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A Kinder, Gentler Critique of Van Gorkom and Its Less Celebrated Legacies

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A KINDER, GENTLER CRITIQUE OF *VAN GORKOM* AND ITS LESS CELEBRATED LEGACIES

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We all know about the treatment in *Smith v. Van Gorkom*[1] of the director's fiduciary duty of care. It has been discussed extensively, and we continue to discuss it today, over sixteen years later. It would be unfortunate, however, if *Van Gorkom* were widely known only for its treatment of the duty of care. Many commentators have sternly criticized *Van Gorkom*'s legal analysis of that duty.[2] Moreover, and like many others, I believe the result in the case was wrong and that damages actions premised solely upon an alleged lack of director care are a poor, even destructive, corporate governance tool.[3] Indeed, I have gone so far as to suggest that *Van Gorkom* is an inappropriate case to teach in an introductory business organizations course.[4]

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[1] 488 A.2d 858 (Del. 1985).

[2] *See, e.g.*, Daniel R. Fischel, *The Business Judgment Rule and the* Trans Union *Case*, 40 BUS. LAW. 1437, 1455 (1985); Bayless Manning, *Reflections and Practical Tips on Life in the Boardroom After* Van Gorkom, 41 BUS. LAW. 1, 1 (1985).

[3] Professor Langevoort nicely summarizes the adverse effects of subjecting directors to monetary liability for lack of care: "overprecaution, refusals of good people to serve, demands for increased insurance, indemnification rights, and compensation for the residual risk." Donald C. Langevoort, *The Human Nature of Corporate Boards: Law, Norms, and the Unintended Consequences of Independence and Accountability*, 89 GEO. L.J. 797, 818 (2001). To this list, Professor Langevoort adds the cost of overcommitment to past bad decisions by managers who perceive a threat of judicial sanction for such decisions and seek to protect themselves by refusing to acknowledge and correct error. *Id.* at 826-27.

[4] Lawrence A. Hamermesh, *Why I Do Not Teach* Van Gorkom, 34 GA. L. REV. 477 (2000). To be sure, this pedagogical position has been described—accurately, no doubt—as "iconoclastic." Faith Stevelman Kahn, *Transparency and Accountability: Rethinking Corporate Fiduciary Law's Relevance to Corporate Disclosure*, 34 GA. L. REV. 505, 506 n.5 (2000). In commenting upon that pedagogical position John Olson, a justifiably well-respected corporate practitioner, has suggested that the failure to teach *Van Gorkom* is equivalent to a failure to teach *Brown v. Board of Education*, 347 U.S. 483 (1954), in an introductory constitutional law course. I do not wish to join issue on which opinion is better reasoned, or which is historically more significant in its subject-matter context. Two points of distinction between *Van Gorkom* and *Brown*, however, are indisputable: the facts recited in *Brown*, unlike those recited in *Van Gorkom*, are readily understandable to students; and the entire opinion in *Brown* takes up less than four casebook pages, as compared to the usual twenty or more for *Van Gorkom*. *See* Hamermesh, *supra*, at 480-82. Given these distinctions, I respectfully disagree with Mr. Olson that a decision not to teach *Van Gorkom* in an introductory course is equivalent to a decision not to teach *Brown*.

Van Gorkom, however, was about much more than the director's duty of care. Its legacies in other areas, while less celebrated (or bemoaned), deserve separate attention and even commendation. For looking back at the development of corporate law jurisprudence, especially in the mergers and acquisitions field, it is striking how clean the slate was—how little guidance the Delaware Supreme Court had—when *Van Gorkom* was decided. As demonstrated below, *Van Gorkom* exposed and took on deeply important issues that judges and practitioners had either not perceived or had preferred not to wrestle with. And it resolved these issues correctly, setting the stage for important developments in the fiduciary law that became central to the takeover jurisprudence that subsequently blossomed in the Delaware courts.

While many of *Van Gorkom*'s legacies beyond the general subject of the director's fiduciary duty of care have already been noted, I hope that gathering them together in one place may illustrate *Van Gorkom*'s considerable impact upon corporate law.

I. REJECTING THE PASSIVITY THESIS

According to the court's opinion, the directors of Trans Union believed they were entitled to submit the challenged merger agreement to a vote of the stockholders without endorsing it themselves; in other words, they could "take a noncommittal position on the merger and 'simply leave the decision to [the] shareholders.'"[5] No case had ever held that such a position was legally untenable, and indeed, there was strong academic support for the view that such a position was appropriate with respect to any acquisition bid at a price above prevailing market prices.[6] That academic view argued for a passive role for directors in dealing with takeover bids—one in which decisions about selling stock to a bidder for the company should rest with the stockholders themselves.[7]

A less perceptive court might have been inclined to condone the Trans Union directors' willingness to let the stockholders exclusively determine the merits of the merger. The Delaware Supreme Court, however, must be credited with recognizing the close link between the Trans Union directors' position and the developing controversy over the proper role of directors in hostile takeover bids.[8] In an environment in which such bids were burgeoning, a ruling that a board of directors could passively allow stockholders to determine whether and on what terms the company should be sold could

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[5] *Van Gorkom*, 488 A.2d at 887-88 (alteration in original).

[6] *See, e.g.*, Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981).

[7] Frank H. Easterbrook & Daniel R. Fischel, *Takeover Bids, Defensive Tactics, and Shareholders' Welfare*, 36 BUS. LAW. 1733, 1750 (1981).

[8] Jonathan R. Macey & Geoffrey P. Miller, Trans Union *Reconsidered*, 98 YALE L.J. 127 (1988). Macey and Miller deserve at least primary credit for recognizing and articulating *Van Gorkom*'s significance as a takeover case.

have significantly bolstered the proponents of director passivity in the face of hostile takeover bids.

Thus, the Trans Union directors' position presented an issue that the Delaware Supreme Court was not inclined to finesse. To the contrary, that court surely saw the *Van Gorkom* case as a rare opportunity to address the proper role of directors in dealing with acquisition bids. The court took up that opportunity eagerly, ruling unequivocally that the board of directors could not "take a neutral position and delegate to the stockholders the unadvised decision as to whether to accept or reject the merger."[9] According to the court, the pure "shareholder choice" approach held out by the Trans Union directors was not even an option, let alone a legally required approach: The court explained that this approach simply was "not viable or legally available to the Board under 8 Del. C. § 251(b)."[10]

True, the court had more than gently foreshadowed this rejection of the director passivity thesis a few months before it decided *Van Gorkom* in 1985.[11] But *Van Gorkom*'s role in sharpening and emphasizing that rejection is unmistakable: just a few months after *Van Gorkom* was decided, the Delaware Supreme Court directly addressed and upheld an aggressive and novel anti-takeover tactic in *Unocal Corp. v. Mesa Petroleum Co.*[12] At the point in the *Unocal* opinion in which the court explicitly rejected the director-passivity thesis, *Van Gorkom* was the only case cited.[13] *Van Gorkom*'s legacy—the belief that directors must actively consider takeover bids as interlocutors for the stockholders—has resurfaced continually in Delaware takeover jurisprudence ever since.[14] It surely represents one of *Van Gorkom*'s most important and enduring contributions to corporate law.

II. CREATING THE "RECOMMENDATION" DUTY OF DISCLOSURE

Well before *Van Gorkom*, the Delaware courts had identified disclosure obligations of corporate directors and controlling stockholders, and in so doing had developed what came to be described as a general "duty of candor."[15] Before *Van Gorkom*, however, that fiduciary disclosure duty had

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[9] *Van Gorkom*, 488 A.2d at 888.

[10] *Id.* For a merger to be effective under § 251(b), the board of directors must adopt a resolution approving the merger agreement and "declaring its advisability." DEL. CODE ANN. tit. 8, § 251(b) (1999).

[11] Pogostin v. Rice, 480 A.2d 619, 627 (Del. 1984) (rejecting claim that directors' failure to negotiate with bidder was a *prima facie* breach of duty, noting that "[e]stablishing such a principle would rob corporate boards of all discretion, forcing them to choose between accepting any tender offer or merger proposal above market, or facing the likelihood of personal liability if they reject it").

[12] 493 A.2d 946 (Del. 1985).

[13] *Id.* at 954 ("[W]e are satisfied that in the broad context of corporate governance, including issues of fundamental corporate change, a board of directors is not a passive instrumentality.").

[14] *See, e.g.*, Quickturn Design Systems, Inc. v. Shapiro, 721 A.2d 1281, 1291-92 (Del. 1998).

[15] *See* Lynch v. Vickers Energy Corp., 383 A.2d 278 (Del. 1977). The development of the law before and after *Lynch* is outlined in Lawrence A. Hamermesh, *Calling Off the* Lynch *Mob: The Corporate*

been limited to cases in which corporate directors and officers either (i) sought stockholder ratification of questioned (usually self-dealing) transactions in which they were involved, or (ii) bought or sold the corporation's shares using material inside information.[16] Outside of these two contexts, no court had ever held that when disinterested directors seek or recommend stockholder action, they have a fiduciary responsibility to disclose to the stockholders all reasonably available material information.[17]

The defendants' arguments in *Van Gorkom* did not stray from the worn path: the directors had argued, in a conventional fashion, that stockholder ratification cured any flaws in the directors' deliberative process.[18] Having found that material facts were not disclosed, the court could have simply announced that the directors' ratification defense had failed.

Van Gorkom did more than that, however. The court characterized the directors' disclosure failings as a breach of "their *original* duty of knowing, sharing, and disclosing information that was material and reasonably available for their discovery."[19] Later, in summarizing its opinion, the court identified, as a distinct breach of fiduciary duty, the directors' "failure to disclose all material information such as a reasonable stockholder would consider important in deciding whether to approve the Pritzker offer."[20]

Thus, *Van Gorkom* accomplished a jump-shift in the law of fiduciary disclosure duty: Now, it is hornbook law that "the directors owe the shareholders a duty of full disclosure *whenever* the board requests the shareholders to approve a transaction (such as a merger or the like)."[21] *Van Gorkom*'s terse, unexplained, and forceful extension of the law of fiduciary disclosure duty is nevertheless entirely consistent with the theoretical underpinnings of fiduciary responsibility.[22] And, as the Delaware Supreme Court subsequently took pains to point out, *Van Gorkom*'s legacy of fiduciary duty disclosure duty is one of the few and notable domains of securities-disclosure class actions that Congress explicitly insulated in 1998 from federal preemption.[23]

By extending the state law fiduciary disclosure duty to disinterested director recommendations of shareholder action, however, the court in *Van Gorkom* also inevitably broached the deeper question addressed thirteen years later in *Malone v. Brincat*:[24] if directors have a distinct, state law duty

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Director's Fiduciary Disclosure Duty, 49 VAND. L. REV. 1087 (1996).

[16] *Id.* at 1112-23.

[17] *Id.* at 1122.

[18] Smith v. Van Gorkom, 488 A.2d 858, 889-90 (Del. 1985).

[19] *Id.* at 893 (emphasis added).

[20] *Id.*

[21] FRANKLIN A. GEVURTZ, CORPORATION LAW 218-19 (2000) (emphasis added).

[22] Hamermesh, *supra* note 15, at 1159-64.

[23] Malone v. Brincat, 722 A.2d 5, 13 (Del. 1998) (citing Section 16(d) of the Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227 (1998)).

[24] *Id.*

to manage corporate information so as to present it to stockholders when the directors solicit stockholder action, do they likewise have such a duty at all other times, since stockholders continuously face the sell-or-hold decision with respect to shares traded in a public market?[25] There are good arguments on both sides of this question,[26] but the question itself lay dormant until *Van Gorkom* opened up the entire subject. Like its rejection of the director passivity thesis, *Van Gorkom*'s treatment of fiduciary disclosure duty has been a fundamental and enduring contribution to corporate law.

III. REINVIGORATING THE LAW OF CONTRACT IN CORPORATE MERGERS

When a board of directors approves a merger agreement, two facts loom large: the agreement cannot be concluded without stockholder approval as well, and stockholder approval almost always comes significantly later.[27] These facts implicate a variety of intricate and overlapping questions of contract law and fiduciary duty, questions that arise from the tension between the buyer's desire for certainty of consummation despite the lapse of time between board approval and stockholder action, and the seller's desire for flexibility in the event that superior bids emerge during that same time lapse.[28] These questions include:

- Can the board of directors, in a merger agreement, effectively commit to prohibit the corporation from later entering into a different merger agreement considered more beneficial to the stockholders? Does the directors' fiduciary duty overcome any such contractual undertaking? Does that duty limit the duration of any such commitment?

- Can the board effectively commit to refrain from soliciting superior offers? To refrain from negotiating in response to an unsolicited superior offer? To refrain from responding to unsolicited requests for proprietary information made by a potential bidder in order to formulate and evaluate whether to present a superior offer? To refrain from communicating at all with any potential competing bidder?

- Can the board effectively commit to terms or arrangements that re-

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[25] For a thoughtful analysis of this state law duty and its relation to the federal securities laws, see Kahn, *supra* note 4, at 515-18. It is submitted, however, that *Malone* does not even come close to creating a generalized fiduciary duty to apprise stockholders continuously and currently of information material to the sell/hold decision. All that *Malone* did was to emphasize the fiduciary responsibility to refrain from "knowingly disseminating to the stockholders false information about the financial condition of the company." 722 A.2d at 10.

[26] *See* Hamermesh, *supra* note 15, at 1173-77; Kahn, *supra* note 4.

[27] *See, e.g.*, DEL. CODE ANN. tit. 8, § 251(c) (1999).

[28] For detailed treatment of these questions, see Paul L. Regan, *Great Expectations? A Contract Law Analysis for Preclusive Corporate Lock-Ups*, 21 CARDOZO L. REV. 1 (1999); Leo E. Strine, Jr., *Categorical Confusion: Deal Protection Measures in Stock-for-Stock Merger Agreements*, 56 BUS. LAW. 919, 921 n.4 (2001).

quire the corporation to give the other party to the merger significant benefits if the merger agreement is terminated because of the failure of the corporation's stockholders to approve it?

- Can the board effectively commit not to disclose to stockholders the terms of a subsequent nonpublic acquisition proposal that is superior to the pending merger agreement? If not, in such a case may the board recommend that the stockholders vote down the original merger agreement, in light of the subsequent superior offer? And if not, is the board nonetheless free to submit the original merger agreement to the stockholders, but without a recommendation that the stockholders vote in favor of it?

When *Van Gorkom* was decided, the courts had hardly begun to answer these complex questions.[29] Surely Mr. Van Gorkom himself was not alone in 1980 in supposing that "under corporate law, directors always have an inherent right, as well as a fiduciary duty, to accept a better offer notwithstanding an existing contractual commitment by the Board."[30] Why else, he might have plausibly thought, would his merger agreement set forth Trans Union's obligation to seek and recommend stockholder approval, but then qualify that obligation by explicitly referring to the directors' "competing fiduciary obligations," if not to acknowledge such a right and duty?[31]

Whatever Mr. Van Gorkom and other executives and corporate lawyers thought in 1980, however, was emphatically dispelled by the opinion in *Van Gorkom*. That opinion made clear that having entered into a merger agreement, the directors of Trans Union were simply not in a legal position, if a better deal came along, to submit the original merger agreement to a

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[29] A notable exception, decided just a few months before *Van Gorkom*, was the decision in *Jewel Cos. v. Pay Less Drug Stores Northwest, Inc.*, 741 F.2d 1555 (9th Cir. 1984). *Van Gorkom* did not cite the *Jewel* opinion, perhaps because the case was fully submitted in the Delaware Supreme Court before the *Jewel* opinion was issued.

[30] Smith v. Van Gorkom, 488 A.2d 858, 879 (Del. 1985).

[31] *Id.* The Trans Union merger agreement provided that

> The Board of Directors shall recommend to the stockholders of Trans Union that they approve and adopt the Merger Agreement ("the stockholders' approval") and to use its best efforts to obtain the requisite votes therefor. [Purchaser] *acknowledges that Trans Union directors may have a competing fiduciary obligation to the shareholders under certain circumstances.*

Id. Similar qualifying language in the merger agreement at issue in *ConAgra, Inc. v. Cargill, Inc.*, 382 N.W.2d 576 (Neb. 1986), led the court in that case to conclude that a selling corporation's "best efforts" obligation did not preclude it from accepting a subsequent superior offer and refusing to recommend the original agreement for stockholder approval. Applying Delaware corporate law, the court explained that

> [t]he directors of MBPXL [the seller] could not agree to assist ConAgra [the buyer] by pledging their best efforts if by doing so the directors of MBPXL violated their legal duties to the MBPXL shareholders . . . . They had an obligation at that point to investigate the competing offer, and if, in the exercise of their independent good faith judgment, they found that the Cargill offer was a better offer for the MBPXL shareholders, they were bound to recommend the better offer.

Id. at 587-88. Interestingly, the court in *ConAgra* did cite *Van Gorkom* but, obviously, gave the directors of the seller considerably greater license to reject the original deal in favor of a subsequent better one.

stockholder vote but recommend that the stockholders vote it down.[32] Consistent with that position, the court also made clear that a subsequent higher bid would not absolve the corporation and its directors of a breach of contract claim if they abandoned the original merger agreement.[33] Finally, and foreshadowing its celebrated opinion the following year in *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*,[34] the court pointedly criticized the one-million-share purchase option granted to the buyer, suggesting that it undermined any claim that a subsequent "market test" effectively corroborated the merger agreement's fairness.[35]

By these holdings, *Van Gorkom* almost certainly helped encourage the corporate bar to pay more attention to the terms of the merger contract. Several pertinent databases provide a crude but interesting indicator of this impact. Before January 29, 1985, when *Van Gorkom* was decided, the term "fiduciary out" occurred just once in reference to a provision governing the termination of a merger agreement; since January 29, 1985, however, there have been hundreds of such references, and the term "fiduciary out" is now commonplace.[36] The corporate legal community is now thoroughly familiar with contract provisions, such as "fiduciary outs," that attempt to clarify the options of a board of directors faced with a merger proposal that might be superior to the original merger agreement.[37]

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[32] *Van Gorkom*, 488 A.2d at 888. *Cf. Jewel*, 741 F.2d at 1564 n.13 ("We do not decide the question whether upon the unsolicited receipt of a more favorable offer after signing a merger agreement the board still must recommend to its shareholders that they approve the initial proposal."). As explained in note 38, *infra*, however, subsequent legislation has modified *Van Gorkom*'s holding on this question.

[33] *Van Gorkom*, 488 A.2d at 888.

[34] 506 A.2d 173 (Del. 1986).

[35] *Van Gorkom*, 488 A.2d at 879-80.

[36] The following table summarizes the results of searches in various LEXIS and Westlaw databases during June 2001 for documents containing both the terms "fiduciary out" and "merger":

OCCURRENCES BEFORE JANUARY 29, 1985	OCCURRENCES AFTER JANUARY 29, 1985	DATABASE
0	75	LEXIS News Group Beyond 2 Years
n/a	35	LEXIS News Group < 2 Years
1*	51	LEXIS, Law Reviews Combined
0	20	Westlaw LEGALNP
0	32	Westlaw MBUS-CS
1**	182	BUS-TP

* The one law review article using the search terms did not relate to "fiduciary outs" in merger agreements.

** Robert L. Friedman et al., *Representing the Public Company in a Going-Private Transaction*, *in* GOING PRIVATE 1984, at 115-17 (PLI Corp. Law and Practice Course, Handbook Series No. 453, 1984).

[37] *See, e.g.*, Ace Ltd. v. Capital Re Corp., 747 A.2d 95 (Del. Ch. 1999); William T. Allen, *Understanding Fiduciary Outs: The What and the Why of an Anomalous Concept*, 55 BUS. LAW. 653 (2000); Diane Holt Frankle, *Fiduciary Duties in Considering Deal Lockups: What's a Board to Do?*, *in*

Van Gorkom certainly did not answer all the difficult questions about the range of permissible provisions in a merger agreement, and at least one of its answers to such a question has been overruled by statute.[38] Nor was *Van Gorkom* the first case to examine the relation between fiduciary duty and the terms of the merger agreement.[39] Moreover, even if *Van Gorkom* had never been decided, it is possible that the sheer level of merger activity would have called attention to "fiduciary outs" and related legal issues sooner or later.[40] Still, even an imperfect opinion that calls attention to and resolves latent and largely unexplored questions of merger and acquisition law must be considered to have achieved considerable success.

IV. ENRICHING THE LAW OF SHARE VALUATION

Van Gorkom's other significant contributions to the law governing mergers and acquisitions relate to the valuation of corporate shares. In the (long) course of addressing the adequacy of the directors' deliberative process, and in prescribing a remedy for the directors' breach of their duty of care, *Van Gorkom* established two notable propositions governing share valuation. The first of these propositions, which the court described as undisputed, was that "a publicly-traded stock price is solely a measure of the value of a minority position and, thus, market price represents only the value of a single share."[41] The second proposition, tossed off in a very short paragraph at the very end of a long opinion, was that in order to determine damages attributable to the directors' failure to exercise the requisite care in selling the company, the trial court should determine the extent to which the "intrinsic value" of the company's shares exceeded the merger price.[42]

HANDLING HIGH-TECH M&AS IN A COOLING MARKET: ENSURING THAT YOU GET VALUE 879-918 (PLI Corp. Law and Practice Course, Handbook Series No. B-1255, 2001).

[38] In 1998, the Delaware General Assembly amended Section 251(c) of the Delaware General Corporation Law, DEL. CODE ANN. tit. 8, § 251(c), to authorize the inclusion in a merger agreement of a provision committing the board of directors to submit a merger agreement to a stockholder vote, even if the directors determine, between approving the merger agreement and submitting it for stockholder approval, that they can no longer recommend stockholder approval of the agreement. 2 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS IX-38 (3d ed. Supp. 2001). As the legislative synopsis acknowledges, *id.* at IX-40.2, this amendment apparently countermands *Van Gorkom*'s instruction that the board of directors "could not remain committed to the Pritzker merger and yet recommend that its stockholders vote it down . . . ." 488 A.2d at 888.

[39] *See* Jewel Cos. v. Pay Less Drug Stores Northwest, Inc., 741 F.2d 1555 (9th Cir. 1984); Belden Corp. v. InterNorth, Inc., 413 N.E.2d 98 (Ill. App. Ct. 1980).

[40] Worldwide merger and acquisition activity has increased, more or less steadily, from $239 billion in 1985 to $3.372 trillion in 2000. Theodore N. Mirvis et al., *Takeover Law and Practice 2001*, *in* 2001 13th Annual Tulane Corporate Law Institute, vol. I, tab 11, at A-16 (on file with author).

[41] *Van Gorkom*, 488 A.2d at 876.

[42] *Id.* at 893. "Intrinsic value" was to be determined "in accordance with *Weinberger v. UOP, Inc.*, [457 A.2d 701,] at 712-15 [(Del. 1983)]." *Id.* at 893. The court's reference to *UOP* encompasses its earlier exposition of the determination of the "fair value" of shares in an appraisal proceeding pursuant

The articulation of the first proposition was enormously significant. Most immediately, this proposition was at least implicitly at the core of the court's previously discussed rejection of the director passivity thesis.[43] Once the court concluded, as it did, that a director's reference to current and historical stock market prices could not alone discharge that director's duty of care in considering a merger proposal,[44] a passive response to any above-market acquisition proposal, "friendly" or "hostile," became legally unacceptable.[45] If a hostile bid at a price in excess of current trading prices could nevertheless be considered inadequate, directors necessarily had an active role to play in evaluating bids and resisting inadequate bids. Given the intense interest in hostile takeovers leading up to the time *Van Gorkom* was decided, it could not be too farfetched to think that the court issued its valuation ruling in *Van Gorkom* with this message to directors very much in mind.

A more subtle corollary of *Van Gorkom*'s first valuation ruling took much longer to emerge. If publicly traded stock prices reflect only the value of a minority position, as *Van Gorkom* held,[46] then valuations premised on stock market multiples necessarily reflect some discount attributable to that minority position.[47] And since it became clear within a few years after *Van Gorkom* was decided, if not well before that, that such a discount could not be taken into account in determining the "fair value" of corporate shares, at least for purposes of Delaware's appraisal statute,[48] some compensating upward adjustment would have to be made in order to offset the minority discount implicit in reported trading prices.[49] This corollary of *Van Gorkom* did not come to fruition easily or quickly, but it has now been widely accepted.[50]

Van Gorkom's second valuation ruling, however, has remained largely unexplored[51]—perhaps fortunately so, for the reasons explained below. Having determined that the directors of Trans Union failed to use the requisite care in evaluating the terms of the merger, one would think that the

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to Section 262 of the Delaware General Corporation Law. DEL. CODE ANN. tit. 8, §262(h) (1999).

[43] *See supra* text accompanying notes 5-14.

[44] *Van Gorkom*, 488 A.2d at 876.

[45] *See supra* text accompanying notes 9-10.

[46] *Van Gorkom*, 488 A.2d at 876.

[47] John C. Coates IV, *"Fair Value" as an Avoidable Rule of Corporate Law: Minority Discounts in Conflict Transactions*, 147 U. PA. L. REV. 1251, 1265 (1999).

[48] Cavalier Oil Corp. v. Harnett, 564 A.2d 1137, 1145 (Del. 1989).

[49] Professor Coates has elaborately documented and explained the development of the judicial treatment of implicit minority discounts in Delaware appraisal law. Coates, *supra* note 47, at 1273-87.

[50] *Id.* at 1286-87 (citing Kleinworth Benson Ltd. v. Silgan Corp., 20 DEL. J. CORP. L. 1079 (Del. Ch. June 15, 1995)).

[51] In another article, I discussed the weaknesses of *Van Gorkom*'s remedial valuation prescription in support of my decision not to teach the case in the introductory business organizations course. Hamermesh, *supra* note 4, at 488-89.

damages resulting from that failure would be measured by the difference between what the company could have been sold for had the directors been more careful, and the price actually paid (fifty-five dollars per share). Instead of remanding to estimate what price a duly deliberate sale of the company would have yielded, however, the court chose to measure damages by reference to the difference between the "fair value" of the Trans Union shares, determined in accordance with Delaware appraisal law, and the actual fifty-five dollars per share sale price.[52]

These are two highly divergent measures, however. Any sale price for Trans Union—even the fifty-five dollars price actually paid—would surely account for the significant value of Trans Union's unused investment tax credits.[53] Yet, as the court itself noted, those same tax credits were essentially worthless in Trans Union's own corporate hands because of insufficient taxable income.[54] If the value of the tax credits could only be realized through purchase of the company, however, it is impossible to say that they should be reflected in the value of Trans Union as an independent going concern; more likely, the value of the tax credits should have been considered an element of value "arising from the accomplishment or expectation of the merger," or some merger, and therefore excluded by statute from consideration in determining the "fair value" of Trans Union's shares.[55]

In its choice of share valuation standards for purposes of calculating damages, therefore, *Van Gorkom* got it wrong: the court appears to have taken the valuation tool with which it was most familiar—"fair value" under the appraisal statute—and reflexively but inappropriately applied it to the valuation issue at hand.[56] Such reflexive reference to "fair value" as a valuation standard, however, hardly makes *Van Gorkom* an outlier in the case law. For many years, the opinions of the Delaware courts have recited, without much analysis, that the "fair price" concept in "entire fairness" reviews of controlled mergers is equivalent to the concept of "fair value" under the appraisal statute.[57] The arguably incorrect equation of these two concepts has roots going back nearly twenty years before *Van Gorkom* was decided.[58] The predilection to rely reflexively on the "fair value" concept

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[52] *See supra* note 42.

[53] Hamermesh, *supra* note 4, at 489.

[54] Smith v. Van Gorkom, 488 A.2d 858, 864 (Del. 1985).

[55] DEL. CODE ANN. tit. 8, § 262(h) (1999) (requiring the court to determine "fair value exclusive of any element of value arising from the accomplishment or expectation of the merger").

[56] The colloquialism that best characterizes this jurisprudential approach is the maxim that if all you have is a hammer, everything looks like a nail.

[57] *See, e.g.*, Onti, Inc. v. Integra Bank, 751 A.2d 904, 930 (Del. Ch. 1999); Coates, *supra* note 47, at 1261 n.33 (collecting cases and other authorities).

[58] Poole v. N.V. Deli Maatschappij, 224 A.2d 260, 263 (Del. 1966). *Poole* holds that in an action for damages due to fraud in the purchase of stock, "[t]he general rule is that in determining the actual value of stock, consideration should be given to the various relevant factors of value including earnings, dividends, market price, assets, and any other pertinent factors on a 'going concern' basis. This is the

from the appraisal statute, moreover, seems quite persistent: In a very recent case[59] the court assumed, without analysis, that what stockholders would have paid for shares in an effort to prevent a shift in control would be "a 'fair value' price equivalent to that determined through appraisal."[60]

CONCLUSION

For better or worse, *Van Gorkom* will surely be remembered predominantly because of its finding that directors of a Delaware corporation breached their fiduciary duty of care. If nothing else, the placement of *Van Gorkom* in law school casebooks under the heading of the duty of care will ensure this result.[61] *Van Gorkom*'s other significant contributions to the law of mergers and acquisitions, however, should not be lost in the glare of its controversial and questionable treatment of the duty of care. It is hoped that the foregoing remarks will help assure that *Van Gorkom*'s less-celebrated—but perhaps sounder—contributions are duly acknowledged.

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rule in fraud cases." *Id.* (citations omitted). This is also the approach to valuation in stock appraisal proceedings under DEL. CODE ANN. tit. 8, § 262 (1999).

[59] Miller v. Agranoff, 750 A.2d 530 (Del. 2000).

[60] On remand, the Court of Chancery thoughtfully questioned whether a reflexive resort to "fair value" standards derived from appraisal litigation really fits the remedial purpose in a different context. Agranoff v. Miller, 2001 Del. Ch. LEXIS 71, at *18-19 (Del. Ch. May 15, 2001).

[61] Hamermesh, *supra* note 4, at 483.