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Delaware Supreme Court Issues Guidance On "Fair Price" In Appraisal Actions

In a "cash-out" merger, where a company is bought out by another company and stockholders receive cash in exchange for their shares, Delaware law normally provides stockholders with the remedy of appraisal. Pursuant to the appraisal process, stockholders who have been cashed out are entitled to seek fair value for their shares. What constitutes "fair value," however, is an evolving concept.

Traditionally, the stockholder seeking appraisal and the acquired company (or sometimes, the acquiring company) retain experts who present competing valuation theories based on a series of financial analyses. There are three traditional valuation analyses: (i) a comparable companies analysis, which ascertains an implied value for the target company based on metrics relating to purportedly similar companies; (ii) a precedent transactions analysis, which ascertains a value based on analogous mergers and acquisitions; and (iii) a discounted cash flow analysis, which calculates a present-day value for the target company using its long-term financial projections.

The parties' respective experts make numerous assumptions and can take wildly different approaches in their analyses. These differences may include which companies to include in or exclude from the analyses, which transactions are more or less similar to the one at issue, and what discount rates and other adjustments should be

applied to the target company's forecasts. The experts also decide how much weight a given analysis has over the others, anywhere from 0% to 100%.

The court's job is to resolve the dispute over whose expert did a better job, took the more realistic approach, made the more defensible assumptions, and ultimately made the more convincing case regarding the target company's "fair value." The court can adopt any of the parties' positions, or it can fashion its own solution. The stockholder then receives (or pays, in some cases) the difference between the deal price and the court-determined fair value.

The foregoing discussion reflects how courts have traditionally ascertained fair value in appraisal cases. Recently, however, courts have disregarded this traditional analysis-based approach to valuation and, instead,

(Continued on Page 2)

In This Issue

Attorney Insights

News & Events

Firm Information

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(Continued from Page 1)

have determined that the negotiated deal price reflects a company's fair value. In fact, the Delaware Supreme Court even reversed a lower court decision that gave weight both to the deal price and to the valuation analyses to determine a fair value.

In 2014, DFC Global Corp. was acquired by an affiliate of private equity firm Lone Star Funds for $9.50 per share. Following the acquisition, Muirfield Value Partners, a former DFC Global stockholder, commenced an appraisal proceeding to seek fair value for its shares. Using a discounted cash flow model, the stockholder's expert asserted that DFC Global was worth nearly double the deal price. The company's expert performed a discounted cash flow analysis and a comparable companies analysis to argue that DFC Global was worth less than the deal price.

Following a lengthy litigation, including trial, Chancellor Andre G. Bouchard of the Delaware Court of Chancery ruled that DFC Global was worth $10.21 per share, roughly 7.5% more than the actual deal price. In reaching his decision, Chancellor Bouchard accepted and rejected various aspects of both experts' analyses, and the Court decided to give equal one-third weight to the discounted cash flow analysis, the comparable companies analysis, and the deal price. The Court explained its weighting decision: "In sum, all three metrics suffer from various limitations but, in my view, each of them still provides meaningful insight into DFC's value, and all three of them fall within a reasonable range."

On appeal, which was decided on August 1, 2017, the Delaware Supreme Court vacated the lower court's decision. While it declined to make a definitive ruling on fair value, the Delaware Supreme Court explained that there was no logical basis in the record to give equal weight to the three valuation approaches. Moreover, because the merger resulted from a seemingly fair and open process during which numerous potential parties were contacted, the Delaware Supreme Court tacitly encouraged the lower court to find that the $9.50 per share deal price, in fact, reflected DFC Global's fair value.

Commentators have subsequently observed that Delaware's statutory scheme allowing for appraisal, and decades of case law, did not emphasize a reliance on the deal price anywhere near to the extent that the Delaware Supreme Court and the Delaware Court of Chancery seem to have embraced in recent decisions.

Beyond the normal complexity of offering, defending, and refuting granular aspects of financial analysis, appraisal actions now invite a new set of disputes, including over market efficiency, the fairness and efficacy of a pre-merger sales process, and anything else bearing on whether the final merger price reflects the full value of a going concern. It remains to be seen whether the Delaware legislature will intervene to turn back the clock on recent developments. Indeed, appraisal actions were designed to be relatively narrow, almost summary proceedings, yet the decision in the DFC Global case and others have opened Pandora's Box.

Pending any legislative action, stockholders still have options if they contest a merger or acquisition due to concerns about inadequate consideration.

A Stockholder can still file a claim for breach of fiduciary duty against the board of directors, and stockholders can also file an action under the federal securities laws, if the disclosures filed with the U.S. Securities and Exchange Commission and sent out to stockholders misrepresent or omit material information.

Upcoming Lead Plaintiff Deadlines

Johnson Fistel is investigating many potential cases arising under the federal securities laws. If you would like more information, or if you wish to participate in an action, please contact us as soon as possible to ensure that your rights are fully protected. Listed below are matters that the firm is investigating and the applicable deadlines for filing a motion with the court to be appointed as a "lead plaintiff" under the Private Securities Litigation Reform Act of 1995.

COMPANY	DEADLINE
Applied Optoelectronics, Inc. *(NASDAQ:AAOI)*	Oct. 4, 2017
Maximus, Inc. *(NYSE:MMS)*	Oct. 6, 2017
GlobalSCAPE, Inc. *(NYSEMKT:GSB)*	Oct. 8, 2017
Sequans Communications S.A. *(NYSE:SQNS)*	Oct. 8, 2017
Electronics for Imaging, Inc. *(NASDAQ:EFII)*	Oct. 9, 2017
TransDigm Group Incorporated *(NYSE:TDG)*	Oct. 9, 2017
Acacia Communications, Inc. *(NASDAQ:ACIA)*	Oct. 13, 2017
Forterra, Inc. *(NASDAQ:FRTA)*	Oct. 13, 2017
ZTO Express (Cayman) Inc. *(NYSE:ZTO)*	Oct. 14, 2017
Blue Apron Holdings, Inc. *(NYSE:APRN)*	Oct. 16, 2017
Rayonier Advanced Materials Inc. *(NYSE:RYAM)*	Oct. 16, 2017
Depomed, Inc. *(NASDAQ:DEPO)*	Oct. 17, 2017
Zillow Group, Inc. *(NASDAQ:Z)*	Oct. 21, 2017
Teva Pharmaceutical Industries Ltd. *(NYSE:TEVA)*	Oct. 22, 2017
Top Ships Inc. *(NASDAQ:TOPS)*	Oct. 22, 2017
Dr. Reddy's Laboratories Limited *(NYSE:RDY)*	Oct. 24, 2017
PetMed Express, Inc. *(NASDAQ:PETS)*	Oct. 24, 2017

Recent Noteworthy Decisions

United States v. Martoma, No. 14-3599, 2017 U.S. App. LEXIS 16084 (2d Cir. Aug. 23, 2017)

The United States Court of Appeals for the Second Circuit upheld the conviction of a hedge fund portfolio manager for insider trading in a decision that assists prosecutors in pursuing such misconduct. The defendant had obtained confidential information by meeting regularly with a paid consultant who worked with a pharmaceutical company that was developing an Alzheimer's drug. When the consultant disclosed to the portfolio manager that the drug test was unsuccessful, the hedge fund sold its position in two pharmaceutical companies and then shorted the shares before the prices dropped on disclosure of the results, generating profits and avoiding losses of more than $250 million. The Second Circuit's decision abandoned the requirement that prosecutors establish a "meaningfully close personal relationship" provided that a quid pro quo or other mutually beneficial relationship existed. In so doing, the court reversed its previous position from *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014).

Kahn v. Stern, C.A. No. 12498-VCG, 2017 Del. Ch. LEXIS 158 (Ch. Aug. 28, 2017)

In a case arising out of the acquisition of a small aerospace manufacturing company, Kreisler Manufacturing Corporation, the Delaware Court of Chancery dismissed a post-close challenge to the deal on price, process, and disclosure grounds. Specifically, the Court held that a 20% interest in the company, in and of itself, did not implicate any liquidity concerns such that the 20% stockholder's decision to sell put him at odds with the rest of the stockholders. Moreover, insofar as there were any disclosure concerns, the standard a plaintiff must meet is much greater after the deal has been completed. Indeed, the disclosures might have supported pre-close injunctive relief, but the plaintiff had to (but did not) allege bad faith in order to pursue disclosure claims for damages after the deal had closed.

In re Wal-Mart Stores, Inc. Delaware Derivative Litigation, C.A. No. 7455-CB, supp. op. (Del. Ch. July 25, 2017)

In a stockholder derivative case that had been dismissed because of the outcome of other related litigation, the stockholder plaintiff tried to reinstate his case based on the argument that another court's decision at the preliminary stages should not bind a different stockholder plaintiff who presented much more detailed and thoroughly researched pleadings. The case has bounced back and forth between the Delaware Court of Chancery and the Delaware Supreme Court, and the trial court most recently advocated for the high court to adopt a rule that one court's dismissal would not preclude another court from entertaining the suit until after the complaint withstood a preliminary challenge regarding the stockholder's standing to bring the suit.

Employment Law
Forget the Labels—Know Your Rights

Many of the hard-working people in today's labor force have money and benefits taken from them in the workplace—by their own company. Misclassification of workers as independent contractors and improper application of overtime exemptions are ways that businesses attempt to unlawfully reduce labor-related expenses. Companies save thousands (and millions) of dollars each year by engaging in these practices, which result in wrongful denial of substantial benefits, rights, and pay. Most workers are simply unaware they're being improperly misclassified or exempted. Those aware are often afraid to complain, for fear of discipline or termination.

When in doubt, you should always seek the advice of an attorney to determine whether your employer is engaging in one of the illegal practices described below.

A. Exemptions to Overtime Pay

One way that businesses cut costs is by minimizing overtime pay. Employers typically achieve this by applying one of the several exemptions permitted by the Fair Labor Standards Act, as exempt employees are not entitled to overtime pay. These exemptions include "executive," "administrative," "professional," "computer employee," and "outside sales," among others. However, workers are not "exempt" merely because the employer labels them as such. For example, the following factors—each of which must be satisfied—determine whether an employee truly falls under the executive

(Continued on Page 4)

(Continued from Page 3)

exemption:

(1) The employee must be compensated on a salary basis (as defined in the regulations) at a rate not less than $913 per week (or $47,476 annually for a full-year worker);

(2) The employee's primary duty must be managing the enterprise, or managing a customarily recognized department or subdivision of the enterprise;

(3) The employee must customarily and regularly direct the work of at least two or more other full-time employees or their equivalent; and

(4) The employee must have the authority to hire or fire other employees, or the employee's suggestions and recommendations as to the hiring, firing, advancement, promotion, or any other change of status of other employees must be given particular weight.

Unless all of these factors are met, the employee does not qualify under the executive exemption, and he must be paid overtime (unless another exemption applies). As another example, the following factors define whether an employee truly falls under the commonly-applied administrative exemption:

(1) The employee must be compensated on a salary or fee basis (as defined in the regulations) at a rate not less than $913 per week (or $47,476 annually for a full-year worker);

(2) The employee's primary duty must be the performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and

(3) The employee's primary duty includes the exercise of discretion and independent judgment with respect to matters of significance.

Once again, unless each one of these factors is met, the employee must be paid overtime (unless another exemption applies). As with misclassifications, employers have substantial financial incentives to avoid paying overtime, which must be paid at a rate of one and one-half times the employee's regular rate of pay for all hours worked beyond 40 in a workweek (and in several states, beyond 8 in a single-workday).

B. Employees v. Independent Contractors

Businesses often characterize workers as "independent contractors" and treat them accordingly. This practice is, by itself, not improper. However, employers have significant financial incentives to maximize the number of workers classified as "independent contractors."

Unlike "independent contractors," workers characterized as "employees" typically receive costly benefits, which may include overtime pay, minimum wage, medical insurance, life insurance, 401(k), pension, holiday pay, sick pay, paid time off, family and medical leave, workers' compensation, unemployment insurance, salary increases, promotional opportunities, rights to appeal disciplinary actions, and more. For "independent contractors", these various benefits are denied, taxes are not withheld, and a Form 1099-MISC is provided at the end of each year, purportedly confirming that they are not employees.

But beware—a worker may truly be an "employee" despite being told they're not. The Fair Labor Standards Act, regulations and interpretations of the U.S. Department of Labor, and decisions of courts nationwide have made clear that companies may not simply place labels on workers, or pay them in certain ways or intervals, in order to avoid treating them as "employees." Rather, the following factors define the true relationship:

(1) the extent to which the work performed is an integral part of the employer's business;

(2) whether the worker's managerial skills affect his or her opportunity for profit and loss;

(3) the relative investments in facilities and equipment by the worker and the employer;

(4) the worker's skill and initiative;

(5) the permanency of the worker's relationship with the employer; and

(6) the nature and degree of control by the employer.

This analysis is not mechanically applied, and no one factor is determinative of whether a worker is truly an "employee" or an "independent contractor." Rather, these factors seek to determine the ***economic realities*** of the situation, in other words, whether a worker is economically dependent on the employer (*i.e.*, an "employee") or instead is in business for himself (*i.e.*, an "independent contractor"). Accordingly, the more vital an individual is to the business, and the more control the business exercises over the individual's work, the more likely that individual should be classified as an "employee."

If you have any doubt as to whether your employer properly classified you as an "independent contractor" or has properly denied you overtime on the basis of an exemption, you may be entitled to recover the amounts withheld from you, and potentially much more. To determine whether your rights may have been violated, contact attorney David A. Weisz in the Marietta, Georgia office of Johnson Fistel, LLP, either by email at DavidW@JohnsonFistel.com or by phone at (770) 200-3108. You can also contact Managing Partner Frank J. Johnson in the San Diego, California office, either by email at FrankJ@JohnsonFistel.com or by phone at (619) 230-0063.

Recent Accomplishments

Johnson Fistel Appointed Co-Lead Counsel in *Henstein v. Cempra, Inc.,* Case No. 1:16-cv-01303-TDS-JEP (M.D.N.C.): In a case alleging violations of the Securities Exchange Act of 1934 for the issuance of false and misleading statements, Johnson Fistel's client was appointed as co-lead plaintiff and the firm was appointed co-lead counsel under the Private Securities Litigation Reform Act of 1995. The complaint filed in the action alleges that defendants made false and misleading statements in connection with the safety of the Company's new drug candidate, solithromycin. The complaint further alleges that as a result of these false and misleading statements, Cempra stock traded at artificially inflated prices during the Class Period. Co-lead plaintiffs seek damages on behalf of themselves and all other persons or entities who purchased or otherwise acquired the common stock and call option of Cempra between July 7, 2015 and November 4, 2016, inclusive, and were damaged thereby.

Johnson Fistel Appointed Co-Lead Counsel in *In re United States Steel Corporation Derivative Litigation,* Lead Case No.: 2:17-cv-01005-CB (W.D. Pa.): Johnson Fistel was recently appointed co-lead counsel in a stockholder derivative action brought on behalf of U.S. Steel alleging, among other things, that certain executives and directors of U.S. Steel violated federal and state law by making false and misleading statements to investors, thereby artificially inflating the stock price. The complaint filed in the action also alleges that while the price of U.S. Steel stock was artificially inflated, certain corporate insiders engaged in unlawful insider trading of their personally-held U.S. Steel stock holdings. Plaintiffs seek damages and disgorgement from the alleged wrongdoers on the Company's behalf, as well as corporate governance reforms to prevent the recurrence of similar misconduct in the future.

Settlement Approved in *In re Journal Media Group, Inc. Shareholder Litigation,* No. 15-CV-9686 (Wis. Cir. Ct.): In a case arising out of the acquisition of communication company Journal Media Group, Inc., Johnson Fistel, acting as co-lead counsel, helped to secure significant relief for Journal Media stockholders through a settlement. The settlement addressed the claim that Journal Media's proxy materials were materially inadequate and misleading by providing for numerous additional disclosures, including previously omitted detail regarding the company's financial projections and information regarding the sales process. The court recently approved the settlement, holding that it conferred a substantial benefit to Journal Media's former stockholders.

Johnson Fistel Files Suit Against the City of Roswell, Georgia on Behalf of City Firefighters, *David Bible v. City of Roswell,* No. 2017-cv-294723 (Fulton Cnty. Super. Ct.): In a case arising out of the non-payment of benefits to City of Roswell firefighters, Johnson Fistel filed suit on behalf of the firefighters against the City. The plaintiffs allege, among other things, that the City breached its contracts with the firefighters by treating them as part-time personnel, and thus refusing to pay them valuable employment benefits, despite the fact that the firefighters worked as full-time employees.

Settlement Approved in *Krystek v. Ruby Tuesday, Inc., et al.,* No. 3:14-cv-01119 (M.D. Tenn.): A $5 million settlement in a securities fraud action against Ruby Tuesday, Inc. recently received final approval by a judge sitting in the United States District Court for the Middle District of Tennessee. The settlement was reached after extensive litigation. Johnson Fistel represented the court-appointed lead plaintiff and assisted lead counsel in prosecuting this matter.

Settlement Approved in *In re MobileIron, Inc. Shareholder Litigation,* Lead Case No. 1-15-cv-284001 (Santa Clara Super. Ct.): A $7.5 million settlement in a shareholder class action against MobileIron, Inc. recently received final approval by a judge sitting in the Superior Court of the State of California, for the County of Santa Clara. The settlement was reached after extensive litigation. Johnson Fistel represented one of the three plaintiffs in the consolidated class action and assisted lead counsel in prosecuting this matter.

Johnson Fistel appointed Lead Counsel in *In re Endologix, Inc. Shareholder Derivative Litigation,* No. 8:17-cv-01155-AB (PLAx) (C.D. Cal): On September 7, 2017, Johnson Fistel, LLP was appointed Lead Counsel in *In re Endologix, Inc. Shareholder Derivative Litigation,* No. 8:17-cv-01155-AB (PLAx), a shareholder derivative action filed in the United States District Court for the Central District of California. Endologix is a medical devices company based in Irvine, California. Plaintiffs in the case allege, among other things, that certain officers and directors of Endologix violated Section 14(a) of the Securities Exchange Act of 1934 and breached their fiduciary duties by causing the Company to issue various false and misleading statements and/or omitting material information from its public filings and communications with analysts and investors. The alleged false and misleading statement concern, among other things, Endologix's inability to obtain FDA approval in 2016 for its Nellix EVAS System, which was touted by the Company as a new and groundbreaking medical device for the treatment of abdominal aortic aneurysms.

About The Firm

Johnson Fistel is a firm built on the following five core values that every member embraces: trust, hard work, determination, integrity, and excellence in everything we do. Our interests are aligned with those of our clients. Their success determines our own. We embrace and embody those ideals in everything we do. Whether we're pursuing damages for or against a billion-dollar corporation or we're challenging a small transaction, Johnson Fistel devotes the necessary resources to secure the best result possible.

We believe we are only as good as our people, and Johnson Fistel recruits only the best and brightest and most determined candidates possible. Our lawyers include those who started their training by working for esteemed judges in both state and federal courts and have also worked at the largest law firms in the world. We pride ourselves on providing the same level of service with a greater level of efficiency. As a result, we have developed the reputation for delivering big-firm results with the efficiency and personal touch of a small firm.

Partners


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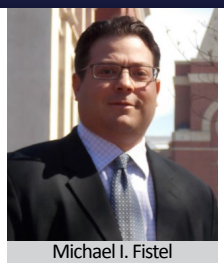
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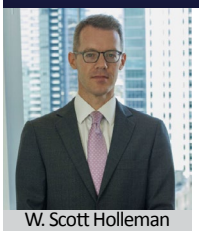
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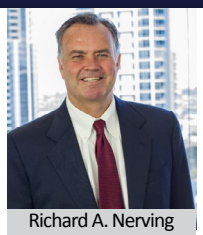
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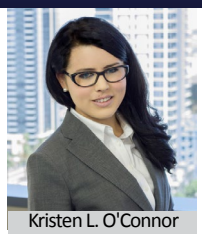
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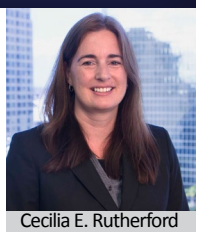
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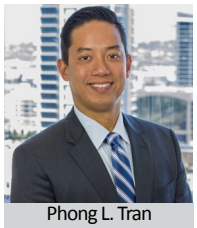
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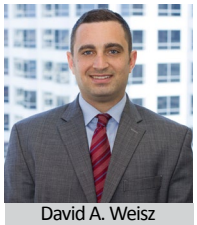
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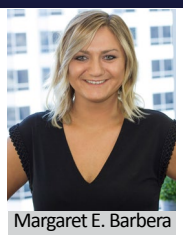
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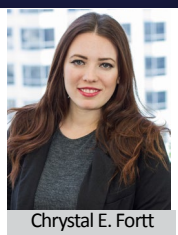
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