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Regulatory: M&A in the Boardroom

How general counsel can assist the board with Revlon duties.

By Gardner Davis
March 23, 2011

The *Revlon* Doctrine requires the board of directors, when dealing with the sale of the company, to seek the best value reasonably available for the stockholders. Moreover, courts apply “enhanced judicial scrutiny” to probe the deliberative process and the information relied upon by the board of directors, as well as the reasonableness of the directors’ decisions.

Although the Delaware courts routinely articulate a policy of deference to the board of directors’ judgment, such as “directors are not insurers” and there is “no single blueprint” that must be followed, the reality is that the Chancery Court is quick to fault the board for not doing enough to satisfy *Revlon* and therefore find a breach of fiduciary duty.

For example, the Delaware Chancery Court recently held that the board of Del Monte Foods Company breached its fiduciary duty in connection with a $5.3 billion leveraged buyout of the company by failing to adequately supervise the sale process in light of an alleged taint arising from the investment bankers’ misconduct. Reviewing recent Delaware Chancery Court decisions, including the notorious *Lyondell Chemical* opinion that was subsequently reversed, it is abundantly clear that the board carries a heavy burden when managing the sale of the company.

Although the board or the special transaction committee will usually rely heavily on outside counsel, the general counsel can and should set the tone for the process and educate the directors regarding the exceptional demands and high standards currently being applied by Delaware Chancery Court.

General counsel must emphasize the need for the directors to engage actively in the process and the personal risks to individual directors of failing to be sufficiently involved. General counsel must push for the directors to meet a sufficient number of times for a sufficient period to adequately deliberate.

The directors should solicit and follow the advice of financial and legal advisors. As part of this process, however, general counsel must be very alert for potential conflicts of interest, and urge the directors to ask potential advisors pointed questions regarding conflicts during the interview process. For example, in *Del Monte*, the board was faulted for not asking the investment banker about potential plans to also seek to represent the buyer in arranging buy-side financing and about ties with certain private equity firms that resulted in an alleged bias to “steer” the deal to another client.

The general counsel must also educate the board that its position under *Revlon* is “materially enhanced” where a majority of the board consists of independent, outside directors. The same result can be achieved where a majority of the board does not consist of independent directors, if authority to act is delegated to a special committee consisting solely of independent directors. The establishment of an independent special committee can serve as powerful evidence of fair dealing.

In the final analysis, general counsel must push for the board to be actively involved in the process, encourage steps to strengthen the likelihood of success and be on the lookout for potential problems that may undermine the integrity of the sale process.

This column is the fourth in a series of articles on the impact of increasing and evolving governmental regulation and reform in the corporate governance arena.

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Read Gardner Davis' previous column.