IN THE SUPREME COURT OF THE UNITED STATES

SANTA FE INDUSTRIES, INC., SANTA FE NATURAL RESOURCES, INC., and KIRBY LUMBER CORPORATION, Petitioners,	
v.	No. 75-1753
S. WILLIAM GREEN, et al., Respondents.	

Washington, D.C.
Wednesday, January 19, 1977

The above-entitled matter came on for argument at 10:05 o'clock a.m.

BEFORE:

WARREN E. BURGER, Chief Justice of the United States
WILLIAM J. BRENNAN, JR., Associate Justice
POTTER STEWART, Associate Justice
BYRON R. WHITE, Associate Justice
THURGOOD MARSHALL, Associate Justice
HARRY A. BLACKMUN, Associate Justice
LEWIS F. POWELL, JR., Associate Justice
WILLIAM H. REHNQUIST, Associate Justice
JOHN PAUL STEVENS, Associate Justice

APPEARANCES:

WILLIAM R. GLENDON, Esq., 200 Park Avenue, New York, New York 10017; for the Petitioners.

SIDNEY BENDER, Esq., 405 Lexington Avenue, New York, New York 10017; for the Respondents.

P R O C E E D I N G S

MR. CHIEF JUSTICE BURGER: We will resume arguments in Santa Fe Industries against Green. Mr. Glendon, you may pick up where you left off yesterday.

ORAL ARGUMENT OF WILLIAM R. GLENDON, ESQ.,

ON BEHALF OF THE PETITIONERS

[Resuming]

MR. GLENDON: I would like to reserve three minutes for rebuttal, Mr. Chief Justice.

Mr. Chief Justice, and may it please the Court:

I think as we suspended yesterday I was referring to Judge Moore's dissent in saying that to say that the circumstances here presented a scenario of fraud was a patent distortion of the term. To put the facts into a little sharper focus, I would like to refer to a couple of matters. Judge Medina in the majority opinion, in approaching the subject involved, made reference to schemes of wile and cunning and so sophisticated as to almost defy belief. In fact, as Judge Moore noted, the circumstances here were such that he found they were matters of utmost simplicity and patent reasonableness.

In the concurring opinion, Judge Mansfield inveighed against the idea of companies going public when the market is flourishing and then going private when the market is depressed. In fact, as the record shows here, Kirby has always been a public company. The price that was paid for the stock--offered

for the stock--was much higher than anything shown in the record before. We do not know what the plaintiffs' basis here for the stock was, but it is interesting to note--I think it is at page 102 of the joint appendix--that he pleads and complains of the fact that he is going to have to pay a capital gains tax on this transaction, which is certainly a most unusual complaint of a victim of a claimed fraud.

Q Of course his claim was addressed to the fact that he did not have any option about the source.

MR. GLENDON: He has another option, of course, of getting a fair evaluation. And the Delaware statute, as I pointed out, Mr. Chief Justice, specifically provides and is part of his contract and the charter of the corporation that minority stockholders can be eliminated from the corporation.

I think the first principle that we should consider here is the fact that the Securities Acts, the '33 and '34 acts, are disclosure statutes. This Court said in the Affiliated Ute case that the philosophy was to substitute a philosophy of full disclosure for that of caveat emptor. We think the court below ignored that as well as ignored their own holding in the Popkin case only two years before when they said the function of the statute is primarily to disclose and inform rather than becoming enmeshed in passing judgments on the information disclosed.

They ignored too, we feel, the language of the

statute itself, which, as this Court said in the Ernst & Ernst case, speaks so specifically of manipulation and deceit. And we find no reference in the Court's decision, the majority decision, to the statute itself. And we think that of course we must begin there with the statute.

The language prohibits manipulative and deceptive devices and contrivance, in contravention of the rules of the commission. And to us it is clear that they are talking about deceit and deception. The Court of Appeals met this problem not by taking it on headlong but simply eliminating deception and deceit from the statute even though, as I said, they had just previously stated a couple of years before that the disclosure was a key purpose of the statute.

The plaintiff tries to avoid this problem by a variety of references to other cases, other statutes, relying principally, it seems to us, upon arguments in cases which invoke matters of constructive fraud. But the statute is a disclosure statute. It did not--I repeat, did not--try to take on all the wrongs of the world. The Congress adopted a philosophy of disclosure, and it said that when you disclose, you cannot make deceitful disclosures, deceptive disclosures. And that, we feel, is the problem before the Court today.

The cases that this Court has considered on the matter we think support that. The plaintiffs seem to get support from the Bankers Life case, but that was a clear case

where this Court said the statute should be read flexibly, and we certainly agree with that. But the Bankers Life case was a deception case. It was a clear case of deception. The Court referred there to the fact that misrepresentations had been made, that the board of directors had been duped. So, that case really offers no help, in our view, to the plaintiffs.

The Court too has said that the statute will not be read narrowly and has removed artificial barriers to the administration of the statute. For example, in Bankers Life it said just that. And it broadened some of the categories in terms of reliance and such. But it has not and it has never--and I do not believe it should or could remove the concept of deceit from the statute because, if you do, if that is done, then you do not have a statute that involves deception. And it seems to us it is as simple as that.

There may be wrongs that people can lay claims to. We do not think so in this case. There may be conflicts of interest. There may be fiduciary breaches. There may be actions of waste. But they are not actions for deceit. And the statute says deceit.

Q Mr. Glendon, what if majority shareholders moving under the Delaware short-form merger statute did engage in deceptive conduct, say, in discussing valuation with the minority shareholders. Would the minority shareholders then have a 10b-5 action for damages?

MR. GLENDON: If they engaged in deception in the disclosure, yes, Mr. Justice Rehnquist, I think they would. And the Popkin case made clear that 10b-5 in a short-form merger is not a nugatory thing because the splinter shareholder has an investment decision to make. He can either accept the offer, or he can take his appraisal remedy under the Deleware statute.

I think perhaps the fallacy in the plaintiffs' approach and in the majority's decision is simply that they believe that every wrong or possible wrong or conceivable wrong that may arise in connection with securities should be cured by the application of 10b-5. I will discuss later what that may do to the federal courts. But quite apart from the result of such a thing, the fact simply is, we feel, that the Congress never intended that and, starting as we must, with the clear language of the statute, it just seems there is no basis for doing it.

It is not--and Judge Medina in his majority opinion recognized this--10b-5 is not a panacea for all wrongdoing. It has a limited purpose which should be construed broadly, of course. But it has a limited purpose of requiring disclosure and having an informed investor.

The court below, passing fraud, moved into the area of fiduciary breach, and it engrafted upon 10b-5 not fraud but said that there was a fiduciary breach here. We do not

think that fiduciary breach and fraud are the same thing. There may be deception in a fiduciary breach. But whether there is overreaching or conflict of interest or other aspects of fiduciary breach, they do not come under 10b-5. We think it is difficult to understand how the court did that, to engraft a fiduciary breach onto it, but it is almost impossible to explain what the breach was here. And I would like to go into that just briefly.

The court said that the allegation of gross undervaluation alone was not enough. That was not a fiduciary breach. But what it said was that undervaluation, combined with a lack of express corporate purpose other than the obvious advantages that may come to a company from going private, but the court said that in the absence of other express corporate purpose, in the absence of prior notice, although as I think I said yesterday, the Delaware statute requires post-merger, not prior notice.

The court said that the combination of those three things constituted a breach of fiduciary duty, and that breach resulted in the violation of 10b-5. It was a scheme and contrivance and artifice to defraud.

That, we think, is a startling proposition. It has the obvious vice of rewriting the Delaware statute because the court had to rewrite the Delaware statute in order to come to that result. The Delaware courts have said that the very

purpose of 10b-5 is to permit the elimination of the splinter shareholders. And I may say that some 30 other states have the same or similar provisions where minority shareholders can be eliminated.

So, to engraft on that a requirement of corporate purpose nullifies in effect the Delaware statute.

Secondly, to engraft on or amend the statute which now says you must give notice within ten days after the merger, to say you must give notice before the merger, again rewrites the Delaware statute. Judge Moore said something to the effect that the court, while it was engrafting changes on corporate charters, was also putting the torch to Erie v. Tompkins. And I think that is a fair statement of fact. The court simply rewrote the Delaware law.

In terms of corporate purpose, it seems to us that apart from changing the statute, not supplementing state law but supplanting state law, in doing that--

Q Mr. Glendon, could I interrupt for just a second? I do not quite understand the significance of your argument on rewriting the Delaware statute. If, for example, the Delaware statute said that certain information shall not be disclosed and it required that there be a non-disclosure, and rule 10b-5 would require a disclosure, would not rule 10b-5 prevail?

MR. GLENDON: That would be in the area of disclosure,

and that is what the statute is about, Mr. Justice Stevens. The statute requires disclosure. It is not, however, a statute--

Q But in the event there is a conflict between the Delaware statute and the requirements of Rule 10b-5, Rule 10b-5 would apply, would it not?

MR. GLENDON: But we are saying to you here, sir, that there cannot be that conflict under this aspect of the case. This is not a disclosure requirement. It is a regulation. It is a regulation of Delaware corporations who are chartered by the State of Delaware and set up and governed by the laws of the State of Delaware. And the State of Delaware says that you may eliminate a minority shareholder, and they have a statute. The Supreme Court of Delaware has said that the very purpose of that statute is to be able to eliminate. That is what it is about.

What the court has done here is said, "You have got to have another purpose." This is not disclosure. This is not under the disclosure statute. This is regulating a Delaware Corporation contrary to what the Delaware law says.

Q But is not your basic proposition that there is simply no violation of Rule 10b-5?

MR. GLENDON: Yes.

Q And if that is true, why then it does not matter whether a violation would require a revision of the

Delaware statute or not.

MR. GLENDON: What we are saying simply is that to get to the result that it got, the court had to rewrite the statute. And to do that, to take a federal statute and apply it so that you have got to rewrite a state statute, in the absence of a clear intent by the Congress that they are to do that, an express intent that if Congress had said, "Here you may regulate" and they pass a federal corporation law and say, "Everything that is unfair from now on in corporate matters will be governed by federal law"--they have not done that. They have said simply one thing. They have said that there shall be disclosure. I am trying to point out that when they say not only disclosure but when they say you have to have an express different corporate purpose, they are telling Delaware how to run its corporation and amending, we say, the statute.

They amend it in another way too, and that is on the fact of notice. I think I pointed that out. This is interesting, I think, because that requirement is a useless requirement really. They have said that there must be prior notice, but Delaware has said that you can eliminate the shareholders, and they have set up the statutory procedure in that fashion. There is no pre-merger going into court. The Delaware Court has said, as a matter of fact--the Supreme Court has said that it would be difficult to assume any situation where there

could be such actual fraud as to set aside a merger because the whole purpose of the statute is to do that.

Q What if Delaware had said you may not eliminate minority stockholders in this manner. Your client had come along and given notice to these shareholders and said, "We know it is a violation of Delaware law, and this is what the Delaware law says, and this is what we are going to do. It is contrary to Delaware law." But there was no misrepresentation in connection with it.

MR. GLENDON: I do not think that would be a 10b-5 case. I do not think it would be because of this disclosure, and this is what we are talking about.

Q You are not foreclosing the possibility of state remedies by that statement.

MR. GLENDON: Of course not, Mr. Chief Justice. And there is here of course a state remedy. If they do not like the price that is offered to them, they go the appraisal route and in fact appraisal proceedings by others are going on now in the Delaware courts. There always are, I suppose, in this type of merger.

I do wish though to advert to our concern, Mr. Justice Stevens, to the question that you raise. We think it is a very serious matter. We think that the principles of federalism have really been abused by this decision. And I would think that any Delaware legislator would feel the same

way. They have determined in their legislative wisdom that this can happen; it can happen under certain circumstances. There may be those who do not like it. There may be some who feel it is unfair. There may be others--and 38 states have felt this way--that elimination of minority splinter interests where there is 90 or 95 percent ownership is socially desirable. But that is not a question for the courts when you get into the policy of that. And we fear that that is what the majority have done in this case.

Your Honor, I think at this point I would reserve the rest of my time.

MR. CHIEF JUSTICE BURGER: Very well, Mr. Glendon.

Mr. Bender.

ORAL ARGUMENT OF SIDNEY BENDER, ESQ.,

ON BEHALF OF THE RESPONDENTS

MR. BENDER: Mr. Chief Justice, and may it please the Court:

This case first arose because of the fact that the defendants made a motion to dismiss so that all the allegations and the fair inferences from the facts stated in the amended complaint are deemed to be true for purposes of this particular appeal.

Ernst & Ernst stated that the 1933 act was to protect investors against fraud and to promote ethical standards of honesty and fair dealing. And certainly the same

stricture applies to the '34 act. The '34 act uses the term manipulative or deceptive device in contravention of the rules to be promulgated by the Securities and Exchange Commission, and the SEC did promulgate 10b-5. 10b-5 clearly on its face covers fraud. And this Court in Ernst & Ernst when it was talking about 10b and 10b-5 used the term deception, manipulation or fraud. Deception and fraud are synonymous. When a person deceives, he may deceive by non-disclosure in a non-verbal way, or he may be deceived by affirmative misrepresentation. Clauses one and three of 10b-5, as held by this Court in Superintendent of Insurance, stated that misappropriation is a garden variety type of fraud. The most important part about the deceit and fraud in Superintendent of Insurance was the fact the majority stockholder used the funds of the corporation to purchase the controlling interest.

But the defendants do not quarrel with the Schoenbaum case, which has been decided in the Second Circuit. And what did Schoenbaum decide? It was an en banc decision. The majority stockholder--

Q Mr. Bender, you are going to point out where the fraud lies here?

MR. BENDER: Yes, Your Honor. Should I get to that right now?

Q You were leading up to it, and I would like to have you pin it down.

MR. BENDER: The fraud here, Your Honor, is that an appraisal was made in February of 1974 by Santa Fe of the timberlands of Kirby Lumber Company. That showed a fair market value for those timberlands of $320 million. The book value was $9 million. So that means that Santa Fe knew that the true worth of the assets, the physical assets, of Kirby was equivalent to $772 per share, and that has to be an assumed fact that has been alleged, and it is accepted as a fact for purposes of this appeal.

Q No stock has ever moved at that figure, has it?

MR. BENDER: No, it has not because it was never a disclosure to the stockholders that the timberlands were worth $320 million.

Q And you will explain the non-satisfactory character of the state remedy?

MR. BENDER: Yes, I will, but I want to first get into the fraud, as Your Honor first addressed yourself to.

With a physical value of $320 million and a book value of $9 million, fair market value means that Kirby could go out, obtain a willing buyer, and sell those timberlands for $320 million. So, for our purposes and for valuation purposes, that is cash in the bank. So that the physical assets must be deemed to be the equivalent of $772 cash in the bank.

They retained the prestigious firm of Morgan Stanley

& Company to come in and appraise the worth of the shares. They appraised it at $125 a share. That was in June of '74. In July of '74 they created a dummy corporation, Forest Products, Inc., solely for the purpose--and it is stated in the information statement which went out after the merger took place--solely for the purpose of increasing their percentage of ownership from 95 percent to 100 percent of that corporation, which meant eliminate the minority.

Then in the end of July the merger effectively took place between FPI corporation and Kirby. There was no notice given to the stockholders. And what was the effect, and what were the terms of the merger? The terms of the merger were that Santa Fe decided that they were going to pay the minority stockholders unilaterally $150 per share--no stockholders meeting, nothing on July 30, 1974. There was no reason given on July 30, 1974 as to why they decided $150 was fair. They only had the Morgan Stanley appraisal which showed a fair value, according to Morgan, at $120. But Morgan had in its possession of Appraisal Associates, which showed that the breakup value of these physical assets was $320 million just for the timberlands.

Q Mr. Bender, would I be defrauding you if I offered to sell you stock at $150 a share and it the same time said, "Here is an appraisal which says the stock, if you liquidate it and were able to sell all of the assets, would

be worth $720 a share"?

MR. BENDER: You would be defrauding me, Mr. Justice Powell, if you had in your power 95 percent of the stock, which meant that you could force me to accept $150 a share and, if I refused, despite my refusal you voted in such a way that I had to accept that $150 a share. And the mere fact that you disclosed to me beforehand the fact that the true value was $720 a share would still amount to a fraud because you were breaching your fiduciary obligation to me because you would be in effect forcing me to accept by reason of your 95 percent control--forcing me to accept the transaction. And, in addition to that, you would deliberately undervalue the shares at $150 a share when you knew the true worth was $772 a share or $720.

Q But you have omitted one very important fact in this situation, and that is that nobody has forced your client to take $150 a share.

MR. BENDER: They certainly have, Your Honor.

Q Wait just one minute. Let me finish the question.

MR. BENDER: I am sorry.

Q You have the right, if you think that is an unfair price, to pursue your appraisal remedy, of course.

MR. BENDER: Let me first answer that in a two-pronged way, Your Honor. First of all, on the date that my clients

were required to accept $150 a share, they did not even know they sold their shares at $150. So, there was no disclosure. This is a complete myth that there was disclosure before the fraud took place. When they purchased the shares of the minority on July 31, 1974, there was no disclosure. They had within their own possession the knowledge that they had an appraisal which showed the true worth was $770 a share, and it is no different from a majority stockholder who knows that oil has been discovered, like in the Schoenbaum case, goes to the corporation and says, "Gentlemen, I would like to buy your treasury shares because I am the controlling stockholder, at the prevailing market price," when no disclosure has been made to the public so that the prevailing market price does not reflect the fact that a major oil discovery has been made.

In Schoenbaum Judge Hays, in the Second Circuit, said a clearer case of fraud could not be set forth because the majority controlling influence used his shares to force the corporation to sell him shares at a totally inadequate price--

Q May I ask this question?

MR. BENDER: --which was a fraud on the corporation and a fraud on the minority stockholders.

Q You talk so fast you do not give me an opportunity to ask any questions.

MR. BENDER: I am sorry, Your Honor, but I do have a limited time.

Q I understand that, and I will not try to

interrupt you too frequently. The District Court found there was no misstatement of immaterial fact or omission of a material fact. The Court of Appeals accepted that. You are arguing, as I understand, that both those courts were wrong in those respects.

MR. BENDER: No, I am not arguing that the Court of Appeals was wrong. The Court of Appeals said and Judge Mansfield said that disclosure after the consummation of the merger is virtually equivalent to no disclosure at all. And that is certainly true. It is like the president of a corporation, dealing with securities of that corporation, were to abscond to Florida with $15 million of securities while the corporation was selling securities. After he gets to Florida, the next day he sends a wire to the corporation and says, "Gentlemen, I have absconded with your securities, and here I am in Florida."

Now, because of that confession--

Q Just a minute, Mr. Bender.

MR. BENDER: Excuse me.

Q Slow down and start answering some questions, will you?

MR. BENDER: I am sorry.

Q Supposing he absconds but before he absconds, he tells the corporation, "I am going to abscond to Florida tomorrow morning, and I am going to take $15 million worth of

securities that do not belong to me with me." Has he defrauded anybody?

MR. BENDER: Of course he has because the mere fact of disclosure does not mean that--if he has in his control the ability to still steal those securities, disclosure does not cure a fraud. If I have the possession--to consummate the transaction because of the fact that I have 95 percent of the stock in my possession and I tell the minority, even in a full disclosure case beforehand, which did not happen here, if I tell the minority beforehand, "Gentlemen, your stock is worth $770 per share but yet I am going to pay you, because I am the majority stockholder, $150 a share. And if you do not like it, you can seek an appraisal in state court."

Now, that has two vices. The majority stockholder is breaching his fiduciary obligation, number one, because of the fact that he has the ability, because of his 95 percent ownership, to force the transaction on the minority, even if they say, "No, we are not going to accept it." Because of the fact that he is a 95 percent shareholder, he can force them to take that $150 or seek an appraisal. And I will get to the question of whether or not that is an adequate remedy.

And why is it a fraud? Because he knows that the true worth of those shares is $772 per share and yet despite that, he has fixed as a fair value only $150 a share.

Q Mr. Bender, do you see--

MR. BENDER: $150 a share.

Q Mr. Bender, what is the difference between violation of your fiduciary relationship and fraud?

MR. BENDER: The difference between--

Q They are different animals, are they not?

MR. BENDER: No, they are not, Your Honor. This is--

Q They are synonymous?

MR. BENDER: They are not synonymous. They are not synonymous in this respect. What we have here, as Justice Powell stated in Ernst & Ernst, what is required under 10b-5 now is an intent to defraud. What do we have here? What have a fiduciary--and what is intent to defraud? It is a knowing, willful conduct to misappropriate. What did the court say in Superintendent of Insurance? Misappropriation is a garden variety type of fraud, and that is what we have here. It is a misappropriation of the difference between the true worth of $772 and what they agreed to pay, namely, $150.

Q Mr. Bender, you place a great deal of emphasis on what you call the true worth. At other times you refer to it as a fair value and a fair market value. Suppose somebody asked you right now, "What is the fair market value of, say, IBM or AT&T or any other stock that is traded actively?" Take International Paper, which probably owns more timberland than any company in the world. Where would you go to find out the fair market value of that stock? Would you not go to the

stock exchange quotation--

MR. BENDER: Well, in that kind of--

Q --that closed yesterday?

MR. BENDER: In that kind of case, yes, that would be true right now.

Q Let me finish my question.

MR. BENDER: I am sorry.

Q Are you suggesting that the fair market value of stock always is equivalent to the net asset value per share?

MR. BENDER: Not always. Well, the net asset value?

Q Yes.

MR. BENDER: If it is going to be liquidated and the majority stockholder is going to capture the underlying values, yes, if that was higher than a capitalization of earning situation.

Q But if you are right on that, you get your $752 a share or whatever it is.

MR. BENDER: We would not, not under Delaware law. Delaware law provides, number one, that they will not consider anything except historical earnings. It does not say anything about--in fact, the cases say--and this was pointed out by Judge Mansfield at I think it was page 138 to 140 in the appendix in his footnote, that it does not pay for prospective earning power, potential. And under Delaware law you are not in an adversary proceeding. I could not go into

Delaware and obtain a discovery and inspection of this company's books to determine true value. Only the appraiser is permitted to see the books.

Furthermore, the Delaware law has this further shortcoming. There is no equitable relief. The merger could not be set aside on grounds of fraud. And appraisal is your exclusive remedy. Procedurally if I were the party to initiate the appraisal in Delaware, I cannot go to others who have sought appraisal and seek a contribution for expenses to further the appraisal proceeding. And, in addition to that, this crucial evidence of potential value has been thereby captured by the majority stockholder at his whim and caprice when he has decided that it is time to buy the minority stockholder out.

It is clear under regular corporate purposes. What is this? This is a forced tender offer.

Q Mr. Bender, could I ask you a question?

MR. BENDER: Yes.

Q The appraisal dated February 19, 1974 contains this fair market value of $320 million in it. That is, in effect, an admission by your adversary that that is the fair market value of the tangible assets.

MR. BENDER: That is correct.

Q Would that be admissible in evidence in the appraisal proceeding?

MR. BENDER: I think now it would, certainly, because they disclosed it after the fact.

Q At the time you filed your lawsuit you had that appraisal in your possession.

MR. BENDER: I sure did have it in my possession. That was the reason that we alleged that the true value of the assets was $772 per share.

Q And so all of the information on which you relied for your allegation of $772 per share is available in that appraisal in form which would be admissible in the appraisal proceeding in the Delaware court?

MR. BENDER: In this particular case, yes. In fact, the value of those timberlands may even be greater than $320 million. I have been in many proceedings where experts have been retained, sir, and with all due deference to experts, when they have been retained by a particular party to give appraisals, that many, many times we found that even though the appraisal is substantially more than what appears on the books, that nonetheless that that is even an understatement of the true worth.

Q You have alleged that the appraisal was an undervaluation.

MR. BENDER: Pardon me?

Q You have alleged that the appraisal was too conservative.

MR. BENDER: We have alleged that the value of the shares was at least $772, and this matter has proceeded to this point without any discovery or inspection by us of books and records of Santa Fe. This was strictly a pleading matter, and the pleading was dismissed on the face of it. And all the allegations in the pleading are deemed to be correct. But since the defendants were stuck with that $772 because of the fact that after the fraud was consummated they disclosed that fact to the stockholders, then we come to the situation, well, sure we have it to allege in our complaint--

Q Is it not correct, just so I have the sequence right, that after the February appraisal of tangible assets had been completed, that appraisal was given to Morgan Stanley and that was one of the factors they considered in coming up with $125 per share price?

MR. BENDER: That is correct, and that is why we allege that Morgan Stanley rendered a fraudulent appraisal because, gentlemen, here is a situation where $772 is the breakup value of an asset. Now, what is happening? The majority stockholder has simply, at its time and at its price, decided to pay--and only for the purposes of appearing generous--upping the price to $150 and is in effect paying the total minority of 25,000 shares approximately $3,800,000. And what are they getting back from the minority? They are getting back the total equity interests of the minority in

this corporation, which is truly worth close to $20 million.

Q Mr. Bender, suppose the corporation in this short-form merger had offered minority stockholders the $772. Would you be here?

MR. BENDER: No, I would not, Your Honor.

Q You are not attacking the validity of short-form mergers?

MR. BENDER: Not per se. I only say in this particular case that was a means, a device, utilized and abused to eliminate the minority at a fraudulently low price which the majority knew to be fraudulently low.

Q Let me ask you this question. You are talking about liquidation. Any number of stocks on the New York Stock Exchange sell at prices far in excess of liquidating value. Let us turn these figure around. Suppose the market price of this stock by the appraisal of one of these investment banking houses such as the one you mentioned were $772 and the liquidating value were $150. Would a fraud have been committed on you if the liquidating value had been offered?

MR. BENDER: Of course it would because--

Q You want it either way.

MR. BENDER: Justice Powell, with all due deference to the assumption behind the question, it is not that I want it either way. I want it that the stockholder be treated

honestly. Honesty requires in a situation like this that if the fair market value is $772, naturally he is entitled to that. And if the majority stockholder knows that the shares are not being traded at all, which is this situation and yet knows that he himself can go out and sell these timberlands for $320 million and pocket that $320 million, if he only pays the minority shareholder on a pro rata $150, he is gaining the difference between that $150 and $772. What could be a clearer case of misappropriation? He did not ask the minority stockholder would he sell it at $150. He told him, "I am taking your stock at $150, like it or not."

Q Mr. Bender, is it correct that your legal theory is that the fraud consists in the failure to make any disclosure before the transaction is completed?

MR. BENDER: My legal theory is--

Q Because you do not complain of the adequacy of the disclosure after the transaction is completed.

MR. BENDER: We do, but I will explain that in a moment. The legal theory is this. Yes, it is non-disclosure. But it is more than non-disclosure. It is a knowing taking. It is a knowing devaluation, a knowing undervaluating.

Q Why does that have to be so? Why would not under your theory any non-disclosure--it is a material non-disclosure if you do not tell the minority shareholder anything until the short-form merger is completed.

MR. BENDER: Because the important thing here is that a fiduciary owes a duty--

Q Of disclosure in advance; is that not your point?

MR. BENDER: More than that. Of a self-deal. He is sitting on both sides of the table.

Q I really want to understand your theory--

MR. BENDER: It must be effectively fair.

Q --Mr. Bender. I am trying to understand your theory, not to debate it with you.

MR. BENDER: That is what I want to say too.

Q Is it critical to your case that there was no disclosure before the transaction was completed?

MR. BENDER: I would say this, that on the facts as they have been presented, it is not critical because in my opinion, whether or not a majority stockholder discloses the facts beforehand or not is irrelevant in a case where he has the ability with a 95 percent ownership to force the transaction on the minority and still deliberately undervalue. But I am stronger than that because I also have non-disclosure.

Q Would you be here if the disclosure had been ten days in advance of the--

MR. BENDER: I would still be here if the disclosure had been ten days in advance.

Q So, you do not quarrel with the Delaware

procedure then?

MR. BENDER: Pardon me?

Q You do not quarrel with the Delaware procedure. You just say--

MR. BENDER: I do quarrel with the Delaware procedure because as far as we are concerned, the Delaware procedure is unconscienable. As Judge Hays stated in the Marshel case, a majority cannot eliminate a minority simply by voting his shares under regular corporate processes. So, what did they do here? Under Delaware law, without any business purpose, they create a dummy corporation solely for the purpose of eliminating the minority.

Q Am I correct in believing you say all of these 30 state short-form merger statutes conflict with Rule 10b-5?

MR. BENDER: In my opinion, sir, they all do conflict because they are performed without any notice to the stockholders and--

Q Would they not also conflict if they provided for notice in advance but did not give the minority shareholder the option to say no? It would still conflict if I understand your theory correctly.

MR. BENDER: In my opinion, any freeze-out--

Q Any freeze-out violates 10b-5.

MR. BENDER: Any freeze-out without business purpose violates 10b-5. I add without business purpose because the

purpose here is just to create a dummy corporation for eliminating the minority.

Q On the business purpose point, what is the minority shareholder's reason for being interested in business purpose if business purpose justifies getting him out of the company?

MR. BENDER: Well--

Q He has no interest in the business purpose after he is out. So, why should that be critical?

MR. BENDER: But business purpose means a purpose other than just to eliminate the minority. These stockholders--it is like the Court said in Lebold--

Q I understand what it means, but I would be interested in your answer to the question.

MR. BENDER: I am sorry.

Q Why is it relevant--why do you attach so much significance to the business purpose of the surviving company as a justification for eliminating the squeezed out shareholder?

MR. BENDER: It is not the business purpose of the surviving company. It is the business purpose of consummating the merger. And there must be a business purpose to consummate the merger, not just to line the pockets of the controlling stockholder. In this particular case the sole purpose of the merger was to increase the ownership of the

majority stockholder from 95 percent to 100 percent, and also to cheat them at the same time.

Q But leaving out the also to cheat, the first part, accepting everything you say, how does that conflict with Rule 10b-5?

MR. BENDER: Because, sir, in my view, a stockholder--

Q Can never be squeezed out. I think your view is he can never be squeezed out no matter what the statute provides.

MR. BENDER: Or cashed. This was a public company.

Q I understand.

MR. BENDER: Santa Fe is a public company.

Q And maybe you are right. I just want to understand your theory.

MR. BENDER: Right. My theory is--and this is not necessary to a holding of Rule 10b-5 in this case. I want to say that so Your Honor understands fully that it is not necessary to my position in this case. You have asked me for my philosophical opinion. My philosophical opinion is that it is wrong to squeeze out a minority stockholder when the parent corporation is a continuing public company. And Santa Fe was a continuing public company, and all they were doing was--

Q Not after they own a hundred percent of the

stock, it is not.

MR. BENDER: Santa Fe was still a continuing--the parent is still a continuing public. All they were doing was squeezing out the minority in one finger of their giant enterprise.

Q Mr. Bender, it seems to me that you are arguing the old doctrine of vested constitutional right of a stockholder never to squeezed out or cashed.

MR. BENDER: Your Honor, this is why I cautioned--made my comment to Justice Stevens. I really do not think--and it really detracts from my argument to get into the question of whether or not my personal philosophy and what I believe happened here also is necessarily a violation of 10b-5. That is really the perimeter of my case. And I want to focus on what I consider to be--and what you asked before, Justice Powell or Justice Stevens, I forget--as to what the heartland of my case is. In heartland my case is this, that when a majority stockholder with his 95 percent ownership uses that 95 percent ownership solely for the purpose of increasing his own onwership from 95 to 100 and at the same time knows that the true value of the shares of the minority is $772 and deliberatley undervalues those shares at $150, then he has misappropriated the difference $150 and $772, and it is an intentional misappropriation under Ernst & Ernst. And for that reason, we have a clear 10b-5 fraud case, and

they used the device--

Q But, Mr. Bender--

MR. BENDER: --of the short-form merger statute.

Q --if this is the heart of your case, then in every short-form merger case or every merger case, all the minority shareholder has to do is allege that the shares have a higher value than they have offered me.

MR. BENDER: No. Your Honor, I am glad you asked that question because this is what we stated in our brief. It is not like we the plaintiffs came in and said this value is $772 a share.

Q Or they allege it is higher and the other side knew it and did not disclose it, did not say so.

MR. BENDER: Right. It is their own knowledge that we are alleging.

Q Let me ask you just one question. When you get into the state appraisal proceeding, can you show the valuation of $320 million?

MR. BENDER: Pardon me?

Q Can you show in evidence?

MR. BENDER: Oh, certainly we can. But that still does not give us an adequate protection because you have stockholders with ten shares, a hundred shares strewn throughout the whole United States. And what it means to go to the State of Delaware is every stockholder has to retain an attorney and

get an appraisal. You know, Your Honors, that as a practical matter, all of the stockholders are not going to do that. And that is the reason these corporations proceed this way, and in Delaware, because the net effect is that if 20 percent of the minority goes to Delaware, that means they have already gotten away with the misappropriation on 80 percent and, to the extent that Delaware does not give a proper and full remedy, then that means as to the other 20 percent they are still going to gain there. This is an incentive, not for a high standard of honesty and fair dealing but, on the contrary, this is an incentive to defraud the minority. And all that this is going to mean is ultimately that people will not have confidence in corporation, because this is not a unique situation. This is happening throughout the country where stockholders--and now there are 39 states, with the lowest state, Nebraska, saying if you have 80 percent ownership, you can do this.

That does not mean that states in the future will not say if you have 50 percent, you can have a short-form merger. And what does this mean? This means the elimination of the minority stockholder. You have a further concentration of wealth. But, in addition to that, people will not buy into corporations in a regular public market for fear that in a two-stage situation--namely, an initial tender offer to get over the required 80 percent and then followed by a freeze-out

merger--people are cheated. That is all this amounts to. This is a simple cheating of minority stockholders because the majority knows the true value is $770 a share, and they paid them $150. What is to stop them from paying them $10 a share or $1 per share?

Q Mr. Bender, are you defending the judgment of the Court of Appeals and its opinion or not?

MR. BENDER: Oh, yes, I certainly am. And the Court of Appeals stated these things.

Q Do you think the Court of Appeals went on the notion that you were cheated?

MR. BENDER: Oh, certainly--

Q Wait a minute. Wait a minute. On the basis that your shares were undervalued?

MR. BENDER: Certainly. That was the prime holding of the Court of Appeals. In Part B of the Court of Appeals decision by Judge Medina, one of the premises--and the assumption in Judge Mansfield's opinion in a footnote--was that the fair value of the shares was $772, and what was being paid was $150 a share.

First of all, if Your Honors would look at--here on page 134a, and this is Judge Medina's decision and conclusion, in his holding. "We hold that a complaint alleges"--and then I will skip.

Q No, do not skip. Just read the rest of the

sentence.

MR. BENDER: Oh, all right. "...a complaint alleges a claim under Rule 10b-5 when it charges, in connection with a Delaware short-form merger, that the majority has committed a breach of its fiduciary duty to deal fairly with minority shareholders by effecting the merger without any justifiable business purpose."

Q Stop right there.

MR. BENDER: Right. That is up to that point.

Q That sounds to me exactly what you said a moment ago to Justice Stevens was your personal philosophical view of the statute.

MR. BENDER: I said that is the perimeter. The perimeter.

Q I know but--

MR. BENDER: That is not necessary to my conclusion.

Q It may not be. I am talking about the Court of Appeals though, what they held.

MR. BENDER: The Court of Appeals thought that was necessary.

Q Well, they--

MR. BENDER: I am not deviating from that. I think that is necessary too. I think--

Q Do you think they felt something else was necessary?

MR. BENDER: Yes. Then they go on. "The minority shareholders are given no prior notice of the merger, thus having no opportunity to apply for injunctive relief, and the proposed price to be paid is substantially lower than the appraised value reflected in the Information Statement."

Q You think that is an essential part of their holding?

MR. BENDER: I think it certainly is. I think that what is most significant here is that the corporation knew that the value was $772 per share and yet paid only $150 per share.

Q And then they go on and say, "We do not hold that the charge of excessively low valuation by itself"--

MR. BENDER: By itself.

Q --"satisfies the requirements Rule 10b-5."

MR. BENDER: And I think what they mean there is that if we were a stockholder and if it was in a situation where you have an arm's length negotiation and no self-deal--that is what they are talking about. And, in addition, even arguendo they are certainly not talking about our situation because here the plaintiffs did not opine that the true worth was $772. Our case is much narrower. Our case is that the majority stockholder knew that the true value was $772 and yet paid $150, and that is a fraud.

MR. CHIEF JUSTICE BURGER: Your time is up,

Mr. Bender.

MR. BENDER: Thank you, Your Honor.

MR. CHIEF JUSTICE BURGER: Mr. Glendon, you have about three minutes left.

REBUTTAL ARGUMENT OF WILLIAM R. GLENDON, ESQ.,

ON BEHALF OF THE PETITIONERS

MR. GLENDON: The plaintiff I think proceeds from an erroneous assumption as to the facts of life in this case. He is taking an asset valuation and basing on an asset valuation, which is only one element of stock valuation, is charging a fraud and charging undervaluation. Of course that just is not the fact--

Q We assume, do we not, that there was undervaluation for the purposes of this case?

MR. GLENDON: For the purpose of the motion--

Q That is right.

MR. GLENDON: --we of course have to concede. We do not, however, concede anything like the values--

Q We also assume, do we not, or take as true, the allegation that the majority stockholder knew it was worth more?

MR. GLENDON: No. There was no such allegation. They do not make that allegation, and that is the point here. You have to read their complaint. They charge as a legal conclusion that there was a fraudulent appraisal. But you have

to consider it in the light of what was disclosed. And every fact that the plaintiff says constitutes a fraudulent appraisal was disclosed. Would your case be different if we took it as true that the majority stockholder did know it?

MR. GLENDON: Knew that there was a fraudulent appraisal?

Q No, not knew that it was fraudulent but knew that the stock was worth more than the appraisal.

MR. GLENDON: And did not disclose it.

Q It disclosed all the facts, they had an appraisal from Morgan Stanley, and yet they said--they put in this report--that the liquidation value was much higher.

MR. GLENDON: Mr. Justice White, we are dealing with an intangible. We are dealing with a value. And we can do no more than disclose all the facts that we know and have an independent appraisal, and give him all the facts that we have and then disclose all into the stockholders who must make the investment decision.

Q So, your answer to my last question is that it would not make any difference in your case. I mean, you would still be here arguing as you are arguing, that it is not a 10b-5 violation even if the majority stockholder knew; is that right?

MR. GLENDON: Yes.

Q Or not?

MR. GLENDON: If the majority stoockholder put out what he knew to be a fraudulent appraisal and did not disclose it--

Q I thought that was not the case.

MR. GLENDON: That is what we are talking about, Mr. Justice White. We are talking about disclosure.

Q I know, but let us just assume this case is exactly the way it is except for one thing--

MR. GLENDON: Yes.

Q --and that is just add and assume that the majority stockholder knew that the stock was worth more.

MR. GLENDON: Then I think he would be misleading by not disclosing what he knew. But he does not have anything here to know any more than was on the record.

Q Was he supposed to disclose his opinion that it is worth more or what?

MR. GLENDON: No, I think in terms of opinion, no. I think the only thing he can really disclose is facts.

Q He put--

MR. GLENDON: You cannot commit a fraud, I do not believe, by an expression of an opinion, particularly in this area.

Q He disclosed all the facts on the basis of which a valuation judgment would be made?

MR. GLENDON: Yes. Yes. That is right.

Q And on that basis you say it could not be a 10b-5?

MR. GLENDON: That is right, yes. When he makes that--

Q Whatever his private opinion was of the value.

MR. GLENDON: That is right. That would be our position, Mr. Justice White. I think--

MR. CHIEF JUSTICE BURGER: Your time is up, Mr. Glendon.

MR. GLENDON: All right.

MR. CHIEF JUSTICE BURGER: Thank you, gentlemen, the case is submitted.

[Whereupon, at 10:58 o'clock a.m., the case was submitted.]

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