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To Our Clients:

Delaware Clarifies Fiduciary Duties
of Directors in a Takeover Situation

The recency of the takeover phenomenon and the happenstance nature of takeover litigation results in an absence of a body of judicial opinions that would enable a comprehensive synthesis of the law governing the fiduciary duties of the directors of a company faced with a takeover. This has resulted in much confusion. Some have argued that the courts have abandoned the traditional business judgment rule in takeover situations. Some have argued that the directors of a takeover target have only one duty -- to act as auctioneers and get the highest price obtainable.

In the past year there have been a number of cases reaffirming the application of the business judgment rule to takeover decisions by directors. These cases have rejected the argument that the only question is the short-term interests of the shareholders. The courts have now made it clear that the directors of a takeover target may properly determine to reject the takeover bid and decide to remain an

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independent company -- and in reaching that decision may take into account the adequacy of the bid; timing factors; risk of nonconsummation; effect on employees, customers, suppliers and communities; and the past history of the bidder.

Now one of the most troublesome questions also has been laid to rest. Some had read the Transunion and Revlon cases to mean that the directors of a company who had determined to sell the company had an absolute duty to get the highest possible price and that in this circumstance there was no room for the exercise of discretion. In the Fairchild Camera case decided on May 19 the Delaware Chancery Court said it:

is certainly incorrect to assert that [Revlon] recognized a duty on the part of directors when a corporation is "for sale," to get the highest available price. Rather, the duty can only be to try in good faith, in such a setting to get the best available transaction for the shareholders. Directors are not insurers.

The Fairchild Camera court went further and laid to rest the fear that the Transunion case undercut the business judgment rule, the court saying,

In my opinion, where a disinterested board in good faith considers the significance of the decision called for, the available information of which it and its

advisors are aware and the time constraints imposed upon it, and in those circumstances, the board makes a decision that it is in the best interests of the corporation to act, that decision itself is entitled to the benefits of the business judgment rule.

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