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Director Liability

Emerging Trends in Fiduciary Duty Litigation: Lessons Learned from *Emerging Communications* and *Disney*

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The Delaware Court of Chancery's post-trial decisions in *In re Emerging Communications, Inc. Shareholders Litigation*, C.A. No. 16415, 2004 WL 1305745 (Del. Ch. June 4, 2004), and *In re Walt Disney Company Derivative Litigation*, C.A. No. 15452, 2005 WL 2056651 (Del. Ch. Aug. 9, 2005), at first glance appear to have little in common. *Emerging Communications* involved a challenge to a going-private merger where the company's directors, relying on the advice of counsel and independent financial advisors, cashed out minority stockholders at $10.25, almost 50 percent above the company's prior market price of $7.00. After trial, the Court found five of the nine defendants jointly and severally liable for damages exceeding $100 million. *Disney* stemmed from the termination of the Company's president, Michael Ovitz, in a manner that entitled him to approximately $140 million in severance after only 14 months of ineffective performance. In that case, after trial, the court found that the directors did not breach any of their fiduciary duties and the business judgment rule protected them from liability.

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Despite seemingly inconsistent results, the opinions in *Emerging Communications* and *Disney* contain a number of common threads and, read collectively, offer at least three significant lessons for the corporate practitioner. First, the level of scrutiny that Delaware courts will bring to bear in reviewing challenged transactions varies depending on the nature of the transaction and the fiduciary duties implicated. Second, the Court of Chancery may assess the conduct and culpability of directors on an individual basis, rather than collectively. Third, Delaware law remains unsettled as to whether there is a separate fiduciary duty of good faith or whether good faith is merely a subset of the duty of loyalty. While the outcome of *Emerging Communications* and *Disney* may be explained by the varying nature of the relevant transactions and resulting different levels of scrutiny applied, together the holdings in those cases demonstrate that director conduct and culpability may be evaluated on an individual basis and that the standards for evaluating good faith may continue to evolve.

The Facts and Holdings of *Emerging Communications*. *Emerging Communications* was a consolidated appraisal and fiduciary class-action. The Court of Chancery (per Justice Jacobs sitting by designation) ruled that the cash-out price in a ''going private'' merger was unfair and that the controlling stockholder and several of the company's directors were liable for breach of their duty of loyalty.

Emerging Communications, Inc. (''ECM'') was a publicly traded telecommunications company controlled by

Innovative Communications Corp. (''Innovative'') through a 52 percent ownership interest.[1] Innovative in turn was wholly owned by Innovative Communication Co. (''ICC''), which was wholly owned by Jeffrey J. Prosser. Prosser was ECM's chairman and chief executive officer.[2] He also appointed ECM's other six board members.[3]

In early 1998, Prosser proposed and took several preliminary steps to merge Innovative into ECM.[4] In May 1998, however, Prosser changed course and proposed taking ECM private because he believed ECM stock had become undervalued.[5] Under the new proposal, Innovative would acquire the remaining 48 percent of ECM's shares at $9.125 per share.[6]

In response, ECM's board formed a special committee of three purportedly disinterested directors to review the fairness of the proposed going private transaction.[7] The special committee retained independent counsel and a financial advisor.[8] The special committee negotiated with Prosser; these negotiations resulted in an increase of the offer to $10.25 per share.[9] The transaction was ultimately approved at that price by EMC's special committee and full board, with Prosser recusing himself.[10]

Stockholders of ECM filed two separate fiduciary-duty actions and an appraisal action in connection with the transaction.[11] Those three actions were subsequently consolidated and tried on the merits.[12]

After trial, the Court of Chancery issued an opinion finding that the merger consideration paid to ECM's minority stockholders was unfair. Specifically, the Court found that the fair value of ECM was $38.05 per share, or almost four times the amount paid.[13] The Court also found that the transaction was not the product of fair dealing because:

- the freeze-out merger was initiated by the majority stockholder which, ''even though not dispositive, is evidence of unfair dealing;''[14]

- the transaction was timed in a manner that was financially disadvantageous to ECM's minority stockholders because Prosser abandoned his initial proposal to merge Innovative into ECM, only after the drop in ECM's stock price;[15]

- Prosser co-opted ECM's longstanding legal and financial advisors to assist Innovative in the going private transaction; this was significant because those advisors, possessing material nonpublic information about ECM's value, business and prospects, ''were in the best position to represent the interests of the ECM;''[16]

- Prosser misled the special committee by falsely representing that the $10.25 price strained the limits of his available financing;[17]

- Prosser's personal secretary was copied on many of the special committee's confidential communications, potentially giving Prosser access to the committee's deliberations and strategy;[18]

- a majority of the special committee, as well as a majority of the full board, was economically beholden to Prosser by virtue of long-standing financial relationships with Prosser, secret consulting arrangements, and promises of future employment;[19]

- ECM's public disclosures ''misled minority stockholders about the Special Committee's and the board's independence from Prosser'' and falsely stated that a majority of the board that approved the going private transaction were members of the special committee.[20]

Having concluded that the transaction was unfair to the minority stockholders by an amount equal to $27.80 per share (the difference between the merger price and the actual fair value), the Court then proceeded to assess the liability of ECM's directors on an individual basis. An individual assessment was required, the Court stated, because ''the nature of each director's breach of fiduciary duty (if any), and whether they are exculpated from liability for that breach, can vary for each director.''[21] A director could only be liable if he breached his duty of loyalty or good faith because ECM's certificate of incorporation contained a clause that exculpated from money damages those directors found solely to have breached their duty of care.[22]

As Prosser stood on both sides of the transaction, the Court found that he breached his duty of loyalty and that the companies he controlled and through which he effectuated the transaction, Innovative and ICC, were liable under an aiding-and-abetting theory.[23]

The Court also found jointly and severally liable two of ECM's remaining six directors, despite their not having received anything in the transaction. The first such director found liable was John Raynor, a practicing attorney and long-time business associate of Prosser. At various times, Raynor acted as both Prosser's personal attorney as well as ECM's counsel.[24] While Raynor did not personally and directly benefit from the unfair transaction (as did Prosser), the Court found that Raynor ''actively assisted Prosser in carrying out the privatization, and he acted to further Prosser's interests in that transaction, which were antithetical to the interests of ECM's minority stockholders.''[25] Accordingly, the Court found that Raynor breached his fiduciary ''duty of loyalty and/or good faith.''[26]

The Court stated in a footnote that it was employing the ''and/or'' phraseology in discussing the duties of loyalty and good faith, because the Delaware Supreme Court has yet to articulate precisely the distinction be-

[1] 2004 WL 1305745, *1.
[2] *Id.*
[3] *Id.* at *4.
[4] *Id.* at *4-5.
[5] *Id.* at *5.
[6] *Id.* at *5-6.
[7] *Id.* at *6.
[8] *Id.*
[9] *Id.* at *7-8.
[10] *Id.* at *8-9.
[11] *Id.* at *1.
[12] *Id.* at *1.
[13] *Id.* at *24.
[14] *Id.* at *32.
[15] *Id.*
[16] *Id.*
[17] *Id.* at *36.
[18] *Id.*
[19] *Id.* at *33.
[20] *Id.* at *37.
[21] *Id.* at *38.
[22] *Id.* at *38.
[23] *Id.*
[24] *Id.* at *3.
[25] *Id.* at *39.
[26] *Id.*

tween those duties.[27] The Court noted that if a loyalty breach requires that the fiduciary have a self-dealing conflict of interest in the transaction itself, Raynor would only be liable for violating his duty of good faith for consciously disregarding his duty to the minority stockholders.[28] On the other hand, if a loyalty breach does not require a self-dealing conflict of interest or receipt of an improper benefit, then Raynor would be liable for breaching his duties of loyalty and good faith.[29] The Court stated that it need not decide that definitional issue, however, because under either definition, Raynor's conduct amounted to a non-exculpated breach of fiduciary duty.[30]

The Court also concluded, ''albeit with reluctance,'' that a second director, Salvatore Muoio, was similarly liable, even though his conduct was ''less egregious that that of Prosser and Raynor.''[31] The Court found Muoio liable because, as a principal and general partner of an investment advising firm who possessed significant experience in finance and the telecommunications sector, he was in a unique position to know that the $10.25 merger price was unfair.[32] As the Court explained, ''Muoio possessed a specialized financial expertise, and an ability to understand ECM's intrinsic value, that was unique to the ECM board members (other than, perhaps, Prosser).''[33]

Indeed, the Court found that Muoio's expertise in the industry was equivalent, if not superior, to that of the special committee's advisor, which gave Muoio ''far less reason'' to defer to that valuation.[34] Under these facts, the Court concluded that Muoio had inappropriately relied on the fairness opinion and had voted to approve the transaction despite knowledge, or a strong reason to believe, that the price paid was unfairly low.[35]

The Court found that this conduct was only explainable in terms of two possible mindsets.[36] The first is that Muoio made a deliberate judgment that, to further his own business interests, it was of paramount importance to exhibit his primary loyalty to Prosser.[37] The second possibility was that Muoio, ''for whatever reason, consciously and intentionally disregarded his responsibility to safeguard the minority stockholders from the risk, of which he had unique knowledge, that the transaction was unfair.''[38] Thus, just as with Raynor, the Court found that Muoio breached his fiduciary ''duty of loyalty and/or good faith,'' for which ECM's exculpatory clause did not shield him from liability.[39]

The Court stated that the four remaining directors did not ''cover[] themselves in glory, or merit commendation for the manner in which they discharged their responsibility as fiduciaries.''[40] The Court also noted that all four arguably lacked independence from Prosser.[41] But the Court ultimately found that there was no evidence that those four affirmatively colluded with Prosser to effectuate the privatization, or that they otherwise deliberately engaged in conduct disloyal to the minority stockholders' interests.[42] Accordingly, the Court concluded that there was no persuasive evidence that the fiduciary violations of the ECM directors other than Prosser, Raynor, and Muoio implicated conduct other than their duty of care.[43] Accordingly, they were shielded from liability by the exculpatory clause in ECM's certificate of incorporation.[44]

Under the terms of the Court's ruling, Prosser, ICC, Innovative, Raynor, and Muoio would have been jointly and severally liable in an amount exceeding $100 million.[45] Following the issuance of the Court's post-trial opinion, some but not all of the plaintiffs' claims were resolved by a Court-approved settlement, including all claims against defendants Raynor and Muoio. On January 9, 2006, the court issued final judgment against remaining defendants Prosser, ICC, and Innovative. Several days later those defendants appealed the court's post-trial rulings and judgment to the Delaware Supreme Court. That appeal is pending.

The Facts and Holdings of *Disney*. The *Disney* action challenged the conduct of officers and directors in approving the executive compensation and severance package of former Walt Disney Company president Michael Ovitz. Ovitz joined Disney as its president in October 1995.[46] Prior to joining Disney, Ovitz was regarded as one of the most powerful figures in Hollywood, and his hire was generally regarded as a major coup for the company.[47] Within a year, however, it became clear that Ovitz was a poor fit.[48] Many of Disney's directors began discussing the ''disconnect'' between Ovitz and other company executives,[49] and in September 1996, Eisner and Stanford Litvack, Disney's general counsel, began discussing whether Ovitz could be terminated for cause.[50] Eisner hoped to terminate Ovitz for cause to avoid paying a substantial no-fault termination payment required by Ovitz's employment agreement in case of early termination.[51] But Litvack advised that he did not believe that the company would be justified to terminate Ovitz ''for cause'' under the terms of that agreement.[52]

In November 1996, Eisner informed Disney's board that he intended to terminate Ovitz, without cause, by the end of the year.[53] On December 12, 1996, after several conversations between Eisner and Ovitz, Litvack (per Eisner's instruction) sent Ovitz a letter formally notifying him that he was being terminated without

[27] *Id*. at 39 n.184.
[28] *Id*.
[29] *Id*.
[30] *Id*.
[31] *Id*. at *39.
[32] *Id*. at *40.
[33] *Id*.
[34] *Id*.
[35] *Id*.
[36] *Id*.
[37] *Id*.
[38] *Id*.
[39] *Id*.
[40] *Id*. at *41.
[41] *Id*. at *41-43.
[42] *Id*.
[43] *Id*.
[44] *Id*. at *43.
[45] *Id*.
[46] 2005 WL 2056651, *10.
[47] *Id*. at *4.
[48] *Id*. at *11.
[49] *Id*. at *12.
[50] *Id*. at *20
[51] *Id*.
[52] *Id*.
[53] *Id*. at *19, 21.

cause.[54] The board was not shown that letter, nor did it meet to approve the terms of Ovitz's termination.[55]

Shortly after Disney paid Ovitz the substantial severance package required in a no-fault termination, a number of derivative actions followed. Plaintiffs alleged *inter alia* that current and former members of Disney's board of directors breached their fiduciary duties of care and good faith by (1) approving an employment agreement that provided for exorbitant severance terms in the case of no-fault termination and (2) later terminating Ovitz without cause, when they would have been justified in terminating him for cause and thereby could have avoided paying severance benefits valued at approximately $140 million. Plaintiffs also argued that Ovitz breached his fiduciary duty of loyalty in the course of his termination.

In October 1998, the Court of Chancery granted defendants' motion to dismiss, holding that the defendants' conduct was protected by the business judgment rule. On appeal, however, the Supreme Court affirmed in part, reversed in part, and remanded.[56] On remand, the defendants moved to dismiss the second amended derivative complaint, but the Court denied that motion in May 2003, and the case proceeded to trial. The trial commenced in October 2004, and was completed in January 2005.

On August 9, 2005, the Court of Chancery (per Chancellor Chandler) issued its opinion. The Court explained that under well-settled Delaware law the business judgment rule affords the directors of a corporation the presumption that, in making a business decision, the directors acted on an informed basis and that the action taken was in the best interests of the corporation and its stockholders. Unless the plaintiff rebuts that presumption, the board's decision will be upheld unless it cannot be attributed to any rational business purpose or unless the conduct constitutes corporate waste.[57] The Court further noted that the business judgment presumption is rebutted where the board violates one of its fiduciary duties in connection with the challenged transaction, but, citing to *Emerging Communications*, that the liability of directors must still be determined on an individual basis.[58]

In the context of discussing the nature of directors' fiduciary duties, the Court discussed the evolving concept of the duty of good faith.[59] The Court noted that Delaware law is far from clear as to whether there is a separate fiduciary duty of good faith and what good faith is.[60] The Court stated that to ''act in good faith, a director must act at all times with an honesty of purpose and in the best interests and welfare of the corporation.''[61] He then identified three ''salient'' instances that would constitute a failure to act in good faith: (1) ''where the fiduciary intentionally acts with a purpose other than that of advancing the best interests of the corporation,'' (2) ''where the fiduciary acts with the intent to violate applicable positive law,'' and (3) ''where the fiduciary intentionally fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties.''[62] The Court did not state explicitly, however, that there is a separate and distinct fiduciary duty of good faith.

In assessing the defendants' individual conduct in Ovitz's hiring, the Court criticized Eisner's unilateral efforts in hiring Ovitz, stating that the process that Eisner employed ''should not serve as a model for fellow executives and fiduciaries to follow'' and that his ''lapses were many.''[63] Specifically, the Court found that Eisner: (1) ''stretched the outer boundaries of his authority as CEO by acting without specific board direction or involvement'' in announcing Ovitz's hiring; (2) prematurely issued a press release, which placed significant pressure on the board to accept Ovitz and approve Ovitz's employment terms; and (3) stacked the board with friends and other acquaintances who were ''certainly more willing to accede to his wishes.''[64] The Court further advised that Eisner should have kept the board better informed and involved at all levels in accordance with ''how fiduciaries of Delaware corporations are supposed to act.''[65] The Court ultimately concluded, however, that Eisner's actions were taken in good faith, and were not a knowing violation of law or an intentional disregard of his fiduciary duty.[66]

The Court was also critical, in varying degrees, in individually assessing the conduct of Disney's other directors in connection with Ovitz's hiring, similarly citing the ''absence of ideal corporate governance.''[67] The Court focused particular criticism on the directors who were members of the compensation committee that approved Ovitz's employment agreement, but who played almost no role in its negotiation and spent little time deliberating.[68] But just as with Eisner, the Court found that none of Disney's other directors breached their fiduciary duties or acted other than in good faith in connection with Ovitz's hiring.[69]

In rejecting plaintiffs' attempted analogy to *Smith v. Van Gorkom*,[70] where the Delaware Supreme Court found directors liable for breaching their fiduciary duty for failing to exercise due care in approving a merger, the Court distinguished that case on several bases.[71] The Court noted that the transaction in *Van Gorkom* involved a sale of the entire company, while Ovitz's employment agreement, despite its unusually large size, had no potential materially to affect the company's finances.[72] The Court also noted that although Disney's compensation committee met for no more than one hour before approving Ovitz's hiring compared to the approximately two-hour board meeting in *Van Gorkom*, the Disney committee (unlike the directors in *Van Gorkom*) was provided with advance notice and a detailed term sheet.[73] Moreover, the Court stated that the opposition of senior management to the merger in *Van Gorkom* should have been a red flag for the board in

[54] *Id*. at *24.
[55] *Id*.
[56] *Brehm v. Eisner*, 726 A.2d 244 (Del. 2000).
[57] 2005 WL 2056651 at *31.
[58] *Id*.
[59] *Id*. at *35-36.
[60] *Id*. at *35.
[61] *Id*. at *36.
[62] *Id*.
[63] *Id*. at *39-41.
[64] *Id*.
[65] *Id*. at *41.
[66] *Id*.
[67] *Id*. at *47.
[68] *Id*. at *43-47.
[69] *Id*. at *47.
[70] 488 A.2d 858 (Del. 1985).
[71] *Id*. at *44-45.
[72] *Id*. at *44.
[73] *Id*. at *45, citing *Van Gorkom*, 488 A.2d at 875.

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that case, while Disney's senior management made clear that they saw Ovitz's hiring as a boon for the company.[74] The Court also noted separately that Disney was applauded for its decision to hire Ovitz, and Disney's stock price increased 4.4 percent in a single day after the announcement—increasing Disney's market capitalization by more than $1 billion.[75]

After ruling that none of the defendants breached their fiduciary duties in connection with Ovitz's hiring, the Court assessed their respective culpability in connection with Ovitz's termination. The Court found that Ovitz, himself, did not breach his fiduciary duty of loyalty by receiving the no-fault termination payment because he played no part in the decision.[76] The Court found that Eisner did not breach his fiduciary duties or otherwise act in bad faith in connection with Ovitz's termination, noting that Eisner was not personally interested in the termination in any way that would have made him incapable of exercising business judgment and that Eisner considered all information reasonably available when making what the Court acknowledged to be a difficult decision.[77] The Court also found that because Disney's governing corporate documents entitled Eisner unilaterally to terminate Ovitz, the board was not required to act to terminate Ovitz, even though Ovitz would receive such a large severance payment.[78] Because the board had no duty to act, the Court concluded that the defendants did not breach their duty of care and did not act in bad faith.[79] Additionally, the Court concluded that the board's decision to grant Ovitz a no-fault termination did not constitute waste because he could not have been terminated for cause and many of the defendants credibly testified that Disney would have been better off without Ovitz.[80]

The *Disney* case is presently on appeal to the Delaware Supreme Court, with a decision expected within the next few months.

Lesson Learned: The Nature of the Transaction and the Fiduciary Duties Implicated Matter. The seemingly disparate holdings of *Emerging Communications* and *Disney* can largely be explained by the nature of the respective transactions that were challenged and the fiduciary duties that were implicated in each case.

In *Emerging Communications*, because the majority stockholder stood on both sides of the going-private transaction, entire fairness was the undisputed standard of review.[81] Accordingly, in that case, the court was tasked with determining the fairness of that transaction to the minority, with the burden on the defendants to establish by a preponderance of the evidence that the transaction reflected fair dealing and a fair price.

Disney arguably involved less deliberation by the board than in *Emerging Communications*. In *Disney*, however, the Court found that neither Eisner nor the other Disney directors were self-interested in the negotiation of Ovitz's employment agreement or his termination. As a result, the director defendants' conduct was subject to the business judgment rule, and the Court was not required to determine the fairness of the Ovitz hiring and termination. Moreover, as Disney's charter contained an exculpatory provision adopted pursuant to Section 102(b)(7) of the Delaware General Corporation Law ("DGCL"), the Court could have found the director defendants liable for monetary damages only if the plaintiffs were able to establish that they acted in bad faith by consciously disregarding their fiduciary duties.[82]

The *Disney* court ultimately found that the director defendants were not liable for their roles in connection with Ovitz's hiring and termination. The Court's opinion makes clear that it did not condone the process by which the board approved those actions. The outcome resulted instead from the Court's careful evaluation of the evidence and its conclusion that the plaintiffs had failed to establish that the board's conduct in this non-self-dealing transaction was not protected by the business judgment rule.[83]

A primary lesson for majority stockholders is the significance of the process that they employ in a self-dealing transaction. Because of the high level of scrutiny and increased potential for liability in self-dealing transactions, a majority stockholder must establish a process that will enable arms-length negotiations. That may include appointing a special committee of disinterested and independent directors and permitting the special committee to select independent legal and financial advisors. As demonstrated in *Emerging Communications*, actions by the majority stockholder to act in his own interest at the expense of the minority, such as by appropriating to work for the majority stockholder a financial advisor who earlier had been retained to represent the best interests of the minority stockholders, does not create a strong record of facilitating an independent process.

Similarly, the majority stockholder must ensure that the special committee and its advisors receive all relevant information. In *Emerging Communications*, the Court was troubled that the majority stockholder did not make the latest financial projections available to the special committee, its financial advisor, or the ECM board, where these projections were given to the majority stockholder's legal and financial advisors and his lender.[84] The failure of the majority stockholder to ensure that the special committee and its advisors had full information led the Court to reject the majority stockholder's argument that the burden of proof shifted to the stockholders to prove the unfairness of the transaction. This flaw not only prevented the majority stockholder from shifting the burden of proof but also undermined the argument that his negotiations with the special committee and its advisors replicated an arms-length process and constituted material evidence of fairness. [85]

Lesson Learned: Directors Seeking Exculpation Should Be Prepared to Defend Their Conduct on an Individual Ba-

[74] *Id.* at *46, citing *Van Gorkom*, 488 A.2d at 867-68.
[75] *Id.* at *9.
[76] *Id.* at *37.
[77] *Id.* at *50-51.
[78] *Id.* at *49.
[79] *Id.*
[80] *Id.* at *38-39.
[81] 2004 WL 1305745, *9, *30.
[82] *Id.* at *39.
[83] *Id.* at *1.
[84] 2004 WL 1305745 at *7.
[85] For a recent example of the effect on judicial review of a flawed process in an interested transaction, see *In re Tele-Communications Inc. Shareholders Litig.*, 2005 WL 3642727 (Del. Ch.) (court denying summary judgment due to flaws in special committee process).

sis. In both *Emerging Communications* and *Disney*, the Court assessed the conduct and exculpations of the director defendants on an individual basis. As *Emerging Communications* and *Disney* explain, the director-by-director approach is now arguably required to adjudicate whether a director may be liable for money damages where the corporation has adopted an exculpatory provision pursuant to Section 102(b)(7) of the DGCL, shielding from liability those directors found to have violated solely their duty of care.[86] Thus, in *Emerging Communications*, two of the company's six directors who voted to approve the privatization were found liable, while the other four were not. Although the *Disney* court ultimately found that none of the defendant directors were liable for breach of fiduciary duty, it only reached that conclusion after analyzing the individual defendants' conduct on a director-by-director basis.

A director-by-director analysis of challenged transactions may have two consequences. From a policy standpoint, that directors are now on notice that their conduct may be assessed on an individual basis may provide additional incentive diligently to comply with their fiduciary duties and otherwise employ good corporate-governance processes. From the director's standpoint, individual analysis of culpability avoids imposing per se liability on the hypothetical director who may lack complete independence but who has no direct personal stake in an otherwise self-dealing transaction and may be exerting great effort in good faith to comply with his or her fiduciary duties.

Lesson Learned: Conscious Disregard of One's Duties Constitutes Conduct Not Taken in Good Faith; Still Uncertain Whether Good Faith Is Separate Duty or Merely a Subset of the Duty of Loyalty. *Emerging Communications* and *Disney* reinforce the notion that ''conscious disregard'' of one's fiduciary duties constitutes bad faith. *Disney* contains a detailed discussion of what it means to act in good faith, including a nonexclusive list of instances that would constitute bad faith.[87] As previously noted, those instances are: (1) ''where the fiduciary intentionally acts with a purpose other than that of advancing the best interests of the corporation,'' (2) where the fiduciary acts with the intent to violate applicable positive law,'' and (3) ''where the fiduciary intentionally fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties.''[88]

The Court ultimately found that none of the *Disney* defendants acted in bad faith in connection with Ovitz's hiring and termination. It is dangerous, however, to view the conduct in *Disney* as a model to follow to avoid liability, for at least three reasons. First, while the ''conscious disregard'' standard for judging faithful conduct is becoming more accepted, that standard by its very nature is unclear in its application. Second, it is conceivable that the Court—with its harsh criticism of Eisner and the board as a whole—could have reached a different result had the facts been slightly different. Third, as the *Disney* court notes, ''ideals of corporate governance'' have changed considerably in the decade since Ovitz's hiring and firing in the mid 1990s.[89] The Court emphasized that it would be improper to apply ''21st century notions of best practices'' in analyzing those corporate decisions, but officers and directors should expect their conduct post-*Disney* to be measured in an environment where the practices chided by the Court are now well-known.

Emerging Communications does not directly define the nature or scope of the duty of good faith. By finding that defendants Raynor and Muoio breached their duty of good faith, however, the Court reinforces that directors do not act in good faith when they (1) intentionally act to the detriment of the public stockholders to further their own interests or interests antithetical to those of the stockholders or (2) consciously and intentionally disregard their fiduciary responsibilities. Thus, *Emerging Communications* at least offers specific examples of conduct not to follow.

The example of disfavored conduct is potentially significant with respect to Muoio, whom the Court held to a higher standard by virtue of his financial background. While the Court's analysis of Muoio's conduct in *Emerging Communications* is at present an isolated event, and some believe it will remain so,[90] directors and officers with special expertise should be particularly diligent in using their specialized knowledge and skills in the best interests of the company and its stockholders.

Finally, both *Emerging Communications* and *Disney* raise the issue of whether there is a separate fiduciary duty of good faith or whether good faith is a merely a subset of the duty of loyalty.[91] Until the Delaware Supreme Court offers more detailed guidance, directors can take some comfort that in both cases the Court searched for evidence of a knowing or intentional act of misconduct before finding that a director failed to act in good faith. Although the conduct of the *Disney* board did not reflect best practices, the Court of Chancery found that the evidence showed that the decision-makers were well-motivated, did not knowingly or intentionally act improperly, and instead acted to make the best of a bad situation with no benefit to themselves.

In contrast, the Court found that the majority stockholder in *Emerging Communications* received an improper personal benefit and ''eliminate[d] ECM's minority stockholders for an unfair price in an unfair transaction that afforded the minority stockholders no procedural protections.''[92] The other directors held culpable were either found to have knowingly assisted the majority stockholder in carrying out the unfair transaction or to have knowingly approved a transaction they knew or should have known was unfair.[93] Had the board employed a fair process and acted to ensure that neutral decision-makers received full information, the outcome might have differed. Whether or not good faith is a separate duty may be less significant than whether the court is convinced that a director acted knowingly and intentionally to further the interests of a self-dealing fiduciary in a manner contrary to the best interests of the company and its stockholders. However characterized, such conduct both rebuts the business

[86] 2004 WL 1305745 at *38; 2005 WL 2056651 at *31.
[87] 2005 WL 2056651 at *35-36.
[88] *Id*. at *36.
[89] *Id*. at *1

[90] P. Atkins, ''M&A Today—Practical Thoughts for Directors and Deal-Makers'', 60 *The Business Lawyer* 1455, 1465 (Vol. IV, August 2005).
[91] 2004 WL 1305745 at *42 n.184; 2005 WL 2056651 at *35.
[92] 2004 WL 1305745 at *38.
[93] *Id*. at 39-40.

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judgment rule and prevents exculpation under Section 102(b)(7) of the DGCL.

The Process Followed May Affect Litigation Costs and Burdens. Directors in self-dealing transactions with majority stockholders must pay attention to the process they employ in approving the transaction. Even in a non-self-dealing transaction, acting without a record of appropriate deliberation may subject directors to a lengthy and costly trial, as occurred in *Disney*. In the context of a self-dealing transaction with a majority stockholder, failure to establish a fair process will keep the burden of proof on the interested party and subject to a risk of personal liability those who are found to have knowingly assisted the self-dealing party accomplish an unfair transaction.

In all events, directors can expect their conduct to be examined individually as a Delaware court assesses whether they are culpable for a transaction found to be unfair. While we await more definitive guidance from the Delaware Supreme Court on whether there is a separate duty of good faith, it appears that directors who receive no benefit from a transaction distinct from that generally received by all stockholders, are well-motivated and do not act knowingly or intentionally against the best interests of the corporation and its stockholders will continue to receive the benefits of exculpation under Section 102(b)(7) if the stockholders have chosen to incorporate its protections in their charter.