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In the News

The following article appeared in
The National Law Journal

August, 2008

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Breach Case In Company Sale Survives
Ruling Underscores Vulnerability Of Directors to Liability

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Lawyers say a recent Delaware Court of Chancery ruling allowing a trial against corporate directors who approved selling a company for a premium illustrates directors' ongoing vulnerability to breach-of-fiduciary-duty lawsuits — even if their actions benefited shareholders.

Some legal observers say the juxtaposition of the court's ruling addressing the duties of a corporation's directors with a July Delaware Supreme Court decision upholding dismissal of a breach-of-fiduciary-duty case against board members of a limited liability company highlights the greater legal protections LLC directors enjoy.

Both companies had exculpation provisions in their charters or operating agreements to protect board members from certain types of lawsuits, but Delaware law allows LLCs to offer more extensive protections. *Wood v. Baum*, No. 621, 2007 (Del.).

The shareholder class action at issue in the July 29 Chancery decision challenged a $13 billion cash-for-shares acquisition of Lyondell Chemical Co. by Basell AF, a December 2007 deal that created Netherlands-based LyondellBasell Industries. *Ryan v. Lyondell Chemical Co.*, No. 3176-VCN (New Castle Co., Del., Ch.).

A former Lyondell shareholder filed the case against the company's former chairman and chief executive officer, numerous former Lyondell independent directors, Basell and a Basell holding company formed for the merger.

The shareholder plaintiff claimed that Lyondell's directors breached their fiduciary duty of care when selling the company, or their so-called Revlon duties. The Revlon duties, which require directors to maximize value for shareholders when they seek to sell a company, stem from a seminal Delaware Supreme Court case. The plaintiff alleges that the board didn't ensure the very best deal for the shareholders

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because it rushed the deal. *Revlon Inc. v. MacAndrews & Forbes Holdings Inc.*, 506 A.2d 173 (Del. 1986).

Although Vice Chancellor John W. Noble described the $48 per share price for Lyondell stockholders as a ''substantial premium'' and ''very attractive indeed,'' he denied the Lyondell defendants summary judgment on the Revlon claims and set the stage for trial or a settlement.

Noble also detailed a ''troubling board process'' that approved a deal in less than seven days.

''When control of the corporation is at stake…, directors of a Delaware corporation are expected to take context-appropriate steps to assure themselves and, thus, their shareholders that the price to be paid is the 'best price reasonably available,'' Noble wrote.

The opinion, however, rejected the shareholder-plaintiff's other claims, including breach of the duty of loyalty to stockholders, breach of disclosure duties in connection with the merger materials given to stockholders, and the aiding and abetting by the Basell defendants of the Lyondell defendant's fiduciary breaches.

Novel factual scenario

The 73-page opinion discussed the applicability of Revlon to the ''somewhat novel factual scenario'' of an unsolicited sale of a healthy company when the board didn't shop the company and merely served as a ''passive conduit to the stockholders'' for the unsolicited, yet attractive bid.

''The Board, for all intents and purposes, did very little, if anything, to 'seek' the best transaction available to the Lyondell shareholders,'' Noble wrote.

The opinion spells out that Revlon duties are triggered by any proposed sale of a company, not just one initiated by a company and its board, said Clint Krislov of Krislov & Associates in Chicago. Krislov and lawyers from Haverford, Pa.-based Chimicles & Tikellis represented the plaintiff.

''Companies have generally taken the position that they're not required to maximize value unless the sale is initiated by the company's decision to sell,'' Krislov said. ''This obliterates that position.''

Lawyers at Richards, Layton & Finger in Wilmington, Del., and Houston-based Baker Botts, representing Lyondell and the directors, did not return calls for comment. Basell's lawyers at New York's Skadden, Arps, Slate, Meagher & Flom declined to comment.

A lot of lawyers will be surprised the case is going to trial, particularly since the company was sold for a premium, there were no other known buyers and the directors were independent, or not executives of the corporation, said Francis G.X. Pileggi, a corporate lawyer and litigator in the Wilmington, Del., office of Philadelphia-based Fox Rothschild.

''This gives new contours to the Revlon standard,'' Pileggi said. ''The court was trying to say that it's not enough to have somebody give you a good price.''

According to the opinion, Lyondell's corporate charter contained an exculpatory provision protecting its directors from personal liability for breach of fiduciary duty, so the plaintiff must prove the directors failed to act in good faith in approving the merger or were disloyal to the corporation.

Citing a 2006 Delaware Supreme Court case, Noble wrote that ''the Board's failure to engage in a more proactive sale process may constitute a breach of the good faith component of the duty of loyalty as taught in *Stone v. Ritter*.'' *Stone v. Ritter,* 911 A.2d 362 (Del. 2006).

Although it's highly unlikely that the plaintiff can overcome the hurdle of proving that the board didn't act in good faith, the survival of the lawsuit past the summary judgment stage illustrates the need for boards to take their Revlon duties seriously and not allow chief executive officers to run a sale process without oversight, said → **Dick Reinthaler**, a New York partner who co-chairs **Dewey & LeBoeuf's** Securities, Mergers and Acquisitions, and Corporate Governance Litigation Group.

''This provides further reinforcement that any company involved in an M&A transaction needs to pay careful attention to their Revlon duties,'' **Reinthaler** said.

The case seems to be an extension of *Stone v. Ritter* because it's hard to see any cause for board liability not covered by Lyondell's exculpatory charter provision, said Larry Ribstein, a professor at the University of Illinois College of Law in Champaign.

A lone offer from a bidder that would have been likely to balk if the company shopped for other buyers, and a fairness opinion from Deutsche Bank A.G., seemed like a perfect case for giving some respect to the board's business judgment, Ribstein said. ''I'm not sure what the role of exculpatory provisions will be if a board can't escape a trial even on facts like this,'' Ribstein said.

Ribstein said the Ryan decision is particularly startling given its proximity to the Wood decision about the LLC board members, which cited the ''broad'' exculpating provision in the LLC's operating agreement.

''The [Wood] court let the managers off the hook because of the different statutes that applied,'' Ribstein said. ''This will increase firm's incentives to avoid the corporate form when that's feasible.''