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IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE: APPRAISAL OF DELL INC.) Consol. C.A. No. 9322-VCL

RESPONDENT DELL INC.'S POST-TRIAL OPENING BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

PRELIMINARY STATEMENT 1

NATURE AND STAGE OF THE PROCEEDINGS 3

STATEMENT OF FACTS 4

A. Dell's Uncertain Future. 4

B. The Unchallenged Sales Process. 8

LEGAL STANDARD..13

ARGUMENT 14

I. THE MERGER PRICE REPRESENTS A VALUATION CEILING. 14

A. The Merger Price Is A Relevant Factor. 14

B. Petitioners' Efforts To Negate The Significance Of The Merger Price Are Poorly Grounded. 19

1. Structural Hurdles Did Not Deter Potential Bidders. 19

2. The MBO Process. 26

II. HUBBARD'S $12.68 PER SHARE VALUATION IS CREDIBLE, SUPPORTED BY THE EVIDENCE, AND SHOULD BE ADOPTED BY THE COURT. 28

A. A Properly Constructed DCF Yields A $12.68 Pinpoint Valuation. 29

B. Confirmatory Valuations Corroborate Hubbard's Opinion..........................35

III. CORNELL'S VALUATION IS UNRELIABLE AND SHOULD BE REJECTED. 35

A. Cornell's Model Incorporates Unrealistic Assumptions. 36

1. Projections..36

a. BCG Projections 38

b. Bank Case Projections 43

2. Tax Rates..44

3. Perpetuity Growth Rate and Investment..................................46

4. Discount Rate 48

5. Conversion From Enterprise To Equity Value 49

RLF1 13615299v.1

a. Required Cash 50

b. FIN 48 53

c. Residual U.S. Tax Liability 57

B. Cornell's Valuation Is Inconsistent With The Merger Price. 60

IV. PETITIONERS' ALTERNATIVE VALUATION INSUFFICIENTLY ADDRESSES FUNDAMENTAL ERRORS IN CORNELL'S VALUATION. 60

A. Terminal Tax Rate 61

B. Discount Rate...61

C. Required Cash..61

D. Residual U.S. Tax Liability 62

E. FIN 48 62

CONCLUSION 63

TABLE OF AUTHORITIES

Page(s)

Cases

In re Appraisal of Ancestry.com, Inc.,
2015 WL 399726 (Del. Ch. Jan. 30, 2015)....................17, 45, 46

Del. Open MRI Radiology Assocs., P.A. v. Kessler,
898 A.2d 290 (Del. Ch. 2006)....................58

Global GT LP v. Golden Telecom, Inc.,
993 A.2d 497 (Del. Ch.), *aff'd,* 11 A.3d 214 (Del. 2010)....................13

Golden Telecom, Inc. v. Global GT LP,
11 A.3d 214 (Del. 2010)....................16

Henke v. Trilithic Inc.,
2005 WL 399726 (Del. Ch. Oct. 28, 2005)....................46

Highfields Capital, Ltd. v. AXA Financial, Inc.,
939 A.2d 34 (Del. Ch. 2007)....................15, 16

Huff Fund Inv. P'ship v. CKx, Inc.,
2013 WL 5878807 (Del. Ch. Nov. 1, 2013)....................16, 17

Huff Fund Inv. P'ship v. CKx, Inc.,
2015 WL 631586 (Del. Feb. 12, 2015)....................17

LongPath Capital, LLC v. Ramtron Int'l Corp.,
2015 WL 4540443 (Del. Ch. June 30, 2015)....................17

M.G. Bancorporation, Inc. v. Le Beau,
737 A.2d 513 (Del. 1999)....................13

Merion Capital LP v. BMC Software, Inc.,
2015 WL 6164771 (Del. Ch. Oct. 21, 2015)....................17

Merlin P'rs LP v. AutoInfo, Inc.,
2015 WL 2069417 (Del. Ch. Apr. 30, 2015)....................17

Olson v. EV3, Inc.,
2011 WL 704409 (Del. Ch. Feb. 21, 2011) 18

Owen v. Cannon,
2015 WL 3819204 (Del. Ch. June 17, 2015) 29

Reis v. Hazelett Strip-Casting Corp.,
28 A.3d 442 (Del. Ch. 2011) 18

In re Rural Metro Corp.,
88 A.3d 54 (Del. Ch. 2014) 18

In re Rural/Metro Corp. Stockholders Litig.,
102 A.3d 205 (Del. Ch. 2014), *appeal dismissed*, 105 A.3d 990 (Del. 2014) 49

Union Illinois 1995 Investment Ltd. Partnership v. Union Financial Group, Ltd.,
847 A.2d 340 (Del. Ch. 2004) 15

Tri-Cont'l Corp. v. Battye,
74 A.2d 71 (Del. 1950) 13, 53

Statutes

8 *Del. C.* § 262 3

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PRELIMINARY STATEMENT

The sale of Dell was not a game. Real investors with real money spent substantial time and resources evaluating Dell's prospects in an evolving and turbulent market. Investors balanced management optimism with hard data pointing to the rapid growth of competitive products such as smartphones and tablets, the rise of low-cost competitors, the shift from on-site servers to cloud storage, and other threats to the current and future success of the business. They valued Dell based on what the market and their own analyses informed them about the Company and its prospects.

Dell's independent Special Committee similarly did not treat the sale of the Company as a game. The Committee carefully considered a range of strategic alternatives before agreeing to sell the Company. It canvassed the market to identify the most likely and best qualified potential suitors and engaged in a lengthy pre-signing sale process. It required Michael Dell to remain neutral during that process and to work in good faith with potential suitors. It negotiated seven price increases with Silver Lake and contacted more than seventy potential bidders during a go-shop that Petitioners concede was robust. In the end, the Committee obtained for stockholders a 28% premium over Dell's unaffected stock price.

By mischaracterizing the sale of Dell as a game, Petitioners attempt to deflect attention away from a process they do not challenge and a valuation they

cannot defend. Petitioners still have not provided, even after trial and initial post-trial briefing, a cogent explanation, indeed any explanation, as to why the most sophisticated investors in the world supposedly walked away from more than $26 billion in value *above* the merger price. To be sure, Petitioners portray the sale process as an "unwinnable game" that deterred bidding, but they have not presented evidence of such deterrence in the face of actual participants like Blackstone, TPG, KKR and others, nor have they quantified its incremental effect. Instead, they ask the Court to ignore the observable actions of real investors in favor of theoretical investors they cannot identify and imagined obstacles they will not quantify.

Consistent with that strategy, Petitioners press a valuation more than twice the merger price based on projections their expert will not endorse and bottom-line cost savings that ignore real world competitive pressures and performance. Petitioners use near-term tax rates for the terminal period even while acknowledging that those rates are based on deferral strategies. They posit a world in which Dell does not require *any* cash to run its operations and fail to consider billions of dollars of non-operating liabilities disclosed on Dell's balance sheet. They even press a discount rate based on inputs their expert describes as "idiosyncratic." The culmination of these errors is an unsupportable valuation of $28.61 per share.

Petitioners also advance an alternative valuation of $20.24 per share. While this revised calculation corrects some of the excesses associated with their prior valuation, it still contains fundamental errors contributing to an $11 billion deviation from the merger price.

Professor Hubbard, on the other hand, grounded his valuation in observable facts and evidence. He considered the markets in which Dell competes. He struck a balance between management optimism and market realism reflecting the operative reality of the Company on the merger date. He cross-checked his results with alternative methodologies to further confirm the soundness of his valuation. Hubbard's $12.68 per share valuation should be accepted as the fair value of Dell on the merger date.

NATURE AND STAGE OF THE PROCEEDINGS

This consolidated action was brought pursuant to 8 *Del. C.* § 262. On October 5-8, 2015, the Court held a four-day trial, at which it heard testimony from seven fact witnesses and five expert witnesses. Petitioners submitted their Post-Trial Opening Brief on November 18, 2015. Trans. ID 58168297. This is Respondent's Post-Trial Opening Brief.[1]

[1] The Court previously dismissed claims brought by other petitioners in Orders dated June 27, 2014, September 10, 2014, May 13, 2015 and July 28, 2015. Trans. IDs 55652563, 56013130, 57235523, 57235488, 57235442, 57235370, 57619862. A motion for summary judgment remains pending as to claims

STATEMENT OF FACTS

In its pre-trial brief, Dell discussed the markets in which it operates and the process leading to the transaction with Silver Lake.[2] Dell supplements its prior submission with a brief recitation of the trial evidence on those issues.

A. Dell's Uncertain Future.

Michael Dell founded Dell in 1984.[3] Over the next twenty-five years he and his team built the Company into one of the preeminent PC manufacturers in the world with annual revenue approaching $60 billion. In 2009, Mr. Dell concluded that "the business was changing, value was shifting into software and services, and we felt that we needed to go beyond just having products."[4] The Company then embarked on a transformation strategy to expand into the enterprise business.[5] As part of that strategy, the Company acquired eleven businesses to expand its portfolio and extend its core capabilities.[6]

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linked to shares voted in favor of the merger. Trans. IDs 57633321, 57738109.

2 RPTB at 3-25.

3 Tr. 425:10-426:1 (Dell).

4 Tr. 426:11-24 (Dell).

5 Tr. 138:17-19 (Mandl) ("the ESS business was part of the critical strategy to reposition the company away from the PC business into the enterprise business"); JX35 at 4-5; JX630 at 25.

6 JX69 at 28; JX907 at Appendix D.

Four years later, Dell found itself "in a difficult situation economically and competitively."[7] The Company confronted a tepid recovery from the financial crisis in the U.S., an emerging sovereign debt crisis in Europe and slowing growth in Asia.[8] It also faced serious long-term structural challenges in its primary business segments.[9]

In the PC market, tablet and smartphone sales (where Dell had virtually no presence) continued to take away PC business.[10] Dell also faced increased competition from Asian rivals such as Lenovo as the market shifted towards lower-end PCs, where Dell was not as strong.[11] Mandl testified:

> Clearly, Dell was not in a very strong spot at the time. The competitive landscape had shifted dramatically, or significantly for the last few years. The tablet, the new tablet environment had a strong impact on the company because Dell was not participating in that. It focused on the higher-end market, which was not growing. And the faster growing part of the business, or the PC business, was the value end or the lower end in emerging markets, and the company was not competitive in those segments of the market, mostly because of cost efficiencies.[12]

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7 Tr. 198:16-17 (Mandl).

8 JX896 at ¶¶ 21-24.

9 Tr. 241:5-243:12 (Sweet).

10 Tr. 72:18-73:13 (Cornell); JX896 at ¶ 27.

11 Tr. 70:16-72:11 (Cornell); JX896 at ¶ 32.

12 Tr. 137:17-138:8 (Mandl).

In the enterprise market, the shift from on-site servers to "cloud" storage transferred demand from brand name servers to low-cost "white-box" servers at a time when competitive pressures were already reducing margins.[13] In addition, "there were rumors that Google was going to enter the cloud business, in addition to Amazon and Microsoft."[14] This increased pressure on Dell at a time when "acquisitions were not quite as successful as was expected . . . ."[15]

In response to a question from the Court, Hiltz summarized Dell's outlook at the time of the merger:

> I think this was a pretty fundamental change that was occurring in the PC business. PC sales had been, you know, performing poorly for a period of time, and this was just another surprisingly large leg downward. I also think Dell's financial performance, not just in this quarter or this fiscal year, but for a while, had been deteriorating. Let's keep in mind that the PC business still reflected 65 percent of the revenue of Dell. So the enterprise businesses certainly had a better outlook, but you've got two-thirds of your business that is performing really poorly and, in fact, more poorly than anyone expects.

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[13] Tr. 139:10-14 (Mandl) ("the whole new world of the cloud environment developed, which very much was another competitive force against building an ESS type of business"); JX896 at ¶ 38.

[14] Tr. 452:12-21 (Dell).

[15] Tr. 139:5-9 (Mandl); 549:19-23 (Nicol) ("not only were the acquisitions underperforming, but they were acquired at a time after the interest in the market had peaked, so there was evidence that they had overpaid for some of the acquisitions."); JX865 at 67:10-14 (Gladden) ("We had a perception that . . . we were overpaying for acquisitions.").

> The other point I would make is that while the enterprise businesses were better than the PC business, this was not a world-class set of enterprise businesses, either. You know, they had spent $14 billion on acquisitions over the course of the past five years, and the company was only worth $14 billion. So this had not been a particularly good investment for Dell.[16]

These assaults on Dell's business resulted in a decline in consumer and market confidence in the Company's long-term prospects. Cornell wrote in an April 2013 blog post: "***As a consumer, do you want to buy a product from a company whose future is bleak? How comfortable do you feel buying a Dell computer today***?"[17] Analysts were equally bleak in their assessment: they reduced their price targets and cut their FY14 and FY15 EBIT forecasts from over $4 billion per year to just over $2 billion per year.[18] Even then, Dell consistently underperformed those forecasts.[19]

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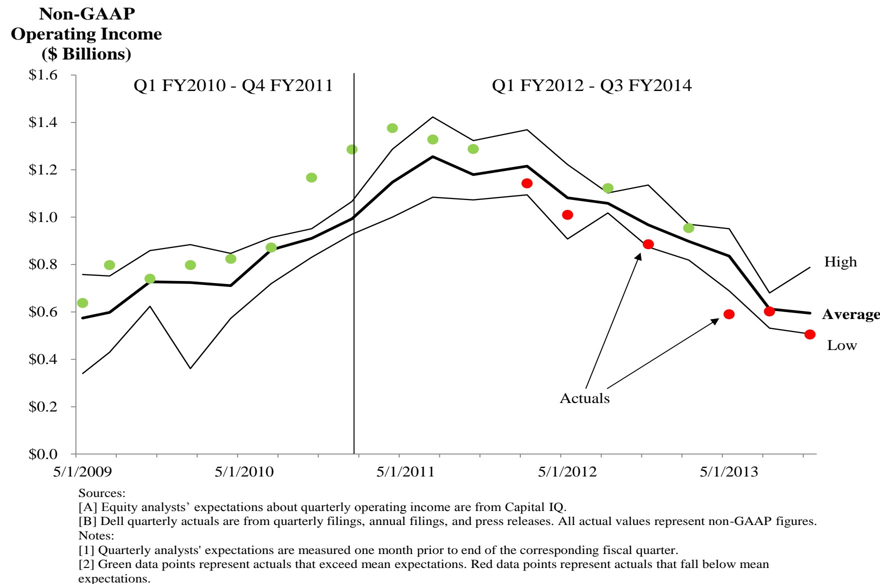
[16] Tr. 385:22-387:6 (Hiltz). On the enterprise side of the business, Dell faced "some of the largest and most successful technology companies: IBM, EMC, Microsoft, Oracle, a number of very strong competitors." Tr. 387:8-16 (Hiltz).

[17] Tr. 77:4-8 (Cornell), quoting B. Cornell, *Apple, Samsung and Google* (http://www.wbcornell.blogspot.com/2013_04_01.archive.html).

[18] JX896 at ¶ 88.

[19] *Id*. at ¶¶ 49-50 & Figures 8-9; JX569 at 24-25.

Dell's Quarterly Operating Income Versus Analysts' Forecasts



Throughout this period of change and uncertainty, the market calibrated management's optimism with a tempered realization that Dell was falling further behind in its performance. Mandl observed that "the company was struggling, had missed a number of expectations from a revenue point of view and from an earnings point of view. And clearly it was in the process of reassessing where it should go, because the current position was not working particularly well."[20] Dell's stock price hovered around $10.[21]

B. The Unchallenged Sales Process.

After Michael Dell approached the Company in August 2012 with an interest in exploring a going-private transaction, Dell's Board formed an

[20] Tr. 137:17-138:14 (Mandl).

[21] JX896 at ¶¶ 49-50; PTO at Ex. A.

independent Special Committee to (i) consider proposals to acquire the Company involving Mr. Dell and alternative proposals from other parties; (ii) engage independent legal and financial advisors; (iii) make a recommendation to the Board with respect to any proposed transaction; and (iv) review other strategic alternatives.[22] The Board resolved not to recommend a transaction for stockholder approval without a prior favorable recommendation by the Special Committee.[23] The Committee's entire focus was to achieve the best outcome for stockholders.

Guided by its advisors, the Special Committee evaluated strategic alternatives available to the Company.[24] The Committee also explored the possibility of continuing to execute management's long-term plan as a public company, potential changes to that plan, and adjustments to the management team.[25]

Mindful that Mr. Dell was a potential participant in a transaction, the Special Committee took additional steps to maintain a level playing field. Mr. Dell was

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[22] JX107 at 1-5.

[23] *Id*. at 3-5.

[24] These included a (i) leveraged buyout; (ii) separation of the Company's end-user computing and enterprise solutions and services businesses; (iii) sale of Dell Financial Services; (iv) spin-merger transaction involving the PC business and a strategic company; and (v) return of capital strategy through a share repurchase or cash dividend funded with new debt and/or existing cash. Tr. 151:8-153:1 (Mandl); JX168 at 2; JX182 at 1-2; JX230 at 2; JX344 at 58.

[25] JX233 at 2.

required to enter into a restrictive confidentiality agreement requiring that he work in good faith with other potential sponsors and later, a voting agreement.[26] The merger agreement contained an unaffiliated vote provision requiring that the merger be adopted by a majority of the shares not held by Mr. Dell and his affiliates.[27] Mr. Dell also was excluded from participating in the deliberations of the Special Committee and Board regarding the transaction[28] and committed that he would remain with the Company in the event stockholders failed to approve the transaction.[29] Finally, to help produce a higher bid, Mr. Dell agreed to take a lesser value for his own shares.[30]

During a pre-signing market canvass, the Special Committee invited multiple bidders into the process, including Silver Lake, KKR, and TPG. Mr. Dell

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[26] JX125; JX944; JX532 at 134-35; *see also* Tr. 144:15-22 and 159:11-18 (Mandl) ("So we made sure in the agreements that he would legally or contractually be supportive of working with other potential buyers, and he did so. And we also wanted to make sure that his voting shares would not be used to vote on his own situation, but he also committed to vote those shares on a pro rata basis for superior offers to whatever he might come up with."); 745:13-15 (Rajkovic) ("Michael commit[ted] at the very beginning that he would be available to any potential bidder.").

[27] JX532 at 51; JX349 at 31-32.

[28] JX532 at 53, 93, 124.

[29] JX549.

[30] Tr. 432:16-19 (Dell) ("they asked me to take a discount, a lesser amount for my shares, to break the impasse in order to effect the higher bid price, and I did agree to that."); JX532 at 49, 93.

"encouraged all the bidders to bid as high as they possibly could."[31] Even though Mr. Dell was close with KKR's principals, the firm withdrew from the process because it "could not get [its] arms around the risks of the PC business."[32] TPG, which also was close with Mr. Dell, dropped out of the process as well because "they felt that the cash flows attached to the PC business were simply too uncertain, too unpredictable to establish an investment case for them."[33] Notwithstanding those disappointments, the Special Committee negotiated multiple increases to the merger consideration despite indications from Silver Lake on at least two occasions that its proposal was a "best and final offer."[34]

The Special Committee also negotiated a 45-day go-shop during which the Company could solicit and negotiate with other potential bidders.[35] During that period, Evercore (which had a $30 million incentive to find a superior transaction) contacted 67 parties: 20 strategic parties (including HP), 17 financial sponsors, and 30 other parties.[36] The Committee also agreed to pay $25 million in expense

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[31] Tr. 465:8-9 (Dell); JX194, JX195.

[32] Tr. 438:1-439:5 and 440:13-14 (Dell); 174:3-7 (Mandl); JX224.

[33] Tr. 441:2-9 and 442:4-6 (Dell); 160:22-161:1 and 161:10-14 (Mandl).

[34] JX556 at 8, 10; JX320 at 1; JX327 at 2.

[35] JX349 at 46-47.

[36] JX424 at 4; JX369. Eleven parties expressed interest in a possible transaction. JX364; JX380; JX386; JX395; JX422.

reimbursement "to help level the playing field."[37] Those efforts led to "potentially superior proposals" from Carl Icahn and Blackstone.[38]

In April 2013, IDC reported a 14% decline in worldwide PC shipments.[39] Shortly thereafter, Blackstone withdrew from the process citing:

> (1) an unprecedented 14 percent market decline in PC volume in the first quarter of 2013, its steepest drop in history, and inconsistent with Management's projections for modest industry growth; and (2) the rapidly eroding financial profile of Dell.[40]

Despite this setback, the Committee negotiated a seventh increase in the merger consideration with Silver Lake.[41] Stockholders approved the merger on September 12, 2013, and the transaction closed seven weeks later on October 29, 2013.[42]

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[37] JX1209.

[38] Blackstone's team was led by Dave Johnson, a former Dell executive responsible for acquisitions and strategy, and included 463 individuals. JX465 at 4.

[39] JX1210 at 8-9.

[40] JX464 at 2; JX476; *see also* Tr. 384:15-19 (Hiltz) ("So Dell's financial conditions – condition was deteriorating very rapidly. They weren't meeting their projections. PC sales were falling out of bed. And so it wasn't surprising that Blackstone elected to drop.").

[41] JX654 at 31-33. Under the revised merger agreement, Silver Lake agreed to (i) increase the purchase price from $13.65 to $13.75 per share; (ii) provide for the payment of a $0.13 per share special dividend; and (iii) guarantee Dell's third quarter dividend of $0.08 per share. JX620 at 2; JX637.

[42] JX702; JX729 at 2.

LEGAL STANDARD

In an appraisal proceeding, the Court determines "the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value." 8 *Del. C.* § 262(h). The Court must "take into account all relevant factors." *Id.* Those include "market value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or which could be ascertained as of the date of merger and which throw any light on future prospects of the merged corporation." *Tri-Cont'l Corp. v. Battye*, 74 A.2d 71, 72 (Del. 1950).

"The entity must be valued as a going concern based on its business plan at the time of the merger, and any synergies or other value expected from the merger giving rise to the appraisal proceeding itself must be disregarded." *Global GT LP v. Golden Telecom, Inc.*, 993 A.2d 497, 507 (Del. Ch.), *aff'd*, 11 A.3d 214 (Del. 2010). "[B]oth sides have the burden of proving their respective valuation positions by a preponderance of the evidence." *M.G. Bancorporation, Inc. v. Le Beau*, 737 A.2d 513, 520 (Del. 1999).

ARGUMENT

I. THE MERGER PRICE REPRESENTS A VALUATION CEILING.

At the conclusion of trial, the Court requested that the parties address the role of the merger price in the valuation in this case.[43] As the Court will recall, Professor Hubbard concluded that the merger price represents a valuation ceiling in this case:

> In summary, I find the sale process to be very thorough and complete. From a finance perspective, it was designed to attract multiple qualified buyers and obtain maximum value for existing stockholders. There were active negotiations with three of the five largest private equity firms in the world, in addition to the negotiations with Silver Lake and several other potential buyers. Overall, the deal process resulted in a $2.66 (24 percent) improvement over the low end of Silver Lake's initial expression of interest ($11.22). The fact that no superior offers were received despite a thorough and rigorous process, with strong safeguards to assure Michael Dell's involvement did not discourage other potential bidders, supports the final deal price of $13.75 being a ceiling on the fair value for Dell.[44]

Hubbard's conclusion was evidentiary-based and legally sound.

A. The Merger Price Is A Relevant Factor.

Delaware law is clear that the merger price is a relevant factor in an appraisal proceeding where there has been an effective sales process.

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[43] Tr. 1040-46.

[44] JX896A at ¶ 125.

In *Union Illinois 1995 Investment Limited Partnership v. Union Financial Group, Ltd.*, then-Vice Chancellor Strine noted that the appraisal statute and case precedent empowered him to draw upon all "facts bearing on the market value of the subject company. This includes the transaction that gives rise to the right of appraisal, so long as the process leading to the transaction is a reliable indicator of value and merger-specific value is excluded. More generally, our case law recognizes that when there is an open opportunity to buy a company, the resulting market price is reliable evidence of fair value." 847 A.2d 340, 357 (Del. Ch. 2004).

Vice Chancellor Strine further observed: "[i]n view of the market's opportunity to price [the company] directly as an entity, the use of alternative valuation techniques like a DCF analysis is necessarily a second-best method to derive value." *Id*. at 359. He added: "[f]or me (as a law-trained judge) to second-guess the price that resulted from that process involves an exercise in hubris and, at best, reasoned guess-work." *Id*.[45]

The weight to be afforded to the merger price in an appraisal proceeding surfaced again in *Highfields Capital, Ltd. v. AXA Financial, Inc.*, 939 A.2d 34 (Del. Ch. 2007). After reviewing the sale process, the Court held that "the transaction giving rise to this appraisal action is a solid indicator of MONY's fair

[45] *See also* RPTB at 39-40 (collecting cases).

value, and the court finds reasonable and appropriate [respondent's expert's] decision to grant the merger price great deference in his valuation analysis." *Id.* at 60.

In *Golden Telecom, Inc. v. Global GT LP*, 11 A.3d 214 (Del. 2010), the Delaware Supreme Court held that it was inappropriate "to defer – conclusively or presumptively – to the merger price, even in the face of a pristine, unchallenged transactional process." *Id.* at 218. "Section 262(h) unambiguously calls upon the Court of Chancery to perform an *independent* evaluation of 'fair value' at the time of a transaction. It vests the Chancellor and Vice Chancellors with significant discretion to consider 'all relevant factors' and determine the going concern value of the underlying company." *Id.* at 217-18.

This does not mean the merger price is irrelevant in an appraisal proceeding. In *Huff Fund Investment Partnership v. CKx, Inc.*, 2013 WL 5878807, at *12 (Del. Ch. Nov. 1, 2013), the Court held that:

> The Supreme Court's holding is clear. The Court of Chancery has a statutory mandate to consider "all relevant factors" in conducting an appraisal proceeding, and, accordingly, the Supreme Court declined to impose a presumption systematically favoring one of those factors – merger price – over the others. The Petitioner's position here, that I should *ignore* the merger price in appraising CKx, is in my view directly at odds with the holding and rationale of *Golden Telecom,* which is that the Court of Chancery has an obligation to consider all relevant factors, and that no per se rule should

> presumptively or conclusively exclude any of those factors from consideration.

The Court then found that the "record and the trial testimony support a conclusion that the process by which CKx was marketed to potential buyers was thorough, effective, and free from any spectre of self-interest or disloyalty." *Id.* at *13. Accordingly, the Court held "that the process that generated the merger price supports a conclusion that the merger price is a relevant factor in determining CKx's fair value." *Id.* The decision was subsequently affirmed by the Delaware Supreme Court. *Huff Fund Inv. P'ship v. CKx, Inc.*, 2015 WL 631586 (Del. Feb. 12, 2015).

In four appraisal cases this year, the Court reached a similar result. *See In re Appraisal of Ancestry.com, Inc.*, 2015 WL 399726, at *23 (Del. Ch. Jan. 30, 2015) ("robust" sales process produced a more reliable determination of fair value than a DCF based on "problematic" projections); *Merlin P'rs LP v. AutoInfo, Inc.*, 2015 WL 2069417, at *17 (Del. Ch. Apr. 30, 2015) (merger price appropriate where "the market prices a company as the result of a competitive and fair auction"); *LongPath Capital, LLC v. Ramtron Int'l Corp.*, 2015 WL 4540443, at *20 (Del. Ch. June 30, 2015) ("in the situation of a proper transactional process likely to have resulted in an accurate valuation of an acquired corporation, this Court has looked to the merger price as evidence of fair value"); *Merion Capital LP v. BMC Software, Inc.*, 2015 WL 6164771, at *18 (Del. Ch. Oct. 21, 2015) ("Taking these

uncertainties in the DCF analysis – in light of the wildly-divergent DCF valuation of the experts – together with my review of the record . . . , I find the Merger price . . . to be the best indicator of fair value of BMC as of the Merger date.”).[46]

The foregoing decisions establish that the merger price is a relevant factor in this case. The appointment of the Special Committee and hiring of independent advisors, the neutralization of Michael Dell's shares, the pre- and post-signing market canvass including reimbursement of third-party fees, the negotiation of multiple bid increases, the absence of any preclusive deal protections, the participation of world-renowned private equity firms, and the unwillingness of any party to come forward with a topping bid following a widely publicized go-shop period all provide a real world check against an increased valuation calculated through some other methodology.

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[46] This Court also has recognized the importance of the merger price in several non-appraisal cases. *See Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 467 n.12 (Del. Ch. 2011) (“a transaction price [that] was forged in the crucible of objective market reality . . . is viewed as strong evidence that the price is fair”); *Olson v. EV3, Inc.*, 2011 WL 704409 at *10 (Del. Ch. Feb. 21, 2011) (“[i]n an arms-length, synergistic transaction, the deal price generally will exceed fair value because target fiduciaries bargain for a premium that includes both a share of the anticipated synergies and a portion of the reduced agency costs”); *In re Rural Metro Corp. S'holders Litig.*, 88 A.3d 54, 102 (Del. Ch. 2014) (“[o]rdinarily this court places heavy reliance on the terms of a transaction that was negotiated at arm's length, particularly if the transaction resulted from an effective pre—or post-agreement market canvas.”).

B. Petitioners' Efforts To Negate The Significance Of The Merger Price Are Poorly Grounded.

In an attempt to negate the significance of the merger price, Petitioners offer two theoretical retorts: (i) "structural hurdles created an unwinnable game that rationally deterred putative competitive bidders from submitting topping bids no matter how much the valuation gap"[47]; and (ii) the "MBO process is not designed to yield a price reflective of fair value."[48] Both theories are wrong.

1. Structural Hurdles Did Not Deter Potential Bidders.

Petitioners assert that the merger price should be disregarded because it does not reflect Dell's intrinsic value. For support, they cite testimony from Subramanian to the effect that a disparity between the merger price and fair value *could* exist as a result of (i) information asymmetries; (ii) a "ticking clock" problem; (iii) valuable management; and/or (iv) incentives that deter a topping bid.[49] Petitioners' reliance on that testimony is misplaced.

First, Subramanian never "assessed whether there was a disconnect between the market price and the intrinsic value" of Dell stock.[50] Subramanian never formed an opinion as to the value of Dell or the impact of his factors on Dell's

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[47] POB at 42.

[48] POB at 52.

[49] POB at 43-52.

[50] Tr. 825:8-12 (Subramanian) (Q. . . . Now, you have not tried in your report in this matter to assess whether there was a disconnect between the market price and the intrinsic value of Dell stock in this case; correct? A. Correct.").

transaction price.[51] He was not even asked by Petitioners to assess how unlevel the playing field allegedly was as a result of his four factors.[52] Subramanian further testified that he was not offering opinions about the process run by the Special Committee or anything it should have done differently, and he distanced himself from any claim that the transaction was opportunistically timed, that management "did anything to talk down the stock price," or that it "engaged in any sort of manipulation."[53] Subramanian does not explain the $26 billion chasm between Cornell's valuation and the merger price.

Second, Subramanian's theories are untethered to actual evidence in this case.

> ***Information Asymmetry***: Petitioners speculate that as a result of Mr. Dell's knowledge of the Company, an information asymmetry existed that deterred bidders from participating in the process.[54] Petitioners claim this asymmetry resulted in a "winner's curse" in which nobody played an "unwinnable game." Petitioners do not identify the information advantage that supposedly existed, how it was unascertainable to other bidders, or even if it would have resulted in a different valuation.

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[51] Tr. 827:5-8 (Subramanian).

[52] Tr. 890:10-13 (Subramanian).

[53] Tr. 862:17-863:2 and 833:19-834:21 (Subramanian).

[54] POB at 44-46.

In addition, apart from the fact that the claim is so hopelessly vague that it could be asserted in a challenge to virtually any transaction, the claim is counterfactual. Potential bidders had an equal opportunity to partner with Mr. Dell on a transaction as he committed from the outset to "explore in good faith the possibility of working with any such potential counterparty or financing source. . . ."[55] Silver Lake, TPG, and KKR were on equal footing during the pre-signing market check and Mr. Dell was equally available to Blackstone and nearly a dozen others who were evaluating the Company during the go-shop period.[56] Blackstone even had the insight of Dell's former head of M&A and strategy leading its team.

Moreover, Subramanian conceded that bidders might negate any information asymmetry through their own diligence or industry knowledge.[57] Bidders also might value Mr. Dell's leadership differently, especially given the Company's poor record in forecasting and its failure to anticipate trends in the PC market.

Finally, Petitioners do not identify any bidder who was deterred as a

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[55] JX125 at 2.

[56] Tr. 847:15-19 (Subramanian) ("Q. Now, you have no reason to believe that any bidder who actually signed a confidentiality agreement and asked for access to management didn't get what it asked for. Correct? A. I have no evidence to that effect.").

[57] Tr. 856:12-15, 859:21-860:4 and 861:2-5 (Subramanian).

result of a perceived information disadvantage. Any information asymmetry, real or imagined, clearly did not dissuade Silver Lake, TPG, KKR, Blackstone, Francisco Partners, Insight Venture Partners, Riverwood Capital, GE or Carl Icahn from playing the "unwinnable game."[58]

Ticking Clock: Petitioners next speculate that the "ticking clock created a powerful disincentive for competing bidders to enter the ring."[59] According to Petitioners, the "sheer size of the Dell deal" created a ticking clock problem that "cannot seriously be disputed."[60] They are wrong. Petitioners ignore the pre-signing market check and Subramanian disclaimed knowledge whether the 45-day go-shop window was a deterrent to anyone "with the capital and sophistication to buy an asset as large and as valuable as Dell."[61] He also would not opine as to the difficulty of forming a consortium to purchase Dell.[62] The fact that Blackstone and Icahn both reached excluded party status demonstrates that the 45-day period was not preclusive. Hiltz further undercuts Petitioners' argument with his observation:

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[58] JX532 at 55-57, 59.

[59] POB at 46-48.

[60] POB at 47.

[61] Tr. 864:4-8 (Subramanian).

[62] Tr. 847:10-14 (Subramanian).

> [W]hat you had to accomplish in the 45 days of the go-shop was a relatively limited number of things. You just had to submit a letter. You were then going to have a period of several months between the end of the go-shop right up until the shareholder vote to spend as much time as you wanted doing due diligence, to arrange your financing, to do all of those things and get to submitting a superior proposal. We felt that that was more than enough time.[63]

Valuable Management: Petitioners next suggest that "[t]hird parties considering a bid undoubtedly were aware that MSD could refuse to sever ties with Silver Lake, giving them yet another reason to decline to get involved,"[64] but they offer no evidence that this concern influenced any prospective bidder. Strategic investors and others who did not view Mr. Dell as essential to their bid would not consider this an obstacle,[65] and the record is unequivocal that Mr. Dell was prepared to work with any potential bidder and in fact did so.[66] Thus, bidders who valued Mr. Dell knew that he was obligated to cooperate in their diligence efforts and work with them in

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63 Tr. 377:2-10 and 365:10-366:11 (Hiltz).

64 POB at 48-49.

65 Tr. 865:2-6 (Subramanian) ("Q. And we agree that if the management team isn't especially valuable, uniquely valuable, then the other obstacles you identify largely evaporate. Fair? A. Yes.").

66 Tr. 159:11-18 (Mandl) ("it was certainly an important part of the discussion that he was prepared to work with others"); JX224 ("Had a full conversation around alternatives, and his willingness to join up with whoever.").

good faith if requested. Mr. Dell also understood that he might not be part of the winning bid and was prepared to accept that outcome.[67]

M. Dell Incentives: Petitioners finally suggest that because Michael Dell was a net buyer in the transaction, he "had powerful incentives to discourage a topping bid."[68] In fact, he testified that he understood that the Special Committee would not sell the Company unless it received a high bid and he further promised that he would seek to maximize the price to the stockholders.[69] Petitioners do not cite evidence suggesting that Mr. Dell did anything to discourage a higher bid. Subramanian also did not question the subjective good faith of Mr. Dell, who was obligated to support a superior proposal,[70] in working with potential bidders. Instead, Petitioners argue that "every $1 increase in deal price would cost him approximately $250 million if debt and equity contributions increase proportionately, or over $1 billion if debt was held constant."[71] Strategic investors – such as HP – which did not need Mr. Dell's participation were not deterred from submitting a topping bid if they thought Dell was undervalued. Even a bidder looking to partner

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[67] Tr. 434:16-435:2 (Dell).

[68] POB at 49.

[69] Tr. 432:13-433:5 and 455:7-456:1 (Dell).

[70] Tr. 853:22-854:2 and 850:13-16 (Subramanian); JX944.

[71] *Id*.

with Mr. Dell would not be meaningfully deterred from doing so because it could always offer him the same economics simply by increasing the value for his exchanged shares, adjusting the equity structure or by increasing the amount of debt undertaken in the transaction.[72]

Third, Petitioners never quantify the magnitude of these supposed structural hurdles.[73] Subramanian did not attempt to evaluate whether they represent "a big hill or a small one, big speed bump, little speed bump."[74] He did not "quantify the magnitude of the information asymmetry."[75] Instead, he acknowledged that the Special Committee took affirmative steps to reduce the significance of the hill by providing expense reimbursement to bidders, limiting Silver Lake to a single match right, and incentivizing Evercore to obtain a superior proposal.[76] Accordingly, when pressed by the Court, Subramanian conceded that the go-shop in this case has "some probative weight" to the value of the Company.[77]

Even if a hill existed (and it did not), Hubbard used Subramanian's own academic research to show that the perceived hill was not as steep or daunting as

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[72] As an example, a $0.10 bump in price resulting in an additional $170 million in debt on the transaction would not deter any serious bidder.

[73] Tr. 880:12-15 (Subramanian).

[74] Tr. 828:3-13 and 843:8-15 (Subramanian).

[75] Tr. 862:11-16 (Subramanian).

[76] Tr. 796:4-16 (Subramanian); 372:22-373:10 (Hiltz).

[77] Tr. 896:6-8 (Subramanian).

Petitioners suggest. Hubbard demonstrated that the go-shop in this case exceeded the parameters of successful go-shops identified by Subramanian in his 2008 study.[78] He also showed that although the standard gap between LBO and MBO premia was on the order of 4-5%, the merger price in this case left no gap compared to a standard LBO.[79] In other words, Petitioners' theory is just wrong.

2. The MBO Process.

Petitioners next state that the MBO process is inherently "not designed to yield a price reflective of fair value."[80] They claim that a MBO model "has nothing to do with a company's fair value" and that "the fact that no one would pay a price approaching what Dell was worth under a DCF analysis in the context of an MBO is no reason to question the reliability of a DCF valuation of Dell."[81] Aside from its circularity, this argument is poorly grounded.

As a starting point, Petitioners' theory does not explain why strategic investors did not submit a topping bid if Dell was wildly undervalued. The theory also does not make economic sense. Both a DCF and MBO model utilize the same cash flows. A DCF model focuses on the cash flows available to the firm's sources of capital and discounts them at the WACC rate. A MBO model allocates

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[78] Tr. 672:18-673:10 (Hubbard); Hubbard Demonstrative 19.

[79] Tr. 673:11-674:13 (Hubbard); Hubbard Demonstrative 20.

[80] POB at 52.

[81] POB at 52-53.

the same cash flows to each source of capital, and the proposed offer price is used to calculate a projected IRR to the equity investors, which is then compared to a desired hurdle rate. Because both models rely on the same cash flows, a MBO model should support the same enterprise value result on a risk-adjusted basis as a DCF model, if the MBO model were oriented toward solving for enterprise value, which it is not.

Finally, Petitioners argue that an October 2012 presentation by JPM to the Special Committee proves their point as the two models produced different valuations.[82] Not so. The two models were based on different assumptions, which led to an inflated DCF value relative to the MBO offer price.

- The MBO model assumed an exit multiple equal to the initial EBITDA multiple, whereas the DCF model assumed an implied expansion of the EBITDA multiple.
- The MBO modeled a tax rate of 25.3% for FY14 and 30.1% for FY15-18, whereas the DCF modeled a tax rate of 21%.
- The MBO model assumed $2.8 billion in repatriation tax, whereas the DCF model did not include any repatriation tax.

[82] POB at 54.

- The MBO model reflects $5 billion in required cash, whereas the DCF model did not account for required cash.[83]

In the end, Petitioners simply cannot explain why investors walked away from more than $26 billion in value *above* the merger price. As Cornell states in his own writings: "[a] market that is not perfectly efficient may still value securities more accurately than appraisers who are forced to work with limited information and whose judgments by nature reflect their own views and biases."[84] For that reason, he cautions that "appraisers should not substitute their own judgment for that of the market."[85] The merger price represents a valuation ceiling in this case.

II. HUBBARD'S $12.68 PER SHARE VALUATION IS CREDIBLE, SUPPORTED BY THE EVIDENCE, AND SHOULD BE ADOPTED BY THE COURT.

Hubbard provided three reports and expert testimony concerning the fair value of Dell's shares.[86] His reports are detailed and extensively sourced from both the evidentiary record and public domain. Hubbard concluded that the fair value of Dell as of the merger date was $12.68 per share.[87]

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[83] JX650.

[84] Cornell, *Corporate Valuation*, at 46.

[85] *Id*. at 47.

[86] JX896A; JX907; JX907A.

[87] Tr. 597:1-3 (Hubbard).

A. A Properly Constructed DCF Yields A $12.68 Pinpoint Valuation.

Hubbard performed a DCF to value Dell. "[T]he DCF . . . methodology has featured prominently in this Court because it 'is the approach that merits the greatest confidence' within the financial community." *Owen v. Cannon*, 2015 WL 3819204, at *16 (Del. Ch. June 17, 2015) (quoting *Cede & Co. v. JRC Acq. Corp.*, 2004 WL 286963, at *2 (Del. Ch. Feb. 10, 2004)).

As with many appraisal cases, a significant issue in this case concerns the selection of projections. Both Hubbard and Cornell agree that projections prepared by management in July and September 2012 were outdated as of the merger date more than a year later.[88] Both also agree that management's record in forecasting the business in the changing market environment was poor.[89] The challenge was finding an appropriate set of alternative projections.

For his part, Hubbard selected projections prepared by BCG in January 2013 as the foundation for his DCF analysis. The Special Committee tasked BCG with providing an independent and objective view as to the Company's likely future performance if it were to remain a publicly held entity.[90] BCG developed and

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[88] Tr. 601:6-21 (Hubbard); 89:7-90:16 (Cornell); JX238 at 2; JX806A at 76-85; JX897A at 32-35, 59-60.

[89] Tr. 75:7-11 (Cornell); JX896A at ¶¶ 49-50 & Figures 8-9.

[90] Tr. 149:2-6 (Mandl) ("given the question around those plans in terms of being overly optimistic, we felt it would be useful to have an external management

refined a detailed forecast model based on the Company's then-current business mix and geographical distribution.[91] BCG's Base Case was predicated on delivering financial performance "given market forces, given the company's position, and if the company continued to perform and continued to execute the strategy that they were in . . . ."[92] BCG also developed sensitivity forecasts reflecting the incremental effect of certain management initiatives. When the BCG projections were prepared, the BCG 25% Case was widely acknowledged by transaction participants as the most reasonable and realistic set of projections, although they later turned out to be overly optimistic.[93]

Hubbard's decision to use the BCG projections in his DCF model was not without its challenges. The PC market continued to deteriorate between the time the BCG projections were prepared and the merger date.[94] The Company's margins also were under duress from price competition even as Dell was

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consulting firm reassess those plans and give us their perspective from an external point of view."); JX238 at 2.

[91] JX532 at 100.

[92] Tr. 490:12-491:2 (Ning).

[93] Tr. 504:14-16 and 505:11-15 (Ning) ("given what we knew at the time, we thought that the most achievable was the 25 percent case."), 424:8-17 (Hiltz); JX335 at 5 (noting Evercore's view "that the BCG 25% productivity case represented the most likely scenario" and that JPM "independently reached the same conclusion regarding the BCG 25% productivity case.").

[94] Tr. 391:12-392:1 (Hiltz) ("the most significant thing that had changed was the continued deterioration in the company's business. . ."); 508:1-5 (Ning); JX464; JX569 at 10; JX1211.

attempting to shore up its market share.[95] Dell also was implementing a $3.3 billion cost savings program during this period.

Hubbard carefully considered the appropriateness of the BCG projections in light of these changes.[96] He reviewed BCG's detailed spreadsheets and discussed the projections with the BCG personnel who prepared them.[97] Rather than discard the only remaining projections prepared for operation as a public company, Hubbard concluded that they could form the basis for his DCF with a few necessary modifications.

Hubbard addressed the continued deterioration of the PC market by looking to the most recent release of the IDC data used by BCG in its modeling.[98] At the time BCG prepared its model in January 2013, the August 2012 data was the most recent IDC data available; at the time of the merger, the August 2013 data was

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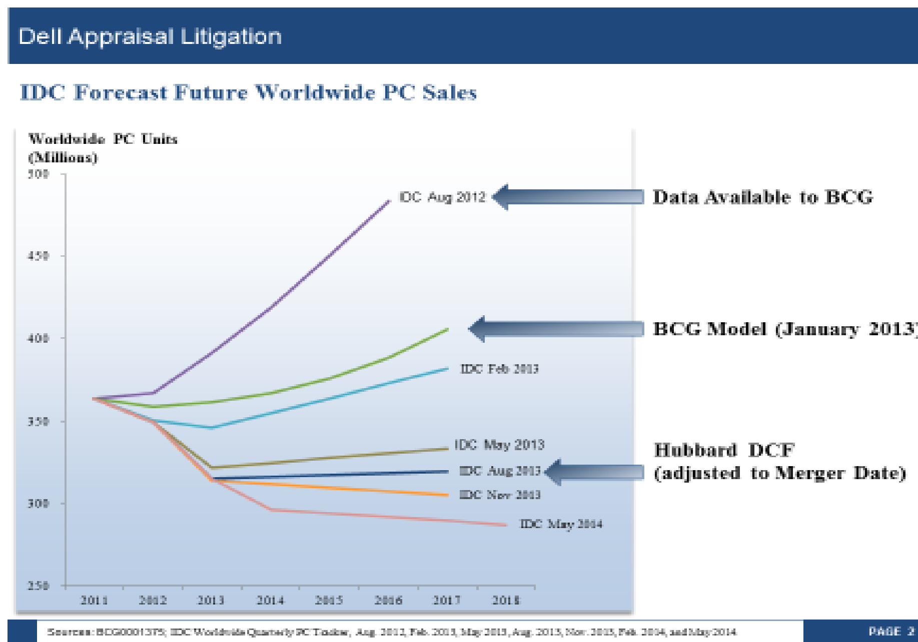
[95] Tr. 247:16-248:9 and 258:8-15 (Sweet); JX460 at 62.

[96] JX896A at ¶ 135.

[97] JX896A at ¶ 156.

[98] Tr. 603:17-19 (Hubbard) ("What I did was essentially adopt the BCG structure but bring it forward to more contemporary data."); JX896A at ¶¶ 192-94. Because of the way BCG created its model, this adjustment also required an adjustment to the model's Support & Deployment revenue. Tr. 608:-9-609:3 (Hubbard); JX896A at ¶¶ 195-96. Hubbard used the same attachment rate provided to BCG by Dell. Tr. 495:19-23 and 523:21-24 (Ning); Hubbard Demonstrative 3; JX907 at ¶¶ 42-43.

available.[99] The data showed that the PC market had further shifted and declined to an extent not foreseen when BCG prepared its model.[100]



Hubbard also reviewed details surrounding Dell's cost savings programs.[101] That led to several important conclusions.

- ***First***, while Dell had achieved a certain degree of success in cutting costs, that success did not translate to improved bottom line financial performance on a dollar for dollar basis, and certainly not into

[99] Tr. 603:19-21 (Hubbard); JX896A at ¶¶ 192-94.

[100] Tr. 604:21-606:2; Hubbard Demonstrative 2. Ning testified that BCG did not simply insert the August 2012 IDC numbers into its January 2013 model, but used judgment in estimating the impact of market changes between the August 2012 and January 2013. Tr. 522:18-523:2 (Ning). Hubbard did not need to make these subjective judgments because he had the more contemporaneous August 2013 IDC reports at the time of his valuation.

[101] JX907 at ¶¶ 60, 68-84.

perpetuity.[102] As Hubbard explained, that did not mean that the cost savings were not real, but rather that they were offset by other factors (price concessions, investment, etc.).[103]

- ***Second***, investors did not expect cost savings to translate to billions of dollars of additional operating income.[104]
- ***Third***, while Sweet testified that he hoped that cost savings designated for investment would ultimately be value creating, declines in Dell's pricing exceeded the total amount of the cost savings.[105] Sweet testified that competitive pressures required Dell to lower its prices and make up the difference from savings achieved in its cost savings program.[106]

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[102] Tr. 264:8-265:17 and 273:10-15 (Sweet); JX907 at Figure 10.

[103] Tr. 613:11-614:19 and 617:7-619:18 (Hubbard); JX807 at 19.

[104] Tr. 622:16-24 (Hubbard); JX907 at ¶¶ 76, 77, 80.

[105] Tr. 626:2-628:16 (Hubbard); JX758 at 72.

[106] Tr. 246:21-249:11 (Sweet) ("The way we thought about it was that if we were going to go try and accelerate on share, which generally meant that we would have to put product into different price bands or lower price bands, as well as become more aggressive in our pricing, while continuing to build the solution capabilities, it was pretty evident that we were going to need to try and -- we were going to need to take the cost out of the business, that we were going to have to reduce spending in certain areas of the business and try and manage the P&L in such a way that, even as we were reducing pricing, and/or investing in the solutions business, that we were funding that, essentially, through some of the cost-out activities.").

- ***Fourth***, neither the additional cost savings nor the gross margin decline were modeled in BCG's Base Case.[107]

Ultimately, notwithstanding Dell's record on cost savings, Hubbard modeled that $810 million of cost savings would fall annually to the bottom line in the BCG model.[108] That far exceeded the $0.29 per share impact expected by investors and analysts when the program was announced.[109]

Hubbard next determined Dell's cash flows for the post-projection period to arrive at his terminal value. Hubbard used a three-stage model incorporating a 5-year transition period to allow for normalization of cash flows, a 2% perpetuity growth rate with appropriate investment and a 35.8% terminal tax rate recommended by Professor Shay.[110] The terminal period cash flows combined with the projection period cash flows produce an enterprise value, which was then converted to an equity value by accounting for non-operating claims on Dell's balance sheet.[111] The end result was a fair value conclusion of $12.68 per share as of the merger date.

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[107] Tr. 492:3-11 and 495:24-496:22 (Ning).

[108] Tr. 630:23-631:7 (Hubbard).

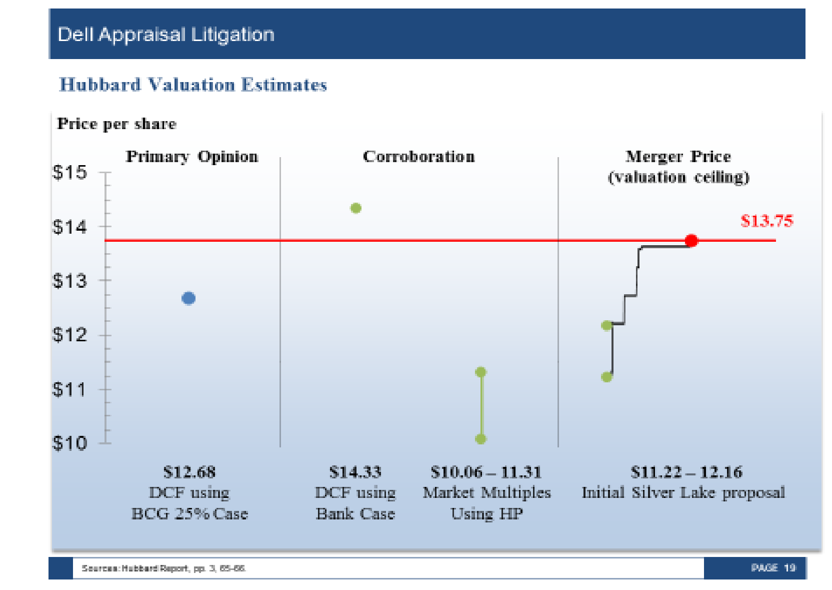
[109] Tr. 622:16-24 (Hubbard); JX907 at ¶¶ 60, 68-84.

[110] JX896A at ¶¶ 200-23; JX922 at ¶¶ 41-46.

[111] JX896A at ¶¶ 129-30, 260, 275.

B. Confirmatory Valuations Corroborate Hubbard's Opinion.

Hubbard confirmed the validity of his valuation by reviewing other methodologies and market indicators, including the merger price, analysts' projections, a DCF valuation based on the Silver Lake projections, and a comparable companies analysis.[112] In each case, the results corroborated his opinion.[113]



III. CORNELL'S VALUATION IS UNRELIABLE AND SHOULD BE REJECTED.

Brad Cornell concluded that the fair value of Dell's shares as of the merger date was $28.61 per share. Although a respected economist, Cornell was placed in an untenable position by being asked to base his valuation on a set of assumptions that he did not test and would not endorse. As a result, he could not explain the

[112] JX896 at 146-58.

[113] Hubbard Demonstrative 19.

huge disparity between his valuation and the market price, and conceded that the market and investors did not ascribe as much value to the projections as he did.[114] His valuation is unreliable and should be rejected.

A. Cornell's Model Incorporates Unrealistic Assumptions.

Cornell's DCF model contains five major errors which undermine its validity.[115]

1. Projections

The most significant error impacting Cornell's valuation resulted from his selection of projections. Cornell conceded that "the goal is to find the most reasonable and realistic set of projections for the company that's being valued."[116] Nevertheless, he made no effort to determine whether the projections used in his DCF analyses were reasonable or realistically achievable.[117] Instead, Cornell mechanically calculated an output from projections provided to him by counsel.[118]

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[114] Tr. 58:16-17 ("I'm afraid I really don't have an explanation"), 108:8-12.

[115] Hubbard's Rebuttal Report identifies several other errors in Cornell's model, but they are smaller in magnitude than the major errors discussed herein. JX907A.

[116] Tr. 84:17-22 (Cornell).

[117] Tr. 104:2-3 (Cornell) ("I am not assessing whether or not those projections were correct."); JX920 at 215:22-25 (Cornell) ("Q. . . . And you haven't made the determination as to the reasonableness of those projections, have you, sir? A. No."). Cornell opined that the difference between his valuation and the merger price reflects a disagreement between a "pessimistic view of the market and some of the buyers" and an "optimistic view of the company and its advisors." Tr. 61:8-24 (Cornell). He modeled the latter even though he admitted that he is

At trial, Cornell attempted to justify this omission by implying that he was relieved of any such obligation because the projections used in his model were prepared by "professional people" who had "access to the company."[119] When pressed on this assertion by the Court, Cornell retreated to the position that "they might not be projections that you will ultimately accept, but they were clearly professionally done, very carefully vetted, and a lot of time and energy went into them with trained people."[120]

Cornell's response to the Court's inquiry was not helpful. Projections do not become reliable or realistically achievable simply because they are prepared by professionals. Dell management prepared projections in July 2012 and September 2012, yet nobody in this case – *including* Cornell – contends that those projections reflect Dell's operative reality as of October 29, 2013.[121] Cornell cannot incorporate projections into a DCF model and then disavow any obligation to

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"not enough of an expert on Dell's business to tell you who is right." Tr. 62:9-13 (Cornell).

[118] Tr. 88:13-17 (Cornell) ("Q. In fact, what you did was value a set of assumed projections. Correct? A. Correct. . .").

[119] Tr. 86:6-87:12 (Cornell).

[120] Tr. 87:20-88:3 (Cornell).

[121] Tr. 89:7-90:16 (Cornell), 601:17-21 (Hubbard).

assess the reasonableness of those projections, particularly since his "valuation depends centrally on the projections."[122]

a. BCG Projections

Cornell apportioned half his valuation to a DCF based on the BCG projections. Cornell bypassed the projections in the BCG Base Case and instead allocated equal weight to the 75% Case and the 25% Case.[123] In doing so, he anchored one end of his BCG valuation to projections for which there is no credible support.

JPM characterized the 75% Case projections as "aspirational at best."[124] Rajkovic explained:

> [A] 75 plan did not seem realistic, at least to us. It meant that the company was going to be able to operate their PC business well above where it had historically. And especially in the context of what was going on in the industry, that business was running around 5 percent operating margins.
>
> And Lenovo had just announced it was going to come in and compete at the high end and mid end, where most of our business was or Dell's business was. Lenovo runs 2 1/2 percent operating margin. So you're having entrants come in that run at a much lower cost base or operating margins, a lot more aggressive on pricing.

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[122] Tr. 88:23-89:5 (Cornell).

[123] Tr. 105:5-8 (Cornell); JX897 at ¶ 18.

[124] JX621 at 9; *see also* JX896A at ¶¶ 172-75; JX907 ¶¶ at 57-64.

> HP was coming into our space. The market was deteriorating. It was really hard to see how they would take the margins to the level that that plan implied.[125]

The Special Committee expressed "doubt as to whether the productivity cost reductions reflected in the BCG 75% Case . . . [were] realistically achievable" because "the [assumed] cost reductions . . . would imply margins in fiscal year 2016 . . . higher than those ever achieved by the Company or its principal competitors."[126] And, of course, no bidder considered those projections credible, as reflected by the absence of a topping bid.

Cornell defended his use of these projections as a way to create a 50% Case.[127] However, Cornell did not assess whether a 50% Case was reasonable or realistically achievable, but left that task to Petitioners who, in turn, argue that the Cornell-created projections are appropriate because Dell achieved $1.6 billion in cost savings in FY14.[128] They ignore that Dell's financial performance was influenced by a number of real world influences which were not reflected in Cornell's static model.

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[125] Tr. 739:2-20 (Rajkovic).

[126] JX532 at 63-64; JX569 at 28.

[127] Tr. 105:15-16 (Cornell).

[128] POB at 20.

Market Deterioration: Cornell concedes that the PC market deteriorated in 2013 (going from long-term forecasted growth to long-term forecasted decline),[129] but he did not update his model to reflect this deterioration.[130] Petitioners defend this omission by claiming "[w]hen the new IDC numbers emerged, BCG considered whether to update its forecasts and chose not to make any changes because there was no evidence of market price declines beyond the Base Case."[131] Petitioners confuse the record. BCG was never asked to update its projections after January 2013.[132] Moreover, the 4% price declines modeled by BCG primarily resulted from a change in the product mix, not additional unanticipated price competition.[133] Finally, the IDC numbers reflect worldwide PC unit demand, not revenue. Simply put, the BCG Base Case was too high at the time of the merger.

Cost Savings: Petitioners assert that "[e]very dollar that Dell saves will, absent action by management, fall to the bottom line in the form of a dollar-for-

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[129] Tr. 107:9-14 (Cornell) ("Q. You would agree with me, sir, wouldn't you, that the PC market deteriorated from the time of the BCG projections to the time of the transaction? . . . A. There was some evidence of that. . .").

[130] Tr. 107:21-23 (Cornell). Petitioners criticize Hubbard for updating just the PC segment for the new IDC numbers. As Hubbard explained, Dell's other segments had not materially changed from the BCG forecast. Tr. 607:16-608:1 (Hubbard).

[131] POB at 16-17.

[132] Tr. 507:18-20 (Ning) ("Q. Was BCG asked to update the model after February 5? A. We were not."); 527:8-11.

[133] Tr. 568:19-569:15 (Nicol); JX520 at 4.

dollar EBTIDA [sic] increase."[134] This merely states that cost savings will increase profits if nothing else changes, and reflects a static approach to a dynamic model.

Price Competition: Cornell acknowledged that "as sales started to fall, there was intensifying price competition."[135] Sweet and others testified that this required Dell to implement a new strategy to preserve market share and stay relevant in the PC market.[136] Cornell explained that this was "kind of an economic necessity. You have to meet the market."[137] He was aware that cost savings were being used for "competitive purposes."[138] Petitioners ignore this fact and continue to assert that the Court should focus solely on Dell's "cost take outs."[139] As Dell's declining margins confirm, Petitioners are asking the Court to ignore Dell's operative reality.[140]

Had Cornell started with the BCG Base Case and appreciated the dynamic factors affecting Dell's business, it would have been obvious that using the cash

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[134] POB at 21.

[135] Tr. 101:20-24 (Cornell); JX569 at 14 ("EUC margins continue to be under pressure due to PC market fundamentals").

[136] Tr. 269:12-16 (Sweet) ("we were reinvesting that savings back into both pricing and into strategic investments."); 463:17-20 (Dell).

[137] Tr. 101:5-11 (Cornell).

[138] Tr. 102:11-17 (Cornell).

[139] POB at 22-23.

[140] Tr. 509:20-510:2 (Ning) ("because they were ceding price to gain share, their margins were eroding on the PC business.").

flows from the BCG 25% Case was generous to Petitioners, as shown in the table below comparing the BCG Base Case, the BCG 25% Case and FY14 Actuals.[141]

	Base Case	Cost Savings	Price Reductions	Other Impacts	**FY14 Actual**	**BCG 25% Case**
Revenue (M)	56448		↑ 353		56801	56448
GM (M)	12894		↓ 1681		11213	12921
GM (%)	22.8				19.7	22.9
OpEx (M)	9536	↓ 1600[142]		↑ 969	8905	9479
OpInc (M)	3358			↓ 1050	2308	3442

In other words, despite "achieving" $1.6 billion in cost savings in FY14, Dell's actual operating income was more than 30% below the BCG Base Case forecast, let alone the 25% Case. There is no basis for using more aggressive projections in a DCF – and investors and the Company's advisors clearly understood that fact.[143]

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[141] JX758.

[142] This amount reflects approximately $0.6 B cost savings targeted to OpEx and $1.0 B targeted to COGS. JX807 at 19.

[143] Tr. 81:1-3 (Cornell) ("stock market investors at the time did not share the views propounded in the projections."); 409:7-12 (Hiltz) ("we didn't have much confidence in anyone's ability to project the numbers for this company. With all due respect for both the company and BCG, neither one of them was able to come close to projecting what happened even in the first year."); 408:19-21

b. Bank Case Projections

Cornell apportioned half his valuation to a DCF purportedly based on the Bank Case.[144] Those projections were prepared by Silver Lake for post-merger operation as a private company and reflected "the Company's refined operational strategies post-Transaction, new ownership represented by Silver Lake establishing a view, secular changes in the industries in which the Company's business units operate in, and two additional quarters of financial results."[145] Cornell cast aside the actual Bank Case projections and added $1 billion in additional EBITDA to reflect incremental cost savings on top of the $2.6 billion already modeled in those projections.[146]

In doing so, Cornell again ignored the effects of price competition and the continued deterioration of the PC market. His modified projections are inconsistent with Dell's historical performance and model greater success than Dell was

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("we had no confidence in the projections."); 415:24-416:1 ("the DCF is only as good as the projections, and we thought the projections were garbage.").

[144] JX897 at ¶ 91.

[145] JX722 at 18.

[146] Tr. 91:21-92:3 (Cornell) ("the bank case base case did not include those incremental savings, that's correct."); 272:20-23 (Sweet) ("Q. Did the plan actually have this extra billion dollars in it? A. No . . .").

forecasting or achieving at the time of the merger.[147] In other words, Cornell's modified Bank Case projections also did not reflect Dell's operative reality.

2. Tax Rates

Cornell's second major error results from his application of a single 21% tax rate throughout his model. Cornell testified that he selected this rate because JPM used it in its modeling for the projection period.[148] Cornell's use of this unitary tax rate is problematic for several reasons.

First, while a 21% effective tax rate might be appropriate for Dell during the five-year projection period, Petitioners presented no evidence justifying that rate for the terminal period. Cornell testified that he did not obtain the rate from Steines.[149] He further testified that he "didn't make an independent decision that it was an appropriate terminal tax rate" and did not perform any analysis to determine whether Dell's "business and tax strategies will allow it to pay a lower effective tax rate in perpetuity."[150] Instead, he simply took the *projection period* tax rate used by JPM and then mechanically inserted it into his model as the terminal tax rate. In doing so, Cornell disregarded actual evidence that JPM "built

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[147] Tr. 108:1-7 and Tr. 79:1-5 (Cornell); JX807 at 24.

[148] Tr. 12:15-21, 39:3-15, 113:14-114:6 and 115:19-21 (Cornell).

[149] Tr. 114:10-12 (Cornell). Steines similarly disavowed any opinion on the appropriate terminal tax rate. Tr. 1032:21-1034:20 (Steines).

[150] Tr. 114:3-6 and 114:16-21 (Cornell).

in a tax rate circa 20 [percent] in the near term as per the management forecast, and then in our terminal year, we stepped it up to the marginal 35 percent tax rate."[151]

Second, there is no sound or compelling reason why the projection period tax rate must equal the terminal tax rate. As Damodaran explains:

> If the same tax rate has to be applied to earnings every period, the safer choice is the marginal tax rate because none of the [] reasons noted can be sustained in perpetuity. As new capital expenditures taper off, the difference between reported and tax income will narrow; tax credits are seldom perpetual and firms eventually do have to pay their deferred taxes. ***There is no reason, however, why the tax rates used to compute the after-***tax ***cash flows cannot change over time.*** Thus, in valuing a firm with an effective tax rate of 24% in the current period and a marginal tax rate of 35%, you can estimate the first year's cash flows using the [effective] tax rate of 24% and then increase the tax rate to 35% over time. It is good practice to assume that the tax rate used in perpetuity to compute the terminal value be the marginal tax rate.[152]

Third, the terminal tax rate should equal the marginal tax rate in a properly constructed DCF.[153] The Court recognized this common sense principle in the *Ancestry.com* appraisal case when it observed:

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[151] Tr. 766:15-21 (Rajkovic); JX650 at DCF (3-yr Street) Tab (Cell G33), DCF (10 yr) Tab (Cell N33), DCF (6yr-Mgmt) Tab (Cell J33).

[152] Damodaran, *Investment Valuation*, at 252 (emphasis added).

[153] Tr. 636:23-24 (Hubbard) ("the steady state tax rate has to be the marginal statutory tax rate"); 913:18-20 (Shay) ("if the operating cash flows are going to be made available to shareholders, deferral cannot go on forever"); *see also* JX751 at 229-30 ("[I]t is critical to use the marginal rate in calculating after-tax

> [I]t strikes me as overly speculative to apply the current tax rate in perpetuity. I agree with this Court's approach in *Henke v. Trilithic Inc.* to use the marginal tax rate "[b]ecause of the transitory nature of tax deductions and credits."

2015 WL 399726 at *20 (quoting *Henke v. Trilithic Inc.*, 2005 WL 2899677, at *9 (Del. Ch. Oct. 28, 2005)). In dwelling on whether Dell's tax rate will have stabilized by 2023 (or any other date), Petitioners miss the critical point that Cornell's terminal rate never equals the marginal rate, or even comes close. They also fail to present an alternative path for transitioning between projection period tax rate and the marginal tax rate required in the terminal period. Their failure to do so incorrectly applies the DCF methodology and overstates Dell's future cash flows.

3. Perpetuity Growth Rate and Investment

Cornell's third major error concerns his assumptions about growth rates and investment during the terminal period. Cornell and Hubbard agree with the fundamental principle that growth requires investment.[154] They also agree that the

operating income in perpetuity. Otherwise, the implicit assumption is that taxes can be deferred indefinitely."); Koller, *Valuation*, at 234 n.4 ("The marginal tax rate used to determine the after-tax cost of debt must match the marginal tax rate used to determine free cash flow."); Subramanyam, *Investment Banking: Concepts, Analysis and Cases,* at 218 ("[I]t is always the marginal tax rate that has to be used since all deferred tax assets get neutralized over a period of time and the company will eventually pay tax at the marginal rate.").

[154] Tr. 109:13-18 (Cornell); 642:5-10 (Hubbard).

proper perpetuity growth rate (PGR) for Dell is somewhere between 1.0% (Cornell) and 2.0% (Hubbard).[155] Their approaches diverge, however, when Cornell fails to harmonize these concepts in his model.

Cornell assumed that $400 million in annual investment is required to support a 1% PGR in his Bank Case valuation.[156] Cornell assumed the same 1% PGR without *any* investment in his BCG Case valuation.[157] The inconsistent modeling of investment by Cornell results in ever-increasing returns that defy the laws of economics. As Hubbard observed: "for Professor Cornell, the same growth rate with similar valuations appears to require radically different amounts of investment. It's impossible to explain."[158]

Adjusting for this error is straightforward. If the Court adopts a 1% PGR, Cornell's BCG model must be adjusted to reflect the $400 million annual investment he acknowledges is required to support that growth rate. And, if the Court adopts a 2% PGR, Cornell's models must be adjusted to reflect the greater investment required to support that higher growth rate.[159]

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[155] Tr. 42:9-43:5 (Cornell); 644:12-22 (Hubbard).

[156] Tr. 111:21-112:8 (Cornell).

[157] Tr. 112:9-16 (Cornell).

[158] Tr. 644:12-645:20 (Hubbard).

[159] Tr. 112:23-113:6 (Cornell). That amount is $574 million annually. JX896A at Ex. 24; Hubbard Demonstrative 12.

4. Discount Rate

Cornell's fourth major error arises from his calculation of the discount rate. With the exception of the equity risk premium (ERP), Hubbard and Cornell essentially agree on most inputs into the WACC calculation.[160]

		Hubbard	Cornell	Stip. Fact
Capital Structure	Equity	74.75%	75.25%	321
	Debt	25.25%	24.75%	321
Equity	Risk-free	3.31%	3.31%	320
	Beta	1.31	1.35	322
	ERP	6.41%	5.50%	
Debt	Cost	4.45%	4.95%	325
	Tax Rate	35.8%	21%	
WACC		9.46%	9.03%	

Petitioners state that Cornell selected a 5.50% ERP "based on current market returns, a thorough review of academic and practitioner literature . . . and his experience, research, and writings."[161] At trial, Cornell conceded that his figure could not be verified or replicated, and could not be found in any treatise or manual.[162] He also stated that his own approach is "idiosyncratic" and that "it may

[160] Tr. 116:7-18 (Cornell); Tr. 646:6-648:9 (Hubbard); JX896 at ¶¶ 226-58; JX907 at ¶¶ 22-28.

[161] POB at 30-31.

[162] Tr. 117:9-118:5 (Cornell).

be hard for Vice Chancellor Laster or anyone else to come to grips with it . . . ."[163] Cornell's "idiosyncratic" approach inflates his valuation.

Hubbard, in contrast, acknowledged the "vigorous" debate within the finance community as to the primacy of the historical and supply-side approaches.[164] He determined the respective figures from the Ibbotson Valuation Yearbook[165] and averaged them as did this Court in *In re Rural/Metro Corp. Stockholders Litigation*, 102 A.3d 205, 226 (Del. Ch. 2014) ("This decision adopts the compromise position of giving equal weight to the supply side and historical equity risk premiums."), *appeal dismissed*, 105 A.3d 990 (Del. 2014).

5. Conversion From Enterprise To Equity Value

A DCF analysis reflects the value of cash flows that are available from the ongoing operations of a company. It does not account for the firm's non-operating assets and liabilities.[166] Cornell's fifth major error occurred when he attempted to

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[163] JX920 at 197:13-18, 200:7-11 (Cornell).

[164] Tr. 648:4-9 (Hubbard).

[165] Petitioners agree that Hubbard correctly determined the ERPs from the Ibbotson Valuation Yearbook. SF 323-324.

[166] Tr. 118:8-13 (Cornell) (Q. "You would agree with me that once you have an enterprise value from the DCF, you have to convert that to equity value by adjusting for nonoperating assets and liabilities . . . A. Yes, that's correct."); JX908A at ¶ 68 ("a company's non-operating liabilities should be subtracted from its DCF value to the extent they reflect additional cash outlays that are not reflected in the DCF analysis"); Damodaran, *Investment Valuation,* at 440 ("To get to the value of the equity from the firm value, you subtract out the nonequity claims on the firm.").

convert the enterprise value derived from his DCF into an equity value. In doing so, he failed to account for three important items: required cash, FIN 48, and residual U.S. income tax on foreign earnings. These three mistakes alone inflate his valuation by almost $6 per share.

a. Required Cash

The parties agree that Dell had a net cash balance – *i.e.*, actual cash less actual debt – of $6.16 billion on the merger date.[167] From this amount, the experts agree that it is necessary to subtract the amount of cash required to support Dell's operations.[168] Sweet testified that as of the merger date Dell required at least $5 billion in cash to support its operations.[169] That testimony was corroborated by contemporaneous documents showing similar levels of required cash.[170] It also is consistent with the fact that Silver Lake – the party with an incentive to draw down

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[167] Tr. 46:3-7 (Cornell) 651:6-14 (Hubbard); Hubbard Demonstrative 15.

[168] Tr. 118:18-23 (Cornell) ("To the extent that they have to have a working cash balance to operate, that would be a deduction."); 710:24-711:3 (Hubbard).

[169] Tr. 277:14-278:2 and 279:3-13 (Sweet) (explaining that cash needs were $3.2-$3.4 billion for working capital and $2 billion for restricted cash).

[170] JX623 at 38 ("Estimate $5 billion minimum cash balance (including $2 billion restricted cash) is adequate to support operating needs"); JX685 at 12 ($5.167 billion required working capital/restricted cash); JX701 at 3 ("minimum cash balance" of $5.0 billion); JX255, at 3 ($5.0 billion "Cash to Keep").

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cash to reduce leverage – left $5.665 billion in cash on the balance sheet immediately after the closing.[171]

Cornell disregarded this evidence and failed to deduct *any* required cash in his conversion from enterprise to equity value.[172] At trial, he tried to explain away this omission by suggesting that he "was waiting for the testimony of Mr. Sweet, who is the current CFO. I don't think I had that at the time."[173] When it was noted that Sweet had testified in his deposition that Dell required $5 billion in cash to support its operations, Cornell conceded that he "did not adjust the model for that testimony."[174] In fact, he never adjusted his model for required cash.

Petitioners continue to defend this omission in their post-trial briefing with specious arguments.

- Petitioners suggest that Dell's operating cash needs are met through its free cash flow generation.[175] But as Hubbard explained: "there is sometimes a confusion that if you generate additional cash for working capital in the future, that somehow you don't need cash for your base of

[171] Tr. 279:8-13 (Sweet); Tr. 652:20-653:5 (Hubbard); JX736, at 4.

[172] Tr. 122:4-7 (Cornell).

[173] Tr. 120:10-14 (Cornell).

[174] Tr. 122:8-12 (Cornell).

[175] POB at 34.

working capital. That's just not true."[176] Dell required cash to address mismatches between disbursements and receipts related to (a) the "seasonality" associated with the business; and (b) "geographical friction."[177]

- Petitioners suggest that Dell's credit lines eliminated the need for required cash.[178] Not so. That would be "like canceling your checking account and just using your Visa card. You would typically think of a line of credit as being contingent financing, not your base of working capital."[179] And, if a line of credit were drawn against, a liability would exist that should be deducted from the firm's enterprise value.
- Petitioners suggest that required cash should be reduced to reflect steps taken by the Company to reduce working capital after it went private.[180] Sweet explained those post-closing actions were unappealing as a public company because Dell was "concerned from a perception with our

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[176] Tr. 651:19-652:2 (Hubbard).

[177] Tr. 278:6-279:1 (Sweet).

[178] POB at 34.

[179] Tr. 653:10-17 (Hubbard).

[180] POB at 33.

investors and analysts around what we called our negative cash conversion cycle."[181]

- Petitioners exclude trapped cash from the required cash reserve amount. Sweet testified that Dell had "roughly $2 billion" in restricted cash at the time of the merger "primarily in China, some in South Africa, some related to contractual commitments. . . ."[182] Petitioners have not presented any evidence or legal basis for excluding this restricted cash.[183]

Petitioners' labored effort to whittle down the amount of required cash reflects an implicit acknowledgement that Cornell's omission of any amount was a mistake.

b. FIN 48

Cornell's next error in the enterprise to equity value conversion resulted from his failure to take into account Dell's FIN 48 liability.[184] FIN 48 is a measurement of expected tax obligations related to ***past*** tax positions taken in

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[181] Tr. 280:8-282:23 (Sweet).

[182] Tr. 277:21-278:2 (Sweet).

[183] Sweet testified that post-merger regulatory changes in China subsequently allowed some of that restricted cash to be released (Tr. 279:14-280:7), but there is no evidence that such changes were known or knowable as of the merger date. *Battye*, 74 A.2d at 72.

[184] Tr. 123:1-3 (Cornell).

various countries.[185] It represents a "reserve reflected on the balance sheet in the liability section in accordance with generally accepted accounting principles."[186] Accordingly, it should be subtracted from enterprise value when converting to equity value.[187] As of the merger date, "Dell had recorded a reserve of $3.01 billion in contingent tax liabilities, penalties, and interest under FIN 48."[188]

Cornell testified that he *assumed* that Dell's FIN 48 exposure was included in Dell's effective tax rate, but did not know if that was true and could not present any facts to support that assertion.[189] Other witnesses lay bare the invalidity of Cornell's assumption. Sweet testified how the FIN 48 reserve is calculated, audited, and adjusted each year to account for exposure related to tax positions that the Company has taken on past-filed tax returns.[190] He referenced financial statements filed with the SEC documenting the Company's roll forward of the reserve each year to account for changes in tax positions from past years, increases

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[185] Financial Accounting Standards Board, "FASB Interpretation No. 48: Accounting for Uncertainty in Income Taxes," *Financial Accounting Series*, June 2006, ("FASB Interpretation No. 48"), codified as FASB Accounting Standards Codification 740-10-55-3.

[186] Tr. 126:5-11 (Cornell).

[187] JX896A at ¶¶ 265-67.

[188] SF 310.

[189] Tr. 123:19-124:15 and 127:11-23 (Cornell).

[190] Tr. 291:10-297:10 (Sweet).

for the present year and audit settlements.[191] He explained how those year-to-year *changes* were incorporated into the *current year* effective tax rate, but not in forward-looking rates where the timing of future changes would not be known.[192] Shay further confirmed that "the effective tax rate wouldn't include the historic 3 billion."[193]

Petitioners advance several other incorrect arguments concerning FIN 48 in their opening brief. They first posit that because other valuations did not deduct for those liabilities, that fact is somehow dispositive of the issue. It is not. FIN 48 is a relatively new requirement that creates a material valuation impact for very few companies.[194] The fact that some appraisers elected not to account for it in their valuations does not negate its validity.

Petitioners next posit that Dell's FIN 48 liability is only $1.3 billion: "$650 million Dell expected to pay to resolve $2.35 billion of the FIN 48 reserve plus the

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[191] JX1022.1-JX1022.6.

[192] Tr. 325:21-326:2 (Sweet) ("It would be taken into account in my effective rate to the extent that I settle or pay differently than how I reserved it"), 326:13-20 ("When I settle a FIN 48 liability, I'm looking at, you know, what's the audit settlement in this case. What do I have reserved to the extent that there is a difference that affects my current year rate either positively or negatively.").

[193] Tr. 995:12-14 and 994:18-995:5 (Shay).

[194] Only two appraisal cases decided since FIN 48 became effective involved companies with FIN 48 reserves of greater than $15 million (Dole, BMC).

remaining $650 million of the total $3 billion FIN 48 reserve."[195] This position finds no support in the document they cite, which states:

> The range estimate includes approximately $650M of the total of $2.35B . . . . The inclusion of the lower amount is attributable to (i) the fact that amounts totaling $650MM are in the most mature stages of dispute resolution, and (ii) the amount and timing of the remainder of the $2.35B balance is highly uncertain.[196]

In other words, the full balance was comprised of $650 million with a near term horizon and $1.7 billion with a longer horizon (*i.e.*, "the remainder of the $2.35B balance").[197] Sweet testified that the full amount remains on Dell's books and reflects "the best estimate" of Dell's FIN 48 liability and that the reserve is heavily vetted with outside advisors.[198] Any contrary argument is simply wrong.

Petitioners lastly suggest that the value of the FIN 48 reserve should be discounted because "many years could elapse between the time when a FIN 48 reserve was first put on for an issue and the time any amount might actually be paid out from that reserve."[199] That also is incorrect. "[P]resent value is not a

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[195] POB at 39.

[196] JX725 at 11.

[197] Interest and penalties bring the total to the $3.01 billion audited amount.

[198] Tr. 302:7-12 and 314:20-315:9 (Sweet); Tr. 937:4-938:22 (Shay).

[199] POB at 39-40.

relevant concept here because of the accrual with interest."[200] As Hubbard explained:

> Q. There's been some discussion in the trial about the fact that FIN 48 amounts will be paid in the future. Should they be discounted to a present value number?
>
> A. No. In fact, it might mildly go the other way. Not to get too much in the weeds, but FIN 48 requires carrying forward with interest, and the interest rate is typically well above the safe interest rate. So if you were to actually be discounting, you would discount a stream that's growing at a relatively high interest rate by the default-free, risk-free rate and it would probably be even higher.[201]

Cornell's failure to properly account for Dell's FIN 48 reserve inflates his valuation by $1.71 per share.

c. Residual U.S. Tax Liability

Cornell's final error in the enterprise to equity conversion resulted from his failure to account for the residual U.S. tax liability that will be imposed on Dell's foreign earnings. Dell's financial statements show approximately $19 billion in undistributed book earnings from its foreign subsidiaries as of February 1, 2013.[202] Dell's tax liability to repatriate those earnings was approximately $6.3 billion as of

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[200] Tr. 718:7-11 (Hubbard); *see also* Tr. 296:15-18 (Sweet) ("Q. Does that liability continue to accrue interest and penalties if you would have to pay it out? A. That's correct, yes.").

[201] Tr. 655:17-656:5 (Hubbard).

[202] PTO at ¶ 281; Tr. 1036:1-5 (Steines).

the merger date, and additional unrepatriated foreign profits will cause the liability to increase during any period in which the tax rate is less than the marginal rate.[203] The issue properly framed is how to model those liabilities for purposes of the DCF analysis. Rather than address that issue, Petitioners offer straw arguments.

Petitioners first claim that because Dell "had no plans to repatriate its offshore earnings and profits at the time of the Transaction," the Court should ignore those potential liabilities.[204] This argument proves too much. If the taxes are to be ignored, then the underlying earnings and profits also should be ignored as they also are unavailable to stockholders. *Del. Open MRI Radiology Assocs., P.A. v. Kessler*, 898 A.2d 290, 329 (Del. Ch. 2006) ("[N]o one should be willing to pay for more than the value of what will actually end up in her pocket . . . ."). The two experts agreed: "if you can't return your cash flows to investors, you're not going to be worth anything."[205] Petitioners must accept both the detriment and benefit of keeping earnings and profits permanently offshore.

Petitioners next claim that there is "no support in the academic literature for deducting deferred taxes in converting enterprise to equity value." That is incorrect. Damodaran included a specific example illustrating the concept in his

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[203] PTO at ¶¶ 326-327; Tr. 1036:6-11 (Steines).

[204] POB 35-36.

[205] Tr. 82:22-83:1 and 84:12-16 (Cornell); Tr. 662:1-3 (Hubbard); 925:17-20 (Shay) ("These earnings can't be kept off-shore forever or else they don't provide value to the shareholders.").

treatise.[206] He discussed deferred tax liability as an example of a nonequity claim that should be subtracted when converting from enterprise to equity value:

> The most sensible way of dealing with this item is to consider it an obligation, but one that will come due only when the firm's growth rate moderates. Thus, if you expect your firm to be in stable growth in 10 years, you would discount the deferred tax liability back 10 years and deduct this amount from firm value to get to equity value.[207]

By spreading out Dell's deferred tax payments over 25 years starting in 2023, Shay adopted a more petitioner-friendly approach than if he had discounted the full $11.7 billion in tax liability all at once in 2023 or spread it over 10 years beginning at the terminal date.[208]

Finally, Petitioners suggest that the repatriation tax liability should be reduced because Dell "has never repatriated offshore earnings at the full marginal rate."[209] This argument misses the point. For purposes of DCF modeling, some assumption must be made as to the repatriation date and tax rate. Rather than speculating as to future tax rates and potential tax holidays, the proper approach is to use the marginal rates existing as of the merger date. The parties agree that this

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[206] Damodaran, *Investment Valuation*, at 254 (10 year repayment beginning in year 5).

[207] Damodaran, *Investment Valuation*, at 441.

[208] JX922 at ¶ 48 and Ex. 5; JX896 at Ex. 23; Shay Demonstrative 5; Hubbard Demonstrative 17.

[209] POB 36.

rate is 35.8%.[210] As a point of reference, Shay's approach to modeling deferred tax payments is roughly equivalent to applying a 6-7% flat rate on overseas earnings and profits. Thus, under either his modeled approach or a "tax holiday" approach, Cornell's failure to account for Dell's deferred tax liabilities inflates his valuation.

B. Cornell's Valuation Is Inconsistent With The Merger Price.

The credibility of Cornell's valuation is further compromised by its complete dissonance from the merger price. *See* discussion *supra*, at pp. 14-18. Petitioners still have not provided a cogent explanation as to how the most sophisticated investors in the world walked away from more than $26 billion in value.

IV. PETITIONERS' ALTERNATIVE VALUATION INSUFFICIENTLY ADDRESSES FUNDAMENTAL ERRORS IN CORNELL'S VALUATION.

Petitioners present an alternative valuation purportedly "based on the various comments the Court made during the trial."[211] They claim that their alternative valuation "removes much of the dispute between the parties."[212] While correct to a point, the alternative valuation is grounded on Dell's operation as a private company rather than the BCG 25% Case and remains above the merger price by more than $11 billion. Since their starting point is the Bank Case, their alternative

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[210] Tr. 1034:24-1035:4 (Steines); 985:24-986:6 (Shay).

[211] POB at 56.

[212] POB at 56-57.

valuation would improperly exceed the merger price even with the adjustments needed below.

A. Terminal Tax Rate

Petitioners continue to model a 21% terminal tax rate in their alternative valuation. In doing so, they double down on one of the major errors in Cornell's original valuation. *See supra*, at pp. 43-46. This error inflates their alternative valuation by $1.95 per share.

B. Discount Rate

Petitioners model a 9.17% discount rate in their alternative valuation. In doing so, they abandon Cornell's "idiosyncratic" approach and use the Ibbotson supply-side figure for the ERP. However, they actually miscalculate the WACC by using a 35.8% rate for the debt shield while modeling a 21% terminal tax rate. Correcting this logical inconsistency results in a discount rate range of 9.34% to 9.67% depending on whether the Court adopts Cornell's or Hubbard's other inputs. Using the average of the range, this error inflates the alternate valuation by about $0.53.

C. Required Cash

Petitioners deduct $2.2 billion for required cash in their alternative valuation. They contend that this amount reflects required working capital following actions taken by Dell post-merger. In selecting this figure, Petitioners

looked away from both the $3.3 billion in working capital that Dell required as a public company and the $3 billion amount reflected in the Bank Case.[213] Petitioners also do not account for nearly $2 billion in trapped cash in China or the costs required to bring those funds back to the United States. Instead, they create a false construct that the required cash ranges from $2.2-$3.3 billion rather than the $5+ billion reflected in testimony and contemporaneous documents. *See supra*, at pp. 50-53. This omission inflates their valuation by $1.58.

D. Residual U.S. Tax Liability

Petitioners deduct $1.1 billion from the enterprise value in their alternative valuation for residual U.S. tax liabilities. They did this by cutting Shay's amount in half and ignoring that he already was generous to them when he delayed repatriation until 2023 and then spread it over 25 years. Petitioners also fail to account for the taxes that will continue to accrue in their alternate valuation if the terminal rate remains less than the marginal tax rate. These errors inflate their alternative valuation by at least $0.63.

E. FIN 48

Petitioners deduct $650 million for Dell's FIN 48 liability in their alternative valuation. They assume that (i) Dell settled $2.35 billion of the FIN 48 liabilities for $650 million; and (ii) such settlement was modeled in the Bank Case

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[213] Tr. 277:15-20 (Sweet); JX701 at 3.

projections. They are wrong on both accounts. As explained *supra* at p. 53-57, Dell did not settle tax matters constituting $2.35 billion of its FIN 48 reserve for $650 million. Moreover, while the Bank Case spreadsheet does reflect $650 million related to FIN 48, that adjustment is not captured in the cash flow portion of the model used by the experts for their DCF valuations. Accordingly, Petitioners' revised position is still $2.35 billion short – an error that inflates their alternative valuation by $1.34.

CONCLUSION

For the foregoing reasons, Dell respectfully requests that the Court (i) dismiss with prejudice appraisal claims as to all shares voted in favor of the merger; (ii) enter judgment determining that the fair value of Dell as of the merger date was $12.68 per share; and (iii) award Dell such further relief that the Court deems just and appropriate.

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CERTIFICATE OF SERVICE

I hereby certify that, on the 31st day of December, 2015, true and correct copies of the foregoing were caused to be served on counsel of record at the following address as indicated:

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