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DIRECTORS' RESPONSIBILITIES AND SHAREHOLDERS'
INTERESTS IN THE AFTERMATH OF *PARAMOUNT
COMMUNICATIONS V. TIME, INC.*

ROBERT E. BULL*

INTRODUCTION

One reason for the formation of corporations was the desire of businessmen to establish a fund of property distinct from the property of any of the members' or their debts, and from the vagaries of descent and distribution when the members died.¹ A further purpose in incorporating was the maintenance of the members' individual property separate from that of the corporation and, presumptively, free from claims of the corporation's creditors.² The structure of corporate control can be viewed as pyramidal in nature, with the shareholders forming the pyramid's broad base³ and exercising their control, for the most part, by selecting the individuals who serve on the board of directors.⁴ Although shareholders do not take part in the daily running of the corporation, as owners they have ultimate control over its policies.⁵ However, the advent of the business judgment rule, which protects directors' informed business decisions from court scrutiny, has led to the erosion of shareholder control. This problem is particularly troublesome in the area of mergers and acquisitions, where directors' desires may conflict with shareholders' interests.

Between 1895 and 1904, a wave of mergers occurred and resulted in a number of near monopolies.⁶ Mergers from the second wave, from 1920 to 1929, resulted in many oligopolies (*i.e.*, markets with few sell-

* The author would like to thank Professor Philip N. Hablutzel for his patient assistance and guidance and Jeffrey R. Platt for his thoughtful suggestions and encouragement in the development of this Note.

1. A. CONRAD, R. KNAUSS & S. SIGEL, *ENTERPRISE ORGANIZATION* 40 (4th ed. 1987).

2. *Id.*

3. R. HOWELL, J. ALLISON & R. PRENTICE, *BUSINESS LAW—TEXT AND CASES* 834 (4th ed. 1988). See also Booth, *Is There Any Valid Reason Why Target Managers Oppose Tender Offers?*, 14 SEC. REG. L.J. 43, 48-49 (1986) ("A corporation is like a contract between shareholders and management. The shareholders agree to invest, and management agrees to do its best to generate a return on that investment.").

4. *Id.*

5. *Id.*

6. Comment, *Business Judgment Rule: A Benchmark for Evaluating Defensive Tactics in the Storm of Hostile Takeovers*, 31 VILL. L. REV. 1439, 1439 n.1 (1986).

ers).⁷ Following World War II, a third wave of mergers involved corporations in different industries, or conglomerates.⁸ The next period of intense mergers occurred from 1966 to 1970 and once more involved conglomerate mergers.⁹ Recently, merger activity has again intensified, resulting in 16,285 mergers involving \$510.9 billion in assets.¹⁰

Various reasons account for this increased merger activity. "First, the potential acquiror may believe that it can increase the profits of the target by replacing the target's management."¹¹ Second, one corporation may seek to acquire another corporation for an "economies of scale" reason—namely the reduction in production and marketing costs associated with a larger scale of operation.¹² "Third, management of an acquiring corporation may take over a target corporation in order to diversify, and thus, maintain corporate stability."¹³ "Fourth, managers may seek to expand the size of their corporation because increased income and prestige are customarily associated with large conglomerates."¹⁴ However, empirical data illustrates that the acquiring corporation often loses money after its merger is successful.¹⁵ Finally, a corporation may want to assure uninterrupted access to raw materials, market outlets, new technology, or research capacity.

Balanced against the directors' desire to increase company prestige and size is their duty to make decisions that are in the shareholders' best interests. The directors occupy a fiduciary relationship to the corporation and must exercise the care of an ordinary prudent and diligent person in a like position and under similar circumstances.¹⁶ This duty is codified in many states. For example, in California, a director must perform duties, "in good faith, in a manner such director believes to be in the best interest of the corporation, and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances."¹⁷

7. *Id.*

8. *Id.*

9. *Id.*

10. *Id.*

11. Comment, *Business Judgment Rule: A Benchmark for Evaluating Defensive Tactics in the Storm of Hostile Takeovers*, 31 VILL. L. REV. 1439 n.2 (1986).

12. *Id.*

13. *Id.*

14. *Id.*

15. See Asquith, *Merger Bids, Uncertainty, and Stockholder Returns*, 11 J. FIN. ECON. 51, 81 table 9 (1983) (value of successful and unsuccessful bidder's stock often decreased during 240 days after outcome of merger contest determined).

16. *Francis v. United Jersey Bank*, 87 N.J. 15, 36, 432 A.2d 814, 824 (1981) (also known as the duty of care).

17. CAL. CORP. CODE § 309(a) (West 1989).

When a company attempts to thwart an unsolicited takeover, the courts apply the business judgment rule in deciding whether directors have fulfilled their duty of care in responding to a takeover attempt.¹⁸ Under the business judgment rule, a court will defer to any board of directors' decision as long as the directors can show that their decision has a rational basis. Therefore, the business judgment rule will protect directors who act in good faith from personal liability for mere errors of judgment or want of prudence, short of clear and gross negligence.¹⁹ Although the directors must make an "informed" decision to fall under the business judgment rule's protection, the directors may still violate their duty of care by not giving appropriate attention to an important corporate matter (e.g., a hostile takeover attempt) and not seeking expert advice when it is clearly needed.²⁰ Another problem arises when, as a result of a merger, stock values go down. In this case, shareholders may lose present value of their stock while their directors hide behind the protection of the business judgment rule, even though they have not furthered the shareholders' best interests.

The problems associated with increased corporate merger and takeover activity have been the subject of much debate.²¹ The deluge of case law²² and scholarly²³ concern has focused on the directors' responsibili-

18. R. HOWELL, J. ALLISON & R. PRENTICE, *supra* note 3, at 895.

19. *Shlensky v. Wrigley*, 95 Ill. App. 2d 173, 237 N.E.2d 776 (1st Dist. 1968). See also Johnson & Millon, *Does the Williams Act Preempt State Common Law in Hostile Takeovers?*, 16 SEC. REG. L.J. 339, 360 (1989) ("The purpose and effect of the business judgment rule is to safeguard board decisions on corporate enterprise matters from judicial second-guessing and to spare directors from personal liability").

20. R. HOWELL, J. ALLISON & R. PRENTICE, *supra* note 3, at 903.

21. See generally Block & Miller, *The Responsibilities and Obligations of Corporate Directors in Takeover Contests*, 11 SEC. REG. L.J. 44 (1983); Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981) [hereinafter Easterbrook & Fischel, *Proper Role*]; Easterbrook & Fischel, *Takeover Bids, Defensive Tactics, and Shareholders' Welfare*, 36 BUS. LAW. 1733 (1981) [hereinafter Easterbrook & Fischel, *Takeover Bids*]; Freund, *Mergers and Acquisitions: The Quintessence of Change*, 36 CLEV. ST. L. REV. 495 (1988); Gilson & Kraakman, *Delaware's Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 BUS. LAW. 247 (1989); Lipton & Brownstein, *Takeover Responses and Directors' Responsibilities — An Update*, 40 BUS. LAW. 1403 (1985); Reder, *The Obligation of a Director of a Delaware Corporation to Act as an Auctioneer*, 44 BUS. LAW. 275 (1989).

22. See, e.g., *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261 (Del. 1989) (directors duties); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986) (directors must maximize the company's value at a sale for the stockholders' benefits) (Although there were two *Revlon* decisions, *I* and *II*, for purposes of this note, I will refer to *Revlon II* only and cite to it as *Revlon*); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985) (directors can authorize a self-tender, to the exclusion of a hostile shareholder, if the self-tender is in the shareholders' best interests); *Robert M. Bass Group, Inc. v. Evans*, 552 A.2d 1227 (Del. Ch. 1988) (directors' choice to restructure the corporation to thwart off a takeover attempt); *City Capital Assoc. v. Interco, Inc.*, 551 A.2d 787 (Del. Ch. 1988) (directors may have to let shareholders choose between takeover offer and corporate restructuring).

23. See *supra* note 21 and accompanying text.

ties and duties during a takeover attempt and the concomitant shareholder rights. However, the scales are tipped toward the directors' decisions, with only grossly negligent decisions falling outside the protected realm.²⁴

While the law of mergers and acquisitions is constantly in a state of flux,²⁵ courts seem content to give directors carte blanche in determining the viability of the corporation. Several times after Delaware courts²⁶ took a small step toward protecting shareholders' interests, it eliminated those advances with larger steps backwards.²⁷

This Note will discuss the courts' expanded protection of directors' decisions under the loose requirements of the business judgment rule. Directors' decisions are easily rationalized to pass muster under the business judgment rule. First, new defensive mechanisms constantly add to the directors' arsenal.²⁸ Second, directors can reject takeovers for finan-

24. See *Smith v. Van Gorkom*, 488 A.2d 858, 873 (Del. 1985) (directors' decisions that are grossly negligent are not afforded the protection of the business judgment rule). See also *Joseph E. Seagram & Sons v. Abrams*, 510 F. Supp. 860, 861 (S.D.N.Y. 1981) (directors cannot sell all of a corporation's assets in a "scorched earth policy" to thwart off a takeover attempt, and hide behind the protection of the business judgment rule); *Post Smith v. Van Gorkom: Director Liability Legislation with a Proactive Perspective*, 36 CLEV. ST. L. REV. 559 (1988) [hereinafter *Post Smith*]. The author states that the *Van Gorkom* decision strips directors of the protective cloak of the business judgment rule when they act with gross negligence. *Id.* at 559.

25. Freund, *supra* note 21, at 500.

26. While this Note is not written exclusively for application to Delaware law, Delaware's status as a corporation haven has resulted in a voluminous amount of precedent in the area of mergers and acquisitions, and most of the seminal cases concerning directors' duties and responsibilities during hostile takeovers have come from its courts. See, e.g., *Post Smith*, *supra* note 24. The Delaware Supreme Court's inherent power in corporate America is unmatched, and its influence transcends to all industries and companies of every size. *Id.* at 567. The Delaware courts' speed and expertise in resolving corporate issues has made Delaware the number one state for business incorporation. *Id.* at 571. See also Fischel, *The Business Judgment Rule and the Trans Union Case*, 40 BUS. LAW. 1437, 1454 (1985) (Delaware offers corporations a solid body of precedents, is receptive to value-increasing transactions, and realizes that allowing firms flexibility in structuring their affairs benefits investors—the result is an overwhelming number of firms incorporating in Delaware).

27. For example, the court in *Unocal* held that the directors' decision to undertake a self-tender to defeat a hostile takeover from a shareholder known to be a greenmailer was protected by the business judgment rule as necessary to protect the shareholders and the corporate enterprise. 493 A.2d at 958. Greenmail refers to a practice of acquiring a substantial block of a company's shares, and receiving a substantial premium for those shares from the corporation in a buy-back. The corporation usually buys back shares held by a potential bidder when they perceive a threat from the shareholder or an outsider, and the company wants to strengthen its position. See Block & Miller, *supra* note 21, at 62. However, also in *Unocal*, the court stated that directors may consider other constituencies (*i.e.*, creditors, customers, employees and possibly the community generally) when deciding whether to reject a takeover bid. 493 A.2d at 955. These added considerations given to the directors, especially in light of the increase in defensive mechanisms (*e.g.*, "Pac-Man," self-tender, "Poison Pill," etc.—to be discussed more fully later), may allow a director to reject a takeover attempt, which may be in the shareholders' best interest, but conflict with another constituency. This rejection could, arguably, be protected by the business judgment rule even though it's not within the best interests of the shareholders, but the directors "believe" the rejection to be a valid corporate decision.

28. For example, there is the "Pac-Man" defense, where a target company attempts its own

cial, legal, and other reasons.²⁹ Third, directors can consider other constituencies (*i.e.*, creditors, customers, employees, or the general community)³⁰ when responding to a takeover attempt. Fourth, the standard for abuse of a director's business judgment is very difficult to meet.³¹ The heavy burden is stacked against any challenger. Fifth, legislatures, by enacting antitakeover statutes,³² have placed their stamps of approval upon directors' responses to takeovers. By implementing these statutes, legislatures allow corporations to incorporate in their state with built-in defensive mechanisms, thereby sanctioning their takeover responses as legitimate and rational business decisions. Lastly, this Note will discuss the added implications of the Delaware Supreme Court's recent decision of *Paramount Communications v. Time, Inc.*

After examining the effects of *Time*, as meshed with current mergers and acquisitions law, the Note concludes that the business judgment rule has been expanded beyond its intended purpose, and that something must be done to protect the rights of shareholders from expropriation.

I. BUSINESS JUDGMENT RULE

As a precursor to any discussion about which directors' decisions the business judgment rule protects, the workings and parameters of the rule must be set forth. Initially, a distinction must be made between the intrinsic fairness standard³³ and the business judgment rule, and when each applies. Under the intrinsic fairness standard, the burden of proof

takeover of the would-be acquiring company (a counteroffer takeover). See *Martin Marietta Corp. v. Bendix Corp.*, 549 F. Supp. 623 (D. Md. 1982); Lipton & Brownstein, *supra* note 21, at 1419. In addition, there are various types of Share Purchase Rights Plans or "Poison Pills," whereby a purchaser who reaches a certain percentage of stock ownership (30, 20, or 15%) triggers the Plan and the remaining shareholders can redeem their present stock with the acquiring company's stock at a 2:1 ratio, therefore making the target company less appealing for a takeover since the value of the acquiring company is diluted. See *Moran v. Household Int'l Inc.*, 500 A.2d 1346 (Del. 1985) (court upheld directors implementation of a Rights Plan to protect corporation from potential takeover); Lipton & Brownstein, *supra* note 21, at 1424. For a more thorough discussion of defensive mechanisms, see *infra* notes 53-141.

29. See *Unocal*, 493 A.2d at 955.

30. *Id.* But cf. *Revlon*, 506 A.2d at 182 (other constituencies are permissible to consider only if there is also a "rationally related benefit accruing to the stockholders"). For a listing of the states which include an "other constituencies" provision in their antitakeover statutes, see *infra* note 139.

31. The standard for director liability is gross negligence, closely approximating fraudulent behavior. See *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985) and *Post Smith*, *supra* note 24, at 559.

32. For a list of the states which have enacted antitakeover statutes, see Note, *The Delaware Takeover Statute: Constitutionally Infirm even under the Market Participant Exception*, 17 HOFSTRA L. REV. 203 (1988).

33. *Sinclair Oil Corp. v. Levien*, 280 A.2d 717 (Del. 1971). The intrinsic fairness test shifts the burden of proof onto the directors to prove, subject to careful judicial scrutiny, that its transaction was objectively fair. *Id.* at 720. See also *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103, 115 (Del. Ch. 1986).

falls on the directors to justify their decisions. In contrast, under the business judgment rule, directors enjoy a rebuttable presumption of sound business judgment which will not be disturbed if the decision can be attributed to any rational business purpose.³⁴ In the latter circumstance, once the court determines that the directors have shown a rational basis for their decision, it will not substitute its own judgment for that of the directors.³⁵ Under Delaware law, the cardinal precept of corporate law is that directors, not shareholders, manage the business affairs of the company.³⁶ From this premise flows certain fundamental fiduciary obligations owed to the company and its shareholders.³⁷ Generally, the courts recognize two components of the fiduciary obligation owed to the company and shareholders. Not so coincidentally, these same two components are part of the business judgment rule. The two components are a duty of care and a duty of loyalty owed to both the company and the shareholders.³⁸

A portion of the duty of care is satisfied when the directors make an informed decision about whether a takeover offer is in the best interests of the company.³⁹ In addition to an informed decision, the directors must act in good faith and with an honest belief that the action taken is in the best interests of the company.⁴⁰ Also, the duty of care applies to

34. See, e.g., *Whittaker Corp. v. Edgar*, 535 F. Supp. 933, 950 (N.D. Ill. 1982); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d at 954; *Sinclair*, 280 A.2d at 720; *Robert M. Bass Group, Inc. v. Evans*, 552 A.2d 1227, 1239 (Del. Ch. 1988).

35. See cases cited *supra* note 34. While most business decisions are presumed to be of sound business judgment, if the decision is a defensive reaction to a takeover bid, the directors must overcome the burden placed upon them by *Unocal*. This burden is met when the directors act reasonably in relation to the threat posed by the takeover bid. 493 A.2d at 955. Thus, all defensive actions taken by a board must meet the *Unocal* "proportionality" test, see *Gilson & Kraakman, supra* note 21, while non-defensive decisions are presumed sound.

36. See *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984). The *Aronson* court cited DEL. CODE ANN. tit. 8, § 141(a) (1982):

"The business and affairs of a corporation organized under this chapter shall be managed by or under the direction of a board of directors"

Id. at 811. See also *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1154 (Del. 1989); *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334, 1341 (Del. 1987); *Unocal*, 493 A.2d at 953; *Pogostin v. Rice*, 480 A.2d 619, 624 (Del. 1984).

37. See *supra* note 36 and accompanying text.

38. *Polk v. Good*, 507 A.2d 531, 536 (Del. 1986). See also *Ivanhoe*, 535 A.2d at 1345; *Smith v. Van Gorkom*, 488 A.2d 858, 872 (Del. 1985); *Reder, supra* note 21, at 276; *Warden, The Boardroom as a War Room: The Real World Applications of the Duty of Care and the Duty of Loyalty*, 40 BUS. LAW. 1431 (1985); Comment, *Business Judgment Rule: A Benchmark for Evaluating Defensive Tactics in the Storm of Hostile Takeovers*, 31 VILL. L. REV. 1439, 1447 (1986) (Courts usually recognize duty of care and a duty of loyalty as the two components to the business judgment rule).

39. *Van Gorkom*, 488 A.2d at 872 (an informed decision is made after the directors have considered all material information reasonably available to them); Comment, *supra* note 38, at 1447-48 (duty of care requires an informed decision about whether the takeover offer is in the target company's best interests).

40. *Moran v. Household Int'l Inc.*, 500 A.2d 1346, 1356 (Del. 1985); *Unocal*, 493 A.2d at 954; *Aronson*, 473 A.2d at 812.

directors' responses to either threats originating from third parties or from other shareholders.⁴¹ In *Unocal Corp. v. Mesa Petroleum Co.*, the Delaware Supreme Court added a further element to balance the duty of care obligation. According to the court in *Unocal*:

[if] a defensive measure is to come within the ambit of the business judgment rule, it must be reasonable in relation to the threat posed.⁴²

Thus, unless . . . the directors' decisions were primarily based on perpetuating themselves in office, or some other breach of fiduciary duty such as fraud, overreaching, lack of good faith, or being uninformed, a Court will not substitute its judgment for that of the board.⁴³

To state *Unocal's* "proportionality test"⁴⁴ another way, "when the business judgment rule applies to adoption of a defensive mechanism, the initial burden will lie with the directors."⁴⁵ The directors must have reasonable grounds for believing that a danger poses a threat to company policy and effectiveness, and the defensive mechanism must be reasonable in relation to the threat posed.⁴⁶ Many courts hold that when a board consists of a majority of outside, independent directors and its decision is in accordance with the foregoing standards, its decision is protected by the business judgment rule.⁴⁷

41. *Unocal*, 493 A.2d at 955. *But see* Easterbrook & Fischel, *Proper Role*, *supra* note 21, at 1199-1204. The authors suggest that directors should act passively in response to a takeover offer. They suggest that any action taken by the directors after the takeover offer was made must be shown to have been undertaken for the economic benefit of the company, and not merely undertaken to defeat the offer. "They also suggest that directors should relax, not consult any experts, and let shareholders decide." Easterbrook & Fischel, *Takeover Bids*, *supra* note 21, at 1750.

42. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985). For an extensive discussion about the *Unocal* "proportionality" test, see Gilson & Kraakman, *supra* note 21.

43. *Unocal*, 493 A.2d at 958. *See also* Block & Miller, *supra* note 21. The business judgment rule does not shield directors' conduct which constitutes bad faith, fraud, overreaching, waste of corporate assets, or abuse of discretion, all to the detriment of the shareholders. *Id.* at 50. *See* Panter v. Marshall Field & Co., 646 F.2d 271, 293 (7th Cir.), *cert. denied*, 454 U.S. 1092 (1981) (fraud, bad faith, gross overreaching or abuse of discretion); *Van Gorkom*, 488 A.2d at 872 (same); Pogostin v. Rice, 480 A.2d 619, 627 (Del. 1984) (same); Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971) (same).

44. Gilson & Kraakman, *supra* note 21.

45. *Moran v. Household Int'l Inc.*, 500 A.2d 1346, 1356 (Del. 1985). To see how the *Unocal* test alters the presumption of sound business judgment afforded to non-defensive decisions, see *supra* note 35.

46. *Moran*, 500 A.2d at 1356; *Unocal*, 493 A.2d at 955.

47. *See* Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1343 (Del. 1987) (proof that the board acted in good faith and upon reasonable investigation is materially enhanced when the independent directors are in the majority); *Moran*, 500 A.2d at 1356 (same); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985) (same). *See also* Martin Marietta Corp. v. Bendix Corp., 549 F. Supp. 623, 634 (D. Md. 1981), where the court noted the significance of the make-up of Marietta's board; namely, that only two of the fourteen directors were part of Marietta's management. *But cf.* Panter, 646 F.2d at 300-01 (Cudahy, J., dissenting). Judge Cudahy thought that a majority of non-management (independent) directors on a company's board should not be dispositive. The independents' interest in keeping "their" management, maintaining their reputations,

In addition to successfully fulfilling the duty of care, the directors must also fulfill the duty of loyalty. From the directors' status as a fiduciary, the duty of loyalty requires that the directors act in the best interests of the shareholders.⁴⁸ Therefore, self-dealing, fraud, overreaching by the directors, and the other *Unocal* prohibitions⁴⁹ apply to the duty of loyalty as they do to the duty of care. If such behavior is shown to have occurred during the directors' decisionmaking process, the directors are not afforded the protection of the business judgment rule. Therefore, mere good faith or an honest belief that the transaction was entirely fair will not suffice, and the directors must prove that their decision was objectively or intrinsically fair.⁵⁰

Starting from the premise that the business judgment rule protects good faith and informed business decisions, a logical corollary concerns the methods and factors (*i.e.*, defensive mechanisms) that the directors can utilize to thrust their decision within the ambit of the rule's protection.

II. DEFENSIVE MECHANISMS

When directors make a corporate decision, ordinarily the decision enjoys a presumption of sound business judgment, which can be overcome only by a showing of a breach of a fiduciary duty (*e.g.*, fraud, self-dealing, perpetuation, etc.).⁵¹ If the decision falls within the ambit of the business judgment rule, the court will not substitute its own judgment, as long as there is any rational business purpose attributed to the decision.⁵² However, when directors take a defensive stance in response to a take-over offer, the burden of proving that the directors' decision was an informed decision shifts to the directors, and they must overcome the two hurdles expressed in *Unocal* before their decision will fall within the ambit of the business judgment rule. First, the directors must have reasonable grounds for believing that a threat to corporate policy and effectiveness exists. Second, any defensive mechanism adopted by the directors must be reasonable in relation to the threat posed.⁵³ These addi-

power, prestige, and prominence casts doubts on the premise that a majority of independent directors materially enhances the court's finding of good faith and reasonable investigation.

48. See *supra* note 38 and accompanying text.

49. See cases cited *supra* note 43.

50. *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103, 115 (Del. Ch. 1986). See also *supra* note 33 and accompanying text.

51. See *supra* note 43 and accompanying text.

52. See cases cited *supra* note 34.

53. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985). See also *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1152 (Del. 1989); *Moran v. Household Int'l Inc.*, 500

tional duties are triggered because of the likelihood that the directors may act primarily in their own interests during a takeover response (*i.e.*, to defeat a tender offer and keep their board intact).⁵⁴

While the enhanced *Unocal* duty is not supposed to allow a corporation "to have unbridled discretion to defeat any perceived threat by any Draconian means available,"⁵⁵ most directors' decisions fall under the expanded reach of the business judgment rule. One reason why directors' decisions almost always fall under the rule's protection is the increasing number of defensive mechanisms within the directors' arsenal.⁵⁶ Directors not only have the right, but a duty to oppose any offer which they believe will harm the corporation.⁵⁷

In recent years, the number of defensive mechanisms has only been limited by the ingenuity of attorneys.⁵⁸ For purposes of this Note, only four recent, yet well-established defensive mechanisms will be discussed. They are: (1) the Shareholder Rights Plan; (2) the sale of a valuable asset; (3) a self-tender; and (4) a retaliation counter offer for the shares of the attempted takeover company.

First, the Shareholder Rights Plan ("Poison Pill") was approved by the Delaware Supreme Court in *Moran v. Household International, Inc.*⁵⁹ Household's management adopted the Rights Plan, not in response to an actual threat, but rather as a pre-takeover move to make the company less vulnerable to a takeover attack.⁶⁰ The Plan was implemented to

A.2d 1346, 1356 (Del. 1985); *City Capital Assoc. v. Interco, Inc.*, 551 A.2d 787, 796 (Del. Ch. 1988); *AC Acquisitions*, 519 A.2d at 113.

54. *Revlon Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 180 (Del. 1986); *Unocal*, 493 A.2d at 954. See also Easterbrook & Fischel, *Takeover Bids*, *supra* note 21. During a tender offer, if a conflict of interest exists, the business judgment rule should not apply to directors' decisions. Frequently, when a tender offer is made, the replacement of the incumbent managers would appear inevitable if the tender offer was successful; therefore, the application of the business judgment rule in these situations should be questioned. *Id.* at 1745.

55. *Unocal*, 493 A.2d at 955.

56. *Supra* note 28 and accompanying text. See also Greene & Junewicz, *A Reappraisal of Current Regulation of Mergers and Acquisitions*, 132 U. PA. L. REV. 647, 682, 700-06 (1984), for a discussion of the "Pac-Man," "scorched earth," "crown jewel," fair price, and "Poison Pill" defenses; Lipton & Brownstein, *supra* note 21, at 1414-26; Comment, *supra* note 38, at 1440-42.

57. Block & Miller, *supra* note 21, at 47; Comment, *supra* note 38, at 1452. See also *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334, 1345 (Del. 1987) (directors have both the duty and responsibility to oppose threats); *Unocal*, 493 A.2d at 954 ("board's power to act derives from its fundamental duty and obligation to protect the corporate enterprise . . .").

58. The dominant defensive mechanisms have included: the "Poison Pill," "crown jewel," "white knight," "Pac-Man," and self-tender. For a more comprehensive discussion of the various defensive mechanisms, see *supra* note 11. Also, with the addition of states' antitakeover statutes, directors faced with a hostile takeover have an array of weaponry to thwart off the attack. See, e.g., Booth, *The Promise of State Takeover Statutes*, 86 MICH. L. REV. 1635 (1988); Hablutzel & Selmer, *Hostile Corporate Takeovers: History and Overview*, 8 N. ILL. U.L. REV. 203 (1988).

59. 500 A.2d 1346 (Del. 1985).

60. *Id.* at 1349.

make takeovers, especially "bust-up" takeovers,⁶¹ more difficult. The Plan contained two triggers: (1) where a tender offer for thirty percent of Household shares was made, or (2) where any single entity or group acquired a twenty percent block of Household shares.⁶² If either of the triggering events occurred, and a successful tender offer resulted, Household shareholders could acquire shares of the tender offeror's company at one-half the market value of the shares.⁶³

The *Moran* court upheld the Rights Plan as a valid exercise of the directors' business judgment. Even though the court stated that the Plan was "adopted to ward off possible future advances, and not a mechanism adopted in reaction to a specific threat,"⁶⁴ it held the Plan legitimate because it did not destroy the assets of Household, impair Household's financial flexibility or the market price of its stock, or usurp the shareholders' right to receive tender offers.⁶⁵ While the Plan deters virtually all hostile tender offers, it is not absolute. Household's directors, if faced with a tender offer, would still have to meet the *Unocal* test.⁶⁶ Both in enacting the Rights Plan (or any other defensive mechanism) and in deciding whether to redeem the Plan during a takeover attempt, the directors had to satisfy the *Unocal* requirements of perceiving a threat to corporate policy and effectiveness and adopting a defensive mechanism reasonable in relation to the threat posed,⁶⁷ and by showing good faith and reasonable investigation.⁶⁸ Since the Court believed that the Household directors complied with these requirements, the directors' decision to adopt the Rights Plan was a legitimate business decision, and therefore, was afforded the protection of the business judgment rule.

Before considering the other defensive mechanisms, *Moran* must be distinguished from other cases because the Rights Plan was not adopted in response to any actual takeover attempt, but rather to make any takeover attempt more difficult to consummate. In contrast, the remaining defensive mechanisms are done in response to a takeover attempt. Therefore, other factors may be considered by the directors in determining whether to oppose the takeover offer and adopt a defensive stance. These factors include the "inadequacy of the price offered, nature and

61. *Id.*

62. *Id.* at 1348.

63. *Id.* at 1349. For a discussion of *Moran*, see Comment, *supra* note 38, at 1460-67; Lipton & Brownstein, *supra* note 21, at 1424.

64. *Moran*, 500 A.2d at 1350.

65. *Id.* at 1354.

66. *Id.*

67. See *supra* notes 35 and 45 and accompanying text.

68. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985) (citing *Cheff v. Mathes*, 199 A.2d 548, 555 (Del. 1964)).

timing of the offer, questions of illegality, the impact on 'constituencies' other than shareholders (*i.e.*, creditors, customers, employees, and perhaps even the community generally), the risk of nonconsummation, and the quality of securities being offered in the exchange."⁶⁹

One caveat must be noted. While *Unocal* included consideration of the impact of the takeover on "other constituencies," the same Delaware Supreme Court, one year later in *Revlon, Inc. v. MacAndrew & Forbes Holdings, Inc.*, added that the consideration of "other constituencies," although permissible, has limitations.⁷⁰ In *Revlon*, the court held that such considerations are only permissible when "there are rationally related benefits accruing to the stockholders."⁷¹

The second type of defensive mechanism is the sale of a valuable asset ("Crown Jewel") to another corporation (sometimes called a "White Knight"),⁷² to make the target company less attractive to the potential acquiror.⁷³ In *Whittaker Corp. v. Edgar*, the court found that the sale of an asset which makes a company less attractive to a tender offeror can fall within the protection of the business judgment rule.⁷⁴ However, directors may not sell all of a company's assets in a "scorched earth" policy⁷⁵ to thwart a takeover attempt and then expect to hide behind the business judgment rule's protection. Another potential drawback of a "crown jewel" approach is that finding a friendly buyer for a particular asset and then restructuring one's business to adjust for the loss of the asset are time-consuming, complicated, and costly.⁷⁶

The third type of defensive mechanism is a self-tender, where the company buys back its shares from its shareholders at a price substantially above the bidder's price.⁷⁷ In *Unocal Corp. v. Mesa Petroleum Co.*,

69. *Id.*

70. *Revlon*, 506 A.2d at 182.

71. *Id.*

72. Comment, *supra* note 38. "A 'white knight' is the friendly corporation with which a target corporation arranges to merge in order to avoid being taken over by a raider." *Id.* at 1441 n.3. See also Lipton & Brownstein, *supra* note 21, at 1421, stating that issuing stock to a "friendly" holder can be a valid defense to a hostile takeover. Greene & Junewicz, *supra* note 56, at 701, 705.

73. *Whittaker Corp. v. Edgar*, 535 F. Supp. 933 (N.D. Ill. 1982). See also Lipton & Brownstein, *supra* note 21. By selling off those assets that are most attractive to the bidder, the target may cause the bidder to go away. *Id.* at 1418. "This tactic may be effective if the bidder values some aspect of the target's assets more highly than does the target itself." *Id.*

74. *Whittaker*, 535 F. Supp. at 951.

75. A scorched earth policy concerns the directors attempt to defeat a hostile takeover attempt by selling the company's assets until the company is rendered worthless. See *Joseph E. Seagram & Sons v. Abrams*, 510 F. Supp. 860, 861 (S.D.N.Y. 1981) (court refused to apply the business judgment rule to the management's scorched earth policy to destroy the company rather than have their tenure as directors ended by a raider who successfully takes over the company).

76. Lipton & Brownstein, *supra* note 21, at 1419.

77. *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985). See also Lipton & Brownstein, *supra* note 21, at 1416, noting that self-tenders pose two problems. First, using a self-tender

the court upheld Unocal's discriminatory self-tender on the basis of the business judgment rule.⁷⁸ The court believed that the self-tender, which discriminated against Mesa (a 13% shareholder and a known greenmailer),⁷⁹ was reasonable in relation to the threat posed by Mesa's coercive two-tier⁸⁰ offer that was inadequate in price and offered poor quality securities (*i.e.*, junk bonds).⁸¹ The court approved of Unocal's sacrificing one short-term shareholder (Mesa), who was a speculator, in the interests of long-term loyal investors.⁸² Again, because the directors exercised good faith and conducted a reasonable investigation, as required by their duty to protect the corporate enterprise,⁸³ the business judgment rule protected their decision as having a rational business purpose.⁸⁴

The fourth type of defensive mechanism is to retaliate by making a tender offer for the company making the takeover attempt. For example, the court in *Martin Marietta Corp. v. Bendix Corp.*,⁸⁵ upheld the "Pac-Man"⁸⁶ defense as a valid defense to a takeover attempt. In *Martin*, Bendix made a tender offer for Martin Marietta. Marietta responded by making a counter tender offer for Bendix by borrowing enormous

may not appear attractive to shareholders faced with a takeover bidder's any-and-all cash tender offer. Second, large-scale self-tender offers are only possible when a target has sufficient unrestricted assets to support large borrowing or can successfully effectuate a crown jewel sale. *Id.* See also Comment, *supra* note 38, at 1453-60, discussing *Unocal*.

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

79. See *supra* note 27 and accompanying text. See also Lipton & Brownstein, *supra* note 21. A greenmailer, who accumulates stock and poses a threat of a takeover attempt or proxy fight, does not strive to acquire the company, but to be bought out at a good price. *Id.* at 1413. Such stock repurchases have been sustained by the courts under the business judgment rule, when such repurchases are for a legitimate business purpose and not solely for entrenching management. *Id.* at 1414.

80. Two-tier offers are recognized as "classic coercive measure[s] designed to stampede shareholders into tendering at the first tier, even if the price is inadequate, out of fear of what they will receive at the back end of the transaction." *Unocal*, 493 A.2d at 956. See also Greene & Junewicz, *supra* note 56, at 679-81; Lipton & Brownstein, *supra* note 21, at 1412-13.

81. Junk bonds are typically high-yielding, low-credit bonds or preferred stocks, frequently with variable rate or exchangeability options with warrants or other equity "kickers." *Id.* at 1411-12. Junk bond financed deals subject the target company to a bust-up sale of assets to finance the takeover. *Id.*

82. *Unocal*, 493 A.2d at 955-56. See also Comment, *supra* note 38, at 1458-59.

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

84. For a more in-depth discussion of *Unocal*, see Comment, *Unocal Corp. v. Mesa Petroleum Co.*, 72 VA. L. REV. 851 (1986); Comment, *Unocal Corp. v. Mesa Petroleum Co.: The Selective Self-Tender — Fighting Fire with Fire*, 61 NOTRE DAME L. REV. 109 (1985).

85. *Martin Marietta Corp. v. Bendix Corp.*, 549 F. Supp. 623 (D. Md. 1982).

86. The "Pac-Man" defense refers to a target company's counteroffer for the shares of the would-be acquiror. Block & Miller, *supra* note 21, at 64. The "Pac-Man" defense has certain liabilities. First, it requires a great many unsecured assets or a large amount of free cash. Second, a counteroffer waives the target's assertion of antitrust violation created by the merger, and implicitly signifies a desirability by the target's board to merge. Lipton & Brownstein, *supra* note 21, at 1420. For a discussion of *Martin Marietta*, see Greene & Junewicz, *supra* note 56, at 700-01.

amounts of money to finance the tender offer.⁸⁷ The court held that Marietta's directors had acted in a manner reasonably believed to be within the best interest of Bendix' shareholders.⁸⁸ Marietta's belief that its tender offer would best suit its needs, rather than Bendix',⁸⁹ was held to be a valid reason for the counteroffer.

III. THE EFFECTS OF THE EXPANDED BUSINESS JUDGMENT RULE

A. Cases that Seemingly Protect Shareholders

Next to the *Unocal* case, *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.* is the most influential decision on a directors' duties during a takeover attempt.⁹⁰ *Revlon* is important because it limits the applicability of *Unocal* when the company is up for sale. As the *Revlon* court found, if it becomes "inevitable" that a target company will be sold, the directors' duties change appreciably:

[t]he duty of the board had thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the shareholders' benefit. This significantly altered the board's responsibilities under the *Unocal* standards. It no longer faced threats to corporate policy and effectiveness, or to the stockholders' interests, from a grossly inadequate bid. The whole question of defensive measures became moot. The directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company.⁹¹

In *Revlon*, a bidding war for Revlon between a hostile party and a friendly bidder resulted in a lock-up⁹² agreement and a no-shop⁹³ provision with the friendly bidder; however, the directors had already authorized management to sell the company. The court found that the buyout and lock-up agreement with the friendly bidder, Forstmann Little, signified that the Revlon directors were amenable to the idea of selling the

87. *Martin Marietta*, 549 F. Supp. at 625. See also Greene & Junewicz, *supra* note 56, at 700 n.262.

88. Bendix was a shareholder in Marietta, and therefore, Marietta's decision to make a counteroffer had to take account of both Bendix' and Marietta's shareholders' interests. *Martin Marietta*, 549 F. Supp. at 633.

89. *Id.*

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

91. *Id.* at 182. See also *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334 (Del. 1987) (discussing when *Revlon* and *Unocal* duties kick in); Gilson & Kraakman, *supra* note 21, at 253 n.26; Reder, *supra* note 21.

92. A lock-up option is an arrangement under which a target agrees to sell part of its assets to a friendly suitor if the raider obtains control of the target. *Revlon*, 506 A.2d at 178, 182-84; Comment, *supra* note 38, at 1441 n.3.

93. *Revlon*, 506 A.2d at 178, 184. A no-shop provision prevents a target company from entertaining any additional takeover bids. See also Comment, *supra* note 38, at 1477.

company.⁹⁴ At that point, the "sale" of Revlon was inevitable and the directors' role changed from a defender to an auctioneer.⁹⁵ Therefore, determining when a sale of the company occurs is a critical question. The directors' determination could either: (1) require the *Unocal* "proportionality" test, or (2) require the *Revlon* auction standard.⁹⁶

Because there is no consensus⁹⁷ concerning the appropriate behavior of directors under attack by a hostile takeover, the directors' survival instinct governs takeover responses.⁹⁸ In addition to the litany of factors that *Unocal* stated are permissible for a director to consider during a takeover,⁹⁹ the standard for proving that a board of directors has acted with such gross negligence as to place its decision outside the protection of the business judgment rule seems insurmountable.

The Delaware Supreme Court in *Aronson v. Lewis*,¹⁰⁰ held that "under the business judgment rule director liability is predicated upon concepts of gross negligence."¹⁰¹ More recently, the court reaffirmed the gross negligence standard¹⁰² and expressed an opinion as to what "minimum" requirements a director must meet. First, the court stated that fulfilling a fiduciary obligation "requires more than the mere absence of bad faith or fraud."¹⁰³

[The directors] cannot succumb to influences which convert an otherwise valid business decision into a faithless act. On the other hand, the duty of care requires a director, when making a business decision, to proceed with a 'critical eye' by acting in an informed and deliberate manner respecting the corporate merits of an issue before the board.¹⁰⁴

Therefore, the requirement that a business judgment must be an informed one requires that the directors inform themselves about all material information reasonably available to them before making a

94. *Revlon*, 506 A.2d at 182; Comment, *supra* note 38, at 1478.

95. *Revlon*, 506 A.2d at 182. *But see* Reder, *supra* note 21, at 280-82, stating that a simple "change in control" attack does not trigger the *Revlon* duties. Only when it is clear that the target is going to be broken up and its effectiveness destroyed do *Revlon* duties arise.

96. Gilson & Kraakman, *supra* note 21, at 253 n.26.

97. Greene & Junewicz, *supra* note 56, at 700 n.265.

98. *Id.* at 700.

99. These factors included: the "inadequacy of the price offered, the nature and timing of the offer, questions of illegality, the impact on 'constituencies' other than shareholders (*i.e.*, creditors, customers, employees, and perhaps even the community generally), the risk of nonconsummation, and the quality of securities being offered in the exchange." *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985).

100. 473 A.2d 805 (Del. 1984).

101. *Id.* at 812. *See also* Sinclair Oil Corp. v. Levien, 280 A.2d 717, 722 (Del. 1971) (fraud or gross and palpable overreaching); *supra* note 43 and accompanying text.

102. *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985). *See also Post Smith*, *supra* note 24.

103. *Van Gorkom*, 488 A.2d at 872.

104. *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334, 1345 (Del. 1987). *See also Van Gorkom*, 488 A.2d at 872; *Aronson v. Lewis*, 473 A.2d 805, 816 (Del. 1984).

decision.¹⁰⁵

On the basis of that line of reasoning, the Delaware Supreme Court in *Smith v. Van Gorkom* held that the directors' decision to enter into a merger agreement was uninformed and grossly negligent. Therefore, the court would not defer to the directors' decision as a valid exercise of the business judgment rule. Several factors contributed to the court's decision. First, the directors accepted an offer without investigating whether a higher price could be obtained, and without investigating the value of its company prior to the sale.¹⁰⁶ Second, the directors "were grossly negligent in approving the 'sale' of the company upon two hours consideration, without prior notice, and without the exigency of a crisis or emergency."¹⁰⁷ Also, at the board meeting, no documents concerning the merger agreement were present. The directors relied entirely upon CEO Van Gorkom's twenty minute oral presentation.¹⁰⁸ In addition to the fact that Van Gorkom himself came up with the fifty-five dollar per share offer price,¹⁰⁹ and that no documentation was given as to the adequacy of the fifty-five dollar price per share offer, the "widespread view of Senior Management [was] that the timing of the offer was wrong and the offer inadequate."¹¹⁰ Lastly, the court considered the impact that the merger agreement had on the company—namely, that it precluded the company from receiving or soliciting any other offers.¹¹¹ As a result of these findings, the court denied the directors the protection of the business judgment rule, and the case was remanded to determine an award of damages.¹¹²

B. Cases Illustrating Directors' Power

While one may think that the "gross negligence" standard of director liability, the *Unocal* "proportionality test," and the *Revlon* "auction" limitation to *Unocal* adequately protect shareholders' interests, the above checks and balances are pro-director and are relatively safe from attack

105. *Van Gorkom*, 488 A.2d at 872.

106. *Id.* at 874. See also *Post Smith*, *supra* note 24, at 559.

107. *Van Gorkom*, 488 A.2d at 874. See also *Post Smith*, *supra* note 24, at 562-63.

108. See case cited *supra* note 107.

109. *Van Gorkom*, 488 A.2d at 877 n.19.

110. *Id.* at 877.

111. Thus, this aspect of the Merger Agreement acted similar to the no-shop provision struck down by the *Revlon* court. See *supra* note 93.

112. *Smith v. Van Gorkom*, 488 A.2d 858, 893 (Del. 1985). For a discussion of *Van Gorkom*, see Fischel, *The Business Judgment Rule and the Trans Union Case*, 40 BUS. LAW. 1437 (1985). Fischel notes that the *Trans Union (Van Gorkom)* case sent a signal to firms to obtain fairness letters or similar documents from outside consultants before making decisions to change the corporation. He further asserts that shareholders are the biggest losers after *Trans Union*, because a company can always procure an expert to state that a tender price is a fair market premium price. *Id.* at 1453.

by disgruntled shareholders. The general consensus that shareholders are "protected" is exemplified by one scholar's statement that the "*Van Gorkom* decision stripped corporate directors and officers of the protective cloak formerly provided by the business judgment rule . . ." ¹¹³ The discussion that follows disputes that statement, as well as the view that shareholders are adequately protected.

An important factor that materially enhances a board of director's decision as one made in good faith is that the decision was made by a board comprised of a majority of independent directors.¹¹⁴ Having a board thus composed lessens the probability that the board acted out of motives that are designed to entrench their positions in the corporation.¹¹⁵ However, in the Seventh Circuit Court of Appeal's decision in *Panter v. Marshall Field & Co.*,¹¹⁶ Judge Cudahy stated in his dissenting opinion that:

[t]he fact that Field's may have had a majority of non-management (independent) directors is hardly dispositive. The interaction between management and board may be very strong even where, as here, a relationship of symbiosis seems to prevail over the normal condition of "management domination."

[T]he very idea that, if we cannot trace with precision a mighty flow of dollars into the pockets of each of the outside directors, these directors are necessarily disinterested arbiters of the stockholders' destiny, is appallingly naive.

Directors of a New York Stock Exchange-listed company are, at the very least, "interested" in their own positions of power, prestige, and prominence They are "interested" in defending against outside attack[s] against] the management which they have, in fact, installed or maintained in power—"their" management (to which, in many cases, they owe their directorships). And they are "interested" in maintaining the public reputation of their own leadership and stewardship against the claims of "raiders" who say that they can do better.¹¹⁷

These concerns seriously call into question the blind faith that courts have placed on such directors' decisions.¹¹⁸

113. *Post Smith, supra* note 24, at 559.

114. *See supra* note 47 and accompanying text.

115. *See supra* note 47 and accompanying text. *See also Panter*, 646 F.2d at 300 n.1 ("hostile tender offers unavoidably create a conflict of interest . . . , [because] nearly all directors and managers are interested in maintaining their compensations and perquisites"); *Warner Communications, Inc. v. Murdoch*, 581 F. Supp. 1482, 1491 (D. Del. 1984) (if a target company fails to exercise its business judgment and engages instead in entrenchment tactics, such defensive actions are illegitimate).

116. 646 F.2d 271 (7th Cir.), *cert. denied*, 454 U.S. 1092 (1981).

117. *Id.* at 300-01 (Cudahy, J., dissenting).

118. *See supra* note 47 and accompanying text.

Furthermore, Judge Cudahy argued that the *Panter* decision shredded any remaining constraints which would preclude directors from placing their own interests before the interests of the shareholders when responding to a takeover offer.¹¹⁹ In a harsh critique of the majority's decision, Judge Cudahy:

emphatically disagree[d] that the business judgment rule should clothe directors, battling blindly to fend off a threat to their control, with an almost irrebuttable presumption of sound business judgment, prevailing over everything but the elusive hob goblins of fraud, bad faith or abuse of discretion.¹²⁰

Judge Cudahy's dissenting opinion goes to the heart of the problem associated with the business judgment rule. First and foremost, the "gross negligence" standard is too stringent a requirement for shareholders to meet. While the *Van Gorkom* court expressly stated that neither an outside valuation study (to determine the value of the company) nor a fairness opinion by an independent investment banker is required to support an informed business judgment,¹²¹ the *Van Gorkom* decision has implicitly given mergers and acquisition players its stamp of approval on the use of valuation studies and fairness opinions to render a board's decision informed.¹²² This conclusion seems reasonable in light of the difficulty in proving gross negligence, fraud, and self-dealing.

Another example of the insurmountable odds that shareholders face when they challenge the board of directors' decisions is the "scorched earth" policy involved in the United States District Court for the Southern District of New York's decision in *Joseph E. Seagram & Sons*.¹²³

119. 646 F.2d at 299. The *Panter* court upheld a board's decision to reject a takeover offer based on its preference to remain an independent company. Thus, a board's desire to build value within the company is a rational business purpose for rejecting a takeover believed to diminish the value of the company. *Id.* at 296. The directors' decision to "just say no" to a takeover not thought to be in the best interests of the company has been upheld as a valid defensive decision. See *Amanda Acquisitions Corp. v. Universal Foods Corp.*, 877 F.2d 496, 499 n.4 (7th Cir.), *cert. denied*, 110 S. Ct. 367 (1989); *Panter*, 646 F.2d 271; *Crouse-Hinds Co. v. Internorth, Inc.*, 634 F.2d 690 (2d Cir. 1980).

The *Panter* majority also upheld, under the business judgment rule, the board's decision to file an antitrust suit as a defensive block to the takeover attempt. 646 F.2d at 297. Such a suit challenges the legality of the takeover attempt. *Id.* See *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985), for the litany of factors directors can consider when deciding to reject or effectuate the takeover offer. See also *Whittaker Corp. v. Edgar*, 535 F. Supp. 933, 950 (N.D. Ill. 1982) (Section 7 of the Clayton Act allows a private right of action to obtain an injunction against an unlawful acquisition posed by a takeover bid); *Block & Miller, supra* note 21, at 55.

120. *Panter*, 646 F.2d at 299.

121. *Smith v. Van Gorkom*, 488 A.2d 858, 876 (Del. 1985).

122. *Fischel, supra* note 112, at 1453.

123. *Joseph E. Seagram & Sons v. Abrams*, 510 F. Supp. 860 (S.D.N.Y. 1981). See also *Block & Miller, supra* note 21, at 61, stating that partial or complete liquidation of the target by its board (scorched-earth defense) rests on the target's assumption that the entity is worth more "dead than alive." However, most state corporation laws, including Delaware's, require sales of "all or substantially all" of a company's assets to be submitted for shareholder approval, but the term "all or

The "scorched earth" violation, as well as the gross negligence perpetrated in *Van Gorkom*, demonstrate the extremity that directors must accomplish before the courts will interject into their decisions. With the exception of these two extreme cases, directors have carte blanche to determine the destiny of their shareholders' company.

An added weapon provided to directors to thwart a hostile takeover is the antitakeover statute which many states have enacted over the past few years.¹²⁴ Directors using these statutes as a basis for implementing a defensive mechanism now have the stamp of approval of the state's legislature.

After the United States Supreme Court in *CTS Corp. v. Dynamics Corp. of America*¹²⁵ upheld the constitutionality of the Indiana Control Share Acquisitions Statute, the states were given the green light to promulgate antitakeover statutes. The *CTS* decision, therefore, makes the Court's decision to strike down Illinois' first generation¹²⁶ antitakeover

substantially all" is narrowly construed; thereby many transactions involving the sale of assets never reach the shareholders. *Id.* at 62.

124. See, e.g., ARIZ. REV. STAT. ANN. §§ 10-1201 to 1223 (Supp. 1988); CONN. GEN. STAT. ANN. §§ 33-374a to 374c (West 1987); DEL. CODE ANN. tit. 8, § 203 (Supp. 1988); FLA. STAT. ANN. §§ 607.109-.110 (West Supp. 1988); GA. CODE ANN. §§ 14-2-1131 to 1133 (Supp. 1988); HAW. REV. STAT. §§ 415-171 to 172 (1985 & Supp. 1987); IDAHO CODE §§ 30-1601 to 1614, 30-1701 to 1710 (Supp. 1988); Illinois Corporate Takeover Law, Public Act 86-126 (effective Aug. 2, 1989); IND. CODE ANN. §§ 23-1-42-1 to 11, 23-1-42-1 to 24 (West Supp. 1988); KY. REV. STAT. ANN. §§ 271B.1-010-271B.18-060 (Michie/Bobbs-Merill Supp. 1989); LA. REV. STAT. ANN. §§ 12:135-.140.2 (West Supp. 1988); ME. REV. STAT. ANN. tit. 13-A, § 611-A (Supp. 1988); MD. BUS. REG. CODE ANN. §§ 3-202, 3-601 (1985); MASS. GEN. LAWS ANN. chs. 110C-110E (West Supp. 1988); MICH. COMP. LAWS ANN. §§ 450.1775-.1784 (West Supp. 1988); MINN. STAT. ANN. §§ 302A.671, 302A.673 (West Supp. 1989); MISS. CODE ANN. §§ 79-25-1 to 9 (Supp. 1988); MO. ANN. STAT. §§ 351.407, 351.459 (Vernon Supp. 1989); NEB. REV. STAT. §§ 21-2431 to 2453 (Supp. 1988); NEV. REV. STAT. ANN. §§ 78.378-.3793 (Michie Supp. 1987); N.J. STAT. ANN. §§ 14A:10A-1 to 6 (West Supp. 1988); N.Y. BUS. CORP. LAW §§ 513, 912 (McKinney 1986); N.C. GEN. STAT. §§ 55-9-01-55-9A-09 (Supp. 1990); OHIO REV. CODE ANN. §§ 1701.83-.85 (Anderson 1985 & Supp. 1987); OKLA. STAT. ANN. tit. 18, §§ 1145-1155 (West Supp. 1989); S.C. CODE ANN. §§ 35-2-101 to 111, 35-2-201 to 226 (Law. Co-op. Supp. 1988); TENN. CODE ANN. §§ 48-35-201 to 209, 48-35-301 to 312 (1988); UTAH CODE ANN. §§ 61-6-1 to 12 (Supp. 1988); VA. CODE ANN. §§ 13.1-725 to 727 (Supp. 1988); WASH. REV. CODE ANN. §§ 23A.50.010-.901 (Supp. 1989); WIS. STAT. ANN. § 180.726 (West Supp. 1988).

125. 481 U.S. 69 (1987).

126. The first generation statutes were the states' first attempts to codify provisions into law that would enable in-state corporations to protect themselves against hostile takeovers. These statutes met their demise with the Supreme Court's decision in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982). See Hablutzel & Selmer, *Hostile Corporate Takeovers: History and Overview*, 8 N. ILL. U.L. REV. 203, 210-13 (1988).

The next form of takeover statutes, second generation statutes, was given some approval by the Supreme Court's decision in *CTS*. However, the second generation statutes came in three different forms: business combination, fair price, and control share acquisition statutes. A business combination statute precludes any person who buys, for example, 20% or more of a company's stock from acquiring the company for a certain period of time (e.g., five years) unless the purchaser of stock had board approval to purchase the stock. *Id.* at 214. A fair price statute requires shareholders to vote to ratify any business combinations, unless two-thirds of the disinterested directors approve the business combination or all shareholders receive a fair price for their shares, as computed by a specific

statute in *Edgar v. MITE Corp.*¹²⁷ less prohibitive to states attempting to formulate an antitakeover statute which can pass constitutional muster. The Indiana Act involved in *CTS* provides states with a model with which to compare their own statutes. The states were given an added shot of confidence when the Seventh Circuit upheld the constitutionality of Wisconsin's Anti-Takeover Statute.¹²⁸ Seventh Circuit Judge Easterbrook, who strongly believes in director passivity during takeovers,¹²⁹ wrote the opinion in *Amanda Acquisition Corp. v. Universal Foods Corp.* upholding the Wisconsin law, even though he stated that "[l]ike our colleagues who decided *MITE* and *CTS*, we believe that antitakeover legislation injures shareholders."¹³⁰ The problem associated with antitakeover statutes is that they preclude shareholders from receiving or accepting a premium offer. Thus, shareholders and the economy are worse off because the higher bid reflects the better use to which the bidder can put the target's assets to.¹³¹

For instance, Wisconsin's Anti-Takeover Statute does not add options to a company's desire to give its directors more discretion to determine the salability of a takeover offer; instead, it destroys the possibility of divergent choices.¹³² Under the Wisconsin law, "[u]nless the target's board agrees to the transaction in advance, the bidder must wait three years after buying the shares to merge with the target or acquire more than 5% of its assets."¹³³ While the Seventh Circuit stated its dislike and skepticism of antitakeover statutes, it concluded that such skepticism does not mean that the law is beyond the state's power.¹³⁴

formulation. *Id.* Lastly, a control share acquisition statute applies to acquisitions of shares which surpass a threshold as established by the directors (e.g., one-fifth, one-third, or a majority of the voting power). Thus, such acquisitions are prohibited unless the acquiror procures prior authorization by obtaining a majority vote of both shareholders and disinterested shareholders. *Id.* at 214-15. For a comparison of the three forms of second generation statutes, see generally *id.* at 226-29.

After the Supreme Court, in *CTS*, upheld the constitutionality of Indiana's statute, many states enacted third generation statutes assuming that the *CTS* decision placed its general stamp of approval on all forms of antitakeover statutes. See Steinberg, *Federal Preemption of State Anti-takeover Statutes: The Time for Congressional Action is Now*, 16 SEC. REG. L.J. 80, 83-85 (1988); Johnson & Millon, *Does the Williams Act Preempt State Common Law in Hostile Takeovers?*, 16 SEC. REG. L.J. 339 (1989). Both of the above cited articles provide support for the argument that the Williams Act may preempt states from regulating merger activity via state antitakeover statutes.

127. 457 U.S. 624 (1982). The Supreme Court held that Illinois' Anti-Takeover Statute was unconstitutional, because it violated the Williams Act and the Commerce Clause.

128. *Amanda Acquisitions Corp. v. Universal Foods Corp.*, 877 F.2d 496 (7th Cir.), cert. denied, 110 S. Ct. 367 (1989).

129. See Easterbrook & Fischel, *Proper Role*, supra note 21.

130. *Amanda*, 877 F.2d at 500.

131. *Id.* at 500-01. See also Easterbrook & Fischel, *Proper Role*, supra note 21.

132. *Amanda*, 877 F.2d at 502.

133. *Id.* at 497-98.

134. *Id.* at 502.

The significance of the antitakeover statutes is that legislatures have now condoned the directors' use of defensive mechanisms. How can a court, confronted with a board's implementation of a defensive mechanism sanctioned by a state legislature¹³⁵ and by the United States Supreme Court,¹³⁶ hold that the board's action falls outside the scope of the business judgment rule—especially in light of the gross negligent standard for abusive behavior? Thus, these statutes only legitimize the shareholders' feelings that they have no say in the control of "their" company.

The following example illustrates the potency of these statutes. On August 2, 1989, Governor Thompson of Illinois signed into law major amendments to the Illinois Business Corporation Act as it relates to corporate takeovers.¹³⁷ One of the most profound provisions, promulgated in 1985, concerned the legislature's granting directors the option of considering the impact of the takeover on "other constituencies,"¹³⁸ but only in the context of considering the best long-term and short-term interests of the company.¹³⁹ The significance of this provision is that directors, who are supposed to make corporate decisions to maximize shareholder welfare, can now justify their decisions by considering the impact of their

135. See statutes cited *supra* note 124.

136. See *CTS Corp. v. Dynamics Corp. of America*, 481 U.S. 69 (1987); *Edgar v. MITE Corp.*, 457 U.S. 624 (1982); *Amanda Acquisitions Corp. v. Universal Foods Corp.*, 877 F.2d 496 (7th Cir.), *cert. denied*, 110 S. Ct. 367 (1989).

137. Illinois Corporate Takeover Law, Public Act 86-126 (effective Aug. 2, 1989 amended §§ 6.05, 8.85, and adding § 11.75).

138. See *Unocal Corp. v. Mesa Petroleum Co.* 493 A.2d 946, 955 (Del. 1985), stating that directors can consider "other constituencies" (e.g., employees, creditors, the community, etc.) when considering a takeover attempt. See also *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del. 1986), where the court imposed a limitation on the consideration of "other constituencies." Cf. Eizenstat & Fullerton, *Crying Wolf on Takeovers*, NAT'L L.J. 13 (1989). The recently passed Exon-Florio provision of the Omnibus Trade Act provides another consideration for directors during a takeover attempt. However, the Exon-Florio provision was initially designed to apply to friendly transactions, not to be misused by directors opposing hostile takeovers. The Exon-Florio provision authorizes the President to investigate and block foreign acquisitions that pose a security risk. The potential abuse arises because every company is in a national security business when threatened by an unwanted suitor. This article demonstrates the breadth of the "other constituencies" consideration, namely that directors can consider the effects of the takeover bid on the national security interests of the United States of America. See also Easterbrook & Fischel, *Proper Role*, *supra* note 21, at 1190-92; Reder, *supra* note 21. "[I]f a benefit to the stockholders can be found, the directors appear able to consider the aggregate of their 'constituencies,' not just their shareholders." *Id.* at 278.

139. *Supra* note 137, at § 8.85 and *supra* note 138 and accompanying text. Other states that have similar provisions include: Arizona, ARIZ. REV. STAT. ANN. § 10-1202(A) (1987); Idaho, IDAHO CODE § 30-1702 (1988); Indiana, IND. CODE § 23-1-35-1(d) (1988); Kentucky, KY. REV. STAT. ANN. § 271B.12-210(4) (Michie/Bobbs-Merrill 1989); Maine, ME. REV. STAT. ANN. tit. 13-A, § 716 (1989); Minnesota, MINN. STAT. § 302A.251(5) (1988); Missouri, MO. REV. STAT. § 351.347 (1988); Nebraska, NEB. REV. STAT. § 21-1983 (1989); New Mexico, N.M. STAT. ANN. § 53-11-35(D) (1987); Ohio, OHIO REV. CODE ANN. § 1701.59(E) (Anderson 1988); Pennsylvania, 42 PA. CONS. STAT. § 8363 (1989); and Wisconsin, WIS. STAT. § 180.305 (1987).

decisions on other groups (e.g., customers, creditors, and the community). The interests of these other groups, however, may not necessarily comport with shareholder interests or wishes.

In addition to state legislatures condoning directors' decisions and the litany of factors that a director can consider when responding to a takeover,¹⁴⁰ the general ease of meeting the business judgment standard makes almost any business decision fall within its protection.¹⁴¹ After all, under the business judgment rule, the directors' decision will not be disturbed if it can be attributed to any rational business purpose.¹⁴² The ease with which one can formulate any "rational" business purpose has the effect of immunizing any directors' decisions from judicial scrutiny—save for the rare cases where the board acts with gross negligence or utilizes fraud, overreaching, or a scorched earth policy. The Delaware Supreme Court's most recent decision on the propriety of directors' actions during a hostile takeover is the culmination of directors' *carte blanche* ability to unilaterally decide the viability of a corporation.

IV. *PARAMOUNT COMMUNICATIONS V. TIME, INC.*

Illustrative of the abusive treatment shareholders have faced and will continue to face is the Delaware Supreme Courts' most recent decision, *Paramount Communications v. Time, Inc.*¹⁴³ According to one source, the *Time* decision may have changed the world for all corporate managers, directors, shareholders, and potential acquirors.¹⁴⁴ The *Time* decision has enlarged the power of corporate directors in that they can run the company as they see fit without seeking a shareholder vote on major decisions.¹⁴⁵ Most notably, *Time* calls into question the validity of *Unocal*'s requirement that takeover responses must be "reasonable" in relation to the threat posed.

Paramount and various Time shareholders sued Time in a Delaware Chancery Court seeking an injunction restraining Time from consummating a merger with Warner Communications.¹⁴⁶ On July 14, 1989,

140. *Unocal*, 493 A.2d at 955.

141. For example, if in *Smith v. Van Gorkom*, 488 A.2d 858, 876 (Del. 1985), the board was fully informed, their accumulation of tax credits would have been an adequate reason to enter into merger negotiations. Also, if the directors in *Joseph E. Seagram & Sons v. Abrams*, 510 F. Supp. 860 (S.D.N.Y. 1981), had only sold some assets or put the sale of assets decision to a shareholder vote, their decision would have fallen within the ambit of the business judgment rule. See *supra* note 123 and accompanying text.

142. See cases cited *supra* note 34.

143. 571 A.2d 1140 (Del. 1989).

144. *A Legal Victory for the Long Term*, FORTUNE, August 14, 1989, at 56.

145. Wall St. J., July 25, 1989, at A11, col. 1.

146. *Time*, 571 A.2d at 1141-42.

Chancellor William T. Allen refused to issue the injunction because he believed that the plaintiffs would be unable to prevail on the merits.¹⁴⁷ Plaintiffs filed an interlocutory appeal, which the Delaware Supreme Court accepted on an expedited basis. On July 24, 1989, the court orally affirmed Chancellor Allen's ruling. A revised written opinion was issued March 9, 1990.

A. *The Genesis of the Time-Warner Merger Agreement*¹⁴⁸

In 1983-84, Time, one of the largest suppliers of information to the populace,¹⁴⁹ decided to expand its entertainment and media markets.¹⁵⁰ Seeking to serve a global economy, Time's management sought out an expansive long-term goal.¹⁵¹ However, because Time wanted to maintain its independence and distinctive and important "Time Culture,"¹⁵² the board attempted to look for a company with which Time could merge, and yet, achieve all of its goals (global economy and Time culture).

In spring 1987, Time's management contacted Warner concerning a joint venture; however, these discussions never led to a definitive proposal.¹⁵³ As an alternative to the failed joint venture with Warner, in July

147. *Id.* at 1142.

148. For a comprehensive explanation of the Time/Warner merger, see Saporito, *The Inside Story of TIME WARNER*, FORTUNE, Nov. 20, 1989, at 164.

149. Time's business was divided into four divisions: publication of magazines (*Time*, *People*, *Fortune*, *Sports Illustrated*, etc.); publication of books (Book-of-the-month club, Little, Brown & Co., Time-Life Books, etc.); production of pay television programs HBO and CINEMAX; and ownership and operation of cable television franchises. *Id.* at 170.

150. Time's desire to expand its video market created a need to own a video or film products company to supply films to its HBO and CINEMAX programs or fall mercy to the quality and price whims of unfriendly suppliers. *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1143-44 (Del. 1989).

151. "In 1987, Time established a special committee of executives to consider and propose corporate strategies for the 1990s." *Id.* at 1143.

152. Time's "culture" stems from its desire to remain independent and its "pride in the history of [its] firm—notably Time Magazine and its role in American life—and its managerial philosophy and distinctive structure that is intended to protect journalistic integrity from pressures from the business side of the [Time] enterprise." *Paramount Communications v. Time, Inc.*, No. 10866, at 6-7 (Del. Ch. July 14, 1989) (LEXIS, States Library, Del.); *Time*, 571 A.2d at 1143 n.4, 1152. See also *supra* note 119 and accompanying text. Time's unique structure of having the Editor in Chief report directly to a special committee of the board of directors protected its "culture" or value of journalistic independence, which Time had found to have been economically advantageous. *Time*, No. 10866, at 9 [LEXIS]. However, the court stated that since Time's magazine business contributes about 40% to its gross revenue, and will contribute about 20-25% of the merged Time-Warner's revenues, then some other motivation besides protecting journalistic integrity might be underlying Time's assertion of the defense of "culture." *Id.* See also *What is Corporate Culture?*, THE BANKERS MAGAZINE, Jan.-Feb. 1988, at 33-34, describing in detail the factors comprising a bank's corporate culture. For example, the company's personality (*i.e.*, culture) is comprised of patterns (beliefs, behaviors, and assumptions) shared by members of an organization and learned over time as a result of past successes. Such a culture is durable, resistant to change, and requires significant time and resources for modification. *Id.*

153. *Time*, 571 A.2d at 1144. After Time management reviewed many studios (*e.g.*, Disney,

1988, Time's board approved negotiation of a merger agreement with Warner provided, however, that certain conditions be met.¹⁵⁴ Negotiations were shaky because the parties could not agree on a management structure that satisfied Time's need to ensure continuation of its "culture"—which required the ultimate succession of Time executives to the senior executive positions.¹⁵⁵ They finally agreed to a twenty-four member board equally divided between incumbent directors of both companies. However, discussions again broke off in August because of disagreement concerning who would succeed as the chief executive officer.¹⁵⁶

In January 1989, negotiation reopened and the companies finally agreed to the succession of Nick Nicholas, Time's President and Chief Operating Officer, as the sole CEO of the New Time-Warner Corporation.¹⁵⁷ The merger agreement consisted of a stock for stock deal that provided Warner shareholders with a 12% premium.¹⁵⁸ The agreement was approved by both boards on March 3, 1989. Such a stock deal required Time to submit the merger agreement for shareholder approval.¹⁵⁹

Before Time obtained the necessary shareholder approval, however, on June 7, 1989, Paramount made a \$175 per share cash offer¹⁶⁰ for all of Time's outstanding common stock.¹⁶¹ The shareholder plaintiffs felt that

MCA-Universal, Columbia, 20th Century Fox, Warner, and Paramount), Warner was considered the best fit, based on its outstanding video and film production capacity and talent, and a substantial and effective international marketing relationship. *Id.* at 1144-45.

154. The negotiations were conditionally approved by a large majority of outside directors, not a unanimous number. The approval was conditional on a "corporate governance" issue, namely that Time's senior management must be assured succession to the ultimate control of the combined entity. *Id.* See also *supra* notes 47 and 54 and accompanying text, self-preservation decisions by the board are not protected by the business judgment rule.

155. *Time*, 571 A.2d at 1145. See also *supra* note 152 and accompanying text.

156. *Time*, 571 A.2d at 1145.

157. *Id.*

158. See *Paramount Communications v. Time, Inc.*, No. 10866, at 11 (Del. Ch. July 14, 1989) (LEXIS, States Library, Del.). The Delaware Supreme Court's opinion does not discuss the percentage of premium that Warner shareholders would receive, only that an exchange ratio of .465 was agreed upon, which gave Warner shareholders 62% ownership of Time-Warner. *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1146 (Del. 1989). The Share Exchange Agreement gave each party the option of automatically obtaining shares of the company should the merger fail to be completed. *Time*, 571 A.2d at 1146. Warner did trigger its share rights in Time (11%) after the Paramount bid. *Time*, No. 10866, at 12 [LEXIS].

159. *Time*, 571 A.2d at 1146.

160. *Id.* at 1147. However, Paramount's offer contained the following conditions: (1) termination of the Time-Warner merger agreement; (2) termination of the Share Exchange Agreement; (3) approval of all franchise transfers; (4) redemption of Time's poison-pill plan and removal of other defensive devices; (5) financing and majority acceptance by Paramount; and (6) judicial determination that Delaware's Anti-Takeover Statute was inapplicable to a Time-Paramount merger. *Id.*

161. Paramount's any-and-all cash offer is different from a coercive two-tier offer. See *supra* note 80 and accompanying text. While the board does not have to act passively when confronted

the signing of the merger agreement, with its effect of "changing" control over Time, put Time in "Revlon Mode"¹⁶² and required Time to seek the best available transaction for the shareholders.¹⁶³ The effect of Paramount's offer caused Time's stock to jump forty-four points in one day.¹⁶⁴ Time's management immediately attacked Paramount for tendering a "smoke and mirrors" offer.¹⁶⁵ Then, Richard Munro, Time's Chairman and CEO, stated both that Time had a binding deal with Warner and that Time was not for sale. He added that he would not even consider what Paramount might be willing to offer on a negotiated basis.¹⁶⁶ Time ultimately did consider Paramount's offer, but the consensus of the board was that Time was under a commitment to the Warner deal.¹⁶⁷ After further negotiations with Warner, Time decided to officially reject the Paramount offer and change the Warner transaction from a stock deal to a cash acquisition of a majority stake in Warner

with an any-and-all cash offer at a fair price, "a defensive step that includes a coercive self-tender (or forced merger as in *Time*) timed to effectively preclude a rational shareholder from accepting the any-and-all offer cannot, in my opinion, be deemed to be reasonable in relation to any minimal threat posed to stockholders by such offer." *AC Acquisitions Corp. v. Anderson Clayton & Co.*, 519 A.2d 103, 114 (Del. Ch. 1986). See also *Robert M. Bass Group, Inc. v. Evans*, 552 A.2d 1227, 1243-44 (Del. Ch. 1988) (depriving shareholders of choosing between an any-and-all offer and a less attractive offer is unreasonable, directors, as fiduciaries, cannot "cram down" the shareholders' throat a less attractive offer in order to "protect" the shareholders from a non-coercive, economically superior offer—"under *Unocal*, the directors were obligated to give the shareholders a choice"); *City Capital Assoc. v. Interco, Inc.*, 551 A.2d 787, 798 (Del. Ch. 1988) (there may come a time when a board's fiduciary duty will require the board to permit the shareholders to choose between a noncoercive offer and another alternative); *Gilson & Kraakman*, *supra* note 21, at 259 ("threats" imposed by a noncoercive come from the directors' belief that shareholders will mistakenly accept the offer). Also, discussing whether *Unocal* provides directors with a screen to unilaterally block shareholders from choosing at all. *Id. But cf. Time*, 571 A.2d at 1153, where the court rejected the plaintiffs' argument that the only threat an all-cash offer poses to shareholders is an inadequate value. The court stated that plaintiffs' argument was "a narrow and rigid construction of *Unocal*." *Id.* Furthermore, the court held that Time's board was not "cramming down" on its shareholders a management-sponsored alternative, but rather had as its goal the carrying forward of a pre-existing transaction in an altered form." *Id.* at 1155 (footnote omitted).

162. *Id.* at 1149. See also *supra* note 95 and accompanying text. In *Time*, plaintiffs contended that the Warner merger constituted an implicit decision, as in *Revlon*, by Time to transfer control of the company to Warner—the 62% ownership by Warner after the merger formed the basis of the plaintiffs' argument. *Time*, 571 A.2d at 1146. Defendants countered that the merger was not intended to sell or transfer control of Time, but to preserve and improve Time's long-term performance. *Id.* at 1144-45.

163. *Id.* at 1149.

164. See *Paramount Communications v. Time, Inc.*, No. 10866, at 13 (Del. Ch. July 14, 1989) (LEXIS, States Library, Del.), for a listing of the increased price of Time's and Warner's shares after the Paramount offer.

165. *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1147 (Del. 1989).

166. *Time*, No. 10866, at 13-14 [LEXIS]. For an argument that directors should allow shareholders to choose between alternative offers, see *supra* note 161.

167. See *Time*, 571 A.2d at 1148, where the Time board stated that the Paramount deal was inadequate and posed a threat to Time's retention of its "culture," while the Warner deal was a much more attractive deal.

followed by a merger for cash, securities, or a combination of both.¹⁶⁸ This alternative became the more attractive course to consummate the merger because it did not require shareholder approval as the stock deal had.¹⁶⁹

However, one problem resulted from Time's decision to switch the method of consummating the merger with Warner. There was some question whether Time's shareholders would applaud the rejection of a \$175 per share cash offer and give management additional years to manage the value of Time shares to levels substantially higher than the \$175 offer amount.¹⁷⁰ Therefore, the directors felt that the alternative mode of acquisition was necessary to consummate the Warner deal and avoid shareholders' temptation to grab the Paramount cash offer and run.¹⁷¹

There were other problems associated with the cash acquisition. First, whereas the original stock deal provided Warner shareholders with a 12% premium for their shares, the new cash acquisition provided them with a 56% premium.¹⁷² Second, as a result of the cash acquisition, Time would incur \$10 billion in debt, severely reducing its ability to support additional borrowing.¹⁷³ Third, reported earnings of the new entity were expected to be eliminated by the amortization of approximately \$9 billion of goodwill.¹⁷⁴

On June 23, 1989, in response to Time's revised merger agreement, Paramount increased its per-share cash bid to \$200.¹⁷⁵ Time's management responded to the increased offer with the same factors relied on to reject the \$175 offer.¹⁷⁶

168. *Id.*

169. *Paramount Communications v. Time, Inc.*, No. 10866, at 14 (Del. Ch. July 14, 1989) (LEXIS, States Library, Del.).

170. *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1148 (Del. 1989). While Time advisors established a range of value for Time between \$189.88-212.25, and Paramount's second offer of \$200 fell within that range, another Time advisor thought that after the merger Time-Warner would trade at around \$150 per share. *Time*, No. 10866, at 15 [LEXIS]. Thus, the court reasoned that most money managers would be tempted by the cash offered by Paramount now, *Id.* at 17, even though Time's advisors projected long-term trading ranges of \$159-247 for 1991, \$230-332 for 1992 and \$208-402 for 1993. *Id.* at 16.

171. *Id.* at 17.

172. *Id.* at 18.

173. *Time*, 571 A.2d at 1148. See also Wall St. J., July 25, 1989, at 43, A11; Saporito, *The Inside Story of TIME WARNER*, FORTUNE, Nov. 20, 1989, at 164. Time-Warner paid \$451 million in interest and financing fees and took a \$40 million earnings loss for amortization of good will, contributing to a loss for the third quarter of \$176 million. *Id.* at 208. Moreover, the \$200 a share Time stockholders did not get, at 12% a year, will be worth \$352 in five years, and \$621 in ten years. Recently, Time-Warner's stock was trading at \$70 7/8 per share. Wall St. J., Sept. 26, 1990, at C5.

174. *Time*, No. 10866, at 18 [LEXIS]. See also *Time*, 571 A.2d at 1148 (the court stated that "[n]ine billion dollars of the total purchase price would be allocated to the purchase of Warner's goodwill").

175. *Time*, 571 A.2d at 1149.

176. *Id.*

After Time rejected Paramount's new offer and elected to acquire Warner with cash, as opposed to the original stock swap, Paramount and various Time shareholders filed suit in Delaware to enjoin Time's proposed acquisition of Warner. The court began part of its analysis by stating that it is not part of the court's function to determine the adequacy or inadequacy of the Time-Warner deal for the shareholders.¹⁷⁷ Time's shareholders complained that not only did Warner's shareholders receive a substantial premium (56%) and Time shareholders get little, but that they were foreclosed from considering the premium from Paramount.¹⁷⁸ While the lower court focused its discussion on two questions: (1) should the court recognize a distinction between managing for current maximization and managing for longer-term value creation, and (2) who should make such choices—the board or the shareholders,¹⁷⁹ the Supreme Court of Delaware sought to answer the following question: "Did Time's board, having developed a strategic plan of global expansion to be launched through a business combination with Warner, come under a fiduciary duty to jettison its plan and put the corporation's future in the hands of its shareholder?"¹⁸⁰

From the start, the court tipped the scales in favor of the directors as the group best suited to understand the undervaluation of the company's stock by the stock market.¹⁸¹ The court concluded that, under Delaware law, directors are under no obligation to maximize the immediate value of the corporation or its shares, except when the corporation is in "Revlon Mode."¹⁸² The lower court held that, "Delaware law does recognize that directors, when acting deliberately, in an informed way, and in the good faith pursuit of corporate interests, may follow a course designed to achieve long-term value even at the cost of immediate value maximization."¹⁸³ The Delaware Supreme Court, while affirming Chan-

177. *Id.* at 1151.

178. *Id.* See also *supra* notes 161 and 170.

179. *Paramount Communications v. Time, Inc.*, No. 10866, at 21 (Del. Ch. July 14, 1989) (LEXIS, States Library, Del.). See Easterbrook & Fischel, *supra* note 41, discussing the passivity role managers should assume during takeover bids.

180. *Paramount Communications v. Time Inc.*, 571 A.2d 1140, 1149-50 (Del. 1989).

181. See *Time*, 571 A.2d at 1150 n.12. See also *Time*, No. 10866, at 22 [LEXIS], discussing the undervaluation of stock by the market, and showing two examples of companies that succeeded after rejecting a takeover attempt.

182. *Time*, 571 A.2d at 1150. See also *Ivanhoe Partners v. Newmont Mining Corp.*, 535 A.2d 1334 (Del. 1987); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986). The court noted that when a board enters into a "change in control" transaction, it enters "Revlon Mode." *Time*, 571 A.2d at 1150. Furthermore, a subjective disinclination to sell the company does not prevent the *Revlon* duty from arising when a "change in control" transaction is involved. See *Time*, No. 10866, at 23 [LEXIS]. *But cf.* *Reder*, *supra* note 95 (a mere "change in control" attack does not trigger *Revlon* mode).

183. *Time*, No. 10866, at 23 [LEXIS]. The court used charitable contributions as an example of

cellor Allen's decision, thought that it was "unwise to place undue emphasis upon long-term versus short-term corporate strategy."¹⁸⁴ Because the court believed that the directors' duty to manage the business and affairs of the corporation¹⁸⁵ encompassed the "authority to set a corporate course of action, including time frame, designed to enhance corporate profitability."¹⁸⁶ The court stated that the directors' duty to set a corporate course could not be delegated to the shareholders.¹⁸⁷

The lower court also considered the shareholders' assertion that, under the duty of loyalty, the directors were obliged to let the shareholders choose whether the company should be sold.¹⁸⁸ This assertion had two parts. First, because the directors initially decided to put the stock deal merger to shareholder vote, they were committed to let the shareholders vote on the merger; therefore, the taking away of the stockholder voting right constituted a breach of the duty of loyalty.¹⁸⁹ Second, the *Unocal* test and its progeny required directors, in some circumstances (e.g., the redemption of a "Poison Pill"), to permit shareholders to choose between two alternative, but functionally equivalent, transactions.¹⁹⁰

The lower court responded by stating that the directors' refusal to consider offers may comport with a valid exercise of business judgment.¹⁹¹ As support, the court cited the litany of factors that the *Unocal* court concluded were valid reasons for rejecting a takeover offer.¹⁹² Moreover, the court held that the merger did not constitute a change in control, thus triggering "Revlon Mode."¹⁹³ That 62% of the Time-Warner shares would be held by former Warner shareholders was considered irrelevant.¹⁹⁴ Furthermore, Chancellor Allen held that the origi-

a long-term policy not within the immediate value maximization interests of the company. *Id.* at 23 n.15. However, charitable contributions neither cause \$10 billion in debt assumption, nor do they result in disgruntled shareholders, as a result of taking away the opportunity to vote on the merger or choose between alternative deals—thus depriving shareholders of a premium. *See also supra* note 161 and accompanying text.

184. *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1150 (Del. 1989).

185. *See supra* note 36 and accompanying text.

186. *Time*, 571 A.2d at 1150. According to the court, this duty renders the question of "long-term" versus "short-term" values irrelevant. *Id.*

187. *Id.* at 1154.

188. *See supra* note 161 and accompanying text.

189. *Paramount Communications v. Time, Inc.*, No. 10866, at 24 (Del. Ch. July 14, 1989) (LEXIS, States Library, Del.).

190. *Id.* *See also supra* notes 41 and 160 and accompanying text.

191. *Time*, No. 10866, at 26 [LEXIS].

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

193. *Time*, No. 10866, at 26 [LEXIS].

194. *Id.* The court reasoned that, under some circumstances, a stock for stock merger could reflect a "change in control" transaction; however, where the shares of both companies were widely held, control remained in the market. *Id.* This is problematic for two reasons. First, Warner owned

nal merger agreement did not legally preclude or impede a *later* sale or result in a change of control transaction.¹⁹⁵

Chancellor Allen's finding that a "change of control" situation did not occur was based on the fact that control of Time existed in the market.¹⁹⁶ While the Delaware Supreme Court stated that this finding was correct as a matter of law, it rejected the plaintiffs' *Revlon* claim on different grounds. The court's decision was based upon the lack of any substantial evidence demonstrating the decision of Time's board to make "the dissolution or break-up of the corporate entity inevitable"¹⁹⁷ According to the court, *Revlon* duties arise in two situations:

[1] [W]hen a corporation initiates an active bidding process seeking to sell itself or to effect a business reorganization involving a clear break-up of the company.

[2] [W]here, in response to a bidder's offer, a target abandons its long-term strategy and seeks an alternative transaction involving the break-up of the company.¹⁹⁸

Therefore, where the board is not abandoning the corporation's existence, but merely taking a defensive response to a hostile takeover, it is not *Revlon* duties which arise, but *Unocal* duties.¹⁹⁹

The Delaware Supreme Court agreed with Chancellor Allen that *Revlon* duties do not arise merely because the transaction may "be construed as putting a corporation either 'in play' or 'up for sale'."²⁰⁰ Moreover, the court held that "[t]he adoption of structural safety devices [such as Time's utilization of a lock-up agreement, no-shop clause, and dry-up agreements]²⁰¹ alone does not trigger *Revlon*."²⁰² A board's adoption of such safety devices, the court noted, were subject to a *Unocal* analysis.

If the directors acted in a defensive manner and invoked the "proportionality" test of *Unocal*, then under *Unocal* the directors were required to prove that any defensive steps taken by them were reasonable

62% of the new entity. This must amount to a large block of shares held by "one" shareholder; therefore, the court's determination that this was irrelevant seems incorrect. Second, all companies have ultimate control in the market if they are publicly held.

195. *Id.* at 27.

196. *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1150 (Del. 1989).

197. *Id.*

198. *Id.*

199. *Id.* at 1150-51.

200. *Id.* at 1151.

201. The dry-up agreements consisted of Time's payment to various banks for confidence letters whereby the banks promised not to provide financing for any potential acquirors of Time. *Id.* at 1146.

202. *Id.* at 1151.

in relation to the threat posed.²⁰³ First, the court noted that Paramount's offer was noncoercive.²⁰⁴ The lower court stated that it was "aware of no principle, statute or rule of corporation law that would hold that once a board approves an agreement of merger, it loses power to reconsider that action prior to a shareholder vote."²⁰⁵ The Delaware Supreme Court, however, stated that noncoercive all-cash, all-shares offers can pose sufficient "threats" to the corporation which can warrant defensive responses protected under *Unocal*.²⁰⁶ Initially, the court noted that any consideration by a court of long-term versus short-term goals distorts the *Unocal* process—most notably, that the defensive measure adopted by the board be reasonable in relation to the threat posed.²⁰⁷ Next, the court listed several legitimate "threats" that Time directors relied upon both in rejecting Paramount's offer and in reformulating the Warner merger.²⁰⁸ Lastly, because the court found that Time directors had adequately informed themselves of any potential benefits from a Paramount takeover, the court held that "Time's board was under no obligation to negotiate with Paramount."²⁰⁹

Because the original merger agreement with Warner occurred before the takeover attempt by Paramount, the court was correct in stating that that particular decision did not fall under the enhanced business judgment rule required by *Unocal*. The *Unocal* standard applies to all defensive actions taken after a hostile takeover attempt has emerged.²¹⁰ However, Time's substitution of the cash acquisition for the stock deal was a defensive action taken after the Paramount takeover bid, and must be analyzed under the *Unocal* "reasonable in relation to the threat

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

204. The court noted that "the Court of Chancery has suggested that an all-cash, all-shares offer, falling within a range of values that a shareholder might reasonably prefer, cannot constitute a legally recognized 'threat' to shareholder interests sufficient to withstand a *Unocal* analysis." *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1152 (Del. 1989). For a more detailed discussion on coercive offers, non-coercive offers, and shareholder choice, see *supra* notes 80 and 161 and accompanying text.

205. *Paramount Communications v. Time, Inc.*, No. 10866, at 29 (Del. Ch. July 14, 1989) (LEXIS, States Library, Del.). However, if a board can reconsider a merger agreement with Company X, then it should likewise have to consider alternative and more attractive offers made by companies A-N. See *supra* note 161 and accompanying text.

206. *Time*, 571 A.2d at 1153.

207. *Id.*

208. The court listed such "threats" as: (1) a concern that Time shareholders would accept Paramount's cash offer because of mistaken belief or ignorance of the benefits of a Warner merger; (2) that the conditions of Paramount's offer resulted in uncertainty; and (3) that Paramount's offer was intentionally timed so as to confuse Time shareholders' vote. *Id.*

209. *Id.* at 1154.

210. *Id.* at 1150-51. See also *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103, 111 (Del. Ch. 1986); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955 (Del. 1985).

posed" test.²¹¹

The court held that because Time's long-term plan to establish a global economy for its products—namely by benefiting from Warner's outstanding video or film production capacity and talent, and its substantial and effective international marketing relationship and organization²¹²—was of unquestionably great importance to Time and was not overly broad, it was a reasonable reaction in relation to the threat posed to the Warner merger by the Paramount offer.²¹³ The court concluded by stating that the financial vitality of the company and the value of its shares are in the hands of the directors and managers, because it is the duty of the directors, not shareholders, to manage the firm.²¹⁴

B. *Analysis of Time*

After the court decided *Time*, an even stronger argument exists that directors have carte blanche to determine the vitality of the company. However, the *Time* decision neglected one very important consideration: that "even finely crafted deals may become unraveled at the eleventh hour."²¹⁵ That consideration should act as a bar on directors' ability to preclude shareholders from accepting a more attractive offer.²¹⁶

211. *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1152 (Del. 1989).

212. *Id.* at 1144-45. See also *supra* notes 150 and 152 and accompanying text.

213. *Time*, 571 A.2d at 1155. However, because Paramount's offer was an any-and-all cash noncoercive offer within the range of values Time's advisors stated, Time's reaction to alter its merger plans with Warner and forego shareholder approval and assume substantial debt seems unreasonable. Furthermore, the court in *Time* stated "that even in light of a valid threat, management actions that are coercive in nature or force upon shareholders a management-sponsored alternative to a hostile offer may be struck down as unreasonable and non-proportionate responses." *Time*, 571 A.2d at 1154. For instance, in an attempt to prevent Paramount from obtaining the franchise transfers, Time directors encouraged local franchisors to bring suit against Paramount. *Id.* at 1148 n.11. See *supra* note 161 and accompanying text. For an example of a case factually similar to *Time*, see *Crouse-Hinds Co. v. Internorth, Inc.*, 634 F.2d 690 (2d Cir. 1980). In *Crouse-Hinds*, a merger agreement between Crouse-Hinds and Belden preceded a takeover offer tendered by Internorth (same as *Time*). The original one-step merger was modified to a two-step merger in response to the takeover bid. *Id.* at 695. However, contrary to *Time*, Crouse-Hind's modification did not require the assumption of substantial debt nor the removal of shareholder vote on the merger consummation.

214. *Time*, 571 A.2d at 1154. But, while the directors have the authority to make business decisions and run the company, they are supposed to make those decisions in the shareholders' best interests. See sources cited *supra* note 38. Moreover, directors are obligated to "abandon a deliberately conceived corporate plan for a short-term shareholder profit [if] there is clearly no basis to sustain the corporate strategy." *Time*, 571 A.2d at 1154.

215. *Mesa Partners v. Phillips Petroleum Co.*, 488 A.2d 107, 116 (Del. Ch. 1984). One commentator thought that a merger deal is "not over 'til the fat lady sings' . . . and the overriding goal of the parties has now become to make it very difficult, or at least expensive, for anyone else to crash the party." Freund, *supra* note 21, at 495.

216. *Supra* note 161 and accompanying text. Consistent with the view of allowing shareholders to choose between alternative offers is the statement that "[a] prophylactic rule that would prevent management from making profitable acquisitions would harm shareholders, [while] application of the usual business judgment rule would give managers free rein to carry out disguised programs of resistance." Easterbrook & Fischel, *Proper Role*, *supra* note 21, at 1202-03. This statement lends

The Time shareholders' interests, as well as the interests of shareholders similarly situated in the future, have been severely lessened by the court's decision. The court's ruling gives directors, who are set on consummating a "long-term" strategic plan, carte blanche to thwart any takeover attempt "threatening" their speculative valuation of the long-term "value" of the company—even contrary to the wishes of the shareholders.²¹⁷ Even though the directors have been given the authority to manage the business and affairs of the corporation, pursuant to the bedrock of Delaware's Corporate Law section 141(a),²¹⁸ they owe duties of care and loyalty to the shareholders.²¹⁹ Therefore, while the directors do run the company, they are supposed to run it for the shareholders' best interests. Furthermore, even though the court stated that distinctions between long-term and short-term plans are irrelevant, directors can now use a long-term plan argument to demonstrate that their corporation's existence is intact. Therefore, because the directors' war chest is filled with endless defensive mechanisms, they should be able to justify any board action short of a scorched earth tactic or an action consummated through gross negligence.

While the Time directors did not act with the same degree of gross negligence as did the directors in *Van Gorkom*, the Time directors' actions could be described as grossly overreaching, thus requiring the directors to prove the objective fairness of their decision.²²⁰ The directors' decision to remain "independent" could be likened to the directors' decision in *Panter*,²²¹ where Judge Cudahy expressed his concern that "one man's desire to 'build value' may be another man's desire to 'keep control at all costs.'" ²²²

Also problematic about the *Time* decision is the justification of the "corporate culture"²²³ defense. Given the ever increasing number of de-

support to the proposition that directors, under the current laws, have carte blanche to determine the corporation's vitality. *But cf.* *Texaco Inc. v. Pennzoil*, 729 S.W.2d 768 (Tex.), *cert. denied*, 485 U.S. 994 (1987) (where the Texas Supreme Court held that there must be a point in time in which a contract is final, and subsequent dealings are a breach of the original contract).

217. See *Arahamian v. HBO & Co.*, 531 A.2d 1204, 1208 (Del Ch. 1987) ("If the will of the stockholders is thwarted . . . there may be considerable hardship to the stockholders and their corporation").

218. *Supra* note 36 and accompanying text.

219. See sources cited *supra* note 38.

220. *Supra* note 33 and accompanying text.

221. *Supra* note 119 and accompanying text.

222. *Panter v. Marshall Field & Co.*, 646 F.2d 271, 306 (7th Cir.) (Cudahy, J., dissenting), *cert. denied*, 454 U.S. 1092 (1981).

223. *Supra* note 152 and accompanying text. See also *Saporito*, *supra* note 148. Protecting a corporate culture might be a valid reason for resisting a takeover. *Id.* at 56.

fensive mechanisms available to directors,²²⁴ the litany of factors *Unocal* allows directors to consider,²²⁵ and the legislative approval given directors under antitakeover statutes,²²⁶ the addition of the "corporate culture" defense presents another powerful defensive response to hostile, as well as nonhostile (any-and-all cash offers) offers. Probably the most damaging aspect of the "corporate culture" defense is its lack of definition. The lack of definable boundaries for "corporate culture" may cause directors to amend by-laws or articles of incorporation, or make acquisitions or sales to give its company a "corporate culture" appearance. Then, when a bidder, either hostile or nonhostile, makes a bid for the company, the board can "Just Say No,"²²⁷ asserting that a takeover would upset its "corporate culture."

Another problem with *Time*, relating back to *Unocal*, is the ability of directors to consider the effects of the takeover on "other constituencies."²²⁸ Even though *Revlon* seemed to curtail the extent to which directors can consider "other constituencies,"²²⁹ directors still can effectuate or thwart a takeover based primarily on considerations of "other constituencies" which at least present minimal "rationally related benefits" to shareholders.²³⁰ This scenario was exemplified perfectly in *Time*, where the merger helped Time set up its global economy, but the merger cost Time \$10 billion and lessened the shareholders' respect for its board (since Time denied them Paramount's premium offer, or in the alternative, the opportunity to vote on the Warner merger).

The last problem associated with *Time* concerns the "threat" posed by Paramount's offer and Time's reaction to that "threat." Given the noncoercive²³¹ nature of the offer presented by Paramount, which fell within the range of values for Time²³²—as established by Time's advisors—the directors' response was not reasonable. The assumption of \$10 billion in debt to merge with a company that as one entity would have a

224. *Supra* note 28 and accompanying text. See also *Taub, LBO's: The Next Lap*, FIN. WORLD, Oct. 31, 1989, at 24-25, stating that the new era of less-leveraged buyouts (more equity based buyouts) are picking up where leveraged buyouts left off. LLBO's mean lower returns for LBO partners and lower prices for takeover targets. Therefore, more equity deals will mean less debt.

225. *Supra* note 99 and accompanying text.

226. See statutes cited *supra* note 124.

227. *Supra* note 119 and accompanying text. See also *Paramount Communications v. Time, Inc.*, 571 A.2d 1140, 1152 (Del. 1989) (the court stated that refusing "to entertain an offer may comport with a valid exercise of a board's business judgment").

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

229. See *supra* note 30 and accompanying text.

230. But see *Gilson & Kraakman, supra* note 21, at 259 n.41, where the authors state that *Revlon* would preclude this scenario from occurring.

231. *Supra* note 161 and accompanying text.

232. *Supra* note 170 and accompanying text.

lower per share value than the takeover offer presented²³³ and the renegeing of shareholder voting rights concerning that merger were not reasonable. The directors' response to the Paramount takeover is tantamount to the "scorched earth" tactic attempted in *Joseph E. Seagram & Sons*.²³⁴ Just as the decision to destroy the company in *Seagram* was not within the ambit of the business judgment rule, neither should *Time's* decision to "destroy" its company fall within the rule's protective reach. The apparent effect of *Time* is that directors may now be able to protect every business decision from either shareholder or judicial scrutiny. The preferred standard would require directors to submit merger or acquisition proposals for a majority vote of both shareholders and disinterested shareholders, as required of takeover companies in some antitakeover statutes.

VI. CONCLUSION

The business judgment rule's emphasis on an informed decision by the directors made in the best interests of the shareholders does not always protect shareholders. While all corporate decisions should be informed, the protection of shareholder investments should be a paramount consideration. When an opportunity arises that maximizes shareholders' interests (*i.e.*, investments), directors owe a duty of care and loyalty to consider that opportunity with a "critical eye."²³⁵ However, until courts decide to place constraints upon directors' authority, shareholders "are on their own and [should] expect little consideration and less enlightenment from their board of directors"²³⁶ and from the courts.

233. *Id.*

234. *Supra* note 24 and accompanying text.

235. *See supra* note 3 and accompanying text.

236. *Panter v. Marshall Field & Co.*, 646 F.2d 271, 312 (7th Cir.) (Cudahy, J., dissenting), *cert. denied*, 454 U.S. 1092 (1981).

