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Panterv. Marshall Field & Co.: The Good Faith Standard for Corporate Directors

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PANTER v. MARSHALL FIELD & CO.: THE GOOD FAITH STANDARD FOR CORPORATE DIRECTORS

Corporate directors traditionally have been immunized from liability for corporate actions involving questions of policy or "business judgment," if such actions are taken in the exercise of due care, in good faith, and in compliance with applicable fiduciary duties.[1] Judicial review of decisions made by corporate boards of directors in unsolicited takeovers[2] generally has been barred by this business judgment rule.[3] A recent challenge to this precept was brought in *Panter v. Marshall Field & Co.*,[4] a Seventh Circuit decision which highlighted many of the issues surrounding application of the business judgment rule in the context of a take-over attempt.

This comment will review the Seventh Circuit's decision in the *Marshall Field* case and assess its implications for directors in exercising "reasonable business judgment" in good faith and for shareholders in challenging the actions of the directors. Although the divided court[5] up-

1. A basic articulation of the business judgment rule is:

> If in the course of management, directors arrive at a decision . . . for which there is a reasonable basis, and they act in good faith, as the result of their independent discretion and judgment, and uninfluenced by any consideration other than what they honestly believe to be the best interests of the corporation, a court will not interfere . . . and substitute its judgment for that of the directors . . . .

H. HENN, HANDBOOK OF THE LAW OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 242, at 482 (2d ed. 1970). If the duty of care or the fiduciary duties owed by directors to the corporation are breached, the directors may be jointly and severally liable to the corporation itself and to the shareholders. *Id.* at 458. The fiduciary duties include those of good faith and fair dealing in the best interests of the corporation. *Id.*

2. A takeover involves an offer or solicitation by a company to purchase all or a portion of the stock of another company during a fixed period of time for a specified price or on specified terms for cash and an exchange of stock. E. ARANOW & H. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL 70 (1973). The "raider's" offer to the "target" company is unsolicited and deemed unfriendly. Such offers are hostile to the management of the target corporation. Bowers, *It's a Raid! Strategies for Avoiding Takeovers*, 3 WHARTON MAGAZINE 22, 22 (Summer 1979). *See also* Panter v. Marshall Field & Co., 486 F. Supp. 1168, 1175 (N.D. Ill. 1980), *aff'd*, 646 F.2d 271 (7th Cir. 1981).

3. *See, e.g.*, Treadway Cos. v. Care Corp., 638 F.2d 357 (2d Cir. 1980); Crouse-Hinds Co. v. InterNorth, Inc., 634 F.2d 690 (2d Cir. 1980); Lewis v. McGraw, 619 F.2d 192 (2d Cir.), *cert. denied*, 101 S. Ct. 354 (1980); Golub v. PPD Corp., 576 F.2d 759 (8th Cir. 1978); Gulf & Western Indus., Inc. v. Great A & P Tea Co., 476 F.2d 687 (2d Cir. 1973); Berman v. Gerber Prods. Co., 454 F. Supp. 1310 (W.D. Mich. 1978); Armstrong Cork Co. v. H. A. Meldrum Co., 285 F. 58 (W.D.N.Y. 1922); GM Sub Corp. v. Liggett Group, Inc., 415 A.2d 473 (Del. 1980).

4. 646 F.2d 271 (7th Cir. 1981).

5. The decision was made by a three judge panel with a vigorous dissent to the majority opinion. *Id.* at 299. *See* notes 145-68 *infra* and accompanying text.

held actions of the defendant-directors taken in exercise of their business judgment, the case seems to point the way to heightened judicial scrutiny of corporate boardroom decisions and perhaps suggests that a new look be taken at duties owed by directors to the corporation and its shareholders.

I. THE BUSINESS JUDGMENT RULE

A. *Definition and Scope of the Rule*

The business judgment rule states generally that a corporate director who conscientiously attends to his or her duties and exercises good business judgment on the questions facing the board will not be personally liable even if the judgment is faulty and the corporation thereby incurs some detrimental effect.[6] "Implicit in this statement of the rule is that there be an affirmative directorial judgment" and some resulting injury to either the corporation or the shareholders.[7] The rule provides a substantive defense for honest, non-negligent errors in judgment and insulates directors from personal liability in the shifting, often hazardous business world.[8] The business judgment rule recognizes the fallibility of directors as human beings and their inability to please all stockholders at all times[9] and facilitates business growth by providing an unshackled environment in which board members may make decisions and freely act on them.[10] It also limits judicial review in areas best left to business expertise and acumen and preserves judicial economy.[11] The Pennsylvania Supreme Court in *Smith v. Brown-Borhek Co.*[12] justified the business judgment rule as follows:

> [I]n the business world . . . it is too often forgotten that all businesses do not flourish, nearly every business has some losses and some bad accounts, and many insolvencies and bankruptcies frequently occur even in these

6. *See* Arsht, *The Business Judgment Rule Revisited,* 8 HOFSTRA L. REV. 93, 93-97 (1979) [hereinafter cited as Arsht, *Business Judgment*]. *See, e.g.,* Hodges v. New England Screw Co., 3 R.I. 9, 18 (1853).

7. Arsht, *Business Judgment, supra* note 6, at 112.

8. *Id.* at 111. *See generally* Johnson v. Trueblood, 629 F.2d 287, 292 (3d Cir. 1980); Smith v. Brown-Borhek Co., 414 Pa. 325, ___, 200 A.2d 398, 401 (1964); H. HENN, *supra* note 1, at 482.

9. Arsht, *Business Judgment, supra* note 6, at 95.

10. *See, e.g.,* Kaplan v. Goldsamt, 380 A.2d 556, 558 (Del. Ch. 1977); Auerbach v. Bennett, 47 N.Y.2d 619, 629, 393 N.E.2d 994, 1000, 419 N.Y.S.2d 920, 926 (1979); 3A W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 1039 (rev. perm. ed. 1975); ABA, *Corporate Director's Guidebook,* 33 BUS. LAW. 1595, 1604 (1978); Johnson and Osborne, *The Role of the Business Judgment Rule in a Litigious Society,* 15 VAL. U. L. REV. 49, 54 (1980).

11. Johnson and Osborne, *supra* note 10, at 54.

12. 414 Pa. 325, 200 A.2d 390 (1964) (case involving negligent mismanagement of corporate funds due to an over-extension of credit to a large customer, which was authorized by the Brown-Borhek Company directors).

> prosperous times. . . . From an early date this court has consistently and realistically recognized the danger of subjecting corporate directors to liability whenever any of the transactions of the company did not meet with success.[13]

Since the management of all corporations rests with the directors,[14] the courts historically have been concerned with obtaining quality directors.[15] Of necessity, directors need to be persons of reason, intellect, and integrity. In order to attract such individuals, the business judgment rule was formulated to protect their decisions from needless attack and "Monday-morning-quarterbacking."[16]

The business judgment rule has been part of corporate law for at least 150 years.[17] It came into being as a result of the growth of industry in the late nineteenth century. Perhaps the earliest expression of the purpose and limits of the rule is found in *Percy v. Millaudon*,[18] an 1829 Louisiana Supreme Court decision involving the liability of bank directors for losses resulting from the misappropriation of funds by the bank's president and cashier. The Lousiana court noted that "the adoption of a course from which loss ensues cannot make the agent responsible, if the error was one into which a prudent man might have fallen."[19] Approximately twenty-five years later, the Supreme Court of Rhode Island succinctly stated the business judgment rule in *Hodges v. New England Screw Co.*[20] In an effort to save the New England Screw Company from bankruptcy, its directors authorized the corporation to purchase stock in another company. It then forced that company to lend money and extend credit to New England.[21] Although the directors were found to have exercised good faith and acted in the company's best interests, their actions had violated New

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13. *Id.* at ___, 200 A.2d at 401.

14. *See, e.g.*, DEL. CODE ANN. tit. 8, § 141(a) (Supp. 1980); N.Y. BUS. CORP. LAW § 701 (McKinney Supp. 1980-1981). *See generally* ABA-ALI MODEL BUS. CORP. ACT § 35 (1977); N. LATTIN, THE LAW OF CORPORATIONS § 69 (2d ed. 1971).

15. The Pennsylvania Supreme Court explained:

> If the test of negligence which is applicable in the field of torts or in the Estate field were similarly applicable in the business or banking field, it would *realistically* be very difficult if not almost impossible to secure the services of *able and experienced* corporate directors. Such persons would rarely ever accept a directorship if they could be held liable for every 'bad' account or every mistake of judgment.

414 Pa. at ___, 200 A.2d at 401. *See also* Godbold v. Branch Bank, 11 Ala. 191, 199 (1847).

16. Panter v. Marshall Field & Co., 646 F.2d 271, 297 (7th Cir. 1981); Cheff v. Mathes, 41 Del. Ch. 494, ___, 199 A.2d 548, 554 (1964); Smith v. Brown-Borhek Co., 414 Pa. 325, ___, 200 A.2d 398, 401 (1964).

17. Arsht, *Business Judgment*, *supra* note 6, at 93. *See, e.g.*, Smith v. Prattville Mfg. Co., 29 Ala. 503 (1857); Godbold v. Branch Bank, 11 Ala. 191 (1847); Percy v. Millaudon, 8 Mart. (n.s.) 68 (La. 1829); Hodges v. New England Screw Co., 1 R.I. 312 (1850).

18. 8 Mart. (n.s.) 68 (La. 1829).

19. *Id.* at 77-78.

20. 1 R.I. 312 (1850), *rehearing denied*, 3 R.I. 9 (1853).

21. 1 R.I. at 342.

England's charter.[22] In refusing to hold them liable for the resulting losses, the court said, "we think a Board of Directors acting in good faith and with reasonable care and diligence, who nevertheless fall into a mistake, either as to law or fact, are not liable for the consequences of such mistake."[23] The articulation of the rule as an abstract principle of law has changed little since that time.[24] Today, in most states, the rule is derived from case law.[25] Twenty states have statutes codifying the standard of care to be exercised by directors.[26]

The standard of care or the duty of due care owed by corporate directors to the corporation found early expression in *Hun v. Cary*,[27] where a receiver of a savings bank sued the directors of the bank for negligent mismanagement. The court said that it was the duty of directors to exercise the same degree of care and prudence that a reasonable man would exercise in the management of his own affairs,[28] and that one who voluntarily takes a position as director represents to the shareholders "that he possesses at least ordinary knowledge and skill, and that he will bring

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22. *Id.* at 346-47.

23. 3 R.I. at 18.

24. *See* Schein v. Caesar's World, Inc., 491 F.2d 17, 18 (5th Cir.), *cert. denied*, 419 U.S. 838 (1974); Financial Indus. Fund, Inc. v. McDonnell Douglas Corp., 474 F.2d 514, 518 (10th Cir.), *cert. denied*, 414 U.S. 874 (1973); Panter v. Marshall Field & Co., 486 F. Supp. 1168, 1194, *aff'd*, 646 F.2d 271 (7th Cir. 1981); Nanfito v. Tekseed Hybrid Co., 341 F. Supp. 240, 243-44 (D. Neb. 1972), *aff'd*, 473 F.2d 537 (8th Cir. 1973).

25. Veasey and Manning, *Codified Standard—Safe Harbor or Uncharted Reef? An Analysis of the Model Act Standard of Care Compared with Delaware Law*, 35 BUS. LAW. 919, 920 (1980).

26. *See* CAL. CORP. CODE § 309 (West 1977); CONN. GEN. STAT. ANN. § 33-313(d) (West Supp. 1979); FLA. STAT. ANN. § 607.111(4)-(7) (West 1977); GA. CODE ANN. § 22-713 (1977); IDAHO CODE ANN. § 30-1-35 (1980); IND. CODE ANN. § 23-1-2-11(2) (Burns Supp. 1981); IOWA CODE ANN. § 496A.34 (West Supp. 1981-1982); LA. REV. STAT. ANN. § 12.92 (West 1969); ME. REV. STAT. ANN. tit. 13-A, § 716 (1964); MD. CORP. & ASS'NS CODE ANN. § 2:405.1 (Supp. 1981); MASS. GEN. LAWS ANN. ch. 156B, § 65 (West 1969); MICH. COMP. LAWS ANN. § 450.1541 (MICH. STAT. ANN. § 21.200 (1973)); MINN. STAT. ANN. § 301.31 (West 1969); N.Y. BUS. CORP. LAW § 717 (McKinney Supp. 1980-1981); N.C. GEN. STAT. § 5535 (1975); OKLA. STAT. ANN. tit. 18, § 1.34(b) (West 1951); PA. STAT. ANN. tit. 15, § 1408 (Purdon Supp. 1981-1982); R.I. GEN. LAWS § 7-1.1-43 (1969); S.C. CODE § 33-13-150 (1976); TENN. CODE ANN. § 48-813 (Repl. Vol. 1979).

The American Bar Association adopted § 35 of the Model Business Corporation Act in an effort to produce a workable, uniform codification of the standard of care owed by directors to the corporation. Section 35 serves as a guide to directors of corporations and also to states in drafting corporate legislation. *See* ABA-ALI MODEL BUS. CORP. ACT § 35 (1975). *See also* ABA, *Corporate Director's Guidebook*, 33 BUS. LAW, 1595, 1604 (1978); Arsht, *Fiduciary Responsibilities of Directors, Officers and Key Employees*, 4 DEL. J. CORP. L. 652, 662 (1979) [hereinafter Arsht, *Fiduciary Responsibilities*]; Veasey, *Directors' Standard of Care Under Section 35 of the Model Business Corporation Act*, 4 DEL. J. CORP. L. 665 (1979).

27. 82 N.Y. 65 (1880).

28. *Id.* at 71. *See also* Briggs v. Spaulding, 141 U.S. 132 (1890) (national bank went bankrupt 90 days after defendant-directors elected to manage bank).

them to bear in the discharge of his duties."[29] When the director uses such care and prudence in making his or her decision, the business judgment rule shields that decision from scrutiny by the courts.[30]

In addition to exercising due care, a director has certain fiduciary duties which require good faith and fair dealing.[31] Some commentators speak of this as a "duty of loyalty."[32] In *Guth v. Loft*,[33] the Delaware Supreme Court stated:

> The duty of loyalty requires the director not only affirmatively to protect the interests of the corporation committed to his charge, but also to refrain from doing anything that would work injury to the corporation, or to deprive it of profit or advantage which his skill and ability might properly bring to it, or to enable it to make in the reasonable and lawful exercise of its powers. The rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest.[34]

Thus, where a director is likely to benefit personally from a decision made by the board, his or her business judgment may be affected by that interest. If it is, the director as an individual, rather than as one serving the corporate best interest, will have governed the decision. Therefore the breach of fiduciary duty precludes application of the business judgment rule.[35]

Claims against a corporation or its directors may be asserted directly by a shareholder, based on his membership contract with the corporation.[36] Suit may be brought by the shareholder individually or on behalf of himself and those of his class who are similarly situated.[37] A cause of action arises when directors breach their duty of care or their fiduciary duties to the corporation and its shareholders.[38] In bringing suit, share-

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29. 82 N.Y. at 74.

30. Casey v. Woodruff, 49 N.Y.S.2d 625, 643 (1944).

31. H. HENN, *supra* note 1, at 457-59.

32. Arsht, *Business Judgment*, *supra* note 6, at 115.

33. 23 Del. Ch. 255, 5 A.2d 503 (1939) (Loft's corporate funds used to build up two corporations owned by Guth, vice-president of Loft and controlling voice on Loft board of directors).

34. *Id.* at 270, 5 A.2d at 510.

35. H. HENN, *supra* note 1, at 459.

36. *Id.* at 740. This contract is based on a theory of corporate personality whereby incorporation is deemed to involve contracts among the members, between the members and the corporation, and between the members of the corporation and the state. *Id.* at 109. The corporation acts through its board of directors.

37. *Id.* at 755-59. Direct suit involves the enforcement by a shareholder of a cause of action, belonging to him on the basis of his membership contract, against the corporation or others. This suit is distinguished from a derivative suit which brings an action on behalf of the corporation itself by a shareholder where harm has been done to the corporation and the corporation has failed to enforce such a claim directly. *Id.*

38. *See* notes 17-35 *supra* and accompanying text.

holders must allege that the directors were involved in a decision which affected the corporation and which resulted in some corporate injury or loss. Directors then may answer by pleading the business judgment rule as an affirmative defense.[39]

To successfully invoke the defense provided by the rule, a director must have exercised reasonable care in obtaining relevant and available facts before making his decision in a transaction.[40] He also must be acting in the good faith belief that the transaction is in the best interests of the corporation. Further, there must be no fraud, self-dealing, or other personal interest of the directors authorizing the transaction.[41] Once raised as a shield to the director's liability, the business judgment rule guides the court's inquiry into the conduct of the directors.[42]

B. *Burden of Proof for Business Judgment Rule*

Most courts place the burden of proof on the plaintiff-shareholders to show that the directors' decision does not warrant the protection of the business judgment rule defense.[43] Once the defense provided by the rule is affirmatively pleaded by the directors of the corporation, a presumption arises in their favor that the questioned decision was made with due care and based on the exercise of good business judgment.[44] The presumption is rebuttable, but the attacking party must present credible evidence to support a conclusion that care was not taken by directors in considering all relevant facts and business advice presented to them or that their decision has no reasonable or rational basis.[45] Such evidence may show that

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39. FED. R. CIV. P. 8(a), (c). *See also* Panter v. Marshall Field & Co., 486 F. Supp. at 1174.

40. The duty to obtain relevant and available facts is embodied in the directors' duty to exercise due care. *See* notes 27-30 *supra* and accompanying text. Reliance on advice of both legal and business investment counsel may be essential to gathering knowledge to make an informed careful decision. *Accord,* Spirt v. Bechtel, 232 F.2d 241, 247 (2d Cir. 1956). *See also* Voege v. Magnavox Co., 439 F. Supp. 935 (D. Del. 1977); Nanfito v. Tekseed Hybrid Co., 341 F. Supp. 240, 244 (D. Neb. 1972), *aff'd,* 473 F.2d 537 (8th Cir. 1973); Arsht, *Business Judgment, supra* note 6, at 111-12.

41. These requirements are embodied in the directors' fiduciary duties. *See* notes 31-35 *supra* and accompanying text. *See also* Guth v. Loft, 5 A.2d at 510; Arsht, *Business Judgment, supra* note 6, at 111.

42. Arsht, *Business Judgment, supra* note 6, at 114.

43. Treadway Cos. v. Care Corp., 638 F.2d 357, 381 (2d Cir. 1980); Crouse-Hinds Co. v. InterNorth, Inc., 634 F.2d 690, 702 (2d Cir. 1980); Johnson v. Trueblood, 629 F.2d 287, 292 (3d Cir. 1980); Warshaw v. Calhoun, 43 Del. Ch. 148, ___, 221 A.2d 487, 493 (1966).

44. *See* Treadway Cos. v. Care Corp., 638 F.2d 357, 381 (2d Cir. 1980); Crouse-Hinds Co. v. InterNorth, Inc., 634 F.2d 690, 702 (2d Cir. 1980); Johnson v. Trueblood, 629 F.2d 287, 292 (3d Cir. 1980); Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971).

45. *See, e.g.,* Marks v. Wolfson, 41 Del. Ch. 115, 188 A.2d 680 (1963). *Cf.* Kaplan v. Goldsamt, 380 A.2d 556 (Del. Ch. 1977) (presumption not disturbed if any rational business purpose can be attributed to decision); Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971) (decision not disturbed if attributable to a rational business purpose).

the directors did not act in light of their actual knowledge or the knowledge that they should have gained by reasonable care and skill.[46] Reliance on both business and legal advice is included in this requirement.[47] Negligently made decisions which breach this standard of care are not protected by the business judgment rule.[48]

Additionally, to overcome the business judgment defense the plaintiff-shareholders must show a lack of good faith through self-dealing or personal interest on the part of the directors.[49] A showing of personal interest in the decision effectively demonstrates to the court that the transaction based on the judgment of the directors was made not in the best interests of the corporation, but rather in the best interests of the directors.[50] Therefore, to remove the defense and rebut the presumption of a good faith exercise of sound business judgment,[51] the shareholders must present evidence of "fraud or gross overreaching,"[52] "bad faith or abuse of discretion,"[53] "profit at the expense of the corporation,"[54] or "improper motive . . . or a reckless indifference to or a deliberate disregard of the stockholders."[55]

Such criteria are generally vague and overbroad, and the courts often do not clearly articulate the measuring standards as to what constitutes fraud, bad faith, or self-dealing.[56] However, when the challenging stockholders satisfy the court that personal interests of the directors are involved and that such interests interfere with the exercise of sound business judgment, the presumption and deference to the business judgment of the directors are no longer present and the business judgment rule is vitiated.[57]

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46. H. HENN, *supra* note 1, at 455.

47. *Id.* at 458. *See also* N. LATTIN, *supra* note 14, at 247. *Accord,* Sprit v. Bechtel, 232 F.2d 241, 247 (2d Cir. 1956).

48. H. HENN, *supra* note 1, at 457.

49. *See* note 43 *supra. See also* Cheff v. Mathes, 41 Del. Ch. 494, __, 199 A.2d 548, 554 (1964).

50. *See generally* Arsht, *Business Judgment, supra* note 6, at 115-16.

51. The courts articulate a presumption of good faith and fair dealing in favor of the directors. *See, e.g.,* Warshaw v. Calhoun, 43 Del. Ch. 148, __, 221 A.2d 487, 493 (1966) (acts of directors presumed taken in good faith and inspired by best interests of corporation); Cheff v. Mathes, 41 Del. Ch. 494, __, 199 A.2d 548, 554 (1964) (decisions initially presumed to be in good faith). However, one commentator states that no presumption is raised regarding personal interests of directors. Arsht, *Business Judgment, supra* note 6, at 116.

52. Sinclair Oil Corp. v. Levien, 280 A.2d 717, 722 (Del. 1971); Getty Oil Co. v. Skelly Oil Co., 267 A.2d 883, 887 (Del. 1970), *rev'g* 255 A.2d 717 (Del. Ch. 1969); Meyerson v. El Paso Natural Gas Co., 246 A.2d 789, 794 (Del. Ch. 1967).

53. Warshaw v. Calhoun, 43 Del. Ch. 148, __, 221 A.2d 487, 493 (1966).

54. Maldonado v. Flynn, 413 A.2d 1251, 1256 (Del. Ch. 1980).

55. Allaun v. Consolidated Oil Co., 16 Del. Ch. 318, __, 147 A. 257, 261 (1929).

56. *See, e.g.,* Issner v. Aldrich, 254 F. Supp. 696 (D. Del. 1966); Chasin v. Gluck, 282 A.2d 188 (Del. Ch. 1971). *See generally* Arsht, *Fiduciary Responsibilities, supra* note 26, at 655.

57. *See* note 43 *supra* and accompanying text. When the presumption is rebutted, the

In summary, the business judgment rule is a defense traditionally used to protect corporate directors from personal liability where their decisions involve an honest mistake in business judgment which results in injury to the shareholders or to the corporation.[58] The initial burden of proof is on the challenger to rebut the presumption that the directors' decisions were made with due care, in good faith, and in the best interests of the corporation.[59] The court will not interfere with the business judgment of directors absent a showing of self-dealing, bad faith, fraud, or personal interest.[60]

II. Application of the Business Judgment Rule in *Panter v. Marshall Field & Co.*[61]

A. *Background of the Marshall Field Decision*

The *Marshall Field* case involved a challenge to the rejection by Field's board of directors of a take-over bid which would have profitted Field's shareholders. The suit was brought by twenty-one shareholders of Marshall Field & Company,[62] a Delaware corporation whose home office and principal place of business are in Chicago, Illinois. The defendants were ten directors of the Marshall Field Company. Seven of the defendant-directors were not affiliated with Field's management; the remaining three were corporate officers.

On several occasions in the late 1960's and early to mid-1970's, Field's management was approached by would-be merger or take-over "suitors."[63] All proposals were rejected by the board. In 1969, Marshall Field hired Joseph H. Flom,[64] an attorney with expertise in the area of corpo-

burden of proof shifts to the directors to show that the transaction is intrinsically fair to the shareholders and to the corporation. The directors' burden of proof is called the intrinsic fairness test. This test has been applied primarily to situations involving parent-subsidiary corporations, purchases where the price is inadequate, or corporations which have common directors. *See* notes 184-87 *infra* and accompanying text.

58. *See* note 8 *supra;* text accompanying notes 43-55 *supra.*

59. *See* note 43 *supra.*

60. *See* notes 31-35 *supra* and accompanying text.

61. 646 F.2d 271 (7th Cir. 1981), *aff'g* 486 F. Supp. 1168 (N.D. Ill. 1980).

62. Marshall Field & Company is a retail corporation which sells general merchandise, apparel, and furniture through its department stores. By the end of 1976, it was the eighth largest department store chain in the United States. It is a publicly held corporation with more than 16,000 shareholders who have purchased in excess of 9,000,000 shares of common stock. 486 F. Supp. at 1174.

63. Marshall Field was approached in 1969 by Associated Dry Goods; in 1975 by Federated Department Stores; in August, 1976, by Dayton-Hudson; and in September, 1976, by Gamble-Skogmo. All of these proposals were evaluated by Field's directors and turned down. 646 F.2d at 278.

64. Flom was hired from the New York law firm of Skadden, Arps, Slak, Meagher & Flom. He is reputed to be the country's most famous take-over lawyer. Feinberg, *The Directors' New Dilemma, The Takeover Crisis: A Special Report*, 13 Instit. Inv. 33, 45 (June

rate mergers, to advise the company in determining how best to respond to the overtures of interested parties.

In 1977, Carter Hawley Hale (CHH)[65] made several informal contacts with Marshall Field expressing an interest in a merger. The board resolved not to consider the merger, but CHH continued to press its attentions. Field's legal counsel[66] began to investigate the antitrust aspects of such a merger and advised the company's board of directors that the proposed combination would be illegal.[67]

On December 10, 1977, the president of CHH called the president of Marshall Field to inform him that unless the company agreed to negotiate a merger by Monday, December 12, CHH would submit a public exchange proposal[68] to the Securities Exchange Commission (SEC) which would make Field's stock worth approximately $36.00 per share. Field's stock was trading at roughly $22.00 per share at the time. The call was construed as an unfriendly take-over attempt.[69]

As a result, a special meeting of Field's board of directors was called at which the directors adopted several defensive tactics. Pursuant to the advice of legal counsel, the board authorized the filing of an antitrust suit against CHH. Based on the advice of Field's investment bankers that fu-

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1979). Flom advised Field's directors how best to fend off "raiders" and was allegedly part of their secret policy of independence. *See* notes 110-15 *infra* and accompanying text.

65. Carter Hawley Hale operates retail department, specialty, and book stores. CHH's Neiman-Marcus division operates retail stores in Texas and the southeastern United States.

66. Field's board of directors had been advised since 1971 by antitrust counsel from Kirkland & Ellis, a Chicago law firm. 646 F.2d at 279.

67. The Clayton Act prohibits acquisitions by a corporation of the stock or assets of another corporation tending substantially to lessen competition in any line of commerce. Clayton Act of 1914, § 7, 15 U.S.C. § 18 (1976) (original version at ch. 323, § 7, 38 Stat. 713 (1914)). A merger between Marshall Field and CHH would tend to lessen competition in the retail department store business. The two companies had stores located near each other and carried on essentially the same business. *See* notes 62, 65 *supra*.

68. In an exchange proposal, the offeror proposes to issue either its common or preferred stock in exchange for stock of the target corporation and to publish the offer pursuant to the publicity, registration and filing requirements of the Securities Act of 1933. E. ARANOW & H. EINHORN, *supra* note 2, at 29.

69. The district court defined an unfriendly take-over as follows:

> [A takeover] is unfriendly when the target company is the object of acquisition by a raider who, complying with state and federal securities laws, makes the required disclosures and proposes an exchange or tender offer for the number of outstanding common shares of the company that will result in control of the target. A takeover, when unfriendly, has a disruptive effect on the management of a target company and its board of directors. It may be welcomed by some, but not all of the target company's shareholders. A takeover can be expensive; it often raises questions of possible violations of the antitrust laws; and it presents problems under the securities statutes and the rules and regulations adopted thereunder. Consequently, a company vulnerable to a takeover must have guidance from lawyers, investment bankers, accountants, and business consultants.

486 F. Supp. at 1175.

ture performance of the company would be favorable, the board determined that the company's stock could bring more than $36.00 a share in a sale or merger of the company.[70] The directors therefore voted unanimously to reject the CHH merger proposal because, in their judgment, the merger would be "illegal, inadequate, and not in the best interests of the corporation, the stockholders, and the community which it serves."[71]

Marshall Field subsequently issued a press release conveying its decision and outlining growth plans. Stock traded that day in a range of $28.00 to $32.00. On December 20, 1977, Field's president addressed a letter to Field's stockholders in which he expressed optimism about the company's future. In the regular January board meeting, the directors of Marshall Field resolved to pursue two expansion programs, one in Houston, Texas, where CHH also had a store, and one in the Pacific Northwest involving five stores. On February 1, 1978, CHH announced its intentions to make an exchange offer of $42.00. Appropriate documents were filed with the SEC for a tender offer.[72] Field's board met subsequently and, once again, affirmed its opposition to merger. The market price of Field's stock rose to $34.00 and fluctuated between $30.00 and $34.00 during this period. On February 8, 1978, Marshall Field announced the acquisition of the Houston store which complicated the antitrust problems of CHH's merger proposal because CHH already had a store in the same shopping mall.[73] On February 22, CHH announced withdrawal of its proposed tender offer before it became effective.[74] Following this announcement, the market price of Field's shares dropped to $19.00.

The shareholder-plaintiffs subsequently filed suit in Federal District Court for the Northern District of Illinois[75] seeking to enjoin Field's directors from engaging in their "policy of independence"[76] and requesting

70. The CHH merger team had noted to one of Field's directors and to Field's president that a foreign firm was likely to make a $60.00 tender offer for Field's stock "at any time." 646 F.2d at 279.

71. *Id.* at 280.

72. A person, corporation, or group of persons making a tender offer, which could result in the offeror owning more than five per cent of certain securities, is required to file a basic disclosure statement under Schedule 13D, promulgated pursuant to the rulemaking authority granted the SEC under Section 13(d)(1) of the Williams Act. 17 C.F.R. § 240.13d-101 (1968). *See also* E. ARANOW & H. EINHORN, *supra* note 2, at 77.

73. The Houston store was located in Galleria, a Houston shopping mall which already contained a CHH owned Neiman-Marcus store. 646 F.2d at 280.

74. Tender offers which are proposed may be withdrawn at any time by the offeror before they become effective. The date and time of effectiveness of the tender offer should be clearly stated in the invitation by the offeror. E. ARANOW & H. EINHORN, *supra* note 2, at 46-52.

75. 486 F. Supp. 1168 (N.D. Ill. 1980).

76. This policy was alleged to have been kept secret by Field's directors in order for them to retain their control of the corporation and reject all merger or take-over attempts. *Id.* at 1173.

damages incurred during the period from December 12, 1977, to February 11, 1978. The shareholders alleged that Field's directors had breached their fiduciary duty and had intentionally interfered with prospective economic advantage.[77] The district court empaneled a jury to try the case.[78] At the end of the plaintiffs' evidence, the court granted the defendants' motion for a directed verdict[79] concluding that "plaintiffs' evidence, considered together with all reasonable inferences favorable to them, totally fails to prove necessary elements of their claims."[80] The plaintiffs appealed the verdict to the Seventh Circuit Court of Appeals.[81]

B. *The Circuit Court's Decision and Rationale*

On appeal, the plaintiffs sought to establish two violations of state law. First, they contended that the defendant-directors breached their fiduciary duty to the corporation and its shareholders (1) by adopting a secret policy to resist acquisitions, regardless of benefit to the shareholders or the corporation; (2) by failing to disclose the existence of such a policy;

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77. Additional claims were brought under the Williams Act, ch. 404, § 10, 48 Stat. 891 (1934) (current version at 15 U.S.C. § 78j(b) (1976) and the SEC rules. Plaintiffs alleged violations of Section 10(b) of the Securities and Exchange Act of 1934, 15 U.S.C. § 78j(b) (1976) and Rule 10b-5, 17 C.F.R. § 240.10b-5 (1980) promulgated under this Act by the Securities Exchange Commission. The court dismissed these claims for the following reasons:

(a) Upon the announcement of a tender offer proposal a target company shareholder may retain his shares, tender them if the offer becomes effective, or dispose of them on the market. Because the CHH tender offer was withdrawn before it became effective, the plaintiffs had no opportunity to decide whether to tender. Therefore, it was impossible for them to have relied on any statement. The element of reliance is vital to a Williams Act § 14(e) claim. 646 F.2d at 283-84 (citing Lewis v. McGraw, 619 F.2d 192, 195 (2d Cir.), *cert. denied,* 101 S. Ct. 354 (1980).

(b) SEC Rule 10b-5 requires proof of manipulation or deception on the part of the defendants. The plaintiffs' allegations and evidence concerning the policy of independence, the press releases and letters by Field's, the filing of an antitrust suit, the defensive acquisitions, and the misleading projections were not sufficient for a finding of manipulation or deception. 646 F.2d at 287-93.

To hear the state claims, the court exercised its pendent jurisdiction. *See* United Mine Workers of America v. Gibbs, 383 U.S. 715, 725-26 (1966) (If state and federal claims are derived from a common nucleus of fact and are such as would ordinarily all be tried in one judicial proceeding, the federal court, in its discretion, will hear the whole.).

78. FED. R. CIV. P. 38(a). *See* Beacon Theaters, Inc. v. Westover, 359 U.S. 500 (1959); Dairy Queen, Inc. v. Wood, 369 U.S. 469 (1962).

79. FED. R. CIV. P. 50(a).

80. 486 F. Supp. at 1195. The court explained that "the facts established by the proof . . . pointed so strongly and overwhelmingly in favor of the defendants" that no reasonable jury could arrive at a contrary verdict. *Id.* The decisions were made in the exercise of business judgment. *Id.* at 1193.

81. The Seventh Circuit also dismissed the plaintiffs' federal securities law claims. The court noted that the Securities Exchange Act of 1934 does not provide a remedy for the breach of fiduciary duty owed by a director to his corporation and its shareholders under state law. 646 F.2d at 287 (citing Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977)).

(3) by making defensive acquisitions;[82] and (4) by filing an antitrust suit against CHH.[83] Second, the plaintiff-shareholders alleged that the defendants interfered with their prospective economic advantage in that the directors' purported wrongful behavior caused CHH to withdraw its proposed tender offer before it became effective.[84]

The focal point of the court's decision is the business judgment rule. Because Marshall Field & Company is a Delaware corporation, Delaware law was applied.[85] Thus the appropriate starting point for analysis was the articulation of the business judgment rule under Delaware law.[86]

The first issue addressed by the court was whether to apply the business judgment rule where a breach of fiduciary duty is alleged. This fiduciary duty is discharged by directors "when in good faith they exercise business judgment in making decisions regarding the corporation."[87] Good faith and fair dealing are essential to the fiduciary duty concept.[88] "When [directors] act in good faith, they enjoy a presumption of sound business judgment, reposed in them as directors, which courts will not disturb if any rational business purpose can be attributed to their decisions."[89] To rebut this presumption, the plaintiffs had to establish a prima facie case of lack of good faith by showing fraud, self-dealing, or abuse of discretion.[90] Field's shareholders contended that the secret policy to resist takeovers, the failure to disclose such a policy, the defensive

82. The defensive acquisitions referred to were the stores which Field's board of directors voted to acquire in pursuance of its expansion program. This included five stores in the Pacific Northwest and one store in Houston, Texas. 646 F.2d at 280.

83. *Id.* at 293.

84. This violation of state law is based on a tort theory. *Id. See* W. PROSSER, THE LAW OF TORTS § 130 (4th ed. 1971).

85. The federal courts apply state law for substantive state law claims. Therefore, the court applied Illinois law concerning the conflict of law, which requires that the law of the state of incorporation be applied where the issues concern internal corporate affairs, duties and liabilities. Field's is incorporated in Delaware. RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 303-04 (1971); R. LEFLAR, AMERICAN CONFLICTS OF LAW §§ 251, 254 (3d ed. 1977). *See, e.g.*, Abbey v. Control Data Corp., 603 F.2d 724, 728 (8th Cir. 1979), *cert. denied*, 444 U.S. 1017 (1980); Zahn v. Transamerica Corp., 162 F.2d 36 (3d Cir. 1947).

86. The court of appeals adopted the district court's articulation of the business judgment rule under Delaware law:

> Directors of corporations discharge their fiduciary duties when in good faith they exercise business judgment in making decisions regarding the corporation. When they act in good faith, they enjoy a presumption of sound business judgment, reposed in them as directors, which courts will not disturb if any rational business purpose can be attributed to their decisions. In the absence of fraud, bad faith, gross overreaching or abuse of discretion, courts will not interfere with the exercise of business judgment by corporate directors.

486 F. Supp. at 1194 (citations omitted).

87. 646 F.2d at 293.

88. *See* notes 31-35 *supra* and accompanying text.

89. 646 F.2d at 293.

90. *Id. See also* notes 49-57 *supra* and accompanying text.

acquisitions, and the antitrust suit were evidence of a desire on the part of the directors to retain control of the corporation.[91] Thus, the plaintiff-shareholders reasoned that a motive to retain control demonstrated bad faith by directors and rebutted the presumption that their actions were taken in the exercise of sound business judgment.[92] Therefore, the plaintiffs argued that the burden of proof should have been placed on the defendant-directors to show the compelling business purpose of the transactions.[93]

In rejecting the argument of the shareholders, the court turned to *Johnson v. Trueblood*,[94] a recent Third Circuit case involving allegations of a purpose to retain control of a corporation. The Third Circuit held that the showing of *a* motive to retain control was not enough to shift the burden of proof to the directors and that the plaintiff at least must show that the retention of control was the defendant's *sole* or *primary* motive in order to rebut the presumption of a rational business purpose.[95] In *Johnson*[96] the court explained that directors are not ordinary fiduciaries[97] because "by the very nature of corporate life a director has a certain amount of self-interest in everything he does."[98] The court reasoned that the business judgment rule alleviates this problem by protecting the director in situations that would involve a conflict of interest for the ordinary fiduciary.[99] The plaintiff bears the burden of showing that "impermissible motives predominated;"[100] if the plaintiff fails to meet that

91. If this were proven, the shareholders would have shown self-dealing by the directors and the burden would have shifted to them to show the intrinsic fairness of the transaction. *See* note 57 *supra.*

92. 646 F.2d at 294.

93. *Id.* at 295.

94. 629 F.2d 287 (3d Cir. 1980).

95. *Id.* at 293. The requirement of "sole or primary" motive was first articulated in Cheff v. Mathes, 41 Del. Ch. 494, ___, 119 A.2d 548, 554 (1964). The Third Circuit also relied on Bennett v. Propp, 41 Del. Ch. 14, 187 A.2d 405 (1962) (directors' actions improper because done for no reason other than to maintain control) and Petty v. Penntech Papers, Inc., 347 A.2d 140, 143 (Del. Ch. 1975) (use of corporate funds to redeem shares improper because done primarily to maintain management's control).

96. The Seventh Circuit stressed this opinion presumably because Delaware is in the Third Circuit, which may be more attuned to Delaware corporate law. The court also noted that Judge Seitz who wrote the *Johnson* opinion was formerly a Delaware Chancellor. 646 F.2d at 293-94.

97. "[A]n ordinary fiduciary may not have the slightest conflict of interest in any transaction he undertakes on behalf of the trust." 629 F.2d at 292. *See also* Godbold v. Branch Bank, 11 Ala. 191, 199 (1847) (if held to extreme standards, "no man of ordinary prudence would accept a trust. . . .").

98. 629 F.2d at 292.

99. *Id.* "[I]f actions are arguably taken for the benefit of the corporation, then the directors are presumed to have been exercising sound business judgment rather than responding to any personal motivations." *Id. See* notes 49-57 *supra* and accompanying text. *See also* note 97 *supra.*

100. 629 F.2d at 292.

burden, the court will presume the defendant-directors exercised their business judgment in good faith.[101] To allow merely the presence of a motive to retain control by corporate directors to shift the burden of proof is contrary to the purpose of the rule, since, as the Third Circuit noted, control is always arguably a motive in any corporate action. Thus, to allow plaintiffs to use this theory would always undercut the business judgment rule.[102] The *Marshall Field* court adopted this rationale and bolstered it by stating that the presumption of the exercise of business judgment in good faith is further heightened where "the majority of the board consists of independent outside directors."[103]

The court also relied on the Second Circuit's decisions in *Treadway Cos. v. Care Corp.*[104] and *Crouse-Hinds Co. v. InterNorth, Inc.*,[105] both cases involving control motivation on the part of defendant-directors in take-over attempts. An allegation of control motivation not supported by proof was found insufficient to shift the burden to the defendants.[106] The Second Circuit stated in both cases that it is necessary for the plaintiff to initially prove the control motivation in order to demonstrate the self-interest of the defendant-directors before the burden of proof shifts to the directors.[107] Following the holdings and rationale of these cases and proceeding under the business judgment rule, the Seventh Circuit in *Marshall Field* refused to apply the plaintiff-shareholders' proposal that "the burden be placed upon the directors to establish the compelling business purpose of any transaction which would have the effect of consolidating or retaining the directors' control."[108]

After deciding that the business judgment rule does apply to allegations of a breach of fiduciary duties, the court turned to the four specific claims of breach to review the sufficiency of the shareholders' evidence of bad faith or self-dealing necessary to vitiate the business judgment defense.[109] First, plaintiffs contended that they presented sufficient evidence as to the existence of a secret policy of Field's directors to remain independent for a jury to decide whether this policy demonstrated the self-dealing or personal interest which breaches the directors' fiduciary duties. The shareholders relied on the directors' history of resistance to prior ap-

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101. *Id.* at 292-93.
102. *Id.*
103. 646 F.2d at 294.
104. 638 F.2d 357 (2d Cir. 1980).
105. 634 F.2d 690 (2d Cir. 1980).
106. 638 F.2d at 382; 634 F.2d at 702.
107. 638 F.2d at 382; 634 F.2d at 702.
108. The court called this proposal alternately a "different test," a "novel rule," and a "novel theory of directors' liability." In declining to shift the burden of proof to the directors, the court stated that it was using the "well-established test" of the business judgment rule. 646 F.2d at 295.
109. *See* notes 82, 90 *supra* and accompanying text.

proaches.[110] The court stated that the evaluation and response to such approaches was "within the scope of the directors' duties."[111] The evidence indicated that the directors carefully considered each merger proposal.[112] The desire to build value within the company and the belief that a take-over might diminish the company's value were viewed by the Seventh Circuit as rational business purposes.[113] The shareholders had "failed to introduce evidence supporting a reasonable inference that any of the rejections of these approaches were made in bad faith."[114] The court also found it unreasonable to infer the existence of a policy of independence.[115] Therefore, the court did not disturb the business judgment of the directors and a directed verdict was properly granted.[116]

Second, plaintiffs contended that failure to reveal the policy of independence "amounted to a breach of fiduciary duty."[117] Citing *Berman v. Gerber Products Co.*,[118] the court stated that the directors were under no duty to reveal every approach made to Marshall Field.[119] Since there is no duty to disclose prior take-over approaches, there can be liability for a failure to disclose a policy of resistance, especially where no such policy can be reasonably inferred to exist.[120] Noting the defensive acquisitions of the stores in the Pacific Northwest and of the store in Houston, the court chided the shareholders for trying to impose liability through "Monday-morning-quarterbacking."[121].

In their third specific claim for breach of fiduciary duty, the sharehold-

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110. *See* note 63 *supra* and accompanying text.

111. 646 F.2d at 296.

112. The district court found that each time an approach was made by a company to acquire Field's, the contacts with the approaching company were made part of Field's records by signed or initialed memoranda, and the directors' actions were recorded in board minutes documenting resolutions taken. The directors "reached their decision [in each case] only after consultation with management, lawyers, accountants, and investment bankers." 486 F. Supp. at 1193.

113. 646 F.2d at 296.

114. *Id.*

115. *Id.* at 297.

116. *Id.* at 296.

117. The court refused to allow the shareholders to delve into the minds of the directors in situations where none of the prior attempts at take-over ever became definite offers or merger proposals. Since the directors exercised due care in their decisions, the court applied the business judgment rule. *Id.* at 296-97. *Cf.* Goldberger v. Baker, 442 F. Supp. 659, 664 (S.D.N.Y. 1977) (actionable deception must allege more than mere failure to disclose unfairness of transaction).

118. 454 F. Supp. 1310, 1318 (W.D. Mich. 1978).

119. 646 F.2d at 296 (citing also Missouri Portland Cement Co. v. H. K. Porter Co., 535 F.2d 388, 398 (8th Cir. 1976)).

120. 646 F.2d at 297. *Accord,* Vaughn v. Teledyne, 628 F.2d 1214, 1221 (9th Cir. 1980).

121. The court points out that hindsight is always perfect vision, and that two of the stores are now unprofitable matters not if the directors exercised sound business judgment in good faith when they decided to acquire the stores. 646 F.2d at 297.

ers contended that two of the stores acquired were not profitable,[122] that the transactions to acquire them were unfavorable to the stockholders, and that the motive in acquiring the stores was to make the company less attractive as a take-over target and to exacerbate antitrust problems.[123] If supported by evidence and proven, these claims would demonstrate that the directors did not act in the best interests of the corporation, thereby breaching their fiduciary duty. The court found, however, that the evidence was uncontroverted that Field's expansion programs were reasonable, natural, and not designed to make the company less attractive as an acquisition.[124] The business judgment rule protects directors from attack when they make a transaction in good faith which proves later to be unprofitable.[125] The court went on to say that even if the desire to fend off CHH were among the motives of the board of directors in acquiring the stores, the plaintiffs failed to establish it as the sole or primary purpose, as required by *Cheff v. Mathes*,[126] in order to show self-dealing or personal interest sufficient to overcome the business judgment rule.[127]

The fourth specific claim of breach of fiduciary duty concerned the filing of the antitrust suit against CHH by Field's directors. The plaintiffs alleged that the suit was motivated by the policy to resist take-overs and remain independent, and, therefore, was in the interest of the directors and not of the corporation.[128] Citing *Gulf & Western Industries, Inc. v. Great A & P Tea Co.*,[129] the court stated that it is the duty of the directors to file an antitrust suit when in their business judgment a proposed combination would be illegal or otherwise detrimental to the corporation.[130] Bringing the suit served the rational business purpose of protect-

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122. The plaintiff-shareholders complained that, even as of January 20, 1978, the directors considered two of the five stores in the Pacific Northwest to be "dogs" or unprofitable ventures. *Id.* at 291.

123. *Id.* at 297.

124. *Id.* Field's executives and directors had long considered expansion in the Pacific Northwest and in Texas. This interest was well known to investment analysts in the department store field. *Id.* at 280.

125. *See* notes 8-13 *supra* and accompanying text.

126. 41 Del. Ch. 494, 199 A.2d 548 (1964). *Cheff* was the first case to articulate the "sole or primary motive" test. *See also* Kaplan v. Goldsamt, 380 A.2d 556 (Del. Ch. 1977); Baron v. Allied Artists Pictures Corp. 337 A.2d 653 (Del. Ch. 1975); Bennett v. Propp, 41 Del. Ch. 14, 187 A.2d 405 (1962); Kors v. Carey, 39 Del. Ch. 47, 158 A.2d 136 (1960).

127. *See* notes 31-35 and 51-57 *supra* and accompanying text. According to one commentator, one of the most prevalent forms of bad faith is an improper attempt by directors to keep themselves in office. The business judgment rule will not shield directors shown to have made a transaction solely or primarily to retain their control, even if the action were in the best interests of the company at the time. However, if control is merely incidental to the transaction, the directors are protected by using their business judgment. Arsht, *Business Judgment*, *supra* note 6, at 127-28.

128. 486 F. Supp. at 1192.

129. 476 F.2d 687 (2d Cir. 1973).

130. 646 F.2d at 297.

ing Marshall Field from the damage that forced divestiture[131] would cause.[132] The decision to file an antitrust suit is within the scope of the business judgment rule, and there was substantial evidence that the defendant-directors were fairly and reasonably exercising their business judgment in filing suit. The directors relied on the advice of experienced and knowledgeable antitrust counsel in initiating the suit.[133] In addition, one member of the board was an experienced antitrust lawyer who could evaluate the soundness of the advice and the action taken.[134] With no evidence that the suit was brought in bad faith, the defendant-directors' desire to perpetuate control was not sufficient to set aside the business judgment defense.[135]

As to all of the plaintiff-stockholders' claims for breach of fiduciary duty, the court concluded that there was insufficient evidence on which a jury could base a rational verdict that the defendant-directors breached any duty. Thus, in applying the business judgment rule, the court affirmed the district court's decision.[136]

The plaintiff-shareholders' second claim of violation of state law involved intentional interference with their prospective economic advantage. Based on contractual relationships,[137] this claim seeks damages for wrongful conduct which results in injury to economic benefits expected by

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131. The Clayton Act of 1914 gives federal district courts the power to impose civil remedies for violations. 15 U.S.C. § 9 (1976) (original version at ch. 349, § 74, 28 Stat. 570 (1894)); 15 U.S.C. § 18 (1976) (original version at ch. 323, § 738, 38 Stat. 731 (1914)); 15 U.S.C. § 21 (1976) (original version at ch. 323, § 11, 38 Stat. 734 (1914)). The courts may order the corporation to divest itself of property, securities or other investments as a remedy for violations. United States v. E. I. Du Pont de Nemours & Co., 366 U.S. 316 (1961). This may be accomplished by separating the going business into two independent enterprises or by means of a spin-off. *See* E. ROCKEFELLER, ANTITRUST QUESTIONS AND ANSWERS 240-54 (1974). *See also* R. POSNER, ANTITRUST LAW 78-95 (1976).

132. 646 F.2d at 297.

133. *Id.* at 279. *Accord,* Spirt v. Bechtel, 232 F.2d 241, 247 (2d Cir. 1956). Reliance on advice is an element in the duty of due care when exercising business judgment. *See* notes 45-48 *supra* and accompanying text. Field's antitrust counsel began its investigation on November 16, 1977. On December 2, 1977, they advised Field's management that in their opinion the proposed combination would be illegal in light of (1) competition between Field's and Neiman-Marcus' stores already in the Chicago area, (2) potential competition between Field's Chicago stores and proposed Neiman-Marcus stores, and (3) existing competition between Field's stores which were second in book sales in Chicago and CHH's Walden division book stores. 646 F.2d at 279.

134. 646 F.2d at 297.

135. *Id.* at 298. The decision of the directors to resolve the antitrust question through litigation in federal court rather than to utilize some other method was within their discretion. *Id.* at 297-98. *See also* Gulf & Western Indus., Inc. v. Great A & P Tea Co., 476 F.2d 687, 698 (2d Cir. 1973); Puma v. Marriott, 283 A.2d 693, 696 (Del. Ch. 1971); Kors v. Carey, 39 Del. Ch. 47, ___, 158 A.2d 136, 140 (1960).

136. 646 F.2d at 298.

137. *See* note 36 *supra.*

the plaintiff in the future.[138] To sustain such a charge, Illinois law[139] requires proof that the defendants acted with the purpose of injuring the plaintiff's expectancies in future profits or economic benefit.[140] This means that the directors' acts must involve some fraud, overreaching, or malicious conduct intentionally interfering with the plaintiffs' business affairs.[141]

The evidence in *Marshall Field* showed that the directors were acting on good faith motives with the well-being of the corporation in mind,[142] and not acting to intentionally decrease the price of stock in order to deprive the shareholders of profits. Absent sufficient evidence of improper motives on the part of the directors to overcome the business judgment defense in an action for breach of fiduciary duty, "a case cannot proceed to the jury on an interference with prospective economic opportunity theory."[143] As to both claims, the plaintiff-shareholders needed to show improper motives such as fraud, self-dealing, or bad faith on the part of the directors.

C. *The Dissent*

Judge Cudahy, concurring in part[144] and dissenting in part, felt that there was "abundant evidence in this casè to go to the jury on the state claims for breach of fiduciary duty."[145] He "emphatically disagree[d] that the business judgment rule should clothe directors . . . with an almost irrebuttable presumption of sound business judgment, prevailing over everything but the elusive hobgoblins of fraud, bad faith or abuse of discretion."[146] The majority, he maintained, had adopted an approach which would immunize a target company's board of directors if they were able to assemble a sufficiently prestigious contingent of financial and legal ad-

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138. W. PROSSER, *supra* note 84, § 130 at 950-53.

139. Delaware courts hold that the law of the place of the tort governs in actions such as this. 646 F.2d at 298 n.10 (citing Bowl-Mor Co. v. Brunswick Corp., 297 A.2d 61, 64 n.2 (Del. Ch. 1972)). The court in *Marshall Field* then looked to Illinois law and commented that both Illinois and Delaware had the same substantive law for this tort action. 646 F.2d at 298 n.10.

140. 646 F.2d at 298. *See* Herman v. Prudence Mut. Cas. Co., 41 Ill. 2d 468, ___, 244 N.E.2d 809, 812 (1969); Crinkley v. Dow Jones & Co., 67 Ill. App. 3d 869, ___, 385 N.E.2d 714, 722 (1978); Parkway Bank & Trust Co. v. City of Darien, 43 Ill. App. 3d 400, ___, 357 N.E.2d 211, 215 (1976).

141. 646 F.2d at 298 (citing City of Rock Falls v. Chicago Title & Trust Co., 13 Ill. App. 3d 359, ___, 300 N.E.2d 331, 333 (1973)).

142. 646 F.2d at 298.

143. *Id.* at 299.

144. Although he dissented on the state claims for breach of fiduciary duty, Circuit Judge Cudahy agreed with the majority's opinion concerning the Securities Act misrepresentation claims. *Id.*

145. *Id.*

146. *Id.*

visors who would later provide rational business reasons for their decisions.[147]

The dissent distinguished the task of managing the business affairs of a corporation from the collection and distribution of corporate profits and losses[148] and took the view that courts should intervene in situations where these profits and losses and their collection and distribution involve the corporation-shareholder relationship.[149] The dissent focused on the potential for abuse and the threat of the self-protective viewpoint of interested directors to stockholder welfare where profits are concerned.[150] Such self-protective, interested directors could manipulate their business decisions to their own benefit at the expense of the shareholders' interests. For example, they could channel expert advice to their own advantage and to the disadvantage of the corporation and the stockholders.[151] "Directors . . . are, at the very least, 'interested' in their own positions of power, prestige and prominence."[152] They are "interested" in keeping their positions and in protecting their management from outside attack.[153] Because of the directors' interests and special position, the dissent was disturbed by the "slavish application" of the majority's version of the good faith presumption under the business judgment defense.[154]

The dissent cited *Treadway Cos. v. Care Corp.*[155] to underscore the precept that once a plaintiff demonstrates a director's interest in the transaction is at issue, the burden shifts to the defendant-directors to prove the transaction was reasonable and fair to the corporation.[156] In *Treadway*, the directors authorized the issuance and sale of a large block of stock which had the effect of preserving their control.[157]

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147. *Id.* For a discussion of this aspect of the directors' decision, see Feinberg, *supra* note 64, at 53-56.

148. 646 F.2d at 299-300.

149. *Id.* at 300. *See* Note, *Protection for Shareholder Interests in Recapitalizations of Publicly Held Companies*, 58 COLUM. L. REV. 1030, 1066 (1958).

150. 646 F.2d at 300.

151. *See* Gelfond & Sebastian, *Reevaluating the Duties of Target Management in the Hostile Tender Offer*, 60 B.U. L. REV. 403, 435-37 (1980); Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981).

152. 646 F.2d at 300.

153. *Id.* at 301. Judge Cudahy put little stock in the fact that a majority of Field's directors were non-management (independent). He noted that the interaction between management and boards of directors is very strong. The directors may be interested in preserving the control of "their" management and thus their own control. 646 F.2d at 300-01. *See generally* Gelfond & Sebastian, *supra* note 151, at 436.

154. 646 F.2d at 301.

155. 638 F.2d 357 (2d Cir. 1980).

156. *Id.* at 382.

157. Judge Cudahy stated:

> The issuance and sale of this stock diluted shareholders' votes, which is not at issue in the case at bar. The Second Circuit found that the Treadway directors were not

According to the dissent, the burden of proof must be shifted to the directors when this interest in control is shown.[158] Examining other cases relied on by the majority, the dissent rejected the Second Circuit's judgment in *Crouse-Hinds Co. v. InterNorth, Inc.*[159] as "inconsistent with apposite case law, corporate reality and sound public policy" to the extent that the language used by the Second Circuit may prevent a shift in the burden of proof.[160] *Crouse-Hinds* placed the initial burden of proving the directors' interest or bad faith on the plaintiff before a shift in the burden of proof could occur. In this case, the target company in a counter-claim was seeking to enjoin the raider company from completing the take-over on the grounds that the Crouse-Hinds exchange offer was designed solely to retain control for their management and had no other rational business purpose.[161] However, *Crouse-Hinds* involved a take-over attempt immediately following a merger.[162] The dissent also criticized the majority's reliance on *Johnson v. Trueblood,*[163] noting that it dealt with how the jury was to be instructed and not, as in the case at bar, with whether the evidence should go to the jury at all.[164] According to the dissent, the proper interpretation of the business judgment rule in these cases was that expressed by the dissent in *Trueblood.*[165] The *Trueblood* dissent felt that the showing of control as *a* motive on the directors' part was sufficient to shift the burden of proof to them to vindicate the transaction.[166]

The dissent then evaluated in detail the evidence presented by Field's shareholders and rejected the majority's affirmation of the directed verdict.[167] In conclusion, the dissent stated that the majority opinion does a disservice to stockholders and undermines confidence in the system of corporate governance, because it gives directors free rein to act to the disadvantage of shareholders and it "announces to stockholders (if they did not know it before) that they are on their own and may expect little consideration and less enlightenment from their board of directors when a tender offeror appears to challenge the directors for control."[168]

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acting primarily to retain control, or for their own interests, but rather in the best interests of the corporation.

Id. at 381.

158. *See* note 57 *supra.*
159. 634 F.2d 690 (2d Cir. 1980).
160. 646 F.2d at 301 n.6.
161. 634 F.2d at 701.
162. *Id.* at 690.
163. 629 F.2d 287 (3d Cir. 1980).
164. 646 F.2d at 304.
165. *Id.*
166. 629 F.2d at 299.
167. 646 F.2d at 305-10.
168. *Id.* at 312.

III. Analysis of the Court's Opinion and Its Ramifications in Corporate Law

The problem with the majority opinion in *Marshall Field* is the confusion caused by terms and concepts which are unclear in meaning and are used interchangeably. The business judgment rule defense has two aspects. First, the rule protects directors' decisions from judicial scrutiny when such decisions made in the exercise of business judgment are based on due care. The duty of due care refers to the consideration given by directors to all relevant facts and to their awareness of all possibilities. Decisions authorizing a transaction must be informed decisions. Upholding this standard of care gives the directors' decision and subsequent actions a rational basis. Breaching it shows a negligent exercise of business judgment not protected by the business judgment defense.[169]

Second, the rule protects directors' decisions from judicial scrutiny when such decisions made in the exercise of business judgment are based on good faith, a lack of personal interest or self-dealing, and with the best interests of the corporation in mind.[170] This is what the majority denominates as fiduciary duty.[171] Upholding this duty demonstrates a rational business purpose or motive. Breaching it indicates bad faith in exercising business judgment which the business judgment defense declines to protect.

The majority in *Marshall Field* does not make a clear delineation between these two duties of corporate directors.[172] The court reviews the due care taken by Field's directors as well as the discharge of their fiduciary duty, but the two aspects are blended together throughout the opinion. It is true that the attacking party may prove a breach of either of the two duties to defeat the business judgment defense and thus shift the burden of proof to the defendants.[173] However, courts should recognize the two distinct duties and clearly outline which duty it is addressing in its review of actions taken in the exercise of business judgment.

One commentator suggests that confusion also results when the courts use terms whose meanings are unclear in stating what the challenging party must show to overcome the business judgment rule's defense.[174] Terms such as "gross and palpable overreaching"[175] are too vague to be of

169. *See* notes 30, 45-48 *supra* and accompanying text.
170. *See* notes 31-35, 49-57 *supra* and accompanying text.
171. 646 F.2d at 293.
172. *See generally* 646 F.2d at 293-99.
173. *See generally* notes 43-57 *supra* and accompanying text.
174. Arsht, *Business Judgment*, *supra* note 6, at 101.
175. This term was taken from the dissenting opinion in Case v. New York Cent. R.R., 19 A.D.2d 383, 390, 243 N.Y.S.2d 620, 627 (1st Dept. 1963) (Steuer, J., dissenting), *rev'd*, 15 N.Y.2d 150, 204 N.E.2d 643, 256 N.Y.S.2d 607 (1965). It was used continuously in subsequent Delaware cases. Sinclair Oil Corp. v. Levien, 280 A.2d 717, 722 (Del. 1971); Getty Oil

aid to either challenging shareholders or reviewing courts. The *Marshall Field* court initially uses the terms "self-dealing, fraud, and overreaching"[176] which, as the dissent points out, are "elusive hobgoblins"[177] which are difficult to define. However, later in the opinion, the majority refers to "improper motives"[178] and "bad faith,"[179] which are perhaps more easily defined and applied to factual situations. It is commendable that the *Marshall Field* court did not resort to obtuse terms such as "gross and palpable overreaching;" however, confusion still is present in the terms it used to define what the attacking shareholders had to prove to overcome the business judgment defense. Perhaps this confusion detracts from a sound, well-reasoned opinion and adds to the quagmire[180] and controversy surrounding the application of the business judgment rule.

The dissent in *Marshall Field* reveals an awareness of the possibility of abuse of the business judgment rule and resulting damage to shareholders. Its intense scrutiny of the facts suggests an awareness of corporate realities which underlies the belief that factual decisions concerning motives and good faith, which are elements of the directors' fiduciary duties, could be best determined by a jury.[181] In the dissent's view, the evidence in the *Marshall Field* case was sufficient to overcome the presumption of good business judgment and should have been placed in the jury's hands.[182]

If the jury had been allowed to rule on the issues presented in *Marshall Field,* and if they had returned a verdict for Field's shareholders against the directors, there would have been great repercussions in corporate boardrooms throughout the country. The courts recognize that boards of directors should be attentive to all their duties regarding the corporation and its shareholders. However, the facts in *Marshall Field* did not justify a ruling that would serve as a harsh reminder to directors. Nevertheless, the mere fact that suit was brought in this case has sparked interest in the corporate world[183] and perhaps thereby has achieved this purpose. The fatalism of the dissent also seems unjustified in light of recent decisions and trends in corporate law. The courts in general seem to scruti-

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Co. v. Skelly Oil Co., 267 A.2d 883, 887 (Del. 1970), *rev'g* 255 A.2d 717 (Del. Ch. 1969); Meyerson v. El Paso Natural Gas Co., 246 A.2d 789, 794 (Del. Ch. 1967).

176. 646 F.2d at 296.

177. *Id.* at 299.

178. *Id.* at 296.

179. *Id.* at 297.

180. To illustrate the quagmire encountered in applying the business judgment rule, *compare* Maldonado v. Flynn, 485 F. Supp. 274 (S.D.N.Y. 1980) *with* Maldonado v. Flynn, 413 A.2d 1251 (Del. Ch. 1980), *and* Singer v. Magnavox Co., 380 A.2d 969 (Del. 1977) *with* Tanzer v. International Gen. Indus., Inc., 402 A.2d 382 (Del. Ch. 1979).

181. 646 F.2d at 304.

182. *Id.* at 305.

183. *See, e.g., The Takeover Crisis: A Special Report,* 13 INSTIT. INV. 32 (June 1979); Bowers, *supra* note 2.

nize decisions of directors more carefully when such decisions are made in situations where large numbers of corporate shares are either issued in defensive maneuvers or bought with corporate funds, as in parent-subsidiary relationships,[184] freeze out attempts,[185] shareholders' derivative actions,[186] and take-over attempts.[187] A recent barrage of articles has addressed the subject of the duties and liabilities of directors not only in law reviews but also in business journals.[188] It is interesting to note, however, that the Supreme Court has refused to review the subject of directors' duties and liabilities.[189] If directors fail to heed this judicial trend, they cannot claim not to have been forewarned.

IV. Conclusion

Panter v. Marshall Field & Co. is a step in the continuing effort to define and clarify the good faith standard for corporate directors. It does not attempt to articulate what challenging shareholders in every case must show to overcome the initial burden of proof in their attack on corporate directors, nor does it attempt to articulate what corporate directors in every case must do to protect their decisions from attack. Rather, it sets forth an example of an insufficient showing by challenging shareholders. This is a *negative* approach to delineating the duties of directors, and its value is perhaps limited to analogous factual situations.

The decision blends the concept of the duty of due care with that of fiduciary duty. As a result, the application by the court of the business judgment rule defense and its presumption of sound business judgment

184. *See, e.g.,* Sinclair Oil Corp. v. Levien, 280 A.2d 717 (Del. 1971); Getty Oil Co. v. Skelly Oil Co., 267 A.2d 883 (Del. 1970); Bennett v. Propp, 41 Del. Ch. 14, 187 A.2d 405 (1962).

185. *See, e.g.,* Tanzer v. International Gen. Indus., Inc., 402 A.2d 382 (Del. Ch. 1979); Singer v. Magnavox Co., 380 A.2d 969 (Del. 1977).

186. *See, e.g.,* Burks v. Lasker, 441 U.S. 471 (1979); Lewis v. Anderson, 615 F.2d 778 (9th Cir. 1980); Abbey v. Control Data Corp., 603 F.2d 724 (8th Cir. 1979), *cert. denied,* 444 U.S. 1017 (1980); Cramer v. General Tel. & Elec. Corp., 582 F.2d 259 (3d Cir. 1978), *cert. denied,* 439 U.S. 1129 (1979); Maher v. Zapata Corp., 490 F. Supp. 348 (S.D. Tex. 1980); Maldonado v. Flynn, 485 F. Supp. 274 (S.D.N.Y. 1980); Zapata v. Maldonado, [1981] Sec. Reg. & L. Rep. (BNA) 604 G-1; Maldonado v. Flynn, 413 A.2d 1251 (Del. Ch. 1980); Auerbach v. Bennett, 47 N.Y.2d 619, 393 N.E.2d 994, 419 N.Y.S.2d 920 (1979).

187. *See, e.g.,* Lewis v. McGraw, 619 F.2d 192 (2d Cir.), *cert. denied,* 101 S. Ct. 354 (1980); Treadway Cos. v. Care Corp., 638 F.2d 357 (2d Cir. 1980); Crouse-Hinds Co. v. InterNorth, Inc., 634 F.2d 690 (2d Cir. 1980); Golub v. PPD Corp., 576 F.2d 759 (8th Cir. 1978); Gulf & Western Indus., Inc. v. Great A & P Tea Co., 476 F.2d 687 (2d Cir. 1973); Berman v. Gerber Prods. Co., 454 F. Supp. 1310 (W.D. Mich. 1978); GM Sub Corp. v. Liggett Group, Inc., 415 A.2d 473 (Del. 1980).

188. *See, e.g.,* note 183 *supra.*

189. *See, e.g.,* Lewis v. McGraw, 619 F.2d 192 (2d Cir.), *cert. denied,* 101 S. Ct. 354 (1980); Abbey v. Control Data Corp., 603 F.2d 724 (8th Cir. 1979), *cert. denied,* 444 U.S. 1017 (1980); Cramer v. General Tel. & Elec. Corp., 582 F.2d 259 (3d Cir. 1978), *cert. denied,* 439 U.S. 1129 (1979).

exercised with care and in good faith is confusing. *Marshall Field* serves as a warning to corporate directors, and yet it also points out that each case involving the relationship of a corporation, its board of directors and shareholders is unique. Consequently, each unique set of facts presents a setting against which the application of the business judgment rule and its aspects of duty of due care and fiduciary duty must be examined individually.

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