THE *TECHNICOLOR* CASE—A LOST OPPORTUNITY

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On October 22, 1993, the Supreme Court of Delaware decided *Cede & Co. v. Technicolor, Inc.*[1] as the latest chapter in a litigation saga of more than ten years.[2] *Technicolor* involves a broad array of difficult and complex corporate governance issues, including aspects of the duty of loyalty, the duty of care, and the business judgment rule. As a result, the court had the opportunity to strengthen and to clarify applicable law. Unfortunately, clarity did not result and the decision may serve to confuse rather than to enlighten.

I. THE *TECHNICOLOR* CASE

A. *Facts*

In the summer of 1982, Ronald Perelman, chairman and controlling shareholder of MacAndrews & Forbes Group, Inc. (MAF), became interested in acquiring Technicolor,[3] a Hollywood film processing company,[4] of which the plaintiff, Cinerama, was a 4.405% shareholder.[5] As a result of an investment banker's contact, Perelman met with Fred Sullivan, a Technicolor director, on September 17, 1982.[6] The purpose of the meeting was to obtain Sullivan's assistance in the acquisition bid.[7] Sullivan failed to advise the other directors of the meeting until a week later when he told Morton Kamerman, Technicolor's CEO.[8] Sullivan did not, however, disclose Perelman's

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1. 634 A.2d 345 (Del. 1993).
2. *See* Cede & Co. v. Technicolor, Inc., Nos. 7129 & 8358, slip op. at 1 (Del. Ch. Jan. 13, 1987), *reprinted in* 13 DEL. J. CORP. L. 225, 229 (1988) (stating that the suit was originally filed March 18, 1983).
3. *Cede & Co.*, 634 A.2d at 352.
4. *Id.* at 351.
5. *Id.* at 349.
6. *Id.* at 352-53.
7. *Cede & Co.*, 634 A.2d at 352-53.
8. *Id.* at 353.

intent to acquire Technicolor stock nor did he disclose the recent increase in his own Technicolor stock holdings.[9]

Perelman and Kamerman met on October 4, 1982.[10] A number of subjects were discussed, including acquisition price and whether Sullivan would receive a finder's fee.[11] After this meeting, Kamerman spoke to two Technicolor directors; Guy Bjorkman, Technicolor's largest shareholder, and George Lewis, Kamerman's tax attorney.[12]

Kamerman met again with Perelman on October 12, 1982, and "reached substantial agreement on all matters . . . except price and financing."[13] Kamerman retained an investment banker and outside counsel without consulting the other directors.[14]

After further meetings, Perelman and Kamerman agreed on a price of $23 per share on October 27, 1982.[15] Perelman and Kamerman had previously agreed that Sullivan would receive a $150,000 finder's fee if the transaction closed.[16] Kamerman then called a special meeting of Technicolor's Board of Directors for October 29, 1982.[17]

The special board meeting was attended by all nine of the directors, three of whom knew nothing about the proposed sale of the company and four of whom had only limited knowledge of the subject prior to the meeting.[18] At the board meeting, Kamerman described the negotiations and opined that the price of $23 per share was "good" as it represented a price of "ten times 'core' earnings."[19]

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9. *Id.* Sullivan had instructed his secretary to purchase 10,000 shares of Technicolor stock on September 13, 1992, just three days after the investment banker had informed Sullivan of Perelman's interest in acquiring Technicolor. *Id.* However, only 1,000 shares were actually purchased. *Id.* at 353 n.8. Sullivan was "ultimately investigated by the Securities and Exchange Commission for insider trading, and the matter was settled, with Sullivan required to pay $13,705.09 to Technicolor." *Id.*

10. *Id.* at 353.

11. *Cede & Co.*, 634 A.2d. at 353-54.

12. *Id.* at 354.

13. *Id.*

14. *Id.*

15. *Cede & Co.*, 634 A.2d at 356.

16. *Id.* at 355.

17. *Id.* at 356.

18. *Id.*

19. *Cede & Co.*, 634 A.2d at 356. The price of Technicolor stock had reached "a new low of $8.37" per share by September 1982, "after falling by the end of June to $10.37 a share." *Id.* at 352. Kamerman stated that the depressed share price of the stock made Technicolor vulnerable to a takeover. *Id.* at 356.

Kamerman also described the structure of the proposed transaction as a friendly tender offer by Perelman's controlled corporation followed by a second step merger,

Kamerman outlined the terms of his proposed employment agreement and disclosed that Sullivan would receive a finder's fee of $150,000 if the transaction closed.[20] Therefore, Kamerman explained that both he and Sullivan had a financial interest in the transaction.[21]

Outside counsel explained the structure of the transaction by summarizing the terms of the proposed merger and reviewing key documents.[22] This explanation was followed by the investment banker's presentation based upon a seventy-eight page "board book."[23] The banker's presentation ended with his oral opinion that the price of $23 per share, subject to further due diligence, was fair.[24]

After the presentations, "several directors suggested pushing Perelman for more money but were advised that Perelman would go no higher."[25] Another director suggested that other offers be solicited, but after discussion the suggestion was rejected.[26]

The board then unanimously approved the agreement and the plan of merger and the board recommended that Technicolor shareholders accept the $23 per share offer.[27] Also, the board unanimously approved Sullivan's finder's fee, Kamerman's new employment contract, and a stock option agreement.[28]

The planned tender offer commenced and MAF, Perelman's controlled corporation, acquired 82.19% of the Technicolor shares

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the proposed options to Perelman's corporation on unissued shares of Technicolor, and the proposed stock purchase agreements with Kamerman, Bjorkman, and their wives. *Id.* at 356-57.

20. *Id.* at 357.

21. *Id.*

22. *Id.*

23. *Cede & Co.*, 634 A.2d at 357.

> The board book included median and mean values for other similar companies, a comparison of acquisitions in the motion picture business, a common stock comparison for other retailing companies, the financial performance of Technicolor and its constituent businesses, a profit and loss statement for each of Technicolor's major divisions, projections for Technicolor through 1989, projections on MAF's ability to consummate the transaction, and a Standard and Poor's tear sheet on MAF.

Id. at 357 n.20.

24. *Id.* at 357.

25. *Id.*

26. *Id.*

27. *Cede & Co.*, 634 A.2d at 357.

28. *Id.* This stock option agreement presumably covered MAF's right to acquire 844,000 shares of Technicolor's authorized but unissued shares which Perelman had sought as part of the transaction. *Id.*

by the time the tender offer closed on December 31, 1982.[29] The second step merger was approved by an 89% vote at a special shareholders meeting held on January 24, 1983.[30]

B. *The Chancery Court Decision*

Chancellor Allen found, at the outset, that the primary issue in the *Technicolor* case was whether the transaction should be reviewed under the business judgment rule or the entire fairness standard.[31] The chancellor noted that the business judgment form of review requires that the board be disinterested[32] and also requires that the board exercise appropriate procedural due care in reaching its decision.[33]

As to the necessary element of independence, the chancellor stated that not every financial interest is sufficient to invoke the entire fairness standard.[34] Only "material" financial interests are sufficient to have that effect.[35] As the chancellor's views were summarized by the supreme court, a director's self-interest is "material" if it creates "a reasonable probability: . . . that the independence of judgment of a 'reasonable person' in the director's position would be affected; and . . . that such director's individual self-interest would have affected the collective decision of the board."[36] The chancellor concluded that Sullivan, and possibly one other director, had materially disqualifying self- interests.[37] However, Chancellor Allen held that the board, as a whole, was not disqualified for business judgment rule purposes since the remaining seven directors had not been "dominated or materially manipulated by Sullivan" or the other director.[38]

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29. *Id.*

30. *Id.* at 357-58.

31. Cinerama, Inc. v. Technicolor, Inc., No. 8358, 1991 Del. Ch. LEXIS 105, at *27 (Del. Ch. June 21, 1991) (revised June 24, 1991), *reprinted in* 17 DEL. J. CORP. L. 551, 568 (1992).

32. *Id.* at *28, *reprinted in* 17 DEL. J. CORP. L. at 568-69. The term "disinterested" has been held synonymous with "independent" by the Chancellor. *Id.*

33. *Id.*

34. *Id.* at *33, *reprinted in* 17 DEL. J. CORP. L. at 571.

35. *Cinerama*, No. 8358, 1991 Del. Ch. LEXIS 105, at *37, *reprinted in* 17 DEL. J. CORP. L. at 572-73.

36. *Cede & Co.*, 634 A.2d at 362.

37. *Cinerama*, No. 8358, 1991 Del. Ch. LEXIS 105, at *49, *reprinted in* 17 DEL. J. CORP. L. at 578.

38. *Id.*

In examining the process due care requirement of the business judgment rule, while the chancellor expressed grave doubts as to whether the board had met its obligations in agreeing to the merger,[39] he ruled for the defendant since the plaintiff had failed to show damages resulting from the alleged breach.[40]

C. *The Holdings of the Supreme Court*

The Supreme Court of Delaware agreed with Chancellor Allen that the pivotal issue was whether the decision of the Technicolor board, on October 29, 1982, was protected by the business judgment rule or whether the board's decision should be subject to judicial review for entire fairness.[41] The court decided that the plaintiff was required to rebut the presumptions of the business judgment rule which, in its opinion, were that the board had met its duties of loyalty and care.[42]

1. The Duty of Loyalty

As to the duty of loyalty, the Supreme Court of Delaware decided that the chancellor was correct in holding that, as to any individual director, "materiality" was an issue in determining whether the director lacked independence.[43] However, the supreme court found that the use by the chancellor of the reasonably prudent man standard in such an inquiry was an error.[44] The court agreed with the chancellor's finding that at least one of the Technicolor directors (Sullivan) had been "self-interested."[45] However, the court disagreed with the way in which the chancellor determined whether the self-interest of Sullivan and the other possibly self-interested director had tainted the decision of the majority of the board.[46] This issue was remanded to the chancery court for further decision.[47]

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39. *Id.* at *8-9, *reprinted in* 17 DEL. J. CORP. L. at 559-60.
40. *Id.* at *12, *reprinted in* 17 DEL. J. CORP. L. at 561.
41. *Cede & Co.*, 634 A.2d at 358.
42. *Id.* at 361.
43. *Id.* at 363.
44. *Id.* at 364.
45. *Cede & Co.*, 634 A.2d at 372.
46. *Id.* While at various points in the opinion the court suggests that one other director, in addition to Sullivan, may have been "interested," the opinion sets forth very little in the way of facts to support such a conclusion.
47. *Id.* at 373.

In addition, the supreme court was intrigued by the possible interplay between section 144(a) of the Delaware Code,[48] which provides a mechanism for removing the taint of conflict in a conflict transaction, and a Technicolor charter provision which required unanimous director approval of a merger proposal absent a 95% shareholder vote.[49] The court also remanded these issues to the lower court.[50]

2. The Duty of Care

The supreme court reaffirmed that "due care" means procedural due care for purposes of the rule.[51] However, the court expanded the process concept beyond a requirement to be appropriately informed under the circumstances.[52] Most significantly, and relying solely upon hostile takeover decisions, the court held that "a director's duty of care requires a director to take an active and direct role *in the context of a sale of a company* from beginning to end."[53] On the

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48. *Id.* at 365-66. DEL. CODE ANN. tit. 8, § 144(a)(1) (1991). Section 144(a)(1) provides:

> (a) No contract or transaction between a corporation and [one] or more of its directors or officers, or between a corporation and any other corporation, partnership, association, or other organization in which [one] or more of its directors or officers, are directors or officers, or have a financial interest, shall be void or voidable solely for this reason, or solely because the director or officer is present at or participates in the meeting of the board or committee which authorizes the contract or transaction, or solely because his or their votes are counted for such purpose, if:
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> (1) The material facts as to his relationship or interest and as to the contract or transaction are disclosed or are known to the board of directors or the committee, and the board or committee in good faith authorizes the contract or transaction by the affirmative votes of a majority of the disinterested directors, even though the disinterested directors be less than a quorum . . . .

Id.; *see infra* text accompanying notes 74-80 (Section II(A)(3)).

Specifically, the supreme court questioned "the Chancellor's requirement that a director's self-interest translate into board self-interest." *Cede & Co.*, 634 A.2d at 365. The court felt that § 144(a)(1) was enacted "to prevent director conflicts of interest from voiding corporate action." *Id.*

49. *Cede & Co.*, 634 A.2d at 365.

50. *Id.* at 373.

51. *Id.* at 367-68.

52. *Id.*

53. *Cede & Co.*, 634 A.2d at 368 (emphasis added) (citing Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 66 (Del. 1989); Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985)). It is crystal clear that *Technicolor* did *not* involve a hostile takeover of the sort necessary to invoke the enhanced

record, the court found, as a matter of law, that the directors had breached their duty of care in deciding to sell Technicolor at their October 29, 1982 meeting.[54] This finding was contrary to the decision of the chancellor, who although expressing "grave doubts" as to the directors' conduct had not so found.[55] Except as to the newly imposed duty on directors in the consensual merger context to take "an active and direct role from beginning to end," it is at least arguable under prior Delaware law that the majority of the directors had not acted in violation of the gross negligence standard of *Smith v. Van Gorkom*.[56]

The chancellor held that it was unnecessary to decide if the process due care presumption of the business judgment rule had been rebutted since the plaintiff had failed to show proof of injury proximately related to the alleged breach.[57] However, the supreme court held that proof of injury was not a requirement plaintiff must meet to rebut the presumptions of the rule.[58]

The court went on to state that when the rule is rebutted, the burden of proof shifts to the defendants to demonstrate that the transaction was entirely fair.[59] When the inquiry is one of entire fairness, and again citing only hostile takeover decisions, the court

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business judgment rule of Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985). "The law is clear that *Unocal* is invoked as the result of any defensive measures taken in response to some threat to corporate policy and effectiveness which touch upon issues of control." Gilbert v. El Paso Co., 575 A.2d 1131, 1144 (Del. 1990). Defensive measures were not taken by the directors in *Technicolor*.

54. *Cede & Co.*, 634 A.2d at 369.

55. *Id.*

56. 488 A.2d 858 (Del. 1985). In *Van Gorkom*, the court found that the directors had breached their duty of procedural due care as they

> did not adequately inform themselves as to Van Gorkom's role in forcing the "sale" of the [c]ompany and in establishing the per share purchase price; . . . were uninformed as to the intrinsic value of the [c]ompany; and . . . given these circumstances, at a minimum, were grossly negligent in approving the "sale" of the [c]ompany upon two hours' consideration, without prior notice, and without the exigency of a crisis or emergency.

Id. at 874.

While the facts in *Technicolor* as to the approval of the sale of the company without adequate consideration or notice are arguably similar to those in *Van Gorkom*, the facts in *Technicolor* as to the other two factors are not. Kamerman's role in the sale and his role in setting the acquisition price *were* spelled out for the board at the October 29th meeting. In addition, the board had the benefit of a reputable investment banker's opinion that the price of $23 per share was "fair." *Cede & Co.*, 634 A.2d at 356.

57. *Cede & Co.*, 634 A.2d at 368.

58. *Id.* at 369.

59. *Id.* at 361.

stated that "the directors have the burden of establishing that the price offered was the highest value reasonably available under the circumstances."[60] The supreme court remanded the case to the chancery court to conduct an entire fairness hearing,[61] which, as to "fair price," was not to be "limited to the difference between the price offered and the 'true' value as determined under appraisal proceedings."[62] More particularly, the chancellor was directed to consider the appropriateness of rescissory damages.[63]

II. ISSUES AND ANALYSIS

A. *Duty of Loyalty*

1. Is There a Distinction Between Disinterest and Independence?

Until *Technicolor*, it was clear that a sharp distinction had been drawn between the concepts of disinterest and independence. The leading case of *Aronson v. Lewis*,[64] in defining "interest," the antonym of disinterest, stated that "[f]rom the standpoint of interest, this means that directors can neither appear on both sides of a transaction nor expect to derive any personal financial benefit from it in the sense of self-dealing, as opposed to a benefit which devolves upon the corporation or all stockholders generally."[65]

As to "independence," the court defined that term as follows:

> Independence means that a director's decision is based on the corporate merits of the subject before the board rather than extraneous considerations or influences. [T]he end result . . . must be that each director has brought his or her own informed business judgment to bear with specificity upon the corporate merits of the issues without regard for or succumbing to influences which convert an otherwise valid business decision into a faithless act.[66]

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60. *Id.* (citing Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1288 (Del. 1988); Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 67-68 (Del. 1989)).

61. *Cede & Co.*, 634 A.2d at 373.

62. *Id.* at 371. The price offered was $23 per share. *Id.* at 349. In an appraisal proceeding in this case, the chancellor had found that a "fair" price was $21.60 per share. *Id.* at 350.

63. *Id.* at 371.

64. 473 A.2d 805 (Del. 1984).

65. *Id.* at 812.

66. *Id.* at 816.

Put another way, to be independent, the director cannot be "beholden to the controlling person."[67]

The distinction between "disinterest" and "independence" is important, particularly in the context of determining the impact of a "tainted" director on the remaining directors' ability to make decisions under the protection of the business judgment rule.[68] However, the *Technicolor* court seriously blurs the distinction between the two throughout its opinion. For example, the court at one point states: "This Court has generally and consistently refrained from adopting a bright-line rule for determining when a director's *breach of duty of independence through self-interest* translates into evidence sufficient to rebut the business judgment presumption accorded board action."[69] The confusion is compounded further by statements which could be read to hold that self- interest may not be a disqualifying factor for a director under the business judgment rule.[70]

2. The Impact of an Interested or Dominated Director on Decisions of an Otherwise Disinterested and Independent Board

The chancellor found that the plaintiff had failed to prove that "the disloyal director either dominated the board or in some way tainted the presumed independence of the remaining board members

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67. *Id.* at 815. *See also* Pogostin v. Rice, 480 A.2d 619, 623 (Del. 1984) (holding "[d]irectorial interest exists whenever divided loyalties are present, or a director either has received, or is entitled to receive, a personal financial benefit from the challenged transaction which is not equally shared by the stockholder"). The court in *Pogostin* stated that "[t]he question of independence flows from an analysis of the factual allegations pertaining to the influences upon the directors' performance of their duties generally, and more specifically in respect to the challenged transaction." *Id.* (citation omitted).

68. *See infra* text accompanying notes 71-73 (Section II(A)(2)).

69. *Cede & Co.*, 634 A.2d at 364 (emphasis added). Fortunately, the court has since noted the error and in a later decision, Rales v. Blasband, 634 A.2d 927 (Del. 1993), spoke at length on the difference between disinterest and independence. *Id.* at 935-37.

70. *Cede & Co.*, 634 A.2d at 364. "To disqualify a director, for rule rebuttal purposes, there must be evidence of disloyalty." *Id.* at 363. The decisions used by the supreme court to illustrate this point did not deal with what had previously been thought to be "self-interest," but, rather, with "good faith," the lack thereof, or in one instance, a decision not involving the business judgment rule at all. *See* Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261 (Del. 1988) (concerning fraud on the corporation or the board); Polk v. Good, 507 A.2d 531, 536-37 (Del. 1986) (regarding an illegal vote buying scheme); Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985) (regarding motives of entrenchment); Lutz v. Boas, 171 A.2d 381, 395-96 (Del. Ch. 1961) (abdicating directorial duty in the non-decision-making context as to which the business judgment rule does not apply).

voting to approve the challenged transaction."[71] As a result, Sullivan's self-interest was held not to have compromised the ability of the board majority to make a decision under the protection of the business judgment rule.[72] However, the supreme court, while not necessarily disagreeing with the foregoing, remanded the issue because of what it perceived to be important unresolved issues.[73]

It is hard to see how the presumptions of the rule can be rebutted as to a majority of a board through the lack of disinterest or independence by a minority of tainted directors *unless the majority can be shown to have been dominated by the tainted minority*. Absent that, there can be no showing that the majority could not, and did not, exercise independent judgment. Assume, for example, that the tainted minority had a financial interest in the transaction approved by the majority. This self- interest per se would in no way affect the disinterestedness and independence of the majority. Only if the tainted minority *dominated* the majority so that they could not exercise independent judgment as to the transaction before the board, should the majority be denied the protection of the rule. Based on the foregoing, it would seem that the court could have decided this issue based upon the record without remanding the matter to the chancery court.

3. The Role of Section 144(a) and the Technicolor Charter Provision

Section 144(a) of the Delaware General Corporation Code provides that if its provisions are met, "no contract or transaction" between a corporation and a director in which the director has a financial interest "shall be void or voidable solely for this reason."[74] Under section 144(a), the taint of conflict can be removed if, after full disclosure, a majority of disinterested directors or a majority of disinterested shareholders approve the contract or transaction.[75] Absent that, the contract or transaction will also be upheld if found by a court to be fair to the corporation.[76]

The Technicolor certificate of incorporation contained a provision requiring, in the case of a merger, that unless the merger

71. *Cede & Co.*, 634 A.2d at 358.
72. *Id.*
73. *See infra* text accompanying notes 74-80 (Section II(A)(3)).
74. DEL. CODE ANN. tit. 8, § 144(a) (1991). *See supra* note 48.
75. *Cede & Co.*, 634 A.2d at 365.
76. *Id.*

was approved by a unanimous vote of the directors, a 95% vote of shareholders was required to approve the transaction.[77] The Technicolor merger was approved by an 89% vote of the shareholders.[78]

Finding that neither the parties nor the chancellor had adequately addressed these provisions, the court directed the chancellor to consider the impact of both section 144(a) and the Technicolor charter provision on the issues of the case.[79]

Section 144(a) should not pose a problem for the chancellor on remand. First, section 144(a) arguably does not *apply* to the approval of the agreement and plan of merger. Was the merger agreement a contract or a transaction between the corporation and a director? Second, even if section 144(a) is applicable, a majority of admittedly disinterested directors approved the agreement and plan of merger after appropriate disclosure.

The certificate provision poses a more substantial problem, particularly if the provision requires, or is interpreted to require, that the unanimous vote must be by *disinterested* directors. Although it is unlikely that disinterested director approval is required,[80] the timing of the various votes of the Technicolor board at the October 29th meeting may put the transaction at serious risk if such approval is required. Assume that a majority of disinterested Technicolor directors, after full disclosure, approved Sullivan's finder's fee and thus removed the taint of conflict stemming from his self-interest. Thereafter, since the taint of Sullivan's conflict would have been removed, a unanimous vote of the directors (including Sullivan) could have been taken to approve the sale of the company. However, if the directorial vote on Sullivan's finder's fee did not take place *before* the vote on the agreement and plan of merger, how could a unanimous vote of *disinterested* directors have taken place?

B. *The Duty of Care*

1. The Court's Formulation of the Business Judgment Rule

After emphasizing that the business judgment rule is both a procedural and a substantive rule of law,[81] the supreme court, ig-

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77. *Id.* at 365-66.

78. *Id.* at 358.

79. *Cede & Co.*, 634 A.2d at 373.

80. As a practical matter, unanimous director approval provisions are normally adopted to allow a veto right by directors in situations where some directors will, in fact, be "interested."

81. *Cede & Co.*, 634 A.2d at 360 (citing Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 64 (Del. 1989)).

noring the often used formulation of *Aronson*,[82] stated the rule as a triad—"good faith, loyalty, and due care."[83] While it is suggested that a preferable formulation is good faith and process due care,[84] the court's formulation is workable so long as the term "good faith" is recognized as being more than subjective good faith. The formulation of the rule, however, is less important than recognizing what constitutes the *substance* of the rule. As to substance, process "due care, subjective good faith, disinterest, and independence [are] necessary for the rule to apply."[85] Equally important, however, there must be an "absence of waste, egregious conduct, illegality, fraud, and ultra vires conduct."[86]

2. Under *Technicolor*, What is the Meaning of Process Due Care?

Smith v. Van Gorkom[87] firmly established the due care standard as process-oriented where decisions are involved. In that case, a class action had been brought by shareholders of Trans Union Corporation, alleging breach of the directors' duty of care by their approval of a $690 million merger of Trans Union with a subsidiary of Marmon Group Inc.[88] The Supreme Court of Delaware found that the board had not taken appropriate steps to become informed about the proposed merger and found the business judgment rule inapplicable.[89] The directors were held liable and the case was remanded for damage determination in an entire fairness hearing.[90] The directors had not followed appropriate *process* in that they were not adequately informed before reaching the decision to merge.

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82. *Aronson*, 473 A.2d at 812. "It is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." *Id.*

83. *Cede & Co.*, 634 A.2d at 361.

84. *See* Charles Hansen, *The Duty of Care, the Business Judgment Rule, and the American Law Institute Corporate Governance Project*, 48 BUS. LAW. 1355 (Aug. 1993) (stating that all the elements of the business judgment rule should fall under the category of good faith and procedural due care).

85. *Id.* at 1369.

86. *Id.*

87. 488 A.2d 858 (Del. 1985). Prior to *Van Gorkom*, some cases seemed to acknowledge that "due care" meant process due care when decisions were involved. *See, e.g.*, Casey v. Woodruff, 49 N.Y.S.2d 625, 643 (N.Y. 1944) ("When courts say that they will not interfere in matters of business judgment, it is presupposed that judgment—*reasonable diligence*—has in fact been exercised.") (emphasis added).

88. *Van Gorkom*, 488 A.2d at 863-70.

89. *Id.* at 893.

90. *Id.*

It is now clear as a result of later decisions that *Van Gorkom's* holding on the duty of care in corporate decision making relates solely to process. "In our case law since *Van Gorkom*, our due care examination has focused on a board's *decision-making process*."[91] In other words, a director can make a decision which would not have been made by the "ordinarily prudent person" and escape liability as long as appropriate "process" was followed.[92] Thus, there is no such thing as liability for a "negligent" substantive decision. The *Technicolor* decision is in accord on this point.[93]

However, beyond taking appropriate steps to become informed,[94] what else must directors do to meet their process due care obligation? In *Technicolor*, the court seemingly sought to expand the directors' obligation beyond becoming informed.[95] Not surprisingly, an earlier case held that directors, in reaching a decision, must also act with reasonable deliberation under the circumstances.[96] Also not surprisingly, the court in *Technicolor* noted that when the decision is the sale of a company, the obligation to become informed includes a "prudent search for alternatives."[97] However, the *Technicolor* court further defines the director's duty of care as "requir[ing] a director

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91. Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 66 (Del. 1989) (emphasis added). *See also* Citron v. Fairchild Camera & Instrument Corp., [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,915, at 90,104 (Del. Ch. May 19, 1988), *reprinted in* 14 DEL. J. CORP. L. 273, 305 (1989) (stating that "[a]s a substantive rule of law, the business judgment rule provides that there is no liability for an injury or loss to the corporation arising from corporate action when the directors, in authorizing such action, proceeded in good faith and with appropriate care").

92. *Citron*, 569 A.2d at 66. "Absent bad faith or some other corrupt motive, directors are normally not liable to the corporation for mistakes of judgment . . . ." Cramer v. General Tel. & Elecs. Corp., 582 F.2d 259, 274 (3d Cir. 1978), *cert. denied*, 439 U.S. 1129 (1979).

93. *Cede & Co.*, 634 A.2d at 638 (holding directors liable only if they failed to fully inform themselves in a deliberate manner).

94. *Van Gorkom*, 488 A.2d at 872 (holding that directors must inform themselves, prior to making a business decision, of all material information reasonably available to them).

95. *Cede & Co.*, 634 A.2d at 367. "Having become so informed, they must *then* act with requisite care in the discharge of their duties." *Id.*

96. Gimbel v. Signal Co., 316 A.2d 599 (Del. Ch. 1974), *aff'd*, 316 A.2d 619 (Del. 1974).

97. *Cede & Co.*, 634 A.2d at 369-70. Following *Technicolor*, the careful counsellor should make sure that alternatives are considered even in the case of a consensual merger. This should not mean, however, that an auction or its equivalent need be conducted except as may be mandated by the recent case of Paramount Communications Inc. v. QVC Network, Inc., No. 13,117, 1994 Del. LEXIS 57 (Del. Feb. 4, 1994). *See infra* text accompanying notes 119-29.

to take an active and direct role in the context of the sale of a company from beginning to end," and that "directors cannot be passive instrumentalities during merger proceedings."[98] *Citron v. Fairchild Camera & Instrument Corp.*[99] and *Unocal Corp. v. Mesa Petroleum Co.*[100] are cited in support.[101]

That these two cases involved hostile takeovers and not consensual acquisitions does not seem to matter to the court. This is surprising since in the hostile takeover cases the classic business judgment rule does not apply—rather the "enhanced rule" is the appropriate standard due to "the omnipresent specter that a board may be acting primarily in its own interests."[102] Under the enhanced rule, defendants have the burden of going forward with the evidence to show that the defensive action taken was "reasonable in relation to the threat posed."[103] "Reasonableness" is a key measure in all hostile takeover cases. This is in sharp contrast to consensual acquisitions where the classic business judgment rule would apply.[104] The concept of "reasonableness" has no place in a classic business judgment rule analysis.[105] The requirements are solely process due care and good faith.[106] As a result, the supreme court's citation of

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98. *Cede & Co.*, 634 A.2d at 368 (citing *Citron*, 569 A.2d at 66). Interestingly, the following quotation from Gilbert v. El Paso Co., 575 A.2d 1131 (Del. 1990), demonstrates that the basis of these statements flows from the hostile takeover context: "Given the injunction of *Unocal* that the duties of care and loyalty prevent a board from being a passive instrumentality *in the face of a perceived threat to corporate control* . . . ." *Id.* at 1146 (emphasis added).

99. 569 A.2d 53, 64 (Del. 1989). The court held that in a due care examination, a court must "look particularly for evidence of a board's active and direct role in the sale process." *Id.* at 66.

100. 493 A.2d 946 (Del. 1985). The court held that "in the broad context of corporate governance, including issues of fundamental corporate change, a board of directors is not a passive instrumentality." *Id.* at 954.

101. *Cede & Co.*, 634 A.2d at 368.

102. *Unocal Corp.*, 493 A.2d at 954.

103. *Id.* at 955.

104. Barris Indus., Inc. v. Bryan, 686 F. Supp. 125 (E.D. Va. 1988). *See* Paramount Communications Inc. v. Time Inc., [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,514, at 93,283 (Del. Ch. July 14, 1989) (revised July 17, 1989), *reprinted in* 15 DEL. J. CORP. L. 700, 748 (1990) (holding that the business judgment rule was the standard by which to measure the stock-for-stock merger phase of the case).

105. *See* Paramount Communiations Inc. v. QVC Network Inc., No. 13,117, 1994 Del. LEXIS 57, at *54 n.21 (Del. Feb. 4, 1994).

106. "Good faith" in this formulation means more than subjective good faith. *See* Hansen, *supra* note 84, at 1361.

The court in *TW Servs., Inc.*, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH)

hostile takeover decisions to support general legal propositions is not only confusing, but produces a serious undermining of basic business judgment rule law.[107]

The court in *TW Services, Inc. v. SWT Acquisition Corp.*[108] explains the difference by noting that as to consensual mergers, the statute specifically provides that the board, as the entity having the ultimate responsibility for the business and affairs of the corporation, must approve a merger and, as a result, its decisions with respect thereto are covered by the classic rule.[109] In contrast, in the hostile takeover context, the board has no statutorily mandated role;[110] rather the board injects itself unilaterally into what, without more, would be a decision solely between the would-be acquirer and the shareholders. The relevant inquiry is whether the shareholders wish to sell their stock to the acquiring company?[111] This has led certain commentators

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at 92,182, *reprinted in* 14 DEL. J. CORP. L. at 1190, stated:

> Should a court be required to review a decision not to pursue a merger, it would, in my opinion, ask itself the two fundamental questions that the business judgment form of judicial review requires: did the board reach that decision in good faith . . . and did it do so advisedly? Supposing that the plaintiff failed to persuade the court that the answer to either question was in the negative, the court would not go on to exercise even the restrained level of substantive review that *Unocal* contemplates. *It would not ask whether the decision could be justified as "reasonable" in relation to anything else, as it is to do when the decision is to preclude a tender offer.*

Id. (emphasis added).

107. The sharp difference between a consensual transaction and a hostile takeover and the care taken by the Delaware courts to distinguish the two is illustrated in *Gilbert*, 575 A.2d at 1144. In explaining why the enhanced business judgment rule of *Unocal* should apply in that case, the court stated: "Thus, we cannot agree that the settlement between El Paso and Burlington represented a *consensual, voluntary* adjustment of their grievances." *Id.* (emphasis added).

108. [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,334 (Del. Ch. Mar. 2, 1989), *reprinted in* 14 DEL. J. CORP. L. 1169 (1989).

109. *Id.* at 92,182, *reprinted in* 14 DEL. J. CORP. L. at 1191. In a merger, the board of directors cannot allow shareholders alone to make the decision to merge. *Van Gorkom*, 488 A.2d at 873.

110. A merger, consolidation, or a sale of substantially all the assets of a Delaware corporation must be approved by its board of directors, followed by shareholder approval. DEL. CODE ANN. tit. 8, §§ 251, 271 (1993). By way of contrast, in a hostile takeover, the acquiring corporation seeks to make the acquisition by purchasing shares directly from shareholders. "[T]ender offers essentially represent the sale of shareholders' separate property and such sales—even when aggregated into a single change in control transaction—require no 'corporate' action and do not involve distinctively 'corporate' interests." *TW Servs., Inc.*, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 92,181, *reprinted in* 14 DEL. J. CORP. L. at 1189.

111. *TW Servs., Inc.*, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 92,181, *reprinted in* 14 DEL. J. CORP. L. at 1189.

to argue that the board should play no role whatsoever in a hostile takeover. Rather, the board should be purely passive and let the market decide.[112] Such passivity would, of course, be impossible in the case of a consensual transaction.

While it can be argued that "the omnipresent specter" may also be present in the consensual context as well as the hostile context, history indicates that the abuses perceived by the courts were hostile takeover abuses, particularly the employment of tactics arguably out of proportion to the takeover threat.[113] This is why the enhanced rule was developed and why its concepts should not be used to undermine classic business judgment rule law.[114]

It is important for the court to preserve the distinction between acquisitions in the consensual and hostile contexts and not to allow a blurring of the differences. As the Supreme Court of Delaware has noted, "Our starting point is the fundamental principle of Delaware law that the business and affairs of a corporation are managed by or under the direction of its board of directors."[115] This critical point is of vital importance and should not be watered down in the slightest as to consensual acquisitions.

In a consensual acquisition, the proper balance between the role of the board of directors in managing the corporation and the interests of the shareholders should be preserved. If the directors reject a proposed consensual acquisition, the rejection is final, provided the requirements of the classic business judgment rule are met.[116] Of

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112. *See generally* Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981) (arguing that a target company's defensive tactics in response to a tender offer often adversely affect shareholder welfare).

113. *See, e.g.*, Buffalo Forge Co. v. Ogden Corp., 717 F.2d 757 (2d Cir.), *cert. denied*, 464 U.S. 1018 (1983) (concerning the sale of treasury stock to a "white knight," coupled with an option to acquire treasury stock at a price less than the price paid by the successful tender offeror); Panter v. Marshall Field & Co., 646 F.2d 271, 290-91 (7th Cir. 1981) (concerning acquisitions made by target to increase tender offeror's antitrust problems); Whittaker Corp. v. Edgar, 535 F. Supp. 933 (N.D. Ill. 1982) (regarding a sale to a third party of a portion of the target's business which accounted for one third of the target's profits to make the target less attractive to tender offeror).

114. *See supra* text accompanying note 102.

115. *Cede & Co.*, 634 A.2d at 360 (citing DEL. CODE ANN. tit. 8, § 141(a) (1991)). Essentially the same language appears in virtually all of the recent Supreme Court of Delaware decisions on matters of corporate governance.

116. *See supra* notes 104-06. One of the requirements of the rule is that the directors be properly informed, measured by standards of gross negligence. Aronson

course, the would-be acquirer has the option to then deal directly with the shareholders, invoking the law of hostile takeovers if the board takes defensive counter measures.[117] On the other hand, if the directors agree to a consensual acquisition, even if the directors have met the requirements of the classic rule, the shareholders may still vote to reject the combination if they perceive that it is not in their best interests.[118]

A case decided after *Technicolor*, *Paramount Communications v. QVC Network*,[119] may be helpful in clarifying some of the confusion in *Technicolor*. This recent decision may also herald new sets of circumstances in which the enhanced business judgment rule will be applied.[120]

Briefly stated, in *Paramount*, as part of a previously established strategic plan, Paramount Communications agreed to merge with Viacom, a company controlled by its chairman and chief executive officer, Sumner Redstone.[121] Thereafter, a higher hostile bid by QVC surfaced.[122] In the ensuing suit by QVC to block the Paramount-Viacom transaction, Paramount cited *Paramount Communications, Inc. v. Time Inc.* (*Time-Warner*)[123] in support of the argument that it had no obligation to abandon its preexisting long term strategy, of which the merger was a part, to accept an offer which would yield greater

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v. Lewis, 473 A.2d 805, 812 (Del. 1984). Being properly informed where the sale of a company is involved should include a prudent exploration of alternatives. This prudent exploration, however, should not include a requirement for an auction or even a market check involving contact with other potential buyers.

117. *See, e.g.*, Panter v. Marshall Field & Co., 646 F.2d 271 (7th Cir. 1980); Resource Exploration v. Yankee Oil & Gas, Inc., 566 F. Supp. 54 (N.D. Ohio 1983).

118. In a merger, consolidation, or a sale of substantially all the assets of a Delaware corporation, even if the transaction is approved by the directors, the shareholders must also approve the transaction in order for it to be effected. DEL. CODE ANN. tit. 8, §§ 251, 271 (1993). In the case of a friendly tender offer made directly to shareholders, the transaction cannot be effected unless the shareholders tender their shares into the offer. *See id.*

119. No. 13,117, 1994 Del. LEXIS 57 (Del. Feb. 4, 1994).

120. A full discussion of *Paramount Communications v. QVC Network*, which in itself is a fertile field for discussion, is beyond the scope of this article. Note, however, that the issue in *Technicolor* is the choice of standard between the business judgment rule and the intrinsic fairness test rather than between the business judgment rule and the enhanced business judgment rule. *See supra* text accompanying notes 40-42.

121. *Paramount Communications*, No. 13,117, 1994 Del. LEXIS 57, at *11.

122. *Id.* at *14.

123. 571 A.2d 1140 (Del. 1989) (revised Mar. 9, 1990).

short term value to the shareholders.[124] The Supreme Court of Delaware, however, upheld a lower court decision which had held that *Revlon* duties applied to the Paramount Board and that these duties had been breached.[125] The court took great pains to limit its decision to the facts of the case; namely, the sale of a company to a company with a controlling person, who had the power, following consummation of the transaction, to oust the public shareholders.[126] The court distinguished *Time-Warner* in which no change of control had been found in the parties' original stock-for-stock merger.[127] Using the reasoning utilized by the chancery court in *Time-Warner*, the *Paramount* court held that the reason there had been no "change of control" in *Time-Warner* was that control "remained in a fluid aggregation of unaffiliated stockholders" before and after the transaction.[128]

The *Technicolor* court could have used the same rationale since Perelman was in control of the acquiring company.[129] From an analytical point of view, this would have been an understandable result. Any time a board acts to sell the company to a firm which has a controlling shareholder or control group, *Revlon* duties are invoked.[130] Such a rule would not have created the problems *Technicolor* raises for all other consensual transactions. In any event, maintaining and strengthening the distinction between consensual and hostile transactions will be helpful in eliminating an unfortunate view which the lay press has of the Delaware court: "A cynical view of Delaware is that it vacillates between protecting shareholder rights . . . and management prerogatives . . . without making anyone angry enough to leave and deprive the state of an important business."[131]

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124. *Paramount Communications*, No. 13,117, 1994 Del. LEXIS 57, at *41-42.
125. *Id.* at *38, *52.
126. *Id.* at *58.
127. *Id.* at *38.
128. *Id.*
129. *Cede & Co.*, 634 A.2d at 350.
130. *See* Revlon v. MacAndrews & Forbes Holdings, 506 A.2d 173 (Del. 1986) (stating that when breakup of a company is inevitable in a bidding contest for control, the board's duties change from preservation of the company as a corporate entity to the maximization of the company's short-term value to the stockholders). The court may have been unwilling to invoke *Revlon* duties in *Technicolor* since the operative transactions in *Technicolor* took place well before *Revlon* was decided.
131. Floyd Norris, *Delaware Law: From a Muddle, Owners Win*, N.Y. TIMES, Nov. 28, 1993, at C1.

3. Under an Entire Fairness Review in a Consensual Merger, Should Directors be Required to Bear the Burden of Showing that the Price was the *Highest Available* under the Circumstances?

The court flatly states that once the presumptions of the business judgment rule have been overcome and the burden shifts to the directors to show entire fairness, the directors, in a transaction involving a sale of the company, have the burden "of establishing that the price offered was the highest value reasonably available under the circumstances."[132]

Why should this be so in a consensual merger? The rule adopted by the court is one of the law of hostile takeovers and the cases cited in support are all hostile takeover decisions.[133] The key case, *Revlon, Inc. v. MacAndrews & Forbes Holdings*,[134] began as a hostile attempt by Pantry Pride to acquire Revlon and evolved into a bidding war between Pantry Pride and Forstmann Little & Co.[135] Various defensive measures were employed by Revlon to fend off Pantry Pride.[136] The court found that at a point well along in the contest, "it became apparent to all that the break-up of the company was inevitable."[137] Then and only then did the court hold that the duty of the directors became one of achieving the highest short-term value for the shareholders.[138] In *Revlon*, the company was already publicly "in play";[139] conducting an auction or its equivalent could cause no further damage to the corporation. This is not so in the case of a consensual merger.[140]

Why in the case of a consensual merger should the application of the entire fairness standard be other than the fair price and fair

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132. *Cede & Co.*, 634 A.2d at 361 (citing *Mills*, 559 A.2d at 1288; *Citron*, 569 A.2d at 67-68).

133. *Id.*

134. 506 A.2d 173 (Del. 1986).

135. *Id.* at 177-78.

136. *Id.* Among the numerous defensive tactics adopted by Revlon were the repurchase of company shares and the adoption of a note purchase rights plan in the nature of a "poison pill." *Id.*

137. *Id.* at 182.

138. *Id.*

139. *See supra* notes 134-138 and accompanying text.

140. Failing to conduct an auction or to announce publicly that the company was for sale was appropriate where directors perceived that by so doing, the value of the company would be diminished. Yanow v. Scientific Leasing, Inc., [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,189, at 91,007 (Del. Ch. July 31, 1991) (noting that "directors were concerned that because [the company] was a 'people business,' a public canvass of the marketplace could adversely affect [the company's] relationships with its employees, customers, and suppliers").

dealing standard of *Weinberger v. UOP, Inc.*?[141] In *Weinberger*, the court held that as to fair price, the thing to be valued was the shareholder's "proportionate interest in a going concern."[142] Value was held to be the true or intrinsic value of the stock taken by the merger, using any techniques or methods which are generally considered acceptable in the financial community.[143] Obviously this value may not be the highest price reasonably available under the circumstances. Why, in a consensual merger, should the directors be bound to find the highest price reasonably available when to do so may serve to put the corporation "in play" and incur adverse unforeseeable consequences for the enterprise?

Interestingly, in *Smith v. Van Gorkom*,[144] a case frequently cited with approval in *Technicolor*, the court held that after the presumptions of the business judgment rule had been overcome, the matter should be remanded to the trial court for an entire fairness hearing in accordance with the principles of *Weinberger*.[145] In this consensual merger, there is no indication that the directors would be held to a standard "of establishing that the price offered was the highest value reasonably available under the circumstances."[146]

4. At the Trial Stage of a Case, Should Proof of Injury be Required to Overcome the Presumptions of the Rule?

Chancellor Allen held that in order to overcome the presumptions of the rule *at trial*, plaintiff must show an injury proximately related to the directors' breach of duty.[147] In the absence of what he believed to be controlling Delaware authority, the chancellor relied on the leading case of *Barnes v. Andrews*,[148] which the supreme court described as "an obscure seventy-year-old decision."[149]

In *Barnes*, a defendant director was found to have breached his duty of care in the supervisory or non-decision-making context.[150]

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141. 457 A.2d 701 (Del. 1983).
142. *Id.* at 713.
143. *Id.*
144. 488 A.2d 858 (Del. 1985).
145. *Id.* at 893.
146. *Cede & Co.*, 634 A.2d at 361 (citing *Mills*, 559 A.2d at 1288; *Citron*, 569 A.2d at 67-68); *Van Gorkom*, 488 A.2d at 878.
147. *Cede & Co.*, 634 A.2d at 370.
148. 298 F. 614 (S.D.N.Y. 1924).
149. *Cede & Co.*, 634 A.2d at 368.
150. *Barnes*, 298 F. at 615.

However, Judge Learned Hand refused to find for the plaintiff because the plaintiff had not proved that the injury to the corporation proximately resulted from the director's breach.[151] The supreme court held, however, that reliance on *Barnes* was "misguided" as "*Barnes*, a tort action, does not control a claim for breach of fiduciary duty."[152]

While it is true that in *Smith v. Van Gorkom* the protection of the rule was denied to the defendant directors absent proof of proximately caused injury,[153] the decision of Chancellor Allen requiring proof of damages is not without merit and perhaps should have been given more consideration by the reviewing court. Why not require plaintiffs to show injury *at the trial stage of a case*, at least in the absence of bad faith, before the presumptions of the rule are overcome and the cause remanded for an entire fairness hearing?

Automatically ordering an entire fairness hearing whenever the protection of the rule is denied can lead to some anomalous results. Assume that a majority of the defendant disinterested and independent directors breached their duty of process due care in approving the sale of a piece of property for a price equal to its fair market value. Assume also that there were no circumstances which would have made the property unusually valuable to the corporation. Under Chancellor Allen's approach, since plaintiff could not show injury to the corporation at trial, the rule would apply and judgment would be granted for defendant. Under the supreme court's approach, however, plaintiff would be held to have rebutted the presumptions of the rule and an entire fairness hearing would be held. Entire fairness requires both fair price and fair process.[154] By assumption, the process was not fair because the directors had not exercised appropriate process due care. But what damage did the corporation suffer since it received what the property was worth? Logic and an

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151. *Id.* at 618. Judge Hand went on to add that "[t]he plaintiff must accept the burden of showing that the performance of the [directors'] duties would have avoided loss, and what loss it would have avoided." *Id.* at 616.

152. *Cede & Co.*, 634 A.2d at 370-71. In *Barnes*, the issue *was* breach of fiduciary duty, but in the non-decision-making context, as opposed to the decision-making context. *Barnes*, 298 F. at 616. Further, if a breach of fiduciary duty is not a tort action, what is it? A contract action?

See W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 1, at 2 (5th ed. 1984) ("Broadly speaking, a tort is a civil wrong, other than breach of contract, for which the court will provide a remedy in the form of an action for damages.").

153. *Van Gorkom*, 488 A.2d at 889.

154. *Cede & Co.*, 634 A.2d at 361. Chancellor Allen defined the term "fair process" as "fair dealing." *Id.*

expeditious administration of justice would seem to be better served by requiring proof of injury at the business judgment phase of the proceeding as held by Chancellor Allen.[155]

C. Other Interesting Aspects of *Technicolor*

The Technicolor decision is helpful in several respects. First, it seems to reaffirm that the business judgment rule protects officers as well as directors.[156] Second, it tends to aid in establishing the applicable standard for directors' conduct in the non-decision-making context; namely, whether it is ordinary or gross negligence.[157]

Van Gorkom made clear the principle that, in the decision-making context, the standard by which the directors' process due care obligation was to be measured was "concepts of gross negligence."[158] However, as to the non-decision-making context, Delaware law is arguably ambiguous. *Graham v. Allis-Chalmers Manufacturing Co.*[159] formulates the duty in reasonably prudent man, or ordinary negligence, terms.[160] Moreover, a later decision, *Rabkin v. Philip A. Hunt Chemical Co.*,[161] expressly held that the standard was ordinary negligence.[162] However, the *Graham* court, in discussing director liability, used "reckless conduct," a term evocative of gross negligence.[163] *Technicolor* helpfully criticizes the *Graham* ordinary negligence formulation, fails

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155. Rightly or wrongly, the rule in *Technicolor* on this point now seems to be firmly embedded in Delaware law. *See* Orban v. Field, No. 12,820, Del. Ch. LEXIS 277, at *2 (Del. Ch. Dec. 30, 1993) (stating that "shareholder plaintiffs have no obligation to plead and to prove causation or injury as part of their complaint").

156. *See id.* Certain commentators have expressed mild concern on this point. *See* A. Gilchrist Sparks, III & Lawrence Hamermesh, *Common Law Duties of Non-Director Officers*, 48 BUS. LAW. 215, 230 (1992) (stating the business judgment rule should also apply to officers to whom the board's discretionary authority is delegated, at least where the officer is discharging such authority).

157. *Cede & Co.*, 634 A.2d at 364 n.31.

158. *Van Gorkom*, 488 A.2d at 873 (adopting the rule of *Aronson*, 473 A.2d at 812 n.6).

159. 188 A.2d 125 (Del. 1963).

160. *Id.* at 130 (stating that "directors of a corporation in managing the corporate affairs are bound to use that amount of care which ordinarily careful and prudent men would use in similar circumstances").

161. No. 7547 (Del. Ch. Dec. 17, 1987), *reprinted in* 13 DEL. J. CORP. L. 1210 (1988).

162. *Id.*, slip op. at 8, *reprinted in* 13 DEL. J. CORP. L. at 1217.

163. *Graham*, 188 A.2d at 130. The court stated that director liability would have been present "[i]f [the director] ha[d] recklessly reposed confidence . . . or ha[d] ignored either willfully or through inattention obvious dangerous signs." *Id.*

to cite *Rabkin*, and seems to interpret *Graham* as requiring a gross negligence standard.[164]

III. CONCLUSION

The *Technicolor* court had an opportunity to clarify and to strengthen the law of corporate governance in a number of important areas. However, this did not happen and instead, the decision may become a source of serious confusion.

In its treatment of the duty of loyalty, the court first blurred the well-established distinction between disinterest and independence. In addition, the court failed to speak decisively on the impact of minority "interested" or "dominated" directors on the ability of the majority to act under the protection of the business judgment rule. The court could have held on the record, but did not, that only when a minority director can be shown to have *dominated* the majority, will the minority director "taint" the ability of the majority to act under the protection of the rule.

In its treatment of the duty of care, the court unwisely expanded the meaning of due care as a component of the business judgment rule by the use of inapposite hostile takeover case law, and also by the use of such case law, redefined the fair price component of entire fairness in a consensual merger. Furthermore, the court rejected a salutary approach developed by the chancellor, which would have required plaintiffs at trial to show injury in the business judgment rule aspect of a case before proceeding to an entire fairness hearing.

While the court did, to some degree, clarify the applicability of the business judgment rule to officers, and also gave support to a gross negligence standard in the non-decision-making context, the opinion, as a whole, is a backward step in the quest for sound and well-articulated rules of corporate law. Hopefully, the court will see fit to address the problems of *Technicolor* in future decisions. This process has already begun with finely crafted decisions in *Blasband v. Rales*[165] and *Paramount Communications Inc. v. QVC Network Inc.*[166]

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164. *Cede & Co.*, 634 A.2d at 364 n.31. The court found the *Graham* formulation "confusing and unhelpful." *Id.* In addition, the court reaffirmed that *Graham* was not a business judgment rule case and was not applicable to the breach of the duty of loyalty standard. *Id.* (citations omitted).

165. 634 A.2d 927 (Del. 1993).

166. No. 13,117, 1994 Del. LEXIS 57 (Del. Feb. 4, 1994).