AS THE WORLD TURNS: THE CHANGING VIEW OF THE DIRECTOR DEFENDANT IN CORPORATE LITIGATION

By David J. Berger [1]

I. INTRODUCTION

As this article goes to print, Martha Stewart has just been sentenced to prison, two members of the Rigas' family are awaiting sentencing, and Ken Lay, Bernie Ebbers and other icons of the late-1990 corporate excesses have been indicted. In terms of civil liability, MCI is suing Ebbers for payments and loans made to him during his tenure as chairman and CEO, Lord Black recently was forced to repay Hollinger International approximately $30 million for allegedly improper payments made to him during his tenure as chairman and CEO, and many other large corporations (including such prominent companies as Nortel, HealthSouth and others) are investigating the past actions of their senior executives, and possibly seeking to recoup millions of dollars paid to these executives in bonuses and/or other forms of compensation.

Such behavior has led many in the boardroom, as well as those responsible for regulating, legislating, and critiquing those in the boardroom, to take numerous actions to prevent such wrongdoing—and the appearance of wrongdoing—in the future. Directors

---

[1] Mr. Berger is a partner in the firm of Wilson Sonsini Goodrich & Rosati. The views expressed herein are solely those of the author, and not those of his firm.

are putting more time in on the job, and using that time for different purposes than in the past. In particular, a considerable amount of director time is being spent on monitoring and oversight rather than the more traditional tasks of strategy and advice. The changing way public boards are forced to operate in this new environment has even led some prominent directors to resign from their positions.

In terms of legislation, seeing the phrase “Sarbanes-Oxley” in the corporate world has become about as common as seeing the Yankees play in October (a Google search using the phrase “Sarbanes-Oxley” returned “more than 1800 items in 0.05 seconds”). As if this were not enough to dishearten those in corporate America who root for the Red Sox, the costs of implementing the regulations and procedures required under “SOX” are skyrocketing faster than Steinbrenner’s payroll. While attacks on Sarbanes are also on the increase, with individuals ranging from NYSE head John Thain to former HealthSouth Chairman and CEO Richard Scrushy criticizing the law in a variety of respects (from being overly burdensome to being unconstitutionally vague), the political realities make it unlikely that the law will be significantly changed (at least by Congress) any time soon. To the contrary, in response to some of these attacks, Senator Joseph Biden of Delaware recently read into the Congressional Record a detailed analysis of the intent of Congress in adopting Sarbanes in an effort to ensure that the law is not weakened as it is challenged in court.

As director behavior changes to meet the new regulatory and political environment, decisions by judges are also impacted by the same factors. Judges are people, too, and are not immune from the environment in which they live, but rather develop views based upon the realities before them in context. This is not to say that a court is deciding a particular legal issue because of extraneous events, but rather to recognize the reality that the best courts look at all of the facts and circumstances when making a decision, including the environment in which that decision is being made.

The changes in the courtroom can be seen in a number of decisions over the last couple of years. While these decisions generally had a basis in precedent and can be defended on their merits, one can also make a rather convincing case that various aspects of these decisions may have come out differently had the case been heard in 1993 instead of 2003. Certainly the scrutiny of a director's decision, and the skepticism concerning a board's process, has increased as a result of the perceived excesses of the late 1990s. Moreover, it is no longer the case that a defendant who is a corporate executive wears the proverbial "white hat" when walking in a courtroom. Indeed, the views espoused in the late 1990s by such prominent academics as Yale law professor Henry Hansmann and Harvard law professor Reinier Kraakman that the success and wisdom of the American system of corporate governance in its then-existing state was so evident that it represented the "End of History" for corporate law, now look more than a bit naive.

There are several lessons for corporate directors and their advisers when considering this new landscape. First, it is clear that transparency has a very significant role in the courtroom as well as in a company's public filings. That is, when considering such issues as director independence, good faith or due care, a director needs to be prepared to go beyond what has traditionally been necessary to meet these tests. This includes reviewing and disclosing all aspects of relationships between directors (*i.e.* personal, familial, professional, *etc.*), making a determination about waiving potentially applicable privileges, as well as making sure that there is a complete record of the process which led to a director's decision and that the board was fully informed of the relevant facts when making a decision.

Second, there is substantially more pressure on the role of the professionals, including the company's lawyers and accountants, when advising the senior management team. Several of the most prominent executives alleged and/or convicted of fraud and other wrongdoing, including such household names as Ken Lay, Richard Scrushy, Bernie Ebbers and John Rigas, have all claimed that they were not responsible for the conduct occurring while they led their respective companies at least in part because they relied on the work of their professional staff. This "professional staff" includes not just the company's officers, but outside accountants, lawyers and others as well. As John Rigas' lawyer said, "John Rigas had a right to trust and rely on professionals and his own staff to get the financials right."

Third, it is clear that we are in an age of a very activist SEC. As part of this process, the SEC is both expanding upon previous legal theories, as well as bringing cases which it had not pursued for many years. For example, according to *Business Week* the SEC's case against Ken Lay is the first time in more than 35 years that it has brought an insider-trading case against a corporate executive for trading in the company's securities while failing to disclose material, non-public information. More generally, the SEC is also said to be investigating numerous situations where insiders borrowed money against their shares or otherwise used their company stock as collateral to determine whether such borrowing should have been disclosed and/or constituted insider trading.

Fourth, the courts, including the courts in Delaware (which remain the most influential courts in the country on corporate governance issues), are also reviewing director conduct with greater scrutiny than ever before. In particular, the corporate scandals and resulting loss of trust has impacted the way courts view the actions of corporate boards. Recent decisions out of Delaware and elsewhere show that decisions made in the boardroom tend to be viewed, if not with a more cynical eye than in the past, then certainly with greater scrutiny. Yet this scrutiny is not designed to remove the traditional protections provided to directors under the business judgment rule. Rather, this scrutiny is focused upon the process by which board action is taken. Norman Veasey, who recently retired from his position as the Chief Justice of the Delaware Supreme Court, described this balance as follows:

> Although the law of fiduciary duty recognizes the evolving expectations of the standards of conduct of directors and officers, we must keep in mind that the business judgment rule continues unabated to protect directors' decisions made in good faith and to enable them to set strategic goals for prudent risk-taking. What has evolved in this new era is a sharper judicial focus on the processes employed by directors, but it is not a regulatory clamp on their business judgment.

This outline briefly summarizes some recent cases under Delaware law concerning the independence of outside directors, the duty of care of officers and directors, and the board's duties in corporate control transactions. The purpose of this outline is not to be an exhaustive review of recent cases, but rather to provide a short summary of how some courts are considering these issues by examining some important cases from the last couple of years.

II. RECENT DEVELOPMENTS IN DELAWARE CASE LAW

a. Director Independence

1. *In re Oracle Corp. Derivative Litig.*, 824 A.2d 917 (Del. Ch. 2003).

The facts in the *Oracle* case are, by now, well known. The case involved a derivative action against four directors of Oracle, including Larry Ellison, Jeff Henley, Don Lucas, and Michael Boskin (the "Trading Defendants"). According to plaintiffs, the Trading Defendants knew in January 2001 that Oracle would fail to meet the earnings and revenue guidance the company provided the market in December 2000. The Trading Defendants, however, allegedly failed to disclose this information until March 2001, and instead sold millions of shares of Oracle stock during January 2001. Consequently, plaintiffs claimed that the Trading Defendants breached their fiduciary duty of loyalty by misappropriating inside information. *See In re Oracle Corp. Derivative Litig.,* 824 A.2d 917, 921-23 (Del. Ch. 2003).

In response to plaintiffs' allegations, Oracle’s board of directors formed a Special Litigation

Committee ("SLC"), which was granted "full authority" to decide, without further board approval, whether to press claims against the defendants. *Id*. at 923. The SLC was composed of two highly prominent outside directors, Hector Garcia-Molina and former SEC Commissioner Joseph Grundfest. Messrs. Garcia-Molina and Grundfest both joined Oracle's board on October 15, 2001. They also shared something else in common: they were both tenured professors at Stanford University. One of the Trading Defendants, Michael Boskin, was also a professor at Stanford, and these professional ties were disclosed in the SLC's report. *See id*. at 929.

In evaluating plaintiffs' claims, the SLC performed an investigation that was "by any objective measure, extensive." *Id*. at 925. Indeed, the Court of Chancery noted that the SLC:

- Interviewed "all the senior members of Oracle's management most involved in [the] projection and monitoring of the company's financial performance";

- Met with its counsel thirty-five times for a total of eighty hours; and

- Produced "an extremely lengthy Report totaling 1,110 pages (excluding appendices and exhibits)".

Id.

At the end of its investigation, the SLC concluded that the Trading Defendants did not possess material, non-public information in December 2000 and January 2001. Moreover, the SLC determined that the Trading Defendants sold only a small percentage of their total holdings in Oracle during January 2001 and none of them had any reason to expose their (considerable) personal wealth to substantial risk by undertaking an insider-trading scheme. For these reasons, among others, the SLC moved to terminate the Delaware action after deciding that Oracle should not pursue claims against the Trading Defendants. *See id*. at 925-28.

In connection with the SLC's motion to terminate, the plaintiffs were granted discovery with respect to, *inter alia*, the independence of the SLC. During the course of this discovery, numerous personal and professional ties emerged between the members of the SLC, certain Trading Defendants, and Stanford University that had not been disclosed in the SLC's report. For instance:

- Defendant Michael Boskin had taught SLC - member Joseph Grundfest when Professor Grundfest was a Ph.D. candidate at Stanford, and both Messrs. Boskin and Grundfest were senior fellows and steering committee members at the Stanford Institute for Economic Policy Research ("SIEPR");

- Defendant Donald Lucas was a Stanford alumnus who had personally contributed $4.1 million to the University between 1998 and 2003. He was also the Chairman of the Richard M. Lucas Foundation, which had contributed over $11.7 million to Stanford since 1981. Additionally, Mr. Lucas was the Chair of the Advisory Board of SIEPR and the SIEPR Conference Center at Stanford was named after him; and

- Defendant Lawrence Ellison was a contributor to Stanford; specifically, Stanford was the beneficiary of $10 million in grants from one of Mr. Ellison's charitable institutions, the Ellison Medical Foundation, and Mr. Ellison previously considered establishing a $170 million scholarship program at Stanford and donating his $100 million home to the University.

See id. at 929-35. Based on these social and collegial relationships, plaintiffs' argued that the SLC members were not "independent" and, thus, the motion to terminate should be denied.

Relying heavily on the fact that its members were not "dominated" or "controlled" by any of the Trading Defendants, the SLC argued that the ties between the SLC members, the Trading Defendants, and Stanford were immaterial and did not impair the impartiality of the committee. *Id.* at 937. The SLC explained that Messrs. Garcia-Molina and Grundfest were both tenured professors and experts in their respective fields and, thus, the Trading Defendants would not have had any practical ability to threaten the SLC members' positions at Stanford or their ability to make a living. *See id*. at 935-36. Further, Messrs. Garcia-Molina and Grundfest were not part of Stanford's official fundraising apparatus and, therefore, they were not beholden to the Trading Defendants for donations to the University. *See id*.

The Court of Chancery denied the motion to terminate, holding that the SLC had failed to establish that its members were independent. The Court began its opinion by setting forth the elements that a special litigation must establish under *Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del. 1981) to terminate derivative litigation: (1) the committee must show that its members were independent; (2) that they acted in good faith; and (3) that they had a reasonable basis for their recommendation. *See Oracle*, 824 A.2d at 928. The Court then noted that it only needed to examine the "independence" issue to render a decision in this case. *See id*. at 929.

While the Court acknowledged that Messrs. Garcia-Molina or Grundfest were not "dominated" or "controlled" by the Trading Defendants, Oracle, or Stanford in a financial sense, the Court found that this did not resolve the issue of whether the SLC members were independent. *See id*. at 938-39. The question of independence, the Court stated, "turns on whether a director is, *for any substantial reason*, incapable of making a decision with only the best interests of the corporation in mind." *Id.* at 938 (*quoting Parfi Holding AB v. Mirror Image Internet, Inc*., 794 A.2d 1211, 1232 (Del. Ch. 2001)) (emphasis in original). The Court explained that a director's judgment may be compromised by "bias-creating factors other than fear that acting a certain way will invite economic retribution by the interested directors." *Id.* at 939 n.55. Indeed, the Court specifically pointed out that a director may be incapable of making an unbiased decision simply because he has "personal or other relationships" with an interested party. *Id.* at 939 (*quoting Orman v. Cullman*, 794 A.2d 5, 24 n.47 (Del. Ch. 2002)). Accordingly, the Court held that a "contextual approach," which looks at "all the facts" that may affect a special litigation committee members' impartiality, should be applied. *Id.* at 941, 947.

In making its decision, the Court expressed “some shock” that the extent of the Stanford ties was not revealed in the SLC’s report, noting that “the plain facts are a striking departure from the picture presented in the Report." *Id*. at 929-30. At the same time, the Court conceded that "the result [it] reach[ed] is in tension with the specific outcomes of certain other decisions." *Id.* at 939 n.55. The Court stressed, however, that it was not creating a "new definition of independence" but was merely recognizing the importance of bias-creating factors other than fear of pecuniary damage for acting in a particular way. *Id.* In addition, while acknowledging that a contextual approach "undoubtedly results in some level of indeterminacy," the Court found that this drawback was outweighed by "the compensating benefit that independence determinations are tailored to the precise situation at issue." *Id.* at 941.

Additionally, the Court determined that there was a reasonable doubt that the SLC members could have made an impartial decision as to whether to proceed with claims against Mr. Ellison for insider trading. The Court stated that "[t]he notion that anyone in Palo Alto can accuse [Mr.] Ellison of insider trading without harboring some fear of social awkwardness seems a stretch." *Id.* at 945. The Court also emphasized that Mr. Ellison "remain[ed] a plausible target of Stanford for a large donation." *Id.* at 946.

Finally, the Court rejected the SLC members' argument that they were not aware of just how substantial the ties were between the SLC members, the Trading Defendants, and Stanford while they were conducting their investigation. The Court stated that "[i]n forming the SLC, the Oracle Board should have undertaken a thorough consideration of the facts bearing on the independence of the proposed SLC members from the key objects of the investigation." *Id.* at 943. Vice Chancellor Strine concluded that "it undermines, rather than inspires, confidence that the

SLC did not examine the Trading Defendants' ties to Stanford more closely in preparing its Report." *Id.*

Significantly, the Court did not consider the other *Zapata* factors after it found that the SLC had not established that its members were independent. *See id*. at 948 ("In the absence of a finding that the SLC was independent, its subjective good faith and the reasonableness of its conclusions would not be sufficient to justify termination"). Thus, the Court did not address the merits of the SLC's investigation.

2. *In re eBay, Inc. S'holders Litig.*, No. Civ.A. 19988-NC, 2004 WL 253521, (Del. Ch. Jan. 23, 2004).

In re eBay involved a derivative action against, *inter alia*, three directors of eBay, Inc. (the "Director Defendants") and The Goldman Sachs Group, Inc. ("Goldman Sachs"), eBay's investment banking advisor. During 1998 through 2001, Goldman Sachs allegedly allocated thousands of shares of lucrative initial public offerings to the Director Defendants and Jeffrey Skoll, eBay's Co-Founder and second largest shareholder. *See In re eBay, Inc. S'holders Litig.,* No. Civ.A. 19988-NC, 2004 WL 253521, at *1 (Del. Ch. Jan. 23, 2004). According to plaintiffs, these "highly profitable investment opportunities" belonged to eBay because they were offered to the Director Defendants and Mr. Skoll as an inducement to maintain the company's business relationship with Goldman Sachs. *Id*. Consequently, plaintiffs claimed that the Director Defendants and Mr. Skoll usurped a corporate opportunity by accepting the IPO share allocations. *See id*.

The defendants moved to dismiss plaintiffs' complaint for failure to sufficiently allege demand futility and failure to state a claim. The defendants argued that the majority of eBay's Board of Directors was "disinterested" and "independent" because four of the company's seven Board members (the "Outside Directors") did not receive *any* share allocations from Goldman Sachs. Moreover, the defendants argued that the Director Defendants and Mr. Skoll could not have usurped a corporate opportunity by accepting the share allocations because investing in IPOs was not within eBay's line of business. *See id.* at *1, 3-4.

The Court of Chancery denied the motion to dismiss, holding that plaintiffs had sufficiently alleged demand futility. The Court began its opinion by pointing out that three of eBay's directors, *i.e.*, the Director Defendants, were "clearly interested in the transactions at the core of this controversy." *Id.* at *2. Since three of eBay's seven directors were "interested" in the IPO transactions, the Court found that plaintiffs were required to "only demonstrate a reason to doubt the independence of *one* of the remaining four directors." *Id.* (emphasis added).

Turning to plaintiffs' allegations regarding the "independence" of the four Outside Directors, the Court held that at least one of these individuals, Scott D. Cook, was not "disinterested" or "independent." *See id.* at *2-3. The Court explained that Mr. Cook had previously been awarded "substantial stock options" for his services as an eBay director. *See id.* at *2. Because these options were now "worth potentially millions of dollars," Mr. Cook had a strong interest in retaining his position as a director of eBay. *Id.* at *2. Because the Director Defendants and Mr. Skoll owned (collectively) approximately 50% of eBay's outstanding common stock, however, they had the ability to remove Mr. Cook from the company's board. *See id.* at *3. Accordingly, the Court concluded that Mr. Cook was “beholden” to the Director Defendants and could not impartially consider a demand to bring litigation against them. *See id.*

The Court also rejected defendants’ argument that investing in IPOs was not within eBay’s line of business. *See id.* at *4. Relying primarily on disclosures in eBay’s Form 10-K for fiscal year 1999, the Court found that eBay had previously invested “more than $550 million . . . in equity and debt securities” and “more than $181 million in ‘short-term’ investments." *Id*. Thus, the Court concluded that “investing was a ‘line of business’ of eBay.” *Id.*

Finally, the Court held that even if the share allocations did not constitute a corporate opportunity for eBay, plaintiffs had stated a cognizable claim against the Director Defendants and Mr. Skoll for breach of the fiduciary duty of loyalty. *See id.* at *5. The Court explained that Goldman Sachs offered the IPO share allocations to obtain eBay’s future business. *See id.* Accordingly, the Director Defendants and Mr. Skoll had, at the very least, improperly diverted “a commission or gratuity” that rightfully belonged to eBay. *Id*.

3. ***Beam v. Stewart*, 845 A.2d 1040 (Del. 2004).**

Beam v. Stewart challenged the independence of the directors of Martha Stewart Living Omnimedia, Inc. (“MSO”), claiming that the directors’ friendships and personal relationships with Martha Stewart made them incapable of rendering an unbiased decision about whether or not to bring claims against her. The complaint alleged that Stewart’s allegedly improper trading of shares of ImClone Systems, Inc. (“ImClone”), as well as other sales of MSO shares by Stewart, constituted a breach of fiduciary duty. The complaint further alleged that demand was futile based on the lack of independence of at least half of MSO's six-member board of directors.

The Chancery Court dismissed the complaint for failing to make demand. The Court noted that while "some professional or personal friendships, which may border on or even exceed familial loyalty and closeness, may raise a reasonable doubt whether a director can appropriately consider demand . . . [n]ot all friendships, or even most of them, rise to this level. . .". *Beam v. Stewart*, 833 A.2d 961,979 (Del. Ch. 2003), *aff'd*, 845 A.2d 1040 (Del. 2004). The Court held that in order to make a "reasonable inference" that a particular friendship rises to this level, the plaintiff must provide "specific factual allegations" concerning the "closeness or nature of the friendship, details of the business and social interactions between the two, or allegations raising additional considerations . . . ." *Id*. at 979-80.

On appeal, the Delaware Supreme Court affirmed. In one of the last opinions written by former Chief Justice Veasey, the Supreme Court began by noting that "[i]ndependence is a fact-specific determination made in the context of a particular case. The Court must make that determination by answering the inquiries: independent from whom and independent for what purpose?" *Beam*, 845 A.2d at 1050. The Supreme Court agreed with the Chancery Court that a director's independence may be questioned for any reason, including "financial ties, familial affinity, a particularly close or intimate personal or business affinity or because of evidence that in the past the relationship caused the director to act non-independently *vis á vis* an interested director." *Id.* at 1051. The Court did hold that allegations that directors moved "in the same business and social circles, or a characterization that they are close friends" is not enough to negate independence. Rather, the Court held that:

> [t]o create a reasonable doubt about an outside director's independence, a plaintiff must plead facts that would support the inference that because of the nature of a relationship or additional circumstances other than the interested director's stock ownership or voting power, the non-interested director would be more willing to risk his or her reputation with the interested director.

Id. at 1051-52. The Court found that none of the Plaintiff's allegations rose to this level.

In a final section of the opinion, titled "A Word About the Oracle Case," the Delaware Supreme Court advocated a relatively limited reading of the Chancery Court's opinion in *Oracle*. The Supreme Court first noted that the *Oracle* case involved the creation of a Special Litigation Committee ("SLC"), and that unlike the demand-excusal context, where the board is presumed to be independent, the SLC has the initial burden of establishing its own independence that must be "like Caesar's wife—above reproach." *Id.* at 1055 (citation omitted). The Court also noted that "the Stanford connections in *Oracle* are factually distinct from the relationships present" in *Beam*. *Id*.

Beam and *Oracle* are two examples of courts conducting a searching inquiry about a director's independence, and that this inquiry will go beyond financial or work relationships. All aspects of the relationship—be it personal, financial, business, or any other relationship—are open for inquiry and will be reviewed on a case-by-case basis to determine the specific nature of the relationship.

b. <u>The Duties of Care and Good Faith</u>

1. ***In re The Walt Disney Co. Derivative Litig.*, 825 A.2d 275 (Del. Ch. 2003).**

In *Disney*, plaintiffs filed a derivative action against The Walt Disney Company's ("Disney") board of directors in connection with the company's hiring and termination of Michael Ovitz, the former President of Disney. Plaintiffs alleged that the company's directors breached their duty of care by blindly approving Mr. Ovitz' employment agreement and non-fault termination benefits. Plaintiffs claimed that, as a result, Mr. Ovitz received approximately $140 million for just over one year of employment.

On October 7, 1998, the Court of Chancery dismissed plaintiffs' complaint with prejudice for, *inter alia*, failure to sufficiently allege demand futility under *Aronson v. Lewis*, 473 A.2d 805, 814 (Del. 1984). *See In re The Walt Disney Co. Derivative Litig*., 731 A.2d 342, 364-65 (Del. Ch. 1998). Plaintiffs appealed, however, and the Delaware Supreme Court reversed the Court of Chancery's decision to the extent that the dismissal of plaintiffs' duty of care claims was *with prejudice*. *See Brehm v. Eisner*, 746 A.2d 244, 248 (Del. 2000). The Supreme Court explained that although plaintiffs had failed to satisfy the pleading requirements under *Aronson*, "[t]his is potentially a very troubling case on the merits." *Id.* at 249. Consequently, the Court gave plaintiffs the opportunity to replead and strongly suggested that they improve their factual allegations by utilizing Section 220 of the Delaware General Corporation Law, which grants stockholders the right to inspect the company’s books and records. *See id*. at 266-67.

Plaintiffs followed the Supreme Court's advice and made a Section 220 demand on Disney. *See In re The Walt Disney Co. Derivative Litig.*, 825 A.2d 275, 279 (Del. Ch. 2003). After reviewing Disney's books and records, plaintiffs filed an amended complaint in the Court of Chancery. According to the amended complaint, Michael Eisner, Disney's Chief Executive Officer and Mr. Ovitz' close friend, decided unilaterally to hire Mr. Ovitz during August 1995. Although the Disney directors initially objected to Mr. Eisner's decision, Mr. Eisner persisted in his efforts to hire Mr. Ovitz as Disney's new president. Indeed, at Mr. Eisner's request, Disney prepared a draft employment agreement for Mr. Ovitz on September 23, 1995. *See id*.

On September 26, 1995, the Disney board's compensation committee met to discuss Mr. Ovitz' potential employment. The meeting lasted "just under an hour" and the committee spent most of this time discussing the fee that Irwin Russell, a committee member and Mr. Eisner's personal attorney, would receive for securing Mr. Ovitz' employment. *Id.* at 280. The compensation committee was not provided with a copy of the draft employment agreement and "no presentations, spreadsheets, written analyses, or opinions were given by any expert for the compensation committee to rely upon." *Id.* Instead, Mr. Russell provided the compensation committee with a "rough summary of the agreement." *Id.* At the end of the meeting, the compensation committee adopted a resolution approving the general terms and conditions of Mr. Ovitz' employment. *See id*. at 280-81.

Shortly thereafter, Disney's full board met and voted to appoint Mr. Ovitz as Disney's new president. The board failed to ask any questions about Mr. Ovitz' compensation package or the potential consequences of his termination. The board did not receive or even request a copy of the draft of the employment agreement and there were no experts present to advise the board. Despite this dearth of information, the board gave Mr. Eisner the authority to negotiate and approve the final terms and conditions of Mr. Ovitz' employment contract. Significantly, the board did not review or approve the final employment agreement until after it was executed and made binding upon Disney. *See id*. at 281-82.

On October 1, 1995, Mr. Ovitz was officially hired as Disney's president for a five-year term. Under the final employment agreement, Mr. Ovitz was entitled to receive a base salary of $1 million per year, a discretionary bonus of up to $10 million, and two sets of stock options that collectively would enable Mr. Ovitz to purchase 5 million shares of Disney common stock. The agreement also provided three ways by which Mr. Ovitz' employment might end. First, Mr. Ovitz could serve his five years and Disney could decide not to renew his contract, in which case Disney would owe Mr. Ovitz a $10 million termination payment. Second, Disney could terminate Mr. Ovitz for gross negligence, malfeasance, or if Mr. Ovitz resigned voluntarily. Under these circumstances, Disney would owe Mr. Ovitz no additional compensation. Finally, Mr. Ovitz could be terminated "without cause," *i.e.*, non-fault termination. In the event of a non-fault termination, however, Disney was required to pay Mr. Ovitz the remaining salary payments under his employment contract, a $10 million severance payment, and $7.5 million for each year remaining on his contract at the time of termination. A non-fault termination would also result in the immediate vesting of Mr. Ovitz' first three million stock options. *See Brehm*, 746 A.2d at 249-50.

Mr. Ovitz's tenure as president of Disney was anything but successful and he began seeking other employment shortly after joining the company. Mr. Eisner also decided within one year of hiring Mr. Ovitz that it would be best for all parties involved if Mr. Ovitz left Disney and gained employment elsewhere. Accordingly, Messrs. Ovitz and Eisner began negotiating Mr. Ovitz' departure. *See Walt Disney*, 825 A.2d at 283-84.

During December 1996, Mr. Ovitz and Disney (through Mr. Eisner) agreed that Mr. Ovitz' employment would be terminated as if there had been a non-fault termination. This allowed Mr. Ovitz to receive all of the severance benefits under his employment agreement which was allegedly worth approximately $140 million. According to plaintiffs, neither the board nor the compensation committee had been consulted or given their approval when Mr. Eisner granted Mr. Ovitz a non-fault termination. Moreover, the board never questioned Mr. Eisner's decision and there was no evidence that the board ever considered any alternatives to non-fault termination. *See id*. at 283-85.

The defendants moved to dismiss plaintiffs' amended complaint for failure to sufficiently allege demand futility under the second prong of *Aronson*. The Court of Chancery denied the motion. The Court explained that in order to establish demand futility under the second prong of the *Aronson* test, plaintiffs must plead particularized facts sufficient to raise a reasonable doubt that (1) the action was taken honestly and in good faith or (2) the Board was adequately informed in making the decision. *See id*. at 285-86. The Court found that, as alleged in the complaint, the defendants failed to exercise any business judgment whatsoever and, instead, "consciously ignore[d]" their duties to the corporation. *Id.* at 290. In making its decision, the Court emphasized that the Board spent "less than an hour" reviewing the decision of whether to hire Mr. Ovitz, never consulted any experts, and allowed Mr. Eisner (Mr. Ovitz' good friend) to negotiate and approve the final terms of the employment agreement. *See id*. at 287-88. Further, the Court pointed out that the board played no role in Mr. Eisner's decision to grant a non-fault termination to Mr. Ovitz, even though Disney's bylaws required board approval for that decision. *See id*. at 285.

The Court also rejected defendants' argument that the amended complaint should be dismissed pursuant to Title 8 Delaware Code Annotated section 102(b)(7), which permits exclusion of directors from personal liability for negligent duty-of-care violations. The Court reiterated that the board had not exercised *any* business judgment in approving Mr. Ovitz' employment and non-fault termination. Consequently, the board's actions were not taken in good faith and did not fall within the ambit of Title 8 Delaware Code Annotated section 102(b)(7). *See id*. at 286.

2. ***In re HealthSouth Corp. S'holders Litig.*, No. Civ. A. 19896, 2003 WL 22769045 (Del. Ch. Nov. 24, 2003).**

HealthSouth involved a derivative action against Richard Scrushy, the Chief Executive Officer of HealthSouth, Inc. During 1999, Mr. Scrushy borrowed approximately $25 million from HealthSouth and then used those funds to purchase over 4 million shares of the company's stock. At the time, HealthSouth's stock was trading at $5.78 a share. On August 1, 2002, Mr. Scrushy repaid his loan by transferring $25 million worth of HealthSouth stock back to the company (the

"Buyback"). *See In re HealthSouth Corp. S'holders Litig.,* No. Civ. A. 19896, 2003 WL 22769045, at *2 (Del. Ch. Nov. 24, 2003).

When Mr. Scrushy repaid his loan, HealthSouth appeared to be a stable and profitable company: HealthSouth's stock was trading at approximately $10 per share and the company's financial statements for 2001 showed revenues of $4.4 billion and net earnings of $202 million. *See id*. at *2, 4. Less than one month after the Buyback, however, HealthSouth announced that it would need to reduce its projected earnings for 2002 and 2003 by $175 million. *See id*. at *2. Further, over the course of the next several months, HealthSouth discovered and disclosed that there were over $2 billion in fraudulent entries in its financial statements for 1997 through 2003. *See id*. at *4.

HealthSouth's stock price plummeted as a result of these disclosures and the federal government began investigating many of the company's top executives, including Mr. Scrushy. *See id*. at *1, 3-4. By November 2003, fifteen HealthSouth executives had pleaded guilty to crimes in connection with the intentional falsification of the company's financial statements. *See id*. at *4. All of these individuals alleged that they had been involved in a conspiracy to falsify HealthSouth's financial statements and that Mr. Scrushy had been an integral part of that conspiracy. *See id*. Mr. Scrushy, however, claimed that he was not involved in any wrongdoing at HealthSouth and was, instead, a victim of a conspiracy by his managerial subordinates. *See id*. at *6.

While the government continued its investigation, plaintiffs filed a derivative action against Mr. Scrushy for unjust enrichment and equitable fraud in connection with the repayment of his $25 million loan. Plaintiffs argued that by repaying his loan in HealthSouth stock, Mr. Scrushy had implicitly represented to the company that HealthSouth's market price was a reliable indicator of the value of his shares. *See id*. at *1, 5. Because the market price for HealthSouth stock was based on information in the company's financial statements, plaintiffs argued that Mr. Scrushy had also implicitly represented that HealthSouth's financial statements were accurate. *See id*. The financial statements, however, were inaccurate and, as a result, plaintiffs claimed that the stock that Mr. Scrushy transferred to the company was worth substantially less than $25 million. *See id*. Consequently, plaintiffs alleged that Mr. Scrushy was unjustly enriched because he was able to retire his debt to HealthSouth "on the cheap." *Id.* at *5.

On plaintiffs' motion for summary judgment, the Court of Chancery held that Mr. Scrushy had been unjustly enriched. The Court explained that as the company's CEO, "[Mr.] Scrushy was the key executive at the company and was responsible to HealthSouth's Board for the accurate preparation of financial statements." *Id.* at *7. The Court found that regardless of whether Mr. Scrushy was actually involved in the fraud at HealthSouth, he failed to ensure that the company's financial statements were accurate and he was undoubtedly enriched when the company bought back shares from him at a price inflated by the false financial statements. *See id*. Accordingly, the Court concluded that Mr. Scrushy "should not, as a fiduciary, benefit at the expense of the object of his trust when his efforts [to ensure the accuracy of the financial statements] were insufficient." *Id.*

Further, the Court held that plaintiffs had established a claim for equitable fraud. The Court explained that by selling stock to the company, Mr. Scrushy had represented to HealthSouth "that the market price was a reliable way to value his shares, thereby vouching . . . for the integrity of the financial statements he had signed." *Id.* at *8. Mr. Scrushy's representations, however, were false and misleading because the company's financial statements were inaccurate and the market price was inflated. *See id*. Consequently, Mr. Scrushy received "unduly excessive value for his shares in the Buyback" and HealthSouth suffered injury. *Id.*

After determining that plaintiffs had established claims against Mr. Scrushy for unjust enrichment and equitable fraud, the Court granted HealthSouth rescissionary relief. Specifically, HealthSouth was ordered to return Mr. Scrushy's shares and, in exchange, Mr. Scrushy's $25 million loan was reinstated as an outstanding debt owed to the company. *See id*. at *10.

3. ***In re Abbott Labs. Derivative S'holders Litig.*, 325 F.3d 795 (7th Cir. 2003).**

Abbott Labs involved the issue of a director's liability for "conscious inaction" in the face of potentially illegal corporate activities. Shareholders of Abbott Laboratories ("Abbott") filed a derivative action against the company's board of directors claiming that the board breached its fiduciary duty of care by deliberately failing to take any corrective action in response to several warning letters from the Food and Drug Administration ("FDA").

Abbott was a diversified health care company that manufactured, among other things, diagnostic kits and devices. *See In re Abbott Labs. Derivative S'holders Litig.,* 325 F.3d 795, 799 (7th Cir. 2003).

These products are heavily regulated by the FDA. *See id*. During a six-year period from 1993 until 1999, Abbott received four formal warning letters from the FDA. *See id*. The letters specifically informed Abbott that some of its products were not in conformance with federal regulations and warned that: "[f]ailure to correct these deviations may result in regulatory action being initiated by the [FDA] without further notice . . . [t]hese actions include, but are not limited to seizure, injunction, and/or civil penalties." *Id.* (citations omitted). Despite receiving these letters, Abbott apparently did not take sufficient corrective action to fix the problems at its manufacturing facilities.

On November 2, 1999, Abbott signed a consent decree with the FDA as a direct result of the company's history of noncompliance. Under the decree, the company was prohibited from manufacturing certain diagnostic devices until independent experts and the FDA determined that Abbott had corrected the problems at its facilities. In addition, Abbott was required to pay a $100 million fine – the largest penalty ever imposed for a civil violation of FDA regulations at that time. Finally, Abbott was ordered to destroy certain inventories of diagnostic kits, which resulted in a loss of approximately $250 million in annual revenue. *See id*. at 801.

Plaintiffs filed a derivative action in the United States District Court for the Northern District of Illinois. According to plaintiffs' allegations, Abbott's directors knew about the FDA warning letters and potential penalties because: (1) Abbott's Chairman personally received three of the four warning letters; (2) Abbott's troubles with the FDA were widely reported in the media; and (3) several of the directors "signed SEC forms attesting to knowledge and responsibility for government regulation compliance". *See id*. at 808.

Despite being aware of the FDA violations and the potential penalties for noncompliance, the directors allegedly "took no steps in an effort to prevent or remedy the situation." *See id*. at 809.

Applying Delaware law, the District Court dismissed plaintiffs' complaint. In making its decision, the Court found that plaintiffs had asserted an "unconsidered failure to act" claim under *In re Caremark Int'l Inc. Derivative Litig*., 698 A.2d 959 (Del. Ch. 1996). *See Abbott*, 325 F.3d at 804-805. Accordingly, the Court applied the demand futility test for claims of corporate "omissions" under *Rales v. Blasband*, 634 A.2d 927 (Del. 1993). *See Abbott*, 325 F.3d at 804. The District Court held that plaintiffs had failed to sufficiently allege demand futility under *Rales*.

Plaintiffs appealed and the Seventh Circuit reversed the District Court's decision. *See id.* at 798-99. Specifically, the Circuit Court found that the District Court erred in concluding that plaintiffs had asserted a claim under *Caremark*. *See id.* at 806. A *Caremark* claim, the Circuit Court explained, is based on allegations that the defendants *did not know, but should have known*, about corporate wrongdoing. *See id.* at 805-806. The Court pointed out that plaintiffs in Abbott had repeatedly alleged in their complaint that the defendants *did know* about the company's problems with the FDA, but *deliberately* refrained from taking corrective action. *See id*. at 806. Consequently, the Court concluded that plaintiffs asserted a conscious board decision and, therefore, the *Aronson* test for demand futility was the appropriate standard. *See id.* at 806-807.

Additionally, the Circuit Court held that plaintiffs had sufficiently alleged demand futility under *Aronson*. Curiously, however, the Court also found that plaintiffs had established a lack of good faith under *Caremark*. *See id.* at 808-809. The Court stated that under the *Caremark* decision, "'a sustained or systematic failure of the Board to exercise oversight . . . will establish the lack of good faith that is a necessary condition to [director] liability.'" *Id.* at 808 (*quoting Caremark*, 698 A.2d at 971). The Court then concluded that the magnitude and duration of the FDA violations demonstrated a "sustained and systematic" failure of the Abbott board to exercise oversight. *Abbott*, 325 F.3d at 809.

Finally, the Circuit Court rejected defendants' argument that plaintiffs' claims must be dismissed in light of the clause in Abbott's certificate of incorporation that exempted directors from liability for duty of care violations. After reviewing Abbott's certificate, the Court found that the exemption clause applied only to "good faith" breaches of fiduciary duty. Because plaintiffs had alleged that the directors "intentionally" failed to address federal violations problems, the Court ruled that defendants' conduct fell outside of the exemption provision. *See id*. at 809-811.

c. <u>Advancement of Legal Expenses</u>

1. ***Bergonzi v. Rite Aid Corp.*, No. Civ.A. 20453-NC, 2003 WL 22407303 (Del. Ch. Oct. 20, 2003):**

Bergonzi involved a dispute over whether Rite Aid Corporation ("Rite Aid" or the "Company") was obligated to continue advancing legal expenses to Frank Bergonzi, the Company's former Chief Financial Officer, after Mr. Bergonzi admitted under oath that he had participated in a conspiracy to defraud Rite Aid. In that case, the SEC and a federal grand jury began investigating Mr. Bergonzi during 1999 in connection with Rite Aid's allegedly improper accounting practices. To defend himself in these proceedings, Mr. Bergonzi retained his own legal counsel and accounting experts. Mr. Bergonzi then sought to have Rite Aid advance him the costs of his defense. *See Bergonzi v. Rite Aid Corp.,* No. Civ.A. 20453-NC, 2003 WL 22407303, at *1 (Del. Ch. Oct. 20, 2003).

At that time, Article Tenth of Rite Aid's Restated Certificate of Incorporation (the "Charter"), provided its directors and officers with the following indemnification and advancement rights:

> The right to indemnification [ ] shall be a contract right and shall include the right to be paid by the corporation the expenses incurred defending any such proceeding in advance of its final disposition; provided, however, that if the [Delaware] General Corporation Law requires, the payment of such expenses . . . shall be made only upon delivery to the corporation of an undertaking . . . to repay all amounts so advanced if it shall ultimately be determined that such director or officer is not entitled to be indemnified.

Id. at *1 (citation omitted). While Article Tenth of the Charter also permitted Rite Aid's officers and directors to bring an action against the company if Rite Aid refused to advance their legal expenses, it expressly provided that:

> It shall be a defense to any such action (other than an action brought to enforce a claim for expenses

> incurred in defending any proceeding in advance of its final disposition where the required undertaking, if any is required, has been tendered to the corporation) that the [officer or director] has not met the standards of conduct which make it permissible under the [Delaware] General Corporation Law for the corporation to indemnify the [officer or director] for the amount claimed.

Id. (citation omitted). In accordance with the Charter, Rite Aid began advancing legal expenses to Mr. Bergonzi after he executed two "forms of undertaking" during 1999. *Id.*

On June 21, 2002, Mr. Bergonzi was indicted by a federal grand jury and accused of participating in a criminal conspiracy to defraud Rite Aid. On June 5, 2003, Mr. Bergonzi pled guilty to these charges and admitted that he had, *inter alia*, deliberately filed false financial statements while serving as Rite Aid's CFO. Following the entry of his guilty plea, Rite Aid informed Mr. Bergonzi that it would no longer advance him the costs of his defense. *See id.* at *2.

Shortly thereafter, Mr. Bergonzi filed an advancement action against Rite Aid, claiming that the entry of his guilty plea did not terminate his right to advancement under the Charter. In response, Rite Aid filed a counterclaim seeking repayment of the amounts that it had previously advanced to Mr. Bergonzi. Rite Aid argued that Mr. Bergonzi's guilty plea constituted an "ultimate determination" that he was not entitled to indemnification under Delaware law. Accordingly, Rite Aid claimed that Mr. Bergonzi's plea cut off his right to any future advancement and triggered his obligation to repay the amounts that had already been advanced. *See id.* at *1-3.

The Court of Chancery dismissed Rite Aid's counterclaim, holding that the entry of Mr. Bergonzi's guilty plea did not terminate his right to advancement. *See id.* at *2. Under Rite Aid's Charter, the Court explained, Mr. Bergonzi was entitled to advancement of his legal expenses until the criminal proceeding reached a "final disposition." *Id.* The Court pointed out that when Rite Aid filed its counterclaim, Mr. Bergonzi had pled guilty in the criminal proceeding, but was still awaiting sentencing. *See id.* Because "the entry of a guilty plea, before sentencing, is *not* a final disposition," the Court concluded that the criminal proceeding had not yet reached a final disposition and, therefore, Mr. Bergonzi still had a right to advancement under Rite Aid's Charter. *Id.* (emphasis in original).

Further, the Court dismissed Rite Aid's counterclaim on the ground that it was not ripe for adjudication. *See id.* at *3. The Court explained that although Rite Aid was permitted by its Charter to deny an indemnification claim when the officer or director "ha[d] not met the standards of conduct which make [indemnification] permissible under the [Delaware] General Corporation Law," Rite Aid was expressly prohibited from asserting this defense in "*an action brought to enforce a claim for expenses incurred in defending any proceeding in advance of its final disposition*." *Id.* at *3 (emphasis in original). Because Mr. Bergonzi's criminal proceeding had not yet reached a final disposition, the Court found that the plain language of Rite Aid's own Charter barred the counterclaim. *See id.* Accordingly, the Court concluded that "[t]he controversy regarding [Mr.] Bergonzi's right to indemnification 'ha[d] not yet matured to a point where judicial action [wa]s appropriate.'" *Id.* at *4 (*quoting Stroud v. Milliken Enters., Inc.*, 552 A.2d 476, 480 (Del. 1989)).

d. <u>Corporate Control Transactions</u>

1. ***In re Cysive, Inc. S'holders Litig.*, 836 A.2d 531 (Del. Ch. 2003).**

Cysive involved a dispute over a proposed merger between Cysive, Inc. and Snowbird Holdings, Inc. ("Snowbird"), an entity controlled by Nelson Carbonell, Cysive's Chairman, Chief Executive Officer, and largest shareholder. On April 24, 2003, Mr. Carbonell informed the company's board of directors that he would make an offer to purchase the Cysive shares that he did not own. *See In re Cysive, Inc. S'holders Litig.,* 836 A.2d 531, 540-41 (Del. Ch. 2003). At the time, Mr. Carbonell personally held 36% of Cysive's outstanding shares and his "close managerial-subordinate" and family members collectively held another 4% of the company's stock. *See id. at* 535.

Prior to Mr. Carbonell's announcement, Cysive's business was failing and the board of directors was aggressively marketing the company to potential acquirors. As of March 2003, however, no one had expressed any serious interest in acquiring or merging with Cysive. *See id*. at 537-40.

On April 25, 2003, the Cysive board, which was comprised of three independent directors and two "interested" directors, formed a special committee (the "Committee") to evaluate Mr. Carbonell's proposed offer to purchase Cysive. *See id*. at 541-43. The Committee was comprised solely of independent directors and was granted full authority to negotiate with Mr. Carbonell on Cysive's behalf. *See id*. at 536, 541-42, 554.

On April 30, 2003, Mr. Carbonell officially offered to acquire Cysive by way of a merger transaction with Snowbird, Mr. Carbonell's acquisition vehicle. This offer stimulated new interest in Cysive. Indeed, several companies suddenly approached Cysive and entered into negotiations with the Committee. The Committee used this development to benefit Cysive's shareholders by convincing Mr. Carbonell to increase his bid for Cysive and lower the termination fee under the proposed merger agreement. *See id*. at 543.

In May 2003, the Committee and Cysive's full board approved the Snowbird merger. The Committee, however, refused to agree to a "no-shop" provision and continued to entertain inquiries from interested bidders *after* signing the merger agreement. *See id*. at 543, 545-46.

Before approving the Snowbird merger, Cysive had contacted thirty-seven potential acquirors and not one had made a bid that was comparable to Mr. Carbonell's offer. *See id*. at 545. In addition, the Committee had met a total of twenty-one times and "undert[aken] a process that was thorough and reasonably designed to obtain the best deal for Cysive's public stockholders." *Id.* at 546.

Nevertheless, several of Cysive's minority shareholders filed an action against Snowbird, Mr. Carbonell, and the remaining members of Cysive's board of directors seeking to enjoin the merger. Plaintiffs claimed that the merger was procedurally and financially unfair due to the "deficiencies" in the Committee's operation. Moreover, plaintiffs argued that Mr. Carbonell was a "controlling stockholder" of Cysive and, thus, the merger was subject to an entire fairness review under *Lynch*. *See id*.

The defendants, on the other hand, argued that the *Lynch* doctrine did not apply because Mr. Carbonell was not a controlling shareholder. According to the defendants, Mr. Carbonell held (at most) 40% of Cysive's stock. Therefore, Mr. Carbonell was not a controlling shareholder because he simply did not have control over a majority of the company's voting power. In the alternative, the defendants claimed that they had satisfied the entire fairness standard under *Lynch*. *See id.* at 547, 552.

The Court of Chancery denied plaintiffs' request to enjoin the merger. The Court began its opinion by determining the correct standard of review. While acknowledging that Mr. Carbonell did not have a majority ownership interest in Cysive, the Court found that this did not resolve the issue of whether he was a controlling shareholder for purposes of *Lynch*. Instead, the Court determined that “the analysis of whether a controlling stockholder exists must take into account whether the stockholder, as a practical matter, possesses a combination of stock voting power and managerial authority that enables him to control the corporation, if he so wishes.” *Id.* at 553. The Court stressed that this "practical" analysis is "intensely factual" and, thus, "the question of whether a large block holder is so powerful as to have obtained the status of a 'controlling stockholder' . . . is a difficult one to resolve on the pleadings." *Id.* at 550-51.

Applying a "practical" analysis, the Court held that Mr. Carbonell was a controlling shareholder and the merger was, therefore, subject to entire fairness review under *Lynch*. *Id.* at 551-53. The Court explained that even though Mr. Carbonell did not control a majority of the company's voting power, he did control "a large enough block of stock to be the dominant force in any contested Cysive election." *Id.* at 551-52. The Court emphasized that Mr. Carbonell was the “Chairman and CEO of Cysive, and a hands-on one, to boot." *Id.* at 552. Thus, the Court concluded that Mr. Carbonell had the "capability" to control Cysive.

Significantly, however, the Court found that the defendants had satisfied the exacting entire fairness standard of review, in large part because:

- Cysive's decision to enter into the Snowbird merger was preceded by "an active and aggressive search for a third-party buyer";
- Cysive formed a special immediately after receiving Mr. Carbonell's initial offer;
- The Committee was given full authority to negotiate with Mr. Carbonell and actually did negotiate with Mr. Carbonell;
- The Committee continued to entertain inquiries from third-party bidders even after Cysive signed the merger agreement with Snowbird;
- The presence of an independent majority on Cysive's board of directors; and
- The absence of another party willing to make a higher bid.

See id. at 553-55.

Consequently, the Court concluded that the Snowbird merger was procedurally and financially fair under *Lynch* and the plaintiffs' request to enjoin the merger was denied. *See id.* at 557-58.

2. *In re The MONY Group S'holders Litig.,* C.A. No. 20554, 2004 Del. Ch. LEXIS 16 (Del. Ch. February 18, 2004).

MONY involved a challenge to the proposed stock-for-stock merger of MONY Group, Inc ("MONY") with AXA Financial ("AXA"). In November 2002, MONY's board had authorized its CEO to begin exploring strategic alternatives. In September 2003, MONY signed a definitive agreement to merge with AXA. The merger agreement contained a non-solicitation provision with a broad fiduciary out clause, as well as a termination fee equal to 2.4% of the transaction value in the event of termination of the merger agreement for a superior proposal. During the five-month period between the announcement of the AXA-MONY transaction and the lawsuit, no third party made a competing proposal for MONY.

Plaintiff's suit alleged that MONY's board violated its *Revlon* duties by (i) delegating to the company's CEO the responsibility for negotiating the merger with AXA, and (ii) not taking adequate steps to ensure that the AXA deal was the best transaction reasonably available for MONY's shareholders. The plaintiff also challenged the termination fee in the merger agreement on the grounds that it rendered any post-agreement market check impractical because of its size.

The Court denied plaintiffs' *Revlon* claims in their entirety. The Court began by noting that *Revlon* and its progeny do "not demand that every change in control of a Delaware corporation be preceded by a heated bidding contest." *See In re The MONY Group S'holders Litig.,* C.A. No. 20554, 2004 Del. Ch. LEXIS 16, at *15 (Del. Ch. Feb. 18, 2004) (citation omitted). Rather, the Court reiterated long-standing Delaware law that when deciding how to sell a company,

> [t]he board of directors is the corporate decision making body best equipped to make these judgments. Accordingly, a court applying enhanced judicial scrutiny should be deciding whether the directors made a reasonable decision, not a perfect decision. If a Board selected one of several reasonable alternatives, a court should not second-guess that choice even though it might have decided otherwise or subsequent events may have cast doubt on the Board's determination.

Id. at *17.

The Court found that the MONY board acted reasonably in its process and decisions. The Court initially noted that the board was comprised of financially sophisticated members who were fully informed about the negotiations, and throughout the process had been repeatedly briefed about the company and its strategic alternatives. The Court then held that the board had engaged an investment banker for additional advice, that the banker had provided a fairness opinion and was incentivized to obtain the highest price as a result of its engagement letter, and that the business fit between AXA and MONY made it likely that AXA would be the high bidder. The Court concluded by holding that at "the root of a judicial inquiry into whether a board met its *Revlon* duties is whether the Board acted *reasonably* . . . . [T]he record certainly supports a conclusion that the Board acted reasonably, especially given Board knowledge that there would be a substantial opportunity for an effective market check after the Agreement was announced." *Id*. at *26-27 (emphasis in original).

Cysive and *MONY* demonstrate again the importance of creating a sufficient record to determine the Board's process and rationale when engaging in any transaction. In both cases, the defendants were able to demonstrate that they were informed and active participants in the process through the use of minutes and other corporate records. In this age of heightened skepticism about the motives and even, on occasion, the wisdom of certain actions by corporate executives and boards, it is more important than ever to ensure that the proper records are maintained.