**Agency: Liability in Contract**

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| **Actual Authority**: RTA §2.01, Reasonable person in A’s position would believe, based on P’s manifestations, that A is acting on P’s behalf and subject to P’s control. (Acting w/n scope of authority?)**Express**: P says or in K; **Implied:** P gives A job that normally has such authority, *Mill Street Church*, *Dweck***Termination**: P or A informs the other of termination |
| **Special Relationships** (*Cargill*) **Debtor/Creditor**: “De facto control test” (Did creditor more or less exert control?)* 1. Taking over mgt of debtor’s business & directing what Ks can and can’t be made? Want interest $ or goods
	2. When near insolvency, creditors have a financial stake in debtors, and they become residual claimants

**Buyer/Supplier:** Fixed price makes buyer more likely P, taking risk, if acting primarily for purchaser |

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| **Apparent Authority:** RTA §2.03, reasonable person in 3P’s position would believe, based on P’s manifestations, that A was acting on P’s behalf & subject to P’s control (detrimental reliance required in DE and CA)**Manifestations**: (1) Job title, *Lind*, *370* (2) past dealings (3) standard industry practice, *370* (4) A hiring expert?**Termination**: When no longer reasonable for 3P to think A acts w/ authority |

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| **Contract Liability****Unidentified P**: RTA §6.02, 3P knows A acting for unknown P, then P and A bound (A not bound if 3P and A agree)**Undisclosed P**: RTA §6.03, 3P has no notice A acting for any P, then P and A bound |

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| **Ratification**: RTA §4.01, A does not have authority, P affirms or acts in way only justified by affirmation**Timing:** Relates back, treated as if A had actual authority – but cannot ratify if P did not exist at the time, RTA §4.04 |

**Agency: Liability in Tort (Vicarious Liability)**

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| **Two-step analysis** from *Murphy*1. Is there a **master-servant relationship**? (P/A relationship plus scope of employment, RTA §2.04)Control of operations? (*Humble Oil*, *Hoover*)**Direct Control**: Right to control physical conduct, how work performed, what products placed, etc.**Indirect Control**: Who bears the risk of loss/profits? (P getting share of profits?)Includes franchises as long as P creates manifestation of master-servant relationship and 3P relies, *McDonald’s*2. Is this **tort one for which master liable**?Control might need to be related to the tort, *Murphy* (narrow test)Or alternatively, control over “instrumentality” that caused harm, *McDonald’s*, *Vandermark* (broad test) |

**Agency: Fiduciary Duties of Agents**

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| **Duty of Loyalty**: RTA §8.01, A must act loyally for P’s benefit in all matters connected w/ agency relationship**Accounting for profits:** RTA §8.02, §8.12, A cannot benefit in connection or through position, *Reading* (soldier)**Adverse dealing**: RTA §8.03, A cannot deal w/ P as an adverse party or on behalf of one, *Gen Auto* (referrals), *Rash***Noncompetition**: RTA §8.04, A cannot compete w/ P or take action on behalf of P’s competitors, *Rash* (scaffolding)A can take action to prepare for competition, *Johnson*. Limited to not competing only in subject-matter of agency**Use of property**: RTA §8.05, A cannot use P’s property or confidential information for A or 3P’s purposes, *Reading***Usurp a corporate opportunity**: A cannot take a business opportunity belonging to P, *Gen Auto***Provide information**: RTA §8.11 A must give P all facts A knows that are material or should know P wants, *Rash***Duty of Care**: RTA §8.08, A must act w/ care, competence and diligence normally exercised by A on his own behalf |
| **Remedy:** Restitution of all gains to A plus any damages to P (not concerned w/ over-deterrence) **Consent**: RTA §8.06, no liability if P consents to A’s violation of a duty, assuming A acts in good faith and discloses all material facts, and that the consent actually concerns the transaction (P cannot blanket-waive entire duty of loyalty) |

**Valuation**

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| FV = PV \* (1 + r) ^ n; PV = FV / (1 + r) ^ n1. Calculate expected return (include all possibilities, adjusted by their respective probability)2. Discount expected return to PV, including any risk premium in the interest rate3. Subtract investment cost from PV of expected return, or compare PVs of different investments |

**Corporate Structure**

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| **Charter**: DGCL §102Number of authorized shares must be listed in charter (Directors can unilaterally issue more shares to dilute control)No minimum capitalization or per-share capitalization requirementsCan have blank-check preferred stock where board writes the terms (incl. possible voting power) when issued, *Benihana***By-laws**: DGCL §109Can have any provision not inconsistent w/ charterCharter may allow board to implement by-laws but cannot alienate that ability from SHs**Limited liability**: Ordinarily, SHs not liable for obligations of the corporation, §102(b)(6)**Agency costs of debt**: debt gets fixed proportion of upside and nothing on the downside, creates incentives to take risksCan be a problem w/ equity as well, but proportion of upside not fixed and board owe fiduciary dutiesIn DE, when firm on edge of insolvency, debt has residual and board owes fid. duties to debt, reduces agency costs, *Francis***Fraudulent conveyance** allows creditors to get amount of wrong back, but piercing veil preferred as can get everything back |

**Piercing the Corporate Veil**

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| **Principal-Agent test/Instrumentality**: Use if firm not run for own sake but cannot show lack of formalities, *Zaist*1. **SH exercises control & domination** over the businessCorporation is the mere instrumentality or agent of another corporation or individual owning all or most of its stockFor example, if it enters into transactions w/ its siblings w/o expectation of profit (no profit-seeking firm would do this)Distinguish from benefits that accrue to SH because the firm is maximizing its profits2. SH used that control to commit a **fraud, wrong or injustice**Shuttling finances around to suit own interests, using firm to achieve own endsSheltering from creditors is indicative, but per *Walkovszky* is not sufficientInjustice in *Zaist* is representation that will perform on the contract, but such representations often do not exist in tort3. Fraud, wrong or injustice is the **proximate cause** of the injury (usually easy) |

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| **Alter ego test**: Use when can show lack of formalities (unusual for public firms, more common for closely held), *Sea-Land*1. Show **unity of ownership and interest**Lack of corporate formalities (no/few meetings, no board, no charter, no bylaws, no stock)Commingling of funds and assets (of corp and SHs, or of different corps)Severe undercapitalization (indicative but not sufficient)Treating corporate assets as one’s own2. Refusal of the court to allow piercing must either (a) **sanction fraud** or (b) **promote injustice**Promote injustice (includes these activities, per *Sea-Land*)A party would be unjustly enriched (defendant or own of his corporations)Intentional scheme to squirrel assets into a liability-free corporation while heaping liabilities elsewhereNOT enough that a corporation cannot pay its debtsSanction fraud (harder to show because elements of legal fraud not easy)Tax fraud is not enough as the fraud is not directed at the plaintiff, *Torco Oil*Misrepresentation from assurances that would be able to pay in *Sea-Land*3. Fraud or injustice must be the **proximate cause** of the injuries |

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| **Reverse Piercing**: Once pierce to a SH, seek to then pierce to his corporate assets in other corporations, *Sea-Land*Show the alter-ego test, exceptionally heightened showing of unity of interest and ownership, fraud/injustice still required |

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| **Horizontal Piercing**: Pierce to related corporations w/o first piercing to a SH, two tests**Beneficiary test**: One firm is getting all of the benefits of the activities of the pierced firm (rare)**Standard test, enterprise liability** (mix of instrumentality and alter ego):1. Unity of interest & ownership (must show lack of formalities)Never issue shares; all one office; boards never meet or meet together; all share a bank acct or money transferred freely2. Fraud or injusticePolicy: Courts reluctant to horizontally pierce as corporate creditors are put in a worse position than they anticipated |

**Centralized Management**

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| **Shareholder Powers**DGCL §216: **Elect board** by (default rule) plurality voting at meeting or via proxy (can change default elections rule in bylaws)§141(k): **Remove board** members with cause (high showing), or without cause if board is not classified§109: **Amend the by-laws** w/o input of the board of directors, power cannot be alienated by charter§§242, 251, 271: Approve **amendments to the charter**, **mergers** and **sale of substantially all assets** (cannot propose)§218: Establish **binding agreements** amongst themselves on how they will vote§228: Call vote by **written consent** for any action the SHs could otherwise perform at a meeting (charter can eliminate this)To elect directors, must have unanimous consent of the voting SHsSHs cannot elect officers; propose amendments, mergers or sales; or direct management decisions (§141(a), *Manson*)Can make suggestions to the board, but board can deny suggestions with any firm-regarding reason |

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| **Board Powers**§102(b)(7): Can include provision in charter to create **protection from liability for breach of duty of care**§109: Board can **amend the by-laws** if charter explicitly allows, SHs can always amend the by-laws§141(a): **Manage business affairs** of the firm (broad authority, can only be limited in charter)§141(b): Quorum is majority, can alter in bylaw but must be at least one-third; number of directors can be in bylaws or charter§141(c): Can delegate power any and all powers to a **committee**, except amending the charter, dividends or stock rts§141(e): Protection from liability if **rely on an expert** in good faith w/ reasonable belief in competence |
| **Classified boards**§141(d): Can **classify the board** in the **charter**, an **initial bylaw** or a **bylaw adopted by SH vote** (NOT by board bylaw)§141(k): **Cannot remove directors** in classified board w/o cause (major takeover defense) unless charter says otherwiseCould still amend the bylaws by §228 to declassify the board or pack the board, but…**Effective classified board**: Amend charter to classify; fix number of directors in charter, eliminate §228 in charter |
| **Board membership**§141(k): SHs can remove directors w/ cause, or w/o cause if not classified, at a meeting or via written consent§223: Vacancies can be filled by vote of the board or by SHs §216: Board cannot modify bylaws adopted by SHs that provide for the manner of electing directors |

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| **Cumulative voting**, §214**,** protection for minority SHs, minority SHs can unite votes for a single candidate or a few candidates to ensure some representation on the board, contrast ordinary elections where each elected separately |

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| §211: **Annual meeting** of SHs to elect the board, pass bylaws, approve board proposals, etc.§216: Quorum for meetings 50%, can modify in charter or bylaws (but need to protect the bylaw as well)§211(d): Special meetings may be called by board as well*Airgas*: Classified board must serve for approximately full term, look to history for when meetings are typically called |

# Fiduciary Duties of the Board: General Rules

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| **Fiduciary duties** generally only run to SHs/firm, although can run to creditors in insolvencyWhen do you become a fiduciary? When you **formally assume office** as a director/officer***De facto* fiduciary** if you are discharging duties of the office but for some reason do not have *de jure* title to officeBut that does not include preparations for formally assuming officeTwo types of breach of fiduciary duties suits**Direct suit**: Wronged SH personally—usually voting or underpriced merger**Derivative action**: Wronged the firm, SH suing on behalf of corporation, much more common |
| **Business judgment rule**: In making decisions, fiduciaries presumed to have acted disinterestedly, with procedural due care, and in a good faith, rational belief that actions were in best interests of the firm, *Aronson*. Board shall manage, §141(a) |

**Fiduciary Duties of the Board: Waste and *Ultra Vires***

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| ***Ultra vires***: Corporation cannot take actions outside of its purposeHistorically important as corporations used to have narrowly tailored purposesHowever, today in DE corporations may be incorporated for “any lawful purpose”, §§101(b), 102(a)(3)§124: Cannot assert *ultra vires* as a defense to K, but can assert, in theory, in SH action against board (in practice, dead)**Waste**: Modern incarnation of *ultra vires*, outside of any corporate purpose to spend assets w/o intent to increase profitsCan defend against waste claim by articulating any firm-regarding reason, *Kamin*, *Wrigley*, *Barlow*; reason itself gets BJRBut altruism does not count as a firm-regarding reason, must suggest some way that increases profits, *Ford* Once there is no firm-regarding reason, need unanimous SH consent to overcome wasteNote on *Barlow*, NJ changing corporate law to allow donations to charity changed the rules as they applied to the firm |

**Fiduciary Duties of the Board: Duty of Care**

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| **Duty of care**: Directors must act with due care in making decision on behalf of the firmThe duty of care is *procedural only*, cannot challenge the substantive care taken in a decision (reasonableness), *Brehm*Question is whether directors sufficiently informed themselves before making a substantially committing decisionAfter establish duty of care violation, go on to fairness w/ burden on defendant to prove fairness (see below)§102(b)(7): Charter may waive personal liability for directors, but per *London* does not waive injunctions and rescission§141(e): Safe harbor for reasonable reliance on experts |
| *Van Gorkam*: Only case finding violation of the duty of careNo board oversight of negotiations until after completedNo determination of value of controlOutside expert might have been interestedReport was not directly relevantDid not read merger docs; spent two hours deliberatingCEO assumed conflicted as had an interest in cashing outMarket testing of the pricing ineffectiveEven though SHs voted in favor, were not fully informed | *Disney*: No duty of care violation though superficially similarBoard turns over authority to compensation committeeCEO did all of the negotiation, as in *Van Gorkam*Report relied on did not mention terminationBUT, ct says do not need best practices, only good onesDid have other ways to know about termination costsClaim to have known termination costs; ct believes themAlso, no conflicts of interest like in *Van Gorkam*Standard is **gross negligence**, not best practices |
| Summary: (1) importance of decision, (2) conflicts of interest, (3) experts, (4) amount of information, (5) number of meetingsOnce duty of care proven violated, no need for causation, go straight to fairness, *Cinerama*SH vote on the merger itself does not cleanse, need a separate vote, *Gantler* (might cleanse for duty of loyalty w/ disclosure) |

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| **Duty to monitor**: Subset of duty of care, affirmative duty designed to prevent/discourage wrongdoingNote: **No BJR here** as no affirmative decision for director(s) to defend; nonetheless, analysis very similar*Francis*: Extreme case, no monitoring, **cannot abdicate all directorial duties**—not attending meetings or monitoring financials, and relying on reports from interested sources (her sons, who are robbing the firm blind)Proximate cause: Would not have changed behavior to object, but ct assumes that they would haveAlso, if they did not, ct says would have had duty to resign and let someone better take overNote: **Causation matters** (and will still matter in DE; this is in NJ)**Compliance programs**: Subset of duty to monitor, duty to put into place a rigorous monitoring system*Graham*: Previously did not require monitoring system, DE SC did not think there needed to be an affirmative duty*Caremark*: Rejecting *Graham* in settlement affirmation, determining whether settlement was fairTwo duties: (1) **Create compliance program**; (2) **Oversee it in good faith**Choice of program is a decision: Brings board under the BJR! So no substantive determination of quality of programThus, once a compliance program established, only duty is to oversee in good faithMust have **knowing and sustained neglect** to be liable; systemic failure to exercise oversightAlthough board ignored a lot of red flags, did respond to some and stop worst activity, thus not bad faith hereAlso, **causation required**; failure to monitor or failure to institute compliance program must have caused damages*Stone*: DE S.C. approves of *Caremark*, approves bad faith standard, thus directors personally liable even under §102(b)(7)Finds *Caremark* duty in duty of loyalty, but the duty originates in duty of care; not a negligence standardNo liability again despite outside federal law finding of deficiency bc, while not best practices, had dept., officer, etc.*AIG*: Liability under *Caremark* because directors had clear knowledge of fraud (they did it) and no attempt to monitor*Citi*: *Caremark* does not reach decisions other than oversight of illegality, would invite substantive due care through back doorSarbanes-Oxley §404(a): Federal law requires report on effectiveness of monitoring system but no actual monitoring system |

**Fiduciary Duties of the Board: Duty of Loyalty**

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| **Duty of loyalty**: Directors must not partake in transactions where they have a material financial interest (if do, BJR rebutted)Material financial interest: Would a reasonable, prudent person consider this significant?New York, *Bayer*: CEO hires convinces board to hire his wife to perform music to advertise the firmDirectors acting in good faith and with firm-regarding reason; did not know his wife was to be usedAdditionally, equal money, equal quality, and no sign that she was chosen w/o ordinary deliberation (entire fairness)Delaware, §144: May **ratify** w/ **informed, disinterested directors** or **committee**, §144(a)(1), or **informed SHs**, §144(a)(2)*Fliegler*: **SHs must be disinterested**, interested SHs do not count though statute suggests otherwiseIf **ratification**, in a noncontrolling SH context, **back to BJR** and immune to suit unless some other prong rebuttedIf **no ratification**, look to **entire fairness** w/ burden on defendant director(s) (see below)*Benihana*: Firm issues stock to a director in order to dilute control of founder/felon and new wife, founder and wife sueThere is ratification, claim that did not know interested director’s role in negotiating, ct says it was “obvious”, like *Disney*Additional entrenchment claim, needed money, ordinarily BJR, less bc bad faith reason, but maybe no options for financing and had reason to issue w/ voting power bc anyone buying taking on a lot of risk in the corporation as not doing well*Wheelabrator*: Different analysis if controlling SH transaction, go to fairness, ratification only changes burden on fairnessQuestion of what constitutes control, 22% and 4/11 directors not considered control |
| **Corporate opportunity**: Directors/officers have a duty not to usurp corporate opportunity belonging to firm§122(17): Corporation may renounce a business opportunity or class of opportunities in charter or by action of boardSHs can also cleanse, apparently, although this is not mentioned in §122(17)Interested D/O discloses to board, then disinterested directors may vote to renounce opportunity and allow D/O to take itNOT under §144 cleansing as corporation is explicitly not engaging in any kind of business transaction—taken by D/OOld test for whether a corporate opportunityInterest: Firm has a contractual right to the opportunity and D/O is swooping in and taking it awayExpectancy: Firm does not yet have a contractual right but is in negotiations and D/O starts negotiating separatelyNecessity: Transaction is necessary to firm’s survival/existence, e.g. land under a factory being sold, D/O buysNew test for whether a corporate opportunity, *Guth v. Loft* test (account for D/O duty to bring in new opportunities)(1) Activity to which company has fundamental **knowledge**, practical **experience** and **ability to pursue**(2) Activity is **adaptable to company’s business**(3) Consonant with reasonable **needs and aspirations for expansion**Other factors to consider: How did CO come to D/O? Was corp. information used? How far removed from corp. activity is CO?Can also claim financial inability, but that claim is typically weak*Broz*: CO *at a point in time*; would be CO after other corp. bought but not now as corp. currently divesting coverage*eBay*: Need not be principle business, enough IPOs that IPO is line of business; also, came to eBay officers bc were eBay officers*Beam*: Martha Stewart not in trouble because selling stock not CO and came to Stewart bc had stock, not through position**Damages**: Give up the opportunity (or value of the opportunity if exhausted) minus reasonable investment costs made |
| **Note on controlling SHs**: Not an interested transaction unless get some benefit not given to other SHs, *Sinclair* (dividends)Determined by amount going out of the firm not going towards others (different tax rates in *Sinclair*)But, if it were an interested transaction, straight to fairness as discussed later (below) |

**Fairness Determinations**

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| **Fairness**: **Entire fairness**, or fair dealing and fair price**Fair dealing**: Were the procedures by which the transaction was carried out fair? Was negotiation active and equal?Most important: Outside valuation advice sought, relied on carefully constructed reports?§141(e)Timing of transactionHow transaction initiated, structured, negotiatedAggressive bargaining by fiduciary (Substantial effort to obtain the highest price? *Cinerama*)Disclosure to directors and SHsHow approval of directors and SHs obtainedFiduciary’s knowledge of businessSurmountability of lock-ups by third parties**Fair price**: Was the price fair/equal to the value of the shares?Assets, market value, earnings, future prospects, intangible benefits, but do not get to count synergies from mergersAlso consider the magnitude of premium over market price as indicative of fair price, *Cinerama*Rescissory damages, what you would have *now* if firms not merged; appraisal damages, what you had prior to mergerAppraisal: Refuse the merger, opt out of the merger price and seek court determination of fair value, bound by it |

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**Shareholder Enforcement**

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| **Direct v. derivative suits**: *Tooley* testWhat is the nature of the harm alleged?Who suffered harm? Corporation or SHs as individuals? Can SH show injury to himself w/o showing wrong to corp?Is the claim related to the rt of SH to participate in corporate governance? (*Lazer* test) *Eisenberg*Who benefits from relief sought? Injunctions indicate derivative, damages to SHs indicate direct (*Gordon* test), not *Eisenberg***Standing**: (a) Continuous ownership, (b) fairly represent SHs (not interested/a competitor), (c) SH at the time of the wrong**Bond requirement**: *Cohen*, bonds required in NY/NJ, federal ct says procedural, used under *Erie* for DE corps sued in NY/NJ |
| **Demand requirement**: In a derivative suit, demand that board sue or claim demand excused; §141(a), board shall manageEvidence gathered via §220 information requests, determined by pleadings, *Aronson*If you demand, concede demand required, so cannot claim demand excused if lose on demand refused**Demand excused** when there is **reason to doubt** either: (remember *Rales* applies when majority of directors different)…That a majority of the board was not interested or dominated by an interested party, *Aronson* prong 1Note: majority must be interested in transaction; if they are, cleansing insufficient, but otherwise cleansing blocksDominated: does the interested party have the ability to affect a material financial interest of the directors§141(c), committee can decide on demand, then appoint only disinterested directors, get around *Rales* and *Aronson*…Or that the decision was not a valid exercise of business judgment, *Aronson* prong 2 (only way not interested, Duty of care violation, uncleansed interested transaction, or interested transaction w/ controlling SH*Rales*: When majority of directors different, q is whether maj interested in trans or defendants/dominated by defendants**Demand required**, no demand excuse, board has BJR protection unless SH can allege w/ particularity that board vio’d a dutyCases where demand excused treated under this test if you make a demand, *Grimes* (hint might ignore if new info)Duty of care violation: Failed to investigate reasonably whether suit was in firm’s interest (§102(b)(7) irrelevant)Good faith violation, extremely hard like any waste claim |
| **Special litigation committees**: Even if demand excused, board may appoint SLC to decide if litigation goes ahead, §141(a)*Auerbach*: Lots of deference to SLC in New York, allow to dismissDelaware standard on SLCs, *Zapata*Demand required: SLC determines whether to acknowledge demand, proceed on wrongful refusal, no further action for SLCDemand excused: Look to see whether SLC independent, acted w/ due care and in good faith, **burden on defendants**In addition, ct reserves the rt to exercise own business judgment to allow suit to proceed*Oracle*: Independence inquiry more broad than §144(a)(1), includes personal ties, Stanford professors not disinterested*London*: Family members obviously interested, and obvious debts of gratitude also a problem*Beam*: *Oracle* standard ONLY applies to SLCs, nowhere else |

**Proxy Contests**

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| **Proxy contest**: Battle for control of a firm, attempt to replace the entire board§112: Can pass by-laws creating requirements for SHs to nominate directors§213: **Record date**, 10-60 days before meeting, determines SHs w/ rt to vote by proxy, cannot be used as weapon**Reimbursement of proxy expenses**§113: Can pass by-laws allowing reimbursement of expenses incurred in soliciting proxies for short slates (not full control)*Rosenfeld*: Reimbursement of proxy expenses of both old and new directorsOld dirs have automatic rt to reimbursement for proxy expenses unless “personal” rather than policy dispute (rare) Have been elected before and represent the interests of the firm by defaultNew dirs do not have automatic rt, but policy of reimbursing successful proxy contestants firm-regarding; not wasteStill self-dealing, though, have to get SH approval (but do not need unanimous approval as for waste)Firm can also pay for proxy costs directly rather than reimburse, *Levin* |
| **Disclosures of information**§219: SH list must be released at least 10 days before meeting (useless for proxy solicitation, though)§220: Requests for information about the firm, including SH lists, at times other than before the meetingMust be “for a proper purpose”—what does this mean?*Honeywell*: Anti-war protesting is not a proper purpose, must be economic interest related to your position as SH*Crane*: Tender offer for SHs’ stock counts as a proper purpose even though it is not directly related to position as SH*Seinfeld*: To get info related to breach of fid duty, must allege w/ particularity the alleged breach rather than scattershotBut, per *King*, can get information disclosure even after file suit as long as not dismissed w/ prejudice |
| **Federal Regulations**: Allow/encourage SH proposalsSec. Exchange Act, **Rule 14a-8** requires firms to issue SH proposals in the proxy materials firm sends out, at firm’s expenseHas a 1% or $2k stakeholder requirement, proposal must be <500 words, only one proposal per SH per meetingAlso, corp. can exclude if it is (a) illegal (b) false/misleading (c) personal grievance (d) relevant to <5% of assets and insignificant to firm (e) about elections (f) inappropriate for SHs/attempt to micromanage the firm*Lovenheim*: Foie gras investigation significant to firm even though <5% of assets (must have economic significance, here that there is a risk of public backlash against the firm for producing foie gras)*AFSCME*: Requirement to reimburse not excluded under elections bc SHs can adopt amendment on this, but is excluded as board power bc this bylaw *requires* reimbursement, 141(a) violation—must give a fiduciary outDE law has effectively overturned *AFSCME* in §113Sec. Exchange Act, **Rule 14a-9** bans misleading statements in a proxy solicitation; 10b-5 applies elsewhere to fraudImplied pvt rt of action under *Borak*, must allege all of the below; for a public action by the SEC, need only the first three**Breach** of cognizable securities law duty, **Materiality**, *TSC* test, alters “total mix” of info, substantial likelihood SH would consider significant (incl. omissions)*Virginia Bankshares*: Statement of board’s subjective reason for decision can be materially misleading**Scienter**, that is, knowledge of misleading statement/omission; mere negligence suffices for 14a-9**Transaction causation**, must be “essential link” in the transaction going throughDo not need this particular SH to have relied on the statement, though that helps, *Mills*But cannot have transaction causation if controlling SH could approve transaction by himself, *Virginia Bankshares***Loss causation**, must cause the loss the SH claims (obvious, not needed to reach summary judgment) |

**Controlling Shareholder Transactions**

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| **Control**: What does it mean for a SH to be a controlling SH?Presumed controlling SH if 50%+1 of voting stock, even when did not nominate majority of directors, *Weinberger*Can be controlling SH w/o majority of stock, however, if exercise effective control over the board, *Perlman*22% and 4/11 directors probably not sufficient to reach control, however, *Wheelabrator* (not even contested by plaintiff)Deference of the board to decisions, lack of resistance to proposals by controlling SH, compensation control, *Kahn*Must be aggressive in defending firm in order to be independent |

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| **Sale of control**: When controlling SH sells control to an outside SH, may sometimes owe other SHs some dutyOnly dealing w/ controlling SH transaction when controlling SH acting in board-controlling capacity, not in SH capacity, *Digex*Equal Opportunity Rule rejected, no minority SH rt to their part of control premium, *Zetlin*Breach duty if sell control to entity that controlling SH knows/should know will loot the firm/violate fiduciary duties, *Perlman* |

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| **Freeze-out mergers**: Merger in which minority SHs denied a stake in subsequent corporation, forced to sellOnce could only seek appraisal, but after *Weinberger*, *Rabkin* and *Andra*, can seek class action suit for rescission or damages**Step One**: Violation of some duty, e.g. self-interest or duty of candor, *Weinberger*, *Andra* (confidential info, self interest)**Step Two**: Improper cleansing, quasi-§144(a)(1) – ind. committee must exercise bargaining power at arm’s length, *Kahn*Controlling SH does not dictate terms of the deal that were then summarily acceptedBoard put in place defenses (poison pill), negotiated, retained ability to reject deal, attempted to seek alternativesAlternatively, if approved by SHs, quasi-§144(a)(2), must be majority of minority, fully informed and disinterestedSuccessful cleansing **does not return to BJR**, shifts burden of fairness to plaintiff only**Step Three**: Entire fairness, fair dealing and fair price, burden on defendant if not cleansed, burden on plaintiff if cleansedFair dealing factors:Effective negotiating considered again, *Kahn*, *Rabkin* (time-sensitive decision)Controlling SH initiated deal? Relevant but not determinative, *Weinberger*Use of target’s secret data for study, *Weinberger* (need not disclose studies if prepared internally w/o target’s data)Lack of reliance on experts by committee or board, *Weinberger*Timing, cannot time merger to avoid obligation to pay a higher price, *Rabkin*Special committee appointed to negotiate? Helps a lot if the committee acts independentlyShort-form merger, if have 90% or more stock, can force merger of sub w/ parent w/o SH or board vote |

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| **Appraisal**: §262(h), Challenge fair price to minority SH of a freeze-out merger, forced to sell for the fair pricePerfecting appraisal rts: Demand rts, reject merger, file action in ct to value sharesRemedy: Value of pre-merger minority position, stuck w/ it, ct decides attorney’s feesDoes not apply to sales of substantially all assets under §271, so corps can get around appraisal if they really want to do so |

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| **Two-step merger**: Controlling SH makes tender-offer to reach short-form merger stageSince a tender offer, acting in SH capacity, ordinarily would not force a fairness determination, but need some protectionFour-part test from *CNX*, if pass all parts, then no fairness determination, fully cleansed, otherwise fairness w/ burden on DMajority of minority participate in tender offer, *Pure Resources*Controlling SH commits to consummating merger after tender offer, *Pure Resources*No retributive threats against other SHs or the board, *Pure Resources*Ind. committee w/ time for advice, authority to pursue alternatives, ability to reject, not acting for controlling SH, *CNX* |

**Takeover Defenses**

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| **Valid takeover defenses**:1. Effective classified board: Board classified in charter, number of directors fixed in charter, §228 eliminated2. No-shop provision: Agreement w/ white knight that will not negotiate w/ others; court skeptical in *QVC*3. Supermajority voting: Require more than a majority to elect directors or pass bylaws, increases purchasing burden4. Issuance of voting stock to an individual under §102(b)(4): As in *Benihana*, not attempted by any of the firms in question5. Poison pill: Limit to how many shares one SH can acquire w/o triggering debt collapse of the firm, can be retracted6. Bonds/scorched earth defense: Excessive debt makes a firm unappealing7. Cancellation/termination fee: Fee in contract w/ white knight, 1-3% allowed, more is usually excessive (*Revlon*)8. Crown jewels defense: Donna Karan defense, provision that crown jewels go to someone else if taken over9. §203: Waivable, but no business combination w/in three year if SH buys 15% of outstanding stock, unless:Reached 15% w/ prior board approval or own >85% of non-insider stock or approved by board & two-thirds of other SHs**Invalid takeover defenses**: Dead-hand poison pill, no-hand poison pill, discriminatory self-tenders, greenmail |

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| **Sell-mode**: When in sell-mode, standard is *Revlon*; otherwise, in takeover defenses standard is *Unocal*Factors to consider that were present in *Revlon*, not in *Unocal*:Is the board alienating the control premium? Will it ever be available again? Distinguishes *QVC* from *Time* (dispersed SHs)Is the board abandoning its long-term strategy and seeking a break-up or cash-out of the firm? |

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| **Defenses outside of sell-mode**: Bc hostile bidder, board inherently conflicted, desire to retain its position at SHs’ expenseTwo-part test to get back to BJR, largely procedural, *Unocal***Threat to corporate policy and effectiveness** (legally cognizable threat)Step One: Did the board **articulate a threat**?1. Risk of nonconsummation or problematic instrument (subordinated debt in *Unocal*)2. Opportunity loss (e.g., deprives SHs of better offers, long-run value or firm culture), *Time*3. Structural coercion as SHs will rush to take first offer to avoid being stuck a minority, *Unocal*, *Unitrin*4. Substantive coercion, price too low but SHs have reason to be misinformed/accept, not if negotiable, *Unitrin*, *Airgas*Step Two: Did the board engage in **good faith and reasonable investigation**? *Unocal*Extra deference on information from outside directors or investment bankersCan reject deal in favor of long-term value if demonstrate long-term valueBoard action **reasonable in relation to threat** posedStep One: Is the board’s action draconian, i.e., **coercive or preclusive**?Coercive if board forces SHs to choose management, creates penalties to SHs who choose otherwisePreclusive if board makes tender offers essentially impossible for any bidder in the future – fiduciary outStep Two: Is board’s action w/in **range of reasonableness**? *Unitrin*Does not have to be the best option, only a good optionCan “just say no” (Nancy Reagan defense), *Time*; can even “just say never” once meet the rest of the test, *Airgas*Allowed to keep poison pill in place even when SHs clearly have time to be informed**Remedy**: Invalidation of the takeover defense, no damages |

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| **Defenses in sell-mode**: SHs going to lose control premium, thus duty to **get highest price possible**, nothing else (*Revlon*)Two-part test to get back to BJR, stricter test than *Unocal*, more substantive inquiryWas decisionmaking process and investigation **adequate**?Investigate all bids made for synergies, get all relevant information reasonably available, *QVC*Diligent in examining details, acting in good faithWas the board’s action **reasonable under the circumstances** w/ goal of getting highest price possible?Defensive mechanism must be designed to bring in the highest price, *QVC*Cannot preclude new bids, no lock-ups or crown jewels defense, *QVC*Must have a fiduciary out, cannot pre-commit to a deal where a better one may come alongBut *can* take actions like poison pills designed to drive up bidding, *Revlon*Preferential treatment of a bidder permitted as long as reasonably necessary to get higher priceCan prefer lower bid *only if* non-cash payment that might be valued differently (e.g., subordinated debt or equity)**Remedy**: Invalidation of defenses, as in *Unocal*; no contractual rts by white knight bc board did not have authority |

**Interference with Shareholder Voting**

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| **Interference w/ SH voting**: Is the board acting in a way designed primarily to interfere w/ SH voting?Board cannot interfere w/ elections to the board; this only applies to elections to the board, not anywhere else*Schnell*: Resist releasing SH list, then move up meeting to block proxy contest by dissidentImproper use of board power bc goal is entrenchmentCannot interfere w/ SH voting, prevent SH from getting adequate information out to other SHs in time to vote*Blasius*: Expand board and appoint new directors to block attempted §228 maneuver to expand and pack the board**Intent to interfere w/ effect of vote** is sufficient, need not interfere w/ the vote itselfNo “**compelling justification**”, high standard, not clear if could ever meet (maybe 35% SH trying to destroy firm?) |

**Securities Fraud & Insider Trading**

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| **Classic Securities Fraud**: Pvt rt of action exists for R. 10b-5 enforcements just like proxy fraud, similar but not the same**Breach** of cognizable securities law duty, **Materiality**, *TSC* test, alters “total mix” of info, substantial likelihood SH would consider significant (incl. omissions)*Virginia Bankshares*: Statement of board’s subjective reason for decision can be materially misleading*Basic*: Major event w/ some chance to move market price, likely material regardless of whether certain*Matrixx*: Materiality includes facts that might influence SHs (incl. by influencing other parties, e.g. FDA and public)**Scienter**, that is, knowledge of misleading statement/omission; recklessness not sufficient as not “fraud” for §10b*Basic*: Reason for misleading statement irrelevant, can be benevolent (desire to help SHs)*Matrixx*: Also unimportant that did not think information important, only important that knew statement misleadingLack of statistical significance not relevant here, though it might be outside of pharmaceutical context**Standing**, purchaser/seller requirement, must transact during fraud, if rely and choose not to sell/buy, no standing**Transaction causation**, must affect whether the SH chose to buy into the firm*Basic*: Efficient market hypothesis, active market creates presumption that affected stock, claim fraud on the marketCan rebut this presumption if either plaintiff not relying on market (takeover) or market not actively followedCan also rebut by saying that statements were not relied on by market, show analysts did not take them seriously**Loss causation**, must cause the loss the SH claims (obvious)**Insider Trading**: Also established under R. 10b-5; cannot trade on material, nonpublic information about a firmAlso, R. 14e-3 governs in the tender offer circumstance specifically, do not need fiduciary duty violation for tender offers*Chiarella*: Must **violate fiduciary duties**/be insider to be liable, otherwise no literal “fraud” under R. 10b-5*Dirks*: Q is **purpose of disclosure**; tipper must be disclosing for personal reasons; tippee must know info is pvtFootnote 14: Constructive insiders (e.g. attorneys) have fiduciary duties if get information know should be kept pvtReg FD: No selective disclosure to analysts, must open disclosure to all analystsSEC only has to show trading in possession of information, not use, can get around by adopting a plan for when to sellPvt rt of action also exists, again have to show standing and transaction causation as under classic securities fraudMust register holdings w/ SEC if you are an insider; probably not if an Fn 14 person (not clear, though)R. 16, defining statutory insiders |