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Introduction

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Introduction

The pace of corporate mergers and acquisitions rose to a feverish pitch in the 1960s, reaching its apogee in 1968 when over 6,000 mergers were announced for a value of 43 billion dollars.[1] Thereafter the number of mergers fell off dramatically but began to rise again in the last half of the 1970s, until in 1981 there were 2,395 merger announcements for a value of 82.6 billion dollars, or almost double that of the year before.[2] In 1984 eight mergers alone accounted for a transaction value of 58.1 billion dollars,[3] and in 1985 there were 36 deals valued at over one billion dollars.[4] In the first half of 1987 there were only 927 mergers announced for a value of 91 billion dollars;[5] and then in October of 1987 the stock market took a nose dive, and many of the notorious corporate raiders were hard hit. The dramatically lower stock prices, however, made many companies tempting targets, especially for cash-rich corporations. In January of 1988 alone, deals with a total value of more than 36 billion dollars were either announced or completed.[6] This activity has prompted one well-known member of the corporate bar to say, "Corporate takeovers are back."[7]

All of this activity, of course, has a profound effect upon the financial markets and corporate governance; but it has significance for the legal profession as well. Lawyers are drafted into the armies of both the would-be acquiror as well as the beseiged target corporation. The lawyers are called upon not only to guide their corporate clients through the maze of regulatory law at both the federal and state levels, but also to advise in the formulation of strategy and implementation of tactics in

1. ECONOMICS DIVISION OF CONGRESSIONAL RESEARCH SERVICE, 97th CONG., 2D SESS., MERGER TACTICS AND PUBLIC POLICY 14-15 (Comm. Print 1982).

2. *Executives Optimistic*, Wash. Post, Jan. 15, 1982, at E2, col. 3.

3. Morris, *Corporate Wheeling and Dealing in '84 Totals $122.2 Billion*, AM. BANKER, Feb. 4, 1985, at 2.

4. *1985 Merger/Acquisition Record Tops 1984 Level, With Total Value of 179.6 Billion*, Daily Report for Executives (BNA) A-1 (Mar. 18, 1986).

5. Neustadt, *Merger Outlook Depends on Who's Looking*, AM. BANKER, July 16, 1987, at 11.

6. Cowan, *The Resurgence of Takeovers: Buying the Bargains Created in October*, N.Y. Times, Feb. 6, 1988, at 17, col. 3.

7. Statement by Joseph Flom, Esq. of Skadden, Arps, Slate, Meagher & Flom, New York, N.Y., *quoted in* Burroughs, *Back in Action: Companies Take Over the Takeover Game From Flashy Raiders*, Wall St. J., Jan. 25, 1988, at 1, Col. 6.

either the making of or the response to an offer. These tasks can be relatively straight forward if the merger is a friendly one, or they can be the stuff of which ulcers and malpractice suits are made when the merger is contested and counsel is called upon to respond on many fronts, under tremendous pressure to meet fast-breaking developments.

Much has been written about the legal aspects of corporate mergers and acquisitions, particularly with respect to the many highly controversial defense tactics available to an unwilling target corporation. Too little attention, however, has been directed toward the problems posed for counsel in advising clients in the context of corporate mergers and takeovers. In assembling the collection of articles contained in this symposium issue, an attempt has been made to focus on those problems. The authors of the contributions included in this issue do not completely agree as to either the causes of or the solutions to these problems. The nature of the issues defies any simple, definitive answers; indeed, the editors have not attempted to provide any. Rather, in the belief that to identify and discuss the problems is to increase the chances of correct solutions, the editors have only intended to provide a forum for the consideration of these problems.

Conflicts of interest, whether real or potential, arise for counsel in all contexts. The American Bar Association's Model Code of Professional Responsibility and Model Rules of Professional Conduct address this ubiquitous problem. As Professor Marc Steinberg points out in the lead article, *Attorney Conflicts of Interest in Corporate Acquisitions,* these guidelines do not expressly focus on the corporate acquisition context. Addressing the conflicts that may confront the attorney counselling a target corporation, Professor Steinberg identifies the structural bias built into corporate governance. He then examines the benefits and drawbacks of various solutions to the problems created for counsel by such bias, contrasting varying considerations relevant in the takeover context on the one hand and in other merger and acquisition contexts on the other.

George Reycraft's article, *Conflicts of Interest and Effective Representation: The Dilemma of Corporate Counsel,* brings into full relief the practical significance for corporate and securities counsel of the failure to recognize and properly address conflicts of interest: the potential liability of lawyers in lawsuits arising from alleged misconduct. Mr. Reycraft provides the reader with some striking examples of just how far reaching such liability can be. He concludes that the current rules of professional conduct are clearly inadequate to guide counsel so as to avoid lawsuits either for malpractice or even as principals in the misconduct of the management of his corporate client.

In his article, Mr. Reycraft identifies one of the sources of this problem as the inherent conflicts of interest present in the representation of the organizational client. Those conflicts are at least partially attributable, in turn, to the failure of counsel to properly identify whom he is representing. Ralph Jonas' rather pungent essay, *Who is the Client?: The Corporate Lawyer's Dilemma,* illustrates what he terms the "unreality" of counsel's position when representing an unwilling target corporation. If the attorney represents the corporate entity and not the officers, directors or shareholders, is he then to advise each of those groups to retain separate counsel so as to avoid conflicts of interest? Mr. Jonas suggests that such a solution is not only impractical but unrealistic as well. Perhaps more fundamentally, how is counsel, who is retained by and answerable to the board of directors, to be expected to represent the interests of the fictional corporate entity? The answer to the question as to whose interests counsel should represent is particularly significant in the merger or takeover context, in which the ostensible client, the corporation, will not survive.

In response to Mr. Jonas' questions, Professor James McCall undertakes an examination of the "entity as client" concept in *The Corporation as Client: Problems, Perspectives, and Partial Solutions.* He analyzes the development of the concept in the various formulations of professional standards. Professor McCall points out that, while the Model Code of Professional Responsibility embraces the pure "entity as client" concept, the Model Rules of Professional Conduct take a broader view: The corporate attorney's nominal client is the entity, but the corporation's interests are ascertained by consulting the board of directors. Professor McCall further suggests that the dilemma posed by Mr. Jonas would be eased by the adoption of a duty to report constituent misconduct, which was proposed but rejected in the formulation of the Model Rules.

If counsel perceives a conflict of interest at the outset, he or she is free to decline the engagement. Once an engagement is undertaken, however, the ability of counsel to withdraw is restricted by his duty to use his best efforts to serve the interests of his client. In *Resignation of Counsel: Fulfillment or Abdication of Duty,* James Hemmer reviews the application of various sources of the standards that inform counsel's decision whether to resign. He does so using six hypothetical situations, each of which is designed to address counsel's duties in the context of different issues. Although he stresses the seriousness of counsel's duty to use his or her best efforts to serve the interests of the client, he concludes that resignation by counsel may represent in some instances the ultimate fulfillment of his professional duty.

Professor Roberta Karmel's article, *Duty to the Target: Is an Attorney's Duty to the Corporation a Paradigm for Directors?,* turns the focus of the symposium from the complications of counsel's own conflicts of interest to the difficulty of advising the corporate board of directors faced with similiar conflicts. The article begins with an examination of the role of counsel in the corporate takeover context, and concludes that, in the face of potentially adverse interests of the various corporate constituencies, counsel is obligated to represent the interests of the corporate entity. Professor Karmel then turns to the duties of the directors of the target corporation in the context of a threatened takeover. She describes recent assaults, both statutory and judicial, upon the traditional view that the directors ultimately owe their fiduciary duties to the shareholders. Such modifications may reflect changing social values, but they may also create problems for the directors, who are now called upon to represent potentially adverse interests of the various corporate constituents. The article proposes as a possible solution that the directors be assigned a neutral role: like attorneys retained by the corporation, directors should represent the interests of the corporate entity rather than those of any of its various constituents. Such a change would dramatically alter the nature of the advice that counsel renders to his corporate client.

When a battle for corporate control spills over into the courtroom, a frequently litigated issue is the propriety of the defensive actions taken by the board of directors of the target corporation. In such litigation, a question of critical importance is the scope of the protection of the business judgment rule: are the target's directors shielded by the rule from a judicial inquiry into the propriety of their actions? The answer to this inquiry must form a central focus of counsel's advice to the board of his corporate client; counsel must understand the scope of the protection afforded by the rule in order to advise his client's board of directors as to their duties, the alternative responses available and potential liabilities. To the extent that the scope of the protection is unclear—or changing—counsel's task is made that much more difficult.

In her thoughtful note, *The Lawyer as Impresario: Form v. Substance in the Target's Boardroom,* Barbara Gustafson examines the scope of the protection of the business judgment rule under the current state of Delaware law. She argues that the rule, as it has been interpreted and applied by the courts in the takeover context, works to the detriment of shareholder welfare; the interests of the shareholders, the beneficial owners of the corporation, are ignored in the board's decision-making process. She argues that, on the one hand, the board has been afforded too much discretion to implement manipulative defense tactics. On the other hand, she further argues, the board is required to follow a restrictive and burdensome procedure in the decision-making process in order to retain the protection of the business judgment rule. This decision-making procedure—in which counsel acts as a sort of impresario, orchestrating the making of protected business judgments—encourages directors to defer to their legal advisors rather than rely on their own business judgment. The current state of the law, then, results in shareholder interests being ignored and directors failing to exercise their business acumen.

Addressing similar issues in a slightly different context, Gilbert Serota reaches rather different conclusions in *Potholes on the Level Playing Field—The Role of Courts and Counsel in Takeovers.* While conceding at the outset that the courts have perhaps placed too great emphasis on the role played by counsel in advising the target board, he does not criticize the broad discretion residing in the board of directors. Indeed, he suggests that such discretion constitutes the shareholders' best protection from abuse. He explains the emerging concept of the "level playing field," and explores how a mechanistic application of that concept can inhibit the exercise by the directors of their discretion. The realities of the marketplace, he argues, mandate that directors be permitted in some instances to discriminate between bidders for their company. He further posits that counsel properly has a role to play in providing guidance to the target board in responding to a hostile bid.

The outcome of *Smith v. Van Gorkom*[8] shocked the legal and business communities by denying the board of directors the protection of the business judgment rule; the court imposed personal liability upon directors for having failed to adequately inform themselves prior to approving a sale of their company. The opinion was followed by a storm of controversy. In *The Director's Duty of Care Three Years After Smith v. Van Gorkom,* Stephen Radin contends that the case did not work any revolutionary change in the law; rather it was only an example of the traditional jurisprudence applied to "egregious" facts. His article examines *Van Gorkom,* and then procedes to an exhaustive and valuable analysis of subsequent cases and statutory developments. He suggests that the lesson to be learned from these cases is that the director's best protection lies in compliance with the process that should be followed when considering a merger proposal or threatened takeover; and, significantly, that

8. 488 A.2d 858 (Del. 1985).

directors should not rely on the conclusory statements of their legal and financial advisors.

Mergers and takeovers have become a prominent feature of the topography of corporate law. *The Hastings Law Journal* presents this symposium to our readers in the hope that responsible professional organizations and the judiciary will respond to the issues raised in these articles and develop some much-needed guidelines for the corporate and securities bar.

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