



**IN THE SUPREME COURT OF THE STATE OF DELAWARE**

AMERICAN COMMERCIAL LINES )  
INC., )  
 ) Case No. 230, 2013  
Respondent Below, )  
Appellant and Cross-Appellee ) On appeal from the Court of  
 ) Chancery of the State of Delaware  
v. ) C.A. No. 6369-VCL  
 )  
IQ HOLDINGS, INC., )  
 )  
Petitioner Below, Appellee and )  
Cross-Appellant )

**APPELLANT'S REPLY BRIEF ON APPEAL AND  
CROSS-APPELLEE'S ANSWERING BRIEF ON CROSS-APPEAL**

Kevin G. Abrams (#2375)  
Derrick B. Farrell (#5747)  
ABRAMS & BAYLISS LLP  
20 Montchanin Road, Suite 200  
Wilmington, Delaware 19807  
(302) 778-1000

Attorneys for American Commercial  
Lines Inc., Respondent Below,  
Appellant and Cross-Appellee

Date: August 13, 2013

**TABLE OF CONTENTS**

	<b><u>PAGE</u></b>
<b>SUMMARY OF CROSS-APPEAL ARGUMENT .....</b>	<b>1</b>
<b>COUNTER-STATEMENT OF FACTS .....</b>	<b>2</b>
<b>I. THE EXCLUSION OF THE STRATEGIC INITIATIVE SAVINGS LINE ITEM IN MANAGEMENT’S PROJECTIONS IS WELL SUPPORTED. ....</b>	<b>2</b>
<b>APPELLANT’S REPLY ARGUMENTS ON APPEAL .....</b>	<b>5</b>
<b>I. THE COURT OF CHANCERY ERRED IN ADOPTING THE 7.15% YIELD-TO-WORST COST OF THE NOTES ON THE MERGER DATE. ....</b>	<b>5</b>
<b>A. Standard of Review .....</b>	<b>5</b>
<b>B. Merits of Argument .....</b>	<b>5</b>
<b>II. THE COURT OF CHANCERY’S ASSUMPTION THAT THE LIBOR BASE RATE WOULD REMAIN AT 0.26% INTO PERPETUITY IS CLEARLY WRONG. ....</b>	<b>10</b>
<b>A. Standard of Review .....</b>	<b>10</b>
<b>B. Merits of Argument .....</b>	<b>10</b>
<b>III. THE TRIAL COURT CONTRAVENED WELL-ESTABLISHED VALUATION PRINCIPLES BY ADOPTING A SHORT-TERM PROXY FOR THE LONG-TERM COST OF ACLI’S NOTES. ....</b>	<b>15</b>
<b>A. Standard of Review .....</b>	<b>15</b>
<b>B. Merits of Argument .....</b>	<b>15</b>

IV.	BECAUSE ACLI COULD NOT BORROW ON THE MERGER DATE AT THE 5.84% BLENDED INTEREST RATE ADOPTED BY THE COURT OF CHANCERY, THE POST-TRIAL ORDER IS CLEARLY WRONG. ....	18
A.	Standard of Review .....	18
B.	Merits of Argument .....	18
	<b>APPELLANT’S ANSWERING ARGUMENTS ON CROSS-APPEAL.....</b>	<b>20</b>
V.	THE COURT OF CHANCERY PROPERLY EXCLUDED 50% OF THE STRATEGIC INITIATIVE SAVINGS LINE ITEM FROM MANAGEMENT’S PROJECTIONS. ....	20
A.	Question Presented .....	20
B.	Standard of Review .....	20
C.	Merits of Argument .....	21
1.	Delaware Law Does Not Require The Use Of Management Projections.....	21
2.	The Court Of Chancery’s Adjustment To Management’s Projections Is Supported By The Record. ....	22
VI.	THE COURT OF CHANCERY PROPERLY INCLUDED THE OTHER NON-CASH OPERATING ACTIVITIES LINE ITEM IN ACLI’S PROJECTIONS. ....	28
A.	Question Presented .....	28
B.	Standard of Review .....	28
C.	Merits of Argument .....	28

VII. WHETHER THE COURT OF CHANCERY ERRED IN ADOPTING THE BETA AND SMALL STOCK PREMIUM VALUES OF ACLI’S EXPERT. ....	31
A. Question Presented .....	31
B. Standard of Review .....	31
C. Merits of Argument .....	31
1. The Court Of Chancery Properly Relied On ACLI’s Barra Beta. ....	31
2. The Court of Chancery Properly Relied on the Small Stock Premium of ACLI’s Expert. ....	33
<b>CONCLUSION</b> .....	35
<b>EXHIBIT A</b> .....	Attached

## TABLE OF CITATIONS

	<b>Page(s)</b>
<b>Cases</b>	
<i>Air Prods. &amp; Chem., Inc. v. Airgas, Inc.</i> , 2010 WL 5638712 (Del. Ch. Dec. 14, 2010).....	7
<i>Cede &amp; Co. v. Technicolor, Inc.</i> , 758 A.2d 485 (Del. 2000) .....	21
<i>Emerald Partners v. Berlin</i> , 726 A.2d 1215 (Del. 1999) <i>rev'd on other grounds</i> , 12 A.3d 1140 (Del. 2011).....	5, 6
<i>In re Emerging Commc'ns, Inc. S'holders Litig.</i> , 2004 WL 1305745 (Del. Ch. May 3, 2004).....	12
<i>Finkelstein v. Liberty Digital, Inc.</i> , 2005 WL 1074364 (Del. Ch. Apr. 25, 2005).....	16
<i>Gilbert v. M.P.M. Enters., Inc.</i> , 1998 WL 229439 (Del. Ch. Apr. 24, 1998).....	14, 16, 19
<i>Gilbert v. MPM Enters., Inc.</i> , 709 A.2d 663 (Del. Ch. 1997), <i>aff'd</i> 731 A.2d 790 (Del. 1999) .....	22
<i>Gray v. Cytokine Pharmasciences, Inc.</i> , 2002 WL 853549 (Del. Ch. Apr. 25, 2002).....	22
<i>Grimes v. Vitalink Commc'ns Corp.</i> , 1997 WL 538676 (Del. Ch. Aug. 28, 1997) .....	22
<i>Hintmann v. Fred Weber, Inc.</i> , 1998 WL 83052 (Del. Ch. Feb. 17, 1998).....	14
<i>In re Indian Palms Assoc., Ltd.</i> , 61 F.3d 1995 (3d Cir. 1995) .....	11
<i>Kleinwort Benson Ltd. v. Silgan Corp.</i> , 1995 WL 376911 (Del. Ch. June 15, 1995).....	22

<i>Levitt v. Bouvier</i> , 287 A.2d 671 (Del. 1972) .....	21
<i>In re Matter of Appraisal of Shell Oil Co.</i> , 1990 WL 201390 (Del. Ch. Dec. 11, 1990) .....	17
<i>M.G. Bancorporation, Inc., v. Le Beau</i> , 737 A.2d 513, 526 (Del. 1999) .....	5
<i>M.P.M. Enters., Inc. v. Gilbert</i> , 731 A.2d 790 (Del. 1999) .....	21
<i>In re S. Peru Copper Corp.</i> , 2011 WL 5176789 (Del. Ch. Oct. 14, 2011) .....	7, 8
<i>Scion Breckenridge Managing Member, LLC v. ASB Allegiance Real Estate Fund</i> , 68 A.3d 665, 678 (Del. 2013) .....	20
<i>Sears, Roebuck and Co. v. Midcap</i> , 893 A.2d 542 (Del. 2006) .....	6
<i>In re Sunbelt Beverage Corp. S’holder Litig.</i> , 2010 WL 26539 (Del. Ch. Jan. 5, 2010) .....	34
<i>Towerview LLC v. Cox Radio, Inc.</i> , 2013 WL 3316186 (Del. Ch. June 28, 2013) .....	22
<i>Wedderien v. Collins</i> , 2007 WL 3262148 (Del. Nov. 6, 2007) .....	5
<i>West Ctr. City Neighborhood Ass’n v. West Ctr. City Neighborhood Planning Advisory Comm., Inc.</i> , 2003 WL 241356 (Del. Ch. Jan. 24, 2003) .....	7

**Other Authorities**

Ibbotson SBBI 2011 Valuation Yearbook, <i>Market Results for Stocks, Bonds, Bills, and Inflation</i> , (1926-2010) .....	33
Shannon Pratt & Roger Grabowski, <i>Cost of Capital: Applications and Examples</i> (4th ed. 2010) .....	19, 33
Shannon Pratt, <i>Valuing a Business: The Analysis and Appraisal of Closely Held Companies</i> (5th ed. 2007) .....	29, 30, 33

Timothy Koller, *et al.*, *Valuation: Measuring and Managing the Value of Companies* (5th ed. 2010).....19

## **SUMMARY OF CROSS-APPEAL ARGUMENT**

5. DENIED. Consistent with Delaware law, the Court of Chancery properly adjusted a speculative line item included in management's projections based on the credible evidence of ACLI's employees, chief financial officer ("CFO"), and expert. IQ cannot show that the lower court clearly erred in finding such witnesses credible or that the lower court could not adjust management's projections as a matter of law where the facts support such an adjustment.

6. DENIED. The Court of Chancery did not abuse its discretion by including the Other Non-Cash Operating Activities ("ONCOA") line item, less debt cost amortization, in its valuation based on the more credible analysis of ACLI's expert. IQ's expert did not know or make any effort to determine the components of ONCOA despite the fact that they could readily be determined by comparing management's projections and ACLI's 2009 SEC Form 10-K.

7. DENIED. The Court of Chancery did not abuse its discretion by adopting the beta and small stock premium advocated by ACLI's expert. IQ has not shown a mid-point beta is unsupported by the record or that an adjusted beta based on comparable companies was appropriate here, especially since the trial court found no companies comparable to ACLI. Finally, IQ cannot show that adopting both a Barra beta and a small stock premium double-counted the size factor or that the trial court should rely on the stale data utilized by IQ's expert.

## COUNTER-STATEMENT OF FACTS

### **I. THE EXCLUSION OF THE STRATEGIC INITIATIVE SAVINGS LINE ITEM IN MANAGEMENT’S PROJECTIONS IS WELL SUPPORTED.**

The bottom of ACLI’s management projections included a separate line item called “Additional Strategic Initiative Savings in MSO Line” (“SIS”). B-452. This line item included four components of potential cost savings: (1) “Claims,” (2) “Scheduled Service,” (3) “Sales Mix,” and (4) “Improved Maintenance Cost Reductions.” A-203-204 at 281:20–282:17. The projections lacked any detail supporting the SIS, which were described as an “on-top adjustment.” A-203 at 280:1-15; B-294 at 35:15-17. In contrast, the other projection line items had support from “a very detailed build out of barge expenses, boat expenses, revenues, at a very detailed level.” A-203 at 280:1-15.

Throughout the course of trial, during meetings between ACLI’s expert and ACLI, and during the fact witness depositions, the SIS and their component parts were described as being a “go-get,” a “stretch,” a “target,” a “goal,” “a lofty goal,” “unidentified cost savings,” an “internal challenge,” “unspecified, nonspecific improvements,” “pulled out of thin air,” having “significant challenges incorporated into them,” lacking “specific plans for implementation,” a goal that one “wouldn’t feel comfortable...that it was attainable,” a goal “that no one on staff knew how to do it, and still does not,” and “SWAG” (Scientific Wild Ass

Guess).<sup>1</sup> The Court of Chancery explicitly found the testimony of ACLI's management credible in excluding 50% of the SIS. *See* Post-Trial Order at ¶ 7.

Due to the SIS's uncertainty, ACLI's management listed it in a separate line item at the bottom of the projections. B-452; A-203 at 280:1-15. Even IQ's expert conceded the SIS was listed separately "so that anyone reviewing the forecast could evaluate the extent of the strategic initiative savings that was included or considered in the preparation of this forecast." A-162 at 122:5-11.

The record supports exclusion of 100% of the four SIS components:

- **Claims:** Claims referred to a plan to reduce insurance claims, resulting in lower premiums, while simultaneously lowering training budgets for ACLI's employees. A-204 at 283:20-284:6. Grouping these two areas together was problematic because reducing training would likely increase insurance claims. *Id.* at 284:19-285:6. Furthermore, the baseline model already included reduced insurance claims resulting from a younger barge fleet. *Id.* at 282:3-17, 284:7-13.
- **Scheduled Service:** Scheduled service was the idea of ACLI's management to implement "planned and predictable service" for its barges. *Id.* at 285:14. The barge industry has never implemented scheduled service. A-205 at 287:1-4; A-165 at 136:19-21. ACLI previously attempted to implement scheduled service in 2008 and 2009, but failed in both attempts. A-204-205 at 285:18-286:10. ACLI's Director of Financial Planning and Analysis ("Bryant") described scheduled service as the "shakiest" of the strategic cost savings and ACLI's Controller ("Noltemeyer") testified that "scheduled service is not a workable plan...in the barge industry." A-205 at 286:24; A-194 at 249:23-251:2.

---

<sup>1</sup> A-72; A-76-78; A-205 at 288:9; A-208 at 300:1; A-213 at 323:9-324:9; A-246 at 451:6-14; A-322-27; A-389-390; A-1886-87; A-1978-79 at 13:10-15:19; B-294 at 35:3-17; B-296 at 44:23-45:23; B-302 at 67:4-13; B-305 at 81:10-19; B-344 at 18:2-19:5; B-346 at 29:8-18; B-347 at 33:17-24; B-351 at 47:7-8. *See also* B-452; A-203 at 280:1-15.

- **Sales Mix:** The net revenue increases in sales mix were hoped to result from ACLI “trying to get additional lucrative high-margin business from existing customers.” A-205 at 287:8-10. However, management’s base model already included detailed sale assumptions, so it was unclear where these additional sales would come from. A-215 at 328:20–329:21.
- **Maintenance:** Management expected a younger barge fleet to result in fewer maintenance costs. A-205 at 287:15–288:1. However, the base model already factored in reduced maintenance costs. *Id.*

During the ACLI sale process which led to the Merger,<sup>2</sup> Bank of America Merrill Lynch (“BAML”), ACLI’s financial advisor, with the assistance of management, created an alternative downside projection case referred to as the “Deferred Investment Case.” B-293. The Deferred Investment Case assumed a prolonged period of economic stagnation whereby barge fleet reinvestment was delayed and the SIS were given one-third of the effect as they were given in the base case. A-1596-97. ACLI disclosed the Deferred Investment Case in the Proxy, along with two other projections scenarios but did not express a preference as to which scenario was most likely to occur. *Id.*; A-261 at 511:1–513:24.

---

<sup>2</sup> Capitalized terms not defined herein shall have the meaning provided in Appellant’s Opening Brief (“ACLI Br.”). IQ Holdings, Inc.’s Answering Brief on Appeal and Opening Brief on Cross-Appeal is referred to as “IQ Br.”

## APPELLANT'S REPLY ARGUMENTS ON APPEAL

### **I. THE COURT OF CHANCERY ERRED IN ADOPTING THE 7.15% YIELD-TO-WORST COST OF THE NOTES ON THE MERGER DATE.**

---

#### **A. Standard of Review**

To IQ, ACLI's argument that an expert's testimony is consistent with well-established Delaware law turns a legal issue into a factual issue. IQ Br. at 14. IQ cites no support for this proposition. At most, citations to the facts raise a mixed question of fact and law that this Court also reviews *de novo*.<sup>3</sup>

#### **B. Merits of Argument**

Unable to rebut the merits of ACLI's argument that the trial court's appraisal contravened Section 262 by improperly incorporating value related to the expectation of the Merger, IQ repeatedly asserts that ACLI did not raise this issue below. IQ is wrong. ACLI sufficiently preserved this issue by raising it in both its post-trial brief and through the trial and deposition testimony of its expert.<sup>4</sup>

---

<sup>3</sup> *Wedderien v. Collins*, 2007 WL 3262148, at \*3 (Del. Nov. 6, 2007); *Emerald Partners v. Berlin*, 726 A.2d 1215, 1219 (Del. 1999), *rev'd on other grounds*, 12 A.3d 1140 (Del. 2011). IQ's reliance on *M.G. Bancorporation, Inc.* is misplaced, it merely states the undisputed point that "[i]n the absence of legal error,"—unlike here—"this Court reviews appraisal valuations pursuant to the abuse of discretion standard." 737 A.2d 513, 526 (Del. 1999). See IQ Br. at 14.

<sup>4</sup> See A-336 (explaining in ACLI's opening post-trial brief that the yield-to-worst was affected by the Merger announcement because "the yield plummeted after the October 18, 2010 announcement and stayed at an artificially depressed state until the Merger was completed on December 21, 2010.") (citing A-1987 at 47:10-48:6) (ACLI's expert's deposition testimony that the proper measure of cost of debt was the unaffected value prior to the Merger announcement); A-221 at 352:15-20 (ACLI's expert explained at trial that she selected the yield-to-worst prior to the Merger Announcement Date because "that was a rate that was unaffected by the transaction, with the purpose of this exercise being that I did not want to have any impact of the transaction

By failing to contest a number of crucial arguments, IQ waived any response to those arguments.<sup>5</sup> Most importantly, IQ does not dispute that, if the Merger affected ACLI's yield-to-worst, the post-announcement Notes would improperly incorporate an "element of value arising from the accomplishment or expectation of the merger" (ACLI Br. at 18-20) or that the Post-Trial Order provides no explanation for why the Notes' yield-to-worst rate plummeted from 9.6% the day before the Merger Announcement Date to 7.15% on the Merger Date (*Id.* at 19). Nor does IQ claim that the decrease resulted from the general interest rate environment or the disclosures in ACLI's Proxy. *Id.* at 9-10, 20-21.

The only explanation IQ offers for the dramatic reduction in the yield-to-worst of the Notes is that ACLI reported its third quarter financial results. IQ Br. at 18. IQ, however, fails to explain why the results of a single quarter would radically change ACLI's risk profile and significantly reduce its cost of debt. As Noltemeyer testified at trial, "it's not a logical conclusion...that because...one quarter...is up that you're going to take your annual forecast up by that much." B-254 at 56:24-57:2. It is undisputed that ACLI's third quarter earnings did not

---

affect the analysis of the long-term cost of debt."). *See also Sears, Roebuck & Co. v. Midcap*, 893 A.2d 542, 547 n.4 (Del. 2006) (finding issue properly raised on appeal "[a]lthough Sears did not present that precise argument at the trial level, it did object generally.").

<sup>5</sup> *See, e.g., Emerald Partners*, 726 A.2d at 1224.

affect its earnings for 2010 or cause ACLI to update its long-term projections.<sup>6</sup> IQ next claims the market could not have determined ACLI's 2010 third quarter results represented a movement between quarters because ACLI did not disclose that fact in its SEC Form 10-Q. IQ Br. at 18. However, ACLI did not ever provide guidance to the market, so the market had no yardstick from ACLI against which it could measure the reported earnings.<sup>7</sup>

Unable to refute the chart included in ACLI's post-trial and opening appeal briefs demonstrating that the Merger announcement affected the Notes' yield-to-worst (*see* ACLI Br. at 9; A-336), IQ recycles its argument to the trial court that ACLI presented this chart too late. IQ Br. at 17. IQ's argument fails for the simple reason that the data in ACLI's chart is accurate and was reported publicly by multiple sources.<sup>8</sup> The Court of Chancery may take judicial notice and give appropriate weight to publicly available information, even if that information is not directly admissible.<sup>9</sup> In any event, the Court need not even consider the chart to

---

<sup>6</sup> ACLI's annual revenues fell every year from 2008 to 2010, and ACLI's year-by-year quarterly EBITDA results fell in six of the eight quarters in the same period. B-254 at 56:19-22; ACLI Br. at 20 n.22; A-308-309; AR-73; A-1345; A-1801; *see also* A-190 at 236-237.

<sup>7</sup> B-311 at 103:20-23; B-313 at 113:1-8. IQ offers no explanation for the sharp rise in the Notes' yield-to-worst after the Merger Announcement Date and Merger Date (*see* chart at ACLI Br. at 9), presumably because it would be inconsistent with IQ's improving financial condition theory.

<sup>8</sup> *See generally* IQ Br. at 17-18; *see also* AR-4-5; AR-12-13; AR-17-18.

<sup>9</sup> *See, e.g., Air Prods. & Chem., Inc. v. Airgas, Inc.*, 2010 WL 5638712, at \*1 (Del. Ch. Dec. 14, 2010) (considering the uncontested Schedule TO and all of its exhibits); *West Ctr. City Neighborhood Ass'n v. West Ctr. City Neighborhood Planning Advisory Comm., Inc.*, 2003 WL 241356, at \*1 n.8 (Del. Ch. Jan. 24, 2003) ("Although not presented as an exhibit at trial, I take judicial notice of the City Council Resolution.") (citing D.R.E. 201). IQ's reliance on *Southern*

rule that the Merger announcement affected the Notes' yield-to-worst. IQ does not dispute that the Notes' yield-to-worst prior to the Merger announcement was 9.6% and then plummeted to 7.15% on the Merger Date.<sup>10</sup> IQ offers no meritorious justification other than the Merger announcement for this drop.

IQ further claims the cost of debt conclusion of ACLI's expert "was analytically inconsistent with the amount of debt she used." IQ Br. at 16. It was appropriate to use the October 15, 2010 yield-to-worst cost of the Notes and the December 21, 2010 market value of the Notes because the December 21, 2010 market value appropriately reflected ACLI's obligation as of the Merger Date. IQ has presented no evidence demonstrating the Merger impacted the market value of ACLI's Notes similarly to the yield-to-worst rate. A-229 at 383:8-14; *id.* at 384:18-22; A-230 at 386:20-389:19.<sup>11</sup>

Finally, IQ repeatedly asserts that both ACLI and IQ's experts supported a 7.15% cost of the Notes. IQ Br. at 11, 16-17. That simply is not true. IQ's expert consistently advocated for a 9.26% cost of the Notes. IQ refers to its pre-trial brief and the rebuttal report of its expert which contend that if ACLI's expert had used

---

*Peru* is misplaced. See IQ Br. at 17. The plaintiff in *Southern Peru*, unlike ACLI, did not address why the contested exhibits should be properly considered after trial, and the opinion does not indicate the additional evidence could be judicially noticed, as is the case here. *In re S. Peru Copper Corp.*, 2011 WL 5176789 (Del. Ch. Oct. 14, 2011).

<sup>10</sup> A-124-25 at ¶¶ 27-28, 34 (stipulating to the dates of the announcement and Merger).

<sup>11</sup> IQ continues to erroneously argue that ACLI's expert failed to separately consider the cost of the Revolver in reaching her 9.6% blended cost of debt. IQ Br. at 16. However, as explained in ACLI's opening appeal brief, ACLI's expert confirmed her blended cost of debt in her rebuttal report by separately analyzing the Notes and the Revolver. See ACLI Br. at 14-15.

the yield-to-worst on the Merger Date instead of prior to the Merger announcement, her cost of debt would have been 7.15%. A-52; A-1946.<sup>12</sup>

However, during trial, IQ's expert made clear he did not believe the yield-to-worst on the Merger Announcement Date accurately reflected the cost of the Notes:

I thought that the 9.2 percent debt rate was a better proxy for the long-term rate because it assumes in its calculation that you'll go out to 2017. And the horizon on the long-term notes calculated at 7.1 percent. The yield-to-worst is only a two and a half-year period. And that's why I didn't use it as the cost of debt.<sup>13</sup>

IQ misleadingly claims that ACLI's expert "admitted that 7.15% was the realistic cost of the Notes" and suggested it was "an appropriate value for the long-term cost of the Notes." IQ Br. at 18. While ACLI's expert applied the 7.15% yield-to-worst on the Merger Date as a *starting point* in Exhibit 4 to her rebuttal report (A-180-81 at 196:13–197:12), she then proceeded to calculate the Notes' appropriate yield for 27 more years to reflect their long-term weighted average, reaching a 10.83% cost for the Notes. *See* ACLI Br. at 14-15. ACLI's expert consistently argued that 7.15%, with its 2.5-year horizon, did not accurately represent the long-term cost of the Notes.<sup>14</sup> Had the Court of Chancery properly used ACLI's 10.83% long-term cost of the Notes, ACLI's value would have decreased from \$38.16 using the Court of Chancery's analysis to \$30.53 per share.

---

<sup>12</sup> The rebuttal report of IQ's expert incorrectly indicated the Notes' yield-to-worst on the Merger Announcement Date was 7.16%. *Compare* A-1946 ¶ 15 *with* IQ Br. at 27.

<sup>13</sup> A-180-81 at 196:13–197:12.

<sup>14</sup> *See* A-223 at 358:19; A-237 at 417:2–418:14; A-250 at 467:8-15; A-251 at 470:6-22; A-1932; A-2172-73.

## **II. THE COURT OF CHANCERY’S ASSUMPTION THAT THE LIBOR BASE RATE WOULD REMAIN AT 0.26% INTO PERPETUITY IS CLEARLY WRONG.**

### **A. Standard of Review**

IQ does not dispute—nor could it—that the Court of Chancery’s factual rulings are entitled to less deference because they do not relate to witness credibility or result from evidence presented at trial. *See* ACLI Br. at 22.

### **B. Merits of Argument**

ACLI has provided this Court with sufficient grounds to overturn the Court of Chancery’s erroneous ruling that the one-month LIBOR rate on the Merger Date (*i.e.*, 0.26%) was the best estimate of ACLI’s long-term LIBOR base rate on the Revolver due to the Court of Chancery’s unsupported and inaccurate belief that the Federal Reserve has stated “its intent to maintain a low interest rate environment going forward.” Post-Trial Order at 9(a). In particular, IQ does not dispute that (1) “[t]he Federal Reserve’s intent was not addressed in any testimony by any fact or expert witness, any brief submitted to the Court of Chancery, or any expert report” (ACLI Br. at 23-24); (2) the Post-Trial Order offers no support for its assertion that the Federal Reserve indicated its intent to maintain a low interest rate environment going forward (ACLI Br. at 23); (3) the Federal Reserve indicated its intent to keep interest rates low “for an extended period” but stated it would ultimately “act to increase short-term interest rates”—that is, *not keep interest rates low* into perpetuity (ACLI Br. at 23-27); (4) neither expert advocated for use

of the actual cost of the Revolver on the Merger Date (ACLI Br. at 26); and (5) the 4.0% average LIBOR over the last 20 years was consistent with the SWAP market's prediction of a 4.15% future LIBOR rate (ACLI Br. at 27-28, n.37).

IQ ignores a mountain of evidence cited in ACLI's opening brief, including the Congressional transcript of Federal Reserve Chairman Bernanke, indicating the Federal Reserve did not intend to keep interest rates low into perpetuity and instead argues incorrectly that this Court cannot consider the proffered evidence reflecting the Post-Trial Order's clearly erroneous assumption. *See* ACLI Br. at 23-24, 26-28, n.27, n.32. This Court may take judicial notice of the proffered evidence as to the Federal Reserve's intent for long-term interest rates, as it comes from publicly available documents "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned" and are not reasonably subject to dispute.<sup>15</sup>

Because IQ cannot rebut ACLI's primary argument—that the Court of Chancery relied on an erroneous inference and applied a short-term measure to determine a long-term input—IQ inaccurately asserts that "[t]he Court of Chancery never tried to determine what LIBOR would be in the future." IQ Br. at 21. But

---

<sup>15</sup> *See supra* Note 9; *see also In re Indian Palms Assocs., Ltd.*, 61 F.3d 197, 205 (3d Cir. 1995) (applying Federal Rule of Evidence 201(f) which is identical to Delaware Rule of Evidence 201(f) and holding that "[j]udicial notice may be taken at any stage of the proceeding, *including on appeal*, as long as it is not unfair to a party to do so and does not undermine the trial court's fact-finding authority.") (citations omitted, emphasis added).

that is exactly what the Court of Chancery did. Consistent with well-established valuation principles, the *Emerging Communications* opinion on which IQ relies,<sup>16</sup> and IQ's own expert,<sup>17</sup> the Court of Chancery estimated the cost of the Revolver by measuring its expected cost over a long period of time. ACLI Br. at 26 n.31, 31-32, n.42. The Court of Chancery concluded that the LIBOR rate on the Merger Date was the best estimate of the long-term cost of the LIBOR component of the Revolver based on the unsupported and incorrect belief that the low interest rate environment would continue. Post-Trial Order at ¶ 9(a).

To contradict the strong testimony of ACLI's expert as to the long-term cost of the Revolver,<sup>18</sup> IQ has attempted to revive its argument that ACLI improperly relied on the swap market and incorrectly interpreted the upward sloping yield curve on forward Treasury Rates (which both indicate the market expected LIBOR

---

<sup>16</sup> *In re Emerging Commc'ns, Inc. S'holders Litig.*, 2004 WL 1305745, at \*16 (Del. Ch. May 3, 2004) (holding that the company's "actual observed cost of debt" was "the more reasonable long-term debt cost assumption) (emphasis added); IQ Br. at 22.

<sup>17</sup> IQ's expert testified "I think the one-year premium...is an appropriate reflection of the expectation for the cost of that type of capital for the company at the time and into the future." A-2049 at 171:18-24.

<sup>18</sup> As explained in ACLI's opening brief, IQ inaccurately states that the stipulated rate "is also the actual rate that ACLI was paying on the Revolver on the Merger Date." ACLI Br. at 6-8; IQ Br. at 20, 22. ACLI's actual cost of the Revolver exceeded LIBOR plus 3.75%. *See id.* Additionally, IQ claims that nothing in the records suggests that the Revolver distinguishes between "LIBOR Loans" and "Base Rate Loans." IQ Br. at 24. IQ is wrong. ACLI's SEC Form 10-Q filed August 7, 2009 outlines a refinance of the Revolver and specifically discusses that there are separate "LIBOR and base rate loans." AR-194. IQ's complaint regarding the dearth of underlying evidence regarding the cost of the Revolver is precisely ACLI's reason for appeal—the Court of Chancery relied on its own incorrect and unsupported inference to determine the cost of the Revolver and the appropriate LIBOR rate rather than the cost of the Revolver advocated by either party's expert.

rates to rise) because ACLI did not eliminate the impact of a so called “horizon premium.” IQ Br. at 22-23; A-179-180 at 191:22–193:2.<sup>19</sup> ACLI’s expert, however, confirmed at trial that a horizon premium did not materially impact the LIBOR rate predicted by the swap market or forward Treasury rates by looking “for reference purposes at projections from other sources..., particularly in relation to the analysis of long-term interest rates...relevant to the bonds, [and]...long-term interest rate projections for Treasuries.” A-253 at 479:5-12. ACLI’s expert explained that the swap market estimates three-month LIBOR over a 30-year period. A-223 at 358:1-9; A-251 at 473:3-12. Therefore, ACLI’s expert concluded that the proper long-term base rate cost of the Revolver was the 4.15% 30-year LIBOR swap rate, which contractually binds parties that exchange short-term floating payments based on the three-month LIBOR in return for long-term fixed payments. A-2172 at n.51; A-222 at 355:22-356:7.

IQ next argues that the Court of Chancery’s reliance on one-month LIBOR as the base rate for the Revolver was proper because well-established Delaware law and financial literature supports the use of a company’s actual cost of debt. IQ Br. at 3, 11, 22. ACLI agrees: it would be appropriate and consistent with Delaware law for the Court to overrule the Post-Trial Order and apply instead

---

<sup>19</sup> IQ’s claim that ACLI must remove the horizon premium is also disingenuous because IQ’s expert used a risk-free rate in his WACC analysis that incorporated a horizon premium he did not remove. *See* A-181 at 199:5-15; A-2051 at 179:8-19.

ACLI's actual cost of debt.<sup>20</sup> Nevertheless, if the Court utilizes the actual cost of debt, it must do so for all debt instruments, not just the Revolver.<sup>21</sup> Indeed, ACLI is aware of no decision other than the Post-Trial Order where a Delaware court applied the actual cost of debt to one debt instrument and a different measure for the cost of debt for other debt instruments. Had the Court of Chancery consistently applied ACLI's actual cost of debt, the blended cost of debt would be 9.41%—very close to the 9.6% blended cost of debt of ACLI's expert.<sup>22</sup>

For these reasons, the Court should reverse the Court of Chancery's adoption of the 1-month LIBOR rate to determine the cost of the Revolver and apply either (1) the appropriate 7.9% long-term cost of the Revolver (*see* A-2194; ACLI Br. at 14-15) or (2) the actual cost of both the Notes (13.1%) and the Revolver (4.29%), based on the actual amount ACLI paid on each debt facility, resulting in a pre-tax weighted average cost of debt of 9.41%. Solely increasing the cost of the Revolver from the Court's assumption of 4.01% to the correct assumption of 7.9%, decreases ACLI's per share value from \$38.16 to \$32.55.

---

<sup>20</sup> *See* ACLI Br. at 25-26. *See also, e.g., Gilbert v. M.P.M. Enters., Inc.*, 1998 WL 229439, at \*2 (Del. Ch. Apr. 24, 1998) (ordering parties to use actual cost of debt rather than estimated cost of debt in determining WACC).

<sup>21</sup> *See* ACLI Br. at 25-26. *See also, e.g., Hintmann v. Fred Weber, Inc.*, 1998 WL 83052, at \*13 (Del. Ch. Feb. 17, 1998) (considering each of the "actual rates [a company] has paid to banks, commercial lenders and other persons or entities, in arm's length transactions" to determine the company's weighted average cost of debt). IQ advocates for different methodologies in determining the cost of debt for the Notes and the Revolver. IQ Br. at 23. This is for good reason: IQ seeks to take advantage of the fact that ACLI paid below long-term rates on the Revolver, but avoid the fact that ACLI paid above long-term rates on the Notes.

<sup>22</sup> *See* ACLI Br. at 25-26.

### **III. THE TRIAL COURT CONTRAVENED WELL-ESTABLISHED VALUATION PRINCIPLES BY ADOPTING A SHORT-TERM PROXY FOR THE LONG-TERM COST OF ACLI'S NOTES.**

#### **A. Standard of Review**

IQ incorrectly contends abuse of discretion applies because ACLI “argues that the Court of Chancery did not agree with ACLI’s expert.” IQ Br. at 25. ACLI’s objection is not that the Court of Chancery disagreed with its expert; ACLI appealed because the lower court contravened the well-established valuation principle that the “cost of debt used for a WACC in a DCF valuation should reflect expected average interest rates over a long period of time.” ACLI Br. at 31. IQ does not dispute and therefore waived any argument that appellant raises an issue of law reviewed *de novo* where, as here, the trial court in an appraisal case did not apply established valuation methodologies. *See* ACLI Br. at 30, n.39, n.40.

#### **B. Merits of Argument**

Rather than address the issue ACLI appealed, IQ contends ACLI’s expert “ignored ACLI’s actual market cost of debt in favor of an assigned long-term cost of debt.” IQ Br. at 25. ACLI agrees it is consistent with a long line of Delaware opinions to apply the actual cost of the Notes (13.1%), rather than a market-based cost of debt. In the three opinions IQ cites, the Court of Chancery correctly applied the interest rates actually paid on the companies’ debt instruments to determine the actual cost of debt, not a market’s “manufactured long-term cost of

debt” based on “prediction[s] about the future.”<sup>23</sup> In contravention of this case law, the Post-Trial Order applied a market-based measure of the cost of debt. Using the actual cost of debt, the cost of the Notes is 13.1% (not 7.15%), the cost of the Revolver is 4.29% (not 4.01%), and the blended cost of ACLI’s debt is 9.41%—much higher than the 5.84% applied in the Post-Trial Order.

IQ offers no reason for this Court to reject the position ACLI raised on appeal. IQ does not dispute that (1) the Notes’ yield-to-worst represents ACLI’s borrowing costs over 2.5 years, rather than a long period of time; (2) Delaware courts look to a company’s long-term weighted cost of debt, rather than the short-term cost of debt for the WACC input for a DCF analysis; and (3) IQ’s own expert testified that he did not use the yield-to-worst because “[t]he yield-to-worst is only a two and a half-year period.” A-181 at 197:7-9.

IQ’s expert never previously claimed, as IQ does now, that the yield-to-worst cost of debt only applies if the Court selects the book value rather than the market value of ACLI’s debt. This is unsurprising because IQ’s expert, like ACLI’s expert, selected a market-based measure to estimate ACLI’s cost of the Notes. IQ’s expert used the 9.26% yield-to-maturity, which unlike the yield-to-

---

<sup>23</sup> IQ Br. at 26-27 (citing *Emerging Commc’ns*, 2004 WL 1305745, at \*16) (holding the company’s actual observed cost of debt was the more reasonable long-term cost of debt assumption); *Gilbert*, 1998 WL 229439, at \*2 (“[T]he parties should use MPM’s actual cost of debt when calculating the discount rate.”); *Finkelstein v. Liberty Digital, Inc.*, 2005 WL 1074364, at \*27 (Del. Ch. Apr. 25, 2005) (“[P]etitioners have not shown why their figure better captures that value than Katz’s use of the actual debt instruments.”).

worst, estimated ACLI's cost of debt over a long rather than short 2.5-year period. A-139 at 30:13-21. In contravention of its own expert's testimony, IQ incorrectly claims the financial literature does not support the use of the long-term cost of debt and that ACLI's only support for this proposition "is a citation to the trial testimony of ACLI's own expert." IQ Br. at 28. This is wrong. ACLI cited to three valuation treatises in its opening brief, which IQ has failed to rebut and IQ has not provided the Court any valuation literature whatsoever supporting its clearly incorrect argument that "[f]inancial literature...does not advise looking at long-term rates when determining cost of debt in a fair market valuation."<sup>24</sup> IQ has waived any opposition to this literature and the Court of Chancery's failure to comport with well-established valuation literature applying the long-term cost of debt is legal error in contravention of Section 262.<sup>25</sup>

---

<sup>24</sup> IQ Br. at 28. See also ACLI Br. at 26 n.31 (citing Shannon Pratt & Roger Grabowski, *Cost of Capital: Applications and Examples*, at 692-3 (4th ed. 2010) ("The cost of debt capital should reflect the expected average of interest rates over a long period of time."); Aswath Damodaran, *Applied Corporate Finance*, at 398 (3d ed. 2011) (same); Timothy Koller, *et al.*, *Valuation: Measuring and Managing the Value of Companies*, at 232 (5th ed. 2010) (same)); see also *In re Matter of Appraisal of Shell Oil Co.*, 1990 WL 201390, at \*37 (Del. Ch. Dec. 11, 1990) (same).

<sup>25</sup> IQ's claim that the Court of Chancery disagreed with the cost of debt adopted by ACLI's expert fails to aid its case. IQ's citation to the Post-Trial Order relates to the Court of Chancery's statements rejecting the position of ACLI's expert related to the LIBOR portion of the Revolver, and not the Notes. Post-Trial Order at ¶ 9(a). Even if the Court of Chancery's statement did relate to the Notes, its holding contradicts the well-established valuation principle that the cost of debt capital should reflect the expected average interest rates over a long period of time. See *supra* Note 24. Similarly, the quoted portion of the order denying ACLI's motion for reargument does not address whether the yield-to-worst improperly reflects ACLI's cost of debt over a long rather than a short period of time.

**IV. BECAUSE ACLI COULD NOT BORROW ON THE MERGER DATE AT THE 5.84% BLENDED INTEREST RATE ADOPTED BY THE COURT OF CHANCERY, THE POST-TRIAL ORDER IS CLEARLY WRONG.**

---

**A. Standard of Review**

As with many of its arguments, rather than address the merits, IQ incorrectly asserts ACLI did not raise this issue below. However, ACLI's expert repeatedly indicated that she relied on bond rates, Treasury forward rates, and other external indices to confirm her calculation of ACLI's cost of debt, and the lower court did not identify this as a new issue when ACLI raised it in its motion for reargument.<sup>26</sup>

**B. Merits of Argument**

IQ asserts four grounds to reject ACLI's argument that its "B" bond rating, which has a long-term yield of 8.85% demonstrates that ACLI could not borrow at a 5.84% blended cost of debt. Notably, IQ does not dispute that several opinions have correctly found the corporate bond yield to be an appropriate source for estimating a company's cost of debt. *See* ACLI Br. at 34-35.

First, IQ claims ACLI failed to preserve this issue below. As explained above, that is incorrect. Second, it claims this Court cannot consider ACLI's bond ratings because the specific ratings were "never offered at trial." IQ Br. at 30. This is likewise incorrect. The Court may take judicial notice of bond and credit ratings as publicly available information not reasonably subject to dispute. *See*

---

<sup>26</sup> *See, e.g.*, A-223 at 358:22–359:11; A-252-53 at 479:5–480:5; A-765-66; A-1124-26; A-1934.

*supra* Notes 9, 15. Third, IQ claims the credit ratings for each of ACLI’s debt instruments rather than ACLI’s overall “B” credit rating is the appropriate metric. *See* IQ Br. at 30. However, the Revolver does not have a public rating, and it is improper to speculate as to its possible rating as IQ has done.<sup>27</sup> Furthermore, using a company’s overall credit profile is actually a better barometer for a company’s long-term borrowing costs than specific credit instruments, which may not represent the company’s long-term borrowing profile.<sup>28</sup> Finally, IQ misconstrues how debt facilities are rated by speculating that the Revolver would have received a better credit rating than the Notes because it was supposedly a lower credit risk than the Notes. IQ Br. at 30; *see also* A-1102-03; A-1135; ACLI Br. at 34. Rating agencies look to similar debt instruments within an industry to rate specific debt instruments, rather than comparing a particular debt instrument with a company’s other debt instruments as implied by IQ.<sup>29</sup> Thus, the Court should reverse the lower court’s findings as to the cost of debt because they do not reflect the actual cost of debt available to ACLI at the time of the Merger.

---

<sup>27</sup> A-1103; *See, e.g., Gilbert*, 1998 WL 229439, at \*2 (The Court’s goal in enterprise valuations is to “determin[e] *with as much accuracy as possible* the fair value of petitioner’s shares on the merger date.”) (emphasis added).

<sup>28</sup> *See Koller, et al., supra*, at 258-59 (“First, determine the company’s credit rating on unsecured long-term debt. Next, examine the average yield to maturity on a portfolio of long-term bonds with the same credit rating. Use this yield as the proxy for the company’s implied yield on long-term debt.”) (emphasis added).

<sup>29</sup> *See, e.g., Koller, et al., supra*, at 259; Pratt & Grabowski, *supra*, at 62-67.

**APPELLANT’S ANSWERING ARGUMENTS ON CROSS-APPEAL**

**V. THE COURT OF CHANCERY PROPERLY EXCLUDED 50% OF THE STRATEGIC INITIATIVE SAVINGS LINE ITEM FROM MANAGEMENT’S PROJECTIONS.**

**A. Question Presented**

Whether the Court of Chancery correctly excluded 50% of the SIS line item included in management’s projections.

**B. Standard of Review**

Although IQ asserts “the trial court’s decision implicates a question of law,” IQ cites no decision holding that the Court of Chancery can never adjust management’s projections as a matter of law. IQ Br. at 31-34. Rather, IQ’s real quibble is with the projections provided in the sale process—an argument it waived<sup>30</sup>—and with the Court of Chancery’s determination that Noltemeyer and Bryant—who testified in support of an adjustment to the SIS line item—were credible witnesses.<sup>31</sup> Issues of witness credibility are reviewed for clear error and, “when a trial judge’s finding is based on his or her decision to credit the testimony of one or two or more witnesses, each of whom has told a coherent and facially

---

<sup>30</sup> IQ’s expert did not challenge the sale process below and IQ has thus waived this argument. See A-2031 at 100:22–101:3 (“Q. Do you have any reason to believe the sales process undertaken by ACLI was inadequate? A. No, I don’t have any opinions as I sit here right now that the sales process was inadequate.”). See also, e.g., *Scion Breckenridge Managing Member, LLC v. ASB Allegiance Real Estate Fund*, 68 A.3d 665, 678 (Del. 2013) (“[A] party may not raise new arguments on appeal.”).

<sup>31</sup> See IQ Br. at 34–39; Post-Trial Order at ¶ 7(c); see also *id.* at ¶ 9 (“Post-merger litigation adjustments are viewed skeptically, *but American and Knoll provided persuasive reasons for the modifications.*”) (emphasis added); B-294 at 35:3-17; B-302 at 67:4-13; B-343-44 at 17:24-18:22.

plausible story that is not contradicted by extrinsic evidence, that finding...can virtually never be clear error.”<sup>32</sup> This Court reviews other findings of fact for abuse of discretion.<sup>33</sup>

### C. Merits of Argument

#### 1. Delaware Law Does Not Require The Use Of Management Projections.

---

IQ fails to cite a single decision in its brief holding that the trial court cannot wholly reject or modify management’s projections if supported by the evidence. *See* IQ Br. at 31–34. IQ recognizes this fact and explains that there is a “preference” rather than a “requirement” for using management’s projections and a “skepticism” of post-merger adjustments to management projections.<sup>34</sup> Completely undercutting its own argument, IQ cites to *Doft*, where the Court of Chancery appropriately determined not to rely on management’s projections.<sup>35</sup>

IQ further claims the Court of Chancery’s adjustment to account for SIS conflicts with *Emerging Communications* because the *Emerging Communications*

---

<sup>32</sup> *Cede & Co. v. Technicolor, Inc.*, 758 A.2d 485, 491-92 (Del. 2000) (citing and quoting *Anderson v. City of Bessemer City*, 470 U.S. 564, 575 (1985)); *see also Levitt v. Bouvier*, 287 A.2d 671, 673 (Del. 1972) (“When the determination of facts turns on a question of credibility and the acceptance or rejection of ‘live’ testimony by the trial judge, his findings will be approved upon review.”) (citing *Barks v. Herzberg*, 206 A.2d 507 (Del. 1965)).

<sup>33</sup> *M.P.M. Enters., Inc. v. Gilbert*, 731 A.2d 790, 795 (Del. 1999).

<sup>34</sup> IQ Br. at 32-33.

<sup>35</sup> IQ Br. at 32 (“Despite the normal preference for management projections, the court concludes that the petitioners failed to prove that Purcell’s reliance on these projections was justified. Thus, the court must disregard Purcell’s DCF analysis.”) (citing *Doft & Co. v. Travelocity.com, Inc.*, 2004 WL 1152338, at \*5-6 (Del. Ch. May 20, 2004)).

decision did not modify management’s projections.<sup>36</sup> However, just because the facts of one case do not support an adjustment to management’s projections does not mean a decision with different circumstances cannot reasonably support such an adjustment. In fact, this Court and the Court of Chancery have adjusted management’s projections where—as in this case—it is appropriate to do so.<sup>37</sup>

2. The Court Of Chancery’s Adjustment To Management’s Projections Is Supported By The Record.

IQ claims the trial court’s SIS findings are unsupported by the record because (1) ACLI’s expert did not speak with “anyone in management involved in forecasting those savings” (IQ Br. at 32); (2) ACLI’s trial witnesses were not involved in forecasting SIS (IQ Br. at 36-37); (3) the adjustment to SIS by ACLI’s expert was inconsistent with ACLI’s SEC filings (IQ Br. at 35-36); and (4) the Court of Chancery incorrectly concluded that bidders did not assume the SIS were achievable (IQ Br. at 34-35)—an issue IQ did not raise below and has thus waived.

Each of these arguments fails as best demonstrated by the extensive record

---

<sup>36</sup> IQ Br. at 33-34 (citing *Emerging Commc’ns*, 2004 WL 1305745 at \*14-15).

<sup>37</sup> *Gilbert v. MPM Enters., Inc.*, 709 A.2d 663, 669 (Del. Ch. 1997), *aff’d* 731 A.2d 790 (Del. 1999) (affirming lower court’s adjustment of management projections “to reflect MPM’s *actual* financial results and other financial information obtained after the preparation of the projections, but before the merger”) (emphasis in original); *Towerview LLC v. Cox Radio, Inc.*, 2013 WL 3316186, at \*14-23 (Del. Ch. June 28, 2013) (using pre-merger management projections as a “starting point” and then modifying management’s projections based on expert witness testimony); *Gray v. Cytokine Pharmasciences, Inc.*, 2002 WL 853549, at \*10-11 (Del. Ch. Apr. 25, 2002) (discounting projected stream of future cash flows by 50% to account for risk that pipeline product would not reach the market); *Kleinwort Benson Ltd. v. Silgan Corp.*, 1995 WL 376911 (Del. Ch. June 15, 1995) (adjusting management’s projections); *Grimes v. Vitalink Commc’ns Corp.*, 1997 WL 538676 (Del. Ch. Aug. 28, 1997) (rejecting aspects of management’s projections).

supporting the Court of Chancery’s ruling.<sup>38</sup>

During trial, both Noltemeyer and Bryant testified at length that the SIS were unlikely to be achieved.<sup>39</sup> While IQ incorrectly contends these individuals were not directly involved in preparing the SIS line item,<sup>40</sup> IQ has not challenged the accuracy of their testimony that the SIS line item was highly speculative for a number of very specific and well supported reasons. *See* discussion *supra* at pages 2-4. IQ asserts Bryant’s testimony suffered from hindsight bias in assessing the SIS. Nevertheless, IQ ignores Bryant’s testimony that she was careful not to base her testimony on hindsight knowledge and instead did her best to put herself “in the position that we were in back in 2010.” A-208 at 298:1-2; A-312. IQ further takes out of context both Noltemeyer and Bryant’s testimony that management’s projections were reasonable. IQ Br. at 37. Both made very clear in their

---

<sup>38</sup> *See* A-72; A-76-78; A-88; A-92-96; A-122 at ¶ 19; A-123-24 at ¶ 26; A-194 at 249:17–251:2; A-196-97 at 259:17–261:2; A-201-205 at 273:14–288:11; A-205-206 at 289:7-290:5; A-206 at 295:1-4; A-207 at 295:1-4; A-208 at 300:1; A-213-14 at 321:21–325:16; A-216 at 331:22–332:10; A-246 at 451:6-14; A-247 at 456:9-19; A-261 at 511:15–513:22; A-298 at 298:1-2; A-311-16; A-322-27; A-388-94; A-390-91; A-393; A-1596-97; A-1886-87; A-1889; A-1899; A-1978-79 at 13:10–15:19; B-251 at 44:19-24; B-294 at 35:3-17; B-296 at 44:11–45:23; B-302 at 67:4-13; B-305 at 81:10-19; B-343-44 at 17:24–19:15; B-346 at 29:8-18; B-347 at 33:17-34; B-351 at 47:7-8; B-369-72.

<sup>39</sup> A-196-97 at 259:17–261:2; A-201-205 at 273:14–288:11; A-205-206 at 289:7–290:5; A-207 at 295:1-4; A-324; A-389-90; *see also* discussion *supra* at pages 2-3.

<sup>40</sup> A-201-205 at 273:14–288:11 (Bryant testifying that she was involved in preparing the projections and understood the projections and their underlying assumptions); A-205 at 289:7–290:5 (same); A-207 at 295:1-4 (same); Post-Trial Order at ¶ 7(c) (“Noltemeyer testified credibly that it was highly unlikely that American could achieve scheduled service”—an element of SIS). IQ also overlooks discussions by ACLI’s expert with ACLI’s CFO, who was indisputably involved in preparation of the projections. *See* B-244 at 16:14-18; B-301 at 64:15-20.

testimony—which the trial court expressly found credible—that all of management’s projections, with the exception of the SIS line item were reasonable and achievable.<sup>41</sup> Similarly, IQ takes out of context the testimony of ACLI’s expert that she “was engaged to [render] a different kind of judgment than what management was coming to.” *See* IQ Br. at 38. In that testimony, ACLI’s expert explained that she had not “come to a better judgment than management had about the achievability” of the SIS. A-247 at 456:9-19. In other words, ACLI’s expert did not substitute her judgment for that of management but instead considered management’s belief as to the achievability of the SIS to reach the proper enterprise value of ACLI.<sup>42</sup> In contrast, IQ’s expert spoke with no ACLI employees, did no analysis to determine whether the SIS were likely to be achieved, and yet openly rejected the deposition and trial testimony of two ACLI employees and ACLI’s CFO that the SIS were completely speculative. *See* A-324-27; A-388-93. Because Noltemeyer and Bryant’s credible testimony adequately

---

<sup>41</sup> *See, e.g.*, A-196 at 258:23–259:4 (Noltemeyer testifying that he believed the board felt that the projections were a “plausible and practical plan...subject to modification for completed third quarter results and newly identified information”); A-194 at 249:20–251:2 (Noltemeyer testifying that ACLI did not believe scheduled service, one of the components of the SIS, could be implemented); A-208 at 299:15–300:1 (Bryant testifying that “[t]he fact that I’m talking about it’s something that [management] developed and got comfortable with doesn’t mean that they believed that we had a plan to get to all of those savings. But it was a goal.”).

<sup>42</sup> *See* discussion *supra* at pages 2-4. IQ erroneously argues that ACLI’s expert did not provide any “reasoned basis for this arithmetic.” IQ Br. at 38. However, ACLI’s expert explained at trial that with few to no specified plans of how to accomplish the SIS, she “actually felt that there was probably a pretty good basis to exclude all of them” but to be conservative, she kept half. *See* A-216 at 332:8-10; A-393.

support the Court of Chancery’s ruling, the Court should reject IQ’s challenge to the SIS.

IQ asserts “there is no evidence that anyone in ACLI management who developed the projections believed they were unlikely to be achieved.” IQ Br. at 37. This is untrue. IQ ignores the testimony of ACLI’s CFO, who developed the projections, that the SIS “were a set of specific initiatives that we thought we would work on. No detail plans put together. More targets. But the projections were based on a lot of other assumptions as well. So it was not just those cost savings.” *See* B-294 at 35:3-17; B-296 at 44:11–45:1; B-302 at 67:4-13; B-305 at 81:10-19.<sup>43</sup>

IQ also contests the adjustment to the SIS on the grounds that it was inconsistent with ACLI’s public filings. *See* IQ Br. at 31-32. However, this adjustment was completely consistent with the Proxy, which presented stockholders with three different projection scenarios, one of which gave 1/3 weight to the SIS and another giving 100% weight to SIS.<sup>44</sup> Therefore, as the Court of Chancery observed, the Proxy allowed ACLI’s stockholders to decide

---

<sup>43</sup> ACLI anticipates IQ will assert this testimony does not support an adjustment to ACLI’s projections because ACLI’s CFO supposedly was only describing the last year worth of projected strategic cost savings as unidentified. A-163 at 127:18-128:12. IQ simply misreads the testimony of ACLI’s CFO, which makes clear he is discussing all of the SIS, not just one year. B-296 at 44:18-45:1. Moreover, ACLI’s CFO never testified that the SIS had specific plans in some years, but not in others and IQ has never identified a single piece of evidence supporting that proposition.

<sup>44</sup> *See* A-325-27; A-1596-97; A-95; Post-Trial Order at ¶ 7(b).

which set of projections was more realistic.<sup>45</sup>

IQ claims that the Court of Chancery incorrectly concluded that “the market check that American conducted shows that actual buyers did not fully credit the undiscounted projections.” Post-Trial Order at ¶ 7(a); IQ Br. at 34-35. However, as the Court of Chancery correctly reasoned:

If the projections had been taken at face value, then any of the 13 [parties that entered into confidentiality agreements with ACLI during the go-shop] would have concluded that the Company represented a profitable investment opportunity at values north of the \$33.00 per share Merger price. No topping bid emerged. This fact implies that sophisticated financial players facing both the incentive and discipline of the profit motive did not view the undiscounted projections as reasonably achievable.<sup>46</sup>

Thus, the lower court rationally concluded that if bidders believed IQ was worth \$41.63 per share, as reflected in the DCF analysis of IQ’s expert (*see* A-2111; A-2136), they would not have ignored the valuations provided them and the opportunity to make a topping bid at a large profit. IQ’s theory is further belied by the fact that the free cash flows disclosed in the proxy are higher than management’s free cash flows. *Compare* A-1596-97 with B-449; B-453. Therefore, the projections disclosed in the Proxy should have led potential

---

<sup>45</sup> Post-Trial Order at ¶ 7(b). The Proxy also included extensive warnings related to ACLI’s projections, including that “readers of this proxy statement are cautioned not to place undue reliance on the financial forecasts” and that including the projections in the Proxy did not mean that the Board “considered, or now considers, it to be predictive of actual future results, and they should not be relied on as such.” A-1597; A-261 at 511:15–513:22 (ACLI’s expert testifying as to same); A-390-91.

<sup>46</sup> Post-Trial Order at ¶ 7(a). *See also* A-122 at ¶ 19; A-123-24 at ¶ 26; A-124 at ¶ 28; A-315-16.

purchasers to place a higher (not lower) value on ACLI.

IQ is also wrong that “potential buyers never had the opportunity to consider (or fully credit) management’s actual July projections.” IQ Br. at 35. The 13 bidders who signed confidentiality agreements had access to a set of management projections including the years 2015 and 2016 and information to independently account for deferred income taxes.<sup>47</sup> But under IQ’s myopic approach, sophisticated purchasers would turn a blind eye to the projections they received from management and instead rely on ACLI’s financial advisor. This makes no sense, as it would completely negate the need for a buyer’s due diligence. Moreover, IQ’s expert conceded that he did not have any reason to question ACLI’s sale process, was unaware of any additional potential purchaser that should have been contacted, and had no reason to believe any purchaser would pay more than the Merger price. A-2031-32 at 100:22–102:11; *see also* A-316. Thus, IQ has offered no evidence to support its new theory that potential purchasers were misled by BAML’s analysis or the projections disclosed in ACLI’s Proxy.

Accordingly, IQ has offered no evidence that indicates the lower court abused its discretion in this finding.

---

<sup>47</sup> B-304 at 76:12–79:3 (ACLI’s CFO explaining that the Company normally only engaged in five-year projections but extended the May 2010 projections to 2016 to account for higher than normal capital expenditures); B-422-453; AR-229 at 51:2-6 (management projections were added to the buyers’ data room); *see also* B-229 (BAML cash flows projections as reported in the Proxy indicating that “Free cash flow [is] defined as Cash Flows From Operations less Capital Expenditures”); A-1596-97.

**VI. THE COURT OF CHANCERY PROPERLY INCLUDED THE OTHER NON-CASH OPERATING ACTIVITIES LINE ITEM IN ACLI'S PROJECTIONS.**

---

**A. Question Presented**

Whether the Court of Chancery properly included the ONCOA line item in calculating ACLI's free cash flows.

**B. Standard of Review**

ACLI agrees abuse of discretion applies. IQ Br. at 40.

**C. Merits of Argument**

IQ claims the record does not support Court of Chancery's inclusion of the ONCOA line item. IQ Br. at 41-42. The Court of Chancery reasonably included the ONCOA line item, less debt cost amortization. At trial, IQ's expert admitted he did not know what elements made up ONCOA and provided no explanation for excluding the line item in his report. A-169 at 149:15–151:16.<sup>48</sup> However, IQ's expert went on to admit that, although he did not attempt to determine the contents of ONCOA, "there's some decomposition of [the non-cash operating activities line item] that's possible if you study carefully the other pages in the fleet reinvestment update." A-169 at 149:15–150:18. Indeed, it is quite easy to understand what the ONCOA line item contains. As demonstrated by the chart presented at trial and

---

<sup>48</sup> IQ disingenuously attempts to argue that it relied on BAML's exclusion of this line item. However, neither expert relied on BAML's projections in their reports, and IQ's brief criticizes BAML's analysis. A-149 at 71:3–72:1; A-212-13 at 317:21–318:5; IQ Br. At 35-36. Furthermore, while IQ certainly had the right to question ACLI's expert regarding her rationale for including ONCOA, it chose not to do so at trial.

attached hereto as Exhibit A, by comparing the actual results in management's projections for 2009 to the results reported in ACLI's 2009 10-K, it is obvious that both documents report the same operating cash flows but contain different line items. *See also* A-327-29. As reflected in the chart, the 2009 results in management's projections do not include (1) \$17,659 in Debt Retirement Costs, (2) \$7,145 in Debt Issuance Cost Amortization,<sup>49</sup> (3) \$11,853 in Impairment and Loss on Sale of Summit Contracting, (4) a -\$20,264 gain on property disposition, (5) \$3,885 in other operating activities and (6) \$2,302 in accounts receivable. These line items from ACLI's 2009 10-K total the precise amount of ONCOA, demonstrating they comprise ONCOA.

Despite the admissions of IQ's at trial expert that he could have determined the components of ONCOA but did not do so, IQ suggests the Court should exclude ONCOA because it is listed as a non-cash line item. IQ Br. at 42. Shannon Pratt, however, counsels that non-cash charges should be considered in calculating free cash flows,<sup>50</sup> and IQ's expert included non-cash charges such as depreciation in his cash flows (A-2136). Therefore, it was important for IQ's expert to understand what the ONCOA line item included to determine whether to include the line item in ACLI's free cash flows. Instead IQ's expert rejected it out

---

<sup>49</sup> IQ's expert conceded that if ONCOA included amortization of debt expense, that element should be excluded from free cash flows. A-170 at 155:15–156:6; A-327-28.

<sup>50</sup> A-168 at 147:11–148:3; Shannon Pratt, *Valuing a Business: The Analysis and Appraisal of Closely Held Companies*, at 180 (5th ed. 2007).

of hand with no analysis.

IQ claims that including ONCOA was improper because some of the line items were “likely one-time revenues or expenses.” IQ Br. at 42. Many of the ONCOA components, like operating activities and accounts receivable, indisputably belong in free cash flows.<sup>51</sup> Moreover, one-time items were included only in the actual results for 2009 and 2010 and not for the projection years that form the bulk of the DCF analyses. In 2009 and 2010, the years that contained one-time items, the ONCOA line item was positive. *See* B-452. Nevertheless, ONCOA was quite negative in the projected years that did not include one-time revenues or expenses.<sup>52</sup> *See id.*

Contrary to IQ’s claim (IQ Br. at 40-41), the ONCOA line item in the opening report of ACLI’s expert report matches the line item in management’s projections. *See* A-1931. ACLI’s expert report includes a footnote explaining that ONCOA “exclude[s] amortization of debt expense.” *Id.* Accordingly, the line item used by ACLI’s expert is derived by simply subtracting the “Amortization of Debt Expense” line item on ACLI’s projected income statement (B-452) from ONCOA included in ACLI’s projected Balance Sheet and Cash Flow statement (B-453).

---

<sup>51</sup> *See* Pratt, *supra*, at 131-32.

<sup>52</sup> *See* B-452. ACLI did not have an opportunity to address this argument before the trial court, as IQ first raised it in its post-trial answering brief. *See* A-372-73.

**VII. WHETHER THE COURT OF CHANCERY ERRED IN ADOPTING THE BETA AND SMALL STOCK PREMIUM VALUES OF ACLI'S EXPERT.**

---

**A. Question Presented**

Whether the Court of Chancery properly adopted the beta and small stock premium of ACLI's expert.

**B. Standard of Review**

ACLI agrees the standard of review is abuse of discretion. IQ Br. at 43.

**C. Merits of Argument**

1. The Court Of Chancery Properly Relied On ACLI's Barra Beta.

IQ claims the Court of Chancery mistakenly found that IQ's expert relied on a single beta, while ACLI's expert considered several beta estimates before settling on a mid-point. IQ Br. at 43-44. The Court of Chancery's finding is correct. Although IQ's expert utilized betas from several companies that he deemed "comparable," he looked to only one source for these betas: the 5-year monthly Bloomberg adjusted beta. A-181 at 199:16-23; A-2137; A-2123-24. In contrast, ACLI's expert analyzed five-year historical monthly betas and predicted betas published by Barra as well as raw and adjusted two-year historical weekly betas; she then selected a conservative unlevered, predicted beta published by Barra of 0.80 which was the mid-point of the beta sources she consulted. A-1896-97; A-223-25 at 361:1-368:24; A-340.

The Court should also reject IQ's appeal for three independent reasons—

each of which IQ has waived on appeal by not raising in its answering brief. First, IQ offers the Court no reason why the Court of Chancery's adoption of the proposed beta adopted by ACLI's expert was unreasonable. *See* Post-Trial Order at ¶ 9(b); A-340-44; A-398-400. Second, the beta selected by IQ's expert is only reliable if the comparable companies IQ's expert selected are in fact comparable to ACLI. *See* A-322; A-400. The Barra predicted beta selected by the Court of Chancery is specific to ACLI and thus directly contemplates risks relative to the company, not the industry in general. *See* A-223-24 at 361:18–362:4; A-255 at 489:14-18. Because the Court of Chancery found “[t]he comparable companies identified by the experts were insufficiently comparable to American”—a ruling IQ does not dispute—it would be illogical to rely on a beta based on comparable companies as IQ's expert did. Post-Trial Order at ¶ 4. Third, IQ has not shown the Court of Chancery improperly rejected IQ's reliance on an adjusted beta in this case. A-181 at 199:16–201:10; Post-Trial Order at ¶ 9(b). In determining adjusted beta, Bloomberg assigns  $\frac{2}{3}$  weight to the actual or raw beta of a company and assigns  $\frac{1}{3}$  weight to the market beta of 1, which has the effect of adjusting the raw beta closer to the market average of 1. *See* A-181 at 199:24–200:14; A-399-400. The Court of Chancery rejected IQ's reliance on an adjusted beta because IQ's expert “could not offer evidence supporting a mean-reverting beta for [ACLI].” Post-Trial Order at ¶ 9(b). Indeed, when asked at trial if there was evidence

suggesting ACLI's beta was likely to revert to the market beta of 1, IQ's expert responded "no." A-182 at 202:16-20.

2. The Court of Chancery Properly Relied on the Small Stock Premium of ACLI's Expert.

IQ asserts the Court of Chancery's adoption of Barra beta and the small stock premium of IQ's expert was improper because the small stock premium captures the same risks that are already accounted for in Barra beta.<sup>53</sup> IQ Br. at 4, 45-47. ACLI also argues the small stock premium selected did not accurately reflect the risk associated with ACLI's value. *Id.* As ACLI's expert explained at trial and ACLI detailed in its post-trial briefing, it is well-accepted in the valuation community that the systematic risk measured by Barra beta does not include the unsystematic risk measured by the market capitalization the Ibbotson Associate Report uses to determine the small stock premium.<sup>54</sup> Data compiled by Pratt and Grabowski clearly shows that Barra betas are *not* higher than historical small stock betas, which would have to be the case if Barra predicted beta accounted for the small-stock premium.<sup>55</sup>

IQ also contends that the Court of Chancery inappropriately determined the

---

<sup>53</sup> IQ's adoption of this argument is misleading, since IQ's expert adopted what he called "an unsystematic risk premium" (2.5%) which he equated to the small stock premium used by ACLI's expert (2.67%). A-137 at 22:12-23:15.

<sup>54</sup> A-225-27 at 369:14-374:21. Pratt, *supra*, at 193. A-341-42; Ibbotson SBBI 2011 Valuation Yearbook, *Market Results for Stocks, Bonds, Bills, and Inflation*, at 88 (1926-2010); Pratt & Grabowski, *supra*, at 177.

<sup>55</sup> Pratt & Grabowski, *supra*, at 178; A-255 at 486:13-487:5; *see also* A-341-42.

small stock premium based on an average of the eighth and ninth deciles of the Ibbotson Associates Report small stock premiums. The decile chosen is important because each decile corresponds to the specific equity value of the company at issue. However, it would make no sense to use IQ's small stock premium based on the eighth decile, since that was based on the valuation of IQ's expert of \$45.01 per share—a valuation the Court rejected—instead of independent market evidence. *See* A-2114; A-2131. The Court of Chancery explained this results-driven approach is improper because it does not provide an “independent basis or value” to determine the propriety of applying a risk premium.<sup>56</sup> In this case, Capital IQ independently reported a market capitalization for ACLI shortly before the Merger Announcement well within the ninth decile. ACLI's market capitalization based on the Merger price fell barely within the ninth decile.<sup>57</sup> Thus, contrary to IQ's claim, the decile chosen by ACLI's expert was not based on her own valuation, but rather on available market valuation information from Capital IQ. *See* IQ Br. at 44-45. Accordingly, it would be completely appropriate to solely rely on the ninth decile; however, ACLI's expert conservatively chose to average the eighth and ninth decile figures. *See* A-399.

Finally, IQ does not dispute the Court of Chancery's ruling that IQ's expert

---

<sup>56</sup> *See In re Sunbelt Beverage Corp. S'holder Litig.*, 2010 WL 26539, at \*11 & n. 38 (Del. Ch. Jan. 5, 2010).

<sup>57</sup> A-399 (citing Capital IQ Market Cap Report).

used stale data that reached a more favorable equity risk premium. Post-Trial Order at ¶ 9(c); *see also* A-344. Because IQ did not question this ruling in its answering brief, the argument is waived and it provides an independent reason not to rely on the small stock premium of IQ's expert. *See supra* Note 5.

### **CONCLUSION**

For the reasons stated herein, ACLI requests that the Court correct the valuation errors by the trial court, reverse the Court of Chancery's cost of debt findings, and instruct the Court of Chancery to consider adopting a blended cost of debt of 9.6%, representing the 10.83% cost of the Notes and the 7.90% cost of the Revolver identified by ACLI's expert. ACLI further requests that this Court uphold the Court of Chancery's well-supported factual findings as to the exclusion of 50% of the ASIS, the inclusion of the ONCOA line item, and the beta and the small stock premium advocated by ACLI's expert.

*/s/ Kevin G. Abrams*

---

Kevin G. Abrams (#2375)  
Derrick B. Farrell (#5747)  
Abrams & Bayliss LLP  
20 Montchanin Road, Suite 200  
Wilmington, Delaware 19807  
(302) 778-1000

*Attorneys for American Commercial  
Lines Inc., Respondent Below,  
Appellant and Cross-Appellee*

Dated: August 13, 2013