RECENT DELAWARE DECISIONS MAY PROVE TO BE "ENTIRELY UNFAIR" TO MINORITY SHAREHOLDERS IN PARENT MERGER WITH PARTIALLY OWNED SUBSIDIARY*

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* This Note covers many of the issues addressed by Kimble C. Cannon in *Augmenting the Duties of Directors to Protect Minority Shareholders in the Context of Going-Private Transactions: The Case for Obligating Directors to Express a Valuation Opinion in Unilateral Tender Offers After* Siliconix, Aquila *and* Pure Resources, *supra* at 191-252. When the two pieces were first slated for publication, they addressed different aspects of related issues in Delaware corporate law. As publication drew closer, and Delaware law developed through recent decisions, the subject matter of the articles converged. Notably, despite their different perspectives, the practitioner and the law student reached similar conclusions and made analogous recommendations. [Ed. note.]

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I. INTRODUCTION

Two Delaware cases that were decided in the summer of 2001 strip a target's minority shareholders of the protections afforded them by an entire fairness review in the context of a parent company's acquisition of a partially owned subsidiary through a tender offer followed by a back-end short-form merger. In *In re Siliconix Inc. Shareholders Litigation*,[1] a class action lawsuit, Delaware Vice Chancellor John Noble held that a unilateral tender offer (whether a cash offer or a stock-for-stock exchange offer) by a parent for a subsidiary does not invoke the entire fairness doctrine, principally because the transaction does not involve a merger requiring any action from the target's board of directors. In *Glassman v. Unocal Exploration Corp.*,[2] handed down a month later, the Delaware Supreme Court held that in a short-form merger pursuant to title 8, section 253 of the Delaware Code,[3] the "parent corporation does not have to establish entire fairness, and, absent fraud or illegality, the only recourse for a minority stockholder who is dissatisfied with the merger consideration is appraisal."[4] As a result of these two decisions, it appears that a parent company can freeze out the minority without ever having to satisfy an entire fairness review by first engaging in a tender offer, and subsequently executing a short-form merger.

For example, in *Siliconix*, Vishay Intertechnology, Inc. ("Vishay"), which owned 80.4 percent of Siliconix Inc., sought to freeze out the other 19.6 percent of shareholders by making a tender offer, which required at least 50 percent of

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1 No.CIV.A. 18700, 2001 WL 716787, at *6 (Del. Ch. June 21, 2001).

2 777 A.2d 242 (Del. 2001).

3 DEL. CODE ANN. tit. 8, § 253 (2002).

4 *Glassman*, 777 A.2d at 243.

the minority shareholders to tender, and then executing a short-form merger, thus freezing out those shareholders who declined to tender their shares. The court in *Siliconix* held that Vishay did not have to prove entire fairness of the tender offer. As a result of the *Glassman* court's reading of section 253, Vishay would not have to prove entire fairness for the short-form merger either. Thus, the law does not require parent companies attempting such transactions to set up the procedural safeguards mandated by the entire fairness review. Consequently, minority shareholders can expect to be frozen out at a price at which at least 50 percent of the minority shareholders agree to tender, or at a price that satisfies the appraisal standard. They are not likely to receive the higher price that could be negotiated for them by an independent committee of board members, which is usually set up to negotiate on their behalf in parent-subsidiary mergers that require the entire fairness review.

Part II of this Note examines the common law and statutory background behind the entire fairness review in Delaware merger law, and the inadequacies of the appraisal remedy as a protective device for minority shareholders. Part III examines several recent Delaware decisions, particularly *Siliconix* and *Glassman*. Part IV examines the implications of these recent developments for future corporate behavior. Part V recommends that the courts overturn *Siliconix*, and recognize the two-part transaction (tender offer followed by a back-end short-form merger) as one overall acquisition, which should be subject to the entire fairness review.

II. BACKGROUND

A. Parent-Subsidiary Merger Warrants "Entire Fairness" Review

For the past few decades, the Delaware courts have been quite protective of minority shareholders of subsidiaries when the company was being merged with, or acquired by, its parent. In such interested transactions, the Delaware Supreme Court has held that "[e]ntire fairness remains the proper focus of judicial analysis in examining an interested merger, irrespective of whether the burden of proof remains upon or is shifted away from the controlling or dominating shareholder, because the unchanging nature of the underlying 'interested' transaction requires careful scrutiny."[5] Moreover, the court has emphasized the entire fairness standard when a director stands on both sides of a transaction:

> There is no dilution of this obligation where one holds dual or multiple directorships, as in a parent-subsidiary context. *Levien v. Sinclair Oil Corp.*, 261 A.2d 911, 915 (Del. Ch. 1969). Thus, individuals who act in a dual capacity as directors of two corporations, one of whom is parent and the other subsidiary, owe the same duty of good management to both corporations, and in the absence of an independent negotiating structure . . . , or the directors' total abstention from any participation in the matter, this duty is to be exercised in light of what is best for both companies. *Warshaw v. Calhoun*, 221 A.2d 487, 492 (Del. 1966).[6]

The courts have recognized that full disclosure does not adequately ensure that minority shareholders will receive as good a price as if the deal were negotiated at arms-length.[7]

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[5] Kahn v. Lynch Communication Sys., Inc., 638 A.2d 1110, 1116 (Del. 1994).

[6] Weinberger v. UOP, Inc., 457 A.2d 701, 710-11 (Del. 1983).

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> [I]n a merger between the corporation and its controlling stockholder -- even one negotiated by disinterested, independent directors -- no court could be certain whether the transaction terms fully approximate what truly independent parties would have achieved in an arm's length negotiation. Given that uncertainty, a court might well conclude that even minority shareholders who have ratified a . . . merger need procedural protections beyond those afforded by full disclosure of all material facts. One way to provide such protections would be to adhere to the more stringent entire fairness standard of judicial review.

Rather, the only way for courts to guarantee that minority shareholders will receive this higher price is to require the parent to satisfy the entire fairness test.[8] "The concept of fairness has two basic aspects: fair dealing and fair price."[9] The burden of proving entire fairness is on the controlling or dominating shareholder.[10] If the controlling shareholder can meet the fair dealing prong with "approval of a merger . . . by an informed vote of a majority of the minority shareholders . . . [it] shifts the burden of proving the unfairness of the merger entirely to the plaintiffs."[11] The purpose of this test is to ensure that the price at which the controlling shareholder freezes out the minority shareholders is the result of an arm's length bargaining process.[12]

B. Why an Entire Fairness Review is More Protective of the Minority Shareholders Than the Appraisal Remedy

One of the most significant benefits to an entire fairness review is the inducement for the controlling shareholder to negotiate the transaction at arm's length with an independent committee of the subsidiary board. This is because in order to satisfy the entire fairness review, the parent must not only prove fair price, but also fair dealing, which requires an arm's length negotiation.[13] If the

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Kahn, 638 A.2d at 1116-17 (quoting Citron v. E.I. Du Pont de Nemours & Co., 584 A.2d 490, 502 (Del. Ch. 1990)).

[8] "Once again, this Court holds that the exclusive standard of judicial review in examining the propriety of an interested cash-out merger transaction by a controlling or dominating shareholder is entire fairness." *Kahn*, 638 A.2d at 1117.

[9] *Weinberger*, 457 A.2d at 711.

[10] *Id.* at 710; *see also* Rosenblatt v. Getty Oil, Co., 493 A.2d 929, 937 (Del. 1985).

[11] *Rosenblatt*, 493 A.2d at 937.

[12] "[A] showing that the action taken was as though each of the contending parties had *in fact* exerted its bargaining power against the other at arm's length is strong evidence that the transaction meets the test of fairness." *Weinberger*, 457 A.2d at 709-10 n.7 (emphasis added).

[13] *See Weinberger*, 457 A.2d at 701; *Kahn*, 638 A.2d at 1115.

committee is truly independent, this will shift the burden of proving *lack of* fair price to the minority shareholders contesting the transaction. When the minority shareholders have a committee of board members negotiating on their behalf, they are likely to receive a price that is not just fair, but is somewhere above the minimum for which the minority shareholders would agree to sell, and below the maximum that the controlling shareholder would be willing to pay. If, for example, the minority shareholders would be willing to sell (in the case of a tender offer, a majority of the minority) for $20 per share, and the controlling shareholder would be willing to pay as much as $24 per share, then with the benefit of a negotiating committee the deal will be consummated at a price somewhere between $20 and $24. Without such a committee, the minority shareholders are likely to receive no more than $20 per share. That price will only be successfully challenged in an appraisal hearing if $20 is unfair. The key to understanding the distinction between the remedies is recognizing that there is a range of fair prices. Without having to satisfy the requirement of the fair procedure prong of entire fairness, the minority shareholders are likely to wind up with the lowest point within the fairness range.

With an appraisal remedy, which under *Siliconix* is exclusive under the facts of the case, only the shareholders who choose to challenge the merger price by seeking an appraisal will benefit from any relief granted.[14] However, under the entire fairness standard, a minority shareholder can challenge the merger price on behalf of all of the minority shareholders in a class action suit. Because there will be more plaintiffs, the overall amount recovered should be much greater than under appraisal. The procedural consequence is that it is generally the lawyer, whose fee is usually set as a percentage of the recovery, that initiates the class action lawsuit, and the members of the class have to do very little to affirmatively participate.

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[14] DEL. CODE ANN. tit. 8, § 262 (2002).

The theory behind the appraisal remedy being available only to dissenting shareholders is that those who have tendered their shares, or voted for a merger, are presumed to have done so in reliance on the fairness of the process and their satisfaction with the price, as opposed to coercion. If the process was corrupt, the class action is available to all shareholders, even to those who had accepted on the theory that the preconditions to appraisal exclusivity had not been satisfied. Thus, it is treated as though all shareholders had dissented.[15]

Furthermore, under an appraisal remedy the sole question is the value of the shares on the date of the merger.[16] Under an entire fairness review, however, the court may award a rescission remedy,[17] or punitive damages, that could reflect an increased value of the shares subsequent to the merger, potentially leading to a much greater damage award. In fact, it is not uncommon for Delaware courts to award large damages to minority shareholders who succeed in an entire fairness challenge. For example, in 1992 Enserch Corp. made an exchange offer for the publicly-held units of Enserch Exploration Partners Ltd., its partially owned subsidiary. The court found the price to be both procedurally and substantively defective, and awarded the plaintiffs $60 million in damages for a transaction which was initially valued at $100 million.[18] The court held that the transaction was a product of unfair dealing, and that the structure and timing of it was unfair to the shareholders. Even though a price lower than $160

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[15] *See* RONALD J. GILSON & BERNARD S. BLACK, THE LAW AND FINANCE OF CORPORATE ACQUISITIONS 1305-06 (2d ed. 1995).

[16] "[T]he value of the appraisal petitioners' shares on the date of the merger is the only litigable issue in a statutory appraisal under Section 262." Alabama By-Products Corp. v. Neal, 588 A.2d 255, 256-57 (Del. 1991) (citing Cavalier Oil Corp. v. Harnett, 564 A.2d 1137, 1142 (Del. 1989); and Cede & Co. v. Technicolor, Inc., 542 A.2d 1182, 1187 (Del. 1988)).

[17] *See* GILSON & BLACK, *supra* note 15, at 1305-06.

[18] *See* MacLane Gas Co. L.P. v. Enserch Corp., No.CIV.A. 10760, 1992 WL 368614 (Del. Ch. Dec. 11, 1992), *aff'd*, 633 A.2d 369 (Del. 1993).

million might have been seen as fair if there had been an arm's length negotiation, the court did its own calculation of value and awarded the minority shareholders a 60 percent premium over the price initially paid.

Whereas under an entire fairness test the court can take equitable considerations into account, and may award damages that reflect a post-merger appreciation of the stock, in a sense the only penalty for setting the price too low under an appraisal standard is having to pay the right price.[19] "[T]he Court shall appraise the shares, determining their fair value exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation."[20] This gives parent corporations an incentive to exploit the gap between the minimally fair price and the better price that could emerge from bargaining.[21] If the transaction were subject to an entire fairness review, then

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[19] *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710-11 (Del. 1983), expands the appraisal remedy to include rescissory damages to take into account some non-speculative synergy gains. *Glassman v. Unocal Exploration Corp.*, 777 A.2d 242, 246 (Del. 2001), expands them to include damages that are not only "known or susceptible of proof as of the date of the merger," thus veering appraisal awfully close to entire fairness damages. The principal difference that remains is that appraisal damages are only awarded to dissenting shareholders, not to all shareholders, as in the case of an entire fairness breach. The other difference is that if there is a fiduciary duty breach, the court is more likely to err on the side of overcompensating the shareholders.

[20] DEL. CODE ANN. tit. 8, § 262(h) (2002).

[21] The Honorable William T. Allen, former Chancellor of the Court of Chancery of the State of Delaware, The Honorable Jack B. Jacobs and The Honorable Leo E. Strine, Jr., Vice Chancellors of the Court of Chancery of the State of Delaware, argue that it is not always the case that appraisals result in only moderate damage awards. *See* William T. Allen, Jack B. Jacobs & Leo E. Strine, Jr., *Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 56 BUS. LAW. 1287, 1306 (2001). *See also* M.G. Bancorporation, Inc. v. Le Beau, 737 A.2d 513, 526 (Del. 1999) (affirming $85 per share appraisal award versus $41 per share merger price); Rapid-American Corp. v. Harris, 603 A.2d 796, 804 (Del. 1992) (affirming $51 per share appraisal award versus $28 per share merger price); Cavalier Oil Corp. v. Harnett, 564 A.2d 1137, 1146 (Del. 1989) (affirming $347,000 appraisal award versus $93,950 offer).

the parent has more of an incentive to set up adequate procedures (e.g. an independent committee) to prevent losing a court challenge, which could cost more than the correct price at the time of the transaction. Such adequate procedures are important to ensuring that minority shareholders get the best price, not just a fair price. In effect, the possibility of excessive damage awards acts as a deterrent to procedural inadequacies, and deters the parent from taking advantage of the minority shareholders in transactions that do not involve arms-length bargaining.

Under the facts of *Siliconix*,[22] described below in greater detail, there was no assurance of fairness of process. Rather the tender offer was taken directly to the shareholders, who did not have a bargaining agent seeking not only a *fair* price for them, but also the *best* price it could extort from the controlling shareholders.[23] In a tender offer setting, any offer that matches the seller's reservation price will be accepted. Yet the Delaware courts have in the past been concerned not just with minority shareholders receiving a fair price, but with them receiving the price that they would have received had there been arms-length bargaining. The legislature, too, has been similarly concerned, as evidenced by section 203's requirement that a tender offeror receive tenders from 85 percent of the shareholders (or meet other stringent requirements) in order to be able to do a subsequent freezeout transaction.[24] This is to ensure that all of the shareholders receive the higher price that the acquirer must offer in order to receive 85 percent acceptance, as opposed to the lower price that would be required for 50 percent acceptance.

The court in *Kahn* described the fiduciary duty of directors as follows:

> The power to say no is a significant power. It is the duty of directors serving on [an independent]

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[22] No.CIV.A.18700, 2001 WL 716787 (Del. Ch. June 21, 2002).

[23] In a traditional tender offer, setting a poison pill forces the acquirer to bargain with the target's board.

[24] tit. 8, § 203(a).

> committee to approve only a transaction that is in the best interests of the public shareholders, to say no to any transaction that is not fair to those shareholders and is not *the best transaction available*. It is not sufficient for such directors to achieve the best price that a fiduciary will pay if that price is not a fair price.[25]

C. Delaware's Short-Form Merger Statute

Delaware's parent-subsidiary merger statute, title 8, section 253 of the Delaware Code, was originally enacted in 1937 to facilitate mergers between parents and their wholly-owned subsidiaries. It was amended in 1957 to allow for short-form mergers in which the parent owned only 90 percent of the stock of the subsidiary.[26] The defining characteristic of a short-form merger is that it does not require any action by either the board or the shareholders of the subsidiary.[27] It makes the procedure relatively simple, by authorizing "the elimination of the minority without notice, vote or other traditional indicia of procedural fairness."[28] Section 253(d)[29] allows for appraisal as the remedy for minority shareholders who are dissatisfied with the consideration received.

[25] *Kahn*, 638 A.2d at 1119-20 (quoting *In re* First Boston, Inc. S'holders Litig., No.CIV.A.10338 (Consolidated), 1990 WL 78836, at *7 (Del. Ch. June 7, 1990) (emphasis added)).

[26] *See* Stauffer v. Standard Brands, Inc. 187 A.2d 78 (Del. 1962), *overruled by* Roland Int'l Corp. v. Najjar, 407 A.2d 1032, 1036 (Del. 1979), *overruled by* Weinberger v. UOP, Inc., 457 A.2d 701, 715 (Del. 1983); *see* Nelson Ferebee Taylor, *Evolution of Corporate Combination Law: Policy Issues and Constitutional Questions*, 76 N.C. L. REV. 687, 801-05 (1998).

[27] *See* John C. Coates IV, *"Fair Value" as an Avoidable Rule of Corporate Law: Minority Discounts in Conflict Transactions*, 147 U. PA. L. REV. 1251 n. 18 (1999).

[28] Glassman v. Unocal Exploration Corp., 777 A.2d 242, 243 (Del. 2001).

[29] tit. 8, § 253(d).

III. RECENT DELAWARE CASES

A. *Siliconix*

Siliconix[30] was a shareholder derivative suit challenging the stock-for-stock tender offer by Vishay Intertechnology, Inc. ("Vishay") for the 19.6 percent equity interest in Siliconix that Vishay did not already own.[31] The plaintiff argued that 1) Vishay's disclosures to the minority shareholders contained material misrepresentations and omitted material facts, 2) the price was unfair, 3) the transaction should be judged by the entire fairness test, and 4) Vishay would fail both the fair procedure and fair price prongs of that test. The plaintiff further argued that the Siliconix board, consisting of mainly Vishay board members, had a conflict of interest, and that even though Siliconix set up an independent committee of directors, the directors failed to adequately assess the proposed tender offer and make a recommendation to shareholders. Nor did they bargain at arms length on behalf of the minority shareholders. In a somewhat surprising decision, the Court of Chancery held that the entire fairness test was inapplicable to this transaction because it involved a tender offer, not a merger, even though the transaction was admittedly to be followed up by a short-form merger to freeze out the minority shareholders.

If this transaction had been structured as a merger, it would have implicated the entire fairness test. The court admits that "[f]rom the standpoint of a Siliconix shareholder, there may be little substantive difference if the tender is successful and Vishay proceeds, as it has indicated that it

[30] No.CIV.A.18700, 2001 WL 716787 (Del. Ch. June 21, 2002).

[31] Vishay actually made the stock-for-stock tender offer through its wholly-owned subsidiary, Vishay TEMIC Semiconductor Acquisition Holdings Corp. For simplicity, the court refers to Vishay and this subsidiary collectively as Vishay.

most likely will, with the short-form merger."[32] The court justifies the two different approaches with two reasons:

> The first is that accepting or rejecting a tender is a decision to be made by the individual shareholder, and at least as to the tender itself, he will, if he rejects the tender, still own the stock of the target company following the tender. The second concept is that the acquired company in the merger context enters into a merger agreement, but the target company in the tender context does not confront a comparable corporate decision because the actual target of a tender is not the corporation (or its directors), but, instead, is its shareholders. Indeed, the board of the tender target is not asking its shareholders to approve any corporate action by the tender target.[33]

It should also be observed that Vice Chancellor Noble felt it particularly important to note, while discussing the fact that the shareholder would still be the owner of the stock of the target company after the tender (should he or she reject the tender offer), that: "[o]f course, if a short-form merger is effected, the time for continued holding of the stock may be short."[34]

The court notes that under title 8, section 251 of the Delaware Code, Delaware's long-form merger[35] statute, a board has the critical role of initiating and recommending a merger to shareholders, but has no statutory role in a tender

[32] *Siliconix*, 2001 WL 716787, at *7 (footnotes omitted).

[33] *Id.*

[34] *Id.* at *7 n. 23.

[35] "A 'long-form merger' is any merger of unaffiliated corporations (the term is used to distinguish such a merger from the 'short-form' merger that is permitted to occur only between parent and subsidiary corporations)." Paul R. DeMuro, *Corporate Structure Company Issues in M&A Transactions, and Special Issues for Physician Practice Management Companies*, *in* HEALTH CARE M&A 1999: HOW TO STRUCTURE THE TRANSACTION 1999, at 140 (PLI Corp. Law and Practice Course, Handbook Series PLI Order No. B0-009J, 1999).

offer, even if the offer is for a controlling interest.[36] The reason is that "tender offers essentially represent the sale of shareholders' separate property and such sales -- even when aggregated into a single change in control transaction -- require no 'corporate' action and do not involve distinctively 'corporate' interests."[37] The court distinguishes this case from *Kahn* based on the fact that in *Kahn*, the controlling shareholder stood on both sides of the transaction, whereas in this case the controlling shareholder is on only one side of the transaction (with each individual minority shareholder being on the other). This decision, when coupled with *Glassman*, *infra*, makes that distinction one based primarily on form, and based very little on substance. If this transaction had been solely a tender offer, the court would be correct in saying that the controlling shareholder is on only one side of the transaction. In such a case, the minority shareholders would have the option of not tendering their shares. The key point though, is that they would still retain their ownership stake in the company. But it is a meaningless distinction when the tender offer is to be followed up by a short-form merger in which the minority shareholders are forced to sell their shares for the consideration that they just rejected.

The court further rejects the plaintiff's argument that *McMullin v. Beran*[38] requires the Siliconix board, either as a

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[36] *Siliconix*, 2001 WL 716787, at *7.

[37] *Id.* (internal citations omitted).

[38] 765 A.2d 910 (Del. 2000).

> *McMullin* teaches, *inter alia*, that in the context of a merger of a subsidiary with a third party . . . where the controlling shareholder wants the merger to occur and the minority shareholders are powerless to prevent it: (i) the directors of the subsidiary have "an affirmative duty to protect those minority shareholders' interests"; (ii) the board cannot "abdicate [its] duty by leaving it to the shareholders alone" to determine how to respond; and (iii) the board has a duty to assist the minority shareholders by ascertaining the subsidiary's value as a going concern so that the shareholders may be better able to assess the

whole or through its independent committee, to take a position on the proposed tender offer, and that their failure to do so is a breach of the duties of care and loyalty, thus implicating the entire fairness test. The court differentiates *McMullin* from this case in that *McMullin* involved a merger of a subsidiary into a third-party, for which the subsidiary board sought the approval of the minority shareholders. The court does recognize that "from the perspective of the minority shareholders, their need for (and their ability to benefit from) the guidance and information to be provided by their boards in accordance with the principles of *McMullin* is virtually indistinguishable."[39] The court distinguished the fiduciary duties in these two cases by noting that *McMullin* involved a merger, whereas *Siliconix* involved a tender offer, and also that the controlling shareholder in *McMullin* did not require the votes of the minority shareholders to proceed with the transaction,[40] whereas in *Siliconix* the tender offer would only succeed upon the acceptance of a majority of the minority shareholders.

Furthermore, the court emphasized that:

> as a general principle, [Delaware] law holds that a controlling shareholder extending an offer for minority-held shares in the controlled corporation is under no obligation, absent evidence that material information about the offer has been withheld or misrepresented or that the offer is coercive in some significant way, to offer any particular price for the minority-held stock.[41]

> acquiring party's offer and, thus, to assist in determining whether to pursue appraisal rights.

Siliconix, 2001 WL 716787, at *8 (citing McMullin v. Beran, 765 A.2d 910 (Del. 2000)).

[39] *Siliconix*, 2001 WL 716787, at *8.

[40] This was because the merger would go through with a greater than 50 percent majority vote and the controlling shareholder owned 80 percent of the stock.

[41] *Siliconix*, 2001 WL 716787, at *6 (quoting *In re* Ocean Drilling & Exploration Co. S'holders Litig., No.CIV.A. 11898 (Consolidated), mem. op. at 6-7 (Del. Ch. Apr. 30, 1991) (Chandler, V.C.)).

The court concluded that "as long as the tender offer is pursued properly, the free choice of the minority shareholders to reject the tender offer provides sufficient protection."[42] The fallacy of that conclusion is that those who reject the tender offer will be frozen out in the subsequent merger, leaving them entirely unprotected.

The Williams Act requires that a target corporation, upon its shareholders receiving a tender offer, file a Schedule 14D-9 with the SEC stating a recommendation as to whether or not the shareholders should tender.[43] The defendants in *Siliconix* argued that because federal law gives the board the right to express no opinion on the offer, the Williams Act preempts Delaware law to the extent that Delaware law requires actions by the board beyond the truthful and complete disclosures required by Schedule 14D-9.[44] The court did not find it necessary to reach this issue, because it held for the defendants on other grounds. Although the argument has some appeal, it is unlikely to succeed either in the Delaware state courts or in the federal courts. The law of fiduciary duties has traditionally been left to the states, and there is no indication that in writing Regulation 14D Congress intended to proscribe the outer limits of fiduciary duties. Rather, in my view, Congress merely meant to not require the board to take a position in the Schedule 14D-9 (as opposed to giving the board a substantive right to remain neutral, even if state fiduciary law requires some action from the board). Additionally, the fiduciary duties of interested board members are different from those of outside directors. Schedule 14D-9 makes no such distinction, and it is unlikely that Congress intended to preempt state law as to this important point. As this issue has never been reached, it is difficult to predict how it might be resolved. A finding for preemption might have severe ramifications in other areas of corporate fiduciary law, which has been left in such large

[42] *Siliconix*, 2001 WL 716787, at *6.

[43] 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (2002).

[44] *Siliconix*, 2001 WL 716787, at *8 n. 36.

part to the states that courts will not find preemption of state law absent a clear intent by Congress to do so.

B. *Glassman*

Glassman v. Unocal Exploration Corp.,[45] handed down by the Delaware Supreme Court just over a month after the *Siliconix* decision, reconciles the "fiduciary's seemingly absolute duty to establish the entire fairness of any self-dealing transaction with the less demanding requirements of the short-form merger statute."[46] Delaware's short-form merger statute, title 8, section 253 of the Delaware Code, specifically allows for an appraisal remedy for minority shareholders who are dissatisfied with the price paid to them by the controlling shareholder. This must be reconciled with *Kahn*, which holds that "[the] exclusive standard of judicial review in examining [the] propriety of an interested, cash-out merger transaction by [a] controlling or dominating shareholder is 'entire fairness.'"[47] The *Glassman* court struggles to balance the statute against the protections the court has created for minority shareholders over the years.

The language of the statute does not expressly make appraisal exclusive. The court infers that because the statute specifies that the appraisal remedy is available, the entire fairness test is not. Furthermore, the rapid procedure in the statute is inconsistent with the procedure that courts have determined is necessary to satisfy the fair dealing prong of entire fairness. Thus, if the court were to require a parent to satisfy the fair dealing test, it would swallow the statute, as parents could no longer take advantage of the summary proceeding for which the statute provides. If "the corporate fiduciary sets up negotiating committees, hires

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[45] 777 A.2d 242 (Del. 2001).

[46] *Id.* at 243.

[47] Kahn v. Lynch Communication Sys., Inc., 638 A.2d 1110, 1110 (Del. 1994). A "cash-out" merger is simply a short-form merger in which the consideration is all cash. A short-form merger may include "securities, cash, property, or rights to be issued, paid, delivered or granted by the surviving corporation." DEL. CODE ANN. tit. 8, § 253(a) (2002).

independent financial and legal experts, etc., then it will have lost the very benefit provided by the statute -- a simple, fast and inexpensive process for accomplishing a merger."[48] The court resolves the conflict in favor of the General Assembly, in order to give effect to the statute and enable the statute to serve its purpose. *Glassman* may have been correctly decided, but when combined with other decisions, it leaves a gaping loophole in Delaware's fiduciary law. A cynical view is that this is an example of Delaware leading a race to the bottom in the area of corporate governance.

C. *Aquila*

After *Siliconix* and *Glassman*, there remained a possibility that despite the fact that the acquirer would not be required to prove entire fairness, the target board would have a fiduciary duty to its shareholders to use whatever tactics it deemed necessary to extract the highest price possible from the parent, including perhaps the implementation of a poison pill. In *In re Aquila, Inc. Shareholders Litigation*[49] the chancery court made it clear that this was not the case, and that the target board is under no duty to negotiate a price with the parent who makes a tender offer.[50]

In *Aquila*, UtiliCorp United Inc. ("UtiliCorp") made a tender offer for the 20 percent of Aquila that it did not already own. Unlike Siliconix, Aquila lacked any outside directors. Its board did not express an opinion either in favor or against the tender offer, but rather obtained and published an independent financial analysis of the offer from

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[48] *Glassman*, 777 A.2d at 247-48.

[49] 805 A.2d 184 (Del.Ch. 2002).

[50] *See also In re* Pure Resources, Inc., S'holders Litig., 808 A.2d 421, 446 (Del. Ch. 2002) (Strine, V.C.) ("I am reluctant . . . to burden the common law of corporations with a new rule that would tend to compel the use of a device [the poison pill] that our statutory law only obliquely sanctions and that in other contexts is subject to misuse, especially when used to block a high value bid that is not structurally coercive.") For these purposes, the situation (described *infra*) is the same as in *Aquila*.

the Blackstone Group. The board did not, however, request a fairness opinion. Plaintiffs brought the lawsuit seeking to enjoin the tender offer until at least two independent directors were appointed to Aquila's board or until a court-appointed expert could conduct an analysis of the financial terms of the tender offer and make a recommendation.

In refusing to grant the preliminary injunction, the court reasoned that even if two independent directors were appointed to the board and those directors concluded that the price was unfair, "they could do little more than communicate their conclusion to the stockholders in the Schedule 14D-9 and recommend that they not tender. Certainly, *UtiliCorp would have no duty to negotiate the price with them*."[51] The court proceeded to conclude that the harm to Aquila's minority stockholders, that UtiliCorp might abandon its offer, far outweighed the possible benefits of an injunction. The court found the only benefit of an injunction to be a potential unbiased recommendation to the shareholders. But the benefit of an injunction could have outweighed the possible harm to the stockholders if the board was found to have a duty to negotiate with the parent company for a better price. In my opinion, that would have been the better outcome. The standard should be that a board of directors has the duty to take any actions to benefit shareholders that it would take were it not for the conflict of interest. The respective boards of Siliconix and Aquila clearly would not have remained inactive upon receipt of a tender offer if their companies had no majority owners and the transaction were not with a related party.[52] In my view, with the transactions in these cases being with the majority owner, it is a clear violation of the principle-agent

[51] *Aquila*, 805 A.2d at 195 (emphasis added).

[52] "Finally, the board's power to act derives from its fundamental duty and obligation to protect the corporate enterprise, which includes the stockholders, from harm reasonably perceived, irrespective of its source. Thus, we are satisfied that in the broad context of corporate governance, including issues of fundamental corporate change, a board of directors is not a passive instrumentality." Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (internal citations omitted).

relationship to allow the subsidiary boards to remain inactive.

D. *Hartley*

In *Hartley v. Peapod, Inc.*,[53] Vice Chancellor Lamb imposed some limitations on the reach of *Siliconix*. He held that entire fairness is required in a two-step freezeout effected pursuant to a merger agreement that contemplates a short-form merger only if the parent obtains over 90 percent of the outstanding shares in the tender offer. If the parent were to obtain less than 90 percent it would plan on doing a long-form merger.

In *Hartley*, the controlling stockholder, Koninklijke Ahold N.B. ("Ahold") entered into a merger agreement with Peapod that called for an initial tender offer, followed by either a short-form or a long-form merger, the short-form being possible only if Ahold were to receive 90 percent of the shares in the tender. Ahold did end up reaching 90 percent in the tender, and subsequently completed a short-form merger. Minority stockholders of Peapod brought a lawsuit to challenge the transaction as violating entire fairness. The defendants argued that under *Siliconix* they are under no duty to prove entire fairness. The court disagreed, and found *Kahn v. Lynch Communication Systems, Inc.*[54] to be the appropriate precedent. Under *Kahn*, entire fairness is required in such a transaction principally because the terms of the merger were part of a negotiated transaction with the target's board of directors.

Vice Chancellor Lamb's ruling builds on a footnote from his *Unocal Exploration*[55] opinion, in which he held that appraisal should be the exclusive remedy in a short-form merger. In that case, he recognized that some short-form mergers are the second step of a negotiated transaction in

[53] No.CIV.A. 19025 (Del. Ch. Feb. 27, 2002) (Lamb, V.C.).

[54] 638 A.2d 1110 (Del. 1994).

[55] *In re* Unocal Exploration Corp. S'holders Litig., 793 A.2d 329 (Del. Ch. 2000), *aff'd*, Glassman v. Unocal Exploration Corp., 777 A.2d 242 (Del. 2001).

which a controlling shareholder goes from owning less than 90 percent to owning 100 percent of the subsidiary. "While those mergers may, ultimately, take the form of a Section 253 merger, their terms were the subject of negotiation with the target company board of directors and should, where appropriate, be examined by using the entire fairness analysis."[56]

E. *Pure Resources*

In re Pure Resources, Inc., Shareholders Litigation,[57] the most recent case to address the question of whether a parent must demonstrate entire fairness in a series of transactions designed to freeze out the minority shareholders, contains some strong language supporting *Kahn* and its justifications for the heightened protection for minority shareholders in parent-subsidiary mergers. However, it curiously switches course and holds that the entire fairness review mandated by *Kahn* should not be extended to tender offers followed by freezeout mergers.

In *Pure Resources*, Unocal owned 65 percent of the shares of Pure Resources. Unocal proposed an exchange offer, in which it would acquire the rest of the shares of Pure Resources in exchange for shares of Unocal. The board of Pure Resources set up an independent committee that had the power to retain financial advisers, take a position on the offer, and negotiate with Unocal to try to get it to increase its bid. The committee initially expressed a desire to have greater power. It wanted to be delegated the full authority of the board under Delaware law to respond to this offer, including searching for alternative transactions or putting a poison pill in place. Instead, its authority was reduced to merely studying the offer, negotiating, and making a recommendation in the Schedule 14D-9. The committee accepted this reduced responsibility, and according to the court "was unwilling to confront Unocal as aggressively as it

[56] *Unocal Exploration*, 793 A.2d at 339 n. 26.

[57] 808 A.2d 421 (Del. Ch. 2002).

would have confronted a third-party bidder."[58] Negotiations proved unfruitful and the committee made its recommendation not to tender.

The plaintiffs argued that the offer was subject to entire fairness review under *Kahn*, even though that case involved a merger and this one a tender offer. The defendants in turn argued that under *Solomon v. Pathe Communications Corp.*,[59] the offer is not subject to the entire fairness standard because the offer was not coercive. *Solomon* holds that in voluntary tender offers, courts do not impose any right of the shareholders to receive a particular price, and entire fairness is not mandatory. It also states that "as to allegedly voluntary tender offers (*in contrast to cash-out mergers*), the determinative factor as to voluntariness is whether coercion is present"[60] or whether there are misleading disclosures. *Solomon* is silent as to whether entire fairness is mandated where the first part of the transaction is a voluntary tender offer, but the tender offer is to be followed up by a cash-out merger at the same price. The *Pure Resources* court subjects the exchange offer to the *Solomon* standard rather than the *Kahn* entire fairness standard, but it notes that many of the concerns that justify the *Kahn* standard are implicated by the facts of *Pure Resources*. The court then states:

> [t]hese concerns should be accommodated within the *Solomon* form of review, by requiring that tender offers by controlling shareholders be structured in a manner that reduces the distorting effect of the tendering process on free stockholder choice and by ensuring minority stockholders a candid and unfettered tendering recommendation from the independent directors of the target board.[61]

Vice Chancellor Strine recognizes that these two strands of cases "appear to treat economically similar transactions as categorically different simply because the method by which

[58] *Id.* at 431.

[59] 672 A.2d 35 (Del. 1996).

[60] *Id.* at 39 (emphasis added).

[61] *Pure Resources*, 808 A.2d at 424.

the controlling stockholder proceeds varies,"[62] and that both methods "pose similar threats to minority stockholders."[63] He even points out that a tender offer followed by a short-form merger is arguably less protective of the minority than a merger negotiated by an independent committee, which requires a majority of the minority vote, because in the tender offer the majority stockholder "has access to inside information, and the offer requires disaggregated stockholders to decide whether to tender quickly, pressured by the risk of being squeezed out in a short-form merger at a different price later or being left as part of a much smaller public minority."[64] Additionally, in a merger vote stockholders can vote no and still receive the same consideration if the merger goes through. In a tender offer, however, a shareholder who declines to tender may not be so fortunate. The tender-offeree who is dissatisfied with the price being offered is often placed in a prisoner's dilemma. Fearing that the transaction will go through and he will be left with even less desirable minority shares,[65] he will choose to tender. If enough shareholders who do not want the transaction to succeed tender for that reason, the offer will succeed. The court further notes that in a tender offer the controlling stockholder can time its offer to "put a bull rush on the target stockholders."[66] Vice Chancellor Strine "remains less than satisfied that there is a justifiable basis for the distinction between the *Kahn* and *Solomon* lines of cases,"[67] noting that the disparities "reflect a difference in policy emphasis that is far greater than can be explained by the technical differences between tender offers and negotiated mergers."[68]

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[62] *Id.* at 435.

[63] *Id.*

[64] *Id.*

[65] This assumes that the greater the percentage of the company that the controlling shareholder owns, the less desirable it is to be a minority shareholder.

[66] *Pure Resources*, 808 A.2d at 443.

[67] *Id.*

[68] *Id.*

Nonetheless, the court refuses to expand the *Kahn* standard to controlling stockholder tender offers. Rather, it justifies adherence to the *Solomon* rubric by noting the "increased activism of institutional investors and the greater information flows available to them."[69] The court notes that institutional investors do not fear retribution in the same way that individual stockholders do. "[T]he corporate law should not be designed on the assumption that diversified investors are infirm but instead should give great deference to transactions approved by them voluntarily and knowledgeably."[70] In my opinion, this overestimates the amount of leverage institutional shareholders have in the face of a controlling shareholder. Furthermore, fiduciary duties should not be adjusted depending on the identity of the minority shareholders.

Vice Chancellor Strine refines *Solomon* as applied in this situation as follows. A *coercive* offer will still be subject to entire fairness under *Kahn*.

> An acquisition tender offer by a controlling stockholder [will be considered] non-coercive only when: 1) it is subject to a non-waivable majority of the minority tender condition; 2) the controlling stockholder promises to consummate a prompt section 253 merger at the same price if it obtains more than 90 percent of the shares; and 3) the controlling stockholder has made no retributive threats.[71]

These provisions do little to ensure that the minority shareholders receive full value for their shares.

The first condition, the majority of the minority provision, is meant to replicate a shareholder vote. It ensures that at least 50 percent of the minority shareholders accept the consideration offered. The price will be the minimum price at which 50 percent of the minority shareholders will tender. This provision does little to protect minority shareholders,

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[69] *Id.* at 444.

[70] *Id.*

[71] *Id.* at 445.

because shareholders will likely accept a small premium over the market value of their shares if they do not have a negotiating committee to try to get an even greater premium for them. The second condition, the promise to complete the freezeout transaction, does protect the shareholders from the prisoner's dilemma. It puts shareholders who do not wish to accept the consideration being offered in the same position as a shareholder who votes no in a merger vote. Both will get the consideration being offered if the transaction goes through. In a merger, however, the target board likely has already negotiated (perhaps through the use of a poison pill) for the highest consideration possible, perhaps even from multiple bidders. As for the third condition, that the controlling stockholder has made no retributive threats, courts have recognized that threats can be feared even if they are not explicitly articulated.

> The controlling stockholder relationship has the inherent potential to influence, however subtly, the vote of [ratifying] minority stockholders in a manner that is not likely to occur in a transaction with a noncontrolling party. Even where no coercion is intended, shareholders voting on a parent subsidiary merger might perceive that their disapproval could risk retaliation of some kind by the controlling stockholder.[72]

These conditions, although helpful, do little to alleviate the concerns of the *Kahn* court, which are also the same concerns that Vice Chancellor Strine echoes throughout much of the *Pure Resources* opinion.

IV. HOW *SILICONIX* AND *GLASSMAN* MAY ALTER CORPORATE BEHAVIOR

If *Siliconix* is upheld, it will expand the range of parent-subsidiary mergers in which the parent has no duty to prove

[72] Citron v. E.I. Du Pont de Nemours & Co., 584 A.2d 490, 502 (Del. Ch. 1990).

entire fairness. If the parent does not have to prove entire fairness, it has little incentive to create an arms-length bargaining situation for the benefit of the minority shareholders. If the only available remedy is statutory appraisal, the minority shareholders can expect to receive the lowest price acceptable under an appraisal, as opposed to the higher price that a bargaining agent might be able to get for them from the controlling shareholder. The Delaware Supreme Court already sees the appraisal remedy as inadequate, even in a short-form merger that falls under title 8, section 253 of the Delaware Code (where the majority owns at least 90 percent of the equity).[73] Yet after *Siliconix* a parent can eliminate a larger majority than allowed by section 253 without ever having to prove entire fairness.

It is not clear that parent companies will immediately seize on this new opportunity. For example, in October 2001, SBC Communications, Inc. made a tender offer for the 58 percent equity stake in Prodigy Communications Corp. that it did not already own. Prodigy formed a special committee, which succeeded in negotiating an extra $81 million for the minority shareholders. Joseph Frumkin, a lawyer for SBC, said "[i]t's a good model. It had the advantage of permitting a greater degree of control over timing for the bidder and the further advantage of not appearing quite so aggressive as doing the deal without taking into account the independent directors."[74] Daniel Sternberg, a partner at Cleary, Gottlieb, Steen & Hamilton, said such a process may be faster than negotiating a merger with a special committee. "The role of the special committee is narrower. It can only make a recommendation to shareholders -- to accept or reject the offer -- or, in theory, it can stay neutral."[75] The controlling shareholders still have to convince a majority of the minority

[73] "[W]e find nothing magic about a 90 percent ownership of outstanding shares which would eliminate the fiduciary duty owed by the majority to the minority." Glassman v. Unocal Exploration Corp., 777 A.2d 242, 246 (Del. 2001).

[74] David Marcus, *An End Run in Delaware*, CORP. CONTROL ALERT 8 (Dec. 2001) (on file with author).

[75] *Id.* at 8-9.

shareholders to tender their shares. A controlling shareholder might find it an easier task with the establishment of an independent committee to issue a fairness opinion. If the committee says that the offer is fair, minority shareholders would be more likely to tender. Another possible reason for this voluntary act is that no parent company wants to be "the poster child for the reversal of *Siliconix*."[76]

Recent anecdotal evidence shows that the fear of shareholder lawsuits is in fact the motivation behind target directors taking on an active role in negotiating a transaction with the parent company.[77] For example, in February 2002, Sabre made an offer for the 30 percent of Travelocity.com Inc. that it did not already own, for $345 million.[78] Travelocity.com's board set up an independent negotiating committee, which determined that the bid was inadequate and recommended that shareholders reject it. Sabre subsequently raised its bid 22 percent to $420 million. Assuming that Sabre had control of Travelocity.com's board, and that it would have preferred to not have paid the additional $75 million, Sabre presumably was worried that it (or the target board, collectively and individually) was subjecting itself to legal liability if it did not set up an effective independent committee.

V. RECOMMENDATION

Ultimately, the *Siliconix* court was persuaded by the difference in form between the stock-for-stock tender offer followed by the short-form merger and a statutory merger, even though there is little substantive difference between the two that is relevant to the protection of the minority shareholders. The court's two reasons for this are as follows:

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[76] Charles M. Nathan, *New Pattern* (Nov. 8, 2001), *at* http://thedailydeal.com (on file with author).

[77] Robin Sidel, *Takeover Targets Force Up Offers in 'Minority Squeeze-Out' Deals*, WALL ST. J., May 10, 2002, at C3.

[78] *Id.*

> First, Delaware law has recognized the tender followed by the short-form merger as separate events. To view it otherwise would preclude, as a practical matter, the efficiencies allowed by the short-form merger process. Second, in this instance, there is no guarantee (although it is most likely) that Vishay will complete the back-end merger.[79]

In my opinion, those two concerns can be alleviated with limitations on the scope of an opinion requiring the entire fairness test under the facts of *Siliconix*. First, the court could have alleviated the uncertainty of whether Vishay would follow through with its plan to complete the back-end merger by limiting the *Siliconix* holding to cases in which the back-end has not been completed. Upon completion of the freezeout, a plaintiff could then bring an action for failure to meet the entire fairness test. Vice Chancellor Strine qualifies the *Pure Resources* opinion by stating "[f]or the purposes of this opinion, my references to tender offers by controlling stockholders means those tender offers in which the controlling stockholder hopes to acquire all of the remaining shares, in the tender itself, or in combination with a later short-form merger."[80] Second, Delaware law has recognized a tender offer followed by a short-form merger as two separate events, but that does not necessarily have to be the case for all purposes.

In one sense it is ironic that Delaware courts, which famously protect the right of a target board to defend itself against a hostile takeover attempt (which is in the form of a tender offer) by refusing to redeem a poison pill,[81] in this case justify the board's passivity in the face of such a takeover attempt by the parent. But in another sense, both the *Unocal* line of cases and *Siliconix* can be seen as pro-management decisions. *Unocal* and later cases that build

[79] *Siliconix*, 2001 WL 716787, at *8 n.35.

[80] *Pure Resources*, 808 A.2d at 424 n.3 .

[81] *See* Jeffrey N. Gordon, "*Just Say Never?*" *Poison Pills, Deadhand Pills, and Shareholder-Adopted Bylaws: An Essay for Warren Buffet*, 19 CARDOZO L. REV. 511 (1997); Paramount Communications, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1990).

upon it permit a role for the target board in a tender offer under the justification of extracting a better deal from the acquirer for the shareholders. But this has the effect of allowing management to entrench itself. *Siliconix* does not mandate a similar role for the target board under the same justification, but this has the effect of allowing the parent's board members to complete the transaction without having to pay such a premium that is often extracted with the imposition of a poison pill. So even though these decisions could be viewed as contradictory, they both have the effect of benefiting boards and management at the expense of shareholders. Although *Siliconix* benefits the controlling shareholder as shareholder, the controlling shareholder is the parent corporation, and the people who make the decision to incorporate both the parent and the subsidiary in Delaware are the people who will benefit by the additional gain in the transaction by not having to prove entire fairness. This comports with the notion that Delaware's law is friendly to those who make the decision to choose the state for incorporation,[82] and in my opinion goes a long way in explaining the courts' decisions on the role of a target board in a tender offer.

My recommendation is based on the assumption that minority shareholders deserve to receive the highest amount possible for their shares. Studies show that, on average, selling shareholders receive large premiums and acquirers' share prices suffer following acquisitions.[83] This is largely because poison pills ensure that a target board will negotiate with the acquirer to extract the largest gain possible for the shareholders. An argument can be made that minority shareholders should not be entitled to the traditional windfall that normally falls upon selling shareholders in an acquisition. In other words, perhaps *Kahn* is wrong for

[82] *See, e.g.*, Marcel Kahan & Edward B. Rock, *How I Learned to Stop Worrying and Love the Pill: Adaptive Responses to Takeover Law*, 69 U. CHI. L. REV. 871, 907 (2002).

[83] Michael Bradley, Anand Desai & E. Han Kim, *Synergistic Gains from Corporate Acquisitions and Their Division Between the Stockholders of Target and Acquiring Firms*, 21 J. FIN. ECON. 3 (1988).

assuming that minority shareholders are entitled to receive the maximum value for their shares that can be negotiated by an independent committee. *Kahn* makes no reference to the traditional abnormal distribution of surplus gains from acquisitions tilting heavily toward sellers. The court seems to assume that entire fairness is necessary to get a price that is most fair to the minority shareholders (even though fair value is already mandated by the appraisal remedy), but it never contemplates the fact that it might force controlling shareholders to grossly overpay to receive 100 percent of the company. Minority shareholders are certainly entitled to fair value, but to entitle them to more might be ignoring the expectations that shareholders have when they buy into a company that has a large controlling shareholder. Because a controlling shareholder can control the assets of the company, it is quite possible that it could act in its own best interest as opposed to the interest of the minority shareholders. As such, minority shares are likely to trade at a discount to what they would trade at if ownership were more widely dispersed. Consequently, if an entire fairness process is mandated, it is even more likely that the selling shareholders will receive a large windfall than in the case of an unrelated acquisition. Although that counter-argument has merit, in my opinion without the entire fairness test of *Kahn* it would be too easy for the parent to take advantage of the minority shareholders by purchasing the shares at too low a price. There are several reasons why I reach this conclusion. First, a parent is most likely to enter into a freezeout merger at a time when it believes that the subsidiary's shares are undervalued by the market. Second, a parent is in a position to depress the shares temporarily by managing accounting numbers or delaying certain business transactions just prior to the freezeout. Third, the appraisal remedy is costly for the plaintiffs to pursue, and the only remedy is forcing the parent to pay fair value. That does not give a parent a great incentive to offer the higher end of fair value in the first place.

Additionally, Delaware case law is rich with discussion of the board being the information agent for the shareholders.[84] Granted, those cases traditionally deal with mergers. But boards of companies that receive tender offers always voluntarily take on the role of information agent for the shareholders. This is quite possibly due to their own personal interests in keeping their jobs (which they will likely lose if the tender offer is successful). Nonetheless, if case law is clear that boards owe a duty to their shareholders to help them make informed judgments in the case of mergers, and boards perform that duty voluntarily in the face of tender offers, then why should the board of a company with a controlling shareholder be permitted to take such a passive role? The Delaware statute that defines the role of the board does not contemplate a less active role in the case of the board of a controlled subsidiary.[85] Such boards have the same fiduciary duties that all boards have and should be required to act vigorously on behalf of the shareholders as a class, which includes the minority shareholders. On their behalf, they should be required to make an informed recommendation to the shareholders as to whether or not to tender their shares.[86]

Consequently, I believe that *Siliconix* should be overturned. I would recommend that the court base its decision on the doctrine of "substance over form" and call these two transactions what they really are, which is one big attempt by the parent to freeze out a large minority at the lowest price possible. Alternatively, the court could impose a procedural fiduciary obligation on the board (or an independent committee) of the subsidiary to negotiate with the parent as zealously as it would with a third-party bidder. Just as the entire fairness doctrine and the fair dealing

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[84] *See, e.g.*, Ace Ltd. v. Capital Re Corp., 747 A.2d 95 (Del. Ch. 1999).

[85] *See* DEL. CODE ANN. tit. 8, § 141 (2002).

[86] *Pure Resources* does state that the independent target directors have a duty to provide "the minority with a recommendation as to the advisability of the offer," but it ignores the claim that the Williams Act, which permits a board to remain silent, preempts Delaware law in this area. 808 A.2d at 445.

prong are common law creations, in my opinion the Delaware courts could create such an obligation on the subsidiary board.

> I'm not sure that the Delaware courts can live with the dichotomy they're [*sic*] created between going private transactions involving target board action where entire fairness applies and those not requiring target board action in which there is no requirement of entire fairness. I think they're going to be very uneasy with it.[87]

I concur, and hope that either the courts or the legislature reconsider this loophole that controlling shareholders can jump through at the expense of the unwitting minority shareholders.

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[87] Marcus, *supra* note 74, at 9.