# **KENTUCKY LAW SURVEY: Corporations**

1985

**Reporter**

74 Ky. L.J. 281 \*

**Length:** 14512 words

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**Text**

**[\*281]** INTRODUCTION

This Survey follows the format of previous Surveys [[1]](#footnote-2)1 by dealing first with developments in corporation law at the federal level. Discussion of these developments is followed by comments on selected state court decisions involving application of state corporate law principles.

Whereas last year's survey period was marked by a lull in corporation law decisions by the Supreme Court of the United States, the current period produced several such decisions. [[2]](#footnote-3)2 Three of these are directly concerned with application of the antifraud provisions of the federal securities laws and have been selected for special comment. [[3]](#footnote-4)3 In the first of these decisions, the Supreme **[\*282]** Court considered the extent to which the *in pari delicto* defense should be available to defendants in insider trading suits brought under the federal securities laws. [[4]](#footnote-5)4 In a second decision,the Supreme Court considered the extent to which misrepresentation or nondisclosure should be regarded as a necessary element in actions brought under section 14(e) of the Securities Exchange Act of 1934, relating to fraudulent conduct in connection with tender offers. [[5]](#footnote-6)5 In a third case, the Supreme Court considered the applicability of the federal securities laws' antifraud provisions to stock sales of a business under the "sale of business doctrine." [[6]](#footnote-7)6 Following the discussion of these three Supreme Court cases, attention is focused on a recent case from the Eleventh Circuit Court of Appeals dealing with recovery of short-swing profits under section 16(b) of the Securities Exchange Act of 1934. [[7]](#footnote-8)7

At the state level, cases decided by the Supreme Court of Delaware continue to remain in the forefront of state corporation law. Two such cases from the Delaware Supreme Court have been selected for special comment. The first relates to an important limitation placed upon the availability of the business judgment rule as a defense to director liability. [[8]](#footnote-9)8 The second relates to approval by the Delaware Supreme Court of management's use of a selective exchange offer as a defense to a hostile takeover bid. [[9]](#footnote-10)9 Discussion of the two Delaware cases is followed by reference to a decision by the Iowa Supreme Court dealing with whether limited liability remains available during a gap in corporate existence resulting from lapse of the corporate charter. [[10]](#footnote-11)10 Finally, reference is made to a recent decision by the Kentucky Court of Appeals in which the court considered whether, under the appraisal provisions of the Kentucky Business Corporation **[\*283]** Act, the appraisal remedy provided dissenting shareholders in merger transactions is the exclusive remedy even where illegality or fraud is alleged. [[11]](#footnote-12)11

I. FEDERAL CORPORATION LAW

A. *Insider Trading*

Cases involving unlawful insider trading activity have long been the source of a substantial volume of litigation under the federal securities laws' antifraud provisions. [[12]](#footnote-13)12 The availability of the *in pari delicto* defense is one issue in these insider trading cases that has remained unresolved in the lower federal courts. [[13]](#footnote-14)13 In *Eichler v. Berner*, [[14]](#footnote-15)14 the United States Supreme Court sought to provide guidelines for the use of this defense in securities cases. [[15]](#footnote-16)15 The Court stated the question before it as: "whether the common-law *in pari delicto* defense bars a private damages action under the federal securities laws against corporate insiders and broker-dealers who fraudulently induce investors to purchase securities by misrepresenting that they are conveying material nonpublic information about the issuer." [[16]](#footnote-17)16

In *Eichler*, a group of investors in T.O.N.M. ***Oil*** & Gas Exploration Corporation (TONM) charged, in an action filed in the United States District Court for the Northern District of California, that they had been induced to buy large quantities of TONM stock in the over-the-counter market as the result of false and misleading inside information about the company conveyed **[\*284]** to them by Leslie Neadeau, president of TONM and Charles Lazzaro, a registered securities broker employed by Bateman Eichler, Hill Richards, Inc. (Eichler). [[17]](#footnote-18)17 Plaintiffs alleged that Lazzaro told them that through his acquaintance with TONM insiders he had learned of a Surinam gold mining venture in which TONM planned to participate that, when announced, would result in a substantial increase in the value of TONM stock. [[18]](#footnote-19)18 When the plaintiffs asked Neadeau about the accuracy of the tips received from Lazzaro, he refused to confirm or deny the information, but did verify that Lazzaro was a "trustworthy" person. [[19]](#footnote-20)19 Although the plaintiffs' TONM stock initially increased in price, the shares ultimately fell below the purchase price when the mining venture failed. [[20]](#footnote-21)20 Claiming that Lazzaro and Neadeau had given the misinformation to manipulate the price of TONM stock for their personal benefit, [[21]](#footnote-22)21 plaintiffs filed suit to recover their losses. Plaintiffs contended that the scheme violated section 10(b) of the Securities Exchange Act of 1934, [[22]](#footnote-23)22 and Securities and Exchange Commission (SEC) Rule lOb-5 promulgated thereunder. [[23]](#footnote-24)23 **[\*285]**

The district court dismissed the complaint as not stating a cause of action, reasoning that the plaintiff investors, as tippees of inside information, were themselves in violation of SEC Rule lOb-5 and, under the *in pari delicto* doctrine, were barred from recovery. [[24]](#footnote-25)24 The Ninth Circuit Court of Appeals reversed the district court's decision. [[25]](#footnote-26)25 In reversing, the court rejected "the notion that a defrauded investor is not entitled to recover damages against a broker or an insider solely because the complaint shows that the plaintiff has violated the federal securities laws." [[26]](#footnote-27)26 The court said that it took this position "[b]ecause we feel that securities professionals and corporate officers who have allegedly engaged in fraud should not be permitted to invoke the *in pari delicto* doctrine to shield themselves from the consequences of their fraudulent misrepresentation." [[27]](#footnote-28)27 The United States Supreme Court granted certiorari. [[28]](#footnote-29)28

In an opinion written by Justice Brennan, the Supreme Court concurred in the court of appeals' judgment that the *in pari delicto* doctrine should not preclude the suit by the plaintiff investors in *Eichler*. [[29]](#footnote-30)29 Referring to its rejection of the *in pari* **[\*286]** *delicto* defense in *Perma Life Mufflers, Inc. v. International Parts Corp*., [[30]](#footnote-31)30 involving application of the defense to a private suit brought under the antitrust laws, the Court held that "the views expressed in *Perma Life* apply with full force to implied causes of action under the federal securities laws." [[31]](#footnote-32)31 This means, said the Court, that

a private action for damages in these circumstances may be barred on the grounds of the plaintiff's own culpability only where (1) as a direct result of his own actions, the plaintiff bears at least substantially equal responsibility for the violations he seeks to redress, and (2) preclusion of suit would not significantly interfere with the effective enforcement of the securities laws and protection of the investing public. [[32]](#footnote-33)32

Relating these tests to tippees who trade on inside information, the Court noted that, as a result of its decision in *Dirks v. SEC*, [[33]](#footnote-34)33 a tippee becomes liable for trading on inside information only if the tippee is aware that the insider passing along the information has breached his fiduciary duties to the corporation's shareholders. [[34]](#footnote-35)34 Accordingly, the Court concluded: "In the context of insider trading, we do not believe that a person whose liability is solely derivative can be said to be as culpable as one whose breach of duty gave rise to that liability in the first place." [[35]](#footnote-36)35 **[\*287]**

Applying its reasoning to the circumstances in *Eichler*, the Court concluded that "[t]here is certainly no basis for concluding at this stage of this litigation that the respondents $ [plaintiff investors were *in pari delicto* with Lazzaro and Neadeau." [[36]](#footnote-37)36 The Court noted that these two had masterminded the "scheme to manipulate the market in TONM securities for their own personal benefit," [[37]](#footnote-38)37 using the plaintiff investors "as unwitting dupes to inflate the price of TONM stock." [[38]](#footnote-39)38 The Court agreed "that the typically voluntary nature of an investor's decision impermissibly to trade on an inside tip renders the investor more blameworthy than someone who is party to a contract solely by virtue of another's overweening bargaining power," [[39]](#footnote-40)39 but it disagreed "that an investor who engages in such trading is necessarily as blameworthy as a corporate insider or broker-dealer who discloses the information for personal gain." [[40]](#footnote-41)40

Furthermore, the public interest would be best served by denying the *in pari delicto* defense as applied to insider trading cases. As the Court pointed out, "the public interest will most frequently be advanced if defrauded tippees are permitted to bring suit and to expose illegal practices by corporate insiders and broker-dealers to full public view for appropriate sanctions." [[41]](#footnote-42)41 Pointing to the limited resources available to the SEC to police fraudulent practices in the securities industry, [[42]](#footnote-43)42 the Court indicated that it felt that "deterrence of insider trading most frequently will be maximized by bringing enforcement pressures to bear on the sources of such information -- corporate insiders and broker-dealers." [[43]](#footnote-44)43 Also, the Court concluded: **[\*288]**

We. . . believe that denying the *in pari delicto* defense in such circumstances will best promote the primary objective of the federal securities laws -- protection of the investing public and the national economy through the promotion of "a high standard of business ethics . ..in every facet of the securities industry." [[44]](#footnote-45)44

B. *Tender Offers*

A troublesome issue regarding the scope and application of section 14(e) of the Securities Exchange Act of 1934 was recently resolved by the United States Supreme Court in *Schreiber v. Burlington Northern, Inc*. [[45]](#footnote-46)45 section 14(e), which was added to the Exchange Act in 1968 by the Williams Act, [[46]](#footnote-47)46 makes unlawful the use of any "fraudulent, deceptive or manipulative acts or practices, in connection with any tender offer." [[47]](#footnote-48)47 The lower federal courts have been divided about whether some form of misrepresentation or nondisclosure is necessary to constitute a violation of section 14(e) or whether manipulative practices affecting market activity in a corporation's stock are sufficient to constitute a violation. [[48]](#footnote-49)48 **[\*289]**

The issue arose in *Schreiber* when Burlington Northern, Inc., through a wholly owned subsidiary, made a tender offer to purchase 25.1 million shares of stock in El Paso Gas Company at twenty-four dollars per share. [[49]](#footnote-50)49 Although the El Paso Gas Company management opposed the attempted takeover, the shareholders fully subscribed the tender offer. [[50]](#footnote-51)50 Burlington Northern, however, did not accept the tendered shares but instead, after negotiating a new and friendly takeover agreement with the management of El Paso Gas Company, rescinded the original tender offer and made a new tender offer to El Paso Gas Company's shareholders for only twenty-one million shares at twenty-four dollars per share. [[51]](#footnote-52)51 The new offer was oversubscribed, thereby subjecting the shareholders who retendered to substantial proration and causing those shareholders who had tendered during the first offer to receive a diminished payment for their shares. [[52]](#footnote-53)52 Barbara Schreiber, one of these shareholders, filed suit on behalf of herself and other shareholders similarly situated, claiming that Burlington Northern's withdrawal of its first tender offer and substitution of its second constituted a "manipulative" practice in violation of section 14(e). [[53]](#footnote-54)53 The district court dismissed the suit, [[54]](#footnote-55)54 reasoning that a key ingredient to stating a claim for manipulation under section 14(e) is deception based upon the lack of full disclosure of information to the corporations's shareholders. [[55]](#footnote-56)55 The Third Circuit Court of Appeals **[\*290]** peals affirmed, [[56]](#footnote-57)56 agreeing that "§ 14(e) was enacted principally as a disclosure statute," [[57]](#footnote-58)57 and that " § 14(e) was not intended to create a federal cause of action for all harms suffered because of the proffering or the withdrawal of tender offers." [[58]](#footnote-59)58 The United States Supreme Court granted certiorari. [[59]](#footnote-60)59

Affirming the court of appeals' judgment, [[60]](#footnote-61)60 the Supreme Court, in an opinion written by Chief Justice Burger, rejected the contention of Schreiber under section 14(e) that acts that artificially affect the price of a target company's stock can be considered "manipulative" even though fully disclosed. [[61]](#footnote-62)61 The Court held that "the term 'manipulative' as used in section 14(e) requires misrepresentation or nondisclosure." [[62]](#footnote-63)62 The petitioner's position regarding the meaning of "manipulative" ignored the normal connotation of "misrepresentation" as used in the antifraud provisions of the securities laws. [[63]](#footnote-64)63 Furthermore, the Court said, "$ [our conclusion that 'manipulative' acts under § 14(e) require misrepresentation or nondisclosure is buttressed by the **[\*291]** purpose and legislative history of the provision." [[64]](#footnote-65)64 In fact, observed the Court:

Nowhere in the legislative history is there the slightest suggestion that § 14(e) serves any purpose other than disclosure, or that the term "manipulative" should be read as an invitation to the courts to oversee the substantive fairness of tender offers; the quality of any offer is a matter for the marketplace. [[65]](#footnote-66)65

Based upon this reasoning the Court failed to find the actions of Burlington Northern manipulative since there were no allegations "that the cancellation of the first tender offer was accompanied by any misrepresentation, nondisclosure or deception." [[66]](#footnote-67)66

Perhaps one of the most important consequences of *Schreiber* will be removing the cloud cast by the Sixth Circuit Court of Appeals upon the defensive use of the "lock-up" option to battle hostile takeover attempts. In *Mobil Corp. v. Marathon* ***Oil*** *Co*., [[67]](#footnote-68)67 the Sixth Circuit treated the "lock-up" option as manipulative under section 14(e) even in the presence of full disclosure. [[68]](#footnote-69)68 Since the Second Circuit flatly rejected this position **[\*292]** in the *Data Probe* [[69]](#footnote-70)69 and *Buffalo Forge* [[70]](#footnote-71)70 cases, this conflict the lower federal courts made effective use of the "lock-up" option somewhat doubtful, especially in the Sixth Circuit. [[71]](#footnote-72)71 At least as far as section 14(e) is concerned, the *Schreiber* case should help to put the "lock-up" option on a firmer foundation as a legitimate defensive tactic in combatting hostile tender offers. [[72]](#footnote-73)72

*C. Sale of Business Doctrine*

During the present survey period, the United States Supreme Court, in *Landreth Timber Co. v. Landreth*, [[73]](#footnote-74)73 settled a sharp **[\*293]** conflict that has existed among the federal circuits regarding the applicability of the sale of business doctrine to the sale of the controlling interest in a corporation through a sale of its stock. [[74]](#footnote-75)74 The doctrine has been described as "a judicial limitation on the application of federal securities laws" by removing stock from the category of a federally defined security. [[75]](#footnote-76)75

In *Landreth*, Samuel Dennis, a Massachusetts tax attorney, purchased all of the common stock in a lumber company owned by Ivan Landreth and his sons. [[76]](#footnote-77)76 Under the terms of the stock purchase agreement, Dennis assigned the stock he purchased to B & D Company, a corporation formed for the sole purpose of acquiring the lumber company stock. B & D Company was then merged with the lumber company to form Landreth Timber Company. [[77]](#footnote-78)77 Dennis and a former client, John Bolton, acquired all of Landreth Timber Company's Class A stock, representing an eighty-five percent interest in the equity of the company. The remaining fifteen percent interest was represented by Class B stock owned by six other investors. Purchase of the lumber business did not turn out as favorably as expected and resulted in the company's selling at a loss its sawmill, which had been heavily damaged by fire before the purchase of the business. [[78]](#footnote-79)78 Landreth Timber Company then filed suit seeking rescission of the stock sale and $ 2,500,000 in damages. The company claimed that the Landreth family, through the sale of their stock in the **[\*294]** lumber company, had violated the Securities Act of 1933 [[79]](#footnote-80)79 by offering and selling stock without registering it as required by the Act; [[80]](#footnote-81)80 and had violated the Securities Exchange Act of 1934 [[81]](#footnote-82)81 by misrepresenting and omitting information concerning the financial condition and future prospects of the lumber company. [[82]](#footnote-83)82

The Landreth family sought summary judgment on the ground that Landreth Timber Company, under the sale of business doctrine, had not purchased a "security" within the meaning of that term as used in the 1933 and 1934 Acts. [[83]](#footnote-84)83 The district court granted summary judgment and dismissed the complaint, joining what it considered to be "the growing majority' of courts that had held that the federal securities laws do not apply to the sale of 100% of the stock of a closely held corporation." **[\*295]** [[84]](#footnote-85)84 The Ninth Circuit Court of Appeals affirmed. [[85]](#footnote-86)85 The United States Supreme Court granted certiorari. [[86]](#footnote-87)86

Reversing the court of appeals' decision, [[87]](#footnote-88)87 the Supreme Court, speaking through Justice Powell, held that when an instrument labeled "stock" contains the usual characteristics associated with stock it should be treated as a "security" within the meaning of the securities acts and the sale of business doctrine should not apply. [[88]](#footnote-89)88 The Court rejected the argument that its decision in *United Housing Foundation, Inc. v. Forman* [[89]](#footnote-90)89 required it to look in every instance to the economic substance of the transaction to determine whether its test in *SEC v. W.J. Howey Co*. [[90]](#footnote-91)90 had been satisfied. [[91]](#footnote-92)91 The *Howey* test for determining whether an instrument could be properly classified as a "security" was stated in *Forman* to require "the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others." [[92]](#footnote-93)92 The *Landreth* Court noted that in both *Howey* and *Forman* the Court applied the economic realities test to instruments that did not bear the usual characteristics associated with stock. [[93]](#footnote-94)93 In *Landreth*, however, the instrument involved traditional stock and thus came plainly within the statutory definition. [[94]](#footnote-95)94 Furthermore, the Court said, "We would note that the *Howey* economic reality test was designed to determine whether a particular instrument is an investment contract,' not **[\*296]** whether it fits within *any* of the examples listed in the statutory definition of security.'" [[95]](#footnote-96)95

In rejecting the sale of business doctrine, the *Landreth* Court stressed the undesirability of adopting a doctrine that necessitated determining whether control of a business has passed to a purchaser. [[96]](#footnote-97)96 If the doctrine were applied to a case such as *Landreth* where one-hundred percent of a company's stock was sold, it "would also have to be applied to cases in which less than 100% of a company's stock was sold," [[97]](#footnote-98)97 which would inevitably "lead to difficult questions of line-drawing." [[98]](#footnote-99)98 This would produce "the prospect that parties to a transaction may never know whether they are covered by the Acts until they engage in extended discovery and litigation over a concept as often elusive as the passage of control." [[99]](#footnote-100)99

It is significant that in a companion case decided by the United States Supreme Court on the same day as *Landreth*, the Court, in *Gould v. Ruefenacht*, [[100]](#footnote-101)100 held that the sale of only fifty percent of a company's stock was subject to the antifraud provisions of the federal securities laws and that the sale of business doctrine did not apply. [[101]](#footnote-102)101 Referring to the fact that in any given case application of the sale of business doctrine depends primarily upon a determination that actual control has passed to the purchaser, the Court observed that what constitutes actual control "may not be determined simply by ascertaining what percentage of the company's stock has been purchased," [[102]](#footnote-103)102 but that **[\*297]** "actual control may also depend on such variables as voting rights, veto rights, or requirements for a super-majority, . . . such as may be required by state law or the company's certificate of incorporation or its by-laws." [[103]](#footnote-104)103 This, thought the Court, could only lead to "arbitrary distinctions between transactions covered by the Acts and those that are not," [[104]](#footnote-105)104 thus again calling for rejection of the sale of business doctrine as applied to instruments labeled "stock" and possessing "all of the characteristics typically associated with stock." [[105]](#footnote-106)105

*D. Short-Swing Profits*

Although the volume of litigation involving insider trading under section 10(b) of the Securities Exchange Act of 1934 and SEC Rule lOb-5 has exceeded that under section 16(b) of the 1934 Act, [[106]](#footnote-107)106 relating to short-swing trading in corporate stocks, nevertheless there continues to be a steady flow of cases under section 16(b). [[107]](#footnote-108)107 One issue that is frequently litigated under section **[\*298]** 16(b) is the proper meaning of "purchase" and "sale" as used in that section. [[108]](#footnote-109)108 This issue arose once again in *Super Stores, Inc. v. Reiner*, [[109]](#footnote-110)109 where a defeated tender offeror sold stock he had acquired in a target company within six months of **[\*299]** purchase for cash to a rival tender offeror who had won the takeover battle. [[110]](#footnote-111)110

Defendant, Reiner, president and a director of plaintiff, Super Stores, Inc., purchased 47,709 shares of plaintiff's common stock on December 16 and 17, 1982, for ten cents per share. [[111]](#footnote-112)111 Reiner later, on May 27, 1983, sold 130,148 shares of common stock at a price of fifty-five cents per share to two individuals, Lyons and Hirsch, who had made a public tender offer for plaintiff's stock. [[112]](#footnote-113)112 This sale included the 47,709 shares of stock acquired earlier by Reiner. [[113]](#footnote-114)113 Reiner realized a profit of forty-five cents per share, amounting to $ 21,469.05, on the sale of the 47,709 shares. [[114]](#footnote-115)114 Plaintiff sought to recover this profit as having been received in violation of section 16(b). [[115]](#footnote-116)115 Defendant contended that he should not be found liable for a violation of secton 16(b) since, having been thwarted in his bidding war for plaintiff corporation's stock, his sale to Lyons and Hirsch was "involuntary" and "was not the type of transaction to which Congress directed § 16(b) in as much as there was no possibility of abuse of inside information." [[116]](#footnote-117)116 Reiner based this defense upon the United States Supreme Court's decision in ***Kern*** *County Land Co. v. Occidental Petroleum Corp*. [[117]](#footnote-118)117 There, the Court applied the "pragmatic" test, based upon Congressional purpose, in exonerating Occidental Petroleum Corporation from **[\*300]** liability for short-swing profits growing out of a merger transaction. [[118]](#footnote-119)118

The Eleventh Circuit Court of Appeals in *Reiner* rejected this defense and adopted as its opinion the recommendations of a magistrate to whom the case had been referred by the district court. [[119]](#footnote-120)119 In recommending that judgment be entered in favor of the plaintiff, the magistrate pointed to the emphasis that the Supreme Court gave in ***Kern*** to looking at Congressional purpose in cases "where characterization of transactions as sales' was not obvious" as compared with "orthodox cash for stock transactions," which were clearly within the purview of the statute. [[120]](#footnote-121)120 Based on this distinction between the "orthodox" or "unorthodox" nature of the transaction giving rise to the short-swing profits, the magistrate concluded: "In this action a corporate **[\*301]** officer and director facing defeat in a tender offer battle voluntarily tendered his stock to his opponents for cash. Nothing in ***Kern*** creates an exception for such a transaction from the short-swing profit prohibitions of § 16(b)." [[121]](#footnote-122)121

Cases such as *Reiner* serve as a warning to defeated tender offerors in takeover battles that they cannot assume that they will be given the benefit of protection from short-swing liability under section 16(b) if they sell their stock in the target company for cash within the prescribed six month period. This applies even though defeated tender offerors may be able to demonstrate that their sale was not based upon inside information. [[122]](#footnote-123)122 As the Supreme Court said in ***Kern***: "The statute requires the inside, short-swing trader to disgorge all profits realized on all purchases' and sales' within the specified time period, without proof of actual abuse of insider information, and without proof of intent to profit on the basis of such information." [[123]](#footnote-124)123

II. STATE CORPORATION LAW

*A. Business Judgment Rule*

Turning to developments in corporation law at the state level, perhaps one of the most significant judicial decisions handed down during the survey period was that by the Delaware Supreme Court in *Smith v. Van Gorkom*, [[124]](#footnote-125)124 involving application of the business judgment rule. [[125]](#footnote-126)125 **[\*302]** Courts have repeatedly stated that they will not interfere with the exercise of business judgment by a board of directors so long as that judgment is honestly exercised. [[126]](#footnote-127)126 By the same token, courts have also stressed the need for directors to exercise due care and diligence in performing their managerial duties [[127]](#footnote-128)127 Even though courts have not always found it easy to draw the line between errors of judgment and negligent conduct, [[128]](#footnote-129)128 they do recognize that exercise of care enters into the formulation of judgment. [[129]](#footnote-130)129 As one judge put it: "When courts say that they **[\*303]** will not interfere in matters of business judgment, it is presupposed that judgment -- reasonable diligence -- has in fact been exercised." [[130]](#footnote-131)130 It was this need for an informed business judgment that the Delaware Supreme Court stressed in *Van Gorkom*. [[131]](#footnote-132)131

In this case, Jerome W. Van Gorkom, Chief Executive Officer and Chairman of the Board of Directors of Trans Union Corporation, a publicly-traded diversified holding company, approached Jay A. Pritzker, a well-known corporate takeover specialist, about his possible interest in a leveraged buy-out of Trans Union at a price of fifty-five dollars per share. [[132]](#footnote-133)132 After further discussions between Van Gorkom and Pritzker, Pritzker made a cash-out merger offer for Trans Union at Van Gorkom's proposed price, which was substantially higher than the then current thirty-eight dollars per share market price. [[133]](#footnote-134)133 At a special meeting of the Trans Union board of directors on September 20, 1980, the directors approved the proposed merger. [[134]](#footnote-135)134 Subsequently, at a meeting of the shareholders of Trans Union held on February 10, 1981, a total of 69.9 percent of the outstanding shares voted in favor of the merger proposal. [[135]](#footnote-136)135 Shareholders representing other shares of Trans Union brought a class action in the Delaware Court of Chancery to rescind the merger or, in the alternative, to obtain damages from members of the Trans Union board of directors and the Pritzker interests. [[136]](#footnote-137)136

The court of chancery held for the defendant directors, [[137]](#footnote-138)137 finding that the directors had acted in an informed manner and that the shareholders had been "fully informed" when voting on the proposed merger. [[138]](#footnote-139)138 The Delaware Supreme Court, in a **[\*304]** 3-2 decision, concluded that both of these rulings by the court of chancery were "clearly erroneous." [[139]](#footnote-140)139 The supreme court held that the trial court "committed reversible error in applying the business judgment rule in favor of the director defendants." [[140]](#footnote-141)140 The supreme court remanded the case to the court of chancery with orders that the court "conduct an evidentiary hearing to determine the fair value of the shares represented by the plaintiff class, based on the intrinsic value of Trans Union on September 20, 1980," [[141]](#footnote-142)141 and to award damages "to the extent that the fair value of Trans Union exceeds $ 55 per share." [[142]](#footnote-143)142

In reversing the court of chancery's finding that the defend directors were entitled to the protection of the business judgment rule because they had acted in an informed manner, the supreme court stressed that "[t]he determination of whether a business judgment is an informed one turns on whether the directors have informed themselves prior to making a business decision, of all material information reasonably available to them.'" [[143]](#footnote-144)143 Pointing out that "[a] director's duty to inform himself in preparation for a decision derives from the fiduciary capacity in which he serves the corporation and its stockholders," [[144]](#footnote-145)144 and that "fulfillment of the fiduciary function requires more than the mere absence of bad faith or fraud," [[145]](#footnote-146)145 the supreme court said that "a director's duty to exercise an informed business judgment is in the nature of a duty of care, as **[\*305]** distinguished from a duty of loyalty." [[146]](#footnote-147)146 Referring to their previous decision in *Aronson v. Lewis*, [[147]](#footnote-148)147 in which the court had adopted a gross negligence standard for director liability under the business judgment rule, [[148]](#footnote-149)148 the court in *Van Gorkom* once again confirmed that "[w]e think the concept of gross negligence is also the proper standard for determining whether a business judgment reached by a board of directors was an informed one." [[149]](#footnote-150)149

Under the guidelines thus established, the *Van Gorkom* court concluded "that the Board of Directors did not reach an informed business judgment on September 20, 1980 in voting to sell' the Company for $ 55 per share pursuant to the Pritzker cash-out merger proposal." [[150]](#footnote-151)150 In support of this conclusion, the court expressed its concern over the undue reliance by the board of directors upon Van Gorkom's oral presentation of the Pritzker proposal at the September 20, 1980 meeting; failure of the members of the board to properly inform themselves through outside advice, or otherwise, as to the intrinsic value of the company; and the action of the board "in approving the sale' of the Company upon two hours' consideration, without prior notice, and without the exigency of a crisis or emergency." [[151]](#footnote-152)151 The importance to the court of the directors' failure to properly inform themselves about the intrinsic worth of the company [[152]](#footnote-153)152 **[\*306]** was also reflected in the court's rejection of the chancellor's finding that the shareholder vote on February 10, 1981, should serve to exonerate the directors from liability. [[153]](#footnote-154)153 Referring to the need for complete candor by corporate directors in seeking approval of director action by the shareholders of the corporation, [[154]](#footnote-155)154 the court pointed out that the board in *Van Gorkom* had failed to disclose to its shareholders that it "had not made any study of the intrinsic or inherent worth of the Company." [[155]](#footnote-156)155

The *Van Gorkom* decision serves to underscore what "may become a significant limitation on the use of the business judgment rule to shield directors from liability," [[156]](#footnote-157)156 namely, the need for directors to exercise the proper standard of care in arriving **[\*307]** at their business decisions. [[157]](#footnote-158)157 In view of the stern manner in which the court applied the duty of care to corporate takeovers in *Van Gorkom*, corporate takeover lawyers have been quoted as saying, with some concern, "that boards of directors may have to act with extra caution if they want continued protection for their decisions under the business judgment rule." [[158]](#footnote-159)158

*B. Takeover Defenses*

In a second significant decision, *Unocal Corp. v. Mesa Petroleum Co*., [[159]](#footnote-160)159 the Delaware Supreme Court considered "the validity of a corporation's self-tender for its own shares which excludes from participation a stockholder making a hostile tender offer for the company's stock." [[160]](#footnote-161)160

Mesa Petroleum Company, as owner of approximately thirteen percent of Unocal's stock, "commenced a two-tier front loaded' cash tender offer for 64 million shares, or approximately 37%, of Unocal's outstanding stock at a price of $ 54 per share." [[161]](#footnote-162)161 The "back-end" of the tender offer involved an exchange of securities purportedly worth fifty-four dollars for the remaining publicly held shares of Unocal. [[162]](#footnote-163)162 After lengthy deliberation **[\*308]** and, on the advice of its investment bankers, the Unocal board of directors, which consisted of eight independent outside directors and six inside directors, only one of whom did not participate, unanimously approved a self-tender for its own stock. [[163]](#footnote-164)163 The terms of the board resolution provided that "if Mesa acquired 64 million shares of Unocal stock through it own offer (the Mesa Purchase Condition), Unocal would buy the remaining 49% outstanding for an exchange of debt securities having an aggregate par value of $ 72 per share." [[164]](#footnote-165)164 Unocal's offer expressly excluded Mesa from the proposal. In a suit brought in the Delaware Court of Chancery, Mesa challenged its exclusion from Unocal's exchange offer. The Vice Chancellor granted Mesa a preliminary injunction. [[165]](#footnote-166)165 While he agreed that the Unocal directors had acted in good faith in opposing Mesa's proposal as inadequate, [[166]](#footnote-167)166 he nevertheless did not believe a selective exchange offer such as that made by the Unocal directors was entitled to protection under the business judgment rule. [[167]](#footnote-168)167 The Delaware Supreme Court accepted an interlocutory appeal certified to them on this issue by the court of chancery.

Reversing the court of chancery's decision, the Delaware Supreme Court held that the board of directors' action in countering Mesa's inadequate and coercive tender offer with its own exchange offer was a reasonable response consistent with the directors' duty to ensure that the minority shareholders of Unocal were treated fairly. [[168]](#footnote-169)168 Responding to Mesa's argument that it is unlawful for a corporation to discriminate against one shareholder in making a self-tender offer, [[169]](#footnote-170)169 the court pointed out that "the principle of selective stock repurchases by a Delware corporation is neither unknown nor unauthorized" [[170]](#footnote-171)170 and that "[t]he restriction placed upon a selective stock repurchase is that the directors may not have acted solely or primarily out **[\*309]** of a desire to perpetuate themselves in office." [[171]](#footnote-172)171 In addition to the requirement that the directors must have acted "for the welfare of the corporation and its stockholders" rather than for their own self-interest, [[172]](#footnote-173)172 the defensive measure must be "reasonable in relation to the threat posed." [[173]](#footnote-174)173 Noting that the board, in adopting the selective exchange offer, had stated that its objective was either to defeat the inadequate Mesa offer or protect the forty-nine percent of its shareholders who would otherwise be forced to accept "junk bonds," the court said that it was "satisfied that the selective exchange offer is reasonably related to the threats posed." [[174]](#footnote-175)174

The court concluded that "there was directorial power to oppose the Mesa tender offer, and to undertake a selective stock **[\*310]** exchange," [[175]](#footnote-176)175 and that "the selective stock repurchase plan chosen by Unocal [was] reasonable in relation to the threat . . . posed." [[176]](#footnote-177)176 Thus, "[u]nder those circumstances the board's action is entitled to be measured by the standards of the business judgment rule." [[177]](#footnote-178)177 So, said the court:

[U]nless it is shown by a preponderance of the evidence that 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. [[178]](#footnote-179)178

While there has been some concern about whether a board of directors should take an active role in determining whether tender offer is in the best interest of the corporation and its shareholders, or rather should assume a passive role, [[179]](#footnote-180)179 the Delaware Supreme Court's decision in Unocal should provide further reassurance to Delaware corporations' management that Delaware will continue to support management's use of appropriate defenses in responding to hostile takeover bids that management reasonably concludes are not in the best interests of the shareholders. [[180]](#footnote-181)180

**[\*311]** *C. Limited Liability*

Turning to the more traditional areas of state corporation law, a recent decision by the Iowa Supreme Court, *Adam v. Mt. Pleasant Bank & Trust Co*., [[181]](#footnote-182)181 illuminates courts' attitude about the continued availability of limited liability when a gap in a corporation's existence occurs through expiration of its period of duration. [[182]](#footnote-183)182

In Adam, plaintiffs, a group of Iowa farmers, delivered grain to an elevator operated by Prairie Grain Company. Later, the company was unable to return the grain due to shortages. [[183]](#footnote-184)183 Plaintiffs then brought a suit naming as defendants, among others, the company's officers and directors, alleging that the individual defendants, as owners, were operating the business as a partnership and were therefore individually liable for the partnership's debts. Blake Phelps, an individual defendant, denied that he was a partner in Prairie Grain Company but rather was only involved with Prairie Company, a legally incorporated business. Plaintiffs countered that Prairie Company had no legal status as a corporation because its corporate existence had expired before the grain transactions with the plaintiffs. [[184]](#footnote-185)184 Prairie **[\*312]** Grain Company's corporate existence had terminated on August 14, 1978, prior to the transactions involved, and the business had not been reincorporated until February 7, 1980, after the grain transactions. [[185]](#footnote-186)185 Although the effect of the gap in Prairie Grain Company's corporate existence had not been briefed when the case went to the Iowa Court of Appeals on an appeal from a partial summary jugment entered by the trial court in favor of Phelps, the court of appeals determined that "the reestablishment of the corporate charter did not retroactively restore the privilege of limited liability during the gap in corporate existence." [[186]](#footnote-187)186

On review of the court of appeals decision, the Iowa Supreme Court held that "[t]he court of appeals was correct in determining that limited liability for Prairie Grain's officers, agents, and shareholders does not exist for matters occurring during suspension of the corporate charter." [[187]](#footnote-188)187 Recognizing that "[i]n the absence of a statutory expression, the authorities are not entirely clear on the existence of limited liability during suspension after a corporate charter has expired and before it has been reinstated," [[188]](#footnote-189)188 the court considered the better-reasoned view to be that expressed by the Fourth Circuit Court of Appeals in *Moore v. Occupational Safety and Health Review Commission*. [[189]](#footnote-190)189 The court in Moore said that, in the absence of statutory direction to the contrary, it preferred to follow those jurisdictions, a majority, that "have construed their statutes of dissolution as imposing personal responsibility on the directors for any liabilities, whether in contract or in tort, incurred in the continued operations of the dissolved corporation's business after forefeiture **[\*313]** of its charter." [[190]](#footnote-191)190 Noting that the Iowa Business Corporation Act was silent on the subject, [[191]](#footnote-192)191 the Iowa Supreme Court in Adam reversed the trial court's judgment treating the revival of the corporate existence of Prairie Company as protecting the individual defendants, such as Phelps, from personal liability. [[192]](#footnote-193)192

Since the Kentucky Business Corporation Act is similar to the Iowa statute in this regard, [[193]](#footnote-194)193 *Adam* serves to underscore the potentially traumatic effect that allowing corporate charters to expire may have upon the limited liability status enjoyed by corporate directors, officers, and shareholders. [[194]](#footnote-195)194

**[\*314]** *D. Appraisal Remedy*

The Kentucky Court of Appeals, in *Yeager v. Paul Semonin Co*., [[195]](#footnote-196)195 considered whether the appraisal remedy provided dissenting shareholders in corporate mergers by the Kentucky Business Corporation Act is the exclusive remedy for such shareholders. [[196]](#footnote-197)196

This exclusivity issue has been particularly troublesome in jurisdictions, such as Kentucky, that follow the older provisions on dissenters' rights in the Model Business Corporation Act since those provisions contain no specific exceptions to the appraisal remedy. [[197]](#footnote-198)197 After requiring that a shareholder dissenting from a merger or sale of assets make written demand on the corporation for payment of the fair value of such shareholder's shares, the Kentucky Business Corporation Act states: "Any sharehold making such demand shall thereafter be entitled only to payment as in this section provided and shall not be entitled to vote to exercise any other rights of a shareholder." [[198]](#footnote-199)198 This language **[\*315]** contains strong implications that the appraisal remedy is intended to be exclusive under any and all circumstances. [[199]](#footnote-200)199

In *Yeager*, plaintiff Yeager sought to enjoin the merger of Paul Semonin Associates, Inc. and Paul Semonin Co. (PSC), in which he owned one hundred of 698,222 outstanding shares of stock. Yeager also wished to recover the amount he originally paid for the stock owned by him plus interest ftom the date of purchase. [[200]](#footnote-201)200 Yeager had paid four dollars per share for the stock but was to receive only $ 1.20 per share under the merger plan. He contended that the merger was unlawful because its primary purpose was to freeze-out the minority shareholders in PSC. The trial court dismissed the complaint, treating Yeager's exclusive remedy as appraisal and payment for his shares under the appraisal provisions of the Kentucky Business Corporation Act. [[201]](#footnote-202)201

On appeal from the order dismissing the complaint, the court of appeals, agreeing that the legislature may have intended the appraisal remedy to be exclusive as the general rule, commented that "it does not appear to us as likely that it intended dissenting stockholders to be so limited where a merger was being effected in contravention of law, or where some species of fraud was being worked upon the dissenters." [[202]](#footnote-203)202 Otherwise, "[t]his would be a signal departure ftom the customary public policy where illegal or fraudulent acts are involved." [[203]](#footnote-204)203 Therefore, the court concluded that "[i]n the absence of a more specific expression of legislative policy to the contrary, we do not construe a legislative purpose to deny judicial relief in a merger situation where illegality or fraud are involved." [[204]](#footnote-205)204

Despite the court's position as to the continued availability of judicial relief where either fraud or illegality is involved, the **[\*316]** court nevertheless affirmed the trial court's judgment dismissing Yeager's complaint because the court did not believe that the record disclosed any issue as to fraud. [[205]](#footnote-206)205 The court said that "[w]hile this kind of merger might strike one as somewhat unfair," it did not constitute ftaudulent or illegal conduct simply because the merger allegedly was being consummated "only for the purpose of freezing out' the minority" since the provisions in the Kentucky Business Corporation Act dealing with corporate mergers "do not limit the purposes for which corporations may be merged." [[206]](#footnote-207)206 Further, the court said, "we have not been referred to any case law from this jurisdiction which proscribes merger for the purpose of freezing out' minority shareholders." [[207]](#footnote-208)207 Addressing the effort made in the Kentucky Business Corporation Act to balance the interests of the majority an minority in merger transactions, the court concluded:

In balancing the competing interests, the Legislature has attempted to come up with a scheme that is reasonable. No doubt, the remedy of appraisal will not always work to the satisfaction of the minority, or even the majority. Still, it presents a generally fair and a reasonable alternative to frequent and protracted litigation, the cost of which minority shareholders would often find prohibitive. [[208]](#footnote-209)208

The Kentucky Court of Appeals' position in *Yeager* that mere charges of unfairness by minority shareholders in cash-out **[\*317]** mergers do not entitle such minority shareholders to seek injunctive or other equitable relief under Kentucky law in lieu of appraisal rights would also seem to carry significant implications for these shareholders under federal law. In *Santa Fe Industries v. Green*, [[209]](#footnote-210)209 the United States Supreme Court stated that to support an action under the antifraud provisions of section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 1Ob-5 there must be allegations of "manipulative or deceptive" conduct as distinguished from allegations of corporate mismanagement "in which the essence of the complaint is that shareholders were treated unfairly by a fiduciary." [[210]](#footnote-211)210 Thus, minority shareholders in cash-out mergers may find that their exclusive remedy under either federal or state law is the state appraisal remedy, absent some allegation of misrepresentation or nondisclosure. [[211]](#footnote-212)211

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Kentucky Law Journal

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1. 1 The survey period runs from July, 1984, to July, 1985. For previous corporation law surveys, see Ham, *Kentucky Law Survey-Corporations*, 73 KY. L.J. 275 (1984-85); Ham, *Kentucky Law Survey-Corporations*, 72 KY. L.J. 279 (1983-84); Ham, *Kentucky Law Survey-Corporations*, 71 KY. L.J. 251 (1982-83); Ham, *Kentucky Law Survey-corporations*, 70 KY. L.J 223 (1981-82); Ham, *Kentucky Law Survey-Corporations*, 69 KY. L.J. 453 (1980-81); Ham, *Kentucky Law Survey-Corporations*, 68 KY. L.J. 495 (1979-80); Ham, *Kentucky Law Survey-Corporations*, 67 KY. L.J. 457 (1978-79); Ham, *Kentucky Law Survey-Corporations*, 66 KY. L.J. 477 (1977-78); Ham, *Kentucky Law Survey-Corporations*, 65 KY. L.J. 255 (1976-77); Ham, *Kentucky Law Survey-Corporations*, 64 KY. L.J. 253 (1975-76); and Ham, *Kentucky Law Survey-Corporations*, 63 KY. L.J. 739 (1974-75). [↑](#footnote-ref-2)
2. 2 See notes 4-6 *infra* and accompanying text. [↑](#footnote-ref-3)
3. 3 United States Supreme Court decisions of interest to corporate and securities lawyers, other than those specifically discussed in this Survey, include: Dean Witter Reynolds, Inc. v. Byrd, 105 S. Ct. 1238 (1985) (Plaintiffs in federal securities fraud suits with pendent arbitrable state claims and nonarbitrable federal claims arising out of the same transaction cannot be denied arbitration of the state claims under the "doctrine of intertwining."); Lowe v. SEC, 105 S. Ct. 2557 (1985) (publishers of nonpersonalized investment advice in securities newsletters not required to register as investment advisers under Investment Advisers Act of 1940); and Sedima, S.P.R.L. v. Imrex Co., 105 S. Ct. 3291 (1985) (prior conviction and racketeering requirements for civil actions under the Racketeering Influenced and Corrupt Organizations Act (RICO) rejected). [↑](#footnote-ref-4)
4. 4 *See* Eichler v. Berner, 105 S. Ct. 2622 (1985). [↑](#footnote-ref-5)
5. 5 *See* Schreiber v. Burlington N., Inc., 105 S. Ct. 2458 (1985). [↑](#footnote-ref-6)
6. 6 *See* Landreth Timber Co. v. Landreth, 105 S. Ct. 2297 (1985). A companion case involving the sale of business doctrine decided by the United States Supreme Court on the same day as *Landreth* will also be mentioned. *See* Gould v. Ruefenacht, 105 S. Ct. 2308 (1985). [↑](#footnote-ref-7)
7. 7 *See* Super Stores, Inc. v. Reiner, 737 F.2d 962 (11th Cir. 1984). [↑](#footnote-ref-8)
8. 8 *See* Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985). [↑](#footnote-ref-9)
9. 9 *See* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985). [↑](#footnote-ref-10)
10. 10 *See* Adam v. Mt. Pleasant Bank & Trust Co., 355 N.W.2d 868 (Iowa 1984). [↑](#footnote-ref-11)
11. 11 *See* Yeager v. Paul Semonin Co., 691 S. W. 2d 227 (KY. Ct. App. 1985). [↑](#footnote-ref-12)
12. 12 For an overview of the law pertaining to insider trading, see Carlton & Fischel, *The Regulation of Insider Trading*, 35 STAN. L. REV. 857 (1983). [↑](#footnote-ref-13)
13. 13 *In pari delicto* means literally "of equal fault." Tarasi v. Pittsburgh Nat'l Bank, 555 F.2d i 152, 1156 (3d Cir.), *cert. denied*, 434 U.S. 965 (1977). For decisions holding that the *in pari delicto* defense is available, see *id*. at 1152; Kuehnert v. Texstar Corp., 412 F.2d 700 (5th Cir. 1969). For a discussion holding that the defense is unavailable, see Berner v. Lazzaro, 730 F.2d 1319 (9th Cir. 1984), *aff'd sub. nom*. Eichler v. Berner, 105 S. Ct. 2622 (1985). [↑](#footnote-ref-14)
14. 14 105 S. Ct. 2622 (1985). [↑](#footnote-ref-15)
15. 15 For an earlier discussion of the *in pari delicto* defense in the context of other securities law issues, see Ruder, *Mutiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy, In Pari Delicto, Indemnification, and Contribution*, 120 U. PA. L. REV. 597, 659 (1972). [↑](#footnote-ref-16)
16. 16 105 S. Ct. at 2624. [↑](#footnote-ref-17)
17. 17 *Id*. [↑](#footnote-ref-18)
18. 18 *Id*. According to the plaintiffs' allegations, Lazzaro had told them that " 'TOMN stock, which was then selling from $ 1.50 to $ 3.00/share, would increase in value from $ 10 to $ 15/share within a short period of time, and… might increase to $ 100/share' within a year." *Id*. [↑](#footnote-ref-19)
19. 19 *Id*. [↑](#footnote-ref-20)
20. 20 Id. at 2624-25. [↑](#footnote-ref-21)
21. 21 Id. at 2625. [↑](#footnote-ref-22)
22. 22 15 U.S.C. § 78j(b) (1982). This section provides:

    It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or the mails, or of any facility of any national securities exchange -- . . . .

    (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors. *Id*. [↑](#footnote-ref-23)
23. 23 17 C.F.R. § 240.10b-5 (1985). The rule provides:

    It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

    (a) To employ any device, scheme, or artifice to defraud,

    (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

    (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

    *Id*. [↑](#footnote-ref-24)
24. 24 105 S. Ct. at 2625. [↑](#footnote-ref-25)
25. 25 Berner v. Lazzaro, 730 F.2d 1319 (9th Cir. 1984). [↑](#footnote-ref-26)
26. 26 Id. at 1324. [↑](#footnote-ref-27)
27. 27 Id. at 1320. Stressing that the federal securities laws aim to protect public investors, the court remarked that "[t]he rule we adopt today will further public policy by providing greater protection for the investing public." Id. at 1323 (citation omitted). The court added that "[t]o allow professionals in the securities industry and corporate officers to hide behind the *in pari delicto* defense gives them a license to defraud the investing public with little fear of prosecution," and that "[a]ny deterrent effect against the use of insider information through imposition of the *in pari delicto* defense is outweighed by the resulting adverse consequence to the market and innocent investors." *Id*. [↑](#footnote-ref-28)
28. 28 Eichler v. Berner, 105 S. Ct. 776 (1985). [↑](#footnote-ref-29)
29. 29 105 S. Ct. at 2626. Chief Justice Burger concurred in the judgment. Justice Marshall did not participate in the decision. Id. at 2633. [↑](#footnote-ref-30)
30. 30 392 U.S. 134 (1968). [↑](#footnote-ref-31)
31. 31 105 S. Ct. at 2629. [↑](#footnote-ref-32)
32. 32 *Id*. [↑](#footnote-ref-33)
33. 33 463 U.S. 646 (1983). [↑](#footnote-ref-34)
34. 34 105 S. Ct. at 2630. In *Dirks* the Court held that "a tippee assumes a fiduciary duty to the shareholders of a corporation not to trade on material nonpublic information only when the insider has breached his fiduciary duty to the shareholders by disclosing the information to the tippee and the tippee knows or should know that there has been a breach." 463 U.S. at 660 (footnote omitted). The *Dirks* case was a sequel to Chiarella v. United States, 445 U.S. 222 (1980), in which the Court held that liability for failure to disclose material nonpublic information was "premised upon a duty to disclose arising from a relationship of trust and confidence between parties to a transaction." Id. at 230. [↑](#footnote-ref-35)
35. 35 105 S. Ct. at 2630 (footnote omitted). Commenting that a tippee's liability to disclose or abstain turns upon whether the insider breached a fiduciary duty to shareholders in tipping material nonpublic information, the *Dirks* Court remarked that in determining whether disclosure is a breach of duty "the test is whether the insider personally will benefit, directly or indirectly, from his disclosure." 463 U.S. at 662. The Court added that "[a]bsent some personal gain, there has been no breach of duty to stockholders" and"absent a breach by the insider, there is no derivative breach." *Id*. (footnote omitted). [↑](#footnote-ref-36)
36. 36 105 S. Ct. at 2631. [↑](#footnote-ref-37)
37. 37 *Id*. [↑](#footnote-ref-38)
38. 38 *Id*. [↑](#footnote-ref-39)
39. 39 Id. at 2630. [↑](#footnote-ref-40)
40. 40 *Id*. [↑](#footnote-ref-41)
41. 41 Id. at 2633. [↑](#footnote-ref-42)
42. 42 Id. at 2631. [↑](#footnote-ref-43)
43. 43 Id. at 2632. The Court added that "[i]n addition, corporate insiders and broker-dealers will in many circumstances be more responsive to the deterrent pressure of potential sanctions; they are more likely than ordinary investors to be advised by counsel and thereby to be informed fully of the 'allowable limits on their conduct.' " *Id*. (citing Kuehnert v. Texstar Corp., 412 F.2d 700, 706 (5th Cir. 1969) (Godbold, J., dissenting). [↑](#footnote-ref-44)
44. 44 105 S. Ct. at 2631 (quoting SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186-87 (1963). The *Eichler* Court did not believe that failure to provide "a vigorous allowance of the *in pari delicto* defense" would encourage tippee insider trading by giving tippees what some lower courts had referred to as " 'in effect, an enforceable warranty that secret information is true.'" 105 S. Ct. at 2632 (quoting 412 F.2d at 705). For one thing, the Supreme Court said "tippees who bring suit in an attempt to cash in on their 'enforceable warranties' expose themselves to the threat of substantial civil and criminal penalties for their own potentially illegal conduct." 105 S. Ct. at 2633 (footnote omitted). [↑](#footnote-ref-45)
45. 45 105 S. Ct. 2458 (1985). [↑](#footnote-ref-46)
46. 46 Williams Act, 15 U.S.C. § 78m(d)-(e), 78n(d)-(f) (1982). [↑](#footnote-ref-47)
47. 47 *Id*. § 78n(e). The full text of the section reads:

    It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which whey were made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation. The Commission shall, for the purposes of this subsection, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative. [↑](#footnote-ref-48)
48. 48 Compare Mobil Corp. v. Marathon ***Oil*** Co., 669 F.2d 366 (1981), *cert. denied*, 455 U.S. 982 (1982), in which the Sixth Circuit Court of Appeals treated manipulation alone as sufficient, *with* Data Probe Acquisition Corp. v. Datatab, Inc., 722 F.2d 1 (2d Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984) and Feldbaum v. Avon Prods., Inc., 741 F.2d 234 (8th Cir. 1984), in which the Second Circuit and the Eighth Circuit stressed the need for some form of misrepresentation or nondisclosure. [↑](#footnote-ref-49)
49. 49 105 S. Ct. at 2460. [↑](#footnote-ref-50)
50. 50 *Id*. [↑](#footnote-ref-51)
51. 51 *Id*. The new takeover agreement, in addition to revising the original tender offer, provided for purchase by Burlington Northern of 4,166,667 shares from El Paso Gas Company at $ 24 per share, procedural protections against a squeeze-out merger of the remaining El Paso Gas Company shareholders, and "golden parachute" contracts on behalf of four of El Paso Gas Company's senior officers. *Id*. [↑](#footnote-ref-52)
52. 52 *Id*. [↑](#footnote-ref-53)
53. 53 Id. at 2460-61. [↑](#footnote-ref-54)
54. 54 Schreiber v. Burlington N., Inc., 568 F. Supp. 197 (D.C. Del. 1983). [↑](#footnote-ref-55)
55. 55 at 202-03. The district court commented:

    If the Court were to hold that defendants' actions in terminating the December tender offer and initiating the January tender offer constituted

    manipulation under Section 14(e), then potential offerors and management of target companies would be subject to liability every time a tender offer is revised or negotiated. Some latitude must be given in the application of the Williams Act for it was designed to enhance market activity through open supply and demand, not artificially restrain it. Id. at 203. [↑](#footnote-ref-56)
56. 56 Schreiber v. Burlington N., Inc., 731 F.2d 163 (3d Cir. 1984). [↑](#footnote-ref-57)
57. 57 Id. at 165-66. [↑](#footnote-ref-58)
58. 58 Id. at 165. The court of appeals commented that "[a]bsent a requirement of deception, the Williams Act would mandate that the federal courts supervise the substantive fairness of practically all tender offers." Id. at 166. The court felt that this result would conflict with the Supreme Court's concern expressed in *Santa Fe Industries* where it said: "Absent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transcriptions in securities, particularly where established state policies of corporate regulation would be overriden." Santa Fe Indus. v. Green, 430 U.S. 462, 479 (1977). [↑](#footnote-ref-59)
59. 59 Schreiber v. Burlington N., Inc., 105 S. Ct. 81 (1984). [↑](#footnote-ref-60)
60. 60 [↑](#footnote-ref-61)
61. 61 [↑](#footnote-ref-62)
62. 62 [↑](#footnote-ref-63)
63. 63 [↑](#footnote-ref-64)
64. 64 105 S. Ct. at 2463. [↑](#footnote-ref-65)
65. 65 Id. at 2464 (footnote omitted). The Court added this further observation:

    Congress' consistent emphasis on disclosure persuades us that it intended takeover contests to be addressed to shareholders. In pursuit of this goal, Congress, consistent with the core mechanism of the Securities Exchange Act, created sweeping disclosure requirements and narrow substantive safeguards. The same Congress that placed such emphasis on shareholder choice would not at the same time have required judges to oversee tender offers for substantive fairness. It is even less likely that a Congress implementing that intention would express it only through the use of a single word placed in the middle of a provision otherwise devoted to disclosure.

    Id. at 2465. [↑](#footnote-ref-66)
66. 66 *Id*. [↑](#footnote-ref-67)
67. 67 669 F.2d 366 (6th Cir. 1981), *cert. denied*, 455 U.S. 982 (1982). Lock-up options have been described as "an arrangement whereby the target company agrees to sell or grants an option to sell assets, treasury stock or authorized-but-unissued stock to a white knight to give the friendly suitor a competitive advantage over a raider in the takeover battle." Lewkow & Forrest, *The Lock-Up Under Exchange Act* SEC. 14(e), THE NAT'L L.J Mar. 26, 1984, at 15 (footnote omitted). [↑](#footnote-ref-68)
68. 68 669 F.2d at 377. *Marathon* involved the attempt by Marathon ***Oil*** Co. to thwart a takeover by Mobil Corp. through granting to U.S. Steel Corp as a competing tender offeror, an option to purchase additional authorized but unissued shares of Marathon common stock and an option to purchase Marathon's interest in ***oil*** and mineral rights in a valuable ***oil*** field referred to as the Yates Field. With reference to the options thus granted by Marathon, the court said:

    In our view, it is difficult to conceive of a more effective and manipulative device than the "lock-up" options employed here, options which not only artificially affect, but for all practical purposes completely block, normal healthy market activity and, in fact, could be construed as expressly designed solely for that purpose.

    Id. at 374. [↑](#footnote-ref-69)
69. 69 Data Probe Acquisition Corp. v. Datatab, Inc., 722 F.2d I (2d Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984). [↑](#footnote-ref-70)
70. 70 Buffalo Forge Co. v. Ogden Corp., 717 F.2d 757 (2d Cir.), *cert. denied*, 464 U.S. 1018 (1983). [↑](#footnote-ref-71)
71. 71 The Sixth Circuit Court of Appeals was careful to state in *Marathon* that, in ruling as it did on the lock-up options in that case, it did "not purport to define a rule of decision for all claims of manipulation under the Williams Act, or indeed for all forms of options which might be claimed to lock-up takeover battles or otherwise discourage competing tender offers." 669 F.2d at 377. Nevertheless, as pointed out by one commentator, the *Marathon* decision painted "a potentially dismal picture for the future of defensive tactics available to targets in their efforts to oppose unwanted bidders." Note, *The Future of Lock-ups After* Mobil Corp. v. Marathon ***Oil***, 27 ST. Louis U.L.J. 261, 280 (1983). [↑](#footnote-ref-72)
72. 72 Putting use of the lock-up option on a solid legal foundation would not necessarily mean that *all* lock-up options would thereby be sanctioned since, as has been suggested, their use in any given instance should depend upon whether management has acted within the boundaries of the business judgment rule in seeking to protect the best interests of the corporation and its shareholders. *See* Note, *supra* note 71, at 281-82. *See also* MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239 (Del. Ch. 1985), *aff'd*, [Current Binder] FED. SEC. L. REP. (CCH) P92,357 (Del. Nov. 1, 1985), in which the Delaware Court of Chancery held that a board of directors' action extending a lock-up option "to foreclose further bidding in an active bidding situation and to promote an agreement which relieves the directors of the potentially damaging consequences of their own defensive policies" violated the directors' fiduciary duty to the corporation's shareholders and was not therefore entitled to the business judgment rule's protection. Id. at 1250. [↑](#footnote-ref-73)
73. 73 105 S. Ct. 2297 (1985). [↑](#footnote-ref-74)
74. 74 For a thorough discussion of the development and application of the sale of business doctrine in the lower federal courts, see Seldin, *When Stock Is Not a Security: The "Sale of Business" Doctrine Under the Federal Securities Laws*, 37 Bus. LAW. 637 (1982). [↑](#footnote-ref-75)
75. 75 Easley, *Recent Developments in the Sale-of-Business Doctrine: Toward a Transactional Context-Based Analysis for Federal Securities Jurisdiction*, 39 Bus. LAW, 929, 930 (1984). If the transaction falls outside the purview of federal securities laws, then there is no subject matter jurisdiction in federal courts. Should applicable state securities laws be patterned after the federal acts, then additional problems are encountered. Id. at 930 n.7. [↑](#footnote-ref-76)
76. 76 105 S. Ct. at 2300-01. [↑](#footnote-ref-77)
77. 77 Id. at 2301. [↑](#footnote-ref-78)
78. 78 *Id*. After the fire, potential purchasers of the lumber business were advised of the damage to the sawmill but were told that "the mill would be completely rebuilt and modernized." Id. at 2300. Nevertheless, "[r]ebuilding costs exceeded earlier estimates, and new components turned out to be incompatible with existing equipment," resulting in the mill's failing to live up to the purchasers' expectations. Id. at 2301. [↑](#footnote-ref-79)
79. 79 Section 2(1) of the Securities Act of 1933 defines the term "security" to include (unless the context otherwise requires):

    [A]ny note, *stock*, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in ***oil***, gas, or other mineral rights . . . or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

    15 U.S.C. § 77(b)(1) (emphasis added). [↑](#footnote-ref-80)
80. 80 105 S. Ct. at 2301. [↑](#footnote-ref-81)
81. 81 Section 3(a)(10) of the Securities Exchange Act of 1934 defines the term "security" to include (unless the context otherwise requires):

    [A]ny note, *stock*, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any ***oil***, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting trust certificate, certificate of deposit, for a security, . . . or in general, any instrument commonly known as a "security;" or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing . . . .

    15 U.S.C.

    78(a)(10) (Supp. 1985) (emphasis added).

    In *Landreth*, the United States Supreme Court commented that "[w]e have repeatedly ruled that the definitions of security' in § 3(a)(10) of the 1934 Act and § 2(1) of the 1933 Act are virtually identical and will be treated as such in our decisions dealing with the scope of the term." 105 S. Ct. at 2302 n.1 (citations omitted). [↑](#footnote-ref-82)
82. 82 105 S. Ct. at 2301. [↑](#footnote-ref-83)
83. 83 *Id*. [↑](#footnote-ref-84)
84. 84 *Id*. (citation omitted). [↑](#footnote-ref-85)
85. 85 Landreth Timber Co. v. Landreth, 731 F.2d 1348 (9th Cir. 1984). [↑](#footnote-ref-86)
86. 86 Landreth Timber Co. v. Landreth, 105 S. Ct. 427 (1984). [↑](#footnote-ref-87)
87. 87 105 S. Ct. at 2308. [↑](#footnote-ref-88)
88. 88 *Id*. at 2302-03. *See also* Gould v. Ruefenacht, 105 S. Ct. 2308, 2311 (1985). Justice Stevens filed a dissent in both *Landreth* and *Gould* in a separate opinion at 105 S. Ct. 2312 (1985). [↑](#footnote-ref-89)
89. 89 421 U.S. 837 (1975). [↑](#footnote-ref-90)
90. 90 328 U.S. 293 (1946). [↑](#footnote-ref-91)
91. 91 105 S. Ct. at 2304. [↑](#footnote-ref-92)
92. 92 421 U.S. at 852. [↑](#footnote-ref-93)
93. 93 105 S. Ct. at 2303-04. *Howey* involved "an offering of units of a citrus grove development coupled with a contract for cultivating and marketing the fruit and remitting the proceeds to the investors." Id. at 2303. *Forman* involved "the sale of shares of stock entitling the purchaser to lease an apartment in a housing cooperative." Id. at 2302. [↑](#footnote-ref-94)
94. 94 Id. at 2304. [↑](#footnote-ref-95)
95. 95 Id. at 2305. The Court added that "applying the *Howey* test to traditional stock and all other types of instruments listed in the statutory definition would make the Acts' enumeration of many types of instruments superfluous." *Id*. (citations omitted). [↑](#footnote-ref-96)
96. 96 Id. at 2306-08. [↑](#footnote-ref-97)
97. 97 Id. at 2307. [↑](#footnote-ref-98)
98. 98 *Id*. [↑](#footnote-ref-99)
99. 99 Id. at 2308 (citation omitted). [↑](#footnote-ref-100)
100. 100 105 S. Ct. 2308 (1985). [↑](#footnote-ref-101)
101. 101 Id. at 2311. [↑](#footnote-ref-102)
102. 102 Id. at 2310-11. The Court said:

     To be sure, in many cases, acquisition of more than 50% of the voting stock of a corporation effects a transfer of operational control. In other cases, however, even the ownership of more than 50% may not result in effective control. In still other cases, de facto operational control may be obtained by the acquisition of less than 50%.

     Id. at 2311. [↑](#footnote-ref-103)
103. 103 *Id*. [↑](#footnote-ref-104)
104. 104 *Id*. [↑](#footnote-ref-105)
105. 105 Id. at 2310 (citing 401 U.S. at 851). Justice Stevens dissented in both the *Landreth* and *Gould* cases. *See* note 88 *supra*. Justice Stevens said that since "[t]he legislative history of the 1933 and 1934 Securities Acts makes clear that Congress was primarily concerned with transactions in securities that are traded in a public market," he believes that "Congress wanted to protect investors who do not have access to inside information and who are not in a position to protect themselves from fraud by obtaining appropriate contractual warranties." 105 S. Ct. at 2312 (Stevens, J., dissenting). Therefore, he "would hold that the antifraud provisions of the federal securities laws are inapplicable unless the transaction involves (i) the sale of a security that is traded in a public market; or (ii) an investor who is not in a position to negotiate appropriate contractual warranties and to insist on access to inside information before consummating the transaction." Id. at 2313. Referring to the fact that both the *Landreth* and *Gould* cases involved closely-held corporations in which the buyers were in a position to protect themselves by appropriate warranties, Justice Stevens said that he did not believe "Congress intended the federal securities laws to govern the private sale of a substantial ownership interest in these operating businesses simply because the transactions were structured as sales of stock instead of assets." *Id*. [↑](#footnote-ref-106)
106. 106 15 U.S.C. § 78p(b) (1981). [↑](#footnote-ref-107)
107. 107 The relevant portion of SS 16(b) provides:

     For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, unless such security was acquired in good faith in connection with a debt previously contracted, shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months.

     15 U.S.C. § 78p(b).

     The reference to "such beneficial owner, director, or officer" in § 16(b) relates to those persons required to file reports of their ownership of corporate "equity securities" with the SEC under § 16(a). These persons include persons owning more than 10% of an equity security required to be registered with the SEC pursuant to § 12 of the Securities Exchange Act of 1934 and persons who are directors or officers of the issuer. Such persons must report all equity securities owned by them in the corporate issuer. *See* 15 U.S.C. § 78p(a). The term "equity security" is broadly defined in § 3(11) of the Securities Exchange Act to include "any stock or similar security; or any security convertible, with or without consideration, into such a security; or carrying any warrant or right to subscribe to or purchase such a security; or any such warrant or right. . . ." . *See* 15 U.S.C. § 78c(11). [↑](#footnote-ref-108)
108. 108 Early cases tended toward a literal or objective reading of the statute. See, e.g., Park & Tilford, Inc. v. Schulte, 160 F.2d 984 (2d Cir.), *cert. denied,* 332 U.S. 761 (1947), where the Second Circuit Court of Appeals treated a conversion of preferred stock into common stock pursuant to a conversion privilege attached to the preferred stock followed by a sale of the common stock within six months as a "purchase and sale" within the meaning of those terms as used in § 16(b). Referring to the definition of "purchase" in § 3(a)(13) of the Securities Exchange Act of 1934 as including "any contract to buy, purchase, or otherwise acquire," the court commented: "Defendants did not own the common stock in question before they exercised their option to convert; they did afterward. Therefore they acquired the stock, within the meaning of the Act." 160 F.2d at 987. Later, the courts began to use a more subjective or pragmatic reading of the statute to determine whether the transaction was one that lent itself to theevils that Congress sought to control through enactment of the statute. See, e.g., Roberts v. Eaton, 212 F.2d 82 (2d Cir.), *cert. denied*, 348 U.S. 827 (1954), in which the Second Circuit, applying the pragmatic approach, held that a reclassification of stock did not result in "purchase" within the meaning of that term as used in § 16(b). In a Iater conversion case arising in the Sixth Circuit, Judge Stewart, after referring to the Second Circuit's decisions as having "marked out an approach to the problem which is pragmatic rather than technical," remarked: "The standard that emerges from these decisions can be simply stated: Every transaction which can reasonably be defined as a purchase will be so defined, if the transaction is of a kind which can possibly lend itself to the speculation encompassed by Section 16(b)." Ferraiolo v. Newman, 259 F.2d 342, 344-45 (6th Cir. 1958), *cert. denied*, 359 U.S. 927 (1959) (footnote omitted). For a review of the history and development of the pragmatic approach, see Lowenfels, *Section 16(b): A New Trend in Regulating Insider Trading*, 54 CORNELL L. REV. 45 (1969). [↑](#footnote-ref-109)
109. 109 737 F.2d 962 (11th Cir. 1984). [↑](#footnote-ref-110)
110. 110 The Fifth Circuit had occasion to consider this issue in a somewhat similar situation in Texas Int'l Airlines v. National Airlines, Inc., 714 F.2d 533 (5th Cir. 1983), *cert. denied*, 465 U.S. 1052 (1984) (cash-for-stock transaction comes within the statutory language). [↑](#footnote-ref-111)
111. 111 737 F.2d at 963. [↑](#footnote-ref-112)
112. 112 Id. at 963, 964. [↑](#footnote-ref-113)
113. 113 Id. at 964. [↑](#footnote-ref-114)
114. 114 *Id*. A bidding war for the plaintiff's stock resulted after the approval on October 28, 1982 of a proposed merger agreement between the plaintiff and SDS of Bog, Inc. Reiner was the president and sole shareholder of SDS of Bog, Inc. Under the merger agreement, which was submitted to the plaintiff's shareholders for approval, the plaintiff's dissenting shareholders were given an option to receive 10 cents per share for their stock. The price offered to dissenting shareholders was raised several times as a result of changes in the offer price by Lyons and Hirsch. *Id*. [↑](#footnote-ref-115)
115. 115 Id. at 963. [↑](#footnote-ref-116)
116. 116 Id. at 964. [↑](#footnote-ref-117)
117. 117 411 U.S. 582 (1973). [↑](#footnote-ref-118)
118. 118 In ***Kern***, Occidental Petroleum Corp., seeking to acquire ***Kern*** County Land Co. (Old ***Kern***), obtained more than 10% of the outstanding shares of Old ***Kern*** through a tender offer to the shareholders of Old ***Kern***. The management of Old ***Kern*** arranged a friendly merger with Tenneco, Inc., whereby a new corporation, ***Kern*** County Land Co. (New ***Kern***) would be formed and the shareholders of Old ***Kern*** would receive shares of Tenneco stock for each share of their Old ***Kern*** stock. The Old ***Kern***-Tenneco merger transaction was closed within six months thereby creating an irrevocable right for Old ***Kern*** shareholders to receive Tenneco stock in exchange for their Old ***Kern*** stock. In the meantime, Occidental Petroleum Corp., finding its takeover attempt blocked, gave Tenneco an option to purchase the Tenneco stock it was to receive in exchange for its Old ***Kern*** stock when the Old ***Kern***-Tenneco merger was closed, the option not to exercisable until a date six months and a day after Occidental's tender offer expired. The Supreme Court held that neither the option nor the exchange constituted a "sale" of Old ***Kern*** shares within the meaning of § 16(b). 411 U.S. at 596, 601. [↑](#footnote-ref-119)
119. 119 737 F.2d at 963. [↑](#footnote-ref-120)
120. 120 Id. at 964. In ***Kern***, the Court, after conceding that "traditional cash-for-stock transactions that result in a purchase and sale or a sale and purchase within the six-month statutory period are clearly within the purview of § 16(b)," went on to observe:

     In deciding whether borderline transactions are within the reach of the statute, the courts have come to inquire whether the transaction may serve as a vehicle for the evil which Congress sought to prevent-the realization of short-swing profits based upon access to inside information-thereby endeavoring to implement congressional objectives without extending the reach of the statute beyond its intended limits.

     411 U.S. at 593-95 (footnote omitted).

     The source for the ***Kern*** Court's distinction seems to be a statement made by Justice Stewart in Reliance Elec. Co. v. Emerson Elec. Co., 404 U.S. 418 (1972), where, in denying recovery of short-swing profits in a cash-for-stock transaction, he remarked that "where alternative constructions of the terms of § 16(b) are possible, those terms are to be given the construction that best serves the congressional purpose of curbing short-swing speculation by corporate insiders." Id. at 424 (footnote omitted). [↑](#footnote-ref-121)
121. 121 737 F.2d at 965 (citation omitted). [↑](#footnote-ref-122)
122. 122 For a general discussion of the role of § 16(b) in the context of failed takeover bids, see Comment, *Short-Swing Profits in Failed Takeover Bids -- The Role of Section 16(b)*, 59 WASH. L. REV. 895 (1984). [↑](#footnote-ref-123)
123. 123 411 U.S. at 595. This objective method of proof was recognized early in Smolowe v. Delendo Corp., 136 F.2d 231 (2d Cir.), *cert. denied*, 320 U.S. 751 (1943), where the court said:

     A subjective standard of proof, requiring a showing of an actual unfair use of inside information, would render senseless the provisions of the legislation limiting the liability period to six months, making an intention to profit during that period immaterial, and exempting transactions wherein there is a bona fide acquisition of stock in connection with a previously contracted debt.

     136 F.2d at 236. [↑](#footnote-ref-124)
124. 124 488 A.2d 858 (Del. 1985). [↑](#footnote-ref-125)
125. 125 As stated by the Supreme Court of Delaware in *Van Gorkom*: "The business judgment rule exists to protect and promote the full and free exercise of the managerial power granted to Delaware directors." Id. at 872 (citation omitted). [↑](#footnote-ref-126)
126. 126 See, e.g., Hathaway v. Huntley, 188 N.E. 616 (Mass. 1933), in which the court remarked: "Directors of a business corporation in the absence of positive statutory enactment are not responsible for errors of judgment or want of prudence in conducting the business of a corporation provided they act honestly." Id. at 618 (citations omitt *See generally* 3A W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 1039 (rev. perm. ed. 1975). [↑](#footnote-ref-127)
127. 127 See, e.g., Kavanaugh v. Gould, 119 N.E. 237 (N.Y. 1918), where, referring to directors of financial institutions, the court remarked:

     They should know of and give direction to the general affairs of the institution and its business policy, and have a general knowledge of the manner in which the business is conducted, the character of the investments, and the employment of the resources. No custom or practice can make a directorship a mere position of honor void of responsibility, or cause a name to become a substitute for care and attention.

     Id. at 238. [↑](#footnote-ref-128)
128. 128 See, e.g., Litwin v. Allen, 25 N.Y.S.2d 667 (N.Y. Sup. Ct. 1940), where the court, in holding directors of a bank liable for losses sustained by the bank resulting from the purchase by the bank of railroad debentures at par with an option given to the seller to repurchase the debentures for the same price within a period of six months, remarked:

     In the last analysis, whether or not a director has discharged his duty, whether or not he has been negligent, depends upon the facts and circumstances of a particular case, the kind of corporation involved, its size and financial resources, the magnitude of the transaction, and the immediacy of the problem presented.

     Id. at 678, [↑](#footnote-ref-129)
129. 129 See, e.g., Selheimer v. Manganese Corp. of America, 224 A.2d 634 (Pa. 1966), where the court, in finding directors liable for using funds obtained from a sale of stock to promote an unprofitable manganese plant in Paterson, New Jersey, instead of a new plant in Colwyn, Pennsylvania, remarked:

     Defendants' actions in respect to the Colwyn plant were not the result of errors in judgment or a calculated business risk nor can such actions be classified as mere negligence. With the knowledge which defendants had of the unsuitability of the Paterson plant for profitable production, the pouring of Manganese's funds into this plant defies explanation; in fact, the defendants have failed to give any satisfactory explanation or advance any justification for such expenditures.

     Id. at 646. [↑](#footnote-ref-130)
130. 130 Casey v. Woodruff, 49 N.Y.S.2d 625, 643 (N.Y. Sup. Ct. 1944). [↑](#footnote-ref-131)
131. 131 488 A.2d at 872. [↑](#footnote-ref-132)
132. 132 Id. at 864-66. Van Gorkom's seeking a sale of Trans Union had originated from senior management's concern about the company's inability to generate sufficient taxable income to offset increasingly large investment tax credits. *d*. at 864, [↑](#footnote-ref-133)
133. 133 Id. at 867. [↑](#footnote-ref-134)
134. 134 Id. at 869. [↑](#footnote-ref-135)
135. 135 Id. at 870. [↑](#footnote-ref-136)
136. 136 Id. at 863-64. The Pritzker interests included New T. Co., a wholly owned subsidiary of Marmon Group, Inc., into which Trans Union was to be merged, and Jay A. Pritzker and Robert A. Pritzker, who owned Marmon Group, Inc. *Id*. The Pritzkers were later dismissed, with prejudice, as defendants by stipulation of the parties. Id. at 864 n.2. [↑](#footnote-ref-137)
137. 137 Id. at 864. [↑](#footnote-ref-138)
138. 138 *Id*. [↑](#footnote-ref-139)
139. 139 *Id*. Justice Horsey wrote the majority opinion. Separate dissenting opinions were filed by Justices McNeilly and Christie. Id. at 893, 898. [↑](#footnote-ref-140)
140. 140 Id. at 893. Summarizing the results of its lengthy opinion, the court said:

     We hold: (1) that the Board's decision, reached September 20, 1980, to approve the proposed cash-out merger was not the product of an informed business judgment; (2) that the Board's subsequent efforts to amend the Merger Agreement and take other curative action were ineffectual, both legally and factually; and (3) that the Board did not deal with complete candor with the stockholders by failing to disclose all material facts, which they knew or should have known, before securing the stockholder's approval of the merger.

     Id. at 864. [↑](#footnote-ref-141)
141. 141 Id. at 893. [↑](#footnote-ref-142)
142. 142 *Id*. [↑](#footnote-ref-143)
143. 143 Id. at 872 (footnote omitted) (quoting Aronson v. Lewis, 473 A.2d 805, 81 (Del. 1984)). [↑](#footnote-ref-144)
144. 144 488 A.2d at 872 (citations omitted). [↑](#footnote-ref-145)
145. 145 *Id*. [↑](#footnote-ref-146)
146. 146 Id. at 872-73. [↑](#footnote-ref-147)
147. 147 473 A.2d 805 (Del. 1984). [↑](#footnote-ref-148)
148. 148 Id. at 812. In Aronson, which dealt with the application of the business judgment rule to shareholder derivative suits, the Supreme Court of Delaware, referring to the applicable standard of care expected of directors in Delaware, commented: "While the Delaware cases use a variety of terms to describe the applicable standard of care, our analysis satisfies us that under the business judgment rule director liability is predicated upon concepts of gross negligence." *Id*. (footnote and citation omitted). [↑](#footnote-ref-149)
149. 149 488 A.2d at 873 (footnote omitted). [↑](#footnote-ref-150)
150. 150 Id. at 874. [↑](#footnote-ref-151)
151. 151 *Id*. [↑](#footnote-ref-152)
152. 152 Id. at 878 (footnote omitted). In reply to an argument by the defendant directors that "the magnitude of the premium or spread between the $ 55 Pritzker offering price and Trans Union's current market price of $ 38 per share" indicated that the Board's decision was an informed one, the court said: "A substantial premium may provide one reason to recommend a merger, but in the absence of other sound valuation information, the fact of a premium alone does not provide an adequate basis upon which to assess the fairness of an offering price." Id. at 875. Further, the court the adequacy of a premium is indeterminate unless it is assessed in terms of other competent and sound valuation information that reflects the value of the particular business." Id. at 876. Criticizing the board of directors for failing to request a valuation study either from inside management or from Salomon Brothers, Trans Union's investment banker, the court did hasten to add:

     We do not imply that an outside valuation study is essentiai to support an informed business judgment; nor do we state that fairness opinions by independent investment bankers are required as a matter of law. Often insiders familiar with the business of a going concern are in a better position than are outsiders to gather relevant information; and under appropriate circumstances, such directors may be fully protected in relying in good faith upon the valuation reports of their management.

     Id. at 876 (citations omitted). [↑](#footnote-ref-153)
153. 153 Id. at 890. [↑](#footnote-ref-154)
154. 154 *Id*. [↑](#footnote-ref-155)
155. 155 Id. at 891. Justice McNeilly, in his dissenting opinion, chastising the majority of the court for taking what he considered to be a narrow and limited view of the record in the case, disagreed with the majority that the board had acted "in a grossly negligent manner in informing themselves of the relevant and available facts before passing on the merger." Id. at 897. Pointing to the background and expertise of both the "inside" and "outside" Trans Union directors, Justice McNeilly said that he disagreed with the majority's view that the Trans Union directors had been guilty fast shuffle" by Van Gorkom and Pritzker but rather believed that the directors "were more than well qualified to make on the spot informed business judgments concerning the affairs of Trans Union including a 100% sale of the corporation." Id. at 894, 895. Since he believed that "[t]he Chancellor's opinion was the product of well reasoned conclusions, based upon a sound deductive process, clearly supported by the evidence and entitled to deference in this appeal," Justice McNeilly felt compelled to dissent from the decision reached by the majority. Id. at 894. Justice Christie, in a brief separate dissenting opinion, likewise said that he would have affirmed the court of chancery's judgment since he believed "that the record taken as a whole supports a conclusion that the actions of the defendants are protected by the business judgment rule." Id. at 898 (citations omitted). [↑](#footnote-ref-156)
156. 156 SEC. REG. & L. REP. (BNA) 221 (Feb. 1, 1985). [↑](#footnote-ref-157)
157. 157 The standard of care expected of directors in the discharge of their managerial duties varies somewhat from jurisdiction to jurisdiction. With the Delaware "gross negligence" standard, compare the standard of care prescribed in the New York Business Corporation Law, which is "that degree of care which an ordinarily prudent person in a like position would use under similar circumstances." N.Y. BUS. CORP. LAW § 717 (McKinney Cum. Supp. 1984-85). For a general discussion of the duties of due care imposed upon directors and officers, see H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS § 234 (3d ed. 1983). [↑](#footnote-ref-158)
158. 158 Middleton, Lawyers *See Warning in Court's View of Business Judgmenl Standard*, THE NAT'L L.J Feb. 18, 1985, at 8. For an interesting review of the implications of the *Van Gorkom* decision, see Manning, *Reflections and Practical Tips on Life in the Boardroom After* Van Gorkom, 41 Bus. LAW. 1 (1985). [↑](#footnote-ref-159)
159. 159 493 A.2d 946 (Del. 1985). [↑](#footnote-ref-160)
160. 160 Id. at 949. [↑](#footnote-ref-161)
161. 161 *Id*. The legal and economic ramifications of the two-tier tender offer have been widely discussed. *See, e.g*., Dennis, *Two-Tiered Tender Offers and Greenmail: Is New Legislation Needed*?, 19 GA. L. REV. 281 (1985); Finklestein, *Antitakeover Protection Against Two-Tier and Partial Tender Offers: The Validity of Fair Price, Mandatory Bid, and Flip-Over Provisions Under Delaware Law*, 11 SEC. REG. L.J. 291 (1983-84). [↑](#footnote-ref-162)
162. 162 493 A.2d at 949. Mesa Petroleum Co. explained in a supplemental proxy statement sent to the shareholders of Unocal Corp. that the securities being offered in the second step of the merger, referred to as "junk bonds" by Unocal, "would be highly subordinated, and that Unocal's capitalization would differ significantly from its present structure." Id. at 949-50. [↑](#footnote-ref-163)
163. 163 Id. at 951. [↑](#footnote-ref-164)
164. 164 *Id*. [↑](#footnote-ref-165)
165. 165 Id. at 952. [↑](#footnote-ref-166)
166. 166 Id. at 952-53. [↑](#footnote-ref-167)
167. 167 Id. at 953. [↑](#footnote-ref-168)
168. 168 Id. at 956-57. [↑](#footnote-ref-169)
169. 169 Id. at 957. [↑](#footnote-ref-170)
170. 170 *Id*. (citations omitted). [↑](#footnote-ref-171)
171. 171 Id. at 955 (citations omitted). Perhaps the leading Delaware case recognizing a board of directors' rigbt to authorize repurchase of a corporation's own shares from a corporate raider is Cheff v. Mathis, 199 A.2d 548 (Del. 1964), in which the Supreme Court of Delaware adopted the following test:

     [I]f the actions of the board were motivated by a sincere belief that the buying out of the dissident stockholder was necessary to maintain what the board believed to be proper business practices, the board will not be held liable for such decision, even though hindsight indicates the decision was not the wisest course . . . . On the other hand, if the board has acted solely or primarily because of the desire to perpetuate themselves in office, the use of corporate funds for such purposes is improper.

     199 A.2d at 554 (citations omitted).

     The court based this distinction upon a similar standard used in evaluating management's use of corporate funds to support its position in a proxy contest. *See* Hall v. Trans-Lux Daylight Picture Screen Corp., 171 A. 226 (Del. Ch. 1934). In *Hall*, the Delaware Chancellor, after reviewing previous English and American authorities, said:

     I gather the principle from these authorities to be that where reasonable expenditures are in the interest of an intelligent exercise of judgment on the part of the stockholders upon policies to be pursued, the expenditures are proper; but where the expenditures are solely in the personal interest of the directors to maintain themselves in office, expenditures made in their campaign for proxies are not proper.

     171 A. at 228. [↑](#footnote-ref-172)
172. 172 493 A.2d at 955. [↑](#footnote-ref-173)
173. 173 *Id*. The court added that "[t] his entails an analysis by the directors of the nature of the takeover bid and its effect on the corporate enterprise." *Id*. Examples of such concerns, the court said, might include such matters as "inadequacy of the price offered, nature and timing of the offer, questions of illegality, the impact on constituencies' other than shareholders (i.e., creditors, customers, employees, and perhaps even the community generally), the risk of nonconsummation, and the quality of securities being offered in the exchange." *Id*. (citation omitted), [↑](#footnote-ref-174)
174. 174 Id. at 956. [↑](#footnote-ref-175)
175. 175 Id. at 958. Earlier in its opinion the court had remarked that under § 141(a) the Delaware General Corporation Law "[t]he board has a large reservoir of authority upon which to draw" in discharging its managerial responsibilities. Id. at 953. Sectio 141(a) provides, in part: "The business and affairs of every corporation organized und this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation . . ." DEL. CODE ANN. tit. 8, § 141(a) (1983). The Kentucky Business Corporation Act contains a similar provision. *See* Ky. REV. STAT. ANN. § 271A.175 (Bobbs-Merrill 1981) [hereinafter cited as KRS]. [↑](#footnote-ref-176)
176. 176 493 A.2d at 958. The court cautioned, however, that a board's power to protect the corporation and its owners from perceived harm was not absolute and that "[a] corporation does not have unbridled discretion to defeat any perceived threat by any Draconian means available." Id. at 955. [↑](#footnote-ref-177)
177. 177 Id. at 958. [↑](#footnote-ref-178)
178. 178 *Id*. [↑](#footnote-ref-179)
179. 179 *See, e.g*., Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1980-81). [↑](#footnote-ref-180)
180. 180 For a helpful discussion of the Delaware business judgment rule in the context of a takeover attempt involving defensive acquisitions by the target company, see Panter V. Marshall Field & Co., 646 F.2d 271, 293-97 (7th Cir.), *cert. denied*, 454 U.S. 1092 (1981). [↑](#footnote-ref-181)
181. 181 355 N.W.2d 868 (Iowa 1984). [↑](#footnote-ref-182)
182. 182 Of course, this problem has been greatly reduced through permission granted in current corporation statutes to make corporate existence perpetual. *See, e.g*., KRS § 271A.270(1)(b) (1981). Indeed, in Delaware, and under some of the more recent statutory revisions, corporate "istence is made perpetual unless limited by provisions in the articles of incorporation. *See* DEL. CODE ANN. tit. 8, § 102(b)(5); REVISED MODEL BUSINESS CORP. ACT § 3.02 (1984) [hereinafter cited as REVISED MODEL ACT]. [↑](#footnote-ref-183)
183. 183 355 N.W.2d at 870. [↑](#footnote-ref-184)
184. 184 *Id*. The plaintiffs also asserted that "the company was not a legal corporation because of various violations of Iowa corporation law as to the operation of the corporation, such as holding annual meetings." *Id*. There were also allegations that Raymond Keller, another of the individual defendants, "dominated the business, that the board of directors and shareholders never set policy, and that Raymond Keller used Prairie Grain funds for his own purposes." *Id*. The trial court had taken the position that challenges to corporate existence based upon allegations that formalities had not been satisfied could be made only by means of a quo warranto proceeding. *Id*. The Supreme Court of Iowa agreed with the Iowa Court of Appeals that the quo warranto remedy was not the exclusive remedy, or even the appropriate remedy, when the challenge to corporate existence was in the context of private litigation not involving the public interest. Id. at 871. Treating the plaintiff's theory as one based upon "piercing the corporate veil," the Iowa Court of Appeals said, as quoted by the Supreme Court of Iowa:

     Under this theory, plaintiffs do not challenge the fact that the elevator was organized as a legal corporation; instead, they contend that the corporate entity may be disregarded due to particular circumstances in this case. Thus, the quo warranto remedy is neither the appropriate procedural device nor relevant to plaintiffs' theory of piercing the corporate veil.

     Id. at 871-72. [↑](#footnote-ref-185)
185. 185 Id. at 872. [↑](#footnote-ref-186)
186. 186 Id. at 873. [↑](#footnote-ref-187)
187. 187 Id. at 874. [↑](#footnote-ref-188)
188. 188 Id. at 873. [↑](#footnote-ref-189)
189. 189 591 F.2d 991 (4th Cir. 1979). [↑](#footnote-ref-190)
190. 190 Id. at 994 (footnote omitted). In Moore, the corporation involved, Life Science Products Co., had been dissolved automatically as a matter of law under the Virginia corporate dissolution statutes "for failure to file the annual report and to pay certain franchise taxes and penalty required by law." Id. at 992. The Virginia statutory provisions permit application for reinstatement of the corporate existence in such cases and state that upon entry of reinstatement order "the corporate existence shall be deemed to have continued from the date of dissolution." *See* VA. CODE § 13.1-92 (Supp. 1984) (subsequently repealed and replaced by § 13.1-754 (1985)). The Virginia reinstatement statute, however, further provides that sucb reinstatement "shall have no effect on any question of personal liability of the directors, officers or agents in respect of the period between dissolution and reinstatement." *Id*. In the face of such specific language as this the *Moore* court said that it was clear to them that "the Virginia reinstatement statute does not relieve the directors, who have continued the corporate business, of individual liability for actions in the interim period between dissolution and reinstatement." 591 F.2d at 996. As to the liability of directors and officers for continuation of a business after dissolution by operation of law, see generally 16A W. FLETCHER, *supra* note 126, § 8132.1 (Supp. 1985). [↑](#footnote-ref-191)
191. 191 *See* IOWA CODE ANN. § 496A.102 (1962). The relevant portion of this section reads: "If the period of duration of a corporation has expired, it may . . . amend its articles of incorporation at any time within five years after the date of such expiration so as to extend its period of duration." *Id*. [↑](#footnote-ref-192)
192. 192 355 N.W.2d at 874. [↑](#footnote-ref-193)
193. 193 *See* KRS § 271A.515 (1981). This section, which deals generally with survival of remedies after dissolution of a corporation and which provides for a period of two years for bringing actions, provides, in part: "If such corporation was dissolved by the expiration of its period of duration, such corporation may amend its articles of incorporation at any time during such period of two (2) years so as to extend its period of duration." *Id*. It is interesting to note that under the provisions of the Revised Model Business Corporation Act, where dissolution has occurred because the corporation's period of duration has expired, reinstatement of its corporate existence can be achieved within two years after the effective date of dissolution and under such circumstances the reinstatement "relates back to and takes effect as of the effective date" of the dissolution. *See* REVISED MODEL ACT § 14.22 (1984). [↑](#footnote-ref-194)
194. 194 One further possible protection for persons carrying on business in the corporation's name after the term of its existence has expired would be through use of the de facto doctrine. However, there has existed "a conflict of authority as to whether, in the absence of any *bona fide* attempt to extend corporate existence, a corporation can be considered to have a *de facto* existence by continuing to carry on the business in its corporate name after the term of existence specified in its articles has expired." H. BALLANTINE, CORPORATIONS § 34 (rev. ed. 1946). *See also* 13A W. FLETCHER, *Supra* note 126, § 6658 (rev. perm. ed. 1984). [↑](#footnote-ref-195)
195. 195 691 S.W .2d 227 (Ky. Ct. App. 1985) (discretionary review denied by the Kentucky Supreme Court and the opinion ordered published). In another Kentucky case decided during the survey period, the Kentucky Supreme Court held that a minority shareholder could be treated as a third-party beneficiary of an agreement between the majority shareholder and a purchaser of the corporate assets. *See* Simpson v. JOC Coal, Inc., 677 S.W.2d 305 (Ky. 1984). [↑](#footnote-ref-196)
196. 196 691 S.W.2d at 228. [↑](#footnote-ref-197)
197. 197 Statutes in some jurisdictions contain specific language making the right to dissent exclusive, but these statutes usually, as in New York, expressly except conduct that is "unlawful or fraudulent." *See, e.g*., N.Y. Bus. CORP. LAW § 623(k) (McKinney Cum. Supp. 1984-85). This issue was clarified in the Model Act's revised appraisal provisions, which became effective in 1978. An exclusivity provision was added to § of the Model Act making the appraisal remedy exclusive except in cases of "unlawful or fraudulent conduct." ABA-ALI MODEL BUSINESS CORP. ACT § 80(d) (rev. ed. 1979). For a discussion of the 1978 revisions, *see* Conard, *Amendments Of Model Busininess Corporation Act Affecting Dissenters' Rights* (Sections 73, 74, 80 and 81), 33 Bus. LA 2587 (1977-78). These changes have been carried forward and made a part of the Revised Model Business Corporation Act. *See* REVISED MODEL ACT § 13.02(b) (1984). [↑](#footnote-ref-198)
198. 198 KRS § 271A.405(l) (1981). Further confirmation that appraisal is the only remedy contemplated under the statute is found in the following language contained in KRS § 271A.405(1): "Any shareholder failing to make demand . . . shall be bound by the terms of the proposed corporate action." [↑](#footnote-ref-199)
199. 199 Comments to § 81 of the Model Act from which the Kentucky provision was taken tend to confirm this interpretation of the appraisal provisions. These comments state: "A few jurisdictions permit the shareholder to have his stock appraised or to sue to set aside the transaction objected to, but ordinarily he may not do both. Some jurisdictions expressly provide that the appraisal remedy shall be exclusive. The provisions of the first paragraph of section 81 have the same result." 2 MODEL BUSINESS CORP. ACT ANN. § 81, 1 2 (1971). [↑](#footnote-ref-200)
200. 200 691 S.W.2d at 228. [↑](#footnote-ref-201)
201. 201 *Id*. [↑](#footnote-ref-202)
202. 202 *Id*. [↑](#footnote-ref-203)
203. 203 *Id*. (citation omitted). [↑](#footnote-ref-204)
204. 204 *Id*. [↑](#footnote-ref-205)
205. 205 Id. at 229. [↑](#footnote-ref-206)
206. 206 Id. at 228. [↑](#footnote-ref-207)
207. 207 *Id*. [↑](#footnote-ref-208)
208. 208 Id. at 229. The court added: "Consideration of the future prospects of the merged corporation in appraising the value of a dissenter's shares, to the extent that evidence of these prospects, beyond speculation, is available as of the statutory date for valuation, would do much to enhance the fairness of the appraisal." *Id*. (citing Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983)). In *Weinberger*, the Supreme Court of Delaware stressed that appraisal should ordinarily be considered the only remedy available under Delaware law to minority shareholders in a cash-out merger, except where "fraud, misrepresentation, self-dealing, deliberate waste of corporate assets, or gross and palpable overreaching are involved." Id. at 714 (citation omitted). The Delaware Supreme Court ruled that, in the future, appraisal proceedings should be liberalized to "include proof of value by any techniques or methods which are generally considered acceptable in the financial community and otherwise admissible in court." Id. at 713. The court said that "the standard Delaware block' or weighted average method of valuation, formerly employed in appraisal and other stock valuation cases, shall no longer exclusively control such proceedings." Id. at 712-13. [↑](#footnote-ref-209)
209. 209 430 U.S. 462 (1977). [↑](#footnote-ref-210)
210. 210 Id. at 477. [↑](#footnote-ref-211)
211. 211 In response to an argument by a group of minority shareholders in a subsidiary corporation that the parent corporation's failure to give the minority shareholders advance notice of a short-form merger was a material nondisclosure even though such prior notice was not required by the applicable Delaware short-form merger statute, the United States Supreme Court in *Santa Fe Indus*. replied:

     But respondents [the minority shareholders] do not indicate how they might have acted differently had they had prior notice of the merger. Indeed, they accept the conclusion of both courts below that under Delaware law they could not have enjoined the merger because an appraisal proceeding is their sole remedy in the Delaware courts for any alleged unfairness in the terms of the merger. Thus the failure to give advance notice was not a material nondisclosure within the meaning of the statute or the Rule.

     Id. at 474 n.14 (citation omitted). [↑](#footnote-ref-212)