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Delaware Court Ruling on Trading Price and Fair Value Appraisal

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On February 15, 2018, the Delaware Court of Chancery issued its post-trial decision in *Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*,[1] a statutory appraisal proceeding arising from Hewlett-Packard's 2015 acquisition of Aruba Networks.[2] The court concluded that the "most persuasive evidence" of Aruba Networks' fair value was its 30-day average unaffected market price of $17.13 per share—significantly lower than the merger price of $24.67 per share. This decision comes in the wake of the Delaware Supreme Court's recent decisions in *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*[3] and *DFC Global Corporation v. Muirfield Value Partners, L.P.*,[4] which endorsed the use of the merger price as evidence of fair value in appraisals involving publicly traded companies sold in arm's-length transactions. Heeding the Delaware Supreme Court's admonition in those cases that market indicators should be given significant weight over "exercises of human judgment" such as the Delaware courts' historical reliance on discounted cash flow analyses, Vice Chancellor Laster—who was the trial court judge in *Dell*—concluded that, under the circumstances presented, Aruba Networks' unaffected stock price was the most persuasive evidence of fair value over even the merger price.

The court considered three methods of valuing Aruba: the parties' competing discounted cash flow analyses, the merger price, and the company's unaffected market price. Relying on *DFC*, Vice Chancellor Laster rejected the discounted cash flow valuations, observing that such models were useful only when the "respondent company was not public or was not sold in an open market check," neither of which applied to Aruba. Turning to the merger price, the court acknowledged the "heavy, if not overriding, probative value" of that method given the Delaware Supreme Court's recent decisions and the facts at hand. However, because of the "substantial synergies" included in the merger price that would have to be deducted using an imprecise, "judgment-laden exercise," the court determined that while the merger price represented a "ceiling for fair value," it was an "uncertain[]" standalone estimation of fair value.

[1] C.A. No. 11448-VCL (Del. Ch. Feb. 15, 2018).

[2] WSGR represented Aruba Networks and its directors in connection with the merger and in related pre-closing merger litigation, but did not represent Aruba Networks in the appraisal litigation.

[3] — A.3d –, 2017 WL 6375829 (Del. Dec. 14, 2017).

[4] 172 A.3d 346 (Del. 2017).

Instead, the court examined the market for Aruba's shares and found attributes similar to those present in *Dell* and *DFC* that indicated an efficient market for the stock. The court reasoned that the Delaware Supreme Court's recent decisions compelled the conclusion that the unaffected trading price was the "best evidence" of Aruba's fair value. The court also emphasized language from *Dell* that "[t]he issue in an appraisal is not whether a negotiator has extracted the highest possible bid. Rather, the key inquiry is whether the dissenters got fair value and were not exploited." Comparing the merger price of $24.67 per share to the unaffected market price of $17.13, it was "not possible to say that Aruba's stockholders were exploited," and therefore the unaffected price was "persuasive evidence of fair value."

There are several important takeaways from this decision:

- Relying extensively on language from *Dell* and *DFC*, the court placed significant emphasis on the efficient market for Aruba's stock, which not only created a reliable method for determining fair value but also overcame certain deal process issues that before *Dell* and *DFC* might have called into question the reliability of the merger price. The court found, for example, that the petitioners proved that the acquiror knew it had no competition for Aruba and was not incented to offer top-dollar and that Aruba's bankers "catered" to the acquiror and their "interests made them less effective negotiators than they might have been." The court concluded that Aruba likely could have commanded a higher merger price absent these issues. However, because the unaffected price was lower than the merger price, Aruba's stockholders were not "exploited," and any additional value would only have resulted in the acquiror sharing a greater portion of synergies, which "would not have changed Aruba's standalone value." As the court concluded, "[w]ith a reliable market price as the base line, an arm's-length deal at a premium is non-exploitative."
- Relatedly, because of the court's focus on the efficient market for Aruba's stock in light of language in the Delaware Supreme Court's recent opinions, the court suggested that future appraisal litigants consider engaging an expert in market efficiency.
- The decision also suggests that, in light of *Dell* and *DFC*, Delaware courts may be skeptical of the argument that the merger price is unreliable evidence of fair value where an acquiror times its acquisition to take advantage of a trough in the market for the target's stock. As the court noted here, it would be improper to regard the acquiror's "belief that it had seized upon an opportune time to purchase Aruba as sufficient to undercut the reliability of Aruba's market price."