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Client Alert

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Reexamining Director Conduct – A Sign of the Times

A recent Delaware Chancery Court decision is another sign that courts are reexamining traditional notions of director conduct.

The July 29, 2008 ruling, in *Ryan v. Lyondell Chemical Co*., involved a class-action lawsuit challenging the $13 billion cash sale of Lyondell Chemical Co. to Basell AF in December 2007. In the suit against Lyondell's former independent directors, among other defendants, Lyondell stockholders alleged that the directors breached their fiduciary duties in approving the sale on an expedited basis.

It is well established under Delaware law that, when corporate directors determine to sell the corporation, they generally must seek to maximize the value to the corporation's stockholders under the principle first enunciated more than 20 years ago in *Revlon Inc. v. MacAndrews & Forbes Holdings Inc*. The *Revlon* case, itself, and most subsequent Delaware court decisions addressing directors' *Revlon* duties, involved a corporate sale initiated by the corporation, itself. Lyondell, however, was not up for sale when it received an unsolicited cash offer at a price that the Delaware Chancery Court characterized as "very attractive indeed" to Lyondell stockholders and which represented a "substantial premium" over the prevailing price of Lyondell shares. The Lyondell directors obtained a customary fairness opinion before accepting the offer, but otherwise took no action to evaluate the offer price.

Many commentators previously believed that directors' *Revlon* duties were not implicated by an unsolicited cash offer at an attractive price, and that directors would be justified in agreeing to such an offer and presenting it to the corporation's stockholders. The Court's ruling in *Lyondell*, however, suggests that *Revlon* duties are triggered in connection with any proposed sale of a company, not just one initiated by the company, and that directors may be obliged to shop the company or take other steps to achieve a better price or deal for stockholders even at the risk of alienating the unsolicited bidder.

The Court in *Lyondell* also refused to dismiss plaintiffs' allegations that the Lyondell directors breached their duty of loyalty to the company by approving the sale of the company in less than seven days and doing "little, if anything" to obtain the best price for Lyondell stockholders. According to the Court, these allegations, if true, could amount to a breach of the good faith component of the directors' duty of loyalty. If so, it would mean that the Lyondell directors would not be entitled to protection from personal liability for monetary damages under Lyondell's corporate charter. The possibility that mere inaction by directors could amount to a breach of the duty of loyalty (as opposed to the duty of care) was first suggested by the Chancery Court's first decision in *The Walt Disney Company Shareholders Litigation* case several years ago.

The *Lyondell* decision reinforces the lesson in *Disney* that directors must be scrupulous in attending to their duties, including possible *Revlon* duties, in connection with important corporate matters. Many directors are aware they may face personal liability for their actions, but assume that the usual exculpation and indemnification from the corporation will protect them. As *Lyondell* indicates, however, directors may not be protected from personal liability if they do not act in good faith, or do not act at all, in the face of a duty to act.