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Re: Timothy Tansey v. Trade Show News Network, Inc., et al.
C.A. No. 18796

Dear Counsel:

Plaintiff Timothy Tansey prevailed on an earlier motion for summary judgment in this case and was held to be entitled to a remedy for the wrongful conversion of his shares of stock in defendant Trade Show News Network, Inc. ("TSNN").[1] The purpose of this opinion is to decide the appropriate remedy to be awarded to Tansey.

The conversion of Tansey's TSNN shares occurred as a result of an invalid merger (the "Merger") that was purportedly consummated between TSNN and defendant Tarsus Partners ("Tarsus")[2] on January 24, 2001. The Merger was later "redone" properly several months later. The events that

[1] *Tansey v. Trade Show News Networks, Inc.*, 2001 WL 1526306, at *6-*9 (Del. Ch. Nov. 27, 2001).

transpired after the date of the invalid Merger are not germane to this decision and were described in the prior summary judgment opinion. They will not be repeated here. Indeed, given the unusual posture of this case, which I will explain next, I assume the reader's familiarity with that prior opinion and rely upon it for context that I would typically include in this opinion. Similarly, I do not start over in terms of my legal analysis; instead, this opinion flows out of my earlier one.

In that earlier summary judgment decision, I noted that the "traditional remedy for a conversion claim is to award the plaintiff the 'value of the property at the time of conversion, with interest.'"[3] Although there are variations on this approach that might come into play depending on the circumstances, the standard method is applicable here, as Tansey accepts the proposition that the value of his TSNN shares did not increase after the Date of Conversion. For that reason, I am required to come up with a responsible estimate of the value of Tansey 's block of 142,94 1 shares, or 7% of TSNN, on January 24, 2001 (the "Conversion Date").

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[2] Tarsus Partners was an acquisition vehicle formed by defendant Tarsus Group PLC. Their distinct identities are not important to the resolution of this case.

[3] *Tansey*, 2001 WL 1526306, at *8 (quoting *Wyndham, Inc. v. Wilmington Trust Co., 59* A.2d *456,459* (Del. Super. Ct. 1948)).

The parties have asked me to answer this question by examining a paper record, which they have stipulated is the record in lieu of a trial. Notably absent from this record is any formal valuation of TSNN performed by a financial professional, prepared either in the course of official duties by an employee of TSNN or by a testimonial expert for either party. This absence is important because TSNN's shares were not traded on a public market; thus, there were no regular trades in the stock from which to draw a reliable inference about value. The reason the parties have chosen to submit the issue to me in such an unusual form is obvious: the amount at stake if Tansey prevails in receiving the full amount of conversion damages he now seeks — $1.15 per share, which equals $164,382.15, before pre-judgment interest — is too insubstantial to make a full trial and the retention of financial experts economically rational.

It would be less than candid were I not to admit that the record before me provides me with a confusing and unreliable basis to make a valuation judgment. From the facts provided, it is impossible for me to approach even the imprecise "precision" of an appraisal ruling, which should suffice to alert the sophisticated reader that my estimate of value should be taken for what it is: a good faith effort to craft a sensible remedy based on an inadequate factual record.

With those preliminaries out of the way, I turn to the job at hand beginning with a brief description of TSNN.

As of the year 2000, TSNN was a non-public company with a small group of stockholders. The largest stockholders were defendants David Larkin, TSNN's CEO, and members of Larkin's family. The company was run very informally, with Larkin observing few of the necessary formalities required of a corporation. Indeed, the principal source of funding for the company was Larkin himself, who purports to have funded the company with personal loans — loans that were not approved, as required, by the TSNN board — a board that happened to have an invariable practice of not having meetings.

TSNN intended to make money in the trade show industry. How? First, by creating a searchable database, or on-line "yellow pages,"[4] regarding trade shows. Second, by helping companies involved in the trade show industry to create and to maintain websites.

[4] Larkin Dep. at 4-5.

As of mid-2000, TSNN was typical of other Internet companies — it had monthly revenues that were much smaller than the monthly costs of doing business. Because its cash position was strained, TSNN explored the possibility of a merger with its primary competitor, TSCentral, Inc., another fledgling company that had its own financial problems, but which was apparently better financed and had more users of its services as of that time than TSNN did. The merger with TSCentral did not pan out, however.

In June 2000, Larkin resumed discussions he had earlier had with Tarsus. As of then, Tarsus was a British company that produced trade shows in Europe and the United States, published trade show directories in Europe, and maintained an Internet directory of European trade shows. One of Tarsus's possible next moves was to expand its informational businesses into the United States, and TSNN's trade show Internet directory was a wedge into that market.

TSNN's need for capital and Tarsus's interest in the U.S. trade show information market formed the foundation for a transaction on June 6, 2000. Tarsus committed $500,000 to TSNN. In exchange for $250,000 of those funds, Tarsus purchased 217,800 shares of TSNN common stock for $1 .15 a piece. By this method, Tarsus acquired 9.9% of the equity of TSNN. The other $250,000 was in the form of a loan, which could be repaid in cash or in stock, equal to another 9.9% of TSNN's common stock at the time of repayment.

As part of the deal, Tarsus received the right to place a director on the TSNN board. It soon exercised that right and placed defendant Douglas Emslie on the board. Additionally, Tarsus was granted a right of first refusal triggered in the event that a third-party made an offer to buy 5 1% or more of TSNN's stock, as well as a preemptive right to newly issued TSNN shares. Finally, Tarsus gained access to TSNN's business information and trade show database, and the two companies agreed to cooperative marketing efforts.

The parties hotly contest the significance of the $1.15 per share price used in this transaction. The defendants argue that the price was not a good indicator of market value because: 1) Tarsus was not focused on price but on gaining a less than 20% toehold in TSNN, which could give it the opportunity to buy more later if that made sense; 2) Larkin simply matched TSNN's need for a certain amount of cash ($500,000) to a level of equity he was comfortable parting with; and 3) Tarsus obtained valuable rights in addition to the shares. As a result, the defendants contend that the Tarsus transaction is not good evidence of the value of an ordinary block of TSNN shares as of June 2000.

By contrast, Tansey points out that Tarsus and TSNN were dealing at arms-length in a real negotiation. It makes no sense, he says with more than a little justification, that the parties did not care about price, when it is obvious that they did.

Without an extended explanation, the inference I draw from the record is that the $1.15 price does have meaning, but that, in itself, it is not a reflection of the price that Tarsus, or any other buyer, would have paid for Tansey's shares, even in June 2000. Although I am not able to quantify by the penny the percentage of the price that goes to these factors, I am confident that Tarsus's willingness to pay $1.15 per share was heavily influenced by the board seat it was obtaining, the right of first refusal, the preemptive rights, and the information and marketing sharing — and perhaps more pervasively by an implicit understanding that it was entering into the embryonic stages of a relationship that could flower into a full joint venture or acquisition. It is unlikely that Tarsus would have paid $1.15 a share to purchase 9.9% of TSNN's shares on the open market without these additional benefits.

The $1.15 price also cropped up in another transaction consummated by TSNN in July 2000. That month, TSNN sold 40,000 shares of its common stock to its Chief Operating Officer, Patrick Buchen, for a total price of $45,880, or $1.147 a share. (The purchase price was actually loaned to Buchen by TSNN with the understanding that the loan would be forgiven in consideration for future services Buchen would provide.) In his deposition, Larkin testified that the Buchen transaction was part of Buchen's compensation package and was designed to make employment with TSNN more attractive to Buchen.[5]

Tansey argues vigorously that the price of this transaction is probative of the fair market value of TSNN shares because the company was trying to induce Buchen stay with the company. Because of this motive on the part of TSNN, Tansey submits that the $1.15 per share price likely understated the actual value of TSNN shares — i.e., that TSNN was giving Buchen a bargain.

By contrast, the defendants argue that the price per share was not an important factor in the Buchen transaction. TSNN simply tied that price to the Tarsus price in order not to dilute Tarsus (an explanation Tansey rightly

[5] Larkin Dep. at 28-29.

contends is at odds with the defendants' assertion that Tarsus did not care what amount of equity it received). Moreover, the transaction's purpose as an incentive did not turn primarily on the per share price but on the number of shares, especially since TSNN was fronting the money with little expectation of repayment. In this sense, the defendants say that I should view the transaction as more like a stock option grant than a negotiated sale of equity.

On balance, the defendants' explanation strikes me as the more plausible one. This is not to say that the $1.15 per share price is not some evidence of the value of TSNN shares as of July, 2000. It is. But it is to acknowledge my conclusion that the per share price was not the major feature of this transaction, and that this transaction is a relatively poor predictor of what a third-party would have paid to buy 40,000 shares in July 2000.

After the June 2000 Tarsus transaction, TSNN had funds to get it through the rest of the year. During the latter half of 2000, monthly revenues increased for a period of time and expenses declined, which resulted in lower losses per month than TSNN had experienced previously. Tansey sees these results as promising, which is a plausible half-full perspective on the TSNN drinking glass. Nonetheless, this was not a period of unconflicted optimism at TSNN. For one thing, the stock market had begun to sour on Internet companies, as a sharp decline in the NASDAQ began in earnest. For another thing, TSNN needed additional capital if it was to survive, because even though its revenues were up somewhat and its costs were down, its bottom line was still written in red.

Tarsus was an obvious source of new capital, and in the autumn of 2000 it had expressed an interest in purchasing the rest of TSNN. Ultimately, the economic terms of an acquisition transaction were negotiated between TSNN, through Larkin, and Tarsus. In that transaction — which became the flawed Merger that gave rise to Tansey's conversion remedy — Larkin received certain elements of consideration that were not shared generally with TSNN's other stockholders.

These included an agreement to pay $900,000 to Larkin as partial repayment for the loans he had purportedly made to TSNN. Of that total, $500,000 was to be payable upfront as the whole amount of a cash advance Tarsus made on its purchase of all of TSNN's shares.[6] The other $400,000 was to be the first $400,000 in deferred payments that were to be made to

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[6]PX 16, §§ 2.2(b), 2.3(a).

TSNN's stockholders. These payments were contingent on TSNN's 2001 performance under the formula described below.[7]

Larkin also secured an agreement for himself to remain President of TSNN. Larkin was also to become CEO of another business, Global Exhibition Portal, that Tarsus operated, a position that Tarsus thought would be highly lucrative to Larkin.

Tarsus's acquisition was originally structured as a straight purchase of all TSNN shares, but Tansey would not consent to it. It was then changed to the Merger, albeit one that was not approved correctly.

The Merger provided for the TSNN stockholders to receive transfer-restricted shares of Tarsus stock equal to $500,000 in total — or 25¢ per TSNN share;[8] a very modest amount of cash per share;[9] plus the possibility of additional compensation equal to:

> the difference between an amount equal to three (3) times [the surviving corporation's] net revenues (gross revenues minus sales tax, VAT or other comparable taxes only) for the calendar year ending December 3 1, 2001, multiplied by eighty and 1/10 percent (80.1%),[10] minus an amount

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[7] **PX 16,** §§ 2.2(b), 2.4(f).

[8] **PX 16, § 2.3(a).**

[9] **PX 16, § 2.3(a).**

[10] **This factor accounts for Tarsus's implied ownership of 19.9% of TSNN's stock, a provision that treats the earlier $250,000 loan as having been converted** into equity.

> equal to three (3) times [the surviving corporation's] net loss from operations, if any (specifically excluding extraordinary items or events), for the calendar year ending December 3 1, 2001, and minus an amount equal to any working capital provided to TSNN and/or [the surviving corporation] by Tarsus Partners prior to December 3 1, 2000.[11]

Summarized, this "Merger Formula" gave the TSNN the possibility of receiving additional consideration if the company's 2001 full-year revenues were impressive in relation to its expenses. The additional consideration was to be paid within seven days of the finalization of TSNN's fiscal year 2001 financial statements, a date I will assume to be February 15, 2002. As noted, Larkin was supposed to receive the first $400,000 in cash generated by the Merger Formula, and in the event that TSNN's 2001 performance fell below a certain threshold, the cash payments made at closing to Larkin and the other TSNN stockholders were to be repaid to Tarsus.

In regard-to what TSNN expected to receive from the Merger Formula, Tansey notes that Larkin prepared a "Budget" in November 2000 estimating TSNN's performance for the year 2001. Larkin admitted that the Budget was intended to be the best prediction of the company's next year

[11] PX 16, § 2.2(a).

In contrast to the defendants, I find the Budget prepared by Larkin to be highly probative of TSNN's value. By November 2000, Larkin had access to a substantial part of the year's results. He was generating the Budget when he was in active discussions with Tarsus about an acquisition, and the amount of consideration that would result for TSNN would obviously have been on his mind. Because Tarsus sought to acquire TSNN largely for consideration dependent on the performance of the company in the year following the acquisition, Larkin — if properly motivated — had an incentive to come up with a realistic prediction of results, which, if achieved, would generate sufficiently good returns to require a decent payment from Tarsus.

In considering this issue, I am, of course, mindful that Larkin's interests were not wholly aligned with those of the other TSNN stockholders. Although he and his family had the largest equity stake in TSNN, Larkin secured for himself other valuable benefits in the negotiation process. And from Tarsus's perspective, the most important thing to it was probably not how the total acquisition consideration was allocated, but the amount of the total. That is, Tarsus was probably morally indifferent as to whether it cut Larkin in on a bigger share of the pie than he deserved (e.g., through a new employment arrangement) so long as the total size of the pie did not change and so long as payments to Larkin did not endanger the deal.

Nonetheless, the Merger Formula, when taken together with Larkin's budget, provides what — in the context of this admittedly less than reliable record — is the most reliable evidence of the value of TSNN as of the Conversion Date. Because Tarsus was dealing at arms' length, the Merger Formula provides some indication of a negotiated price, especially because Larkin's ability to recoup all his loan repayments was tied to the formulation. At the same time, because Larkin was also receiving Merger-related benefits not shared with the other TSNN stockholders — a new employment opportunity — the Merger Formula is unlikely to be extravagantly generous to TSNN's stockholders. Finally, because Larkin's estimate was his best one and because he was then trying to negotiate the Merger Formula, the Budget provides good evidence of his perception of the expected performance of TSNN as of January 2001, particularly because the defendants have not produced any evidence that suggests any sharp negative change in the company's performance in January 2001 from November 2000. For all those reasons, I give great weight to the 92¢ per share generated by the Merger Formula when Larkin's Budget is used, while recognizing that that number also reflected a value that would not be paid until February 15, 2002.

For understandable reasons, the defendants try to shift my focus to events after the Conversion Date, rather than the Budget. During the period after the Conversion Date, TSNN did not perform as well as Larkin's Budget had predicted. When combined with the overall malaise in the Internet sector and with the serious problems that befell TSNN's competitor, TSCentral, which ended up being acquired by Tarsus at a-modest price, the bleak picture that the defendants paint has persuasive appeal but is of limited legal relevance.

The critical question is what the value of Tansey's shares were as of the Conversion Date. The by-now obvious reality that many market participants in early 2001 were still too optimistic about Internet companies cannot obscure my duty, which is to ascertain the value of TSNN shares in the market as it existed on the Conversion Date. The defendants are not permitted to take advantage of post-Conversion events to benefit themselves but must pay the value of Tansey's shares on the Conversion Date, a value that in turn must be estimated from what was knowable at that time. That said, I do give some weight to the evidence suggesting that as of the

Conversion Date the sector in which TSNN was participating was struggling and that industry participants with some stronger attributes than TSNN were having difficulties.

Aclmowledging the considerations the defendants point to convinces me that some discounting from the value the Merger Formula and Budget imply is in order. The discounting reflects the risk that existed as of the Conversion Date that TSNN would not perform up to the Budget, as well as my recognition that Tansey held an illiquid minority block.” For a few reasons, the discounting is not as severe as the defendants would like. For starters, the subsequent non-achievement of the Budget is not critical, because parties dealing in TSNN shares in January 2001 would not know whether TSNN would do worse or better than the Budget. Furthermore, I give some weight to the earlier Tarsus transaction at $1.15 per share, which suggests that — at least to Tarsus — TSNN had real value

[15] As indicated, on the Conversion Date, this risk presented a possibility of a higher than 92¢ per share payment, a lower one, no additional payment, or a requirement to repay the cash paid by Tarsus at closing.

to it. No convincing evidence persuades me that Tarsus did not continue to believe that TSNN had value of as of the Conversion Date and there is no evidence that convinces me that a marked departure from the 92¢ per share price implied by the Merger Formula and Budget is warranted. Finally, I am persuaded that Larkin was a less-than-impartial negotiator for TSNN and that the Merger's structure to.some extent reflected a diversion of consideration towards Larkin and away from TSNN's stockholders.

Because I find the Merger Formula and the Budget to be the best available indicator of value, I grant a remedy equal to 87¢ per share for each of Tansey's shares — which is a 5¢ per share discount from the 92¢ per share price implied by those factors — with pre-judgment interest running on that amount from February 15, 2002, the date on which I assume the 87¢ would have been payable under the First Merger? This avoids any need to calculate the difference between the value of 87¢ on the Conversion Date and February 15, 2002. The pre-judgment interest shall be calculated from those dates until the date of the final order at the statutory rate compounded monthly. Any reasonable investor would expect compounded interest. Post-judgment interest in accordance with the statute will run on the full amount of the judgment.

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[16] In coming to this remedy largely based on the Merger Formula and the Budget, I have balanced two of the cross-cutting factors I previously identified. The first is that the Merger Formula was designed to implement a transaction in which Tarsus would gain full control of TSNN. As a result, the price it would pay per share would be different from that it would have paid to buy only Tansey's 7% block. Because this is not a statutory appraisal, the remedy should consider this real-world influence on the fair market value of the converted property, which contributes in part to the 5¢ discount I impose.

The second factor cuts the other way, which is that Larkin appears to have diverted consideration that could have gone to other TSNN stockholders to himself. Given his apparent hostility to Tansey and his own self-interest, Larkin was in an awkward position to negotiate selflessly (or even for his own interests solely as a TSNN stockholder *qua* stockholder). I have accounted for this partially by not giving any weight to Larkin's supposed right to receive the first $400,000 of the additional compensation contemplated by the Merger agreement, a right which was somewhat dubious, to say the least, given that the "loans" Larkin made to TSNN were never properly authorized. PX 16, § 2.4(f). I have not, however, added back the $500,000 payment made to Larkin at the time of the invalid Merger, which was to be the first payment toward the "loans," as Tansey would have me do. In my view, that adjustment would produce an unduly harsh result, especially given the reality that Larkin now must repay that amount, because of TSNN's actual performance in 2001. PX 16 §§ 2.2(b), 2.3(a). For similar reasons, I have also not included within the damage award any compensation to Tansey to account for the small cash and stock payments he would have received if he had actually supported the Merger, elements of consideration that the parties' briefs failed to address in a helpful way. Rather, with the 5¢ per share discount and my decision to ignore Larkin's preferred claim on the additional compensation, I believe that these cross-cutting factors — Tansey's minority block versus the additional benefits Larkin secured for himself in the Merger — are accounted for in my remedial calculus in an appropriately balanced way.

The parties shall confer and submit a conforming final order within ten days.

Very truly yours,

Leo E. Strine, Jr.

oc: Register in Chancery