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Aruba Share Payout Cut 30% In $2.8B HP Tie-up Appraisal

By **Jeff Montgomery**

Law360 (February 15, 2018, 2:39 PM EST) -- Hedge fund investors lost big Thursday in a Delaware Chancery Court appraisal lawsuit that challenged the $2.8 billion price Hewlett-Packard Co. paid for Aruba Networks Inc. in 2015, when a judge pegged the fair value 30 percent lower than the acquisition payout.

Vice Chancellor J. Travis Laster, in a 129-page opinion, found that stockholders who held out and sued for a better deal should get $17.13 per share rather than the $24.67 actual payout or the $19.75 per share that Aruba later proposed in response to the deal challenge.

The opinion, which followed a three-day trial in December 2016, cited recent Delaware Supreme Court decisions that reversed Chancery Court opinions calling for payouts well above deal price for Dell's $25 billion take-private deal and DFC Global's $1.3 billion private equity buyout.

"The Delaware Supreme Court's decisions in Dell and DFC endorse using the market prices of a widely traded firm as evidence of fair value," Vice Chancellor Laster wrote. He cautioned later that "this decision is not interpreting Dell and DFC to hold that market price is now the standard for fair value."

Stuart M. Grant, lead counsel for the stockholders who sued, offered a blunt assessment of the ruling, which potentially slashed nearly $17.3 million from the per-share return for the largest investors in the suit, Verition Partners Master Fund Ltd. and Verition Multi-Strategy Master Fund Ltd.

"The Aruba opinion is theater of the absurd. But that was likely its intent. It shows how foolish the Delaware Supreme Court's opinions in Dell and DFC are when applied to other cases," Grant said. "The Nobel Prize in economics was awarded this year for a theory diametrically opposed to the one espoused in Dell."

The stockholders had been arguing for an $18 million higher price for their shares, based on a complex analysis of the company's current and future cash flows and guided in part by research questioning the expectation that markets always act rationally. A Nobel Prize was awarded last year to University of Chicago scholar Richard Thaler for his work in that area.

In a statement on Thursday, Aruba counsel Marc J. Sonnenfeld of Morgan Lewis & Bockius LLP said: "Aruba urged that its pre-transaction market price is the single most important mark of its fair value. We are gratified that the Chancery Court agreed."

While acknowledging some information leaks, confidentiality breaches and conflicts, the vice chancellor said the deal appeared “run-of-the-mill,” saying that “nothing about the deal structure could be considered exploitive” or a reason to look beyond the market. HP was not a controlling shareholder looking to squeeze out a minority, he said, insiders had no advantage, there were no clear conflicts, and both sides negotiated energetically.

Although the challenging stockholders cited a lack of competition as a reason to suspect the price, Vice Chancellor Laster said that Dell and DFC found that appraisal litigants needed to identify likely bidders willing to pay more. They were unable to do so in the HP-Aruba deal, he said, and were unable to show that incentives for completion of the deal tainted the outcome.

He found that synergies from the tie-up between the two companies could push the price to $18.20, and also found that Aruba might have failed to get a price that reflected those benefits. But he also found weaknesses in the synergy analysis that warranted sticking with the 30-day average market price.

An alternative valuation method called discounted cash flow analyses, or estimates of the present value of cash flows over time, varied widely between the two sides, Vice Chancellor Laster said. The shareholder method led to a $32.57 company valuation, while Aruba’s came back with a $19.75 estimate.

The Supreme Court, however, had cautioned that, while a DCF analysis can be used as a valuation substitute when there is a lack of credible market information, its weaknesses are subject to dispute and data gaps.

“Despite its seemingly sound methodology, these market indicators combine to create significant doubt regarding the reliability” of the method used by the challenging stockholders, the Vice Chancellor said.

“Forceful discussions” in the Dell and DFC opinions about reliance on valuations based on efficient capital markets justified giving market value substantial weight, the vice chancellor said.

“This approach does not elevate ‘market value’ to the governing standard under the appraisal statute,” Vice Chancellor Laster wrote. “The governing standard for fair value under the appraisal statute remains the entity’s value as a going concern.”

Appraisal actions under Section 262 of Delaware’s general corporation law can pay large dividends if a court chooses a higher price. Dissenting stockholders also receive interest on any gain from the appraisal at 5 percent plus the Federal Reserve discount rate, compounded quarterly from the date of the deal.

In the case of the two hedge funds, the difference between HP’s deal price and the alternative, higher fair value used in the hedge fund claim amounts to more than $18 million, based on the 2,288,234 shares held for appraisal in the suit.

The Verition funds are represented by Stuart M. Grant, Michael J. Barry, Christine M. Mackintosh, Michael T. Manuel and Rebecca A. Musarra of Grant & Eisenhofer PA.

Aruba is represented by Michael P. Kelly and Steven P. Wood of McCarter & English LLP and Marc J. Sonnenfeld, Karen Pieslak Pohlmann and Laura Hughes McNally of Morgan Lewis & Bockius LLP.

The case is Verition Multi-Strategy Master Fund Ltd. et al. v. Aruba Networks Inc., case number 11448, in the Court of Chancery of the State of Delaware.

--Editing by Emily Kokoll.