Commentaries from the Bar

1987 DEVELOPMENTS IN DELAWARE CORPORATE LAW

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I. INTRODUCTION

In decisions rendered in 1987, Delaware courts made important rulings concerning fiduciary duty principles and issues arising under the Delaware General Corporation Law (GCL).¹ The GCL was also amended in 1987 in several important respects. These recent decisions and statutory amendments are important to corporate legal advisors and to anyone involved in the management of a Delaware corporation.

This article summarizes developments in Delaware corporate law during 1987. While summarization of the extensive body of Delaware corporate law and review of every Delaware corporate decision in 1987 are beyond the scope of this article, a wide range of the corporate issues addressed by the Delaware Court of Chancery and the Delaware Supreme Court will be considered. The amendments to the GCL in several important areas will also be reviewed.

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II. Case Law

A. The Internal Affairs Doctrine: McDermott, Inc. v. Lewis

Among the most important tenets of Delaware corporate law is the internal affairs doctrine, which provides that "the law of the state of incorporation should determine issues relating to internal corporate affairs."12 In McDermott, Inc. v. Lewis,3 the Delaware Supreme Court reaffirmed the vitality of the internal affairs doctrine in holding that "a Delaware subsidiary of a Panamanian corporation may vote the shares it holds in its parent company under circumstances which are prohibited by Delaware law, but not by the law of Panama."4 The plaintiffs, stockholders of the Delaware subsidiary, sought to enjoin or rescind a reorganization under which the Delaware corporation became a 92%-owned subsidiary of a Panamanian corporation. The Delaware corporation emerged from the reorganization owning approximately 10% of the stock of the Panamanian corporation. The plaintiffs conceded that the issues in the case did not involve the internal affairs of the Delaware subsidiary5 and did not offer evidence with respect to whether the law of Panama permitted the Delaware subsidiary to vote its shares in its parent corporation.6

The court found that Delaware's "well established" conflict of laws principles required that the laws of the jurisdiction of incorporation govern the dispute involving voting rights in the Panamanian corporation.7 Among the considerations critical to the court's con-

3. 551 A.2d 206 (Del. 1987).
4. Id. at 208-09. The court decided the appeal, even though a change in circumstances had rendered the appeal technically moot, because of "the importance of [the] matter to Delaware corporation law." Id. at 211-12.
5. Id. at 209.
6. Id. at 211. Plaintiffs relied on Norlin Corp. v. Rooney, Pace, Inc., 744 F.2d 255 (2d Cir. 1984), which prohibited "a similar device" involving a Panamanian subsidiary seeking to vote the shares it held in the Panamanian parent. McDermott, 531 A.2d at 209. The supreme court declined to follow Norlin. Id. The court relied instead on the affidavits and opinion letters of a Panamanian attorney and the deans of two Panamanian law schools, setting forth a statement of the applicable Panamanian law. Id. at 209-10.
clusion were that the internal affairs doctrine serves the vital need for a constant law to avoid fragmentation of continuing, interdependent internal relationships, facilitates planning and fosters predictability.

Given the significance of these considerations, application of the internal affairs doctrine is not merely a principle of conflicts law. It is also one of serious constitutional proportions—under due process, the commerce clause and the full faith and credit clause—so that the law of one state governs the relationships of a corporation to its stockholders, directors and officers in matters of internal corporate governance. The alternatives present almost intolerable consequences to the corporate enterprise and its managers. With the existence of multistate and multinational organizations, directors and officers have a significant right, under the fourteenth amendment's due process clause, to know what law will be applied to their actions.8

The court also found support for its holding in recent decisions of the United States Supreme Court concerning state antitakeover laws—Edgar v. MITE Corp.9 and CTS Corp. v. Dynamics Corp. of America.10 The Delaware court concluded: "[W]e believe that full faith and credit commands application of the internal affairs doctrine except in the rare circumstance where national policy is outweighed by a significant interest of the forum state in the corporation and its shareholders."11 The court also concluded that application of Delaware voting principles to the Panamanian corporation would violate the commerce clause since the foreign corporation could conceivably be subjected to the different laws of all fifty states on matters relating to corporate governance.12

B. Target Company Responses to Takeovers

1. Ivanhoe Partners v. Newmont Mining Corp.

In 1987, the supreme court continued its examination of the propriety of various responses by a target's board of directors to a

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8. McDermott, 531 A.2d at 216.
10. 481 U.S. 69 (1987); McDermott, 531 A.2d at 217 & n.12.
11. McDermott, 531 A.2d at 218 (footnote omitted).
12. Id. at 218-19.
hostile acquisition and the threat to control.\textsuperscript{13} In \textit{Ivanhoe Partners v. Newmont Mining Corp.},\textsuperscript{14} the court addressed certain defensive maneuvers which were taken in a battle for control of Newmont Mining Corporation (Newmont). In an attempt to block a hostile tender offer by entities controlled by T. Boone Pickens, Jr. (Ivanhoe), Newmont declared a $33 per share dividend to all its stockholders. That dividend helped its largest stockholder, Consolidated Gold Fields PLC (Gold Fields), to engage in a "street sweep"\textsuperscript{15} of Newmont stock, thereby increasing its ownership of Newmont from 26\% to 49.7\%.\textsuperscript{16}

Facts relating to a prior attempt by Gold Fields to acquire a large position in Newmont's stock were significant to the court's consideration of Newmont's response to the Ivanhoe takeover attempt. After Gold Fields began acquiring Newmont stock in 1981, Newmont agreed to allow Gold Fields to purchase up to one-third of the stock in return for Gold Fields' entry into a standstill agreement. Of particular significance in the standstill agreement was the provision which allowed Gold Fields to terminate the agreement upon acquisition by a third party of 9.9\% of Newmont's outstanding stock.\textsuperscript{17}

Once the Ivanhoe group increased its Newmont holding to over 9.9\%, thereby freeing Gold Fields to terminate the standstill agreement, Newmont began implementing traditional defensive mechanisms.\textsuperscript{18} In doing so, "Newmont found itself in the peculiar position of having simultaneously to fear and to court Gold Fields."\textsuperscript{19}

In late August and early September of 1987, Ivanhoe requested a meeting with Newmont in order to discuss the possible acquisition

\begin{itemize}
    \item \textsuperscript{13} Earlier cases in which the supreme court considered responses of the target's directors to a hostile takeover attempt are Revlon, Inc. v. MacAndrews & Forbes Holdings, 506 A.2d 173 (Del. 1986) and Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).
    \item \textsuperscript{14} 535 A.2d 1334 (Del. 1987).
    \item \textsuperscript{15} "Street sweep' refers to the rapid acquisition of securities on the open market during and shortly after the pendency of a tender offer for the same class of securities. The shares are ordinarily purchased at a premium from arbitrageurs." \textit{Id.} at 1337 n.3. Street sweeps have been unsuccessfully challenged as a violation of the Williams Act. \textit{See} Hanson Trust Plc v. SCM Corp., 774 F.2d 47 (2d Cir. 1985); SEC v. Carter Hawley Hale Stores, Inc., 760 F.2d 945 (9th Cir. 1985).
    \item \textsuperscript{16} \textit{Ivanhoe}, 535 A.2d at 1337.
    \item \textsuperscript{17} \textit{Id.} at 1338.
    \item \textsuperscript{18} \textit{Id.} The Newmont board approved "golden parachute" severance agreements for 25 management employees and a $2.25 billion revolving credit agreement which provided for default of the loans if an entity acquired 50\% or more of Newmont. \textit{Id.} at 1338-39 & n.7.
    \item \textsuperscript{19} \textit{Id.} at 1338.
\end{itemize}
by Ivanhoe of all of Newmont's common stock. Ivanhoe also sought to discuss "a broad range of alternatives" with Gold Fields concerning the disposition of its Newmont stock. After receiving no satisfactory response, Ivanhoe commenced a hostile tender offer on September 8 for 42% of Newmont's stock at $95 per share. The tender offer was contingent upon, among other things, Ivanhoe's obtaining financing.20

Based in part upon a presentation by its financial adviser, the Newmont board determined that the $95 offer was inadequate. Ivanhoe's actions then provoked further reaction by Newmont. In response to Ivanhoe's attempt to remove Newmont's board by shareholder consent, Newmont's directors amended the company's bylaws to delay the effect of any consent solicitation for twenty days. The board also began exploring alternatives with Gold Fields to discourage it from terminating the standstill agreement and proposed an aggressive business and capital program which included the disclosure of liberal estimates of reserves and a corresponding increase of 50% in the corporation's gold production estimates.21

Newmont also proposed a "restructuring" in response to the threats posed by Gold Fields and Ivanhoe. Newmont's proposal envisioned the declaration of a large dividend to be financed by the sale of Newmont's non-gold assets, and the signing of a new standstill agreement with Gold Fields to ensure Newmont's independence. The court found that "the purpose of the dividend was to reduce liquidity, thus making Newmont a less attractive target, to distribute the value of its non-gold assets to all of the shareholders (including Ivanhoe), and to facilitate Gold Fields' street sweep."22 The proposed new standstill agreement was designed to limit Gold Fields' control of Newmont in order to assure Newmont's continued independence. On September 21 and 22, Gold Fields, "consistent with the terms of the accord, and facilitated by the dividend, swept the street" by purchasing approximately 15.8 million Newmont shares at an average price of $98 per share, thereby increasing its position to 49.7% of Newmont's stock.23

The court began its analysis of the various defensive measures by noting that "[b]ecause Newmont's actions here are so inextricably related, the principles of Unocal require that they be scrutinized

20. Id. at 1339.
21. Id.
22. Id. at 1339-40.
23. Id.
collectively as a unitary response to the perceived threats.” 24 In addition, “for the purpose of evaluating the fiduciary duties of Newmont, [the court viewed] the street sweep as part of Newmont's own comprehensive strategy.” 25

The court affirmed the court of chancery's conclusion that:

the decisions of Newmont's board to facilitate the street sweep by issuance of the dividend, and to consumate [sic] a new standstill agreement, were taken in good faith after reasonable investigation in response to threats by both Gold Fields and Ivanhoe to Newmont's corporate policy and effectiveness. Under the circumstances, Newmont had both the power and the duty to oppose Ivanhoe's tender offer. The record also sustains the conclusion that these defensive measures were reasonable in relation to the threats posed, and that the board acted to meet them in the proper exercise of its sound business judgment. Further, the Revlon obligation to conduct a sale of the corporation did not arise under the circumstances here. Newmont was not for sale. Thus, there was no duty of its directors to maximize “the company's value at a sale for the stockholders' benefit.” Accordingly, there being no entrenchment, the defensive measures adopted by Newmont are protected by the business judgment rule. 26

2. Bershad v. Curtiss-Wright Corp.

Delaware courts also addressed claims arising under the supreme court's 1986 decision in Revlon 27 in several other cases in 1987. In Bershad v. Curtiss-Wright Corp., 28 the supreme court rejected a claim that Revlon requires a majority shareholder to sell its stock in a subsidiary to the highest bidder. 29 The court recognized the rights of majority stockholders in such circumstances:

24. Id. at 1343. The court read Unocal as requiring it “to carefully assess the reasonableness of the defensive measures employed and the results achieved.” Id. at 1342-43.
25. Id. at 1343.
26. Id. at 1337-38 (footnotes and citations omitted).
27. 506 A.2d 173 (Del. 1986).
29. Id. at 841-42. Plaintiff challenged the 1979 cash-out merger of Dorr-Oliver Incorporated (Dorr-Oliver) by its parent, Curtiss-Wright Corporation (Curtiss-Wright). Prior to the merger, Curtiss-Wright owned approximately 65% of Dorr-Oliver's outstanding common stock. Id. at 842.
Stockholders in Delaware corporations have a right to control and vote their shares in their own interest. They are limited only by any fiduciary duty owed to other stockholders. It is not objectionable that their motives may be for personal profit, or determined by whim or caprice, so long as they violate no duty owed other shareholders. Clearly, a stockholder is under no duty to sell its holdings in a corporation, even if it is a majority shareholder, merely because the sale would profit the minority.30


In Freedman v. Restaurant Associates Industries, Inc.,31 the plaintiffs sought an order, in effect, requiring a corporation, which was the target of a management-sponsored leveraged buy-out,32 to grant an

30. Id. at 845 (citations omitted). The court also held that the defendants were under no duty to disclose the substance of their discussions concerning possible acquisition of Dorr-Oliver or casual inquiries concerning Dorr-Oliver. The court stated that:

[efforts by public corporations to arrange mergers are immaterial under the Rosenblatt v. Getty standard, as a matter of law, until the firms have agreed on the price and structure of the transaction. See Flamm v. Eberstadt, 814 F.2d 1169, 1174 (7th Cir. 1987); Greenfield v. Heublcn, Inc., 742 F.2d 751, 756-58 (3d Cir. 1984); Reiss v. Pan American World Airways, Inc., 711 F.2d 11, 14 (2d Cir. 1983); Staffin v. Greenberg, 672 F.2d 1196, 1204-07 (3d Cir. 1982). Cf. Levinson v. Basc, Inc., 786 F.2d 741, 746 (6th Cir. 1986), cert. granted, U.S. , 107 S. Ct. 1284 (1987). Since it is undisputed that: (1) Dorr-Oliver was not for sale, and (2) no offer was ever made for Dorr-Oliver, the defendants were not obligated to disclose preliminary discussions regarding an unlikely sale.

Id. at 847 (footnote omitted).

This bright line rule is useful. First, the effect of premature disclosure of merger discussions may be substantial. The probability of completing a merger benefiting all shareholders may well hinge on secrecy during the negotiation process. Second, the benefits of certainty supply additional support for a price and structure standard. Without this bright line standard, it would be very difficult for those responsible individuals to determine when disclosure should be made. Regardless of when disclosure is made, some investors will always argue that disclosure should have been made earlier. See Flamm v. Eberstadt, 814 F.2d 1169, 1175-78 (7th Cir. 1987).

Id. at 847 n.5.


32. The court found that voting control of Restaurant Associates Industries, Inc. (Restaurant) was "effectively held in the hands of a group controlling the management of the Company." Id., slip op. at 3-4, reprinted in 13 Del. J. Corp.
option to acquire shares of the company to a third party with an interest in making a competing bid.\textsuperscript{33} Plaintiffs claimed that such relief was required under \textit{Revlon} since certain directors of the company, who controlled approximately 48\% of the voting power of the company’s stock, had acted in that capacity to advance their own interests as buyers of the company’s stock and had foreclosed the development of a competing bid at a higher price.\textsuperscript{34} The plaintiffs viewed \textit{Revlon} as compelling a board whose company is for sale to take affirmative steps that are necessary to maximize the return to stockholders in the sale.\textsuperscript{35}

\textit{L.} at 654. The group controlled about 37\% of the voting power of Restaurant’s stock even though its aggregate holding amounted to 23\% of Restaurant’s outstanding shares. \textit{Id.}

The management group made a public announcement that it intended to make a cash offer of $14 per share for all of Restaurant’s outstanding shares on August 26, 1987. A special committee of independent directors was formed to evaluate proposals. The special committee hired legal counsel and retained Prudential-Bache Capital Funding (Prudential) to provide it with expert advice. \textit{Id.}, slip op. at 5-6, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 655-56. Then, on September 2, the special committee received a competing proposal from AWR Acquisition Corp. (AWR) for a merger at $16.50 cash per share. \textit{Id.}, slip op. at 6, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 656. On September 3, the special committee rejected the $14 offer as unfair in view of Prudential’s tentative conclusion that the fair value of Restaurant was between $15-$18 per share. \textit{Id.}, slip op. at 7, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 656. After further discussions involving the bidders and the special committee, AWR confirmed a $19 per share offer on September 8, subject to certain due diligence and financing conditions. \textit{Id.}, slip op. at 8-9, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 657. Meanwhile, the management group decided that it might raise its offer to as high as $16 per share. \textit{Id.}, slip op. at 8, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 657.

\textit{Id.}, slip op. at 10-11, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 658. Then, on September 12, the special committee and the management group reached agreement on an offer of $18 per share to the public shareholders and $15 to the management shareholders. AWR was advised that further proposals were not precluded by the agreement. \textit{Id.}, slip op. at 11-12, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 658-59.

AWR then raised its offer to $20 on September 16, conditioned on the signing of a merger agreement, the completion of a due diligence investigation, the completion of financing and the receipt of two options. \textit{Id.}, slip op. at 12, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 659. The special committee decided not to consider AWR’s bid until completion of its due diligence investigation. Finally, AWR made a public statement on September 22 that it had sold much of its interest in Restaurant’s stock and did not contemplate renewal of its offer. \textit{Id.}, slip op. at 13-14, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 659-60.

\textsuperscript{33} \textit{Id.}, slip op. at 1-2, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 653.

\textsuperscript{34} \textit{Id.}, slip op. at 17, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 661.
The court concluded that the supreme court's opinion in *Unocal Corp. v. Mesa Petroleum Co.*\(^{36}\) suggested that:

a board, in order to attempt to achieve the highest available price for the shareholders (in a setting where it appears that the public shareholders are to be eliminated by one technique or another), might be justified in issuing an option that would have the effect of diluting the voting power of an existing block.\(^{37}\)

Nevertheless, the court found that the decision of a special committee of the target's directors, which had been formed to review the competing proposals, not to recommend the granting of an option was a proper exercise of business judgment.\(^{38}\)

Heavy reliance is placed upon the acts of specially constituted committees of disinterested directors when Delaware courts are asked to review the propriety of corporate transactions that involve elements or claims of self-dealing. While that reliance may, given the informal relations that may exist between board members, be seen as providing a possible escape-hatch for the unprincipled, cases such as this demonstrate that this technique of negotiation, when pursued in good faith, is a close surrogate for the structure that ordinarily provides protection to shareholders. Here there is no structural reason to doubt the effectiveness of the independent committee—it was appropriately constituted, well advised and active. Moreover, the results it achieved bespeak an aggressive and effective attempt to maximize public shareholder values.\(^{39}\)

\(^{36}\) 493 A.2d 946 (Del. 1985).


\(^{38}\) *Id.*, slip op. at 21-23, *reprinted in* 13 Del. J. Corp. L. at 663-64. The court noted that it had “no special expertise” in judging the wisdom of incurring the risks that further pursuit of AWR’s proposals would have entailed. “[O]ne of the important reasons for the existence of the business judgment rule is the institutional incompetence of courts to pass upon the wisdom of business decisions.” *Id.*, slip op. at 23, *reprinted in* 13 Del. J. Corp. L. at 664.

\(^{39}\) *Id.*, slip op. at 21 (citation omitted), *reprinted in* 13 Del. J. Corp. L. at 663.

The court of chancery preliminarily enjoined mergers or tender offers in a number of cases in 1987. In *Sealy Mattress Co. of New Jersey, Inc. v. Sealy, Inc.*, the court preliminarily enjoined a proposed cash-out merger of Sealy, Inc. (Sealy) into a wholly-owned subsidiary of Ohio-Sealy Mattress Manufacturing Co. (Ohio-Sealy), Sealy’s majority stockholder. The consideration proposed to be paid was an amount equal to Sealy’s book value. In granting the injunction, the court noted that “if one were setting out to write a textbook study on how one might violate as many fiduciary precepts as possible in the course of a single merger transaction, this case would be a good model.”

For sixteen years prior to the proposed merger, Ohio-Sealy had been involved in antitrust litigation against Sealy and certain of its licensees. In mid-1986, Ohio-Sealy obtained a verdict of $27 million against Sealy and certain Sealy licensees that collectively owned approximately 58% of Sealy’s stock. In response to the judgments and new antitrust litigation filed by Ohio-Sealy in 1986, the antitrust defendant licensees sold their businesses and interests in Sealy to Ohio-Sealy. Ohio-Sealy insisted upon allocating book value to the acquired licensees’ Sealy stock, even though at least several of the licensees believed that the Sealy stock, standing alone, was worth significantly more.

Meanwhile, several events had occurred which supported the claim that Sealy’s book value of approximately $58 million was considerably less than its fair value. Salomon Brothers, Inc. had valued Sealy at $140-160 million in July of 1986 in connection with

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40. 532 A.2d 1324 (Del. Ch. 1987).
41. Id. at 1326. More than 93% of Sealy was owned by Ohio-Sealy. Id.
42. Id. at 1326. The proposed consideration was $178.46 in cash per share, representing Sealy’s book value as of December 31, 1986. Id.
43. Id. at 1335.
44. Id. at 1327. “Because Ohio-Sealy would be taking control of Sealy, Ohio-Sealy’s counsel requested the federal court in the antitrust litigation to defer ruling upon the antitrust defendants’ post-trial motions challenging the antitrust judgments.” Id. at 1328. The court agreed to the request. “Ohio-Sealy’s counsel also instructed Sealy’s antitrust counsel to take no further action to challenge the verdicts.” Id.
45. Id. at 1327-28.
46. Id. at 1328. The court found that “the licensees did not oppose allocating book value as the agreed price for their Sealy stock because the overall purchase price for the combined assets [they sold] was acceptable to them” and the manner in which the price was allocated was not important to them. Id.
assisting the antitrust defendants in meeting security and bond requirements. In November 1986, competing bidders each made offers of over $150 million to acquire Sealy.

Sealy's directors held a meeting by telephone to approve the merger on January 21, 1987. The book value merger price was presented to the directors as a fait accompli; the only document the directors received was a copy of the resolutions. The price was accepted with no discussion as to its basis or adequacy, no disclosure of the Salomon Brothers valuation or other merger proposals, no disclosure by one director to his fellow directors that he thought the Sealy name alone might be worth as much as $300 million, no discussion of the value of the antitrust judgments, and no representation of the interests of the minority stockholders by an investment banker or committee of disinterested directors.

Since Sealy stood on both sides of the transaction and fixed its terms, the court recognized that the defendants had "the burden of establishing the entire fairness of the merger, i.e., the 'most scrupulous inherent fairness of the bargain,' sufficient to pass the test of careful scrutiny by the courts." The court found "substantial (and disturbing) evidence that Sealy's fair value is significantly higher than the $58 million book value price being offered in the merger."

The court also found violations of the defendants' duty of fair dealing in connection with their timing of the merger to occur at a time when valuation of Sealy was difficult as a result of the defendants' refusal to permit post-trial review of the antitrust judgments. Regarding the failure to retain an investment banker or establish a committee of disinterested directors to represent the minority stockholders, the court found that:

the minority stockholders were left exposed to the discretion of a majority stockholder whose interests were in direct conflict with theirs and whose approach to these matters

47. Id. at 1329.
48. Id.
49. Id. at 1330.
50. Id.
51. The court noted the existence of "evidence that the value of the judgments was less than the $122 million gross amount of the verdict." Id.
52. Id.
53. Id. at 1333. See Weinberger v. UOP, Inc., 457 A.2d 701, 710 (Del. 1983).
54. Sealy, 532 A.2d at 1334.
55. Id. at 1336.
was, and has continued to be, unremittingly hostile. The absence of these procedural safeguards, while not actionable of themselves, is highly persuasive evidence that the merger terms were the product of unfair dealing.56

The court also found violations of the defendants' duty of fair dealing in the uninformed board approval of the merger,57 and failure to disclose all material facts relating to the merger.58 As to the inadequate disclosure, the court rejected the defendants' claim that discovery in the action cured any disclosure deficiencies.

If that were the law no disclosure claim would ever succeed, because discovery of the proof of the merit of a disclosure claim would destroy its validity. Moreover, the disclosure burden owed by the fiduciary would be thrust upon the beneficiary to whom the duty is owed. The duty of candor must be discharged by the fiduciary directly to the beneficiary stockholder in the transaction itself, and not by the fiduciary's lawyer to the beneficiary's lawyer in the context of litigation.59

5. Eisenberg v. Chicago Milwaukee Corp.

In Eisenberg v. Chicago Milwaukee Corp.,60 the court of chancery preliminarily enjoined a self-tender offer for any and all shares of the offeror's $5 Prior Preferred Stock61 based on various disclosure de-

56. Id. at 1337.
57. Id. at 1337-38. "Before making a business decision, the directors of a corporation, in discharging their duty of care, must inform themselves of all available material information." Id. at 1337. See Smith v. Van Gorkom, 488 A.2d 858, 872-73 (Del. 1985).
58. Scaly, 532 A.2d at 1338-40. "[T]he defendants had a fiduciary obligation to disclose all material facts in an atmosphere of complete candor." Id. at 1338. See Rosenblatt v. Getty Oil Co., 493 A.2d 929, 944 (Del. 1985). The need for full disclosure is even more important where, as here, "the defendants control the outcome of the vote on the merger and seek to force [its] involuntary acceptance." Scaly, 532 A.2d at 1338 (citing Wacht v. Continental Hosts, Ltd., No. 7954 (Del. Ch. Apr. 11, 1986), reprinted in 12 Del. J. Corp. L. 418 (1987)).
59. Scaly, 532 A.2d at 1340.
61. Id., slip op. at 9-10, reprinted in 13 Del. J. Corp. L. at 1140. The court determined that supplemental notices, containing the information the court found should be disclosed, should be sent to shareholders. Id., slip op. at 29, reprinted in 13 Del. J. Corp. L. at 1151-52.
ficiencies and certain coercive aspects of the offer. In reviewing the standard by which disclosure in a self-tender offer is to be measured, the court stated that "[w]here a corporation tenders for its own shares, the exacting duty of disclosure imposed upon corporate fiduciaries is even 'more onerous' than in a contested offer. That is because in a self-tender, the disclosures are unilateral and not counterbalanced by opposing points of view." The court found disclosure deficiencies in a number of areas. For example, the offering materials suggested that company directors made a considered business judgment, unrelated to stock market price considerations, to conduct the offer in order to reduce costs. This was an inaccurate impression since the self-tender's purpose was "plainly and simply" to enable the issuer to take advantage of the unprecedented "Black Monday" stock market crash that drove down the price of the preferred stock to its lowest level in five years.

Incomplete disclosure was also implicated in the circumstances surrounding a fairness opinion issued by Paine Webber. While Paine Webber's opinion "was given considerable prominence, the fact that [its valuation] work was done over a single long weekend was not disclosed." The court noted that the "need for such a presentation would appear even more essential, because the directors had concluded that the Offer was fair, yet decided not to recommend that the shareholders tender into it."

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62. Prior decisions of Delaware courts indicate that:

two classes of situations have arisen that have been found to deprive a tender offer of its voluntary character: (i) cases involving materially false or misleading disclosures made to shareholders in connection with the offer (e.g., Lynch v. Vickers Energy Group, 383 A.2d at 281; Kahn v. United States Sugar Corp., Del. Ch., C.A. No. 7313, Hartnett, V.C. (December 10, 1985) at 14; Joseph v. Shell Oil Company, Del. Ch., 482 A.2d 335, 342 (1984)), and (ii) cases where the offer, by reason of its terms or the circumstances under which it is made, is wrongfully coercive. (See Kahn v. United States Sugar Corp., supra at 15-16; AC Acquisitions Corp. v. Anderson Clayton & Co., Del. Ch., 519 A.2d 103, 114 (1986).)

Eisenberg, No. 9374, slip op. at 11 (footnote omitted), reprinted in 13 Del. J. Corp. L. at 1141.


64. Id., slip op. at 17, reprinted in 13 Del. J. Corp. L. at 1145. The record evidence indicated that the post-stock-market-crash price level of the preferred stock "was the predominant, if not the sole, factor motivating the directors' decision to make the Offer." Id., slip op. at 6, reprinted in 13 Del. J. Corp. L. at 1137.


The offer also failed to adequately disclose that some of the directors "had a potential conflict of interest by reason of their ownership of significant amounts of [the company's] common stock."67 The directors increased the amount of common shareholders' equity remaining in the company by decreasing the amount paid for the preferred stock in the offer.68

The court also concluded that telling the preferred shareholders that the issuer "intends to request delisting of the Shares from the NYSE" was a disclosure that made "the Offer, even if benignly motivated, operate[] in an inequitably coercive manner."69 According to the court, "[t]he only apparent purpose of such a disclosure would be to induce shareholders to tender by converting a possibility of delisting into a likelihood or certainty."70


The court of chancery also considered other claims that directors were manipulating the corporate machinery for their own benefit. The court granted a preliminary injunction against such alleged unlawful manipulation of corporate machinery in Phillips v. Insituform of North America, Inc.71 The plaintiffs, receivers of certain Class B shares of defendant Insituform of North America, Inc. (INA),72 sought an order enjoining a proposed merger that would recapitalize INA and a declaratory judgment that certain recent actions of the INA board were invalid.73 Plaintiffs sought an order declaring invalid several

67. Id., slip op. at 22, reprinted in 13 Del. J. Corp. L. at 1147. A successful offer would have benefitted those directors by increasing the book value of their common stock by $3.5 million. Id., slip op. at 22, reprinted in 13 Del. J. Corp. L. at 1148.


72. The plaintiff-receivers "were appointed by order of the Chancery Division of the English High Court of Justice and thereafter were instructed by that court to institute this action." Id., slip op. at 1, reprinted in 13 Del. J. Corp. L. at 777.

73. Id. INA's common stock consisted of two classes. "The rights, powers and privileges of each class are identical except that the holders of Class B [stock] are entitled to elect 2/3 of the board of directors of the Company." Id., slip op. at 4, reprinted in 13 Del. J. Corp. L. at 778. The proposed merger would have had the effect of eliminating the Class B stock. Id., slip op. at 11, reprinted in 13 Del. J. Corp. L. at 782.
bystlaw amendments and the sale of sufficient Class B stock to INA’s chief executive officer to remove control of the vote of the Class B stock (and, thus, under INA’s structure, control of the company’s board) from the block of Class B shares held by the receivers. The Class B shareholders claimed that the defendants were attempting to deprive them of rights provided by INA’s certificate of incorporation and that the directors were acting to protect their positions and to thwart plaintiffs’ exercise of their lawful rights.

As to allocation of the burden of proof in the action, the court concluded that:

the extraordinary step of a corporation acting solely or primarily for the express purpose of depriving a shareholder of effective enjoyment of a right conferred by law, requires, when challenged, the board to demonstrate that the action taken was fair or justified given the particular business purpose sought to be achieved and the circumstances of the firm.

The court noted that the defendants’ burden was “somewhat difficult” because the Class B stockholders did not represent a hostile outside entity that had only recently become a stockholder.

After reviewing prior Delaware cases dealing with issuance of stock that has the effect of reducing the voting power of a specific stockholder, the court concluded that no justification had been shown

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74. The bylaw amendments accomplish several things. They (a) determine that a quorum of the board is present only when a majority of the two Class A directors are present; (b) dictate that the board may act only with the concurrence of a majority of the two Class A directors; (c) constitute the Class A directors and the Chairman of the Board as an executive committee with power to call meetings, jurisdiction over certain matters relating to officers and power to call shareholder meetings; and (d) require that any newly created directorship be filled by a majority vote of stockholders of the class entitled to elect and not by directors. Id., slip op. at 12, 26-27, reprinted in 13 Del. J. Corp. L. at 783, 790.

75. Id., slip op. at 1, reprinted in 13 Del. J. Corp. L. at 777.

76. Id., slip op. at 2, reprinted in 13 Del. J. Corp. L. at 777-78.

77. Id., slip op. at 16, reprinted in 13 Del. J. Corp. L. at 785.


to indicate that "the extraordinary step of issuance of stock for the admitted purpose of impeding the exercise of stockholder rights [was] reasonable in light of [any] corporate benefit . . . sought to be obtained." The court held that the issuance of the shares was "an unjustified and invalid corporate act." With respect to the amended bylaws, the court found that a "realistic evaluation" indicated that a fundamental shift in the allocation of power between the two classes of shareholders had taken place "and that that new arrangement is inconsistent with what would have been the reasonable understanding of the effect of the provisions of the certificate." In adopting this interrelated series of amendments, the board became, or rather continued as, intense partisans waging war against the Class B stockholders. Whether regarded as individual owners of Class A stock, as office-holders acting pursuant to a plan to remove the supervising power of control shares (with a concomitant entrenchment effect) or simply as directors choosing to favor the A shares over the B shares, this particular exercise of the legal power to enact by-laws, in this setting, requires a specific justification. . . . I am persuaded that no reasonable apprehension of injury to legitimate corporate interests has been put forward that would justify, in these circumstances, this exercise by the board of the power conferred on it by the charter to amend by-laws. Nor does it appear that any palpable corporate benefit was actually a motivating force for these amendments.

The court concluded that equity required the return pendente lite of the bylaws as they existed prior to the challenged amendments.

Inc., No. 9212 (Del. Ch. Oct. 16, 1987), reprinted in 13 Del. J. Corp. L. 651 (1988), the court read Phillips as suggesting "that issuing stock for the sole or primary purpose of diluting the power of an existing voting block may, in extraordinary circumstances, be valid if the purpose of the issuance is to further an independent corporate purpose rather than to entrench an existing board . . . ." Phillips, No. 9173, slip op. at 25-26, reprinted in 13 Del. J. Corp. L. at 665.

81. Id. at 789.
82. Id., slip op. at 28-29, reprinted in 13 Del. J. Corp. L. at 791.
84. Id., slip op. at 33, reprinted in 13 Del. J. Corp. L. at 793.

In *Smith v. SPNV Holdings, Inc.*, the court of chancery considered a motion to dismiss a claim that SPNV Holdings, Inc. (Holdings) had unfairly timed a freeze-out merger of Shell Oil Company (Shell) to the detriment of Shell’s minority shareholders. On May 31, 1985, Shell declared its $.50 per share quarterly dividend payable to shareholders of record on June 10, 1985. The declaration stated that the dividend would not be paid to the minority shareholders if the merger of Shell into Holdings took place prior to June 10, 1985. Since the merger was consummated on June 7, the dividend of approximately $8 million became the property of Holdings. The court found that:

> [t]he net result of this manipulation was that Shell Oil Company or its subsidiaries did not have to pay $8 million to the minority stockholders and therefore had the benefit of the use of the minority stockholders equity for a quarter of a year without paying any dividend or other consideration.

Relying on the established principles of Delaware law that "*[m]ere technical compliance with legal parameters . . . does not permit inequitable conduct*" and that "the timing of a merger to favor the majority can lead to a cause of action for unfair dealing," the court found that a breach of fiduciary duty could have occurred. The court denied defendants’ motion to dismiss the complaint.

8. *American General Corp. v. Texas Air Corp.*

The court also addressed considerations of unfair dealing and price in a merger in *American General Corp. v. Texas Air Corp.* Plaintiffs

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86. Id., slip op. at 2, reprinted in 13 Del. J. Corp. L. at 1244.

87. Id., slip op. at 6, reprinted in 13 Del. J. Corp. L. at 1246.


challenged a proposed going-private merger whereby Texas Air Corporation (Texas Air), the holder of 72% of the stock of Continental Airlines Corporation (Continental), sought to cash out the minority shareholders of Continental for $16.50 per share.92

While earlier merger proposals by Texas Air had been structured to require an affirmative vote of a majority of the minority stockholders of Continental, that condition was not part of the Texas Air proposal presented to stockholders.93 The court found that the members of a special committee of Continental directors had been issued an ultimatum at the end of their negotiations with Texas Air indicating that the transaction would proceed without their input if they did not accept the $16.50 merger price.94 The court also found that other facts, including the structuring of the transaction in such a way as to jeopardize certain warrant rights95 and the probability “that the market price of Continental’s shares ha[d] been intentionally capped since July of 1985 when Texas Air first indicated that it intended to take Continental private,”96 “seem[ed] to indicate a lack of good faith and fair dealing on behalf of at least some of the defendants.”97

Nevertheless, the court refused to preliminarily enjoin the merger after concluding that “any unfairness in structuring the deal resulted in an unfair price and [could] best be addressed when the issue of price is determined” in an appraisal proceeding or otherwise.98

9. Lieb v. Clark

In Lieb v. Clark,99 the court of chancery declined to enjoin a tender offer made jointly by the company and an ESOP for 47% of

93. Id., slip op. at 7, reprinted in 13 Del. J. Corp. L. at 179. Although there is no legal requirement that such a transaction be subject to veto by a majority of the minority shareholders, “such a provision is preferable and if it exists and the majority of the minority approve the merger the burden of showing its unfairness shifts to an objector.” Id., slip op. at 17, reprinted in 13 Del. J. Corp. L. at 184 (citing Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983)).
94. Id., slip op. at 11-12, reprinted in 13 Del. J. Corp. L. at 181. The court found that the ultimatum, in effect, removed the special committee’s ability to negotiate in an arm’s-length manner. Id., slip op. at 12, reprinted in 13 Del. J. Corp. L. at 181.
95. Id., slip op. at 14, reprinted in 13 Del. J. Corp. L. at 182.
96. Id., slip op. at 16, reprinted in 13 Del. J. Corp. L. at 183. The court also noted that Texas Air’s refusal to pay the minority stockholders a premium “may indicate a lack of judgment but it is not illegal.” Id., slip op. at 20, reprinted in 13 Del. J. Corp. L. at 185.
the stock of Bank Building & Equipment Corporation of America based on claims that the offer had an entrenchment effect and that the failure to structure the offer as one for 100% of the stock was coercive.\textsuperscript{100} Plaintiffs alleged that the $14 offer price virtually forced shareholders to tender since the then current market price of the stock was $8.35 per share.\textsuperscript{101} The court rejected, for lack of evidence, the argument that the offer had an entrenchment effect.\textsuperscript{102} It rejected the coercion argument because no fiduciary duty required that the offer be structured as one for all of the stock.\textsuperscript{103}

10. In re \textit{Sea-Land Corp. Shareholders Litigation}

The court also granted motions to dismiss complaints in cases alleging breaches of fiduciary duty in connection with mergers and merger proposals. In In re \textit{Sea-Land Corp. Shareholders Litigation},\textsuperscript{104} the

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{100} \textit{Id.}, slip op. at 9-13, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 747-49.
\item \textsuperscript{101} \textit{Id.}, slip op. at 10, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 748.
\item \textsuperscript{102} \textit{Id.}
\item \textsuperscript{103} \textit{Id.}, slip op. at 13-14, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 750. The court noted that:
\end{itemize}
\end{footnotesize}
court dismissed claims arising out of the purchase by CSX Corporation (CSX) of the 39.5% stock interest in target Sea-Land Corporation (Sea-Land) owned by a group of stockholders constituting a rival bidder (Simmons) at a premium over the price CSX offered to Sea-Land's remaining stockholders.\(^{105}\) The court found the plaintiffs' fiduciary claim to be flawed in two respects: (1) since Simmons was not a controlling stockholder of Sea-Land, he had no fiduciary obligations to Sea-Land's other stockholders\(^ {106}\) and, (2) even if he were a fiduciary, Simmons was not legally prohibited from selling his stock to CSX, a third party, for whatever price he was able to negotiate.\(^ {107}\)

11. **Lewis v. Honeywell, Inc.**

In *Lewis v. Honeywell, Inc.,*\(^ {108}\) the court dismissed a complaint which alleged that the directors of Honeywell, Inc. illegally, summarily and arbitrarily rejected a cash offer to purchase all of the company's

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\(^{105}\) In re *Sea-Land Corp. Shareholders Litig.*, No. 8453, slip op. at 1-2, reprinted in 13 Del. J. Corp. L. at 798. After CSX publicly announced its proposal to acquire all shares of Sea-Land stock for $28 per share, CSX and Simmons conducted negotiations between themselves. The result was that CSX acquired, for a price of $5 per share, an option to purchase all of Simmons’ Sea-Land shares for $28 per share and agreed to pay $4 million of expenses incurred by Simmons. *Id.*, slip op. at 4-5, reprinted in 13 Del. J. Corp. L. at 800.

\(^{106}\) *Id.*, slip op. at 9, reprinted in 13 Del. J. Corp. L. at 803.

Under Delaware law a stockholder has fiduciary obligations only if it is a controlling stockholder. A stockholder is not deemed controlling unless it owns a majority of the stock, *Aronson v. Lewis*, Del. Supr., 473 A.2d 805, 815 (1984); *Gilbert v. El Paso Co.*, 490 A.2d at 1055; *Kaplan v. Centex Corp.*, Del. Ch., 284 A.2d 119, 122-123 (1971), or has exercised actual domination and control in directing the corporation’s business affairs. *Gilbert*, 490 A.2d at 1055; see *Kaplan*, 284 A.2d at 122-123.


\(^{107}\) In re *Sea-Land Corp. Shareholders Litig.*, No. 8453, slip op. at 12, reprinted in 13 Del. J. Corp. L. at 804. “A controlling stockholder is generally under no duty to refrain from receiving a premium upon the sale of his controlling stock.” *Id.* (citing *Christophides v. Porco*, 289 F. Supp. 403, 405 (S.D.N.Y. 1968)); 12B *Fletcher Cyclopedia Corporations §§ 5805, 5805.10*, at 135, 139. “Under Delaware law, [Simmons] would not have violated a fiduciary duty if it had sold its shares directly to Sea-Land for a premium not available to other stockholders.” In re *Sea-Land Corp. Shareholders Litig.*, No. 8453, slip op. at 12, reprinted in 13 Del. J. Corp. L. at 804 (citing *Polk v. Good*, 507 A.2d 531, 537 (Del. 1986); *Unocal Corp.*, 493 A.2d at 953-54).

common stock at a substantial premium.\textsuperscript{109} The court held that "[w]here the directors discharge [their] duty to make a fully informed business decision concerning the merits of such a transaction] in a proper fashion, they may, in a proper case involving a valid exercise of their business judgment discretion, reject a takeover proposal without further negotiation."\textsuperscript{110} The court also noted that an outside valuation by an investment banker, "while certainly probative, is not essential to establish or support an informed business judgment."\textsuperscript{111}

C. Voting Rights: Williams v. Geier

In Williams v. Geier,\textsuperscript{112} the court of chancery considered a motion to dismiss a complaint attacking the recapitalization of defendant Cincinnati Milacron, Inc. (Milacron). Common stockholders owning shares prior to the recapitalization and those who later acquired stock and held it continuously for three years were entitled to ten votes per share pursuant to the recapitalization, which was approved by the stockholders shortly after the complaint was filed. Any stockholder not falling within one of those two categories was entitled to only one vote per share.\textsuperscript{113} The plaintiff alleged, among other things, that the recapitalization violated Delaware law because it created disparate voting rights within a single class of stock and constituted a restriction on transferability.\textsuperscript{114}

\textsuperscript{109} Id., slip op. at 1, 11, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 731, 736. The plaintiff alleged that the Chairman of the Board of Honeywell, Inc. (Honeywell) contacted the Chief Executive Officer (CEO) of Sperry Corporation (Sperry) and proposed an acquisition of Sperry by Honeywell, a proposal that Sperry rejected. \textit{Id.}, slip op. at 2, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 732. Thereafter Sperry's CEO informed Honeywell's Chairman that Sperry's board had authorized him to propose a friendly offer for Honeywell in which Sperry was prepared to purchase all shares of Honeywell's common stock for $105 per share in cash. \textit{Id.}, slip op. at 2-3, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 732. Plaintiff further alleged that Honeywell summarily rejected Sperry's offer later that day without in any way negotiating or disclosing the offer to stockholders or consulting with its investment advisors. \textit{Id.}, slip op. at 3, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 732.

\textsuperscript{110} Id., slip op. at 7, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 735 (citing Pogostin v. Rice, 480 A.2d 619, 627 (Del. 1984)).

\textsuperscript{111} Id., slip op. at 10, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 737 (citing Smith, 488 A.2d at 876).


\textsuperscript{113} Id., slip op. at 1, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 817.

\textsuperscript{114} Id., slip op. at 3, \textit{reprinted in} 13 \textit{Del. J. Corp. L.} at 818. Plaintiff also alleged that the sole purpose of the recapitalization was to entrench incumbent management, that full disclosure was not made and that Milacron's stockholders had been coerced into voting for the recapitalization. \textit{Id.}
Relying on the supreme court’s 1977 decision in *Providence & Worcester Co. v. Baker*, the court dismissed the claim that the recapitalization was invalid as creating disparate voting rights within a single class of stock. The court found no basis for distinguishing the restriction based on the size of one’s stockholding upheld in *Providence & Worcester* from the restriction based on the duration of one’s stockholding at issue in *Williams*. The court also dismissed the claim that the plan constituted a restriction on transferability since “the complaint does not, and could not, allege that the recapitalization directly restricts the transferability of Milacron common stock.”


In *Marciano v. Nakash*, the supreme court considered the proper standards for review of self-dealing transactions. The court affirmed the court of chancery’s decision that $2.5 million in loans by the 50% owner of Gasoline, Ltd. to the company “were valid and enforceable, notwithstanding their origin in self-dealing transactions.” Plaintiffs argued that section 144(a) of the GCL provides the only basis for immunizing self-interested transactions and that, if its provisions could not be met, the common law rule of per se

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115. 378 A.2d 121 (Del. 1977).
   In *Providence & Worcester*, the company’s certificate provided for differing voting rights depending upon the total number of shares held by each stockholder. Specifically, stockholders were entitled to one vote per share for the first 50 shares they owned and one vote for each additional 20 shares. In addition, stockholders were not permitted to vote more than one fourth of the total number of shares outstanding regardless of how many shares they owned. The Delaware Supreme Court upheld the voting structure on the ground that the certificate did not place voting restrictions on the stock, but only on the stockholder.

117. *Id.*, slip op. at 9, reprinted in 13 Del. J. Corp. L. at 820.
118. *Id.*, slip op. at 11, reprinted in 13 Del. J. Corp. L. at 822. The court noted that “[e]ssentially the same argument” had been made and rejected in Moran v. Household Int’l, Inc., 490 A.2d 1059 (Del. Ch.), aff’d, 500 A.2d 1346 (Del. 1985), where plaintiffs claimed that the rights plan prevented stockholders from selling their shares to a hostile tender offeror. *Williams*, No. 8456, slip op. at 10, reprinted in 13 Del. J. Corp. L. at 821.
119. 535 A.2d 400 (Del. 1987).
120. *Id.* at 401.
voidability applies. The court found that "[i]t overstates the common law rule to conclude that relationship, alone, is the controlling factor in interested transactions." It found that "the continued viability of the intrinsic fairness test is mandated not only by fact situations, such as here present, where shareholder deadlock prevents ratification, but also where shareholder control by interested directors precludes independent review."


In Rainbow Navigation, Inc. v. Pan Ocean Navigation, Inc., the supreme court addressed an issue of first impression concerning a stockholder's entitlement to be treated as a stockholder of record for purposes of examining certain books and records of the corporation

121. Id. at 403. Section 144(a) now provides:
(a) No contract or transaction between a corporation and 1 or more of its directors or officers, or between a corporation and any other corporation, partnership, association, or other organization in which 1 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:
(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; or
(2) The material facts as to his relationship or interest and as to the contract or transaction are disclosed or are known to the shareholders entitled to vote thereon, and the contract or transaction is specifically approved in good faith by vote of the shareholders; or
(3) The contract or transaction is fair as to the corporation as of the time it is authorized, approved or ratified, by the board of directors, a committee or the shareholders.


122. Marciano, 535 A.2d at 404. In Fliegler v. Lawrence, 361 A.2d 218 (Del. 1976), the supreme court had also "refused to view section 144 as completely preemptive of the common law duty of director fidelity, as constituting a grant of broad immunity" or as the exclusive means of validating interested director transactions. Marciano, 535 A.2d at 404.


The court affirmed a court of chancery decision that the plaintiff should be treated as the record owner for purposes of assessing its entitlement to the examination permitted under section 220 of the GCL. The supreme court noted that:

[t]he right to examine the corporation’s stock ledger is hollow, indeed, if it can be defeated by never maintaining such a record. If the common law right of a stockholder to examine a corporation’s books can only be diminished by legislation, a fortiori, the statutorily guaranteed right to examine the stock ledger cannot be frustrated by nonfeasance. We find it implicit in Sections 219 and 220 that Delaware corporations have an affirmative duty to maintain a stock ledger.

The court concluded that a trial court could look to evidence extrinsic to the stock ledger for the purpose of determining status as a record stockholder in “situations in which the stock ledger is blank or nonexistent.”

F. Annual Meeting of Stockholders: Aprahamian v. HBO & Co.

In Aprahamian v. HBO & Co., the court of chancery granted a preliminary injunction enjoining further postponement of the annual meeting of the stockholders of HBO & Company (HBO). The defendant incumbent directors originally scheduled the meeting for

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125. Id. at 1358.

Section 220 provides, in pertinent part:
(a) As used in this section, “stockholder” means a stockholder of record.
(b) Any stockholder, in person or by attorney or other agent, shall, upon written demand under oath stating the purpose thereof, have the right during the usual hours for business to inspect for any proper purpose the corporation’s stock ledger, a list of its stockholders, and its other books and records, and to make copies or extracts therefrom. A proper purpose shall mean a purpose reasonably related to such person’s interest as a stockholder.

127. Section 219(c) provides that the “stock ledger shall be the only evidence as to who are the stockholders entitled to examine the stock ledger.” Del. Code Ann. tit. 8, § 219(c) (1974).
129. 531 A.2d 1204 (Del. Ch. 1987).
130. Id. at 1205.
April 30, 1987. In late March, plaintiffs formed a committee to oppose the reelection of the incumbent directors and to nominate new directors. A program was proposed by the insurgent nominees which would allegedly maximize the value of HBO through the creation of a special committee which would propose transactions, including the possible sale of the corporation.

Then, three business days before the scheduled date of the annual meeting, the incumbent directors "decided to embrace the plaintiffs' platform" and appoint their own special committee. On the day before the scheduled date for the annual meeting, the directors received information from their proxy solicitor that the election results were too close to call. The directors then decided to postpone the meeting until September 22, 1987 with a new record date.

Defendants argued that the postponement of the meeting was justified since such action had been recommended by the special committee of the board. The court rejected this argument since the members of the special committee were both incumbent directors seeking reelection and therefore "obviously interested." The court concluded that defendants had not borne their burden of demonstrating that the postponement of the meeting was "in the best interests of the stockholders." The fact that they wanted more time to convince the stockholders of the merit of their position was not entitled to business judgment deference since "[i]ncumbent directors do not have any preemptory rights to continue to serve as directors."

Regarding the general conduct of corporate elections, the court stated that:

> [t]he corporate election process, if it is to have any validity, must be conducted with scrupulous fairness and without any advantage being conferred or denied to any candidate or slate of candidates. In the interests of corporate democracy,
those in charge of the election machinery of a corporation must be held to the highest standards in providing for and conducting corporate elections.138

G. Appraisal Rights: Enstar Corp. v. Senouf

In Enstar Corp. v. Senouf,139 the supreme court held that only a stockholder of record may demand an appraisal.140 The court noted that where a stockholder elects to hold stock in street name, "the burden must be upon the stockholder to obtain the advantages of record ownership."141

H. Derivative Suits—Rule 23.1


The court of chancery also issued a number of important decisions in 1987 concerning Court of Chancery Rule 23.1 and its requirements relating to derivative suits.142 In Kaplan v. Peat, Marwick, Mitchell & Co.

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138. Id. at 1206-07.
139. 535 A.2d 1351 (Del. 1987).
140. Section 262(a) provides, in pertinent part, that "the word 'stockholder' means a holder of record of stock in a stock corporation" for purposes of demanding an appraisal. Del. Code Ann. tit. 8, § 262(a) (1987). "While the 'holder of record' provision was added to Section 262 in the 1967 revision of the General Corporation Law, for decades this Court had consistently defined the term 'stockholder' as a holder of record." Senouf, 535 A.2d at 1354 (footnote omitted). See, e.g., Carl M. Loeb, Rhoades & Co. v. Hilton Hotels Corp., 222 A.2d 789 (Del. 1966); Olivetti Underwood Corp. v. Jacques Coe & Co., 217 A.2d 683 (Del. 1966); Salt Dome Oil Corp. v. Schenck, 41 A.2d 583, 589 (Del. 1945). While the court of chancery had found that plaintiffs' demands for an appraisal were valid since the corporation had "reasonable constructive notice" that plaintiffs' shares were held by a nominee, In re Enstar Corp., No. 7802, slip op. at 14 (Del. Ch. July 17, 1986), reprinted in 12 Del. J. Corp. L. 694, 705 (1987), the supreme court reversed since the "statutory language, statutory history and prior judicial decisions all make clear that only a stockholder of record may demand an appraisal." Senouf, 535 A.2d at 1352 (footnote omitted).
141. Senouf, 535 A.2d at 1354 (citing Nickles v. United Nuclear Corp., 192 A.2d 628 (Del. Ch. 1963); Lewis v. Corroon & Reynolds Corp., 57 A.2d 632, 634 (Del. Ch. 1948)).
142. Rule 23.1 provides, in pertinent part:
In a derivative action brought by 1 or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, the complaint shall allege that the plaintiff was a shareholder or member at the time of the transaction of which he complains or that his share or membership thereafter devolved on him by operation
the court held that "a defendant other than the corporation [had] standing to challenge the plaintiff stockholders' failure to comply with the demand requirement of Rule 23.1." In a suit against the corporation's former accountants for damages allegedly sustained as a result of financial dealings in which the accounting firm had acted as the corporation's independent auditor, the court granted the accounting firm's motion to dismiss under Rule 23.1.

2. Grobow v. Perot and Levine v. Smith

In Grobow v. Perot and Levine v. Smith, the court considered motions in various derivative actions on behalf of General Motors Corporation (GM), challenging a repurchase by GM of certain securities and notes issued to defendant H. Ross Perot (Perot), a member of law. The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action he desires from the directors or comparable authority and the reasons for his failure to obtain the action or for not making the effort.


143. 529 A.2d 254 (Del. Ch. 1987).

144. Id. at 258-62. While the court suggested that plaintiffs' argument that an "outside" defendant ought not to be entitled to raise the failure to make a demand as a defense "is not without persuasive force," the court found the argument flawed in two respects:

First, it ignores the inherent interest that any defendant would have in being able to challenge a plaintiff's capacity to sue him—a concern reflected in Chancery Rule 9(a), which permits defendants (without distinctions) to challenge a plaintiff's capacity to sue. Second, plaintiffs' argument overlooks the critical importance—emphasized in Haues, Zapata and Aronsen—of the policy underlying the demand requirement, viz., that the decision as to whether and in what manner a corporation should pursue a corporate claim, is ordinarily for the board of directors to make. The policy is not furthered by a restrictive rule of standing.

Id. at 259.

145. Plaintiffs claimed that Peat, Marwick, Mitchell & Co. breached its duty of care and contractual duties owed to the corporation by failing to conduct proper audits in the so-called "Drysdale" and "Penn Square" matters in which the corporation became involved in 1982. Id. at 255.

146. Id. at 257, 263. The court rejected plaintiffs' argument that a demand would have been futile because the corporation's board had previously rejected a prior demand by another shareholder. That argument was found to be "legally insufficient, because plaintiffs have not alleged . . . that the Board's refusal of the prior demand was wrongful." Id. at 257 (citing Allison v. General Motors Corp., 604 F. Supp. 1106, 1122 (D. Del.), aff'd, 782 F.2d 1026 (3d Cir. 1985); Aronsen, 473 A.2d at 813; Zapata Corp. v. Maldonado, 430 A.2d 779, 784 (Del. 1981)).

147. 526 A.2d 914 (Del. Ch. 1987).

of GM's board of directors, and to other persons. In Grobow, the court dismissed the action based on the failure to make a demand on the GM board. It noted that:

the buy-back transaction appears indistinguishable from other repurchases by a corporation, at a premium over market, of its own stock held by a single dissident shareholder or shareholder group at odds with management, that have repeatedly been upheld as valid exercises of business judgment. . . . [E]ven if the repurchase involves the payment of a premium and even if its motivation is to eliminate a threat to the corporate enterprise created by a substantial dissident stockholder, the repurchase is protected by the business judgment rule, unless it involves fraud or unfairness, or its primary or sole purpose is to entrench the directors in office.

The court rejected a claim that the transaction amounted to a waste of corporate assets. The pleaded facts did not show that the consideration received by GM in the transaction "was so inadequate that no person of ordinary, sound business judgment would deem it worth that which the corporation paid."

In Levine v. Smith, a case in which a demand was made on GM's board and refused, the defendants moved to dismiss the

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149. Grobow, 526 A.2d at 917. As alleged in the complaint, "the total cost of the buy-back transaction to GM was $742.8 million, which Perot reportedly characterized as including a 'giant premium' paid to him." Id. at 919. As part of the buy-back transaction, Perot also agreed to refrain from criticizing GM management and to pay liquidated damages of up to $7.5 million if that covenant was found to have been violated. He also agreed, for stipulated periods of time, to refrain from purchasing GM stock, from starting a business that would compete with GM's Electronic Data Systems subsidiary (EDS) and from recruiting EDS executives to another company. Id.

150. Id. at 928-29.

151. Id. at 927. See Polk v. Good, 507 A.2d 531 (Del. 1986); Cheff v. Mathes, 199 A.2d 548 (Del. 1964); Kaplan v. Goldsamt, 380 A.2d 556 (Del. Ch. 1977); Kors v. Carey, 158 A.2d 136 (Del. Ch. 1960).

152. Grobow, 526 A.2d at 928 (quoting Stein v. Orloff, No. 7276, slip op. at 14 (Del. Ch. May 30, 1985), reprinted in 11 Del. J. Corp. L. 312, 319 (1986)). The court found that, in light of the pleaded facts concerning the covenants given by Perot to GM, the allegation that GM paid an "enormous premium" over the market price of the repurchased stock to buy Perot's promise of silence "is not adequately supported to excuse a demand." Id.


154. Id., slip op. at 1.
complaint and for a "protective order staying all discovery pending the outcome of the dismissal motion."155 The court granted the requested protective order since "the board's refusal is presumed to be protected by the business judgment rule, unless and until the plaintiff shows that such protection is not legally justified."155

III. The 1987 Amendments to the GCL

The 1987 amendments to the GCL, involving 23 sections,157 made a number of important changes to the statute. The principal changes involve the provisions regulating action by written consent and the provisions governing the dissolution and liquidation of Delaware corporations.158 The first-generation Delaware takeover statute, which had been found unconstitutional, was repealed.159

Amendments to sections 141 and 172 broadened the scope of those sections by authorizing directors and committee members to rely upon, in addition to corporate records, "information, opinions, reports or statements" presented to the corporation by officers, employees or a board committee "or by any other person as to matters the member reasonably believes are within such other person's pro-

155. Id.

156. Id., slip op. at 9. In a "demand excused" case, however, "a special committee's decision to terminate the litigation is not deemed to be protected by the business judgment rule." Id., slip op. at 8. "That crucial distinction between 'demand excused' and 'demand refused' highlights the basic difference in the nature of these two proceedings, and, as a necessary consequence, the reason why discovery is appropriate in the former setting, but not appropriate in the latter." Id., slip op. at 9.


158. BLACK & SPARKS, supra note 157, at 311.

159. Legislative commentary to 1987 amendments to § 203, S.B. 93, 134th General Assembly, 66 Del. Laws, ch. 136 (1987). The full text of the legislative comments to the repeal of § 203 is as follows: "Section 203 has been held unconstitutional on Supremacy and Commerce Clause grounds, see, e.g., Local Corp. v. Sanders Associates, Inc., D. Del., No. 86-296, Schwartz, J. (July 8, 1986) and the Section is consequently being repealed." While the Delaware bar considered proposing in 1987 a control share acquisition statute modeled after the Indiana statute approved by the U.S. Supreme Court in CTS Corp. v. Dynamics Corp. of Am., Inc., 107 S. Ct. 1637 (1987), no such statute was proposed. BLACK & SPARKS, supra note 157, at 313. (Editor's Note: Early in 1988, Delaware adopted a takeover statute, Del. Code Ann. tit. 8, § 203, with an effective date of February 2, 1988.)
fessional or expert competence and who has been selected with reasonable care by or on behalf of the corporation.'\textsuperscript{160}

Sections 213 and 228 were amended in response to uncertainties about the procedure for the taking of action by consent.\textsuperscript{161} Among other changes in section 213,\textsuperscript{162} the language authorizing the board to fix "in advance" a record date has been changed to specify that the board may fix a record date "which record date shall not precede the date it is adopted"; the directors have been empowered, in certain circumstances, to fix a record date for determining the stockholders entitled to consent to corporate action in writing "which record date shall not be more than ten days" after the date on which the board acts to fix the record date; and the location to which consents must be delivered is stated to be (i) the corporation's registered office in Delaware, (ii) the corporation's principal place of business, or (iii) the officer or agent who has custody of the corporation's minute books.\textsuperscript{163} Amended section 228 requires:

\textsuperscript{160} Black & Sparks, supra note 157, at 312. See legislative commentary to 1987 amendments to sec. 141 and 172, S.B. 93, 134th General Assembly, 66 Del. Laws, ch. 136 (1987). The full text of the legislative comments to the revision of § 141 is as follows:

Two subsections of Section 141, which deals with the authority and operations of the board of directors, have been amended. Subsection (d) of Section 141 has been amended to clarify that in instances when directors elected by a class or series of stock have more or less than one vote, provisions of the Corporation Law which require action by a majority (or other proportion) of directors shall refer to a majority (or other proportion) of the number of votes which may be cast by directors rather than the number of directors. Subsection (e) has been amended to clarify that directors may rely in good faith upon all corporate records, reports of employees and committees of the board and the written or oral advice or opinions of any professionals and experts who are selected with reasonable care and are reasonably believed to be acting within the scope of their expertise.

The full text of the legislative comments to the revision of § 172 is as follows:

Section 172 has been amended to clarify that directors, in determining whether a dividend may lawfully be declared or paid or stock may legally be purchased or redeemed, will be fully protected in relying in good faith upon all corporate records, reports of employees and committees of the board and the written or oral advice or opinions of any professionals and experts who are selected with reasonable care and who are reasonably believed to be acting within the scope of their expertise.

\textsuperscript{161} See, e.g., Empire of Carolina, Inc. v. Deltona Corp., 514 A.2d 1091 (Del. 1985).

\textsuperscript{162} E. Folk, R. Ward & E. Welch, Folk on the Delaware General Corporation Law 430 (1987).

\textsuperscript{163} Id. at 547 n.6. See legislative commentary to 1987 amendments to sec.
that a written consent bear the date of the signature of each shareholder who signs the consent and goes on to provide that no consent will be effective to take corporate action unless written consents sufficient to approve the action are delivered to the corporation within sixty days of the earliest dated consent.\textsuperscript{164}

Section 262 has been amended to clarify when a stockholder must be a stockholder to qualify for appraisal rights.\textsuperscript{165} Sections 274-

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213, S.B. 93, 134th General Assembly, 66 Del. Laws, ch. 136 (1987). The full text of the legislative comments to the revision of § 213 is as follows:

Section 213 has been reorganized to deal separately with the topics of record dates for meetings (in subsection (a)), for consents (in subsection (b)) and other matters for which a record date may be established (in subsection (c)). The principal modification made to subsection (a), and one which has been made to all subsections, is to replace the phrase “in advance” with “which record date shall not precede the date upon which the resolutions fixing the record date is adopted.” This change was made because the “in advance” language was a source of some confusion.

Subsection (b) authorizes the board of directors to establish a record date for determining those stockholders entitled to act by written consent, which date may not be more than 10 days after the date of the board action. If the board has not taken action to establish a record date and no prior board action is required under the General Corporation Law, subsection (b) establishes the record date as the date upon which the first signed consent setting forth the action to be taken has been delivered to the corporation at its registered office in Delaware or its principal place of business. If prior board action is necessary and no record date has been established by the board, the last sentence of subsection (b) provides that the record date shall be on the close of business on the date upon which the board adopts resolutions taking such necessary prior action.

\textsuperscript{164} Black & Sparks, supra note 157, at 314. See legislative commentary to 1987 amendments to sec. 228, S.B. 93, 134th General Assembly, 66 Del. Laws, ch. 136 (1987). The full text of the legislative comments to the revision of § 228 is as follows:

Section 228, which deals with action by stockholders by means of written consent, has been modified to require, in both subsections (a) and (b), the delivery of written consents to a corporation’s principal place of business or the office of the corporation’s registered agent in Delaware for such consents to be effective. A new subsection (c) has been added which requires that consents be dated the date upon which the stockholder or member signs the consent and provides that no written consent is effective unless written consents signed by enough stockholders to take the action referred to in the consent are delivered to the corporation or its registered agent within sixty days of the date the first stockholder or member signs a consent.

\textsuperscript{165} See legislative commentary to 1987 amendments to sec. 262, S.B. 93, 134th General Assembly, 66 Del. Laws, ch. 136 (1987). The full text of the legislative comments to the revision of § 262 is as follows:

Section 262(a) has been amended to resolve any question as to when a
283 relating to dissolution and liquidation of Delaware corporations have also been amended in significant ways. Among other changes, the amended sections include safe harbor provisions for stockholders and directors under certain circumstances against suits by creditors challenging the making of distributions to stockholders.166

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stockholder must be a stockholder to qualify for appraisal rights. In order to be entitled an appraisal of the fair value of his shares, a person must be (a) stockholder both on the date he makes a demand for appraisal under Section 262(d) and on the effective date of the merger or consolidation. In addition, the stockholder must continuously hold such shares of record throughout the period between the date of demand and the effective date of the merger or consolidation. The word "stockholder" means a stockholder as defined in subsection 262(a), i.e., a stockholder of record, and its use is meant to reinforce the fact that appraisal rights are available only to, and may be exercised only by, stockholders of record.

166. See legislative commentary to 1987 amendments to secs. 274-276, 278-282, S.B. 93, 134th General Assembly, 66 Del. Laws, ch. 136 (1987). The full text of the legislative comments to the revision of §§274-283 is as follows:

Commentary on Section 274

Section 274 has been amended to provide a simplified procedure for the dissolution of a corporation which has begun the business for which it was organized but has not issued any stock. Like a corporation which has not begun the business for which it was organized, such a corporation now can be dissolved by the action of a majority of the incorporators or directors, without the necessity of first issuing stock and then obtaining the approval of the stockholders. The section was further amended to provide that, in such a case, the certificate of dissolution shall state that all debts of the corporation have been paid.

Commentary on Section 275

Section 275 describes the dissolution procedures of general application. It has been reorganized by deleting from subsections (b) and (c) the description of the certificates to be filed when the dissolution is approved (i) by both the board of directors and the holders of a majority of the outstanding stock of the corporation entitled to vote thereon (subsection (b)) or (ii) by unanimous consent of the stockholders (subsection (c)). A new subsection (d) is added describing the form and content of a uniform certificate to be filed in either situation. Section 275 is also amended by adding a new subsection (e) permitting a resolution of dissolution to authorize its abandonment by the board of directors or governing body without further stockholder or member action. Finally, Section 275 is amended by adding a new subsection (f) which simplifies the statute by replacing language to the same effect now found in subsections (b) and (c).

Commentary on Section 276

Former Section 276 governed the dissolution of "nonprofit, nonstock corporations." The section is amended by deleting the references to "nonprofit" and "not for profit" to make clear that Section 276 applies to all nonstock corporations and by adding a new subsection (b) describing procedures parallel to those of Section 274 for the dissolution of a nonstock corporation which has not commenced the business for which it was or-
IV. Conclusion

The recent developments in Delaware law again have refined, rather than radically altered, important legal concepts. The supreme

ganized.

Commentary on Section 278

Section 278 generally provides that corporations which dissolve or expire continue their legal existence for a period of three years thereafter, or such longer time as the Court of Chancery may order, for the purpose of winding up their affairs. At the end of that period, the corporation can no longer sue or be sued and, except for defined, limited purposes, ceases to exist. Such a corporation does continue its legal existence beyond that period for the purpose of prosecuting or defending any action begun by or against it prior to the expiration of that period. Section 278 is amended to make clear that any such action does not abate by reason of the dissolution of the corporation and that the continuation of a corporation's legal existence beyond the period described in Section 278 by reason of the pendency of an action, suit or proceeding is solely for the purpose of that action, suit or proceeding. These changes made Section 282 unnecessary and, thus, it has been repealed.

Commentary on Section 279

Section 279 is amended to make explicit that a director of a dissolved corporation is a person entitled to petition the Court of Chancery for the appointment of a trustee or receiver of the corporation's property.

Commentary on Section 280

Former Section 280 is renumbered Section 283. That section, which conferred jurisdiction on the Court of Chancery in actions under Section 279, is expanded to include actions under any provision of Subchapter X, including the new provisions of Section 280.

Commentary on Section 281

Section 281 is substantially new. Subsections (a) and (b) prescribe the procedures for distributing assets, including the distribution of remaining assets to stockholders, of a dissolved corporation which has and has not, respectively, complied with the provisions of Section 280. Subsection (c) deals with the liability of directors (and governing persons of "successor entities") to claimants whose claims against the dissolved corporation are ultimately unsatisfied.

Commentary on Section 282

Section 282 is new and addresses the liability of stockholders to corporate creditors where the assets of the corporation have been distributed by the corporation or a successor entity. Subsection (a) provides that where the corporation has distributed its assets pursuant to either Section 281(a) or (b), the liability of a stockholder to an unsatisfied creditor of the corporation will be the lesser of that stockholder's proportionate share of the claim or the amount of assets distributed to that stockholder in dissolution. In the case of a corporation distributing assets pursuant to Section 281(a), the amount a creditor can recover from a stockholder will not be so limited if the board of directors (or governing body of a successor entity) did not comply with the requirements of that subsection in paying or making reasonable provision for the payment of the claims and obligations of the corporation.
court’s decision in *McDermott, Inc. v. Lewis* discussed important constitutional principles concerning the internal affairs doctrine. The various decisions in the takeover context provide further guidance to directors concerning their obligations of due care and loyalty in the consideration of proposed acquisitions. The judicial decisions and legislative refinement of the GCL reflect well-considered responses to a variety of the day’s most important corporate questions.