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Smith v. Van Gorkom and the Kobayashi Maru: The Place of the Trans Union Case in the Development of Delaware Corporate Law

Robert T. Miller

SMITH V. VAN GORKOM AND THE *KOBAYASHI MARU*: THE PLACE OF THE TRANS UNION CASE IN THE DEVELOPMENT OF DELAWARE CORPORATE LAW

ROBERT T. MILLER*

ABSTRACT

Although it is dangerous to attempt to say anything new about Smith v. Van Gorkom*, the most controversial decision in the history of Delaware corporate law, this Article tries to do so by arguing that the extensive development of Delaware law since the time of the case allows us a perspective on* Van Gorkom *not available when the case was decided in 1985 or, indeed, for a long time thereafter. In particular,* Van Gorkom *had as important a role in the evolution of Delaware law as the three other outstanding cases decided by the Delaware Supreme Court in the miracle year of 1985:* Unocal v. Mesa Petroleum*,* Revlon v. MacAndrews & Forbes*, and* Moran v. Household International.

This Article argues, first and foremost, that Van Gorkom *was an attempt by the Delaware Supreme Court to respond to widespread*

* Professor of Law and F. Arnold Daum Fellow in Corporate Law at the University of Iowa College of Law and Fellow and Program Affiliated Scholar at the Classical Liberal Institute of New York University School of Law. For helpful comments and discussion, I thank Ronald J. Colombo, Mihailis E. Diamantis, Richard A. Epstein, James A. Fishkin, Christopher M. Foulds, Joel Friedlander, Thomas P. Gallanis, Herbert Hovenkamp, J. Travis Laster, Douglas K. Mayer, Mark A. Sargent, Gregory Shill, David M. Silk, Eric Willensky-Clinger, Harwell Wells, Adam J. White and Joseph W. Yockey. I especially thank William M. Owen for very illuminating discussions of his book *Autopsy of a Merger*, for providing me with copies of his articles from *Crain's Chicago Business*, and for sharing his memories of the Trans Union transaction, Jerome Van Gorkom, Jay Pritzker, and many other of the key individuals involved. I thank Hannah Posen, Deysimara Hubner, and Evan Saunders for their excellent work as my research assistants. Most of all, I thank Jennifer L. Miller, whose assistance and comments on all aspects of this Article were indispensable to its completion.

concern about the vast increase in merger-and-acquisition activity in the early 1980s. In particular, the case was the court's first attempt to devise a regime of directorial fiduciary duties to regulate negotiated transactions. Van Gorkom *should have been* Revlon*, and what the Delaware Supreme Court got wrong in* Van Gorkom *in January of 1985—the creation of a new duty of care based on dicta from the 1984 case of* Aronson v. Lewis*—it got right in* Revlon *in November of 1985 by creating what we now call* Revlon *duties. Nevertheless,* Van Gorkom *was not simply a botched first attempt at articulating duties for directors selling their company. The reasoning in* Van Gorkom *was in many ways inadequate, but its essential holding—that the directors breached their duties—would certainly have been the same under the reasoning in* Revlon*. In other words, the basic holding in* Van Gorkom*—that the Trans Union directors breached their fiduciary duties in selling the company—is correct, albeit for not quite the reasons the* Van Gorkom *court gave for this holding. What was truly disastrous about* Van Gorkom *was not the holding that the Trans Union directors breached their duties, but rather the remedy the court imposed on the breaching directors—enormous monetary damages.*

Since Revlon *was a pre-closing action, when the court found in that case that the directors breached their duties in agreeing to sell the company, the court could order relief by means of a preliminary injunction. By contrast,* Van Gorkom *was a post-closing action decided long after the merger was completed, and so that option was not available. Rather, when the* Van Gorkom *court found that the directors breached their duties, the axiom of the common law that every right has a remedy required imposing enormous liability on the directors. We now know that such a system was untenable, for it made the expected costs of serving as a director greatly exceed the expected benefits. Neither the justices of the Delaware Supreme Court nor anyone else could have known it in 1985, but in fact there was no right answer the court could have reached in* Van Gorkom*. If the court got the holding on the merits right (the directors breached their duties), it had to get the holding on remedies wrong (enormous monetary damages).* Smith v. Van Gorkom *was the* Kobayashi Maru *of Delaware corporate law—a problem in which all the possible solutions prove disastrous.*

Moreover, just as in the fictional Kobayashi Maru *in* Star Trek*, a solution to the problem did exist, but it required action from outside the system, action that would violate the fundamental terms of the problem as previously understood. In* Van Gorkom*, that action was the Delaware General Assembly's enactment of Section 102(b)(7), allowing corporations to eliminate personal liability in damages for directors breaching fiduciary duties not involving disloyalty. This extraordinary statute effectively abridges the common law rule that every right has a remedy, and it was necessary if the system of Delaware corporate law was to continue. By eliminating the possibility of monetary damages post-closing, the enactment of Section 102(b)(7) created strong incentives for stockholders alleging their directors had breached their fiduciary duties in approving a merger to bring suit before the merger closed, thus creating a pre-clearance system of fiduciary-duty compliance similar to the pre-clearance system for antitrust compliance under the Hart-Scott-Rodino Act. The Delaware system of pre-clearance, in which stockholder challenges to mergers virtually always take place at the preliminary injunction stage, has proved tremendously successful. Such a system would have been impossible, however, without* Van Gorkom*. For, without* Van Gorkom*, there would have been no Section 102(b)(7), and without Section 102(b)(7), there would have been no* Revlon-Unocal *system of preclearance.* Van Gorkom *was in many ways a mistake, but it was a mistake that had to be made to produce the current system of Delaware law. In its own way, it was as important a step forward in Delaware law as* Revlon*,* Unocal *or* Household International.

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INTRODUCTION

Only with trepidation should anyone approach the topic of *Smith v. Van Gorkom*.[1] Clearly, the most controversial decision in the history of Delaware corporate law,[2] the case has been the subject of a vast scholarly and professional commentary.[3] Although

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[1] *See generally* Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985).

[2] *See generally infra* note 3 and accompanying text.

[3] The literature on *Van Gorkom* is tremendous. Immediately after the decision, there was a flood of commentary from both practitioners and scholars. Among the practitioners, the most important articles include: Dierdre A. Burgman & Paul N. Cox, *Corporate Directors, Corporate Realities and Deliberative Process: An Analysis of the* Trans Union *Case*, 11 J. CORP. L. 311 (1986); Leo Herzel & Leo Katz, Smith v. Van Gorkom*: The Business of Judging Business Judgment*, 41 BUS. LAW. 1187 (1986); Steven F. Mones, *Mining the Safe Harbor? The Business Judgment Rule After* Trans Union, 10 DEL. J. CORP. L. 545 (1985); Morton Moskin, Trans Union*: A Nailed Board*, 10 DEL. J. CORP. L. 405 (1985); William Prickett, *An Explanation of* Trans Union *to "Henny Penny" and Her Friends*, 10 DEL. J. CORP. L. 451 (1985) (Prickett was counsel to the plaintiffs in the case); William T. Quillen, Trans Union*, Business Judgment, and Neutral Principles*, 10 DEL. J. CORP. L. 465 (1985); Stephen A. Radin, *The Director's Duty of Care Three Years After* Smith v. Van Gorkom, 39 HASTINGS L.J. 707 (1988); and Barry F. Schwartz & James G. Wiles, Trans Union*: Neither "New" Nor "Bad" Law*, 10 DEL. J. CORP. L. 429 (1985). Among the scholars, the most important articles include Daniel R. Fischel, *The Business Judgment Rule and the* Trans Union *Case*, 40 BUS. LAW. 1437 (1985), Bayless Manning, *Reflections and Practice Tips on Life in the Boardroom After* Van Gorkom, 41 BUS. LAW. 1 (1985), and Jonathan R. Macey & Geoffrey P. Miller, Trans Union *Reconsidered*, 98 YALE L.J. 127 (1988). In 1986, William M. Owen, who was an attorney in the general counsel's office at Trans Union at the time of the merger, published a book-length account of the acquisition of Trans Union, WILLIAM M. OWEN, AUTOPSY OF A MERGER (1st ed. 1986) [hereinafter OWEN], which he supplemented in William M. Owen, *A CEO Named Van Gorkom*, 24 DIRECTORS & BOARDS 35 (2000) [hereinafter Owen, *CEO*] and *A Shareholder Named Smith*, 24 DIRECTORS & BOARDS 39 (2000). In the same year, there appeared Lawrence A. Hamermesh, *Why I Do Not Teach* Van Gorkom, 34 GA. L. REV. 477 (2000) and a fifteenth anniversary roundtable discussion involving prominent practitioners and academics sponsored by Directors & Boards, *Roundtable: The Legacy of* Smith v. Van Gorkom, 24 DIRECTORS & BOARDS 28 (2000). In 2001, the *Northwestern University Law Review* held a symposium on the topic of *Van Gorkom*. Symposium, Van Gorkom *and the Corporate Board: Problem, Solution or Placebo?*, 96 NW. U.L. REV. 449 (2002). That event produced several more articles, including William T. Allen, Jack B. Jacobs & Leo E. Strine, Jr., *Realigning the Standard of Review of Director Due Care with Delaware Public Policy: A Critique of* Van Gorkom *and Its Progeny as a Standard of Review*

there is a broad consensus that the Delaware Supreme Court's decision in *Van Gorkom* was a serious mistake that the Delaware General Assembly had to move quickly to correct,[4] practically every conceivable opinion about the case, whether favorable or unfavorable, has been defended by someone or other, and thus the possibility of saying anything new about the case after more than thirty years naturally seems remote.[5] With due caution, however, this Article suggests that the extensive development of Delaware corporate law that has occurred since the Delaware Supreme Court decided the case now allows us a perspective on *Van Gorkom* that earlier observers of Delaware corporate law could not possess. T.S. Eliot famously argued that the full meaning of a great work of literature becomes known only as later great works respond to it, and so its meaning—or at least its meaning for us—will develop and increase over time.[6] Something similar

Problem, 96 NW. U.L. REV. 449 (2002); R. Frank Balotti & A. Gilchrist Sparks, III, *Deal-Protection Measures and the Merger Recommendation*, 96 NW. U.L. REV. 467 (2002); Bernard Black & Reinier Kraakman, *Delaware's Takeover Law: The Uncertain Search for Hidden Value*, 96 NW. U.L. REV. 521 (2002); Helen M. Bowers, *Fairness Opinions and the Business Judgment Rule: An Empirical Investigation of Target Firms' Use of Fairness Opinions*, 96 NW. U.L. REV. 567 (2002); Charles M. Elson & Robert B. Thompson, Van Gorkom's *Legacy: The Limits of Judicially Enforced Constraints and the Promise of Proprietary Incentives*, 96 NW. U.L. REV. 579 (2002); Lawrence A. Hamermesh, *A Kinder, Gentler Critique of* Van Gorkom *and Its Less Celebrated Legacies*, 96 NW. U.L. REV. 595 (2002); Jonathan R. Macey, Smith v. Van Gorkom*: Insights About C.E.O.s, Corporate Law Rules, and the Jurisdictional Competition for Corporate Charters*, 96 NW. U.L. REV. 607 (2002); Fred S. McChesney, *A Bird in the Hand and Liability in the Bush: Why* Van Gorkom *Still Rankles, Probably*, 96 NW. U.L. REV. 631 (2002); Edward Rock & Michael Wachter, *Dangerous Liaisons: Corporate Law, Trust Law, and Interdoctrinal Legal Transplants*, 96 NW. U.L. REV. 651 (2002). More recently, articles that have appeared include: Stephen M. Bainbridge, *The Story of* Smith v. Van Gorkom *in* CORPORATE LAW STORIES (J. Mark Ramseyer, ed., 2009); Stephen P. Lamb & Joseph Christensen, *Duty Follows Function: Two Approaches to Curing the Mismatch Between the Fiduciary Duties and Potential Personal Liability of Corporate Officers*, 26 NOTRE DAME J.L. ETHICS & PUB. POL'Y 45 (2012); Bernard S. Sharfman, *The Enduring Legacy of* Smith v. Van Gorkom, 33 DEL. J. CORP. L. 287 (2008).

[4] *See infra* text accompanying notes 330–51.

[5] *See supra* note 3 and accompanying text (listing the wealth of scholarship produced in the years since *Van Gorkom*).

[6] T.S. ELIOT, *Tradition and the Individual Talent, in* THE SACRED WOOD 47, 50–51 (1921).

is true about great cases at law, including *Van Gorkom*.[7] Looking back now and discerning the place of *Van Gorkom* in the development of Delaware corporate law yields not only insights into the case itself that were unobtainable at the time of the decision, but also insights into the system of Delaware corporate law that developed in part as a result of the decision.[8]

In particular, *Van Gorkom* was one of four decisions the Delaware Supreme Court issued in what must be regarded as the miracle year of 1985.[9] *Van Gorkom* was decided in January of that year.[10] In June came the court's decision in *Unocal v. Mesa Petroleum*,[11] and in November, the court decided both *Revlon v. MacAndrews & Forbes Holdings*[12] and *Moran v. Household International.*[13] *Unocal* held that a board responding to a takeover attempt has the burden of proving that it reasonably perceived that there existed a threat to corporate policy or effectiveness and that its response to the perceived threat was reasonable in the circumstances.[14] *Unocal* thus became the basis of the Delaware law governing hostile takeovers. *Revlon* held that when a board decides to sell the company, it has the burden of proving

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[7] *See supra* note 3 and accompanying text (listing scholarship on *Van Gorkom*).

[8] *Id.*

[9] *See infra* text accompanying notes 10–13; Charles M. Elson & Robert B. Thompson, Van Gorkom's *Legacy: The Limits of Judicially Enforced Constraints and the Promise of Proprietary Incentives*, 96 NW. U.L. Rev. 579, 579 (2002) (stating that *Van Gorkom* "is at the center of the most remarkable period of judicial activity in corporate law in the twentieth century" and noting its proximity in time to *Aronson v. Lewis*, *Weinberger v. UOP*, *Unocal v. Mesa Petroleum*, and *Revlon v. MacAndrews & Forbes*).

[10] *See* Smith v. Van Gorkom, 488 A.2d 858, 858 (Del. 1985). The case was submitted on June 11, 1984, and decided on January 29, 1985. On March 14, 1985, the Delaware Supreme Court denied a motion for reargument.

[11] *See* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 946 (Del. 1985). The case was submitted on May 16, 1985, and the Supreme Court rendered an oral decision the next day, May 17, 1985. The written decision followed on June 10, 1985.

[12] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 173 (Del. 1986). The case was submitted on October 31, 1985, and the Supreme Court rendered an oral decision the next day, November 1, 1985. The written opinion did not appear until March 13, 1986.

[13] *See* Moran v. Household International, Inc., 500 A.2d 1346, 1346 (Del. 1985). The case was submitted on May 21, 1985, decided on November 19, 1985, and amended on November 20, 1985.

[14] *See Unocal*, 493 A.2d at 958.

that it took reasonable steps to get the best price reasonably available for the stockholders.[15] *Revlon* thus became the basis of the Delaware law governing negotiated transactions. *Moran* held that the poison pill was legal in Delaware, which gave the board of directors the legal means to block hostile tender offers and so fundamentally altered the balance of power between targets and raiders in hostile transactions.[16] With boards able to protect against takeovers with the poison pill,[17] and with *Unocal* regulating hostile deals[18] and *Revlon* regulating friendly ones,[19] there may seem to be no place for an important role for *Van Gorkom* in Delaware corporate law. Indeed, although the case has been cited in subsequent business judgment cases not involving business combinations,[20] there is no *Van Gorkom* doctrine or *Van Gorkom* line of cases related to mergers and acquisitions.[21] That circumstance, I suggest, is highly misleading.

This Article argues that *Van Gorkom* played a critical role in the development of the Delaware law of mergers and acquisitions. First and foremost, *Van Gorkom* was an attempt by the Delaware Supreme Court to begin working out a regime to regulate negotiated transactions.[22] *Van Gorkom* should have been *Revlon*,[23] and what the Delaware Supreme Court got wrong in

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[15] *See Revlon,* 506 A.2d at 182.

[16] *See Moran,* 500 A.2d at 1357.

[17] *Id.*

[18] *See Unocal*, 493 A.2d at 958.

[19] *See Revlon*, 506 A.2d at 182.

[20] *See, e.g.*, *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 74 (Del. 2006).

[21] *See generally* Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985).

[22] *See id.*

[23] *See generally Revlon*, 506 A.2d 173. Soon after *Van Gorkom* was decided, Manning astutely predicted that the case foreshadowed the development of stricter judicial scrutiny of what he termed "ownership decisions," i.e., board decisions that affect the stockholders' property in their shares. Bayless Manning, *Reflections and Practical Tips on Life in the Boardroom after* Van Gorkom*,* 41 BUS. LAW. 1, 6 (1985). "It is no accident that the court chose a cashout merger case for the lecture it delivered" in *Van Gorkom*. *Id.* "The best way to read the whole … opinion is to say that, whenever a board decision has a direct impact on stock ownership, the board had better be extra careful." *Id*. Macey and Miller argued in 1988 that *Van Gorkom* should be understood not as a business judgment case but as "a takeover case" whose "function is to regulate a target's response to certain types of takeover bids, namely 'rush' offers with short time fuses." Jonathan Macey & Geoffrey Miller, Trans Union *Reconsidered*, 98 YALE L.J. 127, 128 (1988). Indeed, the Delaware Supreme Court

would later say, "[b]oards that have failed to exercise due care are frequently boards that have been rushed." Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 67 (Del. 1989). As noted in the text, like Macey and Miller, I too see *Van Gorkom* as a takeover case, but one that (like *Revlon*) concerns the duties of target directors in negotiated acquisitions generally, not one limited to the rare case of "rush" offers and, moreover, a takeover case that mistakenly tried to cram an entire takeover jurisprudence into the business judgment rule's duty of care. Furthermore, the risk of "rush" offers, which may have seemed significant in 1988, never really materialized. Influenced by *Van Gorkom,* plaintiffs to this day routinely allege that the directors were in a rush to sell the company. *See, e.g.*, *In re* Petsmart, Inc., No. 10782-VCS, 2017 WL 2303599 (Del. Ch. 2017); *In re* Om Group Inc. S'holders Litig., No. 11216-VCS, 2016 WL 5929951 (Del. Ch. 2016); Larkin v. Shah, No. 10918-VCS, 2016 WL 4485447 (Del. Ch. 2016). As far I can determine, no Delaware case since *Van Gorkom* has held that a board breached its duties (including its *Revlon* duties) in approving a merger because it was rushed. Indeed, it is hard even to think of cases in which the board was rushed even without breaching its duties. For the best examples, see Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53 (Del. 1989) and Lyondell Petrochemical Co. v. Ryan, 970 A.2d 235 (Del. 2009), as well as the extraordinary circumstances during the financial crisis in *In re* Bear Stearns Litig., 870 N.Y.S.2d 709 (N.Y. Sup. Ct.) (applying Delaware law). In none of these cases, however, did the court find that the directors breached their duties. *See also Roundtable: The Legacy of* Smith v. Van Gorkom, 24 DIRECTORS & BOARDS 28, 38 (2000) [hereinafter *Roundtable*] (discussing whether it is possible to complete a deal in forty-eight hours post–*Van Gorkom*). However that may be, Macey and Miller think the key point of *Van Gorkom* is that, if an acquirer should present a target with a premium offer with a very short deadline, the board can reject the offer citing *Van Gorkom* to justify taking more time to consider the offer and, for instance, obtain a fairness opinion. Jonathan Macey & Geoffrey Miller, Trans Union *Reconsidered*, 98 YALE L.J. 127, 128 (1988). This ability to delay is important because it "eliminates the possibility that the board … will be held liable to stockholders if it delays making a decision and the bidder … drops the offer." *Id.* at 136. In my view, there are several problems with this reasoning. One is that the text of the majority opinion in *Van Gorkom* contradicts it. The court clearly thought that, while the deadline Pritzker set was short, the board could have complied with its obligations within that timeframe. *Van Gorkom*, 488 A.2d at 877–78 (stating that "the Board did not consider recessing the meeting [on September 20] to a later hour that day … to give it time to elicit more information about the sufficiency of the offer, either from inside Management … or from Trans Union's own investment banker."). Furthermore, although the Trans Union directors had been advised by counsel that they could be liable for not accepting Pritzker's offer, *Van Gorkom*, 488 A.2d at 868, such a possibility was entirely fanciful. Such a proposition had no basis in Delaware law at the time, and its only possible later basis would be the very duty of care imposed by *Van Gorkom* itself. *See* Pogostin v. Rice, 480 A.2d 619, 627 (Del. 1984) (rejecting plaintiffs' claim that a board's refusal to accept a premium offer was a prima facie breach of fiduciary duty and stating that "[e]stablishing such a principle would rob corporate boards of all discretion, forcing them to choose between accepting any tender offer or merger proposal above market, or facing the likelihood of personal liability if they reject it. To put directors to such a Hobson's choice would be the antithesis of the principles upon which a proper exercise of business judgment is demanded of them."). Subsequently, in *Time-Warner*, the Delaware Supreme Court would hold that a board's decision to turn down a takeover proposal and remain independent, whether the offer is a "rush" offer or not, would be reviewed under the business judgment rule, including with respect to the duty of care. Paramount Commc'ns, Inc. v. Time Inc., 571 A.2d 1140, 1142 (Del. 1990); *see also* Phelps Dodge Corp. v. Cyprus Amax Minerals Co., 1999 Del. Ch. LEXIS 202, at *3–4 (Del. Ch. Sept. 27, 1999) (holding that "even the decision not to negotiate … must be an informed one. A target can refuse to negotiate under *Time Warner*, but it should be informed when making such refusal."). Macey and Miller are right that directors faced with a premium offer with a short deadline face a difficult business decision as to whether to take the attractive sure thing and risk losing the possibility of an even better deal, but such directors can surely make this decision without fear of personal liability except for possibly breaching their duty of care. *See* Jonathan Macey & Geoffrey Miller, Trans Union *Reconsidered*, 98 YALE L.J. 127, 128 (1988). Contrary to Macey and Miller, *Van Gorkom* did not ameliorate the difficulty such directors face by eliminating the possibility of personal liability; it rather exacerbated that difficulty by creating the possibility of liability where none had existed before. *Compare id.* at 132–33, *with Van Gorkom*, 488 A.2d at 858. Citing Macey and Miller, Chancellor Allen once stated that, at least for purposes of deciding a motion to dismiss derivative claims not involving allegations of disloyalty or improper motivation, he:

> count[ed] *Smith v. Van Gorkom* … not as a 'negligence' or due care case involving no loyalty issues, but as an early and, as of its date, not yet fully rationalized '*Revlon*' or 'change of control' case … reflecting a concern with the Trans Union board's independence and loyalty to the company's [stock]holders in a critical 'sale of the company' context.

Gagliardi v. Trifoods Int'l, Inc., 683 A.2d 1049, 1052 n.4 (1996). This goes beyond Macey and Miller in what this Article argues is the right direction by seeing *Van Gorkom* as groping attempt towards *Revlon*. Nevertheless, I think Allen's somewhat cryptic remarks conflate concerns of improper motivation (i.e., *Unocal*'s specter of self-interest that haunts decisions by directors that might be perpetuating themselves in office) with concerns about due care in selling the company (i.e., *Revlon* situations, where directors are usually voting themselves out of a job). Other scholars have also occasionally referred favorably to Macey and Miller's suggestion. *See* Lawrence A. Hamermesh, *Why I Do Not Teach* Van Gorkom, 34 GA. L. REV. 477, 488 (stating that "some have cogently argued that *Van Gorkom* is best understood as a crude precursor to

Van Gorkom in January of 1985 it would get right in *Revlon* in November of that year.[24] Nevertheless, *Van Gorkom* was not simply a misstep, taken and then corrected. Indeed, if the court in *Van Gorkom* had formulated and applied the doctrine it soon would in *Revlon*, the outcome in *Van Gorkom* would have been the same: that is, the Trans Union directors *did* breach their fiduciary duties as those duties would soon come to be understood in *Revlon*.[25] Put anachronistically, the Trans Union directors breached their *Revlon* duties when they approved the sale of the company.[26] Assuming *Revlon* is rightly decided, what was wrong in *Van Gorkom* was thus *not* the essential holding that the Trans Union directors breached their fiduciary duties.[27]

How then was *Van Gorkom* so wrong? Part of the answer lies in the *Van Gorkom* court's reasoning.[28] Rather than announce an important new doctrine as it would soon do in *Revlon*, the court in *Van Gorkom* attempted to reach what we can now see as a correct result based on business judgment doctrines involving the procedural duty of care that had entered the law in dicta in *Aronson v. Lewis*[29] in March of 1984—that is, just nine months before *Van Gorkom* was decided and more than *four years* after the Trans Union board had approved the merger challenged in that case.[30] This duty of care reasoning, however,

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Revlon"); Elson & Thompson, *supra* note 9, at 582 n.17 (referring to Macey and Miller, and to unpublished remarks of former Chief Justice Veasey and former Chancellor Allen at the Northwestern University symposium on *Van Gorkom*, to the effect that *Van Gorkom* was "the beginning of the Delaware court's attempt to work out the relative roles of directors and [stock]holders in hostile takeovers that occupied so much of the court's time for the remainder of 1985 and subsequent years"); RONALD GILSON & BERNARD BLACK, THE LAW AND FINANCE OF CORPORATION ACQUISITIONS 1055 (2d. ed. 1995) (stating that *Van Gorkom* "may be the Delaware Supreme Court's first attempt at counseling directors about the right way to sell the corporation.").

[24] *Revlon*, 506 A.2d at 173.

[25] *See Van Gorkom*, 488 A.2d at 893. *See generally Revlon*, 506 A.2d at 173.

[26] *See Van Gorkom*, 488 A.2d at 893. *See generally Revlon*, 506 A.2d at 173.

[27] *See Van Gorkom*, 488 A.2d at 893. *See generally Revlon*, 506 A.2d at 173.

[28] *Cf.* William T. Quillen, Trans Union*, Business Judgment, and Neutral Principles*, 10 DEL. J. CORP. L. 465, 470 (1985) (arguing that the majority opinion "appears to many to be unprincipled, that is, without generality and neutrality transcending the immediate result," and "is burdened by overkill and by needless, and often erroneous, legal and factual excesses.").

[29] *See* Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

[30] *Id.*

was manifestly inadequate to support the dramatic outcome in *Van Gorkom*.[31] For, as virtually the entire corporate bar understood at the time, the court was clearly imposing new fiduciary duties on directors, but the court nevertheless steadfastly refused to admit that it was doing so.[32] As a result, it never articulated a theoretical justification for the new duties it was creating, never explained in adequate detail what they were, and never made clear under what circumstances those duties would apply.[33] This greatly contributed to the shock, chaos, and panic the decision produced.[34]

A few months later in *Revlon*, of course, the Delaware Supreme Court would articulate a justification for a new set of directorial duties based on the idea that, when the board decides to sell the company, the end towards which the board should direct its efforts changes from maximizing the value of the company in the long term to obtaining the best price for the stockholders

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[31] *See Van Gorkom*, 488 A.2d at 872. Allen, Jacobs, and Strine argue that in *Van Gorkom* "while purporting to apply the gross negligence standard of review, in reality (but not explicitly) [the Delaware Supreme Court] applied an ordinary negligence standard." William T. Allen, Jack B. Jacobs & Leo E. Strine, Jr., *Realigning the Standard of Review of Director Due Care With Delaware Public Policy*, 96 NW. U.L. REV. 449, 458 (2002). Then–Vice Chancellor (now Chief Justice) Strine, has written that *Van Gorkom* "is hardly a model for the principled application of the concept of gross negligence and arguably involved facts that, when considered in their totality, did not even amount to simple negligence." Abry Partners V, L.P. v. F & W Acquisition LLC, 891 A.2d, 1032, 1063 n.82 (Del. Ch. 2006). Macey and Miller think that "although the court defined the applicable standard of care as gross negligence, it seemed to apply a more stringent standard on the facts of the case," and "the facts did not support a finding of negligence, much less gross negligence." Macey & Miller, *supra* note 23, at 129. This latter conclusion is not widely shared; it seems most observers agree that the Trans Union board was negligent or grossly negligent. *See Roundtable*, *supra* note 23, at 28 (detailing discussion among eleven eminent professionals and academics, of whom four thought the board grossly negligent, six more thought the board at least negligent, and one thought the board not negligent). In any event, Mones is surely right that *Van Gorkom* differed from prior cases "in its application of the gross negligence standard to directors' actions that, hitherto, undoubtedly would have remained sheltered within the safe harbor" of the business judgment rule. Steven F. Mones, *Mining the Safe Harbor? The Business Judgment Rule After* Trans Union, 10 Del. J. Corp. L. 545, 567 (1985).

[32] *See generally Van Gorkom*, 488 A.2d 858 (Del. 1985).

[33] *See generally id.*

[34] *See supra* note 3 and accompanying text.

in an immediate sale transaction.[35] Thus explained and limited, these *Revlon* duties, while certainly new, were intelligible to the corporate bar and seemed to directors like ones they could comply with in the limited circumstances in which they applied.[36] This was true even though the new *Revlon* duties were in fact *more* stringent than the duties imposed by *Van Gorkom*.[37] For example, the duty of care articulated in *Van Gorkom* required only that the board be fully informed before it decides, but *Revlon* requires not only this kind of procedural due care but also substantively reasonable decisions.[38] The fact that *Revlon* demands more of directors than did *Van Gorkom* shows that the error of *Van Gorkom*, which we already saw did not lie in finding that the Trans Union directors had breached their fiduciary duties, also did not lie in imposing on those directors duties that were too demanding.[39] Rather, a good part of the problem with *Van Gorkom* lay not in the content of the duties the court announced but in the court's failure to explain what that content was and when the new duties would apply.[40]

In particular, by attempting to shoehorn a result that would be correct under *Revlon* (the board had breached its fiduciary duties) into a doctrine inadequate to the task (the procedural duty of care articulated in *Aronson v. Lewis*),[41] the Delaware Supreme Court found itself at key points required to say that certain actions by the Trans Union board were procedural mistakes involving decisions made on the basis of inadequate information when the real objection to those decisions—an objection not stated in the opinion,[42] but apparent in the subsequent light of *Revlon*—was that these actions were manifestly not reasonably calculated to get the best price for the stockholders reasonably available.[43]

[35] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, 506 A.2d 173, 182 (Del. 1985).

[36] *Id.*

[37] *Compare Revlon*, 506 A.2d at 182, *with Van Gorkom*, 488 A.2d at 893.

[38] *Compare Revlon*, 506 A.2d at 182, *with Van Gorkom*, 488 A.2d at 893.

[39] *Compare Revlon*, 506 A.2d at 182, *with Van Gorkom*, 488 A.2d at 893.

[40] *See generally* Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985).

[41] *Compare Revlon*, 506 A.2d at 182, *with* Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

[42] *See generally Van Gorkom*, 488 A.2d 858. Indeed, it seems very likely that the justices in the majority in *Van Gorkom* could not themselves, at the time of the decision, have articulated the real objection.

[43] *See generally id.*

One result of this mismatch between the stated reasons for the holding and the outcome of the case was an unpersuasive and chaotic opinion. Another was great uncertainty for corporate directors.[44] *Van Gorkom* made it clear that the Trans Union directors did something very wrong, but in just what was wrong, was far less clear.[45] Using the analytic tools of *Revlon* and subsequent *Revlon* cases, we today can easily identify the breaches committed by the Trans Union directors.[46] But at the time, with just the text of the *Van Gorkom* opinion to guide them, directors and their counsel could not possibly have done so, and the reason was that the text of the opinion simply does not contain a coherent account of what the directors did wrong and in what the wrongness of their actions consisted.[47]

But *Van Gorkom* was not simply a botched first attempt by the Delaware Supreme Court to regulate friendly transactions. In one critically important way, it was an advance of the first importance in Delaware corporate law, for it was a *necessary* mistake—a mistake without which Delaware very likely would not have the well-functioning system of corporate law it has today.[48] The reason for this becomes apparent when we compare the different procedural contexts in which *Van Gorkom* and *Revlon* arose.[49] *Revlon* arose in the context of the plaintiffs' motion for a preliminary injunction,[50] so that when the plaintiffs won, the result was an injunction that led to a better sales process for the company.[51] By contrast, *Van Gorkom* was a post-closing appeal[52] seeking to hold the directors liable for monetary damages.[53] The

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[44] *See infra* text accompanying notes 45–47.

[45] *See Van Gorkom*, 488 A.2d at 893.

[46] For example, compare the actions of the Trans Union directors in 1985 with those of the Lyondell directors, who faced a very similar factual scenario, in 2007. *See* Lyondell Chemical Co. v. Ryan, 970 A.2d 235, 237–39 (Del. 2009); Robert T. Miller, Lyondell Chemical Co. v. Ryan*: Good Faith Comes to* Revlon-*Land*, 11 ENGAGE 14 (2010). *Id.*

[47] *See generally Van Gorkom*, 488 A.2d 858.

[48] *See generally id.*

[49] *See infra* text accompanying notes 50–52.

[50] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, 506 A.2d 173, 179 (Del. 1985).

[51] *See id.* at 185.

[52] *See* Smith v. Pritzker, No. 6342, 1981 WL 15145 (Del. Ch. Feb. 3, 1981). The plaintiff in *Van Gorkom* had brought the suit pre-closing, but the Court of Chancery denied a preliminary injunction and let the merger continue.

[53] *Van Gorkom*, 488 A.2d 858.

difference is critically important, for the gravest defect of *Van Gorkom* lay not in its reasoning based on procedural due care—though this was definitely inadequate[54]—nor yet its holding that the Trans Union directors had breached their fiduciary duties—which was in fact correct[55]—but in the remedy it imposed on the defendants: enormous monetary damages.[56] With the benefit of hindsight, we know that such a system is untenable: rational businesspeople will not serve as public company directors if an honest mistake in approving a merger can subject them to damages aggregating many times their net worth.[57] The benefits of being a director, financial and otherwise, simply do not come close to compensating a person for bearing such a tremendous risk.[58] Certainly in the merger context, where the sums involved are generally enormous relative to the worth of any individual and vastly exceed the limits of directors' and officers' insurance, personal liability for directors cannot be part of a rational system of fiduciary duties.[59]

But now the tremendous positive contribution of *Van Gorkom* to the development of Delaware corporate law should be clear. Any decision in the case that reached the correct result—that is, any decision that held that the Trans Union directors

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[54] *See supra* text accompanying notes 30–34.

[55] *See infra* text accompanying note 635.

[56] *See infra* text accompanying notes 636–38.

[57] This point is common ground among practitioners and scholars alike. *See, e.g.*, *Roundtable*, *supra* note 23, at 28 (2000) (stating that the case contributed to "a reexamination by many executives of the personal risks of board service"); Gagliardi v. Trifoods Int'l, Inc., 683 A.2d 1049, 1052 (Del. Ch. 1996) ("Given the scale of operations of modern public corporations ... only a very small probability of director liability based on 'negligence,' 'waste,' etc. could induce a board to avoid authorizing risky investment projects."); Bernard S. Sharfman, *The Enduring Legacy of* Smith v. Van Gorkom, 33 DEL. J. CORP. L. 287, 289–90 (2008) (stating that "[t]he enduring legacy of *Van Gorkom* is the understanding that corporate directors should not be held financially liable for corporate board decisions that lack due care"); Jonathan R. Macey, Smith v. Van Gorkom: *Insights About C.E.O.s, Corporate Law Rules, and the Jurisdictional Competition for Corporate Charters*, 96 NW. U.L. REV. 607, 608 (2002) (referring to "the debilitating threat of financial ruin from the personal liability to which the directors were exposed."). Of course, there is always a contrary opinion. *See, e.g.*, Lloyd L. Drury, III, *What's the Cost of a Free Pass? A Call for the Re-Assessment of Statutes that Allow for the Elimination of Personal Liability for Directors*, 9 TRANSACTIONS: TENN. J. BUS. L. 99, 104 (2007).

[58] *See infra* text accompanying notes 650–52.

[59] *See infra* text accompanying notes 650–53.

had breached their fiduciary duties—would have produced the same disastrous results that *Van Gorkom* produced: collapsing directors' and officers' liability insurance (D&O) markets,[60] panicked directors, serious calls for corporations to reincorporate outside of Delaware, and finally action by the Delaware General Assembly to allow corporations to eliminate personal liability for directors for breaches of the duty of care.[61] Such results would have followed even if the reasoning adopted by the Delaware Supreme Court had been the perfectly sound reasoning it would deploy later the same year in *Revlon,* or even the more elaborate version of that reasoning that appears in *Paramount v. QVC*[62] or other of *Revlon*'s progeny.[63] The inadequate reasoning in *Van Gorkom* no doubt made things much worse, but no matter how sound the reasoning had been, the case would still have been a disaster that, if left uncorrected, would collapse the edifice of Delaware corporate law.[64] For, if the law is to have special fiduciary duties for directors

[60] *See* Nancy R. Mansfield, *The Shocking Impact of Corporate Scandal on Directors' and Officers' Liability*, 20 U. MIAMI BUS. L. REV. 211, 228 n.87 (2012); Michael Bradley & Cindy A. Schipani, *The Relevance of the Duty of Care Standard in Corporate Governance*, 75 IOWA L. REV. 1, 50–51 (stating that D&O insurance premiums increased more than tenfold between 1984 and 1986); Stephen M. Bainbridge, *The Story of* Smith v. Van Gorkom, *in* CORPORATE LAW STORIES 198 (J. Mark Ramseyer, ed., 2009) ("perception that the decision had significantly increased director liability exposure drove dramatic changes in the director and officer … liability insurance market."); E. Norman Veasey et al., *Delaware Supports Directors With a Three-Legged Stool of Limited Liability, Indemnification and Insurance*, 42 BUS. LAW. 399, 400–01 (1987) (discussing how some D&O carriers withdrew from the market or raised premiums and deductibles as a result of *Van Gorkom*); Allen, Jacobs & Strine, *supra* note 31, at 458 n.36 (stating that "after *Van Gorkom*, the D & O insurance industry sharply increased their premiums and in some cases, threatened to stop writing D & O insurance policies. This crisis required a legislative solution," which took the form of Section 102(b)(7)); Edward Rock & Michael Wachter, *Dangerous Liaisons: Corporate Law, Trust Law, and Interdoctrinal Legal Transplants*, 96 NW. U.L. REV. 651, 659 (2002) (stating "[i]n the wake of *Smith v. Van Gorkom*, a directors and officers … liability insurance crisis was triggered. Policies were not renewed, premiums skyrocketed, and firms worried about being able to recruit high quality directors.").

[61] *See infra* text accompanying notes 343–50.

[62] *See* Paramount Commc'ns, Inc. v. QVC Network, Inc., 637 A.2d 34, 51 (Del. 1994) [hereinafter *QVC*].

[63] *See, e.g.*, Gilbert v. El Paso Co., 575 A.2d 1131, 1145–46 (Del. 1990); Barkan v. Amsted Indus. Co., 567 A.2d 1279, 1286 (Del. 1989); Mills Acquisition Co. v. MacMillan, Inc., 559 A.2d 1261, 1264, 1279–80 (Del. 1988).

[64] *See infra* text accompanying notes 670–72.

selling the company, then the coherency of the common law required that if directors breach those duties, the stockholders must have an adequate remedy.[65] In the pre-closing context, as in *Revlon*, that remedy was an appropriate injunction, a tool with which the equity courts of Delaware were intimately familiar.[66] But in the post-closing context, as in *Van Gorkom*, the only possible remedy was monetary damages, and that remedy, it turns out, cannot be part of a workable system of corporate law.[67] The Delaware Supreme Court in *Van Gorkom* could not have issued *any* opinion that solved this problem: if the opinion reached the conclusion that the Trans Union directors breached their duties—the result that would clearly follow under *Revlon*—then the court had to hold the directors liable in damages, and that result would bring down the entire system of directorial fiduciary duties.[68] *Smith v. Van Gorkom* was the *Kobayashi Maru*[69] of Delaware corporate law.[70]

[65] *See infra* text accompanying notes 664–67.

[66] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 185 (Del. 1986).

[67] *See infra* text accompanying notes 664–69.

[68] *See infra* text accompanying notes 669–71.

[69] In *Star Trek*, the *Kobayashi Maru* is a training simulation for cadets at Star Fleet Academy. The cadet is commanding a star ship that encounters a civilian ship—the *Kobayashi Maru*—in distress, but aiding the ship requires entering the Neutral Zone, which would violate a treaty with the warlike Klingons. Because of how the simulation is constructed, if the cadet chooses not to aid the ship, its innocent passengers and crew perish; if the cadet aids the ship, Klingon warships appear and ultimately destroy or capture the cadet's ship, perhaps triggering a galactic war. The test is deliberately constructed to present the cadet with a situation in which every possible choice is disastrous. In *Star Trek II: The Wrath of Kahn,* we learn that James T. Kirk was the only cadet in Star Fleet history to defeat the *Kobayashi Maru*, but he did so by covertly reprogramming the simulation—i.e., by creating a new option outside the accepted terms of the problem. The academy commended him for original thinking. Commenting on the episode later, Kirk declares that he does not believe in no-win situations. This is not merely a bit of bravado. Kirk's point is that a computer simulation artificially limits a person's options, but in the real world the set of options is not determined in advance but limited only by human imagination and ingenuity. In the real world, a situation is a no-win situation only because no one has yet devised a winning solution; there can be no certainty *ex ante* that a winning solution does not exist. *Star Trek: The Original Series* (CBS television broadcast 1966–69); *see* Janet D. Stemwedel, *The Philosophy of Star Trek: The Kobayashi Maru, No-Win Scenarios, and Ethical Leadership*, FORBES (Aug. 23, 2015, 10:18 AM), https://www.forbes.com/sites/janetstemwedel/2015/08/23/the-philosophy-of-star-trek-the-kobayashi-maru-no-win-scenarios-and-ethical-leadership/#3d77f05c5f48.

[70] *See infra* text accompanying notes 669–71.

Neither the justices of the Delaware Supreme Court nor anyone else could have known it at the time, but there was no correct answer to the issue posed by the case, no opinion that the Delaware Supreme Court could have issued that would have both decided the case correctly and not fatally undermined Delaware corporate law.[71]

More precisely, just as in the fictional training exercise at *Star Trek's* Star Fleet Academy, *Kobayashi Maru*, in *Van Gorkom* there was no right answer within the system in which the participants were operating in *Van Gorkom*, the common law system.[72] Just as in the *Kobayashi Maru*, where all moves within the computer simulation lead to disaster but reprogramming the simulation opens the possibility of a viable solution, so too in *Van Gorkom* did a viable solution exist, but not within the common law system of Delaware fiduciary law.[73] A workable solution required legislative action: the creation of a very unusual legal structure, a duty—the director's duty of care—that would be enforceable by injunction when the directors *threatened* to violate it, but not by monetary damages when they *had in fact* violated it.[74] If Delaware law was to impose significant duties on directors who were selling their company—that is, if Delaware were to have anything like the *Revlon* duties it has today—then the question had to be faced: what happens when directors breach these duties and the deal closes?[75] The answer to that question had to be that, at least in general, the directors were *not* liable in damages.[76] Knowing all we do now, perhaps we can imagine a court of Solons and Solomons in 1985, farsighted enough to grasp of all this and hold in *Van Gorkom* that directors had special new duties in selling their company and that the Trans Union directors had breached those duties, but that the stockholders

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[71] *Id.*

[72] *Id.* at 656–70.

[73] *See* Stemwedel, *supra* note 69; *infra* text accompanying notes 656–70.

[74] *See infra* text accompanying notes 627–31; *infra* Section II.B.

[75] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 185 (Del. 1986); Derek J. Famulari, *The* Revlon *Doctrine—The Fiduciary Duties of Directors when Targets of Corporate Takeovers and Mergers*, A.B.A. (Jan. 29, 2016), https://www.americanbar.org/content/dam/aba/administrative/young_lawyers/publications/101/fiduciary_duties_of_directors_coporate_takeover.authcheckdam.pdf [http://perma.cc/MJT5-PZQ6].

[76] *See Revlon*, 506 A.2d at 185.

post-closing would have no remedy for these breaches.[77] In 1985, however, no one could realistically have foreseen that *Van Gorkom* required such an extraordinary outcome.[78]

Van Gorkom's reasoning was poor and its outcome was disastrous,[79] but *Van Gorkom* was a disaster that had to occur if the current system of Delaware law, especially the system of *Revlon* duties, was to develop.[80] In Delaware's miracle year of 1985, *Van Gorkom* was not simply a mistake soon to be corrected in *Revlon*.[81] It was a necessary mistake, a mistake that had to be made, either in *Van Gorkom* or some other case, if *Revlon* was to be possible.[82] The creation of *Revlon* duties was a major advance in Delaware law, but the practical existence of those duties critically depends on their *non*-enforceability in the post-closing context, and that essential aspect of Delaware corporate law comes not from *Revlon* but from *Van Gorkom*.[83] We naturally think of the elimination of director liability as flowing from Section 102(b)(7) of the Delaware General Corporation Law (DGCL), for that section, to be sure, is the legal basis for the elimination of that liability.[84] It is no stretch, however, to think of the elimination of that liability as *Van Gorkom* immunity.[85] That kind of immunity was essential to the creation of the Delaware system of merger regulation, for it results in all the critical regulatory decisions—that is, litigations about alleged fiduciary breaches—being made pre-closing.[86] It compels the establishment, as it were, of a system in which the Delaware courts *pre-clear* mergers for fiduciary compliance before they close in much the same way (and for very similar reasons) as the antitrust authorities pre-clear mergers for antitrust compliance under the Hart-Scott-Rodino Act.[87]

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[77] *See infra* text accompanying notes 671–75.

[78] *See* Smith v. Van Gorkom, 488 A.2d 858, 893 (Del. 1985); *infra* text accompanying notes 636–40.

[79] *See supra* text accompanying notes 30–34.

[80] *See infra* text accompanying notes 671–79.

[81] *See id.*

[82] *Id.*

[83] *See infra* text accompanying notes 627–31.

[84] *See* DEL. CODE ANN. tit. 8, § 102(b)(7) (West 2015).

[85] *See infra* text accompanying notes 686–88.

[86] *See infra* text accompanying notes 631–35.

[87] Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (2006). *See generally* PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST

The balance of this Article consists of three parts. Part I reviews the context in which *Van Gorkom* arose and then reconsiders *Van Gorkom* as a *Revlon* case, comparing the reasoning in the case to what the Delaware Supreme Court could have said had it adopted the principles it would espouse ten months later in *Revlon*.[88] This comparison highlights just how unpersuasive and chaotic the *Van Gorkom* opinion was by showing what, with the benefit of thirty years of hindsight, it could have been.[89] Along the way, the Article clarifies a few matters at issue between the majority and the dissent, distinguishing disagreements about how the duty of care applied to the facts of the case from disagreements about whether directors would have new and different fiduciary duties in the context of approving a business combination.[90] Part II elaborates on the argument that *Van Gorkom* was the *Kobayashi Maru* of Delaware corporate law, and that the Delaware Supreme Court had available to it no right answer—that is, if the court reached the correct (by *Revlon* standards) result that the Trans Union directors had breached their fiduciary duties, the court's holding, no matter how well-reasoned, would be fatal to Delaware corporate law.[91] Part II also reconsiders the genius of the legislative solution—the creation of a duty enforceable only by injunction when a breach is threatened and not by monetary damages when a breach has been completed—and explains the similarities of this system to the Hart-Scott-Rodino system for pre-clearing mergers for antitrust purposes.[92] The Conclusion offers some observations about how extraordinary a development in the law *Smith v. Van Gorkom* really was.[93]

LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION (2d ed. 2000); STEPHEN M. AXINN ET AL., ACQUISITIONS UNDER THE HART-SCOTT-RODINO ANTITRUST IMPROVEMENTS ACT (2017); PREMERGER NOTIFICATION PRACTICE MANUAL (Anthony W. Swisher & Neil W. Imus eds., 4th ed. 2007).

[88] *See infra* Part I.

[89] *See id.*

[90] *See id.*

[91] *See infra* Part II.

[92] *See id.*

[93] *See infra* Conclusion.

I. *SMITH V. GORKOM* AS A *REVLON* CASE

This Part (a) reviews the facts in *Van Gorkom*, and then (b) reconsiders how the case would have turned out if the court had applied *Revlon* and its progeny to the facts in the case. In so doing, some of the disagreements between the majority and the dissent may be clarified, including by showing how some disagreements were really about whether directors would have new and special duties in selling the company and other disagreements were more about how pre-*Revlon* doctrine should have been understood and applied.

A. The Facts in Van Gorkom

The facts in this case, at least as found by the Delaware Supreme Court,[94] are familiar to corporate law scholars, but given the disorganization of the majority's opinion—it recites its finding of facts in Part I but then goes on to find some of the most important facts only later in Parts II and III as it applies the law to the facts—recounting the facts in chronological order is probably worthwhile. Moreover, Owen's account in *Autopsy of a Merger*, though generally consistent with that of the Delaware Supreme Court, often includes additional facts that are highly illuminating.[95] The account below generally follows that of the

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[94] The Delaware Supreme Court did indeed find the facts. *See* Smith v. Van Gorkom, 488 A.2d 858, 871 (Del. 1985). In reviewing the findings of fact by the Court of Chancery, the Supreme Court repeatedly held that these findings were "contrary to the record and not the product of a logical and deductive reasoning process." *Id.* (referring to the language of Levitt v. Bouvier, 287 A.2d 671, 673 (Del. 1972), which it had just quoted). The court went on to apply the holding in *Levitt* to the effect that "when the findings below are clearly wrong and the doing of justice requires their overturn," the Delaware Supreme Court is "free to make contradictory findings of fact." *Van Gorkom*, 488 A.2d at 871. This occasioned some severe criticism. *See, e.g.*, Quillen, *supra* note 28, at 472–74. To say the least, it is possible that the Delaware Supreme Court's account of the facts is in some respects mistaken or incomplete; the dissenting justices in the case surely thought this. *See Van Gorkom*, 488 A.2d at 893–94 (McNeilly, J., dissenting) (stating that the majority opinion "reads like an advocate's closing address to a hostile jury" and is a "comedy of errors").

[95] *See generally* OWEN, *supra* note 3. In 1983, the Pritzkers sued Owen to prevent him from publishing this book even as it was being serialized in *Crain's Chicago Business*. *See Pritzkers Seeking to Squelch Book on Trans*

Delaware Supreme Court but, as expressly noted, integrates facts from Owen in several place.

Trans Union was a cash cow company,[96] producing a significant and presumably increasing free cash flow,[97] primarily from its business of leasing rolling-stock to businesses that shipped goods by rail.[98] However, the company had a persistent problem in generating sufficient taxable income to use all of the investment tax credits (ITCs) to which it was entitled under the tax laws as then in effect.[99] Over the years, Trans Union had in part dealt with this problem by acquiring smaller companies that had taxable income against which Trans Union could use its ITCs.[100] In 1980, however, Congress was considering amending the tax code to allow corporations to accelerate depreciation of capital assets, and this would have further exacerbated Trans Union's inability to use all of its available ITCs.[101] Having unsuccessfully lobbied Congress to make the ITCs refundable and dissatisfied with the expedient of acquiring smaller companies with taxable income,[102] the company's chairman and chief executive officer, Jerome W.

Union Merger, CRAIN'S CHICAGO BUSINESS, Dec. 19, 1983, at 2. The Pritzkers' motives for this extraordinary (and unsurprisingly futile) suit remain obscure. *See* Rance Crain, *Don Reuben Plays Both Sides*, CRAIN'S CHICAGO BUSINESS, Dec. 26, 1983, at 10 (stating that in the sections of the book *Crain's* published "the Pritzkers come off very well" and "even in the later sections detailing the dismantling of the Trans Union Corp. staff, there is little that hasn't appeared before or that Bob Pritzker hasn't boasted about elsewhere").

[96] *Id.* at 3 (stating Trans Union was a "cash cow" business). Owen also notes that Trans Union was in the Fortune 500 in 1978 and had revenues of $922 million and net income of $60 million in 1979. *Id.* at 4–5. It had turned a profit every year for sixty-nine consecutive years. *Id.* at 4. For a fascinating account of the origins of Trans Union in the nineteenth century, see Bainbridge, *supra* note 60, at 201–02.

[97] *See* OWEN, *supra* note 3, at 5, 34.

[98] *See id.* at 4. In 1980, Trans Union owned 51,000 tank cars and 12,000 rail cars of other types. *Id.* at 3.

[99] *See id.* at 24–25, 28. On ITCs, and the relation between ITCs and accelerated depreciation, see *id.* at 23–27.

[100] *See id.* at 28–29.

[101] *See id.* at 24, 30. To use all of its available ITCs, Trans Union would then have needed an additional $150 million per year in taxable income. *Id.* at 30. In 1979, Trans Union's total taxable income was only $100.5 million. *Id.*

[102] *See id.* at 25–28, 30; *see also* Bainbridge, *supra* note 60, at 202–03 (discussing Trans Union's tax problems and the options the company's managers considered to deal with them).

Van Gorkom,[103] along with other senior managers of the company, began considering a possible sale of the company to a larger corporation that could make full use of Trans Union's ITCs.[104]

At a meeting on September 5, 1980, prompted by news stories about leveraged buyouts (LBOs), Donald Romans, Trans Union's chief financial officer, presented to Van Gorkom and other senior executives of the company a preliminary study of the feasibility of an LBO of Trans Union.[105] The prices in the study ranged from $50 and $60 per Trans Union share, but at the time, Trans Union's shares were trading in the high thirties.[106] Although not noted by the Delaware Supreme Court, this was the first time Van Gorkom had ever heard of LBOs.[107] Although he thought a management-led buyout involved too many conflicts of interests to be desirable, Van Gorkom found a price of $55 per share attractive, at least from his personal perspective

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[103] For background on Van Gorkom personally, see William M. Owen, *A CEO Named Van Gorkom*, 24 DIRECTORS & BOARDS 35 (2000). *See also* Bainbridge, *supra* note 60, at 204–05.

[104] *See* OWEN*, supra* note 3, at 30–31; *see also* Helen M. Bowers, *Fairness Opinions and the Business Judgment Rule: An Empirical Investigation of Target Firms' Use of Fairness Opinions*, 96 NW. U.L. REV. 567, 568–69 (2002) (describing the larger economic context of the Trans Union merger and arguing that the transaction was typical of the merger wave of the 1980s in which "acquiring firms sought targets that offered the opportunity to liberate cash by some method of post-acquisition restructuring or to take advantage of investment tax credits").

[105] *See* OWEN, *supra* note 3, at 36.

[106] *Id.*

[107] *See id.* at 37 (stating that "Van Gorkom had not heard of the concept of a leveraged buyout before the meeting"). This was not because Van Gorkom was unsophisticated or ignorant; it was because, in the fall of 1980, LBOs were still something new under the sun and, apparently, not well-understood outside of certain financial and legal circles. *See* Richard E. Rustin, *Kohlberg Kravis Hones Its Takeover Technique*, WALL ST. J., Sept. 25, 1980 at 35, in which the Wall Street Journal thought it had to explain to its readers that a certain transaction proposed by KKR was "called a 'leveraged buy-out'" because it "involve[s] using borrowed money to purchase a company ... and then converting it into a privately held concern." As becomes clear below, a general failure by Van Gorkom and other insiders at Trans Union to understand how LBOs work may have been an important reason for the failure of the KKR bid. More generally, it is critical to keep in mind that the world of M&A deal making was vastly less sophisticated in 1985 than it is today. *See Roundtable*, *supra* note 23, at 39 (Stephen M. Waters, stating "this was a much less sophisticated environment").

as a stockholder, and he became intrigued by the possibility of a leveraged buyout by a third party.[108] At sixty-three years of age,[109] he was approaching Trans Union's mandatory retirement age of sixty-five and may have wanted to liquidate the 75,000 Trans Union shares he held.[110] Van Gorkom then secretly directed the company's controller, Carl Peterson, to study the feasibility of an LBO of the company at $55 per share, assuming the acquirer would make an equity contribution of $200 million and would sell certain weaker-performing divisions.[111] In particular, Van Gorkom wanted to know whether, given certain assumptions about the interest rates that would be available for debt financing,[112] the acquirer could retire the debt to be incurred in

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[108] *See* OWEN, *supra* note 3, at 37–39.

[109] *Id.* at 5.

[110] Owen, who seems to treat Van Gorkom and others quite objectively, noting the bad along with the good, never discusses this theory as a serious possibility. It apparently originated in a *Crain's Chicago Business* story. *Id.* at 107–08. As explained below, Owen presents near-overwhelming evidence that Van Gorkom—though not some of the other senior executives at Trans Union—sincerely believed that management's first duty, if the company was to be sold, was to get the best price for stockholders. *See, e.g.*, *id.* at 93.

[111] According to Owen, the other assumptions were that (a) the acquirer would borrow $490 million, (b) the divisions to be sold would net the company some $102 million, (c) the interest rate on the debt would range from 12 percent to 14 percent, and (d) the company would achieve the cash flows projected in the company's existing five-year projections. *Id.* at 45. As far as appears from the opinion of the court and Owen, this analysis took no account of the tax benefit the acquirer would capture from Trans Union's excess ITCs. *See* Smith v. Van Gorkom, 488 A.2d 858, 876 (Del. 1985). *See generally* OWEN, *supra* note 3.

[112] Van Gorkom intended to, and later in fact did, help the acquirer arrange financing from Trans Union's own banks. *See Van Gorkom*, 488 A.2d at 867. *See* OWEN, *supra* note 3, at 127. In contemporary terms, Van Gorkom was arranging a form of stapled financing for the acquirer. *See* Christopher Foulds, *My Banker's Conflicted and I Couldn't be Happier: The Curious Durability of Staple Financing*, 34 DEL. J. CORP. L. 519, 520 (2009). Although never noted by the Delaware Supreme Court and as discussed below the interest rate environment, in which the Trans Union merger was negotiated and consummated was critically important to the participants. *See infra* note 250 and accompanying text. For, on September 20, 1980, the day the Pritzker–Trans Union merger agreement was signed, the prime rate was 12.5 percent, OWEN, *supra* note 3, at 128, and the effective federal funds rate that month was 10.87 percent. *See Effective Federal Funds Rate,* FED. RESERVE BANK OF ST. LOUIS, https://fred.stlouisfed.org/series/FEDFUNDS [https://perma.cc/JZ9S-VVNY]. Interest rates would increase steadily thereafter, and by January of

the transaction within five years.[113] Peterson reported that, on the assumptions Van Gorkom gave him, between $50 million and $80 million of the required debt would remain outstanding after five years.[114]

On Sunday, September 14, Van Gorkom met with Jay Pritzker, who had built his family's business, the Marmon Group, which included the Hyatt Hotel chain, into a vast portfolio of companies, largely through acquisitions.[115] Van Gorkom presented to Pritzker the transaction structure he had devised, including the $55 per share price, which implied an aggregate valuation for Trans Union of about $690 million.[116] Van Gorkom presented Pritzker with a handwritten financial analysis of the transaction very similar to the one Petersen had prepared. It assumed a $200 million equity contribution, $490 million of debt financing at 14 percent interest, and sales of various minor Trans Union units that would net $102 million.[117] Although not noted by the Supreme Court, it seems that Van Gorkom approached Pritzker as much to seek his advice about the feasibility of an LBO of Trans Union as to offer to sell him the company.[118] Pritzker, who thought the meeting would concern the business of the Chicago School Finance Authority, on which he and Van Gorkom both served,[119] was surprised when Van Gorkom began a discussion of a possible acquisition of Trans Union, and he clearly took Van Gorkom to be soliciting an offer to purchase Trans Union.[120] Emphasizing

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1981, when KKR was attempting to arrange financing for its bid for Trans Union, the prime rate had reached 20.5 percent, the highest rate it would ever reach before or since, OWEN, *supra* note 3, at 128, and the effective federal funds rate had reached 19.08 percent. *Effective Federal Funds Rate,* FED. RESERVE BANK OF ST. LOUIS, https://fred.stlouisfed.org/series/FEDFUNDS [https://perma.cc/JZ9S-VVNY].

[113] *Van Gorkom*, 488 A.2d at 866.

[114] *Id.*

[115] *See* OWEN, *supra* note 3, at 8; *see also* Bainbridge, *supra* note 60, at 205–06 (discussing Pritzker's background and the history of the Marmon Group).

[116] OWEN, *supra* note 3, at 49.

[117] William M. Owen, *Trans Union: Behind the Scenes of a Giant, Controversial Merger*, CRAIN'S CHICAGO BUSINESS, Dec. 19, 1983, at 25 [hereinafter Owen, *Trans Union*]; *see also* OWEN, *supra* note 3, at 45.

[118] OWEN, *supra* note 3, at 48.

[119] *Id.*

[120] According to Pritzker, Van Gorkom "commenced talking about the sale or merger of Trans Union" and this "came as something of a shock to me ... because

that Van Gorkom's LBO structure assumed significant increases in Trans Union's cash flow,[121] Pritzker attempted to negotiate the price down to $50 per share, but Van Gorkom refused, and there was no further discussion of price.[122] In what would become a matter of great significance, Van Gorkom told Pritzker that, in any possible transaction, Trans Union would reserve the right to accept a superior offer if such should emerge, and Pritzker replied that, if his organization was to thus act as a stalking horse, he would have to receive an option to purchase a large amount of Trans Union stock at its undisturbed market price to compensate him if another buyer should ultimately acquire the company.[123] By the next day, Monday, September 15, Pritzker informed Van Gorkom that he was interested in pursuing a transaction on the terms they had discussed.[124]

On Tuesday, September 16, and Wednesday, September 17, Pritzker and his representatives met with Van Gorkom and certain Trans Union employees so Pritzker could conduct due diligence on the company.[125] In order to guard against the possibility that news of the potential transaction would leak, Van Gorkom involved only a very small number of senior Trans Union executives in the due diligence process.[126] Most of Trans Union's senior management, including Romans (the chief financial officer) and key operations officers, were kept entirely in the dark—a fact that later became very important.[127] Meanwhile, Pritzker's attorney was drafting a

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you don't usually have the chief executive officer of a company come in this fashion. At least I hadn't had that experience." *Id.* at 48–49.

[121] Owen, *Trans Union*, *supra* note 117.

[122] *See* Smith v. Van Gorkom, 488 A.2d 858, 866 (Del. 1985). Pritzker later stated that Van Gorkom said firmly that Pritzker could not buy the company for less than $55 per share and so Pritzker "quickly concluded that if you were going to make a deal, you might as well think in the $55 term, and if financing could be properly worked out, perhaps you could afford to pay $55 a share." Owen, *Trans Union*, *supra* note 117.

[123] OWEN, *supra* note 3, at 51–52.

[124] *Van Gorkom*, 488 A.2d at 867.

[125] By contemporary standards, of course, the speed and resulting cursory nature of Pritzker's due diligence is astonishing. It is perhaps worth noting that the Trans Union executives involved at the time were shocked as well. *See* OWEN, *supra* note 3, at 58–59. Chelberg, Van Gorkom's heir apparent as chief executive officer, thought—incorrectly—that Van Gorkom had pressured Pritzker to move so quickly. *Id.* at 59.

[126] OWEN, *supra* note 3, at 58–59.

[127] *See Van Gorkom*, 488 A.2d at 874.

merger agreement.[128] Although they had no further discussions about price, Van Gorkom and Pritzker did negotiate further about the stock option and finally agreed that, when Pritzker's financing condition was fulfilled or waived, he would be entitled to acquire from Trans Union one million shares of its common stock at $38 per share, which was seventy-five cents above the closing market price of the shares on Friday, September 19.[129] Also on September 19, Pritzker demanded that the merger agreement be executed no later than the evening of Sunday, September 21, before financial markets opened in the United Kingdom on the following Monday.[130] Accordingly, that same day, September 19, Van Gorkom called a meeting of his senior executives for 11:00 AM, and a special meeting of the Trans Union directors for noon the following day, Saturday, September 20.[131] Van Gorkom did not reveal the purpose of the meeting to either group.[132]

On Saturday, September 20, both meetings were held. At the earlier meeting with the Trans Union executives, Van Gorkom apprised his senior officers of the offer from Pritzker.[133] The reaction of the executives was almost entirely negative, with Romans in particular noting that, based on a further analysis he had conducted, an LBO could be completed at prices ranging from $55 to $65 per share, which put the Pritzker offer at the bottom of the range.[134] Romans stated that he thought a better price for the company could, and should, be obtained.[135]

The Trans Union directors met at noon.[136] The board consisted of five inside directors, including Van Gorkom, and five outside directors,[137] all of whom were eminently well-qualified:

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[128] *Id.* at 867.

[129] *Id.*

[130] *Id.*

[131] *Id.*

[132] Showing remarkable prescience, Romans guessed that Van Gorkom would announce that he had sold the company to Pritzker and he stated to another Trans Union executive before the meeting that it "better not be for less than $60 per share." OWEN, *supra* note 3, at 62.

[133] *Van Gorkom*, 488 A.2d at 867.

[134] *Id.*

[135] *Id.* at 886.

[136] *Id.* at 867.

[137] If we assume that Van Gorkom was interested in the Pritzker transaction, then since five of the ten directors were employees under Van Gorkom's control, a majority of the ten-member board was conflicted and the board

four were chief executive officers of corporations larger than Trans Union, and the fifth was the former dean of the University of Chicago Business School.[138] All of the directors were thoroughly familiar with Trans Union and its business and financial condition, including its ongoing problem of realizing the full value of its ITCs.[139] Van Gorkom made a twenty-minute oral presentation about the Pritzker offer, and it seems that James Brennan, the company's attorney, made a presentation about the terms of the proposed merger agreement,[140] but the directors received no written materials about the transaction.[141] Although not noted by the Supreme Court, at least one director seems to have expressed surprise that Van Gorkom would undertake to sell the company essentially by himself without the input of management or the board of directors.[142] Van Gorkom did not disclose to the board that he selected the $55 per share price based on Peterson's determination of the feasibility of an LBO, nor did he explain the history of price negotiations between himself and Pritzker.[143]

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would have lost the protection of the business judgment rule in approving the merger simply for this reason. *See, e.g.,* Orman v. Cullman, 794 A.2d 5 (Del. Ch. 2002). Furthermore, although not noted by the Delaware Supreme Court, Van Gorkom was on the board of a corporation of which one of the outside Trans Union directors was chief executive officer. OWEN, *supra* note 3, at 19. Under contemporary Delaware law, this might raise an issue as to whether that director also was truly independent. *See* Orman v. Cullman, 794 A.2d 5, 35–36 (Del. Ch. 2002). Consciences were clearly not as delicate in 1985, however, and this issue seems never to have been raised.

[138] *Van Gorkom*, 488 A.2d at 894. Macey has argued that *Van Gorkom* should be understood as creating a one-size-fits-all rule about directorial care that, while not truly needed for directors like those who sat on the Trans Union board, would greatly improve the decision-making of directors who are unqualified, lazy, poorly informed, avaricious or dishonest. Macey, *supra* note 57, at 619–21. Thus, while "the outcome in *Smith v. Van Gorkom*, appears questionable against the backdrop of the tremendous qualifications of [the Trans Union] board," the opinion "would not appear to be so odd if the court's admonishments about high deliberative standards, careful disclosure to [stock]-holders, and the use of qualified independent experts had been made to a board that was of demonstrably low quality." *Id.* at 628.

[139] *Van Gorkom*, 488 A.2d at 876.

[140] The dissent mentions a presentation by Trans Union's attorney, but the majority opinion does not. *See id.* at 895 (McNeilly, J., dissenting).

[141] *Id.* at 874 (majority opinion).

[142] OWEN, *supra* note 3, at 70.

[143] *Van Gorkom*, 488 A.2d at 868.

Romans, who attended the meeting in his capacity as chief financial officer, but who was not a director, told the board: that he had conducted some leveraged-buyout studies at $50, $55, $60, and $65 per share; that these studies were not valuation studies of the company; and that while he thought $55 per share was a fair price, it was at the low end of the range.[144] According to Van Gorkom's later account, the directors knew "that $55 might not be the highest price obtainable,"[145] and there was "considerable discussion about seeking an outside 'fairness opinion,'" but "no such opinion worthy of the name could be obtained" before the expiration of the offer.[146] At the conclusion of the meeting, the Trans Union directors voted to approve the merger agreement.[147]

Later, the board would assert that it did so on two conditions: first, that Trans Union would have the right to accept any better offer that might emerge (but not to solicit such offers), and, second, in order to facilitate such offers, Trans Union would be free to share confidential information with any potential bidder (Pritzker had originally sought to limit Trans Union to providing other potential bidders only publicly available information).[148] In contemporary terms, the board was willing to agree to a no-shop, provided it was qualified by a standard fiduciary-out.[149] Supposedly, the no-shop period was to extend for ninety days from

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[144] *Id.* at 869.

[145] Jerome W. Van Gorkom, *The 'Big Bang' for Director Liability: The Chairman's Report*, 12 DIRECTORS & BOARDS 17, 18 (1987).

[146] *Id.* at 18.

[147] *Van Gorkom*, 488 A.2d at 869.

[148] The Supreme Court majority seemed very skeptical about this. See *Van Gorkom*, 488 A.2d at 878. However, Owen accepts the directors' contention that these conditions were in fact discussed and imposed by the board at the September 20 meeting. *See* OWEN, *supra* note 3, at 73–74. Quillen points out that, in reversing the Court of Chancery's finding of fact on this issue, the Supreme Court disregarded the testimony of *all* the witnesses on this point. Quillen, *supra* note 28, at 473.

[149] *See generally* William T. Allen, *Understanding Fiduciary Outs: The What and the Why of an Anomalous Concept*, 55 BUS. LAW. 653, 653 (1999); Lou R. Kling, Eileen Nugent Simon & Michael Goldman, *Summary of Acquisition Agreements*, 51 U. MIAMI L. REV. 779, 782 (1997); J. Travis Laster, *Exposing a False Dichotomy: The Implications of the No-Talk Cases for the* Time/Revlon *Double Standard*, 3 DEL. L. REV. 179 (2000); Gregory V. Varallo & Srinivas M. Raju, *A Process-Based Model for Analyzing Deal-Protection Measures*, 55 BUS. LAW. 1609 (2000).

the date of the merger agreement (thus from about September 20 to about December 20), with the Trans Union stockholder meeting to consider the merger to follow on January 10 of the next year.[150]

The language of the merger agreement as executed by the parties, however, did not clearly reflect such arrangements.[151] After providing that Trans Union would call a stockholder meeting to consider the merger and that the Trans Union board would recommend that the stockholders adopt the merger agreement and use its best efforts to obtain the requisite vote, the agreement provided that the acquirer "acknowledges that the Trans Union directors may have a competing fiduciary obligation to the stockholders under certain circumstances."[152] The Delaware Supreme Court would make much of the vagueness of this language.[153] But it had to mean something, and at the least it would

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[150] *See Van Gorkom,* 488 A.2d at 878.

[151] *Id.*

[152] *Id.* at 879; OWEN, *supra* note 3, at 76.

[153] *See Van Gorkom*, 488 A.2d at 879. In this regard, see *supra* note 107, regarding the primitiveness of deal technology in 1985. Furthermore, it would likely be a mistake to conclude that Pritzker, the savvy dealmaker, had in this instance drafted the contract to benefit himself and harm Trans Union. It seems, rather, that the entire contract was slipshod even by the standards of 1980. Two examples make this clear. First, just before the eventual stockholder vote in February of 1981, Trans Union paid its usual quarterly dividend, which effectively cost Pritzker about $5 million. OWEN, *supra* note 3, at 185. Second, Trans Union made large retention and severance payments to many employees, which also cost Pritzker a significant amount of money. *Id.* at 204. Pritzker objected to both these actions and complained to Van Gorkom, but as neither action was prohibited by the merger agreement, Pritzker had to acquiesce. *Id.* Nowadays, it would inconceivable that a public company merger agreement not address such issues in the interim covenants section of the agreement. LOU R. KLING, EILEEN NUGENT SIMON & BRANDON A. VAN DYKE, NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS 795–98 (2017). Even in 1980, however, covenants prohibiting the target company from paying dividends or increasing employee compensation in material ways were well known. *See* JAMES C. FREUND, ANATOMY OF A MERGER 293–94 (1975). That a sophisticated dealmaker like Pritzker entered into a merger agreement not containing such standard and customary covenants protecting his interests suggests that, when the Trans Union directors insisted that the artless language in the September 20 agreement gave them a fiduciary out, they may have been correct. As to why the contract may have been so poorly drafted, the answer likely lies with Pritzker's whole philosophy of deal making. Owen, *Trans Union, supra* note 117, at 24, quotes Pritzker as saying that his father "convinced us that it is not the contract that makes a

seem to allow the Trans Union board to withdraw its favorable recommendation of the merger, to decline to use its best efforts to obtain the requisite vote, and probably even to recommend against the merger if the board determined that its fiduciary duties so required.[154] Although the dissent disagreed,[155] the majority found—and from a contemporary perspective this seems plainly correct—that this language did *not* give the Trans Union board the right to terminate the merger agreement in order to accept a superior proposal.[156]

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deal sound but how you behave afterward," and "[w]e've bought a lot of things on just a handshake or a paragraph or two. We're the least legal-minded people you'll ever meet."

[154] Such is Quillen's view as well. Quillen, *supra* note 28, at 473 (stating "this language in the agreement clearly related to the board recommendation" and noting that the extrinsic evidence, including the testimony of Pritzker, supported the view that the language meant that the Trans Union board could withdraw its recommendation of the Pritzker transaction and recommend a superior offer if one materialized). Note, however, that the analysis here and in the text reflects the contemporary understanding that a board may convene a stockholders meeting and bring before the stockholders proposals against which the board recommends. Such a possibility is expressly contemplated by, for instance, Section 146 of the DGCL. DEL. CODE ANN. tit. 8, § 146 (West 2003). In 1985, the law may have been different. For, in *Van Gorkom*, the court says that the board was mistaken to think that it could conduct a stockholders meeting and either recommend against a merger considered at the meeting or take no position in connection therewith; the board's only option, if it should later determine that the merger is no longer in the best interests of the stockholders, is to "rescind its agreement." *Van Gorkom,* 488 A.2d at 888. But if this is right, then the language in the merger agreement, which the majority said did *not* give the board a right to terminate the agreement to accept a better offer, probably did do just that, for then the board's withdrawing its recommendation in favor of the merger is tantamount to terminating the agreement. *Id.* This remains one of the minor mysteries of the case.

[155] While admitting that the language "is not artfully drawn," Justice McNeilly in his dissent maintained that "the evidence is clear that the intention underlying that language was to make specific the right that the directors assumed they had, that is, to accept any offer that they thought was better, and not to recommend the Pritzker offer in the face of a better one." *Id.* at 895 (McNeilly, J., dissenting).

[156] The majority wrote, "[c]learly, this language on its face cannot be construed as incorporating either of the two 'conditions' described above: either the right to accept a better offer or the right to distribute proprietary information to third parties." *Id.* at 879. Nevertheless, Pritzker would later testify that his understanding of the language was the same as that advanced by the Trans Union directors. OWEN, *supra* note 3, at 76.

The distinction was likely not as important, however, as the majority maintained. If a superior proposal for the company emerged, and the agreement allowed the board to recommend that the Trans Union stockholders vote against the Pritzker proposal in order to accept the superior one (or even if the agreement did *not* allow this), then the outcome of any stockholder meeting to consider the Pritzker proposal would likely have been a defeat for the proposal.[157] At that point, the merger agreement with Pritzker would presumably have to be terminated in some way or other, and Trans Union would be free to accept the superior proposal.[158] Pritzker would, of course, still in effect collect a termination fee resulting from the stock option Trans Union had granted him.[159] As to the right to share non-public information with a potential acquirer, surely Trans Union already had this right, and it would lose it only if the agreement *prohibited* such disclosure.[160] The fact that the agreement did not expressly authorize Trans Union to share non-public information about the company with potential bidders clearly cannot be construed as a contractual prohibition on such actions.[161]

In any event, in what was likely the most notorious signing in American corporate history,[162] Van Gorkom and Pritzker executed the merger agreement during the evening of Saturday, September 20, at a formal social event Van Gorkom was hosting for the opening of the Chicago Lyric Opera.[163] The Supreme Court's account of this event almost conjures a picture of Van Gorkom and Pritzker, both dressed in white tie at a lavish party,

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[157] OWEN, *supra* note 3, at 73.

[158] *See Van Gorkom*, 488 A.2d at 895 (McNeilly, J., dissenting).

[159] *Id.* at 858 (majority opinion).

[160] OWEN, *supra* note 3, at 76.

[161] *See generally* Matthew D. Cain & Steven M. Davidoff, *Form over Substance? The Value of Corporate Process and Management Buy-Outs*, 36 DEL. J. CORP. L. 849, 859 (2011).

[162] Surely, it was the only signing ever to produce a whole article dedicated to describing it. *See* William M. Owen, *Opening Night at the Opera*, 24 DIRECTORS & BOARDS 106 (2000). Quillen suggests that it was unfair of the Supreme Court to draw a negative inference from this event, which he describes as a "superficial fact[.]" Quillen, *supra* note 28, at 479. He is right about this. Whatever else went wrong in the deal process at Trans Union, the details of the physical execution of the merger agreement were not relevant.

[163] *Van Gorkom*, 488 A.2d at 869.

with Van Gorkom asking Pritzker to turn around so Van Gorkom can sign the agreement leaning on Pritzker's back.[164] The reality was not quite that dramatic. According to Owen, Van Gorkom was hosting a party in the penthouse of the Trans Union building and, at a certain point, although "[g]arbed in his formal black suit with tails and a white bow tie," Van Gorkom left the party and took the elevator down to a lower floor "carrying a tray laden with drinks."[165] There, "a group of lawyers—the beneficiaries of this thoughtfulness—was working diligently putting the finishing touches on the agreements," and Van Gorkom executed the agreements on behalf of Trans Union.[166]

On Monday, September 22, the parties publicly announced the merger.[167] The result was a rebellion among the company's senior executives, but contrary to the impression that may be created by the Supreme Court's account of the facts, the reason seems to have had little to do with the price Pritzker was offering.[168] At this point, Owen's account in *Autopsy of a Merger* is especially illuminating. To be sure, one group of executives led by Romans was interested in making a competing bid for the company in a management buy-out, and although these executives thought they could pay more than $55 per share and knew they would have to do so in order to outbid Pritzker, they obviously had strong incentives to keep the price as low as possible.[169] While they would argue that a higher price could and should be obtained,[170] they did not envision that price as being higher than the price they themselves were prepared to pay—probably about $60 per share.[171]

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[164] *See generally id.* Bainbridge goes so far as to suggest that "the concise take home lesson of the case may be that one ought not to conclude deals of this magnitude at the opera" because "doing so suggests an unseemly cavalier attitude." Bainbridge, *supra* note 60, at 226. In the retelling, this episode has undergone great transmogrification. According to one article, for example, the signing occurred in the opera house at intermission. Gregory R. Andre, *Tender Offers for Corporate Control: A Critical Analysis and Proposals for Reform*, 12 DEL. J. CORP. L. 865, 895 (1987).

[165] OWEN, *supra* note 3, at 2.

[166] *Id.*

[167] *Van Gorkom*, 488 A.2d at 869.

[168] OWEN, *supra* note 3, at 84–85.

[169] *Id.* at 84.

[170] *Id.*

[171] *See id.*

A larger group of executives was dissatisfied with the transaction for quite different reasons.[172] They worried about the effect the transaction would have on them personally.[173] As compared to those at the Pritzker's Marmon Group, the salaries, benefits, and perquisites offered by Trans Union were extraordinarily generous.[174] Indeed, the overwhelming impression left by Owen's account of the merger's effect on Trans Union's employees—Owen himself was an attorney in Trans Union's general counsel office, and his book describes interviews with over forty of his former colleagues—is that Trans Union was an extreme case of a public company providing lavish benefits to executives and other insiders.[175] As one of the employees interviewed by Owen puts it, Trans Union was "fat, dumb and happy" and deserved for that reason to be acquired.[176] Other Trans Union employees describe the company as being "sleepy,"[177] "relaxed,"[178] "complacent,"[179] and "cushy,"[180] and many said they expected to have at Trans Union "a job for life."[181] Emblematic of this culture was the corporate headquarters. In addition to the Trans Union Building in downtown Chicago, the company had built another headquarters in the Chicago suburb of Lincolnshire; the structure was set on a gigantic wooded parcel and resembled a country manor house (many of the 180 employees who worked there jokingly referred to it as "Camelot").[182] By contrast, the Pritzker's Marmon Group had a no-frills, cost-cutting culture, and Robert Pritzker was famous (or notorious) for insisting employees put out the lights in their offices when they went out to lunch.[183] Marmon was also famous for its extremely lean staffing, and Trans Union staffing levels were, by Marmon standards, exorbitant.[184] Many

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[172] *Id.* at 81.
[173] *Id.*
[174] *Id.* at 80.
[175] *See generally id.*; *infra* text accompanying notes 176–85.
[176] OWEN, *supra* note 3, at 236.
[177] *Id.* at 248.
[178] *Id.*
[179] *Id.* at 249.
[180] *Id.*
[181] *Id.* at 250.
[182] *Id.* at 208.
[183] *Id.*
[184] *Id.* at 210.

Trans Union executives worried—entirely correctly, as it turned out—that if Pritzker acquired Trans Union, many of the existing Trans Union executives would be terminated and those remaining would do much more work for much less pay.[185]

In this context, perhaps it should not have surprised Van Gorkom that many of his executives expressed their anger about the transaction precisely because of its potential effects on them personally.[186] At one critical meeting held to placate the angry executives, one of Van Gorkom's lieutenants flabbergasted him by stating that, in the lieutenant's view, the first duty of management was to the *employees* of the corporation.[187] To his credit, Van Gorkom consistently maintained throughout the process that the paramount concern was obtaining the best price for the stockholders.[188] Indeed, after the merger closed but long before

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[185] *Id.* at 213. After the Pritzker transaction was publicly announced, Van Gorkom called a meeting of the corporate staff at the Lincolnshire headquarters and emphatically assured them that "99.9 percent" of them would continue to be employed by the company under the new owners. *Id.* at 78. Owen suggests that Van Gorkom, suffering from an astonishing naiveté, actually believed this. *Id.* Within a year of the closing of the merger, the Pritzkers had sold the Lincolnshire building and fired virtually all of the 180 Trans Union employees who worked there. *Id.* at 208–10.

[186] *Id.* at 84–85.

[187] *Id.* at 92. According to Owen, "[t]he officer said something that Van Gorkom later testified 'really stunned' him. He said that he thought the company had obligations to its employees, its customers, and its [stock]holders—and that the employees clearly came before the [stock]holders." *Id.* Van Gorkom said that he "didn't want to get into a big argument with him" but told him, "[w]ell, we don't agree with that." *Id.*

[188] *Id.* at 91, 100. Of course, this would be precisely the duty of the directors under *Revlon*. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 184 (Del. 1986). In Owen's account, Van Gorkom consistently and vociferously stated that it was the duty of the directors and the officers to act selflessly to obtain the best price for the stockholders, and Van Gorkom insisted that, in his judgment, he had always so acted. OWEN, *supra* note 3, at 91, 100, 227. Pritzker later stated that Van Gorkom's focus on the interests of stockholders was extraordinary, saying, "I haven't run into many CEOs who view their constituency completely to be their [stock]holders. [Van Gorkom's] only interest seemed to be to get the absolute best price he could get for his [stock]holders." Owen, *Trans Union*, *supra* note 117, at 29. If this is correct—and it very likely is—this means that Van Gorkom fulfilled the subjective part of his *Revlon* duty; whether he fulfilled the objective part—i.e., whether he in fact took reasonable steps to get the best price reasonably available—is of course a separate question.

the decision of the Delaware Supreme Court, Van Gorkom stated to Owen in correspondence, "[o]ne of the most painful revelations growing out of the entire transaction ... was that there was such a total lack of understanding of the real responsibilities of top executives in a corporation like Trans Union. To me ... it was always obvious that our loyalties had to be the stockholders."[189] He goes on, "I was quite amazed to have one of our senior executives tell me that he felt the company's first loyalty should be to the employees and then to the customers and finally to the stockholders."[190]

Finally, a third group of executives was angry about the transaction not because they thought the price was too low nor even because they were worried about the effect of the transaction on them personally, but because they felt insulted that Van Gorkom had sold the company without consulting them.[191] As Romans would later explain say, the senior managers at Trans Union "w[ere] outraged by the way in which the Pritzker offer had been transmitted to them."[192] Indeed, one insider told *Crain's Chicago Business* that "Mr. Van Gorkom previously was viewed with respect," but after his announcing the Pritzker transaction "the attitude toward him is a cross between Faust and Darth Vader."[193] Perhaps difficult to understand in the contemporary world of mergers and acquisitions, these executives felt "disenfranchised" (a word Owen says was used over and over again) by how Van Gorkom had proceeded.[194] Most important among this group was Jack Kruizenga, the executive who headed Trans Union's largest and most profitable division, its rail car leasing business.[195] Van Gorkom had described Kruizenga as the executive "more key than any of the others."[196] At the urging of Romans,

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[189] OWEN, *supra* note 3, at 227.

[190] *Id.*

[191] *Id.* at 84.

[192] *Id.* at 92–93.

[193] *Id.* at 106.

[194] *Id.* at 82, 84, 94. Bainbridge speculates that Van Gorkom's failure to involve his senior managers in the sales process and the resulting often vehement complaints from those managers negatively affected Trans Union's case before the Delaware Supreme Court. Bainbridge, *supra* note 60, at 212–13.

[195] OWEN, *supra* note 3, at 13, 86.

[196] *Id.* at 86. Van Gorkom thought Kruizenga would be very difficult to replace; this was in contradiction to Romans, who Van Gorkom thought could be easily replaced. *Id.* at 90.

Kruizenga signed a letter resigning from Trans Union, and together Romans and Kruizenga obtained similar letters from about fifteen other senior Trans Union executives.[197] Kruizenga then informed Van Gorkom he was holding the letters and threatened to deliver them.[198] At a lunch on October 3, 1980, Kruizenga expressly told Van Gorkom that he had no objection at all to the $55 price.[199] Rather, he was "madder than hell" at Van Gorkom because he and the other senior executives had been disenfranchised.[200] Emphasizing his long and loyal service to Trans Union, Kruizenga told Van Gorkom, "Now you have sold the company … and you didn't permit any of us who helped you build the company participate in that decision. I think it's totally unreasonable for you to take the position that you know everything about everything."[201] Kruizenga threatened to deliver the resignation letters, including his own, "unless [Van Gorkom] g[o]t [the merger agreement with Pritzker] reopened to give [Trans Union] an opportunity to look for another offer."[202] Given that Kruizenga was clear that he was not objecting to the $55 per share price, it seems that, to the extent that Kruizenga was thinking clearly about the matter, what he wanted in reopening the contract with Pritzker was an opportunity to participate in the process, regardless of whether that process produced a higher price for the stockholders—a course of action that may well have involved a breach of the fiduciary duty of good faith.[203] In the same conversation, Van Gorkom argued that their first duty was to the stockholders and that the stockholders should have an opportunity to vote on the $55 per

[197] William M. Owen, *Trans Union's Controversial Merger: Executives Go for a Leveraged Buyout*, CRAIN'S CHICAGO BUSINESS, Dec. 26, 1983, at 17 [hereinafter Owen, *Leveraged Buyout*].

[198] *Id.*

[199] OWEN, *supra* note 3, at 90.

[200] *Id.* at 94.

[201] *Id.* at 95.

[202] *Id.*

[203] The Chancellor says, the protection of the business judgment rule is not available "to a fiduciary who could be shown to have caused a transaction to be effectuated (even one in which he had no financial interest) for a reason unrelated to a pursuit of the corporation's best interests." *In re* RJR Nabisco S'holder Litig., No. 10389, 1989 WL 7036, at *15 (Del. Ch. 1989). He continues, "[g]reed is not the only human emotion that can pull one from the path of propriety; so might hatred, lust, envy, revenge … or shame or pride," *id.*, of which the last may have been relevant to situation discussed in the text.

share offer,[204] but this seems to have made little impression on Kruizenga.[205] Van Gorkom left the meeting thinking that there was little he could do to satisfy Kruizenga and the other executives aligned with him.[206]

Assuming that it would placate the group of executives who thought the price was too low, if not the other groups, Van Gorkom approached Pritzker about amending the agreement.[207] Van Gorkom and Pritzker discussed changes to the merger agreement, but they apparently did not agree on any precise language.[208] Although not noted by the Delaware Supreme Court, Van Gorkom then called a meeting of the executives objecting to the deal and presented to them certain changes to the merger agreement that Pritzker had advised Van Gorkom he would accept: the agreement would be amended to permit Trans Union to actively solicit offers for the company (in contemporary terminology, Pritzker agreed to a "go shop")[209] until January 31, 1981, and the Trans Union stockholder meeting to consider the Pritzker transaction would be pushed back to February 10, 1981.[210] This would give the company almost four months to conduct an active market test of the $55 per share price in the merger agreement with Pritzker. Van Gorkom thought that such changes may well satisfy the executives who were concerned about the price in the Pritzker transaction but would do nothing to appease the executives who opposed the transaction for other reasons.[211] To his amazement, however, Kruizenga and all the other executives whose objections to the merger were not based on the price enthusiastically approved the changes, indicated that they were now satisfied with the terms of the deal, would withdraw their threats to resign, and would even promise to remain with Trans

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[204] OWEN, *supra* note 3, at 95.

[205] *Id.*

[206] *Id.*

[207] *Id.* at 96.

[208] *Id.* at 96–97.

[209] In contemporary terminology, a "go shop." *Go Shop Period*, *Investopedia*, http://www.investopedia.com/terms/g/go-shop-period.asp [https://perma.cc/6KVE-W4QU].

[210] OWEN, *supra* note 3, at 96, 150.

[211] *Id.* at 97.

Union for six months after a transaction (regardless of whether it was with Pritzker or another acquirer) closed.[212]

On October 8, Van Gorkom reconvened the Trans Union board and described the proposed changes to the merger agreement.[213] The Trans Union board approved the proposed changes and engaged Salomon Brothers, its usual financial advisor, to solicit offers for the company during the go shop period.[214] On October 9, the parties announced that the merger agreement had been amended, that Pritzker's financing condition had been fulfilled, and that Pritzker had exercised the stock option to acquire one million Trans Union shares at $38 per share.[215] Only on October 10 did Pritzker's attorney deliver to Van Gorkom a draft amendment to the merger agreement.[216] Van Gorkom executed the amendment and returned it to Pritzker without reviewing it to determine if it actually reflected the terms that he had described to the board and that the company had announced to the public.[217]

The text of the amendment the parties executed did authorize Trans Union to solicit offers for the company through January 31, 1981, but it also contained other provisions the significance of which, the Supreme Court found, Van Gorkom personally seems not to have understood and that the board appears never to have considered.[218] In particular, whereas, under the reading of the original September 20 merger agreement most favorable to Trans Union, the company could terminate the agreement only if, prior to January 10, it received a superior offer for the company,[219] under the October 10 amendment to the agreement Trans Union could terminate the agreement only if, prior to February 10,[220] it either (a) had consummated a merger (or similar transaction), or (b) had entered into a definitive agreement

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[212] *Id.* at 101.

[213] *Id.* at 102.

[214] *Id.* at 103–04. The board specifically did *not* engage Salomon Brothers to provide a fairness opinion related to the Pritzker or any other offer, or to otherwise opine on the value of Trans Union. *Id.* at 103.

[215] *Id.* at 104.

[216] Smith v. Van Gorkom, 488 A.2d 858, 870 (Del. 1985).

[217] *Id.* at 883.

[218] *Id.* at 870.

[219] *Id.* at 895.

[220] The Delaware Supreme Court gives the deadline as February 10, 1981. *Id.* at 896. According to Owen, the date was January 31, 1981. OWEN, *supra* note 3, at 102.

related to such a transaction that was superior to the Pritzker offer and subject only to stockholder approval (*i.e.,* contained no financing condition).[221] Thus, while the shopping period was extended by a month from January 10 to February 10, what Trans Union would have to accomplish in that period in order to avail itself of the right to terminate the agreement was greatly increased.

Contemporary fiduciary outs are virtually always based on the target company's receiving a superior offer, not on its entering into a superior definitive agreement.[222] The reasons for this are many, but a key one is that, while Van Gorkom's experience with Pritzker may suggest otherwise, it typically takes acquirers a considerable period of time to conclude due diligence on the target, for the parties to negotiate the text of a definitive agreement, and for the bidder to secure financing[223] (recall that the October 10 amendments required that the definitive agreement not include a financing condition).[224] But four months—the period

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[221] *Van Gorkom*, 488 A.2d at 895–96. Owen states that the competing agreement could also include, as a closing condition, the absence of an injunction prohibiting the consummation of the merger. OWEN, *supra* note 3, at 103. It is worth noting that, not only could the new bidder not have a financing condition, it also could not have a condition related to antitrust or regulatory approvals—a condition that was potentially quite important because Trans Union had significant Canadian operations and, at the time, under Canada's Foreign Investment Review Act, the Canadian government could block mergers affecting even the indirect ownership of Canadian assets unless it found that the transaction involved "a 'significant benefit to Canada.'" *See id.* at 174. As things developed, KKR dealt with this issue by including Canadian citizens in its proposed transaction. *Id.* at 175. General Electric Credit Corporation (GECC), on the other hand, would have had significant difficulty getting approval, and so any transaction with Trans Union that did not include the obtaining of such approval as a condition to closing would have involved substantial risk for GECC. *Id.* at 174–76. The Pritzker agreement included a condition that, at the time of closing, the Canadian authorities had not *disapproved* the transaction—not a condition that the Canadian authorities had approved it—and so the Pritzkers were bearing some risk that the Canadian authorities would later act to undo the merger. *Id.* at 175.

[222] *Fiduciary Out*, Practical Law Glossary Item 5-382-3460 (West 2017).

[223] Richard D. Harroch & David A. Lipkin*, 20 Key Due Diligence Activities In A Merger And Acquisition Transaction*, FORBES (Dec. 27, 2014, 1:09 PM), https://www.forbes.com/sites/allbusiness/2014/12/19/20-key-due-diligence-activities-in-a-merger-and-acquisition-transaction/#6b83b2dc4bfc [https://perma.cc/6URT-APN5] (describing the multiple due diligence activities that must take place prior to closing of a mergers and acquisitions transaction).

[224] *Van Gorkom*, 488 A.2d at 882.

from October 10 to February 10—is hardly an unreasonably short period of time for a determined acquirer and eager target to negotiate a definitive agreement, and thus, the Delaware Supreme Court's conclusion that the marketing period was "effectively reduced" by requiring Trans Union to obtain a definitive agreement rather than merely an offer in order to terminate the merger agreement may be exaggerated.[225] It remains true, however, that the aggregate effects of the October 10 amendments to the merger agreement were not simply to extend the shopping period. By requiring a definitive agreement and not merely an offer, the net effect of the amendments on the feasibility of Trans Union's exercising its option to terminate the agreement and take a superior offer is unclear. As discussed below, however, the significance of this is questionable. If a bidder launched a credible tender offer for the shares of Trans Union at a price materially above $55 per share, it is very unlikely the Trans Union stockholders would have voted to approve the Pritzker transaction, regardless of whether the Trans Union board could exercise a fiduciary out to terminate the agreement.[226]

During the go shop period, Salomon Brothers approached approximately 150 potential bidders.[227] The most serious interest came from General Electric Credit Corporation (GECC),[228] and its effort was headed by a young Jack Welch.[229] Throughout, GECC proceeded at what Van Gorkom would later call "glacial" speed.[230] The Delaware Supreme Court's opinion fails to mention that Borg Warner, Bendix, and Genstar all conducted due diligence on Trans Union during the go shop period, but none ultimately made an offer for the company.[231] Owen states that

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[225] *Id.* at 883.

[226] For further discussion of how important all this actually was, however, see *infra* Section I.C.4.

[227] *Van Gorkom,* 488 A.2d at 896; *see* OWEN, *supra* note 3, at 119 (suggesting that Salomon Brothers' selling efforts were in some ways defective, noting that it took them three weeks to produce a brochure to be distributed to potential buyers and that, even when completed, the brochure contained inconsistent information).

[228] *Van Gorkom*, 488 A.2d at 896. *See generally* OWEN, *supra* note 3, at 150, 165.

[229] OWEN, *supra* note 3, at 168.

[230] *Id.* at 167.

[231] *Id.* at 188 (mentioning Borg Warner and Bendix); *id.* at 190 (mentioning Genstar).

some Trans Union insiders thought that Pritzker's option to acquire one million Trans Union shares deterred other offers, but assuming a topping offer at $60 per share, that option's value was only $22 million or about 3 percent of the value of the equity value of the transaction.[232] Of course, under contemporary conditions, a 3 percent termination fee in a $750 million transaction would be consistent with market practice and would almost certainly be found to be legal under *Unocal*.[233] Moreover, according to Owen, none of the potential acquirers who conducted due diligence on Trans Union ever mentioned Pritzker's option as an impediment to its making an offer.[234]

Meanwhile, Romans, the company's chief financial officer, who had been critical of the transaction with Pritzker from the beginning, had organized some of the other executives dissatisfied with the merger and approached Kohlberg, Kravis, Roberts & Co. (KKR) about a management buyout of Trans Union.[235] In the Delaware Supreme Court's account of the facts, on December 2, KKR presented a letter to Van Gorkom in which KKR and the Reichmann family of Canada (the owners of Olympia & York), along with certain Trans Union executives (excluding Van Gorkom and his heir apparent Chelberg),[236] offered to acquire

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[232] *Id.* at 120.

[233] *See, e.g., In re* Dollar Thrifty S'holder Litig. 14 A.3d 573, 614 (Del Ch. 2010) (3.9 percent and referring to a 3 percent termination fee as "standard"); *In re* Cogent, Inc. S'holder Litig., 7 A.3d 87 (Del. Ch. 2010) (3 percent termination fee did not violate *Unocal*); *In re* Topps Co. S'holder Litig., 926 A.2d 58 (Del. Ch. 2007) (4.3 percent); *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975 (Del. Ch. 2005) (3.75 percent); *In re* MONY Group, Inc. S'holder Litig., 852 A.2d 9 (Del. Ch. 2004) (3.3 percent termination fee); *In re* Pennaco Energy, Inc., S'holders Litig., 787 A.2d 691, 707 (Del. Ch. 2001) (stating that a 3 percent termination fee was "modest and reasonable"); McMillan v. Intercargo Corp., 768 A.2d 492, 505–06 n.61 (Del. Ch. 2000) (3.5 percent termination fee was within the reasonable range).

[234] OWEN, *supra* note 3, at 121.

[235] Smith v. Van Gorkom, 488 A.2d 858, 884 (Del. 1985).

[236] OWEN, *supra* note 3, at 142 (stating that the list of management participants in the KKR transaction "did not contain the names of either Van Gorkom or Chelberg. Neither Van Gorkom nor Chelberg had been asked to participate. There would be no role for them in the new company."). Owen suggests that, besides Van Gorkom's repeated insistence that he would not participate in an LBO because of the conflict of interest involved, there was another reason that he had to be excluded: so many of the other executives

Trans Union in an LBO at $60 per share (that is, $5 per share more than the Pritzker offer) but otherwise on the same terms offered by Pritzker.[237] KKR's offer contained a financing condition, but Henry Kravis represented to Van Gorkom that he was confident that financing commitments could be obtained in two to three weeks—and thus long before the February 10 deadline.[238] According to the Delaware Supreme Court, Van Gorkom's reaction to the offer was highly negative.[239] He asserted that the financing condition made the offer excessively contingent even when Romans argued that the condition was essentially the same as that in Pritzker's original offer.[240] Van Gorkom also stated that publicly announcing the KKR offer would chill other offers, even though he had previously taken the position that announcing the agreement with Pritzker would generate other offers for the company.[241]

Owen's account of this meeting and the KKR offer is broadly consistent with the Delaware Supreme Court's account, but it differs in certain important respects. First, if anything, the Delaware Supreme Court *downplayed* Van Gorkom's negative reaction to the offer. In fact, Van Gorkom told Kravis to his face that, because of the financing condition it contained, he would not dignify Kravis's letter with the term *offer*.[242] But, unnoted in the Delaware Supreme Court's account, Van Gorkom may have had significant justification for this attitude.[243] Unlike Pritzker's offer, KKR's offer was contingent not only on obtaining debt financing but also on obtaining *equity* financing as well.[244] The equity required in KKR's transaction aggregated $178 million, of which Kravis had commitments for only $153 million ($120 million from the Reichmanns, $25 million from KKR itself, and $8 million from the management participants) or 80 percent; the remaining $25 million Kravis was confident he could raise from

were so angry with him about the Pritzker transaction that they would not have participated in the KKR LBO if Van Gorkom was included. *Id.* at 143.

[237] *Van Gorkom*, 488 A.2d at 884; OWEN, *supra* note 3, at 137.

[238] *See Van Gorkom*, 488 A.2d at 884; *see also* OWEN, *supra* note 3, at 137–38.

[239] *Van Gorkom*, 488 A.2d at 884.

[240] *Id.* at 885.

[241] *Id.*

[242] OWEN, *supra* note 3, at 138.

[243] *Id.*

[244] *Id.* at 137–38.

KKR's limited partners.[245] As to the debt financing, the KKR transaction required $650 million in debt, of which Kravis had commitments in hand for only $200 million ($100 million each from Citibank and Continental Illinois, which had agreed to organize a consortium of lenders to supply the remaining $450 million).[246] Furthermore, as Van Gorkom later explained, he believed that the financing condition in the KKR offer involved more contingency than the facially similar condition in Pritzker's offer "because the Pritzker family and their various organizations constituted an existing entity with visible assets, visible wealth, visible equity, visiting borrowing power."[247] Owen casts doubt on this argument, noting that, at the time, KKR had completed larger acquisitions than the Pritzkers had, but nevertheless Van Gorkom may well have been right: in order to obtain his 14 percent financing for the merger, Pritzker had pledged all of the assets and stock of Trans Union *and also the common stock of the Marmon Group*, which of course was very valuable.[248] Presumably, KKR and its partners would be pledging only the assets and stock of Trans Union, which would naturally make obtaining financing more difficult. Even more significant was another fact never mentioned by the Delaware Supreme Court: on September 20, when the Pritzker agreement was signed, the prime rate had stood at 12.50 percent, but by December 2, the day Kravis presented KKR's offer to Van Gorkom, the prime rate had increased to 18.5 percent.[249] (Similarly, the effective federal funds rate in September of 1980 had been 10.87 percent, and by December it had increased to 18.90 percent).[250] Other things

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[245] *Id.* at 137.

[246] *Id.*

[247] Owen, *Leveraged Buyout*, *supra* note 197, at 19.

[248] OWEN, *supra* note 3, at 121.

[249] OWEN, *supra* note 3, at 128.

[250] *See Effective Federal Funds Rate,* FED. RESERVE BANK OF ST. LOUIS https://fred.stlouisfed.org/series/FEDFUNDS [https://perma.cc/JZ9S-VVNY]. The dramatic increase in interest rates resulted from the extraordinary tightening of monetary policy under Federal Reserve Chairman Paul Volcker to reduce the very high inflation rates of the final years of the Carter Administration. *See* Paul Volker, Remarks at the Alfred M. Landon Lecture Series on Public Issues at Kansas State University in Manhattan, KS: Dealing with Inflation: Obstacles and Opportunities (Apr. 15, 1981), https://fraser.stlouisfed.org /scribd/?item_id=8236&filepath=/files/docs/historical/volcker/Volcker_198104

being equal, KKR's financing was likely to be *between 600 and 800 basis points more expensive* than Pritzker's. But other things were not equal because, assuming, as seems likely, that KKR would not have been providing its lenders with collateral beyond the assets and common stock of Trans Union, KKR would very likely have had to pay a higher spread over the risk-free rate than Pritzker had. Van Gorkom understood this quite clearly, stating later that KKR's "ability at a time where interest rates were 20 percent to raise $650,000,000 was to be questioned."[251] Moreover, because Trans Union made use of large amounts of short-term debt in the ordinary course of its business, its interest expense was rising substantially as interest rates increased,[252] which would have reduced the company's ability to service the debt incurred to fund the LBO. When Romans argued to Van Gorkom that KKR's offer was no more contingent on financing than Pritzker's had been, this was not literally true with respect to equity financing and it was highly misleading with respect to debt financing.[253]

Moreover, Owen's account reveals that KKR's offer was half-baked in other important respects. In particular, as difficult as this may be to believe in a contemporary context, KKR and Romans had done very little to determine which of Trans Union's executives would participate in the buy-out group.[254] Other than Van Gorkom and Chelberg being out and Romans and another executive (Bosner) being in, KKR and Romans seemed not to have confirmed with any other executives whether they were definitely in or definitely out.[255] At his meeting with Kravis, Van

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15.pdf [https://perma.cc/X5HT-LNGB]; Paul Volker, Remarks to the National Press Club in Washington, DC: No Time for Backsliding (Sept. 25, 1981), https://fraser.stlouisfed.org/scribd/?item_id=8243&filepath=/files/docs/historical/volcker/Volcker_19810925.pdf [https://perma.cc/2ZLN-QUA6]. *See generally* ALLAN H. MELTZER, 2 A HISTORY OF THE FEDERAL RESERVE (2014).

[251] OWEN, *supra* note 3, at 139. Although it was probably unknown to Van Gorkom, in their loan commitments to KKR, Citibank and Continental Illinois had agreed to lend at a floating rate above prime, with interest above 15 percent payable at maturity. *See id.* at 137.

[252] Between 1979 and 1980, Trans Union's interest expense increased 46 percent from $90 million to $131 million. *Id.* at 200.

[253] *Id.* at 138–39.

[254] *Id.* at 142.

[255] *Id.*

Gorkom demanded to know which of his executives were involved in the deal, and the best that Kravis and Romans could do was retire to a conference room to produce a list of executives *who would be invited to participate* in the deal.[256] Van Gorkom's reaction that the proposal from KKR was less than fully definite was not entirely unreasonable.

As to what happened next, the Delaware Supreme Court and Owen's accounts diverge significantly. According to the court, soon after receiving the offer, Van Gorkom had a private conversation with Kruizenga, the head of Trans Union's critical railcar business, who the court says was a member of the buy-out group, and immediately after this conversation, Kruizenga withdrew from the KKR group.[257] Although Van Gorkom denied he had influenced Kruizenga's decision, his decision not to participate in the group led KKR to withdraw its offer before the Trans Union board could consider it.[258] According to Owen, armed with KKR's list of executives who would be invited to participate in the transaction, Van Gorkom began speaking with them one-on-one to ascertain whether they were actually going to participate in the buy-out.[259] Some told Van Gorkom that they would participate, but at least one expressed outrage that Romans would include him in such a venture.[260] When Van Gorkom got to Kruizenga, Kruizenga immediately and unequivocally told Van Gorkom that he was not participating in any buy-out.[261] This was not surprising because, as Kruizenga and Romans testified,[262] just the day

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256 *Id.*

257 Smith v. Van Gorkom, 488 A.2d 858, 885 (Del. 1985).

258 *See id.* at 885; *see also* OWEN, *supra* note 3, at 146. Owen asserts:

> Very few people in the [Trans Union] corporate office ... were willing to believe Van Gorkom's account of his encounter with Kruizenga after the KKR offer had been presented. Many seemed to think that Van Gorkom as somehow talked Kruizenga out of participating, even though Kruizenga himself said that Van Gorkom never attempted to influence his thinking on the leverage buyout one way or the other.

Id. (discussing how Kruizenga had told Romans the day before that he would not participate in the transaction).

259 OWEN, *supra* note 3, at 145.

260 *Id.* at 143.

261 *Id.* at 145–46.

262 *Id.* at 146 (stating "both Kruizenga and Romans, in recalling the matter later, gave consistent accounts: Kruizenga had already backed out the day before. 'Count me out' he had said").

before, Kruizenga had told Romans he would not participate.[263] Primarily because of the tremendous increase in interest rates, Kruizenga had concluded that an LBO of Trans Union was unlikely to make money.[264] Just how, under these circumstances, Romans could have felt confident that Kruizenga would participate in the LBO is a mystery, but he apparently did so feel.[265] In any event, after his conversation with Van Gorkom, Kruizenga told Romans and Kravis that he was not participating and would encourage his subordinates not to participate either.[266]

The Delaware Supreme Court and Owen agree that once Kravis learned that Kruizenga (and likely his lieutenants at the railcar business, who throughout acted under his guidance) was not participating, KKR withdrew the offer.[267] The majority opinion makes Kruizenga's dropping out the primary, or even sole, cause of KKR's withdrawing the offer.[268] The dissenting justices in *Van Gorkom* suggest that KKR had also encountered problems with the Reichmanns, who were providing equity financing,[269] but this seems to be a mistake.[270] Owen agrees that Kruizenga's

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[263] *Id.* at 134. At a meeting with his lieutenants the same day, Kruizenga expressed his reservations about the deal, including his worry about rising interest rates. Gerald F. Lahey, one of Kruizenga's subordinates, did not share his concerns, however, and Kruizenga approved Lahey joining Romans in further negotiations with KKR and the Reichmanns—a fact that could have led Romans to believe Kruizenga still had an open mind about participating in the LBO, regardless of what he had said to Romans about not participating. *Id.* at 134–35.

[264] *Id.* at 134.

[265] *See id.* at 147 ("In the frantic pace of activity of the preceding few days, Romans apparently misread the situation, believing that Kruizenga could be brought around notwithstanding his comments of the previous day. In fact, Romans had asked one of Kruizenga's colleagues to review with Kruizenga the events of the preceding day [which involved mostly negotiations with the Reichmanns] and make sure Kruizenga was 'on board.'").

[266] *Id.*

[267] Smith v. Van Gorkom, 488 A.2d 858, 885 (Del. 1985); OWEN, *supra* note 3, at 149.

[268] *Van Gorkom*, 488 A.2d at 896.

[269] *See id.* at 896 (McNeilly, J., dissenting) (asserting that KKR withdrew the offer for two reasons—Kruizenga's change of heart and "complications arising out of negotiations with the Reichmann family," who were also participating in the KKR group).

[270] According to Owen, all issues with the Reichmann family had been settled, and KKR's withdrawal of the offer had nothing to do with the Reichmanns.

decision not to participate was a very important factor in KKR's decision to withdraw the offer,[271] but Owen notes another factor as well: KKR had no interest in an unfriendly transaction, and Van Gorkom's reaction to the offer made it abundantly clear that Van Gorkom opposed the transaction with KKR.[272]

This raises the question of precisely why Van Gorkom was so opposed to the KKR deal. It is true that his objections about the contingent nature of the KKR offer were more serious than Romans or the Delaware Supreme Court allowed, and it was also true that, if Pritzker acquired Trans Union, Van Gorkom was expected to stay briefly till he retired, after which his heir apparent Chelberg would take over as chief executive officer, whereas if KKR acquired the company, his relationship with the company would cease.[273] The real reason, however, seems to lie elsewhere. To understand it, it is important to remember that LBOs were still a new form of transaction in 1980, that Van Gorkom had never even heard of such transactions before September of that year,[274] and that probably none of the Trans Union directors had any meaningful experience with such transactions.[275] From the beginning, perceiving the clear conflict of interest a manager participating in an LBO faces, Van Gorkom declined to participate; his attitude, loudly expressed, was that conflicts of interest should be avoided, not managed.[276] As Romans recognized

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OWEN, *supra* note 3, at 134, 147–49. In January of 1981, when Romans and Kravis attempted to reconstruct the KKR offer, they determined that they did not have sufficient time to arrange financing before the Trans Union stockholder meeting. One of the Reichmanns was involved in those discussions and took a similar view. *Id.* at 148. It seems that Justice McNeilly is conflating the causes of the withdrawal of the December 2 offer from KKR and the causes of the failure to resurrect that offer in January.

[271] *Id*. at 147–48.

[272] *Id*. at 148 (noting that "KKR has a decided antipathy for 'unfriendly deals'—a view shared with the Reichmanns," that KKR had "no desire to get the KKR name in the papers unless there was a good likelihood of the deal closing" and that "[i]t must have been clear to Kravis that Van Gorkom and Chelberg were not exactly thrilled to receive KKR's proposal.").

[273] Not surprisingly, Van Gorkom denied that such considerations affected his estimation of the KKR offer. *Id*. at 143.

[274] *Id*. at 37.

[275] *Id*.

[276] *Id*. at 37, 126.

at the time, this was very convenient for the buy-out group, because it left Van Gorkom free to negotiate on behalf of Trans Union and the stockholders against KKR and the managers participating in the buy-out.[277] In short, Van Gorkom would be on the sell-side, and Romans and Kravis would be on the buy-side.[278]

Van Gorkom, backed by the Trans Union directors, did not see things so clearly. At the October 8 board meeting, which was held to approve the amendments to the Pritzker merger agreement, the Trans Union board instructed Van Gorkom that all negotiations about a potential LBO were to be coordinated through him.[279] Amazingly, they meant by this not simply that Van Gorkom should lead the negotiations *against* any buy-out group, but that he should also participate in and supervise any effort to formulate an LBO with management participation.[280] That is, although Van Gorkom was not a participant of the buy-out group, Van Gorkom and the board thought he should be included in the meetings between the managers participating in the buy-out and KKR and their lenders and generally be kept apprised of all matters related to the formulation of the offer.[281] Van Gorkom candidly admitted that, on at least two occasions, when Romans wanted to meet with KKR, he "invited [him]self" to the meetings even though he "was not asked."[282] Although this did not in fact occur, Van Gorkom likewise wanted Trans Union's financial advisor to participate in the buy-out group's meetings.[283] On occasion, Romans gently protested that there

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[277] *Id.* at 126.

[278] *See id.* (contending that because KKR had recently acquired another company under analogous circumstances, this precedent was on Romans's mind as he worked with KKR on a bid for Trans Union).

[279] OWEN, *supra* note 3, at 103 (noting that at the meeting on October 8, 1980, "[t]he directors made it clear that they wanted all solicitations to be coordinated through Van Gorkom. And they wanted all negotiations—including any for a leveraged buy-out—to be carried on by Van Gorkom.").

[280] *See id.* at 103.

[281] *See id.* at 124.

[282] *Id.* at 125; *see also* Owen, *Leveraged Buyout*, *supra* note 197, at 18 (noting that Van Gorkom invited himself to a meeting in New York between Romans and KKR and then to a meeting with Romans, Kravis, and representatives of Continental Illinois Bank, which was considering providing financing for the management buyout).

[283] *See id.* at 124.

had to be some meetings between the managers participating in the LBO and KKR in which Van Gorkom did not participate, but this seems to have made no impression on Van Gorkom.[284] Understandably, Romans and KKR began meeting without Van Gorkom,[285] and so when Kravis presented his offer letter to Van Gorkom on December 2, Van Gorkom was genuinely surprised to get it.[286] Difficult as it may be to understand today, he seems to have had a feeling, perhaps unarticulated, that his senior managers had been sneaking around behind his back and done something vaguely underhanded.[287] This explains his primary concern on receiving the offer: he wanted to know which of his managers were involved in the scheme,[288] an issue that surely should have been of anything but minor importance. It also explains a comment Van Gorkom made to Kravis when Kravis withdrew the KKR offer. Although he assured Kravis that he thought Kravis had behaved in a professional manner, "he was concerned that he now had a real split among his managers and felt he had not been kept up-to-date."[289]

Again, this was not just some idiosyncratic view on the part of Van Gorkom; it was Trans Union's policy as formulated by its board of directors. Indeed, when Van Gorkom reported to the directors that KKR had made and then quickly withdrew an offer, one director questioned him about whether the executives involved in the potential buy-out "had kept [Van Gorkom] apprised of the matter," and Van Gorkom responded in the negative.[290] At this point, some outside directors "then reiterated that steps be taken to ensure that no future negotiations relating to any leveraged buy-out with management participation be conducted without Van Gorkom's approval and participation."[291] The unavoidable conclusion is that Van Gorkom reacted so negatively to KKR's offer because it had been prepared without his participation and thus in violation of his and the board of directors' orders.[292]

[284] *See id.* at 151.
[285] *See id.* at 147.
[286] *See id.* at 150.
[287] *See id.* at 151.
[288] *See id.*
[289] *Id.* at 149.
[290] *Id.* at 149–50.
[291] *Id.* at 150.
[292] *See id.* at 152.

Van Gorkom expressly confirmed this view the next day in a conversation with Romans. For Van Gorkom, "it was a serious concern that, in his judgment, the handling of the whole situation [with KKR] had been improper" because "the instructions that had been issued on the coordination of inquiries from various suitors had not been followed."[293] Van Gorkom expressed his displeasure to Romans, "indicating that he [Van Gorkom] had not been properly involved" in the process.[294] When Romans protested that because Van Gorkom was not participating in the LBO, KKR and the other participants could not include him in all of their discussions, Van Gorkom merely reiterated that any managers participating in the process would have a severe conflict of interest—a point that was true but obviously not responsive to Roman's objection.[295]

In any event, when Kravis withdrew the KKR offer, this did not in fact end KKR's pursuit of Trans Union.[296] Not noted by the Delaware Supreme Court, Van Gorkom and Romans agreed that they would all cool off for a while and consider whether the KKR offer could be resurrected in the new year, with Van Gorkom involved in the process in the manner he considered proper.[297] Meanwhile, on December 19, the plaintiff stockholders sued the Trans Union board alleging it had breached its fiduciary duties in approving the merger.[298] When

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[293] *Id.* at 151.

[294] *Id.*

[295] *Id.*

[296] *See id.* at 152.

[297] *Id.*

[298] *See id.* at 162. Ironically, Smith, the lead plaintiff, did not object as much to the price in the Pritzker transaction as to the form of consideration it involved—cash instead of stock. *See* Bainbridge, *supra* note 60, at 200. Smith had acquired his Trans Union stock in one of the company's many minor acquisitions, and Smith had a low tax basis in the stock. *Id.* Whereas a stock-for-stock transaction would almost certainly have been tax free to Smith, the cash deal from Pritzker triggered for Smith a significant tax liability. *Id. See generally*, William M. Owen, *A Shareholder Named Smith*, 26 DIRECTORS & BOARDS 39 (2000) (stating that about one-third of the outstanding Trans Union shares were issued in acquisitions of other companies, with the result that the original holders of those shares generally had low tax bases in such shares). As Bainbridge correctly notes, however, the business judgment rule would certainly have protected the board's decision as to the form of consideration it chose to accept. Bainbridge, *supra* note 60, at 200–01.

the new year came, GECC was still conducting due diligence, and eventually indicated it may be willing to offer $60 per share cash to acquire Trans Union.[299] Welch, then on the verge of being appointed chief executive officer at General Electric, told Van Gorkom that GECC was worried that if it made an offer to Trans Union, a bidding contest with Pritzker would result, and GECC had no interest in participating in a such contest.[300] Welch thus convinced Van Gorkom to approach Pritzker with the extraordinary request that Pritzker agree to rescind the merger agreement with Trans Union before GECC would make a bid.[301] Pritzker responded that if he agreed to this and either GECC made no offer or made an offer but never consummated a transaction, then Pritzker would have incurred significant expenses, would not be able to acquire the company, and would have nothing but his option to acquire one million shares of Trans Union common stock at $38 per share.[302] If GECC did not acquire Trans Union, the price of the Trans Union shares would likely fall back to the pre-transaction market price, thus making the option worthless and leaving Pritzker with nothing.[303] It is easy to sympathize with Pritzker when he says that this "was asking an awful lot."[304] Not surprisingly, Pritzker declined this most unusual request.[305] GECC then terminated discussion with Trans Union.[306]

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[299] *See* OWEN, *supra* note 3, at 166.

[300] *Id.* at 169.

[301] *See id.* at 172.

[302] *See id.* at 173.

[303] *See id.*

[304] *Id.*

[305] This episode is utterly bizarre. For one thing, as Van Gorkom explained to Welch, Pritzker would almost certainly *not* have overtopped a $60 per share offer from GECC, preferring instead to make $22 million on the stock option. GECC was thus being almost absurdly cautious. Furthermore, if GECC wanted assurance that Pritzker would not overtop a $60 per share offer, it need only have entered an agreement with Pritzker in which Pritzker promised not to top a $60 per share offer if GECC made one. Pritzker could well have accepted this. If GECC did not make an offer, or made an offer and it failed to close for any reason, he would still acquire the Trans Union in accordance with the terms of the merger agreement. If GECC made an offer and it succeeded, Pritzker would profit under the option. There was no need to rescind the Pritzker–Trans Union agreement to ensure that Pritzker not make an offer topping any offer from GECC.

[306] OWEN, *supra* note 3, at 178.

On January 16, 1981, when an offer from GECC had begun to appear unlikely, Van Gorkom authorized Romans to attempt to resurrect the KKR offer. Romans quickly got in touch with Kravis, and the two men attempted to put together another offer for Trans Union.[307] A flurry of meetings, this time including Van Gorkom, followed. On January 21, Trans Union mailed its proxy statement to the Trans Union stockholders in anticipation of the scheduled February 10 stockholders meeting.[308] On January 26, with the prime rate then at over 20 percent[309] and the effective federal funds rate at 19.08 percent,[310] Kravis and the Reichmann family concluded that they did not have enough time to arrange the financing for the transaction, and Kravis so informed both Van Gorkom and Romans.[311] Had they had a few more weeks to arrange financing, however, both Kravis and the Reichmanns believed they could have made an offer to acquire Trans Union at $60 per share.[312] Apparently, Kruizenga's decision not to participate in the KKR transaction turned out to be irrelevant, for, true to his word, he was not participating in the effort to reconstruct the offer.[313]

Later on January 26, the Trans Union board met, reconsidered the entire sequences of events related to the Pritzker transaction, and resolved to send the stockholders a supplement to the proxy statement, in part in response to disclosure claims that had been raised by the plaintiffs in the litigation challenging the merger.[314] On February 3, Chancellor Marvel of the Court of Chancery declined to issue a preliminary injunction enjoining the merger.[315] On February 10, the Trans Union stockholders

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[307] *See id.* at 177.

[308] *See id.* at 177–78.

[309] *See id.* at 180, 182.

[310] *See Effective Federal Funds Rate,* FED. RESERVE BANK OF ST. LOUIS https://fred.stlouisfed.org/series/FEDFUNDS [https://perma.cc/JZ9S-VVNY].

[311] *See* OWEN, *supra* note 3, at 182.

[312] *See id.* at 172, 182.

[313] *See id.* at 182–83.

[314] *See* Smith v. Van Gorkom, 488 A.2d 858, 864 (Del. 1985); OWEN*, supra* note 3, at 184.

[315] Smith v. Pritzker, No. 6342, 1981 WL 15145, at *5 (Del. Ch. Feb. 3, 1981). This was actually the most fateful decision in the case. If Chancellor Marvel had enjoined the merger, all of the issues would have been resolved pre-closing, and the key issue of personal liability in damages on the part of the directors would never have arisen.

met, and with the board still recommending that they approve the merger, they voted to do so, with 69.9 percent of the shares entitled to vote voting in favor, 7.25 percent against, and 22.85 percent not voting.[316] No Trans Union stockholder sought appraisal of his shares.[317]

After the merger, the plaintiffs amended their complaint to request rescission of the merger and, in the alternative, monetary damages.[318] After the trial in the Court of Chancery, on July 5, 1982, Chancellor Marvel delivered his opinion on the merits and found for the defendants on all counts.[319] The plaintiffs appealed, but aside from the litigants and their counsel, almost no one gave the case another thought.[320]

B. *The Delaware Supreme Court's Opinion and the Reaction Thereto*

This section (1) briefly summarizes the Delaware Supreme Court's disposition of the case, and then (2) discusses the reaction to the court's opinion.[321]

1. *The Delaware Supreme Court's Opinion*

The proceedings in the Delaware Supreme Court were surprisingly protracted. The court first heard oral arguments on February 24, 1983, and the court then ordered reargument on May 16, 1983, and again on June 11, 1984.[322] More than six months later, on January 29, 1985, the Delaware Supreme Court issued its opinion in the case then denominated *Smith v. Van Gorkom*.[323]

The Court was bitterly divided, three to two,[324] an unusual circumstance for the Delaware Supreme Court in a corporate

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[316] *See* OWEN, *supra* note 3, at 192–93.
[317] *Id.* at 194.
[318] *See id.*
[319] *Pritzker*, 1981 WL 15145, at *5.
[320] *See* OWEN, *supra* note 3, at 195.
[321] *See infra* Section I.B.1.
[322] OWEN, *supra* note 3, at 257.
[323] Jay Pritzker and the other non-director defendants had been dismissed from the case, thus resulting in the action being retitled. *See* Smith v. Van Gorkom, 488 A.2d 858, 863–64 (Del. 1985).
[324] OWEN, *supra* note 3, at 255.

case,[325] and not surprisingly, for the majority's holding was truly extraordinary. As every corporate lawyer knows, the majority reversed the Court of Chancery on virtually every issue in the case.[326] The court held that the Trans Union directors breached their fiduciary duty of care, first "by their failure to inform themselves of all information reasonably available to them and relevant to their decision to recommend the Pritzker merger" and second "by their failure to disclose all material information such as a reasonable stockholder would consider important in deciding whether to approve the Pritzker offer."[327] The court remanded the case to the Court of Chancery to compute damages, instructing it "to determine the fair value of the shares ... based on the intrinsic value of Trans Union on September 20, 1980" in accordance with *Weinberger v. UOP* and to enter judgment for the plaintiffs to the extent that the fair value of Trans Union exceeded the $55 per share deal price.[328] Since KKR was apparently willing to pay $750 million for the company and the price in the Pritzker deal aggregated $690 million, the damages owed by the ten individuals who had served on the Trans Union board could easily have exceeded $60 million.[329]

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[325] *Id.*

[326] *See id.* at 256 (stating "[a]s if to tell the directors not to bother to ask for a further hearing on the case, the Court overturned almost every major factual determination made by Chancellor Marvel of the Delaware Chancery Court").

[327] *Van Gorkom*, 488 A.2d at 893.

[328] *Id.*

[329] OWEN, *supra* note 3, at 261. On July 30, 1985, the case—and a related stockholder suit in federal court in Illinois—settled for $23.5 million. According to Owen, of this amount, Trans Union's D&O insurance carrier paid $10 million, the individual defendants paid $1.5 million, and the Pritzkers, even though they were no longer defendants in the case, contributed the balance. OWEN, *supra* note 3, at 319. According to Bainbridge, however, the Pritzkers paid everything over the amount covered by insurance subject only to a requirement that the defendant directors make small contributions to charity. Bainbridge, *supra* note 60, at 225. Bainbridge speculates that the Pritzkers were willing to pay even when they were not legally required to do so because, as serial acquirers, they had an interest in proving to directors at potential targets that they would be held harmless if they sold their companies to the Pritzkers. Owen, however, has suggested to me in private conversation a simpler and more plausible explanation: the parties may have believed that Trans Union, by then a subsidiary of Marmon, was required to indemnify the former Trans Union directors.

2. The Furious Reaction

The reaction was explosive.[330] *The Wall Street Journal* story, which stated that corporate directors considering takeovers "might be under increased pressure" because of the decision, was extremely restrained in comparison to most other reactions in the legal and financial press.[331] More typical was *Business Week*, which said that the decision "shocked the corporate world" and was "a landmark ruling that puts board members in peril."[332] The case "sent shock waves through the corporate bar,"[333] and "reverberated mightily through the boardrooms of Corporate America."[334] Chicago practitioner Leo Herzel said that the court's decision "seems to reflect nothing but the court's need to force haphazardly chosen defendants to repent for the State of Delaware's pro-business ways."[335] *Barron's* said the court had "hurled a thunderbolt into the nation's boardrooms."[336] Bayless Manning reported that "the corporate bar generally views the decisions as atrocious," and he concluded that the court "had exploded a bomb."[337] Daniel Fischel wrote that *Van Gorkom* was "one of the worst decisions in the history of corporate law."[338] Former Justice and former Chancellor Quillen demurely hoped that the case would have "little lasting legal significance" because its holdings

[330] *See* Barry F. Schwartz & James G. Wiles, Trans Union*: Neither 'New' Law nor 'Bad' Law*, 10 DEL. J. CORP. L. 429 (1985) [hereinafter Schwartz & Wiles] (saying that "the condemnations appear to be virtually unanimous," though Schwartz and Wiles themselves defended the decision).

[331] Richard Koenig, *Court Rules Trans Union's Directors Used Poor Judgment in Sale of Firm*, WALL ST. J., Feb. 1, 1985, at 7.

[332] OWEN, *supra* note 3, at 257.

[333] Dierdre A. Burgman & Paul N. Cox, *Corporate Directors, Corporate Realities and Deliberative Process: An Analysis of the* Trans Union *Case*, 11 J. CORP. L. 311, 312 (1986).

[334] *Roundtable*, *supra* note 23, at 28 (2000).

[335] Leo Herzel, Scott J. Davis & Dale Colling, *"Smith" Brings Whip Down on Directors' Backs*, LEGAL TIMES, May 13, 1985, at 14 [hereinafter Herzel et al.].

[336] Richard M. Leisner, *Boardroom Jitters: A Landmark Court Decision Upsets Corporate Directors*, BARRON'S NAT'L BUS. & FIN. WKLY, Apr. 22, 1985, at 34; *see* Herzel et al., *supra* note 335.

[337] Manning, *supra* note 23, at 1.

[338] Daniel R. Fischel, *The Business Judgment Rule and the* Trans Union *Case*, 40 BUS. LAW. 1437, 1455 (1985).

would be confined to its unusual facts,[339] but because of what he argued was the unprincipled nature of much the court's reasoning, "fear resulted that the court was on an undisciplined frolic of its own."[340] Ira Milstein later summed up the reaction by saying that almost everyone who wrote about the decision thought "the Delaware courts are going nuts."[341] Van Gorkom himself published a response to the decision in which he said the Delaware Supreme Court "showed a serious lack of understanding of even the basic functioning of the business and financial worlds."[342] Martin Lipton captured the essence of the corporate bar's objection to *Van Gorkom* when he lamented in a memorandum to clients that "[i]t made no difference that there were no allegations of fraud, bad faith or self-dealing" by the Trans Union directors.[343] Directors of Delaware corporations were now exposed to potential liability for enormous sums far exceeding their personal net worth merely for breaches of a duty of care.[344]

Within months of the Supreme Court's decision in *Van Gorkom*, the directors' and officers' liability insurance market

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339 Quillen, *supra* note 28, at 466.

340 *Id.* at 476. The sense of shock created by the decision has endured. In 1988, Macey and Miller said the case "appears to depart dramatically from prior law" and "apparently displays a mysterious anti-management bias." Macey & Miller, *supra* note 23, at 129. "The outcome of the case was exactly the opposite to what virtually every observer of Delaware law would have predicted." *Id.* at 131. In 2002, McChesney said of the case, "[c]onsidered a legal disaster in 1985, it is judged no less disastrous today." Fred S. McChesney, *A Bird in the Hand and Liability in the Bush: Why* Van Gorkom *Still Rankles, Probably*, 96 NW. U.L. REV. 631, 631 (2002). "If sheer wrongheadedness of result were disqualifying, *Van Gorkom* would not be worth reading." *Id.* In 2009, Stephen M. Bainbridge said the case was "arguably one of the most surprising decisions ever issued by the Delaware Supreme Court" and "continues" to "generat[e] great controversy." Bainbridge, *supra* note 60, at 197–98.

341 *Roundtable*, *supra* note 23, at 32.

342 Van Gorkom, *supra* note 145, at 17.

343 Koenig, *supra* note 331, at 7; *see also* Martin Lipton & Andrew R. Brownstein, *Takeover Responses and Directors' Responsibilities—An Update*, 40 BUS. LAW. 1403, 1410 (1985).

344 *See id*; *see also* Macey & Miller, *supra* note 23, at 132 (stating that the case had "imposed unforeseeable and devastating economic penalties on a corporate board"); Macey, *supra* note 57, at 608 (referring to "the debilitating threat of financial ruin from personal liability").

was collapsing. Insurers were sharply increasing premiums and deductibles, refusing to renew policies, and in some cases exiting the market entirely.[345] Although some have questioned how significant a cause *Van Gorkom* was of the crisis in the D&O market,[346] the sharp decline in the availability of such coverage coupled with the prospect of potentially catastrophic personal liability under *Van Gorkom* led corporate directors to demand increased protection from personal liability.[347]

As a result, the Corporation Law Section of the Delaware Bar Association considered several proposals to amend the Delaware General Corporation Law (DGCL). Based on analogies to the law of trusts, some Delaware practitioners argued that an appropriate provision in the corporation's certificate of incorporation could limit or eliminate personal liability for the directors for breaches of their duty of care. Other practitioners questioned whether such a policy would run afoul of the DGCL and thus be unenforceable.[348] Ultimately, on July 1, 1986, the Delaware General Assembly

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[345] *See* Mansfield, *supra* note 60, at 228 n.87; Bradley & Schipani, *supra* note 60, at 50–51 (stating that D&O insurance premiums increased more than tenfold between 1984 and 1986); Bainbridge, *supra* note 60, at 202–03 (referring to the "perception that the decision had significantly increased director liability exposure drove dramatic changes in the director and officer … liability insurance market"); Veasey et al., *supra* note 60, at 400–01 (discussing how some D&O carriers withdrew from the market or raised premiums and deductibles as a result of *Van Gorkom*); Allen, Jacobs & Strine, *supra* note 31, at 458 n.36 (stating that "after *Van Gorkom*, the D & O insurance industry sharply increased their premiums and in some cases, threatened to stop writing D & O insurance policies. This crisis required a legislative solution," which took the form of Section 102(b)(7)); Edward Rock & Michael Wachter, *Dangerous Liaisons: Corporate Law, Trust Law, and Interdoctrinal Legal Transplants*, 96 NW. U.L. REV. 651, 659 (2002) (stating, "[i]n the wake of *Smith v. Van Gorkom*, a directors and officers … liability insurance crisis was triggered. Policies were not renewed, premiums skyrocketed, and firms worried about being able to recruit high quality directors").

[346] *See* R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, DEL. LAW OF CORPS & BUS. ORGS. 4-99–100 (3d ed. 1998); Charles J. Hartman & Pamela Gayle Rogers, *The Influence of* Smith v. Van Gorkom *on Director's and Officer's Liability*, 58 J. RISK & INS. 525 (1991) (arguing that many predictions of dire consequences flowing from *Van Gorkom* were exaggerated).

[347] BALOTTI & FINKELSTEIN, *supra* note 346, at 99–100.

[348] *Id.*

enacted what is now Section 102(b)(7) of the DGCL,[349] which provides that a Delaware corporation's certificate of incorporation may include a provision eliminating the personal liability of directors for monetary damages for breaches of their fiduciary duties, other than for breaches of loyalty, for acts or omissions not in good faith or involving intentional misconduct or knowing violation of law, for willful or negligent conduct in paying dividends or repurchasing stock out of other than lawfully available funds, or for any transaction from which the director derives an improper personal benefit.[350] That is, Section 102(b)(7) allows corporations to eliminate the directors' personal liability in monetary damages for breaches of the duty of care.[351]

Soon after its enactment, virtually every public company in the United States incorporated in Delaware proposed that its stockholders amend the corporation's charter to add a provision of the kind authorized by Section 102(b)(7), and these proposals passed virtually unanimously.[352] Nowadays, virtually every public company incorporated in Delaware has such a provision in its charter.[353]

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[349] 65 Del. Laws 289 (1986) http://delcode.delaware.gov/sessionlaws/ga133/chp289.shtml [https://perma.cc/47Z7-JQYS].

[350] DEL. CODE ANN. tit. 8, § 102(b)(7) (West 2015). Other states quickly enacted similar provisions. *See, e.g.*, Deborah A. DeMott, *Limiting Directors' Liability*, 66 WASH. U. L.Q. 295, 301 (1988).

[351] *See* R. Franklin Balotti & Mark J. Gentile, *Elimination or Limitation of Director Liability for Delaware Corporations*, 12 DEL. J. CORP. L. 5, 11 (1987); Thomas C. Lee, Note, *Limiting Corporate Directors' Liability: Delaware Section 102(b)(7) and the Erosion of the Directors' Duty of Care*, 136 U. PA. L. REV. 239, 241 (1987).

[352] Hamermesh, *supra* note 23, at 490; *see also Roundtable*, *supra* note 23, at 35 (John C. Wilcox stating that "there was a flurry of management proposals seeking [stock]holder approval for indemnification of directors" and although "there was some question about whether institutional investors would approve these," in the event "they approved them wholesale" because personal liability "would drive people out of the boardroom").

[353] *See* Hamermesh, *supra* note 23, at 490 (reporting that of 100 Fortune 500 companies sampled, each of 98 stock corporations in the sample incorporated in a jurisdiction allowing exculpatory charter provisions had such provisions, including all Delaware corporations in the sample); *see also* Bainbridge, *supra* note 60, at 198 (describing Section 102(b)(7) provisions as "now nearly universal").

Under current law, if a stockholder plaintiff seeking only monetary damages and not some form of equitable relief pleads only a duty of care claim against a director of a corporation with a Section 102(b)(7) provision in its certificate of incorporation, the director can immediately dismiss the suit on the basis of the provision.[354] Indeed,

> a plaintiff seeking only monetary damages must plead non-exculpated claims against a director who is protected by an exculpatory charter provision to survive a motion to dismiss, regardless of the underlying standard of review for the board's conduct—whether it be *Revlon*, *Unocal*, the entire fairness standard, or the business judgment rule.[355]

Hence, when the directors are protected by an exculpatory charter provision and the plaintiffs do not plead non-exculpated claims against them, the "directors are entitled to have those claims against them dismissed."[356] Section 102(b)(7) did not, technically speaking, overrule *Van Gorkom*, but, for many purposes, it may as well have.[357]

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[354] Malpiede v. Townson, 780 A.2d 1075, 1079 (Del. 2001). This was not always so clear. In *Emerald Partners v. Berlin*, No. 9700, 1994 WL48993 (Del. Ch. 1994), the Delaware Supreme Court held that exculpation under Section 102(b)(7) was an affirmative defense, which apparently required the defendant directors to prove that they had not been guilty of an unexculpated breach before they could obtain dismissal of the suit—a result that would have greatly diminished the value to directors of a Section 102(b)(7) provision. *See* Allen, Jacobs & Strine, *supra* note 31, at 463 (arguing that a Section 102(b)(7) provision should be construed as providing a form of immunity and not as an affirmative defense). *Malpiede* quickly corrected this misstep in *Emerald Partners*. *Malpiede*, 780 A.2d at 1079; *see also In re* Cornerstone Therapeutics Inc. Stockholder Litigation, 115 A.3d 1173, 1179–80 (Del. 2015) (holding that, even when the standard of review is entire fairness, independent directors protected by a Section 102(b)(7) provision are entitled to be dismissed from the suit unless the plaintiff pleads against them personally unexculpated breaches of fiduciary duty).

[355] *In re* Cornerstone Therapeutics Inc. Stockholder Litig., 115 A.3d 1173, 1175–76 (Del. 2015).

[356] *Id.* at 1176.

[357] This is one of the main points made in Hamermesh, *supra* note 23. By contrast, Prickett, counsel to the plaintiffs in the case, had predicted that "the *Trans Union* opinion will for years be a judicial beacon, or a legal lighthouse, constantly reminding Delaware directors" of their duties. William Prickett, *An Explanation of* Trans Union *to 'Henny Penny' and her Friends*, 10 DEL. J. CORP. L. 451, 463 (1985).

C. *The Trans Union Board Goes to* Revlon*-Land Before* Revlon*-Land Exists*

Consider how a case with the facts of *Smith v. Van Gorkom* would turn out under current law. By comparing what the Delaware Supreme Court actually said in *Van Gorkom* to what a Delaware court would say today, we can see what the court in *Van Gorkom* got right, what it got wrong, and how its various mistakes mattered—or did not matter—for the development of Delaware corporate law. As will become quickly apparent, under current law, *Van Gorkom* would be a *Revlon* case, and any Delaware court considering the case at the preliminary injunction phase would almost certainly conclude that the Trans Union directors had breached their *Revlon* duties. Given that at least two other bidders (GECC and KKR) were still pursuing Trans Union at the time, and given especially that the board and the chief executive officer were refusing to negotiate with one of them (KKR), the court would almost certainly issue a preliminary injunction to allow a free and fair sales process for the company involving all the interested bidders. At the very least, the court would have required Trans Union to negotiate with KKR and the management group on reasonable terms. Reconsidering *Van Gorkom* as a *Revlon* case also allows us to use the legal distinctions and doctrines that the Delaware courts have developed in the thirty years since *Van Gorkom* to analyze the facts in the case in ways that justices of the Delaware Supreme Court could not have done in 1985. This clarifies a great many issues, including the true nature of some of the quarrels between the majority and the dissent and real reasons that so many practitioners and scholars have found the reasoning in *Van Gorkom* so unpersuasive.

1. *The Trans Union Board's* Revlon *Duties Were Triggered*

Van Gorkom was a *Revlon* case before there was a *Revlon*. Under *Revlon* as interpreted by *Paramount v. QVC*, when the board of directors of a Delaware corporation initiates a sales process involving a change of control of the corporation,[358] its duty changes from the preservation of the corporate entity to the maximization of the value of the company at a sale for the stockholders' benefit.[359] No longer "defenders of the corporate bastion," the directors become "auctioneers charged with getting the best price for the stockholders."[360] In the jargon of M&A lawyers, the board's *Revlon* duties are triggered, or, even more colloquially, the board enters *Revlon*-Land. This means that the board is required to take reasonable steps to get the best price for the stockholders reasonably available.[361]

The paradigm case of a transaction that triggers the board's *Revlon* duties is a cash-out merger, for in such a transaction control passes from a fluid aggregation of stockholders in the market to a single person, the acquirer.[362] Since in the transaction with Pritzker the Trans Union stockholders would receive cash for their shares, there is no doubt that, under contemporary law, the *Revlon* duties of the Trans Union directors would have been triggered. Indeed, when the Delaware Supreme Court held the Trans Union directors to a new and higher standard of fiduciary conduct in selling their company,[363] the Trans Union directors in effect became the first corporate directors in history ever to reach *Revlon*-Land.[364] To be sure, it was done inadvertently, but by initiating the cash sale of Trans Union to Jay Pritzker, Jerome W. Van Gorkom and the Trans Union directors were to boldly go where no director had gone before.

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[358] Paramount Commc'n Inc. v. QVC Network Inc., 637 A.2d 34, 36 (Del. 1993); *see also In re* Smurfit-Stone Container Corp. S'holder Litig., No. 6164-VCP, 2010 WL 2403793, at *10–12 (May 20, 2011) (holding that a sale in which 50 percent of the merger consideration was cash and 50 percent was stock in a non-controlled public company triggered the target board's *Revlon* duties).

[359] Revlon Inc. v. MacAndrews & Forbes Holdings, 506 A.2d 173, 182 (Del. 1985).

[360] *Id.* at 182.

[361] *QVC*, 637 A.2d at 51. *See generally* J. Travis Laster, Revlon *is a Standard of Review: Why It's True and Why It Matters*, 19 FORDHAM J. CORP. & FIN. L. 5 (2013); Stephen M. Bainbridge, *The Geography of* Revlon-*Land*, 81 FORDHAM L. REV. 3277 (2013).

[362] A board's *Revlon* duties are also triggered when the selling stockholders receive for their shares the shares of a corporation with a controlling stockholder. *Revlon*, 506 A.2d at 182.

[363] Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985).

[364] *Id.*

2. *The* Van Gorkom *Duty of Care vs.* Revlon *Duties*[365]

a. *The Origin of the* Van Gorkom *Duty of Care in* Aronson v. Lewis

As Lipton emphasized in his client memorandum, nowhere in the *Van Gorkom* opinion did the Delaware Supreme Court suggest that the Trans Union directors breached their duty of loyalty or acted otherwise than in good faith.[366] In fact, the court had expressly said that "there were no allegations of fraud, bad faith, or self-dealing, or proof thereof."[367] That is, the court proceeded on the assumption—indeed there was not the slightest evidence to the contrary—that all of the Trans Union directors were free from conflicts of interest involving the transaction with Pritkzer[368] and honestly believed that the actions they were taking were in the best interests of the corporation and its stockholders. Holding the Trans Union directors liable, however, required that there be a duty that they had violated, and the Delaware Supreme Court found such a duty in the duty of care: a duty of directors to inform themselves of all the material information reasonably available before making a business decision.[369]

This duty of care is now thoroughly familiar to directors, practitioners, and scholars, but it was a new thing—a very new thing—in 1985. It is true that, outside of Delaware, courts had often spoken in terms of directors being required to use the degree of care that persons of common prudence ordinarily exercise in their own affairs.[370] Likewise, Moravetz had said in 1886 that

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[365] For a somewhat different account of the origin of the duty of care, see the very illuminating article by Rock & Wachter, *supra* note 60 (tracing the history of the duty of care from its origins in trust law through *Aronson* and *Van Gorkom*); *see also* Henry Ridgley Horsey, *The Duty of Care Component of the Delaware Business Judgment Rule*, 19 DEL. J. CORP. L. 971, 974 (1994).

[366] *See generally Van Gorkom*, 488 A.2d at 872.

[367] *Id.* at 873.

[368] Aronson v. Lewis, 473 A.2d 805, 818 (Del. 1984); Orman v. Cullman, 794 A.2d 5, 26 (Del. Ch. 2002).

[369] *Van Gorkom*, 488 A.2d at 872.

[370] *E.g.*, Hun v. Cary, 82 N.Y. 65, 65 (1880) (directors of a bank are "bound to exercise care and prudence in the execution of their trust, in the same degree that men of common prudence ordinarily exercise in their own affairs"); *see also* Horsey, *supra* note 365, at 974. *See generally* Rock & Wachter, *supra*

directors "are required to be diligent and careful in performing the duties which they have undertaken," with the result that "if they commit an error of judgment though mere recklessness or want of ordinary prudence and skill, the corporation may hold them responsible for the consequences."[371] Nevertheless, as Allen, Jacobs, and Strine have said, before *Van Gorkom* the Delaware courts were averse to reviewing director action for any purpose other than remedying breaches of the duty of loyalty.[372] Indeed, before *Van Gorkom*, Delaware directors had never been held liable for a breach of the duty of care not also involving a breach of the duty of loyalty.[373]

In *Van Gorkom*, however, the Supreme Court held that the "determination of whether a business judgment is an informed one turns on whether the directors have informed themselves 'prior to making a business decision, of all material information

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note 60, at 651 (tracing the history of the duty of care from its origins in trust law through *Aronson* and *Van Gorkom*).

[371] VICTOR MORAVETZ, A TREATISE ON PRIVATE CORPORATIONS § 554 (2d ed. 1886); *see also* HENRY W. BALLANTINE, BALLANTINE ON CORPORATIONS 157 (1946) (stating "[directors'] liability is not limited to willful dishonesty and mismanagement; it extends also to negligence, which may consist in mere failure to act."). I am indebted to Harwell Wells for the reference to Ballantine.

[372] Allen, Jacobs & Strine, *supra* note 31, at 450.

[373] Rock & Wachter, *supra* note 340, at 651 (stating "[n]ever before [*Van Gorkom*] had Delaware directors been held liable for a breach of the duty of care absent a breach of the duty of loyalty, at least outside the context of financial institutions"); *see also* Fischel, *supra* note 338, at 1444 (stating that, before *Van Gorkom*, "the business judgment rule ha[d] traditionally precluded judicial review of the merits of business decisions not involving conflicts of interest, including the decision of how much information to acquire"); Joy v. North, 692 F.2d 880, 888 (2d Cir. 1982), where Judge Winter writes that "although it is often stated that corporate directors … will be liable for negligence in carrying out their corporate duties, all seem to agree that such a statement is misleading" because "the fact is that liability is rarely imposed upon corporate directors … simply for bad judgment." Probably the best way to make sense of the pre–*Van Gorkom* law is to say that, while the standard of conduct for directors involved a duty of care, the standard of review applied by courts in applying the business judgment rule did not. *See generally* Melvin Aron Eisenberg, *The Divergence of Standards of Conduct and Standards of Review in Corporate Law*, 62 FORDHAM L. REV. 437 (1993). If so, one way to understand what went wrong in *Van Gorkom* was that the Delaware Supreme Court took for a standard of review what was merely a standard of conduct.

reasonably available to them.'"[374] Here, the court was quoting from its own opinion in *Aronson v. Lewis,* which it had issued on March 1, 1984—that is, more than three years *after* the Trans Union merger had closed in February of 1981, more than eighteen months after the final decision of the Chancery Court on the merits in 1982 that the Supreme Court was reviewing, more than a year after the first set of oral arguments in the Supreme Court in early 1983, and almost a year after the second set of oral arguments in the Supreme Court in mid-1983.[375] Not only could the Trans Union directors not have known of this duty of care in 1980 and 1981, but even the lawyers arguing the case in the Supreme Court in 1983 could not have known of it. *Smith v. Van Gorkom* was certainly the first time that a Delaware court had held directors liable for damages for a supposed breach of their duty of care.[376]

In *Aronson*, the question before the Supreme Court was when, in a stockholder derivative suit, a stockholder's demand that the board of directors redress an alleged wrong to the corporation would be excused as futile.[377] Since the answer to that question involved the business judgment rule,[378] the Court restated its business judgment doctrine. In so doing, it first stated that, to

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[374] *Van Gorkom*, 488 A.2d at 872.

[375] Aronson v. Lewis, 473 A.2d 805, 805; OWEN, *supra* note 3, at 192–93 (noting that the merger closed on February 10, 1981); Smith v. Pritzker, 1981 WL 15145, at *5 (Del. Ch. Feb. 3, 1981) (showing Chancellor Marvel delivered his opinion on July 5, 1982); OWEN, *supra* note 3, at 257 (noting the first set of oral arguments occurred on February 24, 1983 and the second on May 16, 1983). However, *Aronson* was decided a few months *before* the third set of oral arguments the Supreme Court ordered in *Van Gorkom*. OWEN, *supra* note 3, at 257 (noting the date of the third set of oral arguments as June 11, 1984).

[376] *See, e.g.*, Rock & Wachter, *supra* note 60, at 672.

[377] *Aronson*, 473 A.2d at 813–14 (stating that "the *Zapata* demand-excused/demand-refused bifurcation, has left a crucial issue unanswered: when is demand futile and, therefore, excused?").

[378] *See id.* at 814–15. *Aronson* held,

> in determining demand futility the Court of Chancery in the proper exercise of its discretion must decide whether, under the particularized facts alleged, a reasonable doubt is created that: (1) the directors are disinterested and independent and (2) the challenged transaction was otherwise the product of a valid exercise of business judgment.

Id. at 814.

enjoy the protection of the business judgment rule, directors must be both disinterested in the transaction[379] and independent.[380] This part of the court's opinion was unremarkable. Next, however, the Court said that "to invoke the rule's protection directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them"—the language it would figure so prominently in *Van Gorkom* less than a year later.[381] The court cited no authority for this proposition, and indeed it could not do so, for none existed. The duty the Trans Union directors would later be found to have violated came to be for all practical purposes in *Aronson* in 1984, more than three years after the Pritzker–Trans Union merger closed in early 1981.

Albeit inadvertently, the court's discussion of the duty of care in *Aronson* makes clear what an innovation that duty was.[382] Immediately after stating that, prior to making a business decision, directors have a duty to inform themselves of all

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[379] The director may not appear on both sides of the transaction and may not derive any personal financial benefit from the transaction not devolving on stockholders generally. *Id.* at 812.

[380] The director may not be dominated or controlled by another party (such as a controlling stockholder) and the director's decision must be based on the corporate merits of the subject before the board rather than extraneous considerations. *See id.* at 815–16.

[381] *Id.* at 812. The next sentence in the court's opinion reads, "Having become so informed, [the directors] must then act with requisite care in the discharge of their duties." *Id.* This part of the *Aronson* holding, not mentioned in *Van Gorkom*, seems to involve a duty beyond merely being informed, perhaps a duty to deliberate about all the material information reasonably available in a way that meets some standard of care—presumably, gross negligence—before deciding. The Supreme Court's criticisms of aspects of the Trans Union board's decision-making process, beyond mere failures to have information, suggest some support for this interpretation. *See* Smith v. Van Gorkom, 488 A.2d 858, 869 (Del. 1985). Nevertheless, the majority's insistence in *Van Gorkom* that the breaches by the Trans Union directors all involved merely a failure to be informed seems to have prevented any significant development of this idea, much less any development of a more *Revlon*-like review of the substantive reasonability of the board's decisions. Of course, the law is clear today that, except under *Revlon* or some other enhanced standard of review, the duty of care involves care only in the process of decision-making, not its substance. *See In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 74 (Del. 2006).

[382] *Aronson*, 473 A.2d at 812.

material information reasonably available, the court explains this duty, stating, "[w]hile the Delaware cases use a variety of terms to describe the applicable standard of care, our analysis satisfies us that under the business judgment rule director liability is predicated upon concepts of gross negligence."[383] To this proposition, the court attaches a footnote, saying, "[w]hile Delaware cases have not been precise in articulating the standard by which the exercise of business judgment is governed, a long line of Delaware cases holds that director liability is predicated on a standard which is less exacting than simple negligence."[384] This is misleading in two ways. First, it distracts from the important and new holding—that there was a *duty of care* at all, regardless of what the standard of care may be. That critical point gets passed over in silence; the shift from the existence of the duty to its exact content was prestidigitation.

Second, in turning to the whether the standard of care should be simple negligence or some less exacting standard such as gross negligence, the court gets things exactly backwards. What was new and surprising about a duty to be informed before making a business decision was that there was a duty at all—that is, that there was a basis for liability *less than* dishonesty, fraud, self-dealing or conflicts of interest. In its *Aronson* opinion, the Delaware Supreme Court speaks as if the court is, if anything, *constricting* the duties of directors by holding them merely to a gross negligence standard. In fact, the court was greatly *expanding* directors' duties by imposing on them a duty involving a standard *less* than the traditional one of dishonesty, fraud, self-dealing, or conflicts of interest.[385]

The "long line of Delaware cases" holding "that director liability is predicated on a standard which is less exacting than simple negligence" to which the court refers confirms this. [386]

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[383] *Id.*

[384] *Id.* at 812 n.6. (listing Sinclair Oil Corp. v. Levien, 280 A.2d 717, 723 (Del. 1971); Getty Oil Co. v. Skelly Oil Co., 267 A.2d 883, 886 (Del. 1969); Warshaw v. Calhoun, 221 A.2d 487, 492 (Del. 1966); Moskowitz v. Bantrell, 190 A.2d 749, 750 (Del. 1963); Penn Mart Realty Co. v. Becker, 298 A.2d 349, 352 (Del. Ch. 1972); Kors v. Carey, 158 A.2d 136, 140–41 (Del. Ch. 1960); Allaun v. Consolidated Oil Co., 147 A. 257, 260 (Del. Ch. 1929)).

[385] *Aronson*, 473 A.2d at 817.

[386] *Id.* at 812 n.6.

None of these cases held directors liable for breaching a duty of care. None of them even refers to a duty of care. In not one of them does the word "informed" even appear. The *Aronson* opinion makes it sound as if these were duty of care cases that held that the duty of care involves a gross negligence rather than a simple negligence standard. In fact, most were cases based on allegations of director (or controlling stockholder) misconduct involving fraud, dishonesty, self-dealing or other conflicts of interest.[387] The rest challenged the substantive merits of a business decision.[388] None involved even allegations that the directors had not been sufficiently informed before making a business decision.

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387 *See* Sinclair Oil Corp. v. Levien, 280 A.2d 717, 723 (Del. 1971) (challenging transactions between a controlled subsidiary and the controlling parent); Getty Oil Co. v. Skelly Oil Co., 267 A.2d 883, 886 (Del. 1969) (action for declarative judgment by controlling stockholder regarding its duties to controlled corporation); Warshaw v. Calhoun, 221 A.2d 487, 492 (Del. 1966) (challenging transactions taken by directors who were also directors of controlling stockholder alleging that transactions between the corporation and a third party benefited the controlling stockholder at the expense of the minority); Kors v. Carey, 158 A.2d 136, 140–41 (Del. Ch. 1960) (challenging the board's decision to use corporate funds to reacquire a block of the corporation's shares from a large stockholder and alleging that the directors undertook the transaction to benefit and entrench themselves).

388 *See* Moskowitz v. Bantrell, 190 A.2d 749, 750 (Del. 1963) (challenging on the merits the board's decision not to pay higher dividends, but not alleging that the board was uninformed). The court dismissed the complaint because the plaintiff "failed to show any oppressive or fraudulent abuse of discretion." *Id.* at 751; *see also* Penn Mart Realty Co. v. Becker, 298 A.2d 349, 350 (Del. 1972) (challenging the directors' decision to sell stock owned by the corporation at the market price when they knew that they would soon cause the corporation to purchase shares of the same class of stock at a higher price). Of all the cases the *Aronson* court cites, *Penn Mart Realty* comes closest to recognizing a duty of care. Such recognition as exists in the case, however, is limited to the unexplained observation that, in refusing to dismiss the complaint, the court said, "[f]raud and self-dealing are not the only ways in which corporate directors may breach their fiduciary duty; they may also breach that duty by being grossly negligent or by wasting corporate assets." *Penn Mart Realty*, 298 A.2d at 351. There is not the slightest hint, however, that the gross negligence concerned the board's being uninformed. Indeed, the key assertion in the plaintiff's complaint was not that the board knew too little but that it knew too much—that is, that it sold the shares knowing it would soon purchase identical shares at a higher price. Finally, in *Allaun v. Consolidated Oil Co.*, the plaintiff stockholder challenged the directors' approval of a sale of all the corporation's assets, and although the plaintiff alleged that the sale was tainted by self-interest in various respects, the court rejected these

Immediately after saying that the duty of care it was creating would be implemented with a gross negligence standard, the *Aronson* court cited a then-recent law review article, by E. Norman Veasey (future Chief Justice Veasey) and William E. Manning, in which the authors compared the standard of care set

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allegations. Allaun v. Consolidated Oil Co., 147 A. 257 (Del. 1929). Nevertheless, the court went on to say that the majority stockholders (and so presumably directors as well) "favoring the sale owe something more to the minority than to merely refrain from reaping a forbidden personal advantage, either directly or indirectly, from the sale. They owe the further duty of securing to it that the assets shall be sold for a fair and adequate price." *Id.* at 260. But, determining whether a price was fair and adequate:

> invites a study of the value which the assets may be fairly said to possess, and having ascertained the value, a determination of the question of whether or not there is such a disparity between the price to be received and the value found as would indicate legal fraud upon the rights of the dissenting minority.

Id. Further,

> the disparity must be sufficiently great to indicate that it arises not so much from an honest mistake in judgment concerning the value of the assets, as from either improper motives underlying the judgment of those in whom the right to judge is vested or a reckless indifference to or a deliberate disregard of the interests of the whole body of [stock]holders including of course the minority.

Id. Exactly what this meant in 1929 is hard to say, but nowadays such a standard is certainly not the *Van Gorkom* duty to be informed of all the material information reasonably available before making a business decision. It sounds, rather, like the corporate waste standard, as explained by the Supreme Court in *Disney*: "To recover on a claim of corporate waste, the plaintiffs must shoulder the burden of proving that the exchange was so one sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration." *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 74 (Del. 2006). At most, the duty described in *Allaun* is a precursor to the *Revlon* duty to obtain for the stockholders the best price reasonably available. It is true that the *Allaun* court examined the process the controlling stockholder used to shop the company, but it did so not to determine whether the controlling stockholder used due care. Rather, the court considered the sales process as *evidence* that the price obtained was fair. There is simply nothing like the *Van Gorkom* procedural duty of care in *Allaun*. Conversely, there is nothing like the *Allaun* inquiry into the substantive fairness of the price in *Van Gorkom*, where the Delaware Supreme Court based its decision entirely on the supposed inadequacies of the process, expressly declined to determine whether the price in the Pritzker transaction was fair, and remanded the case to the Court of Chancery to make that determination. Smith v. Van Gorkom, 488 A.2d 858, 893 (Del. 1985).

forth in Section 35 of the Model Business Corporation Act to the standard required under Delaware law.[389] There was in the later 1970s and early 1980s an active debate about whether Section 35 involved a simple negligence or gross negligence standard for directorial conduct, and Veasey and Manning take up the question of what the standard was under Delaware law.[390] They observe that the existing Delaware law provided little guidance,[391] and although they come to no definitive conclusion, they seem to favor the idea that in Delaware the standard of care is a gross negligence standard.[392] In reaching this conclusion, they refer only to three cases: *Graham v. Allis-Chalmers Manufacturing Co.*,[393] *Penn Mart Realty Co. v. Becker*,[394] and *Lutz v. Boas*.[395] The first of these is now recognized as being not a business judgment rule case at all but the seminal case concerning director oversight liability,[396] the doctrine that applies not when the board has made a business decision (even a decision to do nothing) but

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[389] E. Norman Veasey & William E. Manning, *Codified Standard—Safe Harbor or Uncharted Reef?*, 35 BUS. LAW. 919 (1980).

[390] *Id.* at 926–28.

[391] *Id.*

[392] *Id.*

[393] Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. 1963).

[394] Penn Mart Realty Co. v. Becker, 298 A.2d 349, 352 (Del. Ch. 1972).

[395] Lutz v. Boas, 171 A.2d 331, 396 (Del. Ch. 1961).

[396] Nevertheless, Justice Horsey, who of course wrote the majority opinion in *Van Gorkom*, has insisted that *Graham* is an important doctrinal basis for the duty of care. *See* Horsey, *supra* note 365, at 974. Although the case does refer to a director's duty "to use that amount of care which ordinarily careful and prudent men would use in similar circumstances," the case does not involve—and given that it sounds in oversight, *could not have* involved—a duty to be informed of all the material facts reasonably available before making a business decision. *Graham*, 188 A.2d at 130; *see* Robert T. Miller, *Wrongful Omissions:* Stone v. Ritter *and Adapting the Process Model of the Delaware Business Judgment Rule*, 10 PA. J. BUS. & EMP. L. 783 (2008) [hereinafter *Wrongful Omissions*]. Moreover, the court in *Graham* also held that the directors had not breached their duties, however defined. *Graham*, 188 A.2d at 131. That those who wish to say that the *Aronson–Van Gorkom* duty of care had some basis in Delaware law before *Aronson* are reduced to pointing to cases such as *Graham* shows, in my opinion, how completely wrong they are. As Thomas Aquinas said, some arguments are so weak that they lend probability to the opposing view. Thomas Aquinas, *On the Eternity of the World (De Aeternitate Mundi),* trans, Robert T. Miller, *in* INTERNET MEDIEVAL SOURCEBOOK (Fordham Univ. 1991), https://sourcebooks.fordham.edu/halsall/basis/aquinas-eternity.asp [https://perma.cc/2MKT-ASCR].

has rather abdicated its responsibilities or merely failed to act at all.[397] The standard in such cases is not negligence or gross negligence but bad faith, that is, conscious disregard of a known duty to act.[398] *Lutz v. Boas*, although it is earlier than *Allis-Chalmers*, also concerns oversight liability, not the business judgment rule.[399] The remaining case, *Penn Mart Realty*, which the court itself had already cited in *Aronson*, did say that directors may breach their fiduciary duty not only by fraud and self-dealing but also by "being grossly negligent or by wasting corporate assets," but this duty was in no way explained, and the opinion certainly never

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[397] As was made clear in *Aronson* itself, when a board "abdicated its functions, or absent a conscious decision, failed to act," the business judgment rule, which concerns actual business judgments, cannot, by its very terms be applied. Aronson v. Lewis, 473 A.2d 805, 813 (Del. 1984) (quoting Graham v. Allis-Chalmers Manufacturing Co., 188 A.3d 125 (1963) ("Although questions of directorial liability in such cases have been adjudicated upon concepts of business judgment, they do not in actuality present issues of business judgment.")).

[398] Stone v. Ritter, 911 A.2d 362, 369–70 (Del. 2006); *see also Wrongful Omissions*, *supra* note 396, at 946. Even at the time of *Van Gorkom*, scholars recognized that *Allis-Chalmers* and the *Van Gorkom* duty of care concerned different issues. *See* Schwartz & Wiles, *supra* note 330, at 444–45.

[399] Veasey and Manning understand *Lutz v. Boas* as holding that certain directors were liable because they "paid little attention to management's actions which even 'average attention to duty' would have revealed as improper or, at best, waste," leading the court to find "that in abdicating their responsibilities these directors were grossly negligent." Veasey & Manning, *supra* note 389, at 928. But as this summary suggests and as the text of the opinion itself confirms, the claim in the case was not that the relevant directors had made a business decision on the basis of inadequate information; it was that they were not monitoring the business at all, with the result that management had looted the company. Thus, the court states, "These men are prime examples of what can happen when a man undertakes substantial responsibility with public overtones without any appreciation of his obligation thereunder," and it goes on to quote from and adopt the conclusions of the Securities and Exchange Commission in a related action:

> [the] directors gave scant attention to the management of the [company]; made no efforts to be informed concerning [the company's] polices and whether such policies were being followed; made no decisions concerning purchases and sales of portfolio securities; and generally permitted the [company] to be managed by [certain officers] without consultation with or approval by the board as a whole.

Lutz v. Boas, 171 A.2d 381, 395–96 (Del. Ch. 1961). In contemporary terms, this is the language of oversight liability, not breaches of the duty of care. *Wrongful Omissions*, *supra* note 396, at 928.

mentioned anything about directors being informed.[400] The opinion contains nothing relating to gross negligence except this one phrase. There was, in short, no basis in prior law[401] for the Delaware

[400] Penn Mart Realty Co. v. Becker, 298 A.2d 349, 351 (Del. 1972); *see also supra* note 388 and accompanying text (discussing *Penn Mart Realty*).

[401] Schwartz and Wiles assert that "the possibility of attacking a sale of control solely on the basis of a lack of due care by the corporation's directors has been recognized in the Delaware cases since at least 1929." Schwartz & Wiles, *supra* note 330, at 439 (citing Allaun v. Consolidated Oil Co., 147 A. 257, 260 (Del. Ch. 1929)). This is not true, as simply reading the cases shows. As to *Allaun*, see *supra* note 388 and accompanying text (discussing *Allaun*). The other cases Schwartz and Wiles cite are similar. In *Mitchell v. Highland-Western Glass Co.*, the question was again the substantive one of whether the consideration received was so grossly inadequate as to suggest fraud. 167 A. 831, 832 (Del. Ch. 1933). True, plaintiffs argued that the defendant directors were uninformed about the value of the purchasing corporation, which was paying with its own stock, but the court rejected this contention on the facts without reaching any legal conclusions as to its merits. *Id.* at 834; *see also* Robinson v. Pittsburgh Oil Refinery Corp., 126 A. 46, 48 (Del. Ch. 1924) (substantive review of transaction's terms, no mention of a duty to be informed). The seminal case in the line, *Allied Chemical & Dye Corp. v. Steel Tube Co. of America*, expressly says, that, in a sale of the company, "[t]he requirements of the statute and of the certificate of incorporation all being satisfied, ... it will be manifest that the only ground upon which he can base his claim for relief is that of fraud." 120 A. 486, 491 (Del. Ch. 1924). The closest approach to something like the duty of care in *Aronson v. Lewis* is in *Gimbel v. Signal Cos.*, where Chancellor Quillen stated that the plaintiffs had *not* shown that the "directors acted so far without information that they can be said to have passed an unintelligent and unadvised judgment." Gimbel v. Signal Cos., 316 A.2d 599, 615 (Del. Ch. 1974), *aff'd per curiam*, 316 A.2d 619 (Del. 1974), Quillen later himself criticized the Supreme Court for misreading *Gimbel* to support the holding in *Van Gorkom*. Quillen, *supra* note 28, at 471 (stating that "even the [S]upreme [C]ourt should not be free to miscite what the chancellor said or what he did to justify what it is now saying or doing"). Mones, *supra* note 31, at 560 (arguing that the "*Trans Union* court's reliance on *Gimbel* may have been misguided"). Nevertheless, Quillen does think that "for years the courts have in fact reviewed directors' business decisions to some extent from a quality of judgment point of view." Quillen, *supra* note 28, at 492 n.109 (he mentions only Bodell v. General Gas & Electric Corp., 140 A. 264, 267 (Del. 1927) ("gross abuse of discretion"), Warshaw v. Calhoun, 221 A.2d 487, 492–93 (Del. 1966) ("reckless indifference"), Muschel v. Western Union Corp., 310 A.2d 904, 908 (Del. Ch. 1973) ("recklessly"), and Gimbel v. Signal Cos., 316 A.2d 599 (Del. Ch. 1974), *aff'd per curiam*, 316 A.2d 619 (Del. 1974)); *see also* Kaplan v. Centex Corp., 284 A.2d 119 (Del. Ch. 1971). In the end, Schwartz and Wiles have to concede that "there appears to be no reported decision prior to *Trans Union* which holds, *solely on the basis of the board's decision-making processes*, that

Supreme Court's assertion in *Aronson* that Delaware imposed on corporate directors a duty to be informed of all the material facts reasonably available before making a business decision.[402]

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a third party merger is invalid as the product of uninformed business judgment." Schwartz & Wiles, *supra* note 330, at 442.

[402] This was recognized by many practitioners and scholars at the time. In some cases, however, there seems to have been significant confusion about what had changed in *Aronson* and *Van Gorkom*. For example, Steven Mones states that, prior to *Van Gorkom*, a finding that the directors had acted in good faith and not breached their duty of loyalty "would have been sufficient to trigger the defense of the business judgment rule," but then says that "[t]he *Trans Union* decision did not break new ground or introduce radical theories" because "it followed the basic standards for the application of the business judgment rule established in *Aronson v. Lewis*." Mones, *supra* note 31, at 567. It cuts quite thinly to say that applying a radical new theory announced in a case the year before in dicta is not to break new ground or introduce radical theories. Of course, there were those who took the opposite view. William Prickett, who represented the plaintiffs in *Van Gorkom*, insisted that "Delaware lawyers (and indeed most lawyers from elsewhere) familiar with Delaware law immediately understood ... in reversing the short unreported opinion of the chancellor dismissing the case, the court had applied, without change, existing Delaware law to the facts in the record." Prickett, *supra* note 357, at 451. Prickett tries to pass off the furious reaction to the case as resulting from non-Delaware lawyers being uninformed about Delaware law. *Id.* at 451–52. However, this is quite absurd (for instance, William T. Quillen, a former justice on the Delaware Supreme Court and a former chancellor on the Court of Chancery, prior to the Supreme Court's decision in *Van Gorkom*, had drafted an article on the business judgment rule based on the assumption that the Supreme Court would affirm the ruling below. Quillen, *supra* note 28, at 465. Similarly, Macey and Miller, referring to Prickett's view, state that "the evidence is overwhelming that the decision shocked and amazed a large segment of the corporate bar." Macey & Miller, *supra* note 23, at 132. Prickett also refers to a "whole line of Delaware cases that have held over the years the directors are liable for gross negligence." Prickett, *supra* note 357, at 458. His footnotes, however, trace back to only "a short survey of case law dealing with directors' duty of care" in *Aronson v. Lewis* and to other cases cited in *Van Gorkom*, none of which, as discussed in the text above, do anything to support a duty of care. *Id.* at 456 n.21; *see also id.* at 459 n.32 (he cites but does not discuss Gimbel v. Signal Cos., 316 A.2d 599 (Del. Ch. 1974), *aff'd per curiam*, 316 A.2d 619 (Del. 1974), Kaplan v. Centex Corp., 284 A.2d 119 (Del. Ch. 1971), and Mitchell v. Highland-Western Glass Co., 167 A. 831 (Del. Ch. 1933)). Schwartz and Wiles do a much more impressive, yet still quite unconvincing, job of finding support for *Aronson* and *Van Gorkom* in prior Delaware Case law. *See supra* note 401 and accompanying text; *see also* Morton Moskin, Trans Union: *A Nailed Board*, 10 DEL. J. CORP. L. 405, 406 (1985) ("The *Trans Union* court did not depart from the established rules").

But something like a duty not to act with gross negligence was in the air in 1984. Besides the Veasey and Manning article, earlier in its opinion the *Aronson* court had cited several law review articles most of which have the common theme that courts needed to do more to control corporate boards.[403] Some of these expressly advocated for a duty of care[404] and some bore alarming subtitles such as "Is Corporate Behavior Beyond the Control of Our Legal System?"[405] More generally, there was a widespread feeling in 1985 that someone, somewhere had to do something about the wave of merger activity that had begun in the early years of the decade. A *Wall Street Journal* article from January 2, 1985—less than four weeks before the Delaware Supreme Court released its opinion in *Van Gorkom*—begins by referring to the "national ruckus over merger mania" and states that "stockholders across the country, as well as state government legislators and regulators, influential lawyers and the heads of the nation's largest corporations" were all expressing frustration about takeovers, and that "[u]nderlying the hysteria is the spreading notion that the merger and acquisition process in America is out of control."[406] The article goes on to provide breathless accounts of junk bonds, bust-up mergers, greenmail, poison pills, and state anti-takeover laws, and it speculates about possible action by Congress to limit merger activity.[407]

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[403] *See* Aronson v. Lewis, 473 A.2d 805, 811 n.4 (Del. 1984). The articles are Daniel R. Fischel, *The Corporate Governance Movement*, 35 VAND. L. REV. 1259 (1982); Bruce Dickstein, *Corporate Governance and the Shareholders' Derivative Action: Rules and Remedies for Implementing the Monitoring Model*, 3 CARDOZO L. REV. 627 (1982); Robert J. Haft, *Business Decisions by the New Board: Behavioral Science and Corporate Law*, 80 MICH. L. REV. 1 (1981); George W. Jr. Dent, *The Revolution in Corporate Governance, The Monitoring Board, and The Director's Duty of Care*, 61 B.U.L. REV. 623 (1981); Michael G. Moore, *Corporate Officer & Director Liability: Is Corporate Behavior Beyond the Control of Our Legal System?* 16 CAP. U.L. REV. 69 (1980); Thomas M. Jones, *Corporate Governance: Who Controls the Large Corporation?* 30 HASTINGS L.J. 1261 (1979); and Marshall L. Small, *The Evolving Role of the Director in Corporate Governance*, 30 HASTINGS L.J. 1353 (1979).

[404] *E.g.*, George W. Jr. Dent, *The Revolution in Corporate Governance, The Monitoring Board, and The Director's Duty of Care*, 61 B.U.L. REV. 623 (1981).

[405] Michael G. Moore, *Corporate Officer & Director Liability: Is Corporate Behavior Beyond the Control of Our Legal System?* 10 CAP. U.L. REV. 69 (1980).

[406] Tim Metz & John D. Williams, *Year-End Review of Markets and Finance: Debate Over Mergers Intensifies Amid Record Surge of Transactions*, WALL ST. J. (Jan. 2, 1985).

[407] *Id.*

Some corporate law scholars had singled out the Delaware courts for not doing enough to control what these scholars regarded as socially harmful transactions.[408] Just what role the scholarly articles and widespread alarm in 1984 and 1985 about corporate takeovers played in the *Van Gorkom* court's decision-making is impossible to say, but it is tempting to believe that the court felt pressure to do something[409] to impose more discipline on directors approving business combination transactions.[410] Whatever the causes, the result was the application of the *Aronson* duty of care in *Van Gorkom*.[411]

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[408] *See, e.g.*, William L. Cary, *Federalism and Corporate Law: Reflections on Delaware*, 83 YALE L.J. 663 (1974).

[409] *Cf.* famous exchange between Otter and Bluto: Otter declares, "I think that this situation absolutely requires a really futile and stupid gesture be done on somebody's part!" and Bluto answers, "We're just the guys to do it." ANIMAL HOUSE (Universal Pictures 1978). Writing soon after the case was decided, Herzel and his co-authors described the majority's opinion as a "grand anti-business gesture." Herzel et al., *supra* note 335, at 14; *see also* Mones, *supra* note 31, at 550 ("Both the length of the majority opinion and its tenor suggest strongly that the court was sending the message to corporate directors generally that the business judgment rule is not an impregnable defense against attacks by dissatisfied [stock]holders."); Lawrence A. Hamermesh, *A Kinder, Gentler Critique of* Van Gorkom *and its Less Celebrated Legacies*, 96 NW. U.L. REV. 595, 596 [hereinafter *Gentler Critique*] (stating that the Delaware Supreme Court "surely saw the *Van Gorkom* case as a rare opportunity to address the proper role of directors in dealing with acquisition bids"). Quillen thinks that it was "the chief criticism of the majority opinion arises ... from the tone of the writing" and suggests "it would have been tactful and consistent with principle in a jurisdiction that has traditionally given wide discretion to directors, for the court not to have engaged in language hostile beyond its holdings or indeed beyond the law of the state." Quillen, *supra* note 28, at 478. Macey and Miller think that "the court seemed determined to make an example of the Trans Union board." Macey & Miller, *supra* note 23, at 131. They too characterize the tone of the opinion as "harsh and uncharitable towards the defendants." *Id.* at 132–33. *But see* Schwartz & Wiles, *supra* note 330, at 431 (stating "[t]he suggestion that there has been a new anti-business departure in Delaware corporate law is simply wrong").

[410] Allen, Jacobs & Strine, *supra* note 31, at 459 n.39 (stating, "*Van Gorkom* … must also be viewed as part of the Delaware courts' effort to grapple with the huge increase in mergers and acquisition activity in the 1980s and the new problems that posed for judicial review of director conduct."); Mones, *supra* note 31, at 566 (stating "the *Trans Union* decision must ... be evaluated against the prevailing state of extensive merger activity" and, thus, is "the court's statement to corporate officers in general that their actions will be subject to stricter scrutiny than in the past").

[411] Smith v. Van Gorkom, 488 A.2d 858, 873 (Del. 1985).

Perhaps ironically, for all its subsequent importance, the entire discussion of the duty of care in *Aronson* was the merest dicta. The plaintiffs in that case were challenging actions by the directors approving an employment agreement for an officer who was also a director and 47 percent stockholder of the corporation.[412] All the allegations concerned breaches of the duty of loyalty and whether the other directors were disinterested and independent;[413] there was no hint of an allegation that they had been uninformed when they approved the challenged employment agreement. The duty of care would not actually figure in any case before *Smith v. Van Gorkom*.[414]

b. The Van Gorkom *Duty of Care vs.* Revlon *Duties—Theoretical Justifications*

Even in *Revlon* itself, *Revlon* duties were much better theorized than the *Aronson–Van Gorkom* duty of care. This comes out in relation to the conditions under which the duty applies, the content of the duty, the normative justification for the duty, and potential damages for a violation of a duty.[415]

Regarding the conditions under which the duty applies, the *Van Gorkom* duty of care by its terms is part of the business judgment rule and so applies to all business decisions that the board may make, not just decisions about business combinations.[416] Thus, in one of the very few duty of care cases involving public companies since *Van Gorkom*, the business decisions that the plaintiff-stockholder challenged involved not a merger, but the hiring and firing of a key employee.[417] This pervasiveness of

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[412] Aronson v. Lewis, 473 A.2d 805, 810 (Del. 1984).

[413] *See id.* at 813.

[414] *Id.*

[415] *See Van Gorkom*, 488 A.2d at 874.

[416] *Id.* at 872–73; *see also* Sharfman, *supra* note 57, at 293 n.40 (stating that "*Van Gorkom* applies outside the world of mergers and acquisitions").

[417] *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 35 (Del. 2006). Macey and Miller predicted that "[i]t is extremely unlikely that *Trans Union* will ever be applied outside the takeover context." Macey & Miller, *supra* note 23, at 140. The implementation of Section 102(b)(7) provisions has largely forestalled any application of the *Van Gorkom* duty of care, but cases like *Disney* show that Macey and Miller were mistaken here. They were misled largely because they thought *Van Gorkom* was "a takeover case." Applying

the duty of care had at least two important effects.[418] On the one hand, because the duty applied to all business decisions, it could not be tailored to the real problem the Delaware Supreme Court seems to have wanted to address—the behavior of directors in dealing with the merger.[419] On the other hand, because the duty applied to all business decisions, the threat of personal liability that it created—which was already gigantic in connection with mergers—loomed over the heads of directors for every business decision they made. For example, if the directors caused the company to borrow $10 billion on an unsecured basis at 10 percent interest for ten years, but a stockholder later convinced the Court of Chancery that the directors were not fully informed about the possibilities of issuing secured debt at 6 percent, the directors would be liable for the incremental borrowing cost of the transaction they approved—potentially up to $400 million.[420] Indeed, since directors of public companies are constantly making business decisions involving vast sums but only rarely consider merger proposals, the tremendous liability exposure *Van Gorkom* created was in fact mostly due to potential liability from run-of-the-mill business decisions, not mergers.[421] This made the *Van Gorkom* duty of care much more difficult for directors to deal with than a heightened duty that applied only in known special circumstances when the directors could make particular efforts to comply with it.

By contrast, from the beginning, *Revlon* clearly applied only when the directors were engaged in selling their company.[422] They had no need to worry about *Revlon* duties in any other context.[423]

Van Gorkom outside the takeover context "would not serve its purposes, which are unique to that context." *Id.* at 128; *see also id.* at 140. The truth, as this Article argues, is not that *Van Gorkom was* a takeover case, but that *it should have been*. Since, by its express terms, the holding in *Van Gorkom* about the duty of care obviously applies to all board decisions, naturally we get cases like *Disney* applying that duty outside the takeover context.

[418] *See Van Gorkom*, 488 A.2d at 872–73.

[419] *Id.*

[420] *Id.* at 878

[421] *Id.* at 872.

[422] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 184 (Del. 1986). As Bainbridge notes, the sale of the company is a final-period problem, which in itself suggests that special legal duties may be justified in such cases. Bainbridge, *supra* note 60, at 223.

[423] *See id.*

True, it took a few years and some great takeover cases to clarify exactly when a board's *Revlon* duties would be triggered: for example, that a decision to engage in a cash merger triggers *Revlon*, but a decision to engage in a stock-for-stock merger does not, except in the extraordinary case of an acquisition with a controlling stockholder.[424] But the end result was a system in which it is very clear that a board's *Revlon* duties can be triggered only by a decision by the board itself to sell the company, with no other party being able to send the board to *Revlon*-Land.[425] Indeed, after *QVC*, there was likely never a case in which a board was surprised to learn that its *Revlon* duties were triggered.[426] Because *Revlon* duties apply only in rare and clearly circumscribed contexts and can be triggered only by the board itself, it has been relatively easy for directors to know when they would be held to the higher standard required by *Revlon* and to act accordingly.[427]

As to the content of the duty, because the *Van Gorkom* duty of care was a general duty incorporated into the business judgment rule, it could of necessity supply directors with little guidance as to what they had to do, whether in selling their company or in any other business decision. They were merely required to be informed of all the material facts reasonably available.[428] *Van*

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[424] *See* Paramount Commc'ns, Inc. v. Time Inc., 571 A.2d 1140, 1142 (Del. 1990); Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 46 (Del. 1994).

[425] *Id.* at 1151 (where the Delaware Supreme Court stated, "we decline to extend *Revlon*'s application to corporate transactions simply because they might be construed [by the market] as putting a corporation either 'in play' or 'up for sale'"); *see also* Lyondell Petrochemical Co. v. Ryan, 970 A.2d 235, 242 (2009), where the court held:

> *Revlon* duties do not arise simply because a company is 'in play.' The duty to seek the best available price applies only when a company embarks on a transaction—on its own initiative or in response to an unsolicited offer—that will result in a change of control.

Id.

[426] C&J Energy Services, Inc. v. City of Miami General Employees', 107 A.3d 1049, 1053 (Del. 2014) is a possible exception, but if so, it is the exception that proves the rule. In the doubtful cases, *Revlon* has been found *not* to apply. *See, e.g.*, *Time Inc.*, 571 A.2d at 1142.

[427] *See QVC*, 637 A.2d at 46; *Time Inc.*, 571 A.2d at 1142.

[428] Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985). The impossibility of specifying how much care directors should take in particular kinds of transactions was known to Moravetz in the nineteenth century. He writes

Gorkom made it very clear that, in approving a sale of the company, some kind of financial analysis, whether from an investment banker or in-house financial experts,[429] would always or virtually always be deemed material information reasonably available, but other than that, *Van Gorkom* offered little guidance for directors considering a business combination and none for directors considering other kinds of transactions. Presumably, had *Van Gorkom* not been effectively overturned by Section 102(b)(7) and replaced by *Revlon*,[430] there could have developed a line of *Van Gorkom* cases determining whether certain kinds of information were material and reasonably available to a board considering a merger.[431] There can be no doubt, however, that the text of the *Van Gorkom* opinion provided much less guidance to directors and the bar than the text of the *Revlon* did.

Furthermore, the *Van Gorkom* duty of care was ill adapted to regulating the various decisions a board might make in the process

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that "directors ... undertake to use as much diligence and care as the proper performance of the duties of their office requires," which "is a question of fact, which must be determined in each case in view of all the circumstances," including "the character of the company, the condition of [its] business, [and] the usual methods of managing such companies." Moravetz, *supra* note 371, at § 552. "It is evident that no abstract reasoning can be of service in reaching a proper solution." *Id.*

[429] *Id.* at 876 (stating "[o]ften insiders familiar with the business of a going concern are in a better position than are outsiders to gather relevant information; and under appropriate circumstances, ... directors may be fully protected in relying in good faith upon the valuation reports of their management").

[430] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc. 506 A.2d 173, 185 (Del. 1986).

[431] *QVC*, 637 A.2d at 44 ("a board of directors is not limited to considering only the amount of cash involved, and is not required to ignore totally its view of the future value of a strategic alliance," and "the directors should analyze the entire situation and evaluate in a disciplined manner the consideration being offered. Where stock or other non-cash consideration is involved, the board should try to quantify its value, if feasible, to achieve an objective comparison of the alternatives."); *e.g.,* Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1282 n. 29 (directors should consider an offer's "fairness and feasibility; the proposed or actual financing for the offer, and the consequences of that financing; questions of illegality; ... the risk of non-consummation; ... the bidder's identity, prior background and other business venture experiences; and the bidder's business plans for the corporation and their effects on [stock]holder interests."); *cf.* the guidance the Delaware courts have offered directors trying to fulfill their *Revlon* duties.

of selling the company.[432] As Chancellor Allen famously said, "[c]ompliance with a director's duty of care can never appropriately be judicially determined by reference to *the content of the board decision*," and

> whether a judge ... considering the matter after the fact, believes a decision substantively wrong, or degrees of wrong extending through 'stupid' to 'egregious' or 'irrational', provides no ground for director liability, so long as the court determines that the process employed was either rational or employed in a *good faith* effort to advance corporate interests.[433]

In other words, as the Delaware Supreme Court would later say, "Due care in the decision[-]making context is *process* due care only."[434] But a duty regulating directorial conduct in handling takeovers that was limited to issues of process and ignored substance would have allowed all manner of decisions that *Revlon* would prohibit: in *Revlon* itself, for example, Revlon's decision not to negotiate with Perelman would have to have been upheld provided only that the Revlon board considered all the material facts reasonably available before deciding.[435] Indeed, as we will see below, the *Van Gorkom* court often struggled, sometimes unsuccessfully, to find a way to shoehorn its criticisms of the Trans Union board into the duty of care, that is, to characterize those decisions as failures to act on a fully informed basis.

By contrast, *Revlon* duties are very well-adapted to the limited context in which they apply: when the board is selling the company, the directors have to take reasonable steps to get the best price for the stockholders reasonably available.[436] In essence, when they approve a merger agreement selling the company, the

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[432] *In re* Caremark Int'l. Inc. Derivative Litig. 698 A.2d 959, 967 (Del. Ch. 1996).

[433] *Id.*

[434] Brehm v. Eisner, 746 A.2d 244, 264 (Del. 2000).

[435] *Id.* at 259.

[436] Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 242 (Del. 2009) (stating "[t]here is only one *Revlon* duty—'to [get] the best price for the [stock]holders at a sale of the company.'"); Paramount Commc'ns. Inc v. QVC Network Inc., 637 A.2d 34, 43 (Del. 1994) (stating "[t]he consequences of a sale of control impose special obligations on the directors of a corporation. In particular, they have the obligation of acting reasonably to seek the transaction offering the best value reasonably available to the [stock]holders").

directors have to reasonably believe that the price provided in the agreement is the best one reasonably available.[437] True, this involves a general standard of reasonability, not bright-line rules,[438] and to that extent it may leave directors unsure as to what they may or may not do, but directors can and do take comfort in the fact that the Delaware courts have emphasized that a court reviewing a board's actions under *Revlon* "should be deciding whether the directors made *a reasonable* decision, not *a perfect* decision," and "[i]f a board selected one of several reasonable alternatives, a court should not second-guess that choice even though it might have decided otherwise or subsequent events may have cast doubt on the board's determination."[439]

As to the theoretical justification for the duty, on the simplest level, everyone is aware that when a board of directors sells the company in a change-of-control transaction (that is, whenever *Revlon* is triggered), this virtually always provides a final opportunity for the stockholders to obtain a significant premium above market for their shares.[440] As to why large premiums are available in such transactions, there is significant debate,[441] but the fact itself is obvious and undeniable. It thus seems eminently sensible that directors charged with maximizing stockholder value should have a duty to capture such a premium when the opportunity arises. As the Delaware Supreme Court put it in *QVC*, "a sale of control impose special obligations on the directors of

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[437] Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1288 (Del. 1989) (holding that "the crucial element supporting a finding" that the board complied with its *Revlon* duties "is knowledge. It must be clear that the board had sufficient knowledge of relevant markets to form the basis for its belief that it acted in the best interests of the [stock]holders.").

[438] In the famous and inevitable phrase, "there is no single blueprint" that a board is required to follow in managing a sale of the company. *Id.* at 1286.

[439] *QVC*, 637 A.2d at 45.

[440] *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 184 (Del. 1986).

[441] *See, e.g.*, Richard A. Booth, *Discounts and Other Mysteries of Corporate Finance*, 79 CAL. L. REV. 1053 (1991); Lynn A. Stout, *Are Takeover Premiums Really Premiums? Market Price, Fair Value, and Corporate Law*, 99 YALE L.J. 1235 (1990); Reinier Kraakman, *Taking Discounts Seriously: The Implications of "Discounted" Share Prices as an Acquisition Motive*, 88 COLUM. L. REV. 891 (1988); J. Michael Harrison & David M. Kreps, *Speculative Investor Behavior in a Stock Market with Heterogeneous Expectations*, 92 Q.J. ECON. 323 (1978).

a corporation," because "[o]nce control has shifted, the ... stockholders will have no leverage in the future to demand another control premium. As a result, the ... stockholders are entitled to receive, and should receive, a control premium," and thus the "directors had an obligation to take the maximum advantage of the current opportunity to realize for the stockholders the best value reasonably available."[442]

By contrast, the theoretical justification of the duty of care is shaky.[443] As Easterbrook and Fischel have pointed out, since gathering and analyzing information is costly, how much and what kinds of information a board should have before making a business decision is itself a business decision just like any other.[444] That is, "there is a limit to how informed managers should be before making a decision," for "information is costly," and "investors want mangers to spend an additional dollar on information acquisition only to the point where there is an additional dollar generated from better decisions making."[445] Hence, "the need to expend resources for additional information will vary from firm to firm, manager to manager, and decision to decision,"[446] which means that the manager's duty to be informed cannot be specified in advance (except in the most general terms) and thus "it is correspondingly difficult to determine when there has been a breach."[447] Accordingly, "[j]udicial inquiry into the amount of information managers should acquire before deciding creates the precise difficulties that the business judgment rule is designed to avoid."[448] Rather than allowing directors to make a

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[442] *QVC*, 637 A.2d at 43.

[443] *See* Fischel, *supra* note 338, at 1438 (stating "[w]hat the opinion lacks … is a coherent theory of the business judgment rule" and "the majority opinion makes no attempt to integrate its extended discussion of the facts with the theory of the rule or what purposes the rule is meant to serve").

[444] FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 107–08 (1991).

[445] Fischel, *supra* note 338, at 1441. Compare with Bainbridge, who writes that "information is costly and [stock]holders will only want managers to invest an additional dollar in gathering information where there is an additional dollar generated from better decisions making." Bainbridge, *supra* note 60, at 217.

[446] Fischel, *supra* note 338, at 1441.

[447] *Id.*

[448] EASTERBROOK & FISCHEL, *supra* note 444, at 107–08 (1991); Leo Herzel and Leo Katz make essentially the same point, arguing that there is no clear

business judgment about which information is worth having before deciding (*e.g.*, whether an investment banker's fairness opinion is really worth $5 million of the stockholders' money), the duty of care substitutes the court's judgment about whether certain material was "material" and "reasonably available." All the arguments that support the business judgment rule generally[449] also support eliminating the duty of care.[450]

c. *The* Van Gorkom *Duty of Care v.* Revlon *Duties—Applications*

Armed with the duty of care announced but not applied in *Aronson*, the Delaware Supreme Court found that the Trans Union directors had breached that duty by not informing themselves of all the material facts reasonably available to them before making business decisions, whether approving the original transaction or approving modifications to it. Below, I reconsider those findings as they would appear to a court applying *Revlon* and its progeny to the same facts. I shall argue that, in many instances, it is easy to agree with the court that the directors were not adequately informed before they made a decision. In other cases, however, it is difficult (sometimes obviously impossible) to justify the court's criticisms of the Trans Union directors' conduct on

distinction between substantive business decisions and decisions about procedures underlying those decisions, and so, it is incoherent for courts to accord extreme deference to one and virtually no deference to the other. Leo Herzel & Leo Katz, Smith v. Van Gorkom*: The Business of Judging Business Judgment*, 41 BUS. LAW. 1187, 1190 (1986) [hereinafter Herzel & Katz] (stating "[w]hy should the failure to hire an investment banker be viewed as part of the decision-making procedure behind the merger rather than the product of a decision about whether to hire an investment banker?").

[449] *See, e.g.*, Joy v. North, 692 F.2d 880, 888 (2d Cir. 1982); EASTERBROOK & FISCHEL, *supra* note 444, at 90–108.

[450] Allen, Jacobs, and Strine have argued that there is yet another problem with the duty of care as applied in such cases as *Van Gorkom*: since the concept is essentially a tort concept, the plaintiffs should have to prove not only a breach of the duty but also harm and causation. Allen, Jacobs & Strine, *supra* note 31, at 449 (in particular, the results of the plaintiffs showing a breach should not be an entire fairness inquiry); *see also* McChesney, *supra* note 340, at 636 (stating "[t]o violate the duty of care, any breach must also have caused some damage to the firm and its [stock]holders," but "the court did not address that issue in its opinion").

this basis. In those cases, however, it is usually quite easy to see why that conduct would amount to a breach of the board's *Revlon* duties.[451] The picture that emerges from this analysis is that of a duty of care being tortured to support conclusions that it cannot in many cases justify. Even if *Van Gorkom* had not suffered from the much more serious problem of creating untenable levels of financial risk for directors, it would nevertheless still have to have been retooled in *Revlon*.

(1) The Original Decision to Approve the Merger with Pritzker

As we saw above, on September 19, 1980, Van Gorkom called a special meeting of the Trans Union directors for the next day, September 20.[452] The notice of the meeting did not state its purpose, and so, the independent directors learned of potential transaction with Pritzker only at the meeting (the inside directors other than Van Gorkom learned of the potential transaction an hour earlier at a meeting of senior executives Van Gorkom had called).[453] In approving the merger, the directors had, besides their admittedly extensive background information about the business and financial condition of Trans Union, only Van Gorkom's twenty-minute oral presentation about the transaction,[454] a presentation from the company's attorney about the merger agreement (assuming the dissent is to be believed),[455] and a brief presentation by Romans about the leveraged-buyout analysis he had conducted and his opinion that the $55 price was

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[451] *See* Allen, Jacobs & Strine, *supra* note 31, at 459 n.39 (stating "[i]ndeed, if decided consistent with the 'enhanced scrutiny' analysis mandated by *Revlon*, with its emphasis upon immediate value maximization, rather than as a 'due care' case, *Van Gorkom* would not be viewed as remarkable"); *see also* Macey & Miller, *supra* note 23, at 131 (arguing that "viewing the case as being rightly decided on the basis of a gross negligence standard is not a particularly satisfying way of reconciling the apparent inconsistency between the facts and the law").

[452] *See supra* text accompanying note 131. In economic terms, the cost of providing the directors these facts was clearly much less than the expected value to the company (in the form of improved decision-making) from the directors having them.

[453] Smith v. Van Gorkom, 488 A.2d 858, 874 (Del. 1985).

[454] *Id.*

[455] *Id.* at 895.

within the range of fair prices for the company, albeit at the bottom of the range.[456] The court specifically faults the board for not informing itself of two things: "Van Gorkom's role in forcing the 'sale' of the Company and in establishing the per share purchase price," and "the intrinsic value" of the company as would be determined by a financial analyst (*e.g.*, a discounted cash flow study).[457]

(i) The Negotiating History

The facts about the negotiating history between Van Gorkom and Pritzker regarding the price in the transaction were surely material facts, and since Van Gorkom needed only to state them at the meeting, they were of course reasonably available to the Trans Union board.[458] If the directors really did not have these facts (which seems very likely), then the Supreme Court was surely right that they breached their duty of care. The dissent, however, seemed to think that Van Gorkom did disclose these facts to directors and that they were thus aware of them, for it states that he "reviewed all aspects of the proposed transaction and repeated the explanation of the Pritzker offer he had earlier given to senior management."[459] However that may

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[456] *Id.* at 877.

[457] *Id.* at 874. By quoting extensively from the transcript of the oral arguments in the Supreme Court, Owen shows that Chief Justice Herrmann was especially concerned about this latter point. He asked counsel for the defendants over and over why the directors did not seek some kind of financial analysis of the company, whether from the company's investment banker or its internal financial staff. He also apparently asked counsel whether counsel was aware of any other similar transaction in which the selling company did not obtain a financial analysis of this kind, and counsel apparently could not produce such an example. OWEN, *supra* note 3, at 257–58.

[458] *Van Gorkom*, 488 A.2d at 895.

[459] *Id.* Owen's account seems to be closer to that of the majority. He says that Van Gorkom's presentation to the board was similar to the one he had given to his senior executives an hour earlier, OWEN, *supra* note 3, at 70, and about that presentation Owen says that "some recall, Van Gorkom left the clear impression that the offer was unsolicited," that he had approached Pritzker to get the viewpoint of a buyer as to whether anyone might be interested in buying Trans Union for $55 per share, and that subsequently Pritzker concluded that he himself might be interested in such a transaction and so made an offer. *Id.* at 63. To the extent that Van Gorkom really did approach Pritzker for advice rather than to solicit an offer, this account might be true, or at least Van Gorkom may have believed it to be true, but it strains

be, I would suggest that the more significant problem lies not so much in whether the outside directors were aware of the negotiating history but rather in that history itself. That is, the larger problem lay not in whether the board had all the material facts about the negotiating history reasonably available to it when it decided, but in whether, under *Revlon*, the decisions made by Van Gorkom (which ought to have been supervised and controlled by the board, but of course were not) in negotiating with Pritzker were substantively reasonably calculated to obtain for the Trans Union stockholders the best price reasonably available for their shares. If they were not, it becomes well-nigh impossible to see how the Trans Union board could approve a transaction at the $55 price Van Gorkom obtained from Pritzker.

The negotiating process began when Van Gorkom, perhaps affected by a desire for a liquidity event to fund his impending retirement[460] or perhaps not,[461] concluded that he would happily

credulity to imagine that Van Gorkom, in arranging his initial meeting with Pritzker, was not hoping Pritzker would himself be interested in acquiring Trans Union.

[460] *Van Gorkom*, 488 A.2d at 866. Quillen notes that, having suggested Van Gorkom wanted to retire, the court then inconsistently suggested that he was put out not to have been included in the buyout group, whose members would have had to remain at the company for several years in order to realize a gain on their investment. Quillen, *supra* note 28, at 479.

[461] On how his imminent retirement may have affected Van Gorkom's incentives, see the discussion in *supra* note 113. Stephen M. Bainbridge observes that, although one could argue that Van Gorkom's imminent retirement gave him an incentive to sell the company not shared by the stockholders generally, nevertheless "the trouble with this argument is that Van Gorkom's incentive clearly is to get the best possible price" because "the more money the buyer paid for Trans Union, the more money Van Gorkom would have in retirement." Bainbridge, *supra* note 60, at 200. On the whole, Bainbridge concludes that Van Gorkom's "self-interest was directly in line with the interests of the [stock]holders." *Id. But see* Macey, *supra* note 57, at 609–11, who argues that the board should be faulted for not realizing that Van Gorkom was not a typical stockholder because (a) his impending retirement really did make his attitude towards a quick cash deal different from that of other stockholders, and (b) many other stockholders had acquired their Trans Union shares in tax-free share exchanges when Trans Union had acquired other companies or otherwise had low tax bases in their shares, which meant that they might well prefer a tax-free stock-for-stock merger rather than an LBO in which the merger consideration would be cash and thus fully taxable. On the tax issue, see William M. Owen, *A Shareholder Named Smith*, 24 DIRECTORS & BOARDS 39 (2000) [hereinafter *Shareholder*] (stating that about one-third of the outstanding

accept $55 per share for his own Trans Union shares.[462] Van Gorkom then approached Pritzker and presented him with an LBO structure, a form of transaction of which Van Gorkom had first heard only days before, after consulting about a buyout at $55 per share with no one except the company's controller, Peterson, whom he directed to run some numbers for him. Van Gorkom knew virtually nothing about the prices that could be paid in LBOs, and, by his own account, he was consulting with Pritzker for exactly this reason. Moreover, he had no reason for thinking that the price obtainable in an LBO would be higher than the price obtainable in, for example, a strategic stock-for-stock merger.[463] He was also fully aware that a cash transaction such as an LBO would be taxable to the Trans Union stockholders, whereas a stock-for-stock transaction generally would not.[464]

Furthermore, the primary reason for the transaction was that Trans Union could not capture the full value of its ITCs. The ITCs could be of considerable value to an appropriate acquirer,[465] but just how valuable would depend on the acquirer's taxable income, and so, the value of Trans Union's ITCs would

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Trans Union shares were issued in acquisitions of other companies, with the result that the original holders of those shares generally had low tax bases in such shares).

[462] *Van Gorkom*, 488 A.2d at 865. According to Owen, Van Gorkom steadfastly maintained that he settled on the $55 per share number because he thought it was an attractive price, not because it was the midpoint of the range in Romans's original LBO study. OWEN, *supra* note 3, at 54.

[463] In fact, at least under normal market conditions, most observers believe strategic buyers can and do routinely outbid financial buyers. *E.g.*, *In re* Netsmart Technologies, Inc. S'holders Litig., 924 A.2d 171, 186 n.42 (referring to the convention wisdom that strategic buyers can usually outbid financial buyers because of their ability to capture synergies); *see also In re* Appraisal of Dell, Inc., No.9322-VCL, 2015 WL 4313206 (Del. Ch. July 13, 2015). On the other hand, Van Gorkom believed that Trans Union's relatively high debt/equity ratio, along with the dilution an acquirer's stockholders would likely suffer in a stock-for-stock merger, would make Trans Union unattractive to a public company buyer. *See* Owen, *Trans Union*, *supra* note 117, at 22–23.

[464] OWEN, *supra* note 3, at 42 (discussing Van Gorkom's views on the relative merits of cash and stock consideration, including the different tax treatments of such transactions); *see also Shareholder*, *supra* note 461, at 39 (2000) (describing reaction to the Pritzker transaction of Trans Union stockholders with low tax bases in their shares).

[465] Owen notes that in late 1980 Trans Union had a $244 million deferred tax asset on its balance sheet. OWEN, *supra* note 3, at 4.

vary from acquirer to acquirer. Presumably, *Revlon* would require that, in selling the company, the directors take reasonable steps to capture not just the intrinsic value of the company but also as much of the value that the ITCs would have to the buyer as they could obtain for the stockholders. Van Gorkom's $55 per share LBO structure effectively attributed no value at all to tax benefit the acquirer would capture from Trans Union's ITCs,[466] and so it seems neither Van Gorkom nor the board took any reasonable steps to obtain a price that impounded the value of the ITCs to the acquirer.[467] In a perfectly competitive market for the sale of the company, Trans Union would capture the entire risk-adjusted value of the ITCs. Of course, the market for an asset like a public company is not perfectly competitive, but, at least at the outset of the sales process, a seller hoping to obtain the best price reasonably available would at least try to capture some of this value.

Nor did negotiations between Van Gorkom and Pritzker give Van Gorkom a reasonable basis for thinking $55 per share was the highest price reasonably available. If anything, those negotiations strongly suggested the opposite, for it was Van Gorkom who first mentioned $55 per share as a price for the Trans Union shares. Now, as Chief Justice (then Vice Chancellor) Strine would later say, it is no breach of a director's *Revlon* duties for the director to be the first to suggest a price for the company to a potential buyer; someone has to be the first to mention a number.[468] But if a seller is to be the first to mention a number, he has to

[466] See the discussion in *supra* note 114.

[467] But see Fischel, *supra* note 338, who argues that the value of the ITC was impounded into the deal price. Fischel, *supra* note 338, at 1449 (stating "[t]he merger at a premium over market price was a method of selling the investment tax credit to an entity that could use it.") In one sense, of course, Fischel is obviously right: since Pritzker and Marmon would get the benefit of the ITCs in exchange for the merger consideration of $55 per share, they were in that sense paying for the ITCs. But that trivial point in no way shows that $55 per share reflected both the present value of Trans Union's future earnings on a standalone basis *plus* the value of the ITCs to the buyer. By Fischel's logic, any price reflecting a premium above market would have reflected the full value of the ITCs, which is absurd.

[468] *In re* Topps Co. S'holders Litig., 926 A.2d 58, 85 (Del. Ch. 2007) (discussing "[a]t some point in the sales dance, someone has to make a move toward specificity").

realize that he is effectively capping the value of the company: he will be very unlikely to ever get more than the price he mentions, at least from the buyer to whom he mentions the price. If the director is to get the best price reasonably available, therefore, the price that he first mentions must be at least as high as his estimate of the highest price any buyer would be likely to pay.[469] He ought not to mention a price that merely seems attractive. As noted above, at the time he suggested the $55 price to Pritzker, Van Gorkom had no reasonable basis for thinking that price was the highest available. Furthermore, when Van Gorkom suggested the $55 per share price to Pritzker, who was universally recognized as one of the sharpest deal-makers in the country (indeed, this was precisely why Van Gorkom wanted to speak with Pritzker), Pritzker almost immediately accepted it, making only one mild attempt to negotiate the price downwards. This strongly suggests that Pritzker regarded the price as low.[470] Hence, if anything, the negotiating history between Van Gorkom and Pritzker, so far from implying that the $55 per share price was the highest available, strongly suggested that it was not.

Putting the question in the language of *Barkan*, when Van Gorkom brought the $55 per share offer to his board of directors, did he have "sufficient knowledge of relevant markets to form the basis for [his] belief" that $55 per share was the best price reasonably available?[471] By his own admission, Van Gorkom did not know how high a price could be obtained in an LBO, and he thus could not know whether a higher price could be obtained from a strategic buyer.[472] He also did not know what value Trans Union's ITCs would have for Pritzker or other potential purchasers, over and above the intrinsic value of Trans Union.[473] Moreover, the history of his negotiations with Pritzker strongly suggested $55 per share was *not* the highest price that

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[469] In *Topps*, when director Greenberg mentioned a price of $10 per share to a potential buyer, other directors objected that the price mentioned *was too high* and would scare off the potential buyer. *Id.* at 69.

[470] *See* Bainbridge, *supra* note 60, at 216 (stating that "Pritzker's quick acceptance of the price suggests that he thought he was getting a bargain, which enhances our questions about the adequacy of the price").

[471] Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1288 (Del. 1989).

[472] *See supra* text accompanying notes 143–44.

[473] *See supra* Section I.A.

could be obtained.[474] Hence, when he brought Pritzker's $55 per share price to the Trans Union board, Van Gorkom clearly did not have sufficient knowledge of relevant markets to reasonably believe that $55 per share was the best price reasonably available for the Trans Union shares.[475] The other directors, who knew nothing of the potential transaction before the meeting,[476] could not know more than Van Gorkom did. Therefore, they too lacked sufficient knowledge of relevant markets to form a reasonable belief that the $55 per share price that Pritzker was offering was the best price reasonably available. Thus, in approving a transaction at that price, the directors breached their *Revlon* duties.

The question thus becomes what the Trans Union directors should have done when Van Gorkom surprised them with Pritzker's offer. To be sure, Pritzker had placed a very short deadline on the offer, but the board was meeting at noon on Saturday, and Pritzker's deadline was sometime late on Sunday evening—more than thirty hours away.[477] At the very least, the directors could have sent Van Gorkom back to Pritzker to attempt to negotiate an increase in the price.[478] They did not do so, nor, apparently, did they even consider doing so, even though Pritzker seems never to have said that $55 per share was his best and final price.[479] The directors also could have sought some kind of

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[474] *See supra* text accompanying notes 125–47.

[475] *See supra* text accompanying notes 125–47.

[476] *See supra* text accompanying notes 129–32.

[477] *See supra* text accompanying notes 130–36.

[478] *See In re* Dollar Thrifty S'holder Litig., 14 A.3d 573, 609 (Del. Ch. 2010) (holding that the board had not breached its *Revlon* duties in part because "[t]hroughout the process, Dollar Thrifty's negotiators consistently pressed for a higher price"); *In re* Smurfit-Stone Container Corp. S'holder Litig. No. 6164-VCP, 2011 WL 2028076, at *18 (Del. Ch. May 20, 2011) (finding that the board had not breached its *Revlon* duties and noting that it "pushed both of the companies that expressed interest in acquiring it to increase the attractiveness of their offers on multiple occasions" and "negotiated two separate price increases" from the ultimate acquirer); *In re* Topps Co. S'holders Litig., 926 A.2d 58, 70, 75 (Del. Ch. 2007) (holding that the board had not breached its fiduciary duties in part because it "voted to continue negotiating with the goal of getting [the acquirer] to increase the price" and because its lead negotiator "was charged with negotiating, and ... twice tried without success to get, a price increase").

[479] *See* Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 238 (Del. 2009) (noting that directors instructed chief executive officer to attempt to negotiate a price

financial analysis or valuation study of the company.[480] As this failure was the second breach of the duty of care by the Trans Union directors the Delaware Supreme Court found,[481] I turn next to this issue.

(ii) The Failure to Obtain a Valuation Study

The Supreme Court held that the Trans Union board breached its duty of care because it failed to inform itself of the intrinsic value of the company, that is, the value of the company as determined by a discounted cash flow or similar financial analysis.[482] In the Delaware Supreme Court's duty of care analysis, the question was whether a valuation study was a material fact reasonably available to the directors. It is hard to argue that it was not.

In economic terms, the question was whether the benefits of having such a study exceeded the costs of obtaining one. Although the cost of engaging an investment banker to produce a valuation study and a fairness opinion would be considerable, contrary to what many commentators have suggested,[483] the court never said

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increase even after buyer had stated that he had already offered his best and final price).

[480] McChesney writes, "All the procedural steps that the court said the board should have undertaken would have required more time than Pritzker's offer allowed, and so the board would have had to reject Pritzker's time-constrained offer at its September 20 meeting." McChesney, *supra* note 340, at 637. As indicated in the text, I do not think the facts support this conclusion; there certainly was time to do at least some of the more important things the majority opinion says ought to have been done, such as attempting to negotiate the price upwards and obtaining at least a rough valuation study; *see also infra* text accompanying note 501.

[481] Smith v. Van Gorkom, 488 A.2d 858, 874 (Del. 1985).

[482] *Id.*

[483] Fischel, *supra* note 338, at 1446, 1453 (referring to "[t]he court's rebuke of the directors for failing to hire outside experts to acquire valuation information" and stating that investment bankers providing fairness opinion "are the biggest winners" in the case). The idea that *Van Gorkom* was a boon to the investment banking industry is widespread, see*, e.g.,* Park McGinty, *The Twilight of Fiduciary Duties: On the Need for Shareholder Self-Help in an Age of Formalistic Proceduralism*, 46 EMORY L.J. 163, 193 n.42 (referring to *Van Gorkom* as the "Investment Bankers' Full Employment Act"); William J. Carney, *Fairness Opinions*, 70 WASH. U.L.Q. 523, 527 (calling the case "the Investment Bankers' Civil Relief Act of 1985"), but apparently quite mistaken. *See* Bowers, *supra* note 104, at 568 (describing empirical study showing that "although target firms' use of fairness opinions did increase immediately following

that the valuation study had to be performed by the company's investment bankers. On the contrary, it expressly referred to the possibility that the analysis might be done by Trans Union's in-house financial personnel.[484] The cost to the corporation of obtaining a valuation study from Romans and his staff would have been virtually zero. Hence, if such a study had any significant value to the corporation in terms of improved decision-making by the directors, it would have been worth having.

As noted above, Van Gorkom later stated that there was "considerable discussion" among the directors at the September 20 meeting about obtaining a valuation study but that no such study "worthy of the name" could be obtained before Pritzker's deadline.[485] This seems clearly wrong. The most obvious type of valuations study to perform, a discounted cash flow analysis, discounts the company's projected future cash flows at various discount rates estimating the company's weighted-average cost of capital to produce an estimate of the value of the company on a standalone basis. On the date of the board meeting to consider the Pritzker offer, the directors already had available to them five-year cash flow projections for the company; indeed, Van Gorkom had used

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the *Van Gorkom* decision, the average frequency of use from 1986 to 1990 (58.2 percent) is not materially different from the 1980 to 1985 period (57.2 percent)" and "there is no significant increase in the portion of revenues earned by financial advisors from fairness opinions in the post–*Van Gorkom* era."); *see also Roundtable*, *supra* note 23, at 37 (2000) (remarks of Henry Lesser to the effect that it is much more likely for an investment banker to be involved in the deal process from the beginning, including in negotiating price, than to merely be brought in at the end of the process to provide a fairness opinion concerning a price already negotiated).

[484] *See Van Gorkom*, 488 A.2d at 876–77; *see also* OWEN, *supra* note 3, at 258 (quoting Chief Justice Herrmann at an oral argument referring to the possibility of having "inside people" perform a financial analysis); Mones, *supra* note 31, at 566–68 (criticizing the court's holding regarding the board's failure to obtain a valuation study); Bowers, *supra* note 104, at 571 (stating "[t]he clarity of the court's statements [that fairness opinions are not legally required] is at odds with the widespread belief that a fairness opinion is required for protection under the business judgment rule" but allowing that the fact *Van Gorkom* can naturally be read as holding that, if the Trans Union board had obtained an outside fairness opinion, it would not have been found liable, may have created an informal requirement); Charles M. Elson, *The Duty of Care, Compensation, and Stock Ownership*, 63 U. CIN. L. REV. 649, 677 (1995).

[485] Van Gorkom, *supra* note 145, at 18; *see also* Fischel, *supra* note 338, at 1446–47 (arguing that the benefits of a valuation study from an investment banker would have been "minimal if not nonexistent").

these very projections in preparing the LBO analysis he presented to Pritzker.[486] The directors also certainly knew Trans Union's own borrowing costs, and Van Gorkom at least knew what interest rates Pritzker was paying to borrow funds to purchase the company.[487] They would thus have had some reliable information about the discount rates to use in a valuation study. Given that this information was ready at hand, Trans Union's in-house financial professionals (or the company's investment banker) could certainly have prepared a discounted cash flow analysis in a matter of hours.[488] Such an analysis would discount the company's projected cash flows at various discount rates to obtain a valuation range for the company on a standalone basis. A more careful study, which would indeed require more time, would improve the model primarily by refining the cash flow projections.[489] In such

[486] OWEN, *supra* note 3, at 45.

[487] Recall that Van Gorkom helped Pritzker arrange financing from Trans Union's own banks. *See Van Gorkom*, 488 A.2d at 867; OWEN, *supra* note 3, at 127.

[488] See Moskin, a leading New York practitioner, who asserts that an investment bank could have produced a reasonably thorough opinion even within Pritzker's deadline. Moskin, *supra* note 402, at 416–18. Moskin and others have detected an inconsistency between *Van Gorkom*, in which the Delaware courts criticized a board for not obtaining a fairness opinion when that opinion would have been prepared in great haste, and cases such as *Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983), and *Joseph v. Shell Oil Co.*, 482 A.2d 335 (Del. Ch. 1984), in which they criticized boards for relying on opinions prepared under such conditions. Moskin, *supra* note 402, at 416–18. But there is surely no inconsistency here: in *Van Gorkom*, haste was required because a third party made an attractive offer with a very short deadline, and the board's choices were a hasty opinion or no opinion, whereas in *Weinberger* and *Shell*, a controlling stockholder unilaterally determined to freeze out the minority stockholders in a quick transaction, which allowed its controlled subsidiary's board only little time to obtain a fairness opinion. In these latter cases, the controlling stockholder, the real defendant, itself chose to shorten the time in which a valuation study could be performed. By contrast, consider the contemporary treatment of freeze-out mergers in *Kahn v. M&F Worldwide Corp.*, 88 A.3d 635 (2014), where, among other conditions, the independent committee at the controlled subsidiary must be allowed to choose and effectively use its own advisors, including financial advisors, before the transaction will be reviewed under the business judgment rule.

[489] *See generally* DAMODARAN, *infra* note 510; TIM KOLLER ET AL., VALUATION: MEASURING AND MANAGING THE VALUES OF COMPANIES (5th ed. 2010). In practice, people use a fairly broad range of discount rates, and so, within reason, no matter how these may be tweaked, the midpoints of the valuation ranges obtained will not vary very much.

cases, if the projections do not change much, neither do the results of the study, and so improving a discounted cash flow analysis will generally produce sharply diminishing returns. In other words, if one starts with detailed cash flow projects, most of the utility of a discounted cash flow analysis will usually be captured in the initial attempt. Therefore, it seems virtually certain that a useful study could readily have been produced prior to Pritzker's deadline. It is obtuse, if not absurd, to say that a discounted cash flow valuation of the company based on the very projections Trans Union had already prepared and that Pritzker was using to value the deal was not worth having. Why should the directors not know at least as much as Pritzker did? There is no good answer to this question. A discounted cash flow study would have been extremely valuable, and it could easily have been obtained.

Now, if the board had sought a discounted cash flow study for the company, what would it have shown? Without management's cash flow projections, it is impossible to say for sure, but we do know that Trans Union's free cash flow in 1980 was about $162 million.[490] We also know that management projections showed that this figure would increase significantly.[491] We know that the prime rate on September 20 was 12.5 percent.[492] Assume conservatively that Trans Union's cost of debt was 14.5 percent and its cost of equity was 22.5 percent (*i.e.*, assume at 8 percent equity risk premium). Trans Union had an unusually high debt/equity ratio for a public company,[493] and assume this ratio was one-to-one. This implies that Trans Union's weighted-average cost of capital (WACC) would be 18.5 percent.[494] Again being conservative, assume that Trans Union's cash flow would increase only 2 percent per year in perpetuity. On these assumptions, Trans Union was worth $982 million on September 20, 1980.[495]

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[490] According to Owen, at all relevant times, Trans Union had outstanding 12,512,956 shares. OWEN, *supra* note 3, at 2.

[491] Owen, *Trans Union*, *supra* note 117, at 25.

[492] OWEN, *supra* note 3, at 128.

[493] Owen, *Trans Union*, *supra* note 117, at 22–23.

[494] That is, (.5)(14.5 percent) + (.5)(22.5 percent) = 18.5 percent.

[495] That is, applying the perpetuity formula, dividing $162 million by (18.5 percent – 2 percent) = $982 million. Naturally, more aggressive assumptions yield an even higher valuation. For example, if we assume at 12.5 percent cost of debt and 3 percent growth in cash flow (holding other assumptions constant), the company was worth $1.2 billion on September 20, 1980.

Indeed, it is difficult to construct an analysis in which the company was worth only the $690 million Pritzker was offering. To get that number, for example, we would have to assume flat cash flows and a discount rate of 23.4 percent. It seems very clear, therefore, that, had the Trans Union board sought a discounted cash flow analysis on September 20, 1980, it would have shown that Trans Union was worth not just more but probably *much more* than Pritzker was offering.[496] In any event, the question of whether the Trans Union board ought to have sought a valuation study on September 20 when Pritzker's deadline was still about thirty hours away is in some ways beside the point. For example, why was Pritzker's deadline treated as sacrosanct? The board could have instructed Van Gorkom to tell Pritzker that the directors were interested in his offer but wanted a few more days to consider it—a request that was surely very reasonable in the circumstances. If Pritzker agreed to extend the deadline, the Trans Union directors could easily have obtained a valuation study and considered the transaction more carefully. If Pritzker steadfastly insisted that he would withdraw the offer on Sunday evening, the Trans Union directors could have decided then what to do next, but at least they would have tried to get more time in which to value the company. Or again, Van Gorkom had known since Monday, September 15, that Pritzker was likely to offer to purchase the company. Why did he not immediately set either some in-house financial professionals or else his investment banker to work on a valuation study? If secrecy was a concern, this

[496] Contrary to what some commentators have suggested, *e.g.,* Julie Andersen Hill & Douglas K. Moll, *The Duty of Care of Bank Directors and Officers*, 68 ALA. L. REV. 965, 984–85 (2016); Charles W. Murdock, *Corporate Corruption and the Complicity of Congress and the Supreme Court—The Tortuous Path from Central Bank to Stoneridge Investment Partners*, 6 BERKELEY BUS. L.J. 131, 147 (2009), even in 1980 it seems that it would have been unusual for a board of directors to approve a sale of the company without some kind of valuation study. Bowers, *supra* note 104, at 568 (reporting that, from 1980 to 1985, 57.2 percent of target firms received an outside fairness opinion, and from 1986 to 1990, 58.2 percent of such firms did). Indeed, at one of the oral arguments in *Van Gorkom*, Chief Justice Herrmann asked counsel for the defendants if he was aware of any case of a public company board of directors approving a sale of the company without seeing some kind of financial analysis or valuation study, and the defendants' counsel could not cite such an instance. OWEN, *supra* note 3, at 257–58.

could have been done without telling the people involved anything about Pritzker or his interest in the company. Had Van Gorkom done this, five days later on September 20, the board could have had a reasonably thorough valuation study before it.

But while the argument that the Trans Union directors should have obtained a valuation study is strong when made in terms of the board's duty of care,[497] it becomes much stronger when we review the board's actions under *Revlon*.[498] As noted above, in *Barkan*, the Supreme Court held that the "crucial element" in finding that a board complied with its *Revlon* duties is "knowledge:" "[i]t must be clear that the board had sufficient knowledge of relevant markets to form the basis for its belief that it acted in

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[497] *Cf.* Sharfman, *supra* note 57, at 301, who concludes that "it is hard to disagree with the *Van Gorkom* court in concluding that the directors of Trans Union were not informed and that they shirked their duties when they approved and recommended the Pritzker buyout." Allen, Jacobs, and Strine think the Trans Union board's "failures of process may well have constituted ordinary negligence … but it is difficult to argue that those failures constituted true gross negligence." Allen, Jacobs & Strine, *supra* note 31, at 458. The authors, however, are equating the gross negligence that defines the duty of care with the extremely lenient rationality test of the substantive portion of the business judgment rule, see *id.* at 457, which the Delaware Supreme Court has identified with the test for corporate waste. *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 28 (Del. 2006). They thus say that that "gross negligence," as they are using the term, "requires a 'devil-may-care' attitude or indifference to duty amounting to recklessness." Allen, Jacobs & Strine, *supra* note 31, at 458. This seems to me to be a mistake. Gross negligence is commonly understood to mean a degree of negligence greater than ordinary negligence but not yet as great as Allen, Jacobs, and Strine have in mind. If negligence is defined as $B < LP$ in the Hand formula, *United States v. Carroll Towing Co.*, 160 F.2d 482 (2d Cir. 1947), then gross negligence is $B << LP$, or, in qualitative terms, a very great risk of a very great loss that can be prevented by a very small expense. In the context of the duty of care, which requires directors to assemble all the material facts reasonably available, gross negligence would thus require a failure to obtain or consider a highly material fact that was very easily and cheaply available. In any case, Allen, Jacobs, and Strine concede that, if the Trans Union directors' actions are reviewed under the enhanced scrutiny standard of *Revlon*, "*Van Gorkom* would not be viewed as remarkable." *Id.* at 459 n.39.

[498] Bainbridge observes that "the gist of the opinion [in *Van Gorkom*] is that a target board must have some credible basis for determining that a proposed merger is in the best interest of the [stock]holders." Bainbridge, *supra* note 60, at 216. In my view, this is more what the court *should* have said than what it actually did say.

the best interests of the [stock]holders," that is, that it obtained for them the best price reasonably available.[499] As the court famously said in that case, "there is no single blueprint that a board must follow to fulfill its duties" under *Revlon*.[500] This is usually taken to mean that there is no particular procedure (*e.g.*, a public auction) that a board *must* follow in order to obtain sufficient knowledge to comply with its *Revlon* duties.[501] It would be more precise, however, to understand this famous holding as meaning that the board must do *something* to obtain the relevant knowledge, albeit any of various things. As *Barkan* and other cases have made clear, a board has many options, including a public auction, a private auction, a pre-signing canvassing of the market, a post-signing canvassing of the market (either passively under a no-shop, or actively under a go-shop), valuation studies from investment bankers or other valuation experts, or perhaps other means. At least pre-signing,[502] the Trans Union board did none of these things and did not even attempt to negotiate upwards the first price offered by the acquirer.

If we ask, as we must under *Revlon*, what basis the Trans Union directors had for thinking that $55 per share was the best price reasonably available, there would seem to be three possible answers: (1) the directors' intuitive judgment about the value of the company was based on their admittedly good grasp of its business and their understanding of economic and financial conditions generally;[503] (2) the large premium to market offered in the Pritzker transaction (the $55 per share price was about 48 percent above the $37.25 closing price of the Trans Union shares the day before the transaction was announced);[504] and (3) the

[499] Barkan v. Amsted Indus. Inc., 567 A.2d 1279, 1288 (Del. 1989).

[500] *Id.* at 1286.

[501] *In re* Talley Indus., Inc. S'holders Litig., No. Civ.A. 15961, 1998 WL 191939, at *10 (Del. Ch. 1998) (quoting *Barkan* 567 A.2d at 1286); Sutton Holding Corp. v. Desoto, Inc., No. 11221, 11222, 1990 WL 13476, at *7 (Del. Ch. Feb. 5, 1990).

[502] *See infra* text accompanying notes 581–82 (discussing Trans Union's post-signing market check, the Supreme Court's treatment of it, and how that market check would be evaluated under *Revlon)*.

[503] Smith v. Van Gorkom, 488 A.2d 858, 877 (Del. 1985); OWEN, *supra* note 3, at 50.

[504] *Van Gorkom*, 488 A.2d at 878; OWEN, *supra* note 3, at 51.

results of the leveraged buyout study that Romans described to the board.[505] As to the first, as the directors urged and as the dissent argued,[506] the Trans Union directors were an extraordinarily well-qualified group of businesspeople and were thoroughly familiar with the business and affairs of Trans Union. We may assume that this is entirely correct.[507] But if a board composed of very talented businesspeople (one may hope all directors of public companies meet this standard) very familiar with the business and affairs of their corporation (something every director should be) could fulfill their *Revlon* duties of having sufficient knowledge of relevant markets to conclude that a given price is the best one reasonably available for the corporation merely by being thus talented and thus informed, then the board's *Revlon* duties would be fulfilled whenever such a board approved a transaction. In other words, there would be *nothing special* directors had to do to fulfill their *Revlon* duties, and if that were right, *Revlon* would come to nothing.[508] When the dissent insisted that the Trans Union directors "knew Trans Union like the back of their hands and were more than well qualified to

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[505] *Van Gorkom*, 488 A.2d at 877; OWEN, *supra* note 3, at 54.

[506] *Van Gorkom*, 488 A.2d at 894.

[507] When we reflect, however, that Van Gorkom had never heard of LBOs until a few days before formulating the transaction and proposing it to Pritzker, we may well wonder just how well he and some of the Trans Union executives grasped many of the relevant factors, *e.g.*, the deterring effect of the stock option on other bidders or the importance of the risk allocations created by financing conditions. Owen never expressly alludes to it, but there may well have been a generational disconnect at play in *Van Gorkom*. Van Gorkom was 63 years old in the fall of 1980. OWEN, *supra* note 3, at 5. His outside directors were 61, 68, 63, 65, and 68. *Id.* at 16–17. Henry Kravis was only 36. *Id.* at 10.

[508] Compare this to Bainbridge, who asks why the board could not "reasonably have determined that the deal Van Gorkom had struck simply was too good to pass up," and concludes that "[t]he short answer seems to be that good resumes will not outweigh a distorted process." Bainbridge, *supra* note 60, at 219*; see also* Fischel, *supra* note 338, at 1446–47 (arguing that because of (a) the outstanding qualifications of the directors, (b) the fact that Van Gorkom as chief executive officer probably knew more about the company than anyone else, and (c) the fact that directors' incentives were aligned with those of the stockholders, the board's decision did not violate the duty of care). Of course, as noted in the text, if general qualifications, intimate knowledge, and proper incentives are enough, breaching *Revlon* is virtually impossible.

make on the spot informed business judgments concerning the affairs of Trans Union including a 100 percent sale of the corporation,"[509] the dissent was not really disagreeing with the majority about the duty of care. It was really opposing the creation of anything like *Revlon* duties—duties that would prohibit the directors from relying merely on their intuitive judgments about the value of the company and require then to engage in some special efforts to ascertain that value before selling the company.[510]

The second possible basis for the Trans Union directors thinking that the $55 per share price was the best price reasonably available was the fact that the price represented an approximately 48 percent premium over the undisturbed market price of the Trans Union shares. The Supreme Court devotes significant effort to showing that the size of the premium was not probative because, on the board's own evidence, the trading prices of Trans Union's shares were depressed due to the ongoing ITC problem, and thus these prices did not "adequately reflect[ ] the true value of the Company."[511] There is both a good deal wrong and a good deal right with the court's argument here.[512] On the one hand, the market price of a company's shares is virtually always far below the result a discounted cash-flow analysis would suggest,[513] which is one reason that acquisitions are generally effected at a substantial premium to market.[514] Delaware courts have recognized this fact, and in valuing companies in appraisal proceedings, the usual procedure of those courts is to add a premium to values based on the market prices of comparable companies but not to values based on discounted cash flow analyses.[515] The *Van Gorkom*

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[509] *Van Gorkom*, 488 A.2d at 895 (McNeilly, J., dissenting).

[510] On the biases from which people suffer in performing valuations and strategies to overcome them, ASWATH DAMODARAN, DAMODARAN ON VALUATION, SECURITY ANALYSIS FOR INVESTMENT AND CORPORATE FINANCE 2–4 (2006).

[511] *Id.* at 875–76; *see also* OWEN, *supra* note 3, at 66–68.

[512] *See* Quillen, *supra* note 28, at 477 (stating "there is no feeling throughout the opinion that the court has grasped the dynamics of the marketplace").

[513] *See* DAMODARAN, *supra* note 510, at 245–46.

[514] *See generally* Booth, *supra* note 441, at 1111; Harrison & Kreps, *supra* note 441, at 323–25; Kraakman, *supra* note 441, at 892; Stout, *supra* note 441, at 1261–63.

[515] *See* Rapid-American Corp. v. Harris, 603 A.2d 796 (Del. 1992); Le Beau v. M.G. Bancorporation, Inc., No. CIV. A. 13414, 1998 WL 44993, at *2 (Del. Ch. Jan. 29, 1998).

court's supposition that the market price, if unaffected by the ITC issue, would be a measure of the intrinsic value of the company as determined by a discounted cash flow analysis is thus likely mistaken. Furthermore, the court's concern that the market price was below the intrinsic value is also misplaced. As indicated above, the market price of a corporation's shares is almost always below its intrinsic value as suggested by a discounted cash flow analysis.[516] If Trans Union's shares were trading below their intrinsic value, this was *not* unusual. Finally, the court's supposition that the board should have considered the premium as a percentage of intrinsic value is also wrong. For, as indicated above, premiums are properly added to values derived from comparable company analyses, which measure relative values, not discounted cash flow analyses, which measure intrinsic value.[517]

But for all it gets wrong on this issue, the Supreme Court's analysis nevertheless suggests a more compelling point. In *Revlon* terms, if the Trans Union directors were relying on the significant premium to market as a factor in showing that they had obtained the best price reasonably available, they would have to be able to show something more than that the price was at a large premium to market. In particular, the directors would need to discern in the premium a reasonable basis for thinking that $55 per share was the best price reasonably available. When relying on premiums, the usual way of doing this is to

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[516] *See supra* text accompanying notes 513–14.

[517] The question of which acquisitions are effected at such large premiums to market is still subject to debate. *See* cases cited in *supra* notes 449, 515. In my view, acquisition premiums are best explained in financial models that allow for market participants to have heterogeneous expectations. In such models, people will disagree about the future value of the company, and so the demand curve for the company's shares will be downwardly sloping. Some people will be willing to pay more for the shares than other people will. The shares will, thus, naturally migrate into the hands of people who value the shares more highly, and the observed market price will be the equilibrium price between willing buyers and sellers. In such models, in order to acquire, say, 90 percent, of the shares, an acquirer must pay a price at least equal to the value assigned to the shares by holders of ninety percent of those shares, which will always be a price above the observed market price—usually, it seems, substantially above that price. *See also* Bainbridge, *supra* note 60, at 213 (criticizing the court's analysis of the control premium by distinguishing the ordinary market for the company's shares and the market for corporate control).

study comparable transactions and determine how the premium in the transaction under consideration compares to premiums paid by other acquirers in other transactions—a so-called comparable transaction study.[518] Of course, the Trans Union board did not do this. Just as it relied on its intuitive judgment that $55 per share was an attractive price for the company, so too did it rely on its intuitive judgment that a 48 percent premium was an attractive premium.[519] The directors' undoubted business acumen and familiarity with Trans Union would be of no avail in showing that they knew what size premiums had recently been paid in acquisitions of companies comparable to Trans Union. Just as the Trans Union directors could have had the company's in-house financial professionals perform a discounted cash flow study before Pritzker's deadline on the following evening, so too could they have had the company's investment banker perform an elementary comparable transaction study before that deadline.

Finally, the Trans Union directors could argue that they had some knowledge about the intrinsic value of the company because Romans, the company's chief financial officer, had spoken briefly at the meeting about leveraged buy-out studies that he had conducted.[520] As the court indicated, Romans told the board that, in his opinion, the $55 per share price was within the range of fair prices for the company, albeit at the bottom of that range.[521] The court notes that, after hearing this, no director requested any details about the study, inquired about the circumstances under which it was undertaken, or asked why Romans put $55 at the bottom of the range.[522] Had they done so,

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[518] *See* DAMODARAN, *supra* note 510, at 38–43; MCKINSEY & CO., VALUATION: MEASURING AND MANAGING THE VALUE OF COMPANIES 331–33 (6th ed. 2015). Delaware courts have considered such studies in appraisal cases. *See, e.g.*, *Le Beau*, 1998 WL 44993, at *7–8.

[519] *But see* McChesney, *supra* note 340, at 638 n.34 (stating that the almost 50 percent premium offered in the Pritzker transaction was "very much on the high side of takeover premiums generally during this period") (citing Gregg A. Jarrell, *The Market for Corporate Control: The Empirical Evidence Since 1980*, 2 J. ECON. PERSP. 49, 51 (1988), for the proposition that "from 1980 to 1985 the average premium was 30 [percent]").

[520] *See supra* note 132 and accompanying text.

[521] Smith v. Van Gorkom, 488 A.2d 858, 869 (Del. 1985).

[522] *Id.* at 877.

Romans "presumably would have responded as he testified: that his calculations were rough and preliminary; and, that the study was not designed to determine the fair value of the Company, but rather to assess the feasibility of a leveraged buy-out financed by the Company's projected cash flow."[523] The court says all this with an eye to the duty of care it was imposing on the Trans Union directors: by not asking these questions, they were failing to obtain material facts reasonably available to them. It is hard to argue with this, but once again, in light of *Revlon* and subsequent cases, we can see that there is much more wrong here than the board's failure to inquire about these matters. That is, even if the board had been fully informed about the details of the study Romans had conducted, the board's relying on that study to determine the best price reasonably available would raise serious concerns under *Revlon*.

For one thing, as the Supreme Court intimated,[524] and as the Court of Chancery held in *Dell*,[525] the value obtainable in a leveraged buy-out—and thus the value returned by a leveraged buy-out study—measures the price an acquirer using a leveraged buy-out structure can pay and still make the level of return such acquirers typically demand.[526] Such values are generally below those returned by discounted cash flow analyses, and thus may well be thought to be below the intrinsic value of the company.[527]

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[523] *Id.*

[524] Quillen suggests that the understanding of the Supreme Court in *Van Gorkom* was hardly so sophisticated. "At some points" in the court's opinion, he writes, "one gets the feeling that a feasible leveraged buy-out does not even qualify as one measure of price." Quillen, *supra* note 28, at 477.

[525] *In re* Appraisal of Dell Inc., No. 9322-VCL, 2015 WL 4313206, at *25 (Del. Ch. July 13, 2015).

[526] *Id.* at *8–9.

[527] This was precisely the result reached in *Dell*. *Id.* at *25. The criticisms of *Dell* (and there have been many) are quite telling here: those who fault Vice Chancellor Laster's analysis in *Dell* do not dispute that an LBO analysis will usually return a lower range of values for a company than a discounted cash flow analysis. Their argument is that a thorough market check showed that there was no buyer willing to pay more than the price the board obtained in the transaction. *See, e.g.*, Martin Lipton, Memorandum, *Some Thoughts for Boards of Directors in 2008*, WACHTELL, LIPTON, ROSEN & KATZ, at *4 (Dec. 6, 2007), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1090970 [http://perma.cc/4DWA-HNJL]. To this, the Vice Chancellor can respond that, although

For another, the price for the company obtainable in a leveraged buy-out is relevant only with respect to acquirers who would use that structure; it is not relevant to other kinds of purchases, such as strategic buyers, who typically would not use that structure. Hence, if the directors had seen Romans's leveraged buy-out study in full, it, at best, would have informed them about the highest price reasonably available *in a leveraged buy-out*, not the highest price reasonably available *simpliciter*. In this regard, it is worth noting that in *Netsmart,* Chief Justice (then–Vice Chancellor) Strine held that the Netsmart board likely breached its *Revlon* duties because, in selling the company, it marketed the company only to financial buyers and merely assumed, on the basis of very little evidence, that there would be no strategic buyers for the company.[528] By analogy, it would seem that a valuation study that considered only the prices a financial buyer (or similar acquirer like Pritzker) could pay, but not how much a strategic buyer could pay, could not provide a reasonable basis for the directors to form an opinion about the intrinsic value of the company under *Revlon*.[529]

(iii) The Obvious Overarching Revlon *Problem*

Overshadowing all such questions, however, is one obvious and fundamental problem with the board's decision to approve the original merger agreement with Pritzker on September 20,[530] which goes to the very nature of the sales process. Under Delaware

no one was willing to pay more for the company, nevertheless, if the price obtained in the LBO was below the value of the company on a standalone basis, the dissenting stockholders were harmed by being required to take the LBO price. The response to this, presumably, would be that, in the particular circumstances of *Dell*, we would have to distinguish the projected future of the company on a standalone basis *as a public company* and *as a private company*, and because the latter future was not available to the public stockholders, it was irrelevant. Only if the value of the company on a standalone basis as a public company exceeded the deal price were the dissenting stockholders harmed by being required to take that price.

[528] *In re* Netsmart Tech., Inc. S'holders Litig., 924 A.2d 171, 199 (Del. Ch. 2007).

[529] See *supra* note 473 concerning Van Gorkom's reasons for thinking that a public company-strategic acquirer would not be interested in purchasing Trans Union.

[530] *See supra* note 147 and accompanying text.

law, "the board of directors has the ultimate responsibility for managing the business and affairs of a corporation," and "[t]his unremitting obligation extends equally to board conduct in a sale of corporate control."[531] Therefore, in selling the company in a change-of-control transaction, the *board of directors* has a duty under *Revlon* to get the best price reasonably available for the stockholders,[532] and it may not abdicate this duty in favor of any other party, even the company's chairman and chief executive officer.[533] In *Van Gorkom*, the chief executive officer, without even consulting the board or even his fellow officers (other than Peterson, whom he asked to run some numbers on possible LBO scenarios), decided to start the process of selling the company.[534] Of the usual means of price discovery in such cases (financial analysis, market checks, and negotiating over price), Van Gorkom used none.[535] Rather, he determined that the price offered was desirable for the stockholders generally because he personally found the price attractive.[536] He then obtained an offer from Pritzker, agreed with him on deal-protection devices,

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[531] Mills Acquisition Co. v. MacMillan, 559 A.2d 1261, 1280 (Del. 1989).

[532] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

[533] *Mills Acquisition, Inc.*, 559 A.2d at 1280 (criticizing the board for being "torpid, if not supine, in its efforts to establish a truly independent auction"); *see also* Bainbridge, *supra* note 60, at 218 (arguing the court "concluded that the Trans Union board had abdicated its role as a deliberative, decision-making body"); Macey, *supra* note 57, at 609 (arguing "a more plausible justification for the court's decision was the board's inappropriate reliance on Van Gorkom's judgment and negotiating" because the board "delegated too much power to Van Gorkom in his negotiations with the acquirer" and "did not properly monitor Van Gorkom's negotiations with the acquirer"); Stephen A. Radin, 'Smith v. Van Gorkom' *on its 15th Anniversary*, 24 DIRECTORS & BOARDS 24, 26–27 (2000) (stating, "[a]ssuming the facts in *Van Gorkom* to be as stated in the majority's opinion, the Trans Union directors' sale of their [stock]holders' company for $700 million, solely on the basis of a two-hour meeting without any prior agenda notice and without any particularized study regarding value, was an egregiously inadequate exercise of the directors' responsibilities.").

[534] Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985); *see also* Macey, *supra* note 57, at 613 (stating that Van Gorkom "ignored the fundamental tenet of corporate law" that "the business and affairs of the corporation are to be run by or under the direction of the board of directors" by "unilaterally negotiating the sale of Trans Union without the involvement of the board").

[535] *See Van Gorkom*, 488 A.2d at 858.

[536] For a discussion of how Van Gorkom's incentives may have differed from those of stockholders, see *supra* notes 113, 473.

helped him arrange financing, and negotiated a definitive merger agreement. Only at that point did Van Gorkom surprise his board with a fully negotiated transaction.[537] Regardless of what happened at the board meeting of September 20, Trans Union's sale process was already terribly, probably fatally, compromised for the simple reason that *the board had not been involved at all* prior that point.[538]

At the September 20 board meeting, whatever else they did, the directors did not at that meeting do the one thing *Revlon* required of them: they did not take reasonable steps to determine whether $55 per share was the best price reasonably available for the company. Their discussion did not include any meaningful discussion of the intrinsic value of the company.[539] When the directors decided to accept this offer and approve the merger agreement, the problem was not so much that they did not have all the material information about the offer reasonably available. The problem was that, because of the nature of the process up to that point, the directors had done literally nothing to obtain the best price reasonably available and they had virtually no basis for thinking that the price Pritzker was offering was the best price.[540]

Van Gorkom later defended the board's decision on September 20 saying that "the $55 offer, while conceivably not the

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[537] *See supra* text accompanying notes 127–31; *see also* Macey, *supra* note 57, at 614 (arguing that by not involving or even informing the board of his sales process with Pritzker until the very last minute, when the merger agreement was already negotiated, Van Gorkom "maneuvered the board into a position from which it was virtually impossible to exercise its fiduciary duty of care.").

[538] OWEN, *supra* note 3, at 70, Owen reports that one board member expressed surprise that Van Gorkom had undertaken to sell the company essentially on his own. *Id.* One assumes that this individual must have been one of the outside directors. It is a mystery why, in even 1980, the other directors did not object as well.

[539] *See Roundtable*, *supra* note 23, at 32 (quoting Ty Sagalow's statement that "[w]e are not dealing with an inadequate examination of intrinsic value. We are dealing with *no* examination of intrinsic value") (emphasis in original).

[540] *See Van Gorkom*, 488 A.2d at 866 (stating that "the record is devoid of any competent evidence that $55 represented the per share intrinsic value of the Company"); *see also* Bainbridge, *supra* note 60, at 214 (stating that "the real issue, which is not well-framed in the majority opinion, is what the firm is worth to Pritzker, and, accordingly, whether the board of directors did a good job in capturing that value on behalf of the [stock]holders").

best obtainable, was too good to be allowed to expire without any opportunity for the stockholders to consider it."[541] Previously, as noted above, taking the offer and allowing it to expire were not the only options available to the Trans Union board. The board could have asked Pritzker for more time. The board and Trans Union's managers, perhaps with its financial advisor, could have worked through the weekend to evaluate the offer more carefully before the deadline.[542] The board could have sent Van Gorkom back to Pritzker to negotiate the price upwards. Instead, the directors acted if they had to decide immediately, at meeting early on September 20, either to accept the offer or reject it, and that was not true. There was not much time for more consideration of the offer, but there was enough for significantly more consideration than the directors chose to give it. In a world of diminishing returns, those few hours would have been the most valuable ones, and the Trans Union directors elected not to use even the little time they had. On September 20, the directors had done virtually nothing to maximize company's value at a sale for the stockholders' benefit, and they had virtually no reason to think that $55 per share was the best offer reasonably available. They then chose not to find out even what more they could have known before deciding to accept Pritzker's offer.[543]

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[541] Van Gorkom, *supra* note 145, at 18.

[542] *See Roundtable*, *supra* note 23, at 38 (Boris Yavitz stating that "you could recess the meeting, get two investment bankers in ... and have them push numbers all night, and then have them address the meeting with the directors … [a]nd by Sunday midnight or Monday at 6 a.m. you could have a signed agreement"); Moskin, *supra* note 402, at 418 (speculating that, if the board had sought and failed to obtain from Pritzker an extension of the deadline, worked with its financial advisor overnight, reconvened the next day, and approved the deal after receiving favorable advice from its banker, the result in the case would have been different).

[543] Van Gorkom, *supra* note 145, at 18 (defending the board's approval on September 20 on the basis of the post-signing market check); *see also Roundtable*, *supra* note 23, at 39 (Henry Lesser stating that the directors "thought that somehow (a) the merger agreement entitled them to go out and shake the trees and see what fell off; (b) it entitled them to accept something better if it fell off the tree; and (c) somehow the publicity was going to indicate that. They thought that that would all happen, like on autopilot, and they could go home safe in the knowledge that they had done right by the stockholders. They were, unfortunately, mistaken and misguided because there was no follow-through").

Why did the directors do this? The answer is shocking by contemporary standards but perfectly straightforward. As Van Gorkom later explained, at the September 20 meeting, "The directors did *not* decide that $55 was a fair price at which to sell the company," much less that it was the best price reasonably available.[544] Rather, "all the directors decided was that the offer was too good to be allowed to expire without giving the stockholders a shot at it,"[545] and this "limited decision" by the board "did not constitute approval by the directors of $55 as the sale price."[546] As recounted above, Van Gorkom sincerely believed he and the other directors had a duty to do what was best for the stockholders. Nevertheless, he clearly did *not* believe that a board should approve a sale of the company only if it believes that the price offered is the best one reasonably available.[547] Put anachronistically, Van Gorkom did not believe in *Revlon* duties. Quite the contrary, he believed that, sometimes, a board had a duty to approve a sale of the company even if it was not satisfied that the price offered was the highest price reasonably available. The problem with Van Gorkom's view, however, is that, although approving the merger agreement did in effect give the stockholders an option to sell the company to Pritzker at $55 per share, this option was not obtained for free. It came at a cost. Part of that cost came in the form of diminished opportunities to sell the company at a higher price arising from the difficulties that the existence of the first deal, including Pritzker's stock option, created

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[544] Van Gorkom, *supra* note 145, at 19.

[545] *Id.* The majority opinion alludes to this argument in *Van Gorkom,* (stating, "[c]ertainly in the merger context, a director may not abdicate [his or her duty under Section 251 to make an informed judgment about the advisability of the merger] by leaving to the [stock]holders alone the decision to approve or disapprove the agreement."). *Van Gorkom*, 488 A.2d at 873.

[546] *Id.*

[547] *See Roundtable*, *supra* note 23, at 39 (Donald J. Gogol, stating, "[u]nless a deal is wildly mispriced or the company represents a unique strategic asset, it is unlikely that an interloper is going to come in very quickly against a board-recommended deal," and Robert Friedman, stating, "[t]hat is an important point the board should have known. When you sign a merger agreement, with or without a 'fiduciary out,' that has a chilling effect on other bidders coming in. A board has a greater responsibility to make sure that it gets the best price and not rely on what happens after the merger agreement has been executed.").

for other bidders. Another part came in the form of losing the opportunity to remain independent—a real cost if it turned out that the intrinsic value of the company exceeded the deal price.[548] The question, therefore, was not whether the put obtained in the merger agreement with Pritzker was valuable (it was obviously very valuable); the question was whether it was worth the cost. Since they seem not to have realized that accepting Pritzker's offer came with costs, or at least how great these costs might be, Van Gorkom and his fellow Trans Union directors seem never to have considered that question.[549] This brings us naturally to the next question, which is the effect of the Pritzker stock option as a deal protection device.

(2) The Pritzker Stock Option as a Deal Protection Device[550]

The original merger agreement that the Trans Union board approved at the September 20 meeting included a stock option in favor of Pritzker, exercisable when his financing condition was fulfilled or waived, that entitled him to purchase one million shares of Trans Union common stock for $38 per share. This was $0.75 above the shares' closing market price of $37.25 on the day before the transaction was announced.[551] The Supreme Court does not discuss the stock option in detail, but it does suggest that it may have deterred other bids.[552] As noted above, although there was similar speculation among some Trans Union insiders,[553] in fact none of the potential buyers approached

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[548] *See, e.g.*, Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48 (Del. Ch. 2011).

[549] McChesney, *supra* note 340, considers this issue at length, albeit ignoring the third option discussed *supra* in the text of considering the Pritzker option more closely before deciding whether to accept it.

[550] On the deal protection issues raised by Van Gorkom, see generally R. Franklin Balotti & A. Gilchrist Sparks, *Deal Protection Measures and the Merger Recommendation*, 96 NW. U.L. REV. 467 (2002).

[551] Smith v. Van Gorkom, 488 A.2d 858, 867 (Del. 1985); OWEN, *supra* note 3, at 52.

[552] *Van Gorkom*, 488 A.2d at 876. On the deterrent effect, or lack thereof, of such options, see Ian Ayres, *Analyzing Stock Lock-Ups: Do Target Treasury Sales Foreclose or Facilitate Takeover Auctions?* 90 COLUM. L. REV. 682, 705 n.61 (1990).

[553] OWEN, *supra* note 3, at 117–19.

by Trans Union during the subsequent go-shop period mentioned the Pritzker stock-option as an impediment to the formulation of an offer.[554]

How would the option be treated under current law? Under such cases as *QVC*, the stock option would be a deal protection device reviewed under *Unocal*, and nowadays it is generally settled law that such devices will be found to be reasonable if their value is a sufficiently small fraction of the value of the transaction.[555] Pritzker's option allowed him to profit on the spread between any superior bid and the strike price of $38 per share on one million shares. As explained above, KKR eventually offered to purchase Trans Union for $60 per share.[556] At that price, Pritzker's option was worth about $22 million, which would have been about 3.2 percent of the value of $690 million of his offer for Trans Union and 2.9 percent of the value of the $750 million of KKR's offer.[557] Under current market conditions, a 3 percent termination fee is well within the customary range for a deal of this size,[558] and Delaware courts routinely uphold 3 percent termination

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[554] *Id.* at 121.

[555] Paramount Commc'ns Inc. v. QVC Network, Inc., 637 A.2d 34, 43–45 (Del. 1993); Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 958–59 (Del. 1985).

[556] *See supra* text accompanying note 233.

[557] According to Owen, at all relevant times, Trans Union had 12,512,956 outstanding shares. OWEN, *supra* note 3, at 2. Hence, Pritzker's $55 per share offer valued the company at about $688 million, and KKR's $60 per share offer valued the company, without giving effect to Pritzker's option, at about $751 million. If Pritzker exercised his option, the number of outstanding shares would increase by one million and the value of the company would increase by $38 million, the purchase price Pritzker would have to pay to exercise the option. Hence, if Pritzker exercised the option and KKR acquired the company at $60 per share, KKR would have to pay in total about $811 million ($60 per share times 13,512,956 shares), but on completion of the transaction would recover the $38 million exercise price of the option, thus reducing the effective cost to KKR to $773 million—an increase of $22 million due to the Pritzker option. Conversely, Pritzker's profit on the option would be $60 – $38 = $22 per share on one million shares or $22 million. This amount is about 3.2 percent of the $690 million Pritzker was paying for the company and about 2.9 percent of the $751 million KKR would have had to pay to buy the company at $60 per share in the absence of Pritzker's option. Owen's computations about the value of the option are similar. *Id.* at 120.

[558] *See* Harrison & Kreps, *supra* note 441, at 323, 325–26; Kling et al., *supra* note 149, at 782.

fees under *Unocal*.[559] At these levels, the option would, at least in isolation from other aspects of the transaction, be found reasonable, and the board's decision to approve it was not in violation of its fiduciary duties under *Unocal*.[560]

(3) The No-Shop Market Test and the Go-Shop Market Test

As explained above, at the September 20 meeting at which the Trans Union directors originally approved the merger agreement, they required[561] that the draft agreement be amended to allow Trans Union what would now be thought of as a standard no-shop provision and fiduciary out—that is, to allow Trans Union to entertain unsolicited superior offers from other bidders pending the closing of the merger, to share with such bidders confidential information about the company,[562] and to terminate

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[559] *See, e.g.*, *In re* Cogent, Inc. S'holder Litig., 7 A.3d 87 (Del. Ch. 2010) (3 percent termination fee did not violate *Unocal*); *In re* MONY Group, Inc. S'holder Litig., 852 A.2d 9 (Del. Ch. 2004) (3.3 percent termination fee); *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975 (Del. Ch. 2005 (3.75 percent); *In re* Topps Co. S'holder Litig., 926 A.2d 58 (Del. Ch. 2007) (4.3 percent); *In re* Dollar Thrifty S'holder Litig. 14 A.3d 573, 614 (Del Ch. 2010) (3.9 percent and referring to a 3 percent termination fee as "standard"); *In re* Pennaco Energy, Inc., S'holders Litig., 787 A.2d 691, 707 (stating that a 3 percent termination fee was "modest and reasonable"); McMillan v. Intercargo Corp., 768 A.2d 492, 505–06 n.61 (Del. Ch. 2000) (3.5 percent termination fee was within the reasonable range).

[560] The analysis in the text treats Pritzker's stock option as if it were a cash termination fee. Of course, it was not, and its value would have varied with the price of an overtopping offer. *See QVC*, 637 A.2d at 38–41 (discussing how the value of Viacom's stock option varied with the price of competing bids for Paramount). Its deterrent effect thus increased with the amount of the overtop. Furthermore, Pritzker's option may have made a pooling accounting treatment impossible for other purchasers.

[561] Smith v. Van Gorkom, 488 A.2d 858, 869 (Del. 1985). Although the Delaware Supreme Court was somewhat skeptical, Owen accepts that the board did indeed condition its approval of the merger in these ways. OWEN, *supra* note 3, at 294–95.

[562] Making information about the company available to all bidders on equal terms is, absent special circumstances, required by *Revlon*. *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 184 (Del. 1986) (stating that, in general, bidders must be given equal access to financial data about the company because "directors cannot fulfill their enhanced ... duties by playing favorites with the contending factions," and "[m]arket forces must

the merger agreement before closing in order to accept a superior bid.[563] Of course, these provisions made the merger agreement more favorable to Trans Union, and they are nowadays standard deal protection devices so common that they are no longer challenged under *Unocal*.[564]

The relevance of the Trans Union board's conditioning its approval on the inclusion of the no-shop and fiduciary out is unclear under the Delaware Supreme Court's duty of care analysis. That is, whether the merger agreement as executed actually included the changes the Trans Union board wanted, or if it did, to what extent these changes benefited the Trans Union stockholders, seems quite irrelevant to the question of whether the Trans Union directors had all the material information about the transaction reasonably available when they approved the merger agreement. When we shift to a *Revlon* analysis, however, the relevance of these changes is obvious. Under *Barkan*, one way for a board to acquire sufficient knowledge of market conditions to allow it to reasonably conclude that it is getting the best price reasonably available is to canvas the market.[565] Although a passive market check performed after a deal is signed may in general be the least effective kind of market check, it certainly has some value under *Revlon*. This is particularly true for a company like Trans Union, which was a Fortune 500 company[566] widely followed by securities analysts: the announcement of Trans Union's agreement with Pritzker made national news,[567] and Delaware courts have recognized in *Revlon* cases that mergers-and-acquisitions professionals are hardly shy and retiring types, but can generally be counted upon to make unsolicited offers for

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be allowed to operate freely to bring the target's [stock]holders the best price available for their equity.").

[563] *See supra* Section I.A.

[564] *See* McMillan v. Intercargo Corp., 768 A.2d 492, 498–99 (Del. Ch. 2000); Ace Ltd. v. Capital Re Corp., 747 A.2d 95, 105 (Del. Ch. 1999).

[565] Barkan v. Amsted Indus., Inc., 567 A.2d 1279, 1287 (Del. 1989).

[566] OWEN, *supra* note 3, at 3.

[567] *E.g.*, John C. Boland, *Winners & Losers: Silver and Gold Issues Led Market in September; Sunshine Spurts 75 percent*, BARRON'S NAT. BUS. & FIN. WKLY., Oct. 6, 1980, at 33, 48; *Pritzker Concern Plans Acquisition of Trans Union*, WALL ST. J., Sept. 23, 1980, at 2; *The Latest Pritzker Bid is the Most Ambitious*, BUSINESSWEEK, Oct. 6, 1980, at 38, 40; Joseph Winski, *Marmon Buying Trans Union for $688 Million in Cash*, CHI. TRIBUNE, Sept. 23, 1980, at C1, C5.

companies who have announced transactions, if such professionals perceive a reasonable opportunity for profit.[568] And, in fact, Van Gorkom and the Trans Union directors generally were counting on the publicity surrounding the announcement of the transaction with Pritzker to generate other offers for the company, if there were credible buyers who were interested in paying more than $55 per share for Trans Union.[569] Indeed, Pritzker himself was worried from the beginning that Marmon would end up as a stalking horse,[570] and this is why he demanded compensation in the form of the stock option should his bid for Trans Union be overtopped.[571]

This brings us to the question of whether the merger agreement as executed actually contained a no-shop with a fiduciary out. The question is vexed for several reasons. First, as noted above, the language in the merger agreement supposedly embodying the fiduciary out was at best cryptic, providing only that, although the Trans Union board would (1) call a stockholder meeting to consider the merger, (2) recommend that the stockholders adopt the merger agreement, and (3) use its best efforts to obtain the requisite vote, nevertheless the acquirer "acknowledge[d] that the Trans Union directors may have a competing fiduciary obligation to the stockholders under certain circumstances."[572] As noted above, this language would seem to allow the Trans Union board to decline to do the things specified if the board

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[568] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 185 (Del. 1986).

[569] OWEN, *supra* note 3, at 73–74. Owen quotes Van Gorkom as saying, "I knew that the minute this announcement was made that the Pritzker family was willing to pay $55 a share in cash for all of our stock, that every M&A man ... in every investment banking firm throughout the country would immediately go to his book and start looking at Trans Union." *Id.* The people who work in mergers-and-acquisitions, Van Gorkom thought, are "the least bashful people in the investment business" and would not refrain from making unsolicited offers for Trans Union. *Id*. at 73.

[570] Smith v. Van Gorkom, 488 A.2d 858, 866 (Del. 1985).

[571] Pritzker later testified that he "assumed that all investment banking firms would have their pencils out Monday morning, and start to approach their customers to see whether they could interest them in making an offer." OWEN, *supra* note 3, at 74.

[572] *Van Gorkom*, 488 A.2d at 879; *see also id.* at 895 (McNeilly, J. dissenting); OWEN, *supra* note 3, at 76.

determined that its fiduciary duties so required, not to terminate the merger agreement in order to accept a superior proposal.[573]

Nevertheless, it is unclear how important this right to terminate the agreement really was. If a superior proposal for the company emerged, then any stockholder meeting considering the Pritzker proposal would likely defeat it (regardless of whether the Trans Union directors were recommending the transaction or not),[574] and at that point the merger agreement with Pritzker would presumably have to be terminated in accordance with its terms, which would leave Trans Union free to accept the superior proposal. More importantly, whatever the exact restrictions or lack thereof on Trans Union in the original merger agreement, that agreement was amended on October 10, less than three weeks after the original agreement was executed.[575] There was thus not enough time to determine the effectiveness of a passive market check conducted under the no-shop. For all practical purposes, it was under the agreement as amended that Trans Union performed whatever market check it did.

Under the amended agreement, from October 10 until February 10, Trans Union was permitted to solicit other offers for the company.[576] It had, in other words, a four-month go-shop period.[577] To this end, Trans Union engaged Salomon Brothers to market the company,[578] and Salomon approached about 150

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[573] *See supra* text accompanying note 157.

[574] For example, in the Time-Warner transaction, the Time board was certain that the Time stockholders would vote down the merger with Warner even though the Time board was recommending the merger because Paramount had launched a tender offer for the Time shares at a very attractive price conditioned on the Time stockholders rejecting the merger with Warner. *See* Paramount Commc'ns, Inc. v. Time Inc., 571 A.2d 1140, 1147–48 (Del. 1990).

[575] *Van Gorkom*, 488 A.2d at 870.

[576] *Id.* at 883.

[577] Guhan Subramanian, *Go-Shops vs. No-Shops in Private Equity Deals: Evidence and Implications*, 63 BUS. LAW. 729, 735–36 (2008). On go-shops generally, see *id.* at 730, and Christina M. Sautter, *Shopping During Extended Store Hours: From No Shops to Go-Shops: The Development, Effectiveness, and Implications of Go-Shop Provisions in Change of Control Transactions*, 73 BROOK. L. REV. 525, 530–31 (2008).

[578] *See* Van Gorkom, *supra* note 145, at 18 (describing Salomon Brothers' efforts in the go-shop and noting that the firm would have been entitled to a $2.6 million success fee if it secured an offer of $56 per share and a larger fee if the offer were higher).

potential purchasers. Borg Warner, Bendix, GECC, and Genstar (in addition to KKR, of course) all conducted due diligence.[579] Of course, the Delaware Supreme Court made much of the fact that, to exercise the fiduciary out and terminate the agreement, Trans Union was required, prior to February 10, either to consummate a merger (or similar transaction) with another bidder or enter into a definitive agreement related to such a transaction that was superior to the Pritzker offer and subject only to stockholder approval (*i.e.*, contained no financing condition and no condition related to regulatory or antitrust approvals).[580] As noted above, contemporary fiduciary outs virtually always involve significantly shorter periods but are based on the target company receiving a superior offer, not on its entering into a superior definitive agreement,[581] which makes comparisons to the go-shop in the Pritzker–Trans Union agreement difficult. Perhaps in the Pritzker–Trans Union transaction, the exceptionally long four-month go-shop period may have made executing a definitive agreement reasonably possible. However this may be, since the Trans Union board neither conducted any pre-signing market check nor considered any financial analysis concerning the value of the company pre-signing, the post-signing market check under the go-shop would form virtually the entire factual basis for the board's ultimate conclusion that the $55 per share price offered by the Pritzkers was the best price reasonably available. Since the requirements of the go-shop would be far off market terms today in ways that undoubtedly reduced the effectiveness of the go-shop, it is possible to imagine the Court of Chancery holding that the provisions in the revised merger agreement requiring Trans Union to obtain a definitive agreement (indeed, one not conditioned even on obtaining regulatory approvals) before exercising the fiduciary out, were unenforceable as an

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[579] OWEN, *supra* note 3, at 188 (mentioning Borg Warner and Bendix); *id.* at 190 (mentioning Genstar).

[580] *Van Gorkom*, 488 A.2d at 883–84.

[581] Hence, some go-shops allow the company to formalize a list of parties who expressed interest in acquiring the company during the go-shop period and to continue to negotiate with them after the expiration of the go-shop period and until the requisite stockholder approvals have been attained. Subramanian, *supra* note 577, at 735; *see also In re* Topps Co. S'holders Litig., 926 A.2d 58, 72 (Del. Ch. 2007).

unreasonable deal protection device under *Unocal*.[582] Even if the conditions on the go-shop were consistent with *Unocal*, however, it remains a separate question whether the market test conducted under the go-shop was sufficient to allow the board to fulfill its *Revlon* duties by reasonably concluding that the $55 per share price from Pritzker was the best price reasonably available.[583]

Perhaps the best way to answer this question is to observe that in the more than thirty years since *Revlon*, other than to require additional disclosure to the stockholders prior to a meeting to consider the merger, the Delaware courts have never enjoined a transaction because the board had violated its *Revlon* duties,[584] except when there had emerged another bidder who

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[582] There is no direct precedent, but consider *ACE Ltd. v. Capital Re Corp.*, 747 A.2d 95, 106 (Del. Ch. 1999) (holding that a fiduciary out conditioned on the board receiving a legal opinion that its fiduciary duties required it to negotiate with a potential topping bidder was unenforceable) and *Omnicare, Inc. v. NCS Healthcare, Inc.*, 818 A.2d 914, 939 (Del. 2003) (holding that the board of directors "was required to contract for an effective fiduciary out clause to exercise its continuing fiduciary responsibilities" to the stockholders).

[583] Allen, Jacobs & Strine, *supra* note 31, at 459 n.39, assert, without further analysis, that "the broad market check conducted by the board in *Van Gorkom* would have satisfied its *Revlon* duties" as construed in *Barkan*. It is certainly correct that the market check was thorough in the sense that it lasted for a long time and the company or its financial advisors approached all or virtually all potential buyers of the company. Whether given the other considerations mentioned in the text, such as the requirement for a definitive agreement not conditioned on financing or regulatory approvals and the sharply increasing interest rate environment, the market check was truly effective, however, is less clear. Allen, Jacobs, and Strine never allude to any of these other considerations.

[584] There is perhaps one limited exception to this. In *C&J Energy Services, Inc. v. City of Miami General Employee's,* the Court of Chancery enjoined the transaction, but the Supreme Court quickly reversed and allowed the transaction to proceed. 107 A.3d 1049, 1071 (Del. 2014) (reversing the Order Granting Preliminary Injunction, No. 9980-VCN, 2014 WL 6696435, at *1 (Del. Ch. Nov. 25, 2014)). There are also cases in which, when no other bidders had emerged for the company, the Court of Chancery found it was likely that a plaintiff stockholder would prevail on the merits of its claim that the directors had breached their *Revlon* duties, but nevertheless, declined to issue an injunction on other grounds—generally, the grounds that, assuming the stockholders had full disclosure, the balance of the equities favored allowing them to decide for themselves whether to take the deal on offer. *See, e.g.*, *In re* El Paso Corp. S'holder Litig., 41 A.3d 432, 452 (Del. Ch. 2012); *In re* Netsmart Tech., Inc. S'holders Litig., 924 A.2d 171, 210 (Del. Ch. 2007).

appeared to be willing to offer a superior price for the company and whose transaction was being stymied by an agreement the board had approved.[585] In *Van Gorkom*, however, there emerged several other potential buyers,[586] but only KKR reached the point of presenting a written offer to Trans Union.[587] This naturally takes us to the question of whether the Trans Union board breached its *Revlon* duties in its dealing with KKR, and it is to that question that I now turn.

(4) Trans Union's Dealings with KKR

As recounted above, members of the Trans Union management team, dissatisfied with the Pritzker transaction, had approached KKR to organize a competing proposal.[588] On December 2, more than two months before the end of the go-shop period, KKR and the management team delivered to Van Gorkom for transmission to the Trans Union board a written offer to acquire the company at $60 per share, an offer that valued the company at about $751 million or about $90 million more than the price in the Pritzker transaction, but otherwise on the same terms offered by Pritzker.[589] KKR's offer also contained a financing condition related to both debt and equity financing,[590] but Kravis represented to Van Gorkom that he was confident

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[585] There have been a few cases in which, even in the absence of a competing bidder, on a motion for a preliminary injunction, the Delaware courts have held that the plaintiffs were likely to prevail on their *Revlon* claims. Yet, the courts, nevertheless, declined to issue a preliminary injunction, either because, assuming the stockholders have had full disclosure, they are not threatened by irreparable harm by being allowed to decide for themselves whether to complete the merger, or because the balance of the equities did not favor issuing an injunction. *See, e.g.*, *In re El Paso*, 41 A.3d at 452; *In re Netsmart*, 924 A.2d at 210.

[586] As noted above, Borg Warner, Bendix, Genstar, and GECC were also bidders. *See* OWEN, *supra* note 3, at 188 (mentioning Borg Warner and Bendix); *id.* at 190 (mentioning Genstar). The Delaware Supreme Court discusses Trans Union's dealings with these potential purchasers only briefly, but Owen has a longer account. *See id.* at 188, 190–91.

[587] Smith v. Van Gorkom, 488 A.2d 858, 884 (Del. 1985).

[588] *Id.*

[589] *Id.*

[590] *Id.*

the financing commitments could be obtained in two to three weeks—and thus long before the February 10 deadline.[591] Also as recounted above, Van Gorkom reacted in a highly negative manner to the offer, arguing that it was excessively contingent,[592] a position for which he may have had considerable justification,[593] even if the main reason for his negative reaction was his belief that, as the Trans Union board had determined, he ought to have been included in the internal discussions of the management buy-out group formulating an offer, not just in negotiating against the management group seeking to buy the company.

The duty of care is not well-suited to evaluate Van Gorkom's response to the KKR offer. The issues involved simply do not reduce to questions of whether Van Gorkom (or the board) was fully informed before taking action. Under *Revlon*, however, we come directly to the point: in dealing with KKR, did Van Gorkom (and the other Trans Union directors) take reasonable steps to get the best price for the stockholders reasonably available? Even in 1980, KKR was very well-known and had successfully concluded some very large transactions,[594] though none as large as the $751 million transaction Kravis proposed to Trans Union.[595] Generally speaking, therefore, KKR was a credible and reputable bidder. Hence, especially as Trans Union was in the midst of the go-shop period, Van Gorkom should have welcomed the KKR offer and, rather than belittle it because of the financing contingency it involved, worked with KKR and the management participants to help them secure their financing, just as he

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[591] *Id.*

[592] *Id.* at 884–85.

[593] *Id.* explaining how KKR's financing condition involved more contingency than the facially similar condition in the Pritzker offer.

[594] Owen writes:

> Very much in the spotlight at the time of the announcement of Trans Union's merger agreements with the Pritzkers, KKR seemingly was putting together a new deal every day. In the single week preceding that announcement, it had announced proposals to acquire three different companies for a total consideration of over $800 million.

OWEN, *supra* note 3, at 9. Moreover, at the time, KKR had completed larger acquisitions than the Pritzkers had. *Id.* at 139.

[595] *Id.*

had done with Pritzker.[596] Thus, even to the extent that Van Gorkom's concerns about KKR's financing were justified, whether by the substantial rise in interest rates since the time Pritzker had secured his financing or otherwise, *Revlon* would require Van Gorkom to take reasonable steps to help KKR arrange the necessary financing. No matter how contingent the offer may have been, *Revlon* would not permit a board to dismiss the KKR offer out of hand as Van Gorkom did, when he insulted Kravis by saying to his face that he would not dignify KKR's letter with the term *offer*.[597]

Moreover, if the primary reason that Van Gorkom reacted so negatively to the KKR offer was not the financing contingency it contained but the fact that, contrary to the board's instructions and Van Gorkom's orders, the management participants had met with KKR without his knowledge and formulated the offer without his participation, then Van Gorkom and the Trans Union board had clearly breached their *Revlon* duties. As this condition was imposed only on buyers including management participants, it amounted to "discriminatory treatment of a bidder, without any rational benefit to the stockholders," which is a breach of the board's fiduciary duties under *Revlon*.[598] For, as Romans clearly realized,[599] since Van Gorkom was to be the chief negotiator for the company on the sell-side, he would have an obvious and substantial conflict of interest acting on the buy-side.[600] Just like any other potential buyer, KKR, the Reichmanns, and the management participants would be grossly disadvantaged in subsequent negotiations if someone from the sell-side were privy to their internal discussions. In short, Trans Union would know the buyer's reserve price and could capture the entire joint surplus of the transaction, thus making it worthless to the buyer. To be sure, in one sense, such an arrangement may have been to

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[596] *Id.* at 59–60 (describing how Van Gorkom helped Pritzker arrange financing).

[597] *Id.* at 138.

[598] Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1282 (Del. 1988).

[599] OWEN, *supra* note 3, at 151.

[600] *Id.*; *see also* Macey, *supra* note 57, at 611–12 (explaining that, because neither Van Gorkom nor most of the other directors of the company were going to participate in an LBO, "the usual conflict between management and stockholders inherent in leveraged buyouts did not really exist in the case of Trans Union").

Trans Union's advantage, but it is so disadvantageous to the potential buyer as to ensure that no potential buyer would proceed on such terms—as indeed KKR and the management group did not, for they eventually cut Van Gorkom out of their discussions. In fact, it is difficult to imagine a condition that a selling board could impose on a buyer better calculated to ensure that the buyer would not make an offer for the company than the one the Trans Union board imposed on KKR and the management group.

Perhaps because of their unfamiliarity with the LBO concept, neither Van Gorkom nor the other directors understood what a chilling effect this requirement would have on any potential buyout offer involving management. Even so, the directors' subjective intentions are not dispositive. *Revlon* requires not only that the directors act in subjective good faith to get the best price reasonably available for the stockholders but also that they take steps to do so that are objectively reasonable,[601] and requiring that Van Gorkom be privy to the buyout group's internal discussions is not only unreasonable but, at least by contemporary standards, manifestly absurd. A timely suit by KKR or a stockholder seeking an injunction against the board's instructions that Van Gorkom participate in the internal discussions of the buyout group would surely have succeeded under *Revlon*.

Furthermore, as described above, because he believed that the board's instructions and his orders about the process of formulating the KKR offer had been violated, Van Gorkom immediately began questioning his senior executives to determine which of them were participating in the KKR offer. His manner of doing so surely made it clear that he thought anyone participating in that offer had behaved improperly.[602] Indeed, after the offer was withdrawn, Romans and Bosner, the leaders of the buyout group, worried that they may no longer have jobs at Trans Union.[603] Regardless of his intentions, the natural and

[601] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 180 (Del. 1986).

[602] OWEN, *supra* note 3, at 151 (stating that Van Gorkom thought "the handling of the whole situation [with KKR] had been improper" because "the instructions that had been issued on the coordination of inquiries from various suitors had not been followed.").

[603] *Id.* at 149 (stating that, after KKR withdrew its offer, Romans and Bosner "were concerned about their fate").

foreseeable effect of Van Gorkom's actions was to chill management participation in an LBO; by interrogating his senior executives in the manner he did, therefore, Van Gorkom likely breached his *Revlon* duties. In any event, Van Gorkom's questioning of his senior executives in this way surely was not reasonably calculated to facilitate a superior offer from KKR.

It is possible, however, that things were even worse than this. According to Owen, "it was widely believed that anything Van Gorkom learned about the buyout effort would immediately be channeled to Pritzker."[604] If this is correct, then the board's requirement that Van Gorkom be involved in the buyout group's discussions meant not only that KKR would be severely disadvantaged in any negotiations with Trans Union but also that KKR would be severely disadvantaged in any competitive bidding with Pritzker. To the extent that Van Gorkom was providing information about the KKR bid to Pritzker, Van Gorkom was breaching his *Revlon* duties in an egregious fashion. Indeed, the only reported parallel in the history of Delaware law would be the notorious incident in *Mills Acquisition* in which, in the final round of an auction for the target, the chief executive officer of the company, who was participating with KKR as a bidder in the auction, illicitly learned the details of a competing bidder's bid and shared them with KKR.[605]

Similarly, there is the matter of Van Gorkom's conversation with Kruizenga.[606] In the Supreme Court's account, after receiving the KKR offer letter, Van Gorkom had a private conversation with Kruizenga, the most key employee of the company, and immediately thereafter Kruizenga declined to participate in the

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[604] *Id.* at 143.

[605] Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1267–68 (Del. 1988). The situations would be similar but not identical. Evans's conduct in *Mills* was self-interested and so a breach of his duty of loyalty and morally blameworthy. *Id.* If Van Gorkom shared any information about the KKR bid with Pritzker (and other than the suspicions of some Trans Union insiders, there is no evidence he did this), he was not personally profiting by so doing. *Id.* The overall impression one gets of Van Gorkom is of a good man, accustomed to command, who wished to remain in charge of everything in the midst of a corporate transaction occurring in a new world that his admittedly long and very successful career left him ill-prepared to manage. *Id.*

[606] Smith v. Van Gorkom, 488 A.2d 858, 885 (Del. 1985); OWEN, *supra* note 3, at 145–46.

buyout group.[607] The court does not expressly say so, but it seems to believe that Van Gorkom was responsible for Kruizenga's decision.[608] As noted above, Owen's account seems to disprove this version of events, for Kruizenga had told Romans the day before, in no uncertain terms, that he was not participating in the KKR transaction.[609] In the unlikely event that the Supreme Court's suspicions were correct, however, this would be another egregious breach by Van Gorkom of his *Revlon* duties.[610]

So, even on the version of the facts most favorable to the Trans Union directors, the board surely breached its *Revlon* duties in its dealings with KKR. Rather than working with Kravis to line up financing, as Van Gorkom had done with Pritzker, he practically rejected the offer because of the financing contingency. Rather than treating KKR on a par with Pritzker, the board and Van Gorkom hamstrung the buyout group by requiring that Van Gorkom be involved in all its internal discussions. Rather than taking reasonable steps to allow his executives to participate in the KKR transaction if they wished to do so, Van Gorkom interrogated them as if they had done something wrong and created the impression that participating in the offer could endanger their futures with the company. Moreover, if Van Gorkom was passing information about the KKR offer to the Pritzkers, or if he scuttled the KKR offer by dissuading Kruizenga from participating, the breaches of *Revlon* are even worse.

But—and this is a key point in understanding the significance of *Van Gorkom*, and the same point we saw above—*none of these obvious and gross breaches of* Revlon *duties can even remotely be recast as a breach of the duty of care*. The Trans Union board did many things wrong,[611] but for the most part they were substantive mistakes in the sales process that made it difficult for the stockholders to realize the best price reasonably available for their shares. For the most part, the delicts of the Trans Union directors were breaches of their *Revlon* duties, not their duty of care.

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[607] *Van Gorkom*, 488 A.2d at 885.
[608] *Id.*
[609] OWEN, *supra* note 3, at 145–46.
[610] *Van Gorkom*, 488 A.2d at 885.
[611] *See id.* at 890–92; Herzel & Katz, *supra* note 448, at 1188.

d. The Case on the Edge of Forever

Imagine some eminent Delaware jurist—say Chief Justice Strine—travels back in time from 2017 to 1985, and, knowing all he does about the subsequent history of Delaware law, sits on the Delaware Supreme Court as it considers *Van Gorkom* and changes the past by sharing his knowledge of future law with the rest of the court. What would the Supreme Court likely have held? On the basis of the discussion above, it seems clear that the court would have held that the Trans Union board's *Revlon* duties were triggered when Van Gorkom initiated a sale of the company by approaching Pritzker, and that Van Gorkom and the other Trans Union directors repeatedly breached those duties. That is, on a motion for a preliminary injunction, the court would have held that the plaintiffs had demonstrated a substantial likelihood of success on the merits of their *Revlon* claims.

The court would have held that the directors breached their *Revlon* duties in approving the original merger agreement because the sales process that Van Gorkom initiated and managed, virtually entirely on his own, involved no board control, participation, or monitoring. The court would also have held that, in approving the merger agreement on September 20, the board again breached its *Revlon* duties because it lacked a reasonable basis for believing that $55 per share was the best price reasonably available for the company: the board had undertaken no financial analysis of the value of the company, no market check, and no negotiating over price. The court would have held that the directors breached their *Revlon* duties again, by, requiring that Van Gorkom, as their representative, be included in all internal discussions of any management buyout group, for his involvement in this way would obviously torpedo any possible offer from a management group. The court would have held that, when KKR did make an offer, the directors breached their *Revlon* duties when Van Gorkom did not receive the offer in a manner reasonably calculated to improve it, but rather, turned on his subordinates to discourage them from participating in KKR offer. If the court was considering the case at a point in time when KKR had made and not withdrawn a superior offer to acquire the company, the court would almost certainly have issued an injunction that ensured a fair bidding contest between Pritzker and KKR, and possibly GECC as well.

Crafting the injunction remedy, however, may have been difficult, and in any event, the terms of the injunction would have depended significantly on just when in the process it would have been issued. Assuming KKR had sued immediately after its first bid collapsed, the court would presumably have issued an injunction enjoining the Trans Union board and Van Gorkom from interfering with KKR and its dealings with any managers who wanted to participate in the LBO. It may also have enjoined the more offensive aspects of the go-shop and fiduciary out, such as the requirement that Trans Union enter into a definitive merger agreement before the board had a right to terminate the Pritzker agreement.[612] In reality, of course, Van Gorkom ordered a cooling off period for KKR and his managers. In mid-January, KKR and the managers were still interested in paying $60 per share for Trans Union, but their offer failed only because they no longer had time to arrange financing before the Trans Union stockholder meeting to consider the Pritzker offer.[613] Had the Delaware courts intervened in late 1980 with an appropriate injunction, it seems likely that KKR and the buyout group could have made a fully financed offer to acquire Trans Union at $60 per share. If, on the other hand, the suit was being considered only in January of 1981, when KKR had dropped out definitively and the stockholders meeting was fast approaching, the court would likely have found that, although the plaintiffs were likely to succeed on the merits in proving that the Trans Union directors had breached their *Revlon* duties, nevertheless the court would decline to issue an injunction and would allow the Trans Union stockholders to decide, after receiving full disclosure, whether to accept Pritzker's premium offer.[614]

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[612] On the other hand, the court would not likely have enjoined or voided Pritzker's stock option. Given its reasonable value in relation to the value of the transaction (i.e., only about 3.5 percent), it was probably not deterring materially higher bids, and neither KKR nor any other bidders were complaining about it. Moreover, Pritzker's lack of involvement in the worst aspects of the directors' breaches (*e.g.*, the various ways Van Gorkom interfered with KKR's bid) also militated against enjoining it. *See In re* Dollar Thrifty S'holder Litig., 14 A.3d 573, 575, 591–93, 618 (Del. 2010).

[613] *See supra* Section I.A.

[614] *See, e.g.*, *In re* El Paso Corp. S'holder Litig., 41 A.3d 432, 452 (Del. Ch. 2012); *In re* Netsmart Tech., Inc. S'holders Litig., 924 A.2d 171, 210 (Del. Ch. 2007).

It is important to appreciate the significance of the fact that KKR and the Reichmanns were still interested in bidding $60 per share for Trans Union as late as January of 1981, for their willingness to do so shows that the $55 per share price Pritzker offered was almost certainly *not* the best price reasonably available in September of 1980. Defenders of the Trans Union directors—and critics of the Delaware Supreme Court—have long argued that,[615] for more than four months, the entire financial and

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[615] Mones, *supra* note 31, at 561. McChesney, who agrees about the fundamentally misguided nature of *Van Gorkom*, also thinks that, as far as could be known on September 20, 1980, it was "unlikely that an even better offer than Pritzker's $18 premium would emerge" after that date. McChesney, *supra* note 340, at 639. His reasons are that (a) the 50 percent premium was quite high for the period, (b) Pritzker insisted in the original draft of the merger agreement that Trans Union not seek higher offers, and (c) the financial community had known for a long time about Trans Union's ITC problem, and no one had proposed to take over the company to monetize the ITCs. As indicated in the text, the fact that KKR could afford to pay $60 per share when interest rates were 800 basis points higher than they were on September 20 refutes the idea that the premium in the Pritzker deal made a topping bid improbable. McChesney, unlike virtually everyone else writing about *Van Gorkom*, knows how much interest rates increased from September 1980 to February 1981, see McChesney, *supra* note 340, at 645 n.56, and he correctly concludes that the dramatic increase in rates would have made financing subsequent offers topping Pritzker's offer difficult. *Id.* This seems to me, however, to overlook the key implication of rising rates, which is that if KKR could afford to pay $60 when the prime rate was 20.5 percent and the effective federal funds rate at 19.08 percent, surely it could have paid much more than $60 per share when, in September, the prime rate was merely 12.5 percent and the effective federal funds rate 10.87 percent. As to McChesney's second point, Pritzker, who was clearly the savviest dealmaker involved in the transaction, initially insisted on the no-shop precisely because he was concerned that a higher bid would emerge. This suggests such an offer was likely, not unlikely. As to the third point, it is true that the financial community knew about Trans Union's ITC problem, but that is hardly the same thing as knowing that Trans Union is *for sale*. *See generally In re* Lear Corporation S'holder Litig., 926 A.2d 94, 118–19 (Del. Ch. 2007) (discussing importance of the market's knowledge that a large public company widely followed by analysts has entered into a merger agreement). More generally, McChesney argues that the price Pritzker was offering was so high that the Trans Union stockholders were very likely better offer with the board accepting the offer and locking it in than they would have been in rejecting the offer and hoping to get a better offer from another buyer. This argument assumes, however, that the board could neither have considered Pritzker's offer more carefully in the time provided nor obtained from Pritzker more time to consider it—i.e., that Pritzker would have withdrawn his offer at its expiration

corporate world knew that Trans Union was for sale, but apart from the abortive offer from KKR, not a single bidder emerged to top the $55 per share offer from Pritzker.[616] Normally, such facts would strongly suggest that $55 per share was indeed the best price available for the company,[617] but the autumn of 1980 and the winter of 1980–1981 were anything but normal. Although the Delaware Supreme Court never alludes to it, as noted above, interest rates increased astonishingly during this period, with the prime rate rising from 12.5 percent on September 20 (the date of the Pritzker agreement) to 18.5 percent on December 2 (the date of the KKR offer) to 20.5 percent in January of 1981 (when Kravis was trying to resurrect that offer).[618] Over approximately the same period, the effective federal funds rate increased from 10.87 percent in September of 1980 to 18.90 percent in December of 1980 to 19.08 percent in January of 1981.[619]

The increase in interest rates had several important effects. First and most important, it raised the borrowing costs of any acquirer who needed to finance the merger, which of course reduced the amount the borrower could pay for the company.[620]

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and never have renewed it. The text argues that the first of these assumptions is definitely false. The second also seems dubious to me.

[616] *See, e.g.*, Mones, *supra* note 31, at 561 ("The majority may ... have been off the mark in its outright rejection of the board's market test of the merger proposal.").

[617] Macey, *supra* note 57. He also thinks that $55 per share was likely not the best price Trans Union could have obtained from Pritzker in September of 1980, but he points to reasons different from, though compatible with, those given in the text. *See* Macey, *supra* note 57, at 617–19. He argues convincingly that, if the board had known about the negotiating history underlying the $55 per share price and KKR's interest in the company, it likely could have negotiated a better price from Pritzker. *Id.* at 618. Only because Van Gorkom had kept from the board some of the material facts is the board's "seemingly bizarre failure even to suggest a higher price to Pritzker … comprehensible." *Id.*

[618] OWEN, *supra* note 3, at 128.

[619] *Effective Federal Funds Rate,* FED. RESERVE BANK ST. LOUIS (Oct. 2, 2017), https://fred.stlouisfed.org/serios/FEDFUNDS [http://perma.cc/53LK-TYB7].

[620] *See supra* note 253 and accompanying text. The extraordinary increase in interest rates resulted from the dramatic tightening of monetary policy by the Federal Reserve to reduce the very high inflation rates of the final years of the Carter Administration. Under more normal circumstances, increases in interest rates due to increases in the expected inflation rate would likely result in increases in the cash-flow projections of the company and so any increase in the borrower's financing costs would be, to some extent at least, thereby offset. It is very difficult to venture any speculations about effects of

Indeed, in November of 1980, "Van Gorkom doubted that a leveraged buyout could be arranged" because "[r]ising interest rates would torpedo any deal that involved such extensive borrowings."[621] Second, the increase in interest rates limited the kinds of financing an acquirer might arrange and which financing sources may be available. For instance, Romans concluded that rising interest rates "had priced subordinated debt and preferred stock out of consideration," which would significantly limit the buyout group's ability to obtain financing from the institutional investors who would naturally be interested in such instruments.[622] Third, because Trans Union's leasing business was heavily dependent on short-term borrowing, rising interest rates reduced Trans Union's free cash flow,[623] which made the company less valuable to a potential acquirer. Therefore, the dramatic increases in interest rates guaranteed that, based on a discounted cash flow analysis, Trans Union was *much* more valuable on September 20, the day the Pritzker agreement was signed, than it was on December 2, the day KKR made its offer for the company. Similarly, the company was much more valuable on December 2 than it was in mid-January of 1981 when Kravis tried to resurrect the KKR offer, but ran out of time to arrange financing. If KKR could have paid $60 per share for Trans Union in January of 1981, when the prime rate hit 20.5 percent (and the effective federal funds rate stood at 19.08 percent), surely someone could have paid a good deal more than $60 per share (let alone Pritzker's $55 per share) for the company in September of 1980. There is simply no way that $55 per share was the best price reasonably achievable for Trans Union on September 20, 1980.[624]

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inflation expectations on the future cash flows of Trans Union in the unprecedented monetary environment of late 1980.

[621] Owen, *Leveraged Buyout*, *supra* note 197, at 18.

[622] *Id.* at 22.

[623] Between 1979 Q4 and 1980 Q4, Trans Union's interest expense increased 46 percent from $90 million to $131 million. *Id.* at 200.

[624] The importance of the sharp increase in interest rates was obvious at the time. One Trans Union insider, who as not generally friendly to Van Gorkom, later commented that selling the company in September of 1980 was "a brilliant move financially" on Van Gorkom's part because he "sold the company for way, way more than it would be worth today." *Id.* at 195. Van Gorkom himself said, "[p]erhaps it was sheer luck, ... but the fact is that $55 *was* the proper number, and subsequent events have demonstrated that the

There is additional contemporaneous confirmation for this view. Within days of the merger, Oppenheimer & Co. issued a report recommending the purchase of Trans Union shares on the theory that a $65 per share price could easily be justified.[625] Significantly, the market agreed, and Trans Union shares sometimes traded *above* the $55 deal price after the Pritzker transaction was announced.[626]

II. *SMITH V. VAN GORKOM* AS THE *KOBAYASHI MARU* OF DELAWARE CORPORATE LAW

The final section of the previous Part imagined a time-traveling jurist guiding the Delaware Supreme Court in deciding a motion for a preliminary injunction in *Smith v. Van Gorkom*. That was not, however, the procedural posture of the actual case. For, by the time the Supreme Court decided the case, the merger had been closed for more than four years, and the plaintiffs were not seeking an injunction but either rescission of the merger or, much more plausibly, monetary damages in the amount of the difference between the fair value of their shares and the $55 per share price in the Pritzker transaction.[627] This procedural fact is the most critical aspect of *Smith v. Van Gorkom*.

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company was sold at almost precisely the peak of its value." *Id.* Here, Van Gorkom is right that—because interest rates rose sharply after the date of the September 20 agreement—September 20 was more-or-less the date at which Trans Union could have commanded the highest price. That $55 per share was that price, however, does not follow. As the argument in the text shows, that number was likely very much higher.

[625] Owen, *Trans Union*, *supra* note 117, at 30 (noting Oppenheimer & Co.'s report that "recommended the purchase of Trans Union common stock, indicating that it would not be difficult to arrive at a price of $65 per share—less than five times Trans Union's pre-tax cash flow of $13.40 per share").

[626] Van Gorkom, *supra* note 145, at 19.

[627] *See* Smith v. Van Gorkom, 488 A.2d 858, 863 (Del. 1985) where the court says that plaintiffs were "originally seeking rescission" of the merger, but that "[a]lternative relief in the form of damages is sought against the defendant members of the Board of Directors of Trans Union." In the court's very brief discussion of damages, it never mentions rescission, presumably for the obvious reason that, so long after the consummation of the merger, such a remedy would be entirely impracticable and extremely costly. *Id.* at 890–93. Rather, without further explanation, the court remands the case to the Chancery Court to determine the fair value of Trans Union as of September 20, 1980, in accordance with *Weinberger* and, then, assesses damages as the difference between this fair value and the $55 per share price paid by Pritzker in

In this Part, I explain why this was true. In particular, in Section II.A, I shall argue that, given that the Delaware Supreme Court had to operate within the common law method, if it imposed on directors selling their company *any* stricter duties than those imposed by the traditional business judgment rule (that is, the rule as it existed before *Aronson v. Lewis* invented the duty of care), the result would have been disaster, just as it was in *Van Gorkom*. In other words, if the court got the holding about breach right (*i.e.*, it held that Van Gorkom and the other Trans Union directors breached their duties to the stockholders), then it would necessarily get the holding about remedies wrong, because it would have to impose on the directors such enormous liabilities that Delaware's whole system of corporate law would be threatened with collapse. In other words, within the common law system in which the Delaware Supreme Court operated, there was simply no right way to decide *Smith v. Van Gorkom*. The case is a *Kobayashi Maru*.[628]

In Section II.B, however, I shall argue that *Van Gorkom* was nevertheless a critically important advance in Delaware law. For, the case had shown that any attempt to use the common law system to control directors considering business combinations would produce disastrous consequences, and this prompted the Delaware bar and the Delaware General Assembly to seek a solution outside the confines of the common law system. In other words, just as the young James Kirk was able to defeat the *Kobayashi Maru* by reprogramming the computer simulation to devise a solution not possible under the pre-existing program, so too did the Delaware General Assembly devise a solution not possible under the common law by enacting Section 102(b)(7): to wit, a kind of fiduciary duty enforceable by injunction before the harm from breaching the duty has occurred but not enforceable by damages after the harm has eventuated. The possibility of such duties allowed the Delaware Supreme Court in *Revlon* and later cases to craft a set of fiduciary duties for directors significantly more stringent than those announced in *Van Gorkom* without threatening to undermine the foundations of Delaware corporate law.

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the transaction. *Id.* at 893 (citing Weinberger v. UOP, Inc., 457 A.2d 701, 712–15 (Del. 1983)). Presumably, the plaintiffs included the recession for rescission merely for jurisdictional reasons in the Court of Chancery.

[628] For a discussion the *Kobayashi Maru*, see *supra* note 69.

The ultimate result was an ingenious system of fiduciary duty pre-clearance analogous to the system of antitrust pre-clearance under the Hart-Scott-Rodino Antitrust Improvement Act of 1976.[629] Under the system that resulted from *Van Gorkom*, Section 102(b)(7), and *Revlon*, after a merger agreement is signed, but before the merger closes, plaintiff stockholders can challenge the proposed transaction by alleging that the directors have breached their fiduciary duties in approving the merger, and the Delaware courts will review the directors' action under *Revlon* and similar doctrines, ordering appropriate equitable relief if the courts find a violation. If the courts do not find a violation, however, the transaction will proceed to closing. If the stockholders approve the transaction, then, assuming the corporation has a Section 102(b)(7) provision in its certificate of incorporation, any *Revlon* claims against the directors will become dismissible[630] except for those sounding in the duty of loyalty.[631] Since they are generally unable to recover post-closing, plaintiff-stockholders have the strongest incentives to bring suit pre-closing. The possibility of such a pre-clearance system, therefore, turns on the elimination of personal liability for breaches of a particular kind of fiduciary duty, and that was not a result possible in the common law system. It was possible only by legislative action, and the cause and basis of that action was *Smith v. Van Gorkom*. The elimination of personal liability in damages that underlies the whole Delaware system of pre-clearing mergers could, with some justice, have been called *Van Gorkom* immunity.

A. Van Gorkom *as Necessarily a Mistake*

Having said much about what made *Van Gorkom* a bad decision, I should be clear about what did *not* make it a bad decision. In this section, I summarize (1) what *Van Gorkom* got right, (2) what

[629] Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 189 (2012).

[630] *See, e.g.*, Malpiede v. Townson, 780 A.2d 1075, 1093 (2001).

[631] *Id.* at 1093. Indeed, under recent developments in Delaware law, assuming that the stockholder vote approving the merger was a fully informed, uncoerced vote of the disinterested stockholders, *all* claims against the directors in connection with the merger will be extinguished except for claims of waste, and these will, of course, virtually always be dismissible. *See* Singh v. Attenborough, 137 A.3d 151, 151–52 (Del. 2016); Corwin v. KKR Fin. Holdings, Inc., 125 A.3d 304, 312–14 (Del. 2015).

Van Gorkom got wrong, and (3) why *Van Gorkom* had to get wrong what it got wrong.

1. *What* Van Gorkom *Got Right*

It is important to appreciate that *Van Gorkom* did not get everything wrong. In fact, it got much right. To begin with, there was nothing wrong with the impetus behind *Van Gorkom*: the idea that the Delaware Supreme Court should impose more rigorous fiduciary duties on directors when they were engaged in selling the company. The court would do exactly that in *Revlon* just ten months after deciding *Van Gorkom*,[632] and almost everyone nowadays thinks that *Revlon* has been a major success. Nor did the *Van Gorkom* court err in imposing on directors new fiduciary duties that were too stringent. The *Van Gorkom* duty of care may well be poorly theorized and ultimately incompatible with the theory underlying the business judgment rule, but it requires only that before making a business decision the directors be informed of all material facts reasonably available, and this is a duty much *less* stringent than the duties the Supreme Court would impose on directors in *Revlon*.[633] Indeed, a board's *Revlon* duties *include* the *Van Gorkom* duty of care and then go far beyond it by requiring not only procedural due care but also substantive reasonableness to the extent that they require a board that has initiated a sale process to take substantively reasonable steps to get the best price for the stockholders reasonably available.[634] Nor was *Van Gorkom* wrong in its essential holding that the Trans Union directors had breached their fiduciary duties, for that result would follow—and even follow more easily and clearly—under *Revlon* than it did under the reasoning in *Van Gorkom* itself. Viewed charitably, the worst thing about *Van Gorkom* was that it was an under-theorized[635] and poorly explained early stab at *Revlon*.

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[632] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 173 (Del. 1986).

[633] *Compare* Smith v. Van Gorkom, 488 A.2d 858, 893 (Del 1985), *with* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 185 (Del. 1986).

[634] *See supra* text accompanying notes 35–40.

[635] *See* Quillen, *supra* note 28, at 469 (suggesting that "it is the opinion rather than the decision which has created the depth of the criticism").

2. *What* Van Gorkom *Got Wrong*

The only thing that was *fatally* wrong about *Van Gorkom* was the remedy the Supreme Court imposed when it held the Trans Union directors personally liable in damages that could easily have run to $100 million or more.[636] That is, the Supreme Court ordered the Chancery Court on remand to determine, in accordance with *Weinberger v. UOP*,[637] the fair value of Trans Union as of the date of the board's approval of the merger agreement and to award damages based on the difference between this fair value and price obtained in the Pritzker transaction. Based on KKR's bid of $60 per share, the damages would have aggregated about $60 million.[638] If the Chancery Court had found that the fair value of the company was $65, the high end of range Romans had computed in his leveraged buy-out study, the damages would have been about $120 million. If, as often happens, a discounted cash flow analysis produced a higher value for the company than a leverage buy-out study, say $70, the damages would have been about $180 million. Even at the lowest figure of $60 million, that would come to $6 million per director. By comparison, selling his 75,000 Trans Union shares in the merger at $55 per share, Van Gorkom netted only $4.125 million before taxes. In other words, assuming full contribution by all the directors, each director's individual share of the damages would likely have greatly exceeded the director's net worth.[639]

But this was not merely a catastrophe for the individual directors involved. It also threatened to collapse the entire system of Delaware corporate law. The reason for this may not be immediately obvious. After all, directors had always been liable for certain harms to the corporation and the stockholders arising

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[636] As noted above, this point is generally conceded by all observers. *See e.g.*, Schwartz & Wiles, *supra* note 330, at 430 (defending the decision but conceding that "the court's imposition of personal liability on the board is original"); Sharfman, *supra* note 57, at 287 (stating that "[t]he enduring legacy of *Van Gorkom* is the understanding that corporate directors should not be held financially liable for decisions that lack due care").

[637] Weinberger v. UOP, Inc., 457 A.2d 701, 713–14 (Del. 1983).

[638] As noted above, Trans Union had outstanding at the time of the merger 12,512,956 shares. OWEN, *supra* note 3, at 2. If damages were assessed at $5 per share, the aggregate liability for the directors would have been $62.6 million.

[639] Before the Chancery Court held a trial to determine the fair value of Trans Union, the case settled for $23.5 million. *See also* OWEN, *supra* note 3, at 261.

from some of their decisions. Under the traditional business judgment rule, however, these decisions were only those involving fraud, bad faith, or some other kind of conduct from which the director was deriving a personal benefit not shared by the stockholders generally. As an old Delaware case put it, "an honest mistake of business judgment should not be reviewable by the Court."[640] Granted that *Van Gorkom* expanded the class of decisions for which directors could be liable to include uninformed ones, why does this make such an important difference?

A common answer, but an inadequate one, is that directors can easily avoid transactions that are fraudulent or from which they derive improper personal benefits, but it is much more difficult for them to avoid being (or being later found to be) uninformed. The better answer appeals to the difference in the relevant judicial error rates. That is, the false-positive rate in cases alleging directors have acted disloyally, engaged in self-dealing, or otherwise received an improper personal benefit from a transaction is very low.[641] For duty of care claims, however, the false-positive rate would likely be much higher: courts will often find that a director breached a duty of care of the kind articulated in *Van Gorkom* when in fact the director has not done so.[642] There are two related reasons for this. The first is

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[640] Bodell v. Gen. Gas & Elec. Corp., 140 A. 264, 267 (1927).

[641] Of course, in determining the expected value of serving as directors, potential directors also care about the false-negative rate because this makes defecting and profiting by breaching their duties more valuable. To the extent that the director is honest, however, and refuses to profit illicitly, the false-negative rate is irrelevant, and for this reason it is treated as such in the argument in the text. As Chief Justice Strine would say, absent evidence to the contrary, Delaware presumes directors are honest. Goodwin v. Live Entm't, Inc., No. Civ.A. 15765, 1999 WL 64265, at *24 (Del. Ch. Jan. 25, 1999) (quoting Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 64 (Del. 1989)). On the false-negative problem more generally, see Elson & Thompson, *supra* note 9, at 587–88 (arguing that courts, like all outsiders, cannot reliably distinguish between genuine exercises of due care and mere play-acting by directors attempting to demonstrate to courts that have exercised such care).

[642] Thus, the fatuity of such defenses of *Van Gorkom* as "if a director of a Delaware corporation performs his duties as a director conscientiously and loyally, he has absolutely nothing to fear from the ruling of the court in *Trans Union*." Prickett, *supra* note 357, at 462. The conclusion follows only if one *also* assumes that the Delaware courts will find that a director breached his duty of care if and only if the director actually breached his duty of care—that is, the judicial error is zero. It is no accident here that Prickett is a plaintiff's

hindsight bias, the human tendency to exaggerate the probability that the actual outcome of an uncertain process is the one that would result.[643] In duty of care cases, plaintiffs would sue only when the directors' decision proved to be harmful to the corporation, and hindsight bias would tend to make reviewing courts think that the negative outcome was more probable and predictable (and thus more likely to have involved a want of care) than was really the case.[644]

But hindsight bias affects all cases in which judges or juries review the decisions of others, not just cases involving the decisions of corporate directors, and so if hindsight bias does not result in unacceptably high false-positive rates in other kinds of negligence cases, neither should it do so in business judgment cases either. This brings us to the second and much more important reason.[645] To wit, unlike most decisions of ordinary people in daily

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lawyer. Because plaintiffs rather than defendants decide to initiate a lawsuit, repeat players on the plaintiffs' side, such as plaintiffs' counsel, have a strong personal incentive to favor rules that involve high false-positive error rates. Under such rules, suits against even perfectly innocent defendants have positive settlement value. Indeed, plaintiffs (and their counsel) with weak cases have strong incentives to favor a rule with a high error rate even when the false-positive and false-negative rates are the same.

[643] Hal R. Arkes & Cindy A. Schipani, *Medical Malpractice v. the Business Judgment Rule: Differences in Hindsight Bias*, 73 OR. L. REV. 587, 588 (1994).

[644] *See* Joy v. North, 692 F.2d 880, 886 (2d. Cir. 1982) (stating that "the circumstances surrounding a corporate decision are not easily reconstructed in a courtroom years later," and "a reasoned decision at the time made may seem a wild hunch viewed years later against a background of perfect knowledge"); *see also Gentler Critique*, *supra* note 409, at 493 (discussing hindsight bias as a justification for the business judgment rule); Allen, Jacobs & Strine, *supra* note 31, at 454–55 (discussing importance of hindsight bias in duty of care cases).

[645] Rock & Wachter, *supra* note 373, at 664–71, give a different, though related, explanation of why business decisions are economically different and thus ought be reviewed under a different judicial standard. For them, the key point is that the decisions have characteristics that make them efficiently handled intra-firm as opposed to on the market—e.g., the decisions are part of a relationship that is open-ended in time and scope, transactionally intensive, and often involving assets, physical and otherwise, that are illiquid and difficult to value. *Id*. at 666. From the point of view of the analysis given in the text, however, Rock and Wachter concur on the key point: with business decisions, "judges cannot reliably distinguish between negligent and non-negligent behavior." *Id*. at 667. Similarly, Fischel explains that directors should not be liable for negligent business decisions because, for among other reasons, "the cost of contracting" in such situations is high, which "makes it

life and unlike the decisions of most other professionals in the exercise of their trades, the decisions of businesspeople regularly result in losses even when they were in no way negligent. That is, an automobile accident or a bridge collapse almost always involves a negligent mistake on the part of some individual or other,[646] but a business decision that loses money does not. For example, an investment that has a 90 percent probability of resulting in a complete loss may well have positive net present value because the expected payoff, which occurs with only 10 percent probability, is so great as to give the transaction positive net present value. In such a case, the business decision to make the investment may well be eminently sound. Hence, business decisions are importantly unlike most other decisions in that, much more than other kinds of decisions, they often result in losses even when they were entirely reasonable.[647] This fact,

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extremely difficult to distinguish adequate or reasonable performance from a breach of fiduciary duty." Fischel, *supra* note 338, at 1439. In other words, "[l]iability rules will be most useful in assuring contractual performance when the duty owed can be specified and monitored at low cost," which is not the case with directors making informed decisions. *Id*. at 1440. Rather, "it will frequently be impossible to determine … whether a bad outcome had anything to do with the amount invested in information as opposed to market conditions that could not have been anticipated, bad luck, or any number of other possible factors." *Id*. at 1442. For a very different account, see Sharfman, who maintains that it is efficient not to impose liability on directors for breaches of the duty of care based on a combination of arguments related to Bainbridge's conclusions about director primacy and Blair and Stout's conclusions about mediating hierarchies. *See* Sharfman, *supra* note 57, at 290.

[646] Allen, Jacobs, and Strine argue that "[i]n cases involving comparatively simple decisions such as automobile accidents, there is often little difference between decisions that are bad and good decisions that turn out badly." Allen, Jacobs & Strine, *supra* note 31, at 454, "[i]n such cases, typically only one decision is reasonable in a given set of circumstances, so decisions that turn out badly almost invariably turn out to have been bad decisions." The authors seem to conflate several ideas here: (a) complex, as opposed to simple, decisions, (b) decisions such that, if they produce a bad outcome, they were likely negligent, and (c) decisions such that, in their circumstances, they were the only reasonable alternatives. These are clearly different concepts, and the classes of such decisions do not coincide in reality. The concept that matters is the one identified in the text: decisions such that, if they result in bad outcomes, they were almost certainly negligent—e.g., car accidents do not usually occur unless at least one driver has been negligent.

[647] Again, Allen, Jacobs, and Strine are very close but get distracted by other real, but not essential, properties of business decisions. They write, "Unlike automobile accident cases, it may be hard for judges to differentiate

combined with hindsight bias, explains why a court reviewing decisions of corporate directors for want of due care will likely produce a significant false-positive error rate.[648]

Now, the possibility of being found personally liable, whether for a breach of the duty of loyalty or the duty of care, creates an expected cost for individuals serving as directors.[649] Given the immense size of the potential liabilities, however, the false-positive rate need not be very high to create unacceptable expected costs.[650] For example, suppose a company with market capitalization of $5 billion pays its outside directors $250,000 per year in total compensation.[651] In exchange for this benefit, an individual

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bad business decisions from good business decisions that turn out badly. Business decisions are virtually always made with less than perfect information and thus decisions makers are required to assess and assume some degree of risk." *Id* at 454. But the distinguishing characteristic of business decisions is not that they are made with imperfect information (indeed, all human decisions are made with imperfect information) nor yet that they involve risk or the possibility of negative outcomes (which is also true of all human decisions). The distinguishing characteristic of such decisions, as indicated in the text, is that they may be perfectly reasonable (e.g., have net present value) even though they may very likely result in negative outcomes (e.g., entail losses).

[648] Compare Herzel and Katz's point that markets can evaluate directors' business acumen better than courts can because markets can judge directors on the basis of the large number of decisions they make over a significant period of time but courts can consider only the one decision challenged in a lawsuit. Herzel & Katz, *supra* note 448, at 1189. Because business decisions have the properties described in the text, one business decision working out badly shows very little about the business judgment of the directors. When we consider the aggregate result of a large number of decisions, however, that changes. Whether the aggregate result is positive or negative will correlate well with whether the directors are astute businesspersons or not.

[649] Allen, Jacobs & Strine, *supra* note 31, at 455 (stating, "the risk of liability, at least in the case of non-management directors, could be highly disproportionate to the incentives for serving as a director. Liability for an imprudent decision could be in the millions, but outside directors rarely receive annual fees commensurate with liability risk of that magnitude").

[650] Pogostin v. Rice, 480 A.2d 619, 627 (Del. 1984); Gagliardi v. Trifoods Int'l, Inc., 683 A.2d 1049, 1052 (Del. Ch. 1996) (stating, "[g]iven the scale of operations of modern public corporations … only a very small probability of director liability based on 'negligence,' 'waste,' etc., could induce a board to avoid authorizing risky investment projects").

[651] See the 2016 Director Compensation Report for a report of median annual compensation for non-employee directors at public companies as $260,000 for large-cap companies, $200,000 for mid-cap companies, and $144,625 for small-cap companies. *2016 Director Compensation Report,* FW COOK (2016),

agrees to provide services as a director, which involves a certain cost to him (at least in the form of forgone leisure) that reduces the value to him of serving to some indeterminate amount below $250,000. As a director, this person will also bear certain risks. In particular, whenever he is called upon to make a business decision as a director, no matter how careful he is to be informed, under *Van Gorkom* he will run a risk that a court will later find (erroneously) that he made the business decision on less than an informed basis. Thus, there is a cost to the director of making this business decision equal to the potential liability multiplied by the probability that a court will (erroneously) find he made the decision without being fully informed. Now suppose that the company receives a takeover proposal valuing the company at $6 billion (*i.e.,* a 20 percent premium to market), and the director exercises due care and votes to approve the transaction. If there is just a one in a hundred chance that a court will subsequently (erroneously) find that the director breached his duty of care and that the company was really worth $7 billion (*i.e.,* a 40 percent premium to market), then the potential liability for the director will be 1/100 of $1 billion or $10 million, which is 40 times the director's annual compensation for being a director. If the board has ten members and the director can count on the other nine directors to contribute fully to the judgment, the expected cost of the director's personal liability would still be $1 million or four times his annual compensation as a director.

A takeover proposal is an extraordinarily large transaction and so involves extraordinarily large possible liability for the director, but potential liability would attach to every business judgment the director makes as a director of the corporation.[652] The aggregate value of those decisions in a given year may plausibly be valued at the total revenues of the company. Assuming the $5 billion company from our example above has a 10 percent profit margin[653] and a P/E multiple of 20, its revenues

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https://www.fwcook.com/content/documents/publications/11-30-16_FWC_2016_Director_Comp_Report.pdf [https://perma.cc/4MGG-QPU8]. The report defines large-cap companies as companies with a market capitalization greater than $5 billion. The example thus involves a director very well compensated by current market standards. *Id.*

[652] Herzel & Katz, *supra* note 448, at 1190–91.

[653] For reference, according to the "U.S. Weekly Kickstart" report issued by Goldman Sachs in late July, 2017, the average profit margin of the S&P 500 was

would be about $2.5 billion. Thus, on the same assumptions used above, the expected cost of liability to the director, even absent having to decide about a takeover proposal, would be 1/100 of $2.5 billion or $25 million, which is 100 times the director's annual compensation as a director. Again, assuming full contribution from the other nine members of a ten-member board, the expected cost of the director's personal liability would still be $2.5 million or ten times his annual compensation as a director. Clearly, under these conditions, it would be very difficult to find enough qualified individuals to serve as corporate directors of public companies. Such a system would make serving as a director highly irrational from a financial point of view, with the result that many qualified individuals will decline to serve.[654] That result threatens the very survival of the system as a whole.

3. *Why* Van Gorkom *Had to Get Wrong What It Got Wrong*

If what *Van Gorkom* got wrong was that it made serving as a director economically irrational by imposing on directors potentially enormous liabilities for honest but uninformed business decisions, how could the Delaware Supreme Court have recast the opinion to avoid this result? The simple answer is that there is no way it could have done so, at least not if it was going to create new fiduciary duties to discipline directors considering business combination transactions.

For example, let us abstract from the actual opinion in *Van Gorkom* and assume merely that, on any theory whatever not involving bad faith or a breach of the duty of loyalty, the court had held that the directors breached their fiduciary duties

10 percent. Mark Kolakowski, *Why Techs, Banks Will Lead in 2nd Half: Goldman*, INVESTOPEDIA (July 25, 2017, 6:00 AM), http://www.investopedia.com/news/why-techs-banks-will-lead-2nd-half-goldman/ [https://perma.cc/K84U-RKXA].

[654] *See* Allen, Jacobs & Strine, *supra* note 31, at 449 (stating, "[h]ighly qualified directors may also avoid service if they face liability risks that are disproportionate to the benefits of service"); *id.* at 452 (stating, "the risk of liability under the applicable standard of conduct for assuming a given corporate role may dwarf the incentives for assuming that role"); *see also* Fischel, *supra* note 338, at 1454 (arguing that managers "will be less willing to serve" because not serving is "the best protection against getting sued"); McChesney, *supra* note 340, at 648 (stating that, as a result of *Van Gorkom*, "it … became more difficult for corporations to attract directors to their boards, and existing directors resigned from boards").

to the stockholders. For this breach, there must be remedy, for it is axiomatic in the common law that wherever there is a right, there is a remedy.[655] *Ubi ius, ibi remedium*,[656] or sometimes *Lex dabit remedium*.[657] Thus, Blackstone says that "it is a general and indisputable rule, that where there is a legal right, there is also a legal remedy, by suit or action at law, whenever that right is invaded,"[658] and "all possible injuries whatsoever, that did not fall within the exclusive cognizance of either the ecclesiastical, military, or maritime tribunals, are for that very reason within the cognizance of the common law courts of justice."[659] He continues, "[f]or it is a settled and invariable principle in the laws of England, that every right when withheld must have a remedy, and every injury it's proper redress."[660] This principle was universally adopted in the United States along with the rest of the common law, and it appears in American cases at least as far back as Chief Justice Marshall's opinion in *Marbury v. Madison*.[661] There he writes, "The very essence of civil liberty certainly consists in the right of every individual to claim the protection of the laws, whenever he receives an injury. One of the first duties of government is to afford that protection."[662] For Chief Justice Marshall, the principle lies at the foundation of the new republic. He writes, "[t]he government of the United States has been emphatically termed a government of laws, and not of men. It will certainly cease to deserve this high appellation, if the laws furnish no remedy for the violation of a vested legal right."[663]

Naturally, this universal principle became part of the common law in Delaware, as it did everywhere else in the United

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[655] "The modern jurist assumes the other, the more ideal of the two correlated terms, to be the more evident, and acts upon the converse maxim: Where there is a Right there is a Remedy; or, Given the Right, the Remedy follows." GAIUS, INSTITUTES OF ROMAN LAW 445 (Edward Poste, trans., Oxford at the Clarendon Press 1904).

[656] *Ubi jus, ibi remedium*, BLACK'S LAW DICTIONARY (6th ed. 1990).

[657] AARON X. FELLMETH & MAURICE HORWITZ, GUIDE TO LATIN IN INTERNATIONAL LAW 167 (Oxford University Press 2009).

[658] 3 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND 23. (1794).

[659] *Id.* at 108–09.

[660] *Id.* at 109.

[661] Marbury v. Madison, 5 U.S. 137, 147 (1803).

[662] *Id.* at 163.

[663] *Id.*

States. Indeed, in 1844, in *Short v. Piper,* the Superior Court of Delaware proclaimed as an axiom accepted by all "the principle of law … that wherever there is a right there ought to be a remedy."[664] In 1985, therefore, in the Delaware Supreme Court, which is a common law court and a court of equity, this principle was too fundamental to be questioned. Not surprisingly, therefore, the court in *Van Gorkom* never even considered the possibility that, having shown that the Trans Union directors had breached their fiduciary duties to the stockholders, the stockholders might have no remedy. It was obvious beyond question that the stockholders had a remedy. But what remedy? Delaware courts have on occasion entertained the possibility of rescinding a merger, but they have virtually always[665] declined to do so on what might be thought of as the doctrine of not unscrambling the eggs.[666] The obvious impracticality of such a remedy, coupled with what would undoubtedly be a strong preference of the plaintiffs for cash, left just one option: monetary damages.[667] As Manning put it, "[h]aving decided that the directors' behavior was substandard, the [S]upreme [C]ourt reached for its only remedial tool—damages."[668]

But at that point, the essential problem of *Van Gorkom* was created: the relatively high false-positive error rate in nonloyalty cases, coupled with the tremendous sums at stake in corporate transactions, especially business combinations, causes the expected costs of serving as a director to rise sharply and quickly exceed the benefits of such service, and we are back to the untenable result of *Van Gorkom*. Within the common law system in which the Delaware Supreme Court operated, the only

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[664] Short v. Piper, 4 Harr. 181, 182 (Del. Super. Ct. 1844).

[665] As far as I know, when the case involved public companies, they always declined to do so.

[666] The phrase entered the Delaware lexicon in the opinion of the Court of Chancery in *Gimbel v. Signal Cos., Inc.*, 316 A.2d 599, 603 (Del. Ch. 1974), *aff'd*, 316 A.2d 619 (Del. 1974), apparently borrowed from *Metro-Goldwyn-Mayer Inc. v. Transamerica Corp.*, 303 F. Supp. 1344, 1348 (S.D.N.Y. 1969), but the metaphor goes back at least as far as President Lincoln, who once quipped, "Broken eggs cannot be mended." 2 MICHAEL BURLINGAME, ABRAHAM LINCOLN: A LIFE 587 (2008) (quoting Abraham Lincoln).

[667] Quillen writes, "[a]lthough there was a continuing prayer for rescission, after the denial of preliminary injunctive relief, the real question was whether the Trans Union directors were liable personally for money." Quillen, *supra* note 28, at 490.

[668] Manning, *supra* note 23, at 4.

way to avoid this result would be to find, as the Court of Chancery below found,[669] that the Trans Union directors did *not* breach their fiduciary duties. *Any* result in the Supreme Court that did the *right* thing by holding that the Trans Union directors had breached their duties would necessarily do the catastrophically *wrong* thing and hold those directors liable in damages, thus undermining the economic viability of the entire Delaware system of corporate law. For the justices of the Delaware Supreme Court, *Smith v. Van Gorkom* was a problem in which every available solution was wrong. It was a *Kobayashi Maru*.

B. Van Gorkom *as a Necessary Mistake*[670]

Now, since *Van Gorkom* was a *Kobayashi Maru*, any solution the court adopted was necessarily going to be mistaken, and in this sense, *Van Gorkom* was thus necessarily mistaken. Most *Kobayashi Marus*, however, are not necessary mistakes; that is, a person can avoid adopting a mistaken answer to the *Kobayashi Maru* by declining to address the problem, by simply refusing to play the game. In one sense, of course, that option was unavailable to the Delaware Supreme Court since its jurisdiction over appeals of final orders from the Court of Chancery is mandatory.[671] Hence, once the plaintiffs in *Van Gorkom* lost on

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[669] Smith v. Van Gorkom, 488 A.2d 858, 864 (Del. 1985).

[670] In a very perceptive article, Lawrence Hamermesh follows Macey and Miller's suggestion that *Van Gorkom* be viewed as a takeover case and argues that, apart from the misguided duty of care analysis, the case in fact includes several holdings that advanced corporate law in the right direction. *See generally Gentler Critique*, *supra* note 409, at 595. He argues that, among other things, the case (a) rejected the board passivity thesis of Easterbrook & Fischel, *see, e.g.*, Frank H. Easterbrook & Daniel R. Fischel, *Takeover Bids, Defensive Tactics, and Shareholders' Welfare*, 36 BUS. LAW. 1733 (1981), and held that the board must take a position on the advisability of the merger under DGCL 251(b), *id*. at 596–97, (b) established the director's duty of candor, requiring that the board disclose to the stockholders all the material information in its possession when seeking a stockholder vote, even when directors are not interested in the matter placed before the stockholders, *id*. at 598, and (c) made clear the importance of fiduciary-outs in merger agreements by holding that target boards were not generally free to accept a superior offer on general fiduciary grounds. *Id*. at 601.

[671] DEL. CODE ANN. CONST., ART. 4, § 11(4) (2015). Of course, even if the Delaware Supreme Court avoided deciding the case, the Court of Chancery certainly could not have done so.

the merits below and filed a notice of appeal, the Delaware Supreme Court was legally required to hear the case. In a more important sense, however, the disastrous holding in *Van Gorkom* was necessary in order for Delaware to develop the well-functioning system of takeover law it has today. In that sense, *Van Gorkom* was a necessary mistake—necessary for the salutary development of Delaware law. The purpose of this Section II.B is to explain and support that claim.[672]

1. *The Need for* Van Gorkom *Immunity*

As explained above, if the Delaware Supreme Court created any special set of fiduciary duties, including *Revlon* duties, governing the conduct of directors approving the sale of their company, then those duties would have to support appropriate remedies, including monetary damages for breaches not enjoined pre-closing[673]—or at least this is implied by the common law axiom that wherever there is a right, there is a remedy.[674] But we now know that he remedy of monetary damages, which was the only possible remedy post-closing, was untenable. The solution to this problem—a solution that allowed the creation of meaningful fiduciary duties governing the board's consideration of business combination transactions, but that did not render service as a director financially irrational for qualified individuals—was possible, but not within the common law system that the Delaware Supreme Court inhabited. The solution lay in surrendering what seemed like the most obviously correct principle in the system—the principle that for every right there is a remedy. As often happens, genius is manifested in the denial of what everyone knows to be indisputably, irrefutably, necessarily true.

In particular, the solution lay in abolishing the remedy of monetary damages for violations of the duty of care. While stockholders always *could* bring actions pre-closing seeking to enjoin

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[672] *Cf.* Sharfman, *supra* note 57, at 289–90 (arguing that "the enduring legacy of *Van Gorkom* is the understanding that corporate directors should not be held financially liable for corporate board decisions that lack due care" and attributing this legacy not to the decision itself but the chain of events it set off, principally the enactment of Section 102(b)(7)).

[673] *See supra* text accompanying notes 54–56.

[674] *See supra* note 655 and accompanying text.

a transaction and in fact often did so (indeed, Smith in *Smith v. Van Gorkom* did so),[675] nevertheless abolishing the post-closing remedy of damages greatly incentivizes stockholders dissatisfied with a sale approved by their board to sue pre-closing when equitable relief is not only available but the preferred remedy. Creating such powerful incentives for stockholders to sue and present their best arguments pre-closing thus required something like Section 102(b)(7).[676]

And without *Van Gorkom* there would be no Section 102(b)(7). That is, perhaps a very wise legislator, devising a pre-clearance system in which a regulator reviews the actions of

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[675] *See* Smith v. Pritzker, No. 6342, 1981 WL 15145, at *5 (Del. Ch. Feb. 3, 1981).

[676] As noted above, since 2015, if the stockholder vote approving the merger was a fully informed, uncoerced vote of the disinterested stockholders, then all claims against the directors in connection with the merger are extinguished except for claims of waste, which will virtually always be immediately dismissible. Singh v. Attenborough, 137 A.3d 151, 151–52 n.3 (Del. 2016); Corwin v. KKR Fin. Holdings, Inc., 125 A.3d 304, 309 (Del. 2015). The defendant directors in *Van Gorkom* argued that the stockholder vote approving the merger with Pritzker extinguished the stockholder's claims. Smith v. Van Gorkom, 488 A.2d 858, 888 (Del. 1985). The Delaware Supreme Court accepted this argument. *Id.* It is now well understand that *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009), did not overrule *Van Gorkom* on this point but merely clarified that the term *ratification* does not properly apply to stockholder votes required by the DGCL to approve a corporate action, such as the vote required by Section 251 to approve a merger. *Corwin*, 125 A.3d at 309–11. But the Supreme Court in *Van Gorkom* also held that the proxy statement used in connection with the stockholder meeting to consider the Pritzker transaction did not disclose all of the material facts in possession of the board, and thus, the stockholder vote was not fully informed and hence ineffective in extinguishing the fiduciary claims against the directors. *Van Gorkom*, 488 A.2d at 890–92. Even after *Corwin*, in the absence of a Section 102(b)(7) provision in the corporate charter, a plaintiff-stockholder may argue post-closing that the stockholder vote was not fully informed, and if the plaintiff succeeds on this score, the directors would be liable in monetary damages for any breaches of their duty of care, including under *Revlon*. In the presence of a Section 102(b)(7) provision, the plaintiff-stockholder has to argue that any material misstatement or omission in the disclosure resulted from a breach of the board's duty of loyalty—a claim that, in a third-party transaction in which the directors were not otherwise interested—is very unlikely to succeed. *See* Larkin v. Shah, C.A. No. 10918-VCS, 2016 WL 4485447, at *20 (Del. Ch. Aug. 25, 2016). The upshot is that, even after *Corwin*, Section 102(b)(7) remains very important in insulating directors from post-closing actions for damages in merger cases.

directors in approving a sale of the company, would realize that an effective overall system required the elimination of personal liability of directors in the relevant cases. Delaware corporate law, however, is not a regulatory scheme designed by some jurisprudential mastermind, but a common law system that proceeds one case at a time, with judges reasoning by analogy from one case to the next.[677] There was no mechanism whereby the Delaware courts could implement a pre-clearance system in one fell swoop; on the contrary, the system has to evolve step-by-step in the common law fashion. The development of the law proceeded apace, but in *Van Gorkom* the courts reached a *Kobayashi Maru*: whatever they did next, the result would be disaster. The situation is analogous to that of people playing a very complicated board game who suddenly discover that a position has arisen on the board in which the complex rules of the game require contradictory things—for instance, one rule requires that a certain piece be moved to a given location on the board, but another rule prohibits such moves in the unusual position on the board. In such cases, there is no way forward within in the system. The rules of the system have to be changed, and this can be done only from outside the system. When the Delaware Supreme Court decided *Van Gorkom*, it threw Delaware law into just such a situation, and only action by the legislature could create a way forward.

But this shows the unique, positive contribution of *Smith v. Van Gorkom* to the development of Delaware corporate law. The system contained a latent contradiction: no system of corporate law could simultaneously (a) impose special fiduciary duties on directors (thus creating correlative rights in the stockholders) in approving a sale of the company beyond duties of good faith and loyalty, (b) provide a remedy for every violation of a right, and (c) make the position of directors economically sustainable. Prior to *Van Gorkom*, no one saw the contradiction latent in the conjunction of these three premises. Unless the contradiction became apparent, the legislative action needed to create a right that would sometimes be without a remedy would never have occurred. That contradiction became apparent only with the Delaware Supreme Court's decision in *Van Gorkom*. In short, if there were

[677] *See, e.g.*, Edward H. Levi, *An Introduction to Legal Reasoning*, 15 U. CHI. L. REV. 501 (1948).

no *Van Gorkom*, there would be no Section 102(b)(7), and if there were no Section 102(b)(7), there could be no special duties for directors in selling their company—that is, there could have been no *Revlon* duties. Hence, no *Van Gorkom*, no *Revlon*.[678]

2. *The Solution in Section 102(b)(7) Exculpation Provisions*

Probably no one involved in enacting Section 102(b)(7) in Delaware in 1985 and 1986 was thinking in terms of creating a system of pre-clearance, whereby the Delaware courts would review the actions of directors who had approved a sale of their corporation to determine whether they had complied with their fiduciary duties, enjoining the merger and ordering corrective equitable relief if the courts determined that directors had breached those duties. Part of that system, of course, was in place and had been in place for a very long time. It was already common for stockholders to sue directors, seeking to enjoin a corporate action for which the directors were seeking approval at an upcoming stockholders meeting. This is precisely what happened in *Van Gorkom* and any number of other cases.[679] In one very important sense, Delaware already had a pre-clearance system.

Rather than developing a pre-clearance system of merger review, in the aftermath of *Van Gorkom*, the immediate problem for Delaware lawyers was the collapsing D&O insurance market[680] and the well-grounded fear that directors felt concerning

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[678] By analogous reasoning in the takeover and deal-protection contexts, there could also have been no *Unocal*. Consider, for instance, the potential liability of directors who prevented a hostile takeover by adopting a poison pill and were later found by the court to have breached their duty of care in so doing. Presumably, they would be liable in damages for entire amount of the premium in the lost offer. In this regard, also see the discussion of Macey & Miller, *supra* note 23.

[679] *See, e.g.*, Sinclair Oil Corp. v. Levien, 280 A.2d 717, 721–22 (Del. 1971).

[680] *See* Bainbridge, *supra* note 60, at 198 (stating that the "perception that the decision had significantly increased director liability exposure drove dramatic changes in the director and officer … liability insurance market"); Veasey et al., *supra* note 60, at 400–01 (discussing how some D&O carriers withdrew from the market or raised premiums and deductibles as a result of *Van Gorkom*); Allen, Jacobs & Strine, *supra* note 31, at 458 n.36 (stating that "after *Van Gorkom*, the D & O insurance industry sharply increased their premiums and in some cases, threatened to stop writing D & O insurance

potentially ruinous liability imposed for purely honest mistakes in judgment (or what courts would later *deem* to be mistakes in judgment) about the amount and quality of information they considered before making a business decision. Something had to be done to make serving as a director not economically irrational.

By late 1985, the Corporation Law Section of the Delaware Bar Association was considering various possible amendments to the Delaware General Corporation Law to address the problems created by *Van Gorkom*.[681] Based on analogies to the law of trusts, some Delaware practitioners had argued that a provision in the corporation's charter could limit[682] or eliminate personal liability for the directors for breaches of their duty of care,[683] but others doubted whether such a provision would be legal under the DGCL.[684] Ultimately, on June 18, 1986, the Delaware General Assembly enacted[685] what is now Section 102(b)(7) of the DGCL, which provides that a Delaware corporation's certificate of incorporation may include a provision limiting or eliminating the personal liability of directors for monetary damages for breaches

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policies."). Nevertheless, it remains a matter of dispute whether, or to what extent, the crisis in the D&O insurance markets in 1985 and 1986 resulted from *Van Gorkom* and perhaps other cases holding directors liable in damages or from other factors. *See* BALOTTI & FINKELSTEIN, *supra* note 346, at 4-99–100; Hartman & Rogers, *supra* note 346, at 525 (arguing that many predictions of dire consequences flowing from *Van Gorkom* were exaggerated). Probably, there were many forces at work, some antedating *Van Gorkom*. It would seem clear, however, that *Van Gorkom* exacerbated whatever problems already existed in the market.

[681] *See* BALOTTI & FINKELSTEIN, *supra* note 346, at 4-99 n.565.

[682] Section 102(b)(7) provisions can limit, as opposed to eliminate, such liability by capping the liability at a stated dollar amount. *See id.* at 4-99–100. The fact that the market has clearly rejected this option (Section 102(b)(7) provisions virtually universally eliminate such liability completely) strongly suggests that a system that would fine directors a relatively small amount for careless decisions rather than impose on them liability for the entire harm caused, *see, e.g.*, Renee M. Jones and Michelle Anne Welsh, *Toward a Public Enforcement Model for Directors' Duty of Oversight*, 45 VAND. J. TRANSNATIONAL L. 343 (2012), is inefficient.

[683] *See, e.g.*, UNIF. TRUST CODE § 1008 (UNIF. LAW COMM'N 2000) (amended 2010).

[684] BALOTTI & FINKELSTEIN, *supra* note 346, at 4-100.

[685] 65 Del. Laws Ch. 289, §§ 1, 2, 102(b)(7) (1986); *see also* Bainbridge, *supra* note 60, at 221–22 (discussing the enactment of Section 102(b)(7)).

of their fiduciary duties, other than for breaches of their loyalty, for acts or omissions not in good faith or involving intentional misconduct or knowing violation of law, for willful or negligent conduct in paying dividends or repurchasing stock out of other than lawfully available funds, or for any transaction from which the director derives an improper personal benefit.[686] Section 102(b)(7) thus allows corporations to eliminate the directors' personal liability in monetary damages for breaches of the *Van Gorkom* duty of care.[687] It creates the possibility of what may fancifully be called *Van Gorkom* immunity.

Soon after the enactment of Section 102(b)(7), most public companies incorporated in Delaware proposed to their stockholders an amendment to the corporation's charter adding a provision of the kind authorized by the section, and these proposals virtually always passed.[688] Nowadays, virtually every public company incorporated in Delaware has such a provision in its charter.[689] Moreover, most other states copied Section 102(b)(7),[690] and so public companies in the United States, even those not incorporated in Delaware, almost always have a substantially similar provision in their articles of incorporation.[691]

From practically any jurisprudential point of view, Section 102(b)(7) is an extremely unusual statute. This is certainly true from the point of view of economic analysis. For, whether it be under *Van Gorkom*'s duty of care or *Revlon*'s *Revlon* duties, directors of a Delaware corporation owe certain duties to their stockholders, which means that the stockholders hold correlative

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[686] DEL. CODE ANN. tit. 8, § 102(b)(7) (2015).

[687] *See* Balotti & Gentile, *supra* note 351, at 5, 7, 8–11; Lee, *supra* note 351, at 241, 259.

[688] Lee, *supra* note 351, at 272.

[689] Hamermesh, *supra* note 23, at 477, 490 (reporting that of 100 Fortune 500 companies sampled, each of 98 stock corporations in the sample incorporated in a jurisdiction allowing exculpatory charter provisions had such provisions, including all Delaware corporations in the sample); *see also* Bainbridge, *supra* note 60, at 198 (describing Section 102(b)(7) provisions as "now nearly universal"). *See generally* Veasey et al., *supra* note 60, at 401–04 (1987) (discussing Section 102(b)(7) exculpation).

[690] *See* DeMott, *supra* note 350, at 297; Hamermesh, *supra* note 23, at 477, 479 (stating that statutes like Section 102(b)(7) have been "almost universally enacted since *Van Gorkom*").

[691] DeMott, *supra* note 350, at 301 n.33; Hamermesh, *supra* note 23, at 490.

rights against the directors. It is a truism in the economic analysis of law that a right may be enforced by a property rule, under which a violation of the right supports an injunction enjoining the violation, or by a liability rule, under which a violation of the right supports an action for monetary damages,[692] with the choice of rule turning on which involves the lower transaction costs in the particular situation.[693] In corporate law, the situation is complicated because the allocation of rights between directors and stockholders is so complex, but from the economic point of view, the pre–Section 102(b)(7) system seems fairly typical. When the directors take action threatening an inefficient transfer of rights (for instance, by agreeing to sell the corporation too cheaply), the stockholders' rights are protected from the anticipated breach by a property rule supporting an injunction, the reason being that, prior to an actual breach, this is by far the cheapest remedy. When an inefficient transfer of rights has actually occurred, however, the pre–Section 102(b)(7) system provided a remedy implementing a liability rule—that is, monetary damages. The reason was that, at that point, enforcing a property rule would amount to rescission—returning the rights to the parties who valued them most highly—but of course the transaction costs of unscrambling the eggs are extremely high, higher even than the expensive and error-prone battle of evaluation experts involved in awarding monetary damages. Expensive as it may be, a liability rule in such cases is cheaper.

But then *Van Gorkom* revealed that implementing the post-closing remedy based on the liability rule ran into the problem that directors, who would have to pay monetary damages under the liability rule, either literally did not have enough money to do so—the damages exceeded their net worth and would send them into bankruptcy—or would decline to participate in a system in which their expected costs greatly exceeded their expected benefits. In other words, *Van Gorkom* highlighted an assumption of the economic analysis that people almost always forget immediately

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[692] Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089, 1106–10 (1972).

[693] *See, e.g.*, DAVID D. FRIEDMAN, LAW'S ORDER, WHAT ECONOMICS HAS TO DO WITH LAW AND WHY IT MATTERS 57–61 (Princeton U. Press ed., 2000).

after making: that the transfers analyzed produce no wealth effects for the people involved—in practice, that they are all very small in relation to the person's total wealth. The damages to which directors could be subject under a liability rule enforcing post-closing the stockholders' rights would most certainly produce a wealth effect for the directors. Indeed, the costs to the directors were generally so high that they would likely drop out of the system entirely. In these unusual facts, the costs of using a liability rule become the cost of losing the participation of qualified individuals as directors—i.e., ultimately the costs of losing the benefits of the entire system separating ownership and control in public companies.

It is not hard to see how those costs greatly exceed the benefits arising from correcting post-closing inefficient transfers of the stockholders' rights in those (hopefully few) cases that were not enjoined pre-closing. In other words, although the stockholders' rights post-closing could be protected by a property rule requiring rescission of the transaction (which everyone agrees was too costly a remedy), or by a liability rule holding the directors liable in damages (which *Van Gorkom* revealed to be an even *more* costly remedy), there was a third alternative: not protect the stockholders' rights in such cases and suffer a third set of costs, to wit, the costs of allowing some inefficient corporate transactions that occur because of the reduced incentives directors would have to be diligent in approving business combination transactions if they know that, post-closing, they will not be held liable in damages for mere errors in judgment.[694] The costs of this third way are certainly real, but they can be reduced by raising the percentage of claims that are reviewed pre-closing, an outcome that Section 102(b)(7) gives stockholders and their

[694] See Elson and Thompson, who argue that "the *Van Gorkom* context does not fit within the set of circumstances in which judicial gap filling is the optimal constraint" and thus "private ordering by contract or norms by which directors obtain equity ownership in their companies can be more effective than fiduciary duty in addressing the issues that concerned the court in *Van Gorkom*." Elson & Thompson, *supra* note 9, at 582. *Contra* John C. Coffee, Jr., *Litigation and Corporate Governance: An Essay on Steering Between Scylla and Charybdis*, 52 GEO. WASH. L. REV. 789, 798 (1984) (arguing that the duty of care is more useful as expressing an aspiration norm than a legally enforceable one).

counsel a strong incentive to pursue.[695] But *all* solutions to *all* problems are costly, and the economically rational solution is not the costless one (there is no such solution) but the lowest cost solution available. In cases like *Van Gorkom*, we have the very unusual situation in which the cheapest way to enforce a right is not to enforce it at all, for all available means of enforcement produce even higher costs than the costs of not enforcing the right. Section 102(b)(7) allows exactly that outcome.[696]

3. The Van Gorkom–Revlon *Pre-Clearance System*

The result of all this was the current Delaware system of pre-clearance of merger transactions. When the board announces that it has agreed to a merger, almost inevitably a stockholder (or, perhaps most accurately, an attorney specializing in such suits) sues, alleging that directors breached their duties in connection with the merger. The Court of Chancery will consider the case on a motion for a preliminary injunction, which requires the court to determine whether the plaintiffs have demonstrated

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[695] Elson and Thompson argue convincingly that these costs can be reduced in other ways as well, including especially through improving directors' incentives by compensating them with equity in the company rather than cash. "In this setting, it makes more sense to use a pre-decision incentive structure that relies on the personal economic interest of the directors whose conduct we are trying to police instead of after-the-fact judicial sanctions," and "such an incentive structure can be created by linking directors' personal wealth to their companies' success or failure … by making them substantial [stock]holders." Elson & Thompson, *supra* note 9, at 587. *See generally* R. Franklin Balotti, Charles M. Elon & J. Travis Laster, *Equity Ownership and the Duty of Care: Convergence, Revolution, or Evolution?*, 55 BUS. LAW. 661 (2000).

[696] Schwartz and Wiles defended *Van Gorkom* on the grounds that it would "insure the continued confidence of investors and the electorate in the essential fairness of the stock market and of economic society generally" even though the decision may be at odds with "pure economic efficiency and a minimization of transaction costs." Schwartz & Wiles, *supra* note 330, at 445. In its assumption that inspiring confidence on the one hand, and reducing transaction costs and promoting efficiency (they are often the same thing) on the other, cut in opposite directions, this reasoning is fairly confused. Why would the adoption of a rule that reduces the return on stocks inspire people to invest in the stock market? But to the extent that there was any such loss of confidence because of Section 102(b)(7), this is a genuine cost. *Id.*; *see also* Drury, *supra* note 57, at 141–43.

that they have a reasonable likelihood of success on the merits, that they will face an irreparable injury if the injunction does not issue, and that the balance of the equities favors issuing the injunction.[697] If the plaintiffs show a reasonable likelihood of success on the merits—if, that is, they have shown that the directors likely breached their fiduciary duties in approving the merger—then it almost always follows that the plaintiffs have also shown that they face an irreparable injury—the consummation of the merger at too low a price. In such cases, if other bidders have emerged and made superior offers for the company, the Delaware courts have always issued an appropriate injunction. When no other bidders have emerged, the courts have found that, provided that appropriate supplemental disclosure is made to the stockholders, the merger may be considered at a meeting of the stockholders, the theory being that fully informed and uncoerced stockholders are best placed to decide whether the transaction is value-maximizing even despite the fiduciary breaches by the directors.[698]

Of course, if the plaintiffs do not show a reasonable likelihood of success on the merits (or if they do, but, as explained above, the Court of Chancery still declines to issue an injunction), then the plaintiffs can appeal as of right to the Delaware Supreme Court. Assuming the result of this appeal is the same, the merger will be submitted to the stockholders. Only if the stockholders vote to approve the merger, of course, will the merger actually close.[699] Historically, in this situation, most plaintiffs abandon their suits, because unless they are alleging bad faith breaches or breaches of the directors' duty of loyalty, after closing, when the only available remedy is monetary damages, their suits become subject to dismissal because of the inevitable Section 102(b)(7) provision in the corporation's charter.[700] After the

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[697] *See, e.g.*, Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 178, 179 (Del. 1986).

[698] *See, e.g.*, *In re* El Paso Corp. S'holder Litig., 41 A.3d 432 (Del. Ch. 2012); *In re* Netsmart Tech., Inc. S'holders Litig., 924 A.2d 171, 192–95, 209–10 (Del. Ch. 2007).

[699] *See* DEL. CODE ANN. tit. 8, § 251 (2017).

[700] *See, e.g.*, *In re* Cornerstone Therapeutics Inc., S'holder Litig., 115 A.3d 1173, 1179–82 (Del. 2015); Malpiede v. Townson, 780 A.2d 1075, 1093–96 (Del. 2001); *see also* Hamermesh, *supra* note 23, at 490 (stating that exculpatory

Delaware Supreme Court decided *Corwin* in 2015, of course, the plaintiffs' position became even more difficult.[701]

The system thus created is similar to the pre-clearance system under the Hart-Scott-Rodino Antitrust Improvements Act of 1976.[702] Under that system, parties in the United States seeking to effect a business combination meeting certain modest threshold requirements regarding the purchase price paid and the revenues and assets of the parties involved[703] are required to give notice to the Department of Justice (DOJ) or the Federal Trade Commission (FTC),[704] providing the relevant agency with certain information regarding the transaction and the products and services that the parties sell and the markets in which they operate.[705] Under the statute, the filing by the parties starts a thirty-day clock.[706] If the transaction raises no antitrust concerns, the relevant agency will grant "early termination" within this thirty-day period, and the parties are then free to complete the

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provisions like those authorized by Section 102(b)(7) "have rendered damage claims for breach of the duty of care essentially non-existent").

[701] *See supra* note 676 and accompanying text (discussing the effect of *Corwin*).

[702] Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (2006). *See generally*, AREEDA & HOVENKAMP, ANTITRUST LAW (2d ed. 2000); STEPHEN M. AXINN ET AL., ACQUISITIONS UNDER THE HART-SCOTT-RODINO ANTITRUST IMPROVEMENT ACT (2008); PREMERGER NOTIFICATION PRACTICE MANUAL (Anthony W. Swisher & Neil W. Imus, eds., 4th ed. 2007).

[703] The rules are fairly complicated, and the dollar thresholds are indexed to the United States Gross Domestic Product and, thus, are adjusted every year. In 2017, if the value of the transaction exceeds $323 million a filing is required. If the value of transaction falls below $80.8 million, a filing is *not* required. If the value of the transaction is between these two, a filing may or may not be required depending on the revenues and assets of the persons involved. *See* FTC Revised Jurisdictional Thresholds for Section 7A of the Clayton Act, 82 FED. REG. 8524 (Jan. 26, 2017).

[704] The agency that has jurisdiction depends on the industries in which the parties operate as per an inter-agency agreement between the DOJ and the FTC. *See* MEMORANDUM OF AGREEMENT BETWEEN THE FEDERAL TRADE COMMISSION AND THE ANTITRUST DIVISION OF THE UNITED STATES DEPARTMENT OF JUSTICE CONCERNING CLEARANCE PROCEDURES FOR INVESTIGATIONS 3–5, 8–11 (Mar. 5, 2002), https://www.justice.gov/sites/default/files/atr/legacy/2007/07/17/10170.pdf [https://perma.cc/W2X9-4Q85].

[705] AXINN ET AL., *supra* note 702, 295–312 (explaining what information must be included in HSR filing).

[706] 15 U.S.C. § 18a(b) (2006).

merger.[707] If the agency is concerned that the merger may violate the antitrust laws, it will typically issue a "second request" for additional information regarding the issues about which it has concerns.[708] This stops the thirty-day clock and usually triggers an extended regulatory approval process, often involving negotiations between the government and the parties concerning divestitures and other conditions on the operations of the combined company after the merger.[709] If the results of this process satisfy the agency, the agency will terminate the review, and the parties will be free to close the merger in accordance with their agreement with the government. If the agency and the parties do not reach an agreement, then the parties will usually abandon the merger.[710] If they do not, the agency generally sues to enjoin the merger, and a federal court will decide whether to issue an injunction.

Under the HSR Act, providing the required notice to the government is mandatory (except for certain very small transactions), whereas in Delaware review of the transaction depends on a plaintiff bringing a suit, but with 84 percent of all public-company mergers being challenged in 2015, this is not much of a difference.[711] In the HSR system, there is often a negotiation between the government and the parties, and in the Delaware system there is often a settlement process between the plaintiffs and the board, usually concerning additional disclosure the board will make to the stockholders before the stockholder meeting.[712] In

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[707] *See* DEPARTMENT OF JUSTICE ANTITRUST DIVISION, BACKGROUND INFORMATION ON THE 2006 AMENDMENTS TO THE MERGER REVIEW PROCESS INITIATIVE 3, (Dec. 12, 2006), https://www.justice.gov/sites/default/files/atr/legacy/2006/12/15/220241.pdf [https://perma.cc/UZ9B-FG8M].

[708] *Id.* at 3–6.

[709] *Id.* at 6–8.

[710] Justin Sayers & Nathan Bomey, *Aetna, Humana abandon $37 billion merger*, JOURNAL SENTINEL (Feb. 14, 2017), http://www.jsonline.com/story/money/business/2017/02/14/aetna-humana-abandon-37-billion-merger/97889790/ [https://perma.cc/3GAK-J4DZ].

[711] Cornerstone Research, *Shareholder Litigation Involving Acquisitions of Public Companies* 1 (2016), https://www.cornerstone.com/Publications/Reports/Shareholder-Litigation-Involving-Acquisitions-2016.pdf [https://perma.cc/497K-7F7H]

[712] *See In re* Trulia, Inc. S'holder Litig., 129 A.2d 884 (Del. 2015); Peter J. Walsh Jr. & Aaron R. Sims, Trulia *and the Demise of "Disclosure Only" Settlements in Delaware*, BUS. L. TODAY (2016), https://www.americanbar.org/publications/blt/2016/02/delaware_insider.html [https://perma.cc/Z2CY-QARP].

both systems, if there is a serious legal problem with the merger, the transaction will be likely be enjoined (or abandoned), and in both systems if an injunction does not issue, the matter is usually at an end. Although the government can challenge a merger on antitrust grounds after the merger has closed, such cases are rare.[713]

It is notable in this regard that the HSR pre-clearance system is regarded as a great advance in antitrust enforcement and has been widely copied around the world, including by the European Union and the Japanese and Chinese antitrust authorities. As suggested in this Article, its key procedural features have been reproduced in Delaware as well—albeit for quite different purposes.

CONCLUSION

Genius is of various kinds. In some cases, it involves doing much better than everyone else, something that other people are already doing. In other cases, it involves doing something no one else ever thought of doing, thus opening up whole new realms of human achievement. Shakespeare, Mozart, and Gauss had genius of the first kind, while Dante, Beethoven, and Frege had genius of the second kind. It is surely hyperbolic to compare any accomplishment in corporate law with the achievements of Dante, Beethoven, or Frege, but there is still a certain limited analogy. The advances in corporate law achieved by *Unocal* and *Revlon* involved the first kind of genius: they developed existing materials in excellent ways to substantially improve on past results. The advance in corporate law jointly achieved by *Van Gorkom* and Section 102(b)(7), however, is of the second kind.[714] It required seeing that what everyone implicitly assumed was true—that every right has a remedy—need not be true, and that changing

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[713] *See* Brent Kendall, *U.S. Seeks to Undo Parker-Hannifin's Clarcor Deal on Antitrust Grounds*, WALL ST. J. (Sept. 26, 2017). *See generally* J. Thomas Rosch, *Remarks before the ABA Section of Antitrust Law Spring Meeting: Consummated Merger Challenges—The Past is Never Dead*, F.T.C. (May 29, 2012), https://www.ftc.gov/sites/default/files/documents/public_statements/consummated-merger-challenges-past-never-dead/120329springmeetingspeech.pdf [https://perma.cc/LP4D-JGC3].

[714] Martin Lipton's invention of the poison pill, which the Delaware Supreme Court declared legal in *Moran v. Household Int'l, Inc.*, 500 A.2d 1346, 1352, 1355–57 (Del. 1985), the fourth great case in the miracle year of 1985, also involves genius of this second kind.

this assumption could produce a significantly better system. I do not pretend that the justices in the majority in *Van Gorkom* understood all this and intended to create the system of take-over regulation Delaware now has. They surely did not. But that does not change the fact that *Van Gorkom*, albeit in a unique way, was a great and necessary step forward in the development of Delaware corporate law.