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

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| SOURCEHOV HOLDINGS, INC.,<br><br>Respondent Below,<br>Appellant,<br><br>vs.<br><br>MANICHAEAN CAPITAL, LLC, CHARLES CASCARILLA, EMIL KHAN WOODS, LGC FOUNDATION, INC. and IMAGO DEI FOUNDATION INC.,<br><br>Petitioners Below,<br>Appellees. | No. 215, 2020<br><br>Court Below: Court of Chancery of the State of Delaware, C.A. No. 2017-0673-JRS |

**APPELLANT SOURCEHOV HOLDINGS, INC.'S**
**CORRECTED REPLY BRIEF**

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Dated: October 19, 2020

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| AB | Petitioners-Below, Appellees' Answering Brief, filed September 25, 2020 |
| *Amici* | *Amici Curiae* Professors Emeriti Michael Bradley, Bradford Cornell, and Donald J. Puglisi |
| AmiciB | Brief of Corporate Finance Professors As *Amici Curiae* In Support of Appellant And Remand, filed September 2, 2020 |
| Appellees | Manichaean Capital, LLC, Charles Cascarilla, Emil Khan Woods, LGC Foundation, Inc., and Imago Dei Foundation, Inc. |
| APV | Adjusted Present Value |
| AR | Cites to Appendix in Support of Appellant's Reply Brief, filed October 13, 2020 |
| B | Cites to Appendix to Appellees' Answer Brief, filed September 25, 2020 |
| Bloomberg | Bloomberg L.P. |
| Business Combination | Merger of SourceHOV, Novitex, and Quinpario |
| CAGR | Cumulative Annual Growth Rate |
| CAPM | Capital Asset Pricing Model |
| Mr. Chadha | HGM's Chief Executive Officer and Chief Investment Officer and Director of SourceHOV |
| DCF | Discounted Cash Flow |
| E&Y | Ernst & Young Global Limited |
| Exela | Exela Technologies, Inc. |

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|---|---|
| First Lien | First Lien Credit Agreement dated as of October 31, 2014 |
| GPTC | Guideline Publicly Traded Companies |
| Mr. Jonovic | Managing Director, HGM |
| KPMG | KPMG, LLP |
| Leverage Ratio | A measurement of SourceHOV's debt to equity ratio where the numerator represents SourceHOV's total net debt and the denominator is a measure of EBITDA |
| LOI | Letter of Intent |
| Mr. Meinhart | Mr. Timothy Meinhart, Petitioners' expert |
| Novitex | Novitex Holdings, Inc. |
| OB | Appellant SourceHOV Holdings, Inc.'s Opening Brief, filed August 26, 2020 |
| Opinion or Op. | Memorandum Opinion issued January 30, 2020 |
| Order | Final Order and Judgment, dated March 26, 2020 |
| PIPE | Private Investment in Public Equity |
| Professor Jarrell | Professor Gregg Jarrell, Respondent's expert |
| Proxy | Definitive Proxy Statement for Business Combination, Schedule 14A, filed with SEC on June 26, 2017 |
| Quinpario | Quinpario Acquisition Corp. 2 |
| Mr. Reynolds | Director and former Chief Financial Officer of SourceHOV and HGM Partner |
| Rothschild | Rothschild, Inc. |
| Second Lien | Second Lien Credit Agreement dated as of October 31, 2014 |
| SourceHOV | Respondent SourceHOV Holdings, Inc. |

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|---|---|
| Valuation Date | July 12, 2017 |
| Mr. Verma | Senior Vice President, Finance at Exela |
| WACC | Weighted Average Cost of Capital |

## **INTRODUCTION**

Appellees nowhere dispute the extensive record establishing SourceHOV's operative reality on the Valuation Date as a highly-levered company drowning in expensive debt. Nor do Appellees dispute that the Opinion repeatedly acknowledged this precarious operative reality. Yet, the Opinion's analysis of fair value adopted Mr. Meinhart's valuation, which was entirely untethered to that reality.

Appellees primarily respond by resorting to the more deferential "abuse of discretion" standard. But the Opinion's failure to consider SourceHOV's operative reality in its fair value calculation was *legal* error. Even under Appellees' proffered standard, the Opinion's adoption of Mr. Meinhart's analysis, particularly with respect to cost of debt, equity beta, and projections, finds no support in the record.

The Opinion also committed legal error in refusing to consider financial information from the closed second quarter of 2017 that undisputedly existed, and thus was "knowable," on the Valuation Date. That consolidated financial statements were not "available" is irrelevant.

Finally, Appellees continue to spin a backdating tale that is refuted by the record evidence they either ignore or mischaracterize, and they proffer no explanation for how it is relevant to the Opinion's fair value calculation.

## UNDISPUTED FINDINGS BELOW AND TRIAL RECORD

Appellees nowhere dispute the extensive record and findings regarding SourceHOV's precarious operative reality as of the Valuation Date:

- SourceHOV had taken on over $1B in debt to pursue a "[s]trategy of [g]rowth through [a]cquisitions[,]" AB.7; that debt required SourceHOV to maintain defined Leverage Ratios, OB.6; Op.8-9.

- Those covenants had bi-annual step-downs; failure to comply would result in default and, absent cure, permitted demand for immediate repayment. OB.6-7; Op.9-10.

- Concerned with SourceHOV's debt obligations, ratings agencies gave SourceHOV and its bonds low credit ratings and downgraded them three times. OB.7; Op.15-16.

- SourceHOV's revenue stagnation from 2015-2016 and the step-downs posed "particular challenges"; "liquidity pressure" from nine-figure interest payments was "compound[ed]" by increased amortization payments. OB.7-8; Op.13, 15.

- SourceHOV missed seven of eight sets of projections since 2013. OB.8, 35; Op.24. Appellees quote two SourceHOV presentations claiming a "Track Record of Meeting Targets." AB.9, 40. Those were from 2013 and 2014, and discussed 2011-2013 projections. B789; B942.

- Since 2014, SourceHOV's organic growth was negative, averaging -2.4% per year. OB.8, 36. Appellees note CAGR of 10.1% from 2014 to March 2017, AB.8-9, but this growth came from debt-funded acquisitions, OB.8; Op.7, 16, 24.

- SourceHOV had multiple near misses of the Leverage Ratio covenants, and several times resorted to raising money from existing stockholders to meet them. OB.8, 10-11; Op.10, 16-19, 21. Appellees refused to invest in 2016 at $1,600 per share but were enthusiastic sellers at that price. OB.10. Appellees invested at that price in January 2017, *after* the Business Combination was underway. OB.11.

- SourceHOV repeatedly failed to improve its capital structure and amend its imposing financial covenants. OB.9.

- KPMG expressed concern in March 2017 about SourceHOV's ability to continue as a going concern. OB.15.

Yet Appellees claim that SourceHOV "made a false, litigation-driven claim of 'near certain default'," relying on SourceHOV's responses to KPMG's skepticism about SourceHOV's going concern status. AB.21-22. Putting aside the irony of relying on a company's response once an auditor has questioned going concern status—an indication of financial distress—SourceHOV's response was conditioned on its ability to meet projections, OB.15, which were *not* met, Op.24; OB.15. And while Appellees note that rating agencies did not downgrade SourceHOV a *fourth* time, AB.22, that was because of the Business Combination, AR01 (proposed merger was "credit positive . . . the company will benefit from lower debt leverage and greater financial flexibility while addressing key liquidity concerns").[1] Indeed, Appellees have alleged that "at all relevant times after the business combination, SourceHOV was, and remains, insolvent." AR07.[2]

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[1] Appellees note that SourceHOV complied with the Leverage Ratio covenants before the Business Combination, AB.21, but ignore the repeated near misses.

[2] Appellees point to $806M and $645M figures for "SourceHOV's Existing Equity Value" in the Proxy and revised Proxy. AB.7-8. These numbers merely reflect the calculation of 80,600,000 Quinpario shares offered at (i) $10 per share per the LOI, A1658, and (ii) $8 per share in connection with the PIPE, A2488; A2511; A2576-77.

## ARGUMENT

### I. THE OPINION ERRED BY FAILING TO FACTOR SOURCEHOV'S OPERATIVE REALITY INTO ITS COST OF DEBT, EQUITY BETA, AND CHOICE OF PROJECTIONS ASSUMPTIONS

#### A. The Opinion's Failure To Consider SourceHOV's Operative Reality Is Reviewed *De Novo*

The interpretation and application of Section 262 present questions of law reviewed *de novo*. *M.G. Bancorporation, Inc. v. Le Beau*, 737 A.2d 513, 524 (Del. 1999). Section 262 requires that a court "shall take into account all relevant factors," 8 *Del. C.* § 262(h), including the appraised company's "operative reality," which is "an independent element of value that must be taken into account in determining a fair value," *M.G. Bancorporation*, 737 A.2d at 525; OB.21.

Invoking the "abuse of discretion" standard, Appellees contend that the trial court "considered the evidence yet 'ultimately chose not to accord' SourceHOV's arguments 'any weight.'" AB.1, 26-27. Appellees mischaracterize the Opinion and the issue on appeal. The Opinion acknowledged and fully credited the evidence regarding SourceHOV's precarious operative reality. *Supra* at 2-3. Yet the Opinion adopted Mr. Meinhart's fair value analysis that was untethered to that reality, in contravention of Section 262. That was legal error. *See M.G. Bancorporation*, 737 A.2d at 524-25 (whether expert analysis adopted below properly considered company's "operative reality" was question of law that "must be reviewed *de novo*").[3]

This Court's decision in *M.P.M. Enterprises v. Gilbert*, 731 A.2d 790 (Del. 1999), AB.1, 27, is inapposite. There, the trial court considered, but did not accord weight to, prior offers and merger terms; that weighting was reviewed for abuse of discretion. 731 A.2d at 795. Here, the Opinion committed legal error by adopting a valuation analysis that nowhere factored in SourceHOV's acknowledged operative reality.

Thus, the fact that the Opinion made certain "credibility" findings, AB.1, 27, is irrelevant. Regardless, as demonstrated *infra* at 13-17, 23-25, there was no "credibility gap," AB.27, and the Court "may well find clear error even in a finding purportedly based on a credibility determination," *Cede & Co. v. Technicolor, Inc.*, 758 A.2d 485, 492 & n.36 (Del. 2000).

Even if this Court were to review for abuse of discretion, it should still reverse because the Opinion's assumptions regarding SourceHOV's cost of debt, beta, and

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[3] This Court routinely reviews *de novo* trial courts' interpretation and application of factors relevant to a fair value determination. *See Golden Telecom, Inc. v. Glob. GT LP*, 11 A.3d 214, 216-17 (Del. 2010) (merger price); *Paskill Corp. v. Alcoma Corp.*, 747 A.2d 549, 554 (Del. 2000) (net asset value); *Gonsalves v. Straight Arrow Publishers, Inc.*, 701 A.2d 357, 361 (Del. 1997) (whether trial court properly embraced only one expert's valuation); *Cede & Co. v. Technicolor, Inc.*, 684 A.2d 289, 290 (Del. 1996) (business plans and strategies).

projections were unsupported by the record. *See DFC Glob. Corp. v. Muirfield Value Partners, L.P.*, 172 A.3d 346, 348-49, 363 (Del. 2017).[4]

### B. The Opinion's Cost Of Debt Estimates Failed To Account For SourceHOV's Operative Reality

#### 1. Mr. Meinhart's Estimates Were Untethered To SourceHOV's Operative Reality

Appellees nowhere demonstrate that Mr. Meinhart's cost of debt assumptions reflected SourceHOV's operative reality. Mr. Meinhart admitted that he did not consider SourceHOV's ability to borrow, and that his first of three hypothetical scenarios (4.42% cost of debt and capital structure with 17% debt) was "fundamentally different" from SourceHOV's operative reality. OB.3, 23, 29-30. Yet he used that scenario to generate artificially low discount rates to decrease his "averaged" discount rate and increase his valuation. OB.23. That alone requires remand.

Instead, Appellees insist that Mr. Meinhart's remaining two scenarios assumed a 9.73% cost of debt based on a generic bond index (S&P CCC Bond index) that "matched" SourceHOV's CCC rating. AB.2, 18, 34. But SourceHOV suffered three downgrades in two years, and more downgrades may well have come but for the Business Combination. *See supra* at 2-3. Any "match" to the credit rating alone

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[4] *Accord Verition Partners Master Fund Ltd. v. Aruba Networks, Inc.*, 210 A.3d 128, 133-34 (Del. 2019); *Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd.*, 177 A.3d 1, 23-24 (Del. 2017).

is not a sufficient tether to SourceHOV's operative reality.[5] Moreover, Mr. Meinhart indisputably failed to determine whether the companies of the 468 indexed bonds were similar to SourceHOV, or to ensure that the bonds' widely dispersed yields-to-maturity (3%-160%) were tightly packed around the mean. OB.23-24.[6]

The authorities Appellees cite, asserting that cost of debt estimates have been based on indices, are distinguishable. None had to consider, as Professor Jarrell offered here, competing, company-specific cost of debt evidence that differed from an index corresponding to a credit rating.[7]

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[5] Nor can Appellees find support from the ICE BAML 10+ Year Index, AB.3, 18, 34, which Professor Jarrell did "not us[e] or rely[]" on, A4045; A0878; A0887.

[6] SourceHOV does not seek to "break the Index's own rules." AB.35. The wide dispersion in yields-to-maturity and face value of the indexed bonds, A4087, renders the index unreliable, A0884 (when "measures of central tendency from a distribution are all over the place, that's a sign that you have problems"). Professor Jarrell measured averages using different techniques not to use the resulting yields-to-maturity as a proxy for SourceHOV's cost of debt, but to test the central tendency and show the index is unreliable.

[7] *See Merion Capital L.P. v. Lender Processing Servs., Inc.*, 2016 WL 7324170, *28 (Del. Ch. Dec. 16, 2016) (court accepted 5.02% estimate where company held same credit rating for seven years; competing estimate 5.0%); *In re Rural Metro Corp.*, 88 A.3d 54, 109 (Del. Ch. 2014) (court accepted 7.5% estimate where credit rating and capital structure likely to be stable for 10 years; competing estimate 7.3%); *Lane v. Cancer Treatment Ctrs. of Am., Inc.*, 2004 WL 1752847, *31 (Del. Ch. July 30, 2004) (estimate chosen because expert's cost of *equity* calculation had "better developed factual support"); *see also Blueblade Cap. Opportunities LLC v. Norcraft Cos., Inc.*, 2018 WL 3602940, *32 (Del. Ch. July 27, 2018) (court averaged both experts' estimates, including one based in part on return on outstanding loan, including effect of issuance discount).

Appellees claim that Mr. Meinhart's 9.73% assumption was "conservative" given the 9% weighted average interest rate on SourceHOV's outstanding debt just before the Valuation Date. AB.19, 35-36. But even Mr. Meinhart admitted that a company's stated interest rate during the life of a loan is not an accurate measure for cost of debt. A0851; A0392.[8]

2. <u>Appellees Raise No Valid Challenge To Professor Jarrell's SourceHOV-Specific Estimate</u>

Appellees insist that "nothing else supports" Professor Jarrell's 11% cost of debt estimate beyond "inaccurate and unreliable" Bloomberg data. AB.1, 5, 20, 33, 35. That is false.

Professor Jarrell testified: "Let me just make it clear. . . . I did not rely on a [Bloomberg] yield to maturity to do my work." A0878. Instead, he relied on SourceHOV-specific evidence: (i) the 9.5% weighted average yield-to-maturity of the First and Second Liens *at issuance*; (ii) SourceHOV's repeated downgrades and difficulties obtaining additional financing thereafter; and (iii) the 10% interest rate

[8] Equally unavailing is Appellees' reference to the 9.7% weighted interest rate of Exela's acquisition debt. AB.36. Only the 10% interest rate on the $1B notes should be considered, as "that's the kind of debt that a standalone SourceHOV would be looking at." A0887; A0877-78. Appellees falsely claim that SourceHOV and Exela had the same debt ratings. AB.36. SourceHOV's debt was downgraded in August 2016. OB.7.

on Exela's acquisition financing. OB.25. Yields-to-maturity on the First and Second Liens from post-issuance trading were only confirmatory. *Id.*; Op.61 n.297.[9]

Appellees insist that SourceHOV's 9.5% cost of debt in 2014, and Exela's 10% cost of acquisition debt in July 2017, "do not support" Professor Jarrell's "much higher" 11% estimate. AB.3, 35. Putting aside the ratings downgrades that followed 2014 and that Exela was a better rated, less levered company, Appellees' unsupported assertion is contradicted by the record. A0878 ("if 10 percent is the acquisition debt . . . I'm absolutely very confident that the true cost of debt for [SourceHOV] at that roughly same point in time cannot possibly be less than 100 basis points greater than 10 percent.").

Appellees contend that "[e]ven *Amici* decline to support" Professor Jarrell's 11% calculation. AB.35. But *Amici* "[took] no position" on the estimate because it "is a matter based on the specific trial record in this case." AmiciB.7. *Amici* addressed the trial court's findings regarding Professor Jarrell's methodological approach to estimating beta and the various tools that courts can use for such estimations. AmiciB.1-5, 8, 11-12.

Appellees repeat the Opinion's concern that yields-to-maturity may "overestimate the debt cost of capital" because they do not consider default risk.

[9] The Bloomberg pricing was confirmed by at least one actual trade, A4042; A0878, and Appellees thought it was accurate, OB.25.

AB.3, 36; *see* Op.61 n.297. But any "overestimation" on cost of debt would have been remedied by Professor Jarrell's conservative approach on beta. OB.26; *see* AmiciB.8. Appellees have no response. Regardless, Professor Jarrell relied on various pieces of SourceHOV-specific evidence for his 11% estimate, just one of which was the yield-to-maturity *at issuance* on SourceHOV's debt. *Supra* at 8-9. None of Appellees' treatise snippets address using yields-to-maturity *at issuance*, *see* A3993; B2301; B2359-60; B2375, which factor in default risk through, as occurred here, initial discounting. A0875-76. Moreover, the record regarding the trial court's concern was never developed, as Mr. Meinhart also used yields-to-maturity. OB.26; A0849. To the extent there is any question, this Court should remand to the trial court to hear from the experts rather than rely on treatise excerpts appended to post-trial briefing. *See* A1063; A1181; A1198-99.

### C. The Opinion's Beta Estimates Failed To Account For SourceHOV's Operative Reality

#### 1. Appellees Fail To Justify Adoption Of Mr. Meinhart's Indirect Approach

Attempting to justify the Opinion's adoption of Mr. Meinhart's beta stew approach, *see* OB.16-17, 30, Appellees insist that the *required* methodology for estimating equity beta of a privately-held company is to use guideline companies, AB.2, 19-20, 28, 32-33. That is false. Treatises and Delaware cases (including those cited by Appellees) instruct that a beta based on guideline companies should only be used if there are sufficiently comparable companies, and that alternative methods for estimating beta exist. *See Blueblade*, 2018 WL 3602940, *33-34; *Del. Open MRI Radiology Associates, P.A. v. Kessler*, 2006 WL 4764042, *33 (Del. Ch. Apr. 26, 2006); AmiciB.3, 9-11; OB.27, 31.[10]

Appellees fail to meet their burden of proving comparability to support Mr. Meinhart's beta approach. This is not surprising given the "dearth of comparable companies," Op.41, and Mr. Meinhart's concession that his guideline companies were not comparable enough to support reliance on a GPTC analysis, OB.16, 28—which Delaware courts have used to reject reliance on indirect betas, OB.28.[11]

Appellees point to the partial overlap in guideline companies selected by Mr. Meinhart and by SourceHOV advisors Rothschild, Morgan Stanley and E&Y in their various work. AB.2, 14-15, 29. But no advisor estimated beta for purposes of a

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[10] Appellees cherry-pick and mischaracterize treatise snippets. AB.28. The Duff & Phelps excerpt references "[n]ewer estimation techniques," B2379, and reiterates that "[t]here are many variations on the way betas are estimated by different sources of published betas and by valuation analysts," B2397. Professor Damodoran, AB.28, 30-31, has written extensively on alternative methods to estimate beta, OB.31 n.13; AmiciB.11.

[11] Attempting to escape this clear contradiction, Appellees point to three distinguishable cases where courts used indirect betas notwithstanding that experts refused to rely on a GPTC analysis. AB.31. *See Gilbert v. M.P.M. Enters.*, 709 A.2d 663, 671 (Del Ch. 1997) (both sides proposed using indirect beta), *aff'd*, 731 A.2d 790 (Del. 1999); *In re Orchard Enters.*, 2012 WL 2923305, *18 n.116 (Del. Ch. July 18, 2012) (experts agreed on industry beta), *aff'd*, 2013 WL 1282001 (Del. Mar. 28, 2013); *Blueblade*, 2018 WL 3602940, *34 (experts agreed on four of six guideline companies, with remaining two being acknowledged direct competitors).

Delaware appraisal proceeding, which requires consideration of SourceHOV's operative reality. Furthermore, partial overlap cannot demonstrate comparability without some substantive showing of why the advisor selected the guideline companies and that they were indeed comparable.[12]

This showing was not made here. Appellees remain silent on the extensive differences (i) among the 19 guideline companies, and (ii) between those companies and SourceHOV. OB.28-29. Appellees seize on three guideline companies with "similar enterprise values," AB.16-17, 30, but the remaining 16 had enterprise values ranging from *$4.3 billion-$1.1 trillion*, A3876. And these three companies—and three others Appellees highlight, AB.30—differed from SourceHOV in further ways, including higher credit ratings and lower debt, OB.28-29; A3874-76.

Mr. Meinhart's unlevering and re-levering process did not remedy the lack of comparability. AB.2, 15-16, 29-30. These formulas can help control for differences in financial *leverage*, AB.29-30, but they do not account for other significant differences, as existed here. OB.28-29. Regardless, Appellees remain silent on the errors Mr. Meinhart introduced: after unlevering 19 betas with three formulas, he selected the highest beta that corresponded to Cognizant—a company with a $40B

[12] Appellees' reliance on *DFC* and *Blueblade*, AB.29, is unavailing, as all experts in those cases agreed on the guideline company approach and most of the companies to be used, *DFC*, 172 A.3d at 387; *Blueblade*, 2018 WL 3602940, *34.

market cap (SourceHOV's was less than $694M), capital structure with 2.9% debt (SourceHOV's had at least 57%), and a credit rating of Aa (SourceHOV's was CCC). OB.29; A4080; A3874-76; A0842. Mr. Meinhart compounded his error by re-levering using (i) the Hamada method, which assumes *zero* debt, and (ii) three hypothetical capital structure scenarios, including a 17% debt scenario "fundamentally different" from SourceHOV's operative reality. OB.29.

Appellees also stay silent on Mr. Meinhart's dizzying approach of constant averaging and triangulating toward beta (and WACC). *See* OB.16-17, 29-30. That approach generated and recycled artificially low betas of 1.21 and 1.37 (and thus artificially low discount rates) and is antithetical to the precision required for appraisal. *Id.*

#### 2. The Opinion Erred By Rejecting Professor Jarrell's SourceHOV-Specific Approach

Appellees seek to write off Professor Jarrell's SourceHOV-specific approach to equity beta as "novel," AB.2, 19, 32, yet they nowhere dispute that it was "sound and straightforward," "professionally credible," and "solidly grounded in bedrock finance theory," AmiciB.4, 12, 15. Appellees nowhere challenge:

- An implied debt beta can be derived through CAPM, OB.19, 32;
- Professor Jarrell correctly applied CAPM to his cost of debt estimate, *id.*;
- Debt beta can serve as a conservative floor for equity beta, as equity beta must always be higher, *id.*; AmiciB.14-15.

Professor Jarrell's testimony that he had not previously seen these steps combined to estimate equity beta, OB.19-20, does not support a finding that his approach, much less Professor Jarrell himself, lacked credibility. As *Amici* explain, the methodology was "particularly appropriate where, as here, no direct beta could be calculated . . . and no sufficiently comparable companies for an indirect peer-based beta could be identified," and "can be a useful part of the Court of Chancery's appraisal toolkit in cases where the two commonly-used methods for estimating beta are not available or otherwise not appropriate." AmiciB.4-5, 15-16. Other than insisting on a "peer-reviewed study" or treatise discussing the combination of Professor Jarrell's steps, AB.32—which is not required, especially considering *Amici*'s undisputed statements—Appellees proffer no response.

Appellees level the baseless attack that Professor Jarrell's approach was "made-for-litigation." AB.19. Professor Jarrell devised his approach after determining that neither of the two commonly-used methods for estimating beta were available. OB.18-19. He did so during litigation *because he was hired as a litigation expert*; like Mr. Meinhart, he was not involved in the deal process.

Confused, Appellees suggest that Professor Jarrell's beta estimate relied on Bloomberg pricing data for trading in the First and Second Liens. AB.20, 33. Not so. Professor Jarrell did not estimate beta by running regressions on trading returns (as one typically does when estimating beta for publicly-held companies). A0887.

Instead, he estimated SourceHOV's cost of debt; derived a debt beta; and then used that debt beta as the minimum possible estimate for equity beta. OB.19, 32-33.

Appellees also complain that Professor Jarrell's debt beta is "double" Duff & Phelps' debt beta of 0.71 for Caa-rated debt. AB.20, 33-34. Putting aside that the Duff & Phelps index reflects debt betas of unidentified companies with no explanation of comparability, B2394, no expert believed that a 0.71 debt beta was reflective of SourceHOV's operative reality. Mr. Meinhart offered alternative calculations of SourceHOV's debt beta of 1.18 and 1.06. A3713-14. The Duff & Phelps debt beta was inappropriate given "such good information on the company's specific cost of debt." A0339; A0887.

Finally, Appellees nowhere dispute that Professor Jarrell took "a highly conservative valuation approach" to beta. AmiciB.8, 15. When Mr. Meinhart re-levered his betas using hypothetical capital structure assumptions far closer to SourceHOV's actual 57% debt, he generated betas of 2.46 and 2.02, significantly higher than Professor Jarrell's 1.4 beta. OB.34.

### D. The Opinion Erroneously Refused To Consider The Bank Case Projections That Best Took Into Account SourceHOV's Operative Reality

Appellees repeat the Opinion's finding that there was some "disagreement" between Professor Jarrell and SourceHOV regarding the most reliable projections, Op.2-3, 53-55; AB.1, 3, 21, 37, but support it only with mischaracterizations of the record.

SourceHOV's trial briefing did *not* admit that Professor Jarrell chose the Equity Case "as the most reliable indicator of value of SourceHOV." AB.37. The brief explains that he "used both the February 2017 Bank Case and Equity Case in his analysis," and "ultimately concluded that the *APV-based discounted cash flow analysis* relying on the February 2017 Equity Case was the most reliable indicator of value of SourceHOV's shares at the time of the merger[.]" B517 (emphasis added). The brief reiterates Professor Jarrell's "serious reservations" regarding the reasonableness of the Equity Case. B517; *see also* OB.18, 34-35.

Nor did SourceHOV disagree with Professor Jarrell about SourceHOV's equity value. AB.37. SourceHOV's briefing said it would demonstrate that $1,633 per share was SourceHOV's fair value, and that Professor Jarrell would testify that, even employing the more petitioner-friendly projections, fair value still did not exceed $2,818 per share. B473; *see* A3611 ("conservative" use of Equity Case "will likely overstate the actual (unknown) fair value").

Appellees cite one exhibit and two excerpts from Professor Jarrell's testimony to manufacture a non-existent disagreement. AB.37. The purpose of that exhibit was to summarize corrections to Mr. Meinhart's analysis. B2276. Appellees ignore the many times Professor Jarrell relied on both the Equity and Bank Cases and proffered valuations and opinions under both. OB.18, 37.[13]

Appellees also ignore Professor Jarrell's testimony that he was not engaged to opine on the most reliable projections. OB.37. And Appellees omit that Professor Jarrell testified: "Well, you know, I'm complaining about how aggressive the projections are. So, you know, that would imply that the . . . lower projections [in the Bank Case] are more reliable than the higher projections [in the Equity Case]." A0865.[14]

Without the improper lens of some non-existent "disagreement," the Opinion's embrace of the more aggressive Lender Case—assuming 5% annual revenue growth, Op.25—is unsupported by the record. Appellees highlight that SourceHOV used the Lender Case most often and with third parties, AB.3, 11-13, 37-39, but management also missed seven of its last eight sets of projections. Op.24.

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[13] Appellees claim Professor Jarrell changed his views on projections "after the expert discovery cutoff," AB.37, but his opening report noted "serious reservations" with the Equity Case and performed DCF analyses using the Bank Case, OB.18; A3655. In *Merion Capital, L.P. v. 3M Cogent, Inc.*, 2013 WL 3793896, *9-10 (Del. Ch. July 8, 2013), AB.37, the expert's views changed between deposition and trial, with no notice.

[14] Appellees also claim Mr. Verma testified that the Equity Case was the set management "stands behind," AB.37, but ignore his testimony that management stood behind both the Equity and Bank Cases, authorizing *both* to be sent out in the same spreadsheet with a toggle, OB.12-13. Likewise, Appellees state that SourceHOV's Board "sign[ed] off" on the Equity Case, AB.11, when the testimony was that "sign off" was on external release—which was given for *both* cases, A0620.

Management's Lender Case adopted the Equity Case's revenue growth projections, Op.25, which was the "very hopeful" "fire on all cylinders," "no room for error" scenario. OB.12. This aspirational quality undermines reliability. OB.36. Appellees cannot justify these aggressive projections by referencing historic 10% CAGR from acquisitions. AB.3, 37-38. Organic growth since 2014 was negative. *Supra* at 2. Indeed, management itself lowered its 5% revenue growth projections prior to the Business Combination's closing. A2300.

That leaves Appellees arguing that the Lender Case was the most recent and most recently updated of the three sets, AB.3, 13, 39—but also the fastest proven wrong, further undermining reliability, OB.36. Neither *Orchard Enterprises*, 2012 WL 2923305, *12-13, nor *Global GT LP v. Golden Telecom Inc.*, 993 A.2d 497, 501-02, 510 & n.82 (Del. Ch. 2010), *aff'd*, 11 A.3d 214 (Del. 2010), AB.39, aid Appellees, as the most recent projections there were supported by other indicia of reliability and formed the basis for fairness opinions supporting the transactions. Here, the Lender Case was created as a marketing pitch to lenders, counter-parties, and possible investors, yet again undermining reliability. OB.36.[15] Contrary to

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[15] Appellees' cases, AB.38, are distinguishable. In *Owen v. Cannon*, 2015 WL 3819204, *19-22 (Del. Ch. June 17, 2015), there were numerous indicia of reliability for management's projections, and the other side's projections had been created by an expert for litigation. In *Andaloro v. PFPC Worldwide, Inc.*, 2005 WL 2045640, *11 (Del. Ch. Aug. 19, 2005), the experts agreed on projections. In *In re Emerging*

Appellees' suggestion, AB.38, the record lacks evidence that the Lender Case's aggressive growth assumption was "tested" by any third party; the record instead shows that the Lender Model made the minimal reduction necessary to account for actual underperformance in early 2017. A0631 ("So the company did not perform per the expectation, so that's why we decided to, per the collective feedback, to take the model down."). And Appellees' insistence that statements to lenders and auditors must not be intentionally false, AB.38, does not mean that the Lender Case was the most *reliable*, particularly given the context in which it was developed.

While Appellees tout that the Lender Case was the most accurate predictor for a single quarter (first quarter 2017), AB.4, 9-10, 39, that was because it was *the most conservative* for 2017, Op.24. It was off by the second quarter. *Id.*

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*Communications, Inc. Shareholders Litigation*, 2004 WL 1305745, *14 (Del. Ch. May 3, 2004), the other side's projections had been modified by the expert.

## II. THE OPINION COMMITTED LEGAL ERROR BY REFUSING TO CONSIDER SECOND QUARTER FINANCIAL DATA THAT WAS "KNOWABLE" ON THE VALUATION DATE

Appellees insist that SourceHOV's second quarter 2017 financial statements were not "reasonably available" on the Valuation Date. AB.41-43. But Section 262 requires consideration of financial information that is "known or knowable" on the valuation date, not that such data be "available" in consolidated financial statement form. OB.39-40. Even under an abuse of discretion standard, the Opinion's decision to ignore knowable second quarter data is not supported by the record. *See supra* at 5-6 & n.4.

SourceHOV's financial data for the second quarter of 2017—which ended June 30, 2017—was unquestionably knowable on the Valuation Date. It was a matter of fixed historical record as of July 12, 2017. While Appellees reference Mr. Reynolds' testimony that it "usually takes time" to prepare financial statements after quarter-end, AB.42, Appellees ignore his next response: "All the data exists. It just takes time to generate the financial statements." A0776. Mr. Meinhart agreed that any cash flows and changes to net debt would have been accounted for by the Valuation Date. A0840; *see Doft & Co. v. Travelocity.com Inc.*, 2004 WL 1152338, *8 n.53 (Del. Ch. May 20, 2004) (first quarter information was "clearly knowable or 'susceptible of proof' before the actual balance sheet was released only twelve days after the merger"); *accord Kleinwort Benson Ltd. v. Silgan Corp.*, 1995 WL 376911, *6-7 (Del. Ch. June 15, 1995).

Thus, SourceHOV's affirmation to KPMG on July 12, 2017 that "no consolidated financial statements are available as of any date or for any period subsequent to March 31, 2017," B1965; AB.41, is irrelevant.[16] The data was knowable, as Mr. Reynolds' undisputed testimony shows.

Similarly, that SourceHOV told KPMG on July 11, 2017 that it had "estimates" for May and June 2017 financial statements, AB.42, does not render the second quarter data unknowable. The cited email attached an Excel spreadsheet with "the Q1, Q2 (monthly) and 11 days of July" financial statements—confirming that the data existed and was known and knowable as of July 12, 2017. A3924-25; OB.40-41.

Contrary to Appellees' assertion, AB.42, financial data does not need to be "audited" to be knowable. Even the March 31, 2017 financial statements that the Opinion used were unaudited as of July 12, 2017. B1965.

Appellees' cited cases do not support ignoring the knowable second quarter financial data. AB.42-43. In *Lane v. Cancer Treatment Centers of America*, the relevance and admissibility of post-merger documents that showed *pre-merger*

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[16] Appellees misleadingly omit the word "consolidated" before "financial statements." AB.41; B1965.

financial information was undisputed. 1994 WL 263558, *1, 4 (Del. Ch. May 25, 1994). *Tri-Continental Corporation v. Battye* confirmed the "known or knowable" standard. 74 A.2d 71, 72 (Del. 1950) ("any . . . facts which were known or which could be ascertained as of the date of merger . . . must be considered by the agency fixing the value").[17]

SourceHOV's second quarter financial data "existed," Op.71, and was knowable, as of the Valuation Date. Accordingly, it was legal error to ignore it.

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[17] The remaining two cases, AB.43, addressed projected revenue for an event planned after merger and post-merger offers, both unknowable at the time of the merger.

## III. APPELLEES FAIL TO IDENTIFY ANY FACTS SUPPORTING THE OPINION'S IRRELEVANT CREDIBILITY DETERMINATION BASED ON THE "AS OF JULY 2017" ROTHSCHILD DECK

Nothing in the record supports the Opinion's adoption of Appellee's irrelevant backdating tale. OB.42-46.

Appellees nowhere explain how their backdating story was relevant to the Opinion's valuation, a "battle of the experts." Op.51. Likewise, neither Mr. Chadha's nor Mr. Jonovic's testimony served as the basis for the trial court's findings regarding SourceHOV's operative reality. *See supra* at 2-3. Nor do Appellees suggest any rational motive to generate and backdate to July 2017 a Rothschild presentation with a DCF mid-point valuation of \$675M. A3506. As Appellees point out, AB.8, the June 2017 Proxy already disclosed a *lower* \$645M for equity value.

Worse, Appellees remain silent with respect to the actual documents: the presentation had no date (its title was "Komodo Final Structure *as of* July 2017"), and its first page noted that it was prepared on a "retrospective basis." OB.43. Appellees nowhere defend their post-trial briefing falsely describing the presentation as having a "'July 2017' date." OB.43. The January 2018 emails surrounding creation of the deck evidence no plan to backdate or obtain a reduced valuation, but a simple request to memorialize, on a retrospective basis, an updated analysis based on public information from after February 2017 that Messrs. Chadha and Jonovic each recalled Rothschild having done before closing. OB.43-45. Appellees dispute none of this.

Instead, Appellees proffer heavy rhetoric, AB.22-23, 44-45 ("SourceHOV engaged in misconduct," "kept lying," and "falsely testified"), backed only by two slim inferences, each relying on mischaracterization.

First, pointing to SourceHOV's June 2018 Interrogatory Responses, Appellees assert that SourceHOV "swore that Rothschild presented the Backdated Valuation at a meeting 'in . . . July 2017.'" AB.45; *see also* AB.23. That is false. The interrogatory asked for identification of "each presentation made by Rothschild," the meeting at which such presentation was made, and who attended. A3550. SourceHOV's response, which Appellees paraphrase, was: "Rothschild made presentations concerning [the Business Combination] in February and July 2017. Members of the Project Komodo Group and Delos Capital attended the meetings at which the presentations were made." A3550-51. SourceHOV nowhere swore that any specific presentation—let alone a written presentation or the "as of July 2017" PowerPoint deck—was provided in July 2017.

Second, Appellees complain that certain metadata for, and the January 2018 emails surrounding creation of, the "as of July 2017" presentation were not produced until after a Rothschild deposition. AB.23. Appellees' protest about metadata makes no sense; their document requests sought only beginning/ending Bates numbers, AR15, and Appellees nowhere claim such metadata was not provided with the initial production of the deck. As for the January 2018 emails, SourceHOV expressly objected to production of post-July 2017 documents. AR30. Once Appellees demanded production of the January 2018 emails, they were produced—and evidenced no backdating scheme. *See supra* at 23-24.

Appellees' backdating tale is an irrelevant fiction that improperly colored the trial court's views, distracting it from the key issue of SourceHOV's operative reality.

## CONCLUSION

SourceHOV respectfully requests that this Court vacate the Order and remand for the trial court to factor SourceHOV's operative reality into its fair value analysis.

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**CERTIFICATE OF SERVICE**

I hereby certify that on October 19, 2020, the foregoing document was served in hard copy via messenger, and electronically via File & Serve*Xpress*, upon the following counsel of record:

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