1) 95

======== **Start of Answer #1 (1183 words)** ========

the tender offer response

When a company is facing a tender offer from a hostile company they may take reasonable action to resist the tender offer. the first inquiry is whether or not there is a tender offer. here the factpatern itself calls the offer a tender offer and so our inquiry could end there, however the tender offer also meets the test of determining if something is a tender offer. it iss for a large portion of the arget companies stock (51%) it is for fixed non negotiable terms, and is acompanied by an anouncement of both the intent to acquire the stock and the intent to acquire the company. though it is unclear whether that price was above market value or not

since there is a tender offer te target board may resist the tender offer under UNICOL so long as two factors are met.

the first is that there is a valid threat to the company, this threat must be more than just the directors will loose their jobs, there must be a threat to the economic interests of the company itself. usually that intails getting a financial advisor to indicate that the offer is inadaquate. in this case the financial advisor that the board hierd indicated that the ofer was adaquate in the first stage however, he also indicated that the debentures paid in the second tier of the transaction would be worthless in a certain situation. this adverse situation with the debentures remained true for boh the first and second offer by Bumber. this could be enough to indicate that there was a valid treat to the company which would alow the board to initiate measures to resist the offers.

the second factor is that the boards response must be reasonable in response to the preceived threat. in other words the response must be proportional. measures are not reasonable if they are draconian, or preclusive. here the boards first response was to amend the articles of incorporation to include a measure that if anyone acquired a 30% interest in H stock then the current shareholders would be allowed to be aditional shares at a price much lower than the tender offers price. from the cases we read in class this poison pill aproach appears to be a fairly common tactic taken by boards of

directors and assuming that there was a valid threat to the company this type of resistance would probably be considered reasoanble. also going to the reasonableness of this s response is the fact that 5 of H's directors are outside directors, and the views of outside directors in defending against a tender offer are given more weight then the inside directors, so if the outside directors voted to approve this response the court will take that into consideration. further more tender offer resistence falls under the duty of care so the business judgment rule and the exculpation statutes apply. for the business judgment rule, so long as the decision was made in good faith and the directors were reasonably informed the court will not second guess the decision of the directors. so as long as the directors meet that test the court will not second guess the reaonableness of this tactic.

as for the response to the second offer by B. in this case the response of H's board was to merge with U. though H would be the surviving corporation of the merger 51% of its stock would then be owned by consolidated. a 51% ownership by a new entity is a change in control of the company, and as such the merger takes the response out of the unicol standard and the revlon duties attach. under the revlon duties the board of directors have the duty to insure the greatest price for their shareholders. they become in essense auctioneers for the company trying to get the highest price for their company. it is unclear from the factpatern if the merger with U or the sale of stock and merger with B would provide the beter price for the shareholders, but they have the duty once they decide to merge to get the best offer they can. — Should have kept process going.

Good.

the Proxy statement

H is a company with over 500 shareholders and over 10 million in assets, as such they have certain duties under the securities and exchange laws, especially the 1934 act. specifically, based on thsi fact patern, they have a duty not to make a false or materially misleading statement in a proxy statement. here the directors of H issued a proxy statement to their shareholders to change the articles of incorporation in an attempt to block a tender offer by B. in this case the directors told share holders that B had lost

money in the last three fiscal years, which was false, they had not lost money in one of the last three fiscal years. this is a false statement in a proxy statement.

the next issue is whether the statement was material. a statement is material if a reasonably prudent investor would have believed the statement was important. in this case the statement that B was continuously losing money as oposed to only mostly loosing money was very important when making a decision about whether to block a merger with B and would be important to the shareholders when deciding whether or not to approve the resistance measures aproved by the board.

because the action involved amending the articles of incorporation the board needed the votes of the shareholders, as such the vote was a required vote. because the vote would be needed there is causation.

the proxy solicitation was in connection with the sale or purchase of securities. it was initially spurred by a tender offer of B to purchase 51% of H's stock, and the resolution itself was to allow the voting shareholders to buy stock cheaply if B succeeded in gaining a 30% share of the company.

don't need the "connection" req - only 10b-5

as such there may be a cause of action against the board of directors of H for providing a materialy false statement in a proxy solicitation.

the promise to submit the merger to the shareholders even if the board no longer agreed with it is not a breach of the directors duties.

a board of directors may submit a merger agreement to their shareholders even if they no longer support the merger. that first part of their agreement, the agreement to submit the merger to the shareholders under any condition is enforceable. however, a shareholder cannot contract away their fiduciary dities.

Excellent

Directors owe the fiduciary duty here.

exculpation clause.

this is a delaware company and the articles of incorporation provide that the directors liability is limited to the fullest extent of the law. delaware has an exculpation statute that releaves directors from personal liability for any breaches of the duty of good faith, so long as they are not done in bad faith. because of this the companies directors will not

have personal liability for any breaches of the duty of care they may have done, so long as those breaches were not done in bad faith.

======== End of Answer #1 ========

2) 95

======== Start of Answer #2 (1562 words) ========

WILL THE COURT FOLLOW THE COMMITTEE'S RECOMMENDATIOON AND DISMISS THE DERIVATIVE SUIT

Under the internal affiars doctrine the state of incorporation laws will govern disputes. As such, Delaware General Corporations Code and Delaware case law apply to any action taken by the Judy against Fred and the directors of Mixer

A derivative suit is in essense a consolidation in equity of two suits, the first by the plaintiff shareholder agains the directors seeking an order that they pursue a wrongdoer for the corporation, and second the suit by the corporation agains the wrongdoer.

In Delaware a shareholder plaintiff is required to exhaust intracorporate remedies be demanding the the directors take action. Judy is a shareholder so she does have standing. Judy made no demand. However demand may be excused if Judy can show it was futile to demand. The court in *Aronson* held that the question of demand futility is intextrricably linked to the Business Judgment Rule. the Business Judgment Rule is a strong presumpiton tha the directors act on an informed bassis in the utomost good faith and in the honest beleif their actions were in the best intrerest of the corporation, the direcots must first satisfy Unocal's enhanced judicial scrutinty. Under *Aronson* in order for demand to be excused the plaintiff mast plead with particularity a reasonable doubt as to the disintrest or indepndence of the directors or a reasonable doubt that the aciton taken was within the realm of a valid exercise of business judgment.

Here Judy alleged that the boards was not indendent as it was controlled by Fred. A lack of independence can be shown by the facts that a particular board is controlled by one party and that the other directors may feel dependent on that director. However, the mere threat of personal liability is not enough to show that they are interested or not independent. The facts do not state what if any, Judy used to try and convince the court that thre was a reasonable doubt that the directors were indenpendent beyond the

mere fact that Fred controlled the board. Without more particularized facts for the court to be able to determine interstedness on a director by director basis Judy has likely not met the *Aronson* requirements.

SPECIAL LITIGATION COMMITTEE

A board may appoint a special litigation committee to determine whether to pursue a derivitive action. Unlike New York Law (*Auerbach*), in Delaware there is a more difficult burden placed on the board. In *Zapata* the court held that in determining whether or not to reject a shareholder derivitive suit the initial burden is on the board of directors to show that they are disinterested and indpendent, acted in good faith, and reasonably investigated. Even if this burden is shouldeder by the directors the cour in Delaware will then apply its own independent bunisess judgment as to wether the decision to reject the derivative suit is protected.

In this case it will be difficult for the directors to show that the special litigation committee was independent as it includes Fred's lawyer and the investment banker who made the loan to Delicious for acquisition of the McDowells' restaurant. There is a substantially likelyhood the Fred's lawyer will not be considered a distintersted party. Furthmore there are no facts to suggest and reasonable investigation, or even that they acted in good faith. Furthermore, it seems unlikely a truly independent and corrrectly function litigation committee would not find a violation of the duty of loyalty in essentially using Mixers assets as collateral and Fred's use of Mixers to make Delicious profitable at the expense of Mixers. Given these fact the court will likely not follow the committee's recommendation and won't dismiss the lawsuit. Judy has a right as a shareholder to force the corporaiton to pursue remedies against a party that harmed the corpoiation.

FRED'S DUTIES

Fred is a director, officer and shareholder of MIxer. As such he owes the fiduciary duties of care and loyalty to Mixer. In is conduct as a director he is protected by the

business judgment rule, supra. The presumption of the business judgment rule can be rebutted by a showing that the directors breached their fiduciary duties of care or loyalty, were interested in the transaciton, acted not in good faith, or acting in bad faith. Determining a breach of the duty of care is based on a gross negligence standard which can be found when a board fails to adequately inform themselves or adequately assess the interests of shareholders. The court in *Disney* held that a failure to act in good faith requires a showing of something qualtitatively different from and more culpable than the gorss negligence standard used to show violations of the duty of care. While not every bad faith action will equate to a breach of the duty of loyalty, in circumstances in which drectors fail to act, the face of a known duty to act, thereby constituting a conscious disregard for their responsibilites, a bad faith act will equate to a breach of the duty of loyalty.

Here, Fred is basically gutting Mixers in order to fund Delicious of which he is the whole shareholder. Although Fred owes the duties discussed above to both Delicious and Mixers he is clearly favoring Delicisous's interest to Mixers. This is a breach of the duty of loyalty to Mixer and Mixers sharheolders.

SAFE HARBOR STATUTE

Under Delaware General Corporations Code Section 144 when a director is on both sides of a transaction, i.e. intrested, they have the heavy burden of showing the utomost good faith and scrupulous inherent fairness of the transaction. This burden can be lifted by fully disclosing all material information relating to the conflict to the board and ahve the board approve by a majority of disinterested directors (even if less then a quorom) the transaction. If this happens the protection of the BJR applies. Here, the majority of directors did approve the transaction. However, there is good cause to beleive that the direcotrs are controlled by Fred and therefore were not indpendent or disintrensted. This will not invoke protection of the business judgment rule as this was an intrested decision and furthrmore. Even if it was protect by the business judgment rule the Direcotors would likely be liable for Corporate Waste. A showing coprorate

waste requires that no ordinary business person of sound judgment would beleive that the consideration recieved in the transaction was adequate. Here Mixer recieved nothing really, sure they get to sell some of their machines but it is at a discount. THe board of directors will likley be liable under the derivative suit for corporate was and as such under Delaware General Corporations code section 145(b) the will not possibly be indmenfied by the coporation because they will have personally liability under a judgement to the corproation. Futhermore, Mixer's certification of incorporation has a provision under Delaware General Corporations Code section 145(f), allowing a Delaware corporation to adopt its own indemnification rules, this does not allow for indemnificiation for a breach of duty of loyalty, i.e. corporate waste.

CORPORATE OPPORTUNITY DOCTRINE

Under the corporate opprtunity doctrine, line of business test from *Guth* a director may not take advantage of an opportunity if the corporation is financially able to exploit it, the corporation has an interest or expectancy in the opportunity, the opportunity is in the line of business of the corporation and exploiting of the corporation would place the director in a situation inimical to his duties to the corporation.

Here Fred would argue that Mixers could not afford to exploit the opportunity. This claim will fail as even though Mixers did not have enough cash Fred still got the board to use the assets of mixers as collaterol to fund the purchase of McDowell Brothers by Delicious. This could have been done to fund a loan to for Mixer to purchase McDowell Brothers. Mixers had an expectancy and an interest in McDowells as they were interested in being pruchased by MIxer and they were purchasing large amounts of Mixers milkshake machinges. Furthermore by exploiting the opportunity Fred has placed himself in a position inimical to his duties to Mixer, in that he if using Mixers to fund Delicsicous at Mixers loss.

Fred will argue that a burger restaurant is not within the line of business of Mixer corporation whose only known function to manufacture milkshake machines. Although

the line of business test is used when the director is placed in direct competion with the corporation, under the ALI method there are times when the line of business test is not appropriate. This is arguably one of those cases, but doubtful to the the prior sales history and connection and interest between McDowell and Mixers. However, the director can still violate the corporate opprotunity doctrine under the ALI theory by failing to fully dislcose it to the board and have it rejected by the board. Fred will argue he did disclose the opportunity to the board. This argument lacks merit as his would be disclosre was really a request to the board he controlled to use Mixers assets as collateral. This did not give the board an opportunity to take the the opportunity. Furthermore, the certianly never actually rejected the opprotunity.

Fred Will be liable to the corpoation for any profits earned by Deliscious is taking the corpoate opportunity of Mixers

3) 90

======== **Start of Answer #3 (1391 words)** ========

Bill's 16b Violation

Rule 16b makes Directors and officers and 10% shareholders liable for "short swing trades" or the sale or purchase of stock in any 6 month period and they must disgorge any "profits" made back to the corporation. For there to be jurisdiction for a 16b action the corporation must either be publicly traded on a stock exchange, or there must be at least 10 million in assets and over 500 shareholders. Here we have 750 shareholders and 20 million in assets. Thus jurisdiction exists. While 16b was arguably created in an attempt to stave off insider trading, unlike 10b-5 there is no scienter requirement. The party is strictly liable for their trades. Further, 10b-5 is punitive in the sense that profits are determined by taking the lowest buy and matching it to the highest sale price.

Here Bill is an officer, thus he qualifies as a proper party under 16b. Further in a 6 month period he made three trades: a sale for 50,000 shares at $100; a purchase for

100,000 shares at $50; and a sale of 100,000 shares at $90. The court would first use the first sale made on June 15th and subtract 50,000 at $50 bought from his broker. The remaining 50,000 shares sold would be matched against the $90 sale price. Thus, Bill's total liability would be in the amount of 4.5 million dollars.

Janice, Martha, Rick and Tammy are not directors or officers. Nor do the facts state they ever went over the 10% threshold, thus they would not be liable under 16b. However, they may be liable under 10b-5

Rule 10b-5

It is unlawful for any person, either directly or indirectly, through any instrumentality of interstate commerce or the mails, to employ any manipulative or fraudulent device, in conjunction with the sale or purchase of securities. Courts have subsequently ruled that 10b-5 includes a prohibition against insider trading.

In order for the SEC to punish either criminally or civilly they must show; 1) Jurisdiction; 2) Material Fraudulent or misleading statement or ommission (if ommission that there was some fiduciary duty); 3) scienter. For a private action to lie there also must be present; 4) the P must have sold or purchased shares; 5) reliance and causation; 6) Damages.

Here, most likely all of the actions will be brought by the SEC either criminally, or civilly since there are no facts regarding traders on the opposite sides of the transactions. However, in 1988 laws were passed which allow plaintiff's who purchase or sold securities concurrently with insider traders to proceed in a private action.

Good point

Note on Jurisdiction

The jurisdiction element will be met if the stock is publicly traded on the stock exchange

or the traders used any instrumentality of interstate commerce. Here based on the ease at which each individual was able to purchase shares I assume that this is a publicly traded stock.

Materiality

In order to be found liable under 10b-5 the information traded upon must be material. Materiality is defined as what a reasonable person would find important in determining whether to trade in the security.

Janice Liability Under 10b-5

Here the SEC will argue, in an attempt to find Janice liable under 10b-5 that she had insider information (that they were buying new mining equipment) and she owed a fiduciary duty to the corporation. Thus, if she were to trade this would fit under the category of an ommission. However, Janice will argue that in order to have liability under 10b-5 the information must be material. She would argue that companies purchase new equipment all the time and it wouldn't be something which would affect the decision making process of the average investor. SEC will argue that she had reason to believe that they were opening up a new mine and this was really the purpose of her trade and the insider information. Maybe she knew, as well as Bill, that you don't purchase new equipment without a new mine. Further, the SEC would argue that as an accountant at the company she has a fiduciary duty to it not to trade on insider information. However, Janice will argue that she did not have scienter. Scienter is the intent to mislead, or defraud, or in this case to make use of the insider information for personal gain. Janice will argue that she bought the shares because she "wanted to invest in the company she worked for" and not to profit off of insider information. If the court believes her then she will not be liable either criminally, civilly to the SEC or in a private action.

Bill 10b-5

Bill is an officer of the corporation and so owes a direct fiduciary duty not to trade on insider information. He did trade directly on the insider information with the intent to make money off of his insider knowledge thus he does so with scienter. Bill may argue that the information he was relying on was only his guess that the company was about to announce a new mine and thus it wasn't material information. Here the insider information is technically regarding something that hasn't occurred yet and so the court may employ a balancing test to determine if the information is truly material. They will look to see, what at the time was the probability of the transaction occurring and if so what impact would it have on the share price. The SEC would argue that a new mine would be considered a big deal since it could dramatically effect Diamonds (D) bottom line and share price. Further, it was very likely to occur because as Bill "knew" they don't purchase gear without a new mine. Thus it is reasonable to assume that a reasonable investor would find this information important in whether to buy or sell shares of the company. Bill has a fiduciary duty, traded with insider knowledge, and did so with scienter. Thus he could face criminal and civil penalties from the SEC.

Nicely argued

Tipper Bill

Bill also would be considered a Tipper. A "tipper" is one who owes a fiduciary duty to a corporation and shares insider information for their own personal benefit. "Personal benefit" has been defined very broadly and would include friends such as Martha. Thus when he called Martha and gave her the information he would be liable and the SEC could prosecute criminally and civilly.

Tippee Martha

Martha would be liable to the SEC both criminally and civilly for her trade as a tippee if 1) she knew that Bill the tipper had a fiduciary duty not to disclose owed to the corporation; 2) traded on the insider information. Here, Bill tries to shield her by only telling her that she should trade and not why. She will argue that she didn't know that

Bill had a duty not to disclose because she didn't know why he was telling her to buy. The SEC will argue that she, as a friend should know that Bill owes a general set of fiduciary duties to the corporation, and she traded on the information although not knowing. She will retort that there is no way she could have had scienter since she could not have intended to trade on information she had no knowledge of. This would be a tough call if it went to trial.

Misappropriation Rick.

The SEC would argue that Rick misappropriated the insider information which he used with the intent to capitalize on the insider information (done with Scienter he put the note in his pocket and traded on the ill gotten information the next day). Misappropriation is a theory which allows 10b-5 to cast a wider net to include those who don't normally owe a fiduciary duty to the corporation to be found liable under 10b-5. Thus Rick, even if he was not directly employed by Diamond, was employed by a janitorial company which owed a duty to diamond. Thus this limited fiduciary duty not to trade on misappropriated insider information would apply to him as well. Thus he would be liable under 10b-5.

Tammy

The wide net of misappropriation would fall short of Tammy. 10b-5 does not regulate insider trading from those who learn insider trading inadvertently or through due diligence without owning any fiduciary duty to the corporation. Thus, the SEC's reach would not extend to Tammy.

======= End of Answer #3 =======

END OF EXAM