interest (Chitiea Dep. 55-57). (Note)

The representation that the vote of the Board was "unanimous" was not a "technical" point.

There are certain corporate acts, including a proposed merger (8 Del.C. §251), that require board action before

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Note: Though the Court below overlooked it, Mr. Crawford, both a Signal and UOP director, voted for the Signal proposal. Also, Mr. Pizzitola, a director of UOP, was a partner in Lazard Freres, Signal's investment banker. Mr. Pizzitola voted for the Signal proposal (PX U-7).

submission to the stockholders. These include charter amendment (8 Del.C. §242(c)(1), sale of assets (8 Del.C. 271(a), and dissolution (8 Del.C. §275(a). The reason is obvious: the board is elected by the stockholders to manage their corporation (8 Del.C. §221(b)) and are required to make themselves familiar with the affairs of the corporation. In view of this required familiarity and the fiduciary character of their office, it is obviously material to the stockholders to be apprised accurately of the vote of the board. (Note) To misrepresent that the Board was unanimous when it was not (and could not be because of a conflict of interest) clearly violates the basic canon of "complete candor".

"Complete candor" required the defendants to reveal to the minority frankly and completely all of the material facts relating to the majority cashout merger proposal. Instead, discovery disclosed that a tangled web of omissions, misrepresentations and half truths had been presented to UOP's minority shareholders to get them to vote to approve the Signal cashout merger. The lower Court did not measure

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Note: Signal obviously recognized the importance of representing the alleged unanimity of the UOP Board on Signal's proposal to the minority. The disqualified UOP directors specifically stated on the record how they would vote but for the disqualification. It was then represented that the vote of the UOP Board was unanimous. The reason, of course, was to convince the unsuspecting minority shareholders of UOP that the Board, which had fiduciary responsibilities to the minority, had studied and found unanimously the merger, including the price, fair to UOP's minority.

the defendants' conduct against the standard of "complete candor". Instead, the lower Court itself has tried to explain away the defendants' clear and repeated violations of the standard. Unless this Court is prepared also to abandon or modify the required standard of complete candor, the decision of the lower Court should be reversed.

F. The Court Below Erred in Absolving the Defendants From Their Fiduciary Responsibilities to the Minority Shareholders of UOP

Finally, the Court below, though acknowledging the fiduciary status of the defendants Signal and UOP, exonerates them by holding (A1933-1941):

(1) Corporate fiduciaries who place themselves in a conflict of interest position in a cashout merger are absolved from their responsibility to give their undivided loyalty to the advancement of the interests of the minority: their fiduciary obligation is discharged if at trial they testify that they thought the cashout price was fair.

(2) That a Board of Directors fulfills its obligation to the minority to weigh and consider a cashout proposal by the majority if the record shows that their decision was not made "in a vacuum".

(3) That in evaluating the fairness of a cashout price, the Board will be held to have carried out its fiduciary obligations though they have required no appraisal of the undervalued assets, required no provision for payment of the aliquot share of the second

quarter dividend and made no provision for a general or specific rise of the stock market or the stock of the acquiring company.

1. The Court Below Justified the Defendants' Failure to Fulfill Their Fiduciary Responsibilities to the Minority Because of the Defendants' Decision Not to Resolve Their Conflict of Interest

The Court below says (A1933 Op.):

> "Plaintiff makes many assertions which could be categorized under this aspect of his case. I find the most significant of these contentions to be three in number. First, plaintiff again charges that UOP's board failed to negotiate the merger price offered by Signal, again because it made no attempt to obtain any amount over the high figure of $21 originally proposed by Signal. Secondly, plaintiff says that UOP's board failed to properly weigh and consider Signal's proposal. As to this, he points to the hurried manner in which the board met and approved the merger without first seeking a current appraisal or evaluation of the minority interests. Thirdly, and in relation to this second contention, he claims that UOP's board failed to take into consideration the worth of substantial real estate and patent assets of UOP which were carried on the corporate books at a grossly undervalued figure, that it failed to insist on some provision that would have given the minority the benefit of an overall rise in the general value of stock market securities between March 6, 1978 and May 26, 1978, and that it failed to protect the minority against being deprived of a second quarter UOP dividend, the value of which, in effect, went to Signal as of the time the merger was approved."

(a) A Fiduciary Cannot Fulfill His Responsibilities by Claiming a "Pure Heart"

The Court below recognized that in 1975 Signal and UOP bargained at arm's length in order to arrive at a price at which Signal was able to acquire its 50.5% interest (A1935 Op.):

> "As Signal points out, its position with regard to the merger was completely different than its position in 1975 when it set out to acquire an interest in UOP. In the latter situation, it was in a position to bargain for the best possible deal from its point of view. In attempting to arrive at a price for the tender offer which would not be opposed by UOP, in addition to bargaining on a price for the direct purchase of a large number of shares from UOP, it was in a position to start as low as reasonably possible and, through the give and take process, arrive at the best price possible from the standpoint of its own interests."

Thus, in 1975 when it had no fiduciary responsibility, Signal engaged in arm's length bargaining to achieve the best possible price from its own point of view.

The Court below then indicates that, in 1978, the situation had changed. Because of a conflict of interest, Signal could not engage in arm's length bargaining, saying (A1935 Op.):

> "In 1978, however, as majority shareholder of UOP, it had no similar bargaining position. As Signal readily concedes, (Note) it wore two hats with regard to the acquisition of UOP's minority

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Note: Contrary to what the Court below states, Signal did not "readily concede" at all: it was only in the middle of the trial in connection with its oral Rule 41 motion that Signal first conceded that there had not been negotiations because of the conflict of interest position that Signal (and UOP) were in (TR 998-1001). The novel "pure heart" theory of the defense first surfaced at the trial after it was established that (contrary to pleadings and the assertions of the defendants during their depositions) there had been no "negotiations" (TR 998-1001).

though Signal knew (but did not disclose) the cashout would be profitable at any price up to $24. This "pure heart" theory was not pleaded by Signal: it was first advanced in the middle of the trial in Signal's counsel's argument for a Rule 41 dismissal (TR 998-1001). No legal authority was advanced for the "pure heart" defense by the defendants and indeed the Court below suggests none, presumably because there is no precedent or authority that runs so contrary to this Court's holdings that a majority owes fiduciary responsibilities of the highest order to the minority when the majority is seeking to expel the minority by a cashout merger. Thus, the Court below has adopted a new and radical doctrine that drastically changes the fiduciary responsibility of the majority in a cashout merger.

The Court below not only absolved Signal, the majority stockholder, of its fiduciary responsibilities but also absolved the UOP Board. UOP's Board did not have to advance the interest of the minority: all they had to do was to act "reasonably" (A1936 Op.):

> "Thus, if UOP's board, after reviewing the matter, was convinced that the high end of the proposed price range was fair and reasonable to the minority, then its failure to seek a still higher price did not, of itself, constitute a breach of its fiduciary duty owed to its minority shareholders."

Thus, the lower Court again required only a "pure heart" in place of demonstrated adherence to standards of fiduciary responsibility. There was no disclosure to the minority that their Board of Directors, because of a conflict of

> interests. As majority shareholder, it owed a fiduciary duty of fairness to UOP's minority. It could not start at a price below that which it truly felt to be the fair value of UOP's shares and bargain upward. At the same time, Signal's board owed a fiduciary duty to its own shareholders in dealing with Signal's assets. Thus, it had to take care that it did not propose to pay more than was fair and reasonable for the UOP shares."

There are several comments on the foregoing statement. In the first place, this "delicate" situation was not disclosed to the minority shareholders: on the contrary, it was repeatedly represented to the minority that there were ongoing negotiations as to price. Second, if the Court below is right, then the majority (which always has responsibilities to itself, i.e., its own shareholders), will never be in a position to carry out its fiduciary responsibilities to the minority shareholders whom it seeks to displace in the joint enterprise. Furthermore, Signal deliberately preferred its own interest by selecting $21 as a "fair" price though Signal knew from its own "studies" based on inside information that it had received on UOP's present and future financial situation that $21 was $3 less than the $24 which Signal could profitably pay for the minority's shares. Signal never disclosed this material fact to the minority shareholders of UOP (A1888).

The Court below accepted this self-serving "two-hat" justification: it held in effect that Signal had completely fulfilled its fiduciary responsibilities to the minority simply by stating that it thought the $21 price was fair interest, was not operating under corporate fiduciary principles but was simply trying to act "reasonably". From the point of view of a cashout minority stockholder, what he wants and expects is the maximum price that can be obtained by a resolute and intelligent negotiator acting on his behalf in arm's length bargaining. In other words, he expects and is entitled to the same rigorous advancement of his interest by arm's length bargaining as occurred when Signal and UOP engaged in negotiations in 1975.

The solution to the conflict of interest, as the Court below seems to recognize (A1937 Op.), was the appointment of a truly independent committee of the UOP Board charged with the responsibility of carrying out the task of representing the interest of the minority. In Harriman v. E. I. DuPont de Nemours, D.Del., 411 F.Supp. 133 (1975), the affairs and personnel of DuPont Company and Christiana Securities were hopelessly entwined. However, Judge Schwartz noted that prior to the outset of negotiations, the following took place (pg. 142-3):

> "Merger negotiations between Du Pont and Christiana were initiated in late April of 1972 when Christiana's President, Irenee du Pont, Jr., sent a letter dated April 20, 1972, to C. B. McCoy ('McCoy'), then President and Board Chairman of Du Pont, suggesting that a merger between the two entities would be advantageous to both parties. As a result Du Pont agreed to consider such a merger.
>
> "Prior to the start of negotiations the Christiana and Du Pont boards took two basic steps prompted by the extremely close historical relationship and interlocking directorates of the two

> companies: The appointment of special negotiating committees composed of persons unconnected with the opposing negotiating party and the retention of three investment banking firms to provide financial advice with respect to valuations to be employed during negotiations and the fairness of any proposed merger terms.
>
> "The Du Pont board named McCoy and Irving S. Shapiro ("Shapiro"), then Senior Vice-President and a Director of DuPont as its negotiating committee. Christiana similarly designated a two-man board composed of A. Felix du Pont, Jr., a Christiana Vice-President and Director, and E. B. du Pont, its Assistant Treasurer and also a Director. Du Pont and Christiana jointly retained Morgan Stanley & Co. ("Morgan Stanley"), an investment banking firm, as a financial advisor in connection with the merger. Morgan Stanley had previously assisted both of the merger parties. Christiana and Du Pont each then retained separate financial advisors, choosing Kidder, Peabody & Co., Incorporated ("Kidder Peabody") and the First Boston Corporation ("First Boston") respectively. Neither Kidder Peabody nor First Boston had any prior significant relationship with either of the merger parties."

(See also Vice Chancellor Brown's unreported opinion, Casella v. GDV, Inc., No. 5899 (Sept. 13, 1978), a copy of which is attached, marked Exhibit "A".)

Turning back to the decision of the lower Court (A1936 Op.), the offer of the "high end of the range" was not a result of UOP Board consideration or action. Signal agreed to pay $21 before the UOP Board meeting as a result of a single phone conversation between Mr. Crawford (himself a Signal director and committed to the position that Signal's entire offering range was "generous") and Mr. Walkup, the Chairman of the Board of Signal.

(b) The Measure of the Actions of UOP's Board is Whether It Carried Out Its Fiduciary Responsibilities, Not Reasonableness

The lower Court then says (A1936 Op.):

> "Thus, the true focus must be on the reasonableness of the action taken by UOP's board in considering the proposal, and not on its failure to seek a higher price than that suggested."

The plaintiff does not believe that the lower Court's "focus" is correct. Even if it is, the record shows that the consideration by the UOP Board was not "reasonable". The Court below stated as much, saying (A1936 Op.):

> "On this point, plaintiff makes perhaps his strongest showing. UOP's board did act on three business days' notice. It did not seek an independent appraisal of the current value of UOP's shares before acting, and the expedited scheduling of its meeting on March 6 was obviously within the control of Signal."

The Board of Directors has a continuing responsibility to the shareholders to manage the company. As previously noted, under Delaware law, certain corporate matters, including a merger, can only come before the shareholders after action by the Board of Directors. Gimbel v. Signal, Del.Ch., 316 A.2d 599 (1974), holds, a board must act with that degree of deliberation and prudence that is commensurate with the importance of the transaction in question. Kaplan v. Centrex, Del.Ch., 284 A.2d 119 (1971). Where, as here, the transaction in question is a cashout merger of the minority by the majority, in depth consideration by the Board of the fairness of all the terms, but particularly the cashout price, is of paramount importance to the protection and well-being of the minority shareholders. As the lower Court notes and the record confirms, the record shows that the Board of UOP did not give the matter any in depth deliberation: the Board had no advance notice of the terms of the merger, the Board made no demand for the time necessary to give themselves an opportunity for mature consideration of the important matter at hand, the Board did not ask for an appraisal of the current values (as opposed to the book or depreciated value of the assets of UOP, including UOP's vast unused timberlands), and the Board did not refer the matter to a totally independent committee nor did the Board demand a stock-for-stock transaction, though they knew that a cashout merger would impose capital gains consequences for the minority stockholders. (See Lewis v. Great Western United, Del.Ch., No. 5397 (Sept. 15, 1977), 3 Del.J.Corp.Law 583 (unreported decision, a copy of which is attached marked Exhibit "B"). The UOP Board raised no question as to why the merger had to be approved forthwith at the meeting of March 6, 1978, or what justification there was for UOP to agree to Signal's haste. The record shows that the UOP Board met only very briefly and then, without any record for its reasons for approving the merger, simply "rubber stamped" the proposal of the majority for a cashout merger of the minority stockholders.

The lower Court says (A1936 Op.):

"Moreover, I am satisfied that the primary factor considered by those concerned was the comparison of Signal's 1978 proposal with the situation prevailing at the time of the 1975 tender offer."

Signal, UOP's directors and Lehman Brothers' principal justification for the $21 price was because of an alleged similarity between certain of UOP's 1975 and 1978 financial figures. However, the question for these corporate fiduciaries was not the similarity of certain UOP financial figures in 1975 and 1978 but the value as of the time of the proposed cashout merger of the minority's shares. Neither Signal nor UOP's Board nor its management ever had an evaluation made of the value of UOP's shares or even suggested one be made. Lehman's one-page "backup" (PX LB-5) which (incidentally, was not furnished to the UOP directors) is simply just such a comparison. A comparison between the 1975 figures with the 1978 figures is not a measure of the value of the minority's shares in 1978. Nor is the fact that a tender offer to the 1974-75 owners of UOP appealed to 77% of them significant in terms of the value of the shares in a cashout merger of the 1978 owners. The foregoing is especially so since between 1974 and 1978, there had been a heavy turnover in UOP shares: the 1978 owners of UOP stock were obviously not the same persons who had owned shares of the common stock of UOP in 1974 (TR 1705). In addition, as previously noted, the fortunes of UOP were significantly different in 1978 from those in 1975 (PX 11, Trial). The financial consequences of the Come-By-Chance Refinery matter was not known in 1975: in 1978, it was an event in the past. The present situation and future prospects for UOP were much brighter than they had been in 1974-75 when UOP badly needed leadership, cash, etc. (Note)

The Court below says (A1937 Op.):

> "I think it is fairly clear that these factors, taken in conjunction with the financial information available and made available to the independent members of UOP's board as well as the fairness opinion supplied by Lehman Brothers, caused the general feeling to be that if $21 per share was an unnecessarily high price to have paid in 1975, it was a fair price to pay for the minority shares in 1978 under comparable circumstances."

There is nothing in the record that justifies this statement that it was "fairly clear" that there was any such general feeling on the part of UOP's Board. In addition, as previously pointed out, the corporate fiduciaries could fulfill their duty to the minority (not by having a "general feeling" as to what was fair) but in determining by a mature consideration (with professional help, if necessary) what the value of the minority shares was in 1978.

Note: Of course, the future prospects of UOP after the merger are not a factor in determining the value of the minority shares in a statutory appraisal (8 Del.C. 267). However, in the real world, the bright future prospects for UOP, if disclosed, would be of key concern to stockholders and prospective investors. Therefore, in any realistic determination of value, the future prospects of UOP was an important factor in determining the true value of the stock. The record shows that Signal looked carefully at what the future held for UOP in coming to its decision to cash out the minority.

The Court concludes (A1937 Op.):

> "While there are different ways to approach the same problem, and while plaintiff would urge that a different approach than that taken by UOP's board should have been required (i.e., a separate committee to weigh and evaluate the matter), I cannot find on the evidence that UOP's board failed to properly weigh and consider the transaction with regard to the interests of the minority shareholders. It does not appear that they were operating in a vacuum."

The Court below has squarely placed the burden on the plaintiff to prove that UOP did not carry out its fiduciary responsibilities to the minority. Actually, under Singer, it was up to the defendants to prove that they did carry out their fiduciary responsibilities by considering and evaluating the proposed merger rather than simply "rubber stamping" what was presented to them by the majority stockholder. The fact that the Board is found not to have considered the matter "in a vacuum" does not satisfy the fiduciary responsibilities that a board has in protecting a minority from the avaricious designs of a majority who, for its own economic advantage, seeks to cash out the minority.

2. The Lower Court's Justification of the Failure of the Board to Have an Appraisal Made of UOP's Undervalued Assets Based on Sterling is Misplaced

The Court below says (A1938 Op.):

> "In this regard, plaintiff asserts that UOP has some 270,000 acres of timberland which is carried on its books at an acquisition price averaging some $38 per acre. He also says UOP has valuable patent and royalty interests which were not carried on its books at a true present value."

Since Signal would be acquiring these assets as a result of obtaining total ownership of UOP, UOP's Board should have insisted that a current appraisal be made to determine the current market value of these assets. (Note) Signal claims to have paid a fair price for the income producing assets of UOP: it also got the non-income producing assets (land, and timber) as a "plum" since no appraisal was made to determine their fair value or the market value (TR 264, 1179; PX U-1-29, Appendix D). Nothing was included in the $21 price for this windfall (TR 269). The timberlands were not contributing to UOP's income stream (TR 266-268). Thus, a one hundred percent owner, such as Signal, would be free after the merger, without affecting the income stream, to sell these assets, entirely for its own profit. On the other hand, Signal could, if it chose, continue to hold these undervalued assets as an investment (A266). UOP's minority shareholders were entitled to a fair share of these non-income producing, undervalued assets (A268). UOP also owned 3,045 U.S. patents and 6,032 foreign patents (A493). These were contributing to UOP's income stream but were carried at almost nominal value ($2,285,000.00) on UOP's

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Note: Assets such as land, buildings, equipment, are normally listed at historical cost minus depreciation. See L. Rappaport, SEC Accounting Practice and Procedure 3.24-3.32 (3d Ed. 1972), but that practice has been criticized as unduly misleading in situations such as going private transactions in which the current actual value of a company assumes great importance to the minority shareholders. See A. Bromberg, Securities Law: Fraud §6.5 (1977 Supp.).

balance sheet (A494).

The Court below found that no appraisal was made by the Board of the undervalued assets of UOP (A1938). The Court below justified the failure of UOP's Board to obtain such an appraisal, relying on Sterling v. Mayflower, supra, saying (A1939 Op.):

> "The effect of this finding is that the failure of Mayflower's board to consider net asset value in agreeing to the merger terms did not constitute a breach of the fiduciary duty owed to Mayflower's minority where a subsequent review of that element by the courts indicated that it would have made no difference. As stated by the Supreme Court at 93 A.2d 116:
>
> > "'In these circumstances we deem the evidence adduced by the defendants upon the issue of comparative net asset value to be sufficient to discharge whatever duty they were under in respect of the matter; and this notwithstanding the inconclusive nature of the "indicated values" arrived at [in the report].'"

In Mayflower, the Mayflower Board was found to have considered comparative net asset value. This Court confirmed that their consideration was sufficient. In the present case, the UOP Board gave no consideration whatsoever to the understated values of UOP's assets. But the lower Court did not make any such finding. Rather, the lower Court concluded (A1939 Op.):

> "Thus, the failure of UOP's board to obtain and consider the updated value of UOP's timberland and patent and royalty assets does not constitute a breach of its fiduciary duty to the minority if the evidence presented on behalf of the defendants at trial reveals that the value of such assets had no material bearing on the fairness of the terms of the merger. For the reasons set forth hereafter, I find such to be the case, and thus I find no impropriety chargable to UOP's board in this respect."

One has to turn to the lower Court's discussion of the analysis made by defendants' trial expert, Mr. William Purcell, in April, 1980, to find out what is referred to in the underlined portion of the lower Court's opinion. The lower Court said (not in connection with what the UOP Board did) but, in connection with Mr. Purcell's appraisal analysis (A1957 Op.):

> "The net asset value or book value was $19.86 at year-end 1977 and $20.69 as of the end of the first quarter 1978. Net asset value was given little weight [by Mr. Purcell, not by the Board of UOP], however, in view of the fact that Signal was acquiring UOP for its ongoing business value and since there was no plan for its liquidation. I agree with this conclusion on the evidence. It corresponds with the finding in Sterling."

Thus, though UOP's Board did not consider, much less have a valuation made of the undervalued assets of UOP in 1978, the lower Court justifies UOP's Board's failure to do so by finding that, in the 1980 appraisal analysis made by Mr. William Purcell for trial, since Signal was not going to liquidate UOP, no weight should be given to net asset value. While it may be true that net asset value is not significant in an appraisal analysis (8 Del.C. §262) except in the case of liquidation, that is clearly beside the point in a determination as to whether the UOP Board should have had an appraisal made of its undervalued assets in 1978. Signal was buying UOP as a going concern: therefore, the measure of its worth was on a going concern basis (i.e., the value of its income producing assets). So far as the timberlands were concerned, they were non-income producing assets:

i.e., they did not contribute to the income stream. The minority shareholders were entitled to their share of the value of these non-income producing, undervalued assets, not on the basis that the UOP company was going to be liquidated but on the basis that these non-income producing assets were undervalued. Signal obtained all of UOP's undervalued assets in the cashout merger of the minority. It could sell these without affecting the UOP income stream, or retain them as an investment. The minority was entitled to its fair share of the undervalued timber and lands (and the fair value of UOP's patents and royalties).

G. The Court Below Erred in Holding That UOP's Board Had Not Violated Its Fiduciary Obligation In Not Providing An Escalation Provision and In Voting To Give the Entire Second Quarter Dividend to Signal

The announcement of Signal's cashout merger at $21 put a "cap" on the price of UOP stock (A1940). The price of Signal rose dramatically between February 28, 1978, and May 26, 1978 (i.e., from $28 to $39) (Purcell Dep. 221). (Note) The market as a whole rose 13% (A1939). There was no escalation provision in the merger agreement to reflect the price rise in what was paid to the UOP minority (A87-90): the price rise redounded solely to the benefit of the majority

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Note: The spectacular upsurge in Signal's stock was unexplained by Signal. It can only be accounted for by recognition in the marketplace of Signal's very favorable acquisition of the minority's equity interest in UOP.

stockholder. Yet, the lower Court holds that it is "speculation" as to whether UOP's shares would have risen as did the market generally, saying (A1940 Op.):

> "It is true that the approval of the $21 merger price by the boards of UOP and Signal on March 6 put a 'cap' on the value of the UOP shares. But whether they would have otherwise increased or decreased during the two and one-half month period thereafter is a matter of speculation."

The plaintiff has been put in an impossible situation: the action of his corporate fiduciaries has precluded ever knowing definitely whether UOP would have done what the stock market did generally -- that is, rise by 13%. Because his corporate fiduciaries have put a "cap" on the price of the UOP stock, the plaintiff could not prove that the UOP stock would have risen as the market did generally (and Signal stock did). Then the lower Court holds that it is "speculation" as to whether the UOP stock would have risen generally.

Even more draconian is the lower Court's dismissal of the fact that the Board of UOP, the minority's corporate fiduciaries, did not insist on a provision for the allocation of the second quarter dividend. On the contrary, when the time for the dividend came, they simply voted to give it all to Signal. The lower Court does not even suggest any basis for approving the UOP Board's decision to give the majority shareholder the minority's dividend. (A1940 Op.):

> "As to the fact that the merger agreement made no provision for UOP's minority to receive an aliquot share of any second quarter dividend, the defendants have advanced no real argument or

explanation. I can only assume that in view of the price being offered and the right being given to the minority to reject the entire proposal, it was not considered by either board to be a necessary term or item for inclusion in the merger agreement." (Note)

* * *

The Court below has imposed the burden of proof on the plaintiff to show that the defendants carried out their fiduciary responsibilities to the minority. It does more than that: it justifies the defendants' failure to carry out their fiduciary responsibilities by saying that they were fully justified in not doing so because of the conflict of interest that they placed themselves in. The lower Court recognizes that certain of UOP's assets were undervalued: it glosses over UOP's Board's failure to obtain an appraisal on the basis of the appraisal determination made years later for trial by defendants' expert rather than on the basis of what UOP's Board did. The Court below dismisses plaintiff's claim that the Board of UOP should have provided for escalation by holding that (since the market was capped and plaintiff can not definitely prove that UOP's shares would have

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Note: The lower Court's cavalier dismissal of the minority's right to their share of the second quarter dividend is in stark contrast to its treatment of Signal's \$20-\$21 price range. To use a phrase that the Court below used, the Court "conveniently overlooks" the fact that the first quarter dividend amounted to 20 cents (A32). The minority shareholders' aliquot share of a second quarter dividend in the same amount would have been about 15 cents per share. This means an additional \$863,245.30 that UOP's Board gave to Signal, the majority stockholder.

risen as the market did and as Signal's stock did) it was speculation as to whether UOP stock would also have risen. Finally, the Court below countenances UOP's Board's giving of the second quarter dividend entirely to Signal without any explanation.

The Court below should be reversed with further clear directions as to what is meant by the carrying out of fiduciary responsibilities in a cashout merger by the majority of the minority.

III. IN SPITE OF THE APPLICABLE LAW, THE COURT BELOW HAS ADOPTED STATUTORY APPRAISAL AS THE SOLE TEST OF INTRINSIC FAIRNESS OF A CASHOUT MERGER

As in the liability section, the lower Court began its opinion by stating its view of the law governing the determination of the fairness of the price for stock of the minority in a cashout merger. The Court below disregarded a part of the plaintiff's expert's testimony and rejected, based on an apparent misunderstanding, a well-known method of evaluating the worth of UOP (i.e., the discounted cash flow method). Purportedly on the basis of Sterling (a stock-for-stock rather than a cashout merger), the lower Court concluded that the defendants had sustained their burden of proving the intrinsic fairness of the 1978 cashout merger by retaining and calling a trial expert whose solitary calculation was made under the rigid restrictive limitations of a statutory appraisal as provided for in 8 Del.C. §262 coupled with a palpably erroneous calculation of premium.

A. The Decision of the Lower Court Is Contrary to the Court's Decision in Lynch

Since the filing of this appeal, the en banc decision of this Court in Lynch v. Vickers, No. 105, 1979 (hereafter Lynch, Supr. II), has come down. When measured by Lynch, Supr. II, the decision of the lower Court was incorrect in holding that the determination of whether the merger was intrinsically fair is to be determined by the standards of the appraisal statute (8 Del.C. §262).

The plaintiff recognizes that the decision in Lynch, Supr. II was procedurally at a different stage from the present case. The lower Court was determining whether the price of $21 met the test of intrinsic fairness set out in Singer, supra, and Tanzer, supra. In doing so, the lower Court rejected all the plaintiff's experts' various methods of determining worth and accepted the defendant's trial expert's single calculation based on the appraisal method (8 Del.C. §262). Lynch, Supr. II reverses the Court of Chancery's actual determination of damages. However, the significance of Lynch, Supr. II is that this Court has held that, in a cashout merger, the appraisal standard is not appropriate in a determination of the worth of the minority's stock. (Of course, if appraisal were the sole measure in a determination of intrinsic fairness worth, then Singer and the cases since then are an exercise in futility because, without the cost, risk and expense in proving liability, any dissatisfied stockholder can simply petition for appraisal.) Singer, supra, held a cashed out stockholder can not be relegated to appraisal. Lynch, Supr. II is not only applicable in measuring the actual damages but is applicable in determining intrinsic fairness.

This case should be remanded to the Court of Chancery for a determination of intrinsic fairness and the actual damages suffered by the minority in the light of the holding of this Court in Lynch, Supr. II. However, in view of the approach the Court below has taken, this Court should give the lower Court further specific guidance on the rehearing that should be ordered in this case. As a starting point, it should be noted the plaintiff prayed for rescission or, in the alternative, for rescissionary damages in the Amended Complaint (A374):

> "(1) That the Court enter an order enlarging the class to include all outside stockholders of UOP as of May 27, 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 remedy of choice from the outset has been rescission -- i.e., the return of the UOP stock Signal appropriated in the cashout merger. This Court said (Lynch, Supr. II, pg. 9):

> "Rescission is the preferable remedy and if the controversy in its present form had been here and in early stage of the litigation, it might well be ordered."

The Court below should first determine whether rescission is possible. If rescission is not possible, then, pursuant to equity principles, the Court below should fashion a remedy that is as closely akin to rescission as possible -- that is, the Court below should order Signal to issue its own shares to UOP's stockholders who were cashed out (with, of course, a credit for the $21 paid and interest to date) and with a cash alternative.

In Lynch, Supr. II, this Court found that rescission was not possible and, therefore, stated that rescissionary damages should be awarded (Lynch, Supr. II, pg. 13):

> "Specifically, we hold that Vickers will be required to pay rescissionary damages to the plaintiff measured by the equivalent value of the Transocean stock as of the time of the judgment."

The Court's footnote says:

> "Compare the well settled law that entitles a beneficiary to claim all advantages actually gained by a fiduciary as a result of a breach of trust, 4 Pomeroy's Equity Jurisprudence (5th Ed.) §1075; 3 Scott, The Law of Trusts (3rd Ed.) §205; Bogert Trusts and Trustees (2nd Ed. Rev.) §543 (V). That standard has been applied to corporate affairs and directors in this state, Singer v. Magnavox, Supr.; Goth v. Loft, Inc., Supr."

If rescission in any form is not possible, then the Court below should determine rescissionary damages. (Note) It should be made clear that rescissionary damages are not measured by the criteria applicable to an appraisal under 8 Del.C. §262. Rather, damages are measured by the value of the stock Signal wrongfully obtained. The Court below in this case specifically rejected such measure (A1950 Op.).

Note: In Lynch, Supr. II, the Court considered and rejected the defendant's contentions on mitigation. No question about possible purchase of Signal stock on the part of the plaintiff class arises in this case since the defendants never have admitted, much less corrected, their misrepresentations.

In this case, the discovery showed that Signal had determined that it could profit from the acquisition of the minority shares at any price up to $24. The Court below should be directed to commence with $24 as the monetary price that should have been paid for the minority stock and then add interest, costs and attorneys' fees.

The plaintiff believes that Lynch, Supr. II, in itself conclusively demonstrates that the lower Court's view of the standard by which intrinsic fairness and damages in a cash-out merger is incorrect and requires reversal. Nevertheless, the plaintiff will go forward and show why even before Lynch, Supr. II was handed down the decision of the Court below was wrong on the measure to be applied in determining intrinsic fairness and damages in a cashout merger.

B. The Court Below Erred In Accepting the Defendants' Expert's Erroneous Calculation of Premium

In a merger, premium is the difference between the merger price and the market price. Premium is the amount that a buyer gives (and sellers receive) for the acquisition of the attributes of one hundred percent control (i.e., dividends, voting, future conduct of the business (A864 Bodenstein)). Toms "Compensating Shareholders", supra, pg. 492.

Adequacy or inadequacy of premium in a given merger can be determined by measuring the percentage of premium as against percentage premium in other mergers of comparable size at the time in question (A836-891 - Bodenstein).

The plaintiff's expert and the defendants' expert measured the percentage of premium paid by Signal against the percentage of premium in comparable mergers to see whether Signal in paying $21 was paying a premium that was comparable to the percentage premium paid in cashout mergers of comparable size at the time in question. The Court below described the method used by plaintiff's expert, Mr. Kenneth Bodenstein, C.F.A., to calculate the premium as a percentage of the merger price (A1943 Op.):

> "Against this background, Bodenstein conducted a comparison of the premium over market being paid within a related time frame for mergers or tender offer-merger combinations which resulted in 100 per cent ownership to the acquiror and in which the cost of acquisition was $100 million or more. This was to use transactions comparable to Signal's acquisition of the remaining minority interest of UOP.
>
> "Bodenstein selected ten such comparable transactions. <u>As to each he found what he termed a prior market price. In some, this was the market price on the day preceding the first announcement of the transaction. As to others he examined price and volume figures for a period of time prior to the announcement so as, where appropriate, to factor out any distortion in the otherwise prevailing market price that might have been caused by leaks, market premonition of an impending acquisition, etc. -- "noise" as described by Bodenstein.</u>
>
> *   *   *
>
> "Bodenstein thus concluded that a reasonable premium for Signal to have paid so as to become 100 per cent owner of UOP would have been between 70 per cent and 80 per cent."

The Court later described the premium calculation made by Dillon, Read. In each case, Dillon, Read used the day before the formal announcement of the merger without any attempt to factor out distortion caused by leaks or market premonition (A1957 Op.):

> "With regard to the premium, the comparable acquisition transactions selected by Dillon, Read <u>(as to which it used the price on the day preceding the acquisition announcement in all cases)</u> indicated an average market value premium of 48 per cent and a median premium of 41 per cent. At the merger price of $21 paid by Signal, the premium paid over the closing market price of $14.50 on February 28, 1978 was 44.8 per cent."

The plaintiff's and defendants' experts used some of the same merger transactions to measure premium (DX 40; PX 3, Trial; PX 6, Trial). The radical disparity (70-80% vs. 41%) stems from the fact that Mr. Purcell, the defendants' expert, did not have his subordinates, Mr. Daum and Mr. Reid (A1062) screen out "noise": rather, they simply calculated premium based on the difference between the cashout price and the market price on the day of the formal announcement (A1349; DX 40; PX 6, Trial). The difference is obviously significant: where the market has anticipated a merger (either intuitively or through rumors or leaks) as reflected in volume and price increases, the difference in the "market" price and the cashout merger price would obviously be much less. The plaintiff's expert, Mr. Bodenstein, made a complete analysis of each of the transactions used by the defendants' expert to document those where the record of price and volume showed there had been "noise" (i.e., leaks, rumors or market premonition of the merger) that made the day before the announcement a false starting point in measuring premium (PX 6, Trial). PX 6, Trial was admitted in evidence before defendants' expert testified: he simply "stone-walled" on the point (A1238-1261 - Purcell).

The Court below understood (A1261) and accurately delineated the difference in methodology (albeit in separate places in its opinion). However, without any explanation whatsoever, the Court below simply accepted the defendants' expert's opinion that Signal's offer was fair based on an erroneous method of measuring the percentage of premium (A1959 Op.).

The acceptance by the Court below of defendants' premium analysis is not a minor anamoly or oversight: Mr. Purcell was the defendants' only witness on the fairness of the price of $21. (Note) Mr. Purcell used one and only one method to justify the $21 price that Signal had paid. After using strictly conventional appraisal methods, Mr. Purcell purported to measure the percentage of the premium Signal had paid against the percentage of premiums paid in other mergers. Based on this erroneous calculation, he added the

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Note: The defendants, as has been noted, did not call Mr. Glanville or any Lehman employee at trial. However, when all is said and done, an examination of Mr. Purcell's superficially elaborate report boils down to the same rough and ready calculation made by Mr. Glanville in the first week of March, 1978. Mr. Purcell, by use of the appraisal method, calculated that the value of UOP's minority stock was about $14.50 to which he added a 44.8% premium (A1757).

premium to his "appraisal" analysis and concluded that the price of $21 was fair. In other words, Mr. Purcell's failure to have premium measured accurately (by screening out "noise") vitiates not only the defendants' calculation on premium itself but eliminates entirely the only evidence presented by the defendants on the intrinsic fairness of the $21 price.

C. The Court Below, in Rejecting the Plaintiff's Expert's Analysis, Did So Based in Part on Misunderstanding and in Part on a Misconception of the Appropriate Damage Standard

The Court below notes (A1944 Op.) the fact that the plaintiff's expert did a series of comparative analysis to determine value of the minority shares (A1944 Op.). By these comparisons, Mr. Bodenstein showed that the value of the minority shares was not less than $26 (PX 3, Trial; A854-891). The lower Court apparently disregarded what this evidence showed by making no further mention of the plaintiff's expert's comparative analysis or what it disclosed. The Court below not only rejected the foregoing but rejected all evidence of value based on the discounted cash flow method, even though (1) the discounted cash flow method was recognized by defendants' trial expert as a valid method of determining the value of one hundred percent of a business (A1047-49 Purcell), (2) it is a method used by buyers and sellers in the business world (A1047 Purcell), (3) is explained in Graham and Dodd (A1050 Purcell), and (4) was used by Haskins & Sells in valuing the UOP patents Signal acquired (PX 300, pg. 35). The plaintiff's expert confirmed through the application of the discounted cash flow method to 1977, 1978 and UOP's own 5-year forecast that the value of the minority shares was not less than $26 per share (A1948).

The Court below first rejects the discounted cash flow method based on errors as to what the record shows. For example, the court below says (A1947):

> "To begin with, the evidence indicates that there were reasons for UOP's cash status. Some §37 million of the cash accumulation reflected payments advanced on contracts by its customers and thus was not money that could be removed from the company. Also a great deal of it had been advanced to UOP's foreign units and thus was subject to exchange control restrictions of foreign governments. It was not necessarily free for removal at will by a 100 per cent owner as Bodenstein's analysis presupposed."

The Court is simply incorrect on what the $37 million of "excess liquidity" in the "UOP Cash Flow - 1977" (PX 4, Trial) represents. As Mr. Bodenstein made clear at trial, the entry entitled "Excess Liquidity" is represented $50-60 million of cash (reduced to $37 million to be conservative) beyond working capital needed to produce UOP's income stream (A737-740). There is simply nothing in the record to show that the $37 million of Excess Liquidity was reflected in payments "<u>advanced</u>" on contracts by its customers. (Note) Furthermore, the first year as to which the discounted cash flow method was applied was 1977. The year

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Note: The genesis of the Court's idea that the $37 million is an advance by customers or is somehow tied up in foreign exchange comes not from the record but from the Defendants' Post-Trial Brief, pg. 105.

in question was 1977, a closed year: customer advances and restrictions would have no applicability in a closed year.

Another example: the lower Court also misunderstood how the discount factor was calculated. The Court below says (A1947 Op.):

> "In addition, as defendants point out, the discounted cash flow analysis has at its core the fortuitous selection of a discount factor which is not necessarily related to any objective standard. This is illustrated by the discount factors utilized by Bodenstein in his 1977 analysis: one being the 'high side' of the 'discount range' found in a sample of 1977-1978 selected acquisitions; the other being Moody's Industrial Bond yield average for the month of February 1978." (Note)

The quotation itself above shows that the selection was not "fortuitous" at all. Rather, Mr. Bodenstein has utilized two sets of transactions that the market itself had <u>used</u> in determining what to pay for income streams on a retrospective basis (i.e., in 1977). That the Court below simply did not understand the evidence is shown by what it goes on to say (A1948 Op.):

> "Presumably, other analysts might choose to use any number of other points of reference in trying to calculate an appropriate return on investments to be applied as a discount factor."

Mr. Bodenstein did not simply pull points of reference "out of the air" for his discount factor: he used and explained discount factors based on what the market had done in the

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Note: The source of the Court's error in suggesting that the selection of the discount factor is not necessarily related to any objective standard is again the Defendants' Post-Trial Brief, pg. 106.

year 1977 in this connection (A731-737). (Note)

A final example where the lower Court placed mistaken reliance on the defendants is illustrated by the following (A1948 Op.):

> "As defendants also point out, an adjustment in the discount rate to be applied can dramatically change the end result. For example, for the first two months of 1978 UOP's stock had averaged trading for just under $15 per share. For the year 1977, its earnings from continuing operations had been $2.12 per share. This equates to a price/earnings ratio of approximately 7:1, which thus represents a return of about 14 per cent. In other words, it could be argued that immediately prior to the merger announcement the market was willing to pay about $15 for a share in UOP in order to get a 14 per cent return of $2.12 per share. If one selects this as a basis for using a discount rate of 14 per cent, and uses all other figures contained in Bodenstein's 1977 cash flow analysis, the value per share becomes $16.81."

The lower Court has mistaken (based on the Defendants' Post-Trial Brief, pg. 106) earnings with free cash throw off. The stockholders of UOP did not receive $2.12 per share: rather, they were receiving 80 cents in annual dividends (PX U-7). On a market price of $14.50, a dividend of 80 cents represents a 5.5% yield. If a 5.5% discount factor were used (rather than what the market actually paid) the results from the discounted cash flow method as applied in 1977 would be far higher. The lower Court then applied its

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Note: The Court below does not seem to realize that the comments about the "fortuitous" nature of the discount factor is more applicable to the P/E ratios utilized by Mr. Purcell in his appraisal calculations (i.e., value of UOP was "probably in the range of 6.5 to 7.0 times its 1977 earnings") (A1957).

mistaken view of the discounted cash flow method to Mr. Bodenstein's 1978 analysis.

The foregoing is only a sample of some of the manifest errors of the Court below in connection with what the evidence showed the value of the minority shares to be when analyzed using the discounted cash flow method. The source of this error stems from the fact that the Court below simply accepted (as the lower Court frankly stated) the defendants' position as stated in the Defendants' Post-Trial Brief, rather than examining the voluminous trial record and the illustrative exhibits. However, the real reason for all the foregoing lies in the fact that the Court below totally rejected the concept and the approach that is the rationale lying back of the discounted cash flow method (i.e., to determine the present and future value of the enterprise as a whole, in order to determine just what the acquiror (Signal) obtained and what the minority was deprived of). The lower Court stated (A1949 Op.)

> "Thirdly, I have difficulty with the entire concept employed by plaintiff's expert. As noted previously, it is viewed from the standpoint of the value of a share of UOP to Signal, (or to any majority shareholder in a similar situation) because of the fact that the acquisition is transforming it into the 100 per cent owner of its subsidiary. Thus, as I perceive it, plaintiff seems to be arguing that in order for the transaction to be fair to UOP's minority shareholders, they must be paid the value of the stock to Signal. And this would appear to be in contrast to the value of a share of UOP in the hands of all shareholders as of the time of the merger."

The short answer to the foregoing is found in this Court's opinion in Lynch, Supr. II in which this Court has held that the correct measure of value is the value of the stock in the hands of the acquiror. The Court below makes it perfectly clear that it holds a view contrary to the one that this Court has announced in Lynch, Supr. II (A1950 Op.):

> "Thus, plaintiffs seems to be suggesting that in evaluating the fairness of the merger terms to the minority in such a proceeding as this, one must look to what it is reasonably worth to the former majority shareholder to be rid of all other shareholders so as to become the sole owner of the enterprise, and then, using that as a basis or starting point, determine what is a fair amount for it to have paid the minority for the right to become sole shareholder. The resulting figure the plaintiff, through the approach employed by his expert, would transform into the fair value of the minority shares in the context of a cash out merger."

The Court below continues (A1951 Op.):

> "I do not find this approach to correspond with either logic or the existing law. In the first place, it assumes that a stock has more than one value in the hands of a minority shareholder."

That is precisely what Lynch, Supr. II holds -- that is, where there is simply a disagreement on price and nothing more, then the value of the minority stock is to be determined under appraisal standards. On the other hand, if a fiduciary wrongfully appropriates the stock of the minority, then a different standard is applied to measure the damages. The legal reason is obvious: a wrongful transaction should be enjoined, if possible. If it has taken place, then it will be rescinded, again if possible. However, if the acts of the wrongful majority have proceeded to such an extent that they can not be rescinded (i.e., because of "scambling" or the rights of third parties), then under well-known equitable and fiduciary principles, the minority stockholders should receive back the value of what the corporate fiduciary has wrongfully appropriated from them; that is, rescissionary damages.

The Court below justifies its position again in reliance on what it believes Sterling holds, saying (A1951 Op.):

> "Aside from this, the case law does not support the distinction that plaintiff is attempting to make. Again, as directed by Singer, Tanzer and Roland International, I return to Sterling v. Mayflower Hotel Corp., supra, for the final analysis. There it was stated by the Supreme Court that upon the conversion of the Mayflower stock into HIlton stock a minority shareholder of Mayflower was entitled to receive 'the substantial equivalent in value of the shares he held before the merger.' 93 A.2d 110. That was the test. A Mayflower shareholder was not entitled to 'something that he did not have before the merger and could not obtain' -- in that case the liquidating value of his stock. 93 A.2d 111."

The Court below has missed the point of Mayflower. A stockholder of Mayflower was entitled to what he had before the merger (just as a UOP stockholder is entitled to that which he had just before the merger): that is, his shares of stock with right to participate in the future of the enterprise. In this case, Signal has wrongfully taken this away from him. Unless this Court finds that Signal can return the UOP stock to him, then Signal must give back to the UOP stockholder that which he had before: that is, Signal must make the minority stockholder whole through rescissionary damages.

Liquidation value was what the plaintiff sought in *Mayflower*. Liquidation value is not what UOP's stockholders want. They want and are entitled to rescission or, if rescission is not possible, then rescissionary damages. The Court below then equates the *Sterling* remedy to appraisal, saying (A1951 Op.):

> "I take this to mean that the approach to valuing shares under the *Sterling* rationale is no different than that to be employed in appraisal proceedings." (Note)

Finally, having disregarded the comparative analysis made by Mr. Bodenstein that showed that the value of the minority share was not less than $26 and having rejected the discounted cash flow method, the Court below then accepted the defendants' view -- that is, an appraisal based on 8 *Del.C.* §262, saying (A1955 Op.):

> "The Dillon, Read report, as presented at trial by William K. Purcell, its Senior Vice President, approached the task in the manner generally approved by the Delaware case decisions dealing with appraisal actions under 8 *Del.C.* §262. It considered market value, net asset value and investment value, including UOP's dividend record."

The Court did not explain how or why it was accepting the appraisal method of Dillon, Read (with the addition of

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Note: Somewhat incongruously, the Court below says (A1953 Op.):

> "At the same time, it is presumably proper to view the benefits that may flow to the majority shareholder as a result of becoming the 100 per cent owner as one of the elements to be considered in determining the fairness of the transaction. I say this again because of the decision in *Sterling*."

premium based on a falacious base line). All the Court said was (A1958 Op.):

> "From all of the foregoing, as well as the supporting statistics and documentation provided in the Dillon, Read report, there is a reasonable basis for finding that the merger price of $21 per share represented a price which was fair to the minority shareholders of UOP."

Thus, the Court below is clearly mistaken in its approach and decision on the intrinsic fairness as to price (and the calculation of damages) in a cashout merger. Lynch, Supr. II clearly shows that the measure is not use of the truncated appraisal remedy found in 8 Del.C. §262 but rather, under equitable principles, rescission or rescissionary damages. The Court below should be reversed for reconsideration in the light of Lynch, Supr. II.

IV. THE COURT BELOW ERRED IN APPROVING THE SIGNAL CASHOUT MERGER BASED ON THE STRUCTURE OF THE MERGER VOTE

The final section of the opinion of the Court below is curiously circuitous. The Court in its previous parts of the opinion has exonerated the defendants, one and all, from any wrongdoing under its interpretation of the law governing corporate fiduciary standards. In effect, the Court below holds that all the defendants dealt fairly and candidly with the minority. If this is upheld by this Court, then the fact that there was a majority of the minority which approved the transaction is of no significance. If, however, the record shows the course of conduct of the defendants was tainted by lack of candor, by manipulation and by a failure on defendants' part to carry out their fiduciary responsibilities, then the fact that the merger was structured so that it took a majority of the minority to approve the transaction and that it also took two-thirds of the outstanding votes to approve the transaction is of no significance. The wrongful acts of the defendants themselves prevents them from claiming that the majority of the minority vote insulates the transaction from judicial scrutiny. The record shows that all of the defendants were guilty of repeated and material violations of the applicable standards of fiduciary responsibility and this vitiates the close majority of the minority vote. Furthermore, the class should be held to consist of all UOP minority shareholders without regard to those who voted or who have turned their shares in. In other words, only if the defendants are found to be free of wrongdoing under the standards of _Singer supra_, and its progeny is the structure of the vote significant.

CONCLUSION

Obviously, this is an important case. It is important not only to the ousted minority shareholders of UOP but in connection with the Delaware case law applicable to the corporate fiduciaries in a cashout merger of a minority both as to the standard applicable as to liability as well as damages. As to liability, the opinion of the lower Court is directly at variance not only with the basic concept of Singer supra (and the cases which have followed Singer), but it erodes the basic equitable principles stemming from Guth and Sterling. The decision of the lower Court also contravenes the specific holdings of these decisions. As to damages or intrinsic fairness, Lynch Supr. II shows the lower Court's approach and decision are manifestly incorrect.

The decisions of the lower Court on liability and damages should be reversed. The case should be remanded with directions:

(a) To enter an order enlarging the class to include all minority shareholders of UOP.

(b) To determine whether rescission is possible. If it is not, then the lower Court should determine what equitable remedy will most nearly put the minority shareholders back in the position they would have been in but for the cashout merger. If only rescissionary damages are possible, the lower Court should be directed to start with $26 and add whatever is appropriate to give UOP's stockholders back what Signal appropriated plus costs and attorneys' fees.

Respectfully submitted,

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By ______________________
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