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DELAWARE'S GUIDANCE: ENSURING EQUITY FOR THE MODERN WITENAGEMOT

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INTRODUCTION

THE board of directors is the central focus of corporate law. This institution is a structure inherent to the governance of collective human enterprise. History recurrently offers the paradigm of a single executive, supervised and selected by a board of advisers that itself serves a larger group.[1] One interesting example of this historical phenomenon is the English Witenagemot, or Witan Council. An Anglo-Saxon import to the British Isles, it selected the English King (or confirmed a generally accepted successor), advised him in the perils of state, and represented the interests of the landed gentry that stood to profit from his munificence. The Witenagemot was, in many ways, the precursor to the larger and more powerful English Parliament, and it controlled the bulk of socioeconomic wealth of the period. Turning to the present day in America, economic resources are controlled overwhelmingly by publicly traded corporate entities, the majority of which are incorporated in Delaware. Delaware's sophisticated judiciary is widely recognized as one reason incorporators choose Delaware as the home for their charters.

Social animals have the evolutionary advantage of specialization, the economic value of which is well explored in Adam Smith's *Wealth of Nations*.[2] Yet, the social group, when acting collectively, must negotiate both over the allocation of the spoils of victory and the risk of new ventures. The board, the council, or the Witenagemot is the locus of this negotiation throughout history. It exhibits a useful symmetry; representation distills the various factions into a small enough number of individuals to be cohesive enough to debate contested matters efficiently, while still fairly representing the potentially disparate interests of their constituencies. The board, typically ranging from six to twelve members, represents this critical mass of collective action.[3]

Another developmental step in the evolution of social groups is the invention of nonviolent means for dispute resolution. Law students may be

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1. For instance, the Shogunate of Japan relied on the Han Daimyo, and the Roman Catholic Papacy has the College of Cardinals. *See* Ardath W. Burks, *Administrative Transition from Han to Ken: The Example of Okayama*, 15 [No. 3] FAR E.Q. 371, 375–77 (1956); John Paul II, *Apostolic Constitution Universi Dominici Gregis*, 88 ACTA APOSTOLICAE SEDIS, Feb. 22, 1996.
2. ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS (Edwin Cannan ed., Methuen & Co. Ltd. 1904) (1776), *available at* http://www.econlib.org/LIBRARY/Smith/smWN.html.
3. *See* Charlie Deitch, *Recipe for Logjam: Start With Too Many Cooks*, CORP. BOARD MEMBER MAG., Nov./Dec. 2002, *available at* http://www.boardmember.com/issues/archive.pl?article_id=11284.

Electronic copy available at: http://ssrn.com/abstract=1130088

familiar with the torts history lesson of how the wergeld evolved in ancient Germany.[4] Damages awards fulfill a societal need for restitution and create incentive for responsible participation in the societal enterprise, even when individual interest may, at times, be otherwise more rationally anti-social. As the institutions of judicial authority developed, a method for controlling the anti-social actions of those before it arose in the form of the injunction.[5] The English High Court of Chancery is the historical foundation for that power in Delaware law.[6]

The work of the Delaware Court of Chancery and the Delaware Supreme Court in the arena of corporate law, focusing as it does on the relationship between shareholders, management, and the board of directors, represents a fusion of these two social constructs. This fusion is exhibited in the Courts' review of director and management decisions that control the daily life of the modern, corporate version of the Witenagemot. The two distinct joints in the corporate law system are the points at which responsibility coalesces from the large group to the smaller collective, and from the collective into the singular. These points serve as the foci of judicial interest as courts design legal incentives for the collective negotiation process, through neutral arbitration. In this process of arbitration, judges have created different standards of review and conduct for each of the groups defined by these points. Moreover, this development is further complicated in Delaware's corporate law because the disputes are primarily economic, and thus require increased predictability and efficiency—since all parties typically hope to get back to the business of profit as quickly as possible, there is great benefit in being able to predict future outcomes.

The Delaware Court of Chancery, as an equity court, has wide latitude to craft remedies and mold precedent to fit particular fact patterns in the tradition of the English High Court of Chancery.[7] This fact has allowed the

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4. Anglo-Saxon legal codes consisted "mainly of schedules of payments for common types of wrongs. . . . They specified gelds, which fixed the value of things destroyed, and bots, which fixed payments for damage, including bodily harm. The payment due for killing a person was the wergeld (or wergild), or man-price." Emily Sherwin, *Compensation and Revenge*, 40 SAN DIEGO L. REV. 1387, 1398 (2003).
5. *See generally* David W. Raack, *A History of Injunctions in England Before 1700*, 61 IND. L.J. 539, 539–40 (1986).
6. "The rules of injunctions, like the rules of equity generally, were a product of the institution of the Court of Chancery." *Id.* at 539.
7. The Delaware Court of Chancery "stands as one of the few remaining separate courts of general equity jurisdiction in the nation. It continues to claim essentially the same subject matter jurisdiction possessed by the High Court of Chancery of Great Britain as of the time of the separation of the American colonies in 1776." DONALD J. WOLFE, JR. &

Court of Chancery to maximize efficiency in resolving disputes, while undercutting the future applicability of precedent, which has led to a tension between efficiency and predictability. If precedent were followed absolutely, it would be highly predictable but not flexible, and thus could not deal with difficult problems efficiently. Were courts to read precedent more loosely to respond to unique situations, it would become less predictable. One commentator has argued that this indeterminacy in the Delaware courts is purposeful;[8] yet, it would be more accurate simply to characterize this indeterminacy as a natural drawback to the tension between efficiency and predictability that plagues all courts of equity.[9] Many of the activities undertaken by members of the Delaware judiciary in their unofficial capacity as commentators and observers of corporate adjudication, which we have termed the "Guidance Function," seek to minimize this element of uncertainty.

The purpose of this Article is to examine some of the extrajudicial activities in which members of the Delaware judiciary engage to minimize the systemic indeterminacy that results from the resolution of economic disputes by a court of equity.[10] Such activities come in three unique forms: 1) the frequent speeches and articles issued by the judges about the direction and patterns they perceive in case law from their unique vantage point at the center of the maelstrom; 2) the analysis in the judges' opinions that, though technically dicta, provides useful insight into how open questions not part of the ruling might be expected to play out in the future; and 3) the roles the judges often undertake as formal policy makers, as members of committees of the American Bar Association ("ABA") and other model rule making bodies.

MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 1-1 (2005).

8. *See* Ehud Kamar, *A Regulatory Competition Theory of Indeterminacy in Corporate Law*, 98 COLUM. L. REV. 1908 (1998).

9. For a similar observation that is over 300 years old, see JOHN SELDEN, *Equity*, *in* TABLE TALK (1689), *as cited in* WOLFE & PITTENGER, *supra* note 7, at vii (opening quotation):

> Equity is a rougish [sic] thing. For Law we have to measure, know what to trust to; Equity is according to the conscience of him that is Chancellor, and as that is larger or narrower, so is equity. 'Tis all one as if they should make the standard for the measure we call a "foot" a chancellor's foot; what an uncertain measure this would be! One Chancellor has a long foot, another a short foot, a third an indifferent foot. 'Tis the same thing in the Chancellor's conscience.

10. Though the Delaware Supreme Court is not itself a court of equity, as a court of appellate jurisdiction over a court of equity it is appropriately analyzed together with the Court of Chancery for the purposes of this Article.

I. ACADEMIC COMMENTARY ON INDETERMINACY IN DELAWARE'S CORPORATE CODE

The intent of this Article is, in part, to address the views of a few scholars who argue that Delaware's dominance in the interstate competition for corporate charters is the result of the indeterminacy of Delaware corporate law. Professors Jonathan Macey and Geoffrey Miller argue that the indeterminacy of corporate law accrues to the benefit of the Delaware bar, keeping its members employed with bountiful litigation.[11] Moreover, Professor Ehud Kamar posits that Delaware purposefully maintains a level of indeterminacy for an advantage in the interstate competition for corporate charters, which prevents other states from effectively challenging Delaware's primacy as the source of American corporate law.[12] However, the Delaware judiciary's exhaustive extrajudicial activities to minimize the level of uncertainty in corporate law, especially in those areas subject to principle-based governance standards,[13] argue against the validity of either of these views.

A review of Kamar's work is appropriate. Kamar's contribution to the competition debate is to highlight what he calls "the well-documented indeterminacy of Delaware corporate law, which is evident in the state's ample use of vague standards that make prediction of legal outcomes difficult."[14] He presents three examples of these "vague standards": the reasonableness test for deal protection measures; the doctrine of corporate opportunity; and the two-fold *Aronson* test of a special committee's decision to dismiss derivative litigation.[15] As an example of similar cases that seem to diverge from a principle, he compares *Paramount v. Time*[16] with *Paramount v. QVC*[17] to show that distinctions in the case law can sometimes only be resolved by limiting the holdings to their particular facts.[18]

Granted, the standards are not exact. The predictability of judicial response to each permutation of a certain deal measure or structure is not absolute. Yet, any resulting vagueness is not part of an effort to entrench

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11. *See* Jonathan R. Macey & Geoffrey P. Miller, *Toward an Interest-Group Theory of Delaware Corporate Law*, 65 TEX. L. REV. 469, 491–98 (1987).
12. *See* Kamar, *supra* note 8.
13. For an examination of how Delaware switches from principles-based oversight to rules-based, in requisite need, see Sean Griffith & Myron T. Steele, *On Corporate Federalism: Threatening the Thaumatrope*, 61 BUS. LAW. 1 (2005).
14. Kamar, *supra* note 8, at 1909.
15. *Id.* at 1915–17.
16. Paramount Commc'ns, Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1990).
17. Paramount Commc'ns, Inc. v. QVC Network, Inc., 637 A.2d 34 (Del. 1994).
18. Kamar, *supra* note 8, at 1918.

Delaware as a state of incorporation without care for the erosion of shareholder wealth by artificial uncertainty in the code. Certainly, bright-line rules could be drafted that would make this indeterminacy disappear, but bright lines do not always lend themselves to this field of law, which is fraught with fiduciary duties that rise and fall with the tides of human conscience. The words of Judge Benjamin Cardozo are here appropriate:

> [Certain] relations in life . . . impose a duty to act in accordance with the highest standards which a man of the most delicate conscience and the nicest sense of honor might impose upon himself. . . . Whether novel situations are to be brought within [this] class of relations . . . must be determined, as they arise, *by considerations of analogy, of convenience, of fitness, and of justice*.[19]

More recently, former Delaware Chief Justice E. Norman Veasey reminded us that "[t]he expectations for director conduct evolve over time as business mores evolve, with courts applying the evolving expectations in a common law process in deciding the proper standard of review to apply in specific circumstances."[20]

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19. BENJAMIN N. CARDOZO, THE NATURE OF THE JUDICIAL PROCESS 109–10 (Yale Univ. Press, 8th ed. 1938) (1921) (emphasis added).

20. E. Norman Veasey & Christine T. Di Guglielmo, *What Happened in Delaware Corporate Law and Governance from 1992–2004? A Retrospective on Some Key Developments*, 153 U. PA. L. REV. 1399, 1405 (2005). In more detail, he later adds:

> In fact, criticism of Delaware fiduciary duty law because it is indeterminate is misplaced or disingenuous. A flexible or indeterminate regime, such as we have had in Delaware, is distinct from a rigid codification system that prevails in many systems outside the United States. That is part of the genius of our law. Life in the boardroom is not black and white; directors and officers make decisions in shades of gray all the time. A "clear" law, in the sense of one that is codified, is simply not realistic, in my view. There can be no viable corporate governance regime that is founded on a "one size fits all" notion. Fiduciary law is based on equitable principles. Thus, it is both inherently and usefully indeterminate, because it allows business practices and expectations to evolve, and enables courts to review compliance with those evolving practices and expectations.
>
> The judicial articulation of fiduciary duty law in Delaware is constantly evolving and has developed over about eight or nine decades. It is the quintessential application of the common law process. Directors are fiduciaries, duty-bound to protect and

Kamar argues, however, that the specter of indeterminacy affects a corporation when it is unable to account sufficiently for judicial response to a considered business decision, has to incur costs for legal advice, and faces the risk of litigation over its decision.[21] His main justification for the presence of artificial indeterminacy is the network externality of Delaware corporate law.[22] The network externality of incorporation in one state is the increasing benefit realized by all participants as more firms incorporate in that state. As more firms begin using the same code, more attorneys are able to specialize in that corporate code, and thus more firms are able to take advantage of that specialized body of knowledge in business planning. This benefits the chosen state as well as the attorneys who regularly refer to that state's code. Kamar argues that if Delaware corporate law decisions were more determinate, then other states would be able to replicate Delaware's corporate code and thereby tap into Delaware's network externality benefit.[23] Because Delaware maintains indeterminacy through the judiciary's interpretation of the code, however, firms incorporated in other states cannot reliably look to Delaware corporate law for guidance about the law in their state of incorporation. Thus, Kamar argues, copying Delaware becomes impossible because the code is purposefully ill-defined at any point which another state's copycat code might mimic.[24] Thus, the other state's code cannot simply plagiarize the Delaware General Corporation Law ("DGCL").

But even if a robust law-and-economics analysis of Delaware corporate law, which Kamar does not offer, would evince an advantage to Delaware from indeterminate standards, it still does nothing to show that the indeterminacy is purposeful or contrived. Specifically, the Guidance Function, which this Article explores, indicates exactly the opposite. The Delaware judiciary is cognizant of the effect on business planning that any systemic

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> advance the best interests of the corporation. When those interests conflict—or may conflict—with the personal interests of the fiduciaries, the fiduciaries' interests must be sublimated to those of the corporation. The evolution of fiduciary principles occurs not only because courts must decide only the cases before them, but also because business norms and mores change over time.

Id. at 1412–13.

21. Kamar, *supra* note 8, at 1919.
22. *Id.* at 1923. Network externalities are an economic concept that describes how some benefits to a product that may be unappreciated in its initial demand could increase as more people use the product, thus generating a higher product value to the initial consumer who has already obtained full use of it. *Id.*
23. *Id.* at 1924.
24. *Id.* at 1928–29.

uncertainty in an equity court's rulings may have and, therefore, vigorously attempts to minimize that uncertainty for the benefit of business planners. Indeed, Kamar notes that part of Delaware's network externality is buttressed by the fact that, with one distinct winner of the incorporation competition, "[l]awyers can also refer to the legal commentary, reference tools, and professional symposia that proliferate around a commonly used law."[25] That observation misses a vital fact: Delaware judges are major contributors to those secondary sources. Indeed, they contribute to Delaware's network externality advantage by decreasing the level of indeterminacy inherent to Delaware law, which is further evidence that the indeterminacy of Delaware corporate law is an unintended product of arbitration through courts of equity.

II. SPEECHES AND ARTICLES AS ELEMENTS OF THE GUIDANCE FUNCTION

Members of the Delaware judiciary frequently speak at conferences hosted by the ABA, law schools, and a variety of other legal institutions.[26] Many of these speeches form the basis for articles that are published in academic or peer-reviewed journals, which collectively serve as a secondary source for American common law.[27]

Any analysis of the Guidance Function that focuses on the use of speeches and articles to signal the evolutionary direction of Court of Chancery and Delaware Supreme Court jurisprudence, must necessarily begin with former Chancellor William T. Allen. No one better articulated why corporate law is so naturally fluid:

> The law, like ourselves, is always in flux, always becoming. We accept, or invent, or reconstitute structures in the flux because we want order (some of us more than others) and predictability. The concept of the corporation is such a structure. For a long period it seemed settled, although it was not; it seemed known, even boring. The concept of the corporation became problematic only because real world economic forces changed, and those changes exerted

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25. *Id.* at 1924.
26. For a compilation of some of those appearances, see Lawrence A. Hamermesh, *The Policy Foundations of Delaware Corporate Law*, 106 COLUM. L. REV. 1749, 1788 (2006).
27. Such articles have appeared in the *Virginia Law & Business Review* and many other law journals, including *The Business Lawyer*, *Delaware Journal of Corporate Law*, *Harvard Law Review*, *New York University Law Review*, *Northwestern University Law Review*, and *Virginia Law Review*.

> pressures that forced legal change. But the ever-emergent quality of law suggests that the resolution of the conceptual conflict that was reached in the late 1980s by the endorsement of the entity concept, will not be a final answer to the question, what is a corporation.[28]

One of the valuable insights that readers of the Delaware judges can gain, as we shall see, is a window into the courts' thoughts on an issue. Former Chancellor Allen provided one of the first examples of this fact in 1990 in an article based on a speech he gave at the University of California–San Diego's Seventh Annual Securities Regulation Institute, about the role of independent directors in management buy-out transactions. With candor, he admits:

> [A]s one who has reviewed in one way or another a fair number of special committees in a sale context, I remain open to the possibility that such committees can be employed effectively to protect corporate and shareholder interests. But I must confess a painful awareness of the ways in which the device may be subverted and rendered less than useful. I conclude, as well, that it is the lawyers and the investment bankers who in many cases hold the key to the effectiveness of the special committee.[29]

Yet, he also advises:

> The factor that distinguishes those circumstances in which the decision of a committee of outside directors has been accorded respect and those in which its decision has not, is not mysterious. The court's own implicit evaluation of the integrity of the special committee's process marks that process as deserving respect or condemns it to be ignored. When a special committee's process is perceived as reflecting a good faith, informed attempt to approximate aggressive, arm's-length bargaining, it will be accorded substantial importance by the court. When, on the other hand, it

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28. William T. Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV. 261, 279 (1992).
29. William T. Allen, *Independent Directors in MBO Transactions: Are They Fact or Fantasy?*, 45 BUS. LAW. 2055, 2056 (1990).

> appears as artifice, ruse or charade, or when the board unduly limits the committee or when the committee fails to correctly perceive its mission—then one can expect that its decision will be accorded no respect.
>
> . . . .
>
> . . . [T]he court will be mindful that claims of so-called structural bias in the process are plausible; and, that the court's own power of perception is limited. Thus, in a sale context, counsel for a special committee must accept from the outset that as a practical matter she will have to demonstrate that the special committee's process had integrity; that the committee was informed, energetic and committed in this transaction to the single goal of maximizing the shareholders' interest.
>
> Please don't mistake me. This is not a call to pay even greater attention to appearances; it is advice to abandon the theatrical and to accept and to implement the substance of an arm's-length process.[30]

A mere four years later, the *Kahn v. Lynch* opinion's enhancement of the review of independent director bargaining on behalf of minority shareholders made former Chancellor Allen's observations especially prescient.[31] The following two excerpts from the Supreme Court's opinion, when contrasted with former Chancellor Allen's analysis from the secondary source cited above, provides a uniquely insightful exercise for developing an appreciation for the Delaware Guidance Function:

> The power to say no is a significant power. It is the duty of directors serving on [an independent] committee to approve only a transaction that is in the best interests of the public shareholders, to say no to any transaction that is not fair to those shareholders and is not the best transaction available. It is not sufficient for such directors to achieve the best price that a fiduciary will pay if that price is not a fair price.[32]

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30. *Id.* at 2060, 2062.
31. Kahn v. Lynch Commc'n Sys., Inc., 638 A.2d 1110 (Del. 1994).
32. *Id.* at 1119.

> . . . .
>
> The Court of Chancery's determination that the Independent Committee appropriately simulated a third-party transaction, where negotiations are conducted at arm's-length and there is no compulsion to reach an agreement, is not supported by the record. Under the circumstances present in the case *sub judice,* the Court of Chancery erred in shifting the burden of proof with regard to entire fairness to the contesting Lynch shareholder-plaintiff, Kahn. The record reflects that the ability of the Committee effectively to negotiate at arm's length was compromised by Alcatel's threats to proceed with a hostile tender offer if the $15.50 price was not approved by the Committee and the Lynch board. The fact that the Independent Committee rejected three initial offers, which were well below the Independent Committee's estimated valuation for Lynch and were not combined with an explicit threat that Alcatel was ready to proceed with a hostile bid, cannot alter the conclusion that any semblance of arm's length bargaining ended when the Independent Committee surrendered to the ultimatum that accompanied Alcatel's final offer.[33]

This accurately reflected an increasing willingness on the part of Delaware judges to look beyond mere technicalities when assessing the independence of directors. This lesson would become all the more relevant for assessing independence in the context of reviewing dismissal of litigation. This growing line of thought can be seen culminating nearly thirteen years later in the decision of *In re Oracle*, in which Vice Chancellor Leo E. Strine, Jr. held, in the context of director independence for the purposes of dispensing with the demand requirement for derivative litigation, that

> [s]ummarized fairly, two Stanford professors were recruited to the Oracle board in summer 2001 and soon asked to investigate a fellow professor and two benefactors of the University.
>
> . . . .

33. *Id.* at 1121.

> It seems to me that the connections outlined in this opinion would weigh on the mind of a reasonable special litigation committee member deciding whether to level the serious charge of insider trading against the Trading Defendants. As indicated before, this does not mean that the SLC would be less inclined to find such charges meritorious, only that the connections identified would be on the mind of the SLC members in a way that generates an unacceptable risk of bias.[34]

Note that the Delaware courts maintain a common sense, flexible view of independence. The relevant facts, not an impractical bright-line test, control the determination. The idea is not that a lawyer can read the tea leaves in former Chancellor Allen's article to predict the outcome in *Oracle* or *Kahn*. It need not be that precise to add value. Attorneys for the Oracle special litigation committee or the Lynch negotiating committee, after reading the Chancellor's warning from the preceding cite, should have been able to raise a red flag to their respective committee that its decision would face more scrutiny than reading previous case law alone might suggest.

More recently, Chancellor William B. Chandler III and Vice Chancellor Strine reminded us that the New York Stock Exchange ("NYSE") reforms that define director independence are separate and distinct from Delaware's definition. They analyze the distinction succinctly:

> The 2002 Reforms' tightening of the definitional standards for independent directors will exert leverage on Delaware and other state courts in a less obvious, but quite important, way. The momentum in favor of the independent director concept has, at times, led courts to be less than careful about terminology and about separating out a director's status for purposes of articulating the appropriate standard of review to apply to a transaction from the distinct question of whether that director in fact breached his fiduciary duties in a manner that subjects him to monetary liability. Not only that, many corporate decisions involve a court's examination of whether a particular transaction should be enjoined or rescinded, and do not involve claims for monetary damages against specific directors. The rhetoric used in such decisions

34. *In re* Oracle Corp. Derivative Litig., 824 A.2d 917, 946–47 (Del. Ch. 2003).

> is situation-specific and is of doubtful utility when extended to decisions requiring a director-by-director determination of culpability.[35]

This is the very kind of revelation that evinces intent on the part of Delaware judges to clarify a looming ambiguity in the law, and is entirely inconsistent with Kamar's thesis of purposeful indeterminacy. If the judges of the Court of Chancery somehow benefited from ambiguity, why would they take time out of their busy lives to produce scholarship that counsels against the erroneous assumption that Delaware's definition of independence will be informed by the NYSE's, immediately after the NYSE instituted the "reform"?

As a second and more recent instance of this phenomenon, we look to a group of co-authors who have earned the affectionate appellation of the "Three Tenors" of corporate law. Former Chancellor (now Professor) Allen, Justice (and former Senior Vice Chancellor) Jack B. Jacobs, and Vice Chancellor Strine have co-authored numerous pieces that form the bedrock of Delaware's Guidance Function. Consider, for instance, their summation of due care jurisprudence and their attendant warning from 2002:

> This de facto departure from the gross negligence review standard in *Van Gorkom* and *Cede* prompts us to suggest that the time has come to reexamine the appropriate standard of review in due care cases.
>
> . . . .
>
> The *Cede II* court cited no precedent nor offered any explanation for why, on policy grounds, duty of care claims should receive the same searching substantive review traditionally reserved for duty of loyalty claims. We submit that no reason in law or policy justifies that result.
>
> . . . .
>
> . . . [T]he *Cede II* doctrine—that a director found to have breached his duty of care must demonstrate the entire

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35. William B. Chandler III & Leo E. Strine, Jr., *The New Federalism of the American Corporate Governance System: Preliminary Reflections of Two Residents of One Small State*, 152 U. PA. L. REV. 953, 996 (2003).

> fairness of the challenged transaction—has resulted in another unintended (and, we suggest, unfortunate) consequence: the rule, announced in *Emerald Partners v. Berlin*, that an exculpation defense based on a charter provision authorized by section 102(b)(7) is an affirmative defense that the directors must bear the burden of establishing. Presumably that burden includes the obligation to negate the statutory categories of excepted-out conduct—specifically, breaches of the duty of loyalty to the corporation or its stockholders, acts or omissions not in good faith or that involve intentional misconduct or a knowing violation of law, and transactions from which the director derived an improper personal benefit.
>
> . . . .
>
> Requiring directors accused of a due care violation to prove that they did not act disloyally imports to yet another context the fairness and policy concerns previously discussed in connection with *Cede II*. That is, the *Emerald Partners* doctrine undercuts the policies sought to be achieved by the gross negligence standard of review applicable in due care cases.[36]

Allen, Jacobs, and Strine have highlighted for readers an important, and thus far unresolved, issue in the corporate jurisprudence. The policy decision to allow directors absolution from good-faith duty of care violations through Delaware General Corporate Law section 102(b)(7) risks being subverted if the proper pleading mechanism is not established. A warning has been issued that corporate advisers would do well to heed. Moreover, this valuable insight into the views of the two courts suggests that final resolution of the question is eventually likely. Sometimes, all a judge is capable of doing through the Guidance Function, as one of the authors of this Article noted in a recent speech, is to "rais[e] some issues that [the judge] think[s] are going to come

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36. William T. Allen, Jack B. Jacobs & Leo E. Strine, Jr., *Realigning the Standard of Review of Director Due Care with Delaware Public Policy: A Critique of* Van Gorkom *and its Progeny as a Standard of Review Problem*, 96 NW. U. L. REV. 449, 459–60, 461, 463–64 (2002) (citations omitted).

before [the court], and give [readers] some idea of a doctrinal framework within which [they] can work."[37]

Former Chief Justice Veasey's opus[38] is the most recent cornerstone in the edifice of judicial and academic writings that support the Delaware Guidance Function. In it, he provides numerous examples of the Guidance Function in action. For instance, a number of law firm white papers[39] and academic articles[40] responded to *Disney*[41] with the observation that good faith might become a separate fiduciary duty with the established independent duties of loyalty and care, and thus *Disney* could be read to expand the reach of directors' fiduciary duties. Yet, Veasey counseled in this article that the emphasis on good faith in the then-ongoing *Disney* litigation would not represent a major shift in the Delaware view of the good faith duty, and that good faith has always represented a foundation of the business judgment presumption.[42] One of the authors of this Article made a similar observation in October 2006.[43] Those two observations can be read to comport with *Stone v. Ritter*,[44] in which the Delaware Supreme Court clarified its holding in *Disney* that good faith, in the context of oversight, should be viewed merely as a subset of the duty of loyalty.

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37. Myron T. Steele, Remarks at the Third Annual Symposium on the Law of Delaware Business Entities: Is Good Faith a Viable Standard of Conduct for Corporate Governance, or Vehicle for Second-Guessing by Hindsight? (Oct. 5, 2006) (transcript available at http://blogs.law.harvard.edu/corpgov/files/2007/05/20070523%20Transcript%20of%20Remarks%20of%20Chief%20Justice%20Steele.pdf).
38. *See* Veasey & Di Guglielmo, *supra* note 20.
39. *See, e.g.*, White Paper, Potter Anderson & Corroon LLP, Disney Affirmed: The Delaware Supreme Court Clarifies the Duty of Directors to Act in Good Faith (June 9, 2006), *available at* http://www.potteranderson.com/news-firm-42.html.
40. *See, e.g.*, Hillary A. Sale, *Delaware's Good Faith*, 89 CORNELL L. REV. 456 (2004).
41. *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27 (Del. 2006).

> Cases have arisen where corporate directors have no conflicting self-interest in a decision, yet engage in misconduct that is more culpable than simple inattention or failure to be informed of all facts material to the decision. To protect the interests of the corporation and its shareholders, fiduciary conduct of this kind, which does not involve disloyalty (as traditionally defined) but is qualitatively more culpable than gross negligence, should be proscribed.

Id. at 66.

42. Veasey & Di Guglielmo, *supra* note 20, at 1442.
43. *See* Steele, *supra* note 37.
44. Stone v. Ritter, 911 A.2d 362 (Del. 2006).

Veasey also responds to *Emerging Communications*,[45] a case which, he writes, has been read by some to stand for the proposition that a lack of independence and special financial expertise is sufficient to attribute to a director knowledge that a merger price was wholly unfair and was enough to make him personally liable.[46] Veasey candidly notes that "[s]ome practitioners and directors have become concerned that, as a result of *Emerging Communications*, Delaware jurisprudence is moving toward a generalized heightened standard of liability for directors who have special expertise. I do not share that view."[47] Again, one article by a former justice is far from the final word on this topic. It is, however, useful evidence of an inside view that is not implicated in a case holding but should nevertheless be afforded significant weight in gauging prospective liability.

Veasey also makes a point of addressing the controversial holding in *Omnicare v. NCS Healthcare*.[48] Decided by a rare 3–2 vote, in which Veasey and one of the authors of this Article dissented, Veasey notes how a subsequent holding in *Orman v. Cullman*[49] might signal a shift in a different direction from *Omnicare*, and also offers some guidance for designing appropriate deal protection measures, when he writes:

> *Orman* indicates a possible trend toward limiting the majority holding in *Omnicare* to its facts. Whether and how far that trend will continue and what the Delaware Supreme Court itself will do, if given the opportunity, remain to be seen, leaving dealmakers and deal lawyers to proceed with caution.
>
> . . . .
>
> I will suggest some principles that might guide an analysis of whether particular measures will pass muster. First, the courts are likely to limit and not expand the reach of *Omnicare*. I think most objective observers believe that the majority decision was simply wrong. Second, practitioners should not count on the court to overrule the decision—not only because of stare decisis but also because, if the reach of

45. *In re* Emerging Commc'ns, Inc. S'holder Litig., No. Civ.A. 16415, 2004 WL 1305745 (Del. Ch. May 3, 2004).
46. Veasey & Di Guglielmo, *supra* note 20, at 1445.
47. *Id.*
48. Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914 (Del. 2003).
49. Orman v. Cullman, No. Civ.A. 18039, 2004 WL 2348395 (Del. Ch. Oct. 20, 2004).

> the decision is limited, it will not become necessary or practical for the court to overrule it. . . . Reasonable deal protection measures are often necessary to achieve a deal. . . . A deal protection measure that makes good business sense should pass muster if it allows the board to follow a best practices process. I caution, however, that a disingenuous attempt to use some transparently artificial measure that is too-clever-by-half in order to try to get around *Omnicare* in a superficial way while maintaining an ironclad lockup with no realistic wiggle room is inviting trouble.[50]

The Guidance Function is not limited to the corporate arena. Business lawyers play a vital role in the formation of alternative entities, including LLCs, LLPs, and general partnerships. One of the authors of this Article has offered guidance to the evolution of case law for this more recent trend in the hope that it may be of some use to attorneys in predicting how similar partnership/LLC duties are to corporate fiduciary duties. To briefly summarize the thesis of that piece:

> I suggest that although current judicial analysis seems to imply that fiduciary duties engrained in the corporate law readily transfer to limited partnerships and limited liability companies as efficiently and effectively as they do to corporate governance issues, that conclusion is flawed.
>
> . . . .
>
> Courts should recognize the parties' freedom of choice exercised by contract and should not superimpose an overlay of common law fiduciary duties, or the judicial scrutiny associated with them, where the parties have not contracted for those governance mechanisms in the documents forming their business entity.[51]

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50. Veasey & Di Guglielmo, *supra* note 20, at 1461–62.
51. Myron T. Steele, *Judicial Scrutiny of Fiduciary Duties in Delaware Limited Partnerships and Limited Liability Companies*, 32 DEL. J. CORP. L. 1, 4 (2007).

Former Chief Justice Veasey also reminds us that Delaware judges "have had a substantial role in shaping best practices in corporate governance."[52] This statement speaks to the evolution of standards of conduct, rather than standards of review,[53] but that does not make the communication any less valuable. Standards of conduct are also in flux; the community of corporate scholars and practitioners is frequently divided about which practices are useful. The Delaware judges, from their vantage point at the center of the corporate governance arena, offer their insights to the community of those who regularly think about best practices, and in doing so can help to bring certain questions to the forefront of the collective mind on these issues. Consider, for instance, Veasey's list of important best practices:

- Define and monitor director independence
- Recommend whether to combine or separate the CEO position from chair of the board or to install a "lead director" or to rotate that role
- Assure a system of executive sessions of independent directors
- Develop and monitor law compliance systems
- Instill internal controls
- Develop business ethics code drafting and compliance
- Review, update, and enforce compliance with charters of all board committees
- Review and evaluate board schedules, quality of board meetings, and workload of committees and individual directors
- Ensure director responsibility for disclosure documents
- Identify conflicts of interest and corporate opportunity issues
- Report malfeasance, misfeasance, or nonfeasance within the corporation
- Anticipate and deal with insider trading issues
- Maintain effective stockholder relations and communications
- Ensure effective systems for evaluation and succession planning for officers
- Instill an evaluation process for directors, the board as a whole, and board committees
- Ensure that management has the proper operational structures in place and functioning[54]

52. Veasey & Di Guglielmo, *supra* note 20, at 1404.
53. *Id.* at 1417 (highlighting the difference between standards of conduct and standards of review).
54. E. Norman Veasey, *Policy and Legal Overview of Best Corporate Governance Principles*, 56 SMU L. REV. 2135, 2145–46 (2003).

This does not guarantee a court response, and it does not offer a particular best practice as a "get out of jail free" card. Those who counsel boards and managers, however, have more force behind their recommendations when a judge that stands as the potential reviewer of their decisions has expressed support for the practice.

We have covered a variety of examples of secondary source writings that fulfill the Delaware Guidance Function of establishing a useful basis of informative precedent for counselors of Delaware corporate law, and will now turn to the rich body of guidance in the court opinions themselves.

III. DICTA AS AN ELEMENT OF THE GUIDANCE FUNCTION

Legal scholars generally distinguish between dicta and the holdings of judicial opinions in case law analysis. Admittedly, dicta is not always easily identifiable, but its conventional definition is as analysis in an opinion not required to support the holding.[55] One academic commentator has observed that the distinction between holding and dicta is on the wane, owing to the ease of electronic research and the inclination of some judges to ignore the distinction.[56] Despite any such trend, the distinction is still observed in Delaware, and the Delaware judges have frequently crafted dicta to give valuable guidance to deal lawyers on unanswered questions. The Delaware courts recognize the need to wait for a live controversy to resolve an issue definitively, but fortunately they also recognize that this does not mean that they cannot, or should not, use the attention paid to a published opinion to offer guidance on uncertain but vital areas of corporate law.

Consider the recent example of *In re Toys "R" Us*, in which Vice Chancellor Strine addressed whether stapled financing—where an investment bank advising the board of directors may also be permitted to offer financing to the acquirer after the deal has been approved by the board—may serve as a basis to challenge the board's reliance on the advisory opinion of that bank in approving the sale of a company.[57] Strine writes:

> I do not want to be perceived as making a bright-line statement. One can imagine a process when a board decides to sell an entire division or the whole company, and when the board obtains a commitment from its financial advisor to

55. Michael Abramowicz & Maxwell Stearns, *Defining Dicta*, 57 STAN. L. REV. 953, 953 (2005).
56. Thomas L. Fowler, *Holding, Dictum . . . Whatever*, 25 N.C. CENT. L.J. 139, 140–43 (2003).
57. *In re* Toys "R" Us, Inc. S'holder Litig., 877 A.2d 975 (Del. Ch. 2005).

> provide a certain amount of financing to any bidder, in order to induce more bidders to take the risk of an acquisition. These and other scenarios might exist when roles on both sides for the investment banker would be wholly consistent with the best interests of the primary client company. In general, however, it is advisable that investment banks representing sellers not create the appearance that they desire buy-side work, especially when it might be that they are more likely to be selected by some buyers for that lucrative role than by others.[58]

Strine's dicta guidance was quickly noted in a Practising Law Institute ("PLI") publication on ethics in deals.[59] The dicta observation, then, provides guidance to boards in the form of a warning: to gauge the liability of stapled financing, boards should be aware that there may be situations in which the incentives of stapled financing negate the value of a fairness opinion from the board's investment bank. How much more information has been added than would have been if the Vice Chancellor had offered no observation at all? There is no quantifiable answer to such a question, but in making subjective judgments about deal provisions, lawyers are now aware that the interest of the court has been raised. The negotiated acquisitions bar will begin to pay more attention to this aspect of deal structure, if for no other reason than that, after being mentioned by the Vice Chancellor, commentators and practitioners then discuss it in articles and practice guides. So we see here that Delaware's Guidance Function has value, even if a stapled financing deal is never successfully challenged on that basis. Thus, the court focused negotiated acquisitions practitioners on stapled financing as a result of the dicta in *In re Toys "R" Us*, and the advisers who craft deals have justification for urging caution to those they advise.

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58. *Id.* at 1006 n.46.

59. Stephen M. Besen & Kevin M. Schmidt, *Ethical Issues in Private Equity*, 1549 PLI/CORP. 123, 129 (2006).

> Stapled financing . . . may create appearance of, if not actual, conflict. See *In Re Toys "R" Us, Inc.* (the Delaware Chancery Court noted, in dicta, that, although stapled financing may not actually effect a seller's process, it can create the appearance of impropriety and should generally be avoided when the financial advisor might be chosen by certain buyers).

Id. (citation omitted).

For another example, we need only look to recent shareholder litigation against Caremark Pharmacy Services. Chancellor Chandler elucidated a multi-factor test for the reasonableness of deal protection measures:

> That analysis will, by necessity, require the Court to consider a number of factors, including without limitation: the overall size of the termination fee, as well as its percentage value; the benefit to shareholders, including a premium (if any) that directors seek to protect; the absolute size of the transaction, as well as the relative size of the partners to the merger; the degree to which a counterparty found such protections to be crucial to the deal, bearing in mind differences in bargaining power; and the preclusive or coercive power of *all* deal protections included in a transaction, taken as a whole. The inquiry, by its very nature fact intensive, cannot be reduced to a mathematical equation. Though a "3% rule" for termination fees might be convenient for transaction planners, it is simply too blunt an instrument, too subject to abuse, for this Court to bless as a blanket rule. Nor may plaintiffs rely upon some naturally occurring rate or combination of deal protection measures, the existence of which will invoke the judicial blue pencil. Rather, plaintiffs must specifically demonstrate how a given set of deal protections operate in an unreasonable, preclusive, or coercive manner, under the standards of this Court's *Unocal* jurisprudence, to inequitably harm shareholders.[60]

Chandler goes on to note that, because of the fully informed shareholder vote that was expected after his ruling, he need not rule on whether the particular deal protection measure was valid in that case.[61] Why go to such lengths to discuss the multiple factors that determine whether the measure is permitted? Perhaps the Chancellor did so because of his pragmatic awareness that boards and deal lawyers, when crafting deal protection measures, hope to structure negotiated deals that are advantageous to parties involved without running afoul of their fiduciary duties, yet face overwhelming uncertainty of the line that divides measures protected by the business judgment rule from

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60. Louisiana Mun. Police Employees' Ret. Sys. v. Crawford, 918 A.2d 1172, 1181–82 n.10 (Del. Ch. 2007).
61. *Id.*

those that violate fiduciary duties. This footnote represents the Chancellor's informed decision to provide guidance on that question, even though it is not necessary to the particular case at hand, in order to minimize the uncertainty boards face in this area. Sometimes uncertainty is, nevertheless, unavoidable in corporate law, and an honest admission of where those areas lie can provide valuable warning to those who tread into the perilous arena of corporate litigation. Consider Chandler's observation on the challenges facing the Court of Chancery in administering the appraisal remedy guaranteed by DGCL:

> [I]t is one of the conceits of our law that we purport to declare something as elusive as *the* fair value of an entity on a given date . . . . Experience in the adversarial[ ] battle of the experts' appraisal process under Delaware law teaches one lesson very clearly: valuation decisions are impossible to make with anything approaching complete confidence. Valuing an entity is a difficult intellectual exercise, especially when business and financial experts are able to organize data in support of wildly divergent valuations for the same entity. For a judge who is not an expert in corporate finance, one can do little more than try to detect gross distortions in the experts' opinions. This effort should, therefore, not be understood, as a matter of intellectual honesty, as resulting in *the* fair value of a corporation on a given date. The value of a corporation is not a point on a line, but a range of reasonable values, and the judge's task is to assign one particular value within this range as the most reasonable value . . . based on considerations of fairness.[62]

At first blush, it may seem that this statement merely adds to the uncertainty, or indeterminacy, that Kamar identifies, but nevertheless, the Chancellor's observation is worth appreciation. Appraisals are a risky business. Litigants would do well to realize that, despite the Court of Chancery's exhaustive dedication to the minutiae of the valuation models, there is a significant element of subjective judgment inherent to the financial modeling process. That risk should be taken into account in, for instance, settlement talks in advance of trial on the appraisal. It also means that litigants

62. Cede & Co. v. Technicolor, Inc., 2003 WL 23700218, at 2 (Del. Ch. 2003), *amended and superseded by* 884 A.2d 26 (Del. 2005).

are well advised not to get too caught up in the minutiae of the variables, lest they miss the bigger picture of equity in the case.

Best-practices analysis can also make its way into the dicta aspect of the Delaware Guidance Function. Justice Jacobs could not resist reminding readers of what best practices would have counseled for in the actions leading up to the *Disney* case:

> In a "best case" scenario, all committee members would have received, before or at the committee's first meeting on September 26, 1995, a spreadsheet or similar document prepared by (or with the assistance of) a compensation expert (in this case, Graef Crystal). Making different, alternative assumptions, the spreadsheet would disclose the amounts that Ovitz could receive under the OEA in each circumstance that might foreseeably arise. One variable in that matrix of possibilities would be the cost to Disney of a non-fault termination for each of the five years of the initial term of the OEA. The contents of the spreadsheet would be explained to the committee members, either by the expert who prepared it or by a fellow committee member similarly knowledgeable about the subject. That spreadsheet, which ultimately would become an exhibit to the minutes of the compensation committee meeting, would form the basis of the committee's deliberations and decision.[63]

The lesson for compensation committees: prepare a Monte Carlo sensitivity analysis that includes a number of material possibilities and contingent payments, with expected probable values for each scenario, for board review before approving any compensation package, and you will perhaps avoid running afoul of your fiduciary duties in the approval. Does a best practices reference have more force if it appears in an opinion rather than in merely a journal article or speech? Perhaps, especially if it is in a Delaware Supreme Court opinion joined by the full panel. Either way, a Delaware judge's public focus on a particular best practice can add significant weight to its salience.

Consider also how the Delaware Supreme Court handled the question of overlap between the duty of care and the question of good faith in *Disney*. The following excerpt reads more like a philosophical treatise than a legal opinion:

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63. *In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 56 (Del. 2006).

> The conduct that is the subject of due care may overlap with the conduct that comes within the rubric of good faith in a psychological sense, but from a legal standpoint those duties are and must remain quite distinct. Both our legislative history and our common law jurisprudence distinguish sharply between the duties to exercise due care and to act in good faith, and highly significant consequences flow from that distinction.
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> . . . .
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> An example of such overlap might be the hypothetical case where a director, because of subjective hostility to the corporation on whose board he serves, fails to inform himself of, or to devote sufficient attention to, the matters on which he is making decisions as a fiduciary. In such a case, two states of mind coexist in the same person: subjective bad intent (which would lead to a finding of bad faith) and gross negligence (which would lead to a finding of a breach of the duty of care). Although the coexistence of both states of mind may make them indistinguishable from a psychological standpoint, the fiduciary duties that they cause the director to violate—care and good faith—are legally separate and distinct.[64]

The distinction may seem academic at first, but the court must elaborate on the reasoning that supports its decision through the use of hypothetical scenarios. While some may dismiss this as a mere semantic exercise, all opinions applying standards are, at their very heart, based on questions of semantics. The elaborate, almost philosophical investigation seen in the *Disney* opinion—a discussion blending psychology, law, and policy—is uniquely scholarly. This is the result of a court mindful of how imprecision in word choice can accrete into the tapestry of case law in a way that confuses the function of the standards of care.

64. *Id.* at 65, n.104.

IV. Participation in Formal Committees and Policy Analysis as an Element of the Guidance Function

Many Delaware judges consider participation in improvement of the administration of justice to include active, not simply nominal, involvement in committee work of law-related professional organizations.

Justice Jacobs and others have served on the Corporate Laws Committee of the ABA Section of Business Law; Chancellor Chandler is a founder and active member of the American Academy of Business Court Judges; one of the authors serves currently as an advisor to the Business Section of the ABA and judicial liaison to both the Negotiated Acquisitions and Business and Corporate Litigation Committees of the Section; Justices Carolyn Berger and Randy J. Holland of the Delaware Supreme Court participate in American Law Institute activities focused on substantive law; Vice Chancellor Stephen P. Lamb plays an active role in the PLI.

The preceding list is representative of Delaware judges' direct involvement with constituencies interested in the development of the law at a practical, as well as at a theoretical level. Hands-on participation in discussions about current issues in corporate law allows judges insight into broader ramifications of the tensions at play in corporate transactions and in litigation practices. It is as difficult to imagine sportswriters critiquing athletes' performance without ever having seen a game as it is to imagine judges comprehending the business environment without the opportunity to participate on panels, listen to practitioner discussions, and hear directly how problems evolve from the application of doctrine to real world scenarios. While these experiences do not translate directly into dispositions of particular cases, they do provide opportunities to inform judges about real and potential consequences that flow from the evolution of best governance practices in the field.

Delaware judges also play an active role in policymaking. For instance, in an article just after the Sarbanes-Oxley reforms were instituted, Chancellor Chandler and Vice Chancellor Strine urged a Delaware legislative reform to execute adequate service of process on corporate executives in Delaware fiduciary duty actions: "[S]ection 3114 could also be amended to clarify that any person who aids and abets a breach of fiduciary duty against a Delaware corporation is subject to jurisdiction in Delaware so long as Delaware's exercise of jurisdiction is consistent with federal constitutional standards of due process."[65]

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65. Chandler & Strine, *supra* note 35, at 1004.

In response, the Delaware legislature adopted their recommendation, and corporate executives are now deemed to consent to service of process in Delaware when they accept appointment as a corporate officer of a Delaware corporation.[66] For a more international flavor, we can look to Justice Jacobs's scholarship analyzing the burgeoning growth of a distinct corporate jurisprudence in Japan. He uses the history of Delaware's corporate law development and draws a comparison to Japan's Guidelines on Takeover Defenses (adopted by the Japanese Ministry of Justice).[67] Jacobs's advice:

> The lesson that the Delaware experience teaches, I submit, is that we should not expect the Japanese "fair" rules, whatever form they may take, to remain static. . . . Japanese policy makers have made a judgment to transplant portions of Delaware takeover jurisprudence to Japan. . . . If history is any guide, Japan, in developing "fair" takeover rules, will undergo its own unique evolutionary experience.[68]

The overarching lesson from Justice Jacobs is that some level of indeterminacy in any viable corporate code is unavoidable.

CONCLUSION

Critics might assert that communication outside the four corners of legal holdings, especially in the form of speeches and articles, risks running afoul of the canons of judicial ethics. One counter argument to this line of thought is that the Delaware courts are not unique in their desire to guide thinking about the law outside the context of written decisions. Judge Richard Posner of the United States Court of Appeals for the Seventh Circuit is a prolific author, commenting on legal concepts that fall under the appellate jurisdiction of his court. Indeed, Justice Oliver Wendell Holmes, Jr. was a noted author throughout his service as one of the most notable United States Supreme Court justices, as was Chief Justice William Rehnquist.[69] Neither the court's

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66. DEL. CODE ANN. tit. 10, § 3114 (2004).

67. *See* Jack B. Jacobs, *Implementing Japan's New Anti-Takeover Defense Guidelines, Part I: Some Lessons from Delaware's Experience in Crafting "Fair" Takeover Rules*, 3 U. TOKYO J.L. & POL. 83 (2006).

68. *Id.* at 85.

69. In a timely example of the prescience of judicial writings to future judicial inquiry at the federal level, then-Chief Justice Rehnquist wrote a book entitled *All the Laws but One: Civil Liberties in War Time*, on the habeas corpus rights of enemy combatants throughout U.S. history, just a year before the 9/11 tragedy and a few years prior to the advent of a torrent

flexibility nor its credibility in later decisions is limited by such secondary precedents. Secondary sources are relevant merely as informative precedent, and are most effective in the absence of other justification to rule in a specific direction. In effect, the real cost of analysis in secondary sources that is later directly and patently rejected by the court in a decision is not exhibited in the primary source at all; rather, the cost is in the future effectiveness and credibility of the secondary source writings. The judge thus has the incentive to accurately reflect the landscape of corporate law evolution in his secondary writings, so that the effort would not be in vain. In the event that a party cites his secondary writings in a brief, a judge is certainly free to ignore that writing, as he is free to ignore any secondary source material due to lack of binding authority on his decision. The Three Tenors remind readers in a recent article: "Since our views are expressed only in our capacity as lay commentators, nothing in this Article should be regarded as an opinion or prediction of how we would decide particular issues presented to us in our official capacity."[70] The secondary source, however, does hold a place within the law. The judge as an academic thinker is a relatively recent development of the last two centuries, one which Delaware has embraced to the benefit of its Guidance Function specifically, and to the body of decisions that constitute corporate law more generally.

An analogy can be drawn to the Federal Reserve's process, as that institution faces a similar tightrope walk in its communication role. The Federal Reserve Open Market Committee votes on decisions of bond sales and purchasing policy that governs open market operations, which result in changes to interest rates that ripple out into the economy to affect short-term economic growth. To be sure, the analogy is limited, as one institution sets a single variable (i.e., interest rate policy) using elaborate econometrics, while the other uses broad legal standards potentially applied to limitless fact patterns. Yet there are a number of important similarities. Both the Federal Reserve and Delaware courts issue unofficial guidance so that experts—economists in one case and corporate lawyers in the other—can themselves counsel decision makers—the investing public on one hand and corporate boards on the other. Such expert guidance has a real effect on the economy,

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of litigation on that issue. Amicus briefs in some of the litigation cited to Chief Justice Rehnquist's book. *See, e.g.*, Amicus Curiae Brief of the American Center for Law and Justice at 4, Hamdi v. Rumsfeld, 542 U.S. 507 (2004), *available at* http://www.jenner.com/files/tbl_s69NewsDocumentOrder/FileUpload500/208/AmicusCuriae_AmericanCenter_LawJustice_Hamdi.pdf.

70. William T. Allen, Jack B. Jacobs & Leo E. Strine, Jr., *The Great Takeover Debate: A Meditation on Bridging the Conceptual Divide*, 69 U. CHI. L. REV. 1067, 1068 n.1 (2002).

as it can limit the need for subsequent official action. Communication from the Federal Reserve can ease investor insecurity and limit inflation pressures that may otherwise result in a need for policy shifts.[71] In the corporate sphere, legal counsel can minimize the incidence of board decisions that result in subsequent litigation or liability. Thus, communication in both spheres serves to increase valuable efficiency.

This comparison holds equally for dicta, speeches, and articles. The Federal Reserve originally only issued statements accompanying and explaining its policy actions based on economic data pre-dating the policy decision. In 1998, it implemented a change to offer policy guidance in written statements on future policy courses to minimize uncertainty surrounding its future policy decisions.[72] Additionally, Federal Reserve Chairman Alan Greenspan gave 123 speeches between 1996 and 2003, averaging eighteen a year.[73] Professor Lawrence Hamermesh tallied oratory appearances by the Delaware judiciary, totalling seventy-one from 2003 to 2006.[74] While not all of these speeches will eventually grow into substantive law review articles, many that touched on substantive corporate law questions have already done so.

Communications to experts and decision makers, however, must be circumspect in both instances; both judges and Fed officials want to minimize the possibility that their flexibility to respond to unforeseen difficulty will be foreclosed. Additionally, the analogy holds in that, for both institutions, no single member can speak for the collective organization. This often results in the unofficial communication being vague, yet this does not negate its value. For the Federal Reserve, the economic advantage resulting from a communication can be quantitatively shown.[75] For the Delaware courts, the ability to measure such benefits is much more difficult, since one cannot easily measure the value of board liability that did not occur because of sound advice from informed corporate counsel.

There may nevertheless be a way to empirically demonstrate the utility of the Delaware Guidance Function. We counted citations over the last fifteen years to the three most prolific Delaware judges as based on the number of

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71. *See* Donald L. Kohn & Brian P. Sack, *Central Bank Talk: Does it Matter and Why?*, at 1 (Federal Reserve Board, Finance & Economics Discussion Series No. 2003-55, 2003), *available at* http://www.federalreserve.gov/Pubs/feds/2003/200355/200355pap.pdf.
72. *Id.* at 4.
73. *Id.* at 5.
74. *See* Hamermesh, *supra* note 26, at 1788.
75. *See generally* Kohn & Sack, *supra* note 71 (showing through a regression on market returns correlated with significant policy shifts that speeches and policy statements by members of the Federal Reserve Open Market Committee have a statistically significant, positive effect on market interest rates).

corporate law articles published (former Chief Justice Veasey, former Chancellor Allen, and Vice Chancellor Strine).[76] We included only citations to journal articles focusing on Delaware corporate law topics. Secondary source writings by these three judges were cited seventy-one times in PLI publications. They were cited thirty-eight times in legal opinions, the vast majority issued by the Delaware Court of Chancery or Delaware Supreme Court., and were also cited thirty-six times in briefs before one of these two Courts. Finally, there were 939 citations to the three judges by other authors in other journal articles.

One criticism of this method of measuring the relevance of this aspect of the Guidance Function could be that it does not prove that secondary judicial writings add value, but merely that corporate lawyers and academics believe they have value. But perhaps this is as close as one can come to quantifying such an amorphous concept. One can trust the notion, however, that deal lawyers are highly sophisticated in their approach; if they cite Delaware judges with such frequency, then one can feel comfortable with the assertion that the extrajudicial activities are worth the effort.

The dicta element of the Delaware jurisprudence is more easily defended. The analysis leading to a holding can take many twists and turns, and necessary digressions can assist in analyzing and appreciating the holding. Dicta is an omnipresent and long-standing phenomenon in the American common law system, and thus not as controversial as secondary writings. Its quantitative utility in Delaware is tremendous, as quantified by citations to dicta in practice guides—a Westlaw search for *Delaware /s Dicta* in the "all law reviews and texts" (TP-ALL) database (including practice guides) yields 610 results.[77] To offer an idea of how Delaware dicta is used in the practice

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76. Note that, though these three authors have published numerous articles on related topics, only articles focusing on Delaware corporate law were included in this tally. Furthermore, only articles written while the author was on the bench or co-authored with a sitting judge were included. The following totals are current as of May 16, 2007:
    - All citations, including other academic articles, to Former Chancellor Allen: 472; Citations in PLI: 18; Citations in BNA: 10; Citations in ALI/ABA: 5; Legal Opinion Citations: 10; Citations in Case Briefs: 6; Citations in Am. Jur.: 5.
    - All citations, including other academic articles, to Vice Chancellor Strine (note that articles co-authored with Allen were not included to prevent double counting): 266; Citations in PLI: 19; Citations in BNA: 3; Citations in ALI/ABA: 6; Legal Opinion Citations: 12; Citations in Case Briefs: 16.
    - All citations, including other academic articles, to Former Chief Justice Veasey (note that Veasey's *Retrospective* piece, completed just after the end of his tenure, is included in this tally): 346; Citations in PLI: 34; Citations in BNA: 20; Legal Opinion Citations: 16; Citations in Case Briefs: 14.

77. As of December 2, 2007.

guides, we have quoted from the following five citations, which are but a few examples of the many found throughout corporate law practice guides since the 1980s:

> 1. *Fliegler v. Lawrence* contained dicta to the effect that even if the safe harbor tests of § 144 were satisfied, the transaction in question could still be attacked on fairness grounds.[78]
> 2. The "preponderance of evidence" standard has, it should be noted, been endorsed in dicta by the Delaware Supreme Court. See *Unocal Corp. v. Mesa Petroleum Co.*[79]
> 3. However, the Delaware Chancery Court indicated in dicta that *Revlon* duties may apply in the context of a merger in which over 30% of the consideration was the acquirer's stock and the remainder was cash.[80]
> 4. In *Tafeen v. Homestore, Inc.*, the Delaware Chancery Court noted in dicta that Sarbanes has created uncertainty as to whether corporations may continue to advance costs. The court questioned whether Sarbanes' prohibition of personal loans preempts the Delaware Code's provisions that expressly allow corporations to advance attorney's fees.[81]
> 5. In a ruling in 2005, Chancellor Strine, albeit in dicta, suggested that Delaware courts may be willing to eventually reconcile the different standards of review for the different approaches and extend the business judgment rule's protection in negotiated going-private deals with controlling shareholders where the controlling shareholders proposes a transaction that is subject to (1) special committee negotiation and approval and (2) approval by a majority of disinterested stockholders,

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78. 1 LOU R. KLING & EILEEN T. NUGENT, NEGOTIATED ACQUISITIONS OF COMPANIES, SUBSIDIARIES AND DIVISIONS § 4.02, at n.33 (2006) (citation omitted).
79. DAVID A. DREXLER ET AL., DELAWARE CORPORATION LAW AND PRACTICE, § 15.09 (1991) (citation omitted).
80. 1 MARTIN LIPTON & ERICA H. STEINBERGER, TAKEOVERS AND FREEZEOUTS § 5A.01[2], at 5A-16 (2006) (1978) (citation omitted).
81. Paul S. Diamond & Mathieu J. Shapiro, *Director and Officer Liability*, *in* 6 BUSINESS AND COMMERCIAL LITIGATION IN FEDERAL COURTS § 63:21 (Robert L. Haig ed., Thomson West 2nd ed. 2005) (1998).

> while also tightening the conditions for avoiding entire fairness review through the *Siliconix* approach.[82]

In conclusion: the extrajudicial activities undertaken by the judges of the Delaware Court of Chancery and the Delaware Supreme Court contribute to a more informed understanding of the state's corporate jurisprudence. The intellectual effort has not been in vain. This should finally put to rest the notion that Delaware, or at least the Delaware judiciary, seeks to obtain some advantage from encouraging an artificial indeterminacy in its jurisprudence. The Delaware Guidance Function is an important element of Delaware's unique advantage as a forum for the resolution of the disputes of business entities, and has helped the Delaware judiciary earn its place as the arbiter of equity for the modern corporate Witenagemot.

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82. Theodore N. Mirvis, *What All Business Lawyers & Litigators Must Know About Delaware Law Developments 2007*, 1599 PLI/CORP. 147, 217–18 (2007).