"Presumptions and Burdens of Proof as Tools for Legal Stability and Change"

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INTRODUCTION

Presumptions and burdens of proof are used, among other purposes, to maintain legal stability and at the same time effect change. By imposing the burden of proof on the party asserting a certain outcome, courts can calibrate burdens of proof and substantive rules until experience points to rule retention or amendment. As agents of change, presumptions and burdens of proof are far more flexible and less brittle than rules.¹

This Article tells the story of presumptions and burdens of proof in litigation between corporate shareholders and managers. This litigation is replete with volatile presumptions and innovative burdens of proof, demonstrating their effectiveness and flexibility as tools for legal stability and change. This litigation also demonstrates their limits as tools for change: excessive, varied, and undisciplined use can bring chaos. Because burdens of proof relate to particular facts, constant changes can create too many fact-specific results that defy generalization. More importantly, presumptions impose obligations to respond; burdens of proof constitute the responses. As the courts alter the facts that a party must prove to win, but not the presumptions to

¹ Both a rule on the one hand and a presumption and burden of proof on the other hand affect the outcome of a litigation. Yet they differ: a rule defines what a plaintiff must prove to win his case and what the defendant must prove to defend against liability; presumptions and burdens of proof determine which party (plaintiff or defendant) can take advantage of a presumption of certain facts, and which party must bear the burden of proving certain facts. Courts do not change rules during a litigation; they do change presumptions and burdens of proof from party to party during the litigation.

Thus, a rule might hold that, for the plaintiff to win, facts 1, 2, and 5 must be proved. Throughout the trial the rule does not change. However, a court may grant the plaintiff the advantage of presumption of fact 2, and impose on the defendant the burden of negating it. During the litigation a court may allow the defendant to take advantage of a presumption that negates fact 2, and impose on the plaintiff the burden of proving it.
which the facts respond, the connections between the presumptions and burdens of proof loosen and disintegrate. With no internal relationship, these presumptions and burdens make little sense and provide little future guidance.

Four presumptions are fundamental to this Article, and all four appear in corporate shareholder-management litigation. They are: (i) experience-based presumptions, for example, the presumption that in financial matters, most people will act in their own self-interest rather than in the interest of others; (ii) tradition-based presumptions, for example, that people will follow the trodden path, which underlies the rule that directors must properly inform themselves and deliberate before making decisions; (iii) presumptions of legality, legitimacy, and orderliness, for example, that corporate directors were legally elected, and that fiduciaries hold and manage other peoples' money in accordance with the law; and (iv) initial presumptions in favor of defendants. The set of facts that plaintiffs must prove to win is determined by the initial burden of proof, which in turn varies depending on individual causes of action. In every case, however, plaintiffs must satisfy a burden of proof, however slight.

This Article begins with a discussion of corporate management's duties, then moves to an exposition of presumptions and burdens of proof in shareholder-management litigations, and concludes with an examination of takeover litigation in which changing burdens of proof have rendered the substantive law practically incoherent.

2. Habits, traditions, and customs, as well as experience-based presumptions are related to our limited attentive capacity. It is important for us to focus our attention on new events because the unfamiliar may be more risky than the status quo. We often put ourselves on an "automatic pilot" as to what we repeatedly do in order to have free attention to the new and unexpected. See William M. Best, A Treatise on Presumptions of Law and Fact § 47, 115 (reprint 1981) (1845).

3. This presumption allows people to plan and rely on what seems to be the case without further investigation. Such a presumption also increases the security and the value of legal rights to property, and freedom from intervention by others, whether individuals or organizations or government. A stable society must provide its members with rules that assure them of their ownership, and freedom, rights and duties.

4. Initial presumptions support stability, and may, in many cases, be inevitable. See infra section II.A.
I. CORPORATE MANAGEMENT'S DUTIES

A. The Prohibitions

Most litigation between shareholders and management involves management's fiduciary duties in exercising the powers entrusted to them by virtue of their office. As fiduciaries, it is management's duty both to make informed and deliberate decisions (duty of care). Management must exercise its powers exclusively or primarily in keeping with the purposes for which the powers were given: to benefit the corporation and its shareholders. Therefore, corporate management may not enter the corporation into transactions in which management is self-interested (duty of loyalty).

B. The Exception

These prohibitions do not apply if the person to whom the fiduciary owes his duties, the entrustor, consents to an improper transaction. Such consent temporarily abrogates the entrustor's right to rely on the fiduciary, leaving the entrustor to fend for himself. To release the fiduciary of his duties, the entrustor's consent must be informed, to a great extent by the fiduciary, as well as independently of the fiduciary. That is, the entrustor must be on notice that he cannot rely on his fiduciary with respect to the particular transaction. The prohibitions and the exception together form the basis of the relationship between management on the one hand, and the corporation and its shareholders on the other hand.


6. Statutes and case law say that directors and officers owe their corporations a duty of care: they must exercise that degree of skill, diligence, and care that a reasonably prudent person would exercise in similar circumstances. See, e.g., Joy v. North, 692 F.2d 880 (2d Cir. 1982); AMERICAN LAW INSTITUTE, PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS §§ 2.01, 4.01 (Proposed Final Draft, March 31, 1992). See also ROBERT C. CLARK, CORPORATE LAW § 3.4 (1986).

7. See, e.g., Lewis v. S.L. & E., Inc., 629 F.2d 764 (2d Cir. 1980); Sinclair Oil Co. v. Levien, 280 A.2d 717 (Del. 1971); ALI, supra note 6, at §§ 5.01-5.08. See also CLARK at 141.

8. See, e.g., Fliegler v. Lawrence, 361 A.2d 218 (Del. 1976); ALI, supra note 6, at § 5.02(a)(2)(D). See also CLARK at 248.

9. Arguably, there are limits to this exception based upon public policy. This discussion excludes the issue of a broad future "blank check" consent before the fact. These limits can be overlooked without doing injustice to the discussion.
II. PRESUMPTIONS AND BURDENS OF PROOF IN SHAREHOLDERS-CORPORATE FIDUCIARIES LITIGATION

A. Initial Presumption and Presumption of Legality

At the initial stage of the litigation, plaintiff-shareholders bear the burden of proving that defendant-corporate fiduciaries violated their duties to the corporation and its shareholders. Fiduciaries enjoy the shelter of a presumption of legality. In carrying out their responsibilities, for example, there is a presumption that they satisfied their duties of care and loyalty.

The imposition of the burden of proof on the plaintiff further entrenches the status quo, the existing balance of power and state of affairs between the two parties, which the plaintiff seeks to alter through a court order. Support of the status quo is arguably justice-neutral, strengthening the existing state of affairs regardless of how intrinsically just it is, and without regard to the manner by which it was achieved. This initial presumption in favor of the status quo can serve to protect corporate management that acted legally, as well as those who acted illegally. A rejoinder to this possible criticism is that, as a matter of principle, it is preferable to err on the side of pardoning the culpable rather than sanctioning the innocent. As such, the presumption of legality also serves to strengthen the status quo.

The imposition of initial burdens on the plaintiff can be attacked as inefficient because the burden is not necessarily imposed on the party possessing the relevant information. Arguably, corporate management possesses such information about the flaws in its decisions. As we shall see, management may have to bear a burden of proving some of these facts, but the initial burden of proof does not seem to account for this imperfect distribution of information. Instead, it seems that courts use burdens of proof to induce parties to provide information, starting usually with plaintiffs. Arguably, placing the initial bur-

10. In addition, rules of procedure assist the party bearing the burden of proof to ferret out information from the other party, subject to limits.

11. See 3A WILLIAM M. FLETCHER, PRIVATE CORPORATIONS § 1340.20 (rev. ed. 1994) ("In actions by shareholders on the corporation's behalf, the burden of proof is on the plaintiff."). Charles McCormick had this to say:

In most cases, the party who has the burden of pleading a fact will have the burden of producing evidence. . . . The burden of pleading and proof with regard to most facts has been and should be assigned to the plaintiff who generally seeks to change the present state of affairs and who therefore naturally should be expected to bear the risk of failure of proof or persuasion.

CHARLES C. MCCORMICK, 2 MCCORMICK ON EVIDENCE § 537 (4th ed. 1992)
den on shareholder-plaintiffs violates the principle of equality of the parties before the law. In this vein, each party should be given the opportunity to prove his case, and the party offering the most cogent presentation should prevail. One possible response to this argument is that parties are indeed treated equally, in that all plaintiffs bear the initial burden of proof. The rebuttal would be that some people in positions of power, such as corporate management, are typically the defendants in such actions, while people subject to the exercise of private power, such as small investors, are often the plaintiffs. Thus, the burdens imposed on certain classes of people who fill certain roles may still remain inequitable.

The primary response to arguments against the initial burden of proof is that regardless of whether it is efficient or fair, the burden of proof is inevitable; it is likely to result even from an equality-based burden of proof system in which both parties start on equal footing—"the state of nature." The plaintiffs' burden of proof will inevitably evolve to eliminate arguments and evidence that have been repeatedly accepted over a long period of time. Judges are likely to require further proof where plaintiffs' assertions are contrary to the status quo, rather than from defendants (who demand nothing and assert nothing).\(^\text{12}\) Over time, plaintiffs will be required to bear the initial burden of proof.\(^\text{13}\)

Although the "state of nature" inevitably will result in the plaintiff bearing the initial burden of proof, the specific facts that the plaintiff must prove are not preordained but depend on the plaintiff's cause of action, that is, the facts that it must prove to make its case. These initial facts are also affected by the experienced-based, habit-based presumptions, or social stability-based presumptions that work in the plaintiff's favor. If plaintiffs rely on these presumptions, a conflict among the presumptions arises: at the initial stage of the trial, plaintiffs would be required to prove facts that they could rely upon without proof in later stages. In such cases the winning presumption is not constant; thus courts' decisions can go either way.\(^\text{14}\) Inevitably, however,

\(^{12}\) See generally Best, supra note 2, at 57.

\(^{13}\) Arguably, but for the presumption, management should have to prove that it was legally elected. However, plaintiffs generally do not attack the legitimacy of management's elections, but rather particular transactions. If nothing is proved as to that transaction, management can prevail, since management itself would never bring the case. The "state of nature" leads to presumptions that support the status quo.

\(^{14}\) For example, in criminal cases, the state has the burden of proving that the accused violated the law. Whether the state must also prove that the accused was competent to
the plaintiff must start with some proof. If neither party proves anything, the defendant wins.\textsuperscript{15}

\textbf{B. The Business Judgment Rule}

Plaintiff-shareholders in corporate litigation not only bear the burden of initial proof but also confront a gate-keeper rule limiting the facts that they are allowed to prove at the outset. Plaintiffs may not attack the merits of the corporate boards' decisions subject to complaint, and courts will not scrutinize these merits at the outset.\textsuperscript{16} Plaintiffs must first meet their burden of proving that the board's decision was flawed in one of two ways.

One flaw is that the board's decisions were not informed and deliberate, essentially not in keeping with the duty of care.\textsuperscript{17} This proof is grounded in an experience-based presumption that good decisions are made on the basis of adequate information and after considered deliberation.

The flaw that plaintiffs may prove in the alternative is that the decisionmakers had personal interests in the outcome of the de-
This proof will raise an experience-based presumption that corporate fiduciaries, like all fiduciaries who have a personal stake in the outcome of their decisions and who act both for the corporation and for themselves, will pursue their own interests rather than those of the corporation and its shareholders. The previous presumption is coupled with a second presumption that management's self-interested decisions will not benefit, and might even harm, the corporation and its shareholders.

If plaintiff-shareholders fail to prove that the board's decision was flawed by lack of care or tainted with conflicts of interest, their actions will be unsuccessful. If plaintiffs prove either flaw, the burden of proof then shifts to the defendants. At this point the gate opens up, allowing judicial scrutiny of the merits of the decision.

C. The Entrustor's Consent

The defendants have the burden of proving their defenses. One defense available to all fiduciaries is that their entrustors consented to the careless or self-interested transaction. The presumption underlying this defense is that the protections of fiduciary law are unnecessary when the party whose interest the law is designed to protect—the entrustor—has consented to his fiduciary's flawed decision. The entrustor should be the judge of what is in his own best interest. When he gives consent to a transaction that is tainted by self-interest or carelessness, this is evidence that the entrustor judged the transactions to be in his interest. The entrustor's consent impliedly negates the presumption that the fiduciary's decisions that were reached by flawed process or that were in conflict failed to benefit or even harmed the entrustor. The fact that the transaction benefitted the fiduciary becomes irrelevant.

18. The basic idea of the fraud and conflict of interest exceptions is that, when directors are shown to have been trying to further their own personal ends, or have been strongly tempted to bias the terms of the transaction in their own interest, their judgments are not really within the class of discretionary exercises of power on behalf of the corporation that we want to protect. See, e.g., Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) ("[D]irectors can neither appear on both sides of a transaction nor expect to derive any personal financial benefit from it in the sense of self-dealing as opposed to a benefit which devolves upon the corporation or all stockholders generally."). See also CLARK, supra note 6, at 124.

19. Almost one hundred and fifty years ago the courts established a presumption that people will accept what is for their benefit. See BESl, supra note 2, at 148. Similarly, if people destroy evidence, the presumption is that the evidence destroyed was against their interests. Id. at 128.
To be legally effective, the entrustor's consent must meet a number of conditions. The entrustor must be on clear notice that he can no longer rely on the fiduciary; in essence he must be independent of the fiduciary. To be capable of giving intelligent consent, the entrustor must have certain information that is typically provided by the fiduciary. The defendant fiduciaries bear the burden of proving that the consent satisfied these conditions and was thus valid.

D. Shareholders' Representatives—The Courts and Intra-Corporate Groups: Increased Judicial Role and Consequent Rule Change

Historically, only entrustors or persons they designated to act on their behalf could consent to flawed transactions. The courts refused to uphold such flawed transactions, and they were voidable by the entrustors-shareholders. Over time, however, the courts began to approve transactions tainted by conflict of interest on the part of corporate fiduciaries, even if not all shareholders had approved such transactions. Furthermore, the courts and the statutes recognized intra-corporate groups' authority to consent to flawed transactions on behalf of the corporation and its shareholders.

The substitution of the courts and intra-corporate representative-fiduciaries, for individual, consenting entrustors required change in the substantive law. When entrustors consent personally, judicial scrutiny focuses on their ability and capacity to consent. Ultimately, however, their decisions are entirely their own—they can consent or withhold their consent for any reason and for no reason at all. The presumption is that they will only

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20. If the corporation knowingly and freely rejects an opportunity, and also consents to the executive's taking it, there is little basis in theory for precluding the executive from taking it. See, e.g., State ex. rel. Hayer Oyster Co. v. Keypoint Oyster Co., 391 P.2d 979, 986 (Wash. 1964) (holding that a corporation cannot ratify the breach of fiduciary duties unless full and complete disclosure of all facts and circumstances is made by the fiduciary and an intentional relinquishment of the corporation of its rights); Globe Wooler Co. v. Utica Gas & Electric Co., 121 N.E. 378, 380 (N.Y. 1918) (“The trustee . . . cannot rid himself of the duty to warn and to denounce.”). See also Clark, supra note 6, at 248.

21. See Harold Marsh, Jr., Are Directors Trustees? Conflicts of Interest and Corporate Morality, 22 Bus. Law. 95 (1966). This rule is still in effect under the law governing the fiduciary relationships of trust and agency.

22. See Clark, supra note 6, at 248 (“[M]odern corporate statutes allow the board to delegate . . . its functions to working committees.”). See also Marsh, supra note 21, at 48-51. For a discussion of the sorts of guidelines courts set in reviewing a dismissal of a derivative suit by a special litigation committee, see Zapata v. Maldinado, 430 A.2d 779, 787-789 (Del. 1981); Auerbach v. Bennett, 393 N.E.2d 994 (N.Y. 1979).
consent if the arrangement is in their best interests, which is the result the law favors. Thus, entrustor-shareholders may act arbitrarily in granting consent. When courts or entrustor-representatives approve a flawed transaction, however, a need for standards arises, and this in turn requires changes in the substantive law. As we shall see, these changes have become varied and numerous with their links to the fundamental presumption (regarding flawed fiduciary decisions) becoming increasingly tenuous.

The fundamental presumption is twofold: that fiduciaries faced with a conflict of interest will prefer their own interest to that of entrustors; and that such self-interested transactions will certainly not benefit the entrustors and may in fact prove harmful to them. In exercising their power to approve flawed transactions, the courts require corporate management to rebut the second, more objective prong of the presumption. The more subjective first prong remains irrebuttable. Corporate management fiduciaries who engage in self-interested transactions bear the burden of proving that the transaction is fair to the corporation and its shareholders. These developments in the substantive law afford corporate fiduciaries not only the defense that all the shareholders consented to the flawed transactions, but also the defense that the decisions in question were fair to the corporation or the shareholders, regardless of whether the shareholders agreed to them. If the directors can prove the transaction was fundamentally fair, they will prevail.

E. Disinterested Directors

The legal concept of disinterested directors became accepted in the mid-1970s, and they were recognized as shareholder-representatives. This recognition required changes in the law and the courts' role. In addition to satisfying the preconditions for entrustors' consent, these representatives of entrustors' interests are subject to presumptions applicable to any fiduciary. As such,

23. See, e.g., McKee v. Interstate Oil & Gas, 188 P. 109, 112 (Ok. 1920), cert. denied 258 U.S. 632 (1921) (holding that a corporation may acquire property as a result of a tainted transaction consented to by the shareholders when the corporation used the property for the benefit of the corporation); See also Eastern Oklahoma Television Co., Inc. v. Ameco, Inc., 437 F.2d 138, 142 (Ok. 1971); CLARK, supra note 6, at 248.
24. Id.
25. Unfair transactions can be defined as transactions that reduce entrustors' benefits harm the entrustors, although the two might not be distinct. Benefit to disloyal fiduciaries may imply reduced benefits or harm to the entrustors.
26. See generally CLARK, supra note 6, at 645.
the consent of these representatives must be authorized, informed, deliberate, free of conflict of interest,\textsuperscript{27} and independent of the interested corporate fiduciaries. If the defendant-management can prove that the disinterested directors' consent met these conditions, the courts will view their consent as binding on the entrustors. Thus, courts will not scrutinize either the consent or the transaction subject to the consent on the merits. With the advent of the disinterested director doctrine, defendant-management was afforded the protection of the business judgment rule anytime the disinterested directors gave binding consent to flawed transactions.

The presumption that disinterested directors' decisions are not tainted by conflict of interest, and that these directors are capable of fairly representing the corporation and its shareholders in granting consent, is not entirely experience-based; there were, in fact, manifold indications to the contrary.\textsuperscript{28} As doubts about the disinterestedness of these directors grew, new intra-corporate entities of shareholder-representatives emerged. One example is the proliferation of new litigation committees to evaluate the justification of shareholder derivative suits.\textsuperscript{29} However, some courts expressed skepticism with respect to the disinterestedness of these committees as well.\textsuperscript{30}

As doubts about disinterested directors or litigation committees grew, a new round of judicial supervision of disinterested directors' decisions has emerged. This supervision was intro-

\textsuperscript{27} The likelihood that the shareholders will reach decisions that are harmful to themselves is far smaller than the likelihood that their representatives' decisions will fail to maximize the shareholders' interests.

\textsuperscript{28} Disinterested directors are chosen by the interested directors. Most are members of the same class and share the same opinions, political views, experiences and feelings about shareholders' suits. Disinterested directors are busy, with far greater commitments to other enterprises. Generally, they support management or resign.

Yet, disinterested directors have reputations to protect and resignation may amount to a confession of defeat, or retreat from battle. These directors operate in the shadows of personal and internal conflicts, a shade removed from the direct financial conflicts of interest involved in the transactions they are expected to scrutinize objectively without bias.

\textsuperscript{29} The committees were usually composed of directors who did not serve on the board at the time of the alleged violations.

\textsuperscript{30} See Joy v. North, 692 F.2d 880 (2d Cir. 1982). That opinion stated:

[T]he special litigation committees created to evaluate the merits of certain litigation are appointed by the defendants to that litigation. It is not cynical to expect that such committees will tend to view derivative suits against the directors with skepticism... The conflict of interest which renders the business judgment rule inapplicable in the case of directors who are the defendants is hardly eliminated by the creation of a special litigation committee.
duced by changing burdens of proof. Disinterested directors’ approval of conflict of interest transactions no longer is viewed as equivalent to that of the entrustor-shareholders. However, the courts have refrained from imposing on defendants the same burden of proving transactional fairness as is imposed on the defendants in “strong” conflicts transactions. Instead, the courts shifted the burden of proof to the plaintiffs to prove a different set of facts. For example, plaintiffs are required to prove that the disinterested directors’ decision-process was flawed, and also that the directors lacked reasonable bases for their conclusions. The “reasonable bases” objective prong of the burden provides a opening through which the courts could scrutinize the merits of the decision under attack.

F. Disinterested Shareholders

Another intra-corporate group authorized to give consent to transactions tainted by conflict of interest is the majority of the disinterested shareholders. According to an experience-based presumption, however, these shareholders should either rationally decline to give consent or give their consent without much attention to available information or the merits of the decisions. This is so because the cost of providing informed consent to these shareholders outweighs the value of these shareholders’ stake in the corporation. The basis of the presumption on which the defendant-management’s defense of consent rule rests is thus substantially weakened.

In response, the courts have modified the rule and shifted the burden of proof once again. The full defense that the entrustor-shareholder’s consent protects management has been re-

31. See Zapata, supra note 22, at 788-89 (holding that when courts review the dismissal of a derivative suit by a special litigation committee, the court shall place the burden of proving independence, good faith, and reasonable investigation on the corporation.). See also CLARK, supra note 6, at 646.

32. See Auerbach, supra note 22, at 648; See, e.g., Klinicki v. Lundpa, 695 P.2d 906, 919-20 (Or. 1985) (holding under Oregon law that a director wishing to take advantage of a corporate opportunity must disclose all material facts regarding the opportunity to the disinterested directors or, if none, to the disinterested shareholders.). Note that consent by both disinterested directors and shareholders is a wasteful repetition of the director’s previous acceptance. See CLARK, supra note 6, at 648.


34. See CLARK, supra note 6, at 648.

35. See Gottlieb v. Hayden, 90 A.2d 660 (Del. 1952); ALI, supra note 6, at § 7.11.
duced to a conditional defense. Only if the transaction is adjudged to be fair would the public shareholders' consent become a complete defense for management. If the plaintiffs can prove that the transaction is unfair, management-defendants will lose. Perhaps because the shareholders' consent provides a weak presumption of fairness that favors management, the plaintiffs must bear the burden of proving that the transaction was unfair.36

The story up to this point demonstrates both the legal stability and change courts have maintained through presumptions and burdens of proof. The third part of this Article demonstrates the extreme permutations in presumptions and burdens of proof that have led to incoherent law today. The following Part demonstrates what can happen when courts and legislatures use too much of a good thing.

III. Murky Presumptions and Unstable Burdens of Proof

A. Managements' New Powers as Shareholder-Representatives

As hostile takeovers became popular, management began to take defensive measures against so-called raiders. The courts recognized management's power to respond to takeover attempts, not only of the corporate action variety, for example, mergers, but also tender offers that involve no corporate actions.37 The courts viewed tender offers not only as offers to purchase shares but also as bids for control, sometimes to the detriment of the minority shareholders and always against management's wishes.38 The hostility in "hostile takeovers" is borne by management toward raiders. In most cases, tender offers are followed by a merger of the target corporation with the raider's subsidiary. More importantly, because numerous shareholders are incapable of negotiating with the raiders, management is left to represent their interests. For these reasons, responses to takeovers can be viewed as part of the managerial function and management's authority to oversee the corporations.

There are serious arguments, however, against vesting management with power to negotiate with raiders on behalf of shareholders. The corporate actions involved in takeovers have no

36. See O'Connor, supra note 33, at 956.
37. See CLARK, supra note 6, at 572.
business rationale except that the shareholders' sell their shares to the raiders. Further, representing the selling shareholders, which entails evaluating the adequacy of tender offers and assuring that the raider will treat all shareholders fairly, is not usually a managerial function, although management is well informed about the corporation. More importantly, management is not neutral or disinterested, but with respect to hostile takeovers is hostile.

B. Managements' Conflict of Interest in Takeover Cases

Courts recognize that in defending against takeovers, management's interests may conflict with those of the shareholders. Courts have, however, established a presumption that these conflicts of interest are weak. Therefore, the courts designed a different regime for hostile takeover situations than that for stronger conflict of interest situations. This hostile takeover regime demonstrates the weaknesses and danger of excessive change in presumptions and burdens of proof.

Like all plaintiffs, plaintiff-shareholders in takeover cases bear the initial burden of proof that management's adoption of defensive tactics against raiders was flawed for either lack of information and deliberation, or for conflict of interest. Because the decisions involving defensive tactics were added to the business judgment calculus, the plaintiffs must prove at least one of the flaws before the burden of justifying their decisions shifts to management.

The mere fact that a raider knocks on the door is sufficient to shift the burden of rebutting the presumption that management's weak conflicts of interest did not harm the corporation or shareholders. However, the facts that management must prove to rebut the presumption are different from the facts management must prove when their decisions are tainted by personal financial interests. In the case of "normal" conflicts, the defendant-management must show either that the independent directors or

39. Management have an interest in its office and its prerequisites shareholders have an interest in the highest price and best terms a raider offers. It is unlikely that the raider would retain the current management, especially after paying a high control premium.


41. Id. at 13-14.
other shareholder-representatives have given a binding consent to the transaction or that the transaction was fair. The presumption that in conflict of interest situations the directors will prefer their interests to those of the shareholders and the corporation is not rebuttable. Only that part of the presumption that such preference would result in harm to the corporation is rebuttable by showing binding consent or fairness to the corporation and its shareholders.\footnote{See id. at 13.} Fairness is an objective concept and thus not easy to prove.

In “weak” takeover conflicts of interest management may similarly prove that the disinterested directors have given binding consent to the transaction. If their valid consent cannot be evinced, however, the defendant-management need not show fairness but rather that they acted in good faith with the belief that their actions were “primarily in the corporate interest.”\footnote{Id. at 13-14, n.47.} This test is subjective, and their belief need only be negative, as in absence of malice.\footnote{Id. at 14, n.49.} The facts required to meet the test are aimed at rebutting the first prong of the fundamental presumption, that management will put its interests before those of the entrustors. No rebuttal is required to negate the second part of the presumption, that management’s actions will reduce the corporation’s benefits or do harm to them.\footnote{Id.}

Other facts can be shown to rebut presumptions of weak conflicts, such as a showing of “reasonable grounds” to believe that the presence of the raider posed danger to corporate policy and effectiveness. These facts are probably aimed at rebutting the second part of the original presumption, that if the defendant’s corporate policy is not maintained, the shareholders will be harmed. A second presumption, that the directors’ actions in protecting their own policies will not harm the shareholders, regardless of their conflicts,\footnote{These presumptions fly in the face of numerous experiences to the contrary.} is also required.

Even though the courts have recognized management’s authority to represent shareholders in their negotiations with the raiders and view the authority as a business judgment, they have oscillated in their treatment of this representation. Sometimes courts interfered in management’s decision far more than ever before, and interfered by rules rather than by presumptions and

\footnote{See id. at 13.} \footnote{Id. at 13-14, n.47.} \footnote{Id. at 14, n.49.} \footnote{Id.} \footnote{These presumptions fly in the face of numerous experiences to the contrary.}
burdens of proof. Sometimes courts adopted the business judgment rule and expanded management's powers to eliminate judicial supervision almost entirely. Between these two extremes, courts introduced guides based on unarticulated presumptions that differed from the fundamental presumption. These disparate treatments reflect different roles in which management is cast. As Professor Joel Seligman recently demonstrated, judicial decisions have created a growing distinction between the interests of the shareholders and those of the corporation.

When courts cast management in the role of shareholders' representatives negotiating with raiders, the courts provide management with explicit and fairly detailed guides on what factors to consider and how to exercise managerial authority. Many of these guides constitute effective negotiation techniques in representing the shareholders' interests. These guides are in the form of rules rather than presumptions and burdens of proof: the courts simply tell management how to represent the shareholders. These rules fly in the face of the preemption of "weak" conflicts of interest on the part of management.

When the courts characterize management's decisions as business decisions, they allow management far more leeway than usual. Courts limit the extent to which management can put obstacles in the raiders' way; defensive measures must be "reasonable in relation to the threat posed" to the shareholders and corporate "constituencies other than shareholders, such as creditors, customers, employees, and perhaps even the community generally." In addition, management is allowed to represent the corporation, its shareholders, and numerous other stakeholders. Consequently, management's authority has been vastly expanded, while judicial supervision has been substantially reduced. Management is authorized to preclude shareholders from selling their stock to get a better price, to maintain manage-

48. See Unocal v. Mesa Petroleum Corp., 493 A.2d 946 (Del. 1985) (holding the business judgment rule applicable to takeovers).
49. See Seligman, supra note 40, at 50.
51. Id.
ment's policies, or for the good of the other corporate constituencies.\textsuperscript{54}

Yet the courts have not established standards for determining priorities among the interests of corporate constituencies, and such standards are not easily set.\textsuperscript{55} In addition, management's personal conflicts of interest are subsumed under conflicts between the shareholders and other stakeholders. Those conflicts are not deemed personal conflicts of interest of management, even though the interests of some of these stakeholders, such as employees, are closely aligned and even identical with those of management. Thus, as management acts to protect employees, management also acts in its own interest without incurring the presumption of conflicts of interest and exposing their decisions to judicial scrutiny. Finally, when the representation of shareholders in this case is marked as a "business judgment," and disinterested directors give binding consent to the defensive tactics, the gate-keeper rule precludes the courts from evaluating management's decisions on the merits. If no binding consent is available, the weak conflict of interest is applied, and management must prove that it acted in good faith in the belief that its action benefitted or did not harm the corporation. Management need not prove that the transaction is fair to the shareholders.\textsuperscript{56}

Courts have ruled that the defensive tactics corporate management may adopt must be reasonably related to the threat posed by raiders.\textsuperscript{57} This holding seems to be a rule, limiting management's actions and discretion in takeover cases. These limits are broad because the threat includes making inadequate offers to the shareholders and adversely impacting the corporation and its "constituencies."\textsuperscript{58} Thus, the balancing applies to almost all ac-

\textsuperscript{54} See Cl\textsc{a}rk, supra note 6, at 139.

\textsuperscript{55} The Delaware courts have tried unsuccessfully to develop standards of determining what is a proper business purpose for corporate actions and have abandoned the attempt. See Weinberger v. UOP, Inc., 457 A.2d 201 (Del. 1983).

\textsuperscript{56} See Cl\textsc{a}rk, supra note 6, at 123-24.

\textsuperscript{57} Id. at 584-87.

\textsuperscript{58} This test echoes the judicial limits on management's spending in proxy fights. Management's conflicts of interest in proxy fights and hostile takeovers are similar; in both cases management desires to retain its position. The rationale for allowing directors to expend corporate funds to defend their positions in a proxy fight, however, does not apply to takeovers. In proxy fights shareholders decide for whom to vote; management expends corporate funds to persuade shareholders in making their decision. In takeovers, defensive tactics prevent shareholders from deciding whether to sell to the raider; management is allowed to exercise its power to limit or eliminate the shareholders' freedom to sell their shares. Further, in proxy fights, if management borrows to retain its position, the lenders may obtain undue and hidden influence over corporate affairs. If
tions that management takes on behalf of the shareholders and the corporation in hostile takeovers.

The "balancing test" is puzzling because its response to the fundamental presumption differs from the usual response, and the reason for the "balancing" is a presumption with a different focus. If a raider poses a danger to the shareholders and the corporation, management should be allowed, even required, to adopt defensive tactics that would eliminate this raider as a threat altogether. The halfway defense, the balance, must therefore respond to something other than danger. If the requirement of balancing is strategically necessary to extract better terms from the raider for the corporation and its shareholders, management is better situated to determine the extent of pressure in the particular cases. If the "reasonable relation" is designed to provide a level playing field for management and raiders by limiting management's powers to eliminate raiders altogether, thereby encouraging some takeovers as well as the conduct of auction to reach higher prices and better terms (in the interests of shareholders), the threat of the raider seems to be too broad because it includes the threat to other corporate constituencies.

I suggest that the presumption underlying the "reasonable relation" is partially similar to the fundamental presumption: that this is a conflict of interest situation in which management will not act in the best interests of the corporation. The reasonable relation, however, responds to a somewhat different view of management's duties: management and raiders are viewed as combatants entitled to fight fairly and squarely for the prize of corporate control. This view seems to recognize and legitimize management's right to act in its own interest so long as the rules of combat are fair to raiders. While the fundamental presumption seems to remain intact, the rebutting facts do not rebut the presumption because they do not rebut either the existence of conflict or possible harm to the corporation and its shareholders. All the facts rebut is the presumption that if management were allowed to act without restraint, it would have used most or all corporate resources to win the takeover battle. The rebutting facts merely show that the ground rules for corporate battles are fair.

the management invests its own funds to retain office, and win, it may be tempted to recoup its investment in hidden ways. Allowing management to match the raiders' expenses makes sense as the better of these evils. These factors, however, do not exist in hostile takeovers.

59. See Clark, supra note 6, at 588.
Thus, while management’s conflicts in takeovers are viewed as “weak,” the courts have taken conflicting positions. Courts have (i) increasingly interfered with management’s conduct in hostile takeover situations; (ii) extended management’s powers and discretion and shielded it from scrutiny, and (iii) required rebuttal facts that do not respond to the fundamental presumption.

As courts oscillate between recognizing stronger and weaker management conflicts, between supervising management as representatives of selling shareholders and investors or the corporation and its other constituencies, courts require proof of different facts. The presumptions as to conflicts are not necessarily related to the burden of proof regarding particular facts. It seems that the links between the various burdens to fundamental presumption have been loosened or lost altogether. Without the links confusion reigns.

CONCLUSION

The story of corporate litigation suggests that presumptions are effective judicial tools for maintaining legal stability and change. Courts can adhere to the rules based on underlying presumptions of certain facts, and simultaneously affect the results in particular cases by allocating and changing the burdens of proof regarding these facts. In addition, courts can effect legal change by altering the presumed and rebuttal facts. There are limits, however, to change. Because presumptions and burdens are ground rules for court dialogue, the rebutting burdens of proof must relate to the underlying presumptions. With continuous changes in presumptions and responsive burdens of proof, tailored to particular situations, the link between presumed facts and rebutting facts is likely to disintegrate. The dialogue will thus become incoherent. Burdens of proof might respond to facts that are not presumed, and vice versa, resulting in parallel independent statements. In short, this Article sings the praise of presumptions and burdens of proof as extremely useful tools for

60. Id. at 588.
62. Later cases demonstrate the results. While in Paramount v. Time-Warner, 571 A.2d 1140 (Del. 1989), management was allowed to preclude shareholders from selling at $200 shares that traded at $126, in Paramount, management was not allowed to take similar actions. The court's distinctions between these cases (for example, that the first case did not involve transfer of control while the second case did) is not very convincing.
stability, provided that they remain linked and embraced in the dialogue. Excessive changes may sever the link and turn their usefulness into confusion.