IN THE SUPREME COURT OF THE STATE OF DELAWARE

ALDEN SMITH, et al.,	)	
	)	
Plaintiffs Below,	)	
Appellants,	)	
	)	
v.	)	No. 255, 1982
	)	
JEROME W. VAN GORKOM, et al.,	)	ON APPEAL FROM THE COURT
	)	OF CHANCERY IN AND FOR
Defendants Below,	)	NEW CASTLE COUNTY,
Appellees.	)	CIVIL ACTION NO. 5642

PLAINTIFFS' REPLY SUPPLEMENTAL BRIEF

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I. PLAINTIFFS' REPLY TO DEFENDANTS' RESPONSE TO THE COURT'S QUESTION (a)

THE RECORD SUPPORTS A CONCLUSION THAT THERE WAS AN ABSENCE OF GOOD FAITH ON THE PART OF ONE OR MORE DIRECTORS OF TU WHICH DEPRIVES THEM OF THE PROTECTION OF THE BUSINESS JUDGMENT RULE.

(1) Plaintiffs Have Never Conceded That Defendants' Uninformed Decision Did Not Amount to Absence of Good Faith

In their initial response to question (a), defendants avoid answering the specific question posed by the Supreme Court by diverting the Court's attention to bad faith of a kind evidenced by fraud or self-dealing (DSB 3-4).* Plaintiffs have not represented to this Court that bad faith of a type found in interested director transactions make the Business Judgment Rule inapplicable. Plaintiffs' statement in their original reply brief to this Court makes that clear (PRB 2), and defendants admit as much (DSB 23). However, plaintiffs have maintained from the outset of this litigation that TU directors' failure to inform themselves of the basic facts pertaining to the merger evidences their lack of good faith and deprives them of the protection of the Business Judgment Rule (See, A-26 Complaint, ¶24; A-54 Plaintiffs' Amended Verified Complaint, 1/28/81, ¶24; A-182 Plaintiffs' Amended Verified Complaint, 1/30/81, ¶26). Plaintiffs have never altered their stance on this fundamental point (PRB 4). The TU directors' utter ignorance of all salient facts relating to the merger is still the crucial issue in this case. The TU directors' failure to inform themselves of the facts graphically illustrates their absence of good faith. That lack of good faith cannot be cured by alleging a "pure heart" or by bald pleading after the fact that the directors honestly believed that $55.00 was a good price.

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* Reference to Plaintiffs' Opening Supplemental Brief are designated "(PSB __)"; references to Defendants' Opening Supplemental Brief are designated "(DSB __)".

(2) A Good Faith Defense Requires More Than the Naked Allegation of a Pure Heart

In their response, defendants equate the Court's question as to whether there is sufficient evidence* to support a finding of absence of good faith with the converse: that there was no proof of bad faith (i.e., fraud, self-dealing) (DSB 3-4). The defendants would have the Court hold that, no matter how little the directors do to educate themselves about a pending corporate decision, so long as they allege the purity of their hearts, they are automatically within the protection of the Business Judgment Rule.

If the defendants' position were adopted by this Court, corporate directors would have absolutely no affirmative obligation to educate themselves about any corporate matter before making a decision. In order to come within the protection of the Business Judgment Rule, the directors would only have to refrain from fraud, dishonesty, or self-dealing. The absurdity of this argument is self-evident. Moreover, it contravenes every recognized principle of corporate and fiduciary responsiblity.

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* In a further attempt to divert the Court's attention from the issues at hand (DSB 3), defendants overstate the proper scope of review. In a case such as this where the trial Court sat without a jury, the appeal is upon both the law and facts. On appeal the Court is free, in a proper situation, to make its own inferences and deductions from the facts. This is particularly true where, as here, the trial Court based its findings nearly exclusively on a paper record rather than live testimony. Fiduciary Trust Co. v. Fiduciary Trust Co., Del. Supr., 445 A.2d 927 (1982); International Boiler Works Co. v. General Water Works Corp., Del. Supr., 372 A.2d 176, 177 (1977); Blank v. Steiner, Del. Supr., 224 A.2d 242, 247-49 (1966) (Hermann, J., dissenting); duPont v. duPont, Del. Supr., 216 A.2d 674 (1966); New York Trust v. Riley, Del. Supr., 16 A.2d 772, 783 (1940).

This Court has required as one of the most basic corporate responsibilities under Delaware law that directors undertake the minimum affirmative action of informing themselves of all relevant information before making a corporate decision. Aronson v. Lewis, Del. Supr., No. 203, 1983, Moore, J. (March 1, 1984), slip op. at 13. This minimum duty is required to ensure that directors act affirmatively to protect the corporation and its shareholders. Guth v. Loft, Del. Supr., 5 A.2d 503, 510 (1939).

Defendants' own authority recognizes the importance of the affirmative obligation on the director. In Black and Prussin, The Business Judgment Rule and Shareholder Derivative Actions: Viva Zapata", 37 Bus. Law 27 (1981), the authors stated that corporate directors cannot be found to have acted in good faith unless the directors have first affirmatively investigated the decision to be made. Id. at 33. See, Gimbel v. Signal Cos., Inc., Del. Ch., 316 A.2d 599, 608-609 (1974); accord, Arsht, Fiduciary Responsibility of Directors, Officers and Key Employees, 4 Del. J. Corp. L., 652, 661 (1979). Alleging a pure heart while acting with an empty head is not enough to bring a director within the protection of the Business Judgment Rule. Donovan v. Cunningham, 5th Cir., 716 F.2d 1455, 1467 (1983) (requiring affirmative action by trustees to satisfy fiduciary obligations). Compare, Lutz v. Boas, Del. Ch., 171 A.2d 381, 395 (1961).

In this case, as plaintiffs have demonstrated, the record shows that the directors did absolutely nothing to inform themselves of even the most basic facts about the outright sale of a $690 million corporation (PSB 7-16). Thus, while there is no allegation and no proof of dishonesty, fraud or self-dealing, nevertheless, defendants are liable because there is no evidence that TU's directors exercised the good

faith that is required of directors in order to avail themselves of the shield of the Business Judgment Rule.

(3) Where the Record Reveals a Blatant Disregard of the Factors Going to the Determination of the Merger Price, No Presumption Arises That the Directors Acted to Obtain the Best Price Possible

The defendants further argue that, because the directors of TU were also stockholders, it was obviously in their best interest to get the best price obtainable, and that they must therefore have done so (DSB 4-6). There are several fundamental flaws in this contention.

Even if such an argument were applicable, it would vanish in the light of the evidence to the contrary. TU's stock had been valued by its own Chief Financial Officer, Mr. Romans, at between $55.00 to $65.00 per share in a transfer of the entire company (A-1338). Indeed, prior to the October 4 meeting of the TU Board of Directors, Mr. Romans expressed his disapproval of the $55.00 price, stressing that it was not a fair price and arguing in favor of $60.00 or $65.00 for the merger (Chelberg 192).

Moreover, Mr. Van Gorkom made no attempt to educate himself as to TU's actual value in terms of range of the percentage of premiums paid in comparable mergers or the overall value of TU in a sale of 100% of TU (A-1354-55). Thus, although in certain circumstances it may be said that director-stockholders would demand the best price simply by virtue of their stockholdings, that inference has no applicability where the directors in question accepted an arbitrary price because it was "personally acceptable" to the President, Mr. Van Gorkom, and sought no financial information or analysis from either the company's own Chief Financial Officer (whose section had already prepared a preliminary study of the value of the stock in the transfer of 100% of the company) or their investment banker.

Moreover, defendants' argument fails for a much more basic reason. Defendants' entire defense of the $55.00 price is that, because it represented an amount over market, they honestly believed it to be a good or fair price. However, Mr. Van Gorkom testified that the current market price of TU's stock was substantially below the actual value of TU's stock:

> "There was no reason to think that there was going to suddenly be a greater appreciation of our company if we turned down the Pritzker offer because we had increased our earnings steadily for ten years, and had seen practically no movement in our stock price." (A-1117, emphasis supplied.)

Mr. Van Gorkom further testified:

> "[T]hough our company was not appreciated in the financial world, in my opinion, and that lack of appreciation being represented at the low price we traded at, we had a good earnings record. Our earnings had increased over the last seventeen years almost every year, with a couple of exceptions and at a rate of about 10 or 11 percent." (A-1078, emphasis supplied.)

Mr. Chelberg testified that he and all of TU's senior management believed that the market price of TU's stock did not reflect the strengths of the company (Chelberg 72, 77-80). In addition, Mr. Chelberg testified that TU had not "in the last five years" even requested a determination of fair value of the stock from any source, even their own investment banker or Boston Consulting Group (Chelberg 81-82). Finally, TU had not undertaken at any time a study of the percentage of premium above market paid in comparable mergers (A-1354-55; Chelberg 90).* An obvious question arises in the face of this admission by the defendants: how could the Board "honestly believe" that the price was fair because it was above the market price when they knew that TU stock's current

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* Mr. Van Gorkom stated that there was "no such thing as a comparable situation" ((A-1354). This rather telling admission underscores the fact that the awesome size of this transaction required that a detailed valuation should have been obtained.

market price was far below its actual value in view of TU's performance and its prospects? This is especially true since TU had never undertaken a study of comparable premiums. The overwhelming ignorance of the various factors crucial to the determination that the $55.00 price was fair destroys any presumption that the TU directors honestly thought that $55.00 was a fair price for 100% of the TU shares. The testimony cited by defendants in their Opening Supplemental Brief reiterates this point (DSB 6-9).

Mr. Browder testified that he "felt" that the price was fair because it was substantially higher than the market price (Browder 176). As discussed above, none of the TU management believed that its market price accurately reflected TU's value. However, Mr. Browder did not consider whether the market price was in any way an accurate indicator of the value of TU's stock. Mr. Browder further testified that he "felt" based on his general knowledge of TU's operations and financial results that $55.00 would be a fair price to him. Mr. Browder did not seek, consider or rely upon any reasoned analysis, either from TU's Chief Financial Officer, Mr. Romans, or its investment banker. Rather, because $55.00 "felt" good to Mr. Browder, he was willing to pass that figure on to the shareholders and allow them to evaluate the financial propriety of selling a $690 million "cash cow" at $55.00 per share, a job specifically delegated to Mr. Browder and his cohorts by Delaware law. Again, a pure heart does not excuse an empty head.

Defendants also parade the deposition of Professor Wallis. He simply made a judgment in vacuum that the $55.00 price was "a reasonable price" without taking the time to make an investigation of even the most rudimentary facts concerning the merger, including the terms and the price (Wallis 50-53).

In this connection, it should be noted that, contrary to what

defendants now assert, the directors did not claim to have determined that $55.00 in and of itself was a "fair price". Rather, they claimed that they believed the $55.00 was simply a "floor" and that they were led to believe that the deal that they were accepting would permit TU to receive other higher bids. In fact, the original merger documents, which were never produced and which neither the directors nor Mr. Van Gorkom read, specifically precluded any alternate proposal (PSB 15). Thus, a claim that they acted in good faith is ludicrous.

Defendants also rely on the testimony of Mr. Johnson and Mr. Van Gorkom, the only TU directors to testify at trial,* to support the $55.00 price. The entirety of Mr. Johnson's testimony addresses the $55.00 price in terms of its premium above market. Mr. Van Gorkom reiterated this identical testimony at trial. He said simply that, when compared to the range at which the stock had been selling, the $55.00 price was a good one (A-1116-17). However, as discussed above, none of TU's officers or management, least of all Mr. Van Gorkom, believed that the market price accurately reflected the inherent value of the TU stock. Thus, defendants' reliance on testimony based upon the premium over market price betrays defendants' uninformed judgment.

Moreover, the testimony recited by the defendants in their Supplemental Brief premises that $55.00 was a fair price, but ignores the fact that the sale was of 100% of their company. Even at trial, Mr. Johnson was evaluating the $55.00 price not on the basis of the sale of the entire company but rather as to what he thought the market value of the stock would be in the foreseeable future (B-1227-1228). That price

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* Contrary to defendants' assertion (DSB 9), the overwhelming evidence before the trial Court consisted of documentary evidence. Therefore, the "clearly erroneous" standard of review does not apply. See footnote, supra, p. 2.

differs drastically from one that would be commanded by the sale of 100% of the company. See, Cheff v. Mathes, Del. Supr., 199 A.2d 548, 555 (1964); Kaplan v. Goldsamt, Del. Ch., 380 A.2d 556, 569 (1977).

The foregoing shows just how inadequate Mr. Johnson's, or indeed all of the directors', evaluation was. They should have been provided an analysis by an investment banker or chartered financial analyst not of what the prospective performance of the stock might be expected to be but what a company seeking to buy the TU stock could be expected to pay for 100% of the company. Cf., Kaplan v. Goldsamt, supra, 380 A.2d at 568. Such price would include a premium. The fact that the TU Five-Year Forecast itself had suggested that a $50.00 price would be fair for 30% (not 100%) of the company, the fact that even in the face of the definitive Pritzker merger announcement, KKR made an opening offer of $60.00 per share (A-1423), the fact that G.E. also made a draft offer of $57.00 in stock or $60.00 in cash (A-1461), all constitute solid objective evidence that the $55.00 price that Mr. Van Gorkom recommended and his fellow directors so casually accepted was totally inadequate.

(4) Defendants' Disregard of Their Most Basic Duties in the Face of a Very Unique, Pressurized Takeover Bid Further Evidences Their Lack of Good Faith

In their Opening Supplemental Brief, and indeed throughout this entire litigation, the defendants have attempted to characterize the TU directors' actions as deliberate, thoughtful and conscientious. As the record shows, however, the TU directors were kept wholly uninformed until the September 20, 1980 Board meeting, at which time they approved the merger of TU with GL Corporation in little over an hour (A-1109; PSB 7). In light of these rarified circumstances, defendants were under an even greater duty to demand access to all information relevant to the

merger and to scrutinize and evaluate all aspects of the merger proposal. Lipton, Takeover Bids in the Target's Boardroom, 35 Bus. L. 101, 121-23 (1979). See, e.g., Pennzoil Co. v. Getty Oil, Del. Ch., C.A. No. 7425, Brown, C. (February 6, 1984). Nevertheless, the TU directors sought no expert advice, undertook no current valuation study, resorted to no existing valuation studies, failed to read the merger agreements which they would endorse, and committed the TU stockholders to a cashout merger at $10.00 to $12.00 below what Mr. Romans and the financial press thought to be a good price for the TU stock.* (A-1338; Chelberg 192; PX 34: A-2077) This conduct stands in glaring contrast to that required of corporate directors:

> "The corporate directors should be furnished with appropriate information regarding every important matter requiring board action; in every case, there should be available to the corporate directors sufficient information furnished in time so as to permit an informed judgment. If for any reason sufficient information is not made appropriately available, the corporate directors should request that action be delayed until the information is made available. If action is nonetheless taken, the corporate directors should at a minimum request that his abstention, and reason therefor, be recorded in the minutes of the meeting. Under these circumstances, he should consider the need for his resignation."

The Corporate Director's Guidebook, 33 Bus. Lawyer 1591, 1602 (1978) (emphasis added).

The TU directors measured up to none of these requirements. They are entitled to no good faith defense.

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* In reporting the TU Merger, on September 26, 1980, Oppenheimer & Co., Inc. stated (A-2077): "In considering what price tag Trans Union might command if a competitive bidding situation were to develop, it is interesting to examine Trans Unions' supplemental inflation reporting presentation as required by the FASB. Because of the financial nature of the company's primary leasing business, Trans Union believes that the $67+ per share net asset value arrived at in that presentation is of greater significance than the replacement cost data provided in compliance with SEC requirements. Trans Union, furthermore, boasts pretax cash flow in excess of $13 per share. It would not, in our opinion, be difficult to arrive at a price of $65, close to 'inflation adjusted' book value and less than five times pretax cash flow." (Emphasis added.)

(5) Defendants Have Failed to Respond to the Court's Question

As the above discussion makes clear, defendants have totally failed to respond to the Court's actual question. The Court asked specifically whether there is "sufficient evidence of record to support a conclusion that there was an absence of good faith" on the part of the TU directors. Defendants have not once resorted to the record. Instead, defendants rely on the erroneous opinion of the lower Court (DSB 5) and the presumptions of good faith that normally attend informed business decisions (DSB 9). The Court did not ask the parties to address the ultimate conclusions of the Court below. Rather, the Court instructed the parties to point to evidence in the record that shows the absence or presence of good faith on the part of the directors.

The defendants' reliance on a presumption of good faith is equally circuitous. The Court asked what evidence exists to support a conclusion on the absence of good faith. The defendants say that good faith is proven by a presumption of good faith that is afforded to informed directors of Delaware corporations. This simply does not respond to the Court's question. Moreover, a presumption vanishes in the presence of actual evidence. Karasik v. Pacific Eastern Corporation, Del. Ch., 180 A. 602, 607 (1935); Arsht, supra, 4 Del.J.Corp.L. at 662. The record evidence shows the absence of good faith on the part of the defendant directors.

Because they cannot, the defendants have not pointed to the actual record to substantiate any conclusion other than the fact that there was an absence of good faith on the part of the directors of TU in connection with the events from August 27 through January 26, 1981.

II. PLAINTIFFS' REPLY TO DEFENDANTS' RESPONSE TO THE COURT'S QUESTION (b)

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.

(1) The TU Board Received No §141(e) Reports to Consider in Connection With the Merger

The defendants assert, "As we have already shown, each of the directors acted in good faith." (DSB 11) The defendants have not been able to show that they acted in good faith generally. Specifically, they have not demonstrated that they relied in good faith on the scant oral "reports" made to them at the September 20 and October 8 Board meetings. On the contrary, the total absence of any §141(e) reports such as would be expected to exist in the context of a $690 million cashout merger, negates any possibility of an assertion of good faith by the defendants. Plainly put, it is impossible to find that the Board acted in good faith reliance on Mr. Van Gorkom's one brief oral report, unsubstantiated by any financial information or expert advice either from within or without the company, as the sole basis for approving a $690 million merger agreement which neither the Board nor Mr. Van Gorkom had ever read.

At a bare minimum, the directors should have required detailed written reports commensurate with the magnitude and importance of the transaction under consideration. In this connection, some indication of the minimum requirements is set out in Martin Lipton's article cited in Plaintiffs' Opening Supplemental Brief (PSB 16-18). Instead of asking for any information, written or otherwise, by which they might make a determination of the fairness of the $55.00 proposal, the TU directors simply listened to a 15 to 20 minute recitation by Mr. Van Gorkom, the man who had selected the $55.00 price and proposed the transaction to

Mr. Pritzker. A brief oral report cannot be made the basis for a claim of good faith reliance on corporate reports such that it later insulates directors who fail to inform themselves of the rudiments of the transaction before them. In view of their reckless haste and the absence of any good faith reliance on §141(e) reports, there is no basis for affording the protection of the Business Judgment Rule to TU's directors.

The defendants concede that there were no §141(e) reports made to them. They defer any mention of the only report that was presented to them and seek to shelter their inappropriate decision by relying on Cheff v. Mathes, Del. Supr., 199 A.2d 548, 556 (1964), and Kors v. Carey, Del. Ch., 158 A.2d 136, 141 (1960). Those cases lend no support to defendants' position.

Cheff is not on point for at least three reasons. First, Cheff, a suit challenging a corporation's purchase of its own stock, did not involve a transaction of the magnitude involved here. What constitutes "good faith reliance" by a board on a §141(e) report must depend on the factual context. Compare, Bennett v. Propp, Del. Supr., 187 A.2d 405 (1962). For example, a brief oral report at a board meeting on the rate of absenteeism at one out of twenty plants could reasonably be relied on. On the other hand, many detailed written corporate reports, (as well as reports of independent investment bankers or chartered financial analysts) with timely distribution would be required to invoke good faith reliance in the context of the outright sale or merger of an entire business. Second, in Cheff, the board had considered the stock purchase for several months before acting and had even authorized an investigation of the situation. Third, the Cheff board had before it, in addition to the §141(e) officers' reports on Mr. Maremont's poor business reputation, corroborating evidence of Mr. Maremont's poor

standing, including Dunn & Bradstreet reports and financial statements from his other wrecked business ventures. In view of the subject at hand (i.e., the reputation of Maremont in the business world), the style and manner of the reports upon which the Cheff board relied was entirely appropriate.

The defendants tacitly admit that there were no §141(e) reports to the Board since they quickly allude to matters not within the scope of the Court's question and rely on Kors v. Carey (DSB 12) for the statement:

> "However, the specific categories of reports enumerated in §141(e) are not the only information upon which directors may rely in exercising their business judgment."

Kors was not even a §141(e) case. Kors, also, involved a stock repurchase in which the directors, before making a business decision, carefully considered the transaction at hand seeking, inter alia, outside professional advice from proxy solicitors and members of the Harvard business faculty. 158 A.2d at 141. In any event, here, the Court did not ask what extraneous information the TU Board might have had or what common law principles applied; rather, the Court specifically asked counsel about §141(e) reports. The defendants spend two pages rehearsing and dressing up the directors' general business experience and previous reports to the Board which did not even mention a possible merger. The fact is that there were no reports other than Mr. Van Gorkom's 15 to 20 minute oral presentation, unbuttressed by any written summary or financial information of any kind, and Mr. Roman's unheeded statements that TU's stock was worth between $55.00 - $65.00 per share.

(2) The TU Board Cannot Excuse Their Dereliction by Claiming Reliance on Mr. Van Gorkom's Brief Oral Presentation

Finally, the defendants get to the question posed by the Court, saying (DSB 14):

> "The principal report presented to the directors at the September 20, 1980 Board meeting was Mr. Van Gorkom's presentation of the terms of the Pritzker offer and all aspects of the proposed merger."

The defendants' designation of Mr. Van Gorkom's oral presentation as the "principal report" is obviously designed to foster the impression that there were other reports; however, as the record plainly shows, there were no other §141(e) reports upon which the Board relied. Moreover, in his oral presentation, Mr. Van Gorkom was not even candid to his own Board.* He failed to disclose that the Pritzker offer was nothing more than Mr. Van Gorkom's own offer which he had suggested to Mr. Pritzker, including the $55.00 price (A-1282-83). The suggestion that he presented "all aspects" of the proposed merger is likewise incorrect. If nothing else, the record shows plainly that Mr. Van Gorkom had not even read the very merger documents he is now purported to have presented to the Board.

(3) The TU Board Is Not Protected By Claiming Reliance on the Alleged "Opinion" of Mr. Brennan or the Report of Mr. Romans

The defendants then claim that there is admissible evidence in connection with the alleged opinion of James Brennan, an attorney. Mr. Brennan was not called as a trial witness. At some point, the plaintiffs are entitled to a ruling as to whether there was admissible evidence of Mr. Brennan's presence or opinion at the September 20 meeting. The minutes of the meeting -- the best evidence of what took place at the meeting, Schroder v. Scotten, Dillon Co., Del. Ch., 299 A.2d 431, 440 (1972) -- do not show that Mr. Brennan was in attendance (PX-26: A-1865-68). The plaintiffs made timely objection to the hearsay testimony

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* Mr. Van Gorkom exhibited the same lack of candor in the week preceding the Merger when he refused to inform his Board about Mr. Pritzker's proposal ostensibly because he feared some director would leak news of the deal (A-1084; Chelberg 57).

as to what Mr. Brennan is reputed to have said at the meeting (A-1118). In any case, as the Plaintiffs' Opening Supplemental Brief shows, Mr. Brennan's opinion is not within the scope of §141(e) (PSB 21-22). Even if it were, the mere fact that Mr. Brennan may have said a fairness opinion was not required as a matter of law does not mean that a prudent director should not insist on one before agreeing to a $690 million cashout merger. The Brennan scenario makes clear that the defendants simply sought to minimize doing that which they knew should have been done.

Finally, the defendants seek to convert into a full scale §141(e) report Mr. Roman's brief oral statement that a study made by his department (but not made available to the Board) showed the range of the fair value of the stock of TU between $55.00 to $65.00. Mr. Romans' department's study, had it been produced to and reviewed by the Board, would have been a §141(e) report. Though Mr. Romans had made clear to Mr. Van Gorkom that the study was in existence, neither Mr. Van Gorkom nor Mr. Romans presented the study to the Board (A-1338) and no Board member asked for it (A-1353).

(4) The Record Does Not Support Defendants' Contention That the TU Board Directed Modifications to the Merger Agreement at the September 30 Meeting

The defendants then say (DSB 15):

> "At the September 20 Board meeting, after hearing the reports of Messrs. Van Gorkom, Brennan and Romans, and after extensive discussions among themselves, the directors of Trans Union insisted upon two changes in the draft merger agreements, i.e., to provide any interested party with the same information which had been made available to the Pritzkers, and to make clear that the directors had a fiduciary duty to accept a better offer. The fact that the directors demanded those changes shows conclusively that the directors understood Pritzker's proposal and brought their informed business judgment to bear with specificity on the proposed transaction."

There are several comments to be made. First, in the context of the sale of a $690 million business, a discussion that lasted no more than ninety minutes is not "extensive", especially since the merger documents themselves were not available at the meeting and no other written information had been presented to provide a sound basis for a meaningful discussion. Most important, however, is the fact that the defendants continue to base their whole defense of the Business Judgment Rule on their insistence upon "phantom" conditions supposedly inserted in the merger documents. Though documents evidencing such conditions were requested prior to trial and at trial itself, those documents were never produced. In their prior brief, the plaintiffs pointed out that the defendants resolutely failed to provide the alleged "draft merger agreements" that were supposed to have existed before the alleged two conditions were inserted (PSB 9). The Court below totally ignored the fact that these alleged conditions which the Board is supposed to have insisted on are not reflected in any documents, or even the Board minutes, the best evidence of what took place at the meeting, Schroder, supra, 299 A.2d at 44. The Court below went further: it accepted the defendants' defense (i.e., affirmative Board action) based on nothing more than the oral assertions of the defendants. This Court should not countenance a defense based on documents which were never produced and the absence of which was never explained. Indeed, the logical inference from the defendants' unexplained failure to produce these documents is that they do not support the defendants' assertions and if produced would be adverse to those assertions. Pennzoil Co. v. Getty Oil Co., supra; Wilmington Trust Co. v. General Motors Corp., Del. Supr., 51 A.2d 584, 593 (1947); II Wigmore on Evidence §291 (3d Ed. 1940).

(5) Defendants' Claims as to the So-Called Amendments to the Merger Agreement Are Feckless

The defendants' Opening Supplemental Brief suggests that, at the October 8 Board meeting Mr. Van Gorkom had with him the proposed amendments to the Merger Agreement (DSB 16). In point of fact, Mr. Van Gorkom did not have those proposed amendments: they were not even in existence on October 8. The amendments were subsequently drawn up and signed on October 10, 1980 (TR 870-72, Johnson; PX 55: A-2125).

Mr. Van Gorkom's oral recitation of his conception of his understanding with Mr. Pritzker relating to the proposed amendment to the Merger Agreement and what he supposed the proposed amendments when drafted and signed would contain, are not reports within the meaning of §141(e). Furthermore, as a practical matter, the record shows that Mr. Van Gorkom never understood the complex amendments that were eventually drafted and signed. Indeed, the actual amendments turned out to be far different from what Mr. Van Gorkom presented to the TU Board on October 8. Mr. Van Gorkom represented that the amendments would give TU the "unfettered right to solicit bids", a right that they had not previously enjoyed under the September 20 Merger Agreement. In actuality, the amendments giving TU the right to solicit bids were illusory because they contained severe time constraints and insurmountable restrictions on TU's ability to terminate the Pritzker Merger. This is demonstrated by the fact that G.E. found that they did not have the time to make a competing alternate bid even though they submitted a draft opening offer that was better than the Pritzker $55.00 merger agreement (i.e., $57.00 in stock and $60.00 in cash) (A-1461). More important, G.E. did not want to get into a bidding war with the Pritzkers (A-1469).

(6) The Decision of the TU Board Was Not an Informed One Such As to Permit Them the Protection of the Business Judgment Rule

The defendants concede the poverty of their position by saying (DB 16):

> "The above described oral reports were properly relied on by the directors. Those reports, particularly when coupled with the wealth of experience, prior discussions, and written financial reports which the directors had and had received before, make it clear that the directors were fully informed and had every right to rely on Van Gorkom, Brennan and Romans in exercising their business judgment."

Again, the defendants seek to avoid the Court's question which asked not about the defendants' "wealth of experience", etc., but specifically about §141(e) reports. Furthermore, the TU Board did not have a "wealth of experience" in connection with transfers of 100% of companies particularly the size of TU. They had had no prior discussions whatsoever on the sale or merger of TU. They had no financial reports on the merger or sale of the company or the proper price and percentage of premium that a transfer of 100% of the company should command. The directors were not fully informed; on the contrary, they had no information whatsoever and had been deliberately kept in the dark by Mr. Van Gorkom's hasty and secretive course of action. The TU directors were wrong in relying solely on the brief and mistaken summary of the terms of the Merger by Mr. Van Gorkom. Moreover, there is no admissible evidence as to what Mr. Brennan said. Further, Mr. Romans' brief statement itself gave fair warning that the price that the TU directors were blithely accepting was inadequate.

The defendants have themselves supplied the appropriate answer when they say (DB 16):

"As Mr. Johnson testified at trial:

> "'...If we couldn't have made an informed and rational judgment, then of course it was our obligation to say that we couldn't. ...'"

That was precisely the situation that the Board found itself in and precisely what the Board should have done. Mr. Johnson went forward to try to justify the decision of the Board based on vague general assertions of the experience of the Board of Directors, TU's Five-Year Plan and the work of the Boston Consulting Group. Nothing that Mr. Johnson trots forth is a substitute for the actual hard information in the form of financial analysis and expert advice that would have given the Board a rational basis for deciding what to do about the Pritzker merger proposal that Mr. Van Gorkom had secretively and deliberately sprung on them.

The defendants conclude (DSB 17):

> "Although faced with a deadline imposed by the Pritzkers, it is apparent that the directors of Trans Union were particularly well-informed about Trans Union, its history and its prospects."

It is correct that the TU directors were faced with a deadline imposed by the Pritzkers and acquiesced in and fomented by Mr. Van Gorkom. However, that deadline was no excuse for them not to act deliberately and rationally under the circumstances and to take the full amount of time that was allowed by that deadline. The TU directors did not take even the 36 hours that was available under the deadline. Instead, they met briefly for two hours on a Saturday afternoon and adjourned without even waiting to find out if Mr. Pritzker would accept the two "phantom" conditions which they claimed to have imposed. While the directors may have been informed about Trans Union and its history, they were not informed at all about the Merger or the price that TU's shares could properly command in a merger transaction that involved a transfer of 100% of control.

The defendants wax poetic (quoting Dr. Pangloss in "Candide") (DSB 17):

> "In fact, they had the best of all worlds. When they accepted the Pritzkers' proposal, the directors believed, in good faith, that the $55 per share price was fair, they knew that the $55 price was substantially above the historical and recent market prices for Trans Union's shares, and they knew that that price would be tested in the market for at least three months. Ultimately, the market proved their decision to have been correct."

The defendants had no way of knowing in good faith that $55.00 was fair. They had received no information at all as to what 100% of TU was worth. All they knew was that $55.00 was above the recent market price, a market price which Mr. Van Gorkom admitted did not reflect TU's increased earnings (A-1078, 1117). The assertion that the defendants "knew" that the price would be tested in the market for at least three months is incorrect. The TU directors were so told by Mr. Van Gorkom. But, even a casual examination of the TU merger documents as of that time would have revealed that, in fact, the terms were such that there could be no fair test in the marketplace. If nothing else, the Pritzkers had a substantial time lead, a million-share advantage at a reduced price, and according to the TU press release, a "definitive merger agreement". In fact, the management was so horrified by what Mr. Van Gorkom and the directors had done that they revolted. The result was the October 10th amendments. Mr. Van Gorkom then triumphantly represented, and the Board believed, that these amendments would give TU an unfettered market test. Even with these belated amendments, there could not be and, indeed, there was no free market test.

The defendants conclude "Ultimately, the market proved their decision to have been correct." This statement is patently incorrect. To the extent that the market operated, it showed that the defendants' improvident, hasty decision was wrong. KKR made an offer at $60.00 a share in spite of the existence of a definitive merger agreement with the Pritzkers. G.E. made a draft opening offer of $57.00 in stock and

$60.00 in cash. The G.E. offer was withdrawn because (1) Mr. Pritzker would not stand aside, (2) the G.E. people would not be "stampeded" into making a quick competing offer, and (3) because G.E. would not get into a bidding war with the Pritzkers in view of the Pritzkers' contractual and temporal advantages. Thus, if the directors had not in effect precluded a market test by their hasty action, the TU shareholders would have gotten a far better price for their shares (or would have retained their shares) instead of having been sold out by Mr. Van Gorkom at his personally selected $55.00 price approved on a Saturday afternoon in September by the TU directors.

III. PLAINTIFFS' REPLY TO DEFENDANTS' RESPONSE TO THE COURT'S QUESTION (c)

THE FEBRUARY 10, 1981 VOTE DID NOT RELIEVE ANY DIRECTOR OF THE DUTY TO TIMELY EXERCISE BUSINESS JUDGMENT IN CONNECTION WITH THE SALE OF TU.

(1) The Shareholder Vote Is a Nullity Because It Was Not an Informed Vote

In responding to the Court's question, defendants rely on Michelson v. Duncan, Del. Supr., 407 A.2d 211 (1979), but short-cut their discussion by assuming improperly that the shareholder vote of February 10, 1981 was an informed vote. They state:

> "Informed decision making is part of the common law duty of care. In this case, the transaction which plaintiffs attack was a merger which was approved by Trans Union's stockholders, as well as by its directors." (DSB 19)

In quoting from Michelson (DSB 20), the defendants ignore a key passage from that opinion because it devastates their position:

> "Shareholder ratification is valid only where the stockholders so ratifying are adequately informed of the consequences of their acts and the reasons therefore.
>
> ***
>
> "Whether the shareholders were informed, and thus their ratification valid, turns on the fairness and completeness of the proxy materials submitted by the management to the ... shareholders. ..."

Michelson v. Duncan, supra, 407 A.2d at 220 (emphasis added).

As plaintiffs have demonstrated, both in their original briefing (see Appellants' Opening Brief, pp. 61-67) to this Court and in their Opening Supplemental Brief (PSB 29), the stockholders were neither fully nor timely informed of the matters to be voted on. TU's shareholders were not informed of all material facts related to the Merger, or the facts surrounding the acts of the directors which now deprive those directors of the protection of the Business Judgment Rule. In Michelson by contrast, the complaint was discussed in and attached to the proxy materials which candidly sought shareholder ratification. Michelson v. Duncan, Del. Ch., 386 A.2d 1144, 1154 (1978). Moreover, TU's January 26 "Supplement to Proxy Statement" ("the Supplement") (PX 100: A-2324) was not sent to the shareholders at least 20 days prior to the Merger vote as required by 8 Del.C. §251(c).* Therefore, the shareholder vote was a nullity because it was not validly accomplished. Weinberger v. UOP, Inc., Del. Supr., 457 A.2d 702, 703, 712 (1983); Michelson, supra. Accordingly, defendants stumble irretrievably at the very threshold of the Court's question.

(2) No Shareholder Vote Can Justify Circumvention of a Director's Statutorily Mandated Duty

In their futile attempt to answer to their advantage the Court's question, the defendants misstate the law by saying (DSB 19-20):

> "Under settled law in this State, that (sic) shareholder ratification relates back to cure an invalid act of a director and is a 'full defense' to any claim based upon a breach of fiduciary duty."

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* The Supplement contains a frank concession by defendants that the original proxy statement omitted material facts and credits this litigation for the corrections made (A-2324-2325). Unfortunately for TU's shareholders, the corrections were untimely and incomplete. Cf. American Pacific Corp. v. Super Food Services, Inc., Del. Ch., C.A. No. 7020, Longobardi, V.C. (December 6, 1982) (discussed at PSB 29) (stockholders meeting enjoined where supplemental proxy materials were not provided in sufficient time prior to scheduled vote).

This ignores that director consideration and recommendation of a proposed merger is a statutory duty imposed by §251 of the Delaware General Corporation Law ("DGCL"). Thus, this requirement is not a common law obligation, but rather is mandated by the DGCL for the protection of the stockholders. As plaintiffs explained (PSB 24-28), this directorial duty cannot be delegated. Adams v. Clearance Corp., Del. Supr., 121 A.2d 302 (1956); Field v. Carlisle, Del. Ch., 68 A.2d 817 (1949).

Section 251 is but one instance where the DGCL requires that, before a corporate act can take place, the directors must assemble themselves along with the requisite information and give the owners of the business -- that is, the shareholders -- their informed business judgment on the matter at hand. See Muschel v. Western Union Corp., Del. Ch., 310 A.2d 904, 909 (1973); Lipton, Takeover Bids in the Target's Boardroom, supra; Corporate Director's Guidebook, supra; cf. Weiss, The Law of Takeout Mergers: A Historical Perspective, 56 N.Y. Univ.L.Rev. 624, 676 (1981). By contrast, under §253, there is no requirement of approval of the non-surviving corporation's Board if the majority stockholder owns 90% or more of the stock of the non-surviving corporation.

Thus, the DGCL specifies those circumstances under which directors' approval, and for that matter stockholder approval, may or may not be dispensed with.* The fact that the statutory scheme specifies types of transactions under which director approval is not required dissipates any argument that director approval can be dispensed with under other circumstances. See Norman v. Goldman, Del. Super., 173 A.2d 607, 670

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* See also, 8 Del.C. §242 (Certificate Amendments), §271 (Sales of All or Substantially All Assets), and §275 (Dissolution).

(1961); 2A Sands, Sutherland Statutory Construction, §47.23 (4th ed. 1973). Accordingly, to hold that stockholder ratification cured the invalidity of the Board's action would be inconsistent with the carefully thought-out statutory scheme of the DGCL.

(3) The Directors' Violation of §251 Is a Void Act. It Leaves Defendants Unable to Come to Grips With the Court's Question.

Defendants' reliance on Michelson and Lewis v. Hat Corporation of America, Del. Ch., 150 A.2d 750 (1959), does not help their position. Michelson and Lewis both hold that stockholder ratification cannot cure a corporate action which is void per se. It is axiomatic that action in violation of a statute is void per se. Grynberg v. Burke, Del.Ch., 410 A.2d 169 (1979); Abercrombie v. Davies, Del. Supr., 130 A.2d 338 (1957). Since the directors by their actions violated §251 of the DGCL that action is void per se, and it could not be cured or ratified by the shareholder vote on February 10, 1981.

Because of their inability to argue for a conclusion acceptable to themselves, the defendants stray further from the specific question posed by the Court and address themselves not to the effect of the stockholders' vote but to the scope and ambit of the protection of the Business Judgment Rule as recently explained in Aronson v. Lewis, supra (DSB 20-21). Through this detour, defendants conclude that the TU directors are entitled to the protection of the Business Judgment Rule. Yet, the Court's question states as its premise that the directors are not entitled to the Business Judgment Rule and then asks what effect, if any, the shareholder vote had in curing the director action. The short, and correct, answer to the Court's question is, "none".

The record shows that the defendants did not fully inform their stockholders under the requirements of Weinberger. Neither did they

make timely disclosure under the requirements of 8 Del.C. §251(c) or American Pacific. Accordingly, the stockholders' vote was fatally tainted from the outset. Moreover, since the duty to pass on and approve a merger is statutorily imposed on the Board, it is a duty which even the stockholders cannot be delegated by ratification, especially since there is a statutory exception in a short form merger where the requirement of board recommendation is not mandated but rather omitted in the statute.

IV. PLAINTIFFS ' REPLY TO DEFENDANTS' RESPONSE TO THE COURT'S QUESTION (d)

LESS THAN A UNANIMOUS SHAREHOLDER VOTE CANNOT CURE DIRECTOR ACTION WHICH IS NOT PROTECTED BY THE BUSINESS JUDGMENT RULE.

(1) Despite Defendants' Representation to the Contrary, Waste Was Included in Plaintiffs' Complaint. That Waste Cannot be Ratified by Less Than Unanimous Stockholder Vote

Initially, in answer to the Court's question, defendants assert that there was no allegation of waste in this case. That assertion ignores Count III of the Amended Complaint (1/30/81) which alleges specifically the waste resulting from the sale of the 1,000,000 shares to Mr. Pritzker at $38.00 per share (A-195-196).

Defendants do concede, as they must, that less than a unanimous stockholder vote cannot ratify waste (DSB 22). Gottlieb v. Heyden Chemical Corp., Del. Supr., 91 A.2d 57 (1952); Schreiber v. Bryan, Del. Ch., 396 A.2d 512 (1978). As shown in the Plaintiffs' Opening Supplemental Brief (PSB 31-33), the sale to Mr. Pritzker of a million shares of TU stock at the inadequate price of $38.00 was clearly an act of waste by the directors in connection with the Merger. Kerbs v. California Eastern Airways, Inc., Del. Supr., 90 A.2d 652 (1952). That sale, and the interrelated merger, could not be ratified by less than unanimous vote of the TU shareholders.

(2) Because the Waste Caused Direct Individual Injury to Plaintiffs, They Have Standing to Prosecute the Claim

The defendants, in their footnote (DSB 22), contend that, even if there were a claim of waste, the plaintiffs would have no standing to prosecute the action since waste is derivative in nature and was extinguished by the Merger. What defendants ignore is that plaintiffs and the class sustained the ultimate injury proximately caused by the waste and the other interrelated actions which now deprive the directors of the protection of the Business Judgment Rule. Indeed, waste was such an inherent part of the Merger transaction that the inimical results of that waste were thrust upon the stockholders. In such a case, where stockholders are directly injured, the action ceases to be derivative and becomes individual in nature and is not mooted by a merger. Reeves v. Transport Data Communications, Inc., Del. Ch., 318 A.2d 147 (1974); Elster v. American Airlines, Del. Ch., 100 A.2d 219 (1953); Eisenberg v. Flying Tiger Line, Inc., 2d Cir., 451 F.2d 267 (1971) (reversal of lower court's dismissal of suit with finding that action was really individual not derivative). Considering the firm interrelationship between the waste and the Merger, less than unanimous shareholder vote cannot ratify the transaction.

(3) The Shareholder Vote Did Not Shift the Burden to Defendants

Next, relying on Michelson, defendants argue that the shareholder vote had "the effect of squarely placing upon plaintiffs the burden of showing that no person of ordinary sound business judgment could say that the consideration received in the merger was fair" (DSB 22). Aside from avoiding the Court's question, defendants' response flies in the face of the law of Michelson, 407 A.2d at 224. That is, a shareholder vote does not shift the burden unless that vote is an informed one.

Gottlieb v. Heyden Chemical Corp., Del. Supr., 91 A.2d 57 (1952). Here, since the vote was fatally defective, no burden shifted to plaintiffs.*

(4) Fair Value Requires More Than Consideration of Premium Over Market

The defendants continue their obtuse and summary response to the Court's question by saying (DSB 23):

> "In this case, it has been conceded that there was no interested director action. Even if there were such a claim, plaintiffs did not, and could not, meet their burden of showing that no person of ordinary sound business judgment could say that the merger consideration was fair, in light of Trans Union's business history and prospects and the premium paid by the Pritzkers of 62% over the average high and low prices at which Trans Union stock had traded in 1980, 48% over the last closing price before the merger, and 64% over the average high and low prices at which the stock had traded at any time during the prior six years."

To that comment, there are several responses. First, as previously shown, all that the defendants say has no applicability to the shares sold to the Pritzkers at $38.00 per share in the face of a merger price of $55.00. Second, the defendants continue to believe (as indeed the lower Court did) that the test for fair price is some definitive percentage above the current market price. This mistaken view continues to ignore this Court's mandate in Weinberger v. UOP, Inc., supra, 457 A.2d at 712, that fair value be determined according to all "generally accepted techniques used in the financial community", e.g., in this case that includes cash flow.

Despite the Weinberger mandate, the defendants attempt to dazzle this Court with percentage figures rather than discussing all elements of fair value. While it is true that the percentages are correct, it is plain that, even in the choked-off market situation that existed after

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* For a response to defendants' misguided and continued attempt to limit the inquiry of the directors' conduct to "fraud, bad faith or self-dealing" see Part I, supra.

the signing of the definitive merger agreement on September 20, 1980 with the Pritzkers, the fair price was not less than $65.00. The facts that KKR offered $60.00 in cash, that G.E. offered $57.00 in stock and $60.00 in cash, and that the Five-Year Forecast indicated that 30% of the stock would bring $50.00 are all evidence that cannot be suppressed which indicate that the $55.00 price was unfair, contrary to the defendants' self-serving assertions.

The defendants conclude (DSB 24):

> "Accordingly, whether this Court accepts ratification as a 'full defense', as we submit it must under the facts here, or even assuming hypothetically that such ratification resulted only in a shifting of the burden of proof to plaintiff to show that the consideration received in the merger was so inadequate that no person of ordinary sound business judgment would say it was fair, there is only one possible conclusion. The decision below of Chancellor Marvel must be affirmed."

In response, one thing is clear. The decision of the lower Court was wrong not only as to the law, but factually as well, and must be reversed. Specifically, in the context of question (d) posed by the Court, there could be no ratification of the waste resulting from the million-share transaction, and there could be no ratification at all since the stockholders were so clearly uninformed. "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 (DGCL) requires for the approval of a merger under ordinary circumstances (i.e., where there had been full and fair disclosure to the stockholders)." (PSB 34).

CONCLUSION

For the reasons stated in the Plaintiffs' Original Opening and Reply Briefs and in their Original Supplemental and this Answering Supplemental Brief, the Court should reverse the decision of the Court below and order that judgment on liability and damages be entered for the plaintiffs and the plaintiff class.

Respectfully submitted,

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