

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE

VFB LLC,)
Plaintiff,)
v.) Civil Action No. 02-137 KAJ
CAMPBELL SOUP CO., et al.,)
Defendants.)

POST-TRIAL FINDINGS OF FACT AND CONCLUSIONS OF LAW

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JORDAN, District Judge

I. INTRODUCTION

VFB L.L.C. ("VFB") brought this action against Campbell Soup Company, Campbell Investment Company, Campbell Foodservice Company, Campbell Sales Company, Campbell Soup Company, LTD. (Canada), Joseph Campbell Company, Campbell Soup Supply Company, L.L.C., Campbell Soup Company L.L.C., Northeastern Products Company, Southeastern Wisconsin Products Co., Inc., and Pepperidge Farm, Incorporated (collectively "Campbell"), alleging that Campbell engineered a fraudulent transfer from VFB's predecessor in interest, Vlasic Foods International Inc. ("VFI"), to Campbell of more than \$600 million in cash and assumed liabilities, that Campbell controlled VFI's directors and caused them to breach their fiduciary duties to VFI, that VFI illegally paid dividends to Campbell, that Campbell was the alter ego of VFI, and that Campbell's Proof of Claim against VFI's bankruptcy estate is either voidable or should be equitably subordinated. (Docket Item ["D.I."] 45, ¶ 699-759.) The following are my post-trial findings of fact and conclusions of law, issued pursuant to Federal Rule of Civil Procedure 52(a).

II. FINDINGS OF FACT¹

A. Parties

1. Plaintiff VFB is the successor-in-interest to VFI (D.I. 45 at ¶ 3, the "Complaint"), which was a wholly-owned subsidiary that Campbell spun-off to its shareholders (the "Spin" or "Spin-off") on March 30, 1998. (Defendant's Trial Exhibit ["DTX"] 501 at '1552.)² Campbell transferred to VFI a group of businesses (the "VFI Businesses") which had been grouped together within Campbell prior to the Spin and were known as the "Specialty Foods" division. (D.I. 356, n.9.) As part of the Spin-off, Campbell also transferred a \$500 million debt obligation to VFI. (D.I. 285, Ex. A, ¶ 15.) On the date of the Spin-off, Campbell transferred its shares of VFI stock to its shareholders, so that Campbell's shareholders then owned shares of Campbell and, separately, shares of VFI.³ (*Id.*, ¶ 3.)

2. For reasons discussed in detail herein, VFI did not succeed as an independent company, see *infra*, ¶¶ Findings of Fact ["F"] 72-91, and, on January 29,

¹Throughout these Findings of Fact and Conclusions of Law, I have adopted without attribution language suggested by one side or the other in this dispute. In all such instances, the finding or conclusion in question has become my own, based upon my review of the evidence and the law.

²Citations to page numbers over four digits have been abbreviated using an apostrophe. All abbreviated citations are to documents of such length that the last four digits of the page number is adequate for accurate identification of the cited page.

³Campbell and VFI's fiscal years (FY) ran from August through July, ending the Sunday closest to July 31. (D.I. 285, Ex. A at ¶¶21, 22.) Campbell spun-off VFI on March 30, 1998, two months into the third quarter of Campbell and VFI's FY1998. (*Id.*) The Specialty Foods division was created in the beginning of FY1998 and operated within Campbell until it was transferred to VFI during the Spin-off. See *infra*, ¶¶ F45, F56.

2001, it filed a petition for reorganization under Chapter 11 of the Bankruptcy Code, (D.I. 45, at ¶¶ 1, 3). VFB was created pursuant to VFI's Chapter 11 plan to permit creditors an opportunity to pursue the claims now at issue. (*Id.*)

3. The majority (95.8%) of the VFB creditor interests, measured by value, arose from a \$200 million subordinated, unsecured bond offering conducted approximately fifteen months after the Spin-off. (DTX 618 at '9014; DTX 501; D.I. 318 at 1603:7-17 (McCarthy⁴).) The bonds were issued by VFI pursuant to full SEC disclosure on June 29, 1999. (*Id.*) Another creditor interest represented by VFB is VFI's headquarters landlord, whose allowed claim in the bankruptcy is \$1.66 million. (Plaintiff's Trial Exhibit ["PTX"] 1114; PTX 1122; D.I. 318 at 1586:9-23 (McCarthy).) Campbell entered the lease before the Spin-off, and VFI assumed it on the date of the Spin. (PTX 632 at '408; D.I. 318 at 1586:24-87:11 (McCarthy); PTX 705.) VFB also represents the interests of various employee claimants who joined VFI from Campbell in the Spin-off. (D.I. 318 at 1586:3-8 (McCarthy); D.I. 319 at 1911:18-12:3 (Carter⁵); D.I. 317 at 1208:25-10:2 (Lummis⁶); PTX 15.) Lastly, VFB represents trade creditors.

⁴ Unless the identity of a deponent is already clear from the text, citations to transcripts are followed by a parenthetical identifying the deponent or a reference to a page herein where the identity is explained. Where a citation identifying a deponent appears for the first time in a footnote, rather than in text, the parenthetical follows immediately after the name. Ms. Kathy M. McCarthy is a tax attorney who was asked by Campbell in "late August or early September" of 1998 to assist in the possible sale of VFI assets. (D.I. 318 at 1543:18-25, 1544:1-6 (McCarthy).)

⁵ See *infra*, ¶ F17.

⁶ Eric Lummis ran the Campbell Customer Service Center from its formation until the Spin-off closed. (D.I. 317 at 1161:25, 1162:1 (Lummis).)

(D.I. 318 at 1589:2-6, 1592:5-20 (McCarthy); PTX 1132; PTX 1223; PTX 1224; DTX 618 at '9008-12.)

4. Defendant Campbell Soup Company is a public company organized under New Jersey law. The other defendants are corporate affiliates of Campbell Soup Company. (D.I. 45 at ¶¶ 6-15.)

B. The Decision to Spin-Off VFI

5. Beginning in 1996, Campbell initiated a strategy to improve its performance. It perceived itself as already being "Best in Class," in the sense of being among the best food companies, but it wanted to move to "Best in Show," ranking with the best consumer products companies. (PTX 91 at '1055; D.I. 318 at 1717:19-1718:25 (Walker⁷)). Working with its financial advisor, Goldman Sachs & Co. ("Goldman"), Campbell's management identified a number of strategies to achieve that ambition, including reconfiguring its portfolio of businesses. (PTX 201 at '1013-15; PTX 91 at '1055, '1068.) The planned reconfiguration was to consist of identifying and keeping core businesses, evaluating speciality businesses, and, following the evaluation, divesting non-performing ones. (PTX 91 at '1068.)

6. Goldman recommended that Campbell spin-off non-strategic businesses to Campbell's shareholders. (PTX 233 at '9650.) According to Goldman, the spin-off could be accomplished relatively expeditiously and with no tax impact on Campbell, the newly spun company, or their shareholders. (PTX 233 at '9645; PTX 241 at '0885.)

⁷Tom Walker is the "Managing Partner or Managing Director at Goldman." (D.I. 318 at 1702:2 (Walker).)

7. Campbell decided to take “aggressive action” to achieve Best in Show status and, in keeping with Goldman’s advice, began exploring a leveraged spin-off it dubbed “Project Sweetpea.” (PTX 101 at ‘9414; D.I. 317 at 1244 (Anderson⁸); D.I. 318 at 1726-29, 1733 (Walker); PTX 174 at ‘487; D.I. 315 at 606 (Lord⁹); D.I. 319 at 1978-79 (DiSilvestro¹⁰); 200 at ‘8745.) Many of the business that were ultimately included in the VFI Spin-off were included in the early Project Sweatpea planning.¹¹ (*Id.*)

8. Campbell and Goldman contemporaneously explained in Project Sweetpea documents, and other related documents, Campbell’s purpose in pursuing the Spin-off. Campbell believed that selling the businesses singly was “not attractive” and would be “time consuming,” that it would involve “business difficulties,” divert management attention, and depress Campbell’s earnings per share. (PTX 172 at ‘7032; PTX 174 at ‘3487.) However, Campbell was also concerned that selling the businesses as a group would raise “uncertainty” and result in a “price discount,” as the

⁸ See *Infra*, ¶ F12.

⁹ See *Infra*, ¶ F23.

¹⁰Anthony DiSilvestro was the Vice President/Treasurer of Campbell and, before the Spin, of VFI as well. (D.I. 319 at 2036:19-23 (Emmet (Richard Emmet was a Director of Strategic Planning and Corporate Development at Campbell (D.I. 319 at 2024:7-8 (Emmet))))).

¹¹For a description of all of the different lines of businesses included in the Spin-off see *infra*, ¶ F28.

sale would be "limited to financial buyers."¹² (PTX 172 at '7032; PTX 174 at '3487; D.I. 318 at 1733-34 (Walker); D.I. 319 at 1981-82 (DiSilvestro).)

9. By comparison, Campbell viewed a spin-off as a transaction that could be "completed quickly," had "certainty," would "minimize senior management time," and was "potentially tax free." (PTX 172 at '7031, 7033; PTX 174 at '3487; D.I. 318 at 1733, 1736 (Walker).)

10. Further, Campbell decided that, by leveraging the Spin-off, it could "receive value similar to a sale" while "control[ling] the process." (PTX 172 at '7033; D.I. 317 at 1249 (Anderson); PTX 174 at '3487; PTX 173; D.I. 318 at 1733, 1749, 1753 (Walker); PTX 180 at '0731; PTX 233 at '9648.)

C. Selecting the Management Team

11. During the initial phases of the Spin-off planning, David W. Johnson was Chief Executive Officer ("CEO") and Chairman of the Board of Directors of Campbell. (D.I. 322 at 3038:1-7 (Johnson).) He resigned his position as CEO in July of 1997, but continued to serve as Chairman of the Board. (*Id.*)

12. In March of 1996, Campbell hired Basil Anderson to be its Chief Financial Officer ("CFO"). (D.I. 315 at 606 (Lord).) As CFO, Mr. Anderson was heavily involved with the planning and financial aspects of the Spin-off. (D.I. 315 at 606-607 (Lord).)

13. In 1997, in anticipation of Mr. Johnson's stepping down as CEO, Dale Morrison and Robert Bernstock were competing to be his successor. (D.I. 322 at

¹²The reason for that concern was Campbell's belief that other food companies would not view the VFI Businesses, as a group, as a strategic addition. (D.I. 318 at 1733-34 (Walker).)

3029:4-7 (Sripada¹³.) After a “very close vote,” Mr. Morrison was selected to become Campbell’s new CEO and began his tenure in July of 1997. (D.I. 322 at 3051:3-6, 3054:7-16 (Johnson).)

14. Mr. Bernstock was naturally disappointed that he was not selected for the position. (D.I. 322 at 3054:18 (Johnson).) Shortly after receiving the news, he asked Mr. Johnson to recommend him to Campbell’s Board as the CEO for the contemplated Spin-off company, which came to be known as VFI. (D.I. 322 at 3054:22-25, 3055:1-7 (Johnson).)

15. Mr. Johnson had reservations about Mr. Bernstock’s ability to manage a highly leveraged business. (D.I. 322 at 3055:25, 3056:1-23 (Johnson).) Mr. Johnson was concerned that, given Mr. Bernstock’s background in marketing, he was not accustomed to managing a business for cash.¹⁴ (*Id.*) Mr. Johnson believed that Mr. Bernstock would still do a good job, however, because he was a “top executive” and had “conquered assignment after assignment” in many different roles at Campbell. (D.I. 322 at 3059:17-3060:7, 3055:21-24 (Johnson).) Mr. Bernstock was ultimately selected to be the CEO for the newly formed VFI. (D.I. 322 at 3060:6-12 (Johnson).)

¹³Before the Spin-off, Srinivasa Sripada was a marketing manager for Swanson. (D.I. 322 at 2991:4-5 (Sripada).)

¹⁴ At trial, one of Campbell’s expert witnesses, Michael Silverstein, explained that “managing a company for cash” meant that money should not be invested in advertising, research and development, or any type of innovation. (D.I. 323 at 3372-73 (Silverstein).) In addition, expenses should be minimized in order to maximize the amount of cash generated. (*Id.*) Mr. Silverstein is a Senior Vice President at the Boston Consulting Group. In 1997 he was hired by Campbell “to take an independent view as to whether or not [the Spin-off] made sense.” (D.I. 323 at 3351:9-16, 3353:2-4 (Silverstein).)

16. Kathleen MacDonnell was the Campbell executive who had been running the businesses that ultimately formed the bulk of VFI's operations, namely Vlasic brand pickles and Swanson brand frozen foods. (D.I. 322 at 3059:2-16 (Johnson); 2434:1-5 (Bernstock).) Ms. MacDonnell also wanted to be chosen to lead the contemplated spin-off company. (*Id.*) She believed that Vlasic and Swanson were burdened with unnecessary overhead costs and that, if she could run those businesses outside of Campbell's bureaucracy, she could increase their value. (D.I. 322 at 3059 (Johnson).) After Mr. Bernstock was selected to head VFI, Ms. MacDonnell left Campbell to join another company. (D.I. 322 at 3060-61 (Johnson).)

17. In September 1997, Norma Carter, who was a lawyer in Campbell's in-house legal department, was selected as the general counsel of VFI. (D.I. 319 at 1832 (Carter).) In her 17 years at Campbell, Ms. Carter had acquired extensive experience in mergers and acquisitions, had served as counsel to the Swanson business and other Campbell subsidiaries, and had "significant experience" drafting and negotiating supply and co-packing agreements. (D.I. 319 at 1916:19-1919:21, 1920:20-1921:19, 1922:16-1923:7 (Carter); D.I. 321 at 2842:5-2843:3 (Lipscomb¹⁵)).

18. Ms. Carter was told that there was a strong possibility that if she stayed with Campbell she would be elevated to the position of General Counsel. (D.I. 319 at 1925-26 (Carter).) Nevertheless, when given the choice between potentially becoming General Counsel for Campbell or becoming general counsel for VFI, Ms. Carter chose

¹⁵ See *Infra*, ¶ F23.

VFI, based on what she termed "a lot of knowledge" she had acquired about the Spin-off. (*Id.*)

19. Many other well-regarded Campbell executives who were familiar with the VFI Businesses chose to cast their lot with VFI. James Dorsch, who joined VFI as head of the pickle business, had worked at Vlasic for over 10 years and was very familiar with its operations. (D.I. 315 at 293:23-25, 296:19-297:2 (Dorsch).) Mark McCallum, who joined VFI as the head of its mushroom production business, had been running that business within Campbell for a year before the Spin-off. (PTX 1 at '0926; D.I. 321 at 2592:9-2393:2 (McCallum).) Carlos Funes had been CEO and President of Swift, a processed meat business, since 1983, and he remained as CEO of Swift-Armour ("Swift") after the Spin-off. (PTX 1 at '0925; D.I. 322 at 3183:2-9, 3184:4-6 (Funes).) For the role of CFO, VFI brought in an outsider, William R. Lewis. (D.I. 314 at 83:24-25, 84:1 (Lewis).)

20. That seasoned executives familiar with the businesses that came to constitute VFI chose to join VFI demonstrated that thoroughly knowledgeable people believed the Spin-off would be a successful venture.

D. Negotiations Between VFI and Campbell

21. Campbell recognized that VFI's viability depended on finding an aggressive and highly accomplished CEO. (PTX 303.) However, Campbell also recognized that negotiating with such a CEO over the terms of the Spin-off would be problematic if certain terms were not identified beforehand as being non-negotiable. (*Id.*)

22. The non-negotiable terms included (1) the businesses and assets to be transferred, (2) areas and terms of non-competition between Campbell and VFI, (3) the initial debt level for the new company, (4) the protocol for handling external communications, (5) transition service fees payable to Campbell, and (6) restrictions on soliciting Campbell employees. (PTX 302 at '262; PTX 303 at '156-57; D.I. 322 at 2943-44 (Lipscomb); PTX 233 at '648; D.I. 318 at 1753 (Walker); D.I. 320 at 2405-06, 2431-32 (Bernstock); PTX 330 at '226; PTX 324 at '662.)

23. Mr. Lord, Mr. DiSilvestro, and Ms. Lipscomb, all three of whom were Campbell executives before and after the Spin-off, served as VFI's pre-Spin directors. (D.I. 321 at 2806-07 (DiSilvestro); D.I. 321 at 2853-54, 2857, 2927 (Lipscomb); D.I. 316 at 650 (Lord).) As VFI directors, they approved the agreements reached between negotiators from VFI's management team and negotiators for Campbell. (*Id.*)

24. Mr. Bernstock and Ms. Carter represented VFI in discussions regarding the negotiable aspects of the Spin. (D.I. 321 at 2853:3-2854:12 (Lipscomb); D.I. 319 at 1832 (Carter).) Campbell, however, still held most of the power in these negotiations and dictated many of the terms of the ultimate agreement. (PTX 233 at '648; D.I. 318 at 1753 (Walker); D.I. 320 at 2405-06, 2431-32 (Bernstock); PTX 324 at '662.) Examples of agreements in which Campbell drove a particularly hard bargain included certain co-packing agreements¹⁶ for frozen foods and supply agreements for mushrooms.

¹⁶Co-packing is when one company packages food and another company sells that food under its own brand. (D.I. 319 at 1877-78 (Carter).)

25. With respect to co-packing, VFI entered into short-term agreements where VFI would package food for Campbell at bargain rates. (PTX 12 at §3.1, Sch. B; D.I. 316 at 725:7-19, 726:16-23 (Czerpak); D.I. 317 at 1326:1-7 (Parker¹⁷); D.I. 319 at 2077:17-20 (Miller); D.I. 321 at 2910:14-20 (Lipscomb).) When negotiating the supply agreements for mushrooms, Campbell changed the way in which it had historically ordered mushrooms and began insisting on much lower minimum orders. (D.I. 314 at 271:1-72:25 (Reitnauer); D.I. 317 at 1360, 1362-63 (Parker).)

26. VFI was not powerless in these negotiations, however. The mere threat that the Spin-off might not be completed in a timely manner, and the potential financial effect of such a failure, gave VFI some negotiating leverage. (See PTX 303.) Despite later complaints from VFB witnesses, it appears that Campbell's negotiations with VFI were at arm's length, with qualified and competent negotiators on both sides of the table.¹⁸ That VFI representatives may have been unhappy with terms they believed favored Campbell is a natural result of the give and take of negotiation. Even if Campbell and VFI had not been related, the size and market power of Campbell gave it extraordinary leverage in negotiations with its suppliers. It used its power to extract concessions from longtime friends and coworkers at VFI, which was distressing to them but was not hidden from anyone.

¹⁷ Steven Parker was Director of Worldwide Purchasing for Campbell at the time the Spin-off was announced. (D.I. 317 at 1276:6-11 (Parker).)

¹⁸ Ms. Carter, who was one of the people in charge of those negotiations, had extensive experience negotiating on behalf of Campbell. See *supra*, ¶ F17.

E. The VFI Businesses

27. While the management teams for VFI and Campbell were negotiating the terms of the Spin-off, another contentious negotiation was occurring between the two camps over how the VFI Businesses would be operated during the period leading up to the Spin-off. See *infra*, ¶¶ F45-53. To understand how the pre-Spin operation of the VFI Businesses affected Campbell, it is necessary to examine the financial condition of the VFI Businesses and the impact they had on Campbell.

28. The businesses that were ultimately included in the Spin-off were, by Campbell's estimation, underperforming businesses, businesses with low growth potential, or businesses with low profit margins. See *infra*, ¶¶ F29-39. They included: (1) Vlasic, a U.S. retail and food service line, predominantly selling pickles and condiments; (2) Swanson, a U.S. retail frozen food line; (3) Swanson Canada, a Canadian retail frozen food line; (4) Vlasic Farms, a line of fresh mushrooms; (5) Swift-Armour ("Swift"), an Argentinean processed beef line; (6) Open Pit, a Midwest regional barbecue sauce line; (7) Stratford-Upon-Avon ("SonA"), a U.K. canned beans and pickled vegetables line; (8) Freshbake, a U.K. frozen foods line; and (9) Kattus, a German specialty foods distribution company.¹⁹ (D.I. 45, ¶ 83.)

29. The two most valuable companies included in the Spin-off, and the two that were intended to form the strategic core of the new company, were Swanson and Vlasic. (PTX 269 at '9157; D.I. 323 at 3371-72 (Silverstein).) The rest of the included

¹⁹The names of these businesses are short-hand designations given by the parties. Some of the businesses may have been separate companies, while others were only products lines within a company. Such distinctions were not made by the parties nor are they relevant in this dispute.

businesses generally had declining sales, unpredictable profits, and low value. (PTX 269 at '9160; D.I. 323 at 3372-73 (Silverstein).) According to a consultant hired by Campbell, these other companies should be managed solely for cash; money should not be invested in advertising, research and development, or any type of innovation. (D.I. 323 at 3372-73 (Silverstein).)

30. Although Swanson and Vlasic were profitable companies, they did not have strong growth prospects prior to the Spin, which was part of the reason they were spun-off. (PTX 248 at '0957; PTX 269 at '159; PTX 261 at '591.) They did, however, have strong brands and a history of stable revenue, earnings, and cash flow performance. (*Id.*)

31. Vlasic is a company famous for its pickles. For 15 years prior to the Spin-off, Vlasic held between 27% and 31% of the U.S. pickle market. (DTX 648 at '372, '376-8; D.I. 354 at 4388:20-4389:11 (Bess²⁰)) Vlasic had "better margins by far than most food companies" (DTX 28 at 2), had strong brand equity, enjoyed a leading position in the market, and was profitable. (D.I. 323 at 3374:10-23 (Silverstein); D.I. 354 at 4432:2-8 (Bess).)

32. From 1984 until 1994, however, sales of Vlasic pickles decreased on average 1.8% per year. (PTX 1196.) In 1994, Vlasic successfully introduced a product consisting of pickles sliced lengthwise, which it called "Sandwich Stackers.". (D.I. 315 at 297 (Dorsch); PTX 1196; PTX 1176; PTX 1037 at '238; D.I. 320 at 2401 (Bernstock);

²⁰John Bess, is currently an employee of IBM in their Business Consulting Services Division. He testified as an expert on behalf of Campbell. (D.I. 354 at 4379, 4381:10-25, 4382:1-5 (Bess).)

D.I. 315 at 501 (Silverstein); PTX 248 at '955; PTX 269 at '194; D.I. 351 at 3648 (Blattberg²¹).) The introduction of Sandwich Stackers increased consumption of Vlasic pickles, increased margins for Vlasic, and was a driving force behind record earnings for the brand in FY1996/1997. (*Id.*)

33. Although there was an upturn in the sales of Vlasic pickles through FY1996/1997, Vlasic increased its income during this time primarily through increased prices and hence increased margins. (PTX 1196; PTX 1176; PTX 1037 at '238; D.I. 315 at 501 (Silverstein); PTX 248 at '955; PTX 269 at '194; D.I. 351 at 3648 (Blattberg).)

34. By mid-FY1997, competitors had introduced products similar to Sandwich Stackers, which curtailed Vlasic's growth spurt. (D.I. 315 at 298, 363 (Dorsch); PTX 276 at '539; PTX 260 at '584; D.I. 315 at 501-02 (Silverstein); PTX 248 at '955.) Vlasic, however, was still considered to have the prospect of future growth.

35. Swanson, the owner of a well-known frozen food brand, was the other company that formed the core operations of VFI. (PTX 269 at '159; PTX 261 at '591; D.I. 315 at 513 (Silverstein).) Although Swanson was a relatively large company, it was a "[s]lowly shrinking business, ... losing volume share," in a "[l]ow growth category," with "significant and growing challenges from" competitors, and "[h]igh fixed cost manufacturing." (*Id.*) Campbell was advised by its consultants that, if Swanson were

²¹Robert C. Blattberg is "Polk Brothers Distinguished Professor of Retailing at the Kellogg School of Management, Northwestern University." He was "asked to evaluate the state of three major businesses for VFI: Vlasic Pickles, Swanson Frozen Foods and Open Pit Barbecue Sauce." (D.I. 351 at 3586:22, 3587:1-2, 3589:17-25, 3590:1-3 (Blattberg).) At trial he testified as an expert for VFB.

run as it had been, these "trends [were] likely to continue" with "[w]orsening [f]inancial [p]erformance," resulting in a steady decline in future earnings. (PTX 261 at '591; PTX 250 at '105-06; D.I. 315 at 507-08, 513 (Silverstein).) The Swanson brand, however, had a strong heritage, with brand equity and a loyal consumer following. (D.I. 323 at 3375:6-3376:10 (Silverstein); D.I. 354 at 4390:22-4391:3, 4432:9-12 (Bess).) Prior to the Spin-off, it was believed that, if Swanson were managed more effectively, those strengths could be used to turn around the business. (*Id.*)

36. Consequently, although Vlasic and Swanson were viewed as under-performing companies and non-strategic within Campbell's portfolio of businesses, they were nevertheless solid, stable brands that were capable of forming the foundation of a newly created company.

37. In contrast, the seven remaining companies that were to make up VFI had generally been poor performers and were viewed as having very limited upside potential. The strongest of the remaining companies was Swift. Swift was an Argentinian company that sold beef on the world market and in its domestic market. (PTX 924 at '763.) It had a history of stable earnings and had moderate growth prospects. (PTX 269 at '160.)

38. Prior to the Spin-off, Campbell purchased beef from Swift at a price established by Swift's cost of production plus a 5% mark-up. (D.I. 317 at 1291 (Parker); PTX 63 at '971; D.I. 322 at 3189 (Funes).) Immediately before the Spin-off, that price was 20% above the then-prevailing market price. (*Id.*) This above-market purchase price, of course, increased Swift's profits. Sales to Campbell, however, accounted for less than 20% of Swift's overall sales. (PTX 362 at '756.)

39. The rest of the businesses included in the Spin-off had declining sales, unpredictable earnings, and low value. (PTX 269 at '160.) These businesses were not viewed as having strategic value for VFI, so it was recommended that they be managed purely for cash. (*Id.*)

1. FY1997 Financials

40. The Form 10 filed with the Securities and Exchange Commission (the "SEC") to describe the Spin-off showed that the VFI Businesses had \$116 million of earnings before interest and taxes ("EBIT") in FY1997.²² (PTX 1 at '026.) That figure, however, was not entirely reliable, because the financial results for the Swanson business segment had been inflated. In April of 1997, the management of Swanson had projected that the business would earn \$40 million of EBIT for the fiscal year, which was \$10 million below its \$50 million target. (PTX 163; D.I. 315 at 467 (Applegate²³); D.I. 315 at 620 (Lord).) To help close the gap, Swanson's management recommended, among other things, that the company "load" products,²⁴ change its deduction

²²EBIT is often used to measure how profitable a company is, without regard to debt.

²³Stanley Applegate was the Assistant Controller for Business Planning at Campbell, until becoming Campbell's Finance VP in the spring of 1998. (D.I. 315 at 446:12-16 (Applegate).)

²⁴Product "loading" occurs when a company increases sales and shipments of a product to retailers without there being a corresponding increase in consumption. The shipments increase the inventory carried by retailers or consumers but allow the manufacturer to book increased revenue. (D.I. 351 at 3600 (Blattberg).)

assumptions, use corporate reserves, and create more "last in first out" ("LIFO")²⁵ gains. (PTX 163 at '843; D.I. 315 at 619-20 (Lord).)

41. It is unclear to what extent these suggested tactics were employed, but it is clear that business was not carried on as usual. One unusual step was the initiation of a special sales promotion in the 4th quarter of the fiscal year. Swanson normally ran four promotions a year to encourage customers to purchase Swanson frozen dinners. (D.I. 316 at 804-05 (Kessler²⁶)). In June/July 1997, during the 4th quarter of its fiscal year and at a time of year when Swanson usually did not specifically promote its products, Swanson added a fifth promotion, the so-called "5th deal," to increase its sales and earnings. (PTX 142; D.I. 318 at 1636-1642 (Adler²⁷); D.I. 316 at 705, 743 (Czerpak); D.I. 316 at 804-05 (Kessler); D.I. 322 at 3006-07 (Sripada); D.I. 317 at 1195-96 (Lummis).)

42. The "5th Deal" employed heavy discounting, sweepstakes, and coupons to create a "huge spike in the business," selling 1.3 million more cases of product than had been sold in the 4th quarter of the previous year. (PTX 1037 at '235; D.I. 316 at 830-31, 833-34, 854 (Kessler); D.I. 318 at 1637-38 (Adler); D.I. 320 at 2465-68,

²⁵According to one of VFB's experts, LIFO accounting allows a company to book paper gains by permitting its inventories to run low. (D.I. 352 at 3983:12-17 (Owsley(see *infra*, n.41))).

²⁶Murray Kessler was President of the Swanson Division at VFI before leaving in November of 1999. (D.I. 316 at 762:25, 763:1-9 (Kessler).)

²⁷Joseph Adler was Vice President, Controller of VFI after the Spin-off. (D.I. 318 at 1610:11-16 (Adler).)

2471-72, 2580- 81 (Bernstock); PTX 142 at '757, ¶ 8; DTX 550 at '505; D.I. 317 at 1236-37 (Lummis); DTX 87 at 4; D.I. 354 at 4406 (Bess).)

43. VFB argues that the "5th deal" resulted in a "pantry load," meaning that consumers bought more Swanson products than they normally would have, stored the extra product at home, and consequently bought less from Swanson in the months afterwards. (D.I. 356, ¶ F47.) The sales records for Swanson, however, do not show a drop in sales in the next two quarters, undercutting the conclusion that there was pantry loading. (DTX 550 at '3505.) Nevertheless, the "5th deal" increased FY1997 earnings in an artificial manner, because the full costs of that promotion were not recorded until FY1998. The exact amount of those unrecorded costs is unknown. (D.I. 320 at 2581 (Bernstock); PTX 377 at '466.)

44. Swanson reported \$48 million in EBIT in FY1997, despite a 7% decline in consumption, because it cut advertising, created the "5th Deal," delayed scheduled maintenance,²⁸ and under-accrued trade spending. (D.I. 315 at 399 (Bernstock), D.I. 320 at 2473-74 (Bernstock); PTX 1037 at '235-36.) As Swanson had been projecting \$40 million in EBIT before it utilized those tactics, and it recorded \$48 million in EBIT after using them, it is reasonable to conclude that they were responsible for the approximately \$8 million increase in EBIT. Consequently, since those tactics chiefly involve cost-shifting, much of that \$8 million increase was at the expense of FY1998

²⁸Swanson's scheduled July 1997 plant shutdowns were moved into FY1998, shifting almost \$1 million of Swanson's overhead and expenses into FY1998. (D.I. 316 at 705-06 (Czerpak); PTX 166 at ¶ 4; PTX 150 at '632; D.I. 315 at 591 (Wright (William Wright was the Director of Operations Analysis for Swanson and Vlasic); PTX 276 at '544.)

EBIT.²⁹ This shifting of costs into FY1998 and the consequent inflation of FY1997 EBIT added to the difficulties VFI would face in FY1998.

2. FY1998 Financials

45. In anticipation of the Spin-off, Campbell reorganized at the beginning of FY1998 all of the VFI Businesses into what it named the "Specialty Foods" division.³⁰ The management team that was selected to run VFI became responsible for the operation of the Speciality Foods division. (See D.I. 320 at 2412, 2548-49 (Bernstock); D.I. 314 at 94-95 (Lewis); D.I. 315 at 315-16 (Dorsch).)

46. Despite the struggle Swanson had experienced in reaching its FY1997 EBIT target, the managers of Swanson, at the behest of Campbell's management, set an EBIT target of \$57.6 million for FY1998, a 20% increase over the previous year. (PTX 165 at '971; D.I. 315 at 592 (Wright); D.I. 320 at 2400 (Bernstock); D.I. 315 at 470-71 (Applegate).)

47. Campbell executives were highly motivated to see VFI managers meet the Specialty Foods division's financial projections, no matter how unrealistic. (D.I. 319 at 1842-43 (Carter); PTX 528 at '344.) Those executives were part of an incentive program that rewarded them with significant bonuses, if they met their financial targets for three years in a row. (*Id.*) They had already achieved their FY1996 and FY1997

²⁹It is likely that the "5th deal" also legitimately increased FY1997 EBIT to some unknown degree.

³⁰VFB describes this reorganization in its proposed Findings of Fact and Campbell does not refute it. (D.I. 356 at 33, fn. 9.)

projections, and, naturally, wanted to meet their FY1998 projections in order to receive their bonuses.³¹ (*Id.*)

48. In FY1998, there were two particularly important earnings figures in the reported financial results for the Specialty Foods division. One was the year to date ("YTD") earnings for the second quarter, and the other was YTD earnings up until March 30, 1998, the date of the Spin-off (the "Spin-off YTD Earnings"). Second quarter YTD earnings were important because they were included in the pro-forma earnings section of the Spin-off disclosure document, *i.e.*, the Form 10. (PTX 1 at '905-06.) The Spin-off YTD Earnings were important because the Specialty Foods division's earnings for that period of time were attributed to Campbell.

49. The original FY1998 EBIT target for VFI, which included the Specialty Foods division results prior to the Spin-off, was \$159 million. (D.I. 320 at 2412 (Bernstock).) It was an unrealistic goal, and the first quarter began to prove it so. The Specialty Foods division's first quarter EBIT was \$33 million, 23% below target.³² (PTX 505 at '051; D.I. 315 at 627 (Lord).) Mr. Anderson, Campbell's CFO, pressured the management of the division to meet their target earnings for the second quarter,

³¹The unrealistically high numbers were, it appears, largely driven by the self-interest of Campbell executives like Basil Anderson and Anthony DiSilvestro, who had significant personal financial incentives at stake, because of Campbell's incentive program.

³²Plaintiff alleges that "the VFI businesses [the Specialty Foods division] were \$23 million behind FY1998 plan by December." (D.I. 356, ¶ F223.) A proper reading of the cited document, however, reveals that the number contained in the document referred to the division's percentage behind plan, not the amount behind plan. (PTX 505 at '051.) Doing the arithmetic, it appears that, by December, the Specialty Foods division was about \$9.9 million behind plan YTD.

emphasizing that their bonuses were on the line. (D.I. 320 at 2412, 2548-49 (Bernstock); D.I. 314 at 94-95 (Lewis); D.I. 315 at 315-16 (Dorsch).)

50. Despite such pressure, the Specialty Foods division continued to have difficulty achieving the target EBIT. (D.I. 320 at 2415-16 (Bernstock).) Accordingly, in the second quarter of FY1998, the banks which had extended credit to facilitate the establishment of VFI (the "Banks")³³ were informed that VFI's projected FY1998 EBIT was being lowered to \$143 million. (DTX 381 at '004; D.I. 320 at 2038-42 (Emmet).)

51. Also as a result of the division's problems staying on target, Mr. Bernstock made a presentation to Campbell's management in which he asked that the managers of the division have their bonuses calculated using only the results from the first half of FY1998. (PTX 498 at '647; D.I. 320 at 2548-50 (Bernstock).) Mr. Bernstock explained that if the Specialty Foods division were going to achieve second quarter targets, the costs incurred by doing so would prevent the division from achieving its third quarter targets. (*Id.*)

52. Recognizing that the target EBIT numbers were unattainable, Mr. Anderson agreed to recommend to Campbell's Board of Directors that the EBIT target be lowered, so that the managers of the Specialty Foods division would still have an

³³The Banks consisted of Morgan Guaranty Trust Company of New York ("JP Morgan"), The Chase Manhattan Bank, Bank of America NT&SA, Bank of Montreal, Barclays Bank PLC, Citibank, N.A., Deutsche Bank AG New York, The First National Bank of Chicago, Fleet National Bank, Mellon Bank, N.A., PNC Bank, National Association, Wachovia Bank, N.A., The Bank of New York, The Bank of Nova Scotia, CoreStates Bank, N.A., SunTrust Bank, Atlanta, Westdeutsche Landesbank Girozentrale New York Branch, Banca Nazional Del Lavoro S.p.A. - New York Branch. (PTX 615 at '1117.)

incentive to deliver earnings.³⁴ (D.I. 320 at 2548-50, 2557 (Bernstock).) Mr. Anderson's recommendation was accepted by the Board, and the Specialty Foods division bonus target was reduced. (D.I. 320 at 2548-50, 2556-59 (Bernstock); D.I. 323 at 3416-17 (Anderson); PTX 697 at '078-79.) It is unclear exactly how the new bonus target was calculated, however. The target number was lowered 10% and did not include Swift's results, which were about \$11 million below target. (*Id.*) Additionally, some of Campbell's earnings from other divisions were attributed to the Specialty Foods division's earnings, so that the division could meet its already lowered financial target. (*Id.*)

53. To achieve its second quarter EBIT target, the management of the Specialty Foods division undertook to defer trade spending, sell assets, and to load product by providing customers with incentives to order products earlier than they ordinarily would. (PTX 488; D.I. 320 at 2412-13 (Bernstock); D.I. 316 at 819-20, 822 (Kessler); PTX 497; PTX 498 at '650.) These extraordinary measures allowed the managers of the Specialty Foods division to meet their second quarter financial targets. However, prior to the Spin-off, VFI's projected FY1998 EBIT, which included the

³⁴Maintaining the incentive was not without complications. The managers for the Specialty Foods division knew that they would receive stock options at the time of the Spin-off and that those options would be priced at the trading price of VFI's shares on the date of the Spin. (D.I. 1 at '930-31.) Consequently, VFI's managers had an incentive to push down the opening price of their company's stock, in order to lower the strike price and increase the value of their options. Thus, while VFI's managers wanted to get their bonuses from Campbell for delivering earnings, they also had an incentive to make VFI's performance appear less robust. This is in addition to the obvious incentive to avoid harm to the future earnings potential of VFI, which would follow from being short-sighted in financial planning.