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SUPREME COURT
STATE OF DELAWARE

IN THE SUPREME COURT OF THE STATE OF DELAWARE

MUIRFIELD VALUE PARTNERS, L.P., OASIS INVESTMENTS II MASTER FUND LTD., CANDLEWOOD SPECIAL SITUATIONS MASTER FUND, LTD., CWD OC 522 MASTER FUND LTD., and RANDOLPH WATKINS SLIFKA

Petitioners-Below,
Appellees/Cross-Appellants,

v.

DFC GLOBAL CORPORATION,

Respondent-Below,
Appellant/Cross-Appellee.

No. 518, 2016

Appeal from the Memorandum
Opinion dated July 8, 2016,
as modified by the Order and Final
Judgment dated September 14, 2016,
of the Court of Chancery of the
State of Delaware, Consolidated
C.A. No. 10107-CB

APPELLEES/CROSS-APPELLANTS' ANSWERING BRIEF AND OPENING BRIEF ON CROSS-APPEAL

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES iii

NATURE OF PROCEEDINGS 1

SUMMARY OF ARGUMENT 9

COUNTER-STATEMENT OF FACTS 10

I. Respondent’s Business Has Always Been Highly Regulated 10

II. The U.K. Imposes New Regulations on Respondent’s Business 12

III. DFC’s Projections Incorporated All Known Regulatory Changes 14

IV. DFC Sells Itself at Trough Performance 16

V. Lone Star Manipulated the Sales Process 17

ARGUMENT 22

I. THE TRIAL COURT’S OPINION FINDING THE FAIR VALUE OF DFC AS OF THE TRANSACTION DATE TO BE $10.30 PER SHARE SHOULD BE AFFIRMED 22

A. QUESTION PRESENTED 22

B. STANDARD OF REVIEW 22

C. MERITS OF ARGUMENT 23

1. The Court of Chancery Has Broad Discretion To Consider “All Relevant Factors” 23

2. The Appraisal Statute Does Not Permit Bright-Line Rules 25

(a) The Unambiguous Language of the Statute Has Not Changed 25

(b) This Court Has Previously Declined Respondent’s Proposed Bright-Line Rule 26

(c) Respondent Never Presented Evidence On Deal Price 28

(d) Contemporary Empirical Studies Show That Appraisal Functions As Intended By The General Assembly 28

II. THE TRIAL COURT PROPERLY EXERCISED ITS DISCRETION IN ADOPTING A PGR OF 4 PERCENT IN ITS DCF ANALYSIS 32

A. QUESTION PRESENTED 32

B. STANDARD OF REVIEW 32

C. MERITS OF ARGUMENT 32

III. IN THE ALTERNATIVE, THE TRIAL COURT ABUSED ITS DISCRETION BY ACCORDING THE COMPARABLE COMPANY ANALYSIS ANY WEIGHT IN DETERMINING FAIR VALUE 36

A. QUESTION PRESENTED 36

B. STANDARD OF REVIEW 36

C. MERITS OF ARGUMENT 36

1. The Trial Court Should Not Have Accorded the Comparable Company Analysis Any Weight 36

2. The Trial Court's DCF Analysis Should Have Been Given Substantial, If Not Exclusive, Weight in Determining the Fair Falue of DFC 40

CONCLUSION 46

TABLE OF AUTHORITIES

Page(s)

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In re Adoption of Swanson,
623 A.2d 1095 (Del. 1993) 25

Andaloro v. PFPC Worldwide, Inc.,
2005 WL 2045640 (Del. Ch. Aug. 19, 2005) 41

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2016 WL 3186538 (Del. Ch. May 31, 2016)..24, 40, 42

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884 A.2d 26 (Del. 2005) 22, 32, 36

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65 A.3d 571 (Del. 2013) 25

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902 A.2d 1130 (Del. Ch. 2006) 42

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709 A.2d 663 (Del. Ch. 1997), *aff'd*, 731 A.2d 790 (Del. 1999) 39

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777 A.2d 242 (Del. 2001) 37

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11 A.3d 214 (Del. 2010) 1, 24, 26, 27

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73 A.3d 926 (Del. 2013) 25

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737 A.2d 513 (Del. 1999) 24

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2013 WL 3793896 (Del. Ch. July 8, 2013), *judgment entered sub nom.*,
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2006 WL 2403999 (Del. Ch. Aug. 18, 2006) 38

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28 A.3d 442 (Del. Ch. 2011) 39

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1983 WL 8936 (Del. Ch. Sept. 19, 1983), *aff'd*, 493 A.2d 929 (Del. 1985) 39

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Supr. Ct. R. 8 1

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NATURE OF PROCEEDINGS

On June 13, 2014, Lone Star Fund VIII (U.S.), L.P. ("Lone Star") acquired DFC Global Corporation ("Respondent," "DFC," or the "Company") for $9.50 per share. Following a three-day trial, the Court of Chancery determined that the fair value of DFC was $10.30 per share.[1] Now, on appeal, Respondent seeks to rewrite the appraisal statute and overturn established Delaware law by asking this Court to institute a bright line rule that deal price is the equivalent of fair value when there is an "arm's-length, conflict-free transaction."[2] Appellant's Opening Brief ("AOB") at 1. Respondent's espousal of a deal price rule, however, is extremely curious given that DFC's expert never relied on deal price as evidence of fair value in this case, and Respondent never presented any evidence at trial in support of deferral to deal price.[3]

While the deal price is one of the factors that a court *may* consider under appropriate circumstances, it is not – and should not be – a default rule. The fact

[1] The Court arrived at its $10.30 fair value determination by blending (i) a discounted cash flow ("DCF") analysis (yielding a result of $13.07); (ii) the $9.50 deal price; and (iii) a comparable company analysis (yielding a result of $8.07), according each method one-third weight.

[2] While Respondent postures this as a request for a bright-line rule, what it is actually asking for is an express overruling of *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214 (Del. 2010) ("*Golden Telecom*"), and its progeny.

[3] Indeed, given that DFC did not rely on deal price at all in the valuation analysis it presented to the Court of Chancery, it is questionable whether Respondent's argument for deal price now is properly preserved for appeal. Sup. Ct. R. 8.

that there is no automatic deferral to deal price is what makes Delaware's appraisal statute such an important safeguard for stockholders. Indeed, the whole purpose of Section 262 is to provide stockholders who are unhappy with *the deal price* with a mechanism to protect their rights and challenge the consideration that they are being forced to accept in exchange for their shares. To take away the Court of Chancery's discretion and adopt the one-size-fits-all rule proffered by Respondent would effectively eviscerate appraisals.[4]

Nor would Respondent's proffered rule make appraisal litigation any less costly or predictable. In fact, it would have the opposite effect by creating a preliminary dispute over whether a transaction meets the standard of "arm's length, conflict free." Would an appraisal turn into a bifurcated trial, one to determine what type of transaction transpired and the other to then value the company? Would it have two sets of discovery? Would appraisal now become the same as a breach of fiduciary duty case?

One need look no further than the facts of this case to see that companies will try to shoehorn virtually every challenged merger into the "arm's length, conflict free" box, no matter how ill-fitting it is. Here, the premise for Respondent's appeal, contending that this case presents a "competitive bidding

[4] Albert Choi & Eric Talley, *Appraising the "Merger Price" Appraisal Rule*, Virginia Law & Economics Research Paper No. 2017-01 at 21 (Jan. 18, 2017) ("At least when viewed in isolation, the [Merger Price] rule is tantamount to eliminating the appraisal remedy altogether.").

process" resulting in an "arm's-length, conflict-free merger," AOB at 3, is far afield from reality. There was no competitive bidding process at all. There was one private equity bidder who demanded exclusivity, received that exclusivity in exchange for a required bid of $12 per share, and then executed a bait-and-switch during the exclusivity period whereby it slashed its offer more than 20 percent to $9.50. At this point, there were no other bidders and DFC did not conduct a go-shop. The reality is that there was no auction process at all.[5]

Respondent tries to paint the requirements of the appraisal statute as being "speculative, manipulable, and unpredictable," AOB at 2, but this characterization is complete fantasy. In particular, Respondent focuses the heart of its attack on the trial court's consideration of a discounted cash flow ("DCF") analysis, despite the fact that its own expert relied heavily on such an analysis, according it 50 percent weight in his overall valuation. A DCF analysis is *not* speculative; it is forward-looking. A DCF analysis using projections prepared by a competent management team, in good faith and with the goal of capturing the expected future cash flows of the company focuses on the *real value* of the *actual company being valued*, as opposed to a methodology using a market-based proxy, which could be skewed by

[5] Nowhere in its brief does Respondent assert that this merger resulted from a competitive auction process – nor could it. The only other prospective purchaser involved – J.C. Flowers & Co. LLC ("J.C. Flowers") – had indicated interest at $13.50 per share, significantly higher than Lone Star's eventual bid. Instead of proactively working with J.C. Flowers, Respondent locked up a deal with Lone Star for a much lower price. A801–A802 [74:22–79:12]; A111 ¶117.

a number of external factors.[6] A DCF analysis is the best methodology for determining the long-term value of a company and has been recognized as such by the Delaware courts, academics and valuation experts alike.

Respondent shrouds its attack on appraisal litigation as a criticism of Chancellor Bouchard's determination on a motion for reargument ("Reargument") that a higher perpetual growth rate ("PGR") was required to support the working capital assumptions being relied upon in his DCF model. Reargument Order, attached as Exhibit B to AOB, at ¶¶5–8. The trial court's acceptance of a 4 percent PGR, however, is supported by both established economic principles and the facts of this case. Respondent paints the trial court's choice as arbitrary and capricious, but this characterization ignores the fundamental interrelatedness of working capital and long-term growth. These inputs necessarily go hand-in-hand: if a business is projecting higher growth, it will be required to expend additional working capital to sustain that growth into perpetuity. Likewise, if a company is projecting higher working capital forecasts at the end of a projection period, that supports a higher terminal growth rate. One input is a function of the other and it is inappropriate to simply pick and choose assumptions from different models

[6] These factors include: (i) timing of the transaction; (ii) availability of financing; (iii) general market conditions; (iv) whether the process includes a homogeneous pool of potential buyers; (v) whether there are interested parties on both sides of the transaction; and (vi) whether there have been changes to the business between the time the deal is signed and the time the transaction closes.

without ensuring that they are correlative. Chancellor Bouchard realized this error on Reargument and properly corrected this mistake by adjusting the PGR to 4 percent to account for the working capital assumptions reflected in the March Projections.

Respondent's argument likewise ignores the fact that even where there is a full, fair and open auction process – which there was not here – a number of other short-term factors[7] can affect what a third party acquiror is willing to pay, such as:

- the timing of the transaction;
- the ability of potential acquirors to obtain financing;
- whether the bidding pool includes more than one type of bidder; and
- the general market conditions at the time the company is sold.

All of these factors affect the reliability of the deal price as an indicator of value, which is exactly why the Court of Chancery is given broad discretion in determining fair value. Here, the Chancellor used his discretion to reject Respondent's post-trial argument that fair value should be determined solely from

[7] In addition, the time between signing and closing of the transaction can have a material effect on whether the deal price has any relevance to fair value. *Merion Capital L.P. v. Lender Processing Services, Inc.*, 2016 WL 7324170, at *23 (Del. Ch. Dec. 16, 2016) (noting that the "parties have to address th[e] temporal gap" between signing and close).

the deal price,[8] and his exercise of that discretion was supported by the facts presented at trial.

First, the deal itself was ill-timed, as DFC was in the midst of a tremendous transition in its U.K. market as a result of regulatory changes taking place there. Indeed, DFC considered itself one of the "good guys" in the payday lending space and had proactively adopted anticipated regulations ahead of any requirement to do so, while rogue lenders remained in play under the old rules. DFC knew that this decision would result in temporarily depressed financial results in the short-term, but believed that those changes would ultimately be beneficial for its business as the regulations were imposed on all of its competitors and rogue lenders were forced out of the industry.

Second, as a result of its proactive policies in the U.K., DFC's business was at a trough in 2014 and 2015. Because DFC was operating at trough EBITDA levels when the deal took place in June 2014, Lone Star and all other potential private equity bidders were hampered by the amount of financing available to them to fund the deal, which affected the amount of money Lone Star could pay while still obtaining its required rate of return.

[8] This was a curious approach by Respondent, putting forth an expert who did not rely on deal price at all in his valuation opinion and then shunning that opinion post-trial to argue that deal price should be the sole indicator of fair value.

Third, the fact that only two private equity bidders were involved in the process – coupled with the leverage and lending restrictions affecting the deal – meant that none of the parties to the process were evaluating the intrinsic value of DFC and all of the bids were based on a leveraged buy-out ("LBO") model tied to the private equity firm's required internal rate of return. Thus, the final deal price reflected what Lone Star was willing to pay, not the fair value of DFC as a going concern.

Finally, the market conditions at the time of the Transaction affected the deal price in this case. The market had overreacted to the impact of the U.K. regulatory changes taking place and did not have the information or ability to test the Company's belief that these regulations would be ultimately beneficial to its business. Thus, the market took a negative view of DFC's business and the Company's stock price was depressed at the time the Transaction took place. Short-term market reactions to known temporary conditions of a business do not, however, reflect the long-term value of a company.

The trial court appropriately exercised its discretion in valuing DFC at $10.30 per share, and its opinion should be affirmed. In the alternative, to the extent there was an abuse of discretion, it was with respect to the use of the comparable company methodology by the trial court. Under the facts of this case, it was not appropriate to rely on a comparable company analysis because DFC was experiencing trough EBITDA levels for the comparison years, the selected peer companies were not experiencing the same trough financial condition and were not comparable to DFC either in geography or business mix, and the range of values resulting from the comparable company analysis was extremely wide – ranging from a *negative* number to $18.20 per share. Under the facts of this case, the DCF analysis is the most reliable indicator of fair value of DFC.[9]

[9] To the extent that the trial court wanted to use a blended methodology, it should have limited itself to the deal price and DCF, with the DCF being accorded more weight, as it is more reliable.

SUMMARY OF ARGUMENT

1. Denied. The trial court properly exercised its discretion under the appraisal statute in concluding that the fair value of DFC on June 13, 2014 (the "Transaction Date") was $10.30 per share, and the trial court's opinion should be affirmed. *See infra* at Argument, I.C.1. The Court should decline to establish a bright-line, mandatory rule that the Court of Chancery must defer automatically to the deal price. *See infra* at Argument, I.C.2.

2. Denied. The trial court properly adjusted the PGR used in its DCF analysis to 4.0 percent to account for the increased working capital assumptions reflected in the March Projections. *See infra* at Argument, I.C.3.

3. On cross appeal and in the alternative, to the extent there was an abuse of discretion, it was solely with respect to the weight accorded to the comparable company analysis in the trial court's fair value determination, which here is not a reliable indicator of fair value. *See infra* at Argument, II.C.1. Instead, the trial court should have accorded its DCF analysis substantial, if not exclusive, weight in its fair value determination, as the DCF analysis was the most reliable indicator of fair value. *See infra* at Argument, II.C.2.

COUNTER-STATEMENT OF FACTS

I. Respondent's Business Has Always Been Highly Regulated

Before the Transaction, Respondent was a leading international non-bank provider of alternative financial services, principally consisting of unsecured short-term consumer loans (*i.e.*, payday loans), secured pawn loans, check cashing, gold buying, money transfers, and reloadable prepaid debit cards. B135. It served mostly unbanked and under-banked consumers. B135; B1175–B1181; A437–A438. As of the Transaction Date, the U.K. (including the Republic of Ireland), Canada, and the U.S. were the Company's core markets, and Sweden, Finland, Poland, Spain, Romania, and the Czech Republic were growing markets. B229; B135.

Because of the nature of Respondent's business, DFC historically has been subject to regulatory oversight across all of its markets. B136–B140. As a result, Respondent always has been cognizant of the risk inherent in its business, including the risk that changes to regulations affecting its business could increase the cost of doing business or otherwise limit the Company's opportunities. B142–B144. Despite these risks, Respondent had a proven track record of navigating and overcoming regulatory change within its operating markets. A736 [62:3–64:24]; A453.

For example, five years before the Transaction, DFC's Canadian business – the Company's second-largest market – underwent a complete regulatory overhaul. From 2007 to 2010, the Canadian government reformed its regulation of the payday lending industry by adopting a provincial-level regime. A183–A184 [135:7–137:22]; A736 [63:5–64:24]; A393; A397; A449; A453. As a result of this change, some provinces adopted stricter limitations on lending and affordability requirements, while others prohibited the short-term consumer lending business altogether. A736–A737 [65:6–66:20]; A753–A754 [131:6–137:24]; A449.

These changes took a short-term toll on Respondent's business during the 2008 and 2009 time period and affected both the Company's financial results and stock price. A183–A184 [135:7–137:22]; A935. During this period of transition, DFC's stock price dropped to as low as $5 per share. A183–A184 [136:3–137:10]. Respondent, however, ultimately benefited from the increased regulation in Canada as more aggressive lenders scaled back their operations in response to stricter rules. A453. DFC not only adjusted its business model to comply with the various regulatory changes, but it also gained additional market share as competitors who were unable or unwilling to adapt to the new restrictions left the market. A393; A397; A453. By January 2011, DFC's stock price rose to $20.07 per share. A935. "[T]he stock went up because [the Canadian regulatory transition] was good for the business." A183–A184 [136:22–137:1].

II. The U.K. Imposes New Regulations on Respondent's Business

In the U.K., the Office of Fair Trading (the "OFT") was in charge of regulating the consumer lending industry.[10] Memorandum Opinion ("Op."), attached as Exhibit A to AOB, at 4. In February 2012, the OFT launched an extensive review of 50 of the largest payday lending companies, including DFC's three U.K. payday lending businesses, to assess compliance with the Consumer Credit Act and the OFT's guidance on irresponsible lending. Op. at 4; A99 ¶64; B1190. During its ongoing review of the payday lending industry, the OFT published revised debt collection guidance that required payday lenders to make certain disclosures regarding continuous payment authority ("CPA"), and to refrain from using CPA to collect from consumers who were experiencing financial hardship.[11] Op. at 4–5; A101 ¶72; B1201–B1207.

In response to the OFT's revised debt collection guidance, Respondent began to proactively modify its U.K. payday lending operations throughout 2013 and early 2014 in anticipation of additional forthcoming changes concerning the

[10] In 2014, the OFT was replaced by the Financial Conduct Authority ("FCA") as the governing body regulating DFC's business in the U.K. A106 ¶89.

[11] CPA is a collection procedure in which the customer provides the lender with authorization to automatically debit its bank account in repayment of a loan. Op. at 5; A741–A742 [84:6–88:24]; A535.

number of rollovers[12] that would be permitted. Respondent implemented these changes before any requirement to do so, and knew that this approach would put it at a temporary competitive disadvantage. A394; A283 [533:4–535:12].

Throughout this time period, however, Respondent remained confident that, as a result of these new regulations, many of its competitors would be forced to exit the market, and that it "would be one of the few survivors in the market . . . [with a corresponding] larger market share."[13] A178 [114:2–10]; A747 [106:11–18]; B662 [62:13–63:8]; B779–B781 [41:4–42:13, 44:11–46:19], B794–B795 [98:5–99:15]; A789 [26:2–27:23]; A394; A396; A450; A452; B1182–B1183; A134 ¶205. One of Respondent's key operating assumptions through the close of the Transaction (and beyond) was that it would weather the regulatory storm in the U.K. and come out stronger, just as it had done in Canada. A252 [410:1–411:6]; A267 [470:3–18]; A789 [26:2–28:14]; B779–B781 [41:4–42:13, 44:11–46:19], B794–B795 [98:5–99:15]; B662 [62:13–63:8], B718 [289:4–22]; B977 [69:13–23], B984–B985 [95:8–96:23, 98:11–99:23].

[12] Rollovers allow a borrower to defer repayment of a loan by paying additional interest and fees. Op. at 6; A739 [76:18–22]; A792 [38:11–39:5].

[13] As of March 2014, 19 of the 50 leading lenders in the U.K. had already informed the OFT that they planned to exit the payday loan market as a result of the regulatory changes, and six lenders had already surrendered their lending licenses or had them revoked. A452.

III. DFC's Projections Incorporated All Known Regulatory Changes

DFC's management routinely prepared long-term (typically five-year) financial projections that were used for a variety of routine business purposes, such as debt refinancings, equity issuances, and acquisitions. A109 ¶105; B788 [75:15–76:25]; B666 [81:5–24], B668–B669 [89:9–90:19]. These projections were prepared using the most recent forecast for the business. A109 ¶106; B788 [76]. The corporate finance group would then develop updated forecasts for each business unit by inputting expected drivers for each geographic unit into the forecasting model. A109 ¶106; B788–B789 [76:4–79:22].

Through the close of the Transaction, DFC prepared three sets of five-year projections, each of which was based on the anticipated regulatory changes in the U.K. A109–A110 ¶108; A113–A114 ¶¶123–125; A123 ¶¶160–161. The first set of financial projections was prepared in November 2013 (the "November Projections"), during which time DFC's management team was in active dialogue with the regulatory bodies in the U.K. and continued to implement anticipated changes to the regulatory requirements in that market. A106 ¶89; A108 ¶97; B308; A741–A744 [84:6–90:25, 96:3–18].

In February 2014, DFC revised the November Projections to incorporate the impact of these regulatory changes on its long-term financial forecast (the "February Projections"). A113–A114 ¶¶123–125. That same month, U.K.

regulators issued additional guidance concerning the proposed regulatory changes. A114–A115 ¶¶128–129. Because the final rules were not a surprise to DFC and reflected the Company's prior expectations of what would be required by lenders in the industry, Respondent was able to continue to make adjustments to its business in anticipation of the final rules. A115 ¶129; B612–B613 [92:6–95:24].

In March 2014, following additional correspondence with the governing authorities, Respondent adjusted its operations to incorporate the two-rollover and two-CPA limitations on loans, adjusted its marketing and disclosure practices, implemented additional affordability assessments, incorporated the impact of switching from SPL products to MPL products, and revised its five-year projections again (the "March Projections"). A115 ¶¶130–131; A450–A451; B259–B260; B3320–B337; B367–B380 [30–42]; B699 [212:13–213:18]. **The March Projections incorporated *all* of the regulatory changes that took place before the Transaction Date.** B792 [91:4–92:21]; B676–B677 [121:5–123:7]; A108 ¶97; A749–A750 [117:7–118:20]; B1185–B1188.

While the long-term projections created by management did not typically receive Board approval, the February and March Projections were reviewed and approved by the Board. A113 ¶123; A123 ¶160. The Board specifically concluded that the March Projections reflected the best currently available estimates and judgments of the Company's management. B315; A123 ¶160;

B221–B224. In fact, throughout the entire sales negotiation, including up through the Transaction Date, Respondent viewed the March Projections as being the best and most reliable figures available. A170–A171 [84:20–87:21]; A264 [458:9–21]; A269 [477:4–478:20]; A787–A788 [21:7–22:24]; B806–B807 [149:11–150:20]; B702 [222:3–20]; A123 ¶160; A133 ¶200; B1092 [154:5–155:20]. Houlihan Lokey Capital Inc. ("Houlihan"), the financial advisor retained by Respondent in April 2012 to investigate strategic alternatives, also used the March Projections to prepare the DCF analysis contained in its fairness opinion supporting the Transaction. A155 [22:2–24:13]; A99–A104 ¶¶65–71, 81–84, A106–A111 ¶¶87-88, 91-92, 108-19, A114–A120 ¶¶134-50, A125 ¶171.

IV. DFC Sells Itself at Trough Performance

Respondent embarked on the strategic review process that ultimately led to the sale of the Company at the worst possible time. Despite DFC's belief that it would successfully navigate the regulatory changes and that the business would rebound, the Company sold itself before current management could demonstrate this to the market and while it was in a financial trough. A169 [78:3–79:23]; A178 [114:2–16]; A267 [470:3–471:23]; A789 [26:13–28:25]; A808 [102:9–103:19]; B779–B781 [41:4–42:13, 44:11–46:19]. Throughout 2013 and into 2014, the market overreacted to the temporary downturn in the business and generally took an overly pessimistic and uninformed view of the Company's future prospects.

B1015 [220:6–25]; B1182–B1183. This not only depressed the market value of the Company in that period, but also precluded a thorough and competitive sales process by discouraging potential acquirors of Respondent's business. A791 [36:4–37:16]; [106:7–107:20]; B980–B981 [81:16–83:9]; A111 ¶114; A116 ¶134. J.C. Flowers, a financial sponsor and the only other potential bidder who expressed interest in DFC besides Lone Star, exited the process before submitting a formal bid. A158–A159 [36:8–37:15]; B311; A795 [52:4–22].

After nearly two years of turmoil and regulatory uncertainty, DFC finally obtained clarity on the new regulatory landscape in the U.K. when the FCA issued its final regulations in February 2014 (to be effective on April 1, 2014) and held an in-depth meeting with the Company in March 2014. A802 [78:12–79:12]; A114 ¶128, A115 ¶131. At this point, however, the regulatory uncertainty had driven away all potential bidders (including J.C. Flowers) except for Lone Star. Instead of using this clarity as a means to reevaluate the Company's long-term options, management instead accepted Lone Star's fire-sale offer on the same day the final FCA rules went into effect. A801–A802 [74:22–79:12].

V. Lone Star Manipulated the Sales Process

Respondent's decision to sell the Company at the wrong time and while its stock price was depressed as a result of the regulatory changes in the U.K. presented the perfect opportunity for Lone Star. As a private equity fund, Lone

Star's investment strategy was to maximize investor returns by targeting businesses experiencing a temporary disruption in financial performance and then later disposing of those businesses at a profit after they had recovered.[14] A136 ¶221; B966 [25:4–26:25], B981 [83:10–22].

Given DFC's unusually poor financial performance prior to the Transaction Date, it is easy to understand Respondent's appeal to Lone Star as an investment. A135–A136 ¶¶223–24; B154. Lone Star described DFC as an "opportunity to acquire a best-in-class global platform . . . at trough EBITDA levels." A136 ¶223. Lone Star believed that Respondent's EBITDA had stabilized at an historical low, B979 [76:3–77:22], and described Respondent's EBITDA margins as having "reach[ed] a point not previously seen in its history as a public company." A283–A284 [536:12–537:23]. Lone Star's whole approach was to "opportunistically take advantage" of DFC's unusually poor financial performance prior to and during the sales process, and that is exactly what it did. *Id.*

On February 28, 2014, Lone Star initially offered to acquire Respondent for $11 per share based upon DFC's February Projections. A115 ¶132. Lone Star later wanted exclusivity in the process and, to get it, bargained with the Board to obtain 20 days of exclusivity in exchange for increasing its offer price to $12 per

[14] Lone Star itself describes its target companies with phrases such as "have suffered an economic and/or banking crisis," "dislocation in asset pricing," "financing is constrained," and "balance sheets are under pressure." B1189.

share on March 9th.[15] A117 ¶137. The Board and Houlihan, however, made the fatal mistake of providing Lone Star with exclusivity in exchange for increasing its offer to $12 per share without requiring a binding commitment letter to be signed at that price. A117 ¶¶136–38. This kept the one remaining interested party out of the process and made it extremely unlikely that another bidder would come in with a higher offer, particularly given the rarity of jumped bids (occurring in only 3 percent of transactions involving a private equity buyer). B9; A111 ¶¶117–19, A115–A116 ¶¶132-34, A117 ¶¶136-37, A118 ¶140. Indeed, with exclusivity guaranteed, but no go-shop provision or binding commitment letter required by the Board, Lone Star positioned itself with a tremendous amount of leverage, which it later utilized by dramatically dropping its offer price. A115–A117 ¶¶132, 136–38; A914 ¶111.

On March 27, 2014, Lone Star unilaterally reduced its offer from $12 to $9.50. A287 [551:2–552:17]; A119 ¶147. Four days later, DFC provided Lone Star with the full set of March Projections, which largely mirrored the February Projections, save for some reductions in EBITDA reflected in FY 2014 (and small reductions of a few percentage points in later years). A113 ¶123, A122–A123 ¶¶156, 161; A170 [83:11–84:19]. Lone Star cited the following reasons for

[15] Respondent's brief completely ignores the fact that Lone Star bargained for exclusivity at $12 per share. Indeed, its opening brief does not even mention Lone Star's $12 offer, which was more than 20 percent above the price ultimately paid after Lone Star executed on its "bait and switch." AOB at 13.

reducing its offer: (i) the U.K. regulatory changes; (ii) the supposed threat of increased U.S. regulatory scrutiny;[16] (iii) downward revisions to DFC's projections; (iv) reduced availability of acquisition financing; (v) stock price volatility; and (vi) the weakness of the Canadian dollar. Op. at 11 (citing A116). However, at least three of these reasons – (iv) through (vi) – do not even relate to the fair value of DFC as a going concern, and the U.K. regulatory changes were already known. Indeed, Lone Star did not base its $9.50 offer on any intrinsic valuation or assessment of DFC's long-term value. A285 [541:1–543:18]; B995 [139–140]; A136 ¶226. Lone Star's decision to reduce its bid was solely the result of factors affecting the price it was willing to pay or general market conditions. Because the FY 2014 projections received from DFC reflected lower EBITDA in the near term than those contained in the February Projections, Lone Star became more restricted in the amount of financing that was available to fund the Transaction. A120 ¶148. This reduction in 2014 EBITDA and corresponding reduction in available financing were the driving factors in Lone Star's reduced price, not any valuation analysis contemplating the fair value of the Company. A281 [528:2–21], A286 [548:4–19], A287 [552:1–23]; B977 [68:13–69:12], B1004–B1006 [174:8–175:10, 179:13–182:19]; A136 ¶¶222, 226; B885 [73:5–21]. In fact, according to Houlihan, the changes in cash flow projections from February

[16] There is simply *no* evidence that there would be any significant regulatory changes in DFC's U.S. market, nor did such changes ever transpire.

to March result in only a 9.2 percent reduction in value based on a DCF analysis, from $13.21 per share using the February Projections to $11.99 per share using the March Projections, A868 ¶51, roughly the $12 offer price that got Lone Star its exclusivity.

Nevertheless, Lone Star used this reduction in FY 2014 EBITDA to execute the perfect bait-and-switch and put DFC's Board under a significant amount of pressure to accept its reduced offer price. Lone Star submitted its revised offer while it was still enjoying exclusivity, and the Board was initially only afforded 24 hours to consider an offer reflecting a 20 percent discount to its prior agreement. A118 ¶140; A120 ¶149. Although Lone Star later extended the offer two more business days, A120 ¶149, the Company still was precluded from conducting a market check to vet the reduced offer or from contacting previous potential suitors to seek a higher bid. A121 ¶¶151–54. Nor were any other bidders contacted after the expiration of Lone Star's exclusivity period. Instead, the Board simply accepted the lowball $9.50 price from Lone Star.

ARGUMENT

I. THE TRIAL COURT'S OPINION FINDING THE FAIR VALUE OF DFC AS OF THE TRANSACTION DATE TO BE $10.30 PER SHARE SHOULD BE AFFIRMED

A. QUESTION PRESENTED

Whether the trial court's opinion should be affirmed where (i) the trial court has broad discretion to consider all relevant factors and exercised that discretion by conducting a valuation analysis blending the results of three valuation methodologies to arrive at a fair value award of $10.30 and (ii) the appraisal statute does not provide for bright-line rules deferring automatically to deal price.

B. STANDARD OF REVIEW

Respondent contends that the standard of review is *de novo*. AOB at 19. That is wrong. The issue here is not whether Chancellor Bouchard committed legal error in determining the fair value of DFC, but rather whether he abused his discretion by equally blending three different valuation methods that have been accepted and utilized in other appraisal cases. *See Cede & Co. v. Technicolor, Inc.*, 884 A.2d 26, 35–36 (Del. 2005) (noting that "[t]his Court reviews appraisal valuations pursuant to the abuse of discretion standard, so long as the Court of Chancery has committed no legal error"). Under the abuse of discretion standard, the trial court abuses its discretion only if its factual findings do not have support in the record or its valuation is not the result of an orderly and logical deductive process. *Id.* This Court will only make contradictory findings of fact when the findings below are clearly wrong and the doing of justice requires them to be overturned. *Id.*

To support its argument for *de novo* review, Respondent cites *Paskill Corp. v. Alcoma Corp.*, 747 A.2d 549 (Del. 2000), where the trial court relied upon the "net asset value," which is a theoretical liquidating value and does not reflect the going concern value of a company, as the sole criterion for determining the fair value of the target company. However, unlike the method used in *Paskill,* the three valuation methods relied upon by Chancellor Bouchard in the present case have been accepted and utilized in many other appraisal cases and, importantly, are not proscribed by Section 262. *See, e.g.*, *Laidler v. Hesco Bastion Envtl., Inc.*, 2014 WL 1877536, at *6 (Del. Ch. May 12, 2014) (compiling authorities). Thus, there is no basis for *de novo* review here.

C. MERITS OF ARGUMENT

1. The Court of Chancery Has Broad Discretion To Consider "All Relevant Factors"

The trial court did not abuse its discretion in conducting its valuation analysis and arriving at a fair value award of $10.30 per share. Reargument Order at 2-7; *see* Order and Final Judgment attached as Exhibit C to the AOB. Section 262(h) of the appraisal statute specifically provides that the Court of Chancery "shall determine the fair value of the shares" and, in so doing, "the Court shall take into account all relevant factors." 8 *Del. C.* § 262(h). This Court has interpreted this language as giving the Court of Chancery broad discretion in assessing fair value. *See M.G. Bancorporation v. Le Beau*, 737 A.2d 513, 525-26 (Del. 1999); *Golden Telecom, Inc.*, 11 A.3d 214.

"The [c]ourt may evaluate the valuation opinions submitted by the parties, select the most representative analysis, and then make appropriate adjustments to the resulting valuation." *In re Appraisal of Dell Inc.*, 2016 WL 3186538, at 20 n.3 (Del. Ch. May 31, 2016) (quoting *Appraisal Rights in Mergers & Consolidations*, 38-5th C.P.S. §§ IV(H)(3), at A-31). The trial court also may "make its own independent valuation calculation by . . . adapting or blending the factual assumptions of the parties' experts." *Id.* at 20. (quoting *M.G. Bancorporation*, 737 A.2d at 524). It is also "entirely proper for the [Court of Chancery] to adopt any one expert's model, methodology, and mathematical calculations, *in toto*, if that valuation is supported by credible evidence and withstands a critical judicial analysis on the record." *Id.* (quoting *M.G. Bancorporation*, 737 A.2d at 526). "When . . . none of the parties establishes a valuation that is persuasive, the Court must make a determination based on its own analysis." *Id.* (quoting *Cooper v. Pabst Brewing Co.*, 1993 WL 208763 *8 (Del. Ch. Jun. 8, 1993); *accord Del. Open MRI Radiology Assocs. P.A. v. Kessler*, 898 A.2d 290, 310–11 (Del. Ch. 2006) (Strine, V.C.) ("I cannot shirk my duty to arrive at my own independent determination of value, regardless of whether the competing experts have provided widely divergent estimates of value, while supposedly using the same well-established principles of corporate finance.”). Here, Chancellor Bouchard appropriately applied the discretion provided by the appraisal statute in determining the fair value of DFC on June 13, 2014 was $10.30 per share.

2. The Appraisal Statute Does Not Permit Bright-Line Rules

Respondent argues that the Court of Chancery erred by not deferring to deal price, and claims that a bright-line rule should be created to defer to deal price when there was “a robust, competitive bidding process” resulting “in an arm’s-length sale to a disinterested buyer.” AOB at 19. Even if such a process existed here – which it does not – the appraisal statute by its terms does not permit a one-size-fits-all approach to conducting valuations.

(a) The Unambiguous Language of the Statute Has Not Changed

As this Court has made plain, “[w]hen interpreting a statute, we attempt to determine and give effect to the General Assembly’s intent. We give unambiguous statutory language its plain meaning ‘unless the result is so absurd that it cannot be reasonably attributed to the legislature.’” *Kelty v. State Farm Mutual Auto. Ins. Co.*, 73 A.3d 926, 929 (Del. 2013); *Clark v. State*, 65 A.3d 571, 577-78 (Del. 2013) (same); *In re Adoption of Swanson*, 623 A.2d 1095, 1096-97 (Del. 1993) (“If the statute as a whole is unambiguous and there is no reasonable doubt as to the meaning of the words used, the court's role is limited to the application of the literal meaning of the words."). The language of Section 262(h) has already been determined to be unambiguous. *Golden Telecom*, 11 A.3d at 218-19. Thus, if there is to be such a bright-line, one-size-fits-all rule, it must come from the General Assembly. *Sivakoff v. Nationwide Mut. Ins. Co.*, 21 A.3d 597, 2011 WL 1877610, at *3 (Del. May 16, 2011) (TABLE) ("[W]e . . . have explained that we will not distort the General Assembly's intent when unambiguous statutory language 'clearly mandate[s] a result.'").

(b) This Court Has Previously Declined Respondent's Proposed Bright-Line Rule

While denying any effort to do so, Respondent asks this Court to overrule *Golden Telecom* by imposing a presumption in favor of merger price as evidence of fair value. In *Golden Telecom*, this Court declined to take up that invitation, stating:

> Requiring the Court of Chancery to defer—conclusively or presumptively—to the merger price, even in the face of a pristine, unchallenged transactional process, would contravene the unambiguous language of the statute and the reasoned holdings of our precedent. . . . [W]hile it is difficult for the Chancellor and Vice Chancellors to assess wildly divergent expert opinions regarding value, ***inflexible rules governing appraisal provide little additional benefit in determining "fair value"*** because of the already high costs of appraisal actions. Appraisal is, by design, a flexible process. Therefore, we reject Golden's contention that the Vice Chancellor erred by insufficiently deferring to the merger price, and ***we reject its call to establish a rule requiring the Court of Chancery to defer to the merger price in any appraisal proceeding.***

11 A.3d at 218 (emphasis added).

Since *Golden Telecom*, the Court of Chancery has considered the deal price as a relevant factor where appropriate when determining fair value, but it has never deferred automatically or presumptively to the deal price. Such an inflexible rule would effectively rewrite the appraisal statute to require appraisal petitioners to establish some aspect of self-interest in the sale process, essentially requiring petitioners to prove a breach of fiduciary duty claim to prevail. There is no such requirement in an appraisal action; the only relevant determination is fair value.[17] Thus, while a sale process might pass muster for purposes of a breach of fiduciary claim, it could still constitute a sub-optimal process for relying on the deal price as an adequate indicator of fair value in an appraisal. *Lender Processing*, 2016 WL 7324170, at **15-16.

[17] The suggestion that a chilling effect on deals will result from allowing the Court of Chancery to award fair value in an appraisal case is complete malarkey, as this case illustrates. Here, the trial court awarded Petitioners $10.30 per share, or an 8.4 percent increase on the deal price. The petitioned shares represent less than 12 percent of the total shares outstanding, so the actual effect on the overall deal was only an additional one percent of the total merger consideration. Raising the acquisition cost to an acquiror by one percent is not going to materially change the acquiror's position, nor does it increase the likelihood that a deal will fall through. Indeed, any deal that is make-or-break over a one percent change in price is probably not a deal that should be done in the first place. The magnitude of appraisals on the total consideration in a transaction is generally less than the typical three percent breakup fee, which has been determined not to affect the economics of a deal.

(c) Respondent Never Presented Evidence On Deal Price

Respondent's assertion of deal price now is a flip-flop from all of the arguments and evidence that it presented to the Court of Chancery at trial. Respondent's expert never relied on deal price in his valuation analysis, nor did any of the evidence presented during the three-day trial before the Chancellor advance a position that the deal price was an indicator of fair value here. Instead, Respondent's expert presented a valuation according 50 percent weight to a DCF analysis and 50 percent weight to a comparable company analysis. A971. It is questionable whether this "deferral-to-deal-price" issue is appropriately preserved for appeal.

(d) Contemporary Empirical Studies Show That Appraisal Functions As Intended By The General Assembly

A self-selected group of nine law professors supports Respondent's request for absolute deference to deal price when that price was reached "as a result of an arms-length auction process."[18] Brief of Law and Corporate Finance Professors as *Amici Curiae* in Support of Reversal ("*Amici* Br.") at Argument, I.; AOB at 19–38. They base their argument on the unsupported claim that appraisal "imposes the

[18] However, the *amicus* brief offers no argument as to why this Court should believe that there was an arm's-length auction process, and in fact acknowledges that when the bidding took place there was only one bidder. *Amici* Br. at 6 ("by March 2014 only Lone Star was left").

prospect of costly and unpredictable appraisal litigation on all transactions, which distorts market behavior." *Amici* Br. at 2. These accusations of the evils of appraisal are made without citation or any empirical evidence. *Id.* at 17–19. None of these law professors have undertaken any recent study of appraisals and simply espouse the dogma of Private Equity.[19]

Fortunately, there have been three empirical studies on appraisal by professors who actually have expertise in appraisals and base their work in facts. Those studies strongly disagree with Respondent's efforts to defer to deal price. *See* Charles Korsmo & Minor Myers, *Reforming Modern Appraisal Litigation*, BROOKLYN LAW SCHOOL, Legal Studies Research Paper No. 431 (Jan. 6, 2016); Choi & Talley, *supra* note 4 (arguing that a general deference to merger price depresses both acquisition prices and shareholder welfare, and may only be warranted in certain narrow situations); Jonathan Kalodimos & Clark Lundberg, *Shareholder Rights in Mergers and Acquisitions: Are Appraisal Rights Being*

[19] None of them are economists: most focus on areas other than Delaware corporate law, and of the four who claim to have written about Delaware's appraisal statute, their most recent peer-reviewed work is eight years old. *See* Motion for Leave to File *Amici* Br. at ¶4 (Law Professors' biographies); *Amicus* Br. at iv–v (the peer-reviewed journal articles written by three of the Law Professors—Prof. Carney, Shephard, and Sharfman); Opp. to *Amici* Br. at 3–4 n.1; Reply in Support of *Amici* Br. at 4 n.1 (citing articles written, at least in part by Prof. Kanda, that were published in 2009 and 1985). This lack of expertise might explain why their conclusions are completely unsupported and literally have no citations supporting their most outrageous and aggressive claims. *See* Opp. to *Amici* Br. at 6–7.

Abused?, Finance Research Letters, (Jan. 2, 2017) (finding that appraisal rights are generally being used as a remedy for contracting failures in the merger negotiation process and not for abusive purposes). These studies show that appraisal has a positive effect on *all* transactions. *See* Charles Korsmo & Minor Myers, *Appraisal Arbitrage and the Future of Public Company M&A*, 92 WASH. U. L. REV. 1551, 1598–1604 (2015) (arguing that appraisal benefits both minority and controlling shareholders, and that the practice serves as an effective market check on potentially abusive sales processes); Choi & Talley, *supra* note 4 at 4 ("Indeed, the outside option of seeking appraisal after a merger can functionally alter shareholders' receptivity to an announced deal, effectively committing them to a 'reserve price' of sorts for the sale, at an amount tied to the anticipated appraisal remedy. Under plausible conditions, this *de facto* reserve price can protect shareholders' interests more ably than either a shareholder approval requirement, or reliance on managerial incentives to design a profit—and then commit to—maximizing auction. Sophisticated bidders, moreover, anticipate this effect, and may well modify their bids in response, adjusting them upward to meet (or get close to) the appraisal reserve price, secure shareholder approval, and preempt widespread appraisal litigation.").

In a January 2, 2017 paper by Jonathan Kalodimos and Clark Lundberg – based on an *empirical study* using *actual data* – the authors found that appraisal rights are being deployed appropriately in instances where a target firm is sold below fundamental (*i.e.*, fair) value.[20] The authors of this study gathered all appraisal petitions filed with the Court of Chancery between January 2003 and May 2015, a total of 275 petitions filed on behalf of 622 beneficial stockholders, and excluded transactions with targets having a market capitalization of less than $10 million. A review of the remaining 92 petitioned transactions reflected that the deals subject to appraisal rights during this time period exhibited several characteristics leading to the conclusion that appraisal rights were not being abused, including low premium transaction prices and abnormally high acquiror returns. *Id.* at 2-8. The study concludes that:

> appraisal rights are generally being used as a remedy for contracting failures in the merger negotiation process. Deals petitioned for appraisal tend to have substantially lower premia than a matched sample. Moreover, the acquiring firms of petitioned targets have substantially higher cumulative abnormal returns around the merger announcement relative to a matched sample. We interpret these findings as indicative of inefficient contracting from the perspective of target shareholders. These failures appear to be driven, at least in part, by inexperience and busyness of target firm leadership.

Id. at 9.

[20] Kalodimos & Lundberg, *Shareholder Rights in Mergers and Acquisitions: Are Appraisal Rights Being Abused?*, Jan. 2, 2017.

II. THE TRIAL COURT PROPERLY EXERCISED ITS DISCRETION IN ADOPTING A PGR OF 4 PERCENT IN ITS DCF ANALYSIS

A. QUESTION PRESENTED

Whether the trial court's opinion should be affirmed where the trial court exercised its discretion to adopt a PGR of 4 percent in its DCF analysis, which was supported by the factual record and was within the generally-accepted range.

B. STANDARD OF REVIEW

This Court's standard of review is abuse of discretion. *See Technicolor, Inc.*, 884 A.2d at 35–36. *See also supra* at Argument, I.B.

C. MERITS OF ARGUMENT

Respondent contends that Chancellor Bouchard abused his discretion by adjusting the PGR in his DCF model on Reargument from 3.1 percent to 4 percent, arguing that there was no evidence to support a PGR of 4 percent and that Chancellor Bouchard arbitrarily selected that number so that he could leave his "overall 'fair value' determination essentially unchanged" from his Opinion. AOB at 41–44. Neither the facts nor basic economic principles support this argument.

In his Opinion – and in proper exercise of his discretion – Chancellor Bouchard selected various inputs from across the two experts' DCF valuations and compiled them to create his own independent DCF analysis. *See generally* Op. at 17–55; *see also M.G. Bancorporation*, 737 A.2d at 524 (noting that the Court of Chancery may "make its own independent valuation calculation by . . . adapting or blending the factual assumptions of the parties' experts"). The trial court adopted Kevin Dages' ("Dages") 3.1 percent PGR from his two-stage DCF model, and calculated DFC's weighted average cost of capital ("WACC") to be 10.72 percent, a result "located roughly in the middle of Dages' and Beaulne's respective calculations of 9.5% and 12.4%[.]" Op. at 44. In doing so, however, Chancellor Bouchard failed to take into account the required correlation between a company's growth rate, discount rate, and level of working capital investment necessary to sustain growth into perpetuity.

When a specific PGR is selected for use in a DCF analysis, the underlying projections and assumptions must support that growth rate, including the discount rate and the working capital investment necessary to sustain that growth. A1352 ¶4. Here, the economic relationship between these assumptions requires a PGR that is higher than 3.1 percent using the March Projections and the 10.72 percent discount rate adopted by the trial court. A1352–A1353 ¶5; A1360 (establishing that the March Projections support an average sustainable PGR of 3.9 percent and a median sustainable growth rate of 4.2 percent). After re-examining its decision, the trial court acknowledged that "it [had] failed to appreciate the extent to which DFC's projected revenue and working capital needs have a codependent relationship, *i.e.*, a high-level requirement for working capital, as reflected in DFC's March Projections, necessarily corresponds with a high projected growth rate." Reargument Order at ¶5. Thus, to rectify this methodological error, the trial court appropriately used its discretion to adopt the higher corresponding PGR of 4 percent in its revised DCF model. Reargument Order at ¶7; A1355 ¶9.

Moreover, to further justify his decision to adjust the PGR, Chancellor Bouchard made clear that he had originally based his selection of a 3.1 percent growth rate on the theory that a company's PGR should not exceed the risk-free rate, which the parties had agreed was 3.14 percent. Reargument Order at ¶6. This proposition, however, only applies to companies that have reached a steady state. *Id.* (citing Aswath Damodaran, *Investment Valuation: Tools and Techniques for Determining the Value of Any Asset* 305 (3d ed. 2012)). The March Projections assumed that DFC would achieve fast-paced growth throughout the projection period and, thus, implied a need for a PGR higher than the risk-free rate, as the Chancellor acknowledged. Reargument Order at ¶6.[21]

The trial court's adjusted PGR of 4 percent is also well within the traditionally acceptable range of inflation and GDP nominal growth. Respondent's own brief suggests that this range is between 2 percent and 4.4 percent for DFC. AOB at 40. While 4 percent is towards the top of that range, it is still appropriate

[21] The fact that DFC was still in a high growth state at the end of the explicit projection period was exactly why Petitioners' expert used a 3-stage DCF model in his analysis. Accounting for projections that do not reflect steady state can be done by *either* extending the projection period out an additional number of years *or* by increasing the terminal growth rate. Both methods are acceptable under economic principles. A905–A906 ¶¶97–98; A901 n.198.

(and within the range) because DFC was coming out of trough financial performance at the end of the forecast period and was not yet at steady state.

In addition, the trial court's 4 percent adjusted PGR is lower than the implied PGR of DFC's expert Daniel Beaulne ("Beaulne"). Beaulne used the convergence model in his two-stage DCF analysis, which calculates the terminal value by dividing net operating profit after taxes by the discount rate. A307 [627:11–629:22]; A334 [736:2–23]. Converting Beaulne's terminal value into a corresponding PGR using the Gordon Growth Model would yield a growth rate of 4.5 percent – a rate even higher than the one adopted by Chancellor Bouchard.[22] A351 [804:2–8]. This result further supports the trial court's discretion in applying a 4 percent PGR in its DCF analysis.

[22] While Respondent contests that Beaulne's model implies a PGR of 4.5 percent, AOB at 41–42 n.2, the convergence model used by DFC's expert can and does imply such a growth rate when converted to the Gordon Growth Model. A209–A210 [240:13–242:20]; A1139–A1141 ¶¶46–47, A1144–A1146 ¶¶53–54.

III. IN THE ALTERNATIVE, THE TRIAL COURT ABUSED ITS DISCRETION BY ACCORDING THE COMPARABLE COMPANY ANALYSIS ANY WEIGHT IN DETERMINING FAIR VALUE

A. QUESTION PRESENTED

Whether the trial court abused its discretion by according the comparable company analysis any weight in its fair value analysis where DFC was exhibiting trough financial performance, there were no companies comparable to DFC, and the results of the comparable company analysis yielded wildly divergent outputs. This issue was preserved for appeal. *See* B1278–B1281; B1345–B1349.

B. STANDARD OF REVIEW

This Court's standard of review is abuse of discretion. *See Technicolor, Inc.*, 884 A.2d at 35–36. *See also supra* at Argument, I.B.

C. MERITS OF ARGUMENT

1. The Trial Court Should Not Have Accorded the Comparable Company Analysis Any Weight

Under the facts of this case, the trial court abused its discretion by according the comparable company analysis one-third total weight in the overall fair value analysis of DFC. "A comparable or market-based approach endeavors to draw inferences about a company's future expected cash flows from the market's expectations about comparable companies." *Merion Capital, L.P. v. 3M Cogent, Inc.*, 2013 WL 3793896, at *5 (Del. Ch. July 8, 2013), *judgment entered sub nom.*, 2013 WL 3833763 (July 23, 2013) (Trial Order). Because it is market-based, the comparable company method does not actually assess a specific company's intrinsic value,[23] and it does not take into account any growth in free cash flow expected after more than two years. A683–A684 [216:4–218:25].

While a comparable company analysis can be a useful valuation tool under the appropriate circumstances, it was completely unreliable in this particular case. First, the comparable company analysis utilized by the trial court was performed on DFC's FY 2014 and FY 2015 EBITDA projections – trough years in the Company's financial performance. Op. 56; A1004; A909 ¶101; A1141-A1143 ¶¶49–50; A206 [228:3–10]. Calculating a multiple using those figures would result in a dramatically understated view of DFC's value, particularly when compared against other companies not exhibiting such trough performance. Performing a market-based analysis on a company exhibiting trough performance is not appropriate. A909 ¶101; James R. Hitchner, *Financial Valuation: Applications and Models*, 278 (3d ed. 2011); *Cf. Glassman v. Unocal Exploration Corp.*, 777 A.2d 242, 248 (Del. 2001) (acknowledging that an appraisal proceeding can and should address the problem of opportunistic timing, including when there is a trough in a company's performance).

Second, the comparable company analysis yielded wildly divergent results. Beaulne's analysis, which was largely adopted by the Court of Chancery, produced

[23] B28; B44; B17; *3M Cogent*, 2013 WL 3793896, at *14.

values ranging from *negative* $0.39 to positive $18.20 per share. A206 [225:5–226:24], A207 [231]; A1157. A valuation range this large instantly calls the reliability and relevance of the underlying methodology into question. A683–A684 [216–218]; A909–A910 ¶102.

Finally, reliance on a comparable company analysis here is inappropriate because none of the selected peers were comparable to DFC. "[T]he utility of a market-based method depends on actually having companies that are sufficiently comparable that their trading multiples provide a relevant insight into the subject company's own growth prospects." *3M Cogent*, 2013 WL 3793896, at *5 (citing *In re Orchard Enters., Inc.*, 2012 WL 2923305, at *9 (Del. Ch. July 18, 2012)). The Court of Chancery has repeatedly declined to attribute weight to comparable company analyses when these were predicated on companies dissimilar to the one being valued, either in size or in substance. For example, in *3M Cogent*, the court completely rejected a comparable company analysis that, amongst other flaws, included several companies that were significantly smaller than the company that was the subject of the appraisal, and several that did not offer the same product and were not considered competitors to the company being appraised. 2013 WL 3793896, at **6-7. Similarly, in *In re PNB Holding Co. Stockholders Litigation*, the court rejected a comparable companies analysis where the "comparable publicly-traded companies all were significantly larger" than the company under appraisal. 2006 WL 2403999, at *25 n.125 (Del Ch. Aug. 18, 2006). *See also Gilbert v. MPM Enters., Inc.*, 709 A.2d 663, 672 (Del. Ch. 1997) (stating that comparable companies whose "median asset value . . . was nearly three times that of [the appraised company]" had "unreasonably skewed the results of this analysis"), *aff'd*, 731 A.2d 790 (Del. 1999); *Rosenblatt v. Getty Oil Co.*, 1983 WL 8936, at *26 (Del. Ch. Sept. 19, 1983) (rejecting analysis that used "smaller oil and gas producing companies as opposed to a major integrated company such as [the appraised company]"), *aff'd*, 493 A.2d 929 (Del. 1985); *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 477 (Del. Ch. 2011); *In re Sunbelt Bev. Corp. S'holder Litig.*, 2010 WL 26539, at *9 (Del. Ch. Jan. 5, 2010).

In this case, both the nature and the size of the so-called "comparable" companies used render them unfit to serve as such. Compared to DFC, the selected companies sold different products, A908–A909 ¶100, operated in different and far fewer geographical areas, A684 [220–221], and had a much smaller exposure to the U.K.'s regulatory overhaul. B1125 [288:6–25]. Each of the chosen companies was also at least 40 percent larger than Respondent, with one company being as much as 6.6 times the size of DFC.[24]

[24] Respondent's market capitalization was $346 million, while the comparables ranged from 40 percent larger (Cash Converters-$459 million) to 660 percent larger (International Personal Finance-$2.3 billion) and the average market capitalization of the Beaulne comparables is $1.15 billion or 333 percent higher than DFC. A952.

The deep flaws and wild outputs serving as the basis for one third of the trial court's valuation seriously undermines the credibility of this methodology under the facts and circumstances of this case. The comparable company analysis should have been accorded no weight in determining DFC's fair value.

2. The Trial Court's DCF Analysis Should Have Been Given Substantial, If Not Exclusive, Weight in Determining the Fair Falue of DFC

While the Court of Chancery is permitted to consider "all relevant factors" in conducting its fair value analysis, the DCF analysis is considered the gold standard in assessing the fair value of a corporation as a going concern, and "is the approach that merits the greatest confidence within the financial community." *In re Appraisal of Dell Inc.*, 2016 WL 3186538, at *45 (quoting *Owen v. Cannon*, 2015 WL 3819204, at *16 (Del. Ch. June 17, 2015) (internal punctuation omitted)).[25] A DCF analysis is the preferred method for valuing a company as

[25] *See also* Donald J. Wolfe, Jr. & Michael A. Pittenger, *Corporate and Commercial Practice in the Delaware Court of Chancery*, § 8-10[d], 8-161 (Release No. 5, 2004) ("Since Weinberger, nearly all appraisals have utilized some type of DCF methodology[.]"); Andrew Metrick & Ayako Yasuda, *Venture Capital & the Finance of Innovation*, § 11.2 at 198 (2d ed., John Wiley & Sons, Inc.); Aswath Damodaran, *Damodaran on Valuation*, at 10 (2d ed. 2006) (explaining that DCF "comes with the best theoretical credentials"); Tim Koller, *et al., Valuation: Measuring and Managing the Value of Companies,* § 16 at 351 (6th ed. 2015) ("Of the available valuation tools, discounted cash flow continues to deliver the best results."); Krishna Palepu, *et al.*, *Business Analysis & Valuation - Using Financial Statements*," § 6–2 (1996); Robert W. Holthausen and Mark E. Zmijewski, *Corporate Valuation: Theory, Practice & Evidence*, § 1 at 13 (2014) ("The discounted cash flow . . . model is one of the most commonly used valuation

compared to other valuation methods because it uses the specific attributes of the actual company being valued, using cash flow forecasts prepared by those who know the business best, as opposed to relying on relative metrics that are based on other companies or the market generally. *Andaloro v. PFPC Worldwide, Inc.*, 2005 WL 2045640, at *9 (Del. Ch. Aug. 19, 2005) ("The DCF model of valuation is a standard one that gives life to the finance principle that firms should be valued based on the expected value of their future cash flows, discounted to present value in a manner that accounts for risk."); *Doft & Co. v. Travelocity.com Inc.*, 2004 WL 1152338, at *5 (Del. Ch. May 20, 2004) ("Delaware law clearly prefers valuations based on contemporaneously prepared management projections because management ordinarily has the best first-hand knowledge of a company's operations."). Because it is the gold standard in determining the intrinsic value of a business, the Court of Chancery "prefer[s] to give [DCF analyses] great, and sometimes even exclusive, weight when it [is] used responsibly." *Gesoff v. IIC Indus., Inc.*, 902 A.2d 1130, 1155 n.138 (Del. Ch. 2006); *see also In re Appraisal of Dell Inc.*, 2016 WL 3186538, at *51 (attributing 100 percent weight to DCF

methods. In a 1998 survey of large corporations and financial advisors, Bruner et al. . . . report[ed] that 96% of corporations use the DCF valuation method to evaluate investment opportunities and 100% of financial advisors do so."); Joshua Rosenbaum and Joshua Pearl, *Investment Banking: Valuation, Leveraged Buyouts, and Mergers & Acquisitions*, at 109 (2009) ("Discounted cash flow analysis . . . is a fundamental valuation methodology broadly used by investment bankers, corporate officers, university professors, investors . . .").

model due to unreliability of market pricing stemming from imperfect sale process).

Here, the trial court constructed a DCF model that estimated the fair value of DFC as of the Transaction Date to be $13.07 per share.[26] Op. at 54–55. The factual record supports the court's reliance on this methodology and the inputs chosen to construct its model.

First, the March Projections were prepared by a competent management team who knew its business well and had significant experience preparing long-term projections. A169 [77], A171 [86, 88], A178 [113]; A108–A109 ¶¶100–07. DFC prepared long-term financial projections on an annual basis for at least 10 years before the Transaction. A262 [451–52]; A109 ¶105. The March Projections were prepared using a rigorous reporting process compiled from the various reporting units, which were then reviewed by management before consolidation into the final projections presented to the Board for approval. A264–A265 [460–63]; A109 ¶106. The March Projections were also approved by the Board, A109 ¶107, A123 ¶160, and were relied upon by Houlihan in preparing its fairness opinion for the deal. A125 ¶171. At no point prior to the Transaction did the

[26] Not only did the trial court rely on a DCF analysis in assessing the fair value of DFC, but both experts also agreed that using a DCF analysis was an appropriate valuation measure, with Petitioners' expert attributing 100 percent weight to the DCF and Respondent's expert according the result of his DCF analysis 50 percent weight. A843 ¶7; A971.

Board or management express any reservation, concern or warning about the reasonableness of the March Projections, nor did Houlihan or Lone Star request that updated projections be prepared. A163 [55], A169 [77], A171 [86], A172–A173 [91–93], A178 [113–14]; A132–A133 ¶¶198, 200, 202; B1008 [191:3–16], B1020 [239:4–17]. Indeed, throughout the entire process leading up to the Transaction, and even after the Transaction Date, Respondent viewed the March Projections as being the best and most reliable estimate of DFC's future performance. A170–A171 [84–87]; A264 [458], A269 [477–78]; A787–A788 [21–22]; B806–B807 [149:11–150:20]; B702 [222:3–20]; A123 ¶160, A133 ¶200; B1092 [154:5–155:20].

Second, the fact that the Company's projections were revised in February and March of 2014 (after their initial preparation in November 2013) only emphasizes that these were the Company's best estimates of DFC's future performance. Respondent was continuously updating the projections to reflect the evolving rules from the U.K. regulators and the expected impact of those changes on DFC's business. A169 [77–78]; A266–A267 [467–69]. The March Projections encompassed all of the regulatory changes known to the Company prior to the Transaction Date and even incorporated Respondent's anticipated launch of the MPL product line. A122–A123 ¶¶158-59; A266–A268 [465–66, 469, 473]; A746 [102–103].

In its brief, Respondent spends a considerable amount of effort discussing all of the regulatory changes happening in the U.K. in an attempt to discredit the March Projections. AOB at 8–10. Yet, *all* of this information was *known* to DFC when the projections were created; indeed, DFC had been preparing for these changes for at least several months. A451; A741–A744 [82–94]; A114–A115 ¶¶128, 130–131; Op. at 61. If anything, this shows that at the time that the March Projections were prepared, all of the regulatory changes were taken into account and factored into the Company's long-term forecasts. Moreover, the trial court found that these regulatory changes could be a golden opportunity for Respondent because DFC was considered to be one of the firms that would be able to excel under these new conditions. Op. at 60–61.

Third, the fact that Lone Star's own independent projections reflected even ***higher*** numbers than the March Projections underscores the reliability of the March Projections, as well as Lone Star's belief in the long-term profitability of the Company.[27] A270 [482–483]; A287 [550]; A128–A129 ¶¶184–85. These higher projections were presented to the ratings agencies to secure ratings on the debt and to the private lenders financing the deal. No one questioned the

[27] The Lone Star projections contained a number of assumptions not contained in the March Projections, but all of these assumptions except for $4 million in public company costs were attainable by DFC as a going concern. A129 ¶186; B982–B983 [89:7–92:24], B988 [112:5–18], B998–B1000 [153:5–154:17, 158:10–159:25].

reasonableness of the expectations contained in those projections prior to the Transaction Date. B1007–B1008 [188:8–191:16]; A128 ¶¶181–82, A132–A133 ¶¶198, 202, A135 ¶219.

In summary, the trial court's DCF analysis is the most reliable indicator of DFC's fair value as a going concern, and should be given substantial, if not exclusive weight.[28]

[28] While Petitioners do not believe the deal price was an appropriate factor to consider under the facts of this case, to the extent the trial court wanted to take the deal price into account it should have given the DCF analysis greater weight. If the trial court had considered deal price and the DCF with equal weighting, the fair value would have been $11.29 per share. At a 75/25 weighting, it would be $12.18 per share.

CONCLUSION

For the foregoing reasons, the Court should either affirm the trial court's fair value award of $10.30 per share or, in the alternative, either rely exclusively on the trial court's discounted cash flow analysis yielding a fair value of $13.07 or some blend of the deal price and the DCF analysis, with the DCF being accorded substantially more weight than the deal price.

Dated: January 27, 2017

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I, Kimberly A. Evans, hereby certify that on January 27, 2017, I caused a copy of *Appellees/Cross-Appellants' Answering Brief and Opening Brief on Cross-Appeal* to be filed and served to all counsel below via File and Serve*Xpress*:

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