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Daniel Vinish

THE DEMISE OF CLARITY IN CORPORATE TAKEOVER JURISPRUDENCE: THE *OMNICARE V. NCS HEALTHCARE* ANOMALY

DANIEL VINISH*

INTRODUCTION

The inception of case law governing duties owed by the board of directors to shareholders in the face of business combinations was clearly defined by *Unocal v. Mesa Petroleum Co.*[1] in 1985.[2] Over the eight years following this case, the Delaware Supreme Court clarified its position by defining the specific situations invoking *Unocal's* enhanced judicial scrutiny and the applicable standards imposed for reviewing board decisions in such situations.[3] In 1995, the final guiding light was decided by the Delaware Supreme Court, solidifying an analysis consonant with the historical conflict between the self-interest of directors and the desire of shareholders for return on investment.[4] Recently,

*Daniel E. Vinish. Juris Doctor from St. John's University School of Law July 2006. Bachelor of Science in Financial Economics from Binghamton University July 2003.

1 493 A.2d 946 (Del. 1985).

2 *See id.* at 955 (holding defensive board action must not be draconian and must be within range of reasonableness); *see also* Sterling v. Mayflower Hotel Corp., 93 A.2d 107, 110 (Del. 1952) (explaining that entire fairness test required directors to bear burden of establishing entire fairness when they stood on both sides of transactions).

3 *See* Michal Barzuza, *Price Considerations in the Market for Corporate Law*, 26 CARDOZO L. REV. 127, 190–97 (2004) (discussing growth of shareholder protection in Delaware corporate law); *see also* Eric A. Chiappinelli, *The Life and Adventures of Unocal – Part I: Moore the Marrier*, 23 DEL. J. CORP. L. 85, 104–43 (1998) (reviewing court's application of business judgment rule, entire fairness test, and Unocal test following *Unocal*).

4 *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1387–88 (Del. 1995) (clarifying approach outlined in *Unocal*); *see also* Michael B. Regan, Note, *Dead End: Delaware's*

however, in *Omnicare, Inc. v. NCS Healthcare, Inc.*[5] The Delaware Supreme Court destroyed the prior lucidity in case law governing corporate directors by holding, first, that an amalgam of stockholder and director action may be taken into account for enhanced judicial scrutiny purposes[6] and, second, that the equivalent of a third requirement, in the form of a fiduciary out, would now be imposed on director action prior to invocation of *Revlon* duties.[7]

In *Omnicare*, the defendants, NCS Healthcare, Inc. (hereinafter "NCS") and Genesis Health Ventures, Inc. (hereinafter "Genesis"), were two corporations who had, prior to the lawsuit, entered into a highly locked up merger agreement.[8] NCS, at the time in question, was a Delaware corporation engaged in providing pharmaceutical services to long term health care institutions.[9] Before entering into the merger agreement with Genesis, NCS's financial condition had been steadily declining, such that NCS was facing an almost inevitable bankruptcy.[10] NCS directors were aware of the company's dire financial position and, with intentions of protecting the investments of debt and equity holders of NCS, obtained outside assistance to canvass the market for possible acquirers or

Response to the Recent Innovation in Corporate Antitakeover Measures, the So-Called "Dead Hand" Poison Pill, in Carmdody v. Toll Brothers, Inc., 44 VILL. L. REV. 643, 651–53 (1999) (describing Delaware Supreme Court's re-articulation of *Unocal* standard in *Unitrin*).

5 818 A.2d 914 (Del. 2003).

6 *See id.* at 936 (describing why stockholder and board action could not withstand *Unocal*'s standard of review requiring enhanced judicial scrutiny); William J. Carney & Leonard A. Silverstein, *The Illusory Protections of the Poison Pill*, 79 NOTRE DAME L. REV. 179, 217 (2003) (articulating *Omnicare*'s expansion of *Unocal* test's scope of review).

7 *See Omnicare*, 818 A.2d at 936 (explaining why, in addition to being preclusive and coercive, omission of fiduciary out clause prevented board from fulfilling fiduciary responsibility to minority shareholders); Carney & Silverstein, *supra* note 6, at 217 (describing *Omnicare*'s clarification "that a 'preclusive or coercive' examination was not the end of Unocal scrutiny").

8 *See Omnicare*, 818 A.2d at 925 (outlining demands upon shareholders by terms of merger agreement); Carney & Silverstein, *supra* note 6, at 217 (discussing *Omnicare* scrutiny of voting agreement received under *Unocal*).

9 *See Omnicare*, 818 A.2d at 918 (introducing NCS as long term health care provider); Christopher J. Moceri, Comment, *M&A Lockups: Broadly Applying the* Omnicare *Decision to Require Fiduciary Outs in all Merger Agreements*, 2004 MICH. ST. L. REV. 1157, 1161 (2004) (noting that NCS was Delaware corporation specializing in long term health care).

10 *See Omnicare*, 818 A.2d at 920 (specifying that adverse market conditions led to NCS's difficulty in collecting accounts receivable and decline in market value of its stock); Moceri, *supra* note 9, at 1161 (noting NCS's "financial difficulty").

investors.[11] After surveying the market through the use of two different financial advisors over nearly two years time, NCS had not received a single adequate offer.[12] However, at around the two year mark in its search, NCS contacted Omnicare, Inc. (hereinafter "Omnicare") and began discussions for an acquisition of NCS by Omnicare.[13] These discussions soon terminated due to Omnicare's insistence upon, and NCS's refusal to allow for, structuring the deal as an asset sale in bankruptcy.[14] At such point, NCS began discussions with Genesis for a transaction outside of bankruptcy that would grant moderate, yet enticing, relief for NCS's concerned debt and equity holders.[15] During these discussions, Genesis demanded, as a precaution stemming from recent historical bidding wars Genesis had been party to, an exclusive negotiation period, to which NCS agreed.[16] Before Genesis and NCS could enter into a definitive merger agreement (hereinafter "Agreement"), however, Omnicare returned to the picture and proposed a financially attractive, yet otherwise unattractive, bid for NCS.[17] Eying the unattractive nature of Omnicare's bid, the NCS directors unanimously approved a merger with Genesis and entered into a

[11] *See Omnicare*, 818 A.2d at 920 (stating that NCS retained UBS Warburg in February of 2000 to identify potential acquirers); *see also* Andrew D. Arons, Comment, *In Defense of Defensive Devices: How Delaware Discouraged Preventive Measures in* Omnicare v. NCS Healthcare, 3 DEPAUL BUS. & COMM. L.J. 105, 107 (2004) (explaining advisory relationship between NCS and UBS Warburg).

[12] *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 921 (Del. 2003) (finding that in December of 2000, NCS terminated its relationship with UBS Warburg and appointed Brown, Gibbons, Lang & Co. as its exclusive financial advisor); *see also* Arons, *supra* note 11, at 107 (noting that while it retained UBS Warburg, NCS received only one unsatisfactory merger offer).

[13] *See Omnicare*, 818 A.2d at 921 (stating that Omnicare began discussing possible merger details with Brown, Gibbons in summer 2001); *see also* Arons, *supra* note 11, at 108 (noting that NCS contacted Omnicare to discuss possible sale of NCS).

[14] *See Omnicare*, 818 A.2d at 921 (finding that Omnicare made number of merger proposals to NCS, but all included sale in bankruptcy); *see also* Arons, *supra* note 11, at 107–08 (discussing Omnicare's several proposals for NCS's asset sale in bankruptcy).

[15] *See Omnicare*, 818 A.2d at 922 (discussing Genesis's proposal that provided possibility of recovery for NCS noteholders and stockholders); *see also* Arons, *supra* note 11, at 108 (noting that in January 2002, NCS contacted Genesis to discuss potential merger).

[16] *See Omnicare*, 818 A.2d at 922–23 (discussing demands by Genesis for exclusivity); *see also* Arons, *supra* note 11, at 109 ("Genesis absolutely refused to continue to work towards closing the agreement unless NCS agreed to act on an exclusive basis with Genesis.").

[17] *See Omnicare*, 818 A.2d at 924 (outlining renewed proposal by Omnicare stating that Omnicare would retire NCS's senior and subordinated debt and offering NCS stockholders $3.00/share); *see also* Arons, *supra* note 11, at 110 (discussing new Omnicare proposal for acquisition outside of bankruptcy).

definitive merger agreement,[18] including: a no shop clause, that prevented NCS from entering into discussions with other parties unless certain preconditions were met;[19] a "force-the-vote" provision requiring, regardless of continued NCS board recommendation of the merger, enforcement of § 251(c)[20] and, consequently, a shareholder vote on the merger;[21] and voting agreements, drafted separate from the Agreement, pledging a majority of NCS's outstanding voting shares in favor of the merger.[22] Omnicare, fearing the potential loss it would incur in market share if the Agreement was fully consummated, irrevocably committed itself to a hostile offer paying in excess of the value NCS equity holders were to receive under the

[18] *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 924–25 (Del. 2003). NCS executives viewed Omnicare's insistence upon due diligence review as substantially undercutting the value of Omnicare's offer. The board believed the risk of losing Genesis's offer was too great to pursue Omnicare's offer, given Omnicare's prior rock solid negotiating position requiring an asset sale in bankruptcy along with its decision to secretly deal exclusively with the Ad Hoc Committee. *Id.* at 924–25. Ultimately, NCS agreed to the merger with Genesis. *See also* Arons, *supra* note 11, at 111.

[19] *See Omnicare*, 818 A.2d at 925. The 'no shop' clause stated verbatim:

NCS would not enter into discussions with third parties concerning an alternative acquisition of NCS, or provide non-public information to such parties, unless (1) the third party provided an unsolicited, *bona fide* written proposal documenting the terms of the acquisition; (2) the NCS board believed in good faith that the proposal was or was likely to result in an acquisition on terms superior to those contemplated by the NCS/Genesis merger agreement; and (3) before providing non-public information to that third party, the third party would execute a confidentiality agreement at least as restrictive as the one in place between NCS and Genesis.

Id. at 925–26.

[20] DEL. CODE ANN. tit. 8, § 251 (2005) (regarding procedural rules of merger votes).

[21] *See Omnicare*, 818 A.2d at 925. The NCS/Genesis merger agreement read, "NCS would submit the merger agreement to NCS stockholders regardless of whether the NCS board continued to recommend the merger." *Id.* A recent amendment to the Delaware General Corporation Law permitted the "force-the-vote" provision. *See* E. Norman Veasey & Christine T. Di Guglielmo, *What Happened in Delaware Corporate Law and Governance from 1999–2004? A Retrospective on Some Key Developments*, 153 U. PA. L. REV. 1399, 1458 (2005).

[22] *See Omnicare*, 818 A.2d at 926. Jon H. Outcalt, Chairman of the NCS board of directors, held 202,063 shares of class A common stock and 3,476,086 shares of class B common stock. *Id.* at 918. Kevin B. Shaw, President, CEO, and a director of NCS, held 28,905 shares of class A common stock and 1,141,134 shares of class B common stock. *Id.* at 919. Outcalt and Shaw entered into voting agreements expressly in their capacity as stockholders and not as directors or officers. *Id.* at 926. The voting agreements required Outcalt and Shaw vote their shares in favor of merger and were specifically enforceable by Genesis. *Id.* The voting agreements contained many requirements. *See also* Kurt M. Heyman & Christal Lint, *Recent Developments in Corporate Law: Recent Supreme Court Reversals and the Role of Equity in Corporate Jurisprudence*, 6 DEL. L. REV. 451, 468 (2003) for list of requirements set forth in voting agreements.

Agreement.[23] NCS, however, was prevented from changing its future course.[24] Sails had been set.

Delaware Supreme Court Justice Holland, writing for the majority of a divided court,[25] began his analysis by deeming "not outcome determinative"[26] a resolution of the applicable standard of review.[27] He then termed the issue of the case as whether the defensive tactics used by NCS to 'lock up' its deal with Genesis were congruous with the board's fiduciary duties.[28] After surveying the law, Justice Holland proceeded to delineate two holdings for the court.[29] First, the Court held that actions by the NCS board to protect its merger with Genesis were preclusive and coercive, in violation of the duties imposed by *Unocal*[30] and,

23 *See Omnicare*, 818 A.2d at 927. Omnicare irrevocably committed itself to a transaction with NCS, paying $3.50 for each share of NCS class A and class B common stock. *Id. See also* Heyman & Lint, *supra* note 22, at 469 for discussion of Omnicare's offer.

24 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 926–27 (Del. 2003). As a result of Omnicare's offer, NCS's board withdrew its recommendation for the stockholders to vote in favor of the NCS/Genesis merger. *Id.* NCS's financial advisor also withdrew his fairness opinion of the NCS/Genesis merger agreement. *Id.* at 927. These were fruitless acts, however, because the combined effect of the NCS/Genesis merger provision requiring the NCS stockholders vote on the NCS/Genesis merger regardless of board approval, along with the voting agreements granted by Outcalt and Shaw, made the NCS/Genesis merger an agreed upon pre-determined conclusion. *Id.* One author described the merger provision and the voting agreements as rendering "moot" any merger talks other than those between NCS and Genesis. *See* Jay. H. Knight, *Merger Agreements Post*-Omnicare, Inc. v. NCS Healthcare, Inc.: *How the Delaware Supreme Court Pulled a Plug on "Mathematical Lock-Ups"*, 31 N. KY. L. REV. 29, 44 (2004).

25 *See* Chiappinelli, *supra* note 3, at 101 n.90 (discussing Delaware Supreme Court's history with respect to overruling recent case law); *see also* Veasey & Di Guglielmo, *supra* note 21, at 1458 (stating that *Omnicare* decision was controversial in part because it involved rare split decision by normally unanimous Delaware Supreme Court).

26 *Omnicare*, 818 A.2d at 929 (discussing effect on this appeal of Court of Chancery's standard of review).

27 *See id.* The Court's decision not to make an affirmative determination of whether *Revlon* or *Unocal* duties applied has the effect of deeming as a third prong to the *Unocal* test the requirement of a fiduciary out. *See id.* The test for board action in the face of a business combination was laid out in Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985). The Court of Chancery believed *Revlon* duties were inapplicable to the NCS/Genesis/Omnicare situation. *See generally* In re NCS Healthcare, Inc., 825 A.2d 240, 254-56 (Del. Ch. 2002).

28 *See Omnicare*, 818 A.2d at 930 (explaining that Delaware law requires "balance of power" between boards and stockholders); *see also* Knight, *supra* note 24, at 48 (describing challenged deal protection measures as locking in NCS/Genesis merger).

29 *See Omnicare*, 818 A.2d at 936 (maintaining that court's decision was two-fold in nature and was based upon both proposition that board's actions were preclusive and coercive and also upon notion that overall terms of merger formulated a "*fait accompli*").

30 *See id.* (holding that board's actions essentially robbed stockholders of vote because there was already predetermined outcome by time vote was to be taken); *see also* Unitrin v. Am. Gen. Corp., 651 A.2d 1361, 1387–88 (Del. 1995) (defining preclusive and coercive within *Unocal*).

therefore, invalid and unenforceable.[31] The Court reached this holding by deeming a unitary response the combination of the NCS board's choice to include a force-the-shareholder-vote provision in the merger agreement and the NCS majority shareholders' decision to grant specifically enforceable voting agreements to Genesis.[32] Second, the Court held a target is prohibited, regardless of the applicable duty given a proposed merger's structure, from agreeing to a merger on terms that formulate *"a fait accompli"* and prevent it from accepting a higher valued bid.[33]

Delaware Supreme Court Justice Veasey led the divided court's dissent, disagreeing sharply with the majority's analysis of *Unocal* and its progeny,[34] as well as the majority's blanket fiduciary out requirement.[35] Justice Veasey began his dissent arguing, with regard to the majority's *Unocal* analysis, that by holding the NCS board's action to be preclusive and coercive, the majority misapplied the principles of "draconian" action outlined in *Unitrin*.[36] To support this view, he emphasized that, unlike the majority opinion, the focus in *Unitrin* was on the coercive or preclusive effect actions taken by the board had on the outcome of a shareholder vote.[37] Concluding his dissent, Justice Veasey

[31] *See Omnicare*, 818 A.2d at 936 (positing that predetermined nature of vote was impermissible coercion and therefore "cannot withstand *Unocal's* enhanced judicial scrutiny standard of review," because it is not "within the range of reasonableness").

[32] *See id.* at 934–36 (concluding that board's actions constituted unitary response and therefore should be reviewed under *Unocal* which states "if defensive measures are either preclusive or coercive they are draconian and impermissible" and extrapolating that in this case, because protection devices of NCS board were both preclusive and coercive, they were undoubtedly impermissible).

[33] *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 936 (Del. 2003) (finding that merger's terms accomplished a *fait accompli* because even though stockholders were not forced to vote for merger, they were required to accept it).

[34] *See id.* at 944–45 (Veasey, J., dissenting) (positing that majority misapplied "the *Unitrin* concept of 'coercive and preclusive'" and therefore used it incorrectly to advance its analysis and highlighting differences between *Unitrin* cases and NCS board's actions).

[35] *See id.* at 946 (Veasey, J., dissenting) (distinguishing reasoning in *QVC* surrounding fiduciary out requirement that did not "create a special duty to protect the minority stockholders from the consequences of a controlling stockholder's ultimate decisions unless the controlling stockholder stands on both sides of the transaction" from *Omnicare* facts).

[36] *See id.* at 943–44 (Veasey, J., dissenting) (noting that draconian measures in *Unitrin* dealt with unilateral board action and explaining that by misapplying concept of "coercive and preclusive" in this case, the majority preempted proper proportionality balancing).

[37] *See id.* at 944 (Veasey, J., dissenting) ("The proper inquiry in this case is whether the NCS board had taken actions that 'have the effect of causing the stockholders to vote

pointed out that no case ever decided by the Delaware Supreme Court supported the majority's blanket fiduciary out requirement,[38] distinguishing the majority's supporting precedent on its facts.[39]

It is submitted that, in holding Unitrin's language allowing inextricably related board actions to be reviewed as a unitary response to reach both board and shareholder action, the Delaware Supreme Court erred in its application of pre-*Revlon* enhanced judicial scrutiny. Furthermore, it is submitted that, in holding as a blanket rule regardless of the circumstances that a fiduciary out must exist in all merger agreements, the Delaware Supreme Court erred in its analysis of the fiduciary duty owed by directors to shareholders. Moreover, both aforementioned holdings ignore the board's fundamental role in determining, absent the fiduciary duty shift initiated by *Revlon*, the corporation's long term profit seeking strategy and thus disable the board from adequately and effectively running the corporation.

Part I of this comment will provide an overview of the distribution of power between shareholders and the board of directors as well as an indication of why enhanced judicial scrutiny is required in certain circumstances. Part II will explain in depth relevant Delaware case law in addition to the various duties imposed on directors by this case law. Part III will juxtapose Delaware case law discussing preclusive and coercive action with the NCS board's actions to illustrate how the court's holding in *Omnicare* is neither consistent with prior applications

in favor of the proposed transaction for some reason other than the merits of that transaction.'").

38 *See id.* at 945 (Veasey, J., dissenting) ("We know of no authority in our jurisprudence supporting this new rule, . . ."); Heyman & Lint, *supra* note 22, at 474 (highlighting that Justice Veasey pointed out that there was no authority in Delaware jurisprudence supporting this rule).

39 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 946 (Del. 2003) (Veasey, J., dissenting). Justice Veasey stated:

> [t]he Majority relies on our decision in *QVC* to assert that the board's fiduciary duties prevent the directors from negotiating a merger agreement without providing an escape provision. Reliance on *QVC* for this proposition, however, confuses our statement of a board's responsibilities when the directors confront a superior transaction and turn away from it to lock up a less valuable deal with the very different situation here, where the board committed itself to the *only* value-enhancing transaction available.

Id. Veasey also points to the contrast between the board in *QVC* and the NCS board in *Omnicare*. *See* Veasey & Di Guglielmo, *supra* note 21, at 1460 n.248.

of preclusive and coercive nor consistent with the theory underlying the *Unocal-Revlon* framework's multilevel enhanced judicial scrutiny analysis.

I. DISTRIBUTIONS OF POWER BETWEEN THE SHAREHOLDERS AND THE BOARD OF DIRECTORS

The correct distribution of power between the shareholders and board has, throughout time, been an issue of much debate.[40] Statutorily, the board of directors of a public corporation is generally empowered with the ability to conduct and direct the business and affairs of the corporation.[41] Consequently, shareholders are at the mercy of the board on a day to day basis.[42] It is, therefore, of utmost importance for a business, when deciding where to incorporate, to consider a jurisdiction's statutory distribution of power, as not all jurisdictions provide shareholders the same rights.[43] The following commentary on Delaware's statutory allocation of power is meant to illustrate the framework governing NCS, a Delaware corporation.

Title Eight of the Delaware Code Annotated ("Title Eight")[44] defines the law governing Delaware corporations and delineates

40 *See* Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 837 n.5 (2005) (explaining that corporation's board is responsible for managing its business and affairs); *see also* R. Mathew Garms, Note, *Shareholder By-Law Amendments and the Poison Pill: The Market for Corporate Control and Economic Efficiency*, 24 IOWA J. CORP. L. 433, 434–35 (1999) (describing historical tension over distribution of power between shareholders and directors); *see also* E. Norman Veasey, *The Defining Tension in Corporate Governance in America*, 52 BUS. LAW. 393, 403 (1997) (describing tension between deference to business judgment and judicial review).

41 *See* DEL. CODE ANN. tit. 8, § 141 (2005) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the directors of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation."); *see also* Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985) (noting that under Delaware law business and affairs of Delaware corporations are managed by or under its board).

42 *See* Grimes v. Donald, 673 A.2d 1207, 1215 (Del. 1996) (discussing power held by boards with regard to demand in derivative suits); *see also* Miriam P. Hechler, *The Role of The Corporate Attorney Within The Takeover Context: Loyalties to Whom?*, 21 DEL. J. CORP. L. 943, 947 (1996) ("Under Delaware corporation law, the officers of the corporation run the day-to-day operations of the company, with the oversight of the board of directors.").

43 *Compare* N.Y. BUS. CORP. § 505 (2005) (requiring shareholder vote to authorize share-purchase options to directors, officers and employees of corporation), *with* DEL. CODE ANN. tit. 8, § 157 (2005) (authorizing board of directors to by resolution designate officers who may allocate stock options to officers and employees of the corporation without shareholder approval).

44 *See* DEL. CODE ANN. tit. 8 (2005) (containing Delaware General Corporation Law in Chapter One).

power among voting shareholders and directors.[45] Specifically, voting shareholders are granted eight distinct fundamental, inalienable rights.[46] This group of fundamental powers can be summarized generally into three categories: creation and destruction of internal documents; determination of directors; and fundamental alteration the corporate existence.

The power to amend and adopt a corporations internal documents, including the by-laws and certificate of incorporation, is granted to the shareholders under Delaware Code §§ 109[47] and 242.[48] The Certificate of Incorporation, unlike the by-laws, is a publicly filed document and, therefore, is generally limited to containing only that which is required by § 242.[49] The by-laws, on the other hand, are permitted to be kept private and thus generally contain all of the corporation's internal governance rules not required by § 242 to be stated in the Certificate of Incorporation.[50] Power to control the contents of these

45 *See id.* Various provisions of Title 8 provide for shareholder voting rights, as well as those powers which are reserved to the board of directors and can be exercised without shareholder approval. *Id.* The Delaware jurisprudence relating to this issue was discussed in Blasius Indus. v. Atlas Corp., 564 A.2d 651, 659–60 (Del. Ch. 1988).

46 *See* DEL. CODE ANN. tit. 8, § 109 (2005) (regulating adoption and amendment of bylaws); DEL. CODE ANN. tit. 8, § 242 (regulating amendment of certificate of incorporation); DEL. CODE ANN. tit. 8, § 141 (regulating election and removal of directors); DEL. CODE ANN. tit. 8, § 251 (regulating mergers and consolidations); DEL. CODE ANN. tit. 8, § 271 (regulating sale of assets); DEL. CODE ANN. tit. 8, § 275 (regulating dissolution); Hubbard v. Hollywood Park Realty Enters., Inc., No. 117791, 1991 Del. Ch. LEXIS 9, at *34 (Del. Ch. 1991) ("That those rights are fundamental does not mean that their exercise cannot be restricted for valid corporate purposes by board-created procedural rules. However, those restrictions must not infringe upon the exercise of those rights in an unreasonable way."); *see also Blasius*, 564 A.2d at 658–63 (holding shareholders' right to elect directors cannot be taken away).

47 *See* DEL. CODE ANN. tit. 8, § 109 (vesting this power solely with shareholders once corporation has received any payment for its stock); *see also* Kidsco, Inc. v. Dinsmore, 674 A.2d 483, 492 (Del. Ch. 1995) (describing this allocation of power).

48 *See* DEL CODE ANN. tit. 8, § 242 (2005) (allowing shareholders to vote on proposed amendments affecting corporations' certificate of incorporation); Paramount Commc'ns v. QVC Network, 637 A.2d 34, 42 (Del. 1994) ("Under the statutory framework of the General Corporation Law [including § 242], many of the most fundamental corporate changes can be implemented only if they are approved by a majority vote of the stockholders.").

49 *See* DEL CODE ANN. tit. 8, § 242 (2005) (delineating items that may be amended by shareholder vote); Farahpour v. DCX, Inc., 635 A.2d 894, 897 (Del. 1994) (citing items regarding certificate of incorporation amendable through shareholder vote).

50 *See* DEL. CODE ANN. tit. 8, § 109(b) (2005) ("The bylaws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the rights or powers of its stockholders, directors, officers or employees."); Chandler, Chancellor, *Unreported Case:* Di Loreto v. Tiber Holding Corp.*: No. 16,564*, 25 DEL. J. CORP. L. 456, 467 n.12 (2000) (explaining statute's few limitations regarding what shareholders may enact for corporation's by-laws).

documents, therefore, enables the shareholders to prohibit the board of directors from changing the structure of and rules governing the board and the corporation in general.[51] Consequently, directors, whose interests are not always in line with that of the shareholders, are, at least in part, stymied from preventing corporate attainment of the shareholders' primary goal: return on investment.[52]

Consonant with the shareholder right to amend and adopt the certificate of incorporation and by-laws is the shareholder right to both elect and remove directors from office.[53] In short, the shareholders right to control director positions is near absolute.[54] Some limitations do, however, exist.[55] The right to elect directors is slightly limited, depriving shareholders only of the right to fill untimely vacancies and newly created positions.[56] Alternatively, the right to remove directors may in certain circumstances, as per the bylaws, be limited to a greater degree, such as requiring shareholders to show cause before removing directors.[57]

51 *See* DEL. CODE ANN. tit. 8, § 242(b) (2005) (establishing limited methods of major corporate change whereby only stockholder vote can finalize decision); *Paramount,* 637 A.2d at 42 (fermenting general policy set forth by General Corporation Law in Delaware that fundamental corporate changes must be approved by majority of stockholders).

52 *See* Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 315–16 (1999) (describing directors' incentive to maximize returns for their own benefit and that of shareholders in order to retain director positions); Richard A. Booth, *Junk Bonds, the Relevance of Dividends and the Limits of Managerial Discretion*, 1987 COLUM. BUS. L. REV. 553, 553 (1987) (implying shareholders' primary desire is high return on investment).

53 *See* DEL. CODE ANN. tit. 8, § 141(k) (2005) (allocating establishment or removal of board members by shareholders election); Duffy v. Loft, Inc., 152 A. 849, 852 (Del. 1930) (establishing role of directors as elected positions, chosen at annual shareholder meetings).

54 *See* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 959 (Del. 1985) (highlighting shareholders' ability to vote out directors if displeased with their actions); Brian T. Corrigan, *Corporate Governance under Chapter 11: Should Directors Serve Shareholders, Creditors, and/or the Corporation?*, 688 PLI/Comm 9, 49 (1994) ("In Delaware, shareholders' right to elect directors is 'virtually absolute,' even when the corporation is insolvent and in a Chapter 11 case."). *But see* Blair & Stout, *supra* note 52, at 310 (contesting nuances that shareholder voting rights give them more than nominal control over directors).

55 *See* DEL. CODE ANN. tit. 8, § 141(k) (2005) (limiting power of shareholders in appropriate circumstances such as inability to remove directors without showing cause); DEL. CODE ANN. tit. 8, § 223 (2005) (allowing directors to fill temporary vacancies if any others resign).

56 *See* DEL. CODE ANN. tit. 8, § 223 (reserving power to fill vacancies for board of directors); *see also* Robert W. Hamilton, *Private Sales of Control Transactions: Where We Stand Today*, 36 CASE W. RES. L. REV. 248, 269 (1986) (noting boards have power to temporarily shift control due to its ability to fill vacancies).

57 *See* DEL. CODE ANN. tit. 8, § 141(k) (2005) (requiring showing of cause by shareholders before directors may be removed under qualified circumstances); *see also*

Rounding out shareholder power is the ability to control fundamental changes to the corporate enterprise.[58] For directors to enter the corporation into a merger,[59] to sell substantially all of the corporation's assets out of the ordinary course of business,[60] or to dissolve the corporation, an affirmative majority vote representing all outstanding voting shares is required.[61] Limited exceptions apply, but it is the general fundamental change in the corporate enterprise that triggers this right to vote.[62] Courts and legislatures have recognized shareholders should not be divested from such decisions, on the idea that decisions to fundamentally change the corporate enterprise could potentially stem from myriad reasons disparate with shareholder interests. [63]

Ellen S. Friedenberg, *Jaws III: The Impropriety of Shark-Repellent Amendments as a Takeover Defense*, 7 DEL. J. CORP. L. 32, 41 (1982) (discussing shareholders' inherent power to remove directors for cause and ability to limit shareholders' right to remove directors without cause if their charter so provides).

58 *See* In re Wheelabrator Technologies, Inc., 663 A.2d 1194, 1200, (Del. Ch. 1995) (explaining how board actions affecting corporate makeup need shareholder approval); *see also* Williams v. Geier, 671 A.2d 1368, 1381 (Del. 1994) (stating that "some fundamental measures require stockholder action" including "all amendments to certificates of incorporation and mergers").

59 *See* DEL. CODE ANN. tit. 8, § 251 (2005) (requiring merger agreement to be submitted to shareholders); *see also Williams*, 671 A.2d at 1381 (explaining how shareholder approval under section 251 is needed in order for board of directors to go forward with merger).

60 *See* DEL. CODE ANN. tit. 8, § 271 (requiring shareholder approval for sale, lease or exchange of assets); *see also* J. P. Griffin Holding Corp. v. Mediatrics, Inc., No. 4056, 1973 Del. Ch. LEXIS 153, at *4 (Del. Ch. 1973) (paraphrasing statute in how it governs sale of Delaware corporations' assets).

61 *See* DEL. CODE ANN. tit. 8, § 275 (requiring stockholder vote for dissolution); *see also* In re Arthur Treacher's Fish & Chips, No. 5357, 1980 Del. Ch. LEXIS 489, at *11 (Del. Ch. 1980) (explaining Delaware statute as permitting voluntary dissolution when it is deemed advisable by board and approved by majority of stockholders).

62 *See* Alexander G. Simpson, *Shareholder Voting and the Chicago School: Now is the Winter of Our Discontent*, 43 DUKE L. J. 189, 204–05 (1993) (noting that shareholders are given power to vote on major corporate structural changes but not on mundane daily activities); *see also* Janet E. Kerr, *Delaware Goes Shopping for a "New" Interpretation of the Revlon Standard: The Effect of the QVC Decision on Strategic Mergers*, 58 ALB. L. REV. 609, 667 (1995) (discussing fundamental changes in corporate structure necessitating enhanced judicial scrutiny under *Revlon*); *cf.* David Cohen, Comment, *Valuation in the Context of Share Appraisal*, 34 EMORY L. J. 117, 122 (1985) (explaining that short-form mergers do not require shareholder vote because "result of the vote is obvious").

63 *See* Robert B. Thompson & D. Gordon Smith, *Toward a New Theory of the Shareholder Role: "Sacred Space" in Corporate Takeovers*, 80 TEX. L. REV. 261, 294 (2001) (discussing director entrenchment in merger situations); *see also* Donald Lund, Comment, *Toward a Standard for Third-party Advisor Liability in Mergers and Buy-outs: Schneider and Beyond*, 52 U. PITT. L. REV. 603, 603 (1991) (relating that shareholders' right to vote exists "because a prospective merger or take-over can potentially alter the fundamental nature of a corporation, or substantially affect the valuable investments of every shareholder").

Although shareholder power to govern the corporation extends across vital grounds, directors retain the power to run the corporation's everyday activities.[64] Delaware courts have taken an active role in solidifying this right.[65] Consistently, cases uphold board action attacked by majority-block shareholders claiming a right to step over the board's managerial discretion.[66] This treatment is a necessary requirement incident to the effective functioning of a publicly traded corporation.[67] For-profit corporations must be able to adapt to market conditions in their day to day transactions to remain competitive and profitable; having to cope with the impediments inherent in large governing bodies would prevent attainment of efficient competition.[68]

II. GOVERNING LAW

As a result of the board's power to control every day business and affairs, the law has recognized that, in certain circumstances, shareholders may require protection against external competition related sources as well as internal authority

64 *See* DEL. CODE ANN. tit. 8, § 141 (articulating power of board); Levine v. Smith, 591 A.2d 194, 200 (Del. 1991) (explaining how board of directors posses duty to manage 'business and affairs' of corporation and illustrating that determination of whether to bring derivative suit is within 'business and affairs' of corporation).

65 *See* Emerald Partners v. Berlin, 787 A.2d 85, 91 (Del. 2001) (expounding upon protection that business judgment rule provides); A. Mechele Dickerson, *Approving Employee Retention and Severance Programs: Judicial Discretion Run Amuck?*, 11 AM. BANKR. INST. L. REV. 93, 100 (2003) (enouncing bounds of managerial discretion protected by business judgment rule).

66 Hollinger Inc. v. Hollinger Int'l. Inc., 858 A.2d 342, 349 (Del. Ch. 2004) (deeming board action to sell 'trophy asset' to be within board's business judgment and not subject to shareholder consent); *see also*Robert K. Rasmussen & David A. Skeel Jr., *The Economic Analysis of Corporate Bankruptcy Law*, 3 AM. BANKR. INST. L. REV. 85, 93 n.32 (1995) (noting deferential treatment courts extend to board of director decisions absent fraud or other misconduct).

67 *See* Royce de R. Barondes, *Dynamic Economic Analyses of Selected Provisions of Corporate Law: The Absolute Delegation Rule, Disclosure of Intermediate Estimates and IPO Pricing*, 7 DEPAUL BUS. L.J. 97, 115 (1994) (explaining inefficiency that exists in placing right to vote on 'wide array of business decisions' in widely held group of stockholders); K.A.D. Camara, *Shareholder Voting and the Bundling Problem in Corporate Law*, 2004 WIS. L. REV. 1425, 1481–82 (2004) (noting consistency in corporate decision making to be extremely difficult to achieve when substantial voting power is placed in shareholders).

68 *See* Jennifer Arlen & Eric Talley, *Precommitment and Managerial Incentives: Unregulable Defenses and the Perils of Shareholder Choice*, 152 U. PA L. REV. 577, 581 n.13 (2003) (citing authority for increasing board's managerial discretion); Lawrence A. Hamermesh, *Corporate Democracy and Stockholder-Adopted By-Laws: Taking Back the Street?*, 73 TUL L. REV. 409, 453–57 (1998) (outlining reasons why direct management by widely dispersed stockholder groups is inefficient).

figures.[69] It is the "omnipresent specter that a board may be acting primarily in its own interests,"[70] rather than in the interests of the corporation and shareholders, that prompts heightened scrutiny when the board acts to defend against "threats" to the "corporate enterprise."[71] Although directors owe at all times to the corporation a duty of care and of loyalty,[72] depending on a given transaction's characteristics, courts may inflict higher standards of review on a board to meet its duties.[73] Additionally, the board's duty of loyalty may shift so as to no longer be owed to the corporation as an entity.[74]

A. Delaware Precedent

i. Unocal

Unocal Co., v. Mesa Petroleum Co.[75] marks the beginning of current enhanced judicial scrutiny application.[76] In *Unocal*, the board was faced with a highly coercive front-loaded back-end-

69 *See* Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985) (stating that directors are charged with an "unyielding fiduciary duty to the corporation and its shareholders"); MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239, 1247 (Del. Ch. 1985) (discussing balancing of internal and external interests corporate directors are faced with).

70 Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (examining reasons for need of judicial examination of certain board decisions before protections of business judgment rule can be given).

71 *Id.* at 957. "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." *Id.* at 955.

72 *See id.* at 955 (stating that corporate directors have a "fiduciary duty to act in the best interests of the corporation's stockholders"); Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967–70 (Del. Ch. 1996) (outlining duty of care owed by directors to corporation).

73 *See Unocal*, 493 A.2d at 954 (discussing need for judicial examination of certain board decisions before business judgment rule can be applied); Kerr, *supra* note 62, at 617-20 (positing Delaware imposes enhanced judicial scrutiny in certain transactions prior to protection of business judgment rule).

74 *See* Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986) (establishing shift in fiduciary duty from "the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit"); Gary von Stange, Note, *Corporate Social Responsibility Through Constituency Statutes: Legend or Lie?*, 11 HOFSTRA LAB. L. J. 461, 476 (1994) (discussing shift in fiduciary duty that occurs when board action leaves realm of *Unocal* and enters *Revlon*).

75 493 A.2d 946 (Del. 1985).

76 *See id.* at 954 (discussing need for heightened judicial scrutiny of certain board decisions); Kerr, *supra* note 62, at 617–18 (discussing *Unocal* and its predecessors as establishing enhanced judicial scrutiny).

cash-out tender offer.[77] Financial advisors for Unocal deemed this hostile tender offer's front end to be far below the liquidation value of Unocal's stock and the back end to be junk rated.[78] In response, the Unocal board attempted to remove the hostile tender offer's coerciveness by initiating a counter self-tender offer which effectively supplanted an alternative to the hostile offer's back-end junk bonds.[79] The court upheld as valid both of Unocal's purposes, to defeat an inadequate hostile offer and to prevent the back end issuance of junk bonds, in initiating its tender offer in the face of the coercive hostile offer.[80] In upholding these purposes, the court established a new test, applicable prior to application of business judgment rule protections, for when corporate boards are placed in the context of a takeover.[81] First, directors are required to show they had reasonable grounds for perceiving a threat to the corporate enterprise.[82] This can be satisfied by "showing good faith and reasonable investigation,"[83] of which is materially enhanced when the board is comprised of outside, independent directors.[84] Directors are further required to demonstrate their actions were "reasonable in relation to the

[77] *See Unocal*, 493 A.2d at 949–50. *See generally* Abraham Bell & Gideon Parchomovsky, *The Integration Game*, 100 COLUM. L. REV. 1965, 1997 (2000) (describing attributes of two-tier, front-loaded tender offer).

[78] *See Unocal*, 493 A.2d at 950–51 (explaining "minimum cash value that could be expected from a sale or orderly liquidation for 100% of Unocal's stock was in excess of $60 per share" and that back-end of proposal would be financed with "junk bonds"); *see also* John C. Anjier, Comment, *Anti-Takeover Statutes, Shareholders, Stakeholders and Risk*, 51 LA. L. REV. 561, 622 n.174 (1991) (defining Unocal's two-tier front-end, back-end offer).

[79] *See Unocal*, 493 A.2d at 951 (explaining Unocal's discriminatory self-tender offer for 49% of Unocal's remaining shareholders upon consummation of Mesa's tender offer); *see also* Adam R. Waldman, Comment, *OTC Derivatives Systemic Risk: Innovative Finance or the Dance into the Abyss?*, 43 AM. U. L. REV. 1023, 1053 n.209 (1994) (citing studies alleging junk bond default rate is approximately 34%).

[80] *See Unocal*, 493 A.2d at 956 (adopting selective exchange offer, Unocal was attempting to defeat Mesa's inadequate offer and provide those stockholders who would otherwise be coerced into accepting junk bonds).

[81] *See* Unocal Co. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (discussing newly devised business judgment test).

[82] *See Unocal*, 493 A.2d at 955 (explaining proper directorial measures to protect against inherent conflict); *see also* Cheff v. Mathes, 199 A.2d 548, 555–56 (Del. 1964) (stating reasonable grounds for believing danger exists in corporate policy and effectiveness must be shown).

[83] *Unocal*, 493 A.2d at 955 (quoting Cheff v. Mathes, 199 A.2d, 548, 555 (Del. 1964)).

[84] *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1375 (Del. 1995) (holding presence of mostly outside independent directors materially enhances evidence of reasonableness); *Unocal*, 493 A.2d at 955 (proffering that outside independent directors should have acted according to standards).

threat posed."[85] Considerations involving price terms, nature of the present market environment, timing and legality of the offer as well as effects on constituencies, risk of non-consummation and the quality of securities offered may be reviewed to determine whether director action fits within the guise of reasonableness.[86] The key aspect of this approach is that directors, in carrying out their duties, must focus solely on protecting the "corporate enterprise," which includes preconceived plans for long term financial growth.[87] Given that directors are perpetually conflicted between attainment of personal self-interest and of corporate goals, it is clear why the Delaware Supreme Court reached the result it did.[88]

Delaware court decisions subsequent to *Unocal* intimated the bounds of its two step test; however, it was not until *Unitrin, Inc. v. American General Corp.*[89] was decided that the Court outlined a definitive analysis.[90] The facts of *Unitrin* involved a situation analogous to that of Unocal; specifically, a bidder attempting to acquire, via hostile tender offer, ownership and control of a target, namely Unitrin.[91] In this case, the board employed two

85 *Unocal*, 493 A.2d at 955 (delineating balance analysis).

86 *See* Newell Co. v. Vt. Am. Co., 725 F. Supp. 351, 372–73 (N.D. Ill. 1989) (referencing Delaware's method for determining whether there is threat to corporation); *Unocal*, 493 A.2d at 955 (providing examples of concerns regarding takeover bids).

87 *See Unitrin*, 651 A.2d at 1376 (stating, "the directors of a Delaware corporation have the prerogative to determine that the market undervalues its stock and to protect its stockholders from offers that do not reflect the long term value of the corporation under its present management plan."); Unocal Co. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (explaining board must protect corporate enterprise, including stockholders).

88 *See Unocal*, 493 A.2d at 955 ("We must bear in mind the inherent danger in the purchase of shares with corporate funds to remove a threat to corporate policy when a threat to control is involved. The directors are of necessity confronted with a conflict of interest, and an objective decision is difficult."); Michael B. Dorff, *Softening Pharaoh's Heart: Harnessing Altruistic Theory and Behavioral Law and Economics to Rein in Executive Salaries*, 51 BUFF. L. REV. 811, 813 n.19 (2003) (explaining that during hostile takeovers, board members risk losing their jobs, but must still keep interests of shareholders in mind when an offer is beneficial to those shareholders).

89 651 A.2d 1361 (Del. 1995).

90 *See id.* at 1387 (defining "draconian" as preclusive and coercive board action and delineating tests for determining "preclusive" and "coercive"); *see also* Paul L. Regan, *Great Expectations? A Contract Law Analysis for Preclusive Corporate Lock-Ups*, 21 CARDOZO L. REV. 1, 96 (1999) (explaining that *Unitrin* test asks first, whether Board responses to a hostile takeover are either preclusive or coercive to shareholders, and if not, whether it was reasonable response).

91 *See Unitrin*, 651 A.2d at 1368–70 (finding Unitrin board unanimously concluded the American General's offer was not in the best interests of Unitrin's shareholders); *see also* Alexander B. Johnson, *Financial Services Regulation: A Mid-Decade Review: Note: Is Revlon Only Cosmetic?: Structuring a Merger in the Mid-1990s*, 63 FORDHAM L. REV. 2271,

defensive strategies, a Rights Plan and a Repurchase Plan,[92] in addition to a preexisting limitation in Unitrin's certificate of incorporation on the ability of Unitrin to enter into a business combination of any making.[93] The Court of Chancery concluded that the above defensive combination had the effect of "chill[ing] any unsolicited acquiror from making an offer."[94] On appeal, the Delaware Supreme Court found the Court of Chancery to have applied the wrong standard of review and, although the Delaware Supreme Court agreed with the lower court's holding, remanded the case for application of the correct standard of review.[95] In its directions for remand, the Delaware Supreme Court, in a less than novel directive, explicated thoroughly what has become standard *Unocal* application.[96] To begin, the court clarified that "inextricably related" defensive actions taken by a board were to be viewed as a unitary response for Unocal application purposes.[97] Following this, the Court elucidated a two step analysis for the second prong of *Unocal's* test, expanding the Court's prior prohibition on defensive board action "draconian" in

2274 (1995) (explaining Unitrin Board's repurchase plan was in response to American General's unsolicited bid).

92 *See Unitrin*, 651 A.2d at 1370–71. On recommendations by Morgan Stanley, Unitrin's Board authorized an open stock repurchase plan, allowing the company to repurchase 1/5 of Unitrin's outstanding common shares. *Id.*

93 *See id.* at 1377–78. According to the certificate, a director majority vote, or a stockholder supermajority vote of 75% was required to approve a takeover. *Id.*

94 *See id.* at 1377–78 (finding repurchase plan did more that protect stockholder's interests and was possibly made to secure director's own positions on the Board).

95 *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1389 (Del. 1995) (finding Chancery Court erred in substituting its judgment on the necessity of the Repurchase program, for the judgment of the Board); *see also* Troy A. Paredes, *The Firm and the Nature of Control: Toward a Theory of Takeover Law*, 29 IOWA J. CORP. L. 103, 158 (2003) (explaining on remand, Chancery Court was to determine if Unitrin's responses were within a "range of reasonableness").

96 *See Unitrin*, 651 A.2d at 1386–88 (giving case history following *Unocal*, outlining steps made in first determining whether Board response is "draconian" and second whether board responses are founded on reasonable business judgment); *see also* Ronald J. Gilson, *Unocal Fifteen Years Later (And What We Can Do About It)*, 26 DEL. J. CORP. L. 491, 506 (2001) (articulating standard on remand, that responses to takeover attempts must be determined to not make proxy fights "'mathematically impossible" or "realistically unattainable'").

97 *See Unitrin*, 651 A.2d at 1387 (explaining Board's overall response, with justifications for each action, should be evaluated by the courts); *see also* Gilbert v. El Paso Co. 575 A.2d 1131, 1145 (Del. 1990) ("In assessing the plaintiffs' allegations, we must evaluate the El Paso directors' overall response to the December offer, including the justification for each challenged defensive measure, and the results achieved thereby."); Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1343 (Del. 1987) ("Because Newmont's actions here are so inextricably related, the principles of *Unocal* require that they be scrutinized collectively as a unitary response to the perceived threats.").

nature.[98] Board action now found to be preclusive or coercive with respect to the stockholder vote violates the second prong; however, even if not preclusive or coercive, it remains to be determined whether the action was within or without the "range of reasonableness."[99] The conclusion stands, therefore, absent fraud or other misconduct, reasonable, non-preclusive and non-coercive action taken in response to a reasonably perceived threat will yield business judgment rule protection.[100]

The only remaining extension of *Unocal* due noting was decided four years after *Unocal* in *Moran v. Household Int'l, Inc.*[101] *Moran* involved the Household International, Inc ("Household") board enacting preemptively a defensive mechanism to prevent future takeovers.[102] In brief explanation, the plan consisted of two triggering events, each having the effect of empowering the board to counter and forestall takeover attempts until the board could thoroughly review the given

98 *See Unitrin*, 651 A.2d at 1387–88 (expounding upon *Unocal* proportionality test); *see also* Gilbert L. Henry, Note, *Continuing Director Provisions: These Next Generation Shareholder Rights Plans are Fair and Reasoned Responses to Hostile Takeover Measures*, 79 B.U. L. REV. 989, 1010 n.157 (1999) (acknowledging the *Unitrin* court's exposition of *Unocal* test to entail twofold inquiry).

99 *Unitrin*, 651 A.2d at 1388. The court noted that, when confronted with a defensive measure neither preclusive nor coercive, a court applying *Unocal* must then concern itself with whether the action is within the "range of reasonableness." *Id.* The Delaware Supreme Court directed that courts take into account three factors when reviewing "range of reasonableness." *Id.* at 1389. The first factor is to determine whether the action is "a statutorily authorized form of business decision which a board of directors may routinely make in a non-takeover context." *Id.* Second, the court should consider whether, as a defensive response, the action was "limited and corresponded in degree or magnitude to the degree or magnitude of the threat, (*i.e.*, assuming the threat was relatively 'mild,' was the response relatively 'mild?')." *Id.* Finally, the court must consider whether the defensively acting board "properly recognized that all shareholders are not alike, and provided immediate liquidity to those shareholders who wanted it." *Id.* There are several factors pertinent to a "range of reasonableness" determination. *See* Gregory W. Werkheiser, Comment, *Defending the Corporate Bastion: Proportionality and the Treatment of Draconian Defenses from* Unocal *to* Unitrin, 21 DEL. J. CORP. L. 103, 120 (1996).

100 *See Unitrin*, 651 A.2d at 1388 (concluding that defensive response which is not draconian and is within range of reasonableness shall be accorded judicial deference); *see also* Kimberly J. Burgess, Note, *Gaining Perspective: Directors' Duties in the Context of "No-Shop" and "No-Talk" Provisions in Merger Agreements*, 2001 COLUM. BUS. L. REV. 431, 458 (2001) (noting that it is only when corporate directors satisfy *Unocal* that defensive measures by board will fall within ambit of the business judgment rule).

101 500 A.2d 1346 (Del. 1985).

102 *See id.* at 1349 (noting that the measure was not adopted by the corporation in the context of a hostile takeover). *See generally* Suzanne S. Dawson, Robert J. Pence, & David S. Stone, *Poison Pill Defensive Measures*, 42 BUS. LAW. 423, 423 (1987) (defining "poison pill[s]" as "defensive measures adopted by boards of directors in response to takeover attempts or in advance of possible takeover attempts that can cause sever economic repercussions in acquirer or potential controlling person").

proposal.[103] This defensive action was not arbitrarily taken by Household's board, but rather was prompted by concerns related to recent market takeover rates and Household's inherent attractiveness as a target candidate.[104] Expanding the application of *Unocal*, the Delaware Supreme Court held the Household board's implementation of the defensive Rights plan to be within the board's business judgment.[105] In dictum, however, the court succinctly noted that whether the rights plan remains within the board's business judgment will depend on the board's actions if and when it is faced with an actual tender offer.[106]

ii. Revlon

Inaugurated in the same year the Delaware Supreme Court first embarked on the *Unocal* analysis, the *Revlon* duty, termed after *MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc. (Revlon)*,[107] governs situations calculated to fundamentally change the structure of corporate control.[108] Three parties were engaged in the *Revlon* discourse: Revlon, Inc. ("Revlon"); Pantry

[103] *See Moran*, 500 A.2d at 1348-49. The two triggering events were: one, an announcement of a tender offer for 30% of Household's shares; and two, the acquisition of 20% of Household's shares by any single entity or group. *Id.* For a discussion of the various provisions of "poison pill" plans and their efficacy as takeover preventatives, *see generally* Dawson, *supra* note 102, at 426–32.

[104] *See Moran*, 500 A.2d at 1349 (noting the concerns which actuated defensive measure); Moran v. Household Int'l, Inc., 490 A.2d 1059, 1064 (Del. Ch. 1985) (noting corporation's susceptibility to takeover).

[105] *See Moran*, 500 A.2d at 1357 (concluding that directors acted in good faith in exercising an informed business judgment in adopting Rights Plan and that Plan was reasonably related to takeover threat with which board was confronted); *see also* Peter V. Letsou, *Are Dead Hand (and No Hand) Poison Pills Really Dead?*, 68 U. CIN. L. REV. 1101, 1116–17 (2000) (echoing *Moran* court's conclusion that there existed reasonable grounds to believe that corporation was susceptible to takeover proposal and that defensive measure was reasonably related to this threat).

[106] *See Moran*, 500 A.2d at 1357 ("The ultimate response to an actual takeover bid must be judged by the Directors' actions at that time[.]"); *see also* David A. Rosenzweig, Note, *Poison Pill Rights: Toward a Two-Step Analysis of Directors' Fidelity to their Fiduciary Duties*, 56 GEO. WASH. L. REV. 373, 373 (1988) (reiterating Moran court's admonition that, while Rights Plan was proper in pre-takeover bid context, judicial scrutiny of director action in the face of takeover bid must be deferred until actual takeover bid arises).

[107] 501 A.2d 1239 (Del. Ch. 1985).

[108] *See id.* at 1250 (stating that board of directors, when acting as voluntary negotiators, must prove the rationality their decisions); Paramount Communications, Inc. v. Time Inc., 571 A.2d 1140, 1150 (Del. 1989) (defining two situations that implicate Revlon's enhanced judicial scrutiny); QVC Network, Inc. v. Paramount Communications Inc., 635 A.2d 1245, 1266 (Del. Ch. 1993), *aff'd* 637 A.2d 828 (Del. 1993) (holding Revlon's enhanced judicial scrutiny to apply when there is a change of corporate control).

Pride; and Forstmann Little & Co ("Forstmann Little").[109] Following discussions between Pantry Pride and Revlon executives for a possible acquisition of Revlon by Pantry Pride, Revlon instituted two anti-takeover defense mechanisms, neither of which entirely foreclosed potential offerors.[110] Subsequently, over the course of roughly two months, Pantry Pride and Forstmann Little partook in a bidding war for Revlon.[111] Despite communication by Pantry Pride to Revlon that Pantry Pride intended to counter every offer made by Forstmann Little, Revlon tilted the bidding process in favor of Forstmann Little,[112] eventually granting Forstmann Little both a "lock-up"[113] and "no-shop"[114] provision. Together, these provisions effectively ended all bidding and spawned *Revlon*.[115] The Delaware Supreme Court, addressing this situation, held that, given the Revlon board of directors' prior concession to a break up of Revlon,[116] the fiduciary duty Revlon's board of directors owed to Revlon's

109 *See Revlon*, 501 A.2d at 1242 (stating parties involved in case); *see also* Daniel S. Cahill & Stephen P. Wink, *Time and Time Again the Board is Paramount: The Evolution of the Unocal Standard and the Revlon Trigger Through* Paramount v. Time, 66 NOTRE DAME L. REV. 159, 170 (1990) (listing parties involved in lawsuit).

110 *See Revlon*, 501 A.2d at 1244, 1247 (referring to two anti-takeover defense mechanisms authorized by board of directors and noting adoption of defensive devices, such as those adopted by Revlon, are, in general terms, within board's business judgment as "calculated to strengthen the board's bargaining position"); *see also* Cahill & Wink, *supra* note 109, at 170 (commenting on Revlon's defensive tactics to thwart Pantry Pride's takeover).

111 *See Revlon*, 501 A.2d at 1244–46 (explaining bidding war between Pantry Pride, Forstmann Little and Adler & Shaykin); *see also* Cahill & Wink, *supra* note 109, at 170-71 (describing the tactical maneuvers taken by each corporation during the bidding war).

112 *See Revlon*, 501 A.2d at 1248 (referring to exclusionary methods against Pantry Pride by Revlon); *see also* Note, *Lock-Up Options: Toward a State Law Standard*, 96 HARV. L. REV. 1068, 1079 (1983) (deciphering between legal and illegal lock-up options by applying primary purpose test so that if corporation's primary purpose is to exclude parties from participating in bidding process, then it qualifies as illegal lock-up option).

113 *See* MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239, 1249 (Del. Ch. 1985) (defining lock-up provision); *see also* Cahill & Wink, *supra* note 109, at 171 (referring to Forstmann's demand for lock-up provision for two of Revlon's divisions).

114 *See Revlon*, 501 A.2d at 1249 (defining no-shop provision); *see also* Cahill & Wink, *supra* note 109, at 171 (referring to Forstmann's demand for no-shop provision in the agreement).

115 *See* Unocal Co. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985) (explaining parameters of defense mechanisms under business judgment rule); *see also Revlon*, 501 A.2d at 1250 (noting that Revlon's board of directors breached its duty of loyalty by excluding Pantry Pride from bidding process).

116 *See Revlon*, 501 A.2d at 1248 (referring to defense mechanisms used by Revlon's board of directors); *see also* Robert E. Bull, Note, *Directors' Responsibilities and Shareholders' Interests in the Aftermath of* Paramount Communications v. Time, Inc., 65 CHI.-KENT L. REV. 885, 888–89 (1989) (commenting that board of directors' prior acts were signals of board's willingness to sell corporation).

shareholders shifted from protecting the 'corporate bastion'[117] solely to maximizing shareholder wealth.[118] The Court then deemed the Revlon board's issuance of the "lock-up" and "no-shop" provisions to Forstmann Little to be in breach of this fiduciary duty.[119] Specifically, in reaching this holding, the court acknowledged abandonment by the board of future prospects as a going concern in the present form, consequently requiring the board to auction the corporation to the highest bidder.[120]

Following its decision in *Revlon,* the Delaware Supreme Court noted in *Paramount Communications, Inc. v. Time Inc.*[121] *Revlon's* application to two distinct situations: one, where 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;"[122] and two, where a corporation, "in response to a bidder's offer . . . abandons its long-term strategy and seeks an alternative transaction also involving the break-up of the company."[123] Limiting *Revlon's* application to the above two instances, *Time's* holding solidified the interrelationship between *Unocal* and *Revlon* by deeming defensive action taken by a target board to ward off long-term-goal-threatening hostile bidders during a merger not to be within *Revlon.*[124] Notably, the structure of the discourse in *Time* is distinguishable from that of *Revlon* and, thus, requiring of different treatment. Unlike

117 *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1388 (Del. 1995) ("When a corporation is not for sale, the board of directors is the defender of the metaphorical medieval corporate bastion and the protector of the corporation's shareholders."); *see also* Cahill & Wink, *supra* note 109, at 172–73 (commenting during that time, defense mechanisms were useless and that board's only responsibility was to protect shareholders' value).

118 *See Revlon,* 501 A.2d at 1250–51 ("[T]he recognition of [a] breakup . . . required the board to view its primary role as the promoter of bids, with price the dominant consideration.").

119 *See Revlon,* 501 A.2d at 1250 (citing how board did not conform to duty of loyalty component to of business judgment rule).

120 *See Revlon,* 501 A.2d at 1251 (explaining how court failed its primary role as promoter of bids by permitting other considerations to dictate its approach to shareholders); *see also* Wells M. Engledow, *Structuring Corporate Board Action To Meet The Ever-Decreasing Scope of* Revlon *Duties,* 63 ALB. L. REV. 505, 513 (1999) (discussing holding of *Revlon*).

121 571 A.2d 1140 (Del. 1990).

122 *Id.* at 1150.

123 *Id.*

124 *See id.* at 1150–51 (explaining that if "the board's reaction to a hostile tender offer is found to constitute only a defensive response . . . *Revlon* duties are not triggered, though *Unocal* duties attach"); *see also* Engledow, *supra* note 120, at 514 (comparing similarities and differences between *Revlon* and *Unocal*).

Revlon, the hostile bidder's target in *Time* was, and intended to remain, the acquirer and not the acquiree.[125] As such, the Court in *Time* deemed defensive actions taken with regard to protecting the corporation's continued existence to be outside the clutches of *Revlon* analysis.[126]

Thought to be definitively limited in *Time* to two situations, *Revlon* proved in *QVC Network, Inc. v. Paramount Communications Inc.*[127] to be a more controlling adversary.[128] The *QVC* dilemma began with an initial highly locked up agreement [129] between Paramount Communications ("Paramount"), the defendant, and Viacom to merge the two entities. The merger would transfer a controlling, seventy percent block of shares to Viacom's pre-merger majority shareholder.[130] In an attempt to prevent hostile intervention, Viacom and Paramount executives released press statements that neither company was up for general sale, phoned possible interested parties to dissuade them from acting,[131] and deliberately avoided inquiry into candidates Paramount knew were of interest.[132] All of this action was, however, to no avail and a hostile bidder, QVC, entered negotiations.[133] Over the

125 *See Time*, 571 A.2d at 1143–49. Time's board had first considered expanding operations in the spring of 1987. *Id.* at 1144. As Paramount made successive bids, Time reiterated its position that only a deal with Warner was in its future. *Id.* at 1149.

126 *See id.* at 1150–51 (holding *Unocal* duties attach to *Time's* actions).

127 635 A.2d 1245 (Del. Ch. 1993).

128 *See Time*, 571 A.2d at 1265 (citing how under Delaware law, there are two circumstances which may implicate *Revlon* duties); *see also* Engledow, *supra* note 120, at 516 (clarifying how *Revlon* duties should be interpreted).

129 *See QVC*, 635 A.2d at 1251 (discussing asset and stock option lockup terms); *see also* S. Todd Barfield, Note, *Directors Or Auctioneers? Turning Back Time in* Paramount v. QVC, 62 UMKC L. REV. 893, 908 (1994) (stating that heightened duties of *Revlon* must apply because of lockup provisions).

130 *See QVC*, 635 A.2d at 1249 (noting by selective deployment of poison pill, Paramount is forcing shareholders to favor Viacom's lower price).

131 *See id.* at 1252 (explaining that Mr. Redstone called executives from TCI and QVC to discourage them from bidding).

132 *See id.* at 1253 (noting board quickly rejected unwelcome offer with little data).

133 *See* QVC Network, Inc. v. Paramount Communications, Inc., 635 A.2d 1245, 1252–58 (Del. Ch. 1993). QVC began contact with Paramount by offering to acquire Paramount at $80 per share. *Id.* at 1252. Despite Paramount's prompt public announcement that a deal with Viacom was in its best interests, Paramount agreed to go over the QVC proposal. *Id.* at 1253. QVC also attempted to meet in person and discuss the deal, but Paramount delayed meeting. *Id.* at 1253–54. Frustrated, QVC decided, after seeing private negotiations were of no avail, that its only option would be to initiate a public, hostile tender offer. *Id.* at 1254. It did so at $80 cash for the first 51% of Paramount's common stock, followed by a second step stock-for-stock exchange on non-coercive terms. *Id.* In response to this, Viacom upped its bid. *Id.* Financial advisors for Paramount

ensuing three months Paramount's board provided preferential treatment to Viacom.[134] The Delaware Court of Chancery addressed this situation, beginning its analysis by rejecting the limited approach of *Time*.[135] The court then proceeded to hold that a mere change of corporate control requires directors to maximize short-term shareholder wealth.[136] Fundamental to this holding is the reality that long term goals become irrelevant to pre-merger minority shareholders who remain shareholders in a control-changing merger, in that, absent supermajority provisions or other like protections,[137] nothing prevents the new controlling shareholder from squeezing-out in a second step the remaining minority shareholders and thus depriving them of any long term benefits.[138] The bottom line, therefore, now stands that business combinations having the effect of fundamentally altering the control structure of a corporation invoke *Revlon*.[139]

concluded new Viacom's offer to be worth roughly $1.65 more per share than QVC's offer as well as likely to yield $3 billion more in incremental shareholder value. *Id.* at 1256. Based upon these financial reports, Paramount executed an agreement with Viacom. *Id.* Following this agreement signing, both QVC and Viacom upped their bids again. Paramount, however, stuck its ground, refusing to agree to any procedures amounting to an auction. *Id.* at 1257. In the end, Paramount concluded, based on a new set of financial reports by its financial advisor, not to further pursue negotiations with QVC. *Id.* To note, however, these financial statements only stated a merger with Viacom was "fair" and expressly warned no opinions were being given with regard to QVC's offer. *Id.* at 1255. This lack of opinion followed from Paramount's prohibition on its financial advisor from speaking with QVC. *Id.*

134 *See id.* at 1252–53 (explaining that Viacom and Paramount publicly and privately clarified that other bids were unwelcome and Mr. Redstone called executives from TCI and QVC to discourage them from bidding).

135 *See id.* at 1265 (noting that circumstances here are different and raise fiduciary and fairness concerns).

136 *See id.* at 1266 ("In colloquial terms, that duty is to do for the shareholders what the shareholders would otherwise do for themselves—to seek the best premium-conferring transaction that is available in the circumstances.").

137 *See id.* at 1267 n.42 (describing possible post-merger minority protections). *See generally* Barfield, *supra* note 129, at 910–11 (noting the board was required to take a closer look at increased bid).

138 *See QVC*, 635 A.2d at 1267 (noting that shareholders will have no long –run benefits); *see also* Joseph W. Bartlett & Kevin R. Garlitz, *Fiduciary Duties in Burnout/Cramdown Financings*, 20 IOWA J. CORP. L. 593, 603 (1995) (noting the compelling element effect 'squeeze out mergers' have on minority shareholders); Carol Goforth, *Proxy Reform as a Means of Increasing Shareholder Participation in Corporate Governance: Too Little, But Not Too Late*, 43 AM. U. L. REV. 379, 425 n. 291 (1994) (explaining process of "squeeze out merger").

139 *See* QVC Network, Inc. v. Paramount Communications, Inc., 635 A.2d 1245, 1266–67 (Del. Ch. 1993) (noting there are few events that are as significant as change in control); *see also* Barfield, *supra* note 129, at 908 (noting this case is clearly change of control case).

III. PRECLUSIVE AND COERCIVE BOARD ACTION

Corporate directors owe a fiduciary duty to act in the best interests of the corporation's shareholders and may take defensive action to protect the corporate enterprise, and thus the shareholders, from reasonably perceived dangers.[140] Threats of opportunity loss, structural coercion and substantive coercion are legitimate concerns a board may support its defensive action upon.[141] It is imperative that this leeway be extended to boards if they are to be expected to succeed in their fundamental duties;[142] however, the law prevents the totality of board action from being preclusive or coercive of the shareholders' will.[143] As previously stated, the Court in *Omnicare* held a mixture of shareholder and board action to constitute "board action" within the context of *Unocal-Revlon* precedent and, accordingly, concluded that the

[140] *See* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985) (noting that fiduciary duty to act in best interests of corporation's shareholders extends "to protecting the corporation and its owners from perceived harm, whether a threat originates from third parties or other shareholders"); *see also* Grand Metropolitan Public, Ltd. v. Pillsbury Co., 558 A.2d 1049, 1055 (Del. Ch. 1988) (discussing how fiduciary duties of care and loyalty owed to corporation and its shareholders apply "with equal force" to corporate mergers and corporate takeovers).

[141] *See* Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1153 n. 17 (Del. 1989) (highlighting three different types of hostile threats that exist and how some commentators believe that acceptance of "substantive coercion" helps to guarantee legitimacy of *Unocal* standard). *See generally* Ronald J. Gilson & Reinier Kraakman, *Delaware's Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 BUS. LAW. 247, 269 (1989) (noting courts should classify various types of "threats" into three categories of opportunity loss, structural coercion, and substantive coercion in order to apply appropriate test effectively).

[142] *See* Richard M. Buxbaum, *American Law in a Time of Global Interdependence: U.S. National Reports to the XVITH International Congress of Comparative Law: Section III Facilitative and Mandatory Rules in the Corporation Law(s) of the United States*, 50 AM. J. COMP. L. 249, 258 (2002) (noting Delaware courts have denied shareholders' right to amend corporate bylaws to enable shareholders to participate in regulating corporate business and affairs); Kurt F. Gwynne, *Employment of Turnaround Management Companies, "Disinterestedness" Issues Under the Bankruptcy Code, and Issues Under Delaware General Corporation Law*, 10 AM. BANKR. INST. L. REV. 673, 703–04 (2002) (describing board's duty to run the corporation's business and affairs and noting duty is non-delegable).

[143] *See* Jeffrey N. Gordon, *Mergers and Acquisitions: "Just Say Never?" Poison Pills, Deadhand Pills, and Shareholder-Adopted ByLaws: An Essay For Warren Buffett*, 19 Cardozo L. Rev. 511, 525 (1997) (describing Unocal/Unitrin analysis as "significantly [circumscribing] a reviewing court's scrutiny of defensive tactics"); Henry, *supra* note 98, at 1016–18 (explaining thoroughly second prong of Unocal/Unitrin analysis and applying analysis to poison pills); Thomas A. Swett, Comment, *Merger Terminations after* Bell Atlantic*: Applying a Liquidated Damages Analysis to Termination Fee Provisions*, 70 U. COLO. L. REV. 341, 367–68 (1998) (positing *Unocal/Unitrin* framework recognizes greater respect for shareholder franchise as well as the board of directors' need for latitude when exercising their duties).

amalgamation was preclusive and coercive.[144] It has been previously submitted that the Delaware Supreme Court erred in its application of *Unocal* and *Revlon*, as well as both their progeny.

A. Unocal Offending Board Action

i. Overview

At this point, before delving into a juxtaposition of *Omnicare* with prior interpretations of preclusive and coercive enounced by the Delaware courts, I would like to make two observations, each of extreme significance. First, the initial post-*Unocal* statements of the Delaware Supreme Court regarding openness to board action in times of corporate distress were enounced in *Revlon*.[145] The Court opined in *Revlon* that judicial review will be different where only one genuine bidder exists in the market and fear of losing that genuine bidder prompts decisive board action.[146] This declaration by the Court was ostensibly intended to grant greater deference to a board to lock-up a deal where, as in *Omnicare*, it is faced with no viable alternative.[147] Furthermore, this declaration, by recognizing the need of a board to grant more favorable terms in certain circumstances, purports to narrow the definitions of preclusive and coercive action in such situations lacking an array of bidders.

Finally, of major significance is the Court's prior interpretation of *Unocal* in *Mills Acquisition Co. v. Macmillan Inc.*,[148] the

144 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 932 (Del. 2003) (noting that when examining reasonableness of board action, "defensive devices" employed must be "proportionate to the perceived threat" to both corporation and shareholders, if merger transaction does not occur).

145 MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239 (Del. Ch. 1985).

146 *See id.* at 1250 (discussing business judgment rule and how it doesn't apply to lock-up options which ultimately relieve directors of liability for their own defensive policies).

147 *See* Black & Decker Corp. v. American Standard, Inc., 682 F. Supp 772, 784 (D. Del. 1988) (highlighting another factor determining validity of lock-up options is the timing of auction process); *see also Revlon*, 501 A.2d at 1250 (discussing significance of lock-up provisions and how they must not be used to "retard" bidding process, enforcing idea that shareholders are best served in competitive marketplace).

148 559 A.2d 1261 (Del. 1989).

approach oddly declared as didactic by the Court in *Omnicare*.[149] In *Mills*, the court focused on board actions that enhanced the shareholder's interest and were "reasonable in relation to the advantage sought to be achieved."[150] Be it that this is simply a rewording of *Unocal* in positive terms, it illustrates that the Court's focus, at least before the year 2000, was in protecting board action motivated by intentions to boost shareholder wealth.[151] Taking into account the Court's statements in *Revlon*, which arguably narrowed preclusive and coercive board action in situations with dismal bidder alternatives, the Court's statements in *Mills Acquisition Co. v. Macmillan Inc.* seemingly indicate boards are to have a more expansive power to act, before their action is declared preclusive or coercive, to protect shareholders by locking in for them the best of available alternatives, given otherwise imminent harm to occur absent the protective action.

ii. Preclusive and Coercive

An analysis juxtaposing *Omnicare* with historical Delaware case law begins with *AC Acquisitions Corp. v. Anderson, Clayton & Co.*,[152] the case in which the Delaware Court of Chancery held preclusive and contrary to *Unocal's* mandate a board's defensive action taken toward a hostile tender offer.[153] Faced with an arguably fair and non-coercive tender offer by AC Acquisitions, the Anderson, Clayton & Co. board initiated as a defense a self-tender offer for eight million shares at sixty dollars per share.[154] If successfully consummated, this self-tender offer would have had the effect of depressing all non-tendering shares to roughly one third of their pre-consummation values.[155] Prior to *AC*

149 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 933 (Del. 2003) (holding the *Macmillan* analysis inapplicable in situations involving defensive devices being "challenged vis-à-vis their effect on a subsequent competing alternative merger").

150 *Mills*, 559 A.2d at 1288.

151 *See id.* (noting that if board believed that shareholder interests were enhanced, and if board's actions were reasonable, then those actions are entitled to protection of business judgment rule); *see also* Karl F. Balz, *No-Shop Clauses*, 28 DEL. J. CORP. L. 513, 533 (2003) (explaining benefits and problems arising from deal protection devices enacted while boards are under a duty to maximize shareholder wealth).

152 519 A.2d 103 (Del. Ch. 1986).

153 *See id.* at 114 (holding that breach of duty of loyalty was likely).

154 *See id.* at 109–110 (describing terms of tender offer).

155 *See id.* at 106–110 (noting lack of choices that shareholders had).

Acquisitions Corp., acceptable board of director action taken in defense of a corporation was limited by *Unocal* to that which was not 'draconian' in nature; however, although the Court in *Unocal* noted the duty of loyalty owed to shareholders, it did not explicate what constituted draconian action toward shareholders.[156] In *AC Acquisitions Corp,* the Court added clarity to *Unocal* by focusing on the coercive affect that the Anderson, Clayton & Co. board's action had on the shareholder franchise.[157] The court noted that timing of the self-tender offer such that the shareholders would have a backup in the event the A.C. Acquisitions Corp. offer failed, rather than initiating the self tender offer as a prefatory defensive action, would have been non-coercive and a different story.[158] This decision marks the beginning by the Delaware courts of a focus on actions that disrupt the shareholder franchise when determining whether to invoke *Unocal.*[159]

Albeit the Delaware Supreme Court is not bound by pronouncements of the lower Delaware courts, the Court's holding in *Omnicare* was in stark contrast to that previously declared by the Court of Chancery in *A.C. Acquisitions Corp.*[160] Specifically, in *Omnicare*, the Court held the target board's actions coercive and preclusive, despite the fact that these actions lacked persuasive effect on the shareholder franchise.

156 *See* Moore Corp. Ltd. v. Wallace Computer Servs., 907 F.Supp. 1545, 1555 (D. Del. 1995) (juxtaposing draconian means with defensive measures that are reasonable in relation to threat posed); *see also* Unocal v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985) (stating "A corporation does not have unbridled discretion to defeat any perceived threat by any Draconian means available").

157 *See* AC Acquisitions Corp. v. Anderson, Clayton & Co., 519 A.2d 103, 113–14 (Del. Ch. 1986) (noting that board decisions left shareholders with no recourse).

158 *See id.* at 114 (discussing how alternative tenders would have benefited shareholders' interests).

159 *See* Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1154–55 (Del. 1990) (discussing court's emphasis that *Unocal* applies to those situations where shareholders are coerced to act contrary to their wishes thus disrupting stability of corporation); s*ee also AC Acquisitions Corp.*, 519 A.2d at 113 (depicting court's application of *Unocal* when it reasoned that defendants' option is unreasonable in relation to threat posed because it is coercive and precludes shareholders from having ability to accept reasonable, alternative option).

160 Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 937 (Del. 2003) (ruling that NCS' board could not ignore its fiduciary duties to minority stockholders by leaving it solely to stockholders to decide when two stockholders had already combined to make outcome a "foregone conclusion"); *see also A.C. Acquisitions Corp.*, 519 A.2d at 113 (applying Unocal's test and ruling that it was unreasonable in relation to threat for board "to structure such an option so as to preclude as a practical matter shareholders from accepting" the opposing offer).

This holding seemingly abolished the prior approach, as seen in *A.C. Acquisitions Corp.* and many Delaware Supreme Court cases to follow, which focused primarily on protection of shareholder will.[161]

Chronologically following *A.C. Acquisitions Corp.* is *Paramount Communications, Inc. v. Time Inc.* ("Time").[162] In *Time*, two companies, Time and Warner, conceived a business combination consisting of a stock for stock exchange.[163] At Warner's request, Time included two protective mechanisms in the merger, specifically a no shop clause and a share exchange agreement.[164] Paramount, interested in Time and aware of the activity between Time and Warner, subsequently initiated a hostile tender offer for Time.[165] In response to Paramount's offer, Time restructured its merger with Warner into an all cash acquisition so as to remove the need for majority stockholder approval and, thus, guarantee consummation of the Time-Warner deal.[166] Suit was

161 *See Omnicare*, 818 A.2d at 944–45 (Veasey, J., dissenting). Justice Veasey clarified in his dissent that Outcalt and Shaw, the two majority shareholders, were fully informed and made an "informed choice to commit their voting power to the merger." *Id.* at 944. Justice Veasey also emphasized Outcalt and Shaw held a combined 65% of NCS's outstanding voting shares and, therefore, it was irrelevant whether the minority felt any "coercion" because, even if the voting agreements were not granted, the minority 35% would have had no controlling say. *Id.* It is also important to note here that both Outcalt and Shaw were experienced businessmen holding high level executive positions within NCS (Outcalt being the Chairman of NCS's board of directors; Shaw being the President, CEO and director of NCS) and, therefore, are educated in the current matter and less likely of being subject to coercion of franchise. *Id.* at 918–19.

162 571 A.2d 1140 (Del. 1990).

163 *See id.* at 1146 (noting date of Time's unanimous approval of "the stock-for-stock merger with Warner"); *see also* Phillip J. Azzollini, Note, *The Wake of* Paramount v. QVC*: Can a Majority Shareholder Avoid Triggering the Auction Duty During a Merger and Retain a Significant Equity Interest? Suggestion: A Pooling of Interests*, 63 FORDHAM L. REV. 573, 583–84 (1994) (describing merger between Time and Warner).

164 *See Time*, 571 A.2d at 1146–47 (detailing no-shop clause and share exchange agreement adopted by Time at Warner's insistence to prevent Warner being "left 'on the auction block'"); *see also* Lisa A. Duda, Comment, Paramount Communications, Inc. v. Time, Inc.*: A Decision of Paramount Significance?*, 16 DEL. J. CORP. L. 141, 153–54 (1991) (listing various protectionary measures included in Time and Warner's agreement).

165 *See Time*, 571 A.2d at 1147 (characterizing Paramount's all-cash tender offer to purchase Time as "surprising" to Time and Warner, and noting that Paramount's tender offer was not hastily planned and had been discussed for months); *see also* Steven J. Fink, *The Rebirth of the Tender Offer?* Paramount Communications, Inc. v. QVC Network, Inc., 20 DEL. J. CORP. L. 133, 153–54 (1995) (recounting circumstances surrounding Paramount's hostile tender offer).

166 *See Time*, 571 A.2d at 1148 (noting Time's decision to "recast its consolidation with Warner into an outright cash and securities acquisition of Warner by Time"); *see also* Marcel Kahan, Paramount *or Paradox: The Delaware Supreme Court's Takeover Jurisprudence*, 19 IOWA J. CORP. L. 583, 595 (1994) (noting that "[i]n response to Paramount's hostile tender offer for Time, the original merger agreement was revised to a cash tender offer by Time for Warner shares"); Mark Lebovitch & Peter B. Morrison,

eventually commenced between the parties and the Court acquired another opportunity to further *Unocal's* directive.[167] In *Time*, the Court held Time's acquisition of Warner not to invoke *Revlon* and, in addition, not to violate the principles of *Unocal*.[168] The Delaware Supreme Court's holding emphasized that Time's actions were not "aimed at 'cramming down' on its shareholders a management-sponsored alternative,"[169] but rather were centered on carrying out a preexisting board strategy.[170] The *Time* holding also noted that none of Time's defensive actions precluded Paramount from acquiring in the future the combined Time-Warner.[171]

The Court's decision in *Omnicare* again stands at diametric odds with a prior Delaware pronouncement focused on protecting shareholder rights; this time, however, the prior pronouncement being one of the Delaware Supreme Court.[172] In *Omnicare,* the

Calling a Duck a Duck: Determining the Validity of Deal Protection Provisions in Merger of Equals Transactions, 2001 COLUM. BUS. L. REV. 1, 33–34 (2001) (referring to "Time and Warner boards' defensive restructuring of their merger, a defensive action that prevented the stockholders of Time from voting on the merger").

167 *See Time*, 571 A.2d at 1141–43 (discussing facts leading to suit and affirming "Chancellor's ultimate finding and conclusion under *Unocal*"); *see also* Kerr, *supra* note 62, at 641 (noting that Paramount sought to "enjoin Time's acquisition of Warner" in Delaware's court of chancery).

168 *See* Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1150–51 (Del. 1990) (stating, " [i]f, however, [as here,] the board's reaction to a hostile tender offer is found to constitute only a defensive response and not an abandonment of the corporation's continued existence, *Revlon* duties are not triggered, though *Unocal* duties attach"); *see also* Portia Policastro, Note, *When Delaware Corporate Managers Turn Auctioneers: Triggering the* Revlon *Duty After the* Paramount *Decision*, 16 DEL. J. CORP. L. 187, 225 (1991) (noting that "[t]he Delaware Supreme Court affirmed the chancery court's ultimate finding that the *Revlon* duty had not been implicated").

169 *Time*, 571 A.2d at 1154–55. The court restated and affirmed the Chancellor's finding that Time's response was "reasonably related to the threat". *Id.* The court also discussed the facts of the closely analogous case that the Chancellor relied upon in deciding this issue, citing Shamrock Holdings, Inc. v. Polaroid Corp., 559 A.2d 257 (Del. Ch. 1989). *Id.* at 1155 n.19.

170 *See Time*, 571 A.2d at 1154 (noting Time's lengthy "investigation of potential merger candidates, including Paramount," prior to Paramount's tender offer); *see also* Lebovitch & Morrison, *supra* note 166, at 57–58 (arguing that driving force in *Time* decision was "extensive market check Time performed before it selected Warner as its merger partner").

171 *See Time*, 571 A.2d at 1155 (explaining that Time's actions were ultimately unsuccessful).

172 *See generally* Arons, *supra* note 11, at 122 (outlining changes in Delaware law as result to *Omnicare*, and noting Delaware Supreme Court's adoption of two-tiered proportionality reasonableness test for corporate defensive devices); Brian C. Smith, Comment, *Changing the Deal: How* Omnicare v. NCS Healthcare *Threatens to Fundamentally Alter the Merger Industry*, 73 MISS. L.J. 983, 999 (2004) (arguing that "[t]he court's rigid application of *Unocal* is an unwarranted step away from the

Court held as preclusive and coercive board action which unconditionally vested in the majority shareholders the decision of whether to grant voting agreements to Genesis.[173] Accordingly, the Court in *Omnicare*, by deeming the NCS board's action preclusive and coercive, misinterprets *Unocal's* focus as enounced in *Time*.[174] It is worth noting that the Court in *Omnicare* additionally ignored another crucial part of its prior analysis in *Time* by failing to recognize that future acquisition by Omnicare of the combined NCS/Genesis entity was not impossible. None of the defensive actions taken by NCS, an otherwise floundering company, prevented Omnicare from acquiring the combined NCS-Genesis entity.[175] At the very least, the NCS-Genesis merger increased NCS's otherwise illaudable bargaining position in future negotiations for merger with or acquisition by Omnicare or other like entities and, thus, created greater potential future value in the shareholders.[176]

traditionally fact-specific decision-making process that is the hallmark of Delaware corporate law").

173 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 921–26 (Del. 2003) (explaining that Outcalt and Shaw granted the voting agreements with due care and that NCS was unable to find any structurally or financially attractive transaction prior to Outcalt and Shaw granting voting agreements other than with Genesis).

174 *Compare* Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1154–55 (Del. 1989) (holding Time's defensive mechanisms did not 'cram down' on its shareholders a management-sponsored alternative or preclude Paramount from making offer for combined Time-Warner entity), *with Omnicare*, 818 A.2d at 926 (holding NCS's defensive mechanisms – forcing shareholder vote and allowing majority shareholders to grant voting agreements – to be preclusive and coercive).

175 *See Omnicare*, 818 A.2d at 925–26. The only two defensive mechanisms instituted by NCS were, one, a provision requiring the decision on whether to merge with Genesis to be sent to the shareholders regardless of the directors' opinion and, two, voting agreements representing a majority of the outstanding NCS voting shares cast in favor of a merger with Genesis. *Id.* Neither of these defensive devices had any effect on the merge-ability of the combined NCS/Genesis entity. For an example of a defensive mechanisms having this preventative effect, see Bonnie Green Camden, Note, *The Reasonableness of Defensive Takeover Maneuvers when the Corporate Raider is Mr. T. Boone Pickens:* Ivanhoe Partners v. Newmont Mining Corporation, *535 A.2d 1334 (Del. 1987)*, 57 U. CIN. L. REV. 739, 750–52 (1988), which discusses various anti-takeover measures taken by target companies.

176 *See Omnicare*, 818 A.2d at 919 (explaining that NCS was the leading provider of healthcare and support services for the elderly and, therefore, likely to add much value to a transaction with NCS); *see also* Heath D Rodman, Comment, *Death Toll for the Dead Hand?: The Survivability of the Dead Hand Provision in Corporate America*, 48 EMORY L. J. 991, 1004–05 (1999) (discussing dead hand provision and its effects); Roberta Romano, Article, *A Guide to Takeovers: Theory, Evidence and Regulation*, 9 YALE J. ON REG. 119, 161–62 (1992) (explaining ways a target may increase its bargaining position and reasoning behind it); Annette Simon, Note, MM Companies, Inc. v. Liquid Audio, Inc.*: An Attempt to Clarify the Blasius/Unocal Framework*, 52 KAN. L. REV. 1153, 1155 n.19 (2004) (indicating that new defensive techniques have emerged that have "increased the leverage of the board of directors in finding a better deal").

Unocal was clarified further by the Delaware Supreme Court in *In re Santa Fe Pacific Corp. Shareholder Litigation (Santa Fe).*[177] In *Santa Fe,*[178] the Delaware Supreme Court, responding to a motion for summary judgment, again spoke on the effects of defensive board action on the shareholder franchise.[179] The Court made two important findings: first, board action that "coerces stockholders to accede to a transaction to which they would otherwise not agree is problematic;"[180] and second, enhanced judicial review is "designed to assure that stockholders vote or decide to tender in an atmosphere free from undue coercion."[181] As in the cases noted above, the Delaware Supreme Court's focus was not solely on what outcome the board was trying to reach, but rather predominantly driven by whether the board's actions materially interfered with the shareholder's ability to independently, meaning without unwarranted influence, choose the corporation's future.[182]

Again the *Omnicare* decision is in contradiction with that previously held by the Delaware Supreme Court, such that it

177 669 A.2d 59 (Del. 1995).

178 *See id.* at 63–65. Four companies were involved in the Santa Fe litigation: Santa Fe, Burlington, Allegheny Corporation, and Union Pacific. *Id.* To begin the discourse, Burlington and Santa Fe entered into an initial merger agreement whereby Santa Fe's stockholders would receive roughly $13.50 per share as consideration. *Id.* at 63. *Union* Pacific contacted Santa Fe soon after this initial agreement was reached and proposed a merger with Santa Fe yielding roughly $18.00 per share for Santa Fe's stockholders. *Id.* Santa Fe proceeded to reject the Union Pacific offer, claiming it would not receive the requisite Interstate Commerce Commission approval. *Id.* In addition to this rejection, Santa Fe recommended to its stockholders that they not tender their shares to Union Pacific's subsequent tender offer. *Id.* at 64. In a meeting between Santa Fe and Burlington, occurring after Union Pacific's tender offer, Santa Fe requested and received a higher price for its shareholders, now roughly $20 per share. *Id.* As a final seal on its actions, Santa Fe devised three separate transactions (stock purchase by Allegheny Corporation whereby Santa Fe waived its rights provision to allow it; joint tender offer between Santa Fe and Burlington; and a Repurchase Program by Santa Fe of 10 million of is shares), having the combined effect of placing 33% of the Santa Fe shareholder vote under the control of Santa Fe. *Id.* at 64–65.

179 *See id.* at 68 (noting issues up for judgment); *see also* Kimble C. Cannon & Patrick J. Tangney, *Protection of Minority Shareholder Rights Under Delaware Law: Reinforcing Shareholders as Residual Claimants and Maximizing Long-Term Share Value by Restricting Directorial Discretion*, 1995 COLUM. BUS. L. REV. 725, 755–58 (1995) (explaining Delaware corporate law with regard to protecting shareholder franchise); William J. Carney, *Panel I: The Legacy of "The Market for Corporate Control" and Origins of the Theory of the Firm*, 50 CASE W. RES. L. REV. 215, 221–25 (1999) (discussing historical perspective on balance of power between shareholders and management).

180 *Santa Fe*, 669 A.2d at 68.

181 *Id.* at 68.

182 *See id.* (analyzing whether shareholders were given chance to vote on offering without undue influence); AC Acquisitions Corp. v. Anderson, Clayton & Co., 519 A.2d 103, 114 (Del. Ch. 1986) (noting coercive nature of tender offer for shareholders).

failed to take into account or, at the minimum, properly weigh the shareholder franchise.[183] The Court's decision in *Omnicare*, specifically that portion deeming NCS's actions preclusive and coercive, neither mentions nor alludes to disruption of the shareholder franchise. Furthermore, it does not analyze or even address the competence of the two majority shareholders who granted the voting agreements in question.[184]

The analysis now reaches the case declared by the Court in *Omnicare* to contain the "test for stockholder coercion:"[185] *Brazen v. Bell Atlantic Corporation*.[186] In *Brazen*, the Court held that coercion occurs "where the board or some other party takes actions which have the effect of causing the stockholders to vote in favor of the proposed transaction for some reason other than the merits of that transaction,"[187] noting the analysis must be done on a case-by-case basis.[188] The Court then applied the test to hold as non-coercive a $550 million termination fee, on the ground that no proof was adduced to conclude shareholders were swayed by its existence.[189]

Interestingly, although *Omnicare* was decided just five years after *Brazen* and *Brazen* was directly referred to as authoritative in *Omnicare*, the Delaware Supreme Court seems to wholly ignore its stricture.[190] At the time the NCS majority shareholders granted voting agreements, they were at the very minimum wholly informed of NCS's financial status; otherwise dismal economic future prospects; fruitless attempts to find other

183 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 935–36 (Del. 2003) (failing to address or even mention general disruption of shareholder franchise). S*ee generally* In re Santa Fe Pac. Corp. Shareholder Litig., 669 A.2d 59, 67–68 (Del. 1995) (concluding that special import exists in certain circumstances to protect shareholders' franchise).

184 *See Omnicare*, 818 A.2d at 936, 944–45 (stating that "[t]he deal protection devices adopted by the NCS board were designed to coerce the consummation of the Genesis merger and preclude the consideration of any superior transaction" and explaining competence of *Outcalt* and *Shaw*).

185 *Id.* at 935.

186 695 A.2d 43 (Del. 1997).

187 *Id.* at 50.

188 *Id.* (describing proper way to analyze cases in which directors induce shareholders to tender shares for improper motives).

189 *See id.* (finding $550 million termination fee to be "reasonable forecast of damages").

190 *See generally* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 936 (Del. 2003) (failing to give weight to the reasonableness of decision to enter agreement); *cf. Brazen*, 695 A.2d at 49 (applying reasonableness test).

suitors; and highly conditional, speculative alternatives.[191] Therefore, it is exceedingly speculative to hold, as did the Delaware Supreme Court, that the majority shareholders in *Omnicare* voted in favor of the transaction with Genesis for any reason other than the merits of the transaction.

Following *Brazen*, the Delaware Chancery Court in *Carmody v. Toll Brothers, Inc.* [192] held a "dead-hand" provision enacted within a Rights plan, which had the effect of disenfranchising the company's stockholders, to be sufficient to state a claim on the pleadings for coercion and preclusion.[193] Perceiving itself as a potential takeover candidate given recent market activity, Toll Brothers adopted a standard Rights Plan containing both a flip-over and flip-in provision.[194] Unique to this Rights Plan was a "dead-hand" provision that placed into current and continuing directors, or those other persons expressly designated by such current and continuing directors, the sole discretion to redeem the Rights.[195] The effect of this provision was to prevent any and all directors not specifically endorsed by Toll Brother's current or continuing directors from eliminating the Rights and, thus, from taking over Toll Brothers in anything but a financially disastrous way.[196] The court deemed important for analysis of coerciveness within the *Unocal* framework the disenfranchisement of voters caused by the Rights Plan's disempowering effect on insurgent-directors; specifically, the deprivation of full directorial power.[197] The court in *Carmody* also reasoned, consonant with that

191 *See Omnicare*, 818 A.2d at 921–27 (discussing NCS's financial deteriation).

192 723 A.2d 1180 (Del. Ch. 1998).

193 *See id.* at 1195 (holding that provision disenfranchises shareholders by forcing them to vote for incumbent directors if shareholders want to be represented by board entitled to exercise its full statutory prerogatives).

194 *See id.* at 1183 (explaining "flip-in" feature of rights plan triggered when acquirer crosses specified ownership threshold regardless of intentions, and "flip-over" feature entitling target company shareholders to purchase shares of acquiring company at reduced price which is activated after "flip-in" triggering event, such as merger or sale of assets).

195 *See id.* at 1184 (explaining "dead hand" provision as preventing any directors of Toll Brothers, except those in office as of date of Rights Plan's adoption from redeeming Rights until they expire ten years after such date).

196 *See id.* (noting poison pill in effect makes take-over "prohibitively expensive"); *see also* Mark J. Loewenstein, *Delaware as Demon: Twenty-Five Years after Professor Cary's Polemic*, 71 U. COLO. L. REV. 497, 515 (2000) (explaining effects of "dead hand" poison pills on potential bidders).

197 *See Carmody*, 723 A.2d at 1195 (holding that disenfranchisement of shareholders caused by their being forced to vote for incumbent directors if shareholders want to be represented by board is sufficiently coercive).

previously held in *Time*,[198] that the Rights Plan worked to preclude shareholders from reaping benefits possible from future takeovers of Toll Brothers and, therefore, was preclusive.[199]

Decided just five years before and cited in *Omnicare*, *Carmody* appears to exhibit a one-hundred-and-eighty degree view from that later expressed in *Omnicare*.[200] The Court in *Omnicare* radically shifted the focus from preserving independence of the shareholder franchise, as expressed in *Carmody*, to a prohibition on acquiring shareholder votes on an accelerated basis regardless of intrusion into the shareholder franchise.[201] As the NCS board actions did not prevent Omnicare from acquiring the combined NCS/Genesis entity (an option Omnicare admitted in the Court of Chancery it contemplated attempting via proxy contest)[202] and did not skew the shareholders options prior to voting, the NCS board actions neither precluded shareholders from reaping future benefits possible through merger or acquisition nor coerced them into acting in contradiction to their intentions.[203]

In conclusion, the tests of time seem to indicate that as long as a board of directors' actions do not destroy the independence of the shareholder franchise or prevent shareholders from fighting for control of the board, and do stem from a desire to enhance the shareholders interest, the Delaware courts will uphold such

198 Paramount Communications, Inc. v. Time Inc., 571 A.2d 1140, 1154–55 (Del. 1989) (noting defensive devices adopted by Time did not prevent Paramount from acquiring combined Time/Warner entity in future).

199 *See* Carmody v. Toll Bros., 723 A.2d 1180, 1195 (Del. Ch. 1998) (stating that defensive measures are preclusive if they makes a bidder's ability to wage a successful proxy contest and gain control either mathematically impossible or realistically unattainable as was at issue here).

200 *Id.* at 1195 (focusing on issue of disenfranchisement of shareholders as result of who they are forced to vote for).

201 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 936 (Del. 2003). The court focused on the fact that the defensive measures that protected the merger transaction were unenforceable not only because they were preclusive and coercive but specifically because the merger contract required board to act or not act in such a fashion as to limit the exercise of fiduciary duties, which is invalid. *Id.* The court also stated that the voting agreements and the absence of an effective fiduciary out clause made it mathematically impossible and realistically unattainable for Omnicare transaction or any other proposal to succeed. *Id.*

202 In re NCS Healthcare, Inc., Shareholders Litig., 825 A.2d 240, 263 (Del. Ch. 2002) (noting that testimony admitted that Omnicare made bid on Genesis).

203 *See Omnicare*, 818 A.2d at 925–26 (describing NCS's defensive mechanisms); *see also* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 958 (Del. 1985) (determining that "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").

actions.[204] Thus, it was a vast and unexplainable departure by the Delaware Supreme Court to hold in *Omnicare* contrary to these established norms.[205]

iii. Unitary

Ivanhoe Partners v. Newmont Mining Corp.,[206] the first case to conceptualize perceiving "inextricably related" board action as a "unitary" response for *Unocal* analysis, was decided two years after *Unocal*.[207] In *Ivanhoe*, the Delaware Supreme Court deemed a tripartite defense, including a dividend paid by the target, an acquisition-standstill agreement, and a "street-sweep" target-stock purchase, to constitute 'unitary' board action.[208] Unique to this defense is the fact that all three components were designed by the target board and carried out by a specific stockholder at the express direction of the target board.[209]

This tripartite action, effectively wholly within the dominion of the target board, is distinguishable from that deemed "unitary" in *Omnicare*.[210] Unlike the tripartite defense in *Ivanhoe*, the

204 *See Omnicare*, 818 A.2d at 928 (noting that if board's decision is "attributed to any rational business purpose," then courts will not substitute their judgment); *see also Unocal*, 493 A.2d at 949 ("We will not substitute our views for those of the board if the latter's decision can be 'attributed to any rational business purpose.'").

205 *See Omnicare*, 818 A.2d at 936 (finding that defensive devices of NCS directors were not reasonable because they were "preclusive and coercive" and therefore unenforceable); *see also* Paramount Communications, Inc. v. Time Inc., 571 A.2d 1140, 1152 (Del. 1989) (holding that decision by board to merge that does not involve change in control is entitled to judicial deference pursuant to business judgment rule).

206 535 A.2d 1334 (Del. 1987).

207 *See id.* at 1343 ("Because Newmont's actions here are so inextricably related, the principles of *Unocal* require that they be scrutinized collectively as a unitary response to the perceived threats."); *see also Unocal*, 493 A.2d at 955 (requiring courts to carefully assess defensive measures reasonableness and results achieved).

208 *See Ivanhoe*, 535 A.2d at 1345 ("The comprehensive defensive scheme consisting of the dividend, standstill agreement, and street sweep accomplished the two essential objectives of thwarting the inadequate coercive Ivanhoe offer, and of insuring the continued interest of the public shareholders in the independent control and prosperity of Newmont."); *see also* Scott P. Towers, Comment, Ivanhoe Partners v. Newmont Mining Corp.—*the* Unocal *Standard: More Bark Than Bite?*, 15 DEL. J. CORP. L. 483, 486-87 (1990) (arguing that "the business judgment rule protected the board's tripartite defensive measure").

209 *See Ivanhoe*, 535 A.2d at 1341 (suggesting that "target directors must satisfy these prerequisites by showing good faith and reasonable investigation before enjoying presumptions afforded by the business judgment rule"); *see also* Towers, *supra* note 208, at 486 (discussing that "*Ivanhoe* involved a challenge to a three-pronged defensive strategy implemented by a target board of directors in response to a takeover attempt").

210 *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 932 (Del. 2003) (specifying that when defensive measures employed are inextricably related, they must be

amalgam of board and stockholder action considered a "unitary" response in *Omnicare* did not include shareholder action designed and directed by the target board such that its outcome was determined through board persuasion.[211] In *Omnicare*, the target board decision to consummate a merger required the majority vote of approval of all outstanding voting shares.[212] The majority shareholders' prefatory granting of voting agreements to meet this requirement, contrary to the target board devised and implemented street-sweep stock purchase in *Ivanhoe*, consisted merely of an acceleration of the inevitable stockholder vote.[213] Furthermore, given the dismal situation, any collateral attack of the majority vote on grounds of coercion is fatally weakened by the Chancery Court's finding that the shareholders who executed the voting agreements were fully informed stockholders aware of the company's and its constituents' future prospects absent the successful vote.[214]

Unitary board action was next discussed by the Delaware Supreme Court in *Unitrin, Inc. v. American General Corp.*,[215] where the Court further elaborated that all inextricably related defensive actions taken by a board must be "scrutinized collectively as a unitary response to [a] perceived threat."[216] The target board in *Unitrin* instituted two defensive mechanisms:

scrutinized collectively to perceived threats); *see also Ivanhoe*, 535 A.2d at 1343 (instituting tripartite defense of dividends, acquisition-standstill agreement and "street-sweep").

211 *Compare Omnicare*, 818 A.2d at 944–45 (Veasey, J. dissenting) (highlighting qualifications and degree of independence the NCS majority shareholders possessed when granting voting agreements to Genesis), *with Ivanhoe*, 535 A.2d at 1340 (commenting on interrelationship between and mutual additional benefit from Newmont board and Gold Fields with regard to "street sweep").

212 *See Omnicare*, 818 A.2d at 934 (explaining that voting agreements committed board to irrevocably vote their majority power in favor of merger); *see also* Knight, *supra* note 24, at 30 ("The court held that when a force-the-vote provision is coupled with a voting agreement signed by owners of a majority of voting power, there must be an effective fiduciary out clause so that the board can discharge its fiduciary duties.").

213 *Compare Omnicare*, 818 A.2d at 932 ("A board's decision to protect its decision to enter a merger agreement with defensive devices against uninvited competing transactions that may emerge is analogous to a board's decision to protect against dangers to corporate policy and effectiveness when it adopts defensive measures in a hostile takeover contest."), *with* Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1340 (Del. 1987) (explaining that "street-sweep" transactions would effectively defeat Ivanhoe's bid).

214 *See Omnicare*, 818 A.2d at 944 (Veasey, dissenting) (noting that NCS controlling stockholders Outcalt and Shaw were fully informed stockholders who made informed choice to commit their voting power to merger).

215 651 A.2d 1361 (Del. 1995).

216 *Id.* at 1387.

one, a Repurchase program designed to increase the board's existing twenty-three percent ownership block;[217] and two, a Poison Pill.[218] In its direction to the lower court on remand, the Court deemed both actions to constitute a single unitary response with regard to *Unocal*.[219] The important detail to focus on in *Unitrin* is that, as in *Ivanhoe*, the Court referred only to actions specifically taken at the direction of the board to forestall hostile intervention. The court neither showed intention nor desire to include as within the concept, such as it proceeded to do in *Omnicare*, a combination of defensive board action and unpersuaded, independent shareholder approval.[220]

B. Fiduciary out

The initial problem with regard to an across the board requirement for inclusion of a fiduciary out in defensive mechanisms is the shifting fiduciary duty owed by the board of directors.[221] As noted earlier, prior to the invocation of *Revlon's* requirements, the fiduciary duty associated with *Unocal* governs and boards of directors owe a duty to protect the corporate

217 *See id.* at 1370–71. The Unitrin board instituted a Repurchase Program as a defense to American General's bid, having the effect of repurchasing 10 million of Unitrin's outstanding shares. *Id.* at 1370. The important factor here is that Unitrin had in place a provision requiring a supermajority vote mergers. *Id.* Unitrin's press release stated "Unitrin's stock is undervalued in the market and that the expanded program will tend to increase the value of the shares that remain outstanding;" however, a more pessimistic view of this action clearly shows the board was intending to solidify its ability to block a merger. *Id.* In addition, the press release stated that Unitrin's board controlled roughly 23% of Unitrin's outstanding voting shares and the repurchase plan would effectively increase this percentage. *Id.*

218 *See id.* at 1370 (mentioning that Poison Pill was implemented but not going into any detail with regard to Poison Pill).

219 *See id.* at 1387 (highlighting that principles of *Unocal* require analyzing target board's actions together as unitary response to perceived threat).

220 *Compare* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 935–36 (Del. 2003) (highlighting that deal protective measures adopted by board had preclusive and coercive effect on stockholder vote), *with Unitrin*, 651 A.2d at 1387 (stating that Court of Chancery's analysis of defensive target board actions should focus collectively on all of board's defensive actions).

221 *See* Bryan Ford, *In Whose Interest: An Examination of the Duties of Directors and Officers in Control Contests*, 26 ARIZ. ST. L.J. 91, 132 (1994) (noting shift in fiduciary duty that occurs once Revlon is invoked); Brian K. Kidd, Note, *The Need for Stricter Scrutiny: Application of the* Revlon *Standard to the Use of Standstill Agreements*, 24 CARDOZO L. REV. 2517, 2544–45 (2003) (describing shift in fiduciary duty as one of protector to auctioneer); Policastro, *supra* note 168, at 195 ("The role of a corporate board of directors shifts dramatically when the board assumes the Revlon duty . . . There is only one role remaining for the board of directors, and that is to maximize the current value of the company for the benefit of its shareholders.").

enterprise, including the shareholders, from impending harm.[222] Cases have consistently held that, while the board of directors is governed by *Unocal*, the board may take into account long term goals when determining what actions are in the best interests of the "corporate enterprise."[223] That being said, board decisions to avert tender offers yielding high short-term premiums for shareholders have been deemed wholly within the board's business judgment and, accordingly, *Unocal*, even when the alternative board action taken expects solely long term profitability.[224] Vastly different to the fiduciary duty owed by a board of directors under *Unocal*, however, is that owed under *Revlon*.[225] A shift occurs after *Revlon's* invocation, changing the fiduciary duty owed by the board from that of protector of the corporate bastion to that of maximizer of shareholder wealth.[226]

222 *See* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (stating that board has fundamental duty and obligation to protect the corporate enterprise, including stockholders from harm reasonably perceived); *see also* Towers, *supra* note 208, at 484 (discussing basic requirements of *Unocal* duties).

223 *See* Moore Corp. Ltd. v. Wallace Computer Servs, Inc., 907 F.Supp. 1545, 1563 (D. Del. 1995) (holding target board's actions of defending against hostile offer on grounds that targets future profitability prospects were much greater than currently recognized by the market, to be within range of reasonableness); Paramount Communications, Inc. v. Time Inc., 571 A.2d 1140, 1150 (Del. 1990) ("This broad mandate includes a conferred authority to set a corporate course of action, including time frame . . . Thus the question of 'long-term' versus 'short-term' values is largely irrelevant because directors, generally, are obliged to charter a course for a corporation which is in its best interests without regard to a fixed investment horizon."); Henry, *supra* note 98, at 1031–32 (discussing post-*Time* decisions applying Delaware corporate law and stating how they allow directors to set long term profitability goals).

224 *See* E. Ashton Johnston, Note, *Defenders of the Corporate Bastion in the* Revlon *Zone*: Paramount Communications, Inc. v. Time Inc., 40 CATH. U.L. REV. 155, 184–85 (1990) (summarizing Delaware Supreme Court's view on board's freedom to set 'investment horizon' prior to Revlon's invocation); Patricia A. Terian, Comment, *"It's Not Polite to Ask Questions" in the Boardroom:* Van Gorkom's *Due Care Standard Minimized in* Paramount v. QVC, 44 BUFF. L. REV. 887, 918 n. 210 (1996) (inferring long-term goals may be taken into account prior to Revlon's invocation because, at that time, there is no fear shareholders will be 'cashed out' by new controlling shareholder); Jonathan T. Wachtel, Comment, *Breaking Up is Hard to Do: A Look at* Brazen v. Bell Atlantic *and the Controversy over Termination Fees in Mergers and Acquisitions*, 65 BROOK. L. REV. 585, 617–18 (1999) (explaining board may act to protect "synergistic business combinations" yielding long term profitability as long as its protections are not so broad as to violate fiduciary duties owed).

225 *See* Kent Greenfield & John E. Nilsson, *Gradgrind's Education: Using Dickens and Aristotle to Understand (and Replace?) the Business Judgment Rule*, 63 BROOK. L. REV. 799, 820–25 (1997) (emphasizing differences in court deference to business judgment given *Unocal* versus *Revlon* duty application); Lebovitch & Morrison, *supra* note 166, at 38–40 (positing *Revlon* to be an alteration of *Unocal* analysis applicable only specific factual scenarios).

226 *See* MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239, 1250 (Del. Ch. 1989) (noting that board failed in its primary responsibility to its shareholders);

In addition to the change in board focus, there is the limitation on what future profitable ventures the board may take into account when determining how to maximize shareholder wealth.[227] Under *Revlon*, the board is prohibited from taking into account long-term strategies for profitability and must focus solely on maximizing the current, short-term profit that shareholders will succumb to upon consummation of the inevitable fundamental structural change to the corporation.[228] Therefore, absent invocation of *Revlon,* there is no concomitant need for a fiduciary out[229] and its inclusion is counterintuitive.[230]

Two main grounds for this exist. First, fiduciary-outs work to allow a target board to walk away from a given transaction so as to remain in line with a fiduciary duty owed.[231] Provided *Revlon* has not been invoked and the target's actions are within the bounds of *Unocal*, a tender offer yielding a short-term value far in excess of the board's chosen alternative could, within the applicable fiduciary duty's constraints, be ignored. Accordingly, a fiduciary-out would serve no purpose in this situation other

see also Greenfield & Nilsson, *supra* note 225, at 820–21 (discussing changes in duties of boards since *Revlon*).

227 *See* Gregory G. Faragasso, Note, *A Policy Analysis of New York State's Security Takeover Disclosure Act*, 53 BROOK. L. REV. 1117, 1133–34 (1988) (analyzing socio-economic concerns created by director emphasis on short term profitability goals of company); Henry, *supra* note 98, at 1026–27 (discussing conflict between investors seeking short-term profitability and economies seeking long-term growth and development); *see also* Mark David Wallace, Comment, *Life in the Boardroom after FIRREA: A Revisionist Approach to Corporate Governance in Insured Depository Institutions*, 46 U. MIAMI L. REV. 1187, 1301 (1992) (noting stance of Delaware Supreme Court on director long-term corporate profitability strategies during Unocal).

228 *See Revlon*, 501 A.2d at 1250 (noting that board's main concern and responsibility is to its shareholders); *see also* Greenfield & Nilsson, *supra* note 225, at 821 (stating that emphasis is on interests of shareholders according to *Revlon*).

229 *See* Unocal v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985) (noting that corporations are limited in ways to combat perceived threats); Arons, *supra* note 11, at 126 (deeming Delaware Supreme Court's requirement of fiduciary out in circumstances such as *Omnicare* to be redundant); Sean J. Griffith, *The Costs and Benefits of Precommitment: An Appraisal of* Omnicare v. NCS Healthcare, 29 IOWA J. CORP. L. 569, 586–95 (2004) (discussing in depth Delaware Supreme Court's authority in *Omnicare* for a blanket fiduciary out requirement and concluding "the doctrinal authority cited in Omnicare . . . does not compel the majority's inflexible rule against precommitment").

230 *See* Griffith, *supra* note 229, at 570–72 (discussing Delaware Supreme Court's rejection of long established Delaware case law outlining board of director fiduciary duty); *see also* Tarik J. Haskins, Comment, *Look Who's Talking: Exploring No-Talk Provisions in Merger Agreements*, 70 U. CIN. L. REV. 1369, 1382-83 (2002) (defining *Unocal/Unitrin* standard).

231 *See* James A. Fanto, *Braking the Merger Momentum: Reforming Corporate Law Governing Mega-Mergers*, 49 BUFF. L. REV. 249, 321–25 (2001) (discussing "fiduciary outs" and addressing court treatment of provisions); Haskins, *supra* note 230, at 1373 (defining "fiduciary out" in context of merger agreements).

than to increase negotiating costs and decrease the number of successful agreements. Second, requiring a fiduciary out be placed by a target into a merger agreement assumes that target directors are always under a duty to obtain the tender offer yielding the highest short term return to shareholders.[232] A duty of this sort, however, is patently incorrect. Such a duty would prevent boards from taking into account long-term plans for profitability and, thus, destroy the power granted to the board by *Unocal* to exercise its business judgment in protecting the corporate enterprise's long-term life.[233]

As mentioned earlier, the fundamental change in corporate control that threatens a shareholders ability to share in the board of directors' long term profit-seeking plans is what invokes *Revlon's* heightened scrutiny.[234] Plans to change corporate control, to abandon long term profit seeking strategies in response to a bidder's offer to break up the company, and to self-initiate an auction to sell or break up the company, each have in common the ability to divest shareholders from the fruits of future corporate pursuit.[235] This threat, however, fails to exist

232 Boards entering into business transactions that do not change the corporation's control structure are governed by the guidelines set out under *Unocal*. *See* Unocal v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985). Simply put, these guidelines only require the board to act in good faith and in the best interests of the "corporate enterprise." *Id.* While in this situation, the board has the authority to protect the corporate enterprise by reasonable, non-draconian means. *Id.* Requiring a fiduciary out is not consonant with this analysis. *Id.* During *Unocal*'s application, a board is attempting to protect the "corporate enterprise," not just the shareholders, from impending harm. *Id.* Taking away the board's ability in all circumstances to acquire the requisite shareholder vote on an accelerated basis diminishes the board's ability to bargain and, consequently, to protect the corporate enterprise. *See* Griffith, *supra* note 229, at 613–14.

233 *See* Griffith, *supra* note 229, at 595–96 (noting *Omnicare* decision prevents boards from entering into business transactions on terms providing degree of certainty); *see also* Justin W. Oravetz, Comment, *Is a Merger Agreement Ever Certain? The Impact of the* Omnicare *Decision on Deal Protection Devices,* 29 DEL. J. CORP. L. 805, 845 (2004) (explaining that broad interpretation of *Omnicare* decision makes adoption of provisions intended to deliver transactional certainty futile).

234 *See* Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140, 1150 (Del. 1990) (explaining and expanding upon *Revlon's* application); *see also* MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239, 1250-51 (Del. Ch. 1989) (discussing duties owed by and rules governing directors in transactions that involve change in corporation's control structure).

235 *See* QVC Network v. Paramount Communications, 635 A.2d 1245, 1266–67 (Del. Ch. 1993) (describing sale of corporation's control and noting shareholders could be cashed out at any time); *Revlon*, 501 A.2d at 1250–51 (describing situation of 'break up' of corporation and noting subsequent, concomitant change in corporation's control structure); *see also* Cannon & Tangney, *supra* note 179, at 750 (juxtaposing change of control situations with non-change of control situations).

prior to *Revlon's* invocation.[236] Ownership at any time prior to *Revlon's* invocation exists in either a "fluid aggregation of unaffiliated shareholders representing a voting majority – in other words, in the market"[237] or in such other way that power remains consistently distributed among shareholders.[238] Therefore, it is contrary to established principles regarding observance of business judgment to allow shareholders to force the board, inconsistent with the fiduciary duty it owes, to abandon long term goals in favor of maximizing short term shareholder wealth.[239] As such, the mandatory inclusion of fiduciary outs, regardless of the circumstances, is without reason.[240]

CONCLUSION

So long as boards act within the duties owed by them at any given time, courts must respect their business judgment in choosing to take the less traveled of two divergent roads. This comment suggests that the *Omnicare* court, by holding preclusive and coercive the combination of, one, board action forcing a decision on whether to merge be sent to the shareholders and,

236 *See* Paramount Communications, Inc. v. Time, Inc. 571 A.2d 1140, 1151 (Del. 1990) (holding that change of control, not merely adoption of structural defensive devices, is necessary to trigger *Revlon*); Cannon & Tangney, *supra* note 179, at 750 (explaining that when two corporations have such widely held shares that neither is controlled by a particular group "the ability of individual shareholders to affect the decision-making of the merged entity is functionally equivalent to their ability to affect the premerger entities," and no change in control triggers *Revlon*).

237 *Time*, 571 A.2d at 1150 (quoting Chancellor's decision in lower court).

238 *See* Kahan, *supra* note 166, at 595 (explicating conflict of interest non-existent when control does not shift yet very prevalent when control does shift in business transactions); Ronald J. Rinaldi, Note, *Radically Altered States: Entering the "*Revlon *Zone"*, 90 COLUM. L. REV. 760, 779–80 (1990) (providing examples of when control does and does not change significantly enough to invoke *Revlon*).

239 *See* Unitrin, Inc. v. Am. Gen. Corp., 651 A.2d 1361, 1376 (Del. 1995) (reaffirming Delaware Supreme Court's decision in *Time* to allow board of directors to deem corporation's market price to under value the corporation's long-term value); Dennis Honabach & Roger Dennis, *Symposium on the Seventh Circuit as a Commercial Court: The Seventh Circuit and the Market for Corporate Control*, 65 CHI.-KENT. L. REV. 681, 699 n. 108 (1989) (emphasizing Delaware Supreme Court's stance on allowing board's to take into account 'preconceived long range corporate plans' and positing board authority to be largely increased by power to defend against unsolicited offers by claiming its preconceived plan to be more valuable).

240 *See* Robert A. Ragazzo, *Unifying the Law of Hostile Takeovers: Bridging the* Unocal/Revlon *Gap*, 35 ARIZ. L. REV. 989, 990 (1993) (arguing that *Revlon* duty is too strict); Rinaldi, *supra* note 238, at 762–63 (stating that duty imposed on directors by *Revlon* is radical and allows little discretion compared with business judgment rule or Unocal standard).

two, shareholder action granting voting agreements to a merger candidate, erred in its application of *Unocal* and its progeny. In addition, this comment suggests that the *Omnicare* court, by holding fiduciary outs to be an indispensable prerequisite of board action taken in furtherance of business combinations, erred in its analysis of *Unocal* and *Revlon*, as well as both their progeny. The Court's holding in *Omnicare* undermines nearly twenty years of established case law regarding duties owed by boards of directors during business combinations and changes of corporate control.[241] In the words of Justice Moore, "Corporate law is not static, but must grow and respond to evolving concepts and needs."[242] Radical departure from established history, however, presents a formidable problem.

[241] *See* Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 943 (Del. 2003) (Veasey, J., dissenting) (stating that new rule created by majority is "unwise extension of existing precedent"); *Omnicare*, 818 A.2d at 950 (Steele, J., dissenting) (criticizing "inflexible" rule created by majority); *see also* Griffith, *supra* note 229, at 623 (positing that *Omnicare* rule is "bad law, bad economics, and bad policy").

[242] *See* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 957 (Del. 1985) (quoting Justice Moore's reasoning in *Unocal*); Moran v. Household Int'l, Inc., 500 A.2d 1346, 1351 (Del. 1985) (reiterating Justice Moore's statement in *Unocal*).