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VICE CHANCELLOR

**COURT OF CHANCERY
OF THE
STATE OF DELAWARE**

COURT OF CHANCERY COURTHOUSE
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GEORGETOWN, DELAWARE 19947

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Re: Huff Fund Investment Partnership v. CKx, Inc.
Civil Action No. 6844-VCG

Dear Counsel:

The Respondent asks me to order the Petitioner in this appraisal action to accept a payment of what the Respondent considers the undisputed portion of the value of its stock, in order to stop, in part, the running of interest at the legal rate. For the reasons that follow, and despite the potential utility of such an approach, I must decline.

I. Background

On November 1, 2013, I issued a Memorandum Opinion in this appraisal action, in which I determined that, under the particular circumstances of this case, the best indicator of fair value of the Petitioner's shares was the merger price generated by an arm's length sales process. However, in that Memorandum

Opinion, and in a supplemental bench decision on the Petitioner's Motion for Reargument dated January 13, 2014, I permitted the parties to supplement the record with additional argument regarding whether the merger price included synergies that should be excluded from going-concern value, and whether the merger price failed to account for opportunities that should be included in going-concern value.

In light of the ongoing proceedings, on November 27, 2013, the Respondents filed a Motion to Stop the Accrual of Interest. The Respondent requests that I order the Petitioner to accept an unconditional tender of $3.63 per share, which represents its expert's base case scenario for valuing CKx, plus accrued interest. In other words, the Respondent agrees that under no circumstances could CKx be valued at less than $3.63 per share, and it is willing to tender that amount to stop the accrual of interest on that payment, which interest is currently accruing at five and three-quarters percent, five percent above the Federal Reserve discount rate. In effect, the Respondent seeks the equitable analog of an offer-of-judgment rule, which allows Superior Court, but not Chancery, litigants the ability to limit the adverse effects of a verdict.[1] In addition to agreeing that the Petitioner would not be required to return the tendered amount to the Respondent, the Respondent has offered to indemnify the Petitioner for any negative tax

[1] *See* Super. Ct. Civ. R. 68.

consequences incurred as a result of accepting a partial payment—an offer conditioned on the Petitioner turning over certain tax decisions to the discretion of the Respondent. Despite those concessions, the Petitioner continues to reject the Respondent's offer, and for the reasons explained below, I deny the Respondent's request for an order requiring the Petitioner to accept it.

II. Analysis

The Delaware General Assembly has codified, in Section 262(h) of the DGCL, the approach this Court must take in determining interest awards in appraisal actions. Prior to its 2007 amendments, that Section provided in part:

> After determining the stockholders entitled to an appraisal, the Court shall appraise the shares, determining their fair value exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, *together with a fair rate of interest, if any*, to be paid upon the amount determined to be the fair value. . . . In determining the fair rate of interest, the Court may consider all relevant factors, including the rate of interest which the surviving or resulting corporation would have had to pay to borrow money during the pendency of the proceeding.[2]

Accordingly, prior to 2007, the Court of Chancery exercised a significant amount of discretion to determine the interest to which a petitioner was entitled.

In 2007, the General Assembly revised its views on interest, and Section 262(h) now provides, in part:

> Unless the Court in its discretion determines otherwise *for good cause shown*, interest from the effective date of the merger *through the date*

[2] 8 *Del. C.* § 262(h) (2001) (emphasis added).

> *of payment of the judgment* shall be compounded quarterly and shall accrue at 5% over the Federal Reserve discount rate (including any surcharge) as established from time to time during the period between the effective date of the merger and the date of payment of the judgment.[3]

The Section prescribes a formula from which this Court may deviate only for good cause shown. The formula is the same legal rate that Delaware law implies when a debt obligation does not specify a rate of interest.[4]

One circumstance in which this Court has understood the "good cause" standard articulated in Section 262(h) to permit a departure from the statutory interest rate is where there has been a demonstration of bad faith or vexatious litigation.[5] The limited discretion the Court retains to determine an alternative award of interest upon such a finding does not otherwise alter the legislature's scheme for awarding interest in appraisal proceedings. While the Section does not expressly prevent this Court from entering a partial judgment to enable the Respondent to pay consideration, thereby stopping the accrual of interest on that

[3] 8 *Del. C.* § 262(h) (2013) (emphasis added).
[4] *See* 6 *Del. C.* § 2301(a).
[5] *See In re Appraisal of Metromedia Int'l Grp.*, Inc., 971 A.2d 893, 907 (Del. Ch. 2009) ("The question of interest on an appraisal judgment has been mercifully simplified. In 2007, the Delaware General Assembly amended the appraisal statute to provide a simple default rule: a party shall be awarded interest from the date of the merger through the date of payment of the judgment compounded quarterly and accruing at 5.0% over the Federal Reserve Discount Rate as measured during that period of time. This is the prescriptive statutory interest rate, unless good cause is shown to depart from it. Adopting a different rate may be justified where it is necessary to avoid an inequitable result, such as where there has been improper delay or a bad faith assertion of valuation claims.").

amount, I believe, for the reasons explained below, that such an order would be incompatible with the General Assembly's intent in revising Section 262(h).

In its Motion, the Respondent points out what it avers is an important problem with the way interest awards now accrue under Section 262(h): namely, that where market rates of return are low, the opportunity for what it describes as a near risk-free return five percent above the Federal Discount rate may penalize a respondent corporation, and may create perverse litigation and investment incentives, including encouragement of litigation of cases without significant potential for an award above the merger consideration, and even arbitrage of appraisal claims. The Petitioner, for its part, argues that actual market returns on equity are significantly higher than the legal interest rate, and because it is an unsecured creditor of the now highly leveraged acquired company, "[t]he notion that Petitioners are somehow benefiting from the accrual of prejudgment interest is—in a word—preposterous."[6] Without considering the specific default risks and costs of capital applicable here, I disagree that such a contention is of its nature *preposterous*, and I note that, compared with fault-based litigation, the opportunities for rent-seeking in appraisal actions are comparatively high;[7]

[6] Pet.'s Br. in Opp'n to Resp't's Mot. to Stop the Accrual of Interest at 2.

[7] I do not mean to imply that the Petitioner here is litigating in response to inappropriate incentives or has maintained this action for any improper purpose.

therefore, factors that tend to create perverse litigation incentives in these actions deserve close consideration by policy makers.

However, I need not address such concerns here, because in drafting Section 262(h), the General Assembly made a determination as to the proper balance of the competing interests of appraisal petitioners, who have been cashed out of their preferred investment and denied the ability to invest the merger consideration in the market pending outcome of the case, and respondents, against whom too large an interest award may operate as a penalty. The legislature chose to strike that balance by providing that appraisal petitioners receive interest at the same "legal rate" generally awarded under Delaware law.[8] The appraisal petitioner receives this rate to compensate for her temporary inability to invest in the market, through the date of payment of "the judgment." With respect to the appropriate interest rate and accrual period in connection with statutory appraisal, the General Assembly has made its call.

The Respondent argues that "[l]ongstanding Delaware and common law principles hold that a valid tender of principal owed will terminate the running of interest."[9] I am aware that equitable principles may support such a tolling of interest, in certain situations. However, where the General Assembly has provided a specific standard governing interest awards, such a statutory directive must trump

[8] *See* 6 *Del. C.* § 2301(a).
[9] Resp't's Br. in Support of Mot. to Stop the Accrual of Interest at 1.

those considerations. Here, the General Assembly has, in enacting Section 262(h), determined that the appropriate way to compensate appraisal petitioners for their lost investment opportunity, and to prevent the respondent corporation from being unjustly enriched by the use of the petitioner's capital, is not to compel petitioners to accept prepayment, even if such prepayment is unconditional, but to award them interest in the amount of five percent over the Federal Reserve discount rate through the payment of a final judgment. That the legislature intended to limit judicial discretion to deviate from this formula is made clear by comparing the pre- and post-2007 versions of the statute. The limited discretion remaining, to be exercised upon a finding of good cause, permits me to deviate from the statutory formula where a consideration of circumstances at the end of the process—of which a wide variety might be relevant—indicates that an award at the statutory rate would be unjust; but not to direct that respondents may avoid the running of interest by prepayment as a matter of right, which is, ultimately, what the Respondent suggests here. While I am sympathetic to the incentives driving this Motion, ultimately I find the relief sought incompatible with the statute.

Finally, the Respondent contends, in the alternative, that good cause exists under Section 262(h) for me to stop the accrual of interest, suggesting that the Petitioner has "pursued overbroad document and third-party discovery, taken irrelevant depositions and filed multiple unauthorized briefs, all of which have

delayed the proceedings."[10] Whether such misconduct has occurred in this case is better evaluated at the conclusion of these proceedings.

III. Conclusion

For the foregoing reasons, I deny the Respondent's Motion to Stop the Accrual of Interest. IT IS SO ORDERED.

Sincerely,

/s/ Sam Glasscock III

Sam Glasscock III

[10] *Id.* at 3.