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IN THE SUPREME COURT OF THE STATE OF DELAWARE

ALDEN SMITH, and JOHN W. GOSSELIN, Plaintiffs Below, Appellants, v. JEROME W. VAN GORKOM, BRUCE S. CHELBERG, WILLIAM B. JOHNSON, JOSEPH B. LANTERMAN, GRAHAM J. MORGAN, THOMAS P. O'BOYLE, ROBERT W. RENEKER, W. ALLEN WALLIS, SIDNEY H. BONSER, WILLIAM D. BROWDER, TRANS UNION CORPORATION, a Delaware corporation, MARMON GROUP, INC., a Delaware corporation, GL CORPORATION, a Delaware corporation, and NEW T CO., a Delaware corporation, Defendants Below, Appellees.	)	No. 255, 1982 ON APPEAL FROM THE COURT OF CHANCERY IN AND FOR NEW CASTLE COUNTY CIVIL ACTION 5642

PLAINTIFFS' OPENING SUPPLEMENTAL BRIEF PURSUANT TO THE COURT'S ORDER OF MARCH 30, 1984

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Dated: May 1, 1984

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QUESTION: a) In connection with pertinent events occurring between August 27, 1980 and January 26, 1981, is there sufficient evidence of record to support a conclusion that there was an absence of good faith on the part of one or more directors of Trans Union Corporation ("TU"), which thereby deprives such director of the protection of the business judgment rule?

RESPONSE: I. THE RECORD SHOWS AN ABSENCE OF GOOD FAITH BY ALL THE DIRECTORS OF TRANS UNION CORPORATION.

A. DEFENDANTS DID NOT MEET THE STANDARD OF GOOD FAITH.

Section 141(a) of the Delaware General Corporation Law ("DGCL"), 8 Del. C. §141(a), charges the directors of a Delaware corporation with the responsibility of managing the corporation. Aronson v. Lewis, Del. Supr., No. 203, 1983, Moore, J. (March 1, 1984) slip op. at 10. In fulfilling their managerial obligations, directors have a fiduciary duty to act in good faith and for the best interests of the corporation and its stockholders. Id. at 10-11; Bodell v. General Gas & Electric Corp., Del. Supr., 140 A. 264, 268 (1927); Bovay v. H. M. Byllesby & Co., Del. Supr., 38 A.2d 808, 813 (1944). Delaware law holds a director to

> the most scrupulous observance of his duty, not only affirmatively to protect the interests of the corporation committed to his charge, but also to refrain from doing anything that would work injury to the corporation, or to deprive it of profit or advantage which his skill and ability might properly bring to it, or enable it to make in the reasonable and lawful exercise of its powers.

Guth v. Loft, Del. Supr., 5 A.2d 503, 510 (1939) (emphasis added).

When applicable, the business judgment rule gives rise to a presumption that directors have acted in good faith in making a business decision. That rule does not come into play and directors do not act in good faith unless the directors, inter alia:

(a) "inform themselves, prior to making a business decision, of all material information reasonably available to them,"* Aronson, slip op. at 13, and

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* The Chancellor created an erroneous standard in applying this part of the good faith test. The Chancellor required plaintiffs to show "that the directors (continued on next page)

(b) "act with requisite care* in the discharge of their duties." Id. at 13.** Moreover, there is an absence of good faith when directors totally abdicate their managerial function. Id. at 14.

When a Delaware corporation proposes to merge with another corporation, 8 Del. C. §251(b) requires that the board of directors adopt a resolution approving the merger agreement. The statutory obligation to pass on and recommend a merger is reserved to the full board of directors and is nondelegable. 8 Del. C. §141(c). (See discussion Section III, infra.) As this case demonstrates, the reason for 8 Del. C. §251(b) is obvious: a merger is of such importance to the future of the corporation that the stockholders are given the right by statute to have the undivided attention of the full board brought to bear on the transaction prior to its submission to the stockholders themselves. Consequently, directors fail to carry out their statutorily imposed obligation if they do not bring their independent, informed business judgment to bear in approving a merger, but instead allow one or two directors to decide when, for what price and if a merger should occur.

The record here reveals a total absence of good faith by all TU's directors in that:

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acted so far without information that they can be said to have reached an unintelligent and unadvised judgment". Smith v. Pritzker, Del. Ch., C.A. No. 6342, Marvel, C. (July 6, 1982) slip op. at 11. However, defendants' total failure to inform themselves concerning the Merger meets even the Chancellor's stringent standard.

* Gross negligence is the standard for determining whether directors have acted with requisite care. Aronson, slip op. at 13-14.

** See also Arsht, Fiduciary Responsibilities of Directors, Officers and Key Employees, 4 Del. J. Corp. L. 652, 661 (1979) ("good faith means that the director has exercised due care by informing himself of the relevant and available facts and that he reasonably believed that the challenged transaction served the best interest of the corporation.")

(a) Mr. Van Gorkom (with Mr. Chelberg's knowledge and acquiescence) usurped the function of the TU Board by seeking out and preliminarily negotiating a cash-out Merger, coupled with a lock up sale of 1 million TU shares to Mr. Pritzker at $17 per share below the Merger price, without Board authorization and without consulting his fellow directors or TU's legal and financial advisors.*

(b) TU's Board then abdicated their statutory and fiduciary obligations by quickly and supinely acquiescing in the unauthorized and reckless conduct of Mr. Van Gorkom and Mr. Chelberg.

(c) TU's Board failed to take any steps to inform themselves, prior to approving the Merger, of the circumstances relating to (1) the inception of the Merger (2) the $55 price, or (3) the actual terms of the Merger and their effect.

(d) TU's Board failed to act with the requisite care in approving the Merger.

B. MR. VAN GORKOM'S DELIBERATE AND SECRETIVE USURPATION OF THE FULL BOARD'S AUTHORITY.

In flagrant disregard of the statutory requirement of full director participation in merger evaluation and approval, Mr. Van Gorkom, without Board approval, took it upon himself to single-handedly negotiate and commit to a merger proposal. In doing so, Mr. Van Gorkom did not act in good faith. 8 Del. C. §251(b); Bennett v. Propp, supra, 187 A.2d at 411-412. Furthermore, his conduct failed to satisfy the requirements of good faith, since he did not seek out all reasonably available information or act with due care in negotiating the Merger. Indeed, his ill-advised, unauthorized actions eventually resulted in TU being trapped in a lock-up Agreement which effectively precluded higher, competing offers and resulted in the TU stockholders receiving far less for their stock than its fair value or what should have been obtained by a diligent fiduciary.

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* Mr. Van Gorkom made Mr. Chelberg, his "designated successor" and President of TU, aware of what Mr. Van Gorkom had done on Tuesday, September 16, 1980 (A-1308). Thereafter, Mr. Chelberg was fully aware of the situation, but remained totally passive. Thus, under Bennett v. Propp, Del. Supr., 187 A.2d 405 (1962), Mr. Chelberg is as liable as Mr. Van Gorkom.

TU's Board of Directors never even discussed much less authorized or directed Mr. Van Gorkom to initiate the Merger discussions (TR 769, Johnson). The Board never gave him any authority to enter into any sort of preliminary agreement with Mr. Pritzker (TR 769, Johnson; Van Gorkom 48; Chelberg 42-43; Wallis 35; Bonzer 24; Browder 60; Morgan 49). Nevertheless, Mr. Van Gorkom deliberately and secretly set out to accomplish a merger without first consulting TU's Board, other officers, or financial or legal advisers.*

1. Mr. Van Gorkom unilaterally decided without Board authorization to seek a merger partner for TU (TR 769, Johnson).

2. The Chancellor found that Mr. Van Gorkom formulated his merger proposal with Mr. Pritzker, a business and social friend, specifically in mind. Smith v. Pritzker, supra, slip op. at 4.

3. Mr. Van Gorkom initiated the Merger by contacting Mr. Pritzker. Id. at 5. He did not contact any other person or entity that might be interested in acquiring TU (A-1273). By his unilateral action, Mr. Van Gorkom intentionally put TU and its Board in a time squeeze as a result of Mr. Pritzker's take it or leave it offer (A-1111, 1113, 1347).

4. Without the advice or consent of the rest of management or the Executive Committee of the Board or the Board itself, and without the counsel of TU's chief financial officer or the investment bankers that TU had traditionally relied upon, Mr. Van Gorkom decided to propose a $55 per share merger price to Mr. Pritzker (A-1282-1283; Smith v. Pritzker, supra, slip op. at 4-5).

5. Mr. Van Gorkom had not consulted TU's investment banker in determining the $55 price. The $55 number was an entirely subjective determination by Mr. Van Gorkom based on his personal views and needs. The $55 price was solely based on the fact that Mr. Van Gorkom himself would not take $50 for his shares: $55 was acceptable to him and $60 would be "preemptive." "I started with 55 because I knew I would take 55" (A-1283).

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* Mr. Van Gorkom set about this Merger immediately after Mr. Romans suggested a leveraged buy out by certain members of TU's management. Mr. Van Gorkom knew that if a leveraged buy out did occur, Mr. Romans and Mr. Bonzer would replace him in the new company (A-1422-1423; Van Gorkom 196, 309). Thus, Mr. Van Gorkom was not acting in "good faith"; actually he was intent on thwarting an attempt to displace him.

6. After selecting the $55 number, Mr. Van Gorkom tested it to see whether Mr. Pritzker would be able to finance it out of TU's cash flow (A-1284). The Court below found that this was Mr. Van Gorkom's approach. Smith v. Pritzker, supra, slip op. at 4-5. Thus, Mr. Van Gorkom's focus was on what would be "doable" by Mr. Pritzker, not what would be good for the TU's stockholders.

7. Mr. Van Gorkom never negotiated the $55 price or had an independent committee of the Board do so (A-1300-1301). Compare Weinberger v. UOP, Inc., Del. Supr., 457 A.2d 701 (1983). The $55 price was such a bargain Mr. Pritzker snapped it up.

8. Between September 13 and September 16, 1980, Mr. Pritzker and Mr. Van Gorkom conversed on several occasions and Mr. Van Gorkom and Mr. Chelberg met with Mr. Pritzker on September 16, 1980 to provide additional information that Mr. Pritzker believed he needed in order to consider the Merger proposal (A-1306-1308). This included disclosure, without Board authorization, of non-public, unpublished financial information (A-1310). Neither Mr. Van Gorkom nor Mr. Chelberg disclosed to TU's Board these meetings or the disclosure of confidential information. In addition, he made Boston Consulting Group available to assist Mr. Pritzker in his evaluation of the Merger (A-1098-1099, 1310-1311; Smith v. Pritzker, supra, slip op. at 6).*

9. Despite being "astounded" at the amazing rapidity with which the events leading up to the Merger were moving (A-1101, 1316), Mr. Van Gorkom still did not consult or inform the other TU Board members or officers when, on September 18, 1980, he learned that Mr. Pritzker was going to formalize the very offer that Mr. Van Gorkom himself had proposed (A-1317-1318, 1333-1334).

10. The Chancellor found that Mr. Pritzker and Mr. Van Gorkom reached an agreement on the Merger before the September 20 Board meeting. Smith v. Pritzker, supra, slip op. at 7.

11. While acquiescing to Mr. Pritzker's insistance that Mr. Pritzker's lawyers draft the Merger Agreement documents (A-1101), Mr. Van Gorkom deliberately refrained from consulting with William Browder, Esquire, a vice president, director and previous head of the TU law department, nor the current head of that department, William Moore, Esquire (A-1328) and only orally briefed outside counsel at the last moment (A-1329-1330).

12. On Friday, September 19, 1980, Mr. Van Gorkom and Mr. Chelberg went with Mr. Pritzker to Continental Bank (A-1320), one of TU's lead banks (A-1322), to help line up Mr. Pritzker's financing for the Merger (A-1106-1107).

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* In fact, Michael Carpenter of Boston Consulting Group was asked to fly down from Boston to consult immediately with Mr. Pritzker (A-1098-1099). Mr. Pritzker, with Mr. Van Gorkom's approval, went so far as to use Boston Consulting Group, TU's own consultants, Whom Mr. Van Gorkom had given carte blanch (A-1099) to work with him to provide information on TU for the Merger (A-1311-1314).

13. Mr. Van Gorkom agreed to Mr. Pritzker's demand that the cash-out Merger be coupled with a "lock up" for Mr. Pritzker (i.e., sale of 1,000,000 TU shares at $38 rather than the $55 cash-out price) (A-1324).

14. On September 19, 1980 Mr. Van Gorkom called a special meeting of TU's Board for noon the next day, Saturday, September 20, 1980, but even then did not inform them that basically the purpose of the meeting was to sell TU to Mr. Pritzker for $55 per share (A-1109).

15. Mr. Van Gorkom summoned senior management to a meeting at 11:00 a.m. on September 20 without telling them the purpose of the meeting (A-1109).

16. No documents were prepared or drawn up for or made available to the Board or management (A-1338-1339). Thus, Mr. Van Gorkom and Mr. Chelberg failed to provide the other directors with any written information or factual analysis by which they could evaluate the Merger.

17. Mr. Van Gorkom's presentation to the Board on the proposed Merger took twenty to thirty minutes (A-1371; Van Gorkom 143). Mr. Van Gorkom simply told the Board orally what he thought was the substance of the proposed Merger Agreement (TR 708, Johnson) though he had never even read the Merger documents at that time (or indeed before he signed the Merger documents later that evening) (A-1378-1379).

18. Mr. Van Gorkom assured the Board that a critical feature of the Merger terms was that the Board was free to accept and enter into higher offers (A-1359-1360). That assurance was plain wrong (PX 25: A-1910).

19. Mr. Van Gorkom squelched the KKR $60 per share leveraged buy-out which was presented to him by Mr. Henry Kravis on December 2, 1980 by rejecting it and refusing to issue a press release concerning it. As to the rejection, Mr. Van Gorkom's reason was that the financing was incomplete (it was 80% complete); yet he would not extend to KKR the "subject to financing" condition which had been received by Mr. Pritzker. As to the press release, his reason was that it would chill other offers; yet he issued the September 22, 1980 Pritzker press release obstensibly to spur other offers (A-1423-1427).

The evidence of record shows overwhelmingly that Mr. Van Gorkom secretly initiated Merger negotiations with Mr. Pritzker and personally decided the Merger price with no input whatever from TU's other directors or officers or TU's financial advisors. Moreover, he and Mr. Chelberg took affirmative steps to keep TU's senior management and Board of Directors completely in the dark up to the meeting at which the Board was asked to vote on the Merger.* In addition, Mr. Van Gorkom failed to seek the advice of TU's financial and legal advisors. He himself made no attempt to perform the careful study and analysis required of fiduciaries before agreeing to a transaction as fundamental as a cash-out merger. Such usurpation of the Board's authority and failure to take even the most basic steps which prudent fiduciaries would take foreclose any inference that Mr. Van Gorkom or Mr. Chelberg acted in good faith. Bennett v. Propp, supra, 187 A.2d at 411. Nonetheless, their improper conduct might not have damaged TU's stockholders had the remaining members of the TU Board carried out their directorial responsibilities.

C. TO A MAN, THE TU DIRECTORS ABDICATED THEIR STATUTORY AND FIDUCIARY RESPONSIBILITIES.

By keeping the remaining members of the TU Board completely ignorant of the Merger until Saturday, September 20, 1980, Mr. Van Gorkom affirmatively prevented the Board from evaluating the Merger prior to the meeting. However, when finally and suddenly confronted by the Merger proposal, the full TU Board still remained obligated to fulfill its fiduciary responsibilities as directors to evaluate independently and carefully the proposed transaction. 8 Del. C. §§141 (c), 251(b). Gimbel v. Signal Companies, Inc., Del. Ch., 316 A.2d 599, 611, aff'd., Del. Supr., 316 A.2d 619 (1974); Weinberger v. UOP, Inc., supra, 457 A.2d at 712.

Indeed, given the tight time constraints Mr. Pritzker had allegedly imposed, the TU Board had an even greater obligation to scrutinize the proposal! If the Board

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* Mr. Van Gorkom's only justification was because he feared "leaks" from his own Executive Committee, the Board itself or the management (A-1084; Chelberg 52-53). Even if his alleged fears were justified, such "fears" do not override the statutory requirements for full Board participation. Mr. Van Gorkom wanted to pull off a single handed "coup" to preclude a leveraged buyout. In his eagerness Mr. Van Gorkom not only violated corporate law but common sense and "sold" his shares and that of all the TU shareholders for at least $10-15 less than their fair value.

could not make a reasoned evaluation of the Merger in the allotted time, the prudent and required course was to reject the Merger. Compare, Pennzoil Co. v. Getty Oil Co., Del. Ch., C.A. No. 7425, Brown, C. (February 6, 1984) slip op. at 10, where the Getty Board of Directors rejected Pennzoil's initial tender offer because of the time squeeze it put on the Getty Board.* See also Herzel, Schmidt, & Davis, Why Corporate Directors Have a Right to Resist Tender Offers, 3 The Corporation Law Review 107 (1980). Nevertheless, while Mr. Van Gorkom's disclosure "surprised" the Board (Chelberg 116; Morgan 52; Lanterman 76), the Board made no effort to make a meaningful, independent evaluation of the Merger. Specifically, the record shows:

1. The Board did not inquire into how the $55 price had been set (A-1348-1349; Chelberg 155-156).

2. The Board did not inquire into the origins of the terms of the proposed Merger (TR 798-799, Johnson).

3. The Board did not inquire into the adverse tax implications for the TU stockholders (A-1351).

4. The Board did not inquire into how the price for the 1,000,000 "lock up" shares was set (A-1351-1352).

5. The Board posed no questions as to why an opinion or evaluation by TU's investment bankers had not been obtained (A-1352-1353).

6. The Board made the affirmative decision not to obtain the advice or opinion of TU's investment bankers (A-1353). Indeed, the TU Board never obtained for themselves or their stockholders an independent investment banker fairness opinion (TR 799, Johnson).

7. The Board made the affirmative decision not to obtain the studies of the value of the TU shares made by TU's financial department headed by Mr. Romans (A-1353).

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* Unlike TU's Board, the Getty Board refused to be "muscled" into a premature, uninformed decision. Instead the Getty Board undertook intense negotiations on behalf of the company and its stockholders. See, Id. at 9-12. The positive results for Getty stockholders from the resolute response of the Getty Board underscores what could and should have happened in this case.

8. The Board did not question or discuss whether Mr. Pritzker would actually withdraw his offer if it was not acted upon by Sunday night (A-1360).

9. There was no discussion of whether potential competing offers would surface if Mr. Pritzker did withdraw (A-1360-1361).

10. The directors had not read the Merger Agreement (A-1379; TR 777-778, Johnson) nor were they furnished any documents concerning the Merger (A-1338-1339; TR 775-776, Johnson).

11. The Board permitted the sale of 1 million shares of TU stock to Mr. Pritzker at $17 less than the Merger price, thus wasting at least $17 million of TU's assets and hamstringing other bidders for TU. Indeed, the very existence of the lock-up Merger Agreement with Mr. Pritzker whereby Mr. Pritzker was issued 1 million TU shares at $38 served to discourage competitive bidding.*

12. Mr. Van Gorkom claimed at trial that the TU Board conditioned TU's acceptance of the Pritzker offer on two alleged conditions: first, the right of TU to share proprietary TU information with other bidders and, second, the right of TU to accept (though not solicit) alternate bids (A-1372-1373). There is nothing whatever in the official minutes of the September 20, 1980 meeting that substantiates any such claim as to the conditions (PX 26: A-1865). As plaintiffs have repeatedly pointed out (A-1374), the form of the Merger documents prior to the incorporation of these "phantom" conditions (though called for by discovery) and called for at trial (A-1374), have never been produced. TU's directors who reviewed and approved TU's minutes are not in good faith. The official minutes do not reflect these two allegedly important conditions supposedly imposed by the Board. (Of course, the other possibility is that no conditions were in fact imposed by the Board before accepting the Pritzker Merger proposal.)

13. The Board issued a press release on September 22, 1980 announcing that TU had entered into "definitive agreements to merge" thereby chilling any other offers (PX 30: A-2074).

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* The court in Mobil Corp. v. Marathon Oil Co., 6th Cir., 669 F.2d 366 (1981), where Marathon agreed to issue 10 million shares of $90 (the "Option") to U.S. Steel as a condition to US Steel's acquiring 30 million shares at $125 with a plan for a follow-up merger, held that the Option was an illegal manipulative device which prevented "all others from competing on a par with USS for control of Marathon". Mobil, 669 F.2d at 375. The Option created "an artificial and significant deterrent to competitive bidding for a controlling block of Marathon shares". Id. In the case sub judice, by virtue of the sale of 1 million shares, Mr. Pritzker had a $17 million "head start" on all other bidders. Practically, that sale created an artificial and significant deterrent to competitive bidding for TU's stock. Thus, the October 10 amendments were but a "will-o'-the-wisp", designed to eliminate management discord with the merger (A-1399-1400).

14. The Board negleted to pursue the KKR $60 per share leveraged buy-out which was complete as of December 2, 1980 except for 20% of the necessary financing (A-1423-1427).

15. The Board's hasty and ill-advised adoption of the Pritzker lock up Merger Agreement enabled Mr. Pritzker to kill the General Electric Credit Corporation $60 per share merger offer in January 1981 simply by refusing to step aside (A-1463-1464).

Thus, without scrutiny, the Board approved the Merger. This unquestioning acquiescence in the Merger hastily and recklessly concocted by Mr. Van Gorkom and speedily proposed by him on behalf of Mr. Pritzker negatives any contention that TU's directors acted in good faith. Such flagrant disregard for the basic responsibilities and duties owed by the directors to the corporation and the stockholders should not and cannot be tolerated. Lutz v. Boas, Del. Ch., 171 A.2d 381, 395-96 (1961).

Chancellor Seitz' evaluation in Lutz of the outside directors of a mutual fund company applies with equal force to TU's directors here:

> These men are prime examples of what can happen when a man undertakes a substantial responsibility with public overtones without any appreciation of his obligation thereunder.

171 A.2d at 395-96. Chancellor Seitz found the directors gave "almost automatic approval" to a transaction proposed by management without examining or discussing the documents and facts "pertinent to a reasonable discharge of their duties." Id. Because "even an average attention to duty by the directors" would have informed them of the improper activities by corporate insiders, the outside directors were held jointly and severally liable. Id. By cavalierly neglecting to perform their duties as directors and ignoring the danger signs inherent in a transaction arranged in haste without Board authorization, without expert advice and without the back-up analysis a Board should expect from management, the TU directors (as well as Mr. Van Gorkom and Mr. Chelberg) are jointly liable for the damage to the TU's

stockholders. Cf. Graham v. Allis-Chalmers Mfg. Co., Del. Supr., 188 A.2d 125, 130 (1963).

Bennett v. Propp, supra, confirms that all TU's directors, (not just Mr. Van Gorkom and Mr. Chelberg), have not acted in good faith. In Bennett, this Court held that Board action at a Saturday meeting ratifying the unauthorized purchase of approximately 200,000 shares of the corporation's stock by the chief executive officer and arranging financing to meet the Monday deadline for paying for the stock in itself did not render the entire Board liable. In Bennett, this Court excused the directors (other than the CEO and another director who had advance knowledge of the purchases) from the liability because:

> (a) Prior to the Saturday meeting, they had no knowledge of the purchases.
>
> (b) They were presented with a fait accompli and a legal commitment that had to be met.
>
> (c) They did the best they could under the circumstances.
>
> (d) They were faced with an immediate emergency that threatened financial disasater and ruinous litigation to the corporation.

187 A.2d at 409-411.

While Mr. Van Gorkom and Mr. Chelberg did keep TU's other directors ignorant of the Pritzker proposal until the Saturday meeting, none of the other above reasons this Court listed in Bennett as justification for the Bennett directors is applicable to the TU directors. The TU directors were not confronted with a fait accompli or a corporate obligation that they could not avoid. The TU Merger required the prior approval of the full Board to satisfy §251. Nor did the TU Board do the best they could to evaluate the Merger as thoroughly as possible in the limited time supposedly available. On the contrary, the TU Board did nothing at all to evaluate the Merger proposal. Finally, there was no corporate emergency of any kind that threatened TU's financial viability if the Merger was not approved prior to Mr. Pritzker's artificial Monday deadline. Like Getty's Board, TU's Board could have refused to be stampeded by an arbitrary time limitation. If Mr. Pritzker would not have agreed to extend the purported "deadline", TU could have continued in operation without any adverse consequences and the TU stockholders would not have been casually sold out by their own (literally) ignorant Board at a brief meeting on a Saturday afternoon in September.*

D. THE DIRECTORS DID NOT MAKE AN INFORMED JUDGMENT IN VOTING FOR THE MERGER.

1. Failure to Review the Merger Agreement.

The record firmly establishes that TU's directors did not inform themselves of all material information reasonably available to them before approving the Merger. None of the Board members ever asked to read or did read the Merger documents or even a written summary of their critical terms (A-1379).** The failure to read the Merger documents they hastily approved conclusively demonstrates the Board's lack of good faith. A board cannot discharge its statutory and fiduciary duty to evaluate a proposed Merger Agreement without reading or reviewing the Merger documents. Despite the abrupt disclosure of the Merger proposal and their conceded surprise, TU's directors passively accepted Mr. Van Gorkom's patently inaccurate representations about the Agreement's contents. The directors' failure to inform

* Since Mr. Romans reported that his department studies estimated that TU's stock was worth between $55-65 per share and TU's Five Year Forecast (PX 21: A-1883) showed no need for a merger, there certainly was no "emergency" justifying defendants' hasty acceptance of Mr. Pritzker's offer.

** Mr. Brennan, TU's outside legal counsel, was never given any written summary of the Agreement; instead he was made to rely on Mr. Van Gorkom's summary of what Mr. Van Gorkom thought the substance of the Agreement was (A-1329-1330). Mr. Van Gorkom himself never read the entire Merger Agreement, though he knew it had been drafted by counsel for the buyer (A-1379).

themselves about the Merger and their resulting ignorance of its fundamental terms resulted in their approval of a Merger Agreement containing (i) an unfair and inadequate cash-out price, (ii) wasteful and treacherous lock-up provisions, and (iii) an unrecognized requirement that the Board recommend the Merger (including the $55 price) and use its best efforts to see it voted through by the stockholders.

2. The Board Failed to Seek or Review Information as to Whether the $55 Price Was Fair.

As noted earlier, Mr. Van Gorkom personally set the $55 price without consulting TU's other directors, other officers or TU's financial advisors. He ignored or did not know that TU's own financial section had done studies indicating that the value of TU's stock ranged between $55 and $65 per share. Moreover, even when he learned about the existence of the studies at the management meeting, Mr. Van Gorkom never directed that the study be produced for the upcoming Board meeting (A-1338). Indeed, Mr. Van Gorkom did not present any written analysis to the Board providing the sort of justification for the $55 price which a reasonable Board could and should expect.

In the face of Mr. Van Gorkom's failure to provide any information necessary to evaluate the $55 price, TU's Board should have demanded complete information. Specifically, the Board should have demanded from TU's financial experts or its investment bankers, Salomon Brothers, (or both) financial analyses showing why $55 was a fair price to TU's stockholders. No such analyses or any information of any kind were asked for by the Board. TU's Board did not take even the most rudimentary steps to assess the $55 Merger proposal.

The Board's failure to demand a justification of the fairness of the $55 price is all the more shocking because that $55 price was at the very bottom of the $55-65 range that TU's own Chief Financial Officer, Mr. Romans, believed the fair range to be. In the context of a cash-out merger, the loss of $10 per share deprived TU's stockholders of $127,344,040.* This amount was (and is) "significant" to TU's stockholders. See Weinberger v. UOP, supra, 457 A.2d at 709. TU's directors did not seek a price higher than $55, nor even question the $55 price, since they had no basis whatsoever on which to make any rationale determination as to a fair price.

E. THE TU BOARD OF DIRECTORS NEVER CURED THEIR BAD FAITH CONDUCT.

TU's Board took no action at any of its four meetings** between September 20, 1980 and the February 10, 1981 stockholders meeting which "cured" the total absence of good faith in the Board's precipitous September 20 approval of the Merger.

Mr. Van Gorkom made an oral presentation to the Board on proposed amendments to the Merger Agreements at an early morning meeting on October 8, 1980 (TR 870, Johnson). However, again the actual amendments were not in existence at the time of the meeting of October 8; the actual amendments were drawn up and signed on October 10, 1980 (PX 55: A-2125). The actual terms could not be reviewed by TU's directors or by counsel for TU (TR 870-872, Johnson). The Board once again failed to take even the most basic step (i.e. insisting on reading what they were approving) to come within the ambit of good faith. Instead, all they relied on was yet another inaccurate oral summary by Mr. Van Gorkom of what he thought the yet undrafted amendments would contain. The Board blindly authorized the amendments without any attempt at determining their actual terms.

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* TU had 12,734,404 shares outstanding. Thus, even a $1 per share increase in the Merger price would have meant an additional $12,734,404 shares for TU's stockholders.

** There was no discussion of the merger at the October 23, 1980 Board meeting (DX 4: A-1871). The December 2, 1980 meeting involved only certain formalities necessary to proceeding with the Merger, not substantive consideration of its terms (PX 84: A-1873).

The October 10 amendments added Article V(e) to the Agreement and Plan of Merger purportedly to allow TU to terminate the Pritzker Merger agreement and abandon the Pritzker Merger if TU got a better offer. However, TU's right to terminate under the amendments was so circumscribed as to be illusory. TU could terminate only if (1) TU had consummated a merger with another party or (2) TU had entered into a definite agreement for merger (PX 55: A-2125 at A-2127-2128). Since a consummated merger without a merger agreement is impossible, only the second termination right had any possible significance. But even that "right" was mere window dressing, since the definitive merger agreement could contain only two conditions: (1) TU stockholder approval; and (2) no injunction or government restraint against the merger. Thus, any alternative merger agreement could not be conditioned on the buyer obtaining financing or any other conditions normally included in merger agreements (and specifically included in the Merger Agreement between the Pritzkers and TU). Moreover, the $17 million windfall to Mr. Pritzker remained in place. Consequently, "the deck was stacked" from the outset against TU being able to land a competing merger proposal.

Despite the filing of this law suit on December 19, 1980, TU's Board did not meet again until January 26, 1981. Meanwhile, the Board issued the January 19, 1981 original proxy statement long after sufficient time had passed for the Board to address in that proxy statement the issues raised in the law suit (PX 98: A-2216).* At the January 26, 1981 meeting, the Board simply attempted to make a "paper" record to show that they were now belatedly bringing their judgment to bear on the

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* Compare Michelson v. Duncan, Del. Ch., 386 A.2d 1144, 1150 (1978); aff'd in part and rev'd in part, Del. Supr., 407 A.2d 211 (1979), where the litigation was described in detail in the proxy statement and the complaint was appended to the proxy statement.

issues that had been before them on September 20, 1980 (DX 8: A-1877). This transparent attempt to bring themselves within Muschel v. Western Union Corp., Del. Ch., 310 A.2d 904, 909 (1973), does not save them because at that late date the Board members could not remedy their original lack of good faith. At that point, they did not have the power to amend the terms of the Merger Agreement. TU was contractually and legally bound to the Pritzkers.

* * *

The foregoing response to the Court's question shows that none of the TU directors did anything at any time in connection with the TU merger that remotely approaches the basic requirements of good faith. What could and should have been done by the directors in discharge of their obligation of good faith is set out in Martin Lipton's article in 35 Bus. Law 101, 121-23 (1979), Takeover Bids in the Target's Boardroom:

> What the Directors Should Do.
>
> * * *
>
> Since we are dealing with takeovers which by definition are within a broad band of discretion, and since some might believe that there are conflicts between management's self-interest in preserving the independence of a target company and the directors' decision to accept or reject a takeover bid, it may be helpful to follow those procedures which in other areas have proven to eliminate or minimize conflicts and produce well founded objective decisions. Thus:
>
> A) Management (usually with the help of investment bankers and outside legal counsel) should make a full presentation of all of the factors relevant to the consideration by the directors of the takeover bid, including:
>
> (1) historical financial results and present financial condition
>
> (2) projections for the next two to five years and the ability to fund related capital expenditures
>
> (3) business plans, status of research and development and new products prospects

(4) market or replacemnt value of the assets
(5) management depth and succession
(6) can a better price be obtained now
(7) timing of a sale; can a better price be obtained later
(8) stock market information such as historical and comparative price earnings ratios, historical market prices and relationship to the overall market, and comparative premiums for sale of control
(9) impact on employees, customers, suppliers and others that have a relationship with the target
(10) any antitrust and other legal and regulatory issues that are raised by the offer
(11) an analysis of the raider and its management and in the case of a partial offer or an exchange offer pro forma financial statements and a comparative qualitative analysis of the business and securities of both companies

B) An independent investment banker or other expert should opine as to the adequacy of the price offered and management's presentation.

C) Outside legal counsel should opine as to the antitrust and other legal and regulatory issues in the takeover and as to whether the directors have received adequate information on which to base a reasonable decision.

D) If a majority of the directors are officers or otherwise might be deemed to be personally interested, other than as shareholders, a committee of independent directors, although not in theory necessary, from a litigation strategy standpoint may be desirable. The exigencies and pressures of a takeover battle are such that it is desirable to avoid profileration of committees, counsel and investment bankers. The target will be best served if it is advised by one investment banker and one outside law firm.

E) It is reasonable for the directors of a target to reject a takeover on any one of the following grounds:
(1) inadequate price

(2) wrong time to sell
(3) illegality
(4) adverse impact on constituencies other than the shareholders
(5) risk of nonconsummation
(6) failure to provide equally for all shareholders
(7) doubt as to quality of the raider's securities in an exchange offer.*

QUESTION: b) In connection with the TU directors' meetings of September 20, 1980 and October 8, 1980, is there sufficient evidence of record to support a conclusion that one or more directors, other than defendants Van Gorkom and Chelberg, may be entitled to claim the protection of the business judgment rule because of reasonable reliance in good faith under 8 Del. C. §141(e), upon reports, including legal advice, rendered to the Board by Van Gorkom, Chelberg and others?

RESPONSE: II. THERE IS NO EVIDENCE THAT ANY TU DIRECTOR REASONABLY RELIED IN GOOD FAITH UPON REPORTS, UNDER 8 DEL. C. §141(e) AT THE SEPTEMBER 20, 1980 AND OCTOBER 8, 1980 MEETINGS.

A. THERE IS NO EVIDENCE THAT ANY REPORTS WITHIN THE MEANING OF 8 DEL. C. §141(e) WERE PRESENTED TO THE BOARD. NOR IS THERE ANY ADMISSIBLE EVIDENCE OF LEGAL ADVICE TO THE BOARD.

8 Del. C. §141(e) protects directors who rely "in good faith upon...reports made to the corporation by any of its officers, or by an independent certified public accountant, or by an appraiser selected with reasonable care by the board of directors or by any such committee...." Since TU had not, in connection with the September 20 and October 8 Board meetings, availed itself of a certified public accountant or an appraiser (A-1353), the only possible applicable provision of §141(e) is the reference to reliance on "reports made to the corporation by any of its officers."

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* Footnotes (including citations to Delaware cases) omitted. The foregoing was repeated verbatim in Lipton, Takeover Bids In The Boardroom: An Update After One Year, 36 Bus. Law. 1017, 1026-27 (1981).

However, the record shows that no §141(e) officers' reports were made at either the September 20 or October 8 Board meetings. The trial testimony of Messrs. Van Gorkom (A-1338, 1347) and Johnson (TR 721, 770, 775-77) and the deposition testimony of the other TU directors, Messrs. Chelberg (127-128), Bonser (57, 60), Browder (34, 87), Wallis (41), Lanterman (32, 55), Morgan (62, 64) and Reneker (59, 67), confirm that the only "reports" to the directors at the September 20 Board meeting were (1) Mr. Van Gorkom's cursory oral presentation of the Pritzker proposal, in which Mr. Van Gorkom outlined his understanding of the general terms and conditions of the merger (Morgan 52) and (2) Mr. Romans' single oral statement that TU's stock was worth $55-65 per share.* Beside these two "reports", the directors had no other information about the Merger itself or the $55 price or whether it was in the best interest of TU's stockholders.**

Likewise, the only "report" rendered at the brief October 20 meeting was Mr. Van Gorkom's oral presentation of his personal understanding of the proposed modifications to the Merger Agreement (TR 870, Johnson). No written materials

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* Although Mr. Romans stated his personal conclusion to the directors assembled at the September 20 meeting, the studies made by TU's financial department were not made available to the directors. No director asked for Mr. Romans' studies or data or otherwise sought to determine whether the $55 price was "fair" or whether a higher price could be obtained before accepting the Pritzker offer (A-1338; Browder, 69).

** In July, 1980 TU's directors were given a Five-Year Forecast prepared by TU's management which discussed various uses for TU's enormous cash surplus (PX 21: A-1883 at A-1896). The Forecast mentioned that one possibility was the repurchase of 30% of TU's stock at $50 per share. The Forecast did not consider any form of a cash-out merger nor the sale of 100% of TU. The Forecast emphasized that there was no emergency of any kind. On the contrary, the Forecast suggested careful and deliberate consideration of several alternative courses of action other than a cash-out merger. In August, 1980 the directors were given a report prepared by the Boston Consulting Group which analyzed TU's business (DX 10, DX 11, DX 12, PX 17). The BCG study never even mentioned the possible sale of TU, much less what a fair price would be for TU's stock in the event of a cash-out merger.

were disseminated at that Board meeting (TR 870, Johnson). The purpose of the meeting, according to Mr. Johnson, was to approve in principle proposed, but undrafted, amendments to the executed Merger Agreement that purportedly were going to allow TU to solicit other offers. (Johnson, 62).

Mr. Van Gorkom's summary oral presentations at the September 20 and October 10 meetings, unsubstantiated by any study or any other documentation, are not "reports" within the meaning of 8 Del. C. §141(e). Section 141(e) protects good faith director reliance upon business information presented by officers of the corporation, independent certified public accountants or appraisers selected by the board. Its protection does not extend to reliance upon officers' oral opinions of an important proposed transaction. C. Israels, Corporate Practice, §261 (3d ed. 1974). Accordingly, Mr. Van Gorkom's statements of the general terms and conditions of the Merger Agreement,* and on the subsequent modifications thereto, are not within the category of reports upon which directors are statutorily entitled to rely. Mr. Romans' statement is not a report within the meaning of §141(e). Moreover, the Board appears to have ignored or discarded Mr. Romans' statement that the stock was worth between $55 and $65 per share. Instead, they committed TU to a merger at $55 per share. The Board never obtained the TU financial department study and analysis of TU's stock.

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* Mr. Van Gorkom had not even read the Merger documents before attempting to explain to the Board (A-1378-1379) what he thought was the substance of the agreement. In other words, all they got was Mr. Van Gorkom's oral presentation of what he thought the Merger documents prepared essentially by Mr. Pritzker's attorneys would contain. As the record shows, Mr. Van Gorkom was flat wrong in his understanding as to the actual terms of the Merger documents. As a result of the Board's haste, there was no way to learn the actual terms before voting to approve the Merger.

No legal advice was given to the directors at the September 20 or October 8 meetings. The official minutes of the September 20 Board meeting make no reference to any legal advice having been given to the Board by James Brennan, Esquire, of Sidley & Austin or even show that he attended the meeting (PX 26: A-1865). While Mr. Van Gorkom testified that Mr. Brennan attended the September 20 Board meeting (A-1118), the defendants introduced no admissible evidence of what legal advice, if any, Mr. Brennan gave the Board. Over plaintiff's hearsay objection, Mr. Van Gorkom testified at trial that Mr. Brennan had advised the directors that they need not seek a fairness opinion before accepting the Pritzker proposal. (A-1117-29, 1132). Although he was their own counsel and lawyers in his firm had come to Delaware in connection with this litigation, the defendants did not call Mr. Brennan as a witness.*

In any event, §141(e) does not extend to legal advice. By its clear language, §141(e) is limited to reliance on (1) books of account; (2) reports to the corporation by officers, certified public accountants or appraisers; and (3) other corporate records. In contrast to §35 of the Model Business Corporation Act** and statutes in numerous jurisdictions,*** §141(e) has no provision for reliance on counsel. Under

* As Chancellor Wolcott wrote in Richards v. Jones, Del. Ch., 142 A. 832, 835 (1928): "The failure of the [party]... to call his most important witness must be taken strongly against them in obedience to the familiar rule on the subject." At 2 J. Wigmore, Evidence, §285 at p. 162 (3d ed. 1940), the author states: "The failure to bring before the tribunal some... witness, when either the party himself or his opponent claims that the facts would thereby be elucidated, serves to indicate, as the most natural inference, that the party fears to do so...."

** In pertinent part, §35 of the Model Act provides: "In performing his duties, a director shall be entitled to rely on information, opinions, reports or statements, including financial statements and other financial data, in each case prepared or presented by:... (b) counsel, public accountants...."

*** E.g., 14A N.J. Stat. Ann. §14A: 6-14 (West 1969); N.Y. Bus. Corp. Law §717 (Consol. 1983 Supp.); Md. Corps. & Assn's Code Ann., §2-405.1 (1983 Supp.); 24 Cal. Corp. Code §309 (West 1977); 7A Ala. Code §10-2A-73 (1975).

the rules of statutory construction, the omission of "counsel" from the class of people set forth in §141(e) evidences legislative intent to exclude "counsel" as a group upon whose reports directors are entitled automatically to rely to insulate them from liability. See Norman v. Goldman, Del. Super., 173 A.2d 607, 610 (1961); 2A C. Sands, Sutherland Statutory Construction, §47.23 (4th ed. 1973).

Nor can the defendants assert reliance on advice of counsel as a common law defense to plaintiff's claims. To establish such a defense the defendants would have to have proved (which they did not) that they: (1) made complete disclosure of all facts to counsel; (2) specifically requested counsel's advice as to the legality of the contemplated transaction; (3) received advice that it was legal; and (4) relied in good faith on that advice. SEC v. Savoy Industries, Inc. D.C. Cir., 665 F.2d 1310, 1314, n. 28 (1981). Even when established, such reliance does not operate as an automatic defense, but is only a factor in determining the propriety of injunctive relief. Id.; SEC v. Manor Nursing Centers, Inc., 2d Cir., 458 F.2d 1082, 1101 (1972). Since the defendants did not prove any of these elements, they cannot claim reliance on legal advice as a defense.*

B. THE RECORD DOES NOT SUPPORT A CONCLUSION THAT ANY DIRECTOR RELIED IN GOOD FAITH ON LEGAL ADVICE OR OTHER REPORTS.

Even if there were admissible evidence of legal advice to the Board and even if Mr. Van Gorkom's short oral presentation to the Board were somehow a "report" within the meaning of §141(e), there is nothing in the record to support a conclusion that any TU director relied in good faith on Mr. Van Gorkom or Mr. Brennan's oral "report" so as to avoid liability. No director testified as to such reliance.

* Indeed, in full post trial briefing in the Court below and in briefs and oral arguments in this Court, defendants never once raised §141(e) or reliance on advice of counsel as a defense.

Furthermore, reliance on Mr. Van Gorkom's brief oral presentation or the inadmissable oral advice of counsel would be neither reasonable nor in good faith.

To claim the protection of the business judgment rule, directors must "inform themselves, prior to making a business decision, of all material information reasonably available to them." Aronson v. Lewis, supra, slip op at 13. (Emphasis added). Having failed under Aronson to fully inform themselves of all material facts,* defendants cannot bootstrap themselves into the business judgment rule by claiming reliance solely on brief oral advice from Mr. Van Gorkom or Mr. Brennan.** Given (1) the magnitude of the transaction on which the directors were passing and (2) the directors' affirmative obligation to fully inform themselves of all material facts reasonably available, the defendants cannot save themselves by asserting that they relied on oral "reports" of such shallow quality in quickly determining to accept, recommend, and use their best efforts to obtain stockholder approval of the Merger. Such mechanical reliance without critical inquiry or careful scrutiny is neither reasonable nor in good faith. Such reliance cannot substitute for the directors' obligation to exercise an informed judgment, particularly here where the Board was not presented with an emergency situation and easily could have sought additional information and taken more time to consider the matter before it.

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* For example, no director asked for Mr. Romans' studies even though Mr. Romans told the Board that his studies showed that the stock was worth between $55 and $65 per share (A-1353).

** Of course, the situation would be quite different if the Board had followed the steps listed at pp. 16-18, supra.

QUESTION: c) If there is insufficient evidence of record to support a conclusion that one or more directors, other than Van Gorkom and Chelberg, are entitled to the protection of the business judgment rule by reasonable reliance upon 8 Del. C. §141(e), what effect, if any, does the stockholder vote of February 10, 1981, have in relieving such director of a duty to timely exercise business judgment in connection with the sale of TU?

RESPONSE: III. THE FEBRUARY 10, 1981 STOCKHOLDER VOTE DID NOT RELIEVE THE DIRECTORS OF THEIR DUTY TO TIMELY EXERCISE BUSINESS JUDGMENT IN CONNECTION WITH THE SALE OF TU.

A. NO STOCKHOLDER VOTE CAN RELIEVE A DIRECTOR OF HIS DUTY TIMELY TO EXERCISE BUSINESS JUDGMENT.

No stockholder vote can relieve directors of the duty timely to exercise business judgment "for the reason that the possible indifference, or sympathy with the Directors, of a majority of the stockholders would not supply the necessary element of good faith exercise of business judgment by directors in dealing with the corporate assets." Beard v. Elster, Del. Supr., 160 A.2d 731, 737 (1960). Directors, not the shareholders, manage the corporation. 8 Del. C. §141(a); Aronson v. Lewis, supra; Maldonado v. Flynn, Del. Ch., 413 A.2d 1251 (1980), rev'd on other grounds sub nom., Zapata Corp. v. Flynn, Del. Supr., 430 A.2d 779 (1981). Long ago, the Court explained the roles of shareholders and directors in Continental Securities Co. v. Belmont, N.Y. App., 99 N.E. 138, 141 (1912).

> The board of directors represents the corporate body. It is provided by statute in this state that the affairs of every corporation shall be managed by its Board of Directors...* The directors hold their office charged with the duty to act for the corporation according to their best judgment, and in so doing they cannot be controlled in the reasonable exercise and performance of such duty.
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* The Delaware General Corporation Law contains a carefully crafted procedure for prior full board of director approval under 8 Del. C. §141(c) of every major corporate action before submission to the stockholders: certificate amendments under §242; mergers or consolidations under §§251 or 252; sales of all or substantially all assets under §271; and dissolutions under §275.

> As a general rule, stockholders cannot act in relation to the ordinary business of a corporation. The body of the stockholders have certain authority conferred by statute which must be exercised to enable the corporation to act in specific cases, but except for certain authority conferred by statute, which is mainly permissive or confirmatory,... they have no express power given by the statute. Any action by them relating to the details of the corporate business is necessarily in the form of an assent request or recommendation.

(Emphasis added). See Campbell v. Loew's Incorporated, Del. Ch., 134 A.2d 852, 862 (1957); Empire Southern Gas Co. v. Gray, Del. Ch., 46 A.2d 741, 744 (1946). Section 141 confers managerial authority on the Board. Liability is tempered by recognition of the business judgment rule. The stockholders are not given power to manage. Nor do they have the power to grant or withhold director liability by voting to excuse the directors from exercising their business judgment. A holding to the contrary would mean stockholder votes would no longer be "confirmatory" or "permissive."

Defendants' professed eagerness to let the TU stockholders pass upon the merger -- without even a rudimentary evaluation or guidance from their directors -- is a transparent attempt to mask a glaring dereliction and illegal delegation of the directors' statutory duty. Before submitting the merger to the shareholders, the TU directors were statutorily required to "adopt a resolution approving an agreement of merger...." 8 Del.C. §251(b). Implicit in that requirement is the fiduciary obligation to make "an informed judgment in good faith which can be attributed to a rational business purpose." Muschel v. Western Union Corp., supra, 310 A.2d at 909; accord, Gimbel v. Signal Companies, Inc., supra No ratification vote can supply the necessary managerial care, deliberation and prudence which the DGCL requires of a board of directors.

Moreover, the directors' statutory duty cannot be delegated. Field v. Carlisle Corp., Del. Ch., 68 A.2d 817 (1949). Such delegation is illegal and will not be permitted. Adams v. Clearance Corp., Del. Supr., 121 A.2d 302 (1956).* In the present case, the stockholder vote followed a total abdication by the directors of their duty of due care and an attendant illegal delegation of their responsibilities to scrutinize the proposed merger. Such irresponsibility by the directors cannot be ratified by the stockholders. As Chancellor Seitz stated:

> So long as the corporate form is used as presently provided by our statutes this Court cannot give legal sanction to agreements which have the effect of removing from directors in a very substantial way their duty to use their own best judgment on management matters.

Abercrombie v. Davies, supra, 123 A.2d at 899;** see also, University Computing Co. v. Lykes-Youngstown Corp., 5th Cir., 504 F.2d 518, 532 (1974) (directors cannot be ousted from managerial responsibility.)

To assert that the February 10, 1981 vote relieves the directors of their duty timely to exercise business judgment ignores both the statutory duty under §251, the prohibition against its delegation, and the fiduciary relationship between directors and stockholders. Implicit in that fiduciary relationship is the trust and confidence

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* Accord, Abercrombie v. Davies, Del. Ch., 123 A.2d 893, rev'd on other grounds, Del. Supr., 130 A.2d 338 (1957); Chapin v. Benwood Foundation, Inc., Del.Ch., 402 A.2d 1205 (1979), aff'd sub nom., Harrison v. Chapin, Del. Supr., 415 A.2d 1068 (1980).

** Under Delaware law, directors are not permitted to delegate the responsibility for adopting an agreement of merger under 8 Del. C. §251 to officers of the corporation or a committee of their number. 8 Del. C. §141(c); cf., Clarke Memorial College v. Monaghan Land Co., Del. Ch., 257 A.2d 234 (1969) (enjoining the delegation to corporate officers of the board's authority to sell corporate assets under 8 Del. C. §271). In this case, Mr. Van Gorkom acting on his own as a self-appointed committee of one, negotiated the agreement of merger with the Pritzkers (See discussion Section I, supra). The board of directors never really took the deliberative steps required by the Delaware merger statute. Such action was illegal. 8 Del. C. §251(b). It cannot be ratified by shareholders. Clarke Memorial College, supra.

rightfully reposed by stockholders in decisions made by directors. Such reliance is evidenced by the extent to which stockholders customarily follow management's recommendations. See, e.g., Mayer v. Adams, Del. Supr., 141 A.2d 458 (1958); Schreiber v. Bryan, Del. Ch., 396 A.2d 512 (1978); see also, Weiss, The Law of Take Out Mergers: A Historical Perspective, 56 N.Y. Univ. L. Rev. 624, 676 (1981) ("shareholders often behave like sheep when asked to vote on a transaction, and support docilely any recommendation management makes"); compare, Note, The Propriety Of Judicial Deference To Corporate Boards Of Directors, 96 Harv. L. Rev. 1894 (1983).

In this case, the TU directors betrayed the trust and confidence reposed in them by the stockholders by (1) failing to analyze and consider the Pritzker proposal and (2) misrepresenting that they had. By recommending the proposal to the stockholders, they falsely represented to the stockholders that they had brought their full attention and expertise to bear on the Merger and had decided that the Merger was in the stockholders' best interest. In fact, they had not. Stockholder ratification of transactions was never intended to remedy failures to carry out statutorily mandated duties and cannot in this case. Michelson v. Duncan, supra; Kerbs v. California Eastern Airways, Inc., Del. Supr., 90 A.2d 652 (1952); 2A W. Fletcher, Cyclopedia of the Law of Private Corporations §764 (Perm ed. 1982) (stockholders empowered to ratify "acts done or authorized by the board of directors" if such "acts are such as may be done or authorized by the stockholders.").

Allowance of ratification would result in an uninformed, unanalyzed adoption of fundamental corporate changes, contrary not only to law but to sound business practice as well. Under Delaware law, stockholders have a right to expect that their directors, who generally have far more business skill than stockholders, will vigorously represent the stockholders' interests. Chazen, Fairness from a Financial

Point of View in Acquisitions of Public Companies: Is "Third-Party Sale Value" the Appropriate Standard?, 36 Bus. Law. 1439, 1475 (1981) ("the business corporate laws hold out to stockholders the promise that their interests will be represented by a board of directors"). If stockholder ratification is held to cure the directors' failure to consider and pass on a proposed merger, then the stockholders are deprived of their right to have the directors make an informed judgment and recommendation on the merger and are left to make their own judgment on the merger.* If that be the rule, the statutory requirement of board approval for a merger would be reduced to a nullity. Therefore, given a finding that one or more TU directors are not entitled to the protection of the Business Judgment Rule, the stockholder vote of February 10, 1981 in no way relieved such directors of their duty timely to exercise business judgment.**

B. THE STOCKHOLDER VOTE OF FEBRUARY 10, 1981 WAS NOT A FULLY INFORMED VOTE AND IS A NULLITY.

Assuming arguendo that a stockholder vote could have cured the TU Board's egregious dereliction of duty, the February 10, 1981 stockholder vote is a nullity because of the inadequate and misleading proxy materials. Weinberger v. UOP, Inc., supra, 457 A.2d at 712; Michelson v. Duncan, supra, 407 A.2d at 220. For a stockholder vote to have any meaning, that vote can be taken only after full

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* "A shareholder vote is a take it or leave it proposition." Chazen, supra, 36 Bus.Law. at 1475. Such vote cannot take the place of genuine negotiation, a task properly assigned to directors. Id.

** The shareholder vote in this case was not taken until February 10, 1981. This lawsuit was instituted on December 19, 1980, two months prior to the vote. Where a shareholder vote, characterized by incomplete disclosure of germane facts, is taken after the institution of a lawsuit contesting the matter to be voted on, that subsequent effort to ratify a challenged act is viewed with "apprehension" by the courts of this State. Blish v. Thompson Automatic Arms Corp., Del. Supr., 64 A.2d 581, 604 (1948). Compare, Michelson v. Duncan, supra.

disclosure of the material facts related to the transaction in issue. Weinberger v. UOP, Inc., supra; Michelson v. Duncan, supra.*

In the present case, the material nondisclosures in the initial proxy materials (PX 98: A-2216) were not cured by the late mailing of the January 26 "Supplement to Proxy Statement" (the "Supplement") (PX 100: A-2324).** Both documents omitted crucial facts, germane to the stockholders' decision to accept or reject the Pritzker offer for TU. (See the catalogue of material omissions contained in Appellants' Opening Brief at pp. 61-67). In addition, the Supplement was not sent out the full 20 days before the merger vote required by 8 Del. C. §251(c). Consequently, TU's stockholders did not have adequate time to receive, consider and act upon the information contained in the Supplement. In American Pacific Corp. v. Super Food Services, Inc., Del. Ch., C.A. No. 7020, Longobardi, V.C. (December 6, 1982), the Court enjoined a stockholders meeting in part because supplemental proxy materials, mailed thirteen days before the meeting, provided insufficient time for Super Food stockholders to receive and act on the supplemental information. (slip op. at 5, 6). At best, TU's Supplement was only mailed 15 days before the February 10 meeting. Even if it had cured defendants' lack of candor, it came too late under §251(c) or American Pacific to cure the tainted vote.

Furthermore, to contend that the stockholder vote of February 10, 1981 is a valid ratification of the merger, is to say that the vote effectively ratified those acts of

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* The burden is on the parties relying on the stockholder vote "to show that they completely disclosed all material facts relevant to the transaction." Weinberger v. UOP, Inc., supra, 457 A.2d at 703. Defendants have not met that burden.

** The Supplement concedes that the recitation of additional facts not found in the original proxy statment relating, inter alia, to the origins of the Merger and the September 20, 1980 meeting where "material" to the TU stockholders. (PX 100: A-2324).

the directors which now deprive them of the business judgement rule. Unless those acts and the facts surrounding them were fully disclosed to the shareholders in a timely fashion prior to the vote (and they were not) there can be no ratification. Michelson v. Duncan, supra; Wyndham, Inc. v. Wilmington Trust Co., Del. Super., 59 A.2d 456 (1948). To obtain the benefit of stockholder ratification of their action, the directors are required to disclose all factual information relative to that action. Michelson v. Duncan, supra.

In Michelson, suit was brought to overturn amendments to a stock option plan as a breach of fiduciary duty and waste. There, the proxy statement described in detail the actions of the board and the effect of the modifications. Moreover, a copy of the complaint was included in the appendix to the proxy statement. Accordingly, the stockholders had before them a detailed factual description of the director action that they were being asked to ratify and the contentions of the plaintiffs opposing that action.

In the present case, the original proxy materials did not disclose facts relating to director action which deprived the directors of the protection of the business judgment rule. For instance, the stockholders were not told that, not only did the directors not read the agreement, but that the Merger documents were not even made available to them at the September 20, 1980 Board meeting. Further, the stockholders were not told how the $55 Merger price was set nor of the fact that the fairness of that price was never evaluated by the Board. The original proxy materials also did not reveal the fact that at the October 8, 1980 Board meeting the Merger amendments were not available to the Board and were not reviewed by the Board or by counsel. The Supplement did make mention of this lawsuit, but did not explain that the Board's recommendation of the Merger and its $55 price was the result of a contractual commitment, rather than a studied decision. It is these facts which the stockholders of TU had to be told with adequate time to consider their import if their vote was to have force and effect. Since the vote was taken without disclosure of such facts to the stockholders that vote is meaningless. Compare, Wyndham, supra (resolution of a board of directors granting broad powers to a fellow director could not be considered ratification of short sales of stock about which the directors had no knowledge). It ill behooves the director defendants, who obtained stockholder approval by the misstatement that they had properly determined that the merger price was fair, to turn around and use that approval to avoid liability for failing to properly determine the fairness of the price before presenting it to the stockholders.

In light of the failure to reveal germane facts which a reasonable shareholder would consider important in deciding whether to approve the merger, Lynch v. Vickers Energy Corp., Del. Supr., 383 A.2d 278, 281 (1977), the stockholder vote of February 10, 1981 has no effect whatever in relieving the directors of their duty timely to exercise business judgment on September 20, 1980 in connection with the sale of TU. "One cannot ratify that which he does not know." Cahall v. Lofland, Del. Ch., 114 A. 224, 234 (1921); aff'd Del. Supr., 118 A. 1 (1922).

QUESTION: d) Can shareholder ratification of the merger, by less than unanimous vote, cure director approval of the merger if one or more directors are found not entitled to the protection of the business judgment rule for absence of good faith?

RESPONSE: IV. SHAREHOLDER RATIFICATION OF THE MERGER, BY LESS THAN UNANIMOUS VOTE, CANNOT CURE DEFENDANTS' APPROVAL OF THE MERGER.

A. LESS THAN A UNANIMOUS SHAREHOLDER VOTE CANNOT RATIFY THE WASTE RESULTING FROM THE SALE OF ONE MILLION SHARES TO PRITZKER AT A SHOCKINGLY INADEQUATE PRICE.

The $55 merger price was not the result of arms-length negotiation. It was suggested by Mr. Van Gorkom and snatched up by Mr. Pritzker (A-1299-1300). In sharp contrast, the price at which the 1,000,000 TU shares were sold to Mr. Pritzker was only $38. There was no negotiation as to that price either (A-1324).

The gross inadequacy of the $38 price paid to TU for Mr. Pritzker's million-share option appears throughout the trial record. For example, Mr. Romans, the Chief Financial Officer of TU, said that the appropriate price range for TU's stock was between $55 and $65. Articles in the financial press indicated that the value of the TU stock was above $65 (PX 34: A-2076). KKR had made an initial offer of $60. Finally, General Electric Credit Corporation made a draft opening offer of $57 in a stock-for-stock transaction with a $60 cash alternative. The $17 million aggregate difference between the $38 price Mr. Pritzker actually paid and the $55 Merger price should have gone to the TU stockholders. Instead, the $17 million lock-up served to deter competitive bids and prevented the TU stockholders from realizing the additional profit competitive bidding would bring. Mobil Corporation v. Marathon Oil Co., supra.

Defendants' acceptance of such a shockingly inadequate price for TU's stock is waste. Kerbs v. California Eastern Airways, Inc., supra; Saxe v. Brady, Del. Ch., 184 A.2d 602, 605 (1962). Only unanimous stockholder approval can ratify waste. Gottlieb v. Heyden Chemical Corp., Del. Supr., 91 A.2d 57 (1952); Schreiber v. Bryan, supra, 396 A.2d at 521; Saxe v. Brady, supra. As the court stated in Gottlieb, supra, 91 A.2d at 58-59:

> If appraisement of these respective values brings the court within the realm in which reasonable men, fully informed and acting in good faith, may be expected to differ, then the court will enter judgment for the defendant. Within this realm the majority may enforce its will upon dissenting minority; outside it they may not. (Emphasis added)

No reasonable person, fully informed and acting in good faith, could conclude under the circumstances of this case that the $38 price for the Pritzker block of stock was proper when the merger price was $55. The sale at $38 was purely an act of waste intended to "lock up" the sale of TU to Mr. Pritzker prior to a stockholder vote. It could not be ratified by less than a unanimous vote of the TU stockholders.

B. A UNANIMOUS SHAREHOLDER VOTE IS REQUIRED BECAUSE THE DIRECTORS HAVE ACTED IN BAD FAITH.

Where, as here, the stockholders were not fully informed, and the directors have not acted in good faith, the uninformed majority is not permitted to force its will upon a dissenting minority:

> The policy of enforcing strict honesty of directors, who occupy a fiduciary position, is undoubtedly furthered by forbidding acquiescence in their misdeeds. The knowledge that his action cannot be condoned — even by approval of a majority — and will always be subject to the scrutiny of dissenting shareholders, may deter the director who contemplates fraud.

Note, Shareholder Ratification of Directors' Fraudulent Acts, 53 Harvard L. Rev. 1368, 1372 (1940). (Emphasis added).

In Gottlieb v. Heyden Chemical Corp., Del. Supr., 90 A.2d 660, 665 (1952), this Court stated:

> Ratification by stockholders, indeed, is frequently decisive of controversies in this field of law. In some instances it is the only type of corporate action which is not voidable. In other instances its purpose is simply to permit the action of the board of directors to be reviewed on its merits, without the handicap of enforced suspicion which would otherwise be present where board members have represented themselves as well as their corporation. But unless ratification is unanimous, it can never constitute the only requisite to validity.

(Emphasis added). Later, in Mayer v. Adams, supra, this Court stated:

> But, correlatively, the policy of our courts has always been to hold the directors and the majority stockholders to strict accountability for any breach of good faith in the exercise of these powers, and to permit any minority stockholder to seek redress in equity on behalf of the corporation for wrongs committed by the directors or by the majority stockholders.

141 A.2d at 461.

In light of that strong mandate requiring strict accountability for breaches of good faith, and where, as here, the directors do not enjoy protection of the business judgment rule because of their manifest absence of good faith, less than a unanimous informed vote by the stockholders does not have a curative effect. A breach of the duty of due care cannot be cured by less than a unanimous vote of the stockholders. Henn, Corporations, §194, p. 380 (2d ed. 1970). To hold otherwise would have the anomalous result of permitting the wrongful conduct of TU's directors to be approved by the same vote as the statute requires for the approval of a merger under ordinary circumstances (i.e., where there has been full and fair disclosure to the stockholders).

CONCLUSION

For the reasons stated both above and in the plaintiffs' original briefs to this Court,

a) There is abundant evidence to support the conclusion that there was an absence of good faith on the part of all the TU directors;

b) There is no evidence that defendants received or relied upon reports under 8 Del. C. §141(e);

c) The February 10, 1981 stockholder vote does not relieve the directors of their duty to timely exercise business judgment in connection with the Merger of TU; and

d) Shareholder ratification cannot cure clearly improper director approval of the merger, especially where waste is involved.

The Court should reverse the decision of the lower Court.

Respectfully submitted,

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