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The Still-Dwindled *Revlon*

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The Still-Dwindled *Revlon*

Lyman Johnson* and Robert Ricca

Abstract

This is a brief Response to Professor Mohsen Manesh’s extensive response to our original article, The Dwindling of Revlon. Our thesis is that today the iconic Revlon doctrine is, remedially, quite substantially diminished. Although Professor Manesh sets out to establish what he calls “the limits of Johnson’s and Ricca’s thesis,” we here maintain, as before, that there is little remedial clout to Revlon unless directors or others very significantly misbehave. We also criticize Delaware’s continuing use of the standard-of-conduct/standard-of-review construct in the fiduciary duty area. This rubric is unhelpful generally and strikingly so in the Revlon setting, as we note.

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I. Introduction

We thank the Editors at the *Washington and Lee Law Review Online* for inviting this Response. And of course we thank Professor Mohsen Manesh for his extensive response¹ to our

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1. Mohsen Manesh, *Nearing 30, Is Revlon Showing Its Age?*, 71 WASH. & LEE L. REV. ONLINE 107 (2014).

original article, where we argued that today the iconic doctrine announced in *Revlon v. MacAndrews & Forbes Holdings, Inc.*² is, remedially, quite substantially diminished.³ Professor Manesh sets out to establish what he calls “the limits of Johnson and Ricca’s thesis,”⁴ but we maintain in this Response, as before, that there is little remedial clout to *Revlon* unless directors or others very significantly misbehave. We believe Professor Manesh’s various points serve only to underscore how unlikely it is that *Revlon* will be the basis for judicial sanctions.

Although we did not set out in our original article to address the liability exposure of advisers or corporate officers under *Revlon* because they have no such direct exposure,⁵ we first briefly respond to Professor Manesh’s arguments with respect to those two types of defendants. We then turn to directors, our central concern and the group most frequently sued for alleged wrongdoing under *Revlon*.⁶

2. 506 A.2d 173 (Del. 1986).

3. Lyman Johnson & Robert Ricca, *The Dwindling of Revlon*, 71 WASH. & LEE L. REV. 167 (2013).

4. Manesh, *supra* note 1, at 107.

5. When a sale of the company becomes inevitable, it is the role of the directors that changes from “defenders of the corporate bastion to auctioneers charged with getting the best price for stockholders.” *Revlon*, 506 A.2d at 182. The board of directors is the governance body empowered as the gatekeeper in approving a merger or other sale of the company. See DEL. CODE ANN. tit. 8, §§ 251, 271 (2012) (giving the power to approve an agreement of a merger or consolidation solely to the board of directors). To the extent officers are involved in the negotiation and execution of a transaction to which *Revlon* would apply, the officers must fulfill their traditional fiduciary duties of care and loyalty when acting under the direction of the board in the sales process. See *Revlon*, 506 A.2d at 179 (reminding parties that the fiduciary duties of care and loyalty apply with force during the merger process). Corporate officers have no statutory responsibilities in the *Revlon* setting. See DEL. CODE ANN. tit. 8, §§ 142, 251 (noting that corporate officers’ duties depend on the bylaws of a corporation while the board of directors has explicit duties set forth in the Delaware Code). It is the unique function of the board to act as the key decision maker and protector of the stockholders in a sales process, not the corporate officers qua officers. See *id.* § 251 (describing the duties of the board of directors in a sales process but not mentioning any duties of corporate officers). Similarly, while advisers must act pursuant to their agency law and contract duties, such advisers are charged with no special duties under *Revlon*. See *Revlon*, 506 A.2d at 179 (“The ultimate responsibility for managing the business and affairs of a corporation falls on its board of directors.”).

6. See Johnson & Ricca, *supra* note 3, at 189–90 (noting that *Revlon* does not change the basic duties owed by directors but does trigger heightened

II. Advisers; Aiding and Abetting

Professor Manesh rightly relates the “egregious facts” in the recent *Rural Metro*⁷ decision.⁸ Much like the conflicted financial adviser we described in the *Del Monte*⁹ case,¹⁰ the bank in *Rural Metro* took “every opportunity to surreptitiously manipulate . . . to advance its own interests.”¹¹ But liability for outrageous, self-serving conduct that aids and abets a fiduciary duty breach, although rare, certainly is not limited to the *Revlon* setting and is not a distinctive attribute or outgrowth of *Revlon* responsibilities. A bank—or anyone else—can be liable for aiding and abetting any breach of fiduciary duty, including a breach of the duty of care, in any setting. Such persons owe no direct fiduciary duties under *Revlon*, or at all for that matter.

These cases remain so rare, moreover, because in *all* such settings, the bank (or other actor) is liable only if it “knowingly participates” in the misbehavior,¹² a high hurdle that is more demanding than the *Revlon* standard itself. Just how high can be seen in a recent Chancery Court decision.¹³ In dismissing an

judicial scrutiny of director conduct); *see also* *Paramount Commc’ns, Inc. v. QVC Network, Inc.*, 637 A.2d 34, 45 (Del. 1993) (explaining that because the case involved a sale of control, “[b]oard action in the circumstances presented here is subject to enhanced scrutiny”).

7. *In re Rural Metro Corp. S’holders Litig.*, 88 A.3d 54 (Del. Ch. 2014).

8. Manesh, *supra* note 1, at 131–32; *see also In re Rural Metro Corp. S’holders Litig.*, 88 A.3d 54, 63–79 (Del. Ch. 2014) (recounting the complicated factual scenario leading up to the litigation). On October 10, 2014, Vice Chancellor Laster ordered the financial adviser—RBC Capital Markets LLC—to pay \$75.8 million in damages to the former shareholders of Rural Metro Corp. Liz Hoffman, *RBC Ordered to Pay \$75.8 Million Over Conflicts Laws*, WALL ST. J. (Oct. 13, 2014, 9:37 A.M.), <http://online.wsj.com/articles/rbc-ordered-to-pay-75-8-million-over-conflicts-lawsuit-1412975652> (last visited Nov. 1, 2014) (on file with the Washington and Lee Law Review).

9. 25 A.3d 813 (Del. Ch. 2011).

10. *See Johnson & Ricca, supra* note 3, at 212 (describing the one instance in which the Chancery Court granted injunctive relief on *Revlon* claims in the pre-closing context in the past several years as involving a “conflicted financial advisor”); *Del Monte*, 25 A.3d at 828 (finding that the selling company’s financial adviser also providing buy-side financing and that this was an obvious conflict).

11. Manesh, *supra* note 1, at 131.

12. *Rural Metro*, 88 A.3d at 84–85, 96–100.

13. *See Dent v. Ramtron Int’l Corp.*, No. 7950-VCP, 2014 WL 2931180, at *17 (Del. Ch. June 30, 2014) (“Dent faces a heavy burden in arguing that Cypress knowingly participated in any breaches of fiduciary duty . . .”).

aiding and abetting claim against a financial adviser, the vice chancellor noted that evidence of arm's-length bargaining by the two companies in a sales process necessarily negates an aiding and abetting claim because it utterly precludes a showing of knowing participation.¹⁴ Thus, plaintiffs, the court observed, face a "heavy burden" in these types of cases.¹⁵

But the burden in a *Revlon* setting can be heavier yet where, as in *Rural Metro*, the directors are not defendants in the case because then the plaintiff must also prove that the directors breached a fiduciary duty.¹⁶ This leaves the plaintiff, not the defendants, with all the burdens—very high ones—in a long-shot aiding and abetting claim.¹⁷ *Rural Metro* is a cautionary tale for egregiously conflicted financial advisers, but, from a remedies perspective, it is a distinct outlier. These types of claims may arise in *Revlon* settings—where they typically fail—but they are not uniquely *Revlon* duty claims, and they do not "limit" our thesis.

III. Corporate Officers

As with aiders and abettors, corporate officers may have liability in *Revlon* settings—although this seems nonexistent to date¹⁸—but not because of officer breaches of *Revlon* duties as such. As we noted in our earlier piece, officers already face greater liability risk than directors because they cannot be

14. *See id.* (describing the Chancery Court's consistent position that evidence of arm's-length negotiation with fiduciaries negates a claim of aiding and abetting).

15. *Id.*

16. *See In re Rural Metro*, 88 A.3d at 84–85 ("By choosing to settle with the directors and continue only with the aiding and abetting claim, the plaintiffs took up the burden of proof on each of the elements of aiding and abetting, including the existence of a fiduciary breach.").

17. *See, e.g., Houseman v. Sugarman*, No. 8897-VCG, 2014 WL 1478511, at *15 (Del. Ch. Apr. 16, 2014) (dismissing *Revlon* claims against directors and aiding and abetting claims against financial adviser).

18. The 2014 case described by Professor Manesh involves two officers and remains ongoing. *See Chen v. Howard-Anderson*, 87 A.3d 648, 693 (Del. Ch. 2014) (granting and denying in part the motion for summary judgment). To our knowledge, no court has imposed judicial sanctions on an officer qua officer for failing to discharge *Revlon*-related responsibilities.

exculpated.¹⁹ This is as it should be.²⁰ What *Revlon* does is set a stiffer standard for corporate directors in the merger and sale context, but as we point out, remedially, the cases rarely impose sanctions on directors.²¹

One critical mistake directors can and do make—albeit more rarely today than in the past, one hopes—is to permit executive officers to play a central and insufficiently supervised role in the sales process. The cases cited by Professor Manesh involved boards of directors allowing senior officers—with obvious conflicts of interests—to negotiate corporate sales.²² Of course, the officers, upon being careless, disloyal, or both in discharging their delegated (or acquiesced in) functions in such settings, face liability exposure, but not because of *Revlon* as such. Officers qua officers have no independent obligations under *Revlon*. They only have those, if any, derived from the board of directors, the governance body that should drive the sale process. It is the directors who theoretically—but do not in actuality, we show—face the risk of sanctions for mishandling their *Revlon* responsibilities. In any event, actual liability of officers in the *Revlon* setting appears, based on reported decisions, to be even rarer than for directors. Vice Chancellor Laster, in the *Chen-Anderson* decision referenced by Professor Manesh, cited an article by Professor Johnson and observed that Delaware law on officer liability is unresolved.²³ This stems from the fact that there are so few Delaware decisions addressing officer liability in any fashion, much less imposing sanctions. To date, officers, like directors, have faced low *Revlon*-related risk.

19. See Johnson & Ricca, *supra* note 3, at 206 (“Thus, while corporate officers remain personally liable for duty of care breaches, directors generally face only injunctive and other equitable remedies for such breaches.”).

20. See Lyman Johnson & Robert Ricca, *Reality Check on Officer Liability*, 67 BUS. LAW. 75, 75 (2011) (arguing that a stricter duty of care for officers is more realistic and theoretically sound).

21. See Johnson & Ricca, *supra* note 3, at 218 (describing the “low likelihood of a remedial sanction under *Revlon*”).

22. See Manesh, *supra* note 1, at 126 n.105, 128 n.117, 129 n.126 (citing various cases that involved boards of directors enabling executive officers to negotiate mergers and acquisitions).

23. See Chen, 87 A.3d at 666 n.2 (acknowledging the “lively debate” surrounding officer liability).

IV. Directors; Rare Remedies

Of the two key judicial opinions discussed by Professor Manesh, one involved no directors and the other granted the independent directors summary judgment. And in the two subsequent decisions we noted above, the Chancery Court granted the directors' motions to dismiss.²⁴ Thus, as we posited in our original piece, directors face a very low likelihood of judicial sanction.²⁵ That plaintiffs now pursue other quarry, such as conflicted advisers and careless or disloyal officers, shows just how challenging it is to obtain sanctions against disinterested, independent directors.

But Professor Manesh helpfully asks us to remember something about bad-faith claims in the *Revlon* setting. Bad faith is not limited to the "conscious disregard" of duty claim found in *Lyondell*,²⁶ but can include subjective bad faith. In fact, and we cited *Disney* which emphasized just this,²⁷ the traditional or "classic, quintessential bad faith" theory is subjective bad faith. But subjective bad-faith claims of the type touted by Professor Manesh require an *intent* to do harm, as *Lyondell* and *Disney* note.²⁸ That is, such a claim requires intentionally acting with a

24. See Manesh, *supra* note 1, at 128 (explaining that "the chancery court granted summary judgment dismissing the *Revlon* claims made against Occam's outside directors"); *Dent v. Ramtrol Int'l Corp.*, No. 7950-VCP, 2014 WL 2931180, at *13 (Del. Ch. June 30, 2014) (discussing that the plaintiffs' must meet their evidentiary burden).

25. See Ariel Yehezkel & Amanda Zablocki, *Fiduciary Duties in the Context of Dent v. Ramtron Int'l Corp.*, MARTINDALE.COM (Sept. 2, 2014), http://www.martindale.com/corporate-law/article_Sheppard-Mullin-Richter-Hampton-LLP_2177584.htm (last updated Sept. 10, 2014) (last visited Oct. 30, 2014) ("The difficulty of winning a *Revlon* claim has been proven time and time again . . .") (on file with the Washington and Lee Law Review).

26. See *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 240 (Del. 2009) (discussing the Chancellor's definition of bad faith as an "intentional dereliction of duty, a conscious disregard for one's responsibilities").

27. See *Johnson & Ricca*, *supra* note 3, at 208 (addressing the Delaware court's view of bad faith); see also *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 64–66 (Del. 2006) (discussing the role of intent in relevant bad-faith standards).

28. See *Lyondell*, 970 A.2d at 240 (discussing the court's view of bad faith as "encompass[ing] not only an intent to harm but also an intentional dereliction of duty"); *Disney*, 906 A.2d at 64–66 (describing subjective bad faith as "motivated by an actual intent to do harm").

purpose other than that of advancing the best interests of the corporation (or stockholders, in *Revlon*).²⁹ As a matter of history, it was a sustained failure by plaintiffs to garner judgments on a traditional subjective bad-faith theory that led so famously in *Disney*, and thereafter in *Lyondell*, to the “conscious disregard” facet of bad faith. Importantly, however, conscious or deliberate wrongdoing is required both for *Lyondell* conscious-disregard bad-faith claims and classic subjective bad-faith claims. Those high scienter requirements are very demanding hurdles to clear, and we believe disinterested, independent directors have little to fear, remedially, on either front. The *Chen* case discussed by Professor Manesh serves exactly to support this point because outside directors there were granted summary judgment, notwithstanding the assertion of a subjective bad-faith claim.

The *Chen* case warrants comment for two other reasons not raised by Professor Manesh, however, and we do so only very briefly here, although the points deserve greater elaboration. As he did in his recent *Revlon* article,³⁰ Vice Chancellor Laster deploys in *Chen* the divergent standard-of-conduct/standard-of-review rubric³¹ that we criticize in our original piece.³² He explains that the standard of judicial review—which under *Revlon* is an enhanced, intermediate standard—is more “forgiving” than the standard of conduct, which pertains to the director duties of care and loyalty.³³ We continue to find this analytical construct to be puzzling as seen in *Chen* itself, a case in a summary judgment posture.

29. See *Lyondell*, 970 A.2d at 240 (discussing the intent requirements in bad-faith standards found in Delaware case law); *Disney*, 906 A.2d at 64–66 (looking at different categories of conduct and noting that bad faith requires intent to harm).

30. See J. Travis Laster, *Revlon Is a Standard of Review: Why It’s True and What It Means*, 19 FORDHAM J. CORP. & FIN. L. 5, 26 (2013) (distinguishing the standard of conduct from the standard of review).

31. See *Chen v. Howard-Anderson*, 87 A.3d 648, 666–67 (Del. Ch. 2014) (noting that Delaware corporate law distinguishes between the standard of conduct and the standard of review).

32. See Johnson & Ricca, *supra* note 3, at 210 n.233 (discussing and criticizing the supposed divergent standards of conduct and review in Delaware).

33. See *Chen*, 87 A.3d at 667 (describing the standard of review as “more forgiving of directors and more onerous for stockholder plaintiffs than the standard of conduct”).

Vice Chancellor Laster draws an inference in *Chen* that the directors may have behaved unreasonably in how they handled the corporate sale process, thus possibly failing the “reasonableness” review standard of *Revlon*.³⁴ Yet Vice Chancellor Laster goes on to grant the outside directors summary judgment because the plaintiffs failed to cite evidence to support an inference of bad faith. He observed that speculation as to an improper motive is not enough.³⁵ Thus, although the directors failed at this stage to meet the supposedly more “forgiving” *Revlon* standard of review, they succeeded in resisting liability and gaining summary judgment.

For plaintiffs, this, at best, was a truly pyrrhic victory. Perhaps Vice Chancellor Laster is introducing yet a third standard here—i.e., a standard of liability—that, unlike the standard of conduct, is more demanding than the standard of review, not less. If so, one then wonders what role the “standard of conduct” notion even plays in Delaware corporate law, being neither, apparently, a liability standard nor a standard of review. Indeed, one wonders, more generally, in what respect it is “law” at all. But that is for another day.

In any event, *Chen* splendidly shows how directors today can fail the *Revlon* standard and yet incur no liability. Thus, this decision bolsters rather than “limits” our thesis of *Revlon*’s diminished remedial significance. We think, more generally, that the standard of conduct/standard of review rubric is unhelpful in fiduciary duty analysis and strikingly so in the *Revlon* setting. *Chen* highlights this.

Relatedly, the parties’ burdens in a *Revlon* case remain murky. More clearly than in many cases, Vice Chancellor Laster assigned to directors the burden to show they had met the *Revlon* standard and to show, in seeking exculpation, that they breached only the duty of care.³⁶ But he emphasized, in granting all outside directors summary judgment, that plaintiffs did not cite or provide evidence to support an inference of subjective bad faith.

34. See *id.* at 672–76 (discussing the ways in which the defendant-directors’ conduct may have been unreasonable).

35. See *id.* at 685 (discussing plaintiff’s lack of evidence to demonstrate bad faith through improper motive).

36. See *id.* at 666 (explaining the defendants’ claim that they “at most breached their duty of care”).

Thus, as we contended in our original article,³⁷ notwithstanding ostensible director *Revlon* burdens, whether in seeking preliminary injunctions or money damages, plaintiffs must meet customary burdens to produce evidence. And, quite separate and apart from the narrow *Revlon* standard itself, because the standards for obtaining injunctions or money damages are so high in lawsuits against Delaware directors,³⁸ today they face a substantially dwindled likelihood of being remedially sanctioned under *Revlon*.³⁹ They may (and should), on advice of counsel, seek

37. See Johnson & Ricca, *supra* note 3, at Part IV.A–B (discussing the burden of proof on plaintiffs and directors).

38. See *id.* (explaining the high burden on plaintiffs to successfully bring a claim against investors). Professor Manesh believes it is not the high burden of obtaining an injunction in the *Revlon* context that has resulted in so few injunctions in recent years. Instead, he puts forward a “boy scout” theory of director behavior, where directors are so diligent in complying with their *Revlon* duties that there are few cases of problematic behavior for the courts to address. See Manesh, *supra* note 1, at 136–41 (arguing that “*Revlon*’s shareholder-focused fiduciary mandate has seeped beyond its specific transactional boundaries and found its way into every corporate decision”). As support, Professor Manesh cites the Delaware Chancery Court’s denial of injunctions for a lack of probability of success on the merits in the *Revlon* setting in eleven out of the fifteen reported cases that we reviewed in our Article over the past six calendar years. Manesh, *supra* note 1, at 138–39. We find this argument lacking. The one transaction in the past six calendar years where the Chancery Court did grant an injunction in the *Revlon* context is telling. The injunction granted by the court was a mere twenty-day delay in the holding of the shareholder vote to approve the transaction despite a sales process where the seller’s investment bank was operating on both sides of the deal, and in fact received significantly more consideration in the deal from the buyer for providing buy-side financing than it received from the seller as the seller’s advisor in the sale, and despite the fact that the buyer in the transaction was an amalgamation of two former bidders for the company who teamed up in direct violation of prior agreements with the seller prohibiting such collusion. See *In re Del Monte Foods Co. S’holders Litig.*, 25 A.3d 813, 817–18, 844 (Del. Ch. 2011) (setting out the facts pursuant to the plaintiffs’ claims). It takes very, very problematic behavior to obtain an injunction in the *Revlon* setting.

39. Even in the *Del Monte* case, Vice Chancellor Laster flatly stated:

To hold that the Del Monte directors breached their fiduciary duties for purposes of granting injunctive relief does not suggest, much less preordain, that the directors face a meaningful threat of monetary liability. On this preliminary record, it appears that the Board sought in good faith to fulfill its fiduciary duties, but failed because it was misled by Barclays. Unless further discovery reveals different facts, the one-two punch of exculpation under Section 102(b)(7) and full protection under Section 141(e) makes the chances of a judgment for money damages vanishingly small.

ex ante to comply with the supposed stricture of *Revlon*, as we observed,⁴⁰ but only extraordinary and intentional misconduct will carry any remedial consequences.

Del Monte, 25 A.3d at 817–18, 844. In his next sentence, the Vice Chancellor went on: “The same cannot be said for the self-interested aiders and abettors.” *Id.* at 818. Vice Chancellor Laster appears to be trying to squeeze some utility out of this diminished doctrine, but one wonders if this is a particularly helpful (remedial) use of *Revlon*, and more importantly for plaintiffs, perhaps there are better claims to bring against such conflicted advisers, including claims for a breach of the adviser’s own stricter agency law duties, fraud claims, or breach of contract claims.

40. See Johnson & Ricca, *supra* note 3, at 215–17 (discussing the ex ante role of *Revlon* in lawyer advice to directors in the sale context).