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IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

WILLIAM B. WEINBERGER,	:	
Plaintiff,	:	
v.	:	Civil Action No. 5642
UOP, INC., et al.,	:	
Defendants.	:	

FILED
APR 5 9 03 AM '84
REGISTER IN CHANCERY
JOHN D. KELLY III

PLAINTIFF'S PRE-HEARING MEMORANDUM

DATED: April 4, 1984

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NATURE AND STAGE OF PROCEEDINGS

This is a breach of fiduciary duty action challenging the fairness of a cash-out merger in which defendant Signal Companies, Inc., ("Signal") the majority stockholder of defendant UOP, Inc., ("UOP") eliminated the UOP minority stockholders at a price of $21 per share. After trial, this Court entered judgment for defendants. Weinberger v. UOP, Inc., Del.Ch., 426 A.2d 1333 (1981). While adopting many of this Court's factual findings, the Supreme Court en banc remanded, holding:

(1) The conduct of Signal, including members of Signal's senior management who were also UOP directors, failed to satisfy "any reasonable concept of fair dealing";

(2) On remand, the fairness of the $21 merger price should be tested against the liberalized valuation standards enunciated in the Supreme Court's opinion;

(3) In determining fair value, this Court should consider plaintiff's comparative analysis of premium over market and discounted cash flow analysis; and

(4) This Court should consider awarding recissory damages if they are susceptible of proof and a remedy appropriate to all issues of fairness.

Weinberger v. UOP, Inc., Del.Supr., 457 A.2d 701, 712, 714 (1983).

The Supreme Court made detailed findings concerning the timing of the merger, the preparation of the Lehman Brothers fairness opinion and the preparation and meaning of the so-called Arledge-Chitiea Report (PX 74). 457 A.2d at 705-709, 711-712. As the Supreme Court specifically noted, its factual findings were drawn from this Court's findings (426 A.2d at 1335-40) which are supported by the record. 457 A.2d at 704. The Supreme Court remanded the case to this Court "for further proceedings consistent herewith." Id. at 715. Its February 15, 1983 mandate directed this Court to conduct "such further proceedings...as may be necessary in conformity with [the Supreme Court's] opinion."

On March 7, 1983, defendants requested a "preliminary hearing" at which they purportedly will prove that recissory damages under Lynch v. Vickers Energy Corp., Del.Supr., 429 A.2d 497 (1981) are not an appropriate remedy because "the items of non-disclosure found by the Supreme Court do not constitute such wrongdoing" as to warrant recissory damages. Defendants have indicated that their intent is to relitigate at the preliminary hearing findings of this Court and the Supreme Court establishing that defendants were guilty of a breach of fiduciary duty. March 17, 1983 Transcript, pp. 50-53; April 20, 1983 Letter to the Court (Appendix A). Plaintiff has objected, pointing out that defendants' proposed procedure is (i) totally at odds with applicable law and the Supreme Court's opinions and instructions and (ii) procedurally unfair because it requires plaintiff to participate in an evidentiary hearing with minimal opportunity for discovery.* March 17, 1983 Transcript, pp. 61-63, 69-70; April 28, 1983 Letter to the Court (Appendix B).

In a March 7, 1984, letter opinion**, this Court set a preliminary evidentiary hearing for April 5-6, 1984 at which defendants will be given the opportunity to prove, if they can, that recissory damages should not be awarded despite the Supreme Court's holdings that Signal breached its fiduciary duty and that the merger failed to satisfy "any reasonable concept of fair dealing." Mem. Op. at pp. 1, 6.*** The Court's opinion indicated that defendants could present testimony of Messrs. Arledge and Chitiea and any other Signal or UOP witnesses they may choose to call. Id., at 2. Plaintiffs**** were granted minimal discovery.

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* Plaintiff's discovery, filed on March 2, 1983, has been stayed for more than a year.

** The Court in a May 25, 1983 opinion enlarged the class and directed notice to the enlarged class at defendants' expense, since the additional notice was only required because of the Supreme Court's "finding on the evidence at trial that the defendants had been quilty of wrongdoing in connection with the merger and had breached a duty of fair dealing owed to UOP's minority stockholders." Slip Op., p.6.

*** The final hearing on damages was set down for June 18, 1984.

**** On July 29, 1983, Edwrad U. Notz entered an appearance as a plaintiff.

At a March 15 discovery conference*, defendants again indicated they plan to present testimony at the preliminary hearing on issues that obviously have already been litigated and decided:

> We intend to explain what the Arledge-Chitiea study is, where the information which appears in that study came from, and what, if any, of it was disclosed to both UOP's directors and its minority shareholders.

Id. at 11.** Defendants' March 22, 1984 letter (Appendix C) identifying their witnesses and the areas of their proposed testimony reconfirms defendants' intent to use the preliminary hearing as a vehicle for retrying issues relating to the Arledge-Chitiea Report.*** Moreover, defendants will rely on documents which either were part of the record considered by this Court and the Supreme Court or

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* Defendants' counsel refused to agree to a discovery schedule consistent with the time constraints. At a discovery conference, defendants' counsel conceded that, though defendants had requested the preliminary hearing a year ago, they had not even spoken to some potential witnesses, had not decided what witnesses they would call and documents they would rely on, and they wanted discovery scheduled to suit their convenience and that of their counsel. Transcript of March 15, 1984, pp. 3-5.

** Plaintiff's counsel renewed plaintiffs' objections to the preliminary hearing. Id. at 5-11, 13-16.

*** The issues defendants propose to retry to include (i) why, when and at whose direction the study was prepared, (ii) the sources of its data, (iii) an explanation of the study's computations (iv) what the study purportedly does and does not show and (v) what the information in the study was disclosed.

which they chose not to place into evidence at trial. Defendants' determination to relitigate issues on which they lost before the Supreme Court was further underscored by the recent deposition testimony of Messrs. Arledge and Chitiea. Again and again, they testified that, though they have not even bothered to read the opinions of this Court and the Supreme Court, they flatly disagree with this Court's findings and with the findings and conclusions reached by the Supreme Court.*

In light of this additional evidence of defendants' intention to engage in an improper attempt to retry liability issues finally determined long ago, plaintiffs renew their application that this Court deny defendants' request for a preliminary hearing, permit full discovery and set a final hearing on damages, including rescissory damages. Recognizing, however, that this Court will likely permit the preliminary hearing, plaintiffs will, without waiving their objections, show that the evidence and the law unquestionably support an award of rescissory damages based on defendants' breach of fiduciary duty.

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* Arledge 3/27/84 Depo., pp 9-11, 14-16, 36-37, 42-45, 52-56, 61-62; Chitiea 3/27/84 Depo., pp. 5, 15-17, 42, 46-47. By asserting in the face of final judicial findings that both this Court and the Supreme Court are "wrong", Signal, its counsel and its witnesses display incredible contempt for the courts of Delaware and indeed the judicial process. Such corporate arrogance should not be contenanced by this Court.

This is Plaintiffs' Pre-Hearing Memorandum* in support of their request that the Court (a) refuse to permit defendants to retry at a preliminary hearing issues already finally determined, (b) vacate the stay of plaintiff's discovery and (c) rule that rescissory damages are appropriate in this case.

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* Though the hearing concerns an application by defendants, defendants have refused to file a pre-hearing memorandum advising the Court and the plaintiffs of their factual and legal contentions. Their refusal only adds to the procedural unfairness of the hearing.

STATEMENT OF FACTS

The applicability of rescissory damages should be determined based on the findings of the Supreme Court on the issue of fair dealing and the facts proven at the hearing on remand on fair value. 457 A.2d at 714. Even without a full record on fair value,* this Court cannot but conclude that this case mandates imposition of rescissory damages. Defendants' argument that rescissory damages are not appropriate is based on contentions concerning the Arledge-Chitiea report which have already been rejected by the Supreme Court. Moreover, reconsideration of the contents and implications of the Arledge-Chitiea report only reinforces the Supreme Court's findings and conclusions.

A. Defendants' Failure to Satisfy any Reasonable Concept of Fair Dealing Warrants Rescissory Damages

The Supreme Court, after detailed consideration of the record, concluded the merger did not meet any reasonable test of fairness and Signal's conduct did not satisfy "any reasonable concept of fair dealing." 457 A.2d at 703, 712. Contrary to defendants' bland suggestion, the Supreme Court did not merely find a few "technical" disclosure violations. Rather, the Court found defendants' conduct deficient

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* Plaintiffs are being required to litigate the applicability of rescissory damages without an opportunity to develop through discovery and a full damages hearing the facts pertinent to fair value. as

to each and every element of the duty of fair dealing. The Supreme Court's findings are the law of the case and are binding on this Court on remand.

1. The Timing of the Transaction Supports Application of Rescissory Damages

The Supreme Court found that Signal decided to cash-out UOP's minority stockholders in February, 1978, because it had been unsuccessful at finding a "friendly" acquisition in which to use the excess cash from its earlier sale of an oil and gas subsidiary. 457 A.2d at 704-705. The Supreme Court also found that Signal, which had been UOP's majority stockholder for over 2 1/2 years, was responsible for setting the unreasonably short time constraints which resulted in the entire transaction being presented to and approved by UOP's Board within four business days. Id. at 711. Moreover, the rush imposed by Signal's time table gave Lehman Brothers only three days to render a fairness opinion and, therefore, the blame for the hurried and cursory preparation of that opinion lies solely and squarely with Signal. Id. at 706, 712.* There was no necessity for the hasty board approval because the merger was not submitted to UOP's stockholders until the annual meeting held more than 10 weeks later. Id. at 707-708.

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* Arledge noted on the Arledge-Chitiea report that the timing of the transaction was "fast". Px 74 at A 1476. However, at his recent deposition, he could give no justification as to why the merger was rushed through. Arledge 3/27/84 Depo. at p. 136.

2. <u>The Initiation and Structuring of Transaction Further Demonstrates that Rescissory Damages Should be Awarded</u>

The Supreme Court found that the merger was "entirely initiated by Signal." <u>Id.</u> at 711. This Court and the Supreme Court found that, at the instigation of Signal's chairman and president, Arledge and Chitiea, who were Signal officers and directors as well as UOP directors, did a feasibility study which concluded that acquiring UOP's minority shares at any price up to $24.00 would be a good investment for Signal. 426 A.2d at 1337; 457 A.2d at 705. In the Arledge-Chitiea study, which was disclosed to and discussed by Signal's senior management and all Signal's directors (457 A.2d at 705, 709), these two UOP directors used confidential UOP data to describe the advantages to Signal of ousting UOP's minority stockholders at a price range of $21.00 to $24.00 per share. <u>Id.</u> at 708. Thus, the Arledge-Chitiea study, which was the basis for Signal's merger plan, was used exclusively for Signal's benefit in structuring a cash-out merger at $21.00 per share. <u>Id.</u> at 705, 708.* Having used UOP information to structure the cash-out merger, Signal's management simply disclosed its intention to acquire UOP at $21.00 per share to Mr. Crawford, who as a Signal director and long-time Signal

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* Chitiea and Arledge both admitted the report was prepared solely for Signal's use and benefit. Chitiea 3/27/84 Depo., p. 20; Arledge 3/27/84 Depo., pp. 42-43.

employee owed his position as UOP's president to Signal and could not possibly be independent. Id. at 705. In summary, "[t]he structure of the transaction, again, was Signal's doing." Id. at 711.

3. The Total Lack of Negotiations Mandates Rescissory Damages

In evaluating the merger, the Supreme Court found an "absence of any attempt to structure this transaction on an arm's length basis." 457 A.2d at 710. Neither Crawford nor any of UOP's non-Signal directors suggested or attempted to negotiate any price higher than the $21.00 Signal had offered. Id. at 705-707, 711.* Indeed, the Supreme Court found that "[o]nly the protection of benefits for UOP's key employees and the issue of Lehman Brothers' fee approached any concept of bargaining." Id. at 711. No independent negotiating committee of outside UOP directors was appointed to bargain with Signal at arm's length. Id. at 709-710, n. 7. Finally, though Signal's press releases and UOP's draft proxy statement stated that there were "negotiations" between Signal and UOP, when the SEC sought details, Signal and UOP evaded the question by substituting "discussion" but

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* Chitiea and Arledge admitted there was no effort to determine what price would be advantageous to UOP's minority stockholders, nor any presentation or discussion as to the advantages or disadvantages of the merger to UOP's minority. Chitiea 3/27/84 Depo., pp. 17-19, 88-89; Arledge 3/27/84 Depo., pp. 49-50.

never told the minority stockholders that no negotiations had ever occurred. Id. at 708.

4. The Incomplete Disclosure to UOP's Directors Warrants Rescissory Damages

As noted earlier, UOP's Board hastily approved the merger only four business days after the Signal announcement, even though the stockholders' meeting was not held until 10 weeks later. Id. at 706-708. Despite defendants' contentions to the contrary, the Supreme Court after an independent review of the record found that neither the Arledge-Chitiea Report, nor the fact that the merger would be a good investment for Signal at any price up to $24.00 per share, were disclosed to UOP's outside directors. Id. at 707-709. Accordingly, the Supreme Court concluded:

> [T]he matter of disclosure to the UOP directors was wholly flawed by the conflicts of interest raised by the Arledge-Chitiea report. All of those conflicts were resolved by Signal in its own favor without divulging any aspect of them to UOP.
>
> This cannot but undermine a conclusion that this merger meets any reasonable test of fairness. The outside UOP directors lacked one material piece of information generated by two of their colleagues, but shared only with Signal.

Id. at 712. In light of its rushed and superficial preparation, the Lehman Brothers' fairness opinion was no substitute for the withheld Arledge-Chitiea study. Id.* Nor

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* The information in the Arledge-Chitiea report was also not disclosed to Lehman Brothers for use in formulating their fairness opinion. Chitiea 3/27/84 Depo., p. 61.

was the three page summary given UOP's directors, which only included the page of the Arledge-Chitiea report which purportedly justified the $21.00 price. 457 A.2d at 709. UOP's outside directors were not given the pages of that report which showed the merger would be a good investment for Signal up to $24.00 per share. Id. Thus, Signal selectively disclosed the data it believed supported the $21.00 price, while deliberately withholding the data showing a higher price might be warranted. Finally, the common Signal-UOP directors participated in the UOP Board meeting without disclosing the conflict of interest they faced because of their knowledge of the Arledge-Chitiea report. Id. at 709. Thus, the hasty board approval, without disclosure of critical information and the conflict of interest of Signal's men on UOP's Board, was not properly obtained and is meaningless.

5. The Blatant Nondisclosures to the Minority Stockholders Demand an Award of Rescissory Damages

The Supreme Court ruled that UOP's minority stockholders were deprived of their right to an informed vote because material information necessary to acquaint them with the respective bargaining positions of Signal and UOP was withheld as a result of defendants' breaches of fiduciary duty. Id. at 703. There was, first of all, a "lack of any candid disclosure of the material facts surrounding the establishment of the $21 price." Id. at 714. Moreover, nothing in the Arledge-Chitiea report, except the justification of the $21.00 price based on comparison to the prior tender offer, was ever disclosed to UOP's minority stockholders prior to their approval of the merger. Id. at 707. Thus, corporate fiduciaries with superior knowledge misled the stockholders by using information derived from UOP financial figures to prepare a study for Signal's sole use and benefit without disclosing the contents of that study to the minority stockholders. Id. at 711.

The Supreme Court also found that the proxy statement said Lehman Brothers had opined that $21.00 was a fair price to UOP's minority, but "did not disclose the hurried method by which this conclusion was reached." Id. at 708. Specifically:

> There was no disclosure of the circumstances surrounding the rather cursory preparation of the Lehman Brothers' fairness opinion. Instead, the impression was given UOP's minority that a careful study had been made, when in fact speed was the hallmark, and Mr. Glanville, Lehman's partner in charge of the matter, and also a UOP director, having spent the weekend in Vermont, brought a draft of the 'fairness opinion letter' to the UOP directors' meeting on March 6, 1978 with the price left blank. We can only conclude from the record that the rush imposed on Lehman Brothers by Signal's timetable contributed to the difficulties under which this investment banking firm attempted to perform its responsibilities.

> Yet, none of this was disclosed to UOP's minority.

Id. at 712.* The Supreme Court further found that Signal withheld from the minority the critical information that Signal considered a $24.00 price a good investment. Id.

Even with the lack of full disclosure, only 51.9% of the total UOP minority shares voted in favor of the merger. Id. at 708. However, based on the non-disclosures and mispresentations described above, the Supreme Court held that the shareholder vote was not an informed one and, consequently, the approval by a majority of the minority was meaningless. Id. at 712.

B. The Facts Concerning Fair Value Also Show Rescissory Damages Should be Assessed

While the Supreme Court did not determine the actual fair value of UOP's minority shares, it did make findings that are relevant to this Court's determination of whether rescissory damages are appropriate. The Supreme Court said that that the Arledge-Chitiea report supports this Court's finding that the $24.00 price would have been a good investment for Signal. Id. at 709. The Court explained that paying $24.00, instead of $21.00, would have had a minimal effect on Signal's return on investment and

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* Other disclosure deficiencies include the representation in press releases and the March 7, 1978 letter to stockholders that there had been negotiations and the subsequent substitution of "discussions" in the proxy statement without telling the stockholders the reason for the change. Id. at 706, 708.

relatively little long-term impact on Signal, but would have meant over $17 million to the minority stockholders. Id. In addition, critical facts relevant to the minority stockholders evaluation of the fairness of the $21.00 were not disclosed under circumstances amounting to a breach of fiduciary duty. Id. at 703, 709, 712. Moreover, plaintiff's premium over market analysis and discounted cash flow analysis,* which the Supreme Court said must be considered, show that UOP's stock was worth at least $26.00 per share on the date of the merger. Id. at 712. Based on the record that was before the Supreme Court, that Court concluded that "there can be no finding at the present stage of these proceedings that the price is fair." Id. at 714. It is defendants' burden to prove fairness of price and on the present record they have not met that burden. Thus, the state of the record at this point is that the $21.00 price was unfair.

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* In a handwritten note page A1475 of PX74, Arledge acknowledged that "Future Earnings Potential" (i.e., the discounted value of the future income flow from UOP) "is real key to value." At his deposition Arledge admitted that discounted cash flow is a commonly used valuation technique in the financial community and that he has used such analyses to value companies Signal might acquire. Arledge 3/27/84 Depo., p. 67.

C. <u>Defendants Arguments Have Already Been Rejected by the Supreme Court</u>

1. <u>Findings by the Supreme Court Concerning the Arledge-Chitiea Report which the Defendants Cannot Relitigate</u>

(a) <u>Purpose and Preparation of the Report</u>

The Supreme Court's opinion thoroughly considered the facts surrounding the Arledge-Chitiea report. The Court adopted this Court's finding that the report was prepared at the direction of certain Signal officers, including Mr. Walkup, Signal's Chairman of the Board, and Mr. Shumway, its President.* 457 A.2d at 705; 426 A.2d at 1337.** The purpose of the study, as found by both courts, was to consider the feasibility of Signal's acquisition of the balance of UOP's outstanding shares. <u>Id.</u> Arledge and Chitiea used UOP data and information in preparing the report and contents of the report were derived from that data and information. <u>Id.</u> at 708-709, 711.

(b) <u>Contents of the Report</u>

The Supreme Court found that the Arledge-

* Chitiea confirmed that Walkup and Shumway requested Arledge and Chitiea to do a feasibility study of Signal's acquisition of the minority shares. Chitiea 3/27/84 Depo., pp. 14-15. See also: Arledge 12/13/78 Depo., p. 11.

** PX 68-3 "Sequence of Events", which Arledge wrote just prior to the February 28 Signal Executive Committee meeting (Arledge 12/13/78 Depo., pp. 12, 15) establishes the timing of the study's initial preparation: "2/8/78 -FNS tells ASC to study; 2/9/78 - AJC tells CSA that we will begin study; 2/13-2/16 - AJC and CSA make study; 2/17 -AJC and CSA make presentation to FNS, WEW, BLA."

Chitiea Report used UOP data in describing the advantages to Signal of ousting UOP minority at a price of $21.00 to $24.00 per share. Id. at 708. The conclusion from the report was that it would be a good investment for Signal to purchase the remaining 49.5% of UOP's stock at any price up to $24.00. Id. at 705. Indeed, the Supreme Court found:

> The Arledge-Chitiea report speaks for itself in supporting the Chancellor's finding that a price of up to $24 was a 'good investment' for Signal. It shows that a return on the investment at $21 would be 15.7% versus 15.5% at $24 per share. This was a difference of only two-tenths of one percent, while it meant over $17,000,000 to the minority. Under such circumstances, paying UOP's minority shareholders $24 would have had relatively little long-term effect on Signal, and the Chancellor's findings concerning the benefit to Signal, even at a price of $24, were obviously correct. Levitt v. Bouvier, Del.Supr., 287 A.2d 671, 673 (1972).

Id. at 709. The one page of the Arledge-Chitiea report that was given to all UOP directors (page A1475) was nothing more than an attempt to justify the $21.00 price and did not reflect the advantage to Signal at $24.00. Id.

The Supreme Court also recognized that the Arledge-Chitiea report focused on the earnings potential of UOP (i.e., the amount of additional income Signal would receive from UOP if it acquired the UOP minority interest.) Id. at 712. Indeed, while page A1475 of their report attempts to justify the $21.00 per share price by comparing it to UOP's

1975 tender offer, Mr. Arledge on his copy wrote above "WHY $21 PER SHARE", the explanation that:

> "Future earnings potential is real key to value but, compared to prior offer;".

(c) Disclosure of the Arledge-Chitiea Report

(i) The Report and Its Contents were not Disclosed to UOP's Outside Directors

Signal had contended that the Arledge-Chitiea feasibility study showing that a price of up to $24 per share would be a good investment for Signal was disclosed to UOP's outside directors and discussed at the March 6, 1978 UOP directors' meeting. The Supreme Court noted that this Court had made no such finding and, after an independent review of the record, the Supreme Court found that there was no such disclosure. 457 A.2d at 707-709.

In rejecting defendants claim of disclosure to UOP's outside directors, the Court cited nine separate reasons for concluding that the information contained in the Arledge-Chitiea report, including the information that Signal considered a price up to $24.00 a good investment, was not disclosed to UOP's outside directors. Id. at 708-709.*

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* The record citations supporting for these reasons are found in Plaintiff's July 21, 1982 letter to the Supreme Court (Appendix 4).

Among the reasons was that Mr. Chitiea had testified that the report had been made available to Signal's directors, but not to UOP's outside directors, and that he did not share the information in the report with UOP's outside directors. Id. at 709.* The Court noted that Signal's counsel, as a matter of strategy, did not claim the report was disclosed to UOP's outside directors, but instead tried to belittle the contents and significance of the report. Id.

The Supreme Court having recognized, as this Court did, the importance of the Arledge-Chitiea report, defendants are belatedly attempting to claim that the information in the report was somehow available to UOP's outside directors. However, the Supreme Court, having reviewed in detail what was made available to UOP's outside directors, has finally determined that nothing whatsoever was done to disclose the critical information in the Arledge-Chitiea report was to UOP's outside directors. Id. at 704, 707-709, 712. Moreover the Supreme Court has already ruled that "the matter of disclosure to the UOP directors was wholly flawed

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* See: Chitiea 12/13/78 Depo., pp. 72-73. Chitiea reaffirmed at his recent deposition that neither the report nor the critical information it contained were shared with UOP's outside directors. Chitiea 3/27/84 Depo., pp. 20, 86-88. Arledge concurred. Arledge 3/27/84 Depo., pp. 32-35, 52.

by the conflicts of interest raised by the Arledge-Chitiea report." Id. at 712.

(b) Nondisclosure of the Report to the Minority Stockholders

The Supreme Court has held that:

> It is clear beyond peradventure that nothing in that report was ever disclosed to UOP's minority shareholders prior to their approval of the merger.

Id. at 707. Specifically, the Court concluded that the report's figures showing (i) that any price up to $24.00 was a good investment for Signal, (ii) that a $24.00 price would only reduce Signal's return on equity by two-tenths of one percent while giving the minority over $17 million additional, and (iii) that paying $24.00 would have had relatively little long term effect on Signal were matters of material significance to UOP's shareholders which were not disclosed. Id. at 709. The Court considered the information in the report so critical that failure to disclose it rendered the minority vote on the merger meaningless. Id. at 712.

2. Defendants Have Already Litigated Their Contentions Concerning the Arledge-Chitiea Report and Lost

The record before this Court and the Supreme Court shows that defendants fully litigated every contention they now make concerning the Arledge-Chitiea report. The Supreme Court rejected these contentions and this Court should, indeed must, do likewise.

(a) <u>The Purpose and Meaning of the Arlede-Chitiea Report</u>

This Court and the Supreme Court found that the Arledge-Chitiea report was a feasibility study conducted for Signal concerning the possible acquisition of UOP's minority shares. 426 A.2d at 1337; 457 A.2d at 705. Both courts also concluded that the report indicated that the acquisition would be a good investment for Signal at any price up to $24.00 a share. Id. The recent depositions of Arledge and Chitiea indicate that defendants plan to challenge these findings at the preliminary hearing, relying on the same explanations of the purpose and meaning of the report which failed to persuade this Court or the Supreme Court the first time.

Shumway, who requested the Arledge-Chitiea study, and Arledge and Chitiea, who prepared it, all testified in pre-trial depositions that the study was prepared to determine the feasibility of Signal acquiring UOP's minority shares, including the range of prices Signal could offer. Shumway Depo., pp. 27-35; Arledge 12/13/78 Depo., p. 15; Chitiea 12/13/78 Depo., pp. 24-26, 47. Indeed, defendants' post-trial brief represented that Arledge and Chitiea were requested by Shumway to study the feasibility of acquiring the UOP minority shares. Defendants' Post-Trial Brief, p. 16.

Thus, the conclusion of this Court and the Supreme

Court that the Arledge-Chitiea report was a feasibility study of the acquisition of the balance of UOP derived from Signal's own evidence. Now, however, defendants wish to contradict that evidence and those findings. Arledge recently testified that the Arledge-Chitiea report was not a feasibility study, but "more of just kind a of statistical study to put the whole thing in perspective for the Signal directors." Arledge 3/27/84 Depo., pp. 38-39. Moreover, Arledge denied that the purpose of the report was to aid Signal's directors in determining what would be a good price for Signal to pay. Id. at 39. Thus, defendants' current position contradicts not only the final factual determination of the Delaware Courts, but also defendants own prior testimony and positions.

Defendants plan a frontal assault on the finding of this Court and the Supreme Court that the Arledge-Chitiea report showed the acquisition of UOP to be a good investment for Signal up to $24.00 per share. Arledge and Chitiea stated emphatically in their recent depositions that the Supreme Court and this Court were totally wrong in so finding. Arledge 3/27/84 Depo., pp. 14-15; Chitiea 3/27/84 Depo., pp. 15-16. However, defendants' arguments as to why this finding is wrong are merely a warmed-over serving of the explanations of the report that were unsatisfactory the first time the issue was litigated.

Plaintiff contended in this Court, both before and after trial, that PX 74 showed that the acquisition would still be a good investment at $24.00 per share and that Signal should have disclosed that information. Plaintiff's Pre-Trial Memorandum on Liability, pp. 5-6; Plaintiff's Pre-Trial Memorandum on Remedy, pp. 8-9, 25-26; Plaintiff's Post-Trial Reply Brief, p. 15. Transcript of October 6, 1980 Argument, pp. 29, 56, 127-128. Defendants' chose to ignore plaintiff's contentions in their post-trial brief, but at argument their counsel raised the same responses defendants now proffer. Transcript of October 6, 1980 Argument, pp. 68-70.

On appeal, plaintiff continued to assert that PX 74 showed that any price up to $24.00 would be a good investment for Signal, relying on this Court's finding below. Appellant's Opening Brief, pp. 10-11, 15, 17, 67, 80-81; Plaintiff's Brief in Reply, pp. 11-15; Transcript of September 14, 1981 Argument, pp. 19, 59; Transcript of June 23, 1982 Reargument, pp. 20-21, 27.* Plaintiff also attacked Signal's failure to disclose to the minority stockholders the fact that the Arledge-Chitiea report showed that any price up to $24.00 would be a good investment for

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* The cited portions of the Supreme Court record discussing the Arledge-Chitiea report are assembled in Appendices 5-9 to this memorandum.

Signal. Id. Defendants countered with the same tactic they intend to use at the preliminary hearing -- claiming this Court's finding was wrong:

> "We strongly disagree with the Vice Chancellor's suggestion that the report done by Arledge and Chitiea 'indicated' that acquiring the minority shares of UOP at any price up to $24 per share would be a 'good investment for Signal.' The study was only a comparison of the econmic effects of a possible acquisition at different stock prices from $17 [sic] to $24 per share, i.e., at $17 [sic], $18, etc. In fact, the study showed that if Signal were to acquire the minority shares at $24 per share, the total investment of more than $136.5 million (5,688,302 x $24 per share) would generate only $7.8 million in additional income, or a return of only 5.7% (A1493). While a return on investment of 5.7% may not represent a negative yield, it is hardly a 'good investment' for a major industrial concern."

Brief of the Signal Companies, Inc. and UOP, Inc., p. 15.* Defendants also claimed that:

(a) The Arledge-Chitiea report was only an internally generated Signal document "to give Signal's management data on which to make a decision on a possible merger";

(b) The report was merely "accounting spread

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* Ironically, defendants' brief castigated plaintiff's brief as "nothing more than a motion for reargument with respect to factual and legal contentions which have been rejected by the trial court after as full trial on the merits." Id. at 9. That "shoe" now fits defendants' "preliminary hearing" arguments perfectly.

sheets" presenting "the financial impact on Signal" of buying the minority shares at up to $24.00 per share; and

(c) The 6% increase in Signal's Plan Income for 1978 resulting from a merger at $24.00 per share would have been a very low return. Id. at 63. At argument Signal's counsel reiterated defendants' arguments concerning the supposed insignificance and nondisclosure of the report. Transcript of September 14, 1981 Argument, pp. 35-36.*

At reargument, Signal's counsel was given every opportunity to explain the report, what it shows and why it was not disclosed to the minority stockholders. Transcript of June 23, 1982 Reargument, pp. 42-59, 70. In response to the Supreme Court's questions, Signal's counsel made every single argument that Signal now intends to make concerning the meaning and disclosure of the Arledge-Chitiea report,** including:

(i) The report "is not a report, but merely 'an

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* Signal's counsel maintained at argument that the Arledge-Chitiea report "clearly on its face shows what it was." Id. However, now that the Supreme Court has decided what that report shows on its face, defendants' counsel claims Arledge and Chitiea must explain what it shows.

* Appendix 10 shows that all the arguments suggested by Arledge and Chitiea's recent deposition testimony were unsuccessfully raised before the Supreme Court.

arithmetic computation of what the assumed return would be on a given investment.'" (p. 43).

(ii) The information in the report was available to the outside UOP directors and minority stockholders. (pp. 43-44).

(iii) Signal and the Signal officers who were UOP directors had no fiduciary duty to disclose the report to UOP's outside directors or the minority stockholders. (pp. 43-44).

(iv) The report was irrelevant to the question of the fairness of the merger. (p. 46).

(v) This Court's finding that the merger would be a good investment for Signal at $24.00 per share was wrong. (pp. 51-52).

(vi) At $24.00 per share, the return on the investment for Signal would not have been sufficiently high. (pp. 52-54).

Thus, since the Supreme Court has already heard all these arguments and decided them against the defendants, there is no point to defendants' proposed preliminary hearing.

D. <u>The Evidence at the Preliminary Hearing Will Confirm the Supreme Court's Findings and Support of an Award of Rescissory Damages</u>

Contrary to defendants' expectations, the evidence at the preliminary hearing will show that, upon reexamination of the Arledge-Chitiea report, the support for the Supreme Court's findings will be strengthened, not diminished. Furthermore, the evidence will show that applying the principles and methodology used in the Arledge-Chitiea report, Signal expected to reap, and in fact has reaped, tremendous profit from breaching its fiduciary duty in connection with cashing out the minority interest in UOP.

1. The Arledge-Chitiea Report

The Supreme Court found that:

> The Arledge-Chitiea report speaks for itself in supporting the Chancellor's finding that a price of up to $24 was a 'good investment' for Signal.

457 A.2d at 709. Indeed, upon analysis the report speaks loud and clear in detailing how Signal obtained an outstanding investment at the expense of UOP's minority stockholders.

(a) Summary of the Proposed Acquisition (p. A 1473)

The report's summary of the proposed acquisition indicated that it would be a "cash merger". Mr. Arledge's handwritten notes point out "not tender offer - rare one step transaction".* Thus, Arledge recognized that

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* PX 74, the copy of the Arledge-Chitiea report that is in evidence in this case, contains certain handwritten comments by Mr. Arledge which he made for the purpose of assisting him in his presentation of the UOP Acquisition Proposal to Signal's Board. These comments are most helpful in showing what Mr. Arledge thought the report showed then, as opposed to the "revisionist history" defendants now plan to offer the Court.

the merger would get rid of all the minority stockholders at one time, including those who would not accept a tender offer at $21.00 per share. The summary showed that the total cost of the merger would be "$103-137 MILLION ($18-24 per share) CASH". Accordingly, the subsequent typewritten comments concerning the purpose of the merger, etc., applied to all prices from $18.00 to $24.00 per share, not just the $21.00 price.

(b) Purpose of the Merger (p. A1474)

The first reason the Arledge-Chitiea report gave for the merger was that it "PROVIDES AN OUTSTANDING INVESTMENT OPPORTUNITY FOR SIGNAL". This typewritten statement refers back to the preceding page which gave a summary of the proposed acquisition at $18.00 to $24.00 per share. Thus, the report not only shows that the merger would have been "a good investment" for Signal at $24.00, but that it would have been "an outstanding investment". Indeed, in presenting the merger to Signal's Board, Arledge described it as "better than any recent acquisition we have seen."

The report also recommended the merger because it "INCREASES SIGNAL'S EARNINGS". Thus, the additional earnings Signal would receive from UOP by acquiring the minority's interest was a primary factor behind the merger. The merger also "ELIMINATES POTENTIAL CONFLICTS OF

INTEREST", after which Mr. Arledge wrote "Always present now". Hence, Signal recognized the conflict of interest position it occupied with respect to UOP's minority stockholders. However, despite this recognition, Signal made no attempt to permit arm's length bargaining and there was no disclosure of the conflicts of interest Signal and the Signal personnel who served as UOP directors faced in connection with the Arledge-Chitiea report. 457 A.2d at 709-712.

(c) <u>WHY $21 PER SHARE (p. A1475)</u>

Page A1475 is the only page of the Arledge-Chitiea report that was given to UOP's outside directors. As the Supreme Court noted, this page is no more than an attempt to rationalize a $21.00 price. 457 A.2d at 709. It does not show that $21.00 was a fair price based on the value of UOP on March 6, 1978 in light of UOP's position then and UOP's future prospects. Rather, page A1475 is simply a comparison between the circumstances at the time of Signal's prior $21.00 tender offer and the circumstances at the time Signal was considering the freeze out merger. Comparison to a tender offer made three years ago is no basis for determining the value of a company today. Duff and Phelps 3/27/84 Report, page 1 (Appendix 11).* However,

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* The tender offer merely enabled those stockholders who wished to accept $21.00 per share voluntarily to take it, while the freeze out merger was designed to eliminate all the minority stockholders whether they wanted $21.00 for their shares or not.

the Court need not take plaintiff's word that comparison to the 1975 tender offer was not the proper basis for determining the merger price, because Mr. Arledge recognized that fact at the time he presented the merger proposal to Signal's Board. Above the heading "WHY $21 PER SHARE" Mr. Arledge noted:

> "Future Earnings Potential is real key to value but, compared to prior offer;"

Consequently, though Signal knew that the real key to valuing the UOP minority interest was UOP's future earnings potential, they justified the $21.00 price to UOP's outside directors and minority stockholders on the basis of an irrelevant comparison to the 1975 tender offer.

(d) <u>Purchase at $21/SH (P A1478)</u>

Page A1478 graphically illustrates the substantial financial benefits Signal expected to reap in 1978 alone compares Signal's expected performance under its "1978 Profit Plan" with the performance expected in 1978 if Signal had owned 100% of UOP for a full year or the last eight months of the year. The figures show that owning 100% of UOP would increase Signal's net income by $10 million in 1978 (assuming ownership for the entire year) or $5 million (assuming ownership of eight months). This additional income would increase Signal's overall earnings per share from $6.56 under the 1978 Profit Plan to full year and eight month figures of $7.06 and $6.84 per share respectively. Furthermore, these results would raise Signal's overall return on equity significantly.

(e) <u>Source of Purchase Funds (p. A1483)</u>

This sheet shows the total purchase price for the 5.7 million minority shares at prices from $18.00 to $24.00 per share and the sources Signal would use to pay for the purchase. Signal planned to call $35 million in loans to its subsidiaries. These funds would otherwise have been invested in money market instruments, so that the "opportunity cost" to Signal was the interest obtainable on such instruments, not the 9% short-term borrowing rate assumed by Arledge and Chitiea in calculating the interest expense of the UOP merger.

(f) <u>Purchase at Greater than $21 Per Share (pp A1490-1492)</u>

The Arledge-Chitiea report shows, as the Supreme Court found, that the purchase of the minority shares at prices up to $24.00 per share would have been a good investment for Signal. Purchase at $22.00 to $24.00 per share would have raised Signal's expected net income, earnings per share, return on equity and book value per share significantly. For example, even at $24.00 per share, Signal's net income for 1978 would have increased $8 million (full year) or $4 million (8 mos.) over the level projected in Signal's 1978 Profit Plan. Earnings per share would have gone from $6.56 to $6.96 (full year) or $6.78 (8 mos.). Signal's overall return on equity would also have risen.

(g) <u>Summary of Additional Income (p. A1493)</u>

As Duff and Phelps, Inc.'s March 27, 1984 report explains in detail (see: pp. 2-4), the Arledge-Chitiea report's summary of additional income shows Signal expected to derive significant additional income in 1978 from UOP by cashing out the minority interest at any price up to $24.

2. <u>Duff & Phelps, Inc.'s 3/27/84 Preliminary Analysis of PX 74</u>

At the preliminary hearing, plaintiffs will introduce Duff and Phelps March 27, 1984 report (the "D&P 3/27/84 Report."). The report not only confirms that PX 74 demonstrates that acquiring UOP's minority interest would have been an outstanding investment for Signal at up to $24.00 per share, but also shows, by application of the principles and methodology of PX 74 that:

(a) Extension of the Arledge-Chitiea study's summary of additional income to prices from $25.00 to $35.00 per share reveals that at any price up to $35 the merger would have increased Signal's 1978 income. (pp. 2-5; Exhibit C).

(b) Signal's total projected additional income for 1978 through 1982 as a result of the $21 cash out was

$71.6 million, while UOP's actual performance from 1978 through 1982 resulted in Signal receiving $80.2 million attributable to the 49.5% minority interest. (p. 5; Exhibit D).

(c) At $24.00 per share, Signal could have expected $62.1 million additional income during 1978-1982 as a result of the merger, and would have actually derived $70.7 million from the minority's shares in that period; at $30.00 per share, expected additional income: $43.1 million, actual additional income: $51.7 million. (p. 5; Exhibit D).

(d) UOP's actual overall performance has been significantly better than projected in the 1978 Five Year Plan. (p. 6; Exhibit E).

(e) Acquisition of the UOP minority interest at any price up to $30.00 would have improved Signal's expected return on total invested capital,* even after considering Signal's additional short-term debt to finance the merger and the associated interest expense (accepting arguendo Signal's assumption that all funds were borrowed at 9%). (p. 7; Exhibit F).

In summary, when the principles underlying the Arledge-Chitiea report are applied to prices above $24.00 per share,

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* As a note to Exhibit F of Duff and Phelps report explains, total invested capital includes equity, long term debt, capitalized leases and the additional short-term debt Signal contemplated to finance the merger.

the results show, using a variety of measures, that acquisition of the UOP minority interest would have been a good investment for Signal at prices well beyond $21.00 or even $24.00 per share. Thus, reconsideration of the Arledge-Chitiea report lends further support to the findings of this Court and the Supreme Court that the merger would have been a good investment for Signal at $24.

ARGUMENT

I. <u>The Law of the Case Precludes Defendants From Relitigating the Liability Resulting from Their Misconduct</u>

Under the doctrine of the law of the case, a decision on an issue made at one stage of a case becomes a binding precedent to be followed in successive stages of the same litigation. <u>Insurance Group Committee v. Denver & RGWR Co.</u>, 329 U.S. 607, 612, (1947); 1B J.Moore, <u>Moore's Federal Practice,</u> ¶0.404[10], pp. 169-74 (3d Ed. 1983). As the United States Supreme Court has explained, the lower court

> is bound by the decree as the law of the case, and must carry it into execution according to the mandate. That court cannot vary it, or examine it for any other purpose than execution; or give any other or further relief; or review it even for apparent error, upon any matter decided on appeal; or intermettle with it, further than to settle so much as has been remanded.

<u>In Re Sanford Fork & Tool Co.</u>, 160 U.S. 247, 255, (1895). See also, <u>Quern v. Jordan</u>, 440 U.S. 332, 347 n. 18, (1979); 1B Moore at ¶0.404[1], pps. 117-119.

The Supreme Court's opinion makes abundantly clear the limited issue remanded:

> On remand the plaintiff will be permitted to test the fairness of the $21 price by the standards we herein establish, in conformity with the principle applicable to an appraisal -- that fair value be determined by taking 'into account all relevant factors' [See 8 <u>Del.C.</u> §262(h), <u>supra</u>]. In our view this includes the elements of rescissory damages if the Chancellor considers them susceptible of

> proof and a remedy appropriate to all the issues of fairness before him.

457 A.2d at 714. The Court did not remand to give the defendants a "preliminary hearing" to relitigate the Arledg-Chitiea report. Nor did the Court authorize this Court to vary the Supreme Court's findings or review the Supreme Court's opinion for apparent error on the factual and legal matters decided on appeal. Rather, the Court's opinion remanded the matter "for further proceedings <u>consistent</u> herewith." 457 A.2d at 715. (Emphasis added). The Mandate specified that the further proceedings were to be "in conformity with the opinion" of the Supreme Court.

The Supreme Court's findings, reached after a full trial, briefing and argument before this Court, and briefing, argument and reargument before the Supreme Court are the binding law of the case on remand. <u>Lee Builders, Inc., v. Wells</u>, Del.Ch., 103 A.2d 918, 919-20 (1954). <u>Lynch v. Vickers</u>, Del.Supr., 429 A.2d 497 (1981), ("Lynch II") is particularly instructive on this point. Lynch was also remanded to the Chancery Court for further proceedings consistent with the Supreme Court's liability findings. 429 A.2d at 499. Given that liability had been established by the Court's opinion on the initial appeal (429 A.2d at 504), the <u>Lynch</u> court recognized that on remand:

> The issue remaining for decision is very narrow. In ultimate terms, it amounts to this: Is the plaintiff entitled to relief, and if so, what is it to be?

429 A.2d at 500. In analyzing the status of Lynch at the time of the appeal from the Chancellor's determination of damages, Justice Quillen noted that the Supreme Court's findings of violations of fiduciary duty by the defendants were the law of the case and were not open to review again even by the Supreme Court. 429 A.2d at 507. (Quillen, J., dissenting).

Indeed, this Court in this very action, recognized the precedential requirements of the law of the case doctrine. In the Court's opinion of April 5, 1979 limiting the class certified under the original complaint in this action, the Court distinguished the class certification decision in Singer v. Magnavox, Del.Ch., C.A. No. 3929, Brown, V.C. (Dec. 14, 1978):

> "In the Singer application, I had the benefit of the Supreme Court's earlier landmark decision. I considered it to be the law of the case to the extent applicable. "

Mem. Op., pp. 9-10. The preliminary hearing to permit defendants to revise the record in order for the Court to reevaluate their unfair dealing toward UOP's minority shareholders violates this long standing principle.

The evidence defendants plan to present at the hearing concerning the Arledge-Chitiea Report relates to issues fully litigated and finally decided by both this Court and the Supreme Court. Section C of the Statements of Facts and Appendix 10 to this memorandum set forth the extensive testimony and argument concerning the Arledge-Chitiea report prior to the Supreme Court's opinion, including argument on the specific issues defendants seek to revisit at the preliminary hearing. The witnesses Signal will call at the preliminary hearing, Arledge and Chitiea, were deposed before trial and questioned on their report. Chitiea 12/13/78 Depo., pp. 24-30, 45-59; Arledge 12/13/78 Depo., pp. 11, 15-16, 33, 50, 54-55. They were listed as witnesses for that trial, but defendants elected not to call them. Moreover, the report itself was placed into evidence at trial and defendants had a full opportunity to explain its contents and their failure to disclose those contents.

Having litigated and lost on the issues on what the report shows and whether it was disclosed, defendants cannot resurrect these issues, which were finally determined by the Supreme Court's opinion. Since the preliminary hearing is merely an effort by defendants to cloud the record with evidence that was previously presented or that they chose not to present at the appropriate stage of this litigation, the law of the case forecloses their belated "explanation" of the report and their failure to disclose its contents. Baumer v. United States, 685 F.2d 1318, 1321 (11th Cir., 1982).

II. Rescissory Damages are Warranted If They Are the Remedy Most Beneficial to the Minority Stockholders

A. The Supreme Court's Guidelines on the Applicability of Rescissory Damages

The Supreme Court's opinion directed that on remand the fairness of the $21.00 price was to be determined based on the liberalized valuation principles outlined in the opinion. 457 A.2d at 714. Because the Court held that the minority stockholder vote did not shift the burden of proof, Signal has the burden of establishing that the minority stockholders received fair value for their shares. Id. at 703, 710. The Court directed that, in determining fair value on remand, this Court consider the elements of rescissory damages if they were susceptible of proof and a remedy appropriate to all issues of fairness before this Court. Id. at 714. Thus, since rescissory damages are an element of fair value, it is Signal's burden to prove that rescissory damages are not an appropriate measure of damages in this case.

The Supreme Court made clear that Lynch II should not be interpreted as making rescissory damages the exclusive monetary formula for relief. Id. at 703-704, 714. Instead, the Supreme Court reaffirmed this Court's power to fashion any form of equitable and monetary relief as may be appropriate, including rescissory damages. Id. at 714. Thus, the issue at the preliminary hearing is whether defendants have met their burden of proving that rescissory damages should not be considered in determining the monetary damages to be awarded to UOP's minority stockholders. Analysis of the pertinent legal principles, as applied to the factual findings of this Court and the Supreme Court, demonstrates that defendants have not come near meeting their burden.

B. <u>The Legal Standard for Awarding Rescissory Damages</u>

In <u>Lynch II</u> the Supreme Court enunciated the standards governing applicability of rescissory damages in breach of fiduciary duty cases. While the Supreme Court in this case has indicated that <u>Lynch II</u> does not require that rescissory damages be the only measure of monetary damages this Court considers (457 A.2d at 703-704, 714), the Court did not alter the principles <u>Lynch II</u> established for determination of the applicability of rescissory damages. Hence, even defendants' motion for preliminary hearing acknowledged that the principles of <u>Lynch II</u> govern the determination of whether rescissory damages apply.

In <u>Lynch II</u>, the class consisted of minority stockholders who had sold their shares voluntarily in a tender offer by the majority stockholder. 429 A.2d at 498. Thus, unlike this case, the minority stockholders had not been frozen out in a cash-out merger regardless of whether they wished to remain in the company or not. The Supreme Court found that the majority stockholder had breached its fiduciary duty by failing to disclose two critical facts to the minority stockholders in its tender offer . Lynch v. Vickers Energy Corp., Del.Supr., 383 A.2d 278, 280 (1977). The first undisclosed fact was an estimate by a petroleum engineer and vice president of the corporation that the company's net asset value was significantly higher than the amount disclosed in the tender offer. The second fact was that the majority stockholder's management had authorized open market purchases at $15.00 per share just prior to the $12.00 per share tender offer.

On remand, the trial court, relying on cases involving fraudulent misrepresentation, applied the "Delaware block" appraisal formula (which has now been rejected by the Supreme Court in this case, 429 A.2d at 712-714) as the measure of damages. Lynch II, 429 A.2d at 500-501. The Supreme Court reversed, holding that, unlike a claim of fraudulent misrepresentation, a claim for breach of fiduciary duty permits equitable relief in the form of an accounting or rescission or other remedy afforded for a breach of trust by a fiduciary. Id.

The Lynch court noted that Delaware law supports the right of stockholders to rescind sales of their stock which were induced by materially misleading representations by a majority stockholder and that rescission is the preferable remedy for disclosure violations when feasible. Id. at 501. However, where rescission is not feasible, rescissory damages may be awarded to reflect "the monetary equivalent of rescission", that is, "the increment in value that [the majority stockholder] enjoyed as a result of acquiring and holding the [minority's] stock." Id.*

In Lynch, the Court found that rescissory damages were appropriate where a majority stockholder had induced minority stockholders to sell their shares voluntarily by omitting two material facts in the tender offer. The award was based on "the principle which prohibits a fiduciary from keeping what he acquired in a transaction preceded by less than a fair disclosure of facts germane to the transaction." 429 A.2d at 503-504. (Emphasis in original).

C. The Supreme Court Findings Destroy Defendants Claims that Rescissory Damages Should Not Be Considered

The rescissory damages issue before this Court is simple:

> Who should receive any profit realized by Signal as a result of it acquisition of UOP's minority shares - Signal, which failed to deal fairly with the minority, or the minority stockholders who were the victims of Signal's breach of fiduciary duty?

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* The Court cited with approval 12A Fletcher Cyclopedia Corporations (Perm. Ed.), §5598 and Myzel v. Fields, 386 F.2d 718, 742 (8th Cir. 1967), cert. denied, 390 U.S. 951 (1968) which state that, where rescission is not possible, the proper measure of damages is the equivalent value of the stock at the time of resale or at the time of judgment. 429 A.2d at 501-502.

Since the equities obviously lie with the minority stockholders (Lynch II, 429 A.2d at 506), Signal has a very heavy burden to demonstrate why, despite its breach of fiduciary duty, it should be allowed to keep the gains resulting from that breach. Aside from its attempted relitigation of the Arledge-Chitiea report, Signal has made no effort to meet its burden.

1. Lynch II Supports an Award of Rescissory Damages In this Case

The Supreme Court overruled Lynch II only to the extent that opinion purported to limit the Chancellor's discretion to a single remedial formula for monetary damages. 457 A.2d at 703-04, 714. Nowhere in the Supreme Court's opinion is there any indication that Lynch II was wrongly decided on its facts or that rescissory damages should not be awarded where a majority stockholder fails to disclose material information to the minority under circumstances amounting to a breach of fiduciary duty. Accordingly, Lynch II is persuasive precedent for awarding rescissory damages for nondisclosure of material facts by a majority stockholder. Certain of the misconduct found in this action is virtually the same as the nondisclosures which the Supreme Court found in Lynch II warranted imposition of rescissory damages. Specifically, Signal, the majority stockholder, has been found to have withheld (a) a report prepared by members of the corporation's management which suggested a higher value for the company, and (b) information suggesting that the majority stockholder was willing to pay a higher price. Consequently, even a narrow reading of both Lynch II and the misconduct found by the Supreme Court in this action justifies application of rescissory damages in this case.

2. Defendants' Misconduct is Far More Pervasive Than Lynch II

Signal would like this Court to believe that the only misconduct the Supreme Court found was the failure to disclose the Arledge-Chitiea report and one or two other germane facts. Signal would further like to pretend that the nondisclosures found were less significant or no more significant than the nondisclosures found in Lynch. However, an examination of the Supreme Court's findings in this case, and a comparison of those findings with the findings in Lynch II which justified application of rescissory damages, shows conclusively that Signal's arguments are no more than the wishful thinking of an adjudicated wrongdoer.

First, Signal's nondisclosure misconduct is far worse than the conduct justifying rescissory damages in Lynch. Here the persons making the report suggesting a higher value were not merely officers of the company, but were directors of both the company and the majority stockholder. Furthermore, the report and information suggesting the majority stockholder was willing to pay a higher price were withheld not only from the stockholders, but also were withheld from the outside directors of the company even though the information was made available to all the majority stockholders' directors. In addition, in Lynch the corporation's board made no recommendation to the stockholders as to whether to accept or reject the tender offer. Lynch v. Vickers Energy Corp., Del.Ch., 351 A.2d 570, 571 (1976), rev'd., Del.Supr., 383 A.2d 278 (1977). In contrast, UOP's proxy statement told the stockholders UOP's Board had unanimously endorsed the merger. 457 A.2d at 708.

Second and more importantly, the Supreme Court did not just find that Signal had failed to disclose germane facts. Rather, based on deficiencies in Signal's conduct as to all five elements of fair dealing, the Supreme Court found Signal had failed to satisfy any reasonable concept of fair dealing and that the merger did not meet any reasonable test of fairness. 457 A.2d at 712. The timing of the transaction was for Signal's benefit and Signal was at fault for the hasty presentation of the merger to UOP's Board and the hurried and superficial preparation of Lehman Brothers' fairness opinion. 457 A.2d at 711-712. Signal initiated the merger and structured it by use of a feasability study prepared by two UOP directors using UOP information -- a study not disclosed to UOP's outside directors or minority stockholders which described the advantages to Signal of ousting the minority stockholders at a price of up to $24.00 per share. Id. at 708-709, 711.

The Court also found that (i) there was no attempt to negotiate the merger on an arm's length basis; (ii) the only thing approaching any "bargaining" was Crawford's attempt to protect benefits for UOP's key employees and to reduce Lehman Brothers' fee; and, (iii) neither UOP's management nor UOP's outside directors even suggested that Signal pay more than $21.00 per share. Id. at 705-708, 710-711. Moreover, the hasty approval of UOP's Board was meaningless because neither the Arledge-Chitiea report nor the fact that Signal considered the merger an outstanding investment at any price up to $24.00 per share was disclosed to UOP's outside directors; nor were the conflicts of interest created by the Arledge-Chitiea study disclosed. Id. at 707-709, 712.

Finally, the Court found that Signal deprived the minority stockholders of germane information including:

(a) The Arledge-Chitiea report and the critical information that Signal considered $24.00 a good investment;

(b) The facts surrounding establishment of the $21.00 price, including the absence of negotiations; and

(c) The circumstances surrounding the rushed and superficial preparation of the fairness opinion, including (i) giving the minority the impression

> that the fairness opinion represented a careful study, (ii) failing to disclose that a draft fairness opinion was brought to the directors meeting with the price left blank, and (iii) failing to disclose that the reliability of the fairness opinion was questionable because Signal had imposed such a rushed timetable.

457 A.2d at 707-708, 711-712, 714.

Even with respect to the Arledge-Chitiea report, the Supreme Court found far more wrongdoing by Signal than just nondisclosure of the material facts in the report. For example, a part of Signal's breach of fiduciary duty was that two UOP directors took confidential UOP data and used that data to prepare a report, exclusively for Signal's benefit, describing the advantages of cashing out the UOP minority. Thus, it was not simply a matter of failing to disclose this germane information; rather, corporate fiduciaries affirmatively used their superior knowledge of UOP data against the interests of the minority stockholders. Moreover, the report created conflicts of interest which Signal resolved in its own favor and, indeed, Signal's members of the UOP Board participated in the March 6 UOP Board meeting without disclosing the conflict of interest they faced because of their knowledge of the report. 457 A.2d at 709, 712. Furthermore, Signal selectively disclosed the portions of the report justifying the $21.00 price, but withheld those portions which supported a higher price. 457 A.2d at 709. Thus, Signal did not just fail to disclose: it used its control of UOP to manipulate the information available to UOP's outside directors.

The Supreme Court's findings of a comprehensive breach of fiduciary duty as to all elements of fair dealing establish a far more powerful justification for rescissory damages in this case than in Lynch II or any other case that has imposed rescissory damages. Given this pervasive pattern of unfair dealing, exclusion of elements of rescissory damages from the fair value determination would mean there would be virtually no circumstances under which a majority stockholder would be required to give back the full profit it made as a result of a breach of fiduciary duty. Thus, majority stockholders will have every incentive to pay an unfair price, since even if a breach of fiduciary duty is found, the most that would be required is that they pay what was the fair price in the first place and retain the balance of their profit. This court should not establish a rule that a majority stockholder who failed to satisfy any reasonable concept of fair dealing to retain any of the profit it realized from its wrongdoing.

CONCLUSION

For the reasons stated above, this Court should (a) deny defendants' application for a preliminary hearing, (b) vacate the stay of plaintiff's discovery and (c) rule that rescissory damages are applicable to this case.

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Dated: April 4, 1984