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The Business Judgment Rule: How Much Board Deliberation is Enough When a Board is Under Time Constraints?-Citron v. Fairchild Camera and Instrument Corp.

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The Business Judgment Rule: How Much Board Deliberation is Enough When a Board is Under Time Constraints? —*Citron v. Fairchild Camera and Instrument Corp.*[1]

I. INTRODUCTION

In the past six years the protection provided by the business judgment rule to a corporation's board of directors in takeover situations has been questioned and eroded. Beginning with *Smith v. Van Gorkom*,[2] courts have heightened the standard of review for determining whether the business judgment rule protects a board's actions taken during a takeover attempt. This has evoked considerable concern and uncertainty among boards of directors. *Citron v. Fairchild Camera and Instrument Corp.*[3] clarified that time constraints placed on a board of directors in takeover situations do not necessarily diminish the likelihood that the business judgment rule will protect the board's decisions from judicial scrutiny. The amount of deliberation required of a rushed board depends upon the specific circumstances.

This note will evaluate existing law regarding the application of the business judgment rule to a board's actions in takeover situations, particularly what the extent of its deliberations should be when it is placed under time constraints. The note will also discuss factors a court might consider in determining whether the business judgment rule will protect a board's rushed decision.

II. BACKGROUND

The business judgment rule is

> a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good

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1. 569 A.2d 53 (Del. 1989).
2. 488 A.2d 858 (Del. 1985).
3. 569 A.2d at 67.

> faith and in the honest belief that the action taken was in the best interests of the company. Absent an abuse of discretion, that judgment will be respected by the courts. The burden is on the party challenging the [board's] decision to establish facts rebutting the presumption.[4]

The rule is "an extension of the fundamental principle 'that the business and affairs of a corporation are managed by and under the direction of its board.' "[5] Since the board, not the shareholders, is given control over the corporation, the rule provides that the board's decisions, made in good faith, should not be second-guessed by the courts.

Traditionally, the rule applied "so long as (1) there was no self-dealing or conflict of interest; (2) the board actually addressed and decided the issue, rather than neglecting it; (3) the board members properly informed themselves prior to reaching a decision; and (4) the board's actions were not completely unjustifiable or irrational."[6]

Four justifications are advanced for the business judgment rule. First, without it, competent individuals would be unwilling to assume the risks of directorships. Second, it allows directors the broad discretion needed to operate a company without fear of judicial second-guessing. Third, it prevents a court from examining decisions it is ill-equipped to evaluate. And fourth, it ensures that directors, rather than shareholders, will control the corporation.[7]

In the past five years, however, the protection afforded to a board's decisions by the business judgment rule in takeover contexts has been substantially eroded.[8] Several reasons for

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4. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (holding that shareholders failed to allege facts sufficient to create a reasonable doubt as to the applicability of the business judgment rule to the board's decision to enter into certain transactions, including a lifetime salary with a 47% shareholder) (citing Kaplan v. Centex Corp., 284 A.2d 119, 124 (Del. Ch. 1971); Puma v. Marriot, 283 A.2d 693, 695 (Del. Ch. 1971); Robinson v. Pittsburg Oil Refining Corp., 126 A. 46 (Del. Ch. 1924)).

5. *Citron*, 569 A.2d at 64 (quoting Pogostin v. Rice, 480 A.2d 619, 624 (Del. 1984)).

6. Jonathon R. Macey & Geoffrey P. Miller, Trans Union *Reconsidered*, 98 YALE L.J. 127, 131 (1988).

7. Dennis J. Block et al., *The Role of the Business Judgment Rule in Shareholder Litigation at the Turn of the Decade*, 45 BUS. LAW. 469, 490 (1990); *see also* Mark J. Loewenstein, *Toward an Auction Market for Corporate Control and the Demise of the Business Judgment Rule*, 63 S. CAL. L. REV. 65, 70 (1989).

8. Michael J. Fricklas & Robert C. Lewis, *Obligations and Responsibilities of Directors of Public Companies in Responding to Takeover Bids*, *in* ACQUISITIONS &

this erosion are offered. First, since the sale of a company is such an important event to any business, it "perhaps inherently deserves closer judicial scrutiny."[9] Second, although the director's own financial interest in retaining her position on the board is not considered sufficient to disqualify her from the protection of the business judgment rule, "the courts nevertheless analyze change of control cases with a heightened skepticism; they tend to scrutinize the board's reasoning for signs of a bunker mentality or undue favoritism for management's recommended course of action."[10] Finally, due to the wide-felt financial impact of takeovers, courts tend to closely scrutinize a board's decisions because of the likelihood that the court's own decision will be heavily scrutinized not only on appeal, but also by the media, the legislature, and the general and legal public.[11]

In *Smith v. Van Gorkom*,[12] the normally predictable, traditionally pro-management Delaware Supreme Court shocked the corporate bar by finding that the business judgment rule would not be available to protect the Trans Union board of directors' decision to approve a cash-out merger at a price fifty percent above the market, under a three-day deadline, made "upon two hours' consideration, without prior notice, and without the exigency of crisis or emergency."[13] The board made the decision thirty-six hours before the expiration of the deadline with hardly any prior deliberation.[14] The court held that due to its failure to adequately deliberate the board failed to exercise its duty of care to shareholders, and thus that the board members were personally liable for the difference (nearly $24 million) between the judicially determined fair market value of the shares and the price paid for the shares in

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MERGERS 1989, at 469 (PLI Corp. L. & Prac. Course Handbook Series No. 652, 1989).

9. *Id.* at 474.

10. *Id.* The Delaware Supreme Court noted that in takeover contexts "[b]ecause of the omnipresent specter that a board may be acting primarily in its own interest, rather than those of the corporation and its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protection of the business judgment rule may be conferred." Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985); *see also* Gary P. Kreider, *Corporate Takeovers and the Business Judgment Rule: An Update*, 30 CORP. PRAC. COMMENTATOR 119, 123 (1988).

11. Fricklas & Lewis, *supra* note 8, at 474.

12. 488 A.2d 858 (Del. 1985).

13. *Id.* at 874.

14. *Id.* at 877.

the merger.[15]

Smith created considerable confusion about application of the business judgment rule to a board's decisions made in takeover situations.[16] *Citron* clarified the degree of deliberation necessary when a board is placed under time constraints in a takeover situation.

III. FACTS OF *CITRON*

In *Citron*,[17] the court found that the Fairchild Camera & Instrument Corporation ("Fairchild") board of directors' decision to accept an all-cash, all-shares offer imposed under a three-hour deadline was entitled to the protection of the business judgment rule. The sale occurred after the Fairchild board had been considering the possibility of selling the company for two years.[18] The board was composed predominantly of outside directors who were experienced businessmen.[19] Gould, Inc. ("Gould") in a hostile takeover battle had made a tender offer. Schlumberger Inc. ("Schlumberger") then emerged as a "white knight," willing to buy Fairchild in order to ward off the unwanted bidder. Gould then offered $70.00 per share for forty-five percent of the shares, but was unclear as to what price would be paid for the remaining shares.[20] On the following day, Schlumberger submitted a $66.00, all-cash, all-shares bid, conditioned upon acceptance within four hours. The board convened for three

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15. *Id.* at 893.

16. *See* Macey & Miller, *supra* note 6; Eric A. Chiappinelli, Trans Union *Unreconsidered*, 15 J. CORP. L. 27 (1989). Macey and Miller argue that *Van Gorkom* actually increases a board's power in takeover situations by allowing it to mask its refusal of an unwanted rush offer under the guise that it has no time to inform itself of relevant information, while allowing it to accept desirable rush offers by merely leaving a paper trail indicating careful discussion of the pros and cons of the offer and arranging for a speedy, favorable valuation. Macey and Miller fail to acknowledge the fact that the Trans Union board, being uninformed as to the company's value and uninformed as to the specifics of the proposed merger agreement (none of the board had even read it before approving it—and Macey and Miller excuse this by asserting that even had they read it, they would not have understood it because most legal documents are too complicated to understand), made a monumentally critical decision in the life of the corporation in only two hours of deliberation when 36 hours remained before the offer expired. *Citron* seems to indicate that had the Trans Union board used the time and information reasonably available to it, director liability would not have been imposed.

17. 569 A.2d 53 (Del. 1989).

18. *Id.* at 67.

19. *Id.* at 56.

20. *Id.* at 61.

hours and, after extensive consideration of both offers, approved the sale to Schlumberger minutes before the deadline.[21] Edith Citron, a shareholder of Fairchild, brought an action against Fairchild's former board of directors for breach of its fiduciary duty and gross negligence in its sale of Fairchild to Schlumberger.[22] She claimed that the directors failed to exercise due care in adhering to the four-hour deadline because they "failed to act in an informed manner as required under *Smith v. Van Gorkom*."[23]

IV. REASONING

In finding that Fairchild's board was entitled to the protection of the business judgment rule, the *Citron* court focused on the "board's decision-making process," looking for "evidence as to whether the board [had] acted in a deliberate and knowledgeable way in identifying and exploring alternatives."[24]

The court found "ample evidence in the record of the board's involvement."[25] Although the board did accede to Schlumberger's four-hour deadline, the court distinguished this case from *Smith*.[26] Fairchild's board, as opposed to Trans Union's board, had been "considering the possibility that the company might be sold for two years prior to receipt of Gould's

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21. *Id.* at 62-63.
22. *Id.* at 54.
23. *Id.* at 66 (citations omitted).
24. *Id.* Some argue that this type of judicial scrutiny of a board's business decision is exactly what the business judgment rule was meant to avoid. Indeed, it seems that in evaluating the board's decision-making process to determine whether a board's decision falls within the ambit of the business judgment rule and deserves not to be second-guessed by courts, courts *are* second-guessing the business judgments of boards. The takeover cases indicate "that courts are willing to immerse themselves in the deliberative process to determine 'what didn't the directors know and why they didn't know it.'" Fricklas & Lewis, *supra* note 8, at 542. With all the information before it, courts are

> sorely tempted to pose the questions which they believe a reasonable, prudent director should have asked . . . .
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> . . . Thus, in most fact settings involving takeover bids, the traditional formulation of the business judgment rule is ancient history—at least in this context, courts now directly address the business rationale and reasonableness of director's decisions.

Id. at 542, 544.
25. *Citron*, 569 A.2d at 66.
26. *Id.* at 67.

unsolicited first proposal."[27] Furthermore, the board had received a large amount of outside investment advice, was well aware of the company's value, and had discussed the sale of the company at several prior meetings.[28] In light of these facts, the Delaware Supreme Court agreed with the lower court that the board "knew enough" at the time of the deadline "concerning the value of the company to make a rational choice with respect to the two offers."[29] The lower court had found:

> [A]n arm's-length adversary imposed a time limit under the threat of losing its proposal. The board believed that risk to be real . . . . [W]here a disinterested board in good faith considers the significance of the decision called for, the available information of which it and its advisors are aware and the time constraints imposed upon it, and in those circumstances, the board makes a decision that it *is* in the best interests of the corporation to act, that decision itself is entitled to the benefits of the business judgment rule.
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> These circumstances all appear from the evidence in this case. The board had a deadline imposed upon it; it clearly knew enough . . . concerning the value of the Company to make a rational choice with respect to the matter before it. I could not conclude that it acted negligently in any respect.[30]

The Delaware Supreme Court affirmed, stating:

> The imposition of artificial time limits on the decision-making process of a board of directors may compromise the integrity of that deliberative process. *See Van Gorkom*. However, whether the constraints are self-imposed or attributable to bargaining tactics of an adversary seeking a final resolution to a belabored process must be considered. Boards that have failed to exercise due care are frequently boards that have been rushed. We conclude that the time constraints placed on the Fairchild board were not of the board's making and did not compromise its deliberative process . . . .[31]

Thus, the Deleware Supreme Court clarified that time deadlines in rush offer situations do not create an impossible dilemma for boards of directors. The business judgment rule

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27. *Id.*
28. *Id.*
29. *Id.*
30. Citron v. Fairchild Camera and Instrument Corp., [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,915, at 90,103-04 (Del. Ch. May 19, 1988).
31. *Citron*, 569 A.2d at 67.

will likely protect a board's rushed decision from judicial scrutiny where it uses the time it has to consider its options carefully.

V. ANALYSIS

Time deadlines imposed by both hostile and friendly takeover bidders pose a difficult dilemma for the target's board of directors. If the board accepts the rush bid, it essentially forecloses the opportunity for an auction to develop, thus depriving shareholders of an opportunity to obtain a substantially higher price. This can result in board liability. On the other hand, if the board rejects the rush bid or refuses to act within the deadline, it might lose the bid; due to the deadline, it might have no time to assure that a higher bidder will appear if the other bidder drops out. This can also result in board liability.[32] Courts, however, are not blind to this dilemma. For example, the *Smith* court noted that it is "a fact of corporate life that today when faced with difficult or sensitive issues, directors often are subject to suit, irrespective of the decisions they make."[33] But this does not mean the board will be liable. Although a suit might result, "Delaware law makes clear that a board *acting within the ambit of the business judgment rule* faces no ultimate liability."[34] The ultimate issue, then, is what actions make it more or less probable that a board is acting within the ambit of the business judgment rule when making a rushed decision during a takeover attempt?

The *Smith* court did not establish an impossible dilemma for boards in a rush offer situation, nor did it impose a meaningless ritual which every board must follow during a takeover situation in order to assure the protection of the business judgment rule. *Smith* simply requires that board members "inform[] themselves as to all information that [is] reasonably available to them."[35] Under this standard, it was clear to the *Smith* court that Trans Union's board had failed to make an informed business judgment, given the amount of time it had to do so. In determining whether the board had made a reasonable effort to evaluate the value of the company,

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32. *See* Macey & Miller, *supra* note 6, at 136.
33. Smith v. Van Gorkom, 488 A.2d 858, 881 (Del. 1985).
34. *Id.* (emphasis added) (citing Pogostin v. Rice, 480 A.2d 619 (Del. 1984)).
35. *Id.* at 877.

the court noted that the board could have done much more in the time it had than merely rely on its Chief Financial Officer's "elicited response that the [price] was within a 'fair price range' within the context of a leveraged buy-out."[36] The court stated:

> No director sought any further information from [the C.F.O.]. No director asked him why he put [the proposed merger price] at the bottom of his range. No director asked [the C.F.O.] for any details as to his study, the reason why it had been undertaken or its depth. No director asked to see the study; and no director asked [the C.F.O.] whether Trans Union's finance department could do a fairness study within the remaining 36-hour period available under the . . . offer.[37]

The court strongly implied that had the board used the remaining thirty-six hours to at least make an attempt at valuing the company, the outcome may have been different:

> None of the directors, Management or outside, were investment bankers or financial analysts. Yet the board did not consider recessing the meeting until a later hour that day (or requesting an extension of . . . [the] deadline) to give it time to elicit more information as to the sufficiency of the offer, either from inside Management . . . or from Trans Union's own investment banker . . . whose Chicago specialist in merger and acquisitions was known to the Board and familiar with Trans Union's affairs.[38]

Citron confirms the *Smith* court's implication that an incumbent board facing a rush bid situation need not always refuse the rush bid because it has no time to make an informed judgment. In *Citron*, the board had only three hours to consider the proposal and yet was still entitled to the protection of the business judgment rule. The rule merely requires that a board, when faced with a rush offer, should know enough "concerning the value of the company to make a rational choice."[39] The court noted that "imposition of artificial time limits on the decision-making process of a board of directors may compromise the integrity of that deliberative process."[40]

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36. *Id.*
37. *Id.*
38. *Id.* at 877-78.
39. Citron v. Fairchild Camera and Instrument Corp., 569 A.2d 53, 67 (Del. 1989).
40. *Id.*

However, depending upon a variety of factors, the board may choose to be rushed. Clearly no set formula exists: "There is no ritual in these matters with which thoughtless compliance will assure later judicial approval or from which thoughtful deviation will risk automatic judicial censure."[41]

However, recent cases reveal a number of factors which may be relevant to a court's decision regarding the applicability of the business judgment rule to a board's decisions in rushed takeover situations. Courts might consider (1) whether the board used the time available to consider its options carefully; (2) whether the deadline was self-imposed; (3) the emergency-like nature of the situation; (4) the extent of prior deliberations; (5) the extent of outside counsel sought and obtained; (6) the composition of the board; (7) the possible consequences of disregarding the deadline; and (8) the possibility of better offers in the future.

A. Use of Available Time

In rush offer situations courts are likely to consider how effectively the board used its allotted time as well as how much of the allotted time the board effectively used, in determining whether a board's decision is entitled to the business judgment rule's protection. For example, in *British Printing & Communication Corp. v. Harcourt Brace Jovanovich, Inc.*,[42] the court found that the incumbent board, in responding to an acquisition proposal, had not breached its duty of care by refusing to negotiate with the offeror. The court reasoned that because the board met five times over the available six days to consider and review the proposal, it had used "the available time to consider its options carefully."[43] Similarly, in *Samjens Partners I v. Burlington Industries, Inc.*,[44] the court held that the business judgment rule applied to protect the board's decision where the board had acted under time pressure imposed by both a hostile offeror and a white knight and used the two available days to negotiate and vigorously bargain.[45] As noted above,[46] had the

41. Citron v. Steego Corp., 14 DEL. J. CORP. L. 634, 648 (Del. Ch. 1988).
42. 664 F. Supp. 1519 (S.D.N.Y. 1987).
43. *Id.* at 1530.
44. 663 F. Supp. 614 (S.D.N.Y. 1987).
45. *Id.* at 625.
46. *See supra* text accompanying notes 36-39; Citron v. Fairchild Camera and Instrument Corp., 569 A.2d 53 (Del. 1989).

Trans Union board used the remaining thirty-six hours available to consider its options and further evaluate the company's intrinsic value, the court would have likely found that it satisfied its duty of care—even if it did approve the merger.

However, a board need not always delay its decision, even if it can. In *Keyser v. Commonwealth National Financial Corp.*,[47] the court noted that even if the board could have taken more time to deliberate, where it had already spent substantial time considering the offer, failure to take more time "does not amount to a breach in fiduciary duty nor does it equate the action the directors did take as unreasonable or in error."[48]

B. Self-Imposed Nature of Deadline

Courts might also consider whether the deadline was self-imposed. As the *Citron* court noted, "[W]hether the constraints are self-imposed or attributable to bargaining tactics of an adversary seeking a final resolution to a belabored process must be considered."[49] In *Hansen Trust PLC v. ML SCM Acquisition, Inc.*,[50] the court found that a board's rushed decision to grant a lock-up option to a third party in defense to a hostile takeover attempt "strongly suggest[s] a breach of . . . duty" where the decision was made in a three-hour, late-night meeting and the board had not been reasonably informed of the value of the two businesses involved in the lock-up.[51] The court noted that no outside force had imposed any deadline which created an "emergency need for a hasty decision . . . . The directors manifestly declined to use 'time available for obtaining information' that might be critical, given 'the importance of the business judgment to be made.' "[52]

Similarly, in *Tomczak v. Morton Thiokol, Inc.*,[53] the court found that reasonable doubt (sufficient to excuse the plaintiff's failure to make pre-suit demand) existed as to whether the business judgment rule would protect the board's rushed decision to sell some of its assets. "[A]lthough there was no emer-

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47. 644 F. Supp. 1130 (M.D. Pa. 1986).
48. *Id.* at 1149.
49. 569 A.2d 53, 67 (Del. 1989).
50. 781 F.2d 264 (2d Cir. 1986).
51. *Id.* at 275.
52. *Id.* (quoting PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 4.01, at 66 (Tent. Draft No. 4, 1985)).
53. 12 DEL. J. CORP. L. 381 (Del. Ch. 1986).

gency requiring the Board to reach an immediate decision,"[54] it made its decision to sell the assets after a fifteen to twenty-minute meeting, with little prior deliberation or consideration, no inquiry into the methods used to value the assets when reports were readily available, and no inquiry into the interest other companies may have had in the assets nor into why higher offers were not sought.[55] As the above cases show, courts are reluctant to afford a board's rushed decision the protection of the business judgment rule when the time limit is self-imposed.

C. Emergency-Like Nature of Situation

In addition to considering whether the deadline was self-imposed, courts also might consider whether there is a legitimate need to rush. In *Keyser v. Commonwealth National Financial Corp.*,[56] the court noted that the defendant's rushed decision to grant a lock-up option was protected by the business judgment rule partially because such transactions, "for security reasons,"[57] often must occur very quickly in the banking industry.[58]

In contrast, the *Smith* court noted that the board's decision in that case was made without any emergency need.[59] Similarly, in *In re NVF Company Litigation*,[60] the court refused to dismiss a derivative suit alleging that the board failed to exercise due care when it decided to sell the company's most valuable asset in a ten-minute "emergency" meeting. The sale proceeds were to pay off a loan which had been in default for five months. The court found that:

> An emergency so pressing as to preclude all discussion is imaginable, I suppose, and might in certain conceivable circumstances yield a different result. Here the emergency was the result of a two year old loan. More than five months before the emergency . . . the loan had been declared in default. Although the default had been forestalled, the . . . loan situation had to be an ongoing concern.[61]

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54. *Id.* at 384.
55. *Id.* at 384, 386.
56. 644 F. Supp. 1130 (M.D. Pa. 1986).
57. *Id.* at 1147.
58. *Id.*
59. Smith v. Van Gorkom, 488 A.2d 858, 874 (Del. 1985).
60. No. CIV.A.90-50, 1989 WL 146237 (Del. Ch. Nov. 22, 1989).
61. *Id.* at *5.

Thus, although a court will consider whether an emergency situation forced a somewhat uninformed decision, it might also consider whether that emergency was foreseeable and whether it was self-created.

D. Extent of Prior Deliberations

The likelihood that a board's rushed decisions will be protected by the business judgment rule is also enhanced if the board spends time prior to the rushed situation—particularly when it senses that a hostile takeover may be in the making—deliberating over share and asset values and possible future transactions. For example, in *Keyser v. Commonwealth National Financial Corp.*,[62] the court noted that prior to the board's rushed decision to enter into a merger agreement it had "been discussing potential merger partners for close to a year,"[63] had become "fairly familiar with merger discussions and its [sic] intricacies,"[64] and the "terms and conditions of merger proposals from [the hostile offeror] were very familiar to the directors by the time they met" to make the final decision.[65] *Keyser* demonstrates that a board's pre-rush situation deliberations regarding a potential takeover may influence a court's decision regarding applicability of the business judgment rule to the board's rushed decision.

E. Use of Outside Counsel and Financial Advisors

Another factor which may bear upon the court's conclusion as to whether the business judgment rule will apply is the extent of outside counsel and financial advice sought and obtained.[66] For example, in *Keyser*,[67] a critical factor in the

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62. 644 F. Supp. 1130 (M.D. Pa. 1986).
63. *Id.* at 1148.
64. *Id.*
65. *Id. See also* Terrydale Liquidating Trust v. Barness, 642 F. Supp. 917, 922 (S.D.N.Y. 1986) (noting that the board had been considering the proposed asset sale as well as other alternatives for four days prior to its rushed decision, whereas in *Hanson Trust PLC v. ML SCM Acquisition, Inc.*, 781 F.2d 264, 271 (2d Cir. 1986), the decision followed a three-hour rushed meeting where the independent trustees "for the first time learned about and approved the new leveraged buyout merger agreement and the proposed lock-up option"), *aff'd*, 846 F.2d 845 (2d Cir. 1988).
66. *See* Samjens Partners I v. Burlington Indus., Inc., 663 F. Supp. 614, 624-25 (S.D.N.Y. 1987); Keyser v. Commonwealth Nat'l Fin. Corp., 644 F. Supp. 1130, 1149 (M.D. Pa. 1986); *In re* RJR Nabisco, Inc. Shareholders Litigation, [1988-1989

court's conclusion that the business judgment rule applied was the fact that detailed outside financial and legal advice concerning all aspects of the proposed merger had been presented to the board prior to its rushed decision.[68]

However, when determining whether outside advice should have been obtained, a court might consider the effect of a time constraint upon that decision. In *Solash v. Telex Corp.*,[69] the court found that the board's failure to seek more outside financial advice where its outside financial advisors had a predominating financial interest was reasonable since such an effort would require a great deal of time where time was limited.[70]

Thus, outside counsel and financial advice are not mandatory.[71] In fact, such a decision is itself protected by the business judgment rule. In *Citron v. Steego Corp.*,[72] the court noted:

> [W]hether the advice of an investment banker would be helpful or not in making a business decision of importance is itself a question demanding business judgment. In some instances—where, for example, the projected market value of a proposed financial instrument forms an important part of the consideration offered to a corporation or its shareholders—one would assume that expertise of a kind found in an investment banking house (and elsewhere) would be invaluable and perhaps essential. Where, however, the transaction offered is all cash and the essential question is the present and future value of the firm, directors with long and intimate contact with the firm may feel less need for the guidance that investment houses may offer.[73]

Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,194 (Del. Ch. Jan. 31, 1989).

67. 644 F. Supp. at 1130.

68. *Id.* at 1149.

69. [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,608 (Del. Ch. Jan. 19, 1988).

70. *Id.* at 97,729.

71. The *Smith* court noted:

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

Smith v. Van Gorkom, 488 A.2d 858, 876 (Del. 1985).

72. 14 DEL. J. CORP. L. 634 (Del. Ch. 1988).

73. *Id.* at 648-49. Macey and Miller argue that requiring outside advisors will often be ineffective: "Such procedures, however, do not provide any reliable guar-

Although not required, a court is much more likely to respect a board's decision if it can show that it obtained objective, outside help in determining the company's value.[74] In any event, a board should be very conscientious about its valuation methods. Outside financial advice and a fairness opinion, where time permits, enhance a board's chances of being protected by the business judgment rule. At the very least, board members should know the valuation methods used to determine the share price, the likely legal and financial consequences of their decision, and, using their best business judgment, should satisfy themseves that those methods and consequences are reasonable and fair.

F. Board Composition

The composition of the board of directors may affect a court's conclusion regarding whether the business judgment rule will protect the board's decision as well as its determination as to whether the board should have sought outside financial advice. In *Samjens Partners I v. Burlington Industries, Inc.*,[75] the court noted that a board's chances of proving that it conducted a reasonable investigation (and thus that the business judgment rule applies) are enhanced when it "is comprised of a majority of outside directors."[76]

A court may consider not only the number of outside direc-

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antee that the transaction will benefit shareholders. Fairness opinions of investment bankers are notorious for the degree to which they can be induced to reflect the wishes of the incumbent board." Macey & Miller, *supra* note 6 at 134-35. This assertion might be true, but Macey and Miller offer no better solution for valuation problems. At least outside investment advisors are likely to be more objective and less swayed by the board than inside financial advisors; and in the *Smith* case, relying on outside financial advisors would have been more reliable than what the board did rely on in order to know the company's value—nothing.

74. *See* Keyser v. Commonwealth Nat'l Fin. Corp., 644 F. Supp. 1130 (M.D. Pa. 1986).

75. 663 F. Supp. 614 (S.D.N.Y. 1987).

76. *Id.* at 623-24 (holding that because 10 of the 13 directors were outside and "[a]ll relevant decisions were made by the outside directors" who received outside advice there was no self-dealing or bad faith by the board) (citing Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985)); *see also* Grobow v. Perot, 539 A.2d 180, 190 (Del. 1988); Polk v. Good, 507 A.2d 531, 537 (Del. 1986); Solash v. Telex Corp., [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,608, at 97,728 (Del. Ch. Jan. 19, 1988) (holding that where 7 of the 10 directors were outside directors with no interest in the company, and where the board retained expert advice, considered alternatives to the proposed agreement, probed market for interested third parties, and met frequently for long hours, it acted in good faith).

tors on the board, but also the board members' qualifications. The *Citron* court noted that the Fairchild board was composed of predominantly experienced businessmen and that they were not dominated by any one director.[77] On the other hand, the *Smith* court pointed out that "[n]one of the directors, Management or outside, were investment bankers or financial analysts."[78] Had some of them been, and had they been involved in the valuation of the price, then the outcome in *Smith* may have been different.

G. Consequences of Disregarding Deadline

In some cases, a court might consider the possible consequences of disregarding the deadline. In *British Printing & Communication Corp. v Harcourt Brace Jovanovich, Inc.*,[79] the court noted that it was appropriate for the board, when faced with a deadline, to consider the "effects of a failure to act swiftly."[80] In *Keyser v. Commonwealth National Financial Corp.*,[81] the court stated, "It must be emphasized that the directors, at this point, had been informed that the [hostile offeror's] offer had been withdrawn and that any further delay might result in [its white knight] walking away altogether."[82] Similarly, in *In re RJR Nabisco, Inc. Shareholders Litigation*,[83] the court found that the board's actions under extreme time pressure were entitled to the protection of the business judgment rule where its decision was made partially out of fear that it would lose the bid if it did not act immediately.[84]

H. Possibility of Future Offers

Finally, a court might consider what the possibility of better offers in the future was at the time the board made its decision. For example, in *Citron v. Steego Corp.*,[85] in denying the shareholders' petition to enjoin an offer, the court noted

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77. Citron v. Fairchild Camera and Instrument Corp., 569 A.2d 53, 56 (Del. 1989).
78. Smith v. Van Gorkom, 488 A.2d 858, 877 (Del. 1985).
79. 664 F. Supp. 1519 (S.D.N.Y. 1987).
80. *Id.* at 1530.
81. 644 F. Supp. 1130 (M.D. Pa. 1986).
82. *Id.* at 1149.
83. [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,194 (Del. Ch. Jan. 31, 1989).
84. *Id.* at 91,708, 91,713.
85. 14 DEL. J. CORP. L. 634 (Del. Ch. 1988).

that "the likelihood of [the board] arranging an alternative transaction" with another offeror "was extremely remote" because the current offeror owned 48.8% of the corporation's stock.[86] On the other hand, in *Tomczak v. Morton Thiokol, Inc.*,[87] the court found that there was reasonable doubt as to whether the board's actions were protected by the business judgment rule where the board "was not advised, nor did it ask, about the other companies which had expressed interest in acquiring [the assets] and why no effort had been made to seek a higher offer."[88]

VI. CONCLUSION

Courts are not blind to the dilemma boards face when deadlines are imposed. *Citron* clarified that a board does not face an insurmountable task when it must make a rushed decision. Depending upon the specific circumstances, the business judgment rule will still protect its decisions from judicial intrusion if the board uses the available time to consider its options carefully. Extreme time pressures are a part of modern corporate life. As the *RJR Nabisco* court noted:

> [W]here an arm's-length negotiating adversary imposes time limits, a board is forced to contend with that circumstance. If it exercises informed judgment in the circumstances, considers the risks posed by the deadline imposed, and concludes that it is prudent to act and acts with care, it has satisfied its duty.[89]

When faced with deadlines in takeover situations, a board should pay close attention to the factors discussed above to assure that its actions are made in good faith and, therefore, that the business judgment rule will protect its business decisions from judicial second-guessing.

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86. *Id.* at 649.
87. 12 DEL. J. CORP. L. 381 (Del. Ch. 1986).
88. *Id.* at 384.
89. *In re* RJR Nabisco, Inc. Shareholders Litigation, [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,194, at 91,714 (Del. Ch. Jan. 31, 1989).