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IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE SUNBELT BEVERAGE CORP. SHAREHOLDER LITIGATION	))	Consol. C.A. No. 16089-CC

MEMORANDUM OPINION

Date Submitted: November 20, 2009
Date Decided: January 5, 2010

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Jesse A. Finkelstein, Srinivas M. Raju, and Blake Rohrbacher, of RICHARDS LAYTON & FINGER, P.A., Wilmington, Delaware; OF COUNSEL: Howard Graff and Judith R. Cohen, of DICKSTEIN SHAPIRO LLP, New York, New York, Attorneys for Defendants.

CHANDLER, Chancellor

This consolidated breach of fiduciary duty and appraisal proceeding arises out of the August 22, 1997 merger (the "Merger") of SBC Merger Corporation ("SBC") with and into Sunbelt Beverage Corporation ("Sunbelt"). One consequence—and a specific goal—of the Merger was the cash-out of Jane Goldring ("Goldring" or "Plaintiff") as a minority shareholder in Sunbelt.

Goldring contends that members of the Sunbelt board of directors ("Defendants") violated their fiduciary duties in cashing her out at an unfair price, for which Goldring seeks rescissory relief in the form of Arizona, Maryland, or another state in Sunbelt's wholesale alcohol distribution portfolio. In the alternative, Goldring seeks an appraisal of the fair value of her shares of Sunbelt stock as of the Merger date, an award of interest on the value of her shares, and an award of all costs and expenses, including attorneys' and experts' fees. Defendants, meanwhile, ask this Court to determine that the fair value of Sunbelt's stock at the time of the Merger was $45.83, that the Merger process was entirely fair, and that Goldring should not be awarded interest or attorneys' and experts' fees. Finally, defendants also ask the Court to strike exhibit A to Goldring's post-trial answering brief.

For the reasons set forth below, I determine that the fair value of Sunbelt at the time of the Merger was $114.04 per share. I award Goldring her pro rata share of Sunbelt's fair value on the date of the Merger, as well as pre- and post-judgment interest, compounded monthly, at the legal interest rate. I also award Goldring all of her court costs and her experts' fees, but not her attorneys' fees. Lastly, I grant defendants' motion to strike exhibit A to Goldring's post-trial answering brief.

I. BACKGROUND

A. The Parties

Plaintiff Jane Goldring was an individual shareholder in Sunbelt. At the time of the Merger, Goldring held 120,000[1] shares of Sunbelt stock, or approximately 14.9% of the company. Although Goldring was the named stockholder, her husband, William Goldring, managed the investment pursuant to a permanent power of attorney to control all matters related to the Sunbelt stock.[2] The Goldring family has been engaged in the wholesale liquor business for four generations. Goldring viewed her investment in Sunbelt as a long-term investment, which would enable her to increase the presence and market share of the Goldring family in the wholesale alcohol distribution industry.

Defendant Sunbelt is a privately-held Delaware corporation engaged in the business of wholesale distribution of wine and spirits in multiple states. Sunbelt

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[1] In their pre-trial stipulation, the parties agreed that Goldring held 120,000 shares of Sunbelt stock. The parties also stipulated that Goldring acquired her shares through two separate transactions, which, as discussed below, involved 54,000 shares and 60,000 shares, respectively. This appears to be a case in which the whole is greater than the sum of its parts. Given, however, that the parties agreed that Goldring held 120,000 shares, I will not probe more deeply the details relating to the number of shares Goldring held.

[2] For purposes of this Opinion, I will not differentiate between Goldring and her husband when I describe business activities and decisions.

formerly was a division of McKesson Corporation ("McKesson"), a public corporation that in 1988 began to divest its wine and spirits operations. McKesson approached Ray Herrmann ("Herrmann"), the former Vice-Chairman of McKesson Wine & Spirits, to inquire whether he would be interested in purchasing McKesson Wine & Spirits from McKesson. Herrmann responded by organizing a group of investors, including investment funds from the private investment firm of Weiss, Peck, and Greer ("WPG"),[3] to purchase McKesson Wine and Spirits. That purchase constituted the birth of Sunbelt. The consideration McKesson received for its 1988 sale of McKesson Wine & Spirits included a block of stock in Sunbelt and the right to designate a member of Sunbelt's board of directors so long as McKesson was a Sunbelt shareholder. Following this sale, McKesson and WPG were the primary shareholders of Sunbelt. Several other individuals held smaller amounts of Sunbelt stock and were involved in the management of Sunbelt.

The individual defendants were all members of Sunbelt's board of directors from at least mid-1994 through at least August 1997. These individuals include: Herrmann, Eugene Luciana, Herman Merinoff ("Merinoff"), Charles Merinoff, Spencer Merinoff, and Charles Andrews. Notably, the Merinoffs had been involved in the wholesale alcohol distribution industry for at least three generations.

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[3] WPG's involvement in this divestiture was its first foray into the wholesale alcohol distribution industry.

B. Industry Background

In 1997, at the time of the Merger, a large number of states regulated the sale and importation of alcoholic beverages through a three-tier system, with suppliers at the top, wholesalers or distributors in the middle, and retailers at the bottom. Separate licenses were required to operate at each tier. Suppliers of alcoholic beverages generally could sell only to licensed in-state wholesalers, and wholesalers in turn generally could sell only to licensed in-state retailers. As of 1997, there were no publicly-traded distributors in the United States; regardless of size, these distributors universally were private closely-held companies, often family-owned, and did not make public disclosures of financial affairs.

C. Goldring Becomes a Sunbelt Shareholder

In 1991, Sunbelt acquired certain alcohol distribution rights in Florida held by Goldring, and in return issued to Goldring 54,000 shares of Sunbelt stock. At that time, the controlling shareholder in Sunbelt was WPG.

D. WPG and McKesson Seek to Sell Their Sunbelt Shares

In 1994, Philip Greer of WPG approached Goldring and asked if Goldring would be interested in acquiring the majority interest in Sunbelt held by WPG and McKesson. Goldring declined to make the acquisition but did express an interest in purchasing some number of additional shares of Sunbelt stock. Herrmann suggested WPG and McKesson approach Merinoff to inquire about his interest in purchasing the controlling share of Sunbelt. By a stock purchase agreement dated March 31, 1994 ("1994 Agreement"), Colmar Investment Company LLC, an investment vehicle for the Merinoff family and certain other persons close to the Merinoffs, acquired Sunbelt common stock from WPG, McKesson, and other Sunbelt stockholders. Peter Pfister ("Pfister") was the WPG representative principally responsible for WPG's role in the negotiations of this agreement. The 1994 Agreement permitted the buyers to make purchases of Sunbelt stock over a period of three years, subject to a formula that would calculate the purchase price for each round of purchases ("WPG Formula" or "Formula").[4] At the same time as the 1994 Agreement, Goldring entered into a share purchase agreement ("1994 Shareholder Agreement") and acquired an additional 60,000 shares of Sunbelt stock. The 1994 Shareholder Agreement established, *inter alia*, that the WPG Formula would be the basis for a put of or call on Goldring's shares should certain triggering events occur.

E. Business Sweetens, Relations Sour

Goldring and Merinoff provide different accounts of events between March 31, 1994 and August 20, 1997. What is indisputable is that Sunbelt faced various business challenges in the early stages of that three-year period, including the loss of a key product line in Florida and South Carolina, but by 1997 Sunbelt seemed to

[4] There is a significant dispute over the implications of the various components of the Formula, which I discuss later in this Opinion.

have overcome those challenges and had posted record profits for the company. Goldring alleges that after becoming a Sunbelt shareholder she had received a steady stream of financial information about Sunbelt's operations, but that the flow dramatically decreased after the Merinoff interests assumed control of Sunbelt in 1994. Merinoff denies any decrease in financial information. By the spring and summer of 1997, an exchange of letters and conversations occurred, in which Merinoff expressed an intent to acquire Goldring's shares in Sunbelt, and in which Goldring expressed no interest in parting with those shares at the price Merinoff was offering. The initial exchange appears to have occurred during a trip to France. In a letter dated May 22, 1997, Goldring indicated he believed Merinoff's offer price extremely undervalued Sunbelt, especially given how profitable a year 1997 was proving to be for Sunbelt. In that letter, Goldring also suggested that an exchange could be made in which Goldring would acquire full rights to certain segments of Sunbelt's portfolio in return for Merinoff acquiring Goldring's shares.

Goldring believed Merinoff's offer price to be so low that she offered in a June 27, 1997 letter to purchase the entirety of the Sunbelt stock she did not already own. The purchase price of Goldring's offer was identical to the per-share price Merinoff had proposed for Goldring's own stock. If any other Sunbelt shareholder took Goldring's offer seriously, no one accepted. The letter and Goldring's offer had no impact. Merinoff reemphasized his intent to acquire

Goldring's shares, and Goldring reemphasized her view that Merinoff's valuation of Sunbelt stock was off the mark.

F. A Brewing Relationship with Young's Market

The summer of 1997 also saw an acceleration of planning for a stock swap between Sunbelt and Young's Market, the largest wholesale alcohol distributor in California as of 1997, with each company receiving 15% of the other. Goldring appears to have heard of the proposed relationship with Young's Market through the grapevine, and she believed a business relationship between Sunbelt and Young's Market would greatly enhance the value of Sunbelt, particularly given the consolidation in the industry that was occurring at that time. She mentioned this relationship and the business benefits in her June 27, 1997 letter. Yet in a July 14, 1997 letter, Merinoff informed Goldring that the stock swap with Young's Market was dependent upon Goldring's 15% share in Sunbelt being the Sunbelt stock that would be used in the stock swap.[5] In that same letter, Merinoff expressed his recollection that Goldring had previously made a verbal agreement with Merinoff to relinquish her shares upon Merinoff's request, at a price to be determined by the WPG Formula. On July 21, 1997, Herrmann sent Goldring a letter expressing that

[5] Vern Underwood, the President, Chairman, and CEO of Young's Market, testified in a 2001 deposition that he had never given a thought to which 15% of Sunbelt's stock Young's Market would need to acquire in 1997. That is, it appears Young's Market was indifferent to whether the Sunbelt stock was stock owned by Goldring or stock owned by any other Sunbelt shareholder, or newly issued shares of Sunbelt.

he too recollected that Goldring had previously promised Merinoff that Goldring would relinquish her Sunbelt stock upon request.

G. Final Purchase of Stock from McKesson and WPG

On July 31, 1997, McKesson and WPG sold their last remaining shares of Sunbelt stock to the Merinoffs ("July 31, 1997 Transaction" or "1997 Transaction"). The WPG Formula price for that transaction was $45.83. In completing the sale and parting with the last of its Sunbelt stock, McKesson was no longer entitled to a seat on Sunbelt's board of directors.

H. The August 6, 1997 Board Meeting

Sunbelt's board convened a week later, on August 6, 1997, to discuss a variety of matters, including the proposed business alliance with Young's Market. The board discussed the promises Goldring was said to have made relating to relinquishment of her stock at Merinoff's request, as well as her denial of having made any such promises. Before the conclusion of the meeting, the board authorized Sunbelt's officers to obtain a fairness opinion for a $45.83 per-share offer for Goldring's stock.

I. The Hempstead Fairness Opinion

Between Friday, August 8, 1997, and Friday, August 15, 1997, Mark Penny of Hempstead & Co. conducted a valuation of Sunbelt and prepared a fairness opinion for a proposed Sunbelt stock transaction at $45.83 per share. Penny prepared this opinion in one week's time while simultaneously working on and traveling for another project. Penny's opinion used the following valuation approaches (and reached the following valuations): a discounted cash flow analysis ($36.68 per share); an analysis of prior transactions involving Sunbelt stock ($45.83 per share);[6] and an asset-based approach ($33.57 to $37.06 per share). On the basis of these valuations, Penny issued a fairness opinion that $45.83 was a fair price for a share of Sunbelt stock.

J. The August 18, 1997 Board Meeting

On August 18, 1997, Penny presented his fairness opinion to the Sunbelt board. The Sunbelt board then issued two authorizations: first, a call (the "Call") on Goldring's shares per the 1994 Shareholder's Agreement—which specified the Call would be at the WPG Formula—and, second, a freeze-out merger at the same WPG Formula price, or $45.83 as of July 31, 1997. The Merger became effective on August 22, 1997.

K. Litigation Commences

By letter to Sunbelt dated September 9, 1997, Goldring demanded appraisal of her shares under Delaware law. On December 12, 1997, Goldring filed her appraisal action in this Court, seeking a determination of the statutory fair value of her stock on August 22, 1997 plus interest, fees, expenses, and costs arising out of

[6] The earlier transactions were those involved in the July 31, 1997 sale of McKesson's and WPG's shares in Sunbelt, at the WPG Formula price.

the Merger. Nearly two years later, on August 12, 1999, Goldring filed a common law action for breach of fiduciary duty against Sunbelt and defendants, seeking rescission and rescissory damages. The latter filing occurred within weeks of a final decision by the United States District Court for the Southern District of New York that compelled Goldring to participate in arbitration that Sunbelt sought pursuant to the 1994 Shareholder Agreement. I stayed the Delaware proceedings, pending the outcome of arbitration in New York.

The New York arbitration hearing was conducted from October 1, 2001 through October 4, 2001. On December 18, 2001, the arbitration panel held that the Call and the Merger were attempts to eliminate Goldring as a minority shareholder without notice and without legal justification and to obtain her stock at a formula price, and that the Call was neither valid nor supported in law or in fact. The panel also held that it found no persuasive evidence that Goldring had ever promised she would relinquish her shares to Merinoff upon request, at the WPG Formula price or at any other price.

Following the conclusion of the New York arbitration, I lifted the stay on the Delaware proceedings and consolidated Goldring's appraisal action and her common law breach of fiduciary duty action. A three-day trial in the consolidated action was held on April 14, 16, and 17, 2009.

L. Expert Valuations

At trial, I heard testimony from valuation experts for both Goldring and defendants. Goldring's expert was Dr. Richard S. Ruback, the Willard Prescott Smith Professor of Corporate Finance at the Harvard Business School. Defendants' expert was Robert Reilly, a managing director of Willamette Management Associates, which is a valuation consulting, economic analysis, and financial advisory services firm.

Ruback used the following valuation approaches (and reached the following valuations): a discounted cash flow analysis ($114.04 per share)[7] and a comparable transactions analysis ($104.16 per share).[8]

Reilly used the following valuation approaches (and reached the following valuations)[9]: a discounted cash flow analysis ($36.30 per share), an analysis of

[7] This analysis and per-share value are Ruback's corrections to Reilly's own discounted cash flow analysis, to account for what Ruback believes are overstatements in Sunbelt's weighted average cost of capital. The Ruback and Reilly valuation models thus do not differ in terms of the underlying financial inputs. I note that Ruback had prepared an earlier discounted cash flow analysis, which involved corrections to Penny's own discounted cash flow analysis and which valued Sunbelt at $116.77 per share. One source of divergence between this value and $114.04 is the differing amounts for Sunbelt's fully diluted shares outstanding, as applied in the Reilly and Penny analyses.

[8] I will discuss below details relating to two versions of Ruback's comparable transactions analysis. The final operative per-share value, however, is $104.16.

[9] These valuations are described in defendants' post-trial briefs as those based upon Reilly's initial calculations but also "adjusted based upon the trial evidence." Defs.' Post-Trial Br., 62.

earlier transactions involving Sunbelt stock ($45.83 per share),[10] and an asset-based approach ($42.12 per share).

II. ANALYSIS

This case consists of both an entire fairness action[11] and a statutory appraisal action. The dual prongs of entire fairness—fair dealing and fair price—must both be satisfied.[12] Here, defendants bear the burden of demonstrating that the Merger was entirely fair, as they did not "use any of the procedural devices that could temper … the application of the entire fairness standard, such as a special negotiating committee of disinterested and independent directors or a majority-of-the-minority stockholder vote provision."[13] The element of fair price, furthermore, relates closely to the determination of fair value under the Delaware appraisal statute, 8 Del. C. § 262.[14] I therefore begin my analysis by examining briefly the issue of fair dealing and then turn to the related issues of fair price and statutory appraisal. I conclude with an examination of additional considerations, including

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[10] The prior transactions were those involved in the July 31, 1997 sale of McKesson's and WPG's shares in Sunbelt, at the WPG Formula price.

[11] The relevant standard of review in this case is entire fairness, as there is no dispute that all defendants stood on both sides of the transaction. *See Kahn v. Lynch Commc'ns Sys., Inc.*, 638 A.2d 1110, 1117 (Del. 1994).

[12] *See Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983).

[13] *Delaware Open MRI Radiology Assoc. v. Kessler*, 898 A.2d 290, 311 (Del. Ch. 2006).

[14] For additional discussion of this, see *id.* at 312 (noting that the "key issues relevant to each type of claim are common, and the differing rubrics have relatively little influence on the bottom line outcome of the case, which turns on whether the merger was financially fair.").

the shifting of fees and costs, and defendants' motion to strike an exhibit to Goldring's post-trial answering brief.

A. Fair Dealing

The goal of the Merger was to eliminate Goldring as a Sunbelt shareholder for the sole purpose of enabling the Merinoff family to join forces with Young's Market. The various attempts to acquire Goldring's shares in the months and weeks leading up to the Merger, itself ultimately a method of last resort, provide clear evidence of the intent behind the Merger. In their totality, defendants' tactics and approaches were nothing short of strong-armed. Sunbelt board members first communicated directly with Goldring in an attempt to acquire her Sunbelt shares at the WPG Formula price, alleging in a coordinated attack that Goldring had promised to sell her shares back to the Merinoffs upon the simple request from the Merinoffs that she do so. When these efforts bore no fruit, defendants issued the Call on Goldring's shares, which under the terms of the Shareholder Agreement was priced per the WPG Formula. Not surprisingly, the New York arbitration panel ultimately held the Call to be without justification in law or fact. Having foreseen the possibility that a court or arbitration panel may hold the Call to have been unjustified, defendants also approved a squeeze-out merger, devoid of procedural protections, as a final means of forcing Goldring out of the company and obtaining her 15% stake.

The process here was anything but fair. Instead, defendants employed a process that was jerryrigged every step of the way and that was transparent in its goal to eliminate Goldring before a stock swap with Young's Market, and to obtain her stock at the WPG Formula price. The ultimate step in the process, the Merger, included no procedural protections designed to ensure arm's-length bargaining or to approximate a fair valuation procedure. There was no special committee, no opportunity for genuine negotiations regarding the merger consideration, and no dissemination of material information that would level the playing field and prevent Goldring from becoming a drastically disadvantaged minority shareholder. Before the Merger was authorized, defendants obtained a fairness opinion for the proposed merger consideration of $45.83. Yet that fairness opinion itself is highly suspect. It was produced in approximately one week—during which the lead appraiser was busy working on at least one other matter that included a cross-country site visit and, thus, unable to work extensively and meaningfully with Sunbelt representatives—and just before the Sunbelt board meeting at which the board voted to issue the Call and to authorize the Merger. The "fairness opinion" was a mere afterthought, pure window dressing intended by defendants to justify the preordained result of a merger at the Formula price of $45.83 per share. In short, defendants abjured any semblance of a fair process.

B. Fair Value and Statutory Appraisal

The fairness of the Merger price is an analytical question "common to both the entire fairness and appraisal claims."[15] For the purposes of fair value, I will address the claims as one, through an analysis of the various methodologies employed in the parties' determination of Sunbelt's value at the time of the Merger. On the basis of that analysis I will determine which methodologies are most appropriate under Delaware law and in light of the particular circumstances of this case. On that basis, I will then determine the fair value of Sunbelt at the time of the August 22, 1997 Merger.

1. <u>WPG Formula</u>

At the heart of defendants' argument lies the WPG Formula. As discussed above, the WPG Formula determined the per-share price of Sunbelt stock for purposes of stock transactions that occurred between 1994 and 1997 and involved Herman Merinoff and others acquiring the remaining holdings of McKesson and WPG in Sunbelt. Defendants describe the WPG Formula as the outcome of an arm's-length negotiation between sophisticated parties and, thus, relevant under Delaware law as evidence of the fairness of the price Goldring received for her shares in the 1997 Merger, even if the negotiations underlying the Formula occurred in 1994 (three years before the cash-out Merger was even contemplated).

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[15] *Id.* at 311.

Goldring asserts that there is no basis to assume the WPG Formula reflects fair value and that defendants' reliance on transactions pursuant to the Formula is circular. Ultimately, I conclude that the WPG Formula price is neither relevant to nor evidence of fair value and, thus, I decline to accord it any weight whatsoever in my determination of Sunbelt's fair value at the time of the Merger.

Defendants are correct in their assessment of the evidentiary import Delaware courts have accorded prior transactions in a company's stock. That import is grounded in the reasoning that the "fact that major shareholders … who had the greatest insight into the value of the company, sold their stock … at the same price paid to the remaining shareholders … powerfully implies that the price received was fair."[16] Additionally, even when provided with the results of expert valuations, a court may find arm's-length negotiations to be the most persuasive evidence of fair value.[17] But the cases to which defendants direct the Court involved transactions very different from the July 31, 1997 Transaction, and those differences are fatal to defendants' argument.

The 1997 Transaction did constitute an exchange of Sunbelt shares for cash, did occur in the weeks leading up to the Merger, and did involve sophisticated

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[16] *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 117 (Del. 1995) (quoting *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134, 1143 (Del. Ch. 1994)).

[17] *See, e.g.*, *Prescott Group Small Cap, L.P. v. Coleman Co.*, 2004 WL 2059515, at *32 (Del. Ch. Sept. 8, 2004) (finding that "the most reliable and persuasive evidence of [the company's] fair value at the time of the [merger] is the value of the consideration that was negotiated at arm's length, and that [the acquirer] actually paid, to acquire the controlling interest [in the company] and to cash out the options held by minority shareholders.").

parties, both of which were members of (or had representatives on) Sunbelt's board of directors immediately before the 1997 Transaction. At first blush, these characteristics of the 1997 Transaction make the transaction seem similar in form to other earlier transactions that Delaware courts have examined and weighed when conducting valuation analyses. Yet this description of the 1997 Transaction does not reveal the key fact that the terms of the transaction were controlled by an agreement negotiated and signed *three years earlier*, in 1994, rather than the results of negotiations that occurred immediately before (or contemporaneously with) the Merger. The latter is the type of transaction that this Court has considered as relevant evidence to the question of fair value. The former is not.

There is no bright-line rule relating to the maximum length of time that may occur between an earlier transaction and a cash-out merger before the Court discounts the weight of the earlier transaction as evidence of fair value. Given the unusual circumstances here and the nature of this particular business, however, I conclude that three years is far too wide a gap between the two events. Defendants present what they describe as an "extensive record which establishes that the 1994 Transaction (whereby the Merinoff interest became shareholders in Sunbelt) and the WPG Formula (used to price subsequent stock purchases) were the result of hard, arm's-length negotiations between knowledgeable, financially sophisticated parties each seeking to maximize their economic self-interests."[18] Those negotiations may have been hard and at arm's length, and the parties to them may have been knowledgeable and sophisticated, but what contractual terms the parties were willing to agree to in 1994 may be—and likely are—very different from the contractual terms that the parties would agree to in 1997, let alone different from the fair value of Sunbelt in 1997 as determined by the valuation techniques Delaware courts most frequently apply.

Defendants ask the Court to bridge the gap between 1994 and 1997 by considering the following question: if Sunbelt's 1997 fair value actually was anywhere close to the value Goldring ascribes to it, why would sophisticated investors such as McKesson, Pfister, and WPG agree to accept $45.83 per share in the sale of their remaining Sunbelt shares? According to defendants, "Pfister, WPG, and McKesson would not have been content to walk away from the many millions of dollars"[19] that adherence to the WPG Formula in effect would have denied them, even if it is the case, as defendants predict Goldring would assert, "that the sellers were contractually obligated to accept [the WPG Formula] price."[20] Furthermore, McKesson had a seat on Sunbelt's board until the sale of its last remaining shares in Sunbelt, which meant McKesson was in a position to have

[18] Defs.' Post-Trial Br., 8.
[19] *Id.* at 19.
[20] *Id.*

great insight into the value of Sunbelt and to gauge if over the course of three years there had grown to be a significant difference between: 1) the value of the company and 2) the share price as determined by the WPG Formula. But it is not up to me to gauge how effectively McKesson used whatever insight its board position provided it between 1994 and 1997. Nor am I entitled to speculate about the possible motivations of McKesson, Pfister, or WPG when they negotiated the terms of their exit strategy in 1994.[21] Ultimately, however, I am not persuaded by (nor do I find credible) any of the evidence offered by defendants that I should accept the valuation of Sunbelt that interested parties had struck *over three years before* defendants decided to cash out Goldring. It was defendants' burden to persuade me to accept the Formula as a proxy for Sunbelt's value, and they failed to meet their burden.

Despite my strong hesitation to accept the 1997 Transaction as evidence relevant to a determination of fair value, there are additional reasons to examine

[21] Nor can I determine the motivations of these individuals and groups at the time they negotiated and signed the 1994 Agreement. As noted above, Sunbelt describes those motivations as involving the maximization of economic interests. Goldring counters with a description of other motivations that may have guided the final decisions of the private-equity investors, even if those decisions resulted in a failure to maximize the value of their shares in Sunbelt as part of the transactions pursuant to the 1994 Agreement. These other potential motivations include ensuring a sufficient return on investment (rather than pure maximization of returns, or gauging returns in the same way Delaware courts determine fair value) or employing exit strategies based more on a strict time schedule rather than on returns on investment (for example, holding assets in a company or industry for no more than five to seven years). In deciding to what extent, if any, to weigh the WPG Formula in my determination of Sunbelt's fair value at the time of the Merger, I need not determine what motivations (or balance of motivations) guided those who were parties to the 1994 Agreement.

the WPG Formula more closely.[22] In short, although I believe the Formula is unreliable for the reason stated earlier, I nonetheless will examine the specific nature of the Formula.

Even a brief examination of that specific nature leads me to believe that the WPG Formula should not be used to determine fair value in this proceeding. First, the WPG Formula relies too heavily on the book value of Sunbelt,[23] provides a premium reliant solely on the company's net income in the two years preceding any Formula-based transaction,[24] and does not adequately incorporate the influence of intangibles and good will on the company's value.[25]

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[22] Goldring alleges that the WPG Formula in fact is the driving force behind Sunbelt's other valuation approaches, and has tainted the methodological integrity of those other approaches. I need not examine the connection between the WPG Formula and the results of Sunbelt's other valuation analyses, as there are independent reasons for rejecting those analyses.

[23] I do not believe Sunbelt to be a company in an industry—wholesale alcohol distribution—whose characteristics merit much, if any, use of book value in a determination of a company's fair value. Companies in this industry rely chiefly on agreements and good relationships with suppliers to conduct their primary business: moving and selling alcohol. Contrast this industry with one based primarily on natural resources or the intense reliance on physical, long-term assets, such as the coal or steel industry. Companies in the latter industries derive far more value from the use and maintenance of their physical assets, thus arguably justifying valuation driven by book value. Sunbelt, however, does not. It is for this reason that I also do not accord weight to Reilly's asset-based valuation approach, and decline to provide here a detailed discussion of that approach's specific findings. For an example of a context in which an asset-based approach is more appropriate, see *Neal v. Alabama By-Products Corp.*, 1990 WL 109243 (Del. Ch. Aug. 1, 1990), *aff'd*, 588 A.2d 255 (Del. 1991).

[24] Although I recognize that this premium did enable Pfister, WPG, and McKesson to realize some of any increases in Sunbelt's profitability that occurred while they remained Sunbelt shareholders, I do not believe a premium based on tax-adjusted net income adequately captures all elements of fair value to which a Sunbelt shareholder, or a former shareholder now contesting the Merger price, is entitled under Delaware law.

[25] As already noted, *see supra* note 23, Sunbelt is a company that relies heavily on agreements and good relationships with suppliers. Sunbelt's reputation in the industry, dependent in part on the names and reputations of the individuals who were shareholders in Sunbelt, is an intangible

Ruback's own quantitative examination of the WPG Formula also gives me pause, even beyond the complaint that the Formula does not calculate what the Court should accept as an indication of fair value. For example, Ruback compared the market capitalization of twelve public companies in SIC Code 514[26] to the value of those companies as calculated by the WPG Formula. On average, the WPG Formula valued these twelve public companies *three times less* than their market capitalizations.[27] Although I recognize that market capitalization is not necessarily—and most likely is not—strictly equivalent to fair value and that the efficient markets hypothesis has received due criticism, I also believe a consistent and drastic undervaluing of companies relative to their market capitalization in liquid equity markets strongly implies that the WPG Formula is valuing something very different from fair value. Furthermore, it is reasonable to expect that the WPG Formula would reach similar, even if not identical, results for a collection of companies outside SIC Code 514. If this Court and its valuation methodologies had, in the past, reliably and consistently determined the fair value of public

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asset. So too are the various agreements Sunbelt has with suppliers, even if those agreements can be canceled at a moment's notice, and particularly if the agreements are less likely to be canceled given Sunbelt's reputation in the industry and any enhancements to that reputation over time, however derived. The WPG Formula excludes these and other intangibles and, thus, fails to capture what I believe to be a significant source of value to Sunbelt, its operations, and its shareholders.

[26] As described in Ruback's expert rebuttal report, SIC Code 514 "includes wholesalers of groceries and related products, the industry with publicly traded firms most comparable to wholesalers of beverage alcohol, which are not publicly traded."

[27] Pl.'s Post-Trial Br., 56.

companies to be one-third of their market capitalization, I might have less concern about valuations using the WPG Formula. Defendants have not, however, provided any credible evidence that this Court's decisions and valuations suggest public securities markets systematically value companies at *three times their fair value*.

Perhaps with complete indifference to the evidence that the WPG Formula calculates the values of companies to be far lower than the value as determined by liquid securities markets, defendants ask the Court to consider the fact that Goldring "agreed that the WPG Formula would be utilized as a pricing mechanism for Sunbelt's option to purchase all of [her] shares (or [her] option to sell [her] shares) upon certain triggering events."[28] Defendants assert that "[w]hile these options are triggered by certain specific circumstances, if there were a chance any of those might occur, it is reasonable and appropriate to conclude that [Goldring] took pains to ensure [she] would receive a fair price for [her] Sunbelt shares."[29] This argument, however, has no legal relevance in the context of an appraisal proceeding. For one thing, there simply are too many variables that can change over the course of three years' time and over the shift in factual and legal contexts from the pricing of a put/call option—which is subject to a variety of triggering

[28] Defs.' Post-Trial Br., 16. This agreement occurred as part of the 1994 Shareholders Agreement.
[29] *Id.* at 18.

events—to the determination of fair value. In 1994, Goldring agreed to a valuation methodology in the event of a valid put or call. But no valid put or call ever occurred. Thus, the agreement has absolutely no relation to Goldring's statutory appraisal rights or to the accompanying valuation methodologies to which Goldring is now entitled under Delaware law.

The WPG Formula may have guided an unrelated transaction that occurred in the weeks before the Merger, but it was the result of an agreement negotiated and signed *three years before the Merger*. Given the potential for change in circumstances affecting Sunbelt's valuation over those three years, as well as the specific nature of the Formula and evidence that suggests the Formula tends to undervalue companies quite significantly, I attach no weight to the WPG Formula in my determination of Sunbelt's fair value at the time of the Merger.

2. Comparable Transactions Analysis

Defendants attack Ruback's comparable transactions analysis in its entirety, on the grounds that the analysis is flawed both methodologically and factually. Goldring proposes that I weigh Ruback's comparable transactions analysis as 50% of my final determination, though it is unclear if Goldring's proposal relates to Ruback's original analysis or his adjusted analysis.[30] For reasons I briefly describe

[30] Reilly indicated that Ruback's original comparables analysis did not account for the potential upwards impact of synergies on the pricing of the comparable transactions and, thus, the analysis's calculation of $149.69 per share may have been an overvaluation. Ruback responded

below, I believe it is most appropriate to accord no weight to either of Ruback's comparable transactions analyses.

The clash on comparables plays out on the field of fact rather than on the landscape of law. Goldring correctly notes that Delaware courts have used the comparable transactions approach when determining the fair value of companies,[31] and defendants are correct that Delaware courts have expressed reservations when using the approach[32] and that "the burden of proof on the question whether the comparables are truly comparable lie with the party making that assertion."[33] The parties do not appear to disagree on the relevant law. Here, the question turns on whether the companies involved in the transactions that underlie Ruback's analysis are sufficiently comparable to Sunbelt to merit inclusion of the transactions and thus to inspire confidence in the results of Ruback's comparables analysis. The inquiry also depends on whether certain aspects of Ruback's methodology

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by explaining his views that synergies likely did not influence the valuation upwards, yet he still completed an adjusted comparable transactions analysis that did account for the possibility that the comparable transactions were valued higher in anticipation of realizing synergies. Ruback's adjusted analysis resulted in an average per-share value of Sunbelt of $104.16.

[31] *See, e.g.*, *Dobler v. Montgomery Cellular Holding Co.*, 2004 WL 2271592 (Del. Ch. Sept. 30, 2004), *aff'd*, 880 A.2d 206 (Del. 2005) (affirming the Chancery Court's decision to give 65% weight to a comparable transactions analysis).

[32] *See, e.g.*, *Kleinwort Benson Ltd. v. Silgan Corp.*, 1995 WL 376911, at *4 (Del. Ch. June 15, 1995) (determining that a merger and acquisition analysis was unhelpful for appraising the going concern value of a company, given that the "merger and acquisition data undoubtedly contain[ed] post-merger value, such as synergies with the acquirer, that must be excluded from appraisal value.").

[33] *ONTI, Inc. v. Integra Bank*, 751 A.2d 904, 916 (Del. Ch. May 26, 1999).

sufficiently compensate for concerns the Court may have regarding the suitability of specific elements of transactions Ruback used in his analysis.

I do have doubts about the comparability of the companies included in Ruback's analysis. These doubts are driven by the differences in size between the comparables and Sunbelt,[34] as well as the differences across product lines and geography, both of which stand to introduce differences across regulatory regimes. Furthermore, the companies were all privately held in a tightly controlled market. I am hesitant to examine what apparently are personality-driven transactions in a private market and to use the terms of those transactions to project what the value of another transaction should be.[35] When faced with these concerns, it is important to be particularly diligent about selecting companies and transactions that are as comparable as possible to the company in question. Ultimately, I am skeptical that Ruback's analysis achieved sufficient comparability, which alone is a basis for me to reject it as a reliable indicator of fair value.

Beyond the question of company comparability lie issues relating to methodology. Even if the companies themselves were more comparable to Sunbelt

[34] Ruback testified that due to economies of scale, Sunbelt's large size relative to the companies in the comparable transactions may mean a multiple should be *larger* for Sunbelt than for the comparables and, thus, the small size of the comparables relative to Sunbelt should not be a concern.

[35] Ruback also testified that the specific facts of the transactions in his comparables analysis suggest the terms of those transactions heavily favored the acquirers and, thus, that the sale prices may have been lower than the true values of the companies. This would result in artificially low calculations of the transaction multiples.

than I am willing to find, Ruback failed to account for important elements of specific transactions that stood to influence the accuracy of his calculations. Two examples of these elements are the transactions' inclusions of real-estate payments and post-closing price adjustments. Defendants assert that Ruback's analysis includes these failures and many other discrepancies. In response, Ruback noted that he could not estimate the impact of any such discrepancies without further studying the specific terms of the transactions, and that ultimately he relied on his use of the median multiple approach to compensate for any shortcomings related to specific companies or transactions. Although I do not agree with defendants that Ruback's comments were "academic doubletalk,"[36] I am not willing to rely on the employment of a median multiple approach as a justification for ignoring several known deficiencies in facts and methodology. The median multiple approach is at its best when it smooths out unknown or immeasurable sources of difference and error in an analysis. When, as appears to be the case here, there are known and measurable variations or errors in an already small sample size, the median multiple approach cannot be the sole justification for a failure to account for such variations or errors. That approach may help here to some extent with smoothing,

[36] Defs.' Post-Trial Answering Br., 41. Methodological issues aside, I believe Ruback's testimony was, in general, quite nuanced, and that nuances are what many academics bear in mind when providing expert testimony. And strict etymology aside, I was not impressed with defense counsel's efforts to characterize an appreciation for nuance as an adherence to Orwellian practices.

but I do not find it sufficient to inspire confidence in according weight to the comparable transactions analysis in my determination of Sunbelt's fair value.

There are a number of disputes about the factual and methodological bases of Ruback's comparable transactions analysis. Some of these bases may have increased the calculated values of Sunbelt, and others may have decreased it. It is unclear what resolution of those disputes would do, on balance, to the comparables calculation, but it is clear that neither party has provided me with the information required to independently address the issues with quantitative and methodological confidence. I could accept Ruback's comparables calculation as a Goldilocks valuation, nestled comfortably between valuations potentially above and below \$104.16. Or I could attach partial weight to the comparable analysis in my final determination of Sunbelt's value, reflecting a marginal confidence that Ruback's comparables calculation hits somewhere in the vicinity of Sunbelt's fair value, even if it misses high or low. Given the clear shortcomings in Ruback's comparables analysis, however, I decline to do either. Instead, I attach no weight to Ruback's comparables analysis.

3. <u>Discounted Cash Flow Analyses</u>

The parties disagree on two components that significantly guide the results of their experts' respective discounted cash flow analyses: the appropriate level of the small-firm risk premium, and the propriety of including any kind of company-specific risk premium. I will analyze these two components as they relate to the facts of this case and then briefly assess the legal basis for adjusting the value of Sunbelt to account for its post-Merger conversion to S-corporation status.

a. Small-Firm Risk Premium

The parties agree on the propriety of including a small-firm risk premium in the discounted cash flow analysis. The appropriate value of the premium, however, is a point of stout contention.

Both parties claim their respective experts followed the instructions of Ibbotson Associates ("Ibbotson")[37] when selecting the appropriate value of the small-firm risk premium. Ibbotson provides a table of the premium values that correspond to the deciles of company size as measured by market capitalization. The relationship between company size and premium value is inverse; that is, the larger a company's market capitalization, the smaller the corresponding risk premium. Ruback selected a premium of 3.47%, which is the value Ibbotson indicates should be used for micro-cap companies whose equity capitalization is at or below $201,169,500, or in the ninth and tenth deciles of equity capitalization on the New York Stock Exchange. Reilly, however, selected a premium of 5.78%,

[37] According to their website, Ibbotson Associates is "a leading authority on asset allocation with expertise in capital market expectations and portfolio implementation." Ibbotson Associates, Overview, http://corporate.morningstar.com/ib/asp/subject.aspx?xmlfile=1383.xml (last visited Dec. 18, 2009). In Delaware appraisal actions, valuation experts and this Court often rely on the data and guidance provided by Ibbotson.

which is the value Ibbotson measures as the size premium for companies in the tenth decile of equity capitalization on the New York Stock Exchange.

The divergence in Ruback and Reilly's selection of risk premiums presents the Court with two questions: what is the market capitalization of Sunbelt and the corresponding decile for that market capitalization, and what is the appropriate Ibbotson premium to use in a discounted cash flow analysis of Sunbelt, given that Ibbotson lists premiums for individual deciles as well as premiums for groups of deciles?

The first question poses an issue of circularity. The Ibbotson table assumes one already knows or has an estimate of a company's market capitalization. Based on that knowledge or estimate, one can determine which decile the company falls into and then select the corresponding premium from the Ibbotson table. But when the very issue in dispute is the value of the company itself and when a discounted cash flow analysis is a proposed means for resolving the dispute, the appropriate risk premium cannot be taken as exogenous. That is, a discounted cash flow analysis both *values* the size of a company (and thus points to the appropriate Ibbotson premium to use) and *relies* on the appropriate Ibbotson premium to determine the value of the company. This process is circular; which should come first, the valuation of the company or the selection of the Ibbotson risk premium?

Ruback's selection of a 3.47% premium ensures a larger calculated equity capitalization (and thus a company perhaps deserving of the 3.47% premium) than Reilly's selection of a 5.78% premium (which in turn ensures a smaller calculated equity capitalization and, thus, one perhaps deserving of the 5.78% premium). Reilly goes as far as to say that because his selection of a 5.78% premium results in a valuation that places Sunbelt in the tenth decile—the decile with a corresponding premium of 5.78%—I should take this as evidence that the 5.78% premium is appropriate. I cannot accept this asserted mathematical proof and proposed flow of causality. It is methodologically problematic to rely on a discounted cash flow analysis to determine the Ibbotson risk premium appropriate to use in the discounted cash flow analysis. There must be some independent basis or value[38] used for determining the propriety of applying a risk premium from the Ibbotson table, particularly when, as appears to be the situation here, the company's valuation may actually place the company close to the line between deciles.

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[38] *See, e.g.*, *In re Emerging Commc'ns, Inc. S'holders Litig.*, 2004 WL 1305745, at *18-19 (Del. Ch. May 3, 2004) (acknowledging the possibility of employing an iterative process involving an independent valuation to overcome a circularity problem (in calculating the weighted average cost of capital), but ultimately: 1) rejecting both experts' assumed enterprise valuations; 2) finding that "the only sensible way (in the Court's view) to avoid the circularity … is to use an enterprise valuation of [the company] that is not litigation-drive"; and 3) declining to employ the iterative process and instead selecting independent estimates of both the company's enterprise value and the company's debt-to-value ratio); *Cede & Co. v. JRC Acquisition Corp.*, 2004 WL 286963 (Del. Ch. Feb. 10, 2004) (finding that the record did not support the methodology of using implied fair value (that is, a non-independent basis) to determine the appropriate equity size premium to select from the Ibbotson tables).

Each party's argument provides me with an option for circumventing this methodological problem. Defendants point to the result of Ruback's own comparable transactions analysis[39]—which calculates a value for Sunbelt that would place the company in the tenth decile—as a basis for selecting the tenth-decile premium of 5.78%. Although this calculation is one independent of a discounted cash flow analysis and thus could provide a basis for selecting a small-firm risk premium from the Ibbotson table, I prefer the option presented by Goldring and employed by Ruback: follow the strict language Ibbotson used to describe how it adjusted for small-firm premiums in its own publication, and apply a premium of 3.47% for companies in the ninth or tenth deciles.[40] This approach also helps to answer the second question posed above, that relating to whether to apply a risk premium from an individual decile or one assigned to a composite of deciles. According to Ibbotson, the 3.47% premium is a weighted balance between the ninth-decile premium of 2.65% and the tenth-decile premium of 5.78%. Given the uncertainty in Sunbelt's own value and whether Sunbelt falls on the smaller or larger side of the line between the ninth and tenth deciles, I believe it is more

[39] The analysis to which Sunbelt points is Ruback's adjusted comparable transaction analysis, which calculated an average per-share value of Sunbelt of $104.16.

[40] I elect not to use the comparable transactions analysis as a basis for determining the appropriate Ibbotson risk premium. As discussed earlier, I have several concerns about the methodology and factual information underlying the comparables analysis and, consequently, I will not factor the comparables analysis into my valuation of Sunbelt. It, therefore, is most appropriate not to rely on the comparables analysis's valuation of Sunbelt as a basis for determining the appropriate Ibbotson risk premium to use in a discounted cash flow analysis.

appropriate to select 3.47%, a small-firm risk premium that accounts for the possibility that the company is on either side of the line and that Ibbotson itself seems to have applied to all firms within (or between) the ninth and tenth deciles.

b. Company-Specific Risk Premium

In an appraisal action, "the proponent of a company specific premium bears the burden of convincing the Court of the premium's appropriateness."[41] Defendants accept this burden and point the Court to cases in which the Court has deemed a company-specific risk premium to be appropriate.[42] Yet as Vice Chancellor Strine explained in one of the cases defendants cited, even though courts may approve the use of these premiums, "[t]o judges, the company specific risk premium often seems like the device experts employ to bring their final results in line with their clients' objectives, when other valuation inputs fail to do the trick."[43] Proponents of a company-specific risk premium thus not only bear a burden of proof but also must overcome some level of baseline skepticism founded upon judges' observations over time of how parties have employed the quantitative

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[41] *Hintmann v. Fred Weber, Inc.*, 1998 WL 83052, at *5 (Del. Ch. Feb. 17, 1998).

[42] *See, e.g., Delaware Open MRI Radiology Assoc. P.A. v. Kessler*, 898 A.2d 290, 340-41 (Del. Ch. 2006) (declining to "quibble" with including a company-specific risk premium, and ultimately selecting the more conservative of the two premiums the parties presented); *Henke v. Trilithic Inc.*, 2005 WL 2899677, at *10 (Del. Ch. Oct. 28, 2005) (agreeing that an upwards adjustment to account for company-specific risk was appropriate); *Lane v. Cancer Treatment Ctrs. Of Am., Inc.*, 2004 WL 1752847, at *30-31 (Del. Ch. July 30, 2004) (accepting adjustments for company-specific risk); *ONTI, Inc. v. Integra Bank*, 751 A.2d. 904, 919-20 (Del. Ch. 1999) (applying a company-specific risk premium yet reducing the suggested value thereof after finding that not all risks outlined by valuation experts were risks specific only to the company).

[43] *Delaware Open MRI*, 898 A.2d at 339.

tool of a company-specific risk premium. Here, defendants have completely failed to clear this hurdle. I believe the use of a company-specific risk premium in this case is unwarranted.

Defendants offer three primary justifications for including a company-specific risk premium: (1) the at-will termination of supplier agreements that prevails throughout the wholesale alcohol distribution industry; (2) the competition Sunbelt faces from specific players such as Southern Wine & Spirits; and (3) the level of optimism contained in Sunbelt's management projections.[44]

I conclude that none of these justifications merits inclusion of a company-specific risk premium for Sunbelt. The first and second justifications clearly relate to the industry as a whole, rather than specifically to Sunbelt.[45] In the absence of defendants showing why Sunbelt *specifically* faces these first two risks in a manner greater than other industry players, I must rely on defendants' own description of

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[44] *See* Defs.' Post-Trial Br., 31-41.

[45] Indeed, it is entirely possible that these first two factors pose *less* of a risk to Sunbelt than they do to other companies. Sunbelt's market size and presence could decrease the risk that a supplier would choose to terminate an agreement and in doing so lose the potential benefits of a relatively large distribution channel. Likewise, Sunbelt's size and presence could decrease the threat of a competitor cherry-picking a supplier from Sunbelt's portfolio, if the competitor believes Sunbelt would be more likely to respond or more likely to respond effectively than would a smaller competitor. Of course, Sunbelt's size could also open it up to greater risks and threats, if suppliers in this industry have an aversion to working with larger or more experienced companies, or if competitors believe a larger portfolio means cherry-picking would feel to Sunbelt more like a prick than a stab and, thus, would be less likely to elicit retaliation. The actual risks Sunbelt faces relative to its competitors are a matter of empirics. Sunbelt both fails to provide evidence demonstrating why the risks it faces are different from those its competitors face, and fails to persuade me that any differences in risk actually find Sunbelt in a more precarious position than are other companies in the industry.

these "unique risks in the alcoholic beverage wholesale industry"[46] as simply that—risks to everyone in the industry, not only to Sunbelt. As a result, these are not risks that merit inclusion of a company-specific risk premium.

I also believe Sunbelt's management projections to be an inappropriate basis for inclusion of a company-specific risk premium. First and foremost, I see no evidence, persuasive or otherwise, that at the time they were developed management projections were excessively or generously optimistic. Defendants thus have failed to meet their evidentiary burden to demonstrate to me that it was riskier for Sunbelt to rely on its specific management projections than it is for all companies to rely on management projections. Furthermore, even had defendants met that burden, I am skeptical that a company-specific risk premium is an appropriate response to optimistic management projections. It is not clear to me how one would or should value the appropriate company-specific risk premium to use as an adjustment for such projections. Also, this risk adjustment certainly would not be without its own irony. I do not believe a company should be able to manufacture justification for a company-specific risk premium (and all the quantitative uncertainty accompanied therewith) simply by adjusting its management projections such that there is a heightened risk in relying on those projections, no matter how unique that risk-thirsty practice may be to the company.

[46] Defs.' Post-Trial Br., 31.

The present case demonstrates another critical consideration in evaluating the propriety of a company-specific risk premium. Even if I were to have found persuasive the arguments defendants have made for inclusion of a company-specific risk premium, I would be especially skeptical of the 3% risk premium which defendants advocate. Reilly has provided no specific, quantitative explanation for why 3% is the appropriate level for a company-specific risk premium. It is important for any proposed company-specific risk premium to be based on a specific financial analysis, so that the Court can verify both the propriety of including the risk premium and the appropriate level of the premium.[47]

Defendants have failed to meet their burden to demonstrate why Sunbelt faces company-specific risks rather than risks faced by all companies in its industry and thus why valuations of the company merit inclusion of a company-specific risk premium. They also have failed to provide a rigorous, quantitative explanation for why their proposed company-specific risk premium of 3% is an appropriate discount. Accordingly, I make no adjustments to a calculation of Sunbelt's fair value on the basis of company-specific risks.

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[47] *See, e.g.*, *Gesoff v. IIC Industries, Inc.*, 902 A.2d 1130, 1158-59 (Del. Ch. 2006) (noting that the valuation expert's "application of the [company-specific risk premium] was based almost entirely on his subjective beliefs as to the correct discount rate," that the expert was "unable, crucially, to point to specific financial analyses on which the court could rely to derive such a discount," and that although the calculation of a company-specific risk premium inherently involves some level of subjectivity, the expert's analysis was "unmoored to any objective financial analysis the court can reasonably evaluate, and thus cannot be the basis of what are, in aggregate, substantial discounts to [the company's] fair value.").

c. Subchapter S Conversion

Both parties adjusted their respective valuations to take into account the effect of a conversion in Sunbelt to Subchapter S status, a 26% increase in the company's value, as calculated by Reilly and later accepted by Goldring. Though it may seem unusual for a court to interfere with rare harmony in opposing parties' valuation methodologies,[48] I now must do just that, for the parties have, in my view, failed to apply a fundamental principle of Delaware appraisal law.

As noted above, it is well settled that "[t]he basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him"[49] or her, and that "speculative elements of value that may arise from the 'accomplishment or expectation' of the merger are excluded."[50] Goldring owned shares in a C corporation, and those shares were taken from her. Further, it may be inaccurate even to describe Sunbelt's conversion to S-corporation status as an "accomplishment" or "expectation" of the Merger itself, for the Merger was only one part of a broader corporate reorganization plan that included a post-merger conversion to S-corporation status. Yet however one

[48] Sunbelt argues in its post-trial briefs that there should be no adjustment in the value of Sunbelt for its conversion to S-corporation status. This argument arises now, despite the fact that Sunbelt had already instructed Reilly to adjust the results of his discounted cash flow valuation to account for potential enhancements in the value of Sunbelt stock after Sunbelt's post-Merger conversion to S-corporation status. Following Sunbelt's instructions yet despite his own objection to the propriety of the adjustment, Reilly increased his valuation by 26%, and Goldring saw no reason to refrain from following suit.

[49] *Tri-Continental Corp. v. Battye*, 74 A.2d 71, 72 (Del. 1950).

[50] *Weinberger v. UOP, Inc.*, 457 A.2d 701, 713 (Del. 1983).

describes Sunbelt's conversion to S-corporation status in the context of the corporate reorganization, Goldring never held nor ever would have held Sunbelt shares at the time it was an S corporation. She was cashed out as a shareholder in a C corporation.

Accordingly, I conclude that there is no basis for an upwards adjustment of the per-share value of Sunbelt on the basis of Sunbelt's post-merger conversion to an S corporation.[51] Consequently, I will not accord weight to valuation calculations that have incorporated an adjustment on the basis of Sunbelt's S-corporation conversion.

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[51] Sunbelt explains its issuance of the instruction as a response to inquiries from Goldring's counsel, during depositions, about the potential impact of S-corporation conversion, though a 26% increase in Reilly's calculations is a most generous response to mere inquiries during depositions. I also wonder to what extent generosity and methodological flexibility—whether benefiting Sunbelt or not—may underlie other aspects of Sunbelt's valuations and arguments. Strictly in terms of the issue of S-corporation status, however, I need not explore the issues of generosity and flexibility or the question of why Sunbelt's position appears inconsistent. Nor do I need to examine Sunbelt's new argument against adjustment on the basis of S-corporation status, which is not an argument based on law but rather one of complete conjecture: the specific level of distributions Sunbelt may or may not make to its shareholders and thus the value those shareholders may or may not enjoy as a result of Sunbelt's status as an S corporation. Goldring correctly notes that the Court in *Delaware Open MRI* did not accept such conjecture, though Goldring fails to distinguish that Delaware Open MRI, unlike Sunbelt, was an S corporation *at the time of its merger*. Delaware Open MRI's pre-merger status as an S corporation is what entitled the minority shareholders in that case to a valuation incorporating the future benefits of being a shareholder in an S corporation. No matter what level of distributions Sunbelt ultimately elected to provide its shareholders after the Merger, Delaware law clearly excludes from the valuation of Goldring's shares any enhanced value stemming from Sunbelt's post-Merger conversion to S-corporation status.

4. Court's Valuation of Sunbelt and Determination of Appropriate Remedy

Because I have rejected Ruback's comparable transactions analysis, the WPG Formula, and adjustments based on Sunbelt's post-merger conversion to S-corporation status, I will value Sunbelt using the experts' discounted cash flow methodology. In doing so, I draw on the financial inputs as provided by Sunbelt and agreed upon by the valuation experts, and I use the discount rates employed by Ruback. Applying this methodology, I determine that the fair value of Sunbelt at the time of the 1997 Merger was $114.04 per share.

This determination represents fair value, will fully and fairly compensate Goldring, and suffers from none of the practical problems that afflict Goldring's proposed rescission remedy. The rescissory damages Goldring requests would require the Court to carve out approximately 15% of Sunbelt's distribution portfolio to reflect the 15% stake Goldring held in Sunbelt at the time of the Merger. Goldring suggests the distribution market of Arizona or Maryland as an example of an appropriate state market for the Court to carve out and award to her as "rescissory damages." I do not believe, however, that rescissory damages are appropriate in this case. Any such award would present significant issues related to complexity and implementation, not the least of which would find the Court engaged in another valuation analysis. I would first have to determine what valuation metric is most appropriate to use in seeking to identify 15% of Sunbelt's portfolio, and I would then have to determine the period of time over which to value the company. Both of these elements, as well as others, pose an issue of arbitrariness, and certainly would not guarantee an award that accurately reflects 15% of Sunbelt's portfolio as of the Merger date, particularly given the ever-changing system of overlapping and tiered regulations in which an alcohol distributor such as Sunbelt operates. Simply put, Sunbelt and its business portfolio are too complex to unscramble and, ultimately, rescission is an equitable remedy that a court of equity will only grant, as an exercise of discretion, when that remedy is clearly warranted.[52] Here, given practical difficulties in crafting rescissory relief and the fact that $114.04 per share in money damages is a clearly adequate substitute remedy, I decline to award rescissory damages

C. Additional Considerations

1. Fees and Costs

Goldring seeks a shifting of attorney fees and costs in her favor.[53] Defendants oppose any such shift and propose that any shifting of fees should be in Sunbelt's favor.[54] I award to Goldring all court costs and expert witness fees that

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[52] *See, e.g.*, *Weinberger v. UOP, Inc.*, 457 A.2d 701, 714 (Del. 1983) (outlining examples of circumstances under which "the Chancellor's powers are complete to fashion any form of equitable and monetary relief as may be appropriate, including rescissory damages.").
[53] Pl.'s Post-Trial Br., 48.
[54] Defs.' Post-Trial Answering Br., 45 ("Given the evidence in this case of Mr. Goldring's ever-changing testimony at trial and Professor Ruback's cavalier approach to his expert obligations, if there is to be any fee-shifting in this case, it should be in favor of Sunbelt.").

she incurred in the process of litigating this consolidated action, but I decline to shift attorneys' fees.

It is within my discretion to determine costs of the proceedings and to tax the costs "upon the parties as the Court deems equitable in the circumstances."[55] In the present circumstances and on the basis of my analysis of defendants' conduct, I believe it is most equitable for defendants to pay the court costs Goldring incurred during the course of litigation. Likewise, I award Goldring all costs incurred in association with the testimony and preparation of her expert witness valuations.[56] The expert fees total $841,763, an amount that defendants have objected to as unreasonable both in the timing and activities upon which the fees were based.[57] Nevertheless, I have rejected defendants' objection, principally on the ground that a litigant who has paid fees at a time when it was uncertain the fees would be recovered is evidence of the fees' reasonableness.[58] In addition, after reviewing the fees, I have independently determined that they are reasonable

[55] 8 *Del. C.* § 262(j).
[56] *See* 10 *Del. C.* § 8906 ("[F]ees for witnesses testifying as experts … in cases in … the Court of Chancery … shall be fixed by the court in its discretion [and] taxed as part of the costs in each case and shall be collected and paid as other witness fees are now collected and paid."). *See also Dobler v. Montgomery Cellular Holding Co., Inc.*, 2002 WL 31112195 (Del. Ch. Aug. 29, 2002) (awarding expert costs on the basis of the discretion that 10 *Del. C.* § 8906 provides the Court).
[57] Defendants did not use the word "concern" or "objection" in their November 20, 2009 letter, but I believe it appropriate to accept defendants' letter as one expressing concern and objection over the total and source of the fees.
[58] *See, e.g.*, *Arbitrium (Cayman Islands) Handels AG v. Johnston*, 1998 WL 155550, at *2 (Del. Ch. Mar. 30, 1998) (determining fees to be reasonable, in part on the consideration that litigant had paid fees even though it was unclear if fee recovery would be possible later in the proceedings), *aff'd*, 720 A.2d 542 (Del. 1998).

for complex and hard fought litigation involving difficult valuation issues. Accordingly, I award Goldring $841,763 in expert fees.

I agree with defendants' analysis on the issue of shifting attorney fees: "to constitute bad faith [and thus warrant shifting of attorney fees contrary to the American Rule], the defendants' action must rise to a high level of egregiousness."[59] Here, I cannot find defendants' actions to be of the egregious, vexatious, or bad-faith sort that have merited the shifting of attorney fees in earlier cases.[60] Most notably, although I acknowledge many of the similarities Goldring identifies between the present matter and *Montgomery Cellular Holding Co. v. Dobler*,[61] I believe defendants' reliance on the transactions priced at the WPG Formula was sufficiently reasoned to preclude a finding that there was no legal issue in this case upon which reasonable parties could differ. That is, parties could and did reasonably differ on the legal import of the WPG Formula. The WPG Formula ultimately may have had no weight in my valuation analysis and may

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[59] *Judge v. City of Rehoboth Beach*, 1994 WL 198700, at *2 (Del. Ch. Apr. 29, 1994).
[60] *See, e.g.*, *Arbitrium (Cayman Islands) Handels AG v. Johnston*, 705 A.2d 225 (Del. Ch. 1997) (finding that defendants acted in bad faith by, *inter alia*, opposing the action despite their knowledge that plaintiff's claim to majority shareholder status was valid and altering testimony, changing positions repeatedly, and falsifying evidence at trial), *aff'd*, 720 A.2d 542 (Del. 1998); *Abex Inc. v. Koll Real Estate Group, Inc.*, 1994 WL 728827, at *20 (Del. Ch. Dec. 22, 1994) (describing the case as one contrary to "a defendant resist[ing] a contractual liability on grounds as to which reasonable men could differ" and the defendant as having operated in bad faith via having "contest[ed] liability, threaten[ed] litigation, and force[d] plaintiffs to prosecute this action and litigate defenses that had no factual or legal merit.").
[61] 880 A.2d 206, 228 (Del. 2005) (upholding a Court of Chancery decision to award attorney fees on the basis of, *inter alia*, the merger price having been set unilaterally as well as unfairly low and not on the basis of any legitimate valuation of the company).

have played an unduly large role in guiding defendants' other valuations of Sunbelt stock at the time of the 1997 Merger, but it did present me with a legitimate legal question and a potentially legitimate valuation metric for Sunbelt. I therefore do not find defendants to have conducted themselves with the necessary egregiousness or vexatiousness to warrant shifting attorneys' fees.

2. Interest

Plaintiff seeks interest no lower than 7.14%, the highest rate of Sunbelt's borrowing costs as calculated by Reilly, defendants' valuation expert.[62] Defendants, meanwhile, propose two alternatives from which the Court can choose, the first being the prudent investor rate as calculated by Reilly (3.56% on a simple basis) and the second being a weighted combination of i) the 3.56% prudent investor rate, and ii) two different calculated rates for Sunbelt's actual cost of borrowing (in total, this weighted combination is 4.90%).[63]

Although in earlier cases this Court has awarded interest rates similar in value and justification to those for which both parties in the present case advocate,[64] in this case I will exercise my statutory discretion to award interest at

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[62] Pl.'s Post-Trial Br., 60.
[63] Defs.' Post-Trial Br., 65.
[64] *See, e.g.*, *Delaware Open MRI Radiology Assoc., P.A., v. Kessler*, 898 A.2d 290, 343-44 (Del. Ch. 2006) (awarding a pre-judgment interest at a rate of 6.9%, compounded monthly, that is an average of a prudent investor rate and the company's actual cost of borrowing, and is the "more generous, but still responsible, rate of interest proposed by [plaintiffs]."); *Henke v. Trilithic Inc.*, 2005 WL 2899677, at *12-13 (Del. Ch. Oct. 28, 2005) (awarding the prudent investor rate of 6.14%, compounded monthly, rather than a weighted combination of a prudent investor rate and

the legal rate (5% greater than the Federal Reserve discount rate as measured during that period of time), compounded quarterly.[65] I do not find either party to have demonstrated good cause for me to depart from this statutory interest rate. When calculating the interest due, parties should be certain to adjust appropriately for each and every change in the Federal Reserve discount rate that has occurred over the course of this lengthy litigation.

D. Defendants' Motion to Strike

Defendants ask the Court to strike exhibit A of plaintiff's post-trial answering brief. Exhibit A is a 2007 *BeverageWorld* article that examines Sunbelt's success and its future prospects. The article quotes extensively from an interview with Charles Merinoff. Defendants argue that "Mr. [Charles] Merinoff's 2007 statements about Sunbelt's circumstances a decade [after the Merger] prove nothing about Sunbelt's fair value as of 1997—or about the fairness of the Merger consideration when it was set in 1997."[66] Goldring contests the assertion that there is no relevant link between the 2007 *BeverageWorld* article and the Court's

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the company's actual cost of borrowing, given "the Petitioner's failure to diligently prosecute [the] action."); *Chang's Holdings, S.A. v. Universal Chemicals and Coatings*, 1994 WL 681091, at *2, *5 (Del. Ch. Nov. 22, 1994) (employing "a sliding scale that alters the relevance of the prudent investor rate and the cost of borrowing rate according to the relative fault of the parties in causing the delay [in the appraisal action]" to award a simple interest rate of 7.79%).

[65] *See* 8 *Del. C.* § 262(h) (stating that "[u]nless the Court in its discretion determines otherwise for good cause shown, interest from the effective date of the merger through the date of payment of the judgment shall be compounded quarterly and shall accrue at 5% over the Federal Reserve discount rate … as established from time to time during the period between the effective date of the merger and the date of payment of the judgment.").

[66] Defs.' Reply in Further Support of Mot. to Strike, 4.

process of determining Sunbelt's fair value at the time of the Merger. According to Goldring, the 2007 article and the success of Sunbelt it covers are "relevant both for purposes of impeachment [of Sunbelt's claims of industry and company risk] and to show Defendants' bad-faith in connection with this litigation."[67] Specifically, Goldring asks the Court to weigh the contents of the 2007 *BeverageWorld* article and its description of Sunbelt's stellar success in the alcohol distribution industry against defendants' arguments that Sunbelt operated in a high-risk industry, that its management projections in and before 1997 were optimistic and aggressive, and that Reilly's discounted cash flow analysis incorporated appropriate adjustments for industry-specific and company-specific risk.[68]

Exhibit A, an article written and published ten years after the Merger, is irrelevant to my analysis of issues prevailing at the time of the Merger. I have already ruled on the propriety of the risk adjustments found in both defendants' and plaintiff's discounted cash flow analyses. My findings and conclusions on those adjustments are based entirely on evidence known to the parties in 1997. Evidence discussing Sunbelt's success as of and in the years immediately before 2007 and Sunbelt's prospects for future growth is beyond the time relevant to my determination of Sunbelt's fair value in July-August 1997 (the time of the Merger) and my determination of the propriety of the methodology underlying both parties'

[67] Pl.'s Resp. to Defs.' Mot. to Strike, 2.
[68] *Id.* 3-4.

expert valuations. It matters not that Sunbelt has performed extremely well since defendants squeezed Goldring out, and despite the high levels of risk that, according to defendants and their experts, Sunbelt faces. Accordingly, I grant defendants' motion to strike exhibit A.

III. CONCLUSION

For the reasons discussed above, I determine that the fair value of Sunbelt Beverage Corporation at the time of the Merger was $114.04 per share. Goldring is entitled to her pro rata share of Sunbelt's fair value on the date of the Merger, as well as pre- and post-judgment interest, compounded quarterly, at a rate of five percent above the Federal Reserve discount rate on each day of the relevant time period. I also award Goldring all court and filing costs and experts' fees, and I grant defendants' motion to strike exhibit A to Goldring's post-trial answering brief.

Counsel shall agree upon a form of implementing Order, which shall be submitted within twenty days of this date.

IT IS SO ORDERED.