Delaware Improves Its Treatment of Freezeout Mergers: *Weinberger v. UOP, Inc.*[1] In considering challenges to corporate takeover tactics, state courts have long had difficulty striking a satisfactory balance among the competing interests of a target corporation's management, controlling stockholders and minority shareholders.[2] While Congress[3] and many state governments[4] have enacted takeover legislation, traditionally the state courts have been left with the difficult task of deciding issues of fiduciary duty and fairness in challenges to corporate takeovers.[5] State courts have had particular difficulty deciding these issues in cases involving freezeout mergers,[6] where the acquiring corporation is also the majority shareholder of the target company.[7] Because the laws of many states, such as Delaware, allow mergers to be effected upon the affirmative vote of a majority of the shareholders of the corporations involved,[8] freezeout mergers often occur as the second step of a corporate takeover.[9] After purchasing a majority of the outstanding common

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[1] 457 A.2d 701 (Del. 1983).

[2] *See generally* Weiss, *The Law of Take Out Mergers: A Historical Perspective*, 56 N.Y.U.L. REV. 624, 626-57 (1981). The particular takeover device bidders use often depends on how receptive the target's management is to an acquisition attempt. *See* Fischel, *Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers*, 57 TEX. L. REV. 1, 5 (1978).

[3] In 1968, Congress passed the Williams Act. 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1982). The Williams Act was designed to protect investors by requiring full and fair disclosure of the terms of a tender offer. H.R. REP. NO. 1711, 90th Cong., 2d Sess. 3, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS 2811, 2813, S. REP. 550, 90th Cong., 1st Sess. 3 (1967).

[4] Most of the leading commercial states have enacted takeover legislation. *See, e.g.*, DEL. CODE ANN. tit. 8, § 203 (1983); MASS. GEN. LAWS ANN. ch. 110c, §§ 1-13 (West Supp. 1983-1984); MICH. COMP. LAWS ANN. §§ 451.901 to .917 (1983); N.J. STAT. ANN. §§ 49:5-1 to :19 (West Supp. 1983-1984); N.Y. BUS. CORP. LAW §§ 1600-1614 (McKinney Supp. 1983-1984); PA. CONS. STAT. ANN. tit. 710, §§ 71-85 (Purdon Supp. 1983-1984). As a result of the Supreme Court's decision in Edgar v. MITE Corp., 457 U.S. 624 (1982), the future vitality of state takeover legislation is uncertain. In *MITE* the Court invalidated the Illinois Act, because it found that the Illinois legislation constituted an impermissible regulation of interstate commerce. *Id.* at 646. State takeover legislation also has been attacked successfully on federal preemption grounds. *See* Great W. United Corp. v. Kidwell, 577 F.2d 1256, 1280-81 (5th Cir. 1978) (Idaho statute declared preempted by Williams Act and invalid under commerce clause), *rev'd on other grounds sub nom.* Leroy v. Great W. United Corp., 443 U.S. 173, 187 (1979). For an analysis of the *MITE* decision see Note, *The Unsung Death of State Takeover Statutes: Edgar v. MITE Corp.*, 24 B.C.L. REV. 1017 (1983).

[5] *See* Folk, *State Statutes: Their Role in Prescribing Norms of Responsible Management Conduct*, 31 BUS. LAW. 1031, 1033-34 (1976).

[6] For a detailed account of the historical development of judicial treatment of freezeout mergers, see Weiss, *supra* note 2, at 626-57.

[7] Greene, *Corporate Freeze-out Mergers: A Proposed Analysis*, 28 STAN. L. REV. 487, 489 (1976).

[8] Delaware General Corporation Law contains two merger provisions. Section 251 is commonly referred to as Delaware's long-form merger statute. DEL. CODE. ANN. tit. 8, § 251 (1983). Section 251 authorizes the consummation of a merger upon the affirmative vote of a simple majority of the shareholders of the acquiring and acquired corporations. *Id.* § 251(c). Delaware's short-form merger statute simplifies the merger process in situations where the acquiring corporation owns 90% or more of the stock of the target company. *See id.* § 253. Section 253 allows a merger to be effected by the passage of a resolution by the board of directors of the acquiring corporation. *Id.* § 253(a). Section 253 vests the power to consummate a short-form merger solely with the directors of the acquiring corporation. *See id.* A merger effected pursuant to section 253 does not have to be approved by a vote of the shareholders of the target company. In fact, when a parent company effects a short-form freezeout merger pursuant to section 253, the parent company is not required to notify the subsidiary's minority shareholders prior to the consummation of the merger. *See id.*

[9] *See* Greene, *supra* note 7, at 491-94. Commentators have identified three types of freezeout mergers: 1) two-step mergers 2) parent-subsidiary mergers and 3) going-private mergers. *See* Brud-

stock of the target corporation,[10] the acquiring corporation can achieve sole ownership of the target company by voting its majority interest in the target company in favor of a merger with itself.[11] As a result of this majority vote, the target corporation's minority shareholders are, in effect, forced to sell their shares to the acquiring corporation.[12]

Freezeout mergers differ in several important respects from arm's-length mergers between unaffiliated corporations.[13] Unlike negotiated mergers between unaffiliated corporations, the target company's shareholders are not treated equally.[14] In a typical arm's-length merger acquisition, each shareholder of the target company exchanges his stock for the same proportionate amount of cash or other securities.[15] In a freezeout merger, the majority shareholder continues its investment in the target company's business, while the minority shareholders must either accept the consideration offered by the majority or challenge the adequacy of the merger price in litigation or in an appraisal proceeding.[16] In a freezeout merger, therefore, there is a significant danger that the

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ney & Chirelstein, *A Restatement of Corporate Freezeouts*, 87 YALE L.J. 1354, 1359-76 (1978); Greene, *supra* note 7, at 491-96. In both two-step mergers and parent-subsidiary mergers, a freezeout merger is part of a corporate takeover. *See* Greene, *supra* note 7, at 491-94. A parent-subsidiary merger differs from a two-step merger, however, because in a parent-subsidiary merger the acquiring company first operates the target company as a subsidiary before effecting a freezeout merger to achieve sole ownership of the target. *See id.* at 492-93. Going-private mergers differ substantially from two-step mergers and parent-subsidiary mergers. In a going-private merger, a company's management, having determined that its shares are undervalued, seeks to eliminate the public stockholders of the company and return the firm to the status of a closely held corporation. Brudney & Chirelstein, *supra*, at 1365. The insiders typically create a holding company to which they transfer their controlling shares, and then propose a merger of the operating company into the holding company. *Id.* As a result of the merger, the insiders gain sole ownership of the corporation and the public shareholders generally receive cash in exchange for their shares. *Id.* Going-private mergers involve problems of fairness that are quite different from the problems created by two-step mergers and parent-subsidiary mergers. *See id.* at 1365-70. *See generally* Borden, *Going Private - Old Tort, New Tort, or No Tort*, 49 N.Y.U.L. REV. 987 (1974); Note, *Going Private*, 84 YALE L.J. 903 (1975).

[10] The acquiring company frequently acquires a controlling interest in a corporation through a cash tender offer. *See* Austin, *Tender Offer Update: 1983*, 18 MERG. & ACQ. 57, 57 (1983). Cash tender offers composed 89% of the total number of tender offers made in 1982. *Id.*

[11] *See* Greene, *supra* note 7, at 491. Generally, the acquiring corporation forms a wholly-owned subsidiary and merges the target company into this newly created shell corporation. *See* Brudney & Chirelstein, *supra* note 9, at 1357; Weiss, *supra* note 2 at 624.

[12] *See* Brudney & Chirelstein, *supra* note 9, at 1357.

[13] *See id.* at 1357-59. Brudney & Chirelstein maintain that while majority rule is an appropriate means of deciding whether an arm's-length merger should be allowed, majority rule in freezeout mergers does not merit the same deference. *See id.* at 1357-58. Arm's length mergers are considered presumptively fair because it is thought that the majority vote of the shareholders of each corporation represents the best interests of all the shareholders involved in the transaction. *See id.* at 1357. Brudney & Chirelstein argue that the majority vote of the shareholders of the target company in an arm's-length merger should be respected because all the target company's shareholders share the common goal of maximizing the returns of their stock and each shareholder will be affected identically by the outcome of the vote. *See id.* Brudney & Chirelstein argue that majority rule is not the appropriate means of determining whether a freezeout merger should be allowed. *See id.* at 1358-59. Because a danger exists in freezeout mergers that a self-interested majority stock-holder has ruled infairly, Brudney & Chirelstein conclude that special safeguards are necessary to ensure that the minority shareholders' interests are protected. *Id.*

[14] *See id.* at 1357.

[15] *Id.* at 1358.

[16] Greene, *supra* note 7, at 490. The dissenter's appraisal remedy is entirely a statutory creation. *See, e.g.*, DEL. CODE ANN. tit. 8, § 262 (1983); N.Y. BUS. CORP. LAW § 623 (McKinney Supp.

target company's minority shareholders will be treated unfairly, because the acquiring company is acting in its own self-interest in effecting the merger in order to gain sole ownership of the target corporation.[17] Futhermore, the minority shareholders stand in an inferior position in relation to the majority shareholder because the majority shareholder controls the bargaining process, the flow of information and the valuation of the minority's stock.[18] The Delaware courts have had particular difficulty deciding issues of fairness in freezeout merger challenges because the Delaware merger statutes technically allow the consummation of freezeout mergers regardless of any unfairness or breach of fiduciary duty by the majority shareholder.[19] *Weinberger v. UOP, Inc.* is the Delaware Supreme Court's most recent attempt to establish an appropriate standard of review for freezeout merger challenges.[20]

In *Weinberger*, a former shareholder of the Universal Oil Products Company ("UOP") brought a class action suit in the Delaware Court of Chancery challenging the elimination of UOP's minority shareholders through a freezeout merger with The Signal Companies,

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1983-1984). Appraisal statutes provide that under certain circumstances, a stockholder of a corporation may force the corporation to pay cash for the "value" of his shares. *See* Manning, *The Shareholder's Appraisal Remedy: An Essay for Frank Coker*, 72 YALE L.J. 223, 226 (1962). Manning characterized statutory appraisal remedies as "bail-out" provisions. *Id.* Although appraisal statutes vary in scope and form, virtually all appraisal statutes include mergers as transactions that will trigger the remedy for some or all shareholders. *See, e.g.*, DEL. CODE ANN. tit. 8, 262(b) (1983); N.Y. BUS. CORP. LAW § 623(c) (McKinney Supp. 1983-1984). The Delaware statute provides in pertinent part:

> Any stockholder of a corporation of this state who has complied with subsection (d) of this section and has neither voted in favor of the merger or consolidation nor consented thereto in writing pursuant to § 228 of this title shall be entitled to an appraisal by the Court of Chancery of the fair value of his shares of stock under the circumstances described in subsections (b) and (c) of this section.

DEL. CODE ANN. tit. 8, § 262(a) (1983). The right of appraisal is not necessarily absolute, however. For instance, Delaware law provides that no appraisal rights shall be available:

> for the shares of any class or series of stock which, at the record date fixed to determine the stockholders entitled to receive notice of and to vote at the meeting of stockholders to act upon the agreement of merger or consolidation were either (i) listed on a national securities exchange or (ii) held of record by more than 2,000 stockholders; and further provided that no appraisal rights shall be available for any shares of stock of the constituent corporation surviving a merger if the merger did not require for its approval the vote of the stockholders of the surviving corporation as provided in subsection (f) of § 251 of this title.

Id. § 262(b)(1).

[17] *See* Brudney & Chirelstein, *supra* note 9, at 1358.

[18] *See* Brudney, *Efficient Markets and Fair Values in Parent-Subsidiary Mergers*, 4 J. CORP. L. 63, 71 (1978). Brudney states that once a parent company contemplates a merger with a subsidiary, the parent corporation is "not unlikely to" control both the use of accounting conventions and flow of financial information so as to decrease the market price of the subsidiary's stock below its intrinsic value. *Id.* Brudney argues that for this reason the market price of the subsidiary's stock should not be an important factor in evaluating the fairness of a merger price. *Id.* at 64.

[19] *See, e.g.*, Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983); Tanzer v. International General Indus., Inc., 379 A.2d 1121 (Del. 1977); Singer v. Magnavox Co., 380 A.2d 969 (Del. 1977); Stauffer v. Standard Brands, Inc., 41 Del. Ch. 7, 187 A.2d 78 (Del. 1962); Coyne v. Park & Tilford Distillers Corp., 38 Del. Ch. 514, 154 A.2d 893 (Del. 1959); Sterling v. Mayflower Hotel Corp., 33 Del. Ch. 293, 93 A.2d 107 (Del. 1952); Federal United Corp. v. Havender, 24 Del. Ch. 318, 11 A.2d 331 Del. 1940. Young v. Valhi, Inc., 382 A.2d 1372 (Del. Ch. 1981); David J. Greene & Co. v. Schenley Indus., Inc., 281 A.2d 30 (Del. Ch. 1971); David J. Greene & Co. v. Dunhill Int'l, Inc., 249 A.2d 427 (Del. Ch. 1968); Bruce v. E.L. Bruce Co., 40 Del. Ch. 80, 174 A.2d 29 (Del. Ch. 1961).

[20] 457 A.2d 701 (Del. 1983).

Inc. ("Signal").[21] The plaintiffs sought to set aside the merger on the grounds that Signal had unfairly used its majority stock ownership position in UOP to freeze out the minority shareholders at an inadequate price.[22] Plaintiffs specifically alleged that Signal had effected the merger for the sole purpose of eliminating the minority shareholders from UOP, that Signal and UOP had misrepresented material facts concerning the bargaining process in the proxy material and certain press releases and that UOP's board of directors had breached their fiduciary duty by not attempting to negotiate a higher merger price with Signal.[23] Signal had acquired a 50.5% interest in UOP in 1975 through a cash tender offer.[24] In 1978, Signal decided to investigate the possibility of acquiring the remainder of UOP's publicly held stock.[25] As part of the investigation, two Signal directors, who were also directors of UOP, prepared a feasibility study for Signal's board of directors.[26] The study concluded that it would be a good investment for Signal to acquire the remaining 49.5% of UOP's shares at any price up to $24 per share.[27]

At a meeting of Signal's executive committee, UOP's chief executive officer, James V. Crawford, who was also a director of Signal, indicated that a Signal proposal to pay $20-$21 per share for UOP's remaining publicly held stock was "generous" and should be submitted to UOP's minority shareholders for their consideration.[28] At this meeting, Signal's executive committee authorized its management to negotiate with UOP for the cash acquisition of UOP's minority shares.[29] Signal's executive committee requested that a proposal be submitted to Signal's board of directors in four business days.[30] During those four days, Crawford spoke with UOP's outside directors by telephone.[31] During that period, Crawford also retained Lehman Brothers Kuhn Loeb, Inc. ("Lehman Brothers"), an investment banking firm,[32] to render a fairness opinion as to the price offered for the minority's stock.[33] After a summary examination of UOP's relevant financial records,[34] Lehman Brothers concluded that a price of $20-$21 per share "would be a fair price for the remaining shares of UOP."[35] The directors of both corporations approved the merger

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[21] Weinberger v. UOP, Inc., 426 A.2d 1333, 1334-35 (Del. Ch. 1981).

[22] *Id.* at 1341.

[23] *Id.*

[24] 457 A.2d at 704. Signal purchased 1,500,000 of UOP's authorized but unissued common stock at $21 per share. *Id.* This negotiated purchase was contingent on a successful tender offer for 4,300,000 of UOP's publicly held shares, also at a price of $21 per share. *Id.* Immediately before the announcement of the tender offer, UOP's common stock had been trading at a fraction under $14 per share. *Id.* The tender offer was greatly oversubscribed, but Signal limited its purchase to 4,300,000 shares, enough when coupled with its purchase of the unissued shares, to give it a 50.5% ownership interest in UOP. *Id.*

[25] *Id.* at 705.

[26] *Id.*

[27] *Id.*

[28] *Id.* At this meeting, UOP's president did not try to negotiate a price higher than $21. *Id.* Apparently, UOP's president was not informed about the results of Signal's feasibility study indicating that Signal was prepared to pay as much as $24 per share for UOP's stock. *Id.* at 705-06.

[29] *Id.*

[30] *Id.* at 705-06.

[31] *Id.* at 706.

[32] *Id.* Lehman Brothers had previously performed services for UOP and was familiar with UOP's business. *Id.*

[33] *Id.*

[34] Lehman Brothers only spent three days preparing the fairness opinion for UOP due to the time constraints imposed by Signal. *Id.* at 706-07.

[35] *Id.* at 707.

proposal,[36] but conditioned the consummation of the acquisition on the approval of a majority of UOP's minority shareholders.[37] At UOP's next annual meeting, a majority of UOP's minority shareholders approved the merger with Signal at the price of $21 per share and the merger was subsequently consummated.[38] As a result of the merger, UOP became the wholly-owned subsidiary of Signal.[39]

Not all of UOP's minority shareholders were satisfied with the merger terms, however. On behalf of all of UOP's former shareholders who had not exchanged their shares for the merger price, William B. Weinberger instituted a class action suit in the Delaware Court of Chancery asking for an injunction rescinding the merger.[40] In the event that the court found an injunction to be inappropriate, the plaintiffs requested the court to award damages in an amount the economic equivalent of rescission.[41] The plaintiffs charged that Signal had effected the merger for an improper purpose, that both Signal and UOP were guilty of misrepresentation and that UOP's directors had breached their fiduciary duty by failing to negotiate a higher merger price.[42] The plaintiffs also maintained that Signal had used its majority stock ownership position in UOP to eliminate the minority shareholders at a grossly inadequate price.[43]

After a trial on the merits,[44] the Chancery Court found in favor of the defendants, holding that the merger terms were legally fair to the plaintiffs.[45] In so holding, the court

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[36] *Id.* The directors of both companies met simultaneously. *Id.* Signal's men on UOP's board of directors participated in various aspects of UOP's board meeting, although they abstained from voting. *Id.* The minutes of the meeting, however, reveal that each of them stated that if they had voted, they would have voted in favor of the proposed merger. *Id.*

[37] *Id.* The merger proposal also required that the minority shares voting in favor of the agreement, when coupled with Signal's 50.5% interest, comprise at least two-thirds of all UOP shares outstanding. *Id.*

[38] *Id.* at 708. As of the record date of UOP's annual meeting there were 11,488,302 shares of UOP common stock outstanding. *Id.* Signal owned 5,688,302 shares. *Id.* UOP's minority shareholders owned 5,688,302 shares. *Id.* At the meeting 3,208,652 (56%) of the minority shares voted. *Id.* Of these 2,953,812 voted in favor of the merger and 254,840 voted against it. *Id.*

[39] Weinberger v. UOP, Inc., 426 A.2d 1333, 1335 (Del. Ch. 1981). UOP was merged into Sigco Incorporated, a shell corporation created by Signal for the purposes of the merger. *Id.*

[40] *Id.* The Chancery Court dismissed Weinberger's first complaint, ruling that Weinberger had not alleged sufficient facts demonstrating the unfairness of the challenged merger. Weinberger v. UOP, Inc., 409 A.2d 1262, 1266-68 (Del. Ch. 1979). According to the court, because UOP's minority shareholders had approved the merger, Weinberger had to allege specific acts such as fraud or misrepresentation to state a cause of action for unfairness. *Id.* Weinberger subsequently filed an amended complaint alleging specific acts of fraud, misrepresentation and misconduct. Weinberger v. UOP, Inc., 426 A.2d 1333, 1340-41 (Del. Ch. 1981).

[41] Weinberger v. UOP, Inc., 426 A.2d 1333, 1335 (Del. Ch. 1981). Weinberger argued that a damage award could be in the form of cash or an equivalent amount of Signal stock. *Id.*

[42] *Id.* at 1348-56.

[43] *Id.* at 1356-62. The plaintiffs also alleged that Lehman Brothers had conspired with Signal and its controlled UOP board of directors to deceive UOP's minority shareholders into voting to approve the merger terms. *Id.* at 1347. The plaintiffs contended that Lehman Brothers actually worked in the interests of Signal rather than UOP's minority shareholders in rendering its fairness opinion. *Id.* The Chancellor held that the plaintiffs had failed to establish such a conspiracy and entered a judgment in favor of Lehman Brothers. *Id.* at 1348. The plaintiffs did not appeal this aspect of the Chancellor's decision. Weinberger v. UOP, Inc., 457 A.2d 701, 702 (Del. 1983).

[44] Subsequent to the completion of the trial, Weinberger also filed a motion seeking to enlarge the class to include all former shareholders of UOP at the time of the merger other than Signal. Weinberger v. UOP, Inc., 426 A.2d 1333, 1335 (Del. Ch. 1981).

[45] *Id.* at 1363. The court reasoned that this result made it unnecessary to consider plaintiff's motion to enlarge the class. *Id.*

rejected the plaintiffs' allegations of improper purpose, misrepresentation, breach of fiduciary duty and unfair price.[46] The plaintiffs argued that the merger should be enjoined because Signal had effected the merger for the sole purpose of eliminating UOP's minority shareholders in violation of the business purpose requirement established in *Singer v. Magnavox Co.*[47] In *Singer*, the Delaware Supreme Court held that the use of corporate power by a majority shareholder "solely to eliminate the minority" is a violation of its fiduciary duty.[48] The Chancellor ruled that Signal had not breached its duty in this respect because its desire to make a favorable investment with its cash reserves constituted a valid business purpose for effecting the merger.[49] The court rejected plaintiffs' allegations of misrepresentation because it found that both Signal's press releases and UOP's proxy materials were not misleading.[50] The court also found that UOP's board of directors had not breached their fiduciary duty to the plaintiffs because UOP's directors were not required to negotiate a higher merger price for UOP's stock if they believed Signal's original offer to be fair.[51] Finally the court examined the plaintiffs' allegations concerning the fairness of the merger price.[52]

The plaintiffs argued that notwithstanding the Chancellor's findings concerning their claims of improper purpose, misrepresentation and breach of fiduciary duty, they nonetheless were entitled to relief because the merger price of $21 per share was "inadequate and indefensible" on the facts.[53] The plaintiffs offered the testimony of a chartered investment analyst who stated that UOP's stock had a fair value of not less than $26 per share when valued according to the discounted cash flow valuation method[54] and

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[46] *Id.* at 1348-62. The Chancellor stated at the beginning of his opinion that due to the numerous contentions made by plaintiff, some matters urged by the plaintiff were not specifically addressed in the opinion. *Id.* at 1335. As to those contentions not addressed, however, the Chancellor stated that he nonetheless had considered them. *Id.*

[47] *Id.* at 1341. Singer v. Magnavox Co., 380 A.2d 969 (Del. 1977).

[48] Singer v. Magnavox Co., 380 A.2d 969, 980 (Del. 1977).

[49] Weinberger v. UOP, Inc., 426 A.2d 1333, 1350 (Del. Ch. 1981).

[50] *Id.* at 1352.

[51] *Id.* at 1354, 1356.

[52] *Id.* at 1356-62.

[53] *Id.* at 1356.

[54] *Id.* According to plaintiffs' expert, the discounted cash flow valuation method values a firm's stock according to the cash generating capabilities of a company as a going concern. *Id.* The following are plaintiffs' expert's calculations for 1977:

Sources	*In Millions*	
Income before extraordinary items	$24.3	
Depreciation	15.0	
Deferred income taxes	2.3	
Cash flow from operations	$41.6	41.6
Uses		
Additions for plant and equipment	$16.3	
Long-term debt payment (net)	4.5	
Cash requirements	$20.8	(20.8)
Net free cash from operations		$20.8

under a comparative analysis of premiums paid in similar acquisitions.[55] Although the Chancellor received the plaintiffs' evidence, he rejected it indicating that past Delaware practice precluded the use of the discounted cash flow valuation method.[56] Instead, the Chancellor accepted the evidence offered by the defendants who presented expert testimony valuing UOP's shares under the "Delaware block" approach, the valuation approach traditionally approved by Delaware decisions dealing with appraisal proceedings.[57] Under the Delaware block approach, the value of a corporation's stock generally is calculated as a weighted average of the corporation's asset value, market price and earnings per share.[58] The defendants' expert's calculations considered UOP's market value,[59] net asset value[60] and investment value,[61] including UOP's dividend record.[62]

	7.5%*	8.5%**
Present value of net free cash	$277.3	$244.6
Excess liquidity	37.0	37.0
Extraordinary items	7.0	7.0
Total discounted cash flow	$321.3	$288.6
Per share value	$28.09	$25.21

* High side of discount range found in sample of 1977/1978 acquisitions.
** Average Moody's industrial bond yield average: February, 1978.

Id. at 1357-58. Non-cash expenses such as depreciation and deferred expenses are added back to the income from operations figure in order to derive the cash flow generated from operations. *Id.* at 1357. Plaintiffs' expert also made similar calculations for 1978 and under UOP's five year business plan for the years 1978-1982. *Id.* at 1358. Under the 1978 analysis, he found the value of the minority's shares to have been $27.16. *Id.* Under UOP's five year business plan, plaintiffs' expert testified that the value of UOP's minority interest was either $25.94 or $30.59 per share. *Id.*

[55] *Id.* at 1358. Plaintiffs' expert concluded as a result of his comparative analysis of premiums paid in similar acquisitions that a reasonable premium for UOP's publicly held shares would have been between 70 and 80 per cent. *Id.* at 1357. Applying this to UOP's high of 14⅞ on February 28, 1978, the last trading day before the announcement of the merger negotiations, plaintiffs' expert concluded that under this method of analysis, the fair value of UOP's shares was between $25.65 and $27.30 per share. *Id.* The defendants' expert testimony concerning acquisition premiums indicated an average market premium of 48% and a median premium of 41% for comparable transactions. *Id.* at 1362.

[56] *Id.* at 1359-60. The Chancellor also seemed concerned that the conclusions reached under the discounted cash flow method were somewhat speculative because the valuation could be manipulated by varying the discount rate or varying the estimates necessary to arrive at the net free cash figure itself. *See id.* at 1359.

[57] *Id.* at 1361. The Delaware block approach originated in the case of In re General Realty & Utilities Corp., 29 Del. Ch. 480, 496, 500, 52 A.2d 6, 14-15 (Del. Ch. 1947).

[58] *See In re General Realty & Utilities Corp.*, 29 Del. Ch. 480, 496-500, 52 A.2d 6, 14-15 (Del. Ch. 1947).

[59] The defendents' expert testified that the average high-low market price for the five year period immediately preceeding the merger was $13.87. Weinberger v. UOP, Inc., 426 A.2d 1333, 1362 (Del. Ch. 1981).

[60] The defendants' expert calculated the net asset value of UOP to be $20.69 as of the end of the first quarter in 1978, but he argued that this figure should be accorded little weight because Signal was acquiring UOP for its ongoing business value. *Id.*

[61] According to the defendants' expert, the investment value of UOP broke down to be approximately $14.31 per share on a going concern basis and $16.39 per share on a book value basis. *Id.*

[62] *Id.* at 1361.

Based on the evidence presented by the defendants, the Chancellor found that there was a reasonable basis for finding the merger price of $21 per share to be a fair price to the minority shareholders of UOP.[63] The Chancellor concluded that when viewed overall, the terms of the merger were legally fair to the plaintiffs.[64] Dissatisfied with the Chancellor's findings, the plaintiffs sought review in the Delaware Supreme Court.

On appeal, the Delaware Supreme Court reversed the Chancellor's decision,[65] specifically eliminating the *Singer* business purpose requirement from Delaware law.[66] The court examined the Signal-UOP merger under the entire fairness test first articulated in 1952 in the case of *Sterling v. Mayflower Hotel Corp.*[67] In *Sterling*, the Delaware Supreme Court ruled that, because the parent company stood on both sides of the transaction, the parent company had to establish the "entire fairness" of the merger terms to the subsidiary's minority shareholders.[68] In *Weinberger*, the court stated that the concept of entire fairness is composed of two "basic aspects:" fair dealing and fair price.[69] After a review of the facts of the transaction, the court concluded that the Signal-UOP merger did not satisfy "any reasonable concept of fair dealing."[70] Consequently, the court reversed the Chancellor as to this aspect of his decision.[71] For the purpose of determining fair price under the entire fairness test, and for the purpose of determining fair value in future appraisal proceedings, the *Weinberger* court ruled that Delaware courts are no longer restricted to the exclusive use of the Delaware block, weighted average valuation method.[72] The court held that Delaware courts may now employ any modern valuation technique generally accepted by the financial community in determining the fair value of a corporation's stock.[73] Although the court found that Signal had not established the entire fairness of the merger terms, the court refused to set aside the merger, finding it "too involved to undo."[74] The court remanded the case and instructed the Chancellor to decide what, if any, damages to award to the plaintiffs "based upon entire fairness standards, i.e. fair dealing and fair price."[75]

The *Weinberger* decision represents a significant improvement in Delaware's treatment of freezeout merger challenges. First, the decision improves the treatment of minority shareholders involved in freezeout mergers. Even though the *Singer* business purpose requirement represented a possible ground for an injunction, the *Weinberger* court's elimination of the business purpose test actually improves judicial treatment of minority shareholders involved in freezeout mergers. By directing the attention of the Delaware courts to a review of the twin components of the entire fairness standard, fair dealing and fair price, the *Weinberger* court has made certain that in future cases the

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[63] *Id.* at 1362.

[64] *Id.* at 1363.

[65] Weinberger v. UOP, Inc., 457 A.2d 701, 715 (Del. 1983).

[66] *Id.* at 704, 715.

[67] *Id.* at 710-11 (citing Sterling v. Mayflower Hotel Corp., 33 Del. Ch. 293, 93 A.2d 107 (Del. 1952)).

[68] Sterling v. Mayflower Hotel Corp., 33 Del. Ch. 293, 298, 93 A.2d 107, 110 (Del. 1952).

[69] 457 A.2d at 711.

[70] *Id.* at 712.

[71] *Id.*

[72] *Id.* at 712-14.

[73] *Id.* at 713.

[74] *Id.* at 714.

[75] *Id.*

treatment of the minority shareholders will be the sole subject of judicial review. In addition to focusing the Delaware courts' scrutiny of future freezeouts on the treatment of minority shareholders, the *Weinberger* court also improved the appraisal remedy available to minority shareholders. Although apparently restricting the financial remedy available to minority shareholders to appraisal,[76] the *Weinberger* court improved the effectiveness of the appraisal remedy by allowing the use of modern valuation techniques in future appraisal proceedings.[77] The use of such techniques in appraisal proceedings will serve to guarantee that former shareholders receive fair value for the shares expropriated from them.

In addition to improving the treatment of minority shareholders, the *Weinberger* decision also improves the state of Delaware merger law from management's point of view by eliminating the *Singer* business purpose requirement. No longer will management have to face the uncertainty that a merger will be enjoined because a court found the purpose for the merger to be impermissible. The *Weinberger* court articulated clear guidelines and procedures that will facilitate the structuring of parent-subsidiary freezeout mergers in the future.[78] By following the procedures suggested by the *Weinberger* court, management should be able to structure future merger transactions without fear of judicial attack from dissatisfied minority shareholders. *Weinberger*, therefore, improves the quality of minority shareholder treatment in Delaware and clarifies the expected role of management in structuring parent-subsidiary mergers.

This casenote begins with a discussion of the development of Delaware case law regarding freezeout mergers in order to establish the context in which *Weinberger* was decided.[79] This historical discussion begins with a description of the important Delaware decisions preceding *Singer v. Magnavox Co.*[80] This discussion includes a brief discription of the United States Supreme Court's decision in *Sante Fe Industries, Inc. v. Green*, which immediately preceded the *Singer* decision and may have influenced the Delaware Supreme Court's decision in that case.[81] This background section concludes with a discussion of *Singer* and its companion case *Tanzer v. International General Industries, Inc.*, the two cases in which the Delaware Supreme Court announced the business purpose requirement for freezeout mergers.[82] After the background section, this casenote presents a description of the Delaware Supreme Court's opinion in *Weinberger*.[83] This casenote then analyzes the reasoning and impact of the *Weinberger* court's decision.[84]

The *Weinberger* decision represents an improvement in Delaware's treatment of freezeout mergers for two reasons. First, *Weinberger's* adoption of the entire fairness test as the sole standard of review affords minority shareholders more effective protection against unfair treatment by a majority shareholder than did the *Singer* business purpose test. Rather than providing minority shareholders with effective protection, the *Singer* business purpose requirement only served to create confusion among the Delaware courts as to what constituted a valid business purpose for effecting a freezeout merger. Second,

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[76] *Id.* at 715.
[77] *Id.* at 712-13.
[78] *See id.* at 709 n.7.
[79] *See infra* notes 86-185 and accompanying text.
[80] *See infra* notes 86-152 and accompanying text.
[81] *See infra* notes 130-52 and accompanying text.
[82] *See infra* notes 152-85 and accompanying text.
[83] *See infra* notes 185-239 and accompanying text.
[84] *See infra* notes 240-371 and accompanying text.

the *Weinberger* decision improves the law from management's point of view by providing management with guidelines for structuring future freezeouts. This casenote will analyze the impact of future use of the procedural guidelines suggested by the *Weinberger* court.[85] While *Weinberger* improves the law of freezeout mergers in Delaware, the Delaware Supreme Court should have gone further in prescribing management procedures. Because the Delaware Supreme Court indicated in *Weinberger* that in the future it would defer to the form of transactions complying with the procedural guidelines it suggested, this casenote submits that the *Weinberger* court should have completely outlined the structural framework these procedures should take by establishing specific negotiating guidelines.

I. THE HISTORY AND DEVELOPMENT OF DELAWARE'S TREATMENT OF FREEZEOUT MERGERS PRIOR TO *Weinberger v. UOP, Inc.*

Historically, minority shareholders have been largely unsuccessful in their attempts to enjoin freezeout mergers entered into under Delaware law.[86] By and large, the Delaware courts have relegated dissatisfied minority shareholders to an independent valuation of their shares in an appraisal preceeding as provided for in Delaware's corporation statutes.[87] Delaware's appraisal statute provides that under certain circumstances, a stockholder of a corporation involved in a merger can petition for an appraisal of the fair value of his shares.[88] If the appraiser finds the fair value of the dissenting shareholder's stock to be higher than the actual merger price, the appraiser will require the corporation to pay cash for the fair value of the stock.[89] Prior to *Singer v. Magnavox Co.*, the Delaware courts generally refused to enjoin freezeout mergers which complied with the technical requirements of the Delaware merger statutes.[90] This policy of judicial *laissez-faire* towards mergers complying with the Delaware merger statutes began in 1940, in the case of *Federal United Corp. v. Havender*.[91]

Havender involved a shareholder challenge to the proposed stock for stock merger of the Federal United Corporation ("Federal") with the Bond and Share Company, Federal's wholly-owned subsidiary.[92] The proposed merger would have recapitalized Federal and eliminated the accumulated dividends that had accrued on its preferred stock.[93] Federal's preferred shareholders filed suit in the Court of Chancery seeking an injunction against the payment of dividends on the newly issued stock until all the arrearages on the old stock had been paid.[94] The Chancery Court granted the injunction,[95] finding that al-

[85] *See infra* notes 372-91 and accompanying text.

[86] *See, e.g.*, Tanzer v. International General Indus., Inc., 379 A.2d 1121 (Del. 1977); Stauffer v. Standard Brands, Inc., 41 Del. Ch. 7, 187 A.2d 78 (Del. 1962); Coyne v. Park & Tilford Distillers Corp., 38 Del. Ch. 514, 154 A.2d 893 (Del. 1959); Federal United Corp. v. Havender, 24 Del. Ch. 318, 11 A.2d 331 (Del. 1940); David J. Greene & Co. v. Schenley Indus., Inc., 281 A.2d 30 (Del. Ch. 1971); Bruce v. E.L. Bruce Co., 40 Del. Ch. 80, 174 A.2d 29 (Del Ch. 1961).

[87] *See* cases cited *supra* note 86. For a detailed description of the historical development of the law relevant to freezeout mergers prior to the *Singer* decision see Weiss, *supra* note 2, at 644-57.

[88] *See* DEL. CODE ANN. tit. 8, § 262 (1983).

[89] *See id.*

[90] *See* Weiss, *supra* note 2, at 644-57.

[91] 24 Del. Ch. 318, 334, 11 A.2d 331, 338-39 (Del. 1940).

[92] *Id.* at 322, 11 A.2d at 333.

[93] *Id.*

[94] Havender v. Federal United Corp., 23 Del. Ch. 104, 113, 2 A.2d 143, 147 (Del. Ch. 1938).

[95] Havender v. Federal United Corp., 24 Del. Ch. 96, 109, 6 A.2d 618, 624 (Del. Ch. 1939). The case was heard twice in the Chancery Court. *See* Havender v. Federal United Corp., 24 Del. Ch. 96, 6

though the transaction was structured as a merger, in substance the transaction was an impermissible recapitalization.[96] On appeal, the Delaware Supreme Court reversed the Chancery Court.[97] According to the *Havender* court, a single shareholder should not be allowed to block a merger that had met Delaware's statutory requirements, provided that the merger terms were both fair and equitable.[98] The court stated that the power to merge was "plain, understandable and general," and "not qualified by limitation or exception."[99] The court also explained that under Delaware law, minority shareholders take their stock with notice that the corporation in which they own stock may merge with another corporation upon an affirmative vote of the requisite number of stockholders as provided for by Delaware's merger statutes.[100] The court concluded that if a shareholder is dissatisfied with the terms of a merger, the stockholder should demand and receive the fair value of his shares as provided for by Delaware's appraisal statute.[101]

In 1952, in the case of *Sterling v. Mayflower Hotel Corp.*,[102] the Delaware Supreme Court for the first time allowed minority shareholders to attack a merger on fairness grounds even though on its face, the merger complied with the relevant Delaware statutes.[103] In *Sterling*, the minority shareholders of the Mayflower Hotel Corporation ("Mayflower") filed suit in the Chancery Court seeking a preliminary injunction to prevent the proposed stock for stock merger of Mayflower and Mayflower's parent company, the Hilton Hotels Corporation ("Hilton").[104] The plaintiffs alleged that the terms of the merger were fraudulent and unfair to Mayflower's minority shareholders.[105] The Chancery Court found no evidence of fraud and concluded that the terms of the merger were "legally fair" to Mayflower's minority shareholders.[106] Accordingly, the court refused to issue a preliminary injunction.[107] On appeal, the Delaware Supreme Court affirmed the Chancery Court's decision.[108] Unlike its previous decision in *Havender*, however, the *Sterling* court did not relegate Mayflower's minority shareholders exclusively

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A.2d 618 (Del. Ch. 1939); Havender v. Federal United Corp., 23 Del. Ch. 104, 2 A.2d 143 (Del. Ch. 1938). The first time the case was heard, although the Chancellor found generally in favor of the plaintiffs, he stated that he wished to consider further the effects of issuing an injunction before entering a final decree. Havender v. Federal United Corp., 23 Del. Ch. 104, 113-14, 2 A.2d 143, 147 (Del. Ch. 1938). The Chancellor died before he entered a final decree and the case was heard a second time on a motion for reargument by the defendant. Havender v. Federal United Corp., 24 Del. Ch. 96, 99, 6 A.2d 618, 624 (Del. Ch. 1939).

[96] Havender v. Federal United Corp., 24 Del. Ch. 96, 104, 6 A.2d 618, 622 (Del. Ch. 1939). The Delaware Supreme Court had previously held that accumulated dividends could not be extinguished by amending the corporate charter. Keller v. Wilson & Co., 21 Del. Ch. 391, 412-13, 190 A.2d 115, 125 (Del. 1936).

[97] Federal United Corp. v. Havender, 24 Del. Ch. 318, 348, 11 A.2d 331, 344 (Del. 1940).

[98] *Id.* at 334, 11 A.2d at 338-39.

[99] *Id.* at 330-31, 11 A.2d at 337.

[100] *Id.* at 333, 11 A.2d at 338.

[101] *Id.* at 334-35, 11 A.2d at 339.

[102] 33 Del. Ch. 293, 93 A.2d 107 (Del. 1952).

[103] *Id.* at 297-98, 93 A.2d at 109-10.

[104] Sterling v. Mayflower Hotel Corp., 33 Del. Ch. 20, 22-23, 89 A.2d 862, 864 (Del. ch. 1952). The merger agreement provided that each share of Mayflower stock would be converted into one share of Hilton stock. *Id.* at 23, 89 A.2d at 864. At the time of the proposed merger, Hilton owned approximately five-sixths of Mayflower's outstanding stock. *Id.*

[105] *Id.* at 22, 89 A.2d at 864.

[106] *Id.* at 35, 89 A.2d at 871.

[107] *Id.*

[108] Sterling v. Mayflower Hotel Corp., 33 Del. Ch. 293, 315, 93 A.2d 107, 119 (Del. 1952).

to the statutory appraisal remedy.[109] Instead, the *Sterling* court allowed the minority shareholders to challenge the proposed merger, ruling the Hilton had the burden of establishing the "entire fairness" of the transaction because Hilton's directors stood on both sides of the transaction.[110] The court reasoned that this was the appropriate allocation of the burden of proof because Hilton, as the majority shareholder of Mayflower, stood in a fiduciary position in respect to its dealings with Mayflower's minority shareholders.[111] Although the *Sterling* court allowed the minority shareholders to challenge the merger, the court refused to enjoin the merger because it found that Hilton had established that the terms of the merger were in fact fair to the minority shareholders.[112]

Although the entire fairness requirement announced in *Sterling* seemed to afford minority shareholders with a means for seeking equitable relief in freezeout merger challenges, subsequent decisions by the Delaware courts did not utilize the *Sterling* standard as a basis for enjoining unfair mergers. For example, in *Stauffer v. Standard Brands, Inc.*,[113] the Delaware Supreme Court did not require the parent company to satisfy the *Sterling* entire fairness requirement.[114] The *Stauffer* case involved the merger of the Planters Nut and Chocolate Company ("Planters") and Standard Brands, Inc. ("Standard").[115] Because Standard owned more than 90% of Planters' outstanding stock,[116] Standard's board of directors effected the merger with Planters by adopting an appropriate resolution, as provided for by Delaware's short-form merger statute.[117] The minority shareholders of Planters brought a class action suit in the Court of Chancery[118] seeking to set aside the merger on the grounds that the merger price was so inadequate that it constituted a constructive fraud on Planters' minority shareholders.[119] The plaintiffs also alleged that Standard, as the majority shareholder of Planters, breached its fiduciary obligation to the minority by failing to offer a fair price for their shares.[120] The Chancery Court granted the defendants' motion to dismiss, ruling that the plaintiffs' "only remedy lies in their right to an appraisal."[121]

On appeal, the Delaware Supreme Court affirmed the Chancery Court's ruling.[122] Because the court found that the "very purpose of the statute [section 253] is to provide the parent corporation with a means of eliminating the minority shareholder's interest in

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[109] *See id.* at 298, 93 A.2d at 110.

[110] *Id.* The defendants apparently conceded that the minority shareholders could attack the merger and did not argue that appraisal should be their exclusive remedy. *Id.*

[111] *Id.* at 298, 93 A.2d at 109-110. In support of this proposition, the court cited Keenan v. Eshleman, 23 Del. Ch. 234, 2 A.2d 904 (Del. 1938) and Gottlieb v. Heyden Chem. Corp., 33 Del. Ch. 82, 90 A.2d 660 (Del. 1952). *Sterling*, 33 Del. Ch. at 298, 93 A.2d at 109-10. The *Gottlieb* case concerned self-dealing on the part of directors involved in a stock option plan. *Gottlieb*, 3 Del. Ch. at 83-84, 90 A.2d at 661. The Delaware Supreme Court stated that "the burden is upon the directors to prove not only that the transaction was in good faith, but also that its intrinsic fairness will withstand the most searching and objective analysis." *Id.* at 88, 90 A.2d at 663.

[112] *Sterling*, 33 Del. Ch. at 311, 93 A.2d at 117.

[113] 41 Del. Ch. 7, 187 A.2d 78 (Del. 1962).

[114] *See id.* at 11, 187 A.2d at 80.

[115] *Id.* at 8, 187 A.2d at 79.

[116] *Id.* at 9, 187 A.2d at 79.

[117] *Id.* at 9-10, 187 A.2d at 79. *See* DEL. CODE ANN. tit. 8, § 253 (1983).

[118] Stauffer v. Standard Brands, Inc., 40 Del. Ch. 202, 203, 178 A.2d 311 (Del. Ch. 1962).

[119] *Id.* at 205, 178 A.2d at 312.

[120] *Id.*

[121] *Id.* at 212, 178 A.2d at 316.

[122] Stauffer v. Standard Brands, Inc., 41 Del. Ch. 7, 11, 187 A.2d 78, 80 (Del. 1962).

the enterprise," the court held that equitable relief would not be appropriate in the instant case.[123] In fact, the court stated that it would be "difficult to imagine a case under the short merger statute in which there could be such actual fraud as would entitle a minority to set aside the merger."[124] The court found that the directors of Planters had not breached any fiduciary obligations owed to the minority shareholders by not attempting to negotiate a higher merger price, because section 253 explicitly authorized unilateral action by Standard's directors by virtue of its 90% ownership interest in Planters.[125] The court concluded that because the instant case only involved a dispute over the value of the plaintiffs' stock in Planters, the minority shareholders' only remedy was to seek appraisal.[126] Because the Delaware courts had continually ruled that absent a showing of actual fraud or gross overreaching equitable relief was inappropriate in freezeout merger challenges,[127] disgruntled minority shareholders began to look to the federal courts for relief.[128] Although plaintiffs initially met with some success under the federal securities laws under Rule 10b-5,[129] the Supreme Court in *Sante Fe Industries, Inc. v. Green*[130] placed severe restrictions on obtaining such relief in the future in federal court.[131]

The *Sante Fe* case involved the merger of the Kirby Lumber Corporation ("Kirby") and Sante Fe Industries ("Sante Fe").[132] Sante Fe owned more than 95% of Kirby's stock at the time of the merger.[133] Pursuant to Delaware's short-form merger statute, Sante Fe's board of directors adopted a resolution approving the merger of the two companies and the merger was subsequently consummated.[134] Dissatisfied with the merger terms, the former minority shareholders of Kirby brought a class action suit in federal district court.[135] The plaintiffs alleged that the merger itself, its statutory means of consummation and the merger price constituted a "device, scheme or artifice to defraud" in

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123 *Id.* at 10-11, 187 A.2d at 80.

124 *Id.* at 10, 187 A.2d at 80. The court ruled that because the minority shareholders' only claim involved the adequacy of the merger price, it was not necessary to hold that under no circumstances could a minority shareholder obtain equitable relief for fraud. *Id.* at 11, 187 A.2d at 80.

125 *Id.* at 11, 187 A.2d 80.

126 *Id.*

127 *See, e.g.*, Coyne v. Park & Tilford Distillers Corp., 38 Del. Ch. 514, 522, 154 A.2d 893, 898 (Del. 1959) (merger agreement providing for a cash payment to the minority shareholders was authorized by section 253); David J. Greene & Co. v. Schenley Indus., Inc., 281 A.2d 30, 36 (Del. Ch. 1971) (court of equity should not impede the orderly consummation of a merger absent a showing of fraud or overreaching); Bruce v. E.L. Bruce Co., 40 Del. Ch. 80, 82, 174 A.2d 29, 30 (Del. Ch. 1961) (absent fraud or a showing that the merger terms were so unfair as to shock the conscience of the court minority shareholders would not be allowed to block the merger). In the case of David J. Greene & Co. v. Dunhill Int'l, Inc., 249 A.2d 427, 436 (Del. ch. 1968), however, the Chancery Court did issue a preliminary injunction restraining the consummation of a merger on the grounds that the parent company could not adequately prove the entire fairness of the merger terms. *Id.*

128 *See, e.g.*, Green v. Sante Fe Indus., Inc., 553 F.2d 1283 (2d Cir. 1976), *rev'd*, 430 U.S. 462 (1977); Marshel v. AFW Fabric Corp., 553 F.2d 1277 (2d Cir. 1976), *vacated*, 429 U.S. 881 (1977).

129 *See id.* Rule 10b-5 is found at 17 C.F.R. § 240.10b-5(c) (1983).

130 430 U.S. 462 (1977).

131 *Id.* at 465.

132 *Id.*

133 *Id.*

134 *Id.* at 465-66. Pursuant to the merger agreement, Kirby's minority shareholders were paid $150 per share, $50 above the prevailing market price. *Id.* at 466. Kirby's assets, however, were estimated to be worth more than $600 per share. *Id.*

135 Green v. Sante Fe Indus., Inc., 391 F. Supp. 849, 850-51 (S.D.N.Y. 1975), *rev'd*, 553 F.2d 1283 (2d Cir. 1976), *rev'd*, 430 U.S. 462 (1977).

violation of Rule 10b-5.[136] Specifically, the plaintiffs alleged that the means for effecting the Sante Fe-Kirby merger operated as a fraud on Kirby's minority shareholders because the merger was consummated for the benefit of Sante Fe without any legitimate business purpose except to eliminate Kirby's minority shareholders.[137] The plaintiffs also alleged that the low value placed on their shares by Sante Fe was in itself fraud actionable under Rule 10b-5.[138] The district court granted the defendants' motion to dismiss,[139] stating that the reach of Rule 10b-5 did not prevent Delaware from providing majority shareholders with a means of eliminating a minority from the future affairs of a corporation.[140] Absent a showing of misrepresentation or lack of disclosure, the district court ruled that the plaintiffs had failed to state a cause of action under Rule 10b-5.[141] On appeal, the Second Circuit Court of Appeals reversed the district court's ruling.[142] The Circuit Court held that the plaintiffs had stated a cause of action under Rule 10b-5, because, according to the court, Rule 10b-5 encompasses "breaches of fiduciary duty by a majority against minority shareholders without any charge of misrepresentation or lack of disclosure."[143] On writ of certiorari, the Supreme Court reversed the court of appeals.[144]

The Supreme Court held that a transaction had to involve some element of deception or manipulation in order to constitute a violation of Rule 10b-5.[145] The Court found no deception in the matter before it because Sante Fe had made disclosure to the minority shareholders after the consummation of the merger as provided for in Delaware's short-form merger statute.[146] In addition, the Court found that Sante Fe had not employed any manipulative devices in effecting the merger.[147] The Court concluded, therefore, that plaintiffs' only remedy was to petition for an appraisal of their shares, as provided by Delaware law.[148] The Court reasoned that it would be inappropriate for the federal courts to interpret Rule 10b-5 as outlawing transactions that complied with state law and had been consummated without deception.[149] Significantly, however, the Court stated that,

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[136] *Id.* at 852.

[137] *Id.*

[138] *Id.*

[139] *Id.* at 856.

[140] *Id.* at 853.

[141] *Id.* at 854-55.

[142] Green v. Sante Fe Indus., Inc., 533 F.2d 1283, 1287 (2d Cir. 1976), *rev'd*, 430 U.S. 462 (1977).

[143] *Id.*

[144] Sante Fe Indus., Inc., v. Green, 430 U.S. 462, 480 (1977).

[145] *Id.* at 473-74.

[146] *Id.* at 474 n.14. Section 262 provides in pertinent part:

> If the merger or consolidation was approved pursuant to § 228 or § 253 [short-form merger provision] of this title, the surviving or resulting corporation, either before the effective date of the merger or consolidation or within 10 days thereafter, shall notify each of the stockholders entitled to appraisal rights of the effective date of the merger or consolidation and that appraisal rights are available for any or all of the shares of the constituent corporation, and shall include in such notice a copy of this section.

DEL. CODE ANN. tit. 8, § 262(d)(2) (1983).

[147] 430 U.S. at 476.

[148] *Id.* at 474.

[149] *Id.* at 479. The Court stated: "Absent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established state policies of corporate regulation would be overridden." *Id.*

although there may be a need for federal fiduciary standards to govern mergers, "those standards should not be supplied by judicial extension of section 10(b) and Rule 10b-5 to 'cover the corporate universe.' "[150] Consequently, while it did not approve of Delaware's treatment of freezeout mergers, the Court refused to allow the federal courts to deal with the problems created by freezeout mergers under Rule 10b-5.[151] *Sante Fe,* therefore, decisively threw the matter of freezeout mergers back to the states, setting the stage for the Delaware Supreme Court's landmark decision in *Singer v. Magnavox Co.*[152]

Singer involved a challenge to the cash merger of Magnavox Company ("Magnavox") and T.M.C. Development Corporation, a wholly-owned subsidiary of the North American Philips Corporation.[153] Philips had acquired 84% of Magnavox through a cash tender offer.[154] Dissatisfied with the terms of the merger, the minority shareholders brought a class action suit in the Delaware Court of Chancery alleging that the merger was fraudulent because its only purpose was to eliminate the minority shareholders of Magnavox at a grossly inadequate price.[155] The Court of Chancery granted the defendants' motion to dismiss, ruling that the merger was not fraudulent merely because it was accomplished for the sole purpose of eliminating Magnavox's minority shareholders.[156] The Chancery Court stated that, in any event, the plaintiffs' remedy was to seek an appraisal of their shares if they were dissatisfied with the merger price.[157] The plaintiffs appealed this ruling to the state Supreme Court.[158]

The Delaware Supreme Court reversed.[159] The court began its opinion by articulating the obligations owed by a controlling shareholder in the context of a long-form merger.[160] The court explained that the controlling shareholder in a freezeout merger owes a high standard of fiduciary fairness to minority shareholders, which is not always satisfied by full compliance with the Delaware merger statutes.[161] The court stated that despite statutory authorization for the merger and the defendants' compliance with the statute's terms, the transaction was not insulated from review by a court of equity.[162] According to the *Singer* court, Delaware courts would not be indifferent to mergers

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[150] *Id.* at 479-80. In support of this statement, the Court cited Professor Cary's article attacking Delaware's corporate jurisprudence and urging the adoption of new laws incorporating federal fiduciary standards. *Id.* at 480 n.17 (citing Cary, *Federalism and Corporate Law: Reflections Upon Delaware,* 83 YALE L.J. 663, 700 (1974)).

[151] *See* 430 U.S. at 479-80.

[152] 380 A.2d 969 (Del. 1977).

[153] *Id.* at 971.

[154] *Id.*

[155] *Id.* at 972.

[156] Singer v. Magnavox Co., 367 A.2d 1349, 1358 (Del. Ch. 1976).

[157] *Id.* at 1362.

[158] Singer v. Magnavox Co., 380 A.2d 969 (Del. 1977).

[159] *Id.* at 980. *Singer* was decided shortly after the Supreme Court decided *Santa Fe. Santa Fe's* suggestion of possible federal corporate legislation, see *supra* note 149-50 and accompanying text, may have influenced the *Singer* court's decision to establish a business purpose test for minority shareholder protection. The *Singer* court stated: "*Santa Fe* is a current confirmation by the Supreme Court of the responsibility of a state to govern the internal affairs of corporate life." 380 A.2d at 976 n.6.

[160] *Id.* at 972-73.

[161] *Id.* at 975.

[162] *Id.* The court held that the merger was assailable because " 'inequitable action does not become permissible simply because it is legally possible.' " *Id.* (quoting Schnell v. Chris-Craft Industries, Inc., 285 A.2d 437, 439 (Del. 1971)).

effected solely for the purpose of eliminating minority shareholders from further equity participation in a corporation, despite earlier case law holding that minority shareholders take their stock with constructive notice that Delaware's merger statutes provide for majority shareholder action in accomplishing mergers.[163] The court then articulated a two pronged test for determining the validity of freezeout mergers.[164] First, the court held that in a parent-subsidiary merger, the majority shareholder must prove a valid business purpose for effecting a merger in order to satisfy Delaware's high fiduciary standards.[165] Second, even if the defendants meet this burden, the court held that the lower courts must also scrutinize all aspects of a merger for compliance with *Sterling's* mandate of entire fairness.[166]

While the business purpose test announced in *Singer* clearly marked a shift in Delaware's treatment of freezeout mergers, the court explicitly declined to specify whose business purpose would be relevant in the examination of a merger challenge.[167] More importantly, the court did not articulate any criteria for evaluating what constituted a valid business purpose. The *Singer* court also failed to elaborate on the concept of entire fairness which was originally developed in *Sterling*.[168] The Delaware Supreme Court's decision in *Tanzer v. International General Industries, Inc.*[169] provided partial answers to some of the issues left unresolved by *Singer*.[170]

One month after the *Singer* decision was handed down, the Delaware Supreme Court decided the *Tanzer* case. *Tanzer* involved a challenge to a proposed long-form merger of the Kliklok Corporation ("Kliklok") and International General Industries ("IGI").[171] At the time of the proposed merger, IGI owned 81% of Kliklok's outstanding common stock.[172] The Tanzers, owners of Kliklok stock, brought suit in the Court of Chancery seeking a preliminary injunction to prevent the merger on the ground that the sole purpose of the merger was to serve the interests of the majority shareholder.[173] The Chancery Court granted the defendants' motion for summary judgment and the plaintiffs appealed.[174]

On appeal, the Delaware Supreme Court affirmed the Chancery Court's decision,[175] ruling that the *Singer* business purpose requirement could be satisfied when a merger was effected solely to advance the business purposes of a parent company.[176] The court found

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[163] 380 A.2d at 979. The *Singer* court distinguished *Havender, Bruce, Stauffer* and *Schenley* as factually different from the instant case. *Id.* at 978-79. For a discussion of *Havender* and *Stauffer* see *supra* notes 91-101 and 113-36 and accompanying text. The *Singer* court stated that none of these cases involved straight "cash-for-stock" mergers in which the only purpose for the merger was the elimination of the subsidiary's minority shareholders. 380 A.2d at 987.

[164] *Id.* at 980.

[165] *Id.*

[166] *Id.*

[167] *Id.* n.11.

[168] For a discussion of the *Sterling* test, see *supra* notes 102-12 and accompanying text.

[169] 379 A.2d 1121 (Del. 1977).

[170] *Id.* at 1124.

[171] *Id.* at 1122.

[172] *Id.*

[173] Tanzer v. International Gen. Indus., Inc., 402 A.2d 382, 384 (Del. Ch. 1979) (Chancery Court on remand describing unreported procedural history of the case).

[174] *Id.* at 395.

[175] Tanzer v. International Gen. Indus., Inc., 379 A.2d 1121, 1125 (Del. 1977).

[176] *Id.* at 1124. The court reasoned that IGI, as a stockholder of Kliklok, had a right to "look to its own corporate concerns in determining how to conduct the latter's affairs, including a decision to cause it to merge." *Id.* The court cited the *Ringling* rule that a stockholder may vote in his own

that IGI had satisfied the *Singer* requirement by demonstrating that its merger with Kliklok facilitated its own long-term debt financing.[177] As in *Singer*, the *Tanzer* court stated that the establishment of a "bona fide" business purpose would not necessarily discharge the parent company's fiduciary obligations.[178] Employing *Singer's* two pronged test, the *Tanzer* court held that even after proving a valid business purpose for effecting the proposed merger, the parent company had to establish that the merger terms were entirely fair to the subsidiary's minority shareholders.[179] Although the *Tanzer* court affirmed the Chancellor's ruling denying injunctive relief, the court remanded the case because it found that the plaintiffs were still entitled to a "fairness hearing under *Singer*."[180]

While *Tanzer* answered some of the questions left open by *Singer*, the decision significantly weakened the potential minority shareholder protection offered by the *Singer* business purpose test because it upheld a merger effected solely for the business purposes of a parent corporation.[181] Additionally, the *Tanzer* decision, like *Singer*, failed to provide the lower courts with any definite guidelines for determining what would constitute a valid business purpose for effecting freezeout mergers in the future.[182] The lower courts were left to decide what constituted a valid business purpose on a case by case basis, and presumably would allow corporations to justify freezeout mergers by advancing purposes no more compelling than the purpose approved in *Tanzer*.[183] Consequently, because the lower courts were deciding merger challenges on a case by case base without clear guidelines as to what constituted a valid business purpose, the Chancery Court decisions were often conflicting and somewhat arbitrary.[184] The doctrinal confusion that followed *Singer* and *Tanzer* culminated in *Weinberger v. UOP, Inc.*.[185]

self-interest as supporting this conclusion. *Id.* (citing Ringling Bros. Barnum & Bailey Com. Shows. v. Ringling, 29 Del. Ch. 610, 622, 53 A.2d 441, 447 (Del. 1947)).

[177] 379 A.2d at 1124. The *Tanzer* court emphasized that while a merger may be effected solely for the business purposes of the parent company, the purpose advanced by the parent company had to be "bona fide" and not a "subterfuge" created to eliminate the minority shareholders. *Id.*

[178] *Id.* at 1125.

[179] *Id.*

[180] *Id.*

[181] *See id.* at 1124-25.

[182] *See id.* at 1124.

[183] *See* Brudney & Chirelstein, *supra* note 9, at 1371. Brudney & Chirelstein believe that it would be impossible to deny that a commercial goal was wholly lacking in any parent-subsidiary merger. *Id.* The possibility of economic gain for the parent company always exists because the combined overall value of the enterprises may become greater than the value of the firms as separate entities, prior to the merger. *Id.* Brudney & Chirelstein maintain that even if these "synergistic gains" are minimal, management still would have other economic justifications for accomplishing a parent-subsidiary merger. *Id.* A parent-subsidiary merger would reduce the difficulty of establishing fair intercompany dealings in allocating overhead costs, tax benefits and growth opportunities. *Id.*

[184] *See* Young v. Valhi, Inc., 382 A.2d 1372, 1378 (Del. Ch. 1978). The Chancery Court's decision in Young v. Valhi, Inc., demonstrates the difficulty the lower courts experienced in applying the *Singer* business purpose test. *Id.* In *Young*, the Chancery Court enjoined a parent-subsidiary merger because it found that the "basic purpose" of the merger was to eliminate the minority shareholders of the subsidiary. *Id.* at 1378. The court rejected the parent company's contentions that the merger would lead to tax savings for the parent company and avoid possible conflicts of interest. *Id.* at 1377. The court stated that the tax savings could be achieved by other means and that the conflicts were "somewhat contrived." *Id.* There is little doubt that the merger in *Young* advanced the economic interests of the parent company and that a "basic purpose" of the parent company in *Tanzer* was to eliminate the minority shareholders of the subsidiary. The distinctions between the purposes of these two mergers appear to be largely metaphysical.

[185] 457 A.2d 701 (Del. 1983).

II. The *Weinberger* Decision

In a unaminous decision, the Delaware Supreme Court ruled that the business purpose requirement announced in *Singer* was "no longer the law of Delaware."[186] The court ruled that the entire fairness prong of the *Singer* test was the only appropriate standard of review for shareholder challenges to freezeout mergers.[187] According to the *Weinberger* court, the concept of entire fairness as first announced in the *Sterling* case, was comprised of two "basic aspects:" fair dealing and fair price.[188] The Delaware Supreme Court reversed the Chancellor's findings concerning the fair dealing aspects of the case, stating that the Signal-UOP merger did not satisfy "any reasonable concept of fair dealing."[189] The *Weinberger* court also held that the Delaware courts were no longer restricted exclusively to the use of the Delaware block, weighted average valuation method in determining fair price.[190] The court ruled that the Delaware courts were free to use modern stock valuation techniques for the purpose of determining fair price under the entire fairness test and for the purpose of determining fair value in an appraisal proceeding.[191] Although the *Weinberger* court reversed the Chancery Court regarding its findings of fair dealing and its strict application of the Delaware block valuation method, the Delaware Supreme Court refused to set aside the "long completed transaction."[192] Instead, the court remanded the case to the Chancery Court for a determination concerning a possible damage award.[193]

The *Weinberger* court began its review of the Signal-UOP merger by articulating the appropriate allocation of the burden of proof.[194] According to the court, in order to challenge a merger under the *Sterling* entire fairness standard, minority shareholders must allege specific acts of "fraud, misrepresentation, or other items of misconduct."[195] Once the plaintiff has invoked the *Sterling* entire fairness obligation, the court stated that the parent company must prove, by a preponderance of the evidence, that the merger terms were entirely fair to the minority shareholders.[196] The court stated, however, that the parent company could shift the burden of proof entirely back to the minority shareholders if it could demonstrate that the terms of the merger were approved by an informed vote of a majority of the minority shareholders.[197] In order to prove that the minority shareholder vote was "informed," the court stated that the parent company had to demonstrate that it completely disclosed all the material facts relevant to the transaction to the minority shareholders.[198]

Turning to a consideration of the facts before it, the *Weinberger* court found that the vote of UOP's minority shareholders approving the terms of the merger was ineffective, because it was not informed.[199] The court based this finding on the fact that the results of

[186] *Id.* at 704.
[187] *Id.* at 711.
[188] *Id.*
[189] *Id.* at 712.
[190] *Id.*
[191] *Id.* at 712-13.
[192] *Id.* at 714.
[193] *Id.*
[194] *Id.* at 703.
[195] *Id.*
[196] *Id.*
[197] *Id.*
[198] *Id.*
[199] *Id.*

the feasibility study prepared by two Signal executives who also served on UOP's board of directors, were not disclosed to UOP's minority shareholders.[200] This study indicated that it would be to Signal's advantage to acquire the remainder of UOP's publicly held shares at any price up to $24 per share.[201] Because of this inadequate disclosure, the court ruled that the burden of proof remained Signal's and that in order to prevail, Signal had to prove that the terms of the merger were entirely fair to UOP's minority shareholders.[202] The court then moved to a discussion of whether the transaction in *Weinberger* was "entirely fair" under the standard developed in *Sterling*.[203]

According to the *Weinberger* court, although the concept of entire fairness is comprised of two basic components, fair dealing and fair price, these components should not be considered in isolation in considering the validity of a corporate merger.[204] The court explained that while proof of both fair dealing and fair price would be necessary to satisfy the entire fairness standard, the concept of entire fairness required that a merger also be reviewed in light of the total circumstances surrounding the transaction.[205] The court then discussed the various aspects of a merger transaction that should be examined under each component of the entire fairness standard.[206] The test for fair dealing, the court stated, includes considerations of "when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained."[207] The court, also stated that fair dealing requires "complete candor" in disclosing information to the shareholders and directors of the subsidiary.[208]

Applying this standard to the facts of *Weinberger*, the court stated that Signal's directors sitting on UOP's board violated this duty of complete candor when they failed to disclose the results of the feasibility study.[209] The *Weinberger* court found that Signal breached its duty of fair dealing with UOP's minority shareholders in several other instances as well.[210] The court objected to the serious time constraints Signal imposed on UOP's management when the merger proposal was first presented.[211] In addition, the court found that the negotitions that preceded the merger fell far short of the ideal for arm's-length bargaining.[212] The court observed that UOP's president's only attempt at negotiating a higher merger price was to convey to Signal the view of UOP's outside directors that, as to the $20-$21 price range proposed by Signal, the merger price would

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[200] *Id.* at 709.

[201] *Id.* at 705. *See supra* notes 26-27 and accompanying text.

[202] 457 A.2d at 703.

[203] *Id.* at 710.

[204] *Id.* at 711.

[205] *Id.*

[306] *Id.*

[207] *Id.* at 711.

[208] *Id.* at 711. The court stated that the requirement of complete candor is another way of articulating that Signal's directors serving on UOP's board owed UOP and its shareholders an "uncompromising duty of loyalty." *Id.* at 710.

[209] *Id.* at 711-12. The court also found that the minority shareholders were not informed about the hurried method in which Lehman Brothers prepared the fairness opinion concerning the merger price. *Id.* at 712.

[210] *Id.* at 710-12.

[211] *Id.* at 711. The court was careful to note, however, that the time constraints, standing alone, would not necessarily be indicative of a lack of fairness by a majority stockholder. *Id. See supra* notes 30-31 and accompanying text.

[212] 457 A.2d at 711.

have to be $21 per share.[213] These negotiations were characterized by the court as being "modest at best."[214] The court also objected to the level of participation by the Signal directors sitting on UOP's board at the UOP board meeting concerning the merger proposal.[215] The court found that, although the Signal directors abstained from voting, they actively participated in other aspects of the meeting.[216] Taking all of these factors into consideration, the court found that the circumstances surrounding the Signal-UOP merger did not satisfy "any reasonable concept of fair dealing."[217]

Significantly, the court articulated two methods by which Signal could have established "strong evidence" of fairness in the instant case. First, the court stated that if Signal had engaged in arm's-length negotiations with a committee comprised of UOP's outside directors, the result of the case "could have been entirely different."[218] Second, the court noted that Signal could have achieved the same result if Signal's directors serving on UOP's board had totally abstained from any participation in the transaction.[219] In the absence of an independent negotiating structure or proof of the total abstention of the subsidiary's interested directors in the matter, the court found that Signal was required to prove that it had discharged its fiduciary duty "in light of what is best for both companies."[220] The court concluded that on the facts before it, Signal had not met this obligation.[221]

Turning to the price component of the entire fairness standard, the *Weinberger* court began its analysis by articulating what it meant by "fair price."[222] The court explained that fair price relates to the economic and financial considerations of the merger.[223] In determining whether a merger price is fair, according to the court, "assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock" must be considered.[224] Moreover, the court held that in determining the value of a corporation's stock, the Delaware courts were no longer restricted to the use of the "Delaware block" weighted average valuation approach, but

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[213] *Id.* The court stated that UOP's president, James V. Crawford, never really "talked price with Signal." *Id.*

[214] *Id.* The court noted that UOP had to alter the original draft of the proxy statement that was to be sent to UOP's minority shareholders. *Id.* at 708. The proxy statement actually sent to UOP's minority shareholders stated that "the price was determined after discussions between James v. Crawford, a director of Signal and Chief Executive Officer of UOP, and officers of Signal which took place during meetings of February 28, 1978 and in the course of several subsequent telephone conversations." *Id.* In the original draft of the proxy statement the word "negotiations" had been used rather than "discussions." *Id.* When the Securities and Exchange Commission began investigating the details of these "negotiations," however, the term was deleted and the word "discussions" was substituted. *Id.*

[215] *Id.* at 710.

[216] *Id.* at 707.

[217] *Id.* at 712.

[218] *Id.* at 709 n.7.

[219] *Id.* at 710-11.

[220] *Id.* The court stated that Delaware case law had previously established the principle that directors standing on both sides of a transaction are required to demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain. *Id.* at 710. *See* Warshaw v. Calhoun, 43 Del. Ch. 148, 156, 221 A.2d 487, 492 (Del. 1966). Gottlieb v. Heyden Chem. Corp., 33 Del. Ch. 177, 178-79, 91 A.2d 57, 57-58 (Del. 1952).

[221] 457 A.2d at 711.

[222] *Id.*

[223] *Id.* at 711.

[224] *Id.*

instead could also take into account other generally accepted stock valuation techniques.[225] This decision, the court continued, was in keeping with the legislative intent expressed in a then recent amendment to the Delaware corporation law, section 262(h), which provided that "all relevant factors" should be taken into account in valuing the shares of a dissenting shareholder.[226] The court did not examine the fairness of the merger price under the new standards it had announced, deciding that the issue was to be decided by the Chancellor on remand.[227]

After determining that Signal had failed to prove the entire fairness of the transaction, the court turned to a discussion of the appropriate remedy to be applied in the instant case. The court stated that in most instances the financial remedy available to minority shareholders in freezeout merger challenges would be appraisal.[228] In future appraisal proceedings the court noted that minority shareholders would be able to receive the fair value of their stock as determined by modern valuation techniques.[229] The court recognized, however, that such a monetary remedy may not be adequate in certain cases involving "fraud, misrepresentation, self-dealing, deliberate waste of corporate assets or gross and palpable overreaching."[230] The court stated that in these circumstances, "the Chancellor's powers are complete to fashion any form of equitable and monetary relief as may be appropriate, including rescissory damages."[231] Considering the matter before it,

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[225] *Id.* The court was careful not to adopt or suggest any particular valuation technique, preferring to leave the selection of valuation techniques to the parties involved in the dispute. *Id.*

[226] *Id.* at 713-14. Section 262(h) states, in pertinent part:

> After determining the stockholder entitled to an appraisal, the 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, together with a fair rate of interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors. . . .

DEL. CODE ANN. tit. 8, § 262(h) (1983). The court pointed out that the first references to "fair value" appeared in a 1976 amendment to section 262(f). 457 A.2d at 713-14. The court also noted that in that 1981 amendment to section 262 the notion of fair value was repeatedly emphasized and the language instructing the courts to "take into account all relevant factors" appeared in section 262(h). *Id.* at 714.

[227] 457 A.2d at 714.

[228] *Id.* at 714-15. The court stated "[t]hus we return to the well established principles of *Stauffer v. Standard Brands*, . . . and *David J. Greene & Co. v. Schenley Industries, Inc.*, . . . , mandating a stockholder's recourse to the basic remedy of an appraisal." *Id.* at 715 (citations omitted).

[229] *Id.* at 712-713.

[230] *Id.* at 714.

[231] *Id.* In *Weinberger*, the plaintiffs had not sought an appraisal under Section 262. *Id.* The plaintiffs had instead sought rescissory damages of the type considered by the Delaware Supreme Court in Lynch v. Vickers Energy Corp., 429 A.2d 497, 505-06 (Del. 1981). In *Lynch*, a parent company had acquired the majority interest in a controlled subsidiary through a misleading tender offer solicitation. *Id.* at 499. The price of oil, the principal asset of the subsidiary, rose rapidly during the period in which fairness of the tender offer solicitation was being litigated. *Id.* at 501. The Delaware Supreme Court awarded "rescissory damages," which allowed the former minority shareholders to reap the benefits of the increase in oil prices which occurred while the case was being litigated. *Id.* This result was accomplished by valuing the plaintiffs' stock at the date of the appeal rather than at the date of the merger. *Id.*

The *Weinberger* court seemed to indicate that minority shareholders generally would not be entitled to realize windfall profits merely because a majority shareholder had breached some fiduciary duty in connection with the merger. *See* 457 A.2d at 714. The court left open the possibility that rescissory damages could be awarded in the instant case, however, if the Chancellor, on remand, considered them susceptible of proof and a "remedy appropriate to all the issues of fairness before that even though Signal had not satisfied the entire fairness test, the merger should not be set aside.[232] The court stated that "this long completed transaction is too involved to undo."[233] Remanding the case to the lower court, the court directed the Chancellor to decide the amount of monetary damages to be awarded, if any, based upon entire fairness standards of fair dealing and fair price.[234]

Finally, the court addressed the *Singer* business purpose doctrine. The *Weinberger* court concluded that the business purpose doctrine articulated in *Singer* should be overruled.[235] The court explained that given the "expanded" appraisal remedy now available to dissenting shareholders through the use of modern valuation techniques and the broad powers of the Chancellor to fashion equitable relief appropriate to the particular circumstances, no "additional meaningful protection" would be afforded to minority shareholders by the application of the *Singer* business purpose requirement.[236] The *Weinberger* court observed that in the proceedings below, the Chancellor had "clearly circumscribed the thrust and effect of *Singer*" by ruling that Signal's desire to make an investment of its cash reserves constituted a valid business purpose for effecting the merger.[237] The *Weinberger* court admitted that the Chancellor's decision demonstrated that the business purpose doctrine could, in effect, be interpreted out of existence.[238] Consequently, with little else in the way of explanation, the *Weinberger* court eliminated the *Singer* business purpose test from Delaware corporation law.[239]

III. The Rationale of *Weinberger v. UOP, Inc.*

The *Weinberger* decision represents a significant improvement in Delaware's treatment of freezeout merger challenges. In *Weinberger*, the Delaware Supreme Court eliminated the *Singer* business purpose test from Delaware law[240] and established the *Sterling* entire fairness test as the sole standard of review for freezeout merger challenges.[241] This section of the casenote analyzes the different aspects of the Delaware Supreme Court's decision in *Weinberger*, beginning with an analysis of the *Weinberger* court's elimination of the *Singer* business purpose test.[242] Next, this section of the casenote examines the *Weinberger* court's decision to establish the *Sterling* entire fairness test as the sole standard of review for freezeout merger challenges.[243] The two components of the concept of

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him." *Id.* Because the Signal-UOP merger was conditioned on appproval by a majority of the minority shareholders and approval may not have been secured if Signal had made full disclosure, the Delaware Supreme Court left it to the trial court to decide, on remand, whether the minority interest in UOP should be valued as of a constructive rescission date rather than the date of the merger. *Id.*

[232] 457 A.2d at 714.

[233] *Id.*

[234] *Id.*

[235] *Id.* at 715.

[236] *Id.*

[237] *Id.*

[238] *Id.* (citing Weiss, *The Law of Take Out Mergers: A Historical Perspective,* 56 N.Y.U.L. Rev. 624, 671 n.300 (1981)).

[239] 457 A.2d at 715.

[240] *Id.* at 715.

[241] *Id.* at 710-11.

[242] *See infra* notes 246-99 and accompanying text.

[243] *See infra* notes 300-50 and accompanying text.

entire fairness, fair dealing[244] and fair price,[245] are examined separately in this section of the analysis. This casenote submits that the *Weinberger* decision improves Delaware merger law by enhancing the quality of minority shareholder protection and by eliminating the uncertainty which surrounded the *Singer* business purpose test.

A. *The Business Purpose Doctrine*

The *Weinberger* court's decision to overrule the business purpose requirement represents a significant improvement in the Delaware judiciary's treatment of freezeout merger challenges. The business purpose doctrine originated in 1977 in the case of *Singer v. Magnavox Co.*[246] when the Delaware Supreme Court held that the minority shareholders bringing the merger challenge had stated a cause of action by alleging that the majority shareholder had breached its fiduciary duty by effecting the merger for the sole purpose of eliminating the minority shareholders from the corporation.[247] By so holding, the *Singer* court, in effect, required majority shareholders to demonstrate in future merger challenges that the merger in question was effected for business reasons other than the elimination of the minority shareholders from the entity.[248] In the subsequent case of *Tanzer v. International General Industries, Inc.*,[249] the Delaware Supreme Court limited the scope of the business purpose requirement by holding that the business reasons of a parent company satisfied the business purpose requirement announced in *Singer.*[250]

It is submitted that the business purpose requirement was an inappropriate standard of review for challenges to freezeout mergers. This section of the casenote first examines the business purpose doctrine as developed by the Delaware Supreme Court in *Singer* and *Tanzer.*[251] Next, this section of the casenote analyzes the effectiveness of the business purpose doctrine in achieving minority shareholder protection in light of the court's holding in *Tanzer.*[252] Finally, this section of the casenote demonstrates that the *Weinberger* court's decision to eliminate the *Singer* business purpose requirement clarifies Delaware merger law and improves the Delaware judiciary's treatment of minority shareholder interests.[253]

In *Singer*, the Delaware Supreme Court established a two pronged standard of review comprised of a business purpose requirement and an entire fairness test.[254] The entire fairness prong of this standard was first established in 1952 in the case of *Sterling v. Mayflower Hotel Corp.*.[255] Subsequent to *Sterling*, however, the Delaware courts had not consistently required majority shareholders to establish the entire fairness of challenged mergers.[256] The two pronged standard of review announced by the *Singer* court marked a

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[244] *See infra* notes 300-37 and accompanying text.

[245] *See infra* notes 338-50 and accompanying text.

[246] 380 A.2d 969 (Del. 1977).

[247] *Id.* at 980.

[248] *See id.*

[249] 379 A.2d 1121 (Del. 1977).

[250] *Id.* at 1124.

[251] *See infra* notes 254-83 and accompanying text.

[252] *See infra* notes 284-93 and accompanying text.

[253] *See infra* notes 294-99 and accompanying text.

[254] 380 A.2d at 980. *See supra* notes 159-68 and accompanying text.

[255] 33 Del. Ch. 293, 298, 93 A.2d 107, 110 (Del. 1952).

[256] *See, e.g.*, Stauffer v. Standard Brands, Inc., 41 Del. Ch. 7, 187 A.2d 78 (Del. 1962); Coyne v. Park & Tilford distillers Corp., 38 Del. Ch. 514, 154 A.2d 893 (Del. 1959); David J. Greene & Co. v. Schenley Indus., Inc., 281 A.2d 30 (Del. Ch. 1971); Bruce v. E.L. Bruce Co., 40 Del. Ch. 80, 174 A.2d 29 (Del. Ch. 1961).

shift from Delaware's previous treatment of freezeout mergers. Prior to *Singer,* the Delaware courts had relied almost exclusively on the statutory appraisal remedy for the protection of minority shareholder interests.[257] Before 1977, the Delaware courts had been reluctant to enjoin mergers that complied with the relevant Delaware merger statutes.[258] The *Singer* court's adoption of a business purpose requirement and its revival of the *Sterling* entire fairness test provided minority shareholders with the two possible grounds on which to seek an injunction to set aside a freezeout merger.[259] Previously, Delaware courts had held that, absent a showing of fraud or gross overreaching, minority shareholders would be restricted to the statutory appraisal remedy.[260] While the entire fairness prong of the *Singer* standard of review had roots in prior Delaware law, the business purpose requirement announced by the *Singer* court plainly seemed to be inconsistent with earlier Delaware merger decisions. Previous Delaware case law had not inquired into the business purposes behind mergers that complied with Delaware's merger statutes.[261]

By establishing the business purpose requirement, the *Singer* court opened the door to the possibility that equitable relief would be granted in cases where a parent company could not advance sufficient business reasons to justify a decision to merge.[262] In support of its adoption of the business purpose requirement, the *Singer* court stated that an investor has a legitimate interest in the form, as well as the value, of his investment.[263] This statement appears to be inconsistent with the court's earlier decisions in *Federal United Corp. v. Havender*[264] and *Stauffer v. Standard Brands, Inc.*[265] in which the court found that minority shareholders only had the right to receive the cash value of their shares in an appraisal proceeding if they were dissatisfied with the merger terms.[266]

The *Singer* court applied a narrow reading to the holding in *Havender,* stating that "*Havender* stands for the proposition that a merger must be 'fair and equitable in the circumstances of the case' in order to withstand the veto of a dissenting shareholder."[267] The *Singer* court's characterization of Havender ignored the overrall thrust of the opinion which stressed the absence of limits on the majority shareholder's power to merge.[268] The *Havender* court did not suggest the possibility of equitable relief if a merger was not "fair and equitable," but instead spoke only of the statutory appraisal remedy.[269] In *Stauffer,* the Delaware Supreme Court ruled that absent a showing of fraud or overreaching, equitable relief would not be appropriate.[270] In its review of the short-form merger in

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[257] *See* cases cited *supra* note 256. *See supra* notes 92-126 and accompanying text.

[258] *See supra* notes 92-126 and accompanying text.

[259] 380 A.2d at 980.

[260] *See supra* note 256.

[261] *See supra* notes 92-126 and accompanying text.

[262] 380 A.2d at 980.

[263] *Id.* at 977-78.

[264] 24 Del. Ch. 318, 11 A.2d 331 (Del. 1940).

[265] 41 Del. Ch. 7, 187 A.2d 78 (Del. 1962).

[266] *See id.* at 11, 187 A.2d at 80; Federal United Corp. v. Havender, 24 Del. Ch. at 334-35, 11 A.2d at 339.

[267] 380 A.2d at 979. The court also attempted to distinguish *Havender* on the ground that cash mergers were not authorized when *Havender* was decided. *Id.*

[268] *See* 24 Del. Ch. at 330-31, 11 A.2d at 337.

[269] *Id.* at 334-35, 11 A.2d at 339.

[270] 41 Del. Ch. at 10, 187 A.2d at 80.

question, the *Stauffer* court had stated that "the very purpose of the statute [section 253] is to provide the parent corporation with a means of eliminating the minority shareholder's interest in the enterprise."[271] The *Singer* court stated that it did not read the *Stauffer* decision as approving mergers effected for the sole purpose of freezing out the minority shareholders of a controlled subsidiary.[272] Despite the *Singer* court's efforts to reconcile the business purpose requirement with prior case law, the court's decision to allow minority shareholders to challenge a merger on the ground of improper purpose was inconsistent with previous Delaware case law which relegated minority shareholders exclusively to the statutory appraisal remedy.[273]

In addition to the difficulties the court experienced explaining the inconsistencies surrounding the business purpose requirement, the *Singer* court was also unable to establish a clear conceptual foundation for the business purpose test. The *Singer* court attempted to base the business purpose requirement on the fiduciary obligations previously imposed by Delaware courts on majority shareholders.[274] In support of its conclusion that a "§ 251 merger, made for the sole purpose of freezing out minority shareholders, is an abuse of the corporate process,"[275] the *Singer* court cited a number of decisions that invalidated actions taken by controlling shareholders or corporate officers designed to perpetuate themselves in office.[276] The Court reasoned that if the use of corporate power to perpetuate control violated the fiduciary duties owed by majority shareholders, then "[b]y analogy, if not *a fortiori*, use of corporate power solely to eliminate the minority is a violation of that duty."[277] In using this analogy, however, the *Singer* court failed to take into account the significant factual distinctions between freezeout merger cases and cases involving perpetuation of control by majority shareholders.[278]

The use of corporate power to perpetuate control is thought to be objectionable because the forces of efficient market allocation of control are frustrated.[279] One current theory is that management should not be allowed to block a takeover solely to retain control, because in many instances, takeovers facilitate the replacement of inefficient management.[280] When management eliminates a minority interest in a subsidiary corporation in a freezeout merger, however, this transaction has nothing to do with a management tactic to retain control. Indeed, the very fact that the majority shareholder is able to

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[271] *Id.* at 10-11, 187 A.2d at 80.

[272] 380 A.2d at 978-79. The *Singer* court implicitly acknowledged the conflict between its holding and the *Stauffer* decision, stating "[a]ny statement in *Stauffer* inconsistent herewith is held inapplicable to a § 251 merger." *Id.* at 980.

[273] *See* Stauffer v. Standard Brands, Inc., 41 Del. Ch. at 11, 187 A.2d at 80; Federal United Corp. v. Havender, 24 Del. Ch. at 334-35, 11 A.2d at 339.

[274] *See* 380 A.2d at 975-78.

[275] *Id.* at 980.

[276] *Id.* at 979 (citing Schnell v. Chris-Craft Indus,. Inc., 285 A.2d 437 (Del. 1971); Condec Corp. v. Lunkenheimer Co., 43 Del. Ch. 353, 230 A.2d 769 (Del. Ch. 1967); Bennett v. Breuil Petroleum Corp., 34 Del. Ch. 6, 99 A.2d 236 (Del. Ch. 1953)).

[277] 380 A.2d at 980.

[278] *See id.* at 979-80.

[279] *See* Gilson, *A Structural Approach to Corporations: The Case Against Defensive Tactics on Tender Offers*, 33 STAN. L. REV. 819, 841-42 (1981); Weiss, *Disclosure and Corporate Accountability*, 34 BUS. LAW. 575, 576-78 (1979).

[280] *See* Gilson, *supra* note 279, at 841-42. *But see* Lipton, *Takeover Bids in The Target's Boardroom*, 35 BUS. LAW. 101, 106-13 (1979).

effectuate the merger demonstrates that the minority shareholders were not a threat to the majority's control of the subsidiary. Because the analogy drawn by the *Singer* court was not parallel,[281] the conceptual basis of the business purpose requirement was suspect in the context of freezeout mergers. Despite the court's efforts, therefore, the business purpose requirement and the implicit minority shareholder veto power granted by its enactment were inconsistent with prior Delaware merger law.[282]

In addition to the questionable basis of the business purpose requirement, the *Singer* court did not fully explain what business reasons would satisfy the requirement. Because it was ruling on a motion to dismiss, the court only held that the plaintiffs had stated a cause of action by alleging that the parent company had effected the merger for the sole purpose of eliminating the subsidiary's minority shareholders.[283] The court's decision in the subsequent case of *Tanzer v. International General Industries, Inc.* created substantial uncertainty as to what circumstances would merit equitable relief under the business purpose requirement. In *Tanzer,* the court allowed the business purpose of a parent company to suffice as justification for accomplishing a merger.[284] Specifically, the court held that the parent company had satisfied the business purpose requirement by demonstrating that the merger with its subsidiary facilitated its own long-term debt financing.[285] In so ruling, the court significantly decreased the probability that the *Singer* business purpose test could be used successfully to enjoin freezeout mergers. After *Tanzer,* therefore, it seemed that a parent company would almost certainly be able to justify a merger with a subsidiary by showing it received some financial benefit as a result of the transaction.[286] For example, the business purpose approved in *Tanzer,* that the merger was accomplished to facilitate the parent company's long-term debt financing, certainly seemed to be less than compelling.[287] Even though the *Singer* court apparently devised the business purpose test in order to protect minority shareholder interests in the context of freezeout mergers,[288] the business purpose requirement, as weakened by the court's holding in *Tanzer,* did not afford minority shareholders any real protection from unfair treatment by majority shareholders. Although, in theory, the business purpose requirement represented a possible ground on which minority shareholders could win injunctions, plaintiffs were largely unsuccessful in enjoining mergers on improper purpose grounds.[289]

While the overall effect of the *Tanzer* decision significantly decreased the probability that the business purpose requirement would be used successfully as a grounds for equitable relief, parent companies planning mergers with subsidiaries still had to be

[281] *See supra* notes 274-78 and accompanying text.

[282] *See supra* notes 92-126 and accompanying text. In *Weinberger*, the Delaware Supreme Court admitted that "[t]he requirement of a business purpose is new to our law of mergers and was a departure from prior case law." 457 A.2d at 715.

[283] 380 A.2d at 980.

[284] *Tanzer*, 379 A.2d at 1124.

[285] *Id.*

[286] *See* Brudney & Chirelstein, *supra* note 9, at 1371. Brudney & Chirelstein maintain that it would be impossible to deny that a commercial goal was wholly lacking in any parent-subsidiary merger. *Id.*

[287] 379 A.2d at 1124.

[288] *See* Weiss, *supra* note 2, at 657-58.

[289] *See, e.g., Tanzer*, 379 A.2d 1121 (Del. 1977). Weinberger v. UOP, Inc., 426 A.2d 1333 (Del. Ch. 1981); The Chancery Court's decision in *Weinberger* illustrates the ineffectiveness of the business purpose requirement as a grounds for equitable relief. 426 A.2d 1333 (Del. Ch. 1981). The Chancellor held that Signal's desire to make a favorable cash investment was a proper purpose for effecting the Signal-UOP merger. *Id.* at 1350.

concerned that, in the event of a minority shareholder challenge, their purposes for effecting the merger might be considered improper by a Delaware court. The *Tanzer* court emphasized that while parent companies had a right to look to their own interests in effecting mergers with subsidiaries, the purposes advanced by the parent company had to be "bona fide" and not suspect as a "subterfuge, the real purpose of which is to rid itself of unwanted minority shareholders in the subsidiary."[290] In one subsequent merger challenge, the Chancery Court, in the case of *Young v. Valhi, Inc.*,[291] enjoined a parent-subsidiary merger because it found that the "basic purpose" of the merger was to eliminate the subsidiary's minority shareholders.[292] Because the lower courts were left to decide what constituted a "bona fide" purpose for effecting a merger on a case by case basis, a great deal of uncertainty surrounded the business purpose doctrine in the years following *Singer* and *Tanzer*.[293]

In addition to the doctrinal confusion created by the *Singer* business purpose requirement, many commentators criticized the business purpose requirement as being unrelated to the goals of minority shareholder protection.[294] The basis for this view was that Delaware's long-form merger statute technically allows freezeout mergers, regardless of the business reasons for the merger, through its majority vote provision.[295] In Delaware, therefore, absent a showing of fraud or other gross misconduct, it was not reasonable to allow a minority shareholder to block a parent-subsidiary merger, even if the sole purpose of the merger was to eliminate the minority shareholders from further equity participation in the company. Nevertheless, the minority shareholders do have a right to expect fair treatment from the parent company. Minority shareholders have a right to expect that their interests will be adequately represented in the merger negotiations and that they will be paid a fair price for their forced departure from the enterprise. Requiring a showing of a proper business purpose for effecting a merger did nothing to guarantee that minority shareholders who were frozen out of a corporation were treated fairly by the majority shareholder.

The *Weinberger* court's abandonment of the *Singer* business purpose requirement represents an improvement in the law governing freezeout mergers in Delaware. The elimination of the business purpose doctrine clarifies Delaware merger law by eliminating the doctrinal confusion created by the conflicting and seemingly arbitrary distinctions drawn by the lower courts between valid and invalid business purposes.[296] Although the lower

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[290] 379 A.2d at 1124.

[291] 382 A.2d 1372 (Del. Ch. 1978).

[292] *Id.* at 1378. For a discussion of *Young,* see *supra* note 184.

[293] *See* Weiss, *supra* note 2, at 668-70.

[294] *See, e.g.,* Weiss, *supra* note 2, at 670-71; Brudney & Chirelstein, *supra* note 9, at 1356. Brudney & Chirelstein's main criticism of the *Singer* business purpose test was that it failed to take into account the different contexts in which freezeout mergers can arise. *Id.* Brudney & Chirelstein divided freezeout mergers into three categories: 1) two-step mergers 2) mergers of long held affiliates and 3) pure going private transactions. *Id.* This division was based on similar analysis undertaken by Greene. *See* Greene, *supra* note 7, at 491-96. Brudney & Chirelstein argue that different fairness criteria are appropriate to each category. Brudney & Chirelstein, *supra* note 9, at 1356. They propose that because two-step mergers are essentially the same as arm's-length acquisitions by third parties they could be effectively overseen by impossing disclosure requirements on the acquiring company. *Id.* at 1359. Brudney & Chirelstein argue that going private mergers do not achieve economic gains and should be prohibited completely. *Id.* They believe parent-subsidiary mergers, however, do advance macro-economic efficiencies, and should be allowed, subject to review for fairness of price to protect minority shareholders from mistreatment. *Id.*

[295] *See* DEL. CODE ANN. tit. 8, § 251 (1983).

[296] *See* Weiss, *supra* note 2, at 670.

courts were mandated by the *Tanzer* decision to review the purposes offered by a parent company in order to determine whether the purposes were "bona fide,"[297] the lower courts rarely found a parent company's reasons for effecting a merger to be improper.[298] The practical effect of the business purpose doctrine as applied to parent-subsidiary freezeout mergers, therefore, was that it did not provide minority shareholders any significant protection. Furthermore, when the Delaware courts were examining the business purposes behind a challenged merger, their focus was not directed at the issue that most concerns minority shareholders: the fairness of the merger price.[299] Perhaps the most important consequence of the *Weinberger* court's decision to overrule the *Singer* business purpose requirement is that the treatment received by minority shareholders is now the sole subject of review in freezeout merger challenges. The *Weinberger* court's decision to overrule the *Singer* business purpose test and to establish the *Sterling* entire fairness standard as the sole standard of review for freezeout merger challenges better guarantees that majority shareholders will recieve fair treatment in the future.

B. *Entire Fairness*

The Delaware Supreme Court in *Weinberger* reaffirmed the entire fairness prong of the two pronged standard of review announced in *Singer.*[300] The concept of entire fairness originated in *Sterling v. Mayflower Hotel Corp.* when the Delaware Supreme Court determined that the parent company, because it stood on both sides of the transaction, had to establish the entire fairness of the merger terms to the subsidiary's minority shareholders.[301] In *Singer,* the court held that even if a parent company was successful in establishing that the merger had been effected for a proper purpose, the parent company still had to prove the entire fairness of the transaction.[302] The *Singer* court, however, did not explain what the concept of entire fairness required, nor did it explain under what circumstances it would be invoked.[303]

The *Weinberger* court improved the *Sterling* entire fairness standard by explaining when it would be invoked and how it could be satisfied. The *Weinberger* court explained that every law suit challenging the fairness of a freezeout merger would not be reviewed under the entire fairness test.[304] According to the court, minority shareholders challenging a merger would have to allege "specific acts of fraud, misrepresentation, or other items of misconduct" in order to challenge a merger under the entire fairness standard.[305] The *Weinberger* court further improved the entire fairness test by articulating some specific guidelines regarding what would be necessary in order for a freezeout merger to be considered "entirely fair."[306]

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[297] See 379 A.2d at 1124.

[298] *See, e.g.,* Weinberger v. UOP, Inc., 426 A.2d 1333 (Del. Ch. 1981). The Chancery Court's decision in *Weinberger* is an excellent example of the court's reluctance to enjoin a merger on improper purpose grounds.

[299] *See Weinberger,* 457 A.2d at 711. The *Weinberger* court noted that in a non-fraudulent transaction, price is often the "preponderant consideration." *Id.*

[300] 457 A.2d at 710-11.

[301] 33 Del. Ch. at 298, 93 A.2d at 110.

[302] 380 A.2d at 980.

[303] *See supra* notes 167-68 and accompanying text.

[304] *See* 457 A.2d at 703.

[305] *Id.*

[306] *Id.* at 709 n.7.

1. Fair Dealing

The *Weinberger* court stated that the concept of entire fairness was comprised of two "basic aspects," fair dealing and fair price.[307] The court stressed, however, that the concept of entire fairness required that all the elements of a transaction be considered as a whole in determining whether a parent company had sustained its burden of proof.[308] Under the first aspect, the *Weinberger* court clearly articulated the factors necessary to demonstrate fair dealing in a parent-subsidiary merger.[309] The court stated that once the entire fairness standard had been invoked by a subsidiary's minority shareholders, the parent company had to establish that the manner in which the transaction was timed, initiated, structured, negotiated and disclosed was "entirely fair" to the subsidiary's minority shareholders.[310]

The *Weinberger* court drew upon the laws of directors' fiduciary obligations as the conceptual foundation for the fair dealing component of the entire fairness test.[311] Citing prior Delaware case law, the court reaffirmed the general duties and obligations of corporate officers acting in dual capacities as directors of two corporations.[312] Prior Delaware case law had clearly established the requirement that when directors of a Delaware corporation stand on both sides of a transaction, they owe the same duty of good management to both corporations.[313] In order to discharge this duty in the context of a parent-subsidiary merger, the *Weinberger* court announced that dual directors would have to prove that all the elements of the transaction, when considered as a whole, were structured in the best interests of both companies.[314]

The appropriate discharge of this duty of good management in the context of a parent-subsidiary merger would be difficult to achieve in practice given the inherent conflicts of interest that face dual directors. In addition to the difficulties involved in discharging the duty of good management in practice, it would be even more difficult for dual directors to establish that this duty has been discharged in court. The entire fairness standard necessarily requires that courts apply subjective judgment to the facts of a particular case. Because different courts sometimes reach different conclusions based on the same facts[315] and because the duty of good management in parent-susidiary dealings

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[307] *Id.* at 711.

[308] *Id.*

[309] *See id.*

[310] *Id.*

[311] *Id.* at 710-11. The court cited Warshaw v. Calhoun, 43 Del. Ch. 148, 156, 221 A.2d 487, 492 (Del. 1939) (individuals acting in a dual capacity owe the same duty of good management to both corporations); Gottlieb v. Heyden Chemical Corp., 33 Del. Ch. 82, 91 A.2d 57, 57-58 (Del. 1952) (directors standing on both sides of a transaction are required to demonstrate their utmost good faith and the most scrupulous inherent fairness of the bargain); Guth v. Loft, Inc., 23 Del. Ch. 255, 270, 5 A.2d 503, 510 (Del. 1939) ("The rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest.").

[312] *See Weinberger,* 457 A.2d at 710-11. *See supra* note 311.

[313] *See* Warshaw v. Calhoun, 43 Del. Ch. 148, 156, 221 A.2d 487, 492 (Del. 1966).

[314] *See* 457 A.2d at 710-11.

[315] The proceedings in *Weinberger* are illustrative of this fact. For example, the Chancellor did not object to the fact that UOP's directors had not pressed Signal for a higher merger price. Weinberger v. UOP, Inc., 426 A.2d 1333, 1353-54 (Del. Ch. 1981). The Chancellor concluded that UOP's directors could properly accept Signal's original proposal if they considered the offer to be fair. *Id.* at 1354. The Delaware Supreme Court felt quite differently about UOP's failure to negotiate on behalf of the minority shareholders. The court stated that these negotiations were "modest at

is a particularly difficult one to discharge, the *Weinberger* court sought to provide management with an objective mechanism for establishing the fairness of a parent-subsidiary merger.

The *Weinberger* court went beyond recapitulating the laws of fiduciary duty by suggesting specific procedures for the discharge of the fiduciary obligations owed by dual directors in the context of a parent-subsidiary merger.[316] The court strongly urged that, in the future, independent negotiating committees composed of subsidiaries' outside directors be appointed to deal wth parent companies at arm's-length.[317] The *Weinberger* court stated that "in a parent-subsidiary context, 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."[318] In addition, court stated that a bargaining arrangement involving the total abstention of the interested directors of the subsidiary would achieve the same result.[319] According to the court, absent these suggested bargaining structures, dual directors would be left to discharge their fiduciary duties "in light of what is best for both corporations."[320] A failure to follow the court's suggested guidelines would leave parent companies with the difficult task of proving to the satisfaction of a court that the elements of the transaction were structured in the best interests of both companies.

By advocating an arm's-length bargaining structure, the *Weinberger* court entrusted much of the responsibility for striking a fair deal with the subsidiary's independent directors.[321] While the *Weinberger* court stated that it would treat such a bargaining structure as strong evidence of fairness,[322] the opportunity nonetheless exists for substantial abuse of this process.[323] Past experience has demonstrated that independent directors have not always vigorously pursued the interests of minority shareholders in negotiations with a parent company.[324] Directors of controlled subsidiaries often are prone to viewing themselves as serving at the pleasure of the parent company.[325] The actions of UOP's independent directors in the Signal-UOP negotiations evidence this proposition. UOP's independent directors apparently made no effort to press Signal for a price higher than $21 per share.[326] The UOP directors merely acquiesced to the original price range of

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best" and "hardly arm's length negotiations." *Weinberger,* 457 A.2d at 711. While the Chancellor concluded that the terms of the Signal-UOP merger were legally fair, the Delaware Supreme Court reversed, stating that the transaciton did not "satisfy any reasonable concept of fair dealing." *Id.* at 712.

[316] *See* 457 A.2d at 709 n.7.

[317] *Id.*

[318] *Id.*

[319] *Id.* at 710-11.

[320] *Id.*

[321] *See id.* at 709 n.7. Commentators have expressed serious reservations about this reliance on the independent director. *See, e.g.,* Brudney, *The Independent Director — Heavenly City or Potemkin Village?*, 96 HARV. L. REV. 597, 638-39 (1982); Brudney & Chirelstein, *Fair Shares in Corporate Mergers and Takeovers,* 88 HARV. L. REV. 297, 298 (1974).

[322] 457 A.2d at 709 n.7.

[323] *See* Weiss, *The Law of Take Out Mergers: Weinberger v. UOP, Inc. Ushers in Phase Six,* 4 CARDOZO L. REV. 245, 255 (1983).

[324] *See* Brudney, *supra* note 321, at 617.

[325] *See id.* at 610-11.

[326] 457 A.2d at 711.

$20-$21 per share suggested by Signal and then insisted on a price of $21 per share.[327] Even if UOP's independent directors believed that $21 per share was a fair price, they should have attempted to negotiate a higher price for the minority's stock in order to fulfill their fiduciary obligations to the minority shareholders.[328] The irony of this particular case is that if the UOP directors had pressed for a higher price, Signal in all likelihood would have agreed because the report prepared as part of the acquisition investigation indicated that it would have been a good investment for Signal to purchase UOP's remaining publicly held shares at any price up to $24 per share.[329] It seems unlikely that an "independent negotiating committee" of UOP's independent directors would have pressed Signal for a higher price when the group, as a whole, failed to take any action in this direction. Consequently, although the *Weinberger* court sought to achieve fair dealing in freezeout mergers by establishing a committee of the controlled subsidiary's independent directors, the court's failure to recognize adequately the relationship of such directors to the parent corporation limits the ability of such measures to protect minority shareholder interests.

The *Weinberger* decision did, however, establish other devices in order to protect minority shareholders from the inequitable treatment that may occur at the hands of docile independent directors. The court, in effect, adopted a totality of the circumstances approach for examining the dealings between a parent company and its subsidiary in a freezeout merger. According to the court, while an independent negotiating structure may be strong evidence of fairness, it is only one part of the fair dealing component of the entire fairness test.[330] The court stated that once the plaintiff challenging the merger alleges specific instances of misconduct, thus invoking the entire fairness standard, the defendant corporations must prove that the transaction, when considered as a whole, was entirely fair to the subsidiary's minority shareholders.[331] After *Weinberger,* it is clear that in order to satisfy this burden, a parent corporation will have to establish, by a preponderance of the evidence, that the timing, initiation, structure, negotiation and disclosure of the transaction were fair to the minority shareholders.[332] To make the arm's-length bargaining structure it suggested more meaningful and to improve the overall quality of minority shareholder protection, the *Weinberger* court emphasized the quality of the disclosure of information from parent company to subsidiary.[333]

The *Weinberger* court articulated strict disclosure requirements to ensure informed decision making by independent directors and minority shareholders in parent-subsidiary dealings.[334] The court stated that the lower courts are required to measure disclosure in terms of "what the defendants had and to measure it against what they gave to the minority."[335] According to the court, nothing less than "complete candor" is

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[327] *Id.* The merger price also happened to be the same as the 1975 tender offer price. *Id.* at 704.

[328] *See* 457 A.2d at 711. The *Weinberger* court did not rule specifically that UOP's directors had a duty to negotiate a higher merger price with Signal. *See id.* The court took note of the absence of negotiations as one factor in its decision that the Signal-UOP merger did not satisfy any reasonable concept of fair dealing. *Id.* at 712.

[329] *Id.* at 705.

[330] *Id.*

[331] *Id.* at 703.

[332] *See id.* at 711.

[333] *Id.* at 711-12.

[334] *Id.* at 710.

[335] 457 A.2d at 710 (citing Lynch v. Vickers Energy Corp., 383 A.2d 278, 281 (Del. 1977)).

required of the parent company.[336] This complete disclosure requirement is of real practical significance to the independent director and the minority shareholder. A subsidiary's independent directors will have greater bargaining leverage if they are negotiating with knowledge of all the information relevant to the transaction. For example, if UOP's independent directors had known that Signal was prepared to pay up to $24 per share for UOP's minority interest, UOP's directors would have been in a position to bargain for a price higher than the $21 per share to which they actually acquiesced.[337]

Complete disclosure is of practical importance to minority shareholders as well. The complete disclosure requirement supplements the minority shareholder protection achieved by the entire fairness standard. In theory, complete disclosure will, in some instances, provide minority shareholders with the information necessary to make allegations of misconduct in order to invoke the entire fairness standard. In situations where no misconduct is apparent, complete disclosure will enable minority shareholders to evaluate the fairness of the merger price for themselves in deciding whether to accept the offered consideration or seek an appraisal.

2. Fair Price

As discussed above, the *Weinberger* court improved the quality of minority shareholder protection by explaining the fair dealing element of the entire fairness test and by reaffirming strict disclosure requirements for parent companies in the context of freeze-out mergers. In addition to these improvements, the court emphasized that the concept of entire fairness also embraces notions of fair price.[338] The fair price prong of the entire fairness test serves as additional protection for minority shareholders in situations where the fair dealing requirements have been largely satisfied. As a component of the entire fairness test, fair price considerations are only relevant as part of the examination of the total circumstances of a merger after plaintiff has first made the allegations of misconduct necessary to invoke the entire fairness test.[339] When the plaintiff is disputing only the merger price, the *Weinberger* court held that the plaintiff's sole remedy is statutory appraisal.[340] The court recognized that the merger price in a nonfraudulent transaction is probably "the preponderant consideration outweighing other features of the merger."[341] For the purposes of determining fair price under the entire fairness standard and in order to insure that minority shareholders receive fair value for their shares in an appraisal proceeding, the *Weinberger* court held that modern valuation techniques could now be used to establish the value of a minority shareholder's stock.[342]

By allowing the use of modern valuation techniques, the court granted minority shareholders greater latitude in proving the fair value of their stock. Prior to *Weinberger*, the "Delaware block" weighted average approach was the only valuation method allowed to be used by Delaware courts in stock valuation proceedings.[343] The Delaware block

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[336] *See* 457 A.2d at 710.

[337] *See id.* at 705, 711.

[338] *Id.* at 711.

[339] *See id.* 703. The court stated that to invoke the entire fairness obligation, a plaintiff would be required to allege "specific acts of fraud, misrepresentation or other items of misconduct to demonstrate the unfairness of the merger terms to the minority." *Id.*

[340] *Id.* at 715.

[341] *Id.* at 711.

[342] *Id.* at 712-13.

[343] *See* in re General Realty & Utilities Corp., 29 Del. Ch. 480, 496-500, 52 A.2d 6, 14-15 (Del. Ch. 1947). *See supra* note 58 and accompanying text.

valuation method was a weighed average of asset value, market price and earnings per share.[344] In *Weinberger*, the Delaware Supreme Court abandoned the exclusive use of the Delaware block method, authorizing the use of contemporary financial market techniques in the resolution of future valuation disputes.[345] In support of this holding, the *Weinberger* court relied heavily on the language of the Delaware appraisal statute, section 262.[346] Section 262 instructs courts to "take into account all relevant factors" in valuing a dissenting shareholder's stock.[347] According to the court, the factors to be considered in determining fair price include: "assets, market value, earning, future prospects and any other elements that affect the intrinsic or inherent value of a company's stock."[348] Among these factors, the *Weinberger* court emphasized that special consideration should be given to a corporation's "future prospects" in the stock valuation.[349] After identifying the factors to be considered by courts in determining whether the price given to minority shareholders in a freezeout merger was fair, however, the *Weinberger* court did not articulate any workable test for how these factors could be combined into an overall determination of the fairness of the merger price. Instead, the court merely held that courts are required to take "all the relevant factors" into account in determining a shareholder's proportionate interest in a going concern.[350]

IV. Structuring Freezeout Mergers After *Weinberger*

After *Weinberger*, corporations will be able to structure parent-subsidiary mergers that should, in most instances, be immune from challenges by minority shareholders.[351] The *Weinberger* court took decisive steps toward insulating freezeout mergers from judicial attack by minority shareholders. First, the court clearly articulated procedural guidelines that, if followed will be considered strong evidence of fair dealing.[352] Second,

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[344] *See* In re General Realty & Utilities Corp., 29 Del. Ch. 480, 496-500, 52 A.2d 6, 14-15 (Del. Ch. 1947).

[345] 457 A.2d at 712. The court stated: "To the extent [the Delaware block approach] excludes other generally accepted techniques used in the financial community and the courts, it is now clearly outmoded. It is time we recognize this in appraisal and other stock valuation proceedings and bring our law current on the subject." *Id.* For an elaborate criticism of the "Delaware block" approach see generally Schaefer, *The Fallacy of Weighting Asset Value and Earnings Value in the Appraisal of Corporate Stock*, 55 S. Cal. L. Rev. 1031 (1982) (the weighted average method systematically tends to undervalue corporate shares).

[346] 457 A.2d at 713 (citing Del. Code Ann. tit. 8, § 262 (1983)).

[347] Del. Code Ann. tit. 8, § 262(h) (1983).

[348] 457 A.2d at 713-14.

[349] *Id.* at 713. The court was careful to note that section 262 did not mandate a different conclusion. *See id.* The court gave a very narrow reading to the language of the section which excludes from consideration elements of value that may arise from the "accomplishment or expectation" of the merger. *Id.* The court interpreted this language to mean that only the use of pro forma and speculative projections must be excluded from the valuation determination. *Id.* The court continued by stating that "[e]lements of future value, including the nature of the enterprise, which are known or susceptible of proof as of the date of the merger and not the product of speculation, may be considered." *Id.* The court believed that anything less would not be giving full effect to the legislative directive that "all relevant factors" be considered. *Id.*

[350] *See id.* at 713. The court did not express approval for any specific valuation technique, see *id.*, apparently preferring to rely on the adversary system to produce the best evidence of fair value.

[351] *See id.* at 709 n.7.

[352] *See id.* This type of negotiating structure was becoming more popular with management even prior to the *Weinberger* decision. *See* Chazen, *Fairness From a Financial Point of View in Acquisitions*

the opinion limited minority shareholders' financial remedy to appraisal.[353] The *Weinberger* court also established the appropriate allocation of the burden of proof in freezout merger challenges.[354] *Weinberger* makes clear that in order for minority shareholders to seek equitable relief under the entire fairness test, they must allege specific acts of fraud, misrepresentation or other items of misconduct.[355] Once the entire fairness standard has been invoked, the burden of proof rests with the parent company to establish the entire fairness of the merger.[356] Liability is established if the parent company is unable to meet this burden of proof; it is then left to the court's discretion to order any form of equitable or monetary relief required by the circumstances.[357] If minority shareholders are unable to make specific allegations of fraud or other misconduct, the entire fairness test is not invoked and the minority shareholders' only recourse is to seek an appraisal of their shares as provided for by statute.[358]

In discussing the allocation of the burden of proof, the *Weinberger* court provided parent companies with a mechanism for shifting the burden of proof back to the minority shareholders after the entire fairness test has been invoked.[359] In order to shift the burden of proof, the parent company could condition the consummation of the merger on the approval of a majority of the subsidiary's minority shareholders.[360] The court stressed, however, that the minority shareholder vote must be an "informed" one.[361] In order to prove that the vote was informed, the *Weinberger* court ruled that the parent company had to prove that it had disclosed all the material facts relevant to the transaction.[362] If the parent company is unable to demonstrate that it disclosed all the material facts necessary for a court to consider the vote informed, the *Weinberger* court stated that the burden of proof would then remain the parent company's.[363] If the plaintiffs alleged specific acts of misconduct and the parent company demonstrated that a majority of the subsidiary's minority shareholders had approved the merger in an informed vote, the *Weinberger* court ruled that the burden of proof would then be on the plaintiffs challenging the merger to prove the unfairness of the merger terms to the minority shareholders.[364] Consequently, if parent companies wished to place the burden of proof on the minority shareholders in subsequent litigation, they could condition the merger on the informed approval of a majority of the subsidiary's minority shareholders.

If a parent did not want to condition a freezeout merger on a minority shareholder vote, it could take advantage of the independent negotiating structure suggested by the *Weinberger* court.[365] The court advocated the use of an independent negotiating committee composed of a subsidiary's outside directors to deal at arm's-length with the parent

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of Public Companies: Is "Third-Party Sale Value" the Appropriate Standard?, 36 BUS. LAW. 1439, 1440-41 (1981).

[353] 457 A.2d at 715.

[354] *Id.* at 703.

[355] *See id.*

[356] *Id.*

[357] *Id.* at 714.

[358] *Id.* at 714-15.

[359] *Id.* at 703.

[360] *Id.*

[361] *Id.*

[362] *Id.*

[363] *Id.*

[364] *Id.*

[365] *See id.* at 709 n.7.

company in negotiating the terms of the merger.[366] The court stated that the use of such a bargaining structure would be "strong evidence" of fairness.[367] In addition, the *Weinberger* court stated that a showing that the subsidiary's interested directors totally abstained from any participation in the transaction would also be highly probative of the fairness of the deal.[368] Accordingly, it seems unlikely that parent companies will be willing to structure freezeout mergers in the future without conditioning the merger on minority shareholder approval or employing one of the procedural safeguards suggested by the *Weinberger* court. Once the entire fairness test has been invoked, the parent company must establish the entire fairness of the merger and that it fulfilled its duty of good management to both companies in structuring the deal.[369] Without making use of these additional protections, parent companies will have a more difficult time meeting this burden of proof, incurring a greater risk that the merger will be set aside.

One potential drawback to the Delaware Supreme Court's decision in *Weinberger* is that the emphasis the opinion places on compliance with procedural guidelines may cause lower courts to place form over substance in considering challenges to freezeout mergers. Delaware courts should should be alert for situations where the parent company has formally complied with the procedural guidelines set out in *Weinberger*, but has, in fact, subjected the subsidiary's minority shareholders to substantial unfairness.[370] By relying on a self-governed artificial arm's-length bargaining structure, the *Weinberger* court entrusted the subsidiary's independent directors with the responsibility of fairly representing the interests of the minority shareholders.[371] Some judicial checks are necessary to guarantee that the actual substance of the parent-subsidiary negotiations truly approximate arm's-length bargaining.

V. A Recommended Negotiating Structure for Parent-Subsidiary Freezeout Mergers

In *Weinberger*, the Delaware Supreme Court stated that in future merger transactions evidence of negotiations between representatives of the parent company and a committee of its subsidiary's independent directors would be highly indicative of fairness in any subsequent court challenge.[372] While the court, by stating that such a transaction would be presumptively fair, provided management with strong incentive to use such a negotiating structure, it failed to explore the ramifications of this independent negotiating concept.[373] For example, the *Weinberger* court did not provide any guidelines as to how the members of the subsidiary's independent negotiating committee should be selected. Instead, the court merely stated in general terms that the committee should be composed of the subsidiary's independent directors.[374] As noted earlier, behind a facade of arm's-length bargaining, a parent company could dominate merger negotiations by appointing only partisan or indifferent independent directors to the subsidiary's negotiating team.[375] The

[366] *Id.*
[367] *Id.*
[368] *Id.* at 710-11.
[369] *Id.*
[370] *See* Weiss, *supra* note 323, at 255.
[371] *See infra* notes 372-91 and accompanying text.
[372] 457 A.2d at 709 n.7.
[373] *See id.*
[374] *Id.*
[375] *See supra* note 321.

Weinberger court should have instructed the lower courts to examine the selection process behind the subsidiary's negotiating committee to make sure that it was free from the parent company's influence before treating the use of such a bargaining structure as strong evidence of fairness. A transaction, therefore, should only be considered presumptively fair in situations where the subsidiary's negotiating committee is truly independent.

A second area in which the Delaware Supreme Court in *Weinberger* should have taken further steps to protect the interests of minority shareholders is in the determination of a fair price for their stock. Although it is generally recognized that there is no one correct stock valuation method,[376] the *Weinberger* court could have improved the substance of the arm's-length bargaining structure it suggested by articulating specific negotiating guidelines to be used by the parties in negotiating the price for the minority's stock. Specifically, the independent bargaining structure could provide more effectively for fair treatment of minority shareholders in freezeout merger transactions if the negotiated merger price were required to fall within a specified range. Such a price range is necessary for the protection of minority shareholders because even if the subsidiary's independent directors negotiate the merger price, the final figure is likely to be as low as reasonable pessimism will allow.[377] Commentators have found that a subsidiary's independent directors often view themselves as serving at the pleasure of the parent company.[378] As a result of this perception, total reliance upon independent directors to represent the minority shareholders' interests in merger negotiations with the parent company is misplaced. The *Weinberger* court, therefore, should have articulated general price guidelines to serve as ceiling and floor benchmarks for future merger negotiations involving an independent negotiating structure.

Specific ceiling and floor figures would provide courts, management and minority shareholders alike with useful guidelines of fairness. Even though, as noted earlier, there is no one generally accepted stock valuation method for determining the proper price for the minority's shares,[379] there has been some agreement among the commentators concerning the valuation formulas of ceiling and floor values of corporate stock.[380] In parent-subsidiary mergers, two valuation methods in particular have been suggested to determine the approximate ceiling and floor values of the subsidiary's stock. At the lower end of the spectrum is the market value of the acquired company's stock.[381] The merger price in a parent-subsidiary merger should never fall below the prevailing market price for the subsidiary's stock, because the minority shareholders should not be forced to accept a price lower than what they could have received if they had sold their stock in the market prior to the merger.[382] The ceiling figure of the recommended price range would be the amount per share that could be realized if the entire company was sold to a third party in an arm's-length transaction.[383] This third party sale value ceiling figure could be

[376] *See* Banks, *Measuring the Value of Corporate Stock,* 11 CAL. W.L. REV. 1, 1 (1974).

[377] *See* Brudney & Chirelstein, *supra* note 321, at 298.

[378] *See* Brudney, *supra* note 321, at 610-11; Brudney & Chirelstein, *supra* note 321, at 298.

[379] *See supra* note 376 and accompanying text.

[380] *See* Banks, *supra* note 376, at 1.

[381] *See* Brudney & Chirelstein, *supra* note 9, at 1372-73.

[382] *See id.*

[383] *See* Chazen, *supra* note 352, at 1440; Weiss, *supra* note 2, at 678-80. Weiss argues that a parent company should be required to pay at least as much for the minority interest in a subsidiary as the minority shareholders could realize if the subsidiary was sold to a third party in an arm's-length transaction. *Id.*

approximated by analyzing other similar accquisitions or mergers.[384] The representatives of the parent company and its subsidiary should be expected to negotiate the actual merger price within this range of values. Representatives of the subsidiary should press for a premium in excess of the current market price, because it has become customary for the stockholders of a target company to receive a premium above the market price.[385] The representatives of the parent company will be unwilling to pay a premium equal to the ceiling price, however, because the subsidiary's publicly held shares will be worth less to the parent company than they would be to a third party.[386] The subsidiary's publicly held shares are worth less to the parent company because it already owns a controlling interest in the subsidiary. A third party seeking to purchase the entire company would have to pay a higher premium per share because it would be purchasing both the control block owned by the parent company and the minority interest. Because the parent company will, therefore, be unwilling to pay third party sale value for the minority's shares, the subsidiary's negotiating represenitives may properly accept a premium lower than third party sale value.[387]

Imposing a lower limit on the price given to minority shareholders in a parent-subsidiary merger would, in effect, set a minimum fair price standard. The parent company should be required to pay the subsidiary's minority shareholders at least enough money, or other valuable consideration, to enable them to reacquire the same proportionate interest in the parent company that they would have possessed had the merger been a straight stock for stock transaction.[388] A direct effect of establishing a minimum floor requirement would be that merger prices falling below this figure would be considered presumptively unfair. A court examining a parent-subsidiary merger under the entire fairness test should consider such a merger price to be highly probative of the unfairness of the entire transaction.

The above suggested price guidelines could be used in courtrooms as well as at bargaining tables. As the starting point in all merger negotiations, both parties would be

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In *Weinberger*, the plaintiff attempted to introduce evidence to establish a third party sale value price figure for UOP's stock by offering a comparative analysis of the premiums paid over market in ten other comparable tender offer merger combinations. 457 A.2d at 712.

[384] *See* Chazen, *supra* note 352 at 1440.

[385] *See id.* at 1445.

[386] *Id.* at 1471.

[387] *See id.* at 1447. Chazen believes before an arm's length standard of fairness should be accepted, the parent company should be required to demonstrate that the merger price was within "the range that would have resulted from an arm's length transaction." *Id.* Chazen argues that there is a range of fairness based on the range of prices a shareholder might obtain if proposals to buy the company were sought from other potential purchasers. *Id.* at 1439.

[388] Brudney & Chirelstein, *supra* note 9, at 1372-73. Brudney & Chirelstein would go further than this minimum requirement, however. They advocate that the minority shareholders should receive a share of the synergistic gains generated by the merger. *See* Brudney & Chirelstein, *supra* note 321, at 323. This approach was adopted by the Second Circuit Court of Appeals in Mills v. Electric Auto-Lite Co., 552 F.2d 1239, 1248-49 (2d Cir. 1977). Brudney & Chirelstein distinguish between cases where the parent company is closely held as a result of the merger and cases where the parent company remains a public company. Brudney & Chirelstein, *supra* note 9, at 1374. If the parent company is closely held after the merger, Brudney & Chirelstein contend that a merger may be unfair per se, because there is no means for minority shareholders to reacquire an equity interest in the parent corporation. *Id.* They pointed out that in situations where the parent company is closely held as a result of the merger, there may be no way to determine whether the merger price was fair. *Id.*

expected to develop their own ceiling and floor price figures. In a subsequent court challenge to the price given to the minority shareholders under the entire fairness standard, the court should require a showing that each party actually developed these price figures and used them in the actual bargaining. In the absence of such a showing, the court should not accept evidence of an independent negotiating structure as strong evidence of the fairness of the entire transaction. By requiring that these price guidelines be followed in all mergers, courts would be able to check for possible abuses of the *Weinberger* independent negotiating structure by parent companies.

Established ceiling and floor price guidelines would also be beneficial in situations where independent negotiating structure were not used by the parties in accomplishing a merger. In the future, parent companies could be required to disclose these price guidelines to the subsidiary's directors and minority shareholders. The disclosure of these standards would be useful to the minority shareholders in assessing whether to approve the merger terms or dissent and seek an appraisal.[389] If a shareholder decided to challenge such a merger, the court could attempt to simulate arm's-length bargaining within this range in the context of an adversarial proceeding.[390]

CONCLUSION

The *Weinberger* decision clarifies and improves Delaware's treatment of parent-subsidiary freezeout mergers. Since 1977, Delaware courts had been examining freezeout mergers under the business purpose requirement announced in *Singer v. Magnavox Co.*. By overruling the *Singer* business purpose test, the *Weinberger* court improved minority shareholder treatment and facilitated the structuring of future freezeout mergers. Delaware courts now can focus on the merger transaction itself to determine whether the minority shareholders were treated fairly. Although minority shareholders will be relegated to the appraisal remedy when the only issue in dispute is the adequacy of the merger price, the *Weinberger* court improved the appraisal remedy by authorizing the use of modern valuation techniques in appraisal proceedings in order to ensure that minority shareholders receive fair value for their stock. *Weinberger* also recognized the need for appropriate equitable relief in situations where appraisal was not adequate, but not in circumstances as broad and ill-defined as those contemplated by the *Singer* court when it announced the business purpose requirement. In circumstances where the minority shareholders make specific allegations of instances of misconduct such as fraud or overreaching, the *Weinberger* court ruled that the parent company would then be required to prove the entire fairness of the transaction. In instances where the parent company could not meet this burden, the *Weinberger* court stated that the Chancellor's powers were complete to fashion any appropriate form of equitable or monetary relief.

To assist parent corporations in meeting the burdens imposed by the entire fairness standard, the *Weinberger* court articulated guidelines. The court recommended the use of an independent negotiating structure, which when used would be considered by the courts as strong evidence of fairness. One weakness with the court's decision is the

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[389] Even if the merger price was presumptively fair, approving the transaction would foreclose a minority shareholder from seeking an appraisal of his shares. *See* DEL. CODE ANN. tit. 8, § 262(a) (1983).

[390] *See* Chazen, *supra* note 352, at 1445. Chazen believes that judicial review of freezeout mergers could be viewed as a substitute for arm's length bargaining on behalf of the public minority shareholders. *Id.*

potential for manipulation of this negotiating structure. The *Weinberger* court could have improved the negotiating structure it suggested by defining specific ceiling and floor price guidelines to be used in the bargaining process. The use of such guidelines would help ensure that the negotiations between parent and subsidiary result in a fair merger price.

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