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NOTES

REVISITING *REVLON*: THE RUMORS OF ITS DEMISE HAVE BEEN GREATLY EXAGGERATED

On November 4, 1982, MacAndrews & Forbes, Inc. commenced a two-stage, friendly tender offer for the shares of Technicolor, Inc.¹ Several large Technicolor shareholders opposed this offer, refusing to tender in the initial offer and subsequently dissenting from the second-stage merger and petitioning the Delaware Court of Chancery for an appraisal proceeding.² Not until fully twelve and one-half years later, after seven reported opinions, including three trips to the Delaware Supreme Court, did the shareholders finally lose on all claims.³ The intervening

1. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1160 (Del. 1995) (*Technicolor III*).

2. *Id.*

3. *Cede & Co. v. Technicolor, Inc.*, No. CIV.A. 7129, 1990 WL 161084 (Del. Ch. Oct. 19, 1990) (finding, after an appraisal proceeding, that the shareholder-plaintiffs had obtained a fair price for their shares), *remanded by* 634 A.2d 345 (Del. 1993) (affirming the chancery court's opinion that the transaction met the entire fairness test, holding that the directors had breached their duty of care, and remanding for a liability hearing to determine whether the transaction was entirely fair), *modified in part*, 636 A.2d 956 (Del. 1994), *remanded sub nom. Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134 (Del. Ch.), *aff'd*, 663 A.2d 1156 (Del. 1995); *Cinerama, Inc. v. Technicolor, Inc.*, *reprinted in* 17 DEL. J. CORP. L. 551, 596 (Del. Ch. June 21, 1991) (entering judgment for the defendants because, although the defendants had breached their duty of care, the plaintiffs had failed to prove that they had been injured), *aff'd in part and rev'd in part sub nom. Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345 (Del. 1993), *modified in part*, 636 A.2d 956 (Del. 1994), *remanded sub nom. Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134 (Del. Ch.), *aff'd*, 663 A.2d 1156 (Del. 1995); *Cede & Co. v. Technicolor, Inc.*, *reprinted in* 13 DEL. J. CORP. L. 225 (Del. Ch. Jan. 13, 1987) (holding that the plaintiff-shareholders must elect between an appraisal or personal liability action and that both such actions could not be maintained), *appeal accepted sub nom. Cinerama, Inc. v. Technicolor, Inc.*, 523 A.2d 981 (Del.), *aff'd in part and rev'd in part sub nom. Cede & Co. v. Technicolor, Inc.*, 542 A.2d 1182 (Del. 1988) (allowing the plaintiff-shareholders to proceed with both appraisal and personal liability duty-of-care actions).

For the sake of clarity, this Note will refer to *Cede & Co. v. Technicolor, Inc.*,

period was an era of unprecedented change not only in corporate finance but in the law governing the actions of corporate directors. This Note will examine the current status of that law following the final two *Technicolor* opinions⁴ and two other cases in which the court revisited the corporate boardroom after a respite of several years.⁵ The most famous of these opinions, *Paramount Communications Inc. v. QVC Network Inc.*,⁶ has been the subject of extensive commentary, often suggesting that the decision represents a significant departure from prior Delaware takeover case law.⁷ This Note will argue that each of these recent cases is consistent with, and a clarification of, existing law, providing not only insight into how courts will examine future litigation but also step-by-step guidance for directors to follow in their decisionmaking process.

The Technicolor tender offer may have been only an advance ripple of the then imminent tidal wave of mergers and acquisitions that would "[shake] corporate America to its very core" during the 1980s.⁸ Rapid financial innovation enabled many acquisitions that would not previously have been possible.⁹ Whereas some companies once felt safe because of their size or

542 A.2d 1182 (Del. 1988), as *Technicolor I*, *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345 (Del. 1993), *modified in part*, 636 A.2d 956 (Del. 1994), as *Technicolor II*, and *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156 (Del. 1995) as *Technicolor III*.

4. *Technicolor III*, 663 A.2d 1156; *Technicolor II*, 634 A.2d 345.

5. *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361 (Del. 1995) (examining Unitrin's defensive measures in response to American General's tender offer); *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34 (Del. 1994) (granting an injunction to QVC to prevent the sale of Paramount to Viacom unless Paramount conducted further bidding).

6. 637 A.2d 34.

7. *See infra* note 30.

8. Steven J. Fink, *The Rebirth of the Tender Offer?* *Paramount Communications, Inc. v. QVC Network, Inc.*, 20 DEL. J. CORP. L. 133, 134 n.7 (1995) (citing Michael Bradley, *SEC Neglect and the Extinction of the Hostile Takeover*, in MODERNIZING U.S. SECURITIES REGULATION: ECONOMIC AND LEGAL PERSPECTIVES 293 (Kenneth Lehn & Robert W. Kamphuis, Jr. eds., 1992)). For a fascinating and insightful collection of war stories of an attorney's role in many of the larger takeover battles in the late 1970s and 1980s, see LAWRENCE LEDERMAN, *TOMBSTONES: A LAWYER'S TALES FROM THE TAKEOVER DECADES* (1992).

9. *See, e.g.*, Lawrence Lederman, *Current Takeover Techniques*, in ANATOMY OF A TAKEOVER BATTLE: FROM INCEPTION TO CLIMAX 41 (Kenneth J. Bialkin et al. eds., 1986).

robust stock price, new financing techniques¹⁰ meant that almost any corporation could be considered a "target"¹¹ and thus subject to unwanted acquisition attempts or offers.¹²

This realization and the increasing pace and size of takeovers, both hostile and friendly,¹³ placed enormous pressure on corporate directors charged with a fiduciary duty to maximize shareholder welfare.¹⁴ The takeover developments forced directors to deal not only with increasingly complex transactions but also with the fundamental notion that someone (the raider) believed that he could run the company better than they could. Initially, target companies responded to the raiders with disdain;¹⁵ eventually this gave way to fear and loathing, such that the mere presence of a raider in a tender offer became a very real threat

10. Most notable among these techniques were the "high-yield" debt securities ("junk bonds") that provided previously unimaginable amounts of capital to potential acquirors. See Deborah A. DeMott, *The Biggest Deal Ever*, 1989 DUKE L.J. 1, 4, 8-9 (noting that Drexel Burnham Lambert played a major role in assisting Kohlberg, Kravis and Roberts (KKR) in achieving the largest leveraged buyout ever by placing \$5 billion of junk bonds); see also CONNIE BRUCK, *THE PREDATORS' BALL* (1989) (providing a background on Drexel and its mastermind, Michael Milken).

11. This Note will use the term "target" to refer to the corporation for sale or of which control is sought.

12. See, e.g., Andrew G.T. Moore, II, *The 1980s—Did We Save the Stockholders While the Corporation Burned?*, 70 WASH. U. L.Q. 277, 277 (1992) (noting that "acquirors and their financial advisors . . . plotted new forms of attack that made virtually any company a takeover candidate"); *id.* at 279 (noting that, because of the shift to institutional ownership, laissez-faire policies, and lower interest rates, "virtually no company, no matter how large, was immune as a potential takeover target"). Justice Moore is a former member of the Delaware Supreme Court and author of several seminal takeover opinions, including *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986), and *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261 (Del. 1989).

13. This Note will use the term "hostile" to refer to tender offers (or other transactions) to which the target's directors are opposed or have not consented. This Note will use "friendly" to refer to transactions having the consent of the target's directors.

14. See Martin Lipton & Theodore N. Mirvis, *Enhanced Scrutiny and Corporate Performance: The New Frontier for Corporate Directors*, 20 DEL. J. CORP. L. 123, 123 (1995) ("The focus was brightly put on directors as overlords of the takeover fights."). For a discussion of the fiduciary duties owed by directors, see *infra* notes 44-139 and accompanying text.

15. See, e.g., LEDERMAN, *supra* note 8, at 262 (noting that, in the face of a hostile offer from a now-famous raider, the chairman of the target company exclaimed "[T.] Boone Pickens is like a barking dog chasing a bus. What's he going to do if he catches it?").

to the target corporation. Such threats bolstered boards' decisions to enact defensive measures.¹⁶

As directors became more adept at thwarting takeover attempts (real or imagined), shareholders became more vocal and litigious in their demands that directors protect shareholder interests. Many of the mega-million dollar deals described in lurid detail on the front page of the *Wall Street Journal*¹⁷ resulted in disgruntled shareholders (angry that a deal had been thwarted or believing that a price was too low) who challenged directorial conduct in lawsuits that produced some of the most significant decisions in Delaware corporate law.¹⁸

The increasing wave of litigation put the courts under pressure as well. Traditionally, the actions of directors were subject to the judicial deference embodied in the business judgment rule: directors' actions were presumed valid because a presumption existed that they had met their duties of loyalty and due care.¹⁹ Suddenly, however, the courts had to question the validity of these assumptions. In addition to the huge amounts of money at stake, a hostile transaction put the directors' personal reputations and, possibly, their livelihood on the line.²⁰

16. Moore, *supra* note 12, at 279 ("Some of [the raiders] . . . became household names, and corporate management ran scared."); see also *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 956 (Del. 1985) (acknowledging that the threat posed by a coercive offer was exacerbated by the fact that it was made by Pickens, "a corporate raider with a national reputation as a 'greenmailer'").

17. For instance, in the last three months of 1988, the *Wall Street Journal* ran almost daily articles playing out the details of the now-historic battle for control of RJR Nabisco. This deal was perhaps the most heavily scrutinized one in history (at least until the Paramount auction, discussed *infra* at note 30), from its inception, see John Helyar et al., *RJR Nabisco Chief Considering Buy-Out of Concern for \$17.6 Billion, or \$75 a Share*, WALL ST. J., Oct. 21, 1988, at A3, through the final bidding, see Bryan Burrough, *KKR Wins Bidding Contest for RJR Nabisco with Offer of \$25.07 Billion, or \$109 a Share*, WALL ST. J., Dec. 1, 1988, at A3. The RJR deal, with its all-star cast of 1980s characters (including Ivan Boesky and Michael Milken), became the symbol of the decade, inspiring a fascinating behind-the-scenes book, BRYAN BURROUGH & JOHN HELYAR, *BARBARIANS AT THE GATE* (1990), which HBO eventually featured as a made-for-cable television movie.

18. See, e.g., *In re RJR Nabisco, Inc. Shareholders Litig.*, reprinted in 14 DEL. J. CORP. L. 1132 (Del. Ch. Jan. 31, 1989).

19. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1993) (*Technicolor II*), modified in part, 636 A.2d 956 (Del. 1994); *Grobow v. Perot*, 539 A.2d 180, 187 (Del. 1988); see also DENNIS J. BLOCK ET AL., *THE BUSINESS JUDGMENT RULE* (4th ed. 1993) (discussing developments in the law concerning the business judgment rule).

20. See, e.g., Alex Devience, Jr., *A Hindsight Review of the Business Judgment*

The courts faced many important questions. If a board enacted defensive measures, did it do so to protect the shareholders? Were defensive measures bargaining chips designed to coerce a higher price from the raider? Or were the measures simply designed to protect the directors' own self-interests and secure their positions? Similarly, if the board favored a sale to a "white knight," was the board getting the best price possible, or was it selling to someone who simply would retain the current slate of directors? Recognition of the potential transfers of wealth at stake,²¹ the personal conflicts involved,²² and, indeed, the fundamental issues of corporate management and control led courts to apply an increased level of scrutiny in transactions involving corporate control.²³

As the acquisitions waned, the suits challenging board activity necessarily tailed off as well. In the early 1990s, many of the companies that had made takeover headlines in the 1980s staggered under enormous debt, much of it in the form of the previ-

Rule in a Takeover Environment: The State of the Business Judgment Rule After the Fall, 5 DEPAUL BUS. L.J. 113, 114 (1992/1993) ("In corporate takeovers, . . . directors are likely to act with ambivalent motives due to the precarious situation in which they find themselves. . . . [T]hey know that they may be terminated if an acquisition is successful."). The situation is even more precarious for "inside" directors who are also management executives of the target. See Anup Agrawal & Ralph A. Walkling, *Executive Careers and Compensation Surrounding Takeover Bids*, 49 J. FIN. 985 (1994) (finding that senior executives of target companies are more likely to be replaced when a bid succeeds than when it fails and that such executives may be unlikely to find new positions at a similar level of responsibility).

21. See Moore, *supra* note 12, at 279 ("[T]he 1980's marked a period of massive wealth shifting, but little wealth creation."). Contrary to Justice Moore's opinion, other commentators have argued that "[t]here is strong evidence that successful tender offers are wealth-creating transactions." Fink, *supra* note 8, at 134 n.7 (emphasis added).

22. In a description that might have applied to any number of potential transactions, a district court observed that a contest for control was "[a] complex drama embrac[ing] personality conflicts, animosity, distrust, and corporate politics, as well as a display of ingenuity and sophistication by brokers, investment bankers and corporate counsel." *Wellman v. Dickinson*, 475 F. Supp. 784, 797-98 (S.D.N.Y. 1979), *aff'd*, 682 F.2d 355 (2d Cir. 1982).

23. See *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985); *infra* notes 140-75 and accompanying text. The Delaware Supreme Court noted recently that "intense scrutiny" is appropriate because of "the magnitude of a sale of control transaction and the possibility, in certain cases, that management may not necessarily be impartial." *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 44 (Del. 1994).

ously vaunted junk bond.²⁴ Several of these were in the national spotlight yet again, "[t]his time, however, the headlines read: layoffs, record losses, defaults [and] bankruptcy."²⁵ As Justice Moore noted, this slowdown gave the Delaware courts time to reflect on their takeover jurisprudence.²⁶

Transactional activity now appears to be on the rise again.²⁷ The advance guard of litigation from this new wave of mergers and acquisitions is already reaching the Delaware judiciary.²⁸ In *Paramount Communications Inc. v. QVC Network Inc.*,²⁹ the Delaware Supreme Court decided what may be the highest profile transactional lawsuit in history.³⁰ Recognizing the impact that its decision would have, the court purposely delayed announcing its ruling until after the stock markets had closed.³¹ Although much of the popular attention arose from the identity (and business) of the companies involved,³² the court's ruling

24. See, e.g., Jeffrey A. Trachtenberg et al., *Buy-Out Bomb: An Extra \$500 Million Paid for Federated Got Campeau in Trouble*, WALL ST. J., Jan. 11, 1990, at A1 (noting that Campeau was on the "brink of insolvency," due in large part to \$1.15 billion in junk bond debt, which had been used to finance Campeau's acquisition of Federated Department Stores following a bidding war with a rival suitor). The problems of high-yield debt, however, were not faced solely by victorious bidders. Many companies had "strapped on" such debt in (often successful) efforts to fend off hostile bidders. See James P. Miller, *USG Will Try To Restructure Its Debt As It Misses Principal, Interest Payments*, WALL ST. J., Jan. 2, 1991, at C15.

25. Moore, *supra* note 12, at 277.

26. *Id.* at 283.

27. See, e.g., Gregg Steinmetz, *Mergers and Acquisitions Ran at Record Pace in Third Quarter*, WALL ST. J., Sept. 30, 1994, at C1.

28. See, e.g., *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34 (Del. 1994). QVC has been described as the "most significant [case] since the landmark Time-Warner judgment four years ago." Martin Dickson, *Barbarians Waiting at the Gate*, FIN. TIMES, Dec. 9, 1993, at 25.

29. 637 A.2d 34.

30. Oral arguments were broadcast live nationwide on Court TV and, due to the large number of people in actual attendance, the Delaware Supreme Court heard these arguments at a larger courtroom in Wilmington, rather than in its usual venue in Dover. Lawrence A. Cunningham & Charles M. Yablon, *Delaware Fiduciary Duty Law After QVC and Technicolor: A Unified Standard (and the End of Revlon Duties?)*, 49 BUS. LAW. 1593, 1593 (1994). In addition, CNN interrupted its afternoon prime news to carry Justice Veasey's announcement of the court's ruling live. See *Live Report: Viacom-Paramount Lose Bid To Merge in Delaware* (CNN television broadcast, Dec. 9, 1993) (LEXIS Transcript #259-1), available in LEXIS, News Library, Script File [hereinafter *CNN Live Report*].

31. *CNN Live Report*, *supra* note 30.

32. See, e.g., *id.* ("We're looking at the future of television in America, and indeed,

and analysis has itself been the subject of commentary suggesting a cataclysmic impact on the nature of directorial duties.³³ This Note, however, will argue that QVC and other recent cases must be read in context and as part of an unbroken chain in the evolution of the business judgment rule as applied in change-of-control transactions.

The fallout of the takeover frenzy of the 1980s and the resulting swarm of litigation resulted in a three-tier system of judicial scrutiny of directorial decisions: "the traditional business judgment rule, the *Unocal* standard of enhanced judicial scrutiny, or the entire fairness analysis."³⁴ Much of the relevant litigation focused on which of these seemingly diverse standards would attach to the board's action because the level of scrutiny often was decisive.³⁵ Invoking the proper standard remains central to the Delaware judiciary's analysis of change-of-control transactions, and it is further possible to classify the cases into two categories: (1) injunctive or "transactional justification"³⁶ suits by bidders seeking to enjoin a target company's defensive measures or to enjoin the imminent sale of the target company to a rival bidder³⁷ and (2) suits brought by disgruntled shareholders following the closing of a change-of-control transaction,

the world.").

33. See, e.g., Cunningham & Yablon, *supra* note 30, at 1595 (arguing that, as a result of QVC and *Technicolor*, "the so-called 'Revlon duty' . . . no longer exists under Delaware law"); Paul L. Regan, *The Unimportance of Being Earnest: Paramount [v. QVC] Rewrites the Rules for Enhanced Scrutiny in Corporate Takeovers*, 46 HAST. L.J. 125, 127-28 (1994) (arguing that QVC represents a "new judicial activism in Delaware . . . which unduly emphasizes responsibility to shareholders at the expense of managerial authority, freedom, and innovation").

34. *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361, 1371 (Del. 1995).

35. See, e.g., *A.C. Acquisitions v. Anderson, Clayton & Co.*, 519 A.2d 103, 111 (Del. 1986) ("Because the effect of the proper invocation of the business judgment rule is so powerful and the standard of entire fairness so exacting, the determination of the appropriate standard of judicial review frequently is determinative of the outcome of [the] litigation.").

36. "Transactional justification" generally refers to the directors' burdens in an injunctive, rather than personal liability, proceeding. See, e.g., *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 180 n.10 (Del. 1986); E. Norman Veasey, *The New Incarnation of the Business Judgment Rule in Takeover Defenses*, 11 DEL. J. CORP. L. 503, 505-06 (1986).

37. See, e.g., *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34 (Del. 1994).

seeking to impose personal liability on and thus receive monetary damages from the directors due to a breach of the directors' fiduciary duties.³⁸ Since 1993, the Delaware Supreme Court has decided several cases that highlight the similarities and mild distinctions between the doctrinal analysis of each of these two litigation postures.³⁹

This Note will analyze the impact of these recent decisions on Delaware law, examining what the cases change as well as what they do *not* change. The first section will briefly explore the history and effect of the traditional business judgment rule and the application of the business judgment rule in postclosing litigation. The second section will focus on the evolution of the business judgment rule to the "enhanced scrutiny" standard of proportionality, as applied to defensive measures taken in response to hostile takeover bids under *Unocal* and its progeny.⁴⁰ This section will discuss the various threats found to justify defensive tactics and the permissible responses to such threats, concluding with the court's most recent decision in *Unitrin*.⁴¹ The third section will examine the so-called "*Revlon* zone,"⁴² in which the directors become reduced to mere "auctioneers charged with getting the best price for the stockholders."⁴³ This section will examine when the auction duty is triggered and what the duty entails. It will argue that such a duty still exists, at least in the boardroom, if not in theory, and will argue that the duty is merely a specialized application of directors' general

38. See, e.g., *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345 (Del. 1993) (*Technicolor II*), modified in part, 636 A.2d 956 (Del. 1994).

39. *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361 (Del. 1995) (examining Unitrin's defensive measures in response to American General's tender offer); *QVC*, 637 A.2d 34 (granting an injunction to QVC to prevent the sale of Paramount to Viacom unless Paramount conducted further bidding); *Technicolor II*, 634 A.2d 345 (examining a closed transaction challenged by a shareholder alleging that Technicolor's board breached its duty of care); *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156 (Del. 1995) (*Technicolor III*).

40. See, e.g., *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985); *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261 (Del. 1989).

41. 651 A.2d 1361.

42. See, e.g., Ronald J. Rinaldi, Note, *Radically Altered States: Entering the "Revlon Zone"*, 90 COLUM. L. REV. 760 (1990).

43. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986).

duty to be informed. Finally, the last section will analyze the overlap and distinctions between the duties of directors in each situation.

THE HISTORY AND OPERATION OF THE BUSINESS JUDGMENT RULE

Origins of Judicial Deference to Directors

Under the traditional scheme of corporate organization and specialization, management of the firm's business is entrusted to the board of directors.⁴⁴ In managing this business, the directors owe to the corporation twin fiduciary duties—the duty of care and the duty of loyalty⁴⁵—which comprise the “bedrock of the law of corporate governance today.”⁴⁶ In simplest terms, the duty of care requires directors to exercise the care that a reasonably prudent person would exercise under similar circumstances, and the duty of loyalty prohibits faithlessness and self-dealing.⁴⁷ Even as they articulated these duties, however, the courts expressed a great reluctance to second-guess⁴⁸ directors' business decisions.⁴⁹ This deference to the directors has been

44. DEL. CODE ANN. tit. 8, § 141(a) (1991) (“The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors.”).

45. *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939); see also BLOCK ET AL., *supra* note 19, at 1; Marcia M. McMurray, *An Historical Perspective on the Duty of Care, the Duty of Loyalty and the Business Judgment Rule*, 40 VAND. L. REV. 605, 606 (1987). Both commentators trace the origin of these responsibilities to an English case decided more than 250 years ago, *Charitable Corp. v. Sutton*, 26 Eng. Rep. 642 (1742). The Delaware Supreme Court recently restated this as a “triad” of duties, encompassing “good faith, loyalty [and] due care.” *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993) (*Technicolor II*) (emphasis added), *modified in part*, 636 A.2d 956 (Del. 1994). Whether this results in any practical change in the duties owed by directors remains to be seen. See, e.g., Charles Hansen, *The Duty of Care, the Business Judgment Rule and the American Law Institute Corporate Governance Project*, 48 BUS. LAW. 1355 (1993) (arguing that, in fact, the business judgment rule encompasses good faith and due care exclusively).

46. BLOCK ET AL., *supra* note 19, at 2.

47. *Norlin Corp. v. Rooney, Pace, Inc.*, 744 F.2d 255, 264 (2d Cir. 1994).

48. See, e.g., *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 50 (Del. 1994). Perhaps the most colorful description of this notion is found in *Gries Sports Enters., Inc. v. Cleveland Browns Football Co.*, 496 N.E.2d 959, 979 (1986) (Holmes, J., dissenting) (applying Delaware law and arguing that a business decision is “not a subject for judicial Monday morning, armchair quarterbacking”).

49. Stuart R. Cohn, *Demise of the Director's Duty of Care: Judicial Avoidance of*

embodied in the business judgment rule for at least 160 years.⁵⁰ The most commonly offered rationale for this deference is that a court, having the benefit of hindsight, should not substitute its business judgment for that of the directors.⁵¹ A second theory that supports this deference is the fear that detailed scrutiny of corporate management would curtail desirable, entrepreneurial risk-taking. All business decisions are considered to have a high level of inherent risk,⁵² and courts view the rule as allowing directors to "purchase opportunity with the coin of risk" without fear of second-guessing.⁵³ Underlying this theory is the notion that running any successful business involves making decisions that turn out, in hindsight, to have been wrong. The business judgment rule protects directors from liability for such honest mistakes.⁵⁴

Standards and Sanctions Through the Business Judgment Rule, 62 TEX. L. REV. 591, 603 (1983).

50. See, e.g., BLOCK ET AL., *supra* note 19, at 4; Franklin A. Gevurtz, *The Business Judgment Rule: Meaningless Verbiage or Misguided Notion?*, 67 S. CAL. L. REV. 287 (1994).

51. See, e.g., *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971); R. Franklin Balotti & James J. Hanks, Jr., *Rejudging the Business Judgment Rule*, 48 BUS. LAW. 1337, 1339 (1993); McMurray, *supra* note 45, at 616. But see Gevurtz, *supra* note 50, at 304-27 (arguing that this and several other purported justifications are, in fact, inaccurate).

52. See MORTIMER FEUER, *PERSONAL LIABILITIES OF CORPORATE OFFICERS AND DIRECTORS* 37 (2d ed. 1974) ("The very nature of managing business enterprises for profit requires continuous risk taking").

53. GEORGE F. WILL, *MEN AT WORK—THE CRAFT OF BASEBALL* 39 (1990). For a discussion of the value and importance of encouraging risk-taking, see *Joy v. North*, 692 F.2d 880, 886 n.6 (2d Cir. 1982) (giving an example of how a "riskier" investment may actually be worth more than a "safe" one), *cert. denied*, 460 U.S. 1051 (1983).

54. This result is true even though "honest" mistakes can be every bit as disastrous as those made with gross negligence. For a colorful discussion of the effect of honest mistakes, see *Gillette Co. v. RB Partners*, 693 F. Supp. 1266, 1288 (D. Mass. 1988). In *Gillette*, the court obtained insight on the issue of honest mistakes by watching a baseball game:

When I went home on Friday night, . . . I turned on the television. The Red Sox were playing the Royals. They were down by one run. There was a man on base and [catcher] Rich Gedman was up. He hit a ball to right field that curved toward the foul pole and went out of the park. The umpire called the ball "foul."

The umpire, I'm sure, was honest. He was competent. He had to make an instant decision. It turns out he blew it. The instant replay showed that the ball hit the foul pole, and it was a home run. It also

The Traditional, "Plain Vanilla" Business Judgment Rule: A Presumption of Validity

Transactions that neither involve a sale of control nor implicate self-dealing or other conflicts of interest are examined under the "plain vanilla"⁵⁵ version of the business judgment rule. In its most prominent form,⁵⁶ the business judgment rule "is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."⁵⁷ The presumed validity attaches to nearly all

showed that the umpire's error cost the Red Sox the game.

Id. at 1288.

55. This phrase is Chancellor Allen's. See *Spiegel v. Buntrock*, No. CIV.A. 8936, 1988 WL 124324, at *3 (Del. Ch. Nov. 17, 1988), *aff'd*, 571 A.2d 767 (Del. 1990).

56. The most prominent form is, of course, the Delaware form. This Note will focus solely on the law of Delaware, whose supreme court has been referred to as "the Mother Court of corporate law." *Kamen v. Kemper Fin. Servs., Inc.*, 908 F.2d 1338, 1343 (7th Cir. 1990), *rev'd on other grounds*, 500 U.S. 90 (1991); see also Jeffrey N. Gordon, *Corporations, Markets, and Courts*, 91 COLUM. L. REV. 1931, 1969 (1991) ("[T]he Delaware Supreme Court remains the national supreme court on corporate law.") (emphasis added). As of 1990, more than 40% of the companies listed on the New York Stock Exchange and more than 50% of the Fortune 500 corporations were incorporated in Delaware. BLOCK ET AL., *supra* note 19, at 2 (citing 1 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, *THE DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS* F-1 (2d ed. 1990 & Supp. 1995)). Commentators have argued that this concentration of resources is a direct result of the "race to the bottom," in which Delaware outpaced other states in its receptiveness to and accommodation of corporations. See, e.g., Daniel R. Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Law*, 76 NW. U. L. REV. 913 (1982); Roberta Romano, *The State Competition Debate in Corporate Law*, in *CORPORATE LAW AND ECONOMIC ANALYSIS* 216 (Lucian A. Bebchuk ed., 1990). Irrespective of the historical reasons, it is now clear that, absent a statutory modification, the overwhelming majority of state and federal courts follow Delaware's lead, especially in the area of takeovers and mergers. See Elliot J. Weiss, *Whose Rules Should Govern Takeovers: Delaware's, the ALI's or Martin Lipton's?*, 33 ARIZ. L. REV. 761, 763 (1991) ("Delaware's approach has become the national approach to resolving takeover-related controversies.").

57. *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1985). This language has been quoted or cited with approval in nearly all of the major Delaware business judgment rule cases decided after *Aronson*. See, e.g., *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361 (Del. 1995); *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 41-42 (Del. 1994); *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1993) (*Technicolor II*), *modified in part*, 636 A.2d 956 (Del. 1994); *Stroud v. Grace*, 606 A.2d 75, 83 (Del. 1992); *Spiegel v. Buntrock*, 571 A.2d 767, 774 (Del. 1990); *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 64 (Del. 1989); *Mills*

disinterested business decisions of directors.⁵⁸ The plaintiff challenging a board's business decision has the burden of rebutting this presumption of validity.⁵⁹ To rebut effectively the presumption that the board met its duty of care, the plaintiff must show that the board was grossly negligent.⁶⁰

Until 1985, much of the litigation challenging board conduct (and thus requiring application of the business judgment rule) involved allegations of directors' self-dealing or other breaches of the duty of loyalty.⁶¹ Most suits alleging only breaches of the

Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1279, 1288 (Del. 1989); Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1341 (Del. 1987); Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 180 (Del. 1986); Unocal v. Mesa Petroleum, Inc., 493 A.2d 946, 954 (Del. 1985); Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985). *But see* Charles Hansen, *The Technicolor Case—A Lost Opportunity*, 19 DEL. J. CORP. L. 617, 627-28 (1994) (arguing that the Delaware Supreme Court in *Technicolor II* ignored "the often used formulation of Aronson"). Given the court's quotation of, and reliance on, the Aronson language in *Technicolor II*, it is difficult to understand precisely what Hansen means. *See Technicolor II*, 634 A.2d at 360. *Cf.* William Prickett & Ronald A. Brown, Jr., *Cede v. Technicolor: The Supreme Court Reilluminates Existing Lines of Delaware's Level Playing Field*, 19 DEL. J. CORP. L. 593, 594-95 (1994) (arguing that *Technicolor II* "does not change Delaware law" and noting that the opinion "has already been misunderstood, even by some knowledgeable Delaware corporate practitioners").

58. *See infra* notes 82-139 and accompanying text (discussing judicial scrutiny of decisions involving conflicts of interest or self-dealing by directors). A well-known example is an Illinois court's deference, in 1968, to the Chicago Cubs baseball team's refusal to install lights and thereby play night games at Wrigley Field. *Shlensky v. Wrigley*, 237 N.E.2d 776 (Ill. App. Ct. 1968).

59. *Van Gorkom*, 488 A.2d at 872. For an argument that this presumption adds little or nothing to the burdens faced by all plaintiffs, see Gevurtz, *supra* note 50, at 292 ("This 'presumption' entails nothing more than saying that the plaintiff who challenges a decision of the board has the burden of proving that the directors breached one of their duties."); accord Balotti & Hanks, *supra* note 51, at 1345 ("The existence of a 'presumption' adds little or nothing to the burden a plaintiff would have as the party alleging gross negligence."). Whatever its technical implications, the practical implication of the business judgment rule is that the board's decision is entitled to great deference. The quibbling over the precise application of the rule has more to do with the general confusion surrounding the nature of a "presumption" than it does with the business judgment rule itself. In perhaps the preeminent article on evidentiary presumptions, Professor Morgan notes the baffling nature of the topic. *See* Edmond M. Morgan, *Presumptions*, 12 WASH. L. REV. & ST. B.J. 255, 255 (1937) (noting that writers "approach[] the topic of presumptions with a sense of hopelessness and [leave] it with a feeling of despair").

60. *Van Gorkom*, 488 A.2d at 873.

61. *See, e.g.,* Pogostin v. Rice, 480 A.2d 619 (Del. 1984); Puma v. Marriott, 283 A.2d 693 (Del. 1971).

duty of care, in any context, were unsuccessful.⁶² Today, however, the business judgment rule has become the focal point in litigation surrounding high stakes corporate control transactions.⁶³ In 1985, in *Smith v. Van Gorkom*,⁶⁴ the Delaware Supreme Court “exploded a bomb” in boardrooms across the country, holding TransUnion’s board personally liable for having violated their duties to the corporation.⁶⁵ The reaction to the case was immediate and covered every imaginable viewpoint,⁶⁶ although the overwhelming weight of the commentary was negative.⁶⁷ In response to this array of commentary and criticism, Justice Moore, who joined in the *Van Gorkom* majority opinion, called the court’s decision “one of the most misunderstood cases in corporate law.”⁶⁸

The facts of the case are now well known. Jerome Van Gorkom, the soon-to-be-retiring chairman of TransUnion, concerned about TransUnion’s excessive cash reserves, “pondered the idea of a sale” of the company.⁶⁹ With but the barest of background information concerning the company’s value, Van Gorkom privately convinced Jay Pritzker, a “social acquaintance,” to make an offer to purchase TransUnion’s stock at a

62. Moore, *supra* note 12, at 281; see, e.g., *Shlensky*, 237 N.E.2d 776.

63. See, e.g., *Van Gorkom*, 488 A.2d 858.

64. *Id.*

65. Bayless Manning, *Reflections and Practical Tips on Life in the Boardroom After Van Gorkom*, 41 BUS. LAW. 1 (1985).

66. Compare Manning, *supra* note 65, at 1 (“atrocious”) with Krishnan Chittur, *The Corporate Director’s Standard of Care: Past, Present and Future*, 10 DEL. J. CORP. L. 505, 543 (1985) (“a long overdue judicial affirmation of the need for better informed directors”) and Barry F. Schwartz & James G. Wiles, *Trans Union: Neither “New” Law nor “Bad” Law*, 10 DEL J. CORP. L. 429, 430 (1985) (“merely represents a reiteration of existing Delaware law”). See generally BLOCK ET AL., *supra* note 19, at 71 n.86 (describing commentary from a variety of authors, including the principal defendant, Jerome Van Gorkom).

67. See, e.g., Daniel R. Fischel, *The Business Judgment Rule and the TransUnion Case*, 40 BUS. LAW. 1437, 1455 (1985) (calling the case “surely one of the worst decisions in the history of corporate law”); Manning, *supra* note 65, at 1 (“The corporate bar generally views the decision [in *Van Gorkom*] as atrocious.”).

68. Moore, *supra* note 12, at 281. Chiding the critics of the decision, Justice Moore goes on to note that *Van Gorkom* “was not the harbinger of director upheaval many predicted. Indeed, [it] provided valuable guidance to directors at a most opportune time—just before the takeover winds of the 1980s gained hurricane force.” *Id.* at 282.

69. *Smith v. Van Gorkom*, 488 A.2d 858, 865-66 (Del. 1985).

price of fifty-five dollars per share, a substantial premium over TransUnion's market price.⁷⁰ Without providing advance notice of the subject of discussion, Van Gorkom called a meeting of the board at which he gave a "twenty-minute" oral presentation of the offer, disclosing neither the basis for the fifty-five dollars per share price nor the fact that he had suggested the price to Pritzker.⁷¹ Following a two-hour meeting, the board approved the merger agreement, sight unseen.⁷²

In response to a class action suit on behalf of TransUnion's shareholders, the Delaware court held that, despite the application of the business judgment rule, the board had breached its duty of care by acting with "gross negligence."⁷³ That this test for negligence focuses almost exclusively on the board's process, rather than the substance of its decision, is now well settled.⁷⁴ The crucial question is thus not *what* the board decided but, rather, whether that decision was an informed one.⁷⁵

In focusing on "procedural due care" (rather than "substantive due care"), the Delaware courts consistently have reiterated that they will examine most intensely the information available to, and actually examined by, the directors.⁷⁶ "The need for ade-

70. *Id.* at 866-68.

71. *Id.* at 868.

72. *Id.* at 868-69. The court, in perhaps the most memorable fact in its opinion, also deemed it worth noting that Van Gorkom signed the merger agreement "at a formal social event that he hosted for the opening of the Chicago Lyric Opera." *Id.* at 869.

73. *Id.* at 893. The decision exposed the directors to personal liability to the extent that the fair price of TransUnion was found to be above \$55 per share. *Id.* The certified class of plaintiffs owned 12.7 million shares of stock. *Id.* at 864 n.3. If the fair price were as low as \$60, the directors would be liable for more than \$63 million. "Never before had such a judgment been visited upon such prominent directors of a large corporation." Moore, *supra* note 12, at 281.

74. See Veasey, *supra* note 36, at 505 (noting that courts "scrutiniz[e] the 'process' by which the board reached its decision").

75. Although the business judgment rule is said to apply only to informed decisions made in good faith, the Delaware court has indicated that this may often be a single inquiry: "the crucial element supporting a finding of good faith is knowledge." *Barkan v. Amsted Indus.*, 567 A.2d 1279, 1288 (Del. 1989); see also A. Gilchrist Sparks, III et al., *New Developments: The Business Judgment Rule in Contests for Corporate Control Under Delaware Law*, C938 ALI-ABA 329, 368 (1994) ("The Court [in *Barkan*] held that the knowledge of the market was the key to good faith.").

76. See *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 66 (Del. 1989) ("[O]ur due care examination has focused on a board's decision making pro-

quate information is central to the enlightened evaluation of a transaction that a board must make."⁷⁷ When attempting to obtain the best value for shareholders in a sale of control, "the directors must be especially diligent."⁷⁸ In particular, the Delaware Supreme Court has "stressed the importance of the board being adequately informed in negotiating a sale of control."⁷⁹ The unifying theme throughout nearly all of the court's takeover decisions is the unwavering demand that the directors possess adequate information before embarking on a course of action.⁸⁰ The court has been willing to allow boards to use a variety of techniques and, indeed, recognized that there is "no single blueprint" to follow.⁸¹

When the Business Judgment Rule Does Not Apply: The Entire Fairness Standard

The protections of the business judgment rule do not, however, attach to those transactions in which the plaintiffs allege that the directors have breached their duty of *loyalty* to the shareholders or the corporation.⁸² A breach of the duty of loyal-

cess. We look for evidence as to whether a board has acted in a deliberate and knowledgeable way in identifying and exploring alternatives."); *UIS, Inc. v. Walbro Corp.*, reprinted in 13 DEL. J. CORP. L. 806, 810 (Del. Ch. Oct. 6, 1987) ("[The] failure [by the target's board] to explore to any extent whether a [tender offeror] would make a higher offer for all shares surely is worthy of further inquiry. A board's duty is to act with due care and that duty includes the responsibility to reasonably inform oneself of alternatives.").

77. *Barkan*, 567 A.2d at 1287.

78. *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 44 (Del. 1994).

79. *Id.*; cf. *Ira N. Rosner, Paramount Lessons*, 68 FLA. B.J. 51 (1994) ("[QVC] has more to do with *Smith v. Van Gorkom* than it does with [*Revlon*] or [*Unocal*]").

80. See, e.g., *Rosner, supra* note 79, at 51 ("[T]he foundation of the law of director fiduciary duties, even in esoteric takeover situations, is the basis of the business judgment rule: good faith and *informed judgment*." (emphasis added)).

81. *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1286 (Del. 1989); see also *Barkan*, 567 A.2d at 1287 ("Nevertheless, there is no single method that a board must employ.").

82. *Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983). A full discussion of the duty of loyalty is beyond the scope of this Note. A brief background, however, is necessary in order to fully discuss the impact of the ruling in *Technicolor II* that a breach of the duty of *care* requires application of the entire fairness standard, which previously had been thought to apply only in the context of a breach of the duty of

ty most frequently occurs when directors stand on both sides of a transaction.⁸³ In such situations, once the plaintiff has shown the existence of self-interest, the directors bear the burden of proving the "entire fairness" of the transaction.⁸⁴ This burden consists of two "nonbifurcated components . . . : fair dealing and fair price."⁸⁵ Although the Delaware Supreme Court traditionally has applied this standard only in duty of loyalty cases, the court recently has imposed it on a board that had breached only its duty of care.⁸⁶

In 1982, Ron Perelman decided that Technicolor, after suffering a severe decline in earnings and drop in stock price, was "an attractive candidate for takeover."⁸⁷ Through a mutual acquaintance, he was introduced to and met several times with a member of Technicolor's board, informally discussing the possibility of an acquisition of Technicolor.⁸⁸ This board member later introduced Perelman to Morton Kamerman, Technicolor's chairman.⁸⁹ Kamerman and Perelman had a series of meetings or conversations in which they "reached substantial agreement on all matters . . . except price and financing," although they apparently had narrowed the range of possible prices to between twenty and twenty-five dollars per share.⁹⁰ Kamerman then recruited a team from Goldman Sachs to provide a fairness opinion "based on a price range of \$20-\$22" per share.⁹¹ The team, however, was allowed to talk to no one at Technicolor other than Kamerman and two senior officers.⁹² After reviewing a model

loyalty.

83. See, e.g., *id.* at 710; *Puma v. Marriott*, 283 A.2d 693 (Del. Ch. 1971).

84. *Weinberger*, 457 A.2d at 710; *Puma*, 283 A.2d 693.

85. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1172 (Del. 1995) (*Technicolor III*).

86. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345 (Del. 1993) (*Technicolor II*), modified in part, 636 A.2d 956 (Del. 1994).

87. *Id.* at 352.

88. *Id.* at 353. Recognizing an opportunity to capitalize upon Perelman's interest, the director bought an additional 1000 shares of Technicolor stock. The SEC investigated him for insider trading and eventually required him to pay approximately \$14,000 to Technicolor. *Id.* at 353 n.3.

89. *Id.* at 354.

90. *Id.*

91. *Id.* at 355.

92. *Id.*

that showed that a "\$23 LBO" was feasible, Kamerman and Perelman agreed on this price over the phone.⁹³

The Technicolor board's decisionmaking process replicated almost every one of the mistakes made by TransUnion's board in *Van Gorkom*.⁹⁴ Kamerman called a special meeting on less than two days advance notice, with *no* notice as to the purposes of the meeting.⁹⁵ Kamerman made a brief presentation regarding the proposed transaction, although, unlike Van Gorkom, he had the Goldman Sachs team present an oral opinion stating that the twenty-three dollar per share price was fair.⁹⁶ The board approved the transaction, and the tender offer was successfully completed.⁹⁷

The plaintiff-shareholders refused to tender their stock in the initial tender offer and then dissented from the second-stage merger in 1983.⁹⁸ After dissenting, the plaintiffs petitioned in the Delaware Court of Chancery in 1983 for an appraisal of their shares.⁹⁹ In January 1986, the plaintiffs filed an additional personal liability action against the Technicolor directors.¹⁰⁰ The Delaware Supreme Court explained that the shareholders based this decision upon "deposition testimony [that] caused Cinerama to believe that the directors of Technicolor had failed to comply with their fiduciary duties in connection with the sale of the company."¹⁰¹ One cannot help but notice, however, the coincidental timing of this additional suit—it was filed approximately one year after the Delaware Supreme Court's landmark *Van Gorkom* case¹⁰² (which settled for approximately

93. *Id.* at 356. "LBO" is an acronym for "leveraged buyout."

94. See, e.g., Cunningham & Yablon, *supra* note 30, at 1598 ("The facts [in *Technicolor*] were almost a replay of *Van Gorkom*.").

95. *Technicolor II*, 634 A.2d at 356; see *Smith v. Van Gorkom*, 488 A.2d 858, 867 (Del. 1985).

96. *Technicolor II*, 634 A.2d at 356-57; see *Van Gorkom*, 488 A.2d at 868. In addition, the court in *Technicolor II* noted that there was a dispute as to whether Technicolor's board actually had the "key documents" available for review. *Technicolor II*, 634 A.2d at 357 n.19; see *Van Gorkom*, 488 A.2d at 868.

97. *Technicolor II*, 634 A.2d at 357.

98. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1156 (Del. 1995) (*Technicolor III*).

99. *Id.*

100. *Id.* at 1160.

101. *Id.*

102. *Van Gorkom* was decided on January 29, 1985. *Smith v. Van Gorkom*, 488

\$23.5 million).¹⁰³

Chancellor Allen assumed that the board had breached its duty of care but, because there was no showing of injury to the plaintiffs, dismissed the suit.¹⁰⁴ Prior to *Technicolor II*, this may have been the generally accepted view on this issue of causation or injury.¹⁰⁵ The Delaware Supreme Court disagreed in *Technicolor II*, however, phrasing the issue in the case as whether the board's decision was "protected by the business judgment rule or should be subject to judicial review for its entire fairness."¹⁰⁶ Accepting the Chancellor's opinion that a breach of care existed, the court remanded the case, stating "with uncharacteristic vehemence"¹⁰⁷ that, once such a breach is established, the *board* has the burden to prove that there was *no injury* to the plaintiffs and that the transaction meets the "entire fairness" standard.¹⁰⁸

On remand to evaluate the fairness of the transaction, Chancellor Allen criticized the Delaware Supreme Court for turning the business judgment rule on its head¹⁰⁹ and using it to *increase* the burden on the board.¹¹⁰ Chancellor Allen apparently

A.2d 858 (Del. 1985).

103. Manning, *supra* note 65, at 1 (editor's note).

104. Cinerama, Inc. v. Technicolor, Inc., *reprinted in* 17 DEL. J. CORP. L. 551, 596 (Del. Ch. June 21, 1991).

105. See, e.g., Dennis J. Block, *The Auction Process: Director Duties Revisited*, N.Y. L.J., Nov. 21, 1991, at 5 ("Under the conventional (business judgment) approach to a claim that an arm's-length sale . . . was at too low a price, [the] plaintiff must show that director gross negligence is involved and must show as well that the stockholders were injured by the negligence.").

106. Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 358 (Del. 1993) (*Technicolor II*), *modified in part*, 636 A.2d 956 (Del. 1994).

107. Cunningham & Yablon, *supra* note 30, at 1599.

108. *Technicolor II*, 634 A.2d at 367.

109. Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1134, 1137 (Del. Ch. 1994), *aff'd*, 663 A.2d 1156 (Del. 1995). The chancellor argued:

[M]y [personal liability] opinion was based upon what I had understood to be a recognized principle of corporation law: that in order to recover a judgment against a corporate director for a loss caused by negligence . . . , a shareholder bears the burden to show that such negligent breach of duty by a corporate director was the proximate cause of injury suffered by the corporation or the shareholders as the case may be.

Id. at 1136.

110. *Id.* at 1137 (chiding the Delaware Supreme Court for not observing that "this Delaware version of the meaning and operation of the 'business judgment rule'

had a strong distaste for such a test, and he easily found that the board had met its newly imposed burden under both prongs of the entire fairness test: fair price and fair dealing.¹¹¹ He found that, despite the flaws in the board's process, the negotiation and approval process constituted fair dealing.¹¹² Finally, he characterized a fair price as "one that a reasonable seller, under all of the circumstances, would regard as within the range of fair value; one that such a seller could reasonably accept."¹¹³

Chancellor Allen's opinion set the stage for the final appeal to the Delaware Supreme Court. The court affirmed the Chancellor's decision, applying a relatively lenient standard of review—examining the record only to ensure that the Chancellor's findings were supported by the record and were the "product of an orderly and logical deductive process" (in other words, that they were not "clearly wrong").¹¹⁴ To ensure that this standard of review did not cloud the force of its opinion,¹¹⁵ the court noted no less than seven times that defects in a board's approval process (even though constituting a breach of its duty of care) do not create "per se" liability¹¹⁶ or present an "insurmountable obstacle for a board of directors to overcome."¹¹⁷

makes that rule a *liability enhancing* rule (i.e., it disadvantages director defendants when compared to other classes of persons charged with negligently causing injury to another)") (emphasis added).

111. *Id.* at 1139-43.

112. *Id.*

113. *Id.* at 1143. Note that this description bears a remarkable resemblance to the articulation in *QVC* that a board's decision must only be "within a range of reasonableness." *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 45 (Del. 1994).

114. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1169 (Del. 1995) (*Technicolor III*) (citing *Levitt v. Bouvier*, 287 A.2d 671, 673 (Del. 1972)).

115. The court was perhaps somewhat stung by the above criticism from commentators and the strong reaction from Chancellor Allen.

116. *Technicolor III*, 663 A.2d at 1162 ("Burden shifting does not create *per se* liability on the part of the directors."); *id.* at 1163 ("[A] given breach of a board's fiduciary duties . . . is not outcome-determinative, *per se.*"); *id.* at 1164 (reiterating that "[b]urden shifting does not create *per se* liability on the part of the directors") (quoting *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 371 (Del. 1993) (*Technicolor II*), *modified in part*, 636 A.2d 956 (Del. 1994)); *id.* at 1165 ("[T]he evidence that defeated the procedural presumption of the business judgment rule does not establish liability *per se.*").

117. *Id.* at 1163; *see also id.* at 1175 (noting that flaws in the board's process es-

The court thus strongly reaffirmed its holding in *Technicolor II*: rebuttal of the presumptions of the business judgment rule is not the end of the inquiry.¹¹⁸ The court noted that the "entire fairness standard is not even applied" unless the board has breached its fiduciary duties—that is, until the court has found that the board's process was grossly negligent or disloyal.¹¹⁹ The court in *Technicolor III* thus noted that "perfection is not possible or expected" in determining that the board's process was entirely *fair*.¹²⁰ Because perfection is not possible, the entire fairness review is necessarily conducted in something of a gray area—an area susceptible neither to "bright line precision" nor to an "unstructured or visceral process."¹²¹ As such, the proper entire fairness test must be a "disciplined balancing test," taking into account all relevant factors" on both aspects of entire fairness: fair price and fair dealing.¹²²

The similarity of the factors that the court examined in its review of the fair dealing aspect of the entire fairness test underscores the interplay between the entire fairness test and the examination of the board's duty of care. The court reviewed the negotiation¹²³ and structure¹²⁴ of the transaction and, most importantly, the board's approval process.¹²⁵ Despite the fact that the "board's now undisputed lack of care . . . was a flaw in

tablished that such process was "clearly deficient, [but] did not preclude a finding of entire fairness").

118. *Id.* at 1179.

119. *Id.*

120. *Id.* (quoting *Weinberger v. UOP, Inc.*, 457 A.2d 701, 709 n.7 (Del. 1983)).

121. *Id.* (quoting *Nixon v. Blackwell*, 626 A.2d 1366, 1378, 1381 (Del. 1993)).

122. *Id.*

123. The court noted that "arm's length negotiation provides 'strong evidence that the transaction meets the test of fairness.'" *Id.* at 1172 (citing *Weinberger*, 457 A.2d at 709-10 n.7).

124. The court disagreed with the plaintiff's argument that the structure of the transaction was unfair because it "inhibited . . . alternative bids." *Id.* at 1173 (internal quotations omitted). Although the board could not solicit bids (under a no-shop clause in the merger agreement), it was "free to furnish information and *engage in* rather than solicit discussions with another prospective purchaser." *Id.* at 1173 n.27 (emphasis added). In addition, the court noted that Delaware jurisprudence is quite familiar with situations in which hostile bidders have entered the fray despite the presence of substantial "lock-up" arrangements. *Id.* at 1173-74 (citing *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 39 (Del. 1994)).

125. *Id.* at 1173-76.

its approval process," the court affirmed the overall *fairness* of this process, based on the board's "good faith and the arm's length negotiations."¹²⁶ Each of the elements the court discussed also is inherent in any discussion of a board's breach of its duties of loyalty and care. Reiterating the major theme of its decision, the court noted that the "flaw" in the approval process "did not preclude a finding of entire fairness."¹²⁷

After *Technicolor III*, postclosing personal liability trials present directors with primary and fall-back positions for defending their approval process. First, a board will argue that any flaws that the plaintiff presents simply do not meet the high burden of rebutting the presumptions of the business judgment rule. If this argument is not successful, the board will retreat and assert that the now established flaws do not render the transaction *unfair*. This inquiry may, however, be collapsed into a single question.¹²⁸ The court distinguished *Van Gorkom* by noting that the remand in that case focused only on whether the *price* was fair because the flaws in the board's process were so severe that it "could not withstand an entire fairness analysis."¹²⁹ Under this analysis, a finding of (mere) gross negligence only begins the inquiry.¹³⁰ Such a finding still establishes a breach of the duty of care but leaves the board an opportunity to prove that the transaction was fair (despite their negligence). Only the most egregious conduct or "compound breaches" of the board's duty therefore remove the need to analyze whether the transaction was the product of fair dealing—leaving only an inquiry as to whether the price was fair.¹³¹

The court noted that all of the credible evidence also favored the conclusion that the transaction presented a fair price to the

126. *Id.* at 1175.

127. *Id.*

128. *See id.* at 1165.

129. *Id.* at 1166.

130. *Id.*

131. *Id.* Of course, the Delaware Supreme Court recognized long ago that the fair price aspect may dominate the analysis. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 703-04 (Del. 1983). To say that the final question will be, as it should, whether the shareholders received a fair price, irrespective of which fiduciary duty the directors have breached, seems fair.

shareholders.¹³² The court accepted the Chancellor's finding that the Technicolor shareholders received a premium (116% over the then current market price) that was the highest of, and was greater than four times more than the average premium (26.55%) of, sixty-one other transactions that occurred between 1981 and 1984.¹³³ Demonstrating the "non-bifurcated" approach that courts must use for both elements of the entire fairness test, the court utilized shareholder approval as evidence that both standards were met.¹³⁴ After noting that the tender by the overwhelming majority of shareholders was "substantial evidence of" fair dealing, the court also observed that the fact that "major shareholders, including [two directors] who had the greatest insight into the value of the company, sold their stock . . . at the same price paid to the remaining shareholders also powerfully implies that the price received was fair."¹³⁵ Finally, the court noted that its own recent decisions lent credence to the directors' argument that the price was fair.¹³⁶ Because no rival bidder emerged with a higher offer, the court reasoned that the price must have been fair.¹³⁷ It noted that even lock-ups or other "apparent obstacles" had not deterred rival bidders from plunging in.¹³⁸ In fact, the court's ruling in *QVC* that a board's fiduciary duty cannot be limited by the terms of a lock-up and that a board may thus have a *duty* to breach such a provision and to negotiate with a rival bidder further strengthens this rationale.¹³⁹

132. *Technicolor III*, 663 A.2d at 1176.

133. *Id.* at 1176-77.

134. *Id.* at 1176.

135. *Id.* at 1176-77.

136. *Id.* at 1177.

137. *Id.*

138. *Id.* (citing *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34 (Del. 1994)).

139. *QVC*, 637 A.2d at 51. The court held:

The No-Shop Provision could not validly define or limit the fiduciary duties of the Paramount directors. To the extent that a contract . . . purports to require a board to act or not act in such a fashion as to limit the exercise of fiduciary duties, it is invalid and unenforceable.

Id.

EXAMINATION OF DEFENSIVE MEASURES: ENHANCED SCRUTINY

Whereas the business judgment rule historically was raised in shareholder suits challenging the propriety of a completed transaction, the 1980s saw an explosion in suits seeking expedited injunctive relief either to prevent the consummation of a pending deal or to strip a target of its defensive measures, thus allowing a tender offer to commence.¹⁴⁰ In these "transactional justification"¹⁴¹ settings, the Delaware Supreme Court announced that it would not automatically apply the business judgment rule but would first apply threshold scrutiny to determine whether target board decisions deserve protection.¹⁴²

Defensive Measures: Unocal

In *Unocal Corp. v. Mesa Petroleum Co.*¹⁴³ the Delaware Supreme Court announced that, before the protections of the business judgment rule would attach to that decision, it would scrutinize the defensive measures taken by a target's directors.¹⁴⁴ In 1985, T. Boone Pickens, Jr., made an unsolicited two-tiered tender offer for Unocal stock.¹⁴⁵ The front end consisted of an offer for thirty-seven percent of the outstanding stock of Unocal at fifty-four dollars per share.¹⁴⁶ The offer disclosed that, once Pickens obtained control of Unocal,¹⁴⁷ the remaining stockholders (those who failed to tender in the initial thirty-seven percent phase) would see their shares exchanged for debt securities in the resulting company in the "back-end" phase.¹⁴⁸ Unocal's board, believing the offer to be coercive and inadequate,

140. See, e.g., *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986).

141. See *supra* note 36.

142. See, e.g., *Revlon*, 506 A.2d 173.

143. 493 A.2d 946 (Del. 1985).

144. *Id.* at 954-58.

145. *Id.* at 949.

146. *Id.*

147. Because Mesa already owned slightly more than 13% of Unocal, *id.*, successful completion of the tender offer would have given Mesa, and Pickens, control of the corporation.

148. *Id.* The court characterized these securities as "junk bonds' worth far less than \$54." *Id.* at 956.

launched a defensive "self tender offer" under which Unocal would redeem all of the outstanding shares, except those held by Mesa Petroleum, for debt securities valued at seventy-two dollars per share.¹⁴⁹

Mesa, as a Unocal stockholder, brought suit to enjoin the self-tender as a violation of the directors' fiduciary duties to Unocal.¹⁵⁰ The Chancery Court, refusing to apply the business judgment rule in that context, agreed with Mesa.¹⁵¹ The Delaware Supreme Court reversed, holding that it was wrong to declare as a matter of law that the business judgment rule did not apply to defensive measures.¹⁵² In recognition of the "omnipresent specter that a board may be acting in its own interests" by implementing defensive measures,¹⁵³ the court nevertheless announced a two-prong "threshold" test that corporate boards must satisfy before the protections and presumptions of the business judgment rule will attach to their decisions.¹⁵⁴

In order to be protected by the business judgment rule, the directors thus had the burden to prove first "that they had reasonable grounds for believing that a danger to corporate policy and effectiveness existed"¹⁵⁵ and second that the defensive action taken was "reasonable in relation to the threat posed."¹⁵⁶ The first prong of the test, requiring a board to show "good faith and reasonable investigation,"¹⁵⁷ was merely a "reformulation of what previously constituted the entire test . . . for assessing the validity of a defensive stock repurchase."¹⁵⁸ The second prong, however, seemed to be entirely new; in addition to examining the process of arriving at a decision, the courts would

149. *Id.* at 950-51.

150. *Id.* at 952-53.

151. *Id.* at 953.

152. *Id.* at 958.

153. *Id.* at 954; see also *supra* note 20 (discussing the personal risks faced by target management).

154. *Unocal*, 493 A.2d at 954.

155. *Id.* at 955 (quoting *Cheff v. Mathes*, 199 A.2d 548, 555 (Del. 1964), which previously had set the standard for examining the validity of defensive measures and defined this burden as that of "showing good faith and reasonable investigation").

156. *Id.*

157. *Id.*

158. Regan, *supra* note 33, at 150 n.112.

assess the *substance* of a board's decision.

In actuality, however, *Unocal* represented a balanced and highly significant restatement of business judgment analysis. . . .

This shift was far from semantic. While retaining basic business judgment terminology, *Unocal* adjusted the focus in a critical way— . . . empowering courts to review, objectively and *substantively*, [directors'] judgments under tests that go well beyond simple assessment of director good faith and the absence of grossly negligent conduct.¹⁵⁹

Applying the new test to the case at hand, the court found that *Unocal*'s board met both prongs of the test and that the business judgment rule would therefore apply to the board's decision.¹⁶⁰ The court did not, however, actually go through and apply the business judgment rule to the proposed transaction. The reason for this omission lies in the overwhelming impact of the "level" of judicial scrutiny to be applied. In order to obtain a preliminary injunction, the plaintiff must establish a reasonable probability of success on the merits.¹⁶¹ Because the level of scrutiny applied by a court is likely to be outcome determinative,¹⁶² that issue alone will decide the plaintiff's likelihood of success. That is, if the defendant meets the *Unocal* enhanced scrutiny burden and the business judgment rule applies, the plaintiff's likelihood of success, while not nil, is extremely low. In contrast, if the defendant fails to meet his burden, the business judgment rule will not apply, and it is then extremely likely that the plaintiff will prevail under an entire fairness review.¹⁶³ This form of analysis, however, makes the whole con-

159. Lipton & Mirvis, *supra* note 14, at 124 (emphasis added).

160. *Unocal*, 493 A.2d at 958.

161. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1279 (Del. 1989).

162. See, e.g., *id.* ("Because the effect of the proper invocation of the business judgment rule is so powerful and the standard of entire fairness so exacting, the determination of the appropriate standard of judicial review frequently is determinative of the outcome of derivative litigation.") (quoting AC Acquisitions v. Anderson Clayton & Co., 519 A.2d 103, 111 (Del. Ch. 1986)).

163. Note that it is implicit in this discussion that the Delaware courts consistently have assumed that, if the business judgment rule does not apply (without reference to whether it fails due to a breach of loyalty or of care), then the entire fairness standard would apply. See *supra* notes 82-139 and accompanying text.

cept of the plaintiffs likelihood of success dependent on the defendant's ability to meet its burden under *Unocal*.¹⁶⁴

The court expressly found a "two-tiered 'front-loaded'" offer to be a cognizable threat to the target's shareholders.¹⁶⁵ The use of front-loaded offers has waned as a direct result of the court's express authorization of defensive tactics in the face of such an offer. Ironically, however, the defensive tactic that *Unocal*'s board employed has since been barred by the "All Holders" rule under the Williams Act,¹⁶⁶ which prohibits selective tender offers by requiring that any such offer be made available to *all* holders of the class of security being purchased.¹⁶⁷

Later decisions expanded the range of threats to which a board might permissibly respond with defensive measures.¹⁶⁸ Most prominent among these threats is inadequate price. Proponents of management passivity may argue that shareholders are quite capable of discerning whether a price is too low and thus declining to tender their shares. Such reasoning however, ignores the "prisoner's dilemma" that many shareholders face.¹⁶⁹

164. See *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361, 1375 (Del. 1995) ("Thus, the plaintiffs likelihood of success . . . was initially dependent upon the inability of the [defendant] Board to discharge the burden placed upon it first by *Unocal*.").

165. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 956 (Del. 1985) ("[S]uch offers are a classic coercive measure designed to stampede shareholders into tendering at the first tier, even if the price is inadequate, out of fear of what they will receive at the back end . . ."). In addition, the court found it significant that the threat came from Pickens, "a corporate raider with a national reputation as a 'greenmailer.'" *Id.*

166. Securities and Exchange Act of 1934, ch. 404, 48 Stat. 881 (codified as amended in scattered sections of 15 U.S.C.).

167. Rule 14d-10, 17 C.F.R. § 240.14d-10 (1995).

168. Commentators have classified the following types of threats:

(i) opportunity loss, . . . [which is the risk that] a hostile offer might deprive target shareholders of the opportunity to select a superior alternative offered by target management; (ii) structural coercion, or the risk that disparate treatment of non-tendering shareholders might distort shareholders' tender decisions; and, finally, (iii) substantive coercion, or the risk that shareholders will mistakenly accept an underpriced offer.

Ronald J. Gilson & Reinier Kraakman, *Delaware's Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 BUS. LAW. 247, 267 (1989). The Delaware courts have adopted this classification scheme. See, e.g., *Unitrin*, 651 A.2d at 1384; *Paramount Communications, Inc. v. Time Inc.*, 571 A.2d 1140, 1153 n.17 (Del. 1990).

169. The "prisoner's dilemma" refers to the situation in which distrust and self-in-

That is, although each shareholder may be better off by refusing to tender, an individual shareholder may fear that a majority of other shareholders will tender.¹⁷⁰ If so, the market value of her stake in a corporation controlled by a single person (the offeror) would be greatly reduced. Although shareholders realize that, as a group, they may be best served by refusing to tender, each shareholder's self-interest will convince her to tender because of shareholders' likely inability to coordinate their activities.¹⁷¹ The onset of the "arbs" compounds this problem.¹⁷² When a tender offer is commenced,¹⁷³ a large portion of the public shares are bought up by arbitrageurs seeking only a short-term, almost immediately realizable profit; these "arbs" are likely to tender as long as the price provides some positive return.¹⁷⁴ Under this rationale, if management "reasonably perceives" that an offer price is inadequate, it should meet the first prong of *Unocal*.¹⁷⁵

terest may lead to an inefficient result. In its classic articulation, the prisoner's dilemma refers to the choice faced by prisoners X and Y, arrested together. Each is asked to inform on the other in exchange for a reduced sentence or to remain silent and face the full penalty. Although both prisoners are better off remaining silent (the problem assumes that, without testimony, neither would be convicted), each prisoner is likely to be better off, individually, if he chooses to testify. See Robert A. Prentice & John A. Langmore, *Hostile Tender Offers and the "Nancy Reagan Defense": May Target Boards "Just Say No"? Should They Be Allowed To?*, 15 DEL. J. CORP. L. 377, 435 n.289 (1990) (citing A. RAPOPORT & A. CHAMMA, PRISONER'S DILEMMA (1965)).

170. *Id.* at 435.

171. *Id.* at 446.

172. See generally EDWARD R. ARANOW & HERBERT A. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL 173-91 (1973) (discussing the role of professional arbitrageurs in tender offers).

173. See Fink, *supra* note 8, at 139 n.24 (noting that "professional traders with substantial expertise usually buy up most of the target stock before it is tendered to a bidder"). This phenomenon may even commence on the basis of rumors or other information prior to the formal announcement. Trevor S. Norwitz, "The Metaphysics of Time": A Radical Corporate Vision, 46 BUS. LAW. 377, 387 (1991) (suggesting that, "usually by the time a tender offer for a company is launched, a significant proportion of the stock has been bought up by arbitrageurs") (emphasis added).

174. See ARANOW & EINHORN, *supra* note 172, at 173-74. "[P]rofessional arbitrageurs often make substantial open-market purchases of the target's shares at prices somewhere between the market price . . . and the tender price, for the purpose of subsequently tendering such shares at a profit." *Id.* at 173. The reason that the "arbs" are able to acquire such shares below the tender price is due to the market's uncertainty as to whether the offer actually will succeed. *Id.* at 177.

175. *Paramount Communications, Inc. v. Time Inc.*, 571 A.2d 1140, 1153 (Del. 1990)

Reasonable Responses

The question of whether a target board could, in the words of Nancy Reagan, "just say no" to an inadequate offer has been the subject of much debate. The answer appears to be "yes." A board may simply decline to enter into negotiations with the bidder provided that the board has "a reasonable basis for concluding that the offer does not provide the best value reasonably available for the shareholders."¹⁷⁶ "A refusal to entertain offers may comport with a valid exercise of business judgment."¹⁷⁷ Any such refusal, however, must be based on adequate information regarding both the offer and the value of the corporation. Indeed, the necessity of becoming informed about the offer may require entering into preliminary negotiations or discussions with the bidder.¹⁷⁸ In any event, a hostile tender offeror does not need the board's approval, or even acquiescence, to complete its offer—it simply buys the shares from all shareholders willing to sell. Because a large portion of stock is likely to find its way into the hands of the arbitrage professionals, the offeror likely will acquire control.¹⁷⁹

Until the mid-1980s, boards had little success at preventing the completion of tender offers, perhaps because such offers were rare, and nobody really worried too much about them.¹⁸⁰ As

(recognizing that "inadequate value," even in the context of an all-cash offer for all shares, is a "legally cognizable threat").

176. Cunningham & Yablon, *supra* note 30, at 1622 (noting, however, that a decision to "just say no" is not favored by Delaware doctrine).

177. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1285 n.35 (Del. 1989).

178. See Robert A. Ragazzo, *Unifying the Law of Hostile Takeovers: Bridging the Unocal/Revlon Gap*, 35 ARIZ. L. REV. 989, 993 n.21 (1993) ("Although there is no duty to negotiate with a bidder, some courts have required the equivalent on the theory that the target company's board is required to investigate the bidder's offer in fulfillment of its duty of care.") (citation omitted).

179. See Thomas O'Boyle, *Changing Tactics in Tender Offers*, 25 BUS. LAW. 863, 866 (1970) (estimating that at least 50% of all shares actually received in a tender offer are tendered by arbitrageurs).

180. See, e.g., Fink, *supra* note 8, at 134 n.7 (noting that tender offers were "[a] relatively new phenomenon in the 1960's"). In fact, "[t]he first hostile tender offer by one New York Stock Exchange listed corporation for another . . . generally date[s] back to only" the mid-1970s. John C. Coffee, Jr., *Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer's Role in Corporate Governance*, 84 COLUM. L. REV. 1145, 1205 (1984).

they became more common, however, astute practitioners in New York and elsewhere, most notably Martin Lipton,¹⁸¹ began devising ever more devious means of repelling hostile tender offers.¹⁸² Despite (or perhaps because of) the ever expanding arsenal of defensive tactics, *Unocal* held that the board "does not have unbridled discretion to defeat any perceived threat by any Draconian means available."¹⁸³ That is, under the second prong of the *Unocal* enhanced scrutiny test, a court must determine whether the board's chosen defensive measures are "reasonable in relation to the threat posed."¹⁸⁴ The Delaware Supreme Court's most recent takeover case, *Unitrin, Inc. v. American General Corp.*,¹⁸⁵ clarifies the nature of this examination. Seizing on the above language from *Unocal*, the court declared that the first inquiry is whether the defensive measure is "Draconian."¹⁸⁶ After citing Webster's definition,¹⁸⁷ the court identified as Draconian those defensive measures that are "coercive"¹⁸⁸ or "preclusive."¹⁸⁹ The court then went on to incorpo-

181. Lipton is "generally acknowledged as the inventor of the poison pill," perhaps the most potent defensive weapon in a target board's arsenal. Martin M. Cohen, "Poison Pills" As a Negotiating Tool: *Seeking a Cease-Fire in the Corporate Takeover Wars*, 1987 COLUM. BUS. L. REV. 459, 460 n.3; see also Robert M. Daines & Jon D. Hanson, *The Corporate Law Paradox: The Case for Restructuring Corporate Law*, 102 YALE L.J. 577, 592 n.77 (1992) (reviewing FRANK H. EASTERBROOK & DANIEL R. FISCHER, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* (1991)) (commenting on the amount of money Lipton has made since inventing the poison pill).

182. See generally Lederman, *supra* note 9 (defining and discussing many common defensive tactics).

183. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985).

184. *Id.*

185. *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361 (Del. 1995).

186. *Id.* at 1386-88.

187. "DRACONIAN, adj. . . . barbarously severe; harsh; cruel." *Id.* at 1383-84 n.34 (citing WEBSTER'S NEW INTERNATIONAL DICTIONARY 780 (2d ed. 1951)).

188. *Id.* at 1387. Coercive defenses are those that are "aimed at 'cramming down' on its shareholders a management-sponsored alternative." *Id.*

189. *Id.* Preclusive measures are those that prevent a third party from making an offer for the corporation. See *id.* Here, the court apparently meant "legal" rather than "practical" preclusion because it cited Paramount Communications, Inc. v. Time Inc., 571 A.2d 1140 (Del. 1990). In *Time-Warner*, see *infra* note 214, Paramount had argued that the sheer size of the combined entities (Time and Warner) would financially preclude a tender offer; however, the court refused to accept such an argument, noting instead that such an offer was still feasible. *Time-Warner*, 571 A.2d at 1154-55.

rate the new QVC "range of reasonableness" standard.¹⁹⁰ The court set forth three criteria to evaluate whether such measures are in this range. Specifically, a court must look at whether:

(1) [i]t is a statutorily authorized form of business decision which a board of directors may routinely make in a non-take-over context; (2) as a defensive response to [the tender] Offer it was limited and corresponded in degree or magnitude to the degree or magnitude of the threat (*i.e.*, assuming the threat was relatively "mild," was the response relatively "mild?"); (3) with [a] Repurchase Program, the [defendant] Board properly recognized that all shareholders are not alike, and provided immediate liquidity to those shareholders who wanted it.¹⁹¹

Although the method of analysis is new, it appears merely to formulate expressly the analysis that courts previously have undertaken. The first section seems to authorize adoption, in the hostile context, of those measures that the Delaware General Corporation Code expressly authorizes.¹⁹² The second prong is merely a restatement of the traditional proportionality test.¹⁹³ Finally, the third prong appears to articulate more clearly the court's notion of what is *not* a coercive program under its "Draconian" standard.¹⁹⁴

Ultimately upholding Unitrin's combination of defensive measures, the court noted that a court should not inquire as to whether a defensive measure was, in its judgment, "unnecessary" to rebuff the threat.¹⁹⁵ This statement of judicial re-

190. *Unitrin*, 651 A.2d at 1387-88 ("If a defensive measure is not draconian, however, because it is not either coercive or preclusive, the *Unocal* proportionality test requires the focus of enhanced judicial scrutiny to shift to the 'range of reasonableness.'"); see *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 45-46 (Del. 1994). Perhaps a more logical progression of analysis would first examine the measures by the "range of reasonableness" standard. As "draconian" measures (*i.e.*, those that are coercive or preclusive) are not within the range of reasonableness standard by definition, see *supra* note 183, an initial finding of reasonableness would eliminate the need for a second-stage analysis.

191. *Unitrin*, 651 A.2d at 1389.

192. See DEL. CODE ANN. tit. 8, § 141 (1991).

193. See *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985).

194. See *id.*

195. *Unitrin*, 651 A.2d at 1367.

straint is remarkably similar to the court's cautionary statements in *Technicolor III* and *QVC*. In those cases, the court noted that the proper test is one of reasonableness, not of *perfection*. In *Technicolor III*, the court noted that, although the board's process was flawed, those flaws did not preclude a finding of entire fairness: "A finding of perfection is not a sine qua non in an entire fairness analysis."¹⁹⁶ In *QVC*, the court stated that the proper inquiry was whether the "directors made a *reasonable* decision, not a *perfect* decision."¹⁹⁷ The court thus has seemed to indicate consistently that, although heightened or enhanced scrutiny will apply in change-of-control situations, this scrutiny must allow directors some leeway in their decisions.

THE DUTY TO AUCTION: THE "REVLON ZONE"

Less than a year after handing down its *Unocal* decision, the Delaware Supreme Court in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*¹⁹⁸ confronted the issue not of defensive measures designed to keep a target independent but rather actions taken to ensure that control passes to a management-chosen, friendly acquiror instead of to a hostile raider.¹⁹⁹ *Revlon* addressed the "battle for corporate control of Revlon" between Forstmann Little & Co. and Ron Perelman's Pantry Pride.²⁰⁰ In lieu of consenting to a hostile tender offer by Pantry Pride, Revlon's management attempted to negotiate a sale of control to Forstmann, thus precipitating an auction of the company.²⁰¹ Even though Pantry Pride had announced that it would engage in "fractional bidding" and would (slightly) top any bid by Forstmann,²⁰² Revlon's board entered into a merger agreement with Forstmann that included (1) a lock-up on two key divisions of Revlon,²⁰³ (2) a no-shop provision,²⁰⁴ and (3) a

196. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1179 (Del. 1995) (*Technicolor III*).

197. *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 45 (Del. 1994).

198. 506 A.2d 173 (Del. 1986).

199. *Id.* at 176-79.

200. *Id.* at 175.

201. *Id.* at 178-79.

202. *Id.* at 178.

203. The lock-up essentially gave Forstmann an option to acquire Revlon's Vision

termination fee of twenty-five million dollars.²⁰⁵ Pantry Pride filed suit²⁰⁶ and obtained an injunction invalidating Revlon's agreement with Forstmann.²⁰⁷

The Delaware Supreme Court affirmed this decision not because the agreement resulted in improper defensive measures under *Unocal* but because the agreement prevented the board from maximizing shareholder wealth.²⁰⁸ After it became apparent that the sale or break-up of the company was inevitable,

[t]he duty of the board had thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholder's benefit. This significantly altered the board's responsibilities under the *Unocal* standards. . . . The whole question of defensive measures became moot. The directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.²⁰⁹

Many commentators have written about the various circumstances that will trigger the *Revlon* duties²¹⁰ or that cause a

Care and National Health Laboratories divisions in the event that another party acquired 40% of Revlon's stock. *Id.* at 178. Such a provision, often called a "crown jewel," is designed to make the target, if not worthless to the rival bidder, then certainly worth far less than the bid on the table. See generally BLOCK ET AL., *supra* note 19, at 156-71 (discussing asset lock-up options).

204. A "no-shop" provision requires the target to negotiate exclusively with one bidder, in this case, Forstmann. *Revlon*, 506 A.2d at 178. Currently, it appears that a no-shop provision may be invalid in the face of the target board's fiduciary duties. *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 51 (Del. 1994). The best description, therefore, may be that a no-shop provision may do *only* what the name implies—prevent the directors from "shopping" the corporation (i.e., soliciting other bids). Such a provision probably would not prevent the target directors from responding to, providing information to, or even negotiating with other bidders.

205. This required Revlon to place \$25 million in escrow to be paid to Forstmann if another party acquired more than 19.9% of Revlon's stock. *Revlon*, 506 A.2d at 178. Such a fee may be viewed as the cost of bringing a "white knight" to the table. See generally BLOCK ET AL., *supra* note 19, at 140-88 (discussing the sale of corporate assets to a "white knight").

206. MacAndrews & Forbes Holdings, Inc., the named plaintiff in *Revlon*, was the controlling stockholder in Pantry Pride. *Id.* at 175 n.1.

207. *MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc.*, 501 A.2d 1239 (Del. Ch. 1985), *aff'd*, 506 A.2d 173 (Del. 1986).

208. *Revlon*, 506 A.2d at 185.

209. *Id.* at 182.

210. See, e.g., Ronald J. Gilson & Reinier Kraakman, *What Triggers Revlon?*, 25

board of directors to enter the "Revlon zone"²¹¹ or "Revlon land."²¹² The *Revlon* trigger is the subject of such intense debate because a decision to apply the *Revlon* standard often is outcome determinative, and defendant directors thus will struggle mightily to avoid application of this duty. Both the "Revlon trigger" and the "Revlon zone" itself were greatly refined in subsequent years.²¹³

Development Prior to QVC

What Triggers Revlon

The most significant of the "triggering" cases is *Paramount Communications, Inc. v. Time Inc.*²¹⁴ As a result of a long-standing strategic plan, Time's board announced its intention to enter into a merger with Warner Brothers.²¹⁵ Shortly thereafter, Paramount announced a "fully negotiable" all-cash, all-shares bid for Time at \$175 per share, conditioned, however, on

WAKE FOREST L. REV. 37 (1990); Portia Policastro, Note, *When Delaware Corporate Managers Turn Auctioneers: Triggering the Revlon Duty After the Paramount Decision*, 16 DEL. J. CORP. L. 187 (1991); Theodore N. Mirvis, *What Triggers 'Revlon'?* *Some New Answers*, N.Y. L.J., Dec. 3, 1990, at 5.

211. See, e.g., Rinaldi, *supra* note 42.

212. See, e.g., Cunningham & Yablon, *supra* note 30, at 1593 (referring to "Revlon land" as a "common phrase of the mergers and acquisitions bar"). The Delaware Supreme Court, however, is apparently less than enchanted with such terminology. The court recently chastised a plaintiff's use of the phrase "Revlon duties" in his brief: "Presumably, plaintiff is referring colloquially but inappropriately to the enhanced scrutiny courts apply to certain types of transactions . . ." *Arnold v. Society for Sav. Bancorp., Inc.*, 650 A.2d 1270, 1289 n.40 (Del. 1994). During oral argument in *QVC*, Viacom's attorney's use of the phrase "Revlon land" drew a "perceptible grimace from Justice Andrew Moore, author of the *Revlon* decisions, who admonished counsel by stating 'the Court doesn't use those kinds of terms.'" Cunningham & Yablon, *supra* note 30, at 1593 (quoting from a videotape of oral argument, Dec. 9, 1993).

213. See generally Cunningham & Yablon, *supra* note 30, at 1593 (discussing the "end of Revlon duties").

214. 571 A.2d 1140 (Del. 1989). Because the strategic combination between Time and Warner was at issue and out of a desire to avoid confusion with *QVC*, this case has come to be known as "*Time-Warner*." See, e.g., Cunningham & Yablon, *supra* note 30, at 1595 n.14. Because this is the nomenclature used by the Delaware court, see, e.g., *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 38 (Del. 1994), this Note will adopt it as well.

215. *Time-Warner*, 571 A.2d at 1143-44.

termination of the merger agreement with Warner.²¹⁶ Finding this offer inadequate, Time's board decided to "recast" its merger with Warner into an outright acquisition by Time of Warner via a two-tiered tender offer, thus avoiding the delays associated with obtaining shareholder approval of a merger.²¹⁷ Although Paramount raised its offer to \$200 per share, Time's board refused to break off the deal with Warner, citing the long-term benefits of the Time-Warner combination and the preservation of the Time "culture."²¹⁸

Paramount and several Time shareholders sued on the basis of both *Revlon* and *Unocal* claims.²¹⁹ The Delaware Supreme Court held that Time's board did not trigger *Revlon* by its announcement of Time's intention to purchase and merge with Warner.²²⁰ The board therefore had no duty to maximize immediate (short-term) shareholder revenue, at the expense of abandoning its long-term strategy.²²¹ The court specifically noted that *Revlon* is not triggered "simply because they might be construed as putting a corporation either 'in play' or 'up for sale.'"²²² Legal commentators have interpreted this decision as implying that a target board cannot "inadvertently" put itself in play.²²³ Furthermore, the threat that shareholders would undervalue the long-term value of the combination, as well as the preservation of the Time "culture," were sufficient justifications for the board's move to commence a defensive tender offer for Warner.²²⁴

216. *Id.* at 1147.

217. *Id.* at 1148.

218. *Id.* at 1149.

219. *Id.*

220. *Id.* at 1151.

221. *Id.* at 1150-51.

222. *Id.* at 1151.

223. See, e.g., E. Ashton Johnston, Note, *Defenders of the Corporate Bastion in the Revlon Zone: Paramount Communications, Inc. v. Time Inc.*, 40 CATH. U. L. REV. 155, 180-81 (1990).

224. *Time-Warner*, 571 A.2d at 1153.

What Are the Revlon Duties? Importation of the Proportionality Standard

"Despite the 'auction' language from the *Revlon* opinion, the board is not required to commence an auction."²²⁵ Nevertheless, *Revlon* does require that, in the event of an auction, a target board treat all bidders equally.²²⁶ To obtain a maximum price, a board ideally would allow round after round of bidding until one bidder remains standing. Such a prolonged auction, however, is itself a significant threat to the corporation because of the uncertainties that it creates regarding ongoing ownership. As a result, the board must, at some point, declare an end to the auction. At that point, the bidders obviously cannot truly be treated equally; in order to end an auction, one bidder (the winner) must be treated preferentially (being allowed to buy the company) to the detriment of all others.²²⁷ *Revlon's* greatest lasting impact, therefore, is in governing the conditions under which a target may permissibly move to declare an end to the auction and close a sale of the company to one of the bidders.

"In the face of disparate treatment [of bidders], the trial court must first examine whether the directors properly perceived that shareholder interests were enhanced. In any event the board's action must be reasonable in relation to the advantage sought to be achieved"²²⁸ When examining such disparate treatment, the court must inquire "whether the board properly perceived that shareholder interests were enhanced by such treatment."²²⁹ Further, auction-ending steps must be designed to result in a "substantial benefit" to the shareholders to meet the enhanced *Revlon* scrutiny.²³⁰

225. Ragazzo, *supra* note 178, at 1000 (citing *Barkan v. Amsted Indus.*, 567 A.2d 1279, 1286 (Del. 1989)) (footnote omitted).

226. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 184 (Del. 1986) (holding that "directors cannot fulfill their enhanced *Unocal* duties by playing favorites with the contending factions").

227. This assumes a situation in which two or more competing bidders have not yet reached their maximum bids.

228. *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1288 (Del. 1989).

229. *Yanow v. Scientific Leasing, Inc.*, reprinted in 17 DEL. J. CORP. L. 659, 676 (Del. Ch. July 31, 1991).

230. *Macmillan*, 559 A.2d at 1284 (emphasis added); see also Ragazzo, *supra* note 178, at 1000 n.60 ("*Revlon* and *Macmillan* taken together stand for the proposition

The Revlon Duties After QVC: Alive and Well

In *Paramount Communications Inc. v. QVC Network Inc.*,²³¹ the Delaware Supreme Court revisited and refined the *Revlon* duties when analyzing the contest for control of Paramount.²³² Paramount and Viacom entered into a merger agreement pursuant to which Viacom would acquire all of Paramount's stock.²³³ The Paramount shareholders would receive a combination of Viacom stock and cash,²³⁴ valued at \$69.14 per Paramount share.²³⁵ The merger agreement contained a "no-shop" provision,²³⁶ a termination fee of \$100 million (payable if Paramount accepted or recommended a competing transaction or if the Paramount shareholders rejected the merger), and a stock option giving Viacom the right to acquire 19.9% of Paramount's outstanding stock if "any of the triggering events for the Termination Fee occurred."²³⁷ Despite these provisions, QVC proposed an alternative transaction to Paramount, offering to acquire Paramount's stock for a combination of QVC stock and cash, valued at eighty dollars per Paramount share.²³⁸ Frustrated by what it believed to be a slow response from Paramount, QVC launched a tender offer for fifty-one percent of the Paramount stock at eighty dollars (cash) per share.²³⁹

The bidding war was on, and America watched eagerly from the sidelines. Viacom and Paramount amended their merger agreement to match QVC's price of eighty dollars cash for fifty-one percent of Paramount's stock.²⁴⁰ In a meeting with QVC,

that bidder favoritism that results [merely] in a marginal increase in the bidding price is unlawful.").

231. 637 A.2d 34 (Del. 1994).

232. *Id.*

233. *Id.* at 39.

234. *Id.*

235. Randall Smith, *The Paramount Takeover: Wall Street's Final Analysis: Might Made Right*, WALL ST. J., Feb. 16, 1994, at B1.

236. See *supra* note 204 (describing the effect of a no-shop provision).

237. QVC, 637 A.2d at 39. These provisions were intended to "discourage a competing bid" and Viacom's chairman, Sumner Redstone, publicly announced that "only a 'nuclear attack' could break the deal." *Id.*

238. *Id.*

239. *Id.* at 40.

240. *Id.* The "back-end" price was to be a combination of Viacom stock, purportedly valued at \$80 per Paramount share. *Id.* The "defensive" measures (i.e., the no-shop

Paramount rejected a proposed auction process, citing its agreement with Viacom.²⁴¹ Nonetheless, Viacom unilaterally raised its tender offer price to eighty-five dollars per share.²⁴² In response, QVC raised its offer to ninety dollars per share, with a corresponding back-end increase.²⁴³ Despite QVC's higher bid, the Paramount board voted to accept the Viacom proposal, citing uncertainties in the QVC offer.²⁴⁴ QVC sought and obtained a preliminary injunction barring consummation of the Viacom offer.²⁴⁵ In a ruling carried live on CNN,²⁴⁶ the Delaware Supreme Court upheld this injunction,²⁴⁷ setting the stage for yet more bidding. When the dust finally settled, Viacom won control of Paramount with a bid of \$107 per share for 50.1% of the Paramount stock.²⁴⁸

In upholding the injunction, the court found that it should apply "enhanced scrutiny."²⁴⁹ In doing so, however, the court chose not to rely on the traditional *Unocal* rationale of the "omnipresent specter" of director self-interest articulated in most of its previous transactional justification decisions.²⁵⁰ Instead, the court noted that every "approval of a transaction resulting in a sale of control" calls for enhanced scrutiny.²⁵¹ The court then stated that the directors have a duty in *every* change-of-control transaction "to secure the transaction offering the best value

provision, termination fee, and stock option), however, were left unchanged. *Id.*

241. *Id.* at 41.

242. *Id.* Again, the back-end securities were increased as well. *Id.*

243. *Id.*

244. *Id.*

245. *QVC Network, Inc. v. Paramount Communications Inc.*, 635 A.2d 1245 (Del. Ch. 1993), *aff'd*, 637 A.2d 34 (Del. 1994).

246. See *CNN Live Report*, *supra* note 30.

247. *QVC*, 637 A.2d at 51.

248. *Smith*, *supra* note 235, at B1. In addition, the Viacom bid added stability to the back-end price, containing a "contingent value right" security that would rise if the Viacom stock fell in value. *Id.*

249. *QVC*, 637 A.2d at 45.

250. See, e.g., *Stroud v. Grace*, 606 A.2d 75, 82 (Del. 1992); *Barkan v. Amsted Indus.*, 567 A.2d 1279, 1286 (Del. 1989); *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1287 (Del. 1989); *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334, 1341 (Del. 1987); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 180 (Del. 1986); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985).

251. *QVC*, 637 A.2d at 42.

reasonably available for the stockholders—and they must exercise their fiduciary duties to further that end.”²⁵² Despite the enhanced level of scrutiny, the court reiterated that “courts will not substitute their business judgment for that of the directors.”²⁵³ Instead, a court will only “determine if the directors’ decision was, on balance, within a range of reasonableness.”²⁵⁴

QVC appears to have resolved the question of whether a board may inadvertently subject itself to the *Revlon* duties.²⁵⁵ “Since the Paramount directors had already decided to sell control, they had an obligation to continue their search for the best value reasonably available to the stockholders.”²⁵⁶ Because the board has a duty in all sales of control to obtain the best price and because the best price often can be obtained only by an auction, any friendly sale of control may now implicate the *Revlon* duties when a hostile bidder lurks in the background.

QVC also shed further light on *Time-Warner’s* discussion of what constitutes a sale of control. Sale of a majority of the stock of the target corporation is not a transfer of control if the buyer is, in turn, owned by a fluid aggregation of public shareholders.²⁵⁷ That is, if the buyer is publicly owned without a controlling individual or group of shareholders, the sale does not constitute a transfer of control. The court’s concern was the protection of minority shareholders’ interests and the minority shareholders’ ability to exert their will.²⁵⁸ This ability is sub-

252. *Id.* at 44.

253. *Id.* at 45.

254. *Id.* This standard already has been incorporated into the review of defensive tactics. See *supra* note 190 and accompanying text (discussing *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 361 (Del. 1995)).

255. *QVC*, 637 A.2d at 47 (“The Paramount Board, albeit *unintentionally*, had ‘initiate[d] an active bidding process seeking to sell itself’ by agreeing to sell control of the corporation to Viacom in circumstances where another potential acquiror (*QVC*) was equally interested in being a bidder.”) (alteration in original) (emphasis added). Note the court’s use of the word “bidder” even though it did not contemplate an auction.

256. *Id.* at 48-49.

257. See, e.g., *Arnold v. Society for Sav. Bancorp, Inc.*, 650 A.2d 1270, 1290 (Del. 1994) (“[T]here is no ‘sale or change in control’ when “[c]ontrol of both [companies] remain[s] in a large, fluid, changeable and changing market.””) (quoting *QVC*, 637 A.2d at 47) (first alteration added).

258. See *QVC*, 637 A.2d at 47.

stantially diminished or eliminated when an individual or cohesive group acquires a controlling interest.²⁵⁹ The court apparently believed that no real difference distinguishes minority shareholders in any two public corporations because of the general inability to affect substantially the corporate decisionmaking process.²⁶⁰ The sale of Paramount to Viacom implicated the *Revlon* duties because Sumner Redstone's controlling interest in Viacom would result in his controlling Paramount.²⁶¹ "[T]he proposed transaction would have denied the stockholders the power to effectuate policies that they believe to be in their best interests."²⁶²

Commentators frequently have argued that the *Revlon* duties either already are or are about to become nonexistent.²⁶³ This view, however, simply does not match reality, as the Delaware judiciary consistently has viewed *Revlon* as an integral (and consistent) part of Delaware law. As early as 1989, the Delaware courts noted that *Revlon* did not represent a significant departure from their traditional principles.²⁶⁴ The requirement that a board of directors deal fairly with a competing bidder was neither revolutionary nor novel and does not seem likely to disappear from the map.²⁶⁵ "Even where there is no specific

259. See *id.*

260. See *Arnold*, 650 A.2d at 1290.

261. See *QVC*, 637 A.2d at 48. For an interesting depiction of Sumner Redstone and the domination that he asserts over Viacom (and now its subsidiary Paramount), see Robert Lenzner & Marla Matzer, *Late Bloomer*, *FORBES*, Oct. 17, 1994, at 40, 40-45 (noting that the "Forbes Four Hundred" ranks Redstone the 16th wealthiest person in America and describing his ownership of Viacom as follows: "[T]here is only one boss."); Marla Matzer & Robert Lenzner, *Winning Is the Only Thing*, *FORBES*, Oct. 17, 1994, at 46, 46-48.

262. Thomas A. Gentile, *Recent Developments, Refining the Revlon Doctrine's Applicability to Changes of Control*, 17 *HARV. J.L. & PUB. POL'Y* 895, 905 (1994).

263. See, e.g., Cunningham & Yablon, *supra* note 30, at 1595 ("[T]he so-called 'Revlon duty' . . . no longer exists . . ."); Ragazzo, *supra* note 178, at 1035 ("Subsequent to *Revlon*, the Delaware Supreme Court has narrowed that case to the greatest possible extent. . . . The ever-decreasing scope of *Revlon* may be some indication that the Delaware Supreme Court is less than comfortable with . . . the enhanced *Revlon* duties.").

264. See, e.g., *Barkan v. Amsted Indus.*, 567 A.2d 1279, 1286 n.2 (Del. 1989) ("Because the rule in *Revlon* is derived from fundamental principles of corporate law and flows directly from precedents such as *Unocal*, its announcement did not produce a seismic shift in the law governing changes of corporate control.").

265. See *Thomas v. Kempner*, No. Civ.A. 4138, 1973 WL 460, at *6 (Del. Ch. Mar.

Revlon duty to conduct an auction, however, a board must ensure that it is informed regarding alternatives such as an auction."²⁶⁶ The court has expressly recognized that an auction is simply one example of an important information-gathering technique.²⁶⁷

Unless a second bidder is present, the Delaware courts seem quite willing to defer to a board's knowledge and reasonable investigation. "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 shareholders."²⁶⁸ As soon as more than one suitor becomes interested in the target, however, the court consistently has applied the *Revlon* standard and required the board to conduct an auction.²⁶⁹ Although this may seem to be a different duty, it is merely a specialized application of the general duty to be informed.²⁷⁰

22, 1973) (finding that the "fundamental error of business judgment . . . [was the directors'] insistence in continuing to deal solely with [the friendly offeror] after it was readily apparent that at least one other group was not only interested in acquiring the [assets] but was willing to top [the friendly offeror's] offer as to cash").

266. BLOCK ET AL., *supra* note 19, at 266.

267. *Barkan*, 567 A.2d at 1286-87.

Revlon does not demand that every change in . . . control . . . be preceded by a heated bidding contest. *Revlon* is merely one of an unbroken line of cases that seek to prevent the conflicts of interest that arise . . . by demanding that directors act with scrupulous concern for the fairness to shareholders. . . . When the board is considering a single offer and has no reliable grounds upon which to judge its adequacy, th[e] concern for fairness demands a canvass of the market to determine if higher bids may be elicited. When, however, the directors possess a body of reliable evidence with which to evaluate the fairness of a transaction, they may approve that transaction without conducting an active survey of the market.

Id. (citations omitted) (emphasis added).

268. *Id.* at 1288.

269. *See id.* at 1286.

270. The court has cited with approval Chancellor Allen's observation that "the due care theory and the *Revlon* theory do not present two separate theories justifying shareholder recovery. . . . [B]oth theories reduce to a claim that directors were inadequately informed An auction is a way to get information." *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 369 n.37 (Del. 1993) (*Technicolor II*) (quoting *Cinerna, Inc. v. Technicolor, Inc.*, reprinted in 17 DEL. J. CORP. L. 551, 581 (Del. Ch. June 21, 1991), *aff'd in part and rev'd sub nom.* *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345 (Del. 1993), *modified in part*, 616 A.2d 956 (Del.)) (alteration in original) (emphasis added), *modified in part*, 636 A.2d 956 (Del. 1994).

To speak of an end to the duty to conduct a fair auction is to ignore the reality of the duty to be informed.²⁷¹ Whenever more than one bidder is interested in the company, the practical effect will continue to be that a board will feel compelled to conduct an auction so as to obtain the "best value reasonably available" for the shareholders.²⁷² Even Professors Cunningham and Yablon (the commentators leading the charge to pronounce *Revlon* dead) acknowledge that the directors' fiduciary duties articulated under any standard "may still lead management to conduct an auction in many cases."²⁷³ This result remains true simply because the board's duty is to be informed as to the best value available and "[a]n auction is a way to get information."²⁷⁴ Accordingly, any variation between a standard that explicitly requires an auction and one that requires a board to be fully informed is merely a distinction without a difference.²⁷⁵ A duty to auction is simply a specific application of the duty to be informed.²⁷⁶ Stated differently, the duty to be informed requires that a board conduct an auction between competing bidders. Although valuation studies or fairness opinions may be important in many situations, a hotly contested auction often leads to a price wildly beyond expectations—a price that a board cannot know, absent an auction.²⁷⁷ *Technicolor III* also represents the

271. See Alexander B. Johnson, Note, *Is Revlon Only Cosmetic?: Structuring a Merger in the Mid-1990s*, 63 FORDHAM L. REV. 2271, 2273 n.21 (1995) (arguing that the statement of Professors Cunningham and Yablon "may be only . . . semantics . . . [because] the fiduciary duties enunciated in *Revlon* still exist under Delaware law").

272. *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 43 (Del. 1993). For a statistical analysis of the benefits (at least to targets) of an auction, see Michael Bradley et al., *Synergistic Gains from Corporate Acquisitions and Their Division Between the Stockholders of Target and Acquiring Firms*, 21 J. FIN. ECON. 3, 22 (1988) ("Clearly, target shareholders earn greater returns from multiple-bidder contests than from single-bidder offers.").

273. Cunningham & Yablon, *supra* note 30, at 1617.

274. *Technicolor II*, 634 A.2d at 369 n.37 (quoting *Technicolor*, reprinted in 17 DEL. J. CORP. L. at 581).

275. Cf. Johnson, *supra* note 271, at 2273 n.21 ("Rather than argue that *Revlon* duties are extinct, it is [sic] seems better to understand *Revlon* duties as requiring a board to obtain the best value reasonably available for shareholders.").

276. Cunningham & Yablon, *supra* note 30, at 1604 ("*Revlon* is simply a particularized application of the duty of care . . .").

277. The battles for RJR and Paramount are prime examples of auctions leading to

Delaware Supreme Court's encouragement to directors to negotiate fully and fairly with rival bidders. In its decision, the court noted that the absence of a rival bid is evidence that the price obtained was fair and is thus "supportive of the board's decision to proceed" with the transaction.²⁷⁸ If the absence of a competing bid is evidence that the proposed price is fair, the *presence* of a rival party ready to bid must at least be some evidence that a higher price might be obtained. A theoretical elimination of the *Revlon* duty to auction thus simply does not exist in the reality of the boardroom. Experienced counsel must now advise directors that the failure to deal fairly with all bidders will (1) result in an injunction if the bidder challenges the board action prior to closing or (2) be considered strong evidence that a higher price may have been available (and that the transaction just might not have been entirely fair to the shareholders) if it is challenged in a personal liability suit brought after closing. Under this analysis, target directors bear dual pressures from the Delaware courts to explore fully *all* bids for their corporations. These pressures demonstrate that, in the boardroom (if not necessarily in analytical theory), the rumors of *Revlon's* demise seem to

prices wildly beyond the "fair" price at which the directors were prepared to sell the company. See *supra* notes 17, 214-24 and accompanying text. The reason for this may not be so much economic as emotional. At some point in the auction process, pride and arrogance are likely to affect the bids and produce a price based as much on a desire to win as on the actual value of the company. See, e.g., Paul Noglows, *Act Two in Par Spar*, VARIETY, Dec. 20, 1993, at 1, 63 (statement of Mario Gabelli) ("With the egos involved [in the Paramount battle], who knows how high [prices] will go?"); Randall Smith, *Biggest Buyout Ever Finishes As Flop for KKR and Dozens of Large Investors*, WALL ST. J., Mar. 16, 1995, at A5 (statement of John Coffee) ("Once you get into auctions, hubris takes over, and parties pay extraordinary amounts' for acquisitions."). As a result, auctions are still likely to produce prices well beyond what may be "fair." Consider, for example, the sale of Stokely-Van Camp, the maker of frozen and canned foods and what came to be the crown jewel—Gatorade. A group led by the inside management persuaded the board that a price of \$55 per share was fair. LEDERMAN, *supra* note 8, at 195. While this group was finalizing its financing, Pillsbury unexpectedly announced that it would pay \$62 per share: *Id.* at 199. Now that the company was fully "in play," the board had to conduct an auction. In the end, Quaker Oats won the bidding at \$77 per share. *Id.* at 201. With 2.7 million shares outstanding, *id.* at 191, the unanticipated auction resulted in an additional \$60 million payout to the shareholders.

278. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1177 (Del. 1995) (*Technicolor III*) (quoting *Barkan v. Amsted Indus.*, 567 A.2d 1279, 1287 (1989)).

have been greatly exaggerated.²⁷⁹

ANALYSIS AND COMPARISON: ARE THESE POSTURES INTERNALLY CONSISTENT? DO THEY NEED TO BE?

The Burden Shift Under Technicolor II Is Consistent with Prior Cases

The *Technicolor II* decision, applying the entire fairness standard to the breach of a board's duty of *care*, already has provoked significant commentary suggesting that entire fairness review is a radical development in Delaware law.²⁸⁰ A closer reading, however, suggests that this holding is merely a clarifying reiteration of existing, well-established precedent.²⁸¹ The court in *Van Gorkom* found the defendants liable based solely on a showing that they had breached their duty of care; the plaintiff did not prove causation or harm.²⁸² In *Technicolor III*, the Delaware Supreme Court distinguished *Van Gorkom* on the basis that the "compound breaches of the duties of care . . . could not withstand an entire fairness analysis."²⁸³ The plaintiffs had established the directors' liability, and the only issue left to be

279. This phrase, and indeed the title of this Note, is based on the popular, if not the correct, version of a quotation from a cable from Mark Twain to the Associated Press after several newspapers printed a story concerning his reported death: "The reports of my death are greatly exaggerated." See, e.g., ASHTON APPLEWHITE ET AL., AND I QUOTE: THE DEFINITIVE COLLECTION OF QUOTES, SAYINGS, AND JOKES FOR THE CONTEMPORARY SPEECHMAKER 186 (1992). Although that is the more famous version, the actual quote was probably: "The report of my death was an exaggeration." OXFORD DICTIONARY OF QUOTATIONS 554 (3d ed. 1979). Perhaps the best comment on the accuracy of popular quotations in general comes from Yogi Berra, who once complained, "I didn't say everything I said." DANIEL OKRENT & STEVE WULF, BASEBALL ANECDOTES 207 (1989).

280. E.g., Cunningham & Yablon, *supra* note 30, at 1596 (describing the application of entire fairness as a "novel holding"); cf. Prickett & Brown, *supra* note 57, at 595 (noting that "doomsayers" of the bar in Delaware and elsewhere, as well as legal academia and the media, have already rolled their eyes to heaven in false alarm").

281. See Prickett & Brown, *supra* note 57, at 595-96 (arguing that *Technicolor* "does not change [Delaware] law").

282. *Smith v. Van Gorkom*, 488 A.2d 858, 889 (Del. 1985) (noting that the question of whether the \$55 price was "inadequate . . . is irrelevant to the threshold question of whether an informed judgment was reached" or whether the duty of care was met).

283. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1166 (Del. 1995) (*Technicolor III*).

resolved was the amount of that liability.²⁸⁴

Based on such a finding, the court remanded the case to the chancery court for "an evidentiary hearing to determine the fair value of [plaintiffs'] shares . . . in accordance with *Weinberger v. UOP, Inc.*"²⁸⁵ *Weinberger*, a duty of loyalty case, clearly provides that the defendants have the burden of proving the fair price at such a hearing.²⁸⁶ Furthermore, subsequent decisions seem to reinforce this requirement, implying that, if the business judgment rule does not apply (for *either* loyalty or care reasons), the entire fairness standard naturally would be the appropriate standard of review.²⁸⁷ Indeed, from the shareholders' economic perspective, it makes no difference whether their losses were caused "by a board's gross negligence or by acts of board disloyalty."²⁸⁸ Consequently, either fault logically should entail the same consequences—that the directors be required to prove the fairness of the transaction.²⁸⁹

If the business judgment rule can be described as a judicial unwillingness to inquire into the reasonableness of a business decision by a disinterested, informed board,²⁹⁰ it is only rational that any decision made by *either* a self-interested or an uninformed board *is* subject to second-guessing²⁹¹ to ensure that the outcome was fair to the shareholders. The application of the intrinsic fairness standard to both interested and uninformed boards thus is consistent with prior Delaware case law. If the

284. *Id.*

285. *Van Gorkom*, 488 A.2d at 893.

286. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983).

287. *See, e.g., Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1279 (Del. 1988) (noting that a court should not "evaluate the wisdom and merits of a business decision unless . . . the decision was not the product of an *informed*, disinterested, and independent board" and further noting that, "[i]n such a context, the challenged transaction must withstand rigorous judicial scrutiny under the exacting standards of entire fairness") (emphasis added) (citations omitted).

288. *Regan, supra* note 33, at 144 (citing Michael P. Dooley, *Two Models of Corporate Governance* 47 BUS. LAW. 461, 486 (1992)).

289. *See id.* (discussing the impact of a "decision-making process . . . gone awry" from *either* gross negligence or disloyalty).

290. *See supra* notes 44-139 and accompanying text.

291. *See, e.g., Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985) ("Under the business judgment rule there is no protection for directors who have made 'an unintelligent or unadvised judgment.'" (quoting *Mitchell v. Highland-Western Glass*, 167 A. 831, 833 (Del. Ch. 1933))).

business judgment rule does not apply, irrespective of whether the plaintiff rebuts the presumption of loyalty or the presumption of due care, the burden shifts to the defendant board to prove the entire fairness of the deal.²⁹²

Beyond noting that such a shift of burdens to the defendant directors is consistent with corporate-law precedent, it may be helpful to analyze whether it makes sense and, further, whether it is fair. The majority of suits seeking damages arise out of transactions involving a single prospective buyer.²⁹³ The *Technicolor II* burden shift in practice, therefore, is likely to be significant only to suits challenging transactions involving a single offeror, even though it is not so limited in theory.²⁹⁴ A court will most likely reach the entire fairness stage of the analysis only in cases in which there was a single bidder. When a jilted bidder thinks it has been wrongfully spurned by such a decision of a target board, the bidder will most likely bring an immediate (pre-closing) suit seeking injunctive relief ordering the target's board to commence or to reinstate the *Revlon* auction process or to void the target's defensive measures.²⁹⁵ If, however, the

292. Cunningham & Yablon, *supra* note 30, at 1596 ("Technicolor is clear in its novel holding that violations of the duty of care imply substantially the same consequences as violations of the duty of loyalty."). As discussed above, this holding is not necessarily as "novel" as it may have appeared. See *supra* notes 82-139 and accompanying text.

293. Cede & Co. v. Technicolor, Inc., 634 A.2d 345 (Del. 1993) (*Technicolor II*), modified in part, 636 A.2d 956 (Del. 1994); Barkan v. Amsted Indus., 567 A.2d 1279 (Del. 1989); *Van Gorkom*, 488 A.2d 858; Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983); *Rand v. Western Airlines*, reprinted in 19 DEL. J. CORP. L. 1292 (Del. Ch. Feb. 25, 1994); *Arnold v. Society for Sav. Bancorp, Inc.*, reprinted in 19 DEL. J. CORP. L. 1127 (Del. Ch. Dec. 17, 1993); *In re Vitalink Communications Corp. Shareholders Litig.*, reprinted in 17 DEL. J. CORP. L. 1311 (Del. Ch. Nov. 8, 1991); *Yanow v. Scientific Leasing, Inc.*, reprinted in 17 DEL. J. CORP. L. 659 (Del. Ch. July 31, 1991).

294. Some transactions, however, give rise to both types of suits. See, e.g., *Shamrock Holdings, Inc. v. Polaroid Corp.*, 559 A.2d 257 (Del. Ch. 1989).

295. See, e.g., *Dynamics Corp. of Am. v. CTS Corp.*, 805 F.2d 705 (7th Cir. 1986) (remanding for further consideration a tender offeror's suit to enjoin the target company's poison pill); *Edelman v. Fruehauf Corp.*, 798 F.2d 882 (6th Cir. 1986) (granting injunction to hostile tender offeror); *Hanson Trust PLC v. ML SCM Acquisition Inc.*, 781 F.2d 264 (2d Cir. 1986) (granting an injunction sought by a hostile tender offeror seeking to enjoin exercise of a lock-up option); *Black & Decker Corp. v. American Standard, Inc.*, 682 F. Supp. 772 (D. Del. 1988) (granting a preliminary injunction sought by a hostile bidder); *Unitrin, Inc. v. American Gen. Corp.*, 651

board's process has been adequate,²⁹⁶ it is entitled to the protections of the business judgment rule and no injunction will issue.²⁹⁷ Courts will permit the transaction to close, foreclosing any subsequent challenge. If a court finds the board's decisionmaking process defective,²⁹⁸ the court will not protect the board's decision and will issue an injunction, thereby preventing either the consummation of an unfair transaction or the improper use of a defensive measure.²⁹⁹ Thereafter, a court order will cover the board to ensure that it goes through a proper

A.2d 1361 (Del. 1995) (reversing and remanding the chancery court's grant of injunction to a hostile offeror); *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 36 (Del. 1994) ("QVC . . . [was] seeking preliminary and permanent injunctive relief."); *Paramount Communications, Inc. v. Time Inc.*, 571 A.2d 1140, 1142 (Del. 1989) (denying injunctive relief sought by rejected bidder Paramount); *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261 (Del. 1989) (granting an injunction to an "[u]nsuccessful bidder at corporate auction [seeking] to preliminarily enjoin lockup agreement between corporate directors and white knight"); *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334, 1346 (Del. 1987) (denying injunctive relief sought by T. Boone Pickens's rejected acquisition vehicle, Ivanhoe); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986) (granting an injunction sought by the "bidder for corporation's stock . . . to enjoin certain defensive actions taken by the target corporation"); *Moran v. Household Int'l, Inc.*, 500 A.2d 1346 (Del. 1985) (denying an injunction sought by a bidder to rescind the target's defensive measures); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985) (vacating an injunction obtained by a hostile tender offeror); *In re RJR Nabisco, Inc. Shareholders Litig.*, reprinted in 14 DEL. J. CORP. L. 1132 (Del. Ch. Jan. 31, 1989) (denying a preliminary injunction to enjoin the closing of a tender offer); *Grand Metro. Pub. Ltd. Co. v. Pillsbury Co.*, 558 A.2d 1049 (Del. Ch. 1988) (granting an injunction sought by a hostile tender offeror to invalidate the target's poison pill); *City Capital Assocs. v. Interco, Inc.*, 551 A.2d 787 (Del. Ch. 1988) (granting an injunction sought by a hostile tender offeror to invalidate the target's poison pill); *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103 (Del. Ch. 1986) (granting an injunction sought by hostile tender offerors). *But see Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 54 (Del. 1989) (denying the shareholder-plaintiff's contention that directors improperly accepted a \$66 all-cash, all-shares bid over a competing two-tiered bid of \$70 for 58% of the shares, with an unspecified back-end price). The failure of the bidder in *Citron* to challenge the board's decision may have been a tacit acknowledgment of the inadequacy of its offer, which it later withdrew. *Id.* at 63. In any event, its "failure to submit a firm and unconditional offer [as had been requested by the board], precluded a [heated] bidding contest." *Id.* at 68.

296. That is to say, the board's decision was the result of an informed and loyal procedure. *See Regan, supra* note 33, at 144 (discussing the impact of a "decision making process . . . gone awry" from *either* gross negligence or disloyalty).

297. *See, e.g., Unocal*, 493 A.2d at 958-59.

298. *See Regan, supra* note 33, at 144.

299. *See, e.g., QVC*, 637 A.2d at 51.

process and fairly and informedly completes the sale.

Not coincidentally, the single bidder situations are also the most likely to give rise to suits challenging the directors' loyalty.³⁰⁰ Further, these sales of control place the greatest premium on an informed directorate because there is no "market check" mechanism. Perhaps because of these similarities and inherent risks, courts have held that the proper analogy for breach-of-care cases is other fiduciary duty cases, not tort cases.³⁰¹ Consequently, it seems appropriate to apply a standard of review analogous to that applied in the duty-of-loyalty context.³⁰²

When deciding how best to allocate the burdens of proof, one commentator has suggested that courts consider "factors such as the ease with which the respective parties can gather and present evidence [and] the fairness of making one side rather than the other bear the burden of producing evidence."³⁰³ A brief

300. See, e.g., *Puma v. Marriott*, 363 F. Supp. 750 (D. Del. 1973); *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156 (Del. 1995) (*Technicolor III*); *Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983). In fact, one commentator has argued that even *Van Gorkom* is based on a breach of the duty of loyalty rather than of the duty of care. Carey H. Kirk, *The TransUnion Case: Is It Business Judgment Rule As Usual?*, 24 AM. BUS. L.J. 467, 481 (1986).

301. See *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 370 (Del. 1993) (*Technicolor II*) ("*Barnes*, a tort action, does not control a claim for breach of fiduciary duty. . . . The tort principles of *Barnes* have no place in a business judgment rule standard of review analysis."), modified in part, 636 A.2d 956 (Del. 1994). The latter rejection of tort principles is rather unusual, considering the court's holding that the business judgment rule did *not* apply. The court's rejection and apparent bafflement at the use of *Barnes* seems somewhat disingenuous. See Cunningham & Yablon, *supra* note 30, at 1599 n.41 (noting that *Barnes* was included in a leading corporations casebook for many years). In any event, "[r]ather than analogize [corporate control] duty of care cases to other tort cases, as the Chancery Court did, Justice Horsey [in *Technicolor II*] insist[ed] that the appropriate analogy is to other fiduciary duty cases" (i.e., the duty of loyalty cases). Cunningham & Yablon, *supra* note 30, at 1601.

302. Indeed, this approach is closely analogous to that applied by New York courts in evaluating actions for involuntary dissolution under § 1104-a of the N.Y. Business Corporation Law. N.Y. BUS. CORP. LAW § 1104-a (Consol. 1983). In such actions, when the plaintiff has met its burden of showing "oppression," the court presumes that he is entitled to a dissolution of the corporation unless the defendant can rebut such presumption. See, e.g., *In re the Judicial Dissolution of Kemp & Beatley, Inc.*, 473 N.E.2d 1173, 1180 (N.Y. 1984) ("Assuming the [plaintiff] has set forth a prima facie case of oppressive conduct, it should be incumbent upon the [defendants] to demonstrate to the court the existence of an adequate, alternative remedy [in lieu of dissolution].").

303. RICHARD O. LEMPert & STEPHEN A. SALTZBURG, A MODERN APPROACH TO

analysis of each of these elements indicates that it makes sense for the defendant directors to bear the burden of proving the entire fairness upon a showing of gross negligence. In this context, the board *should* have easier access to the information necessary to produce the valuation studies needed to show the entire fairness of the transaction. The board has access and in-depth knowledge of the corporation³⁰⁴ and might therefore have easier means of producing the relevant information.³⁰⁵ Further, because the directors are in control of the transaction, they have the ability to frustrate a potential plaintiff simply by following "the overriding rule for the merger wars: take no notes and avoid leaving a paper trail."³⁰⁶

With respect to the fairness of allocating the burden to the directors, the desired goal of the legal standard should be to force boards of directors to be adequately informed before accepting or rejecting a transaction resulting in a change of control.³⁰⁷ After a plaintiff has proved that a board was not ade-

EVIDENCE 795 (2d ed. 1982).

304. This fact is likely to be true even in a duty-of-care case when a court finds the board insufficiently informed as to the value of the company.

305. In effect, this fact is precisely the reverse of *res ipsa loquitur*. Assuming that the circumstances meet the prior conditions for the *res ipsa* doctrine (exclusive control by the defendant, no contributory fault by the plaintiff), the theory is that, in all cases in which a plaintiff is injured, it is more likely than not that the defendant was negligent because such harm does not ordinarily occur if the defendant had used due care. See generally W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 39, at 242-57 (5th ed. 1984) (describing the theory of *res ipsa loquitur*). Accordingly, the defendant must rebut the presumption of negligence. *Id.* In these cases, the theory posits that, when the board has breached its duty, it is more likely than not that the plaintiff was injured (because the transaction was not entirely fair).

306. LEDERMAN, *supra* note 8, at 179. Lederman goes on to note that, from his own personal experience, being confronted with documentation from a deal is "worrisome" at best. "Seeing the file [documenting the deal and], . . . [l]ooking back over the decision process, all the second thoughts were obvious." *Id.* at 185.

307. Additionally, the nature of what is at stake justifies placing the burden of showing that a board decision is the result of a "dysfunctional process" on the plaintiff. Regan, *supra* note 33, at 144. In the transactional justification setting, the plaintiff is seeking only an opportunity—an opportunity to accept tenders (if any) or an opportunity to bid, perchance to win. In the postclosing context, however, the plaintiff is seeking to impose enormous personal liability on the directors. For instance, *Van Gorkom* settled for more than \$23 million, without any showing that the price was actually too low. Manning, *supra* note 65, at 1 (editor's note). To foist upon the directors a burden of proof to avoid such monumental liability offends

quately informed, the *Technicolor* cases require that the board show that the transaction was fair to the shareholders. The board can show fairness by doing precisely what it should have done earlier to meet its duty of care—obtaining “a body of reliable evidence with which [to now allow the trier of fact] to evaluate the fairness of a transaction.”³⁰⁸ That is, the board can have an expert conduct a valuation study or fairness opinion³⁰⁹ and conduct a canvass of the market to determine the “going price” for a similarly situated business.

Accordingly, the Delaware courts will require corporate directors to complete an orderly information-gathering process in all change-of-control transactions. If a party (most commonly a jilted bidder) challenges the directors’ actions prior to closing and the board lacks information, the court will order the board to gather more information before concluding the transaction. In other words, the so-called *Revlon* duties will apply. If a party challenges the board’s actions after closing (usually in a shareholder suit seeking to impose personal liability on the directors) and the court finds that the process was flawed, the directors must, under the *Technicolor* line of cases, go back and complete the information-gathering process—they must prove that the transaction was entirely fair to the shareholders. The modern

fundamental notions of fair play and justice.

308. *Barkan v. Amsted Indus.*, 567 A.2d 1279, 1287 (Del. 1989).

309. However, the accuracy of valuation studies conducted strictly for the purposes of litigation can be debated. The court in *Technicolor III* seemingly agreed with Chancellor Allen that the “methodology and conclusions” of the plaintiff-shareholders’ valuation expert were “troubling” and “too strikingly odd” to be accepted. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1177 (Del. 1995) (*Technicolor III*) (quoting *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134, 1144 (Del. Ch. 1994), *aff’d*, 663 A.2d 1156 (Del. 1995)). For an extreme example of what might be termed a battle of “hired gun” experts, see *Taines v. Gene Barry One Hour Photo Process, Inc.*, 474 N.Y.S.2d 362, 365 (Sup. Ct. 1983), in which the court rejected both parties’ purported valuation studies of a corporation that employed an innovative photo-finishing method:

I find both experts’ reasoning fallacious and their conclusions preposterous, and I give no weight whatsoever to either of their ultimate conclusions as to the value of the business. The petitioner’s expert valued the business, as of August 27, 1981, as \$20,700,000. The respondent’s expert valued the same business, as of the same day, at \$71,000—a difference of nearly thirty thousand percent!

Id. (emphasis added).

status of Delaware law thus is entirely consistent: boards must sooner or later obtain the same information, either (1) during the course of negotiating, approving, or defending against an imminent control transaction or (2) to prove the intrinsic fairness of the transaction.

The Burdens of Proof Should Be Allocated Differently in Different Litigation Postures

One criticism of *Technicolor II* might be that Delaware law now allocates different burdens to the parties based solely on the litigation posture of the case (i.e., the burdens on directors are higher in a "transactional justification" case than in a postclosing personal liability case). Traditionally, before an injunction will issue, a plaintiff must prove (among other things) *irreparable injury*.³¹⁰ To require a plaintiff seeking an injunction to prove injury but to remove that burden from a party seeking to actually impose monetary damages upon a board of directors seems somewhat anomalous. As discussed above, the distinction may be more important in theory than in reality. In suits brought by a frustrated bidder seeking to enjoin the sale of the target to a rival, if the board is uninformed, it will fail the first prong of the *Unocal* enhanced scrutiny test and the court will order appropriate action. The shareholders should be able to obtain court-ordered protection from injury because the actions likely to be ordered (i.e., those necessary to become informed and/or otherwise obtain the maximum value for shareholders) will be precisely the same actions that avoid any injury to potential postclosing plaintiff-shareholders.³¹¹ In short, for the board to become informed, it must necessarily conduct the auction or further investigate the spurned offer.

Under current Delaware law, a plaintiff challenging a board's actions with respect to a transaction that has already closed

310. *Gimbel v. Signal Cos.*, 316 A.2d 599, 603 (Del. Super. Ct. 1988).

311. Cases in which shareholders are the parties seeking an injunction to force an auction are rare, and courts can resolve them by reference to the fact that the shareholder has an adequate remedy by bringing a suit for damages. *See, e.g., Norberg v. Young's Mkt. Co.*, reprinted in 16 DEL. J. CORP. L. 351, 359 (Del. Ch. Dec. 19, 1989) (noting that monetary damages would be available to shareholders if they proved a breach of the board's duty of care).

must rebut the presumption that the board was adequately informed. The burden requires the plaintiff to show that the decision was procedurally flawed—in effect, that the board did not have “a body of reliable evidence with which to evaluate the fairness of the transaction.”³¹² If a plaintiff fails to rebut this presumption, a court will *not* examine the substantive reasonableness of the board’s decision.

In the transactional justification setting, however, heightened or enhanced scrutiny will apply, requiring the board to prove that it *was* informed and that its actions on that information were within a “range of reasonableness.”³¹³ Because language in *QVC* suggested that the court mandated enhanced scrutiny due to the fact that the transaction involved a change in control,³¹⁴ one commentator has suggested that all control transactions (apparently irrespective of their litigation posture) will be subject to review under enhanced scrutiny.³¹⁵ Despite that language in *QVC*, it is highly unlikely that the court intended, or will intend, to expand enhanced scrutiny out of transactional justification (historically its birthplace and exclusive domain) into postclosing litigation. First and foremost, the court took extreme pains both to reconcile prior decisions and to note that *QVC* represented no departure from prior precedent. Applying enhanced scrutiny in a postclosing posture would rend an enormous gulf in existing Delaware law. *Technicolor II*, decided less than a year before *QVC*, applied the traditional *Van Gorkom* business judgment rule in the postclosing context and made no attempt whatsoever even to suggest that enhanced scrutiny would be appropriate. That the Delaware court would so suddenly make such a severe break with its prior precedents is nearly inconceivable. Perhaps anticipating such a suggestion, the court in *QVC* repeatedly noted that it was deciding only the facts before it.³¹⁶

312. *Barkan*, 567 A.2d at 1287. Of course, a plaintiff also could attack a board’s decision by asserting duty-of-loyalty issues.

313. *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 45 (Del. 1994).

314. *Id.* at 42.

315. Regan, *supra* note 33, at 126.

316. *QVC*, 637 A.2d at 43 n.13 (“We express no opinion on any scenario except the

Enhanced scrutiny is justified in the pre-closing setting by the "omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its shareholders," thus forcing the board to prove the procedural and substantive adequacy of its decisionmaking process.³¹⁷ In situations in which the transaction has already closed, however, several events have taken place that may limit this "specter." First, in order for the transaction to close, a majority of shareholders must have either approved the transaction (in the case of a merger) or have tendered their shares to the offeror.³¹⁸ Because of the "prisoner's dilemma,"³¹⁹ however, shareholder approval or tenders alone may not be enough to justify placing the burden on the plaintiffs. The more important factor is the very likely absence of a second bidder. Because of court receptiveness to auction requirements,³²⁰ a bidder who believes a price to be

actual facts before the Court."). The court also limited its holding by noting that its conclusions apply only "under the facts of this case" and "only [to] the case before us." *Id.* at 51.

317. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985).

318. Under *Van Gorkom*, however, shareholder approval is not alone sufficient to avoid liability on the part of the directors. *Smith v. Van Gorkom*, 488 A.2d 858, 873 (Del. 1985) ("[A] director may not abdicate [his fiduciary] duty by leaving to the shareholders alone the decision to approve or disapprove the agreement."). The fact that such approval is not sufficient to avoid liability does not diminish its usefulness in shifting the burden to the plaintiff. In fact, this is precisely the procedure that *Weinberger* called for in examining the entire fairness of cash-out mergers. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 703 (Del. 1983) ("[W]here corporate action has been approved by . . . a majority of the minority shareholders, . . . the burden entirely shifts to the plaintiff to show the transaction was unfair.").

A deeply divided Delaware court recently struggled with the question of exactly what weight to give shareholder approval of board recommendations, especially with respect to board actions possibly involving a breach of the duty of loyalty. See *Williams v. Geier*, No. 380, 1994, 1996 Del. LEXIS 65 (Del. Sup. Jan. 23, 1996). The majority in *Williams* relied, to some extent, on shareholder approval of a recapitalization plan to avoid imposing liability on the corporation's directors based on their recommendation of the plan. See *id.* at *29-34. The majority opinion explicitly distinguished "voidable" transactions, such as the one in *Van Gorkom*, without elaboration and simply "express[ed] no opinion on the question whether a 'duty of loyalty claim' may or may not be ratified." *Id.* at *32 n.23. The dissent was far less willing to rely on a shareholder vote, noting the possibility of shareholder coercion. *Id.* at *56 (Hartnett, J., dissenting).

319. See *supra* notes 169-71 and accompanying text.

320. At the very least, the court will impose a duty to "realize for the stockholders the best value reasonably available," which will in fact force a board to conduct such

too low has a tremendous incentive to plunge in with a rival offer.³²¹ *QVC* is an excellent example of a rival bidder's ability to plunge in and break up even an agreement containing formidable lock-up provisions that one participant bragged would take a "nuclear attack" to break up.³²² The knowledge that the board will give a potential acquiror a fair opportunity to bid on a company should prevent most "targets" from being stolen at inadequate prices.³²³ In *Technicolor III*, the court reaffirmed the importance of both of these factors, citing each as persuasive evidence that the Technicolor shareholders received a fair price. The court agreed with Chancellor Allen that the sale by major inside shareholders (including two directors) "powerfully implie[d] that the price received was fair."³²⁴ Despite a delay in closing the Technicolor tender offer, the court found the absence of a rival bidder to be even more persuasive evidence that the price was fair.³²⁵

Chief Justice Veasey, writing several years ago while still in private practice, suggested that there is, in fact, a distinction between the business judgment "doctrine" and the business judgment "rule," arguing that the "doctrine" is used to protect the validity of the directors' decision (as in a transactional justification case), whereas the "rule" is used to shield the directors themselves from personal liability:

In the takeover arena . . . not only will the process be scruti-

an auction. *QVC*, 637 A.2d at 43.

321. See, e.g., *Barkan v. Amsted Indus.*, 567 A.2d 1279, 1287 (Del. 1989) (observing that, "when it is widely known that some change of control is in the offing and no rival bids are forthcoming over an extended period of time, that fact is supportive of the board's decision to proceed" with the pending transaction). One reason for this is that the costs of litigation (which may limit the desirability of reliance on a party to bring a suit in other settings) are infinitesimal in the corporate takeover context in comparison to the potential gains involved in an acquisition.

322. *QVC*, 637 A.2d at 39 (quoting Sumner Redstone, CEO of Viacom); see *supra* notes 155-67 and accompanying text.

323. Indeed, the Delaware court in *Technicolor III* recognized that its *QVC* ruling should make it easier for other bidders to intervene, even in the face of "apparent obstacles" such as lock-ups or no-shop provisions. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1177 (Del. 1995) (*Technicolor III*).

324. *Id.* (quoting *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134, 1143 (Del. 1994), *aff'd*, 663 A.2d 1156 (Del. 1995)).

325. *Id.*

nized, but substantive decisions will be examined for "reasonableness" Such a jurisprudential approach should have no rightful place in the application of the defensive business judgment rule, but in the application of the business judgment doctrine in transactional justification cases . . . there is a new scrutiny emerging.³²⁶

Chief Justice Veasey's court now seems to be implementing the very distinction that he previously advocated as a practitioner, but thus far it has declined to adopt the terminology.³²⁷ Perhaps, at this time, the court may use a return to the distinction to clarify the differences between a *QVC* or a *Revlon* and a *Technicolor*.

CONCLUSION

The predictions of cataclysmic change accompanying recent Delaware Supreme Court decisions are unwarranted. *Technicolor II* did not change Delaware law; it merely applied existing precepts to a situation not previously faced by the courts (notably due to the settlement of *Van Gorkom* prior to the hearing on damages). *QVC* also does not represent the seismic shift in focus that commentators have predicted. Although the court articulated new rationales for its positions and holdings, the main thrust of the case is consistent with well-established principles. The ultimate result of the recent change-of-control cases may well be that all scrutiny of directors' conduct under the duty of care will result in an examination of whether those decisions were "within the range of reasonableness."³²⁸ In fact, the court consistent-

326. E. Norman Veasey, *Business Judgment Rule: The New Incarnation*, LEGAL TIMES, Mar. 10, 1986, at 25, 40 (emphasis added); see also Veasey, *supra* note 36, at 504-06 (discussing the distinction between transactional justification cases and the business judgment rule); cf. Joseph Hinsey IV, *Business Judgment and the American Law Institute's Corporate Governance Project: The Rule, the Doctrine and the Reality*, 52 GEO. WASH. L. REV. 609, 609 (1984) ("analyz[ing] the treatment of the business judgment rule . . . by the American Law Institute").

327. In *Revlon*, decided before Chief Justice Veasey joined the Delaware Supreme Court, the court expressly declined to adopt such terminology. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 180 n.10 (Del. 1986). In its discussion, however, the court did not rule out the usefulness of such a distinction. *Id.*

328. *Paramount Communications Inc. v. QVC Network Inc.*, 637 A.2d 34, 45 (Del.

ly has indicated that the proper standard for reviewing board conduct is one of reasonableness. Ultimately upholding Unitrin's combination of defensive measures, the court noted that there is to be no inquiry into whether a defensive measure was, in its judgment, "necessary" to rebuff the threat.³²⁹ This statement of judicial restraint is similar to the court's cautionary statements in *Technicolor III* and *QVC*. In those cases, the court noted that the proper test is one of reasonableness not of perfection. In *Technicolor III*, the court noted that, although the board's process was flawed, those flaws did not preclude a finding of entire fairness: "[a] finding of perfection is not a sine qua non in an entire fairness analysis."³³⁰ In *QVC*, the court described the proper inquiry as whether the "directors made a reasonable decision, not a perfect decision."³³¹ The court thus has seemed to indicate consistently that, although heightened or enhanced scrutiny will apply in change-of-control situations, courts must reserve this scrutiny to enable directors some leeway in their decisions. This enhanced but flexible standard thus preserves the original goals of the business judgment rule while holding steadfast in the demand that directors be especially diligent in change-of-control situations, obtaining the "best value reasonably available" for shareholders.³³² Such a goal has always been the essence of *Revlon* and will survive as its enduring legacy

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1994); *Unitrin, Inc. v. American Gen. Corp.*, 651 A.2d 1361, 1385 (Del. 1995).

329. *Unitrin*, 651 A.2d at 1391.

330. *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1179 (Del. 1995) (*Technicolor III*).

331. *QVC*, 637 A.2d at 45.

332. *Id.* at 43.