COMMENTS

IS A MERGER AGREEMENT EVER CERTAIN? THE IMPACT OF THE *OMNICARE* DECISION ON DEAL PROTECTION DEVICES

ABSTRACT

The board of directors for a corporation adopts defensive measures, such as shareholder agreements, to protect the corporation from hostile bidders. The deal protection devices increase the likelihood that a transaction will be consummated in merger transactions. Deal protection devices are advantageous for both the bidding and the target corporation. The Delaware Supreme Court, in Omnicare, Inc. v. NCS Healthcare, Inc., *addressed the issues of "locking-up" a merger transaction with deal protection devices and a board of directors' fiduciary duties surrounding the transaction. In a rare 3-2 split, the court held that deal protection devices in merger transactions will be reviewed with enhanced scrutiny, deal protection devices which result in a "locked-up" transaction are invalid without a "fiduciary out" clause and the board of directors has fiduciary duties to minority shareholders in merger transactions.*

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I. INTRODUCTION

A corporation's board of directors implement deal protection devices to protect the corporation from potential hostile invaders. Some common devices adopted by corporations are no-talk provisions, termination fees, requirements to recommend the transaction to stockholders, shareholder agreements, and supermajority voting requirements.[1] Deal protection measures, in the context of a "merger of equals" transaction,[2] increase the likelihood that the transaction will be consummated.

There are certain advantages for both the target and the bidding company[3] to ensure that the negotiation process will result in a completed merger transaction. The indebted target, under the threat of bankruptcy, may be comforted in knowing that its debt will be paid without fearing that the bidder will withdraw from the transaction.[4] The bidder, conversely, is comforted by the certainty that the transaction will be consummated

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[1]*See* DANIEL Q. POSIN, CORPORATE TAX PLANNING: TAKEOVERS, LEVERAGED BUYOUTS, AND RESTRUCTURING ch. 2 (1990) (explaining various merger protection devices).

[2]A merger of equals transaction is a stock-for-stock merger transaction in which neither the buyer nor seller company has one person or one entity owning the majority shareholder voting power before the merger, and the combined company also does not have one person or entity owning the majority voting shareholder voting power after the merger transaction. Mark Lebovitch & Peter B. Morrison, *Calling A Duck A Duck: Determining the Validity of Deal Protection Provisions in Merger of Equals Transactions*, 2001 COLUM. BUS. L. REV. 1, 2 (2001).

[3]The corporation that is acquiring or buying is recognized as the bidding corporation and the corporation that receives cash and/or debt of the acquiring corporation is recognized as the target corporation.

[4]Additionally, by ensuring certainty in the deal, the target can avoid being put on the market or "in play" and forced into an unwanted transaction. *See* ARTHUR FLEISCHER, JR. & ALEXANDER R. SUSSMAN, TAKEOVER DEFENSE § 15.05 (6th ed. Supp. 2002).

without fearing interference from another corporation.[5] A court's inherent conflict when reviewing merger transactions is balancing the corporation's advantages to ensuring certainty against a board of directors' fiduciary duties to the corporation and its creditors.

The Delaware Supreme Court recently addressed the issues of "locking-up" a merger agreement to ensure that the merger will be consummated and a board of directors' fiduciary duties in *Omnicare, Inc. v. NCS Healthcare, Inc.*[6] In a rare 3-2 split, the majority held that deal protection devices in merger transactions will be judicially reviewed under an enhanced scrutiny standard, deal protection measures which result in a "locked-up" merger agreement are invalid absent a "fiduciary out"[7] provision, and the board of directors have a fiduciary duty to protect minority stockholders.

To fully understand the impact of the *Omnicare* decision, Part II of this comment will discuss the different standards of review applied by the court. Part III.A will provide a summary of the events leading to the NCS board of directors' decision to "lock-up" the merger transaction. Then, Parts III.B and C will analyze the Delaware Court of Chancery's decision and the Delaware Supreme Court's majority and minority decisions. Finally, Part IV will evaluate the potential impact from the *Omnicare* decision on Delaware corporation law and Delaware's corporations.

II. STANDARDS OF REVIEW

The increased number of hostile raids in the 1970s and 1980s led

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[5]The bidder, by ensuring certainty, will not risk serving as a "stalking horse" for a better deal or risk expending time, effort, and money on an uncertain transaction. *Id.*

[6]818 A.2d 914 (Del. 2003). Although the holding is not binding on other jurisdictions, the impact of the courts decision may be great since "Delaware corporate and takeover law is also the most developed of any state and is looked to by federal and state courts in applying its law." *See* FLEISCHER & SUSSMAN, *supra* note 4, § 1.03(c). Additionally, the greatest number of major companies are incorporated in Delaware. *Id.*

[7]A "fiduciary out" provision in a merger agreement provides the target corporation an escape to terminate a merger transaction under certain circumstances. Generally, the provision permits a board to provide confidential information to third parties, withdraw its recommendation for the merger, and seek and accept offers from third parties if a third party offers a superior proposal. *See generally* POSIN, *supra* note 1, at 191 (stating that a "fiduciary out" provision permits a board of directors to provide confidential information or seek offers from third parties); William T. Allen, *Understanding Fiduciary Outs: The What and the Why of an Anomalous Concept*, 55 BUS. LAW. 653 (2000) (explaining that "fiduciary out" provides an escape hatch to a board from performance of a contractual agreement prior to a merger or acquisition agreement).

corporations to adopt defensive measures against hostile takeovers.[8] Since a board of directors "is the only group with effective opportunity to both advance and protect the best interests of all shareholders,"[9] Delaware courts have established standards to review directors' decisions and fiduciary duties in the context of a defensive measure.[10]

Section 141 of the Delaware General Corporation Law (DGCL) affords a corporation's board of directors the power to manage all the affairs of a corporation.[11] Traditionally, Delaware courts under most circumstances would not second guess a board's decision and substitute its judgment for that of the board. However, in 1985, the Delaware Supreme Court modified the existing business judgment standard in *Unocal Corp. v. Mesa Petroleum Co.*[12] The court held that, in certain circumstances, an enhanced scrutiny standard shall apply to the boards' actions before applying the deferential business judgment rule. The court then further refined the enhanced scrutiny standard in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*,[13] which upheld the *Unocal* standard but imposed a special duty on directors to approve the highest priced transaction upon a change of central transaction. The majority in *Omnicare* defined each standard and the situations that it applies in the merger transaction context.

A. *The Business Judgment Rule*

The business judgment rule is a common law rule that shields a

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[8]The cause of the surge in takeovers is speculative: "While a number of contributing factors have been cited, there can be little doubt that the rise and growth of the institutional investor has played a major part." Dean James F. Hogg, *Hostile Takeovers and Other War Games*, *in* THE PREDATOR AND THE PREDATEE 1, 32 (1988).

[9]*Id.* at 30.

[10]For examples of differing approaches to the appropriate standard of review for deal protection devices, see Allen, *supra* note 7; Leo E. Strine, Jr., *Categorical Confusion: Deal Protection Measures in Stock-for-Stock Merger Agreements*, 56 BUS. LAW. 919 (2001); Gregory V. Varallo & Srinivas M. Raju, *A Process-Based Model for Analyzing Deal Protection Measures*, 55 BUS. LAW. 1609 (2000).

[11]DEL. CODE ANN. tit. 8, § 141(a) (2001) provides:

> The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation. If any such provision is made in the certificate of incorporation, the powers and duties conferred or imposed upon the board of directors by this chapter shall be exercised or performed to such extent and by such person or persons as shall be provided in the certificate of incorporation.

[12]493 A.2d 946 (Del. 1985).

[13]506 A.2d 173 (Del. 1986).

board of directors' actions from being second-guessed by the courts.[14] In *Sinclair Oil Corp. v. Levien*,[15] the Delaware Supreme Court summarized the rule: "A board of directors enjoys a presumption of sound business judgment, and its decisions will not be disturbed if they can be attributed to any rational business purpose."[16] The presumption of a sound business judgment assumes, unless proven otherwise, that the directors "acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interest of the company."[17] The business judgment rule is premised on the general acknowledgment that courts lack the information and skill necessary to evaluate the judgments of directors.[18]

When applying the business judgment rule, a court places the burden to prove a breach of the directors' fiduciary duties on the "party challenging the [board's] decision to establish facts rebutting the presumption."[19] If the party challenging the board's decision fails to rebut the rule's presumption, "a court will not substitute its judgment for that of the board if the [board's] decision can be 'attributed to any rational business purpose.'"[20]

B. *Application of the* Unocal *Enhanced Scrutiny Standard*

Delaware courts apply the *Unocal* heightened standard of review when a board of directors adopt defensive protection devices in response to a hostile takeover. Under the *Unocal* analysis, the burden shifts to the directors to show that they had reasonable grounds to believe a threat to

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[14]Corinne Ball et al., *Advising the Board of Directors in the Context of Mergers and Acquisitions*, *in* STRUCTURING MERGERS & ACQUISITIONS 183, 191 (2001).

[15]280 A.2d 717 (Del. 1971).

[16]*Id.* at 720. The American Law Institute's formulation of the business judgment rule provides that directors fulfill their fiduciary duty if they:

> (1) [are] not interested in the subject of the business judgment; (2) [are] informed with respect to the subject of the business judgment to the extent the director or officer reasonably believes to be appropriate under the circumstances; and (3) rationally believes that the business judgment is in the best interests of the corporation.

AM. LAW INST., PRINCIPLES OF CORPORATE GOVERENCE: ANALYSIS & RECOMMENDATIONS § 4.01(c) (1994).

[17]Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1373 (Del. 1995) (quoting Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984)).

[18]*See* Gregory V. Varallo & Srinivas M. Raju, *A Fresh Look at Deal Protection Devices: Out from the Shadow of the Omnipresent Specter*, 26 DEL. J. CORP. L. 975, 977 (2001).

[19]*Unitrin*, 651 A.2d at 1373 (quoting *Aronson*, 473 A.2d at 812).

[20]*Id.* (quoting Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985)). The court noted that boards comprised of disinterested, independent directors, who are acting in accordance with established standards, increase the probability that the business judgment rule will be applied. *Unocal*, 493 A.2d at 955.

corporate policy existed before the protection of the business judgment rule is conferred.[21] The court recognizes the need for an enhanced standard because of the inherent conflict of interest that directors, when making decisions regarding defensive measures, may act solely or primarily in their own interests.[22]

Under *Unocal*, two prerequisites must be met before directors receive the protection of the business judgment rule. First, the "directors must show they had reasonable grounds for believing that a danger to corporate policy and effectiveness existed."[23] A board of directors can satisfy the first prong by showing that the board acted in "good faith," based upon a "reasonable investigation."[24]

Second, the defensive measures "must be reasonable in relation to the threat posed."[25] The court noted that directors "do not have unbridled discretion to defeat any perceived threat by any Draconian means available."[26] The directors, in order to satisfy the second prong, must

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[21]For a discussion of actions board of directors' may take to establish their burden, see FLEISCHER & SUSSMAN, *supra* note 4, § 3.03.

[22]*Unocal*, 493 A.2d at 955. The court noted that "[b]ecause of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and its stockholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred." *Id.* at 954.

In *Unocal*, Mesa Petroleum Co., a minority shareholder of Unocal's common stock, commenced a two-tier "front loaded" tender offer which would result in Mesa owning all of Unocal's common stock. *Id.* at 949. In the front tier, Mesa would become the majority shareholder by purchasing thirty-seven percent of Unocal's stock at a reasonable price. *Id.* On the "back-end," Mesa would purchase the remaining shares for what Unocal deemed "highly subordinated . . . junk bonds." *Id.* at 949-50. The board of directors met and decided they would reject Mesa's tender offer as inadequate, and if Mesa commenced the front end of the tender offer, their defensive response would be that Unocal would self-tender the remaining shares at higher price than Mesa's offer. *Id.* at 950-51. Additionally, the board decided that they would exclude purchasing any Mesa shares in their proposed self-tender. *Id.* at 951. After Unocal's exchange offer was commenced, Mesa challenged the defensive action by filing a suit in the chancery court claiming, among other things, that the board breached its fiduciary duties by excluding Mesa, as a minority shareholder, from Unocal's defensive self-tender offer. *Id.* at 951.

The Delaware Supreme Court held that the self-tender response was made in good faith upon a reasonable investigation, and was reasonable in relation to the threat that the board rationally and reasonably believed was posed by Mesa's inadequate two tiered tender offer. *Id.* at 958. The court stated that under those circumstances, the directors were afforded the protections of the business judgment rule. *Id.* at 958-59.

[23]*Id.* at 955.

[24]*Id.* (quoting Cheff v. Mathes, 199 A.2d 548, 555 (Del. 1964)).

[25]*Id.*

[26]*Unocal*, 493 A.2d at 955.

analyze the nature of the takeover threat and its effect on the corporation as a whole.[27]

The second requirement, commonly known as "the proportionality paradigm/test," was further defined by the supreme court in *Unitrin, Inc. v. American General Corp.*[28] The court interpreted the case law to include two determinations. The first determination is whether the defensive measures were "preclusive" or "coercive."[29] If the first determination is satisfied, the proportionality paradigm then shifts to "the range of reasonableness" standard, in which a board of directors garners latitude in discharging its fiduciary duties when adopting defensive measures against perceived threats.[30]

In sum, when a court applies the *Unocal* enhanced scrutiny standard, the court initially determines whether a board of directors, through good faith and a reasonable investigation, has a reasonable belief that a threat posed a danger to the corporation. If the directors' belief is reasonable, the court then analyzes the proportionality paradigm to determine whether the defensive measures adopted are reasonably related to the perceived threat. In analyzing the proportionality paradigm, a court first determines whether the defensive measures were preclusive or coercive. If the measures are not preclusive or coercive, then the court, giving latitude to the board, determines whether the defensive measures are within the range of reasonableness. Once a board satisfies this standard, the board receives the protection of the business judgment rule and courts will not "substitute its judgment for the board's."[31]

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[27] *Id.* The court included examples of concerns for a board to analyze: "[the] inadequacy of the price offered, [the] nature and timing of the offer, questions of illegality, the impact on 'constituencies' other than shareholders (i.e., creditors, customers, employees, and perhaps even the community generally), the risk of nonconsummation, and the quality of securities being offered in the exchange." *Id.*

[28] 651 A.2d 1361 (Del. 1995).

[29] *Id.* at 1387-88. A defensive measure is "coercive" if it is aimed at forcing a management sponsored alternative upon stockholders in response to a hostile offer. *Omnicare*, 818 A.2d at 935 (citing *Unitrin*, 651 A.2d 1387-88). Additionally, a response is "preclusive" if it deprives stockholders of the right to receive all tender offers or precludes a bidder from seeking control by fundamentally restricting proxy contests or otherwise. *Id.* (quoting Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1154 (Del. 1989)).

[30] *Unitrin*, 651 A.2d at 1388 (quoting Paramount Communications, Inc. v. QVC Network, Inc., 637 A.2d 34, 45-46 (Del. 1994)). [? why "quoting" b/c there aren't any inner quotes in text]

[31] *Id.* (citing *Paramount Communications*, 637 A.2d at 45-46). The *Unitrin* court also elaborated on the judicial function in applying the enhanced scrutiny standard:

> a court applying enhanced judicial scrutiny should be deciding whether the directors made a *reasonable* decision, not a *perfect* decision. If a board selected one of several reasonable alternatives, a court should not second

C. *Situations Where* Revlon *Duties Apply*

In addition to the *Unocal* enhanced scrutiny, the Delaware Supreme Court, in *Revlon,* imposed a special fiduciary duty on directors that arises when the transaction results in a change-of-control or the corporation is put up for sale.[32] In this situation, a special fiduciary duty is imposed on the board of directors to seek the best price for the stockholders, thus requiring directors to negotiate with a hostile corporation if it proposes a better deal.[33]

When courts analyze directors' action in a *Revlon* setting, the *Unocal* standard is distinguished, but not overturned. Following the standards set forth in *Unocal*, the court shall review *Revlon* duties under an enhanced scrutiny standard, which requires that directors' actions comply with the fiduciary standards to, among other things, determine the best interests of the corporation and its stockholders.[34] The difference between the *Revlon* and *Unocal* standards is that when a corporation is put up for sale or engaged in transactions leading to a change-in-control, thus triggering *Revlon*, directors no longer need to adopt defensive measures upon a belief that a threat to corporate policy or effectiveness exists.[35] The directors'

> guess that choice even though it might have decided otherwise or subsequent events may have cast doubt on the board's determination.

Id. at 1385-86 (quoting *Paramount Communications*, 637 A.2d at 75-76).

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

[33]*Id.* at 182. The relevant facts in *Revlon* are as follows: After unsuccessful discussions for Pantry Pride, Inc. to acquire Revlon, Inc., Pantry Pride's board authorized the acquisition though negotiation or by making a hostile tender offer. *Id.* at 176. The Revlon board countered this threat by implementing two defensive measures: first, that the company repurchase five million of its approximately thirty million outstanding shares; and second, to exchange each share of common stock for a $65 Revlon note at twelve percent interest with a one year maturity. *Id.* at 177. These defensive measures would become effective whenever someone acquired twenty percent or more of Revlon share. *Id.* at 177. While Pantry Pride unsuccessfully attempted to acquire Revlon through its hostile tender offer, Revlon began negotiations to sell its cosmetics and fragrance divisions to and merge with Forstmann Little & Co. *Id.* at 177-78. At a meeting where representatives of all three companies were present, Pantry Pride announced that it would engage in fractional bidding for control of Revlon and would top any Forstmann offer. *Id.* at 178. Forstmann subsequently proposed, and the Revlon board approved, a $57.25 per share offer, subject to various conditions such as a lock-up and no-shop provision. *Id.* at 178-79. Pantry Pride then outbid Forstmann, proposing a cash offer of $58 per share. *Id.* at 179.

The supreme court held that under all the circumstances the directors did not take into consideration the maximization of shareholder profit and ceased the auction for Revlon to the ultimate detriment of its shareholders. *Id.* at 185. Furthermore, the court held that the directors' actions do not withstand the enhanced scrutiny standard and are not entitled to the protection of the business judgment rule. *Id.*

[34]*Id.* at 181. The court noted that, under *Revlon*, the directors' actions are still held to the fiduciary duties defined in *Unocal*. *Id.*

[35]*Id.* at 182.

duty changes from preserving the corporate entity to the maximization of the company's value for the benefit of the stockholders.[36] In *Omnicare,* the majority seemed to dissolve the bright line between *Revlon* and *Unocal,* holding that, absent any sale or change of control, when a board locks up a merger transaction using defensive measures, the directors have a special duty to its minority shareholders.

III. ANALYSIS OF THE *OMNICARE* DECISIONS

Prior to the majority's decision in *Omnicare,* the creation of standards for the review of deal protection devices had been the subject of intense debate.[37] The Delaware Supreme Court majority, under vigorous dissenting opinions, established a uniform standard and bright line factors for future courts to review protection measures under the *Unocal* standard.

A. *The Facts*

1. NCS's Financial Woes

The defendant, NCS Healthcare, is an independent provider of pharmacy services to long-term care institutions.[38] NCS common stock consisted of Class A shares and Class B shares.[39] The board of directors for NCS, all named defendants, consisted of four members: Jon H. Outcalt and Kevin B. Shaw (the majority shareholders),[40] and Boake A. Sells and Richard L. Osborne.

Beginning in late 1997, governmental and third-party provider changes in the level of reimbursements and timing adversely affected the

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

[37]*See supra* note 10.

[38]NCS Healthcare, Inc. provided services to institutions, which included skilled nursing centers, assisted living facilities and hospitals, in thirty-three states and managed hospital pharmacies in fourteen states, totaling approximately 203,000 residents. Press Release, NCS Healthcare, Inc., *NCS Healthcare Recommends that Stockholders Reject Omnicare's Tender Offer* (Aug. 20, 2002), *available at* http://www.ncshealth.com/TenderOffer.htm (last visited Nov. 1, 2004). NCS Healthcare is headquartered in Ohio and incorporated in Delaware. Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 918 (Del. 2003).

[39]*Omnicare*, 818 A.2d at 918. Class A shares and Class B shares are virtually identical; the difference being that Class B shares entitled the holder to ten votes per share and Class A holders were entitled to one vote per share. *Id.*

[40]Jon H. Outcalt is the chairman of the NCS board of directors and Kevin B. Shaw is president, CEO, and director of NCS. *Id.* at 918-19. Outcalt and Shaw own 202,063 and 28,905 shares of Class A and 3,476,086 and 1,141,134 shares of Class B common stock, respectively, out of NCS 18,461,599 Class A and 5,255,210 Class B shares outstanding. *Id.* at 919.

market conditions in the health care industry.[41] NCS experienced difficulty in collecting accounts receivables, which led to a decline in the market value of its stock.[42] NCS's common stock, which once traded at over $20 in 1999 was worth only $0.09 to $0.50 per share by 2001.[43] The declining common stock value reflected NCS's default on approximately $350 million in debt, including $206 million in senior bank debt and $102 million of its 5.75 % Convertible Subordinated Debentures.[44]

NCS began to explore strategic alternatives to address the problems it was confronting.[45] NCS retained UBS Warburg, L.L.C. (UBS) in February 2000 to solicit potential acquirors and possible investors.[46] By October 2000, UBS's efforts resulted in one non-binding indication of interest valued at $190 million, which has substantially less than the face value of NCS's senior debt.[47] NCS terminated its relationship with UBS in December 2000 and retained Brown, Gibbons, Lang & Company (Brown Gibbons) as its exclusive financial advisor.[48]

During NCS's search for a viable suitor, its financial condition continued to deteriorate.[49] In April 2001, NCS received a formal notice of default and acceleration from the trustee for holders of the notes.[50] While NCS discussed with various investor groups a restructuring in a "pre-packaged" bankruptcy, the noteholders formed a committee to represent their financial interests (Ad Hoc Committee).[51] Full recovery for NCS's creditors was a remote prospect, and any recovery for its stockholders seemed impossible, since NCS had failed to receive any proposal that it believed provided adequate consideration for its stakeholders.[52]

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[41] *Omnicare*, 818 A.2d at 920.

[42] *Id.*

[43] *Id.*

[44] *Id.*

[45] *Omnicare*, 818 A.2d at 920.

[46] *Id.*

[47] *Id.* UBS Warburg made a good faith effort to solicit interest in NCS. UBS contacted over fifty different companies in an effort to solicit interest. The company that showed interest reduced its $190 million proposal by twenty percent after it conducted a due diligence review of NCS. *Id.*

[48] *Id.* at 921.

[49] *Omnicare*, 818 A.2d at 921.

[50] *Id.*

[51] *Id.*

[52] *Id.*

2. *Omnicare* Enters the Field

Omnicare opened discussions for conducting a possible transaction in the summer of 2001. Joel Gemunder, Omnicare's president and CEO, sent NCS a written proposal to acquire NCS in a bankruptcy sale under Section 363 of the Bankruptcy Code.[53] Omnicare's initial proposal was for $225 million conditioned upon satisfactory completion of a due diligence review.[54] NCS then asked Omnicare to execute a confidentiality agreement so that more detailed discussions could take place.[55]

Omnicare by August 2001 increased its bid to $270 million, but retained its intent to structure the deal as an asset sale in bankruptcy.[56] Omnicare's proposal was substantially lower than the face value of NCS's outstanding debt and would have provided only a small recovery for Omnicare's Noteholders and no recovery for its stockholders.[57] NCS then sent Glen Pollack of Brown Gibbons to meet Omnicare's financial advisor, Merrill Lynch, to further discuss Omnicare's interest in NCS.[58] Omnicare responded that it was not interested in any transaction other than an asset sale in bankruptcy.[59]

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[53]*Omnicare*, 818 A.2d at 921. For the federal rights and powers of a trustee and the rights of parties that have interests in property with respect to the sale of property, see 11 U.S.C. § 363 (2002).

Omnicare, Inc. is a Delaware corporation headquartered in Covington, Kentucky. *Omnicare*, 818 A.2d at 919. At the time the suit was pending, Omnicare provided clinical research for the pharmaceutical and biotechnology industries, serving about 746,000 residents in forty-five states, comprising of about twenty-eight percent of the total market. Roy Wood, *Omnicare Set to Solidify NCS Merger*, THE CINCINNATI POST, Dec. 17, 2002, *available at* http://www.cincypost.com/2002/12/17/omni121702.html (last visited Nov. 2, 2004).

[54]*Omnicare*, 818 A.2d at 921.

[55]*Id.* This particular confidentiality agreement was important because Omnicare was NCS's largest competitor. *In re* NCS Healthcare, Inc., S'holders Litig., 825 A.2d 240, 245-46 (Del. Ch. 2002). The nature of the relationship of the two companies made it important to keep some information confidential. *Id.* at 246 n2. Omnicare refused to execute the initial agreement and objected to provisions prohibiting it from soliciting NCS's customers outside the ordinary course of Omnicare's business. *Id.* at 246. In addition to Omnicare's attempt to acquire NCS though a bankruptcy sale, it was attempting to target NCS's customers by luring customers away from NCS and toward Omnicare, an effort characterized as the "NCS Blitz." *Id.* at 246 n3. Eventually, in late September 2001, Omnicare executed a modified confidentiality agreement that limited the scope of information received, forcing NCS to withhold highly sensitive, non-public competitive information. *Id.* at 246.

[56]*Omnicare*, 818 A.2d at 921.

[57]*Id.*

[58]*Id.* At this meeting, Pollack pressed Omnicare to propose a merger transaction rather than an asset sale in bankruptcy due to potential synergies in a NCS/Omnicare merger. *In re NCS Healthcare, Inc.*, 825 A.2d at 246.

[59]*Omnicare*, 818 A.2d at 921.

Between November 2001 and January 2002, Omnicare had no further contact with NCS.[60] Omnicare, rather, began secret discussions with a representative of the Ad Hoc Committee, Judy K Mencher.[61] Omnicare continued to pursue a transaction structured as a sale of assets in bankruptcy and, in February 2002, the Ad Hoc Committee notified the NCS board that Omnicare proposed an asset sale in bankruptcy for $313,750,000.[62]

3. The Emergence of Genesis as a Knight in Shining Armour

The Ad Hoc Committee, in January 2002, contacted Genesis Health Ventures, Inc.[63] (Genesis) concerning a possible transaction with NCS.[64] Genesis agreed to negotiate, executed NCS's confidentiality agreement, and began a due diligence review.[65] Genesis had recently emerged from bankruptcy because, like NCS, it suffered from dwindling government reimbursements.[66]

NCS directors, in early 2002, began to believe that it might be possible to enter into a transaction that would provide some recovery for NCS stockholders' equity, due to an improvement in NCS's operating performance at the start of the year.[67] In March 2002, NCS formed an independent committee comprised of members who were neither NCS employees nor major stockholders (Independent Committee).[68] The Independent Committee was given the authority to consider and negotiate

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[60] *Id.*

[61] *Id.*

[62] *Id.* This new proposal represented the highest proposal Omnicare would offer until July 2002 and was still less than the face value of NCS's debt and provided no recovery for NCS's stockholders. *In re NCS Healthcare, Inc.*, 825 A.2d at 246.

[63] Defendant Genesis is a Pennsylvania corporation with its principle place of business in Kennett Square, Pennsylvania. *Omnicare*, 818 A.2d at 919. Genesis is a leading provider of healthcare and support services to the eldery. *Id.* Also named as defendant in the suit was Geneva Sub, Inc., a Delaware corporation which is a wholly owned subsidiary of Genesis, formed to acquire NCS. *Id.*

[64] *Id.* at 921.

[65] *Id.*

[66] *Id.*

[67] *Omnicare*, 818 A.2d 922.

[68] *Id.* The NCS board thought the committee was necessary because it felt that fiduciary duties were owed to NCS as a whole rather than solely to NCS stockholders. *Id.* The Independent Committee, which NCS board members Sells and Osborne were selected, retained the same legal and financial counsel as the NCS board. *Id.*

possible transactions for NCS, but reserved the right to approve such a transaction with the NCS four-member board.[69]

The Independent Committee met with Glen Pollack of Brown Gibbons on May 14,2002.[70] Pollack suggested that NCS seek a "stalking horse" merger partner to obtain the highest possible value for NCS in any transaction.[71] The Independent Committee agreed with Pollack's suggestion.[72]

On May 16, 2002, Glen Pollack, Scott Berlin of Brown Gibbons, and Sells met with George Hager, CFO. of Genesis, and Michael Walker, Genesis's CEO.[73] Genesis made it clear at the meeting that they were not going to engage in negotiations with NCS as a "stalking horse" and wanted a degree of certainty that it would be able to consummate the transaction it negotiated and executed.[74] Genesis did not want to set forth a valuation that could create an environment where Omnicare could match and exceed that level to maintain its competitive monopolistic position.[75]

Genesis proposed a transaction outside the bankruptcy context in June 2002.[76] As negotiations continued, the terms of the transaction continued to improve.[77] On June 25, the terms of the Genesis proposal included full repayment of NCS's senior debt, an exchange offer or direct purchase of the NCS's notes,[78] and $20 million in value for NCS's common stock.[79] Subsequent to this proposal, Pollack asked Genesis to increase its offer to NCS stockholders and Genesis agreed to offer a total of $24 million for NCS common stock in the form of Genesis common stock.[80]

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[69] *Id.*

[70] *Id.*

[71] *Omnicare*, 818 A.2d at 922.

[72] *Id.*

[73] *Id.*

[74] *Id.*

[75] *Omnicare*, 818 A.2d 922. Genesis wanted to protect itself from Omnicare as a result of a prior bidding war that Genesis lost. *Id.* at 921. This led to bitter feelings between Genesis and Omnicare and led to Genesis's insistence to lock-up any transaction with NCS. *Id.*

[76] *Id.* at 922. The proposed transaction did not provide full recovery for the NCS Noteholders, but did provide the possibility that NCS stockholders would be able to recover something. *Id.*

[77] *Id.*

[78] The exchange offer or direct purchase provided NCS Noteholders with a combination of cash and Genesis common stock equal to the par value of the NCS notes, permitting the Noteholders recovery of the Notes less accrued interest. *Id.*

[79] *Omnicare*, 818 A.2d at 922. Genesis's proposal continued to include consents from a significant majority of the Noteholders and support agreements from the majority stockholders to protect the consummation of the deal. *Id.*

[80] *Id.* at 922-23.

At the June 26, 2002 meeting, Genesis's representatives demanded that NCS enter into an Exclusivity Agreement with Genesis before further negotiations take place.[81] On June 27, 2002, Genesis legal counsel sent a draft of the Exclusivity Agreement to NCS's legal counsel, and the Independent Committee met to consider the Exclusivity Agreement on July 3.[82] Pollack presented the terms of a possible Genesis merger, which included (1) full repayment of NCS senior debt, (2) payment of par value for the Notes (without accrued interest) in the form of a combination of cash and Genesis stock, (3) payment of $24 million in the form of Genesis common stock, and (4) Genesis's assumption of additional liabilities to trade and other unsecured creditors.[83] Additionally, Pollack told the Independent Committee that "Genesis wanted the Exclusivity Agreement to be the first step toward a completely locked up transaction that would preclude a higher bid from Omnicare."[84]

After NCS executed the Exclusivity Agreement, Genesis provided NCS with drafts of the merger agreement, noteholder support agreement and voting agreements for NSC's majority shareholders Outcalt and Shaw.[85] Genesis and NCS continued negotiating the terms of the merger over the next several weeks, ending with the Independent Committee authorizing the extension of the exclusivity period though July 31, 2002.[86]

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[81] *Id.* at 923. As George Hager, the CFO of Genesis, explained:

> [I]f they wished us to continue to try to move this process to a definitive agreement, that they would need to do it on an exclusive basis with us. We were going to, and already had incurred significant expense . . . . We wanted them to work with us on an exclusive basis for a short period of time to see if we could reach agreement.

Id. (citations omitted).

[82] *Id.*

[83] *Omnicare*, 818 A.2d at 923.

[84] *Id.* Sells testified that:

> Pollack explained that Genesis felt that they had suffered at the hands of Omnicare and others . . . they, Genesis, had tried to acquire, I suppose, an institutional pharmacy, I don't remember the name of it. Thought they had a deal and then at the last minute, Omnicare outbid them for the company in a like 11:59 kind of thing, and that they were unhappy about that. And once burned, twice shy.

Id.

[85] *Id.*

[86] *Id.* The events after the execution of the Exclusivity Agreement until the July 31 extension are as follows: the Independent Committee and the Ad Hoc Committee persuaded Genesis to further improve the terms of the merger; the exclusivity period was initially extended to July 26, 2002; Genesis proposed a short extension though July 31 to finalize the deal. *Id.*

4. The Battle for NCS: *Genesis v. Omnicare*

Omnicare, by the end of July 2002, came to believe that NCS was negotiating a transaction with Genesis or another competitor that presented a threat to Omnicare's interests.[87] The board of directors of Omnicare met on the morning of July 26, 2003 and, on management's recommendation, authorized a proposal to acquire NCS outside the sale of assets in bankruptcy.[88] Omnicare faxed to NCS a letter outlining the proposed acquisition on the afternoon of July 26, 2002, in which acceptance was expressly conditioned on negotiating a merger agreement, obtaining certain third-party consents, and completing it due diligence review.[89]

Judy Mencher, the Ad Hoc Committee representative, reviewed Omnicare's letter and concluded that "while its economic terms were attractive, the 'due diligence' condition substantially undercut its strength."[90] Mencher then telephoned Joel Gemunder, Omnicare's president and CEO, to raise the value of Omnicare's proposal. Mencher told Germunder that Omnicare's last minute proposal is unlikely to succeed unless it dropped the "due diligence outs."[91] Germunder considered Mencher's warning "very real," but decided to retain the due diligence condition in accordance with the wishes of his advisors.[92]

In addition to the letter, NCS representatives received voicemail messages on July 26, asking NCS to discuss the letter.[93] The Exclusivity Agreement with Genesis prevented NCS from returning the calls.[94] Despite the Exclusivity Agreement, the Independent Committee met to consider a response to Omnicare.[95] The Independent Committee concluded that

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[87] *Omnicare*, 818 A.2d at 924. Omnicare also came to believe that the transaction probably included a payment for NCS's common stock due to the increased trading price of NCS's common stock. *Id.*

[88] *Id.*

[89] *Id.* Omnicare proposed to retire NCS's senior and subordinated debt at par plus accrued interest, and pay NCS stockholders $3 cash for their shares. *Id.*

[90] *Id.*

[91] *Omnicare*, 818 A.2d at 924.

[92] *Id.*

[93] *Id.*

[94] *Id.* The Exclusivity Agreement precluded NCS from engaging or participating in any discussions or negotiations with respect to a competing transaction or a proposal for one; and Omnicare's letter met the definition of a "competing transaction." *Id.*

[95] *Omnicare*, 818 A.2d at 924.

Omnicare's letter presented an unacceptable risk of harm[96] and instructed Pollack to use the letter to negotiate for improved terms with Genesis.[97]

5. Genesis's Merger Agreement and Voting Agreements

Genesis responded to Omnicare's letter and NCS's request to improve its offer the next day with substantially improved terms.[98] Genesis, in exchange for improved terms, stipulated that NCS had to approve the transaction by midnight on July 28, 2002 or Genesis would withdraw its offer and terminate discussions.[99]

The Independent Committee and the NCS board both scheduled meetings for July 28.[100] The Independent Committee concluded that Genesis's threat was sincere and voted unanimously to recommend the transaction to the full board.[101] The NCS board, after receiving reports and advice from its legal and financial advisors, concluded that "balancing the potential loss of the Genesis deal against the uncertainty of Omnicare's letter, results in the conclusion that the only reasonable alternative for the Board of Directors is to approve the Genesis transaction."[102] The board first voted to authorize the voting agreements for purposes of Section 203 of the DGCL.[103] The board was advised by its legal counsel that the terms of the merger and voter agreements would prevent NCS from engaging in

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[96]The Independent Committee believed that the risk of losing the Genesis deal is too substantial if they began discussions with Omnicare, given Omnicare's past bankruptcy proposals and unwillingness to consider a merger, and its decision to negotiate exclusively with the Ad Hoc Committee. *Id.*

[97]*Id.*

[98]*Id.* Genesis improved proposal included: (1) retirement of the Notes in accordance with the terms of the indenture, payment of all accrued interest plus a small redemption premium, thus eliminating the need for Noteholder consent to the merger; (2) an eighty percent increase in the exchange ratio to one-tenth of Genesis common share for each NCS common share; and (3) lowering the proposed termination fee in the merger agreement from $10 million to $8 million. *Id.* at 924-25.

[99]*Omnicare*, 818 A.2d at 925.

[100]*Id.*

[101]*Id.* The court of chancery determined, and the supreme court affirmed, that from the minutes of this meeting that the Committee was fully informed of all material facts relating to the proposed transaction. *Id.*

[102]*Id.*

[103]*Omnicare*, 818 A.2d at 925 (internal quotations omitted). Section 203 of the DGCL describes the process and limitations for a board of directors to approve a transaction that involves interested stockholders. *See* DEL. CODE ANN. tit. 8, § 203 (2001).

any alternative or superior transaction in the future.[104] The board then listened to a summary of the merger terms[105] and agreed that the terms were advisable, fair, and in the best interests of NCS stockholders. They executed a definitive merger agreement and the stockholder voting agreements later that day.[106]

> The NCS/Genesis merger agreement provided, among other things, the following:
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> - NCS stockholders would receive 1 share of Genesis common stock in exchange for every 10 shares of NCS common stock held;
> - NCS stockholders could exercise appraisal rights under section 262;
> - NCS would redeem NCS's Notes in accordance with their terms;
> - NCS would submit the merger agreement to NCS stockholders regardless of whether the NCS board continued to recommend the merger;
> - NCS would not enter into discussions with third parties concerning an alternative acquisition of NCS, or provide non-public information to such parties, unless (1) the third party provided an unsolicited, bona fide written proposal documenting the terms of the acquisition; (2) the NCS board believed in good faith that the proposal was or was likely to result in an acquisition on terms superior to those contemplated by the NCS/Genesis merger agreement; and (3) before providing non-public information to that third party, the third party would execute a confidentiality

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[104] *Omnicare*, 818 A.2d at 925. Legal counsel for the NCS board advised that under the terms of the merger agreement and because NCS shareholders representing in excess of 50% of the outstanding voting power would be *required* by Genesis to enter into stockholder voting agreements contemporaneously with the signing of the merger agreement, and would agree to vote their shares in favor of the merger agreement, shareholder approval of the merger would be assured even if the NCS Board were to withdraw or change its recommendation.

Id.

[105] The court of chancery held, and the supreme court affirmed, that it was not a per se breach of fiduciary duty that the NCS board never read the NCS/Genesis merger agreement word for word. *Id.*

[106] *Id.*

agreement at least as restrictive as the one in place between NCS and Genesis; and

- If the merger agreement were to be terminated, under certain circumstances NCS would be required to pay Genesis a $6 million termination fee and/or Genesis's documented expenses, up to $5 million.[107]

The voting agreements entered into between Outcalt/Shaw and Genesis[108]

provided, among other things, that:

- Outcalt and Shaw were acting in their capacity as NCS stockholders in executing the agreements, not in their capacity as NCS directors or officers;
- Neither Outcalt nor Shaw would transfer their shares prior to the stockholder vote on the merger agreement;
- Outcalt and Shaw agreed to vote all of their shares in favor of the merger agreement; and

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[107]*Omnicare,* 818 A.2d at 925-26.

Section 262 provides, among other things, that shareholders whom neither voted in favor of a transaction nor consented to the transaction are entitled to an appraisal of the fair value of the shares of stock owned. DEL. CODE ANN. tit. 8, § 262 (2001).

This "force the vote" provision is permitted under section 251(c) of the DGCL, which states in pertinent part:

> The agreement required by subsection (b) of this section shall be submitted to the stockholders of each constituent corporation at an annual or special meeting for the purpose of acting on the agreement. The terms of the agreement may require that the agreement be submitted to the stockholders whether or not the board of directors determines at any time subsequent to declaring its advisability that the agreement is no longer advisable and recommends that the stockholders reject it.

DEL. CODE ANN. tit. 8, § 251(c) (2001).

[108]NCS was also required to be a party to the voting agreement. *Omnicare*, 818 A.2d at 926. Voting agreements are authorized by section 218 of the DGCL, which provides in pertinent part:

> An agreement between 2 or more stockholders, if in writing and signed by the parties thereto, may provide that in exercising any voting rights, the shares held by them shall be voted as provided by the agreement, or as the parties may agree, or as determined in accordance with a procedure agreed upon by them.

DEL. CODE ANN. tit. 8, § 218(c) (2001).

- Outcalt and Shaw granted to Genesis an irrevocable proxy to vote their shares in favor of the merger agreement.
- The voting agreement was specifically enforceable by Genesis.[109]

6. Omnicare's Response: Its Superior Proposal

Hours after the NCS/Genesis merger was executed, Omnicare faxed a letter to NCS restating its conditional proposal and attached a draft merger agreement.[110] On the morning of July 29, 2002, Omnicare issued a press release publicly disclosing the proposal.[111] Omnicare filed a lawsuit on August 1, 2002, attempting to enjoin the NCS/Genesis merger, and announced that it intended to launch a tender offer for NCS's shares at a price of $3.50 per share.[112] Omnicare sent NCS a letter on August 8 expressing its desire to discuss the terms of the offer.[113] The tender offer continued to be conditioned on satisfactory completion of a due diligence investigation of NCS.[114]

The Independent Committee and the NCS board met separately, with legal counsel and financial advisors present at both meetings, to consider the Omnicare tender offer.[115] The board was unable to determine that Omnicare's proposal was likely to lead to a "Superior Proposal" as defined in the NCS/Genesis merger agreement.[116] The board did not have to make this determination because, on September 10, 2002, NCS requested and

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[109] *Omnicare*, 818 A.2d at 926. The Delaware Supreme Court noted that the merger agreement provided that if either Outcalt or Shaw breached the terms of the voting agreements, Genesis would be entitled to terminate the merger agreement and receive a $6 million termination fee from NCS. *Id.* But such a breach is impossible since the voting agreements were specifically enforced by Genesis.

[110] *Id.*

[111] *Id.*

[112] *Id.*

[113] *Omnicare*, 818 A.2d at 926.

[114] *Id.*

[115] *Id.*

[116] *Id.* On August 20, 2002, NCS sent a press release to its stockholders recommending them to reject Omnicare's offer and not tender their shares in the offer because: (1) the offer was highly conditional; many of the conditions cannot be satisfied in light of its transaction with Genesis; (2) the offer was illusory; the conditions vague and reserved in Omnicare the right to determine whether the conditions were satisfied; (3) the Genesis merger is more certain; (4) the Omnicare offer, in contrast to the Genesis merger, does not contain a binding commitment to provide full recovery to debt holders; and (5) the offer does not provide NCS stockholders the opportunity to participate in any long-term appreciation in the value of Omnicare. SEC Press Release, NCS Healthcare, Inc., *supra* note 39.

received a waiver from Genesis allowing NCS to enter into discussions with Omnicare.[117]

On October 6, 2002, Omnicare irrevocably committed itself to a transaction with NCS to acquire all the outstanding NCS Class A and Class B shares at a price of $3.50 per share in cash.[118] As a result of Omnicare's irrevocable offer, the NCS board withdrew its recommendation that the stockholders vote in favor of the NCS/Genesis merger agreement on October 21.[119]

7. Rejection of the NCS/Genesis Merger Is Impossible

Although the NCS/Genesis merger agreement contained a provision which permitted NCS to enter into discussions with any person that introduced an unsolicited bona fide proposal which the board deemed likely to constitute a superior proposal, that provision had absolutely no effect on the Genesis merger agreement.[120] Even if the NCS board changes, withdraws, or modifies its recommendation to approve a superior proposal, it must still submit the merger to a stockholder vote, which was locked into approving the Genesis merger pursuant to Outcalt and Shaw's voting agreements.[121]

B. *The Delaware Court of Chancery Decision*

On August 1, 2002, Omnicare filed a lawsuit to enjoin the NCS/Genesis merger.[122] Omnicare amended the complaint on

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[117] *Omnicare*, 818 A.2d at 926.

[118] *Id.* As a result of the irrevocable offer, Omnicare lifted the due diligence commitment.

[119] *Id.* NCS's financial advisor also withdrew its fairness opinion of the NCS/Genesis merger agreement. *Id.* at 927.

[120] *Id.* at 127.

[121] *Omnicare*, 818 A.2d at 127. In another press release on October 22, 2002, the NCS independent committee and the NCS board of directors withdrew their recommendations of the Genesis merger agreement and recommended that the NCS stockholders vote against the approval and adoption of the Genesis merger. They recognized, however, that the existing contractual obligations to Genesis currently prevent NCS from accepting the Omnicare proposal because the board was required to submit the Genesis merger to the shareholders and the voting agreements ensured NCS stockholder approval of the Genesis merger. Press Release, NCS Healthcare, Inc., NCS Healthcare Withdraws Genesis Merger Recommendation (Oct. 22, 2002), *available at* http://www.ncshealth.com/WDGenesisRec.htm (last visited Nov. 2, 2004).

[122] *Omnicare,* 818 A.2d at 926. The defendants in Omnicare and the NCS minority stockholder's claims are NCS Healthcare, Inc.; Genesis Health Ventures, Inc.; Geneva Sub, Inc., a wholly owned subsidiary of Genesis; and the four member NCS board, Jon H. Outcalt, Kevin B. Shaw, Boake A. Sells, and Richard L. Osborne. Omnicare, Inc. v. NCS Healthcare, Inc., 818

September 23, 2002, alleging five counts[123] consisting of breaches of fiduciary duties and challenging the Genesis voting agreements.[124] NCS responded by filing a motion to dismiss Omnicare's claims on October 3, 2002, alleging that Omnicare lacked standing to file a grievance.[125] The Delaware Court of Chancery dismissed Omnicare's fiduciary duty claims[126] for lack of standing and denied NCS's motion to dismiss regarding Omnicare's voter agreement claim.[127]

A.2d 914 (Del. 2003); Omnicare, Inc. v. NCS Healthcare, Inc., 825 A.2d 264 (Del. Ch. 2002); *In re* NCS Healthcare, Inc., S'holders Litig., 825 A.2d 240 (Del. Ch. 2002); Omnicare, Inc. v. NCS Healthcare, Inc., 809 A.2d 1163 (Del. Ch. 2002).

[123]Specifically,

> Omnicare allege[d] that: (1) the voting agreements between Genesis, Outcalt and Shaw violated NCS's charter and thus automatically converted Outcalt and Shaw's Class B shares into Class A shares (Count I); (2) the board violated [Section 141(a) of the DGCL] by entering into an exclusivity agreement with Genesis on July 3, 2002, and approving the Voting Agreements and the Merger Agreement on July 28, 2002 in violation of their fiduciary duties (Count II); (3) the Board breached their fiduciary duties by approving the Genesis merger and by refusing to consider Omnicare's July 26, 2002 indication of interest (Count III); (4) Genesis aided and abetted these alleged breaches of fiduciary duties (Count IV); and (5) the termination fee provided for in the Merger Agreement is the result of a fiduciary breach and, thus, is invalid and unenforceable (Count V).

Omnicare, 809 A.2d at 1168.

[124]*Id.*

[125]*Id.*

[126]The procedures that led to the dismissal of Omnicare's fiduciary duty claims (counts II-V) are explained hereafter. After Genesis and NCS announced the merger in a press release, Omnicare subsequently purchased 1,000 shares of NCS Class A common stock. *Id.* at 1167. Omnicare's argument is that they have standing as an interested party due to their stock purchase after the merger announcement or, in the alternative, they have standing as a competing bidder. *Id.* at 1169. As to the stock purchase argument, Vice Chancellor Lamb held that "our courts have held that plaintiffs who purchase stock after disclosures have been made cannot pursue claims for breaches of the duty of disclosure." *Id.* at 1170 (citations omitted). The Chancellor noted that granting Omnicare standing on this ground would "violate a longstanding Delaware public policy against the 'evil' of purchasing stock in order 'to attack a transaction which occurred prior to the purchase of the stock.'" *Id.* at 1169 (quoting Rosenthal v. Burry Biscuit Corp., 60 A.2d 106, 111 (Del. Ch. 1948)).

As to the bidding claim, the Vice Chancellor noted that there is little or no support in Delaware law that allows a bidding company standing when the bidding company does not own stock at the time of the breach. *Id.* at 1171. Additionally, Vice Chancellor Lamb recognized that no Delaware court has recognized the standing of a non-stockholder bidder for a target company. *Id.* at 1172 (citations omitted). Vice Chancellor Lamb concluded with a policy argument, stating that a company's fiduciary duty is owed only to holders of stock, not bidding companies, even if they only own one share. *Id.* Following this rationale, Omnicare's fiduciary duty claims (counts II through V) were dismissed for lack of standing. *Id.* at 1173.

[127]*Omnicare*, 809 A.2d at 1174. Omnicare's claim alleges that, pursuant to the terms of NCS's certificate of incorporation, the voting agreements between the majority shareholders, Outcalt and Shaw, and Genesis resulted in the automatic conversion of the shareholders Class B

The Delaware Court of Chancery presided over Omnicare's voter agreement claim on October 29, 2002.[128] The court held that the irrevocable proxies granted by Outcalt and Shaw to vote their shares in favor of the merger did not result in an automatic conversion of their Class B shares to Class A shares.[129]

After Omnicare successfully attempted to prevent the merger, NCS minority shareholders filed an application for a preliminary injunction to prevent the merger, based on alleged fiduciary duty breaches.[130] Vice Chancellor Lamb denied the application for the preliminary injunction and held that the NCS board did not breach any fiduciary duties[131] and the NCS/Genesis deal protection devices were reasonable.[132]

Included within the stockholder-plaintiff's claim that the NCS board of directors violated their duty of care[133] during the negotiation and approval process of the NCS/Genesis merger was the plaintiff's argument that the NCS boards breached their duty to seek a transaction that would yield the highest value reasonably available to the stockholders, thus invoking enhanced *Revlon* duties.[134] The plaintiffs set forth two viewpoints to support their argument. First, they claimed that the Genesis merger would decrease the voting power of the majority shareholders, which constituted a change in control.[135] Second, the shareholders-plaintiff claimed that the process that the NCS board and the Independent Committee agreed to pursue put NCS "up for sale" in a way that invoked *Revlon* duties.[136]

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common shares to Class A common shares. *Id.* at 1173. Because of the number of votes attached to each Class, *see supra* text accompanying note 40, a ruling in Omnicare's favor would diminish Outcalt and Shaw's voting power from sixty-five percent to approximately twenty percent, thereby not ensuring stockholder approval of the NCS/Genesis merger. *Id.* The court of chancery held that Omnicare had standing, as owner of 1,000 shares of common stock, to challenge an issue that it would no doubt have standing to challenge, if Omnicare had to wait until after the vote to approve the merger, at a future date. *Id.*

[128]Omnicare, Inc. v. NCS Healthcare, Inc., 825 A.2d 264 (Del. Ch. 2002).

[129]*Id.* at 275.

[130]*In re* NCS Healthcare, Inc., S'holders Litig., 825 A.2d 240 (Del. Ch. 2002).

[131]*Id.* at 260-61. The court noted that the overall quality of the testimony given by the NCS directors is among the strongest it has ever seen and "makes manifest the care and attention given to this project by every member of the board." *Id.* at 260 n.46.

[132]*Id.* at 261.

[133]The plaintiffs did not argue that the board acted disloyally or in bad faith during the negotiation or approval process of the Genesis transaction. *Id.* at 254. Furthermore, the court held that the record supports an inference that the board's interests were aligned with all the NCS stockholders, mooting plaintiff's minor conflict of interest argument. *Id.* at 254 n.19.

[134]*In re* NCS Healthcare, Inc., S'holders Litig., 825 A.2d at 254.

[135]*Id.* at 254-55.

[136]*Id.* at 255.

In resolving the plaintiff's claims, the court analyzed the circumstances that trigger a *Revlon* enhanced scrutiny review and whether they apply to the facts surrounding the board's decision to approve the Genesis merger. The court of chancery followed *Paramount Communications, Inc. v. QVC Network, Inc.*,[137] which recognized that one circumstance that triggers *Revlon* is a sale of a company in a transaction that constitutes a change in control in the targeted company.[138] The court noted that a stock-for-stock merger does not result in a change of control, when the surviving company lacks a controlling person or group.[139] Analyzing the NCS/Genesis merger, the court found that there was no change of control as a result of the merger; Outcalt and Shaw's positions as majority shareholders merely shifted to stockholders in a company without a controlling stockholder or group.[140] Determining that *Revlon* did not apply in this case under a change of control, the court of chancery moved to plaintiff's next claim that NCS was put "up for sale."

In support of their argument that the NCS board put NCS "up for sale," the plaintiffs cited to *Arnold v. Society for Savings Bancorp.*[141] The *Arnold* court noted that the enhanced scrutiny of *Revlon* required the company to not only have been "seeking to sell itself," but also have "initiated an active bidding process."[142] The stockholder-plaintiffs argued that the Independent Committee and the NCS board's agreement to pursue a "stalking horse auction process" initiated an active bidding process, which put NCS "up for sale" and imposed *Revlon* duties.[143]

The court of chancery distinguished *Arnold*, in which they held that *Revlon* duties are not implicated solely by seeking to conduct an auction that, if successful, would result in a change of control.[144] In *Arnold*, after a year long process of exploring alternatives to enhance stockholder value, including a plan to sell the company in pieces for cash, the board of directors finally began negotiations for a non-change of control stock-for-stock merger with Bank of Boston.[145] Determining whether *Revlon* applied, the Delaware Supreme Court distinguished between the company's

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[137]637 A.2d 34 (Del. 1994).

[138]*In re NCS Healthcare*, 825 A.2d at 254, *Paramount*, 637 A.2d at 42-43.

[139]*In re NCS Healthcare*, 825 A.2d at 254; *see* Arnold v. Society for Sav. Bancop., Inc., 650 A.2d 1270, 1290 (Del. 1994) (noting that there is no change of control when control remains "in a large, fluid, changeable, and changing market").

[140]*In re NCS Healthcare*, 825 A.2d at 255.

[141]650 A.2d 1270 (Del. 1994).

[142]*Id.* at 1290; *In re NCS Healthcare*, 825 A.2d at 256.

[143]*In re NCS Healthcare*, 825 A.2d at 255.

[144]*Id.*

[145]*Arnold*, 650 A.2d at 1274-75.

activities pre- and post-May 1992. The court held that *Revlon* did not apply since the post-May 1992 negotiations ultimately led to a non-change of control transaction.[146]

Following this rationale, the court of chancery found that *Revlon* did not apply because the facts show that the NCS board never started an active bidding process.[147] Even if the board had initiated bidding, the process was abandoned when the board initiated negotiations with Genesis for a stock-for-stock merger, which ultimately did not involve a "sale or change of control" within the meaning of *Revlon*.[148] The court found that the Independent Committee was largely devoted to private discussions with Genesis and "it is the very *lack* of an active auction process that gives rise to the complaint."[149] Furthermore, the committee abandoned any "stalking horse" idea when it agreed to negotiate exclusively with Genesis for a non-change of control stock-for-stock merger.[150] The court of chancery concluded that *Revlon* did not apply and applied the business judgment rule to the board's decision to approve the NCS/Genesis merger.

Before turning to the plaintiff's arguments on the breach of fiduciary duty claim, the court of chancery established which persons the NCS board owed fiduciary duties. The court recognized that the board, in fulfilling its responsibilities under section 141(a) of title 8 of Delaware General Corporate Law,[151] not only owed fiduciary duties to NCS and its stockholders, but also the company's creditors.[152] Thus, "when choosing a course of action to pursue, the directors . . . had a fiduciary duty to take into account the interests of all of the effected corporate constituencies."[153] The court of chancery noted that the directors, in weighing whether to meet the Genesis deadline or pursue Omnicare's conditional proposal, were obligated to give due consideration that any effort to achieve better terms for the

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[146] *Id.* at 1289-90.

[147] *In re NCS Healthcare*, 825 A.2d at 256.

[148] *Id.*

[149] *Id.* (emphasis added).

[150] *Id.*

[151] *See supra* note 11.

[152] *In re NCS Healthcare*, 825 A.2d at 256. The court of chancery recognized the duty to NCS's creditors because NCS was in the "zone of insolvency," that is, it was insolvent throughout the events that led to these proceedings being in default on and unable to pay approximately $350 million in debt. *Id.* at 256-57. *See* Geyer v. Ingersoll Publ'n Co., 621 A.2d 784, 789 (Del. Ch. 1992) ("The existence of fiduciary duties at the moment of insolvency may cause directors to choose a course of action that best serves the entire corporate enterprise rather than any single group . . . .").

[153] *In re NCS Healthcare*, 825 A.2d at 257.

stockholders might result in the loss of a highly desirable deal for its creditors.[154]

The plaintiffs argued that when the Independent Committee met to consider its options, the board breached its fiduciary duties for not including Omnicare in negotiations over a possible transaction as early as May 14, 2002.[155] Deferring to the board under the business judgment rule, the court of chancery engaged in a pre- and post-May 14 factual analysis and concluded that the board did not breach their duty by failing to contact Omnicare over a possible transaction. In performing its pre-May 14 analysis, the court looked at the history of the relationship between Omnicare and NCS, in which NCS made a significant effort to solicit Omnicare's interest in a suitable transaction for over one year.[156] These attempts failed due to Omnicare's interest in pursuing only an asset sale in bankruptcy.[157] This type of transaction would run contrary to the NCS directors' desire to provide some recovery to NCS stockholders.[158] The court of chancery found that not only did the board not beach their duty of care before May 2001, but the record fully supported a conclusion that had NCS continued to negotiate with Omnicare, it would have continued to press for a bankruptcy transaction.[159]

In reviewing the post-May discussions between NCS and Genesis, the court of chancery found that the NCS board made a rational and reasonable decision to pursue a transaction with Genesis.[160] The Genesis proposal was outside the bankruptcy context and provided recovery for

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[154] *Id.*

[155] *Id.*

[156] *Id.* at 258.

[157] *In re NCS Healthcare*, 825 A.2d at 258. The court of chancery noted that all three offers that Omnicare made before July 26, 2002 involved a section 363 asset sale in bankruptcy. *Id.* Furthermore, NCS's financial advisor, Glen Pollack, met with Omnicare in October 2001 and requested a merger or another transaction outside the context of bankruptcy; Omnicare refused and stated it would only consider a deal structured as a bankruptcy sale. *Id.*

[158] *In re NCS Healthcare*, 825 A.2d at 258. Omnicare's transaction structured in a asset sale in bankruptcy would have provided only partial recovery for NCS's Noteholders, no recovery for NCS stockholders, and NCS's other creditors "being left to fight over the remains of the corporation." *Id.* The NCS board found this unacceptable because they were striving for, at a minimum, full recovery for NCS's Noteholders, partial recovery for the other creditors, and some recovery for NCS's stockholders. *Id.*

[159] *Id.* The court of chancery provided an excerpt from the deposition of Cheryl Hodges, a director at Omnicare, stating that Omnicare made its July 26 merger proposal only because it learned that a competitor was close to making a deal with NCS and that it included a payment for NCS stock. *Id.* at 258 n.39. Additionally, when Omnicare's bankruptcy proposals failed with the NCS board, Omnicare unsuccessfully engaged in secret negotiations with the ad hoc committee for a transaction in bankruptcy. *Id.* at 258.

[160] *Id.* at 259.

NCS shareholders.[161] Moreover, Genesis's proposed transaction was superior to any proposal that Omnicare had made, and there was little reason for the directors to believe that Omnicare would propose any transaction outside the bankruptcy context.[162] The court found that the NCS board did not violate their duty of care at any time preceding the approval of the Genesis merger.

The plaintiff's second argument was that the NCS board breached its fiduciary duty of care by failing to contact Omnicare after its July 26 conditional proposal letter arrived.[163] The court of chancery concluded that the NCS directors acted with adequate knowledge, made a rational judgment as to all the risks and rewards of agreeing to the Genesis merger, and did not have a duty to contact Omnicare.[164] Additionally, the court stated that the directors' actions and decisions would have been appropriate even under the enhanced scrutiny of *Revlon*.[165]

In its decision, the court of chancery discussed the directors' risk of losing the Genesis merger. "Genesis made clear that its new offer was a 'take it or leave it' proposition."[166] The court of chancery was convinced that Genesis would terminate its offer if NCS violated the Exclusivity Agreement or permitted the deadline to pass.[167] Moreover, the court noted the uncertainty of Omnicare's proposal letter.[168] Since the proposal letter was subject to various conditions,[169] further negotiations with Omnicare would create a "real risk."[170] Past dealings with Omnicare led NCS to believe that the risks were too great to pursue the proposal letter.[171] After

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[161] *Id.* at 258. By July 3, when the Exclusivity Agreement was signed, the proposal included full recovery for NCS's creditors and $24 million to NCS's stockholders. *Id.*

[162] *In re NCS Healthcare*, 825 A.2d at 258-59.

[163] *Id.* at 257-58.

[164] *Id.* at 259.

[165] *Id.* The court of chancery reasoned that at the time when the merger agreement was signed, the Genesis merger proposal was superior to Omnicare's proposal, thus conforming with the directors' fiduciary duty to seek the highest and best transaction available. *Id.* at 261.

[166] *In re NCS Healthcare*, 825 A.2d at 260.

[167] *Id.*

[168] *Id.*

[169] The most problematic was the "due diligence out" clause that permitted Omnicare to back out of the transaction upon an unsatisfactory review. *Id.*

[170] *In re NCS Healthcare*, 825 A.2d at 259-60. Independent Committee and NCS board member Osborne testified that "he would not have considered it wise to risk losing a definitive deal with Genesis for the sake of pursuing Omnicare's 'highly conditional expression of interest." *Id.* at 260.

[171] *Id.* at 260. The court of chancery relied on, among other things, the minutes of the NCS board meeting on July 28, 2002:

> Mr. Sells . . . emphasized that reliance on Omnicare's July 26 letter would not be reasonable in light of Omnicare's historic conduct in negotiations

concluding that the NCS board did not breach their fiduciary duties of care in negotiating and approving the Genesis merger, the court then evaluated the "Deal Protection" devices in the merger agreement.

The plaintiffs argued that the voting agreements coupled with the requirement that the merger agreement be presented to the stockholders constituted "defensive reactions" subject to *Unocal* analysis,[172] and that these defensive measures were coercive, preclusive, and unreasonable.[173] The court of chancery agreed with the plaintiffs to the extent that *Unocal* is the appropriate standard, but concluded that the plaintiffs did not show that the provisions were improperly preclusive or coercive of stockholder action.[174]

The plaintiffs argued that the "force the vote" provision, authorized by section 251(c) of the DGCL,[175] combined with the voting agreements guaranteed that the Genesis merger would be accomplished.[176] They contended that these provisions were unreasonable because they were not

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> with [NCS]. After further discussion, the Board concluded that balancing the potential loss of the Genesis deal against the uncertainty of Omnicare's letter, results in the conclusion that the only reasonable alternative for the Board of Directors is to approve the Genesis transaction.

Id. at 260 n.48. Furthermore, the court included a statement from Judy Mencher, a representative on the Ad Hoc Committee:

> Omnicare already had shown themselves as being unable to complete a transaction that people had agreed to; hence, I thought there was a huge amount of risk going back to Omnicare, because I was afraid it would chase Genesis away, and a bird in the hand is always worth more than two in the bush.

Id. at 260.

[172] *Id.* at 261. The plaintiffs also argue that the $6 million termination fee and the no-talk provisions subject this transaction to a *Unocal* analysis. *Id.* at 262 n.58. The court of chancery found that these provisions were not the devises that "locked-up" the Genesis merger but concluded that the provisions were reasonable under the *Unocal* test in a footnote:

> [T]he termination fee represents 2% of the total transaction value, which is by no means coercive or preclusive . . . . As far as the limited "no-talk" provision . . . . This court has questioned the validity of limited no-talk provisions only where a board of directors has not informed itself or completely foreclosed the opportunity to negotiate with a third party . . . . Here, as previously explained, the NCS board was well-informed before agreeing to this no-talk provision. Further, NCS did not foreclose itself from negotiating with Omnicare.

Id.

[173] *Id.* at 261.

[174] *In re NCS Healthcare*, 825 A.2d at 261.

[175] *See supra* note 108.

[176] *In re NCS Healthcare*, 825 A.2d at 262.

adopted in response to any legitimate threat to corporate control and they prevented the stockholders' from accepting the Omnicare offer.[177]

The court of chancery found that the provisions surrounding the NCS/Genesis merger transaction did not amount to an unreasonable "lock-up" of the Genesis merger.[178] Furthermore, Outcalt and Shaw expressed a willingness to enter into the voter agreements only as a means of completing the Genesis merger.[179] The court found no evidence to suggest that the board authorized the provisions to preclude a vote on what they knew to be a superior transaction, and concluded that the board adopted the only proposal reasonably available at the time to meet the Genesis deadline.[180]

C. *The Delaware Supreme Court Decision*

1. The Majority Decision

Before evaluating the defensive measures provided in the merger agreement, the Delaware Supreme Court majority first decided whether the court of chancery applied the appropriate standard of review. The majority did not review the court of chancery's decision to apply the business judgment rule to the NCS board's decision to merge with Genesis, assuming that the business judgment rule applied and the board exercised due care in their decision.[181] Since the majority concluded that the only dispositive issues in the appeal were the defensive devices that protected the agreement, the majority reviewed the court of chancery's decision to apply the *Unocal* enhanced scrutiny standard to those deal protection devices.[182]

Before applying the *Unocal* standard to the Genesis merger, the majority discussed the reasons why deal protection devices require an enhanced scrutiny standard. First, since Delaware corporate law expressly

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[177] *Id.*

[178] *Id.* at 262-63.

[179] *Id.* at 263.

[180] *In re NCS Healthcare*, 825 A.2d at 263. The court also dismissed the plaintiff's claim that Genesis aided and abetted a breach of fiduciary duty under the rationale that plaintiffs cannot establish third-party liability when they have not established that they have a reasonable probability of success on the merits that any breaches of fiduciary duties occurred. *Id.*

[181] *Onmicare*, 818 A.2d at 929. The majority assumed that the board exercised due care when it abandoned the Independent Committee's recommendation to pursue a stalking horse strategy, executed the Exclusivity Agreement with Genesis, acceded to Genesis's twenty-four hour ultimatum for making a final merger decision, and executed the merger agreement that was summarized but never completely read by the NCS board. *Id.*

[182] *Id.* at 930.

provides for a balance of power between the board and stockholders,[183] the board of director's decision to adopt deal protection devices may implicate the stockholders' right to oppose the board's initial recommendation.[184] Second, inherent conflicts of interest arise when the board adopts deal protection devices that prevent stockholders from exercising their right to vote.[185] Finally, the inherent conflicts between the board's interest to protect a merger and stockholders' right to make the final decision[186] require a court to determine whether the defensive devices comply with statutory limitations and the board's fiduciary duties. [187] The majority held that any deal protection devices adopted by a board must withstand enhanced judicial scrutiny under *Unocal*.[188]

To identify the features of the enhanced judicial scrutiny test for defensive devices, the majority relied on its past decisions. *Paramount Communications, Inc. v. QVC Network, Inc.*[189] set forth the key elements of the test.[190] The court must first determine whether the board's decision to implement a defensive device was adequate in the decision-making process, including the information on which the board based their decision.[191] The court must then evaluate the reasonableness of the board's action in light of the existing circumstances.[192]

The majority then looked to *Unitrin, Inc. v. American General Corp.*[193] to establish factors for determining whether a board's decision falls within the range of reasonableness. First, the court must determine whether

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[183]Section 251(c) of the DGCL authorizes the board to submit the agreement to the stockholders for approval. *See supra* text accompanying note 108.

[184]*Omnicare,* 818 A.2d at 930.

[185]*Id.*

[186]The majority recognized the inherent conflicts as the board's interest in protecting the merger transaction it had approved, the stockholders' statutory right to make the final decision on whether to approve the merger, and the board's responsibility to exercise their fiduciary duties at all times. *Id.*

[187]*Id.* at 930-31.

[188]*Id.* at 931; *see also Paramount,* 571 A.2d at 1151 (holding that the adoption of structural safety devices, lock-up, no-shop, and "dry-up" provisions, "alone does not trigger *Revlon*. . . . [r]ather . . . such devices are properly subject to a *Unocal* analysis").

[189]637 A.2d 34 (Del. 1994). Unlike the business judgment rule which gives deference to the board's decision, the *Unocal* enhanced scrutiny test places the burden of proof on the board to prove that they were adequately informed and acted reasonably. *Omnicare,* 818 A.2d at 931.

[190]*Omnicare*, 818 A.2d at 931.

[191]*Id.*; *QVC Network, Inc.*, 637 A.2d at 45.

[192]*Omnicare*, 818 A.2d at 931; *QVC Network, Inc.*, 637 A.2d at 45. In *QCV,* the court concluded that a court should not decide whether the board of directors made a perfect decision, but will determine if the decision was within a range of reasonableness. *Id.* (citations omitted).

[193]651 A.2d 1361 (Del. 1995).

the board's collective defensive responses were coercive or preclusive.[194] Second, if the court finds that the defensive devices were not coercive or preclusive, the court shifts its focus to the "range of reasonableness" to determine whether the defensive measures were proportionate to the threat perceived.[195] If a court determines that both prongs of the test were satisfied, then the business judgment rule applies and the court will not substitute its judgment for that of the board.[196]

After establishing the *Unocal* test, the majority determined which agreements adopted by the NCS directors constituted deal protection devices, thereby subjecting them to enhanced scrutiny. The majority noted that deal protection devices are analogous to defensive devices; the terms describe any measure or combination of measures intended to protect the consummation of a transaction. Additionally, the court stated that deal protection devices may not only be attached to the agreement itself, but may also be found outside the four corners of the merger agreement.[197] The majority found that the Section 251(c) agreement coupled with the voter agreements and the omission of a fiduciary out clause fell within the definition of deal protection devices.[198]

The defendants, citing *Williams v. Geier*[199] and *Stroud v. Grace*,[200] argued that the stockholder voting agreements were not subject to the

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[194]*Omnicare*, 818 A.2d at 931; *Unitrin*, 651 A.2d at 1388. The majority noted that since *Unocal*, "this [c]ourt has consistently recognized that defensive measures which are either preclusive or coercive are included within the common law definition of [D]raconian." *Unitrin*, 651 A.2d at 1387. A defensive measure is "coercive" if it is aimed at forcing a management-sponsored alternative upon stockholders in response to a hostile offer. *Omnicare*, 818 A.2d at 935 (citing *Unitrin*, 651 A.2d 1387-88). Additionally, a response is "preclusive" if it deprives stockholders of the right to receive all tender offers or precludes a bidder from seeking control by fundamentally restricting proxy contests or otherwise. *Id.* (citing *Paramount*, 571 A.2d at 1154).

[195]*Omnicare*, 818 A.2d at 932; *Unitrin*, 651 A.2d at 1387.

[196]*Omnicare*, 818 A.2d at 931; *Unitrin*, 651 A.2d at 1388.

[197]*Omnicare*, 818 A.2d at 934.

[198]*Id.*

[199]671 A.2d 1368 (Del. 1996). In *Williams*, the board of directors of Cincinnati Malicron, Inc. approved and submitted to the shareholders a proposal to amend its certificate of incorporation to increase the number of votes per share of stock. *Id.* at 1372. After the shareholders approved the amendment, the court ruled that a board *recommending* shareholders to vote in favor of the amendment did not trigger *Unocal;* the board did not act unilaterally (without shareholder approval) and adopt a defensive measure in reaction to a perceived threat. *Id.* at 1376 (emphasis added).

[200]606 A.2d 75 (Del. 1992). In *Stroud*, the board approved amendments to the Certificate of Incorporation and recommended that the shareholders vote in favor of the amendments, which they subsequently approved. *Id.* at 80-81. The court held that *Unocal* was inapplicable because the boards' decision to recommend the amendments to the shareholders was not defensive. *Id.* at 79.

Unocal standard of review because the stockholders were entitled to vote in their own interest.[201]

The majority held that *Williams* and *Geier* were not dispositive since neither case established a per se rule that excluded voting agreements from a *Unocal* analysis as applied to a combined merger plan.[202] The majority explained that the voting agreements were "inextricably intertwined with the defensive aspects of the merger agreement" and were the "linchpin of Genesis' proposed tripartite defense."[203] Additionally, Genesis made the voter agreements a non-negotiable condition of the merger agreement; without them Genesis would not have had a complete defense.[204] The majority dismissed the defendants' argument and analyzed the deal protection devices under the *Unocal* enhanced scrutiny standard.

Under the first prong of *Unocal*, the majority recognized that the NCS directors must show that they had reasonable grounds to believe a threat to corporate policy and effectiveness existed.[205] The majority found that the NCS board acted in good faith and conducted a reasonable investigation when the board concluded that the possibility of losing the Genesis offer and being left without any comparable alternative transaction posed a threat.[206]

The majority then applied the second prong of the *Unocal* standard. The NCS board had to first show that its deal protection devices were not coercive or preclusive, then prove that the devices were within the range of reasonableness.[207]

The majority cited *Williams* to define coercion in a voting agreement context[208] and held that a stockholder vote may be nullified by wrongful coercion "where the board or some other party takes actions which have the effect of causing the stockholders to vote in favor of the proposed transaction for some reason other than the merits of the transaction."[209]

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[201] *Omnicare*, 818 A.2d at 934.

[202] *Id.*

[203] *Id.* Genesis's tripartite defense included: (1) the "force the vote" provision, (2) the voting agreements, and (3) the absence of a "fiduciary out" clause.

[204] *Id.*

[205] *Omnicare*, 818 A.2d at 935.

[206] *Id.*

[207] *Id.*

[208] *Id.*

[209] *Omnicare*, 818 A.2d at 935 (quoting Williams v. Geier, 671 A.2d 1368, 1382-83 (Del. 1996)). The board's action must *cause* the stockholder to vote one way or the other, not just influence their vote. *See* Brazen v. Bell Atl. Corp., 695 A.2d 43 (Del. 1997) (holding no stockholder coercion when the board adopted a valid termination fee provision, that was not overly excessive, to influence the shareholders to vote for the proposal).

Applying the facts to this definition, the majority found that the protective devices forced NCS public stockholders to accept the merger.[210] The majority concluded that the deal protection devices were coercive, because the "stockholder vote would have been robbed of its effectiveness by the impermissible coercion that predetermined the outcome of the merger without regard to the merits of the Genesis transaction."[211]

The majority then analyzed whether the deal protection devices precluded the consideration of a superior offer. The majority noted that although the minority shareholders could vote to accept or decline the Genesis merger, the deal protection devices would force them to accept the merger since it was a *fait accompli.*[212] Further, even if the NCS board withdrew its recommendation to accept the merger, as NCS did in this situation, the deal protection devices made it "mathematically impossible" and "realistically unattainable" to accept another offer.[213] The majority concluded that the deal protection devices were preclusive because the stockholders and NCS directors could not consider any superior offer.[214] The majority held that deal protection devices that lock-up a merger agreement, like the methods employed in this instance, are invalid and unenforceable because the coercive nature of these devices are outside the reasonable range of responses to the perceived threat of losing the Genesis offer. [215]

After deciding that the deal protection measures were unenforceable, the majority determined to whom the NCS board owed fiduciary duties and what actions were required to satisfy those fiduciary duties. The majority held that the board owed a fiduciary duty to minority shareholders, when a merger agreement is locked-up by irrevocable voter agreements requiring the majority shareholders to approve the merger.[216] Applying the rule to NCS, the majority concluded that the NCS board was not able to discharge

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[210] *Omnicare*, 818 A.2d at 935-36.

[211] *Id.* at 936 (citing *Brazen,* 695 A.2d at 50).

[212] *Id.*

[213] *Id.*

[214] *Omnicare* , 818 A.2d at 936.

[215] *Id.* The court of chancery noted that both deal protection devices, standing alone, are legal. *See supra* notes 108, 109. The majority rejected this assertion, holding that "taking action that is otherwise legally possible, however, does not *ipso facto* comport with the fiduciary responsibilities of directors in all circumstances." *Omnicare,* 818 A.2d at 937. Additionally, the majority noted that support for this rationale is found in the synopsis of the amended Section 251(c) of the DGCL which specifically provides "the amendments are not included to address the question of whether such a submission requirement is appropriate in any particular set of factual circumstances." *Id.*

[216] *Omnicare,* 818 A.2d at 937.

its fiduciary duties to the minority stockholders due to the defensive measures that locked-up the merger.[217]

The majority noted that it previously recognized a board's fiduciary duty to protect minority stockholders in its decision in *Paramount Communications, Inc. v. QVC Network, Inc.*[218] Although *QVC* was decided in the context of an acquisition that resulted in the pre-merger majority stockholder becoming minority stockholders following the merger,[219] the *Omnicare* majority did not distinguish the two cases. The majority followed the rationale in *QVC*, recognizing that when a single person, entity, or a cohesive group acts together to cause the minority shareholder votes to become mere formalities, the "minority stockholders must rely for protection solely on the fiduciary duties owed to them by the directors."[220] The majority concluded that "where a cohesive group of stockholders with majority voting power, [i.e., Outcalt and Shaw,] was irrevocably committed to the merger transaction," the NCS board of directors had an affirmative duty to protect the interests of the NCS minority stockholders.[221]

The last issue that the majority addressed was whether the NCS board, when deciding on a proposed transaction, should only evaluate the current situation or consider future circumstances that may arise. The majority noted that directors have a continuing obligation to discharge their fiduciary duties after announcing a merger agreement as future circumstances develop.[222] Thus, the stockholders were entitled to rely on the board to discharge its fiduciary duties at all times.[223] The majority held that the NCS board was required to negotiate a "fiduciary out" clause to protect the shareholders if a superior proposal emerged.[224] The majority concluded that the NCS board was required to include a "fiduciary out" clause in the Genesis's locked-up merger transaction in order to satisfy its continuing fiduciary duties to the minority stockholders.[225]

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[217] *Id.* at 936.

[218] 637 A.2d 34 (Del. 1994).

[219] *Id.*

[220] *Id.* at 42-43.

[221] *Omnicare*, 818 A.2d at 937.

[222] *Id.* at 938.

[223] *Id.*

[224] *Id.*

[225] *Omnicare*, 818 A.2d at 939.

2. The Dissenting Opinions

Chief Justice Veasey, in his dissent, concluded that the NCS board made a reasonable and well-informed judgment, in which the court should not substitute its judgment for that of the board and an absolute lock-up is not a per se violation of a board's fiduciary duty.[226] The Chief Justice added that this case is unique under Delaware corporation law because of the rare 3-2 split decision.[227] The Chief Justice noted that the uniqueness of the facts presented would "render this case an unlikely candidate for substantial repetition."[228]

Before concluding that the NCS directors made an informed and reasonable decision, the Chief Justice faulted the majority for reviewing the deal protection devices separate from the entire bidding process.[229] The dissent noted that NCS's only potential bidder prior to the non-negotiable Genesis agreements proposed uncertain, unattractive bids conditioned on completion of due diligence.[230] The Chief Justice noted that as a matter of business judgment, the risk of negotiating with Omnicare and losing Genesis, at the time the board approved the agreements, outweighed the possible benefits.[231] The dissent recognized that it is reasonable, under certain circumstances, to lock-up a transaction by "exchanging certainties."[232]

Evaluating the entire bidding process, the Chief Justice noted that the business judgment rule was appropriate for this situation.[233] Assuming that *Unocal* applied, however, the NCS directors' actions still were reasonable

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[226] *Omnicare*, 818 A.2d at 939-46 (Veasey, C.J., dissenting).

[227] *Id.* at 939. The Chief Justice cited *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985), to illustrate how few and far between 3-2 split decisions are in the Delaware courts. *Omnicare*, 818 A.2d at 939 n.90 (Veasey, C.J., dissenting).

[228] *Omnicare*, 818 A.2d at 939.

[229] *Id.* at 941. The Chief Justice reasoned that "the lock-ups here cannot be reviewed in a vacuum." *Id.*

[230] *Id.* Other facts the dissent notes that the majority failed to weigh properly are: Omnicare's initial refusal to buy NCS except through an asset sale in bankruptcy, and Omnicare's proposal would not have paid off all creditors. *Id.*

[231] *Id.*

[232] *Omnicare*, 818 A.2d at 942. The certainties exchanged were the certainty that Genesis would provide a return on equity for NCS stockholders in exchange for the certainty that the merger would be consummated. *Id.* at 941. The Chief Justice also notes that the benefits of permitting certainty are the possibility of the bidder paying a higher price for the target company and the target not risking that it will be perceived as damaged good if it loses the bidder. *Id.*

[233] *Id.* at 943.

in response to the threat.[234] The dissent stated that the majority misapplied the *Unocal* analysis because the NCS board did not adopt the defensive measures unilaterally, but acted jointly with the controlling shareholders.[235]

Further, the Chief Justice stated that the majority incorrectly preempted the proportionality paradigm with the *Unitrin* concept of "coercive and preclusive" measures.[236] The dissent distinguished *Unitrin* in its analysis and held that *Unitrin* only polices coercive and preclusive actions of the board in response to an *existing* threat in order to protect the stockholders.[237] The Chief Justice noted that the deal protection measures that the majority found to have "coerced" the stockholders were the very same measures that NCS stockholders Outcalt and Shaw independently agreed to adopt.[238] Regarding the NCS minority stockholders, the dissent stated that the coercion was meaningless because Outcalt and Shaw, as controlling shareholders, could approve any merger without the need for a minority vote and their votes were already "cast."[239] The dissent concluded that the NCS board action to negotiate the best deal available with the only viable merger partner, Genesis, was reasonable.[240]

The Chief Justice also disagreed with the majority's reasoning that an absolute lock-up was a per se violation of a boards' fiduciary duty. The majority held that a failure to negotiate a "fiduciary out" provision in locked-up transactions is invalid per se.[241] The dissent noted that the new rule is unwise because Genesis would have rejected the transaction if the NCS board negotiated the "fiduciary out" provision.[242]

The dissent also disagreed with the majority's reliance on *QVC* and the conclusion that the board's fiduciary duties prevented the board from negotiating a merger transaction without an escape provision.[243] The Chief Justice stated that the majority misapplied *QVC* because *QVC* is an

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[234] *Id.* at 943. The Chief Justice reasoned that *Unocal* did not apply because the basis of the doctrine is the "omnipresent specter" of the board's self-interest to stay in office and applies to unilateral board actions that are a response to a threat, i.e. "defensive and reactive in nature." *Id.* at 943 n.102.

[235] *Id.* at 943-44.

[236] *Omnicare*, 818 A.2d at 943.

[237] *Id.* at 944 (emphasis added).

[238] *Id.*

[239] *Id.* at 944-45. The Chief Justice dispensed of the "preclusive" element by stating that although the voting agreement precluded an overriding vote by the minority shareholders, "the pejorative 'preclusive' label applicable in a *Unitrin* fact situation has no application here." *Id.* at 945.

[240] *Omnicare*, 818 A.2d at 945.

[241] *Id.*

[242] *Id.*

[243] *Id.*

extension of *Revlon*, which prevents a board from ignoring a bidder who is willing to match or exceed the favored bidder's offer.[244] Further, the Chief Justice noted that the majority's application of "continuing fiduciary duties" is an extension of the *Revlon* concept, and wrongly permits a court to second guess directors' risk and return analysis by weighing the value of the only viable transaction against the prospect of a future offer.[245]

The Chief Justice also disagreed with the majority's establishment of a boards' special duty to protect minority shareholders from controlling stockholder decisions.[246] Distinguishing the majority's reliance on *QVC*, the dissent noted that *QVC* only holds that "minority stockholders must *rely* for protection on the fiduciary duties owed to them by [the] directors"; it does not *create* a special duty to protect minority shareholders unless the controlling stockholder stands on both sides of the transaction.[247] The Chief Justice concluded his dissent by stressing his hope that future courts will narrowly construe the majority's holding only to the unique facts of the present case.[248]

Justice Steele, joining Chief Justice Vesley's, wrote a separate dissent to memorialize his view, in which he concluded that the business judgment rule should apply absent a suggestion of self-interest or lack of care.[249] Justice Steele initially noted that the NCS board fully canvassed the market in an attempt to find an acquirer and provide some financial benefit to stockholders.[250] The only *bona fide* credible merger partner that NCS found though an exhausted process was Genesis. In the absence of the Genesis merger agreement, would have to negotiate with Omnicare, whose plan suggested no regard for the NCS stockholder interests and wanted to structure the deal as an asset sale in bankruptcy.[251]

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[244] *Omnicare*, 818 A.2d at 945.

[245] *Id.* at 945-46.

[246] *Id.* at 946.

[247] *Id.* at 946 (emphasis added).

[248] *Omnicare*, 818 A.2d at 946.

[249] *Id.* at 946-50 (Steele, J., dissenting). Justice Steele wrote that "[w]hen a board agrees rationally, in good faith, without conflict and with reasonable care to include provisions in a contract to preserve a deal in the absence of a better one, their business judgment should not be second-guessed in order to invalidate or declare unenforceable an otherwise valid agreement." *Id.* at 949.

Justice Steele also noted that claims alleging a breach of the fiduciary duty of care should be reviewed "only upon the basis of the information *then reasonable available* to the directors and relevant to their decision." *Id.* at 946 (quoting Smith v. Van Gorkom, 488 A.2d 858, 874 (Del. 1985)) (emphasis added).

[250] *Id.* at 947 (Steele, J., dissenting).

[251] *Id.* Justice Steele noted that NCS found Genesis in the face of Omnicare's initial silence, then to Omnicare's tepid interest to outright hostility toward NCS. *Id.*

Justice Steele then noted that the contract terms did not include "insidious, camouflaged side deals" for the directors or majority stockholders, nor did the terms include any transparent provisions for entrenchment or control premiums.[252] At the time the lock-up provisions were agreed upon, the terms were the best reasonably available for all the stockholders.[253] Justice Steele concluded that the courts should not second guess careful, selfless decisions that receive the approval of a full board and the majority shareholders.[254]

Justice Steele also predicted that the possible effect of the majority's decision could be prospective judicial review on transaction negotiations. Justice Steele questioned whether "we [have] now moved to a bright line regulatory alternative."[255] The potential repercussions, Justice Steele reasoned, prevent a board from honoring its contract obligations even if the board made the decision in good faith, free from self interest, and after exercising due care.[256]

IV. EVALUATION OF THE IMPACT OF *OMNICARE*

The impact of the majority's opinion on corporations, directors, stockholders, and practitioners has yet to be determined. The *Omnicare* decision is one of the most controversial decisions in Delaware Supreme Court history because of the 3-2 split, intensity of the dissenting opinions, broad nature of the majority's opinion language, and influential nature of the Delaware courts in corporation law.[257] The majority established three bright line rules in corporate takeover matters that previously were determined on a case-by-case analysis: (1) the *Unocal/Unitrin* enhanced scrutiny standard will apply to any defensive measures, whether or not the transaction will lead to a change in control; (2) a Section 251(c) "force the vote" provision utilized with affirmative voting agreements with the majority stockholders that effectively "lock-up" the transaction are invalid without a "fiduciary out" clause; and (3) when the majority stockholders

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[252] *Omnicare*, 818 A.2d at 948.

[253] *Id.*

[254] *Id.* Justice Steele "shamed" the majority for finding "no breach of loyalty or care but nonetheless sanctioned these directors for their failure to insist upon a 'fiduciary out' as if those directors had no regard for the effect of their otherwise disinterested, careful decision on others." *Id.*

[255] *Id.* at 950.

[256] *Omnicare*, 818 A.2d at 950.

[257] *See* Glenn Gurtcheff, *Omnicare, Inc. vs. NCS Healthcare, Inc.*, M & A Monitor (Piper Jaffray & Co., Minneapolis, MN), May 27, 2003, *available at* http://www.piperjaffray.com/archives/ma_monitor052603.htm (last visited Nov. 1, 2004).

work together as a cohesive group to approve a transaction, a board of directors has a special fiduciary duty to protect the minority stockholders.[258]

A. *The Future Application of* Unocal

Under the majority rule, a target corporation's board of directors may no longer enjoy the protection of the business judgment rule when negotiating terms of the transaction. A broad reading of the opinion leads to the conclusion that the courts will scrutinze any deal protection measure.[259] Under *Unocal* and its progeny, courts applied enhanced scrutiny when either defensive measures were taken in response to a hostile threat or *Revlon* duties apply during a change in control or sale of the company. The new rule, broadly read, would scrutinize defensive devices adopted not only in response to a present threat, but also the possibility of a future threat.

A narrow reading of the rule would limit the *Unocal* analysis to the facts of the case. Enhanced scrutiny, under a narrow reading, would apply only to deal protection measures that result in a "locked-up" transaction.[260] The board of directors may enjoy the protection of the business judgment rule for defensive devices that do not lock-up the transaction if the devices are not adopted in response to a hostile threat. Regardless of whether *Omnicare* is interpreted broadly or narrowly, the majority established that future courts should evaluate deal protection devices prospectively, taking into account the possibility of future proposals.

The majority concluded that the *Unocal* standard applies to deal protection devices because of the inherent conflicts of interest in merger transactions, following the court's rationale in *Paramount Communications, Inc. v. Time, Inc.*[261] The court noted that "there are inherent conflicts between a board's interest in protecting a merger transaction it has approved, the stockholders' statutory right to make the final decision to either approve or disapprove a merger, and the board's continuing responsibility to effectively exercise its fiduciary duties at all times after

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[258]*See, e.g.*, Sean J. Griffith, *Is a Deal Ever in the Bag?*, 38 MERGERS & ACQUISITIONS 18, 19-21 (2003); J. Travis Lester, *The Omnicare Opinion: A New Rule from Delaware*, 17 INSIGHTS 11, 15-17 (2003); *"Lockup" Agreement Coercive, Invalid, Divided Del. Court Determines*, 35 Sec. Reg. & L. Rep. (BNA) 619 (Apr. 14, 2003).

[259]*See* Lester, *supra* note 259, at 17.

[260]A Delaware attorney predicted that the decision might be viewed narrowly: "[the decision] will depend on whether or not M & A lawyers refrain from trying to lock up transactions because they think that this decision precludes any and all lockups. I'm not sure that has yet been determined." *"Lockup" Agreement*, *supra* note 259.

[261]571 A.2d 1140 (Del. 1989).

the merger agreement is executed."[262] The majority concluded that the inherent conflicts require a court to determine that the board protection devices are within statutory limitations and consistent with the directors' fiduciary duties.[263] The majority analogized *Paramount* to their reasoning, in which the defensive devices adopted by a board to protect the merger agreement are reviewed under *Unocal*, even when the transaction does not result in a change of control.[264]

Conversely, the dissenters believe that the business judgment rule is applicable to deal protection devices in a merger transaction that does not lead to a change of control.[265] Chief Justice Veasey, in his dissent, noted that deal protection measures should not be reviewed in a vacuum. The court, rather, should determine whether the board informed themselves of their available options and acted in good faith.[266] Justice Steele noted that in the absence of self-interest or lack of care,[267] the court should defer to the business judgment of the directors.[268] The dissent distinguished the majority's reliance on *Paramount*, noting that the deal protection measures in *Paramount* were defensive in nature and were adopted in response to a threat.[269]

B. *Can a Merger Transaction Ever Be Certain?*

The majority held that agreements are invalid when a Section 251(c) "force the vote" agreement is coupled with voting agreements of the majority stockholders without a "fiduciary out" escape provision. A broad interpretation of this rule leads to a conclusion that any deal protection devices adopted in a manner that locks up the merger transaction without a "fiduciary out" clause are per se invalid.[270] Following this interpretation, both directors and shareholders must not enter into agreements that would collectively ensure the consummation of a merger without providing an escape clause.

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[262] *Omnicare*, 818 A.2d at 930.

[263] *Id.* at 930-31.

[264] *Id.* at 931 (citing *Paramount*, 571 A.2d at 1151-55) (citations omitted).

[265] The dissent states: "[I]t is debatable whether *Unocal* applies-and we believe that the better rule in this situation is that the business judgment rule should apply." *Id.* at 943 (Veasey, C.J., dissenting).

[266] *Omnicare*, 818 A.2d at 943.

[267] *Id.* at 949 (Steele, J., dissenting).

[268] *Id.* (Steele, J. dissenting).

[269] *Id.* at 950 (Steele, J. dissenting).

[270] *See* Griffith, *supra* note 259, at 20.

A narrow interpretation of the majority's rule would, conversely, result in the conclusion that the ruling is based only on the facts of the *Omnicare* case. Thus, only "force the vote" agreements coupled with voter agreements of the majority stockholders require an escape clause. Under this interpretation, deal protection devices that lock-up merger agreements are not per se invalid, but will still be reviewed on a case-by-case basis.[271]

The majority noted that a merger transaction only becomes final upon a vote of the stockholders under Delaware law.[272] Any board action that robs the stockholders of their ability to exercise their right to vote is per se invalid.[273] Notwithstanding that it was the majority stockholders who entered into the voting agreements, the court reasoned that when deal protection devices, *in toto*, make it "mathematically impossible" for any superior proposal to succeed, the directors are required to negotiate a "fiduciary out" clause.[274]

The dissenting opinion concluded that failing to negotiate a "fiduciary out" provision in a locked-up merger agreement should not make the deal protection devices per se invalid. In the NCS situation, Chief Justice Veasey noted that Genesis's determination was not a "stalking horse."[275] Parting from the majority's reliance on *QVC*, the dissent noted that NCS's situation was not one where the directors "confront a superior transaction and turn away from it to lock up a less valuable deal . . . here, [the NCS] board committed itself to the *only* value-enhancing transaction available."[276] The Chief Justice stated that there was no authority supporting the majority's new rule, and the rule was unwise and unwarranted.[277] This per se rule will cause lower bidding prices for the

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[271]*See Omnicare*, 818 A.2d at 945-46 (Veasey, C.J., dissenting) ("One hopes that the Majority rule announced here—though clearly erroneous in our view—will be interpreted narrowly and will be seen as *sui generis*.").

[272]*Id.* at 930. DEL. CODE ANN. tit. 8, § 251(c), *supra* note 108, requires the shareholder vote.

[273]The majority found that "[t]he record reflects that any stockholder vote would have been robbed of its effectiveness by the impermissible coercion that predetermined the outcome of the merger . . . at the time the vote was scheduled to be taken." *Omnicare,* 818 A.2d at 936 (citing Brazen v. Bell Atl. Corp., 695 A.2d 43, 50 (Del. 1997)). Additionally, the majority recognized that the minority shareholders were able to exercise the right to approve or disapprove the merger, but found that their vote did not matter because they had to accept the merger as a *fait accompli*. *Id.*

[274]*Id.* at 936.

[275]*Id.* at 945 (Veasey, C.J., dissenting.)

[276]*Id.*

[277]*Omnicare*, 818 A.2d at 945 (Veasey, C.J., dissenting).

target corporation and target companies will risk devaluation if the bidder backs out of the transaction.[278]

Although the impact has yet to be determined, corporations may have alternatives to work around the court's bright line rule. First, although locking-up a transaction with majority voting agreements is invalid, corporations may pursue voting agreements of a significant minority.[279] Additionally, a bidder may seek to establish certainty by getting the majority stockholders to commit to a tender offer, thereby allowing the acquiring corporation to replace the majority stockholders, ensuring their approval vote.[280] Even though alternatives may be available, if future courts interpret the bright line rule broadly and bar pre-commitment strategies, any adoption of provisions intended to deliver transactional certainty may be a futile endeavor.[281]

C. *The Special Duty to Minority Shareholders*

The majority relied on *QVC* to recognize that directors have a duty to protect minority stockholders when a majority of a corporation's voting shares are acquired by a single person, entity, or cohesive group acting together.[282] The majority also held that the duty to protect minority stockholders in this situation is ongoing and continues as future circumstances develop even after the merger agreement is announced.[283] A broad interpretation of this special duty would lead to the conclusion that anytime a majority's voting shares are locked-up to approve or disapprove a transaction, directors must protect the minority's financial interests. The

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[278]Chief Justice Veasey stated in full:

> A lock-up permits a target board and a bidder to exchange certainties. Certainty itself has value. The acquirer may pay a higher price for the target if the acquirer is assured consummation of the transaction. The target company also benefits from the certainty of completing a transaction with a bidder because losing an acquirer creates the perception that a target is damaged goods, thus reducing its value.

Id. at 942.

[279]*See* Griffith, *supra* note 259, at 20. It is unclear on what percent of the stockholder vote may be locked-up; there is some authority from Delaware courts suggesting that the forty percent range may be too much. *Id.*

[280]*See id.* at 20-21. The problem that may arise from this situation is that bidder is not guaranteed that the transaction will consummate. A hostile raider may offer a higher tender offer and acquire the target's shares.

[281]*See id.* at 21.

[282]*Omnicare*, 818 A.2d at 937(citing Paramount Communications, Inc. v. QVC Network, Inc., 637 A.2d 34, 42 (Del. 1994)).

[283]*Id.* at 938.

court, therefore, moves closer to the *Revlon* duty to achieve the highest transaction available for stockholders.[284]

The dissent rejected the majority's reliance on *QVC* to support a directors' duty to minority shareholders. The Chief Justice noted that the holding of *QVC* only created a special duty to minority stockholders when the bidder's majority stockholder is also the controlling shareholder in the combined corporation, thereby diminishing the voting power of the target corporation.[285]

If future courts follow the broad rule that directors owe a continuous fiduciary duty to minority shareholders when the majority shareholders work as a cohesive group to approve or disapprove a transaction, courts may have inched closer to a *Revlon* review. By looking to *Paramount Communications, Inc. v. QVC Network, Inc.*, and *Mills Acquisition Co. v. Macmillan Inc.*,[286] the court may have erased the line between change of control mergers and mergers that do not lead to a change of control.[287]

V. CONCLUSION

Although the impact of the *Omnicare* decision is yet to be known, the majority opinion has seemingly attempted to establish a bright line rule for courts to apply when analyzing business transactions. *Unocal*, *Revlon*, and their progeny established the enhanced scrutiny standard in certain circumstances, in which the courts deferentially review the board of directors' decisions. By passing the buck from the directors to the courts, the *Omnicare* majority established a uniform standard to review decisions of directors.

First, the majority established the appropriate analysis to review business transactions under the enhanced scrutiny standard. The enhanced scrutiny analysis is a two-prong test. Under the first prong, a reviewing court must determine whether the board's decision was made on an informed basis and in good faith. The second prong, the proportionality test, requires a reviewing court to determine whether the transaction devices adopted were reasonable in relation to the threat posed. A court, under this prong, must first determine whether the transaction devices are "coercive" or "preclusive." If the devices are not "coercive" or "preclusive," then the court determines whether the devices were

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[284] *See* Lester, *supra* note 259, at 17.

[285] *Omnicare*, 818 A.2d at 946 (Veasey, C.J., dissenting).

[286] 559 A.2d 1261 (Del. 1988).

[287] *See* Lester, *supra* note 259, at 17.

reasonable in relation to the threat posed. If the two prongs are satisfied, then directors are afforded the protection of the business judgment rule.

Additionally, the majority concluded that provisions that lock-up a merger agreement are per se invalid. Under Delaware law, a merger transaction is not final until the stockholders vote to approve the transactions. The majority concluded that locking up a merger transaction before the stockholder vote deprives the stockholders of exercising their statutory right to vote if a superior proposal should arise in the future. The majority, therefore, held that these provisions are coercive and preclusive.

The dissenting judges, however, sought to avoid the creation of a bright line rule and review business decisions on a case-by-case factual basis. The dissenting judges stressed their hopes that the opinion will be *sui generis,* applying only to the *Omnicare* situation.

The dissent also stated that, even if enhanced scrutiny applies, provisions locking up a merger agreement are not per se invalid. Contrary to the majority, the dissenting judges believe that the provisions should be analyzed at the time they were adopted, in light of the circumstances surrounding the adoption. Under this analysis, if a board is well-informed and the circumstances force it to include provisions to lock-up a merger transaction, the provisions should not be invalidated.

Although many questions arise from a rare 3-2 supreme court split decision, one conclusion is clear: when a corporation enters into a merger transaction, the target corporation board must be aware that the court may review their decisions under an enhanced scrutiny standard and forewarned to include an escape provision, like a "fiduciary out" clause, to any protection device that has the possibility of locking up the merger.

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