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Conflicts of Interest and Fiduciary Duties in the Operation of a Joint Venture

by

ZENICHI SHISHIDO*

A joint venture is one of the most important mechanisms by which enterprises can cooperate with each other and enter new product or geographic markets, especially in the context of international business. Joint ventures between U.S. and foreign parent companies, known as "strategic alliances" in trendier circles, are currently a fast-growing form of business venture.

A joint venture creates a synergistic effect: each enterprise in a joint venture can make up for its partner's deficiencies and the marriage of the enterprises in a joint venture can create a new entity whose power is greater than the sum of the powers of the separate enterprises. The formation of a joint venture enables each parent company to gain instant access to key technology, new markets, distribution systems, cheap production methods, or major customers faster and less expensively than if the corporation attempted a takeover or independent development of these assets.2

Because a joint venture may bring together companies with different interests, management styles and goals, it creates a potential risk that the parent companies will not be able to cooperate on a practical level as business partners.3 Conflicts of interest arising from self-dealing, corporate opportunities, and disclosure may cause friction between parent companies.

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1. A recent Business Week cover story listed the following examples of international joint ventures were listed: a joint venture entered into by Boeing, Mitsubishi, Fuji, and Kawasaki to produce small aircraft for the perceived benefits of cutting costs and sharing technology; a joint venture between GM and Toyota to produce autos more cheaply; a joint venture between GTE and Fujitsu to produce communications equipment that aims to obtain new markets and enhance distribution systems; and a joint venture to produce steel run by U.S. Steel and Pohang Iron & Steel that seeks to increase existing market shares and raise capital levels. Levine & Byrne, Corporate Odd Couples, Bus. Wk., July 21, 1986, at 100-01.

2. Id. at 101.

3. This is one of the reasons that successful joint ventures are rather rare. Id. at 101-05.
Interlocking directors and officers\(^4\) often present a fiduciary duty problem in joint ventures.\(^5\) Individual directors and officers may owe fiduciary duties\(^6\) to both the joint venture and their parent company simultaneously. When the interests of the joint venture conflict with the interests of the parent company, the interlocking directors and officers are in contradictory fiduciary duty positions. This Essay will discuss means to resolve the fiduciary duty problem of interlocking directors and officers and address the fiduciary duty problem of parent companies.

Part I of this Essay introduces the reader to the concept of a joint venture by comparing the characteristics of a joint venture with those of a closely held corporation\(^7\) and those of a parent-subsidiary relation.\(^8\) This Essay then argues that there is less need to protect the interests of minority shareholders in a joint venture than there is to protect the interests of minority shareholders in either a closely held corporation or of a subsidiary in a parent-subsidiary relationship. Part I also points out that an analysis of a joint venture is complicated by the multiplicity of distinct interests involved and the possibility of falling afoul of the Sherman Antitrust Act.

Part II illustrates how conflict of interest situations may arise in a joint venture and categorizes these situations into three types: self-dealing conflicts, corporate opportunity conflicts, and disclosure conflicts. Part II will also provide examples of each type of situation.

Part III first explores the argument that dissenting parent companies in certain cases should be estopped from undertaking direct action against a joint venture director for a breach of fiduciary duty by virtue of an implied agreement among the parent companies that recognizes that the representatives of each parent company will vote for his parent's interests. The discussion concludes that normally the implied agreement

\(^4\) Interlocking directors and officers are directors and officers who sit in two or more companies at the same time. There are three variations of interlocking directors and officers: those who sit in a joint venture and a parent company, those who sit in a parent company and a subsidiary, and those who sit in companies that have no ties with each other.

\(^5\) Parent companies are companies that make a substantial investment in a joint venture and take part in operating it.

\(^6\) People who are in fiduciary positions, like directors or officers of corporations, are under obligation to give the interests of their beneficiaries the highest priority. See generally H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 235 (3d ed. 1983) (increasingly statutes are providing that corporate directors and officers owe a fiduciary duty to their corporation—a duty requiring good faith and fair dealing); FrankeL, Fiduciary Law, 71 CALIF. L. REV. 795 (1983) (in a close corporation, the duty owed between stockholders and directors is analogous to the strict duty owed among partners).

\(^7\) See infra text accompanying notes 17-34.

\(^8\) See infra text accompanying notes 36-51.
does not excuse a joint venture director or a parent company from fulfilling fiduciary duties owed to the joint venture and that the implied agreement argument is viable only in limited circumstances.

Section A of part III, on self-dealing conflicts of interest, argues that ratification by noninterested parent companies is the key to avoiding fiduciary duty problems. It recognizes the difficulty of obtaining full and fair disclosure prior to ratification and suggests that parent companies agree on the criteria governing such disclosure in advance. Section A also demonstrates the difficulty faced by courts in applying an arm’s-length standard as a test of the fairness of a self-dealing transaction.

Section B discusses corporate opportunity conflicts of interest, beginning with the observation that the best way for the parent companies to avoid putting the interlocking directors and officers in contradictory positions of duty and loyalty is to employ express agreements to define and limit the scope of corporate opportunities that must be given to the joint venture. It notes that the antitrust laws prohibiting restraint of competition and the business disadvantages of limiting the joint venture’s ability to maximize potential synergistic benefits prevent the use of express agreements from providing a complete solution.

Section B also proposes a new approach to resolving fiduciary duty problems in the corporate opportunity area. This approach, drawing on analyses of the parent-subsidiary relationship advanced by Harvard professors Victor Brudney and Robert C. Clark and by the American Law Institute (ALI), concludes that in a joint venture, absent an express agreement to the contrary, there should be a presumption favoring the assignment of corporate opportunities to the interested parents except in limited circumstances. These analyses are illustrated in a series of matrices (Tables 1-4), with the author’s theory illustrated in Table 4.

Section B also discusses other options for dissatisfied parent companies, such as buy-outs and noncooperation, and suggests that the best strategy for parent companies is to maximize its own long-term gains over short-term benefits. The section examines the conflicts of interest problem presented by the choices a joint venture must make in its dividend policy and regarding its amount of capital. Section B concludes that these problems are too complicated to be handled under the legal schemes discussed and must be resolved through an approach that attempts to balance the interests of the parent companies.

Section C of part III, on the disclosure conflict of interests problem, argues that balancing the interests of a joint venture and a parent, or the interests of parent companies, is the key to resolving the disclosure conflicts. The section discusses three factors which should be used to bal-
ance competing interests: the characteristics of the information, the interest of the other parent companies in the information, and the degree of disclosure. Section C briefly illustrates the relationship between the fiduciary duty problem and the antitrust problem of collusion using the example of the General Motors (GM)-Toyota joint venture. It concludes that full disclosure of all material interests and material facts is not always necessary to enable a parent company or an interlocking director to avoid liability; it notes that partial disclosure, or disclosure of generalized information, might substitute effectively for full disclosure in certain cases.

I. Nature of a Joint Venture

A. Definition of “Joint Venture”

“Joint venture” is an ambiguous term used to describe many kinds of enterprises. Under the classic definition, the terms “joint venture” or “joint adventure” describe any “association created by co-owners of a business undertaking,” differing from a partnership (if at all) in that it has a more limited scope.9 According to this definition, a joint venture is a special form of partnership and is no longer a joint venture for legal purposes once it is incorporated. Some economists, however, define a joint venture as ”formed by two or more separate entities, usually corporations, which typically allocate ownership based on shares of stock controlled.”10

Another approach, used in the antitrust context, defines “joint venture” as:

an integration of operations between two or more separate firms, in which the following conditions are present: (1) the enterprise is under the joint control of the parent firms, which are not under related control; (2) each parent makes a substantial contribution to the joint enterprise; (3) the enterprise exists as a business entity separate from its parents; and (4) the joint venture creates significant new enterprise capability in terms of new productive capacity, new technology, a new product, or entry into a new market.11

This definition focuses on the organization, management, ownership, and operation of a joint venture, not on whether the enterprise is incorporated.

This Essay will employ the functional definition of a joint venture: any form of enterprise in which two or more independent enterprises

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(parent companies) invest and in whose operation all parent companies participate.\textsuperscript{12} Many joint ventures have special agreements among the participating parent companies to prevent majority shareholding parent companies from monopolizing the board of directors. This capacity, referred to in this Essay as the "Principle of Stock Majority," will be discussed later.\textsuperscript{13}

There are both joint venture corporations and joint venture partnerships. The legal affairs of incorporated joint ventures are governed by corporation law and the legal affairs of unincorporated joint ventures are governed by partnership law.\textsuperscript{14} The fiduciary duties owed by incorporated and unincorporated joint ventures, however, are fairly similar.\textsuperscript{15} More importantly, because both joint venture forms increasingly govern their business affairs through the use of prearranged contractual agreements, the management structures and operations of incorporated and unincorporated joint ventures are converging. Accordingly, this Essay focuses on joint venture corporations and makes only passing reference to joint venture partnerships.

B. Comparison of a Joint Venture with a Closely Held Corporation

In a sense, a joint venture is a closely held corporation and has many similar problems. These similarities make analysis of fiduciary duty problems in the closely held corporation context applicable to joint ven-

\textsuperscript{12} See, \textit{e}g., Infusaid Corp. v. Intermedics Infusaid, Inc., 739 F.2d 661 (1st Cir. 1984) (joint venture for manufacturing a device called an infusion pump; parents were a corporation which contributed the licensing rights and information relating to the development of that type of product and a corporation which contributed cash); McRindle & Son, Ltd. v. Durant, 611 F.2d 89 (5th Cir. 1980) (joint venture for shipbuilding and a second joint venture for drilling set up by a Scottish corporation and an American corporation); Gates Energy Products v. Yuasa Battery Co., 599 F. Supp. 368 (D.C. Colo. 1983) (joint venture for manufacturing and marketing sealed rechargeable lead-acid batteries involving an American corporation and Japanese corporation); Delaney v. Georgia-Pacific Corp., 278 Or. 305, 564 P.2d 277 (1977) (joint venture corporation in the wood products business; parent companies were a local corporation, which had experience and prospects for timber acquisition in Montana and Canada, and a nation-wide corporation, which had money, access to financing, and an extensive marketing network).

For purposes of this Essay, the definition of a joint venture excludes subsidiaries whose parent companies are not independent of each other, closely held corporations or partnerships whose equity holders are not enterprises but are instead individuals, and enterprises in which only one parent company operates the business and the other parent companies are merely investors.

\textsuperscript{13} See \textit{infra} text accompanying notes 25-33.

\textsuperscript{14} A. Bromberg, \textit{supra} note 9, § 35, at 192-95.

tures. A joint venture also has some important distinguishing characteristics, however, that set it apart from a closely held corporation. This section will describe the characteristics of a joint venture through a comparison of a joint venture and a closely held corporation.

(1) Similarities Between a Closely Held Corporation and a Joint Venture

A closely held corporation is a corporation that has a small number of stockholders and consequently has no market for its stock, making it very difficult for minority shareholders to liquidate their investments. For example, in a closely held corporation, it is very difficult for a minority shareholder to obtain financial benefits from a corporation in proportion to equity held in the corporation. When a majority shareholder siphons off the profit of the corporation by means of an excessive salary or an unfair transaction and subsequently depresses the dividends, a minority shareholder might be forced to remain in the corporation as a dissatisfied investor.

This difficulty in liquidating investments is the most important factor behind the problem of oppression of minority shareholders. In publicly held corporations, a dissatisfied shareholder can sell his stock in the corporation; in a closely held corporation the shareholder cannot. Even if a minority shareholder of a closely held corporation can liquidate investments by way of, for example, an appraisal remedy or buy-out contract, establishing the fair value of the stock is very difficult because

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17. When shareholders of a corporation want to liquidate or recoup their investment, they must sell their stocks to someone other than the corporation except in some special cases (e.g., appraisal remedy, see infra note 20). In a closely held corporation, it is very difficult for shareholders, particularly minority shareholders, to find buyers for their stock.


20. An appraisal remedy is “essentially a statutory creation to enable shareholders who object to certain extraordinary corporate matters to dissent and to require the corporation to buy their shares at the value immediately prior to the approval of the matter or on the day before the announcement of the proposed matter and thus to withdraw from the Corporation.” H. HENN & J. ALEXANDER, supra note 6, at 997; see also MODEL BUSINESS CORP. ACT § 13.02 (1984) (amended 1986); CAL. CORP. CODE § 1300 (Deering 1977).

21. Buy-out contracts or buy-out arrangements are “provisions, usually in shareholder agreements, whereby in the case of deadlock (as well as other contingencies), one faction can be bought out, thus preserving the corporation as a going concern and assuring a fair price to those whose interests are bought out.” H. HENN & J. ALEXANDER, supra note 6, at 736.
there is no market price.\textsuperscript{22}

Joint ventures like closely held corporations generally have no market for their stocks and thus, minority or equal partners cannot liquidate their investments easily. Once a shareholder dispute or a deadlock\textsuperscript{23} occurs, fair resolution is difficult to obtain. Thus, a joint venture has problems resolving disputes or deadlocks that are similar to those of a closely held corporation and that require similar methods for their resolution such as buy-out contracts or methods of valuing stock.\textsuperscript{24}

(2) Distinctions Between a Joint Venture and a Closely Held Corporation

There are two primary distinctions between a joint venture and a closely held corporation. The first involves a characteristic of both closely held and publicly held corporations, namely, that a shareholder who has a majority of stock can control the corporation (the "Principle of Stock Majority").\textsuperscript{25} The majority shareholder can monopolize all directors and operate the corporation according to his business judgment.\textsuperscript{26}

The Principle of Stock Majority is not always operative in a joint venture for three reasons. First, in a joint venture, directors are allotted to parent companies in proportion to their shares by a special agreement.\textsuperscript{27} A parent company that has only a forty-nine percent share of

\textsuperscript{22} When there is no market price, courts consider many factors including earning value, dividend value and asset value. There is no established method, however, for valuing the stock of a closely held corporation. H. HENN & J. ALEXANDER, supra note 6, at 1003; F. O'NEAL, supra note 16, § 2.16, at 45-48.

\textsuperscript{23} Deadlock occurs when no decision can be made at a shareholder meeting or by a board of directors because no single parent company has enough voting power to approve a decision.

\textsuperscript{24} See generally F. O'NEAL, supra note 16, ch. 8; UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION (UNIDO), MANUAL ON THE ESTABLISHMENT OF INDUSTRIAL JOINT-VENTURE AGREEMENTS IN DEVELOPING COUNTRIES, ch. 8 (1971) [hereinafter UNIDO].

\textsuperscript{25} "[T]he holders of a majority of the shares with voting power control the corporation." F. O'NEAL, supra note 16, § 1.02, at 3.

\textsuperscript{26} In contrast, all partners have equal rights in the management of a partnership. UNIF. PARTNERSHIP ACT § 18(e) (1914). Ordinary matters may be decided by a majority of the partners. Id. § 18(h). Although the concept of majority rule in partnerships is based on one vote per partner, it may be based on capital accounts or other actors. A. BROMBERG, supra note 9, § 65, at 381-82. By agreement, management may be concentrated in one or more partners. Id. § 65, at 374.

\textsuperscript{27} Parent companies use "binding nominations" clauses (for example, "Three Directors shall be appointed by Parent Company A, three by Parent Company B. In their capacities as shareholders, Parent Company A and Parent Company B agree that they shall nominate three and three directors respectively, and that each shall vote for the nominees of the other.")., or "different classes of shares" clauses (for example, "As registered owner of the Class A shares, Parent Company A shall be entitled to make binding nominations for the appointment of three directors, and Parent Company B, as registered owner of the Class B shares, shall be entitled to
the joint venture can account for almost half of the joint venture's directors. By contrast, although many closely held corporations also have special agreements, their usage is less prevalent than in joint ventures.\textsuperscript{28}

Second, the Principle of Stock Majority may not operate because a minority joint venture parent company, by virtue of an express pre-agreement, generally has a veto power in important decisions.\textsuperscript{29} Each parent company may veto any decision that may increase the liability of parent companies, change the controlling share of parent companies, or change the purpose of the joint venture.\textsuperscript{30} Allowing a veto power in everyday business decisions, however, is not wise because it may cause future disputes or deadlocks.\textsuperscript{31} The number of joint ventures which have special veto agreements is much higher than with closely held corporations.\textsuperscript{32}

Third, the bargaining leverage of a minority parent company of a joint venture also affects the operation of the Principle of Stock Majority. Since a joint venture is a cooperative mechanism, a majority parent company cannot ignore the minority parents. For example, a minority parent might supply some essential know-how, license, raw material, or distribution route. Relatively speaking, the minority shareholders of a joint venture are more sophisticated and have more economic power than those in a closely held corporation.\textsuperscript{33}

\textsuperscript{28} F. O'NEAL, supra note 16, § 8.01.
\textsuperscript{29} UNIDO, supra note 24, at ch. 3 § 1(4).

make binding nominations for the appointment of three directors. Both Parent Company \textit{A} and Parent Company \textit{B} agree to take all steps necessary to secure the appointment of the above said nominees in accordance with the laws of California, the United States.\textsuperscript{34}). UNIDO, supra note 24, at ch. 3 § 1(4).

\textsuperscript{28} F. O'NEAL, supra note 16, § 8.01.
\textsuperscript{29} In partnerships, each partner has a veto on extraordinary matters, Fortugno v. Hudson Manure Co., 51 N.J. Super. 482, 144 A.2d 207 (1958), matters enumerated by statute, UNIF. PARTNERSHIP ACT § 9(3) (1914), or matters which are in violation of the partnership agreement. Id. § 18(h). These rights, however, may be varied by agreement. A. BROMBERG, supra note 9, § 66, at 381-82.
\textsuperscript{30} UNIDO, supra note 24, at ch. 3 § 1(7).
\textsuperscript{31} Telephone interview with Frederick C. Rich, attorney with Sullivan & Cromwell, New York (Sept. 22, 1986). For example, a minority parent company may exercise its veto when the joint venture is selecting officers, selling important assets of the joint venture, making loans to a parent company, selecting auditors, liquidating the joint venture, increasing or decreasing the authorized capital, selling stock, changing the joint venture agreement, and issuing new stocks.

\textsuperscript{32} F. O'NEAL, supra note 16, § 8.01. "The hallmark of a joint venture is the great variety of agreements required to establish it." Bergens, Foreign Ventures—A Legal Anatomy, 26 BUS. LAW. 1527, 1542 (1971).

\textsuperscript{33} By definition, shareholders in a joint venture are not individuals but instead are enterprises that have already been operating some other business. See supra text accompanying notes 9-15. Therefore, even a minority shareholder has business experience and knowledge, a business reputation, an established credit line, a clientele, and capital assets. Individual minority shareholders in a typical closely held corporation, on the other hand, do not usually have such tangible and intangible business assets.
The Principle of Stock Majority does not always hold true in a joint venture because of the three characteristics discussed above. Even if one parent company owns more than fifty percent of the joint venture's shares, that parent company is not necessarily guaranteed full control of the joint venture. Therefore, there is less need to protect the minority shareholders of a joint venture than there may be for those of a closely held corporation.

The second distinction between a joint venture and a closely held corporation is the duplicity of joint ventures' directors' interests. Almost all the directors of a joint venture are interlocking directors or employees of one of the parent companies; thus, they have interests not only in the joint venture but also in one of the parent companies. In contrast, directors of a closely held corporation usually represent only the corporation.

The directors' interests in the parent company are usually paramount to their interests in the joint venture. A director may represent parent company interests instead of the joint venture's interests in accordance with the primary objective of creating the joint venture—to maximize the interests of parent companies. A problem thus may arise with joint venture directors in that each has a fiduciary duty not only to the parent company but also to the joint venture.

C. Comparison of a Joint Venture with a Parent-Subsidiary Relationship

(1) Similarities Between a Joint Venture and a Parent-Subsidiary Relationship

A parentsubsidiary relationship can be defined as a relationship between two companies in which a single parent company has control of a subsidiary company. There are two kinds of subsidiaries: (1) a subsidiary in which the parent company is a solitary shareholder; and (2) a subsidiary that has one parent holding a majority of stock and minority shareholders. Only in the latter case does the problem of protecting the rights of minority shareholders arise. The parent company in such cases tends to use its controlling shares to benefit its own interests regardless of the interests of the subsidiary. The parent company may try to "freeze out" minority shareholders of the subsidiary or force the subsidiary to go private.

37. See generally W. CARY & M. EISENBERG, supra note 36, at 1556-60.
There are two primary similarities between a joint venture and a parent-subsidiary relationship. The first similarity focuses on the need to protect minority shareholders. Because directors in a subsidiary company often represent the interests of their parent company, a parent company may deprive its subsidiary of profits that were earned by the subsidiary company or corporate opportunities that should have belonged to the subsidiary company. Thus, the minority shareholders in a subsidiary company are in a vulnerable position. When a subsidiary is a publicly held corporation, the minority shareholders can at least sell their shares in the open market. The minority shareholders in a closely held subsidiary company, however, are in a very vulnerable position. They cannot easily liquidate their investment, and the parent tends to neglect the interests of the subsidiary.\textsuperscript{38}

The vulnerability of minority shareholders can also occur in a joint venture. In reality, however, a minority shareholder in a joint venture is not as vulnerable as a minority shareholder in a subsidiary. Even a joint venture minority shareholder is a parent company and a sophisticated economic actor. The minority shareholder in a joint venture usually has enough economic power and negotiating leverage to contract in advance for the protection of its interests as a minority shareholder.

The second similarity between joint ventures and parent-subsidiary relationships involves the fiduciary duties of parent companies. Thus far this Essay has mentioned only the fiduciary duties of directors or officers of a joint venture who also represent their parent companies. The principles underlying these fiduciary duties also apply to the relationship between parent companies engaged in a joint venture. The fiduciary duties owed by the parent companies of the joint venture to other parent companies are similar to the fiduciary duties owed by controlling shareholders to minority shareholders in a corporation. The fiduciary duty of a controlling shareholder is widely recognized in case law.\textsuperscript{39} The principles that impose fiduciary duties on controlling shareholders with respect to

\textsuperscript{38} Id.

minority shareholders apply without modification to parent companies in parent-subsidiary relationships.40

Parent companies of a joint venture, unlike other corporate parent companies, are not necessarily controlling shareholders. In a joint venture, even a minority-shareholder parent company has a veto power. Any parent company may control or influence the interests of other parent companies through its veto power. Therefore, a parent company of a joint venture, to the extent that it has influence on the other parent companies' interests, has a fiduciary duty comparable to that of a partner in a partnership.41 But because minority parent companies of a joint venture are sophisticated economic actors as a matter of course, there is less need to impose fiduciary duties to protect than there is to protect minority shareholders of a subsidiary.

The directors or officers of a joint venture or a subsidiary will be in contradictory positions when the interests of the joint venture or the subsidiary and the interests of their parent companies collide. In practice, the directors or officers of a joint venture or a subsidiary are likely to give the interests of their parent companies the higher priority.42 In theory, however, a director or an officer of a joint venture has a fiduciary duty to give the interests of the joint venture the higher priority over the conflicting interests of an individual parent company to protect the interests of the joint venture and minority-shareholder parent companies. Similarly, a director or officer of a subsidiary in a parent-subsidiary relationship has a fiduciary duty to give the interests of the subsidiary higher priority than the conflicting interests of the parent company.

(2) Distinctions

The clearest distinction between a joint venture and a parent-subsidiary relationship is the number of parent companies. The multiplicity of parties and their individual interests involved complicates analysis of conflicts of interest in a joint venture. Because a joint venture has at least two parent companies and a subsidiary has only one, by definition a joint

41. "Joint adventures, like copartners, owe to one another, while the enterprise continues, the duty of the finest loyalty." Meinhard v. Salmon, 249 N.Y. 458, 463-64, 164 N.E. 545, 546 (1928) (Cardozo, J.).
42. There are two motives that drive the directors and officers of a joint venture or a subsidiary to favor the parent company's interests. First, the directors or officers of a joint venture or a subsidiary are nominated by their parent companies. They must follow the intent of their parent companies to maintain their positions as directors or officers. Second, interlocking directors or officers "have a greater personal interest in the financial well-being of the parent company." Brudney & Clark, supra note 34, at 1047.
venture has more distinct interests than a subsidiary. A joint venture has at least three distinct interests: those of each of the two parent companies and those of the joint venture. A subsidiary has only two interests: those of the parent company and those of the subsidiary.\textsuperscript{43} Thus, a conflict of interest analysis of the fiduciary duties of parties involved in a parent-subsidiary relationship is inadequate to cover the interests involved in a joint venture.

The antitrust problems which may arise in a joint venture illumi-
nates a second distinction between a joint venture and a parent-subsidiary relationship. The creation of a joint venture has procompetitive effects because it creates new competitive entrants through its synergistic effect.\textsuperscript{44} A joint venture also has some anticompetitive effects, resulting from the unique characteristics of a joint venture as either a combination of enterprises\textsuperscript{45} or a dealing between enterprises,\textsuperscript{46} which may result in antitrust violations: (1) market monopolization,\textsuperscript{47} (2) loss of potential competition,\textsuperscript{48} (3) market exclusion,\textsuperscript{49} (4) collateral or ancillary re-

\textsuperscript{43} A typical subsidiary may be said to have three interests if one counts separately the interests of minority shareholders of the subsidiary.
\textsuperscript{44} Mead, The Competitive Significance of Joint Ventures, 12 ANTITRUST BULL. 819, 823-25 (1967).
\textsuperscript{45} Parent companies do not merge into one entity through the creation of a joint venture. They do combine some of their power, however, and create a separate new entity. Thus, creating a joint venture has an effect on market structure in increasing the degree of monopoly. The degree of the effect depends upon the scale of the joint venture. The antitrust problem of market structure or monopoly is regulated by § 2 of the Sherman Act and § 7 of the Clayton Act. See generally L. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST 18-149 (1977).
\textsuperscript{46} At least three entities (two or more parent companies and a joint venture) exist after the creation of a joint venture; there is only one entity after a merger. When parent companies and their joint venture deal with each other the antitrust problem of agreement may arise. This problem of agreement is regulated by § 1 of the Sherman Act. See generally L. SULLIVAN, supra note 45, at 150-329.
\textsuperscript{47} See generally L. SULLIVAN, supra note 45, at 5-58. A joint venture is a combination of enterprises. Its anticompetitive effect is generally compared to the anticompetitive effect of a merger. Therefore, like a merger, definitions of relevant market and changes in the Herfindahl-Hirschman Index (HHI) in the relevant market are important. See Department of Justice Merger Guidelines, 49 Fed. Reg. 26,823 (1984).
\textsuperscript{48} Co-ownership of a joint venture may partially bind the interests of parent companies and may diminish potential competition between them. Potential competition between a parent company and a joint venture may also be diminished because the existence of the joint venture reduces the incentive for each to enter the other's market. Brodley, supra note 11, at 1531.
\textsuperscript{49} The problem of market exclusion occurs when the product of a joint venture is so valuable for an industry (bottleneck monopoly) that the joint venture should make it available to everyone at a reasonable and nondiscriminatory price. Associated Press v. United States, 326 U.S. 1 (1945); Gamco, Inc. v. Providence Fruit & Produce Bldg., 194 F.2d 484 (1st Cir.), \textit{cert. denied}, 344 U.S. 817 (1952); see 1 W. FUGATE, FOREIGN COMMERCE AND THE ANTITRUST LAWS § 168 (3d ed. 1982); Brodley, supra note 11, at 1532-34.
straint,\textsuperscript{50} and (5) collusion between parent companies.\textsuperscript{51}

In contrast, because there is only one parent company in a typical parent-subsidiary relationship, there cannot be an antitrust conspiracy or a collusion between parent companies. Although the reader should be aware of potential liability, there is only limited discussion of antitrust violations in this Essay.

D. Summary

The similarities between a joint venture and both a closely held corporation and a parent-subsidiary relationship make much of the analysis of the fiduciary duty problems in the context of closely held corporations and parent-subsidiary relationships applicable to joint ventures. As will become clear in later discussion, however, the standard analysis must be modified in some important respects when applied to a joint venture because of the multiplicity of interests present and the potential for antitrust violations.

II. Conflicts of Interest Between a Joint Venture and a Parent Company

There are a number of potential conflict of interest situations in a joint venture, which arise between a joint venture and a parent company, and between parent companies. These conflicts can be divided into three categories: (1) self-dealing conflicts, (2) corporate opportunity conflicts, and (3) disclosure conflicts. The following discussion will illustrate each type of conflict in detail.

50. Joint venture agreements, particularly licensing agreements, often include geographical or customer restraints on the sale of the joint venture’s products. UNIDO, \textit{supra} note 24, at ch. 52. Joint venture agreements often restrain parent companies that compete with a joint venture in the joint venture’s geographic or product market. Yamaha Motor Co. v. Federal Trade Commission, 657 F.2d 971 (8th Cir. 1981), \textit{cert. denied}, 456 U.S. 915 (1982); Brunswick Corp., 94 F.T.C. 1174 (1979). The courts apply a “two-stage” test to collateral or ancillary restraints. The first stage queries whether the restraint is ancillary to a legitimate business purpose of the joint venture or whether it is a “naked” restriction. The second question is, whether the ancillary restraint is necessary to achieve the legitimate goals of the joint venture. Brodley, \textit{supra} note 11, at 1543 n.69.

51. Collusion is the most serious antitrust problem of joint ventures. Most directors or officers of a joint venture are interlocking directors or officers with parent companies or employees of parent companies. Therefore, parent companies may exchange information about price or production levels and may make informal uncompetitive agreements with each other. A joint venture may thus be used as a tool of a cartel. The risk of collusion is almost unavoidable when a joint venture is created. Courts have had difficulty deciding what kind of communication between directors or officers is collusion. Brodley, \textit{supra} note 11, at 1530.
A. Self-Dealing Conflicts of Interest

Self-dealing conflicts of interest may occur when a joint venture transacts with one of its parent companies. The interests of a joint venture and the interests of the parent company may conflict when a transaction is favorable for the joint venture and unfavorable for the parent company or vice-versa. In such situations, interlocking joint venture directors or officers may be confronted with incompatible interests.

For example, when a parent company supplies materials to a joint venture, the interest of the parent company is to sell these materials at the highest price possible, whereas the interest of the joint venture is to purchase them at the lowest price possible. If a joint venture purchases materials from one of its own parent companies at an unreasonably high price, this transaction conflicts with the fair distribution of the joint venture's profits between the transacting parent company and the other non-transacting parent companies.

The joint venture formed by GM and Toyota, New United Motor Manufacturing, Inc. (NUMMI), presents an example of a situation that poses the possibility of a self-dealing conflict. Toyota is the exclusive supplier of auto parts to be used by the joint venture in the manufacture of subcompact cars. GM is the exclusive purchaser and distributor of the finished cars. Toyota may benefit in the long run by charging the joint venture a high price for auto parts and splitting a resulting smaller profit on the finished product with GM, while GM may benefit by buying finished cars at a lower cost than the reasonable wholesale value of the cars. Both of the parent companies have an interest in the success and profitability of the joint venture that is at odds with each parent's individual interest in maximizing its profit on transactions conducted directly with the joint venture.

B. Corporate Opportunity Conflicts of Interest

A corporate opportunity conflict of interest occurs when a joint venture and one of its parent companies compete for the same business opportunity. The interest of a joint venture and the interest of the parent

52. See, e.g., Delaney v. Georgia-Pacific Corp., 278 Or. 305, 315, 564 P.2d 277, 283 (1977) (rate of simple interest charged a joint venture by a parent company could not be unilaterally changed to a compounded interest rate in absence of express agreement). In a partnership, self-dealing without disclosure would be a violation of § 21(1) of the Uniform Partnership Act and the partner which obtains secret profit from the transaction “must account to the partnership for any benefits.” UNIF. PARTNERSHIP ACT § 21(1) (1914); see Reynolds, supra note 15, at 15-16; A. Bromberg, supra note 9, § 68, at 390.
company may conflict if both seek, but only one can take, the business opportunity.

A corporate opportunity is any business opportunity that must be offered to the corporation or that may be considered a corporate asset. For purposes of this Essay, a business opportunity is any opportunity a corporation has to make a profit. There are two types of business opportunities: (1) opportunities to obtain legal rights to possession of tangible property, intangible property, and contractual rights; and (2) opportunities to enter new product or geographic markets. Sometimes one type of business opportunity will lead to another. For example, an opportunity to acquire property may lead to an opportunity to enter into a new market; or a corporation may hear of an opportunity to penetrate a new market, but must then seek out an opportunity to acquire necessary materials or rights. From the viewpoint of a shareholder's expectation, the business opportunities that are within the scope of the business of the joint venture are corporate opportunities.

The conflict arises when a business opportunity within the scope of the joint venture's business is also within the scope of the business of a parent company. The determination of which company, a joint venture or a parent company, may take the corporate opportunity depends on two factors: the relationship of the corporate opportunity and the profitability of the opportunity to each company and how the corporate opp-

53. AMERICAN LAW INSTITUTE PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 5.12(b), comment d, at 186 (Tent. Draft No. 5 1986) [hereinafter ALI CORPORATE GOVERNANCE].

54. Brudney & Clark, supra note 34, at 999.

55. See, e.g., Guth v. Loft, Inc., 23 Del. Ch. 255, 5 A.2d 503 (1939) (involving an opportunity to take over an enterprise similar to a joint venture).


57. ALI CORPORATE GOVERNANCE, supra note 53, § 5.05(b).

58. Id. at 186.

59. Id. at 186-87. The ALI defines corporate opportunities in the context of relationships between dominating shareholders and corporations as follows:

[A] corporate opportunity means any opportunity to engage in a business activity that is held out to shareholders of the corporation as being within the scope of the business in which the corporation is presently engaged or may be reasonably expected to engage, and that is neither developed nor received by the dominating shareholder within the scope and regular course of his own business activities. "A business activity" includes the acquisition or use of any contract right or other tangible or intangible property.

ALI CORPORATE GOVERNANCE, supra note 53, § 5.12(b).

60. This factor is used by Brudney & Clark, supra note 34, at 1049-55.
Although these factors will be examined more closely in part III, it is useful to note for present purposes that a corporate opportunity may arise in different ways. It may come to a director or officer of the parent company as an individual or in his role as a director or officer of the parent company. In the latter case, he may become aware of the opportunity through the use of corporate information or property. A corporate opportunity may also appear to a director or officer of a joint venture as an individual, or in his role as a director or officer or employee of the joint venture. In this case, he may become aware of the opportunity either through the use of the parent company's information or property, or through the use of the joint venture's information or property.

Under the definition of a corporate conflict of interest in this Essay, the means by which funds are raised to acquire a corporate opportunity are not considered part of the corporate opportunity itself, but are closely related to the corporate opportunity problem. Solutions to conflict of interest problems arising between a parent company and a joint venture in determining dividend policies and capital levels will be discussed in a later section.

A corporate opportunity conflict of interest may occur in a variety of contexts. One example is an opportunity to obtain a legal right which will benefit both a joint venture and a parent company. Suppose Parent Company A, a large electronics company in Japan and Parent Company B, a growing software company in the United States, create a joint venture in the United States to manufacture personal computers. If there is a business opportunity to obtain a controlling share of a small computer company in the United States, which is in a dangerous financial position but has valuable know-how and patents, both parent companies as well as the joint venture may wish to acquire the controlling share. The issue is whether the directors from the parent companies should be held personally liable for depriving the joint venture of a corporate opportunity if

61. This factor is used by the ALI CORPORATE GOVERNANCE, supra note 56, § 5.12(b) comment d.
62. See infra notes 158-71 and accompanying text.
63. ALI CORPORATE GOVERNANCE, supra note 53, § 5.05 comment b.
64. Funds may be raised for this purpose by, for example, increasing capital, or obtaining loans. See, e.g., Delaney v. Georgia-Pacific Corp., 278 Or. 305, 313-14, 564 P.2d 277, 282 (1977) (A common officer between a joint venture and a parent was not authorized to cause the parent to pay off a loan the joint venture had from a bank without the knowledge or consent of the joint venture's board, nor was he authorized to execute a demand note to the joint venture on behalf of the parent in the amount of the payoff. The joint venture had an opportunity to renew or extend the loan.)
65. See infra notes 181-91 and accompanying text.
the directors allow their parent company to obtain the controlling share without first offering the opportunity to the joint venture.\textsuperscript{66}

A joint venture's entrance into a new market provides a second example of a corporate opportunity conflict of interest. Assume Parent Company \textit{A}, a large electronics company in the United States, and Parent Company \textit{B}, a domestic wholesaler in the Philippines, create a joint venture in the Philippines to manufacture and sell televisions in the Philippines. A corporate opportunity conflict arises if Parent Company \textit{B} proposes to expand the market of the joint venture into Indonesia, and Parent Company \textit{A} plans to create a subsidiary in Indonesia to manufacture and sell televisions in Indonesia. In the interest of the joint venture, the directors from Parent Company \textit{A} should approve the proposal to expand the joint venture into Indonesia. In the interest of Parent Company \textit{A}, however, the directors should oppose the proposal. In fact, the directors are likely to oppose the proposal to expand the joint venture into Indonesia because the directors give the interests of Parent Company \textit{A} higher priority than the interests of the joint venture.\textsuperscript{67} Such a situation raises the issues of whether the directors from Parent Company \textit{A} should be held personally liable for depriving the joint venture of a corporate opportunity to expand and whether this action by the directors constitutes a violation of their fiduciary duties to the joint venture.

Disputes over dividend policy, which is closely related to the corporate opportunity conflict of interest problem, may create a third conflict of interest problem. For example, Parent Company \textit{B}, a domestic parent wants to limit dividends and retain profits for future expansion of the joint venture. On the other hand, Parent Company \textit{A}, a foreign parent, wants to receive high dividends and recoup its investment as soon as possible. In this example, the interests of the joint venture or Parent Company \textit{B} conflict with those of Parent Company \textit{A}. The decision of directors from Parent Company \textit{A} to make the joint venture pay high dividends raises the issue of the directors' personal liability for violating

\begin{footnotesize}

\textsuperscript{67} If both parents of the joint venture in this case were domestic, this hypothetical would become an antitrust problem of market division. See Huffington v. Upchurch, 532 S.W.2d 576 (Tex. 1976) (geographic expansion).
\end{footnotesize}
their fiduciary duties by depriving the joint venture of corporate opportunities.

A fourth corporate opportunity conflict of interest arises when a joint venture wishes to increase its capital. Using the same facts as the above example, Parent Company \( B \), a domestic parent, wants to increase the capital of the joint venture to expand its business. On the other hand, Parent Company \( A \), a foreign parent, does not want to expand investment because it is uncertain it will be able to recoup its investment. Consequently, there is a conflict between the aligned interests of the joint venture and Parent Company \( B \) and the interests of Parent Company \( A \). Again, the issue arises whether the directors from Parent Company \( A \) can be held personally liable for breaching their fiduciary duties by depriving the joint venture of corporate opportunities if they veto the proposal by Parent Company \( B \) to increase the capital of the joint venture.

C. Disclosure Conflicts of Interest

Disclosure conflicts of interest occur when a director or an officer of a joint venture has information about either the joint venture or a parent company, or when a parent company has sole access to information that is necessary for operating the joint venture.\(^68\) The interests of a joint venture conflict with the interests of the parent company because the disclosure of the information may be beneficial to the joint venture and harmful to the parent company, or vice-versa.

The GM-Toyota joint venture to manufacture and sell subcompact cars presents an example of a disclosure conflict. Toyota has the know-how to manufacture subcompact cars and GM has a distribution network. The product of the joint venture, the Nova, is very similar to one of Toyota's products, the Corolla. When the joint venture determines the price of the Nova, it is in the best interest of the joint venture that Toyota disclose information about the costs and the price of Corolla. Disclosure of the cost and price information of the Corolla, however, is contrary to Toyota's interests.\(^69\) An issue arises as to whether Toyota's directors can be held personally liable for violation of their fiduciary duties to the joint venture for not disclosing information about the Corolla.\(^70\)

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\(^{69}\) This example is based on the 1984 Toyota-GM joint venture in Fremont, California, also known as NUMMI.

\(^{70}\) This example illustrates the antitrust problem of collusion. This problem will be discussed infra text accompanying notes 212-21.
III. Alternative Solutions

There are several alternative solutions to the fiduciary problems in the operation of joint ventures. Specifically, these alternative solutions attempt to resolve the conflicts of interest created when a director of a joint venture favors the interests of the parent company over those the joint venture.

One possible solution, which modifies the fiduciary duties owed by directors or officers to the joint venture, argues that dissenting parent companies in some instances should be estopped from undertaking direct action against a joint venture director for breach of fiduciary duties. Under this theory, there may be an implied agreement between parent companies that allows the representatives of each parent company to vote for the interests of their parent company without the risk of being held personally liable for breach of their fiduciary duties to the joint venture. This theory presupposes that, because a joint venture is created for the purpose of maximizing the interests of parent companies, each parent company understands from the start that the directors and officers of a joint venture will afford the highest priority to their respective parent’s interests. Joint venture parent companies usually contract with each other or include in the articles of incorporation a right to appoint directors in proportion to their corporate shares and the power to veto important corporate decisions. The theory assumes that provisions are an additional indication that each parent company (majority and minority parent companies alike) participating in a joint venture has impliedly agreed to a joint venture structure under which each director can be expected to favor his respective parent company’s interest. The theory concludes that dissenting parent companies in a joint venture should be estopped from seeking to hold directors of a joint venture individually liable for breaches of fiduciary duty to the joint venture.

For several reasons, this theory of implied agreement and estoppel does not, however, serve as a complete solution to the conflict of interest problems of interlocking directors and officers in joint ventures. First, the existence of an implied agreement or recognition among parent companies that certain directors are straw men for the parent companies is not enough to diminish the fiduciary duty owed by corporate directors and officers to the joint venture. When a person takes a position as a

71. Even minority parent companies have those rights. See supra text accompanying notes 29-30.
director or officer of a joint venture, he owes fiduciary duties both to the
corporation (the joint venture) and to its shareholders (the parent com-
panies participating in the joint venture). The directors still run the risk
of being held liable to the joint venture if they violate their fiduciary du-
ties in the context of conflicts of interest between the joint venture and
their parent company.

Second, the argument is based on the assumption that the directors
and officers in joint ventures will be straw men. In many cases, however,
directors and officers of joint ventures have substantial discretion and
authority to make business decisions independent of their parent
company.

Third, even when interlocking directors or officers can act in the
interest of their parent company without risking personal liability for
breach of their fiduciary duty to the joint venture, each parent company
arguably owes fiduciary duties to the other parent companies.\(^7\)

The argument that an implied agreement exists makes sense only
when the directors who have violated their fiduciary duties toward the
joint venture are straw men for their parent company and they can prove
that a complaining parent company knew that they were straw men and
did not expect them to fulfill their fiduciary duties to the joint venture.
In such a case, the complaining parent company should be estopped from
suing the individual directors.

Despite a parent company's fiduciary duty to the other parent com-
panies as the responsible actor for a director's actions, the director owes
fiduciary duties to both the joint venture and other parent companies.
The importance of the director’s fiduciary duty may be different in self-
dealing conflicts, corporate opportunity conflicts, and disclosure conflicts
and may also vary depending on the facts of a particular case. The fol-
lowing section will discuss alternative solutions that enable the directors
of a joint venture to avoid contradictory positions and that balance the
contrary interests of parent companies in each scenario discussed in part
II.\(^7\)

A. Alternative Solutions to Self-Dealing Conflict of Interest Problems

Self-dealing, a controversial issue in corporation law, has been dis-
cussed in three contexts: (1) when a corporation transacts with one or
more of its directors or transacts with another corporation in which one

\(^7\) Cf. Zahn v. Transamerica Corp., 162 F.2d 36, 46 (3d Cir. 1947) (corporation owes
duty to subsidiary's minority shareholder).

\(^7\) See supra notes 52-70 and accompanying text.
or more of its directors has a material financial interest;\textsuperscript{75} (2) when a corporation transacts with another corporation that has one or more interlocking directors but no controlling relationship between them; and (3) when a corporation transacts with another corporation that has one or more interlocking directors and a parent-subsidiary relationship between them. Most of the analysis of self-dealing in these contexts applies to a transaction between a joint venture and one of its parent companies.\textsuperscript{76} In some important respects, however, a self-dealing transaction in the context of a joint venture has peculiar characteristics that distinguish it from self-dealing transactions in other corporate contexts.

A mere conflict of interest is insufficient to find a self-dealing transaction voidable.\textsuperscript{77} The transaction is voidable only when it is unfair.\textsuperscript{78} Two factors determine the fairness of a self-dealing transaction: (1) full disclosure to and ratification by independent directors or independent shareholders;\textsuperscript{79} and (2) fairness of the terms of the transaction.

\textit{(I) Disclosure and Ratification}

The interested directors\textsuperscript{80} of a self-dealing transaction are required to disclose material facts to the board of directors or to the shareholders.\textsuperscript{81} There are two types of information which can be regarded as material: facts regarding the interests of interested directors, and facts regarding the contract or transaction.\textsuperscript{82} The failure to disclose material

\textsuperscript{75}. See, e.g., \textit{Cal. Corp. Code} § 310(a) (West 1977).

\textsuperscript{76}. See \textit{W. Cary & M. Eisenberg, supra note 36, at 565-86; H. Henn & J. Alexander, supra note 6, § 238, at 637-44.}

\textsuperscript{77}. From the late 1880s through around 1910, a self-dealing transaction was voidable on the basis of the conflicting interest alone. See cases cited in Marsh, \textit{supra note 72, at 36, n.3. See also R. Clark, Corporate Law, at 160 (1986).}


\textsuperscript{79}. "Independent directors" and "independent shareholders" are directors and shareholders who have no personal interest in either a transaction between the corporation and one or more of its directors or a transaction between the corporation and another corporation which has one or more interlocking directors. For a discussion of quorum and voting rights, see H. Henn & J. Alexander, \textit{supra} note 6, § 238, at 640.

\textsuperscript{80}. "Interested directors" are directors who transact with the corporation or who are common directors of another corporation which transacts with the corporation.


facts is in itself evidence of unfairness. In a self-dealing transaction between a joint venture and one of its parent companies, disclosure to an independent board of directors is particularly important to avoid unfair self-dealing because this disclosure allows the parent companies to monitor each other's conduct. In a joint venture, even the minority parent companies have bargaining leverage and the ability to monitor the fairness of transactions.

In a closely held corporation or a parent-subsidiary relationship, on the other hand, minority shareholders may lack knowledge of business and may have little voice in the operation of business. Therefore, even if full disclosure was made to minority shareholders before the self-dealing transaction, ratification of a transaction by independent directors or shareholders is a less reliable means of determining the fairness of a self-dealing transaction.

Some legislative schemes have attempted to substitute ratification for a fairness test. For example, before it was revised in 1975, section 310 of the California Corporations Code did not require that a self-dealing transaction be "just and reasonable" when the proper procedures for shareholder ratification were followed. The revised law requires that a self-dealing transaction be "just and reasonable" when the transaction is approved only by the board of directors, or when no proper procedure for ratification is followed. Under the relevant Delaware statute, the courts are directed to look to the fairness of a transaction only if there has been neither disclosure nor valid ratification. The courts, however, have not always interpreted these schemes to allow ratification as a sub-

84. See supra text accompanying note 33.
85. Some commentators argue that a fairness test is necessary "to protect shareholders from voiceless submission to potentially harmful interested directors transactions," although they acknowledge the weaknesses inherent in the fairness test. Bulbulia & Pinto, Statutory Responses to Interested Directors' Transactions: A Watering Down of Fiduciary Standards?, 53 NOTRE DAME L. REV. 201, 227 (1977).
86. CAL. CORP. CODE § 310(a)(1) (West 1977). For an illustration and discussion of the California approach to ratification and the fairness test, see Remillard Brick Co. v. Remillard-Dandini Co., 109 Cal. App. 2d 405, 418, 241 P.2d 66 (1952). See also Bulbulia & Pinto, supra note 85, at 205-16 (under the statute, a self-dealing transaction is neither void nor voidable if any one of three circumstances occurs).
88. Id. § 310(a)(3).
89. DEL. CODE ANN. tit. 8, § 144(a) (1983), see Bulbulia & Pinto, supra note 85, at 212-18; see also MODEL BUSINESS CORP. ACT § 41 (1979) (full disclosure removes the question of fairness from judicial inquiry when the board or shareholders approve a transaction pursuant to the statute).
stitute for fairness. In Fliegler v. Lawrence,90 for example, the Delaware Supreme Court took the position that the defendant's compliance with disclosure and ratification procedures did not preclude judicial inquiry into the fairness of the transaction.91

In assessing the fairness of a self-dealing transaction between a joint venture and one of its parent companies, courts may give more weight to ratification by "independent directors or shareholders" after "full disclosure" than in a general corporate self-dealing transaction92 because of the self-protecting abilities of minority parent companies in a joint venture. Independent directors may include those that represent the interests of other parent companies in a joint venture that have not participated in a particular transaction as well as swing-man directors who are not affiliated with any of a joint venture's parent companies. They do not represent the interests of the particular parent company that has transacted with a joint venture. "Independent shareholders" are parent companies of a joint venture that do not take part in a transaction between a joint venture and one of its other parent companies. The method of ratification required for a self-dealing transaction between a joint venture and one of its parent companies is ratification either by independent directors or by independent shareholders.

Ratification of a self-dealing transaction by the appropriate method is necessary when a parent company desires to transact with a joint venture.93 A corporation will be estopped from challenging a self-dealing transaction if the shareholders unanimously ratified the transaction after full disclosure.94 In addition, a shareholder who ratifies the transaction

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90. 361 A.2d 218 (Del. 1976).
91. Id. at 221-24. In partnerships, almost anything can be provided for in the partnership agreement. Riviera Congress Assocs. v. Yassky, 18 N.Y.2d 540, 548, 223 N.E.2d 876, 880, 277 N.Y.S.2d 386, 392 (1966). If there is disclosure and consent of non-interested partners, the courts will let the transaction stand. See Ben-Dashan v. Plitt, 58 A.D.2d 244, 247, 396 N.Y.S.2d 542, 545 (1977).
92. For purposes of this Essay, a “general self-dealing transaction” is a transaction between a corporation other than a joint venture, including both a closely held corporation and a publicly held corporation, and one or more of its directors or another corporation having common directors.
93. In partnerships, self-dealing transactions may be ratified by express or implied agreement. When there is a “full disclosure of all material facts,” implied consent of the partners could be inferred. Reynolds, supra note 15, at 11, 15.
94. See Schreiber v. Pennzoil Co., 419 A.2d 952, 957 (Del. Ch. 1980). Even in a case of
after full disclosure will be estopped from bringing a derivative suit.\textsuperscript{95} A joint venture usually has few independent shareholders and, compared to independent shareholder ratification in a corporation, it is therefore relatively easy to ratify unanimously a self-dealing transaction. Once the parent company receives unanimous ratification by independent shareholders or independent directors, it can transact with a joint venture.\textsuperscript{96}

Some joint venture agreements prohibit transactions between the joint venture and any parent company unless the other parent companies unanimously ratify the transaction.\textsuperscript{97} Even with these agreements, however, the problem of disclosure remains.

The requirement of "full disclosure" is the most difficult problem in obtaining effective ratification from independent shareholders or directors. Ideally, full disclosure requires two elements: first, a complete description of the director's self-dealing interests in the transaction, and second, a complete description of the conditions of the transaction.\textsuperscript{98} The former is very clear in the context of a joint venture because each director is presumed to represent the interests of his or her respective parent company. There is a problem, however, in judging the adequacy of the disclosure of the conditions of a self-dealing transaction.

The purpose of disclosing the conditions of a transaction is to supply independent directors or independent parent companies with the information necessary to determine whether the conditions are fair to the joint venture. In some cases, it is easy to obtain data because of the conditions

\footnotesize{\textsuperscript{95} Gottlieb v. McKee, 34 Del. Ch. 537, 107 A.2d 240 (1954).}

\footnotesize{\textsuperscript{96} In a joint venture, courts need not differentiate between the effect of ratification by independent shareholders (non-self-dealing parent companies) and ratification by independent directors (representing the interests of non-self-dealing parent companies) because ratification by either reflects the interests of the same parent company. The interested parent company, however, should obtain ratification by independent shareholders (parent companies), rather than ratification by independent directors, because obtaining shareholders' ratification is not much more difficult than obtaining directors' ratification in a joint venture. The shareholders' ratification has more weight than ratification by the directors. For example, § 310(a)(2) of the California Corporations Code requires that the transaction be "just and reasonable" when it is ratified by the board, \textsl{id.}, but does not require any fairness test when it is ratified by the shareholders. \textsc{Cal. Corp. Code} § 310(a)(1) (West 1977).}

\footnotesize{\textsuperscript{97} Telephone interview with Frederick C. Rich, \textit{supra} note 31. Such an agreement would be similar to a veto agreement. \textit{See supra} notes 29-32 and accompanying text; \textit{see also} F. O'\textsc{Neal} \& R. \textsc{Thompson}, \textit{supra} note 36, §§ 9:08-9:12.}

\footnotesize{\textsuperscript{98} \textit{See supra} note 85 and accompanying text.}
of the transaction. For example, a market price, or a product or service whose cost is easily calculated, facilitates determining transaction conditions. In other cases, however, it is difficult for independent directors to obtain transaction data or difficult for the interested directors to disclose data. This is true when there is no market price or when it is difficult to calculate the cost of the product or service, particularly when the cost of certain products or know-how is a corporate secret of the parent company.

If the disclosure of transaction data is incomplete and there is inadequate information to determine the fairness of a transaction, the monitoring effect of independent directors or independent parent companies will be hindered. From the perspective of the interested parent company, it is not advisable to transact with a joint venture without full disclosure because there is a possibility that the contract will be voidable by either the joint venture or by independent parent companies, despite ratification of the transaction by independent directors or independent parent companies.

The best solution to the problem of inadequate disclosure is for the parent companies to agree on a list of mandatory disclosures prior to creating a joint venture when they anticipate transactions between a joint venture and a parent company. Most of the transactions between a joint venture and a parent company can be anticipated because they are usually programmed into the joint venture project prior to its creation. A disclosure agreement that is ratified by independent directors or independent parent companies, combined with ratification of a self-dealing joint venture transaction, may estop parent companies from challenging the transaction. In addition, a disclosure agreement and ratification of a self-dealing transaction may shift the burden of proof from the interested parent company to the parent companies challenging the fairness of the transaction.

(2) Fairness Test

The fairness of the terms of a self-dealing transaction between a joint venture and one of its parent companies is examined by the courts in three contexts: (1) when the transaction is not ratified; (2) when the transaction is ratified by a majority of independent directors or by a ma-

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99. Conflicts of interest will occur when interlocking directors are required to disclose corporate secrets of their parent company. The disclosure of such information, including corporate secrets, also may be an antitrust violation of § 1 of the Sherman Act, 15 U.S.C. § 1 (1976). For a discussion of the disclosure conflict of interest problem, see infra part III, section C.
ajority of independent parent companies but disclosure is inadequate;\textsuperscript{100} and (3) when the transaction is ratified by at least a majority of independent directors or by a majority of independent parent companies after "full disclosure." The court shifts the burden of proof of fairness from the interested parent company to the complaining parent company.\textsuperscript{101}

When a court judges the fairness of the terms of a self-dealing transaction, the standard of fairness is an "arm's length bargain."\textsuperscript{102} Even if there is a market price, it is not always easy to determine whether a self-dealing transaction is conducted at arm's length for two reasons. First, a company usually has some reason for selling the same product to different customers at different prices including the size of the sale, length or course of past dealing, sale of other products, or geographical situation. For example, if the parent company always sells its product at a special discount of $1,200 to large customers, $1,200 can be considered a special market price for all large customers. If the joint venture is a large customer, it also should be accorded a special discount price. In such a case, a price of $1,400 to the joint venture would not appear to be a price resulting from an arm's length transaction. If the parent company has some reason to charge some special customers $1,200 and charges the joint venture $1,400,\textsuperscript{103} and if the range of prices is reasonable, a price of $1,400 may be considered an arm's length transaction.\textsuperscript{104}

A second difficulty in determining whether a transaction was conducted at arm's length arises because a market price often requires modification when applied to a self-dealing transaction between a joint venture and one of its parent companies that would not be required in a non-self-dealing transaction. Sometimes a contract in a self-dealing transaction

\textsuperscript{101} Michelson v. Duncan, 407 A.2d 211, 224 (Del. 1979); Schreiber v. Pennzoil Co., 419 A.2d 952, 957 (Del. Ch. 1980). It is arguable whether the courts will examine the fairness of the self-dealing transaction when the transaction was ratified by a majority of independent directors or by a majority of independent parent companies, if a minority of independent parent company directors bring suit. \textit{See ALI CORPORATE GOVERNANCE, supra} note 53, § 5.02 comment (a), § 5.10 comment (c).
\textsuperscript{102} The "arm's length bargain" standard asks whether the terms of the transaction (price, period of payment, time of delivery, storage or transportation service, guarantee) between a joint venture and one of its parent companies are similar to the terms of a transaction negotiated by unrelated parties, each acting in his or her own self-interest. Jones v. H.F. Ahmanson & Co., 1 Cal. 3d 93, 460 P.2d 464, 81 Cal. Rptr. 592 (1969).
\textsuperscript{103} For example, even if the joint venture buys almost the same quantity of goods as the special large customers, the special large customers might be old and established clients or they might also purchase other products from the parent company which may justify a volume discount.
\textsuperscript{104} This hypothetical situation was suggested during interview with Professor Saul X. Levmore, \textit{supra} note 72.
contains different conditions than contracts governing other transactions. These conditions include differences in the quality of products supplied by the parent company to a general customer compared to what is supplied to a joint venture customer. There are also differences in the collateral conditions of a contract with an ordinary customer compared to a joint venture customer—for example, period of payment, period of delivery, storage or transportation service, and guarantees. The parent company also might provide a joint venture customer with services or benefits that are not provided to ordinary customers, such as guarantee of loans, sending employees, legal or marketing consulting, brand image, or social credit. These differences in contract terms between ordinary customers and a joint venture customer are difficult to measure in monetary terms. Consequently, it is extremely difficult to modify a market price accurately to reflect the true value of products provided by a parent company to a joint venture customer.\textsuperscript{105}

If there is no market price or no comparative transaction, it is more difficult to decide whether a self-dealing transaction has been conducted at arm's length.\textsuperscript{106} When there is no market price, the fair price in a self-dealing transaction could be determined by calculating the cost of the product or service. Cost plus a reasonable profit\textsuperscript{107} would be a fair price or an arm’s length price.

In certain circumstances, it is not easy to define the cost of the product or service. When a parent company supplies a joint venture with special intangible assets or special services,\textsuperscript{108} for example, there often is no standard by which to calculate these costs. A similar situation occurs when a parent company is the joint venture’s exclusive supplier of certain products; the costs of these special products may be corporate secrets of the parent company and may be difficult to disclose.\textsuperscript{109}

There is an important distinction between a self-dealing transaction in a joint venture and a self-dealing transaction in a parent-subsidiary relationship. In the latter, “the parent company will wish to operate the

\textsuperscript{105} This difficult situation in modifying a market price to a joint venture customer is almost the same as a self-dealing transaction between a subsidiary and its parent company. Egashira, supra note 35, at 97-2-181.

\textsuperscript{106} There are many different factors which must be considered depending upon the transaction including loans, sale of property, and service contracts. Note, The Fairness Test of Corporate Contracts with Interested Directors, 61 HARV. L. REV. 335, 337-39 (1948).

\textsuperscript{107} An “unreasonable” profit might even be fair under certain circumstances, for example, in the sale of rare real property.

\textsuperscript{108} See Note, supra note 106, at 339.

subsidiary for the benefit of the group as a whole and not necessarily for the benefit of that particular subsidiary.”\textsuperscript{110} In a joint venture, because there are at least two parent companies, one parent company will be prevented from operating a joint venture for its own benefit and from disregarding benefits to the other parent companies because each parent company has monitoring power.

Considering the difficulty of applying an arm’s length standard, the fairness of a self-dealing transaction between a subsidiary and a parent company may be judged on whether it is a “reasonable profit split” in the group or not.\textsuperscript{111} In the case of a transaction between a joint venture and a parent company, of course, the reasonable profit split standard cannot be applied.

(3) **Summary**

The solution to the problem of self-dealing conflicts of interest in a joint venture is theoretically simple, using an “arm’s length transaction” standard to assess the fairness of the transaction. Although interlocking directors represent the interests of their respective parent companies, they cannot make a disadvantageous transaction for the joint venture in order to benefit their parent company. If the transaction between a joint venture and one of its parent companies is unfair to the joint venture from a standard of an arm’s length transaction, it is voidable by a joint venture.

In reality, however, applying an arm’s length standard to specific joint venture transactions is often very difficult. Therefore, the best way to solve the self-dealing conflict of interest in a joint venture is to enhance the ability of parent companies to utilize their monitoring mechanism more efficiently and to encourage ratification of self-dealing transactions whenever possible. To accomplish this, disclosure of material facts is indispensible. Disclosure may not always be easy to make and presents another conflict of interest problem, which will be discussed in section C.\textsuperscript{112}


\textsuperscript{112} See infra notes 192-209 and accompanying text.
B. Alternative Solutions to Corporate Opportunity Conflicts of Interest Problems

In practice, corporate opportunity problems in joint ventures are not as serious as those in typical corporations because most of the problems are solved by contracts. Theoretically, however, corporate opportunity conflicts of interest are the most difficult problems to resolve. In the context of self-dealing conflicts of interest, despite a disclosure problem, directors or officers in a joint venture only need ratification by independent directors or independent shareholders to ensure an enforceable contract. In the context of corporate opportunity conflicts of interest, however, interlocking directors or officers in a joint venture appear to violate either their fiduciary duty to the joint venture or to their parent company because they appear to be required to choose between two alternatives: either to give higher priority to the interests of the joint venture or to give higher priority to the interests of their parent company. A parent company which obtains a joint venture’s corporate opportunity will be liable for violating its fiduciary duty. This section proposes solutions to the contradictory positions of directors or officers in a joint venture and seeks to resolve the problems of corporate opportunity conflicts of interest.

(1) Express Agreements

The best resolution to the corporate opportunity conflicts of interest is to create express agreements prior to creating a joint venture. Parent companies can define or narrow the scope of the joint venture’s corporate opportunities in such agreements. There are two kinds of corporate opportunities: opportunities to obtain business assets, and opportunities to enter new markets, such as product or geographic markets. Parent

113. Rankin v. Naftalis, 557 S.W.2d 940, 945 (Tex. 1977); see also Huffington v. Upchurch, 532 S.W.2d 576, 578-79 (Tex. 1976) (under partnership agreement terms, partner held under fiduciary duty to offer opportunity to partnership before taking advantage of opportunity personally).

114. See supra text accompanying notes 92-96.


117. A “product market” is a market which is defined by kinds of products, for example, radio, television, or electrical appliances. “Geographic market” is a market which is defined by geographic area, for example, San Francisco, California, or the United States. These are the terms of antitrust law for measuring monopoly power. See L. SULLIVAN, supra note 46 at 17, 19; L. SCHWARTZ, J. FLYNN & H. FIRST, FREE ENTERPRISE AND ECONOMIC ORGANIZATION: ANTITRUST 108-19 (6th ed. 1983).
companies can anticipate corporate opportunity conflicts in the latter case more often than in the former. For example, when parent companies create a joint venture in the Philippines, the creation of new geographical markets in Indonesia or in Singapore will create potential geographical conflicts of interests. Product market conflicts may occur when the parent companies of a joint venture that produces radios allow the joint venture to create new product markets by producing tape recorders or televisions. To avoid market conflicts of interest, parent companies can define their product and geographic markets in an express agreement prior to creating a joint venture. Anticipating corporate opportunity conflicts in the "obtaining business assets" cases, however, is more difficult because these opportunities generally arise in the daily business affairs of the parent, and each opportunity has unique characteristics.

Some joint venture agreements allow parent companies to compete for any business opportunities with the joint venture. In this way, parent companies narrow the scope of the joint venture’s corporate opportunities and eliminate potential fiduciary duty problems.

Two problems arise with these express agreements. First, an agreement which restricts the scope of a joint venture’s business may create an antitrust problem by restraining competition. The product and geographic markets defined by express agreements may restrain competition by permitting the parent companies to exclude a joint venture from their markets or vice-versa. Furthermore, when a joint venture and its parent companies divide a market horizontally by product or geography, an effective monopoly power may be created in each submarket. Although there may be business justifications for these divisions, horizontal market divisions are illegal per se under the antitrust laws.

Agreements which allow parent companies to compete with the joint venture for all business opportunities may have the same anti-com-

118. See, e.g., Huffington v. Upchurch, 532 S.W.2d 576, 579-80 (Tex. 1976).
120. Contrast this with the case of typical parent-subsidiary, in which the minority shareholders have no equivalent opportunity to gain the protection of such an agreement.
121. For example, horizontal product market division will occur when the product of the joint venture is restricted to tape recorders and a parent company makes televisions but does not make tape recorders.
122. For example, horizontal geographic market division will occur when the joint venture sells electrical appliances only in California and Washington and a parent company sells electrical appliances on a nationwide basis but does not sell in the two states.
123. United States v. Topco Assocs., Inc., 405 U.S. 596, 606-612 (1972) (horizontal geographic market division held to be per se violation of § 1 of the Sherman Act); L. SULLIVAN, supra note 45, at 79-82; L. SCHWARTZ, J. FLYNN & H. FIRST, supra note 117, at 425-37.
petitive effect as market divisions. Under these agreements, a parent company can obtain business opportunities in which a joint venture is interested without fiduciary duty problems. Although a parent company may not always obtain a new market in which a joint venture also is interested, a parent company can easily restrict the joint venture's market with these agreements and vetoes.

The necessity of balancing the interests of parent companies poses a second problem with express agreements. Although express agreements can eliminate fiduciary duty problems of interlocking directors or officers and parent companies, parent companies have to balance interests among themselves to maximize the efficiency of a joint venture and the interests of the parent companies.

(2) Balancing the Corporate Opportunity Interests of Parent Companies

When there is no express agreement adequate to resolve a particular corporate opportunity conflict of interest situation, directors of a joint venture and a parent company must balance the interests of the joint venture and the interested parent company in determining who should obtain the corporate opportunity. A balancing of interests of the joint venture and the parent company is also necessary, when, although there is an express agreement, it avoids the legal fiduciary duty problem in corporate opportunity conflicts of interest but ignores the goal of maximizing the synergistic advantages obtainable from the joint venture.

In addition to liability for breach of its fiduciary duty, a parent company may suffer some disadvantages when it gives priority to its own interests over the interests of a joint venture in a context of a corporate opportunity conflict of interest. There is a limit to which a parent company can favor its own interests over those of a joint venture without provoking a response from the parent companies. Dissatisfied joint venture parent companies can be expected to respond in one of three ways: (1) suing the biased parent company for damages or for the remedial creation of a constructive trust to compensate an injured parent company; (2) suing for dissolution of the joint venture or offering to sell their shares in the joint venture because of oppression by the biased parent company; and (3) not suing, but expressing dissatisfaction by not cooperating with the biased parent company in operating the joint venture.

124. For purposes of this Essay, a "biased" parent company is one which obtains a business opportunity in which a joint venture is also interested. Contrast "biased" with an "interested" parent company, in which the interest is present, but the opportunity is not yet obtained.

125. See generally Finnen, supra note 116.
(3) **Responses of Dissatisfied Parent Companies**

a. Seek Compensation for Damages

The most radical option for parent companies participating in a joint venture is to sue for damages suffered or for the remedial creation of a constructive trust when one of the parent companies takes a corporate opportunity from the joint venture. The criteria for determining when a corporate opportunity conflict of interest becomes a legal problem is whether the business opportunity obtained by the parent company clearly belonged to the joint venture. It is often unclear, however, which business opportunities belong to a joint venture.

The discussion of when an opportunity clearly belongs to a joint venture assumes there is no express agreement between the parents and the joint venture to narrow or define the scope of the joint venture's corporate opportunities. The courts generally apply one of three tests to determine when a business opportunity belongs to a corporation: (1) the interest or expectancy test,\(^{126}(2)\) the line of business test,\(^{127}\) and (3) the fairness test.\(^{128}\) These tests sometimes overlap in practice.\(^{129}\)

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127. The line-of-business test is a standard based on "whether activity is closely associated with the existing or prospective activities of the corporation." H. HENN & J. ALEXANDER, supra note 6, § 237, at 633; Guth v. Loft, Inc., 23 Del. Ch. 255, 5 A.2d 503 (1939); Lutherland, Inc. v. Dahlen, 357 Pa. 143, 151, 53 A.2d 143, 147 (1947); Note, *Corporate Opportunity*, 74 Harv. L. Rev. 765, 768-69 (1961). A commentator points out that "only a very few cases have expressly adopted the 'line of business test.'" Walker, supra note 126, at 627.

128. The fairness test was "ethical standards of what is fair and equitable under the circumstances." H. HENN & J. ALEXANDER, supra note 6, § 237, at 634; see also Durfee v. Durfee & Canning, Inc., 323 Mass. 187, 199, 80 N.E.2d 522, 529 (1948) (corporate directors and officers may not use their position to further their private interests; the true basis of the doctrine rests fundamentally on the unfairness in the particular circumstances of the director); Rosenblum v. Judson Eng., Corp., 99 N.H. 267, 273, 109 A.2d 558, 563 (1954) (business opportunity that belongs to the corporation establishes duty upon officers and directors to acquire it for the corporation, not for themselves; bad faith is not essential in the particular circumstances of a director).

129. Miller v. Miller, 301 Minn. 207, 224, 222 N.W.2d 71, 81 (1974); Note, *Corporate Opportunity* — Miller v. Miller — *Proper Application of the Fairness Doctrine in the Corporate Opportunity Area*, 2 J. Corp. L. 405 (1977); see also W. CARY & M. EISENBERG, supra note 36, at 596 (discussing combination of the "line of business" and the "fairness" tests in *Miller*).
also allow the defense of corporate incapacity in three contexts: (1) ultra vires,\textsuperscript{130} (2) rejection by the corporation,\textsuperscript{131} and (3) inability to finance the opportunity.\textsuperscript{132} These approaches to determining when and to whom a business opportunity belongs, however, have been criticized as ambiguous and as allowing excessive judicial discretion.\textsuperscript{133} Some commentators indicate that these case law approaches are suitable only for closely held corporations.

Professors Brudney and Clark insist that the courts should take different approaches when examining the corporate opportunity cases of closely held corporations and publicly held corporations because of differences in the investors' abilities to select and monitor corporate managers, in the investors' abilities to contract with one another, in the managers' duties and compensation agreements, and in the size of corporate opportunities.\textsuperscript{134} Brudney and Clark conclude that the current case law approach is suitable only for closely held corporations.\textsuperscript{135} They recommend providing a larger role for shareholder consent in the taking of corporate opportunities and shifting the burden of proof to the challenged fiduciary who fails to obtain consent in the case of closely held corporations.\textsuperscript{136}

If a joint venture reasonably expects to acquire a business opportunity that a parent company will be unable to acquire, or if a business

\textsuperscript{130} Diedrick v. Helm, 217 Minn. 483, 495-96, 14 N.W.2d 913, 920 (1944).

\textsuperscript{131} Abbott Redmont Thinline Corp. v. Redmont, 475 F.2d 85, 89 (2d Cir. 1973); Diedrick, 217 Minn. at 495, 14 N.W.2d at 919 (1944). See generally Note, When Opportunity Knocks: An Analysis of the Brudney & Clark and ALI Principles of Corporate Governance Proposals for Deciding Corporate Opportunity Claims, 28 CORP. PRAC. COMMENTATOR 507 (1987) (a critique of both traditional and recent approaches to assessing corporate opportunity claims).

\textsuperscript{132} Miller, 301 Minn. at 225, 222 N.W.2d at 81 (1974); Schildberg Rock Prod. Co. v. Brooks, 258 Iowa 759, 769, 140 N.W.2d 132, 138 (1966); see also Klinicki v. Lundgren, 298 Or. 662, 667-82, 695 P.2d 906, 910-21 (1985) (recognizing availability of the defense). Contra Irving Trust Co. v. Deutsch, 73 F.2d 121, 124 (2d Cir. 1934) (solvent corporation's directors cannot take over corporate contract for their own profit because of corporation's financial inability to perform contract), cert. denied, 294 U.S. 708 (1935); Note, supra note 131, at 515-17 (discussing the role of financial and legal inability to take advantage of corporate opportunity).

\textsuperscript{133} Brudney & Clark, supra note 34, at 1001. One commentator has pointed out that courts impose liability on management only where there are elements of patent unfairness. Walker, supra note 130, at 627.

\textsuperscript{134} Brudney & Clark, supra note 34, at 1004.

\textsuperscript{135} Id. at 1061; see also R. CLARK, supra note 77, §§ 7.3, 7.9.

\textsuperscript{136} Brudney & Clark, supra note 34, at 1016. For full-time executives of publicly held corporations, Brudney and Clark recommend a rule forbidding the taking of any active business opportunity. For outside directors (part-time executives) of publicly held corporations, Brudney & Clark recommend a rule forbidding only the taking of opportunities in which the corporation has independent knowledge. Id. at 1061.
opportunity is within a joint venture's line of business and not within a parent company's, the opportunity clearly belongs to the joint venture.\footnote{137} A problem arises regarding the allotment of business opportunities between a joint venture and a parent company in which both have an interest or expectancy, or which are within a joint venture's and a parent company's line of business.\footnote{138}

The same difficult problem of allotting business opportunities occurs in a parent-subsidiary relationship. Brudney and Clark suggest three approaches to the allocation of a business opportunity that is within the lines of business of both a parent company and its subsidiary: (1) the business judgment rule, (2) the highest value rule, and (3) the sharing formula.\footnote{139} They recommend that “all business opportunities be pre-

\footnote{137. The assumption that the corporation in whose line of business the opportunity lies will derive a greater risk-adjusted return from it than other corporations is not always true. Shreiber & Yoran, Allocation of Corporate Opportunities by Management, 23 WAYNE L. REV. 1355, 1369 (1977). A business opportunity that is within a joint venture's line of business and not within a parent company's, however, should belong to the joint venture because the expectation of the other parent companies should be protected.}

\footnote{138. In the case of general interlocking directors and officers who hold positions in two or more corporations which have no controlling relationship among them, they must disclose the opportunity to both the corporations. See Note, Corporate Opportunity, 74 HARV. L. REV. 765, 771 (1961). In joint ventures, however, such a directive does not make sense because even if the information is disclosed to both the parent and the joint venture, the parent may not allow the joint venture to compete for the opportunity on an equal basis.}

\footnote{139. Brudney & Clark, supra note 34, at 1050-54. Under the business judgment rule, the decision as to which company should take a certain business opportunity is made by the directors or officers who first become aware of the opportunity. Id. at 1054. The highest value rule allots a business opportunity to the company which can make the largest profit from the opportunity. Id. at 1050; Shreiber & Yoran, supra note 137, at 1359. Under the sharing formula, the parent and subsidiary develop a business opportunity together in a form of a joint venture. Brudney & Clark, supra note 34, at 1051, 1052; Brudney & Chirelstein, Fair Shares in Corporate Mergers and Takeovers, 88 HARV. L. REV. 297, 325-26 (1974). None of the Brudney and Clark approaches, taken alone, addresses all of the various corporate opportunity problems. Brudney and Clark suggest distinguishing three kinds of opportunities which are within the lines of business of both a parent and a subsidiary: (1) differentially valuable opportunities (“[Opportunities that] may \ldots result in a greater increase in [the] risk-adjusted return if placed in one corporation rather than the other.”); (2) normal opportunities (“[Opportunities that] may be equally valuable with either corporation but [that] may offer only a normal expected return.”); and (3) exceptional opportunities (“[Opportunities that] may be equally valuable [to either corporation and [that] may offer an uncommonly superior risk-adjusted return.”). Brudney & Clark, supra note 34, at 1049. This classification of opportunities is not only applicable to general parent-subsidiary relationships but also to joint ventures because the necessity of allotting business opportunities between two companies is the same. Brudney and Clark also suggest in the context of a general parent-subsidiary relationship that, “the highest value rule should apply to differentially valuable opportunities; the business judgment rule should apply to normal opportunities but could be overcome in cases where a grossly unfair pattern of allocation is shown; and a sharing formula \ldots seems appropriate for exceptional opportunities.” Brudney and Clark admit, however, that the difficulty of classifying opportunities according to their schemes preclude any practical application of the above formula. Id. at 1054;
sumed to belong to the subsidiary except when the parent company clearly proves that the opportunity will have a substantially higher value for the parent than for the subsidiary."\textsuperscript{140} Brudney and Clark apply this rule of a "subsidiary's presumed entitlement" after considering three factors: whether meaningful consent from the public investors in a subsidiary is available to the parent company;\textsuperscript{141} whether the managers who have de facto control of the decisions of both parent company and subsidiary have "a greater personal interest in the financial well-being of the parent company";\textsuperscript{142} and whether shareholders of the subsidiary are in vulnerable positions.\textsuperscript{143}

Brudney and Clark's rule of a "subsidiary's presumed entitlement" cannot, however, be applied to a joint venture because the background of a joint venture is different from that of a parent-subsidiary relationship. First, in a joint venture, consent among parent companies is very useful.\textsuperscript{144} The best way to resolve a corporate opportunity conflict of interest in a joint venture is to make express agreements prior to creating a joint venture. Obtaining contemporaneous consent from other parent companies is also useful to a parent company that intends to obtain a business opportunity in which a joint venture is also interested.\textsuperscript{145}

Second, minority shareholders (minority parent companies) of a joint venture are not as vulnerable as minority shareholders in a subsidiary. In a joint venture, even a minority parent company has considerable bargaining leverage.\textsuperscript{146} Therefore, protection of the minority parent companies of a joint venture is less important than protection of minority shareholders in a subsidiary.

\textit{see also} R. CLARK, supra note 77, § 7.8.1, at 257 (arguing that adoption of the classification scheme would be impractical).

140. Brudney \& Clark, supra note 34, at 1061.

141. \textit{Id.} at 1046.

142. \textit{Id.} at 1047.

143. \textit{Id.} at 1061. Some commentators argue that in parent-subsidiary relationships, business opportunities should be allocated "to maximize the combined net present values of all opportunities." Shreiber \& Yoran, supra note 137, at 1359. This argument, however, cannot be applied directly to situations of a joint venture because of the distinct interest of the joint venture entity vis-à-vis the parent companies.

144. Because there are only a few shareholders in a joint venture, it is not difficult to obtain the shareholders' agreement. Additionally, because even a minority shareholder in a joint venture has bargaining leverage and monitoring ability, it is possible to obtain meaningful consent from the shareholders.

145. Ratification by shareholders after full disclosure may estop the shareholders who joined in the ratification from bringing a later complaint against the interested parent company. Gottlieb v. McKee, 34 Del. Ch. 537, 545, 107 A.2d 240, 244 (1954). Full disclosure, however, would not excuse the usurpation of the corporate opportunity. Schreiber v. Bryan, 396 A.2d 512, 518 (Del. Ch. 1978).

146. \textit{See supra} text accompanying note 33.
Finally, the fact that managers (interlocking directors or officers) have greater personal interest in the financial well-being of the parent company\(^{147}\) is also true in a joint venture context.\(^{148}\) Therefore, there is an assumption in a joint venture that interlocking directors or officers will allot a common business opportunity to a parent company rather than to a joint venture. Because a joint venture is created to maximize the interests of the parent companies, however, the heavy burden of proof imposed on the parent company in a parent-subsidiary relationship to show that an opportunity will have a substantially higher value for the parent\(^{149}\) should not be imposed on a joint venture.

In the context of corporate opportunity conflicts between a dominating shareholder and a corporation, usually a parent and a subsidiary, the ALI also applies a two-step test:\(^{150}\) first, an examination of how the business opportunity arose, and, second, an analysis which is similar to the expectancy test.\(^{151}\) If a business opportunity arose as the parent's opportunity, that is, if it was developed or received by a parent, it is not the subsidiary's corporate opportunity.\(^{152}\) If it was “neither developed nor received by” a parent and it is “held out to shareholders of the [subsidiary] as being within the scope of the business in which the [subsidiary] is presently engaged or may be reasonably expected to engage,”\(^{153}\) it is the subsidiary's corporate opportunity. The parent can obtain the subsidiary's corporate opportunity only when to do so is fair to the subsidiary,\(^{154}\) or is authorized or ratified by disinterested shareholders following disclosure, and the shareholders' action is not equivalent to a waste of corporate assets.\(^{155}\) The ALI observes:

Section 5.12(b) defines a corporate opportunity more narrowly than

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147. Brudney & Clark, supra note 34, at 1047.
148. If there is no tie between the companies in which interlocking directors or officers have their positions, they will be free either to offer to any of their companies any business opportunities that come to them personally, or to retain the opportunities for themselves. See Johnston v. Greene, 35 Del. Ch. 479, 489, 121 A.2d 919, 924 (1956).
149. Brudney & Clark, supra note 34, at 1055, 1061.
150. ALI Corporate Governance, supra note 53, § 5.12.
152. ALI Corporate Governance, supra note 56, § 5.12(b), comment d (2)(b).
154. ALI Corporate Governance, supra note 53, § 5.12(a)(1).
155. “The taking of the opportunity is authorized or ratified by disinterested shareholders [§ 1.11], following disclosure concerning the conflict of interest [§ 1.09(a)] and the facts concerning the corporate opportunity [§ 1.09(b)], and the shareholders' action is not equivalent to a waste of corporate assets [§ 1.34].” ALI Corporate Governance, supra note 53, § 5.12(a)(2).
5.05(b), in order to balance the right of the dominating shareholder to engage in business in competition with the corporation against the need to assure that the dominating shareholder does not seize for himself opportunities that could fairly be said to belong to the corporation.\textsuperscript{156}

In order to allot a business opportunity in which both the joint venture and a parent company are interested, and which is in the line of business of both companies,\textsuperscript{157} two factors should be considered: how the business opportunity arose, and the relative value of the business opportunity to the joint venture and the interested parent company.

There are three basic ways in which business opportunities become known to either a parent company or a joint venture.\textsuperscript{158} First, a business opportunity may be manifested as the joint venture's opportunity. For example, a seller clearly may offer a business asset to a director or officer of the joint venture, the joint venture's directors or officers may discover the opportunity through the use of the joint venture's information or properties, or the joint venture may discover it opportunity through extensive research of potential new product or geographic markets.\textsuperscript{159}

Second, a business opportunity may be manifested as the interested parent company's opportunity. For example, a seller may offer a business asset to one of the directors or officers of the interested parent company, one of the directors or officers of the interested parent company may come upon an opportunity to obtain a business asset through the use of the interested parent company's information or properties, or the interested parent company may learn of a business opportunity through its own research of new markets.

Third, a business opportunity may be manifested ambiguously to the joint venture or the parent company. For example, a seller may offer a business opportunity to an interlocking director or officer without specifying to which enterprise the offer is made, an interlocking director or officer may notice the opportunity to obtain a business asset as an individual,\textsuperscript{160} or a noninterested parent company may propose to enter a new market in which neither the joint venture nor the interested parent company has invested.

Business opportunities also can be divided into three large categories

\begin{itemize}
\item \textsuperscript{156} Id. § 5.12 comment at 186.
\item \textsuperscript{157} See supra text accompanying notes 138-43.
\item \textsuperscript{158} ALI CORPORATE GOVERNANCE, supra note 53, § 5.12(b); see also infra Table 2.
\item \textsuperscript{159} See Comment, Corporations: The Doctrine of Corporate Opportunities, 31 CALIF. L. REV. 188, 189 (1943).
\item \textsuperscript{160} See Johnston v. Greene, 35 Del. Ch. 479, 488, 121 A.2d 919, 924 (1956); see also R. CLARK, supra note 77, § 7.2.5 (some courts distinguish between information obtained in individual and official capacities).
\end{itemize}
according to their relative values to the joint venture and the interested parent company.\textsuperscript{161} The first type of business opportunity is that which may yield a greater economic return to the joint venture or have higher value to the joint venture than to the interested parent company. The second type of business opportunity is one in which it is not clear whether the joint venture or the interested parent would reap a higher return from it.\textsuperscript{162} The third type of business opportunity is one which will yield a greater economic return to the interested parent company than to the joint venture.\textsuperscript{163}

The characteristics of business opportunities can be illustrated and analyzed using a matrix on which the manner in which the business opportunity was manifested appears on the horizontal scale and the relative value of the business opportunity appears on the vertical scale. In the following discussion, this matrix will be used to illustrate and compare the theoretical approaches to corporate opportunities in the context of the parent-subsidiary relationship of Brudney and Clark, the ALI and my reinterpretation of the two in the context of a joint venture.

Brudney and Clark only consider the relative value of the business opportunity (the vertical scale) and ignore the factor of the manner of the business opportunity's manifestation (the horizontal scale). They only reserve for the parent those business opportunities that have substantially higher value to the parent than to the subsidiary and allocate all other business opportunities to the subsidiary.\textsuperscript{164} In their analysis, represented in Table 1, it is irrelevant whether the opportunities were developed or received by the subsidiary or by the parent.

The ALI framework considers only the factor of how the business opportunity was manifested (the horizontal scale) and ignores the relative value of the business opportunity (the vertical scale). The ALI, instead of the relative value of the business opportunity, considers whether the shareholders of the subsidiary expect the business opportunity to be within the scope of the subsidiary's business.\textsuperscript{165} This analysis is represented in the matrix shown in Table 2.

\textsuperscript{161} Brudney & Clark, \textit{supra} note 34, at 1055, 1061; \textit{see also infra} Table 1.

\textsuperscript{162} This type includes what Brudney and Clark refer to as "normal opportunities" and "exceptional opportunities." Brudney & Clark, \textit{supra} note 34, at 1049.

\textsuperscript{163} For example, a business opportunity to obtain uranium ore may yield a greater economic return to a parent company than to a mining joint venture because the ore is "wet ore," which presents mining difficulties and makes the enterprise hazardous and speculative. In this case, only the parent company, which has the skill, experience, and financial capability, should undertake the risk. Homestake Mining Co. v. Mid-Continental Exploration Co., 282 F.2d 787, 799 (10th Cir. 1960).

\textsuperscript{164} Brudney & Clark, \textit{supra} note 34, at 1055, 1061.

\textsuperscript{165} \textit{ALI CORPORATE GOVERNANCE, supra} note 56, § 5.12(b).
Table 1

<table>
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<th>Relative Value</th>
<th>Developed or Received by the Subsidiary</th>
<th>Ambiguous</th>
<th>Developed or Received by the Parent</th>
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<td>S</td>
<td>S</td>
</tr>
<tr>
<td>Ambiguous</td>
<td>S</td>
<td>S</td>
<td>S</td>
</tr>
<tr>
<td>Higher Value to the Parent</td>
<td>P</td>
<td>P</td>
<td>P</td>
</tr>
</tbody>
</table>

(S = Subsidiary's Corporate Opportunity)  
(P = Parent's Corporate Opportunity)

Table 2

<table>
<thead>
<tr>
<th>Shareholder’s Expectations</th>
<th>Developed or Received by the Subsidiary</th>
<th>Ambiguous</th>
<th>Developed or Received by the Parent</th>
</tr>
</thead>
<tbody>
<tr>
<td>W/in the Scope of Subsidiary's Business</td>
<td>S</td>
<td>S</td>
<td>P</td>
</tr>
<tr>
<td>Ambiguous</td>
<td>P</td>
<td>P</td>
<td>P</td>
</tr>
<tr>
<td>Not w/in Scope of Subsidiary’s Business</td>
<td>P</td>
<td>P</td>
<td>P</td>
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</tbody>
</table>

Suppose, however, that the analysis focuses only on those cases in which the business opportunity is within the scope of the business of both the subsidiary (or a joint venture) and the interested parent company. Table 2 can then be rewritten as shown below in Table 3.

The factor of how a business opportunity was manifested is a type of fairness standard. That standard is premised on the notion that all the parent companies involved in the joint venture ought to be treated equally. If an interested parent company obtains a business opportunity that the joint venture originally developed or received, the interested parent company will receive one hundred percent of the profits to the exclusion of the other parent companies involved in the joint venture.

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166. "Any rule for allocating corporate opportunities can be evaluated according to three criteria: (1) economic efficiency, (2) fairness to shareholders and (3) ease of enforcement." Shreiber & Yoran, supra note 141, at 1364.

167. For a corporate opportunity case outside the joint venture context in which the court found that a corporate opportunity had been appropriated, see Klinicki v. Lundgren, 298 Or. 662, 685, 695 P.2d 906, 920 (1985).
Table 3

<table>
<thead>
<tr>
<th>Relative Value</th>
<th>Developed or Received by the Subsidiary</th>
<th>Manifestation</th>
<th>Developed or Received by the Parent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Higher Value to the Subsidiary</td>
<td>S</td>
<td>S</td>
<td>P</td>
</tr>
<tr>
<td>Ambiguous</td>
<td>S</td>
<td>S</td>
<td>P</td>
</tr>
<tr>
<td>Higher Value to the Parent</td>
<td>S</td>
<td>S</td>
<td>P</td>
</tr>
</tbody>
</table>

The result is inequitable in that the non-interested parent companies are not reaping economic return in proportion to the equity they have invested in the joint venture. Therefore, this fairness standard should be considered an important factor in determining whether an interested parent company violates a fiduciary duty by obtaining a business opportunity.

The relative value of the business opportunity is an efficiency standard. If a business opportunity yields a greater economic return to the joint venture than to the interested parent company, it may be more efficient for the interested parent company to have the joint venture obtain the business opportunity than to obtain it itself. This efficiency standard is a very influential factor from the business point of view, but should be only of secondary importance in determining whether an interested parent company violates a fiduciary duty by obtaining a business opportunity.

Because it uses the fairness standard, the ALI framework is more appropriate than Brudney and Clark's framework for determining the legal liability of the parent that obtains a business opportunity in which the subsidiary is also interested. The ALI framework should be modified, however, before it can be applied to joint ventures.

As a general rule, a parent company can freely obtain a business opportunity in which a joint venture is also interested. As exceptions to the general rule, there are some kinds of business opportunities in which an interested parent company must give the joint venture a right of first refusal because of the parent company's fiduciary duty to the other parent companies. In this respect, the corporate opportunities of a joint venture should be more restricted than those of a subsidiary.

There are three reasons for the general rule. First, a joint venture is an entity which from its inception was created specifically to maximize
the interests of the parent companies. The purpose of the joint venture is
to serve as a tool of the parent companies. In contrast, subsidiaries that
are not wholly owned by the parent are not always created to maximize
the interests of the parent company.\textsuperscript{168} Second, even a minority parent
company in a joint venture is usually a sophisticated business entity, hav-
ing less need for protection than a minority shareholder in a subsidiary.
Third, each parent company is usually allowed by pre-agreement a veto
over the joint venture's chance to obtain a business opportunity. For this
reason, the corporate opportunities of a joint venture are intrinsically re-
stricted. The issue is whether there is some legal restriction on the veto
powers of parent companies when there are conflicts of interest.

The framework for distributing business opportunities that are in
the line of business of both a joint venture and an interested parent com-
pany is illustrated in Table 4.

<table>
<thead>
<tr>
<th>Relative Value</th>
<th>Developed or Received by the Joint Venture</th>
<th>Ambiguous</th>
<th>Developed or Received by the Interested Parent Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>Higher Value to the Joint Venture</td>
<td>Joint Venture (1)</td>
<td>Joint Venture (4)</td>
<td>P (7)</td>
</tr>
<tr>
<td></td>
<td>Ambiguous (2)</td>
<td>P (5)</td>
<td>P</td>
</tr>
<tr>
<td>Higher Value to the Interested</td>
<td>P (3)</td>
<td>P (6)</td>
<td>P</td>
</tr>
<tr>
<td>Parent Company</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(Joint Venture = Joint Venture's Corporate Opportunity)
(P = Interested Parent Company's Corporate Opportunity)

The factor of how the business opportunity appeared should be the pri-
mary consideration. If the joint venture developed or received the busi-
ness opportunity, the joint venture gets a right of first refusal\textsuperscript{169} (see
boxes (1) and (2) of Table 4). The only exception is when the opportu-
nity will yield a higher return to the interested parent (see box (3), Table
4).

\textsuperscript{168} Many subsidiaries are not originally subsidiaries but were formerly independent com-
panies. Therefore, there are independent interests of minority shareholders remaining in these
types of subsidiaries.

\textsuperscript{169} Sinclair Oil Corp. v. Levien, 280 A.2d 717, 722 (Del. 1971); Shreiber & Yoran, supra
note 141, at 1372.
In all other cases, the interested parent company may take the business opportunity without offering it to the joint venture (see boxes (5)-(9), Table 4), unless the business opportunity will yield a higher return to the joint venture (see box (4), Table 4). On this point, the joint venture (in fact, the complaining parent company) has the burden of proving that the joint venture developed or received the corporate opportunity.

The relative value of the business opportunity should be a supplementary consideration. First, even though the joint venture developed or received a business opportunity, if the business opportunity has a substantially higher value to the interested parent company than to the joint venture, the interested parent should be allowed to obtain the opportunity (see box (3), Table 4). On this point, the interested parent company has the burden of proof. Second, even though a business opportunity was not clearly developed nor received by the joint venture, if it clearly has substantially higher value to the joint venture, the opportunity must be given to the joint venture (see box (4), Table 4). On these points, the joint venture (in fact, the complaining parent company) has the burden of proof.

The interested parent company can clearly obtain the opportunities in boxes (5), (6), (8), and (9) of Table 4 without yielding a right of first refusal to the joint venture because, under the general rule, these opportunities do not involve factors through which the joint venture may assert a notion of prerogative or joint venture right. In these situations, the joint venture is favored neither by the factor of how the opportunity was manifested nor the factor of relative value.

The joint venture should be able to obtain opportunities in boxes (1) and (2) under a right of first refusal as exceptions to the general rule. If the interested parent company obtains these opportunities, it denies the non-interested parent companies an opportunity to economic return in proportion to the equity that they have invested in the joint venture.

The type of business that falls into the category of box (3) presents a difficult case because it has been developed or received by the joint venture, but will probably yield higher value to the interested parent company. For example, a joint venture researches a new market which turns out to be more profitable for an interested parent company than for the joint venture. In another case, a joint venture may be offered a chance to obtain a plant which may yield much higher risk-adjusted return to an interested parent company. If the interested parent company obtains this kind of opportunity, it may profit to the detriment of the other parent companies. It is not necessarily unfair, however, for the interested parent company to veto the joint venture's chance to obtain an opportunity that
JOINT VENTURE clearly has higher value for the interested parent company. Moreover, in this kind of opportunity, the detriment of non-interested parent companies, if any, will not be significant. Therefore, the interested parent company can obtain this kind of opportunity without violating a fiduciary duty.

Business opportunities represented in box (7) are another difficult case. Box (7) opportunities are developed or received by the parent but will probably yield higher economic return to the joint venture. From the business point of view, it may be more efficient for the interested parent company to have the joint venture obtain the opportunities. From the legal point of view, the interested parent company has no fiduciary duty to do so. The joint venture is an entity which was created specifically to maximize the interest of the parent companies. The interested parent company cannot be expected to yield a right of first refusal to the joint venture of the business opportunity which the interested parent company developed or received.\textsuperscript{170}

The most difficult cases are opportunities represented by box (4). In box (4) cases, it is unclear whether the joint venture or the parent received the opportunity, but clear that the economic return will be higher for the joint venture. For example, a non-interested parent company proposes that the joint venture enter into a new market which may yield a much higher risk-adjusted return to the joint venture than to the interested parent company, or an interlocking director becomes aware of the chance to obtain a plant which may yield a higher risk-adjusted return to the joint venture than to the interested parent company.

The loss to the non-interested parent companies when the interested parent company obtains the opportunities are much higher than the loss to the interested parent company when the joint venture obtains the opportunities. The loss to the interested parent company may not be significant relative to its investment when it has the joint venture obtain the opportunities. Moreover, the interested parent company may reap a higher return when it has the joint venture obtain the opportunities than when it obtains the opportunities itself, because it costs less to have the joint venture take advantage of the opportunity. In contrast, the loss of the non-interested parent companies by losing hypothetical profit when the interested parent company takes the opportunities may be significant. Therefore, the interested parent company has a fiduciary duty to allow the joint venture to obtain those opportunities. From the practical point

\textsuperscript{170} See Burg v. Horn, 380 F.2d 897, 900 (2d Cir. 1967) (applying interest or expectancy test).
of view, this duty will not prevent the interested parent company from obtaining business opportunities in many cases because the non-interested parent company must meet a tough burden of proof.

The preceding discussion assumed there was no express agreement between the parents and the joint venture to narrow and define the scope of the joint venture's corporate opportunities. Such an agreement, however, may avoid the legal problem of fiduciary duties involving corporate opportunity conflicts of interest. Prior to creating a joint venture, parent companies of the joint venture may waive the right to sue for damages suffered in the event that the joint venture is deprived of its corporate opportunity by another parent company. Parent companies of the joint venture are usually sophisticated business entities and even minority parent companies have negotiating leverage. Moreover, the parent companies are usually original shareholders of the joint venture. Therefore, there is no legal obstacle preventing parent companies from abandoning a limited right to sue prior to creating the joint venture.171

An express agreement, however, cannot solve all problems. In addition to the antitrust problem discussed previously,172 problems may arise when other parent companies are dissatisfied and, consequently, do not cooperate in operating the joint venture, sue for liquidation, or force a buy-out.

b. Buy-Outs

When other parent companies are dissatisfied with a particular parent company, which obtained a corporate opportunity in which the joint venture was also interested, a dispute among parent companies may occur. The other parent companies may request dissolution of the joint venture, or that the parent company which obtained the corporate opportunity buy out the shares of the dissatisfied parents.173 If the parent

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171. The ALI's model:

is intended to permit a dominating shareholder to enter into shareholder agreements that permit him to take specifically defined corporate opportunities for himself, provided the agreements are entered into by the other shareholders at the time when they become shareholders. Even in the absence of such an agreement, the dominating shareholder may insulate the taking of the opportunity from a review other than waste if rejection of the opportunity is authorized or ratified by disinterested shareholders under § 5.12(a)(2).

172. See supra notes 121-23 and accompanying text.

173. Usually, joint venture agreements prohibit parent companies from selling shares without the consent of the other parents. A right of first refusal clause and a buy-sell agreement clause are ordinarily used in joint ventures. UNIDO, supra note 24, at ch. 8 § 1(2)-(4). For a related discussion on buy-out arrangements, see F. O'NEAL, supra note 16, § 8.03.
companies agree in advance to liquidation or buy-out proposals, the object of creating the joint venture fails because one of the parent companies may be forced to incur unexpected expenses. On the other hand, if the parent companies do not agree to liquidation or buy-out proposals in a joint venture agreement, or if the parent companies cannot resolve a dispute with these agreements, the dispute can be resolved through conciliation, arbitration or court proceedings.\textsuperscript{174}

In a closely held corporation, many states\textsuperscript{175} allow a dissatisfied minority shareholder to obtain relief through either dissolution or buy-out only when there is a deadlock and when the interests of the minority shareholder have been oppressed\textsuperscript{176} by a controlling shareholder. Some states also allow similar relief for a dissatisfied minority shareholder\textsuperscript{177} when there is reasonable necessity for the protection of the rights or interests of the complaining shareholder.\textsuperscript{178} The courts will determine whether the acquisition of the corporate opportunity was an act of "oppression" or whether it was an act of "reasonable necessity for the protection" of the parent company. Even if the act of the parent company does not deprive the joint venture of its corporate opportunity and impose liability for damages on the parent company, it might be a factor in a suit for dissolution or buy-out. In determining whether dissolution or buy-out should be allowed, equity courts should balance the interests of parent companies in a joint venture. It is not necessary that the deprivation of a corporate opportunity which violates the fiduciary duty of the parent company be the same as the deprivation of the corporate opportunity which becomes a reason for dissolution or buy-out.\textsuperscript{179}

\textsuperscript{174} UNIDO, \textit{supra} note 24, at ch. 9.

\textsuperscript{175} See, e.g., FLA. STAT. ANN. § 607.274 (West Supp. 1987) (deadlock or waste only); ILL. ANN. STAT. ch. 32, para. 12.50(b) (Smith-Hurd Supp. 1987); MASS. GEN. LAWS ANN. ch. 156B, § 99 (West 1970) (deadlock only); MICH. COMP. LAWS ANN. §§ 450.1823, .1825 (West Supp. 1987); N.Y. BUS. CORP. LAW § 1104, 1104(a) (McKinney 1986) (Holdes of at least one-half of all shares may petition for dissolution in case of deadlock. In privately held corporations, shareholders with at least 20% of outstanding shares may petition for dissolution on the grounds of the illegal, fraudulent or oppressive actions of controlling directors toward the shareholders.); OHIO REV. CODE ANN. § 1701.91 (Page Supp. 1986) (dissolution on grounds of deadlock or in cases where dissolution is beneficial to the shareholders); PA. STAT. ANN. tit. 15, § 2107 (Purdon 1967) (any shareholder may petition for dissolution under certain circumstances).

\textsuperscript{176} Oppression is "wrongful conduct by those in control." Hillman, \textit{supra} note 18, at 39.

\textsuperscript{177} See, e.g., CAL. CORP. CODE § 1800(b)(5) (West 1977) (any corporation with 35 or fewer shareholders); N.C. GEN. STAT. § 55-125(a)(4) (1982).

\textsuperscript{178} Hillman, \textit{supra} note 18, at 55-60. In partnerships, each partner has a right to dissolve the partnership. UNIF. PARTNERSHIP ACT § 31 (1969).

\textsuperscript{179} When a parent company obtains a business opportunity in which a joint venture is also interested, the action may not violate fiduciary duty but may be a reason for dissolution or buy-out. That is, it may cause deadlock and oppress the minority parent companies.
After an equity court determines that a buy-out is appropriate, the court must determine the value of the shares of a complaining parent company. In valuing these shares, the court may consider the effect the usurping parent's act had on the value of the joint venture shares. If the parent company deprived the joint venture of an interest that rightfully belonged to the joint venture and consequently lessened the interest of the other parent companies in the joint venture, this decrease of interest should be added to the value of the shares of the complaining parent company.

c. Non-Cooperation

The interested parent company has a tactical problem regarding the degree to which it should insist upon its own interests and the degree to which it should cooperate with other parent companies to maximize their total interests. When a parent company obtains access to a corporate opportunity in which the joint venture is also interested, other parent companies may express their dissatisfaction by not cooperating in the operation of the joint venture even if they decide not to take legal action. If a parent company cannot obtain the cooperation of its partners (other parent companies), the objectives behind creating a joint venture cannot be achieved. A parent company may sacrifice its long-term interest in a joint venture if it obtains a corporate opportunity that offers only short-term benefit. Consequently, a parent company's best strategy in the context of a corporate opportunity conflict of interests is to maximize its own long-term interests. The standards embodied in Table 4 may help a parent company determine whether a particular corporate opportunity would maximize its long-term interests.

(4) Special Problems of Dividends and Increasing Capital

Conflicts of interest between a joint venture and a parent company may also occur in formulating dividend policy. Basically, a joint venture has an interest in limiting dividends to facilitate future expansion, and a parent company has a general interest in receiving higher dividends. Moreover, the interests of parent companies in dividend policy may also differ. Some parent companies may want to limit the dividends of a joint venture to create a long-term profit while other parent companies may want to recoup their investment as soon as possible. These differing views of joint venture dividend policy depend upon many factors, includ-

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ing the joint venture’s future business prospects, the financial condition of the parent company, the existence of specific corporate opportunities for the joint venture or the parent company, and international politics.  

In most disputes regarding the payment of dividends, an issue arises as to whether low dividends or a restraint of dividends can be blamed for oppressing minority shareholders. In both a joint venture and a parent-subsidiary relationship, however, the payment of excessive dividends may also be an issue. The Delaware Supreme Court established the standard and burden of proof a parent company must meet when a shareholder challenges the excessive payment of dividends by a subsidiary in *Sinclair Oil Corporation v. Levien*. In *Sinclair*, a minority shareholder of subsidiary brought a derivative action against the parent company to account for damage sustained by the subsidiary on grounds that the parent company caused the subsidiary to pay excessive dividends, which precluded industrial development of the subsidiary. The Court of Chancery held that the conduct of the parent company must meet the standard of intrinsic fairness because of its fiduciary duty and its control over the subsidiary. The Court of Chancery also shifted the burden of proof to the parent company and held that the parent company did not sustain its burden of proving that these dividends were intrinsically fair to the minority shareholder of the subsidiary.

The Supreme Court of Delaware reversed and held that the business judgment standard should have been applied because the intrinsic fairness standard should be applied only when a fiduciary duty is accompanied by self-dealing. The court observed that the parent company received nothing from the subsidiary to the exclusion of its minority shareholders because the minority shareholders received a proportionate share of the dividends and, as such, the payments of dividends were not self-dealing. The court also noted that the subsidiary could point to no opportunity that came to the subsidiary and ruled that there was no self-dealing because the parent company did not usurp business opportunities belonging to the subsidiary.

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181. For example, an international joint venture in a developing country may create uncertainty for a foreign parent company regarding recoupment of investments.
182. F. O'NEAL, supra note 16, §§ 3.04, 3.05.
183. 280 A.2d 717 (Del. 1971).
184. The subsidiary's dividends exceeded the subsidiary's earnings but the payments were made in compliance with a Delaware statute authorizing payment of dividends out of surplus or net profit. *Sinclair Oil Corp. v. Levin*, 280 A.2d at 721.
185. *Id.*
186. *Id.* at 721-22.
187. *Id.* at 722.
In typical corporations, particularly closely held corporations, majority shareholders or management seek long-term profit, while minority shareholders seek short-term profit. There is no conflict of interest between the directors or officers, who determine dividend policy, and the corporation because the best interest of the corporation is long-term profit. In a joint venture or parent-subsidiary relationship such as in Sinclair, however, excessive dividends occasionally may be an issue. In a joint venture or parent subsidiary relationship, the majority parent company may seek short-term profit and minority shareholders or minority parent companies may seek long-term profit. Although there may be a proportional distribution of profit among shareholders and the parent company receives nothing from the joint venture or the subsidiary to the exclusion of its minority shareholders, there may be a conflict of interest between the majority parent company and the joint venture or subsidiary. Therefore, the business judgment rule cannot be applied to the excessive dividends disputes involving joint ventures or typical parent-subsidiary relations. The better rule is to apply the business judgment rule only when there is no conflict of interest between management and the corporation.\textsuperscript{188}

It is difficult, however, to determine when directors or a majority parent company will be liable for violation of their fiduciary duties for making the joint venture pay high dividends and thereby depriving a joint venture of corporate opportunities. First, it is difficult to correlate the payment of excessive dividends with the usurpation of a corporate opportunity. The fiduciary duty of directors or a majority parent company may be an issue only when a joint venture and a majority parent company compete for a specific corporate opportunity at the time of the payment of dividends. Second, courts are very reluctant to overrule a dividend policy of management or majority shareholders.\textsuperscript{189}

Creating agreements prior to forming a joint venture is advisable for adjusting and avoiding a conflict of interest regarding the payment of

\textsuperscript{188} "If in the course of management, directors arrive at a decision, . . . as the result of their independent discretion and judgment, and uninfluenced by any consideration other than what they honestly believe to be the best interests of the corporation, a court will not interfere with internal management." H. Henn & J. Alexander, supra note 6, § 242, at 661. Therefore, the judgment which is influenced by the consideration for the interest of a parent company cannot be applied by the business judgment rule. Cary, Federalism and Corporate Law: Reflections Upon Delaware, 83 Yale L.J. 663, 680-81 (1974); Shreiber & Yoran, supra note 141, at 1357.

\textsuperscript{189} F. O'Neal, supra note 16, § 3.05. Even if a dividend policy violates the directors' fiduciary duty, they still raise as a defense the financial inability of a joint venture to obtain a certain opportunity. See supra note 132 and accompanying text.
dividends. For example, parent companies can formally agree to a joint venture's payment of dividends at a certain percent of its net annual profit and to giving every parent company a veto to increase or decrease the dividends. Dividend policies, however, should be open to modification in accordance with the changes of a joint venture's business or business environment. Therefore, a rigid agreement regarding the payment of dividends is not always suitable for operating a joint venture. In this regard, balancing the interests of parent companies is also important. The object of creating a joint venture is to maximize the interests of its parent companies. Therefore, the dividend policy of the joint venture should maximize the long-term profits (accumulated dividends plus liquidation assets) of its parent companies.

A similar issue arises in considering whether to increase the joint venture's capital. Sometimes an increase of a joint venture's capital may be necessary to obtain a certain corporate opportunity. Thus, parent companies should increase a joint venture's capital at appropriate times to maximize the long-term returns from a joint venture. In most joint ventures, however, only parent companies have pre-emptive rights and each parent company may veto an increase of capital. Therefore, each parent company must invest more in order to increase a joint venture's capital. Courts would almost never determine that a parent violated a fiduciary duty to the joint venture by not agreeing to an increase of the joint venture's capital or to additional investments in a joint venture.

(5) Summary

A parent company may violate its fiduciary duty when it obtains a business opportunity that clearly belongs to a joint venture. A business opportunity clearly belongs to a joint venture when the opportunity is in the joint venture's line of business or when the opportunity is not in the parent company's line of business. When the opportunity is in both the joint venture's and the parent company's lines of business, the factors of how the business opportunity arose and the relative value of the business opportunity should be considered in distributing the business opportunity between the joint venture and the parent company.

A good way for avoiding the fiduciary duty problem of the parent company that obtains a business opportunity in which a joint venture is also interested is to create an express agreement between parent companies before creation of the joint venture, thereby restricting the scope of

190. In partnerships, as well, income distribution policy is determined by agreement or by majority decision as an "ordinary matter connected with the partnership business." UNIF. PARTNERSHIP ACT § 18(h) (1914); see A. Bromberg, supra note 9, § 65, at 366.
the joint venture's corporate opportunity. This will not, however, resolve all corporate opportunity conflicts of interest. Even though a parent company does not violate its fiduciary duty by obtaining a business opportunity in which a joint venture is also interested, other parent companies may be dissatisfied and refuse to cooperate in a joint venture or may seek liquidation or buy-out of the joint venture. Interlocking directors or officers should consider balancing the long-term interests of their parent companies, the result of which depends on the bargaining power or the fungibility of each parent company.

C. Alternative Solutions to the Disclosure Conflict of Interests Problems

Interlocking directors or officers necessarily have information about both the joint venture and the parent company. These directors or officers may be in difficult positions as to whether, and to what extent, they should disclose certain information. First, interlocking directors or officers have fiduciary duties to both the joint venture and the parent company, and the interest of the joint venture and the interest of the parent company may conflict if the disclosure of information may be beneficial to the joint venture and harmful to the parent company or vice-versa. Second, disclosure of the information may violate antitrust laws as a collusion.

This Essay examines four contexts involving the disclosure of information about Parent Company A to the joint venture: (1) disclosure of the information is harmful to Parent Company A, but beneficial to the joint venture and Parent Company B; (2) disclosure of the information is harmful to Parent Company A, but beneficial to the joint venture and neutral (neither beneficial nor harmful) to Parent Company B; (3) disclosure of the information is neutral to Parent Company A, beneficial to the joint venture, and neutral to Parent Company B; and (4) disclosure of the information is beneficial to Parent Company A, the joint venture, and Parent Company B.

In the first and second contexts, there are conflicts of interest between Parent Company A and the joint venture. The third presents no conflict of interest and no problem involving disclosure of information. In the fourth context, although there is no conflict of interest, the disclo-

191. If directors or officers of a joint venture lack information about their parent company, it will be the parent company’s obligation to disclose the information. By comparison, in a partnership partners have a duty to "render on demand true and full information of all things affecting the partnership." UNIF. PARTNERSHIP ACT § 20 (1969). Although the Act provides the duty of disclosure only on demand, "voluntary disclosure should be considered as necessary both under the Act and at common law." A. BROMBERG, supra note 9, § 67, at 388; see also Berg v. King-Cola, Inc., 227 Cal. App. 2d 338, 341, 38 Cal. Rptr. 655, 657-58 (1964).
sure of information may violate antitrust rules governing collusion or cartels.

(I) Fiduciary Duty Problem

The fiduciary duty problem of interlocking directors or officers occurs in the first two contexts noted above. If the directors or officers seek to give the interest of the joint venture a higher priority, they should disclose the information. If they seek to give the interest of their parent company a higher priority, they should not disclose the information. To solve this problem of conflict of interest, interlocking directors or officers must balance the interests of the joint venture and their parent using three factors: (1) the characteristics of the information; (2) whether other parent companies are interested in the information; and (3) the degree of disclosure.

a. Characteristics of the Information

There are many kinds of information about a parent company which benefit a joint venture and harm the parent company. One category is information which is critical to the competition between the joint venture and the parent company. This category has significance only when the joint venture and the parent company compete or, in other words, are in a horizontal relationship. Information critical to competition may include information about technology, know-how, design, price, cost, and output of the parent company's product. Disclosure of this information may be harmful to the parent company or to the competition between the joint venture and the parent company. Therefore, interlocking directors or officers should not disclose this category of information. Furthermore, failure to disclose this information will not be a violation of their fiduciary duties to the joint venture, and the disclosure of this information will constitute a violation of their fiduciary duty to the parent company.

A second category of the information includes information that is critical to the transaction between the joint venture and the parent company. This category is particularly significant when the joint venture and the parent company are in a vertical relationship. Critical information includes information about cost or about comparable transactions of a product which the parent company sells to the joint venture. This

192. See Brodley, supra note 11, at 1552-54.
193. A vertical relationship occurs, for example, when a joint venture or a parent company is a supplier to the other.
194. For example, if the parent company sells its product not only to the joint venture but
information is closely related to self-dealing conflicts of interest because it is indispensable for an effective ratification.195 When a parent company transacts with a joint venture, ratification by independent shareholders (non-self-dealing parent companies) or ratification by independent directors (who represent the interests of non-self-dealing parent companies) after a “full disclosure” of material facts is required.196 Interlocking directors or officers who have information that is critical to the transaction between the joint venture and the parent company should disclose this category of information if they will be liable for violating their fiduciary duties to the joint venture if they allow the joint venture to transact with the parent company in unfavorable conditions without disclosing material facts.197 In many cases of self-dealing transactions, the harm to the joint venture due to the lack of disclosure of information is greater than the harm that would result if the parent company disclosed the information. When a material fact is a corporate secret of the parent company and disclosure of this information would be harmful to the parent company, however, interlocking directors or officers need not “fully” disclose the information. In such situations, questions arise regarding the degree of disclosure.198

A third category is information that is related to corporate opportunity conflicts of interest199 has particular significance when the joint venture and the parent company are in a horizontal relationship. It includes information about a plan or an intent of the parent company to obtain a certain business opportunity, and information about how the business opportunity was manifested and potential profitability if the parent company obtains the business opportunity.200 Interlocking directors or of-

also to the nonrelated companies, information about the price or other conditions of the latter transactions will be critical to the former transaction.

195. See supra text accompanying notes 98-99.
196. Id.; Talbot v. James, 259 S.C. 73, 190 S.E.2d 759, 764 (1972).
197. The ALI notes that a common director or senior executive does not need to disclose a conflict of interest or material facts concerning the transaction unless:

(1) the director or senior executive participates personally and substantially in negotiating the transaction for either of the corporations; or (2) the transaction is approved by the board of either corporation, and a director on that board who is also a director or senior executive of the other corporation casts a vote that is necessary to approve the transaction.

ALI Corporate Governance, supra note 53, § 5.07(a). The ALI comments also notes that “if the director or senior executive is aware of material facts concerning the transaction [§ 1.09(b)] which could result in harm to the corporation, failure to disclose such facts may result in a breach of the duty of care. . . .” Id. § 5.07 comment c at 140. This section, however, does not take into account the situation of interlocking directors and officers in a joint venture. 198. See infra text accompanying notes 204-09.
199. See supra notes 113-90 and accompanying text.
200. How the business opportunity was manifested and the relative value of the business
Officers may be liable for violating their fiduciary duties to the joint venture if they allow the parent company to usurp a corporate opportunity that clearly belongs to the joint venture by not disclosing the information. Disclosure of the information about a plan or profitability forecast by the parent company concerning the corporate opportunity, however, may be harmful to the parent company and, in many cases, such information may be a protected corporate secret of the parent company. Interlocking directors or officers may not be able to disclose such information or, at least, are restricted in the degree of disclosure.201

b. Other Parent Companies' Interests in the Information

The second factor for balancing the interests of the joint venture and the parent company is the other parent companies' interests in the information. In joint ventures, the disclosure of the information about a parent company to the joint venture is, at the same time, disclosure to other parent companies because most directors or officers represent one of the parent companies. When Parent Company A and Parent Company B are competitors, disclosure of information about Parent Company A will be beneficial to Parent Company B and harmful to Parent Company A. Consequently, interlocking directors or officers from Parent Company A will hesitate to disclose information about their parent company to other parent companies within a horizontal relationship. When Parent Company A and Parent Company B are not competitors, disclosure of information about Parent Company A will not be beneficial to Parent Company B and consequently the disclosure of this information will be less harmful to Parent Company A. Interlocking directors or officers from Parent Company A not only have to consider the conflicts of interest between the joint venture and their parent company but also need consider the conflicts of interest among parent companies when deciding whether to disclose information about this parent company.

Another parent company's interest in information hinders disclosure. Parent company B may be interested in information, because it is opportunity to both the joint venture and the interested parent company are critical factors for allotting the business opportunity between the joint venture and the parent company. See supra text accompanying notes 157-71.

201. According to the ALI comment, a parent company must disclose material facts concerning a business opportunity only when it seeks the approval of disinterested shareholders. "'The dominating shareholder is not obligated to disclose material facts concerning the opportunity unless he seeks the approval of disinterested shareholders. If he does seek such approval, then § 5.12(a)(2) obligates him to disclose material facts known to him concerning the corporate opportunity.'" ALI CORPORATE GOVERNANCE, supra note 53, § 5.12 comment c at 185. Thus, a parent company can obtain a business opportunity in which a joint venture is also interested without disclosure at its own risk.
critical to the competition between the joint venture and Parent Company A and also may be critical to the competition between Parent Company A and Parent Company B. If, for example, Parent Company B is interested in information, the harm to Parent Company A from disclosure of information will be much more than the harm from disclosure if Parent Company B was not interested in the information. Therefore, this category of information becomes highly protected. If Parent Company B is interested in information and is a competitor of Parent Company A, any information which is critical to a transaction between the joint venture and Parent Company A may be information which is critical to the competition between Parent Company A and Parent Company B. Thus, information becomes much more difficult to disclose when the interests of the parent companies become involved. If Parent Company B is a competitor of Parent Company A, any information which is related to a corporate opportunity conflict of interest between the joint venture and Parent Company A also may be information which is critical to the competition between the parents and this category of information also becomes more difficult to disclose. Consequently, it is necessary not only to balance the interests of the joint venture and Parent Company A, but also to balance the interests of Parent Company A and Parent Company B when determining whether a company should disclose information.

c. Degree of Disclosure

Another important factor for balancing the conflicts of interest of Parent Company A and the joint venture or Parent Company B is the degree of disclosure. The degrees or stages of disclosure can be roughly divided into three stages: (1) full disclosure, which discloses every detail of the material facts; (2) partial disclosure, which discloses only a portion of the material facts or discloses only outlines and omits details; and (3) use of information without disclosure, which does not disclose expressly but merely uses the information for the joint venture.

Full disclosure of every category of information is often difficult to require, particularly when parent companies are competitors. In some contexts, however, partial disclosure or use of information without disclosure may be substituted for full disclosure to avoid violating fiduciary duties. Most of the information which is critical to the competition between a joint venture and its parent company need not be disclosed. Interlocking directors or officers, however, can use their knowledge about their parent company to benefit the interests of the joint venture. Recall
the GM-Toyota joint venture described previously, in which the product of the joint venture, the Nova, was very similar to Toyota's product, the Corolla. Interlocking directors or officers who come from Toyota can suggest the best retail price for Nova by considering the cost and the retail price of Corolla.

Interlocking directors or officers may be required to disclose information that is critical to a self-dealing transaction between the joint venture and their parent company. Such critical information, however, often includes corporate secrets of the parent company. Full disclosure of critical information is difficult to achieve, particularly when parent companies are competitors. Ratification of a self-dealing transaction, however, will not be valid without full disclosure. Partial disclosure or the use of information without disclosure often may be enough to avoid liability for unfair self-dealing transactions and violating fiduciary duties. For example, interlocking directors or officers may be able to avoid liability by disclosing only rough figures of the cost of the product which the parent company will sell to the joint venture (e.g., under $10,000) or they can negotiate with the parent company not to charge unfair prices and use their knowledge about the cost while negotiating.

It is also difficult to require full disclosure of information regarding corporate opportunity conflicts of interests. In this context, interlocking directors or officers also may be able to disclose only rough plans about the parent company's corporate opportunities or they can use information to negotiate with a parent company not to usurp a corporate opportunity that belongs to the joint venture.

(2) Antitrust Problems with Disclosure

In a conflict of interest situation, interlocking directors or officers must balance the interests of the joint venture and their parent company and must avoid antitrust problems when considering disclosure of information. Among the many antitrust problems concerning joint ven-

202. See supra notes 69-70 and accompanying text.
203. Using information which is critical to competition without disclosure may create an antitrust problem because parent companies can use that information to create a cartel. Such use of information, however, cannot be effectively regulated because it is very difficult to identify its occurrence.
204. See supra notes 92-99 and accompanying text.
205. See supra notes 193-202 and accompanying text.
206. See supra notes 201-07 and accompanying text.
207. See supra notes 98-99 and accompanying text.
208. See supra notes 199-201 and accompanying text.
tures,\textsuperscript{209} collusion is the most critical.\textsuperscript{210} There are two possibilities: collusion between a joint venture and a parent company, and collusion among parent companies. The latter may create a more serious antitrust problem. When parent companies are competitors, the risk of collusion through the creation of a joint venture is very high. Both direct collusion (e.g., regulating each parent company’s output) and the exchange of information by way of cooperation in operating a joint venture will be unfavorable to competition.\textsuperscript{211} Consequently, a joint venture may become a tool of a cartel.\textsuperscript{212}

If there is collusion between a joint venture and its parent companies, there is no conflict of interest. By exchanging information which is critical to the competition between parent companies,\textsuperscript{213} parent companies can artificially set prices or outputs of their products which maximize their profits. Interlocking directors or officers must refrain from disclosing information about their parent companies to avoid violating antitrust laws even when disclosure will benefit all parties, including both the joint venture and other parent companies.

The GM-Toyota joint venture, NUMMI, is a good example of information disclosure conflict of interest and the antitrust problem of collusion in a joint venture.\textsuperscript{214} The joint venture combines Toyota, the largest auto manufacturer in Japan, and GM, the largest auto manufacturer in the United States. GM and Toyota notified the Federal Trade Commission (FTC) of their intention to create the joint venture under the premerger notification provisions of the Hart-Scott-Rodino Antitrust Improvements Act of 1976.\textsuperscript{215} The FTC accepted the joint venture consent agreement.\textsuperscript{216} Of the many antitrust problems created by this joint

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\item \textsuperscript{209} Examples of such problems are market monopolization, loss of potential competition, market exclusion, collateral or ancillary restraint, and collusion between parent companies. See supra notes 45-51 and accompanying text; Brodley supra note 11, at 1530-43.
\item \textsuperscript{210} Brodley, supra note 11, at 1530.
\item \textsuperscript{211} \textit{Id.}
\item \textsuperscript{212} \textit{Id.}
\item \textsuperscript{213} See supra notes 193-98 and accompanying text.
\item \textsuperscript{216} Statement of Chairman James C. Miller, III, Commissioner George W. Douglas, and
\end{itemize}
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NUMMI manufactures only one type of subcompact car, the Nova. The Nova is similar in design to a car which Toyota produces, the Corolla. GM and Toyota each have a one-half equity share of the joint venture. Toyota offers its know-how to manufacture subcompact cars and GM buys all the cars which NUMMI manufactures and sells them through GM’s sales network. When the joint venture—in fact, GM and Toyota—determines the price of the Nova, it is in the best interest of NUMMI that Toyota disclose information about the cost and price of the Corolla, which is a corporate secret of Toyota. The usefulness of this information to NUMMI places the interlocking directors or officers from Toyota in contradictory positions, assuming that the disclosure of cost and price information will be harmful to Toyota. Moreover, even if the disclosure of information about the cost and price of the Corolla will be beneficial to NUMMI, GM, and Toyota, because of increased profits from a resulting cartel, interlocking directors or officers cannot disclose the information under the terms of the consent agreement.

The consent agreement specifically allows the parties to exchange information “necessary to accomplish . . . the legitimate purpose or functioning of any Joint Venture,” such as the cost and the price of the Nova. The consent agreement, however, prohibits the exchange of competitive sensitive information that is not necessary for the operation of the joint venture, such as the cost and the price of the Corollas. One of the issues of dispute between the majority commissioners of the FTC and the dissenting commissioners is their differing opinions about the effect of the consent agreement on restricting collusion between the parent companies. The dissenting commissioners were particularly concerned that the use of information without disclosure, which the consent agreement attempted to prohibit, could not be prohibited effectively.


Id. Order IV and V at 57, 247; see also 49 Fed. Reg. at 18,290 (final consent decree).

There are two aspects of collusion in this case: collusion between Toyota and NUMMI, and collusion between Toyota and GM.\textsuperscript{221} The collusion between Toyota and NUMMI is closely related to the fiduciary duty problem of disclosure conflict of interests. If there is a disclosure conflict of interest between Toyota and NUMMI, there may be a problem of fiduciary duties of Toyota as a parent company or interlocking directors or officers, but there may be no problem of collusion. In this respect, moreover, there is a trade-off between collusion and market division. If there is an agreement to divide a market between Toyota and NUMMI and there is no competition between them, the problem of collusion will have less importance. In this case, there is no market division between Toyota and NUMMI (they are competitors in the market of subcompact cars in the United States) and the FTC allows Toyota to set its price on Corollas knowing the price of Novas.

The most serious collusion problem, one with which the FTC is particularly concerned, is the possibility of collusion between Toyota and GM by way of NUMMI. In this aspect, there is no fiduciary problem. Even if there is an agreement to restrict the market of the joint venture, there is still a risk of collusion between Toyota and GM as competitors.

(3) Summary

Disclosure conflicts of interest are closely related to self-dealing conflicts and corporate opportunity conflicts. To resolve the problems created by disclosure conflicts of interest, a balancing of the interests of a joint venture and its parent companies should be required. In balancing the interests, interlocking directors or officers should consider the characteristics of the information, the interests of other parent companies, and the degree of disclosure necessary. Moreover, to resolve the problems created by disclosure conflict of interest, interlocking directors or officers must also avoid the antitrust problem of collusion.

Conclusion

Although a joint venture to a closely held corporation and a parent-subsidiary relationship, the fiduciary duty problem in joint ventures has unique characteristics. Compared to a closely held corporation and a parent-subsidiary relationship, there is less need for the judicial and statutory protection of minority shareholders in a joint venture. Further-

\textsuperscript{221} Interview with Professor Thomas J. Campbell of Stanford Law School in Palo Alto, California (September 12, 1986).
more, contractual schemes to preclude these problems are extremely useful in a joint venture.

For all practical purposes, most problems of conflicts of interest and fiduciary duty in a joint venture can be remedied through contracts. Thus parent companies should prevent as many conflicts of interest by contract prior to creating a joint venture as possible. Contractual schemes, however, cannot solve all fiduciary duty problems; neither can they prescribe a regime that uses business considerations to determine, in all cases, how a conflict of interest should be solved. Initially, there are disclosure problems which are difficult to draft around in a contract even if they are foreseeable. Furthermore, contractual schemes cannot adequately address non-legal conflicts of interest that do not involve fiduciary duties.

The conflicts of interest can be divided into three categories: self-dealing, corporate opportunity, and disclosure. Each category has unique problems.

There are two approaches to the self-dealing conflicts of interest problem. If a transaction has not been ratified, the courts should judge the fairness of a challenged transaction using, where possible, a market price or arm's length standard. Often, however, market price is not available for a specific transaction. In that case, a court may attempt to calculate economic fairness based on cost and profit data from the corporations involved. In both cases, it is difficult for courts to determine what would have been a fair price.

A superior alternative to judicial imposition of a fairness standard is the parent companies' use of a full disclosure and ratification process for all self-dealing transactions. Parent companies should agree on the meaning of "full disclosure" in the original joint venture agreement. There are several concepts of "full disclosure," each with different informational requirements. The parent companies should select and modify their own version of full disclosure requirements in the original joint venture agreement. Armed with this definition of full disclosure, a joint venture can require independent approval of self-dealing transactions by independent parent companies.

In the case of corporate opportunity conflicts of interest, interlocking directors and officers may find themselves caught between loyalty to the joint venture and to the parent. They and their parent company must balance the interests of the joint venture and the interested parent to decide which one should obtain a business opportunity.

A parent company can obtain any business opportunity without violating its fiduciary duty towards a joint venture except when the opportu-
nity clearly belongs to the joint venture. Which opportunity belongs to the joint venture should be analyzed in terms of how a business opportunity arose (a fairness standard) and which enterprise will derive a higher relative value from a business opportunity (an efficiency standard).

The legal liability of directors and a parent company for a violation of their fiduciary duties in a corporate opportunity conflict situation can be avoided by an express agreement that narrows the joint venture's scope of business. Although the interested parent company can avoid legal liability, however, dissatisfied parent companies may be able to force a buy-out or may refuse to cooperate in operating the joint venture. Therefore, even when there is an express agreement, an interested parent company needs to balance the interests of all the parent companies.

A disclosure conflict of interest occurs when an interlocking director's or officer's disclosure of information benefits a joint venture or one of the parent companies but harms another of the companies. To resolve this problem, it is necessary to balance the conflicting interests. In the balancing process, three factors should be considered: the characteristics of the information, the other parent companies' interest in the information, and the degree of disclosure.

Although disclosure is critical both to self-dealing conflicts and corporate opportunity conflicts, full disclosure may not always be necessary to avoid the fiduciary duty problem. Partial disclosure or use of the information without disclosure may suffice.

It is more difficult to preclude disclosure conflicts of interest problems through express agreements because they are often difficult to identify and resolve beforehand. Furthermore, the possibility of antitrust violations for collusion complicate the attempt to draft preclusive guidelines.

When a court examines a fiduciary duty problem in a joint venture, a fairness standard is important. The court should consider whether the interested parent company obtains benefit to the detriment of other parent companies, and whether the conduct of the interested parent company clearly disappoints the expectations of other parent companies. Because of the joint venture's special characteristics or contractual scheme the court should not, however, restrict the conduct of a parent company of a joint venture to the same extent it would a parent of a subsidiary or that of a majority shareholder of a closely-held corporation.

When a parent company seeks to resolve a specific conflict of interest, the use of an efficiency standard is also important. The purpose of creating a joint venture is to maximize the long-term interest of each parent company through cooperation with other parent companies.
Therefore, throughout the creation and operating stages of a joint venture, each parent company should deal with and monitor the others to maximize its own long-term interests, which may differ from its short-term interests. A parent company may damage its long-term interests by pursuing short-term interests in a specific conflict of interests situation. Only through balancing their long-term interests can parent companies of a joint venture enjoy the synergistic effects for which the joint venture was established.