Case Alert May 13, 2010

In re. Sunbelt Beverage Corp. Shareholder Litigation, Delaware Court of Chancery Consol. # CA # 16089-CC [Chancellor Chandler] Memorandum Opinion revised Feb. 15, 2010

This opinion is required reading to anyone involved in statutory right actions alleging the freezing-out of minority shareholders, especially under Delaware law. The judge's opinion provides insights about a number of important valuation issues. In the end, the court awarded the minority owner the value of her shares as determined by her appraiser, or more than twice the amount paid in the 1997 merger/freeze-out, plus interest at 5% over the federal discount rate [since the merger/freeze-out] floating, plus costs [but not her legal costs.] The court declined the minority holder's alternate request for an equivalent carve-out of the business, ruling that Sunbelt would be, in any case, difficult to "un-scramble."

The majority holders calculated the cash-out price by reference to the formula in a 1994 stock repurchase agreement negotiated well before the merger. They even obtained a valuation report at the time of the merger, but the court dismissed it as an afterthought without substance since that appraiser only worked on the report for a short time. The formula was heavily dependent on book value, which in the heavily-regulated wholesale wine and liquor industry does not take into account the value of agreements in place with manufacturers and retailers, or any form of goodwill. The valuation also looked at public guideline companies, whose capitalization were much higher than if formula-valued. The court in fact had doubts about whether any guideline companies could be found because the industry is overwhelmingly privately-held.

The majority also asserted that the plaintiff had, through an agreement made at the time of a sale by the 2 largest holders, but before the merger, agreed to the formula price. At that time [1994,] the plaintiff did purchase additional shares, but the court determined that the agreement had no relevance to the terms of the 1997 merger. In the meantime, an arbitration panel convened by the U.S. District Court for the Southern District of NY in 2001 decided that value was much higher than the terms of the merger, and that the call and merger agreement had the result of eliminating the minority owner unfairly.

The Court, once again, preferred a DCF-based valuation approach and followed the plaintiff' s appraiser in not using a specific company premium because it is too difficult to justify. In the end, the plaintiff's valuation was selected by the court because it applied the size premium calculations published by Ibbotson more rigorously. Any S corporation-driven value was rejected because, at the time of the merger, Sunbelt was a C corporation.

The opinion is at http://courts.delaware.gov/OPINIONS/List.aspx?ag=Court+of+Chancery and click on the link to the revised memorandum [on the 2nd page.] A copy is at http://www.NYNJCT-BV.com/SunbeltBevOpinion.pdf.Please do not hesitate to call or e-mail to discuss this or any other valuation issue.

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